

2006 WHOLESALE WATER SUPPLY CONTRACT

KEMPNER WATER SUPPLY CORPORATION
&
CITY OF LAMPASAS

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WHOLESALE WATER SUPPLY CONTRACT

This WHOLESAL E WATER SUPPLY CONTRACT ("Contract") is entered into as of this 2 day of 2, 2006 (the "Contract Date") between KEMPNER WATER SUPPLY CORPORATION ("KWSC"), a Texas water supply corporation, and the CITY OF LAMPASAS, TEXAS, a Texas municipal corporation (the "City") (collectively referred to herein as the "Parties"). This Contract is attached to and executed contemporaneously with the Settlement Agreement of this same date between the same Parties in the case styled *Kempner Water Supply Corp. v. Central Texas Water Supply Corp.*, Civil Action No. 207477, in the 169th Judicial District of Bell County, Texas.

PREAMBLE AND WITNESSETH

WHEREAS, KWSC is a Texas non-profit corporation, organized and established under Chapter 67, Texas Water Code (formerly Article 1434a, R.C.S. of Texas 1924, as amended), and KWSC independently owns and operates its potable water distribution system in order to provide potable water to its customers; and

WHEREAS, KWSC has contracted with the Brazos River Authority ("BRA") to reserve raw water in Stillhouse Hollow Reservoir ("Stillhouse") in order to have a water supply for these purposes; and

WHEREAS, the City is a Texas municipal corporation chartered under Article XI, § 5 of the Texas Constitution, and the City independently owns and operates its potable water distribution system in order to provide potable water to its various classifications of customers; and

WHEREAS, the City has contracted with the BRA to reserve water in Stillhouse in order to have a water supply for these purposes; and

WHEREAS, the Parties entered into a Water Sale and Purchase Contract dated December 19, 1979 ("1979 Contract") and a First Amendment to Water Sale and Purchase Contract dated July 22, 1985 ("1985 Contract"), whereby the City contracted with KWSC for KWSC to (i) have constructed by CTWSC a water treatment plant and (ii) construct and operate a water transmission system designed, in part, to transport water from Stillhouse and deliver it to the City; and

WHEREAS, in order for KWSC to obtain the necessary financing to construct improvements to its system for the benefit of the City and its customers, KWSC sought funding from Farmer's Home Administration, now the U.S. Department of Agriculture - Rural Development ("USDA-RD"), and the City passed a resolution authorizing the City's payment of a portion of the debt service on such funds; and

WHEREAS, USDA-RD required the Parties to pledge the 1979 Water Sale and Purchase Contract and the 1985 First Amendment to Water Sale and Purchase Contract as security for the loan to KWSC and loan to CTWSC to construct improvements to deliver treated water to KWSC; and

WHEREAS, KWSC entered into a Wholesale Water Supply Contract with Central Texas Water Supply Corporation ("CTWSC") dated May 16, 2000 ("2000 Contract"), pursuant to which CTWSC agreed to withdraw, treat and transmit treated water reserved by KWSC and the City in Stillhouse to KWSC in accordance with the terms of that Contract; and

May 16, 2000

WHEREAS, as part of settlement of litigation between the Parties in 2001, the Parties agreed that the 1979 Contract and 1985 Contract needed to be amended, modified and completely replaced by the Wholesale Water Supply Contract entered into as of September 13, 2001 (the "2001 Contract"), which 2001 Contract reaffirmed the Parties' unconditional obligations with respect to the USDA loans; and

Sept 13 2001

WHEREAS, the 2001 Contract was predicated upon, and included provisions derived from, the 2000 Contract; and

WHEREAS, USDA-RD did not approve or concur in the 2000 Contract; and

WHEREAS, although USDA-RD has not yet concurred in the 2001 Contract, the Parties have operated pursuant to the 2001 Contract to this date; and

Letter of Nov 9, 2005 from USDA stating that the parties are part of the contract

WHEREAS, disputes have arisen between and among KWSC, the City, and CTWSC, resulting in litigation brought by KWSC in Cause No. 15,419, *Kempner Water Supply Corporation vs. Central Texas Water Supply Corporation*, 27th Judicial District Court of Lampasas County, Texas, said lawsuit having been transferred to Bell County and now referred to as Cause No. 207,477 C, *Kempner Water Supply Corporation vs. Central Texas Water Supply Corporation*, 169th Judicial District Court of Bell County, Texas; and

WHEREAS, KWSC and CTWSC entered into an Agreement for Sale, as defined herein, subject to conditions precedent to closing specified therein, including, but not limited to, obtaining approval of USDA-RD and certain loans from the Texas Water Development Board; and

WHEREAS, USDA-RD by letter dated February 9, 2006, informed CTWSC and KWSC that it had approved the Agreement for Sale; and

Feb 9, 2006 USDA approved

WHEREAS, KWSC and CTWSC entered into a Wholesale Water Supply Contract dated August 2, 2005 ("2005 Contract"), which was approved by USDA-RD on November 9, 2005, and which was effective December 1, 2005; and

WHEREAS, KWSC and CTWSC entered into a Settlement Compromise and Release Agreement dated August 1, 2005, subject to approval by USDA-RD of the 2005 Contract; and

WHEREAS, the 1979 Contract, the 1985 Contract, and the 2001 Contract are hereinafter collectively called the "Prior Agreements"; and

WHEREAS, the Parties agree that the 2001 Contract needs to be amended, modified and completely replaced by this new Contract, subject to the concurrence of USDA-RD; and

WHEREAS, the provisions of this Contract are substantially similar in intent and concept to the provisions of the 2001 Contract and reaffirm the unconditional obligations of the Parties with respect to the USDA loans; and

Treated water
WHEREAS, subject to the provisions set out herein, KWSC desires to transmit treated water to the City and the City desires to receive treated water from KWSC in accordance with the terms of this Contract; and

WHEREAS, the City has intended by this Agreement to reserve sufficient water treatment plant, storage and transmission capacity in order to meet its regulatory requirements; and

WHEREAS, KWSC has intended historically, and in this Agreement intends for the future, to supply the City with treated water in capacities and at pressures consistent with the design parameters of the KWSC and the CTWSC systems, taking into account both the current and future legitimate water supply requirements of the City and the current and future legitimate water storage transmission, capacity and pressure requirements necessary to allow KWSC and the City to meet their own respective regulatory requirements, but without warranty that KWSC's performance under this Agreement will enable the City, at all times and under all circumstances, to meet all of its regulatory requirements by way of reliance upon flow rates and pressures afforded solely by the KWSC system hereunder; and

WHEREAS, the City and KWSC desire to work together as good neighbors to provide potable water to meet their customers' respective needs, both now and in the future.

NOW, THEREFORE, in consideration of the mutual covenants and agreements herein contained and subject to the terms and conditions set forth in the Settlement Agreement of even date herewith between these Parties, as supplemented by the terms and conditions hereafter set forth, KWSC and the City agree and contract as follows:

ARTICLE I. GENERAL PROVISIONS

1.1 Definitions

The following terms and expressions as used in this Contract, unless the context clearly shows otherwise, shall have the following meanings:

100%
"Adjusted CTWSC Debt Service" means, upon closing of the Agreement for Sale, (i) KWSC's ten percent share of the payments on CTWSC USDA-RD Loan 91-01 and (ii) 90 percent of the debt service on the refinanced principal balance of CTWSC USDA-RD Loan 91-06 which KWSC will refinance with proceeds of TWDB Loan 1. 90%

"Adjusted KWSC Debt Service" means (i) the debt service on KWSC USDA-RD Loan 91-06 and (ii) the debt service on the refinanced principal balance of KWSC USDA-RD Loan 91-07 which KWSC will refinance with proceeds of TWDB Loan 1.

"Agreement for Sale" means that "Agreement for Sale and Conveyance of a Segment of Water System Between and Including State Highway 195 Pump Station Site and Ivy Mountain Tank Site," executed between CTWSC and KWSC on August 2, 2005.

"Board" means the governing body of KWSC.

"BRA" means the Brazos River Authority in Waco, Texas.

"CTWSC" means Central Texas Water Supply Corporation.

"CTWSC Common System" means all facilities of the CTWSC Existing System from the existing raw water intake facilities, through the existing CTWSC Water Treatment Plant, to the CTWSC System Junction, including upon construction the 18-inch parallel line to be constructed by CTWSC which is Item 3 on Exhibit B, and then west approximately 7,400 feet from the corner of Chaparral Road and Stillhouse Lake Drive to the point where the twenty-four (24) inch pipeline ends and the thirty (30) inch pipeline begins on Chaparral Road across the street from Doc Curb's driveway ("Doc Curb's Place"), as shown on the System Map defined herein and attached hereto as **Exhibit A**.

"CTWSC Current Debt Service" means KWSC's ten (10) percent share of the payments on CTWSC USDA-RD Loan 91-01, and KWSC's 90 (90) percent share of the payments on CTWSC USDA-RD Loan 91-06.

"CTWSC Energy Costs" means the amounts paid by CTWSC for electrical energy required to operate the CTWSC Existing System only. CTWSC Energy Costs are limited to those energy costs associated with the withdrawal of water from Stillhouse, operating the existing Water Treatment Plant, and pumping water from the existing Water Treatment Plant at its current capacity via the high service pumps, same being included in the cost KWSC pays per 1,000 gallons of water per Section 2.03 of the CTWSC Wholesale Contract. CTWSC Energy Costs shall not include energy expenses for any CTWSC New Facilities.

"CTWSC Existing System" means the existing water intake structure, the CTWSC Water Treatment Plant at its current rated capacity of 14.35 MGD, the existing storage facilities, pump stations and transmission mains, lighting, and all other facilities currently operated by CTWSC

for the supply, treatment and transmission of treated potable water. The CTWSC Existing System, as constituted in 1999, is described in detail in the Roming Report. The CTWSC Existing System also includes: (i) improvements made since the date of the Roming Report and prior to the date of this Agreement and (ii) those facilities to be built that are described as Item No. 3, Item No. 4, Item No. 5, Item No. 6, and Item No. 7 in the Kallman Estimate defined herein and attached hereto as **Exhibit B**. The CTWSC Existing System shall not include facilities of the CTWSC Existing System that are transferred to KWSC upon closing of the Agreement for Sale, or any CTWSC New Facilities.

"CTWSC New Facilities" means any new facilities constructed by CTWSC after October 27, 2005 including, but not limited to, any new intake structure, new storage facilities, new pump stations, new transmission mains, a new plant or expansions at the location of the current CTWSC Water Treatment Plant, a new treatment plant at another location, and improvements identified as Item No. 1 and Item No. 2 on the Kallman Estimate. The term "CTWSC New Facilities" shall not include those facilities described as Item No. 3, Item No. 4, Item No. 5, Item No. 6, and Item No. 7 in the Kallman Estimate.

"CTWSC Operations and Maintenance Expenses" means those expenses defined in Section 3.5.B.2.

"CTWSC System Component" means each individual component of the CTWSC Existing System as defined above.

"CTWSC System Junction" means the junction where the twenty-four (24) inch pipe leaving the CTWSC Water Treatment Plant splits west to a twenty-four (24) inch pipe serving CTWSC customers to the west, and east to a sixteen (16) inch pipe serving CTWSC customers to the east, as shown on the Roming Report map dated February 23, 1999 as 24" x 24" Junction.

"CTWSC Water Treatment Plant" means those CTWSC System Components required to receive and treat raw water and deliver it into the plant clearwell, including all vessels, mixing equipment filters and chlorination equipment or other equipment, including pumps required to distribute potable water into the CTWSC Existing System.

"CTWSC Water Treatment Plant Capacity" means the continuous twenty-four (24) hour per day potable water production capacity of the current CTWSC Water Treatment Plant, which is currently rated to be 14.35 million gallons per day, as set forth in the Roming Report.

"CTWSC West System" means all CTWSC facilities west of the junction where the twenty-four (24) inch pipe ends and the thirty (30) inch pipe begins on Chaparral Road, referred to herein as Doc Curb's Place as shown on the System Map, to and including the meter station at the discharge side of the 2.0 million gallon Ivy Mountain Tank (provided, however, if the transaction in the Agreement for Sale closes, "CTWSC West System" shall mean all CTWSC facilities west of the junction where the twenty-four (24) inch pipe ends and the thirty (30) inch pipe begins on Chaparral Road, referred to herein as Doc Curb's Place, to and including the

meter station to be constructed under the Agreement for Sale at the State Highway 195 Pump Station).

"CTWSC Wholesale Contract" means that Wholesale Water Supply Contract between CTWSC and KWSC dated October 27, 2005 (as it may be permissibly amended from time to time by CTWSC and KWSC).

"Council" means the governing body of the City.

"Donnell Tank" means the water storage tank located approximately three-quarters of a mile north of F.M. 2808, as shown on the System Map.

"Effective Date" of this contract shall be the date this Contract has received concurrence by USDA-RD in writing which written concurrence shall be attached hereto as **Attachment 1**.

"Effective Water Storage Tank Capacity" means the available storage volume of the tank contained within the tank between the floor of the tank and an upper level six inches below the lowest point of either the overflow weir or overflow pipe.

"Escalator" means a factor used to increase the capital improvement charge per thousand gallons.

"FPS" means feet per second.

"Force Majeure" means such term as it is defined in Section 5.01 of this Contract.

"Georgetown Road Tank" means the water storage tank located on Georgetown Road south of the City, as shown on the System Map.

"GPM" means gallons per minute.

"Hewgley 0.25 Tank" means the water storage tank located on F.M. 580 northeast of the City, as shown on the System Map.

"Hewgley 2.0 Tank" means the water storage tank located on F.M. 580 northeast of the City, as shown on the System Map.

"Improvements" means any reasonable modifications or additions to the KWSC System or the CTWSC Existing System that create additional capacity or cost savings for either Party.

"Kallman Estimate" means Steven D. Kallman's October 6, 2004 Project Cost Estimate attached hereto as **Exhibit B**.

"KWSC Current Debt Service" means the debt service on KWSC USDA-RD Loan 91-06 and USDA-RD Loan 91-07.

"KWSC Energy Cost" means, upon closing of the Agreement for Sale, certain amounts paid by KWSC for electrical energy relating to the State Highway 195 Pump Station as defined in Section 3.5.D.1. Energy costs agreed by the Parties for Improvements as set forth in Section 3.1.C shall be billed and adjusted pursuant to Section 3.5.D.1.

"KWSC Existing System" means the KWSC Transmission Line (commencing at the Ivy Mountain Tank Outlet), the KWSC System Junction, the KWSC North Transmission Line to Lampasas, the KWSC South Transmission Line to Lampasas, the Hewgley 2.0 Tank, the Hewgley 0.25 Tank, the Georgetown Road Tank, the Donnell Tank, and the KWSC Pump Station.

"KWSC New Facilities" means new facilities that KWSC proposes as of the date of this Contract and/or thereafter to construct, including a new raw water intake structure, raw water line, water treatment plant and transmission line that is proposed to connect to the State Highway 195 Pump Station.

"KWSC North Transmission Line to Lampasas" means that existing transmission line, consisting of 24-inch piping, 20-inch piping, and 18-inch piping, generally located in the rights-of-way of F.M. 2313 and F.M. 580 and transporting water from the KWSC System Junction to a metering station located on F.M. 580 northeast of the City, as shown on the System Map.

"KWSC Operation and Maintenance Cost" or "KWSC O&M Cost" means the costs defined in Section 3.5.B.1.

"KWSC Pump Station Site" means the location of the former water pumping station located on KWSC property within the City of Kempner, as shown on the System Map.

"KWSC Purchased Facilities" means the facilities serving both Parties and included in the Subject Water System described in the Agreement for Sale, including the State Highway 195 Pump Station, the 2,000,000 gallon tank at the State Highway 195 Pump Station, the transmission line from the State Highway 195 Pump Station to Ivy Mountain Tank, and the Ivy Mountain Tank.

"KWSC South Transmission Line to Lampasas" means that existing transmission line, consisting of 24-inch piping and 20-inch piping, generally located in the right-of-way of U.S. Highway 190 and transporting water from the KWSC System Junction to a metering station located on U.S. Highway 190 east of the City, as shown on the System Map.

"KWSC System" means the KWSC Existing System and, upon closing of the Agreement for Sale and acquisition of the Subject Water System thereunder, the KWSC Purchased Facilities.

"KWSC System Component" means each individual component of the KWSC Existing System and, upon closing of the Agreement for Sale, the KWSC Purchased Facilities.

"KWSC System Junction" means the point in the City of Kempner where the KWSC Transmission Line, the KWSC South Transmission Line to Lampasas, and the KWSC North Transmission Line to Lampasas meet, as shown on the System Map.

"KWSC Transmission Line" means the existing transmission line, consisting of 30-inch and 27-inch piping, transporting water from the Ivy Mountain Tank Outlet to the KWSC System Junction, as shown on the System Map.

"MGD" means million gallons of water over a daily period of twenty-four (24) hours.

"Pipeline Capacity" means the quantity of water in MGD passing through a section of pipeline with a specific cross-sectional area (A) at a specific, velocity (V).

"Points of Delivery" means the two points designated in this Contract where water delivered by KWSC to the City will be metered. At this time it means at the existing two meters located on F.M. 580 northeast of the City and on U.S. Highway 190 east of the City, as shown on the System Map.

"Reserved Capacity" means capacity in treatment, storage, and transmission in raw water lines, treated water lines, tanks and pumps that a Party has reserved pursuant to this Contract. Reserved Capacity does not confer rights of ownership on the Parties.

"Roming Report" means that engineering report dated February 1999 prepared by Roming, Parker & Kasberg, L.L.P., consulting engineers in Temple, Texas, entitled *The Evaluation and Analysis of Central Texas Water Supply Corporation Facilities*.

"State Highway 195 Pump Station" means the facilities located on the State Highway 195 Pump Station site shown on the System Map and includes, without limitation, the 2.0 million gallon storage tank, pumps, pump stations, pipes, valves, buildings, structures, foundations, fencing, towers, water mains, distribution lines, equipment, facilities, electrical connections, lighting, meters, meter vaults, motors, conduits, transformers, generators, hardware, input lines from the CTWSC System, output lines to the Ivy Mountain Tank Site, yard piping, utility lines, utility facilities and improvements, street and drainage improvements, and all infrastructure at the site used for storage, distribution and transportation of water.

"State Highway 195 Pump Station Capacity" means the maximum continuous water measured in gallons per minute which can be pumped from the station when the associated ground storage tank from which the pumps take suction is at its lowest acceptable level, the largest single pump is out of service and the pressure at the discharge point of the pump is at maximum design pressures (i.e., the design assumes the Ivy Mountain tank is full).

"State Highway 195 Pump Station Tank means the existing 2,000,000 gallon tank at the State Highway 195 Pump Station.

"Stillhouse" means Stillhouse Hollow Reservoir.

"Stored Water" means raw water in Stillhouse Hollow Reservoir.

"System Map" means the map attached hereto as **Exhibit A**.

"TCEQ" means the Texas Commission on Environmental Quality or any successor entity thereto.

"TWDB" means the Texas Water Development Board or any successor entity thereto.

"TWDB Loan" means one or more loans from TWDB with proceeds of approximately \$33,000,000.00, pursuant to a TWDB loan commitment which will expire on November 30, 2006, to provide the necessary funding for KWSC to (i) construct a water treatment plant and related facilities; (ii) purchase certain facilities from CTWSC, which purchase includes paying to USDA-RD an amount necessary to prepay the outstanding balance of CTWSC USDA-RD Loan 91-06 as set out in the Agreement for Sale; and (iii) prepay the outstanding balance of KWSC USDA-RD Loan 91-07 and all other outstanding KWSC indebtedness to USDA-RD.

"TWDB Loan 1" means a TWDB Loan with proceeds of approximately \$8.5 million (of the \$33,000,000.00 as defined in TWDB Loan) which is the anticipated source for prepayment of CTWSC USDA-RD Loan 91-06 and KWSC USDA-RD 91-07, the current principal balances of which are approximately \$3,081,000 and \$2,215,540 respectively (the final principal balance amounts upon prepayment shall be included in the amortization schedules to be attached as **Exhibit C** hereto).

"TWDB Loan 2" means a TWDB Loan with proceeds of approximately \$24.5 million (of the \$33,000,000.00 as defined in TWDB Loan) from the Rural Water Assistance Funds, for, among other things, construction of the KWSC New Facilities.

"USDA-RD" means the United States Department of Agriculture-Rural Development or any successor entity thereto.

1.2 Construction

A. General. Unless the context requires otherwise, words of the masculine gender shall be construed to include correlative words of the feminine and neuter genders and vice versa, and words of singular number shall be construed to include correlative words of plural number and vice versa. This Contract and all the terms and provisions hereof shall be constructed to effectuate the purposes set forth herein and to sustain the validity of this Contract.

B. Effect of Reservation of Capacity. Capacity Reservation in this Contract is not intended, and shall not be construed, to convey an ownership interest in the structures or facilities.

C. Compliance with Regulations. The terms of this Contract shall be construed so as to comply with all applicable laws and rules, including without limitation the rules of USDA-RD.

D. Effect of Agreement for Sale. The Parties acknowledge and agree that the rights and obligations of CTWSC and KWSC under the Agreement for Sale are contingent upon conditions set forth in Article IV thereof and that certain of such contingencies are not within KWSC's control. The Parties agree that this Contract shall be effective upon the terms set forth herein irrespective of the status of the Agreement for Sale.

1.3 Closing of Transactions in Agreement for Sale

A. Under the Agreement for Sale, KWSC proposes to acquire certain CTWSC facilities called therein the "Subject Water System." The Subject Water System includes the State Highway 195 Pump Station Site, the transmission line (including easements) connecting the State Highway 195 Pump Station site to the Ivy Mountain Tank site, and the Ivy Mountain Tank, site, with related real property and improvements, as shown on the System Map, and as further defined and described in the Agreement for Sale. The 2001 Contract reserved to the City certain storage, pumping and transmission capacities in components of the Subject Water System including the State Highway 195 Pump Station and 2,000,000 gallon storage tank; the transmission line from State Highway 195 Pump Station site to the Ivy Mountain tank site, and the Ivy Mountain Tank.

B. Upon closing of the Agreement for Sale, KWSC will purchase the Subject Water System, and as part of the purchase, funds from TWDB Loan 1 will be used for CTWSC to prepay CTWSC USDA-RD Loan 91-06 pursuant to the Agreement for Sale. KWSC will tender prepayment for KWSC USDA-RD Loan 91-07 pursuant to Section 3.4.C., The principal balances of both loans will be refinanced by proceeds of TWDB Loan 1. KWSC shall provide the City with copies of the closing documents for the Agreement for Sale and for the closing of TWDB Loan 1. KWSC shall provide amortization schedule(s) for the TWDB-refinanced principal balances of CTWSC USDA-RD Loan 91-06 and KWSC USDA-RD Loan 91-07 for the City's reference and for use in calculation of the Adjusted CTWSC Debt Service and Adjusted KWSC Debt Service hereunder. The amortization schedule(s) shall be attached hereto for reference as **Exhibit C**.

C. Billing changes upon closing of Agreement for Sale: Upon closing of the Agreement for Sale,

1. The City's monthly invoice for CTWSC Treated Water Cost will exclude the Energy Costs and CTWSC O&M Expense related to the KWSC Purchased Facilities.

Instead, KWSC shall bill KWSC Energy Cost and KWSC O&M Cost separately for the KWSC Purchased Facilities as set forth in Section 3.5.

2. The City's monthly invoice for CTWSC and KWSC Debt Service will exclude monthly payments toward debt service for CTWSC USDA-RD Loan 91-06 and KWSC USDA-RD Loan 91-07. Instead, the City will be billed, on the same schedule as KWSC pays its debt service to TWDB, whether monthly, semi-annually or annually, for payments towards debt service on the TWDB-refinanced principal balances of CTWSC USDA-RD Loan 91-06 and KWSC USDA-RD Loan 91-07.

3. Within 90 days after the Contract Date, the Parties shall meet to develop a mutually agreed bill format.

ARTICLE II. REPRESENTATIONS AND WARRANTIES

2.1 Representations and Warranties of KWSC

KWSC hereby represents and warrants that this Contract has been or will be duly executed by the Parties hereto and that thereafter the Contract will be in full force and effect upon written notification of concurrence by USDA-RD; that KWSC has full power and authority to sell and convey treated water to the City in accordance with the terms of this Contract; that KWSC has rights to Stored Water in Stillhouse in a sufficient amount to supply the treated water that KWSC requires to meet its needs; and that the execution and delivery of this Contract by KWSC and the performance by KWSC of the provisions hereof do not and will not conflict with or constitute on the part of KWSC a breach or a default of any provision of any other contract or agreement of KWSC.

2.2 Representations and Warranties of the City

The City hereby represents and warrants that this Contract has been or will be duly executed by the Parties hereto and that thereafter the Contract will be in full force and effect upon written notification of concurrence by USDA-RD; that the City has full power and authority to purchase treated water from KWSC in accordance with the terms of this Contract; that the City has rights to Stored Water in Stillhouse in a sufficient amount to supply the treated water that the City requires to meet its needs; and the execution and delivery of this Contract by the City and the performance by the City of the provisions hereof do not and will not conflict with or constitute on the part of the City a breach or a default of any provision of any other contract or agreement of the City.

ARTICLE III.
SALE AND PURCHASE OF TREATED WATER;
OPERATING REQUIREMENTS

3.1 Water Conveyance

A. Reserved Water Treatment Plant Capacity. Pursuant to the CTWSC Wholesale Contract, 7.68 MGD of the Water Treatment Plant Capacity is reserved to KWSC. The Parties agree that 4.84 MGD of the 7.68 MGD of Water Treatment Plant Capacity reserved to KWSC pursuant to the CTWSC Wholesale Contract is reserved to the City; provided, however, that 1.06 MGD of the 4.84 MGD of Water Treatment Plant Capacity reserved to the City by this Contract is reserved subject to (i) the City's payment in full of the amounts toward CTWSC and KWSC debt service described in Section 3.4 of this Contract and (ii) the City's agreement to allow KWSC to use this capacity on an interim basis in accordance with the terms and conditions set forth in Section 3.2 of this Contract. The remaining 2.84 MGD of Water Treatment Plant Capacity remains reserved to KWSC. Neither Party shall use the other's reserved capacity without permission.

B. Reserved Storage and Transmission Capacity.

1. CTWSC Transmission Capacity. The Parties agree that the City shall be entitled to delivery of treated water at Ivy Mountain Tank in amounts up to the City's reserved pipeline capacity (6.9 MGD) from Doc Curb's Place to the Ivy Mountain Tank. Pursuant to the CTWSC Wholesale Contract, KWSC contracted with CTWSC to divert, treat and deliver treated water in quantities required by KWSC up to a maximum of 7.68 MGD, and CTWSC must deliver such water (up to 7,000 GPM) to KWSC at the metered outlet at the Ivy Mountain Tank Site. KWSC shall deliver to the City, at the metered outlet at the Ivy Mountain Tank Site, up to 6.9 MGD (4792 GPM) of treated water, as follows (the foregoing in no way is intended to create an additional "Point of Delivery" or to change the defined Points of Delivery):

a. As of the Effective Date, the City's current reserved capacity in the CTWSC Water Treatment Plant is 4.84 MGD. At such time as the City desires to receive delivery in excess of 4.84 MGD of treated water at the metered outlet of the Ivy Mountain Tank Site, the City shall provide notice to KWSC that it requests additional water treatment capacity, in an amount up to 2.06 MGD. The City shall demonstrate financial capability pursuant to Section 3.1.C. Within 30 months of receipt of the City's notice, KWSC shall provide the requested additional water treatment capacity, up to 2.06 MGD, from CTWSC, so that the City has a total of up to 6.9 MGD in water treatment plant capacity. The City shall pay the reasonable costs of the added capacity, as follows (i) the lower of (a) the capital cost of the additional water treatment plant capacity above 4.84 MGD, or (b), if the additional capacity comes from KWSC's reserved capacity in the CTWSC WTP, the price pursuant to the right of first refusal set forth in Section 3.1.D hereof; (ii) energy costs attributable to the added capacity; and (iii) additional O&M costs as defined and calculated hereunder on a volume basis only (not subject to a floor) which are attributable to the added capacity, but the City shall not be required to pay any costs for added pipeline capacity to assure delivery to the City of up to 6.9 MGD from the CTWSC

From: Antick III
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Water Treatment Plant to Ivy Mountain Tank. At KWSC's option, KWSC may provide the added water treatment plant capacity from its water treatment plant instead of from CTWSC, with the City to pay the reasonable costs as set forth above, but in no event shall the City's costs include any costs for added pipeline capacity to the metered outlet, whether that outlet be at the 195 Pump Station Tank Site or at the Ivy Mountain Tank Site. In the event the City seeks more than 6.9 MGD of water treatment capacity, the City shall pay the cost of any additional pipeline capacity needed (above 6.9 MGD).

b. The Parties recognize that despite added treatment capacity for the City hereunder, and the provisions of Section 3.1.B.1 above, delivery of treated water to the City Points of Delivery above the City's initial Maximum Rate of Delivery (3.51 MGD) may also require the City to improve the State Highway 195 Pump Station as set forth in Section 3.9.A or require either or both Parties to provide other Improvements.

c. In the event the Agreement for Sale closes, KWSC shall continue to provide the following reserved capacities to the City: The Pipeline Capacity of the CTWSC West System from State Highway 195 Pump Station to Ivy Mountain Tank is 12.18 MGD. The Parties agree that 6.9 MGD of the Pipeline Capacity in the CTWSC West System from the State Highway 195 Pump Station to the Ivy Mountain Tank is reserved to the City and shall be used by no other entity or customer. The remaining Pipeline Capacity (5.28 MGD) is reserved to KWSC. Neither Party shall use the other's reserved capacity without permission.



2. KWSC Transmission Capacity

a. KWSC Transmission Line The Pipeline Capacity of the KWSC Transmission Line will be determined at a water velocity not to exceed six (6) FPS, which results in a capacity of 19.03 MGD in the 30-inch piping and 15.42 MGD in the 27-inch piping. The Parties agree that 11.99 MGD of the Pipeline Capacity in the 30-inch piping and 9.71 MGD of Pipeline Capacity in the 27-inch piping of the KWSC Transmission Line is reserved to the City. The remaining Pipeline Capacity in the 30-inch piping (7.04 MGD) and the 27-inch piping (5.71 MGD) of the KWSC Transmission Line is and reserved to KWSC. Neither Party shall use the capacity reserved to the other without permission.

b. KWSC North Transmission Line to Lampasas The Pipeline Capacity of the KWSC North Transmission Line to Lampasas will be determined at a water velocity not to exceed six (6) FPS, which results in a capacity of 12.18 MGD in the 24-inch piping, 8.46 MGD in the 20-inch piping, and 6.85 MGD in the 18-inch piping. The Parties agree that 7.67 MGD of the Pipeline Capacity in the 24-inch piping, 5.33 MGD in the 20-inch piping, and 4.32 MGD in the 18-inch piping in the KWSC North Transmission Line to Lampasas is reserved to the City. The remaining Pipeline Capacity in the 24-inch piping (4.51 MGD), the 20-inch piping (3.13 MGD), and the 18-inch piping (2.53 MGD) in the KWSC North Transmission Line to Lampasas remains reserved to KWSC. Neither Party shall use the capacity reserved to the other without permission.

c. KWSC South Transmission Line to Lampasas The Pipeline Capacity of the KWSC South Transmission Line to Lampasas will be determined at a water velocity not to exceed six (6) FPS, which results in a capacity of 12.18 MGD in the 24-inch piping and 8.46 MGD in the 20-inch piping. The Parties agree that 7.67 MGD of the Pipeline Capacity in the 24-inch piping and 5.33 MGD of the Pipeline Capacity in the 20-inch piping is reserved to the City. The remaining Pipeline Capacity in the 24-inch piping (4.51 MGD) and the 20-inch piping (3.13 MGD) in the Kempner South Transmission Line to Lampasas remains reserved to KWSC. Neither Party shall use the capacity reserved to the other without permission.

3. Reserved Storage Capacity

a. CTWSC Storage Capacity Until closing of the Agreement for Sale, 90 percent of the Effective Water Storage Tank Capacity of the 2 million gallon tank at the State Highway 195 Pump Station is reserved to KWSC. The Parties agree that 63 percent of the 90 percent of the Effective Water Storage Tank Capacity of the 2 million gallon tank at the State Highway 195 Pump Station reserved to KWSC shall be reserved and made available to the City. The remaining 37 percent of the 90 percent of the Effective Water Storage Tank Capacity of the 2 million gallon tank at the State Highway 195 Pump Station remains reserved to KWSC. Upon closing of the Agreement for Sale, KWSC shall continue to reserve to the City 63 percent of 90 percent of the Effective Water Storage Tank Capacity of the 2 million gallon tank at the State Highway 195 Pump Station, or 1,134,000 gallons. The remaining capacity, or 866,000 gallons, shall be reserved to KWSC.

Until closing of the Agreement for Sale, 95 percent of the Effective Water Storage Tank Capacity in the Ivy Mountain Tank is reserved to KWSC. The Parties agree that 63 percent of the 95 percent of the Effective Water Storage Tank Capacity in the Ivy Mountain Tank reserved to KWSC pursuant to the CTWSC Wholesale Water Supply Contract shall be reserved and made available to the City. The remaining 37 percent of the 95 percent of the Effective Water Storage Tank Capacity in the Ivy Mountain Tank remains reserved to KWSC. Upon closing of the Agreement for Sale, KWSC shall continue to reserve to the City 63 percent of 95 percent of the Effective Water Storage Tank capacity in the Ivy Mountain Tank, or 1,197,000 gallons. The remaining capacity, or 803,000 gallons, shall be reserved to KWSC.

Neither Party shall use the capacity reserved to the other without permission. KWSC and the City recognize that unless and until the transaction set forth in the Agreement for Sale closes, the operation and control of the water level and capacity in these tanks is the responsibility of CTWSC and beyond the control of KWSC.

b. KWSC Storage Capacity

The Parties agree that the capacity of the following KWSC System Components is reserved to each Party as set forth below:

<u>Tank Name</u>	<u>Maximum Capacity</u>	<u>KWSC Capacity</u>	<u>City Capacity</u>
Hewgley 2.0	2,000,000 gallons	0 gallons	2,000,000 gallons
Hewgley 0.25	250,000 gallons	92,000 gallons	158,000 gallons
Georgetown Road	2,000,000 gallons	740,000 gallons	1,260,000 gallons
Donnell	2,000,000 gallons	2,000,000 gallons	0 gallons

Reserved Pump Station Capacity Prior to improvements made in 2003 which were financed by KWSC, the State Highway 195 Pump Station had an actual pumping capacity for placing water into the Ivy Mountain Tank, when it is full, at 4,300 gallons per minute ("GPM"), or 6.19 MGD, of which KWSC had reserved 5.57 MGD of reserved capacity. The Parties agree that 3.51 MGD of capacity in the State Highway 195 Pump Station shall be reserved to and made available to the City. Neither Party shall use the other's reserved capacity without permission.

C. Improvements.

1. CTWSC Existing System. KWSC has the right to request that CTWSC make Improvements to the CTWSC Existing System for the benefit of KWSC. KWSC will give the City reasonable written notice of any Improvements that KWSC plans to request CTWSC to make to the CTWSC Existing System. The written notice shall describe, in general terms, the nature, location, and timing of the Improvements that KWSC is planning to request. Reasonable notice shall mean not less than 90 days written notice unless: (i) an emergency requires KWSC to request CTWSC to make Improvements to the CTWSC Existing System within a shorter time period or (ii) CTWSC requires KWSC to make a request for CTWSC to make Improvements to the CTWSC Existing System within a shorter time period. Within 60 days of its receipt of such written notice from KWSC, the City has the right to request in writing that the Improvements that KWSC plans to request that CTWSC make to the CTWSC Existing System also provide a specific amount of additional capacity for the benefit of the City. If KWSC receives such a written request from the City, KWSC will include the amount of additional capacity requested by the City in KWSC's request to CTWSC for Improvements; however, KWSC shall have no obligation to make any changes to the nature, location, or timing of KWSC's requested Improvements. In addition, the City may request in writing that KWSC request CTWSC to make Improvements to the CTWSC Existing System for the benefit of the City as separate Improvements. If so, KWSC shall make such a request to CTWSC and, for each Improvement so constructed, shall request that CTWSC cause to be prepared as-built drawings and engineering reports providing (at a minimum) a narrative description of the Improvement, with this report to be kept on file at the CTWSC administrative offices, as provided in the CTWSC Wholesale Contract. The City's written request shall specify the nature and location of the Improvements requested, the proposed timing of the construction of the Improvements, and the requested additional capacity to be provided by the Improvements. The City shall be responsible for providing all information, financing, and other requirements needed by CTWSC prior to making Improvements for the City.

The City shall pay its share of all costs associated with the Improvements to the CTWSC Existing System for the benefit of the City including, without limitation, increased operation and maintenance expenses, cost of water and debt service. KWSC shall pay its share of all costs associated with the Improvements to the CTWSC Existing System for the benefit of KWSC including, without limitation, increased operation and maintenance expenses, cost of water and debt service. Unless the Parties agree in writing to a different methodology for the payment of such costs, KWSC may, from time to time, submit invoices to the City for the amounts due under this section. Each such invoice shall include documentation supporting the amount due. The City shall pay KWSC the amount due within 30 days of the receipt of an invoice. Capacity created by the Improvements to the CTWSC Existing System for the benefit of the City shall be reserved to the City, and capacity created by the Improvements to the CTWSC Existing System for the benefit of KWSC shall be reserved to KWSC; neither Party shall use capacity reserved to the other without permission.

2. KWSC System. KWSC has the right to make Improvements to the KWSC System (which includes, upon closing of the Agreement for Sale, the KWSC Purchased Facilities), including without limitation parallel new pipelines, for the benefit of KWSC. Upon request, KWSC shall provide as-built drawings of improvements and upgrades to the KWSC System (City to pay the reasonable cost thereof). KWSC shall give the City reasonable written notice of any Improvements that KWSC plans to make to the KWSC System. The written notice shall describe, in general terms, the nature, location, and timing of the Improvements that KWSC is planning. Reasonable notice shall mean not less than 90 days written notice unless an emergency requires KWSC to make Improvements to the KWSC System within a shorter time period. Within 60 days of its receipt of written notice from KWSC, the City has the right to request that the Improvements that KWSC plans to make to the KWSC System also provide a specific additional amount of capacity for the benefit of the City. If KWSC receives such a written request from the City, and the City provides KWSC with evidence of its financial ability to participate in engineering cost of the proposed Improvements, upon demonstration by the City of its ability to pay for its share in the proposed Improvements, KWSC will include the additional capacity requested by the City in the Improvements KWSC makes to the KWSC System; however, KWSC shall have no obligation to make any changes to the nature, location, or timing of KWSC's proposed Improvements.

In addition, the City may request that KWSC make Improvements to the KWSC System for the benefit of the City as separate Improvements. The City's written request shall specify the nature and location of the Improvements requested, the proposed timing of the construction of the Improvements, and the requested additional capacity to be provided by the Improvements. Neither Party shall have the right to unilaterally modify the KWSC System so that the KWSC System's maximum deliverable capacity is reached. If the City requests that KWSC make any Improvements to the KWSC System, then KWSC shall engage the services of a registered engineer to produce the engineering design, including detailed plans and specifications, for the Improvements in conformance with good engineering practices and the TCEQ design criteria and construction standards. The plans and specifications shall specify the sizing, routing, materials selection, cost projections, proposed construction schedule, easements, and anticipated capacity

of the Improvements. The plans and specifications shall be submitted to the City for review and approval. KWSC may propose reasonably practicable modifications or alternatives to the proposed Improvements which timely provide the requested additional capacity at reasonable cost prevailing in the industry for such Improvements. Any dispute between the parties concerning the proposed Improvements shall be resolved under Section 4.4. If the City is to be a contracting Party, KWSC shall solicit and publish invitations for bids and award the construction contract to the lowest responsible bidder to the extent required by law. KWSC shall be responsible for obtaining all required permits, consents, easements, inspections, tests and authorizations necessary for the construction, and for monitoring the activities of the construction contractor and day-to-day progress of construction to encourage the timely and efficient completion. KWSC shall review all change orders to the construction contracts and shall submit to the City for review and approval any change orders that result in increased costs to the City and shall prohibit work on change orders that the City has not approved unless required for an emergency.

The City shall pay all costs associated with Improvements to the KWSC System for the benefit of the City including, but not limited to, all costs reasonably and necessarily incurred for design, engineering, construction, easements, permits, consents, authorizations, surveys, tests, inspections, and financing of such Improvements. Increased operation and maintenance costs of such Improvements shall be billed pursuant to Section 3.5.C.1. The Parties shall agree in advance of construction of Improvements as to the defined energy costs, if any, of such Improvements, and such energy costs shall be billed pursuant to Section 3.5.C.1. For costs other than energy costs and O&M costs associated with such Improvements KWSC shall, unless the Parties agree in writing to a different methodology for the payment of costs, submit invoices to the City for amounts due under this section. Each such invoice shall include documentation supporting the amount due. The City shall pay KWSC the amount due within 30 days of receipt of an invoice. KWSC shall pay all costs associated with the Improvements to the KWSC System for the benefit of KWSC including, but not limited to, all costs reasonably and necessarily incurred for design, engineering, construction, easements, permits, consents, authorizations, surveys, tests, inspections and financing of such Improvements, as well as any increased operation and maintenance costs of such Improvements. Capacity created by the Improvements to the KWSC System for the benefit of the City shall be reserved to the City, and capacity created by the Improvements to the KWSC System for the benefit of KWSC shall be owned by and reserved to KWSC.

Notwithstanding the foregoing cost provisions, the Parties may mutually determine the manner and extent to which an Improvement may be funded through the Joint Use Facilities System Account.

3. KWSC New Facilities. KWSC shall give the City reasonable written notice of any Improvements that KWSC plans to make to the KWSC New Facilities. The written notice shall describe, in general terms, the nature, location, and timing of the Improvements that KWSC is planning. Reasonable notice shall mean not less than 90 days written notice unless an emergency requires KWSC to make Improvements to the KWSC New

Facilities within a shorter time period. Within 60 days of its receipt of written notice from KWSC, the City may request that the Improvements that KWSC plans to make to the KWSC New Facilities also provide a specific additional amount of capacity for the benefit of the City. If KWSC receives such a written request from the City and the City provides KWSC with evidence of its financial ability to participate in engineering cost of the proposed Improvements, upon demonstration by the City of its ability to pay for its share in the proposed Improvements, KWSC may include the additional capacity requested by the City in the Improvements KWSC makes to the KWSC New Facilities; however, KWSC shall have no obligation to make any changes to the nature, location, or timing of KWSC's proposed Improvements. The City may also request that KWSC make Improvements to KWSC New Facilities for the City's benefit; in the event that KWSC agrees to make such improvements, the procedures applicable to costs of Improvements to the KWSC System set forth in subsection a. above shall apply to costs of Improvements to the KWSC New Facilities. Upon request, KWSC shall provide information (including copies of plans and specifications) to the City, describing the KWSC New Facilities and proposed operation thereof.

D. Right of First Refusal

1. Parties' Stored Water and/or Capacity. The City agrees that in the event that it has excess Stored Water or reserved capacity that it desires to relinquish or sell, KWSC shall have an absolute right of first refusal as to any such excess Stored Water or capacity. The City shall offer such Stored Water and/or capacity to KWSC in writing. The City's written offer shall set forth the terms and conditions upon which the City proposes or intends to propose to sell such Stored Water and/or capacity to any third Party. KWSC will have 60 days from the date of the City's written offer to accept such offer in writing. If KWSC does not accept the City's offer within 60 days of the date of such offer, then the City may sell such Stored Water and/or capacity to a third Party upon the same terms and conditions. If the terms and conditions of sale change during negotiations with KWSC or any third Party, KWSC retains the right of first refusal on any new terms and conditions. KWSC agrees that in the event that it has excess Stored Water or reserved capacity that it desires to relinquish or sell, the City shall have an absolute right of first refusal as to any such excess Stored Water or capacity. KWSC shall offer such Stored Water and/or capacity to the City in writing. KWSC's written offer shall set forth the terms and conditions upon which KWSC proposes or intends to propose to sell such Stored Water and/or capacity to any third Party. The City will have 60 days from the date of KWSC's written offer to accept such offer in writing. If the City does not accept KWSC's offer within 60 days of the date of such offer, then KWSC may sell such Stored Water and/or capacity to a third Party upon the same terms and conditions. If the terms and conditions of sale change during negotiations with the City or any third Party, the City retains the right of first refusal on any new terms and conditions.

2. Third Parties' Stored Water and/or Capacity. The City agrees that in the event that a third Party offers the City Stored Water or reserved capacity in the CTWSC Existing System, within 10 days of the receipt of such offer, the City shall give KWSC written

notice of the terms and conditions upon which the third Party has offered to sell the City such Stored Water or reserved capacity and offer any excess Stored Water or reserved capacity which the City does not intend to buy to KWSC. KWSC will have 30 days from the date of the written notice to notify the City in writing that it would like to purchase all or part of the excess Stored Water and/or capacity on such terms and conditions. KWSC agrees that in the event that a third Party offers KWSC Stored Water or reserved capacity in the CTWSC Existing System, within 10 days of the receipt of such offer, KWSC shall give the City written notice of the terms and conditions upon which the third Party has offered to sell KWSC such Stored Water or reserved capacity and offer any excess Stored Water or reserved capacity which KWSC does not intend to buy to the City. The City will have 30 days from the date of the written notice to notify KWSC in writing that it would like to purchase all or part of the excess Stored Water and/or capacity on such terms and conditions.

E. Increased or Decreased Capacity

1. CTWSC Existing System. If KWSC's reserved capacity in any CTWSC System Component is reduced below the amount set forth in this Contract, without any fault or procurement by KWSC, then the City and KWSC will each bear a pro rata reduction in their respective reserved capacities in such CTWSC System Component. If KWSC's reserved capacity in any CTWSC System Component is increased above the amount set forth in this Contract by a re-rating of the capacity of such Component, then the City and KWSC will each receive a pro rata increase in their respective reserved capacities in such CTWSC System Component. For purposes of this subsection, a Parties' pro rata share is determined by dividing the capacity reserved to that Party in that CTWSC System Component by the total capacity reserved to both KWSC and the City in that CTWSC System Component. This provision does not apply to any additional capacity that KWSC or the City obtains through the construction of Improvements or by negotiation with or purchase from CTWSC (or its members), which capacity is reserved to the Party that paid for or purchased the reserved capacity.

2. KWSC System. If the capacity in any KWSC System Component is reduced below the amount set forth in this Contract, without any fault or procurement by KWSC, then the City and KWSC will each bear a pro rata reduction in their respective reserved capacities in such KWSC System Component. If the capacity in any KWSC System Component is increased above the amount set forth in this Contract by a re-rating of the capacity of such Component, then the City and KWSC will each receive a pro rata increase in their respective reserved capacities in such KWSC System Component. For purposes of this subsection, a Party's pro rata share is determined by dividing the capacity reserved to that Party in that KWSC System Component by the total capacity reserved to both KWSC and the City in that KWSC System Component. This provision does not apply to any additional capacity that KWSC or the City obtains through the construction of Improvements or by negotiation with or purchase from CTWSC (or its members), which capacity is reserved to the Party that paid for or purchased the reserved capacity.

F. Modifications Required by Others. In the event that modifications to KWSC System Components are required by governmental agencies (including, without limitation, Texas Department of Transportation or a county having jurisdiction) or regulations outside the control of either Party, then KWSC's share of the reasonable and necessary costs for such modifications shall be shared proportionately by both Parties in accordance with each Party's pro rata share of reserved capacity in that Component. KWSC shall provide reasonable notice to the City when a governmental agency requests a modification, and shall provide the City with an estimate of the costs of such modification for the City to be used by the City for planning purposes only. .

3.2 Conditions for Temporary Use of City Water Treatment Plant Capacity

A. Until December 31, 2008. KWSC shall be entitled to use 1.06 MGD of Water Treatment Plant Capacity reserved to the City under Section 3.1.A until December 31, 2008. In return for the right to temporarily use 1.06 MGD of the City's Water Treatment Plant Capacity, the Parties' percentage of the CTWSC Current Debt Service under Section 3.3 shall be temporarily reapportioned, as well as the Parties' percentage of the CTWSC O&M "Floor" under Section 3.5.B. From the Contract Date and for so long as KWSC is entitled to use 1.06 MGD under this Section, the City shall be obligated to pay an amount equal to 49 percent (instead of 63 percent) of the CTWSC Debt Service associated with the Water Treatment Plant, and an amount equal to 63 percent of the remaining CTWSC Current Debt Service; KWSC shall be obligated to pay 51 percent of the CTWSC Current Debt Service associated with the Water Treatment Plant and 37 percent of the remaining CTWSC Current Debt Service. KWSC shall give the City at least 60 days written notice of the date that KWSC intends to relinquish its right to use all of the 1.06 MGD of City Water Treatment Plant Capacity. On the date that KWSC relinquishes all rights to use of the 1.06 MGD, the percentages of the CTWSC Current Debt Service shall be reapportioned as set forth in Section 3.4. KWSC shall take all reasonable steps to ensure that KWSC ceases to use the 1.06 MGD of Water Treatment Plant Capacity on or before December 31, 2008. If, on June 30, 2008, KWSC is still using all or any part of the 1.06 MGD of Water Treatment Plant Capacity, then, on that date, KWSC shall provide the City with a written update on KWSC's plan to cease using the 1.06 MGD of Water Treatment Plant Capacity on or before December 31, 2008. The Parties may mutually agree to extend KWSC's ability to use this 1.06 MGD of the City's Water Treatment Plant Capacity, one year at a time, for a total of up to three additional years after December 31, 2008, or until December 31, 2011, by a written agreement providing a one-year extension, which shall be executed by the Parties at least 60 days in advance of December 31 of the year in which this temporary use of the 1.06 MGD is due to expire.

B. Support for Additional Capacity. The Parties acknowledge that each Party may seek to obtain additional capacity in the CTWSC System in the future. Each Party agrees to fully cooperate with the other Party's reasonable efforts to obtain additional capacity in the CTWSC System.

3.3 Payment of Stored Water

The City shall be responsible for all fees and payments required by BRA to secure, hold and assign its Stored Water. KWSC shall be responsible for all fees and payments required by BRA to secure, hold and assign its Stored Water.

3.4 City Payments Related to Facility Construction

A. City Payments Related to CTWSC Facilities Except during times that KWSC has the right to temporarily use the City's Water Treatment Capacity under Section 3.2, the City shall pay to KWSC on a monthly basis an amount equal to 63 percent of the CTWSC Current Debt Service, i.e., (i) an amount equal to 63% of KWSC's ten percent share of the payments then being made on CTWSC USDA-RD Loan 91-01 and (ii) an amount equal to 63% of KWSC's 90 percent share of the payments then being made on CTWSC USDA-RD Loan 91-06. As an example, for April 2006, such payments by KWSC were respectively \$939.00 and \$22,324.00, and City payments would be \$591.57 and \$14,064.12 (assuming no reduction as provided in Section 3.2.A). During times that KWSC has the right to use the City's Water Treatment Plant Capacity under Section 3.2, then the City's percentage of the CTWSC Current Debt Service for the Water Treatment Plant shall be reduced as provided in Section 3.2.A.

Adjusted CTWSC Debt Service: Upon prepayment of CTWSC USDA-RD Loan 91-06 as set forth in Section 3.4.C below, the City shall pay to KWSC 63% of Adjusted CTWSC Debt Service, as follows: (i) on a monthly basis, an amount equal to 63% of KWSC's ten percent share of the payments on CTWSC USDA-RD Loan 91-01 and (ii) an amount equal to 63% of 90 percent of the debt service on the principal balance of CTWSC USDA-RD Loan 91-06 upon its refinancing by TWDB with proceeds of TWDB Loan 1 in connection with KWSC's purchase of the Subject Water System, as shown on Exhibit C (the amortization schedule described in Section 1.3.B), on the same basis (whether annual, semi-annual or monthly) as KWSC pays the debt service on the refinanced principal balance.

B. City Payments Related to KWSC Facilities The City shall pay to KWSC on a monthly basis an amount equal to 63 percent of the KWSC Current Debt Service, i.e., an amount equal to 63% of the debt service then being paid on KWSC USDA-RD Loan 91-06 and KWSC USDA-RD Loan 91-07. As an example, for April 2006, such KWSC payments were respectively \$27,447.68 and \$17,600.00, and City payments would be \$17,292.03 and \$11,088.00. Adjusted KWSC Debt Service: Upon prepayment of KWSC USDA-RD Loan 91-07 as set forth in Section 3.4.C. below, the City shall pay to KWSC 63% of Adjusted KWSC Debt Service, as follows: (i) on a monthly basis an amount equal to 63% of the debt service on KWSC USDA-RD Loan 91-06 and (ii) an amount equal to 63% of the debt service on the principal balance of KWSC USDA-RD Loan 91-07 upon its refinancing by TWDB with proceeds of TWDB Loan 1, as shown on Exhibit C (the amortization schedule described in Section 1.3.B), on the same basis (whether annual, semi-annual or monthly) as KWSC pays the debt service on the refinanced principal balance.

C. Prepayment by KWSC of CTWSC and KWSC Current Debt Service KWSC applied for and received a loan commitment from TWDB in the amount of \$20,226,000.00, and

such loan commitment will expire on November 30, 2006. The purpose of the TWDB Loans is to provide the necessary funding for KWSC to: (i) construct a water treatment plant and related facilities; (ii) purchase certain facilities from CTWSC, which purchase includes paying to USDA-RD an amount necessary to prepay the outstanding balance of CTWSC's USDA-RD Loan 91-06 as set out in the Agreement for Sale; and (iii) prepay the outstanding balance of KWSC's USDA-RD Loan 91-07. TWDB Loan 1 is the anticipated source for prepayment of these two USDA-RD loans.

In order to secure for the Parties the benefit of lower interest rates, KWSC shall use its best efforts to close TWDB Loan 1 within 90 days following execution by the Parties of this Contract and a settlement agreement in a form satisfactory to TWDB. Within 45 days following receipt of the TWDB Loan 1 Proceeds, KWSC shall submit funds in an amount sufficient to prepay the remaining principal balance plus interest through the date of prepayment of KWSC USDA-RD Loan 91-07, which amount is approximately \$2,215,540 at this time. KWSC agrees it shall prepare and submit all necessary documentation to USDA-RD to facilitate prepayment of KWSC USDA-RD Loan 91-07.

In addition, within 45 days following receipt of the TWDB Loan 1 Proceeds and approval of USDA-RD of the Agreement for Sale, whichever occurs later, KWSC shall submit funds in the amount of the outstanding balance of CTWSC's USDA-RD Loan 91-06, which as of this date is approximately \$3,081,000, plus approximately \$2,254,577, the purchase price of the CTWSC facilities. KWSC agrees it shall prepare and submit all necessary documentation to CTWSC and USDA-RD to facilitate its purchase of the CTWSC facilities and prepayment of CTWSC Loan 91-06.

The City has no obligation to contribute funds toward the purchase price of the CTWSC facilities pursuant to the Agreement referenced above. KWSC will keep the City informed by quarterly written reports of its efforts to (i) close the TWDB Loan, (ii) close under the Agreement for Sale, and (iii) prepay KWSC USDA-RD Loan 91-07 and CTWSC USDA-RD Loan 91-06.

D. Prepayment by City or KWSC of Debt In the event KWSC reasonably decides that USDA-RD approval for prepayment of CTWSC USDA-RD Loan 91-06 and/or prepayment (and application of prepayment amounts) to KWSC USDA-RD Loan 91-07 cannot be obtained despite its best efforts, and in any event by 12 months following the Contract Date (unless a trend of rising interest rates in the bond market reasonably suggests an earlier deadline), Kempner will notify the City and afford the City the opportunity to meet and discuss procedures for the City to prepay its portion of the USDA-RD debt (including some or all of CTWSC and KWSC debt service) and/or for both Parties to take advantage of lower interest rates. The Parties agree to work in good faith to develop a mutually agreeable prepayment protocol so that the prepayment does not cause a hardship for either Party.

3.5 Payment of Treated Water Cost, CTWSC O&M Expense, KWSC O&M Cost, Tank Maintenance Cost, and CTWSC Capital Contribution Charge

The City shall pay to KWSC, on a monthly basis, the following:

A. Treated Water Cost: For each 1000 gallons of water delivered to the City at the City's Points of Delivery, the City shall pay the amount per 1000 gallons that KWSC pays to CTWSC as CTWSC Treated Water Cost, billed at the initial rate of \$.048 per 1000 gallons of treated water (such rate to be adjusted within 90 days of closing of the Agreement for Sale), being the same rate per 1000 gallons of treated water charged by CTWSC to KWSC during the month of January 2006 subject to annual adjustment as provided herein. As an example, using the amount for cost of water billed to KWSC by CTWSC in April 2006, or \$.36 per 1,000 gallons, the City (which was delivered 30,982,000 gallons of water in April 2006), would pay \$11,153.52, or \$.36 per 1,000 gallons, as cost of water for that month; the City's cost of water payment will vary with the cost of water and volume of water delivered to the City for a particular month. CTWSC Treated Water Cost shall be based upon (i) the actual calculated costs for chemicals and (ii) Energy Costs, including energy costs associated with pumping raw water, running equipment in the Water Treatment Plant, and pumping treated water to the Point of Delivery to KWSC. For purposes of the City's payment for treated water cost under this section, production costs charged to KWSC will be based on the metered usage of treated water by KWSC at the KWSC Point of Delivery, and will be prorated based on the annual number of gallons of treated water received by KWSC as a percentage of the total number of gallons of treated water received by all of CTWSC's customers. Payment by KWSC to CTWSC, and by the City to KWSC, of production costs will be based on an amount estimated monthly. The actual production cost attributable to KWSC, and to the City, will be verified and corrected at the end of the fiscal year of CTWSC. KWSC will receive either a refund or a bill from CTWSC as a result of any such correction, and each refund or bill will be itemized and will contain such explanatory notes and backup invoices, receipts and documentation as may be required in order to support the annual correction. KWSC will forward a copy of the refund or bill with attachments from CTWSC to the City. Within thirty days, KWSC shall conduct an audit of the amounts paid by the City as CTWSC Treated Water Cost in the preceding year. The City will then receive either a refund or a bill, and each refund or bill will be itemized and will contain such explanatory notes and backup invoices, receipts and documentation as may be required in order to support the annual correction. Upon closing of the Agreement for Sale, CTWSC Treated Water Cost shall not include Energy Costs for the KWSC Purchased Facilities which shall be separately billed as set forth in Section 3.5.C below.

B. CTWSC Operation and Maintenance Expenses

1. City Payment of CTWSC O&M Expense. The City shall pay to KWSC on a monthly basis a percentage of CTWSC Operations and Maintenance Expense on the CTWSC Existing System (as further defined below, "CTWSC O&M Expense"). The City's percentage for each month shall be the City Percentage defined in Section 3.5.C.1. The City Percentage shall be applied to the amount of CTWSC O&M Expense which is calculated by applying to CTWSC O&M Expense the percentage created by dividing the volume of treated water delivered to KWSC by the total volume of treated water delivered to all customers of CTWSC and multiplying by 100, and which is billed to KWSC by CTWSC. As an example,

using the amount of CTWSC O&M Expense billed to KWSC by CTWSC in April 2006, or \$56,577.00 (a month in which KWSC was delivered 90,813,000 gallons and the City was delivered 30,982,000 gallons), the City's O&M Expense payment for that month would be \$19,304.07; the City's CTWSC O&M Expense for a particular month will vary with the amount of CTWSC O&M Expense for that month and the City's monthly volume use percentage of water for that month (the "City Percentage," defined in Section 3.5.C.1). In the event that KWSC contracts with CTWSC to pay a "floor" or take-or-pay percentage of such CTWSC O&M Expense, then (i) the City will not agree to a floor in excess of 42% and (ii) to the extent that any floor applies to CTWSC O&M Expense in a particular month, the City and KWSC will pay that increment based on the ratio of their respective capacities in their 7.68 MGD of WTP capacity, which are currently 63% for the City and 37% for KWSC. This ratio shall not be adjusted, even if KWSC relinquishes its capacity in the CTWSC Water Treatment Plant, unless the City acquires KWSC capacity in the CTWSC Water Treatment Plant. Thus, the City's "floor," to the extent applicable, will never exceed 26.4% (i.e., 63% of 42%), unless the City subsequently acquires a portion of KWSC's capacity. See examples of calculations in **Exhibit D**. In the event the Parties learn that CTWSC will incur an expense that will increase the CTWSC O&M Expense, the Parties shall cooperate in an effort to approach CTWSC to obtain an equitable allocation of such CTWSC O&M Expense and to adjust the payment schedule.

2. Definition of CTWSC O&M Expense. For purposes of this Section 3.5 CTWSC O&M Expense shall mean, during CTWSC's fiscal year, all direct costs and expenses incurred by CTWSC for general overhead expenses relating to the Existing System, specifically including reasonable amounts for: the total annual cost of salaries; all transportation costs; all office expenses; telephone charges; insurance premiums; all taxes; dues; equipment rentals; consumable and operating supplies except chemicals; accounting and legal fees; engineering fees; conferences, education and certification of employees, managers and Board members; non-capital repairs to the Existing System; maintenance supplies and equipment; independent contractor fees for non-capital repairs; SEP Retirement Account payments; TCEQ/EPA Monitoring Requirements and costs; and solid waste management expenses. Notwithstanding the foregoing, the following costs and expenses are specifically excluded from CTWSC O&M Expense, and may not be included within CTWSC O&M Expense: (i) all Operation and Maintenance Costs of the New Facilities; (ii) all Energy Costs; (iii) all consulting fees and expenses relating to providing service to new customers or increasing service to current customers, which shall be paid for by entity requesting service; and (iv) all costs and expenses (including, without limitation, engineering fees, legal fees, accounting costs and other consulting fees) relating to a dispute between CTWSC and any member including the City whenever such dispute shall occur, including any litigation pending at the date hereof, and/or performance of covenants under agreements between or among CTWSC, the City, and/or KWSC; and (v) capital improvements.

C. KWSC O&M Cost on KWSC System. The City shall pay monthly to KWSC a percentage of costs actually incurred by KWSC in the previous month for operating and maintenance expense as defined herein ("KWSC O&M Cost") on the KWSC System.

1. City Percentage. The City's percentage of KWSC O&M Cost for each month shall be calculated by dividing the metered flow of treated water into the City at the City Points of Delivery by the metered pump discharge flow of treated water from the State Highway 195 Pump Station (i.e., including any flow from KWSC New Facilities) and multiplying by 100 (this monthly volume use percentage is called the "City Percentage"). As an example, assuming a KWSC O&M cost of \$5000.00 in a particular month, and assuming a City Percentage for that month of 34 percent, the City's payment of KWSC O&M Cost for that month would be \$1700.00; the City's payment of KWSC O&M Cost will vary from month to month depending on the KWSC O&M Cost for that month and the City Percentage for that month. To facilitate billing, KWSC shall require a meter to be constructed at the inlet to the State Highway 195 Pump Station Tank as set forth in Item No. 7 of Exhibit B. KWSC shall also install a meter at its point of entry at the State Highway 195 Pump Station. At the City's option, upon closing of the Agreement for Sale, KWSC shall also install a meter at the outlet of the State Highway 195 Pump Station, with the City to pay the cost. These meters shall be subject to the same rights and obligations of the Parties set forth in Section 3.8.A with respect to the meters at the City Points of Delivery. In the event the Agreement for Sale does not close, so that KWSC does not acquire the State Highway 195 Pump Station, the City Percentage shall be calculated by dividing the metered flow of treated water into the City at the City Points of Delivery by the flow at the metered outlet to the Ivy Mountain Tank. The Parties shall meet and agree on an alternate metered flow location in the event that construction of KWSC New Facilities results in inflow from the KWSC New Facilities into the KWSC System downstream of the metered outlet to the Ivy Mountain Tank.

2. KWSC O&M Cost. "KWSC O&M Cost" shall mean, during KWSC's fiscal year, all direct costs and expenses incurred by KWSC for non-capital repair and maintenance directly related to facilities of the KWSC System used in conveying treated water to the City, specifically including reasonable amounts for consumable and operating supplies except chemicals (other than chemicals used to maintain residual levels); equipment rentals; non-capital repairs and maintenance, including materials, equipment, supplies and labor associated with repair and maintenance; independent contractor fees for non-capital repairs and maintenance. KWSC O&M Cost shall not include repair and maintenance of Covered Tanks which is defined and addressed under Tank Maintenance Cost. All work associated with such non-capital repair and maintenance, including all materials, equipment and labor for work complete in place, shall be itemized on a work order for such repair or maintenance event. KWSC monthly invoices for KWSC O&M Cost shall attach copies of work orders and related invoices. All direct labor costs reflected in such work orders resulting from KWSC operation and maintenance personnel shall have a 40% multiplier applied to cover all administration and overhead cost of KWSC associated with such labor. Independent contract fees for non-capital repair and maintenance shall have a 10% multiplier applied to cover all administration and overhead cost of KWSC associated with such activities. All non-capital repair and maintenance to be included in KWSC invoices shall be preceded by notice to the City of such repair and maintenance, and opportunity shall be provided to the City to review repair and maintenance prior to commencement of work (except where emergency circumstances preclude, and in that case as soon as practicable). With respect to line breaks (other than line breaks directly caused

by KWSC personnel or KWSC contractors who are engaged in other than normal repair work) and resulting loss of water, KWSC (and, if available based on the notice provided for herein, the City) shall attempt to estimate the quantity of water lost due to the break or interruption. Based on the estimated loss, the cost related to such water loss shall be determined, including KWSC O&M Cost and energy cost specifically related to the line break. KWSC shall bill for and the City shall pay its percentage of costs of line breaks and loss of water in the same fashion as for other KWSC O&M Cost hereunder (including backup and true-up), applying the City Percentage for the month in which the line break occurred. KWSC shall use its best efforts to recover all cost of line break and resulting loss of water from any third party who caused or contributed to the line break, and shall adjust billing to the City accordingly consistent with this paragraph.

3. Planning. When KWSC anticipates significant O&M Expense on the KWSC System it shall cooperate in advance with the City in planning, scheduling, and paying for such expense. The City shall have the right to review in advance plans and specifications for any significant O&M Expense.

4. Annual True-Up. KWSC shall prepare and submit a report to the City at the end of each calendar quarter detailing KWSC O&M Cost and specifying the method of calculation for the previous quarter. At the end of each fiscal year, KWSC will compare the KWSC Cost billed to the City to the actual KWSC Cost incurred by KWSC in the previous twelve (12) calendar months, and the City shall receive either a refund or a bill as a result of any adjustment for the previous year, prior to the Annual Meeting. Each refund or bill will be itemized and will contain explanatory notes and back-up invoices, receipts and documentation as may be required to support the necessary adjustments.

5. Capital Policy. KWSC shall adopt within twelve (12) months following the Contract Date and implement a Capital Policy mutually agreed to by KWSC and the City which includes a definition of "repair" vs. "capital improvement" intended to clarify when a repair constitutes a capital improvement, as opposed to a non-capital repair, and which clearly delineates between KWSC O&M Cost and capital improvements to the system, permitting proper KWSC O&M Cost allocations in accordance with accepted principles and policies of the American Water Works Association. The Parties shall select a consultant, sharing equally the cost, to develop the Capital Policy.

D. Effect of Agreement for Sale: KWSC Energy Cost and KWSC O&M Cost on KWSC Purchased Facilities. Upon closing of the Agreement for Sale, CTWSC monthly invoices to KWSC will exclude CTWSC's energy cost associated with the State Highway 195 Pump Station and CTWSC O&M Expense on the KWSC Purchased Facilities, and the City shall pay on a monthly basis a percentage of KWSC Energy Cost and KWSC O&M Cost on KWSC Purchased Facilities, as follows:

1. City Payment of KWSC Energy Cost; True-Up. KWSC Energy Cost is defined as the cost of pumping of water from the inlet to the 2,000,000 gallon tank at the State Highway 195 Pump Station to the Ivy Mountain Tank. The City shall pay monthly a

percentage of KWSC Energy Cost, separately detailed on the invoice, using the City Percentage defined in Section 3.5.C.1 above. The City shall not be billed for energy costs related either to KWSC New Facilities or CTWSC New Facilities, and shall not be required to pay additional pumping or other costs attributable directly or indirectly to KWSC's acquisition of KWSC Purchased Facilities except as defined above. KWSC shall provide supporting detail of charges for KWSC Energy Cost. At the end of each fiscal year, KWSC Energy Cost shall also be the subject of the true-up procedure set forth in Section 3.5.C.4 above.

2. City Payment of KWSC O&M Cost on KWSC Purchased Facilities. Upon closing of the Agreement for Sale and KWSC's acquisition of the KWSC Purchased Facilities, KWSC Purchased Facilities shall be treated as part of the KWSC System for purposes of the City's payment of KWSC O&M Cost. To the extent KWSC pays KWSC O&M Cost as defined in Section 3.5.C.2 on KWSC Purchased Facilities, KWSC will bill the City monthly for such costs as set forth in Section 3.5.C. above.

E. Tank Maintenance Cost. The City and KWSC shall pay a percentage of Tank Maintenance Cost of Covered Tanks as set forth below.

1. Covered Tanks. The following tanks in the KWSC Existing System are "Covered Tanks" for purposes of Section 3.5.E:

Hewgley 2.0 (2,000,000 gallon tank)
Hewgley 0.25 (250,000 gallon tank)
Georgetown Road (2,000,000 gallon tank)

2. Tank Maintenance Account. KWSC shall establish an interest-bearing account (whether by bookkeeping entry or otherwise) into which each Party shall pay monthly an amount for Tank Maintenance Cost as defined herein ("Tank Maintenance Account") on Covered Tanks. Based on the Tank Assessment, the Parties shall develop a ten-year rolling schedule of amounts to be paid for each of the next ten years into the Tank Maintenance Account. The amount scheduled to be paid for a particular year shall be called the "Annual Tank Payment" for that year. The Parties shall endeavor to reach agreement on the initial Annual Tank Payment within 120 days following the Contract Date. At their Annual Meeting, the Parties shall review and adjust, as mutually agreed, the rolling schedule of amounts set for Annual Tank Payment. Interest accruing on the Tank Maintenance Account shall be paid quarterly to each Party based on the percentages by which each paid into the Tank Maintenance Account for the preceding quarter. The City shall pay monthly into the Tank Maintenance Account an amount computed by multiplying the City Percentage as defined in Section 3.5.C.1 times the Annual Tank Payment. KWSC shall pay monthly into the Tank Maintenance Account an amount computed by multiplying (100 minus the City Percentage) times the Annual Tank Payment. Upon closing of the Agreement for Sale, the Parties shall meet to adjust the Annual Tank Payment to include the Ivy Mountain Tank and State Highway Pump Station Tank.

3. Tank Maintenance Cost. "Tank Maintenance Cost" shall mean, during KWSC's fiscal year, all direct costs and expenses for non-capital repair and maintenance of the interior and exterior paint coating system reasonably incurred with respect to the Covered Tanks, specifically including reasonable amounts of consumable supplies; equipment rentals; materials, equipment, supplies and labor associated with repair and maintenance; independent contractor fees for non-capital repairs and maintenance. All work orders associated with such repair and maintenance on Covered Tanks, including all materials, equipment and labor for work complete in place, shall be itemized on a work order for each repair and maintenance event. KWSC invoices to the City for Tank Maintenance Cost shall attach copies of work orders and related invoices. All direct labor costs reflected on such work orders resulting from KWSC repair and maintenance personnel shall have a 40% multiplier applied to cover all administration and overhead cost of KWSC associated with such direct labor costs. Independent contract fees for Tank Maintenance Cost shall have a 10% multiplier applied to cover all administration and overhead cost of KWSC associated with such activity. All Tank Maintenance Cost shall be preceded by notice to the City of such Tank Maintenance Cost, and opportunity shall be provided to the City to review proposed Tank Maintenance Cost prior to commencement of work (except where emergency circumstances preclude). Except for costs incurred by KWSC due to an emergency condition, the City shall have no obligation to pay or contribute to any Tank Maintenance Cost incurred by KWSC for planned maintenance prior to October 1, 2007.

4. Effect of Agreement for Sale: Tank Maintenance Cost of Ivy Mountain Tank and State Highway 195 Pump Station Tank. Unless and until closing of the Agreement for Sale, the City shall pay the cost of repair and maintenance to the Ivy Mountain Tank and State Highway 195 Pump Station Tank as part of the City's payment of CTWSC O&M Expense as set forth in Section 3.5. However, following closing of the Agreement for Sale and acquisition of the Ivy Mountain Tank and State Highway 195 Pump Station Tank by KWSC, the Ivy Mountain Tank and State Highway 195 Pump Station Tank shall be included as Covered Tanks, and the City shall pay Tank Maintenance Cost on the Ivy Mountain Tank and State Highway 195 Pump Station Tank as set forth in Section 3.5.E.2 for Covered Tanks.

5. Planning. To assist the Parties in planning and budgeting for Tank Maintenance Costs, prior to the Contract Date KWSC shall provide as information a spreadsheet showing the date on which each Covered Tank and the Ivy Mountain Tank and State Highway Tank were last repainted and/or recoated. In addition, the Parties shall share equally in the cost of an assessment by a mutually agreed contractor, to be performed within 90 days of the Contract Date or as mutually agreed at the monthly manager meetings, which will set forth a proposed schedule for repainting or recoating each Covered Tank as well as the Ivy Mountain Tank and the State Highway 195 Pump Station Tank, and the estimated cost for such repainting or recoating ("Tank Assessment"). The Tank Assessment shall be attached hereto as **Exhibit E**. The Parties shall review and mutually agree to adjustments to the Tank Assessment at their Annual Meeting.

6. Annual True-Up. KWSC shall pay Tank Maintenance Cost out of the Parties' Tank Maintenance Account as incurred. Commencing December 31, 2007, KWSC shall prepare and submit a report to the City at the end of each calendar quarter detailing Tank Maintenance Account payment by each Party and Tank Maintenance Cost for the quarter and specifying the method of calculation of any additional amounts owed by either Party for the previous quarter. At the end of each fiscal year, KWSC will compare the Parties' payments into the Tank Maintenance Account in the previous twelve (12) calendar months with Tank Maintenance Cost actually incurred by KWSC for those months, and the City shall receive either a refund or a bill as a result of any adjustment for the previous year, prior to the Annual Meeting. Each refund or bill will be itemized and will contain explanatory notes and back-up invoices, receipts and documentation as may be required to support the necessary adjustments.

F. \$0.08 per 1000 Gallons. The City shall pay \$0.08 per 1000 gallons received by the City ("CTWSC Capital Contribution") which KWSC shall pay into the CTWSC Capital Investment Account, subject to the following "escalator" provision and special covenants:

1. Definition of "Capital Investment Account Balance." For purposes of this subsection, the term "Capital Investment Account Balance" equals the sum of: (i) the average cash balance of the Capital Investment Account maintained by CTWSC during the month, plus (ii) the amount of accounts receivable for capital investment contributions due to CTWSC from its other members and/or customers, measured as of 5:00 p.m. on the last business day of the month.

2. Escalator Provision and Special Covenants. The City shall be billed for CTWSC Capital Contribution only for such months and at such rates and under such conditions as KWSC has agreed to pay its contribution to the CTWSC Capital Investment Account, which is as follows: During those months and only those months in which the Capital Investment Account Balance for the immediately preceding month is less than \$2,500,000.00 ("Contribution Months"), KWSC has agreed to pay to CTWSC, as a contribution into a Capital Investment Account, a monthly payment based on the number of gallons of water treated by CTWSC and delivered to KWSC in the previous calendar month. Such monthly payment during Contribution Months shall be computed according to the schedule set forth on **Exhibit F** attached hereto and made part hereof ("Capital Contribution Schedule"). The rate of contribution into the Capital Investment Account (initially set at \$0.08 per 1,000 gallons of treated water) shall be adjusted by 6% at the expiration of each period of 36 Contribution Months as provided in the Capital Contribution Schedule. It is agreed and understood that in the event the Capital Investment Account Balance for a month shall exceed \$2,500,000.00 as calculated in the first sentence of this subsection (a), such month shall not be counted as a Contribution Month, and the number of accumulated Contribution Months shall not increase again unless and until the Capital Investment Account Balance for the immediately preceding month is less than \$2,500,000.00. The Parties understand and agree that the consideration for the City's undertaking to pay more than \$.08 per 1000 gallons pursuant to the escalator expressly includes KWSC's commitment to enforce provisions with respect to the Capital Investment Account as set forth in the CTWSC Wholesale Contract, specifically including

CTWSC's agreement to keep facilities in good condition to deliver contractual quantities to the points of delivery.

3. CTWSC Capital Policy. In order to assure that the City is not improperly charged for CTWSC capital improvements as "CTWSC O&M Expense," KWSC shall use its best efforts to require CTWSC to adopt within twelve (12) months following October 27, 2005, and to implement a Capital Policy mutually agreed to by KWSC and CTWSC which includes a definition of "repair" vs. "capital improvement" intended to clarify when a repair constitutes a capital improvement, as opposed to a non-capital repair, and which clearly delineates between CTWSC O&M Expense and capital improvements to the system, permitting proper CTWSC O&M Expense allocations in accordance with accepted principles and policies of the American Water Works Association. KWSC shall consult with the City concerning the proposed CTWSC Capital Policy prior to agreeing with CTWSC on its contents.

3.6 Points of Delivery

The City agrees to take treated water at its Points of Delivery defined as the existing meters located on F.M. 580 northeast of the City and on U.S. Highway 190 east of the City, as shown on the System Map. Any modification to Points of Delivery must be mutually agreed to in writing between KWSC and the City.

3.7 Quality

The water delivered by CTWSC to KWSC is contractually required to be treated water of a quality sufficient to meet the requirements for potable water established by the TCEQ and the United States Environmental Protection Agency. The City has satisfied itself that such water will be suitable for its needs. KWSC shall not be responsible for maintaining any particular amount of chlorine residual at any point in the City's distribution system. However, KWSC will deliver treated water at the City's Points of Delivery with a disinfectant residual that meets or exceeds minimum standards. The Parties recognize that KWSC proposes to construct its own water treatment plant, and to purchase certain components of the CTWSC System including the pipeline from State Highway 195 Pump Station to the Ivy Mountain Tank, and further recognize that it is possible that water treated by KWSC may be commingled with the water delivered by CTWSC. KWSC further warrants and agrees that water entering the City's Points of Delivery from any water treatment plant constructed and operated in future by KWSC will meet applicable state and federal standards, and that KWSC shall collect samples of treated water delivered to its customers and cause them to be analyzed consistent with then-current guidelines established by the TCEQ, and will promptly notify the City if any KWSC water fails to meet applicable state and federal standards. KWSC agrees that it will also monitor water delivered from the CTWSC System via KWSC telemetry capabilities and sampling or functionally equivalent alternative methods, and that it will promptly notify both CTWSC and the City if any CTWSC water fails to meet applicable state and federal standards.

3.8 Metering Equipment

A. Points of Delivery. KWSC will furnish, install, operate, and maintain at its expense the necessary equipment and devices (including a meter house or pit) of standard type required for measuring the quantity of water delivered under this Contract at the Points of Delivery. Such meters and other equipment so installed shall be the property of KWSC. KWSC shall inspect, calibrate, and adjust its meters at least annually, as necessary to maintain accurate measurements of the quantity of water being delivered. The City shall have access to the metering equipment at all reasonable times for reading, inspection and examination, but the calibration, and adjustment thereof shall be done only by employees or agents of KWSC. If requested, a City employee may witness such reading, calibration, and adjustment of meters. Any measuring device that fails to function or which functions incorrectly shall promptly be adjusted, repaired or replaced by a like device having the required accuracy. A meter registering not more than 2 percent above or below the test results shall be deemed to be accurate. The previous readings of any meter disclosed by tests to be inaccurate shall be corrected for one-half the period elapsed since the next preceding meter test, but in no event to exceed 6 months, in accordance with the percentage of inaccuracy above or below 2 percent found by such tests. If any meter fails to register for any period, the amount of water furnished during such period shall be deemed to be the amount of water delivered in the corresponding period immediately prior to the failure, unless KWSC and the City shall agree upon a different amount. All readings of meters will be entered upon proper books of record maintained by KWSC. Upon written notice, the City may have access to said record books during normal business hours.

B. Additional Metering The City shall have the right to install, at the City's sole expense, non-invasive metering equipment (such as a Mag Meter or other similar meter that does not require invasion into the interior of the pipe): (1) at the outflow of the Ivy Mountain Tank Outlet; (2) on the Kempner North Transmission Line to Lampasas downstream of the KWSC System Junction; and (3) on the Kempner South Transmission Line to Lampasas downstream of the KWSC System Junction; all as shown on **Exhibit A**. The plans and specifications for the metering Equipment shall be submitted to KWSC for review and approval prior to installation. After obtaining approval of the plans and specifications from KWSC, the City shall provide written notice to the KWSC Engineer of the date on which installation of the metering equipment is scheduled to begin, and the construction and installation of the metering equipment shall be subject to inspection by KWSC. The City shall have the right to read these meters during normal business hours. All readings of meters will be entered upon the proper books of record maintained by the City. Upon written notice, KWSC shall have access to such records during normal business hours. These meters are not the official Points of Delivery and shall not be used for billing purposes

3.9 Pressure, Backflow, Maximum Rate of Flow

A. Delivery Requirements. The initial "Maximum Rate of Delivery" shall be 3.51 MGD (measured by combining total water delivered to both the 580 Meter and 190 Meter over any consecutive 24-hour period) based on the City's reserved capacity in the State Highway 195 Pump Station. KWSC shall always use best efforts to deliver treated water to the City at each of the two Points of Delivery, at a minimum pressure of 55 psi at the 580 Meter, and 78 psi at the

190 Meter; and, unless the City is drawing water at the Points of Delivery at an instantaneous rate greater than 127 percent of the then applicable Maximum Rate of Delivery, KWSC shall deliver treated water to the City at each of the two Points of Delivery, at a minimum pressure of 55 psi at the 580 Meter, and 78 psi at the 190 Meter. In the event the City makes improvements in the State Highway 195 Pump Station or elsewhere allowing increased deliverability consistent with this contract, then the Maximum Rate of Delivery shall thereafter be increased to include the greater number of gallons per day corresponding to such improvements. KWSC and the City will use best efforts to maintain at a minimum 28 feet of water in the Georgetown Tank. For purposes of calculating the initial Maximum Rate of Delivery to the City, any flow from the Georgetown Tank delivered to KWSC customers shall not be included.

B. Forecasting and Planning Communications

1. Modeling and Usage Planning. If either Party has reason to believe that its usage, at its average daily flow, of its reserved capacity in any component in the KWSC System is at 75% of that reserved capacity, then that Party will notify the other Party and will undertake planning and implementation efforts; and if at 85% of that reserved capacity, then that Party will notify the other Party and cause to be developed or will have in place plans and specifications and financing to add additional capacity to return its capacity usage at its average daily flow to a level below 75%.

2. Ten-Year Plans and Information Exchange. Each Party shall develop and maintain a Ten-Year Plan applicable to water supply and delivery, including long-term capital improvements and related infrastructure upgrades. Each Party shall revise its Ten-Year Plan every five years. The Parties shall promptly exchange their Ten-Year Plans and revisions. Each Party shall also develop an annual forecast of water usage ("Forecast") and summary of past year's usage ("Usage Summary"). The Parties shall exchange their Forecast and Usage Summary at least 2 weeks before the annual meeting between the City Council and KWSC Board.

3. Manager Meetings. The KWSC Manager and City Manager shall use best efforts to meet monthly to share information on system operation and usage.

4. Changes in Demand and Operation. To provide opportunities to improve system operation, when a Party has a reasonable expectation that a new or additional service commitment might significantly impact the operation of the system, that Party will notify the other Party as soon as practicable to offer a meeting for discussion of the matter. In addition, the Parties shall mutually inform each other of events or changes in operation of the CTWSC System that may materially affect the Parties.

C. Remedies for Intrusion. For purposes of this section, an "intrusion" shall mean (i) a measured failure by KWSC to maintain the minimum pressures required at either or both of the Points of Delivery, (ii) the City's measured failure to limit its demand to quantities below the Maximum Rate of Delivery, or (iii) KWSC's measured failure to make available sufficient water to meet the City's demands up to the Maximum Rate of Delivery. No allegation of an intrusion

may be based solely upon theoretic calculations of capacity or of pressure. In the event of intrusions, then the following shall occur:

1. If there are two (2) such intrusions within any 30-day period, then the Parties shall meet within 15 calendar days to discuss the intrusions; unless within the 15 days the intruding Party satisfies the other Party in the other Party's reasonable judgment that the intruding Party has taken steps to remove the intrusion, the intruding Party shall invoke its drought contingency plan.

2. If such intrusion by a Party occurs five (5) times in any 30-day period, or twelve (12) times in any consecutive 120-day period, then the Parties shall meet within 15 calendar days to discuss the intrusions. If no mutual resolution is reached within those 15 calendar days, the intruding Party shall:

- a. invoke its drought contingency plan; and
- b. (i) within 15 calendar days satisfy the other Party that in the other Party's reasonable judgment that the intruding Party has taken prompt steps to remove the intrusion, or
(ii) take immediate steps to design and construct improvements so that within two (2) years, the intruding Party will have completed and paid for sufficient improvements to prevent recurrence of the intrusion.

The intruding Party's drought contingency plan shall remain in effect pending completion of either (b)(i) or (b)(ii).

3. In the event of such intrusions, the remedies set forth in C.1 and 2 above are exclusive to any remedy for alleged damages for alleged loss of capacity or for alleged use of another's capacity; but this Agreement does not prohibit a remedy for specific performance, for injunctive relief, for re-allocation of any shared expenses or other non-damages relief as a court or the Neutral may find appropriate. The Parties intend (i) that the remedies set forth in C.1 and 2 above shall not be subject to the Force Majeure provision of Section 5.1 and (ii) that the non-intruding Party shall have no obligation to invoke its drought contingency plan in response to intrusions under this section.

D. Annual Meeting. The KWSC Manager and City Manager shall coordinate a meeting of the governing bodies of each Party to be held during the first quarter of each calendar year to review the prior year's water usage and delivery and to forecast major anticipated repair or maintenance and shall cooperate in planning in order to provide efficient and cost-effective delivery to City and KWSC water customers.

E. Improvements and Water Assignment. If and when a higher Maximum Rate of Delivery is needed by the City due to City demand in excess of then contractual amounts, the

cost of such Improvements necessary to accomplish such higher Maximum Rate of Delivery will be paid for by the City as provided in Section 3.1. When the City's reserved capacity in the State Highway 195 Pump Station and other CTWSC System Components and KWSC System Components increases pursuant to Section 3.1, the Maximum Rate of Delivery shall increase to reflect the maximum amount of water that may be delivered to the City on a daily basis using the City's reserved capacity in the CTWSC Existing System and the KWSC System. The City shall assign Stored Water to CTWSC sufficient to allow KWSC to deliver the amounts of water required by the City from time to time. KWSC shall assign Stored Water to CTWSC sufficient to allow KWSC to deliver the amounts of water required by its retail customers from time to time. Neither Party shall use the other Party's Stored Water or associated transmission capacity without prior written permission which may include arrangements for compensation.

3.10 Billing

KWSC shall render a bill to the City on the first working day of each month, and each such bill shall set forth the amounts due under this Article, and the quantity of water delivered at the Points of Delivery, and include a copy of the CTWSC billing information to KWSC for the applicable month. The City shall pay the amounts due to KWSC on or before the 15th day of the month. Payments not made when due shall bear interest at the compounded rate of one percent per month on the amount due from their due date until paid.

3.11 Annual True-Up

Pursuant to Sections 3.04 and 3.06 of the CTWSC Wholesale Contract, CTWSC will perform an audit of its actual treated water costs and the actual Operations and Maintenance Expenses, and KWSC will receive either a refund or a bill as the result of any adjustment for the previous year. Within 30 days of its receipt of either a refund or a bill from CTWSC as a result of the audits required by Sections 3.04 and 3.06 of the CTWSC Wholesale Contract, KWSC will perform an audit of the amounts that the City has paid to KWSC for the previous year under Sections 3.5 and 3.6 of this Contract. Based on this audits, KWSC shall deliver to the City either a refund or a bill as a result of any adjustment necessary to ensure that the City paid only the amounts due under Sections 3.5, and 3.6 of this Contract for the previous year, together with the back-up information for the adjustment.

In addition, within 30 days of the City's receipt of either a refund or a bill from KWSC as a result of the this audit, the Parties shall meet to review the monthly usage data of both Parties for the previous year. If the data shows that any Party is exceeding its reserved capacity or the capacity it is authorized to use under Section 3.1 and Section 3.2, then said Party shall: (1) initiate reasonable steps to obtain additional capacity within six months and shall proceed with reasonable diligence to obtain additional capacity within 30 months; and (2) compensate the other Party for the use of the other entity's reserved capacity by paying the other Party the CTWSC Current Debt Service on the CTWSC System Component, CTWSC Operations and Maintenance Expense, and/or KWSC Debt Service on the KWSC System Component associated

with the percentage of capacity used for the time in which the other Party's reserved capacity was used.

ARTICLE IV. SPECIAL CONDITIONS

4.1 Operation and Maintenance of the System

Both Parties agree to operate and maintain their respective systems in an efficient manner and in accordance with good business and engineering practices, and at reasonable cost and expense. KWSC recognizes its right and duty to operate the KWSC System in the most prudent and economical manner for the benefit of all of its customers, including the City. The City recognizes it has a duty to operate its water system in a prudent and economical manner in order for it to receive water from the KWSC System. The Parties shall give each other as much notice as is reasonably practical of any changes in the operation of their Systems that may have an impact on the other's water distribution system.

4.2 Title to Water: Risk of Loss

Except as expressly provided in Section 3.5.C.2, KWSC O&M Cost, concerning certain costs from line breaks, (i) title to all water supplied to the City shall be in KWSC up to the Points of Delivery at which point title shall pass to the City; (ii) risk of loss of water on the KWSC side of the Points of Delivery lies with KWSC, and risk of loss on the City side of the Points of Delivery lies with the City; and (iii) the City shall only be billed for that water that passes through the meters at the Point of Delivery, less any amounts that backflow into the KWSC System.

4.3 Insurance

KWSC agrees to carry and arrange for fire, casualty, public liability, and/or other insurance, including any self-insurance, on the KWSC System up to the Points of Delivery for purposes and in amounts which, as determined by the Board, ordinarily would be carried by a privately owned utility company owning and operating such facilities. Such insurance will provide, to the extent feasible and practicable, for the restoration of damaged or destroyed properties and equipment, to minimize the interruption of the services of such facilities.

4.4 Dispute Resolution Concerning Engineering Issues.

A. Definitions for This Section.

1. A "dispute concerning engineering issues" includes, without limitation,
 - a. a dispute concerning the necessity or sufficiency of improvements required under Section 3.9.C.2(b)(ii) (relating to Intrusion), or

b. a dispute as to whether capital improvements have increased a Party's entitlements or obligations under this Contract, and if so the extent of such increased entitlements or obligations, or

c. a dispute as to whether a Party's usage of water is exceeding its share of capacity of facilities, and if so the extent of such excess, or

d. a dispute as to the design of capital improvements proposed to be constructed by a Party or as to the portion of capital improvements, if any, to be paid by a Party, or

e. any other dispute arising out of or relating to this Contract or any other relationship between the Parties concerning a matter as to which the exercise of engineering experience and judgment is necessary for resolution of the dispute, or

f. any other dispute that the Parties at the time agree to submit to the dispute resolution procedure of this section.

2. "The Neutral" means a civil engineer selected by the agreement of the two Parties or, in the absence of agreement, a civil engineer appointed pursuant to subsection C below.

B. Agreement to Arbitrate. In the event a dispute concerning engineering issues arises, and the Parties have not resolved the dispute by agreement, then the Parties agree to submit the dispute to the Neutral for binding arbitration.

C. Selection of the Neutral.

1. In the event the Parties do not promptly select the Neutral by agreement within 30 days following the request of either Party, then the Parties agree to cooperate promptly and reasonably, and without ex parte communications, in seeking and obtaining the appointment of a civil engineer by the Dean of the College of Engineering of Texas A & M University, or, if such Dean declines to appoint the Neutral, a civil engineer appointed by the presiding district judge of the 27th District Court of the State of Texas.

2. The Parties agree that such Dean, such district judge and the Neutral shall have no liability whatsoever to either of the Parties and shall be deemed by the Parties to enjoy judicial immunity for any role in this dispute resolution process.

D. Procedures and Related Matters.

1. The arbitration shall be held in Lampasas, Texas, or at such other place as may be selected by mutual agreement.

2. Promptly upon billing by the Neutral, the Parties shall each pay one-half of the deposits, fees and expenses charged by the Neutral, subject to such allocation for reimbursement as the Neutral may award as part of the Neutral's decision.

3. The arbitration shall be conducted by such procedure as the Neutral shall determine, with or without reference to available models such as the Commercial Arbitration Rules of the American Arbitration Association.

4. Judgment upon the award rendered by the arbitrator may be entered in any court having jurisdiction thereof.

5. Nothing contained herein shall prohibit a Party from seeking injunctive or other ancillary relief from any judicial authority, before, during or after the pendency of any arbitration proceeding; provided, however, that no relief so granted may operate to reduce or impair the authority of the Neutral as set forth in Article 4.4.

6. The provisions of this arbitration clause shall survive the termination or expiration of this Agreement.

7. In making any determination regarding any dispute concerning engineering issues, the Neutral may consider (i) original design parameters and (ii) that the delivery capacity of the system between the CWTSC Water Treatment Plant and the Points of Delivery to the City is dependent upon hydraulic conditions of the system as a whole, including but not limited to initial pump available head, friction loss, water velocity, pipe diameter, ground elevation along the transmission route, water elevations in storage tanks, and other factors.

8. As to any calculations in which the Neutral is required to use a friction coefficient: KWSC represents, and the City has no basis to dispute, that the KWSC Existing System was designed with the use of a friction coefficient of 140. The Parties agree

a. that the Neutral should use a presumption that the friction coefficient is 140 in the KWSC Existing System unless the Neutral is persuaded based upon empirical evidence that a different friction coefficient is more accurate and reliable as to one or more components of the KWSC Existing System,

b. that the Parties will cooperate in good faith to allow prompt measurement of the friction coefficient in any component of the KWSC System upon either Party's request, and

c. that no presumption shall exist as to the friction coefficient as to any portion of the KWSC Existing System if the Neutral is persuaded based upon empirical evidence that a different friction coefficient is more accurate and reliable as to one or more components of the KWSC Existing System; and in such circumstance, the Neutral's use of any

parameters to be used in any calculations should be based upon the Neutral's judgment, experience and conclusions from any evidence presented by the Parties.

4.5 Records

Upon written notice and during normal business hours, the City shall have the right to inspect, and/or have its independent auditor evaluate, the records of KWSC to the extent necessary to verify the accuracy of any statement, charge or computation made pursuant to any provisions of this Contract. Upon written notice and during normal business hours, KWSC shall have the right to inspect, and/or have its independent auditor evaluate, the records of the City to the extent necessary to verify the accuracy of any statement, charge or computation made pursuant to any provisions of this Contract. Upon request, a Party shall provide the other Party with its audited financial statements.

4.6 Concurrence by USDA-RD

KWSC and the City agree to use their best efforts to obtain the concurrence of USDA-RD and to cooperate in all reasonable ways to amend this Contract consistently with its current substance to the extent, if at all, needed to obtain such concurrence. Following the Effective Date, the City agrees to cooperate with KWSC in seeking the closing of the TWDB Loans.

4.7 Enforcement of CTWSC Wholesale Contract

The Parties acknowledge that KWSC's ability to perform some obligations under this Contract are subject to CTWSC's performance of the CTWSC Wholesale Contract. KWSC shall use its best efforts to insure that each covenant and representation made by CTWSC in the CTWSC Wholesale Contract is performed; such best efforts shall include without limitation KWSC's enforcement of its legal and equitable remedies, including specific performance, in the event CTWSC fails to perform timely these covenants and representations. Upon request the Parties shall meet to discuss KWSC's efforts and CTWSC's response. Without modifying in any way the foregoing, the Parties further acknowledge that the City's agreement to pay the agreed escalator on the \$0.08 per 1000 Gallons is expressly conditioned on KWSC's agreement to use its best efforts to enforce the following:

A. CTWSC shall maintain the current rated capacity of the CTWSC Water Treatment Plant Capacity at no less than 14.35 MGD;

B. CTWSC shall require that all other members and/or customers of CTWSC contribute to the Capital Investment Account according to the Capital Contribution Schedule applicable to KWSC;

C. Funds contributed to the Capital Investment Account by KWSC and by members and customers of CTWSC shall be accumulated in the Capital Investment Account to pay for capital improvements, as the Board may, in its discretion, from time to time deem necessary pursuant to its Capital Policy. CTWSC may also use the Capital Investment Account to (i)

acquire leases, licenses, easements, rights-of-way, and interests in fee simple to extend rights in the Water Treatment Plant site from the Corps of Engineers, Department of U.S. Army from May 10, 2029 to the expiration of the Term of this Contract, (ii) acquire leases, licenses, easements, rights-of-way, and interests in fee simple to extend rights in pipeline easements from the Fort Hood Military Reservation from January 22, 2035 to the expiration of the Term of this Contract, and (iii) obtain renewals and extensions of contracts with BRA.

D. In considering expenditures for capital improvements, CTWSC agrees to keep facilities in good condition to deliver contractual quantities to the respective points of delivery.

E. Payments from the Capital Investment Account will be made only with prior approval of specific item(s) by the Board of CTWSC given after due notice and action by the Board at a regular meeting on items regarding the expenditure of these funds.

4.8 Reserve Accounts and Use of Reserve Fund Earnings

"Joint Use Facilities Base Reserve Account" and "Joint Use Facilities System Account." The Parties have paid into reserve accounts required by certain loans for "Joint Use Facilities" as defined herein. The Parties desire to cooperate to accumulate and make available the interest on reserve amounts and other monies to provide an ongoing source of funding for the purposes set forth herein. KWSC agrees, as a condition precedent to operation of this Section 4.8, that it shall maintain as fully funded its reserve accounts for all indebtedness to USDA-RD.

1. "Joint Use Facilities." The proceeds from KWSC USDA-RD Loans 91-06 and 91-07 and CTWSC USDA-RD Loan 91-06 were used to construct facilities for the water storage and transmission system benefiting both the City and KWSC. KWSC anticipates using proceeds of the TWDB Loans to prepay KWSC USDA-RD Loan 91-07 and CTWSC USDA-RD Loan 91-06, as well as to fund the purchase and construction of certain CTWSC facilities which currently serve both KWSC and the City. Those facilities financed by KWSC with funds from KWSC USDA-RD Loans 91-06 and 91-07 and the facilities and purposes referenced above for which the proposed TWDB Loans will be used by KWSC (including those purchased from CTWSC) are referred to as the "Joint Use Facilities."

The proceeds from KWSC USDA-RD Loans 91-01 and 91-02 were used to construct facilities for the sole benefit of KWSC. Additionally, KWSC expects to use proceeds of TWDB Loan 2 to finance the construction of KWSC New Facilities for the sole benefit of KWSC. The facilities constructed with the proceeds of KWSC USDA-RD Loans 91-01 and 91-02, and the proposed KWSC New Facilities to be constructed by KWSC with TWDB Loan 2 as described in this paragraph, shall not be considered Joint Use Facilities.

2. "Joint Use Facilities Base Reserve Account" and "Joint Use Facilities Base Reserve Amount." Existing USDA-RD loan documents require reserve accounts for each USDA-RD loan and it is anticipated future TWDB loan documents will also require the establishment of a reserve account. The Parties agree it is prudent and necessary for KWSC to segregate and keep separate the reserve accounts for the Joint Use Facilities in an account to be

called the "Joint Use Facilities Base Reserve Account." .At the present time, the Joint Use Facilities Base Reserve Account shall include the following reserve amounts, which together are called the "Joint Use Facilities Base Reserve Amount."

a. Reserve amounts for KWSC USDA-RD Loans 91-06 and 91-07 Under existing USDA-RD loan documents, the Base Amount for KWSC USDA-RD Loan 91-06 is approximately \$329,784.00 and for KWSC USDA-RD Loan 91-07 is approximately \$211,200.00, for an approximate total of \$540,984.00, which amount is fully funded.

b. Reserve amount for CTWSC USDA-RD Loan 91-06, as refinanced. It is anticipated that KWSC will prepay and retire CTWSC USDA-RD Loan 91-06 with TWDB Loan 1 and CTWSC will transfer the funds in its reserve account in the amount of \$297,650.00 to KWSC. In lieu of distributing this amount pro rata to the City and to KWSC based on their payments under the 2000 Contract and 2001 Contract, KWSC will deposit the total amount into the Joint Use Facilities Base Reserve Account.

c. Future loans. In the event that the Parties mutually agree in future to other loan(s) for purpose of improvements to Joint Use Facilities, the reserve amount for such loan (s) shall be added to the Joint Use Facilities Base Reserve Account.

d. Retention of reserve amounts. It is the Parties' intent that, when KWSC USDA-RD Loan 91-07 is prepaid and retired, the reserve amount attributable to Loan 91-07 in the amount of approximately \$211,200.00 will remain in the Joint Use Facilities Base Reserve Account to satisfy requirements of TWDB loan documents for loans related to the Joint Use Facilities. It is also the Parties' intent that the same procedure shall apply in the event KWSC USDA-RD Loan 91-06 is prepaid or the Parties mutually agree to establish other loans for the Joint Use Facilities as set forth in c above and to prepay such other loans. Upon retirement of a loan, provided KWSC's reserve accounts for all indebtedness to USDA-RD are fully funded, the Joint Use Facilities Base Reserve Fund Amount shall be adjusted under the provisions of the existing loan documents and any funds in excess of the Base Reserve Fund Amount shall be transferred to the Joint Use Facilities System Account as defined below, except as follows: if at the time of the proposed funds transfer the balance in the Joint Use Facilities System Account exceeds \$1,000,000.00, or the proposed funds transfer will result in a balance exceeding \$1,000,000.00, then the Parties shall disburse the portion of such funds which if added to the Joint Use Facilities System Account would result in a balance in excess of \$1,000,000.00 to the Parties, 63% to the City and 37% to KWSC.

e. Use of Base Reserve Fund Amount. The Base Reserve Fund Amount may only be used for the purpose of paying the cost of repairing or replacing any damage to the KWSC System which may be caused by any unforeseen circumstance, subject to agreement of the Parties to the contrary. Prior to any such expenditure of the Base Reserve Fund Amount, the Parties shall mutually agree to a timeframe for replacement of such funds in the Base Reserve Fund Amount.

3. Joint Use Facilities System Account. The Parties intend for the Joint Use Facilities Base Reserve Account to accumulate interest to be used as provided herein. Interest earned on the funds in the Joint Use Facilities Base Reserve Account shall be transferred quarterly to the "Joint Use Facilities System Account" which shall be created and administered by KWSC. Upon recommendation by KWSC's auditor, the Parties shall mutually agree on the type of account, including permissible investments and recordkeeping, for the Joint Use Facilities System Account. The funds in the Joint Use Facilities System Account shall be used exclusively for purposes benefiting the Joint Use Facilities as mutually agreed by the Parties, and may include funding of improvements to or maintenance of the Joint Use Facilities and funding of reserves in the event the Parties agree to undertake further loan(s) with respect to the Joint Use Facilities. Such uses may include improvements primarily benefiting one Party or the other Party. The Parties will discuss proposed fund uses at their annual meeting, or more frequently if necessary. Both Parties shall approve in writing any proposal for the expenditure of any funds in the Joint Use Facilities System Account prior to obligating the Parties to any proposed project or use.

4. Account Statements. KWSC shall provide copies to the City of the statements from the Joint Use Facilities Base Reserve Account and Joint Use Facilities System Account.

5. Disbursement of Excess. At such time as the Joint Use Facilities System Account exceeds \$1,000,000.00, then KWSC shall cause the excess to be disbursed to KWSC and to the City. Earned interest in excess of \$1,000,000 in the Maintenance Reserve Account shall be disbursed quarterly to the City and KWSC as follows: (i) 63% to the City and (ii) 37% to KWSC. While the Parties intend that the anticipated use of the proceeds so disbursed shall be discussed at the annual meeting of the Parties, either Party may use the proceeds so disbursed to it as it sees fit.

6. Expiration. At the expiration of the Term of this Contract, any amounts remaining in the Joint Use Facilities System Account and the Joint Use Facilities Base Reserve Account shall be disbursed 63% to the City and 37% to KWSC; unless at such time a Party has no remaining amounts following an expenditure of its portion of such remaining amounts in a mutually agreed project for that Party's exclusive benefit.

4.9 Effective Date Adjustments

A. Escrow Amount. Upon the Effective Date of the 2006 Contract, the City shall cause to be paid to CTWSC the funds deposited by the City into, and currently held in, the escrow account, together with any interest thereon, currently maintained by the Parties to provide for and pay the difference between the amount paid by the Parties to CTWSC pursuant to the Water Sale and Purchase Contract executed by CTWSC and KWSC on or about July 22, 1985 (as may have been amended by agreement or subsequent judgment) and the amount which would have been paid by the Parties to CTWSC under the provision of the 2000 and 2001 Contracts from January 1, 2004 to the effective date of the 2005 Contract.

B. Billing Adjustment. Upon the Effective Date of the 2006 Contract, the Parties shall "true up" the bills to the City from KWSC for CTWSC Operation & Maintenance Expenses for months subsequent to the effective date of the 2005 Contract, so that CTWSC O&M Expenses for months subsequent to the effective date of the 2005 Contract are calculated based upon the "City Percentage" calculated pursuant to Section 3.5.C.1 of the 2006 Contract. In the event any such adjustment results from the "true-up," the Parties agree that the amount of such adjustment, whether a credit or debit, shall be prorated in twelve equal amounts and shall be reflected as adjustments in the next twelve monthly billings. The Parties further agree that bills to the City for months following January 2006 shall be subject to the Annual True-Up as provided in Section 3.11.

ARTICLE V. MISCELLANEOUS

5.1 Force Majeure

If by reason of Force Majeure KWSC or the City shall be rendered unable wholly or in part to carry out its obligations under this Contract, other than the obligation of the City to make the payments required by this Contract, then if such Party shall give notice and full particulars of such Force Majeure in writing to the other Party, as appropriate, within a reasonable time after occurrence of the event or cause relied on, the obligation of such Party, so far as it is affected by such Force Majeure, shall be suspended during the continuance of the inability then claimed, but for no longer period, and such Party shall endeavor to remove or overcome such inability with all reasonable dispatch. The term "Force Majeure" as employed herein shall mean acts of God, strikes, lockouts or other industrial disturbances, acts of public enemy, orders of any kind of the Government of the United States or the State of Texas, or any civil or military authority, insurrection, riots, epidemics, landslides, lightning, earthquake, fires, hurricanes, storms, floods, washouts, droughts, or other catastrophes, arrests, restraint of government and people, civil disturbances, explosions, breakage or accidents to machinery, pipelines or canals, power failure, partial or entire failure of water supply, or on account of any other causes not reasonably within the control of the Party claiming such inability. Notwithstanding the foregoing, this provision shall not be construed to apply to the delivery and pressure obligations set forth in Section 3.9.A, or to supplant Section 3.9.C or the specific remedies for Intrusion provided therein.

5.2 Default

A. No Party shall be deemed to be in default hereunder until the passage of thirty (30) days after receipt by such Party of notice of default from the other Party. Upon the passage of thirty (30) days without cure of the default, such Party shall be deemed to have defaulted for purposes of this Contract. Notwithstanding the foregoing, this provision shall not be construed to apply to the delivery and pressure obligations set forth in Section 3.9.A, or to supplant Section 3.9.C or the specific remedies for Intrusion provided therein.

B. Recognizing that each Party's undertakings under this Contract are obligations, failure in the performance of which cannot be adequately compensated in money damages alone,

each Party agrees, in the event of any default on its part, that the other Party shall have available to it the equitable remedy of specific performance in addition to any other legal or equitable remedies which may also be available.

5.3 Conservation

KWSC and the City agree to provide to the maximum extent practicable for the conservation of water, and each agrees that it will operate and maintain its facilities in a reasonable manner that will prevent waste of water. KWSC and the City further agree to implement water conservation and drought management plans as required by state regulations.

5.4 Term of Contract

This Contract shall be effective on and from the Effective Date, and shall continue in force and effect until July 22, 2084; provided, however, that the reservation of capacity to the City in the KWSC System, in the event of any new or amended contract negotiated by and between the Parties and subject to the terms thereof, shall not terminate at the end of the Contract.

5.5 Approval and Consent

Unless otherwise provided herein, any approval or consent required by the provisions of this Contract by KWSC or the City shall be evidenced by a written resolution adopted by the governing body of the Party giving such approval or consent. Upon receipt of such written resolution duly certified by the appropriate Party, KWSC or the City can conclusively act on the matter requiring such approval.

5.6 Modification and Amendment

This Contract may be amended upon the written consent of the respective Board of KWSC and the Council of the City, subject to the concurrence (to the extent required) of USDA-RD; provided, however, no amendment to this Contract shall affect the unconditional obligations of such Parties to pay the amounts due to USDA-RD under CTWSC USDA-RD Loans 91-01 and 91-06 and KWSC USDA-RD Loans 91-06 and 91-07.

5.7 Notice Relating to CTWSC Contracts

In the event that KWSC contemplates any amendment or modification of any contract KWSC has with CTWSC pertaining to the supply of water, then KWSC shall give notice to the City of the specific contemplated amendment or modification at least 30 business days prior to making the same, with express reference to this Section 5.7. Within 20 business days of the City's receipt from KWSC of any such notice of contemplated amendment or modification, the City shall provide KWSC with its written consent, which shall not be unreasonably withheld, to such contemplated amendment or modification and/or written objection to all or such portion(s) of such contemplated amendment or modification to which it objects, setting out with

particularity the basis for each such objection. Should the City not provide timely, written notice to KWSC of its specific objection(s), the City shall be deemed to have consented to the same; however, notwithstanding the foregoing, (i) failure on the part of the City to object to any amendment or modification of any contract KWSC has with CTWSC shall not constitute or be deemed to constitute waiver or modification of any provision or requirement of this Contract or compliance therewith, and (ii) this Section is not intended to supplant or modify Section 5.6, Modification and Amendment, or to permit any amendment or modification of this Contract without compliance with Section 5.6. KWSC agrees that it shall not amend or modify its contractual relationship with CTWSC with respect to any provision (i) for which the City has timely provided written objection in accordance with this Section (ii) in such manner that has a material adverse impact on the rights of the City under this Contract. City consent is not required for any amendment or modification of KWSC contracts with CTWSC provided such amendment or modification does not impact this Contract. KWSC shall give the City 5 business days' notice of its determination to go forward with any proposed amendment or modification to which the City has provided written objection.

5.8 Addresses and Notice

Unless otherwise provided herein, any notice, communication, request, reply, or advice (herein severally and collectively, for convenience, called "Notice") herein provided or permitted to be given, made or accepted by any Party to any other Party must be in writing and may be given or be served by depositing the same in the United States mail postpaid, certified and addressed to the Party to be notified, with return receipt requested, or by hand delivering the same to an officer of such Party. Notice deposited in the mail in the manner hereinabove described shall be conclusively deemed to be effective, unless otherwise stated herein, from and after the expiration of three (3) days after it is so deposited. Notice given in any other manner shall be effective only if and when received by the Party to be notified. For the purposes of notice, the addresses of the Parties hereto shall, until changed as hereinafter provided, be as follows:

- | | | |
|----|---------------------|--|
| A. | If to KWSC, to: | Office of the General Manager
Kempner Water Supply Corporation
Post Office Box 103
Kempner, Texas 76539
Telephone: (512) 932-3701
Fax: (512) 932-2546 |
| B. | If to the City, to: | Office of the City Manager
City of Lampasas
312 East Third
Lampasas, Texas 76550
Telephone: (512) 556-6831
Fax: (512) 556-7937 |

The Parties hereto shall have the right from time to time and at any time to change their respective addresses and each shall have the right to specify as its address any other or additional address by at least 15 days written notice to the other Parties hereto.

5.9 State or Federal Laws, Rules, Orders, or Regulations

This Contract is subject to all applicable federal and state laws and any applicable permits, ordinances, rules, orders, and regulations of any local, state, or federal governmental authority having or asserting jurisdiction, but nothing contained herein shall be construed as a waiver of any right to question or contest any such law, ordinance, order, rule, or regulation in any forum having jurisdiction.

5.10 Venue

All amounts due under this Contract, including, but not limited to, payments due under this Contract, shall be paid and be due in Lampasas County, Texas, the County in which the principal administrative offices of KWSC and the City are located. The Parties specifically agree that Lampasas County, Texas, is the place of performance of this Contract.

5.11 Assignment

This Contract may be assigned to USDA-RD as security for KWSC's indebtedness. Otherwise, neither KWSC or the City may assign any interest it may have under this Contract without the prior written consent of the other Party.

5.12 Entire Agreement

This Contract and the contemporaneous Settlement Agreement constitute the entire agreement among the Parties with respect to the sale of treated water by KWSC to the City.

5.13 Applicable Law

This Contract shall be governed by and construed in accordance with the laws of the State of Texas, and the obligations, rights, and remedies of the Parties hereunder shall be determined in accordance with such laws without reference to the laws of any other state or jurisdiction, except for applicable federal laws, rules, and regulations.

5.14 No Third Party Beneficiary

The Parties hereto are entering into this Contract solely for the benefit of themselves and agree that nothing herein shall be construed to confer any right, privilege or benefit on any person or entity other than the Parties.

5.15 Counterparts

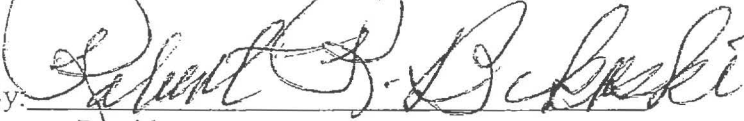
This Contract may be executed in several identical counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument.

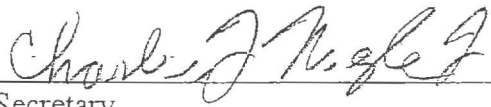
5.16 Conforming Documents

The Parties shall cooperate in conforming and maintaining accurate exhibits and attachments to this Contract, and in assuring correct references, including exhibits and attachments and references arising from or related to any prepayment of USDA-RD CTWSC Loan 91-06 and/or USDA-RD KWSC Loan 91-07, or closing of the Agreement for Sale.

5.17 Signed on the date executed by both Parties.

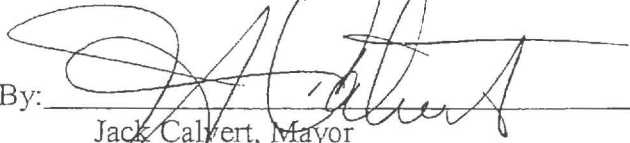
KEMPNER WATER SUPPLY CORPORATION:


By: 
President

Attest: 
Secretary

Date: August 28, 2006

CITY OF LAMPASAS, TEXAS:

By: 
Jack Calvert, Mayor

Attest: 
Stacy Brack, City Secretary

Date: August 28, 2006

UNITED STATES OF AMERICA

By: _____

Name: _____

Title: _____

Date: _____

Rural Development, acting on behalf
of the Rural Utilities Service, State of
Texas, United States Department
of Agriculture

ATTACHMENT 1
USDA-RD Concurrence



United States Department of Agriculture
Rural Development
Texas State Office

AUG 22 2006

The Honorable Jack Calvert
City of Lampasas
312 East Third Street
Lampasas, Texas 76550

Mr. Robert Bikoski, President
Kempner Water Supply Corporation
P.O. Box 103
Kempner, TX 76539

RE: 2006 Wholesale Water Supply Contract

Dear Sirs:

The Agency concurs in the 2006 Wholesale Water Supply Contract, as amended, submitted to this office on July 26, 2006, between Kempner Water Supply Corporation (WSC) and the City of Lampasas, with such concurrence being conditioned upon Kempner WSC paying off USDA Rural Development's notes 91-06 and 91-07.

Notwithstanding positions taken by either party in pending litigation, the parties to this Contract have advised the Agency that neither party asserts an ownership interest in assets of the other contracting party. Certain amendments were made to the Contract to clarify this point. The parties, by accepting this concurrence, agree that the United States has not waived its regulatory or statutory rights, including the right to assert the protections of 7 U.S.C. Sec. 1926(b), notwithstanding any provision contained in the Contract or incorporated therein by reference or appended thereto.

If you have any questions or need additional information, please contact Paco Valentin, Community Programs Director, at (254) 742-9789.

Sincerely,

Bryan Daniel
BRYAN DANIEL
State Director

101 South Main • Federal Building, Suite 102 • Temple, TX 76501
Phone: (254) 742-9789 • Fax: (254) 742-9749 • TDD: (254) 742-8712 • Web: <http://www.rurdev.usda.gov>

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KEMPNER WATER SUPPLY CORPORATION AND CITY OF LAMPASAS CAPITAL POLICY

This capital policy has been developed and adopted for the purpose of clarifying when a repair constitutes a capital improvement, as opposed to a non-capital repair, and which clearly delineates between KWSC O&M Cost and capital improvements to the system, permitting proper KWSC O&M Cost allocations in accordance with accepted principles and policies of the American Water Works Association, as required by the 2006 Wholesale Water Supply Contract between Kempner Water Supply Corporation (KWSC) and the City of Lampasas (City) (2006 Contract). Refer to Section 3.5C of the 2006 Contract. From time to time, KWSC and the City may be called upon to determine whether a particular expenditure should be treated as a “repair” or “capital improvement”. In order to promote uniformity in the decision making, the following guidelines for delineating between repair expenditures and capital expenditures are adopted by KWSC and the City. These guidelines are intended to aid and assist in the decision making process and in no way alter or take precedence over what is set out and established in the 2006 Contract.

Definitions

The following terms and expressions as used in this Policy, unless the context clearly shows otherwise, shall have the following meanings:

“Repair” means that an asset is restored and fully functional by replacing a part, and by putting together that which is torn or broken. A repair consists of any work that restores or extends the useful life of an existing asset and which is not part of general maintenance and operations (i.e. repairing a break in a line, periodic lubrication of moving parts).

“Capital improvement” means the replacement and upgrade, expansion, development, or rehabilitation of capital water system assets that either extends the useful life or reliability of the asset, system or system component or adds new capabilities to enhance the asset, system or system component’s performance. A capital improvement consists of replacements, upgrades or provides for extension of service of an existing asset and that is not used for the general operation or maintenance of the system.

Examples of Capital Improvement

Repair (capital) – Adding a new pump in an existing expansion slot of a pumping facility to increase the facility’s pumping capacity to its design maximum limit (an expansion upgrade).

Replacement of one or more constant speed pumps with a new constant speed longer-life pump (higher quality upgrade), thereby permitting the facility to be used for an additional 10 years.

Replacement of a constant speed pump with a same capacity variable speed pump (capability enhancement upgrade) permitting more flexible operation of the facility.

In the event that further assistance is required in determining whether the expenditure is a repair or capital improvement, the attached Exhibit A chart is intended to provide further guidance. The chart includes simplified examples and is not intended to be all inclusive.

Operations and Maintenance Costs

Operation and maintenance cost allocations are established in the 2006 Contract Section 3.5 and should be referred to when determining cost allocations and expenditures. If questions arise regarding whether or not an expense should be classified as an Operations and Maintenance expense, a repair or a capital improvement reference should be first taken from the 2006 Contract and then from the attached Exhibit A and from definitions provided by the American Water Works Association.

Allocation of Repair or Capital Improvement Costs

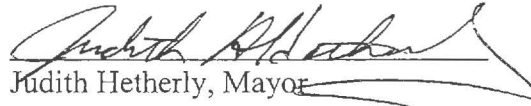
Allocations of such costs shall be in compliance with the 2006 Contract Section 3.5 C.1. Capital expenditures need to be signed off on by both parties prior to expenditure of any funds, unless an emergency situation exists. KWSC should provide the City with a written explanation for the capital expenditure with a section for the City to sign off on or provide written notice back to KWSC as to why the City may oppose the expenditure or dispute it as a capital expenditure.

Dispute Resolution

In the event a dispute arises between KWSC and the City regarding whether or not a particular KWSC expense should be treated as a repair expense or a capital expense, *within 15 days from written notification of either party to the other party that such dispute cannot be remedied*, such dispute shall be reviewed by a committee of four, two from KWSC and two from the City chosen by the president of KWSC Board of Directors and the Mayor of the City. The committee shall make every effort to help the two parties come to terms. If the parties cannot come to terms with the help of the committee, *within 30 days from the appointment of the committee*, it shall then be submitted to a mutually agreed upon independent Professional Engineer and Certified Public Accountant. In the event such independent Professional Engineer and Certified Public Accountant makes a determination as to how the disputed expense should be characterized, the characterization shall be final and binding upon KWSC and the City. The parties to any such dispute shall bear their own respective professional fees and expenses incurred therein, except that the disputing parties shall split the charges and expenses of the independent engineer and accountant, one-half to be borne by KWSC and the remaining one-half to be borne by the City.

In the event that there is a dispute regarding engineering issues regarding any repair or capital matter, KWSC and the City shall refer to the 2006 Contract Section 4.4 regarding "Dispute Resolution Concerning Engineering Issues".

PASSED and APPROVED by the City Council of the City of Lampasas on the 11th
 , day of August , 2008.


Judith Hetherly, Mayor

PASSED and APPROVED by the Kempner Water Supply Corporation Board of
Directors on the 20th, day of August, 2008.

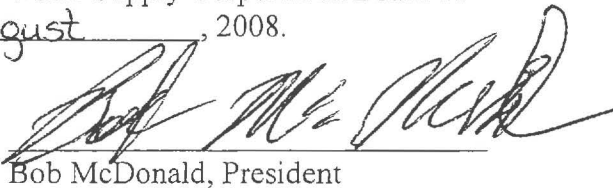

Bob McDonald, President

EXHIBIT A

	Repair Expenses		Capital Improvements Expenses
1.	Accounting. Relatively low cost per unit and recur on a frequent or regular basis – one or more times per budget year. Examples: Pipeline leak repair or monthly sampling. Expenditure is expensed.	1.	Accounting. Relatively high cost per unit, infrequent-less than annually. Examples Planned, engineered project – water treatment plant expansion or transmission pipeline upsizing in high growth area. Expenditure is capitalized.
2.	Expected Useful Life. Items having a useful life of less than two years. Examples: Computer and software.	2.	Expected Useful Life. Items having a useful life of two years or more. Examples: Filter media replacement or ground storage tank.
3.	Purpose. Consumable items used to operate storage, transmission, metering, and remote monitoring of the system. Examples: Contract repairs, or repair inventory items such as coupling or pipe joints.	3.	Purpose. Items that increase holdings in property or increase or replace such things as capacity, water supply services, treatment, storage, transmission, metering, and remote monitoring of the system. Example: Construction of new treatment facilities or transmission lines.
4.	Consultation Application. Consultation incidental to normal or annual support requirements.	4.	Consultation Application. Engineering and legal fees for projects. Examples: Strategic planning, system upgrade and/or capacity expansion; legal for property acquisition, easements.
5.	Maintenance. Repairs of System. Examples: Pipeline leak repair or SCADA RTU repair.	5.	Maintenance. Replacement or rehabilitation of facilities; replacement of dilapidated facilities or items that have exceeded useful life. Example: major reconstruction of storage tank due to obsolescence.
6.	Construction. Correction. Example: Rerouting a pipeline improperly placed in easement.	6.	Construction. New construction. Example: Building a new storage tank.
7.	Labor. Labor incidental to day to day operations. Examples: Employee wages, salaries and benefits.	7.	Labor. Labor used for In-house capital projects. Example: In-house sub-contract (pro-rate share of total compensation).



United States Department of Agriculture • Rural Development
101 South Main • Suite 102 • Temple, TX 76501

Phone: (254) 742-8788 • Fax: (254) 742-8748 • TDD: (254) 742-8712 • Web: <http://www.rurdev.usda.gov>

FAX COVER SHEET

DATE: AUGUST 22, 2006

TO: ROBERT BIKOSKI, PRESIDENT

FROM: Connie Petru, Community Programs
Texas State Office

FAX NUMBER: 512-932-2546

TELEPHONE NUMBER: (254) 742-9793

PHONE NUMBER:

FAX NUMBER: (254) 742-9749

SUBJECT: Water Supply Contract

NO. OF PAGES INCLUDING COVER: 2

message:

CC: CITY OF LAMPASAS

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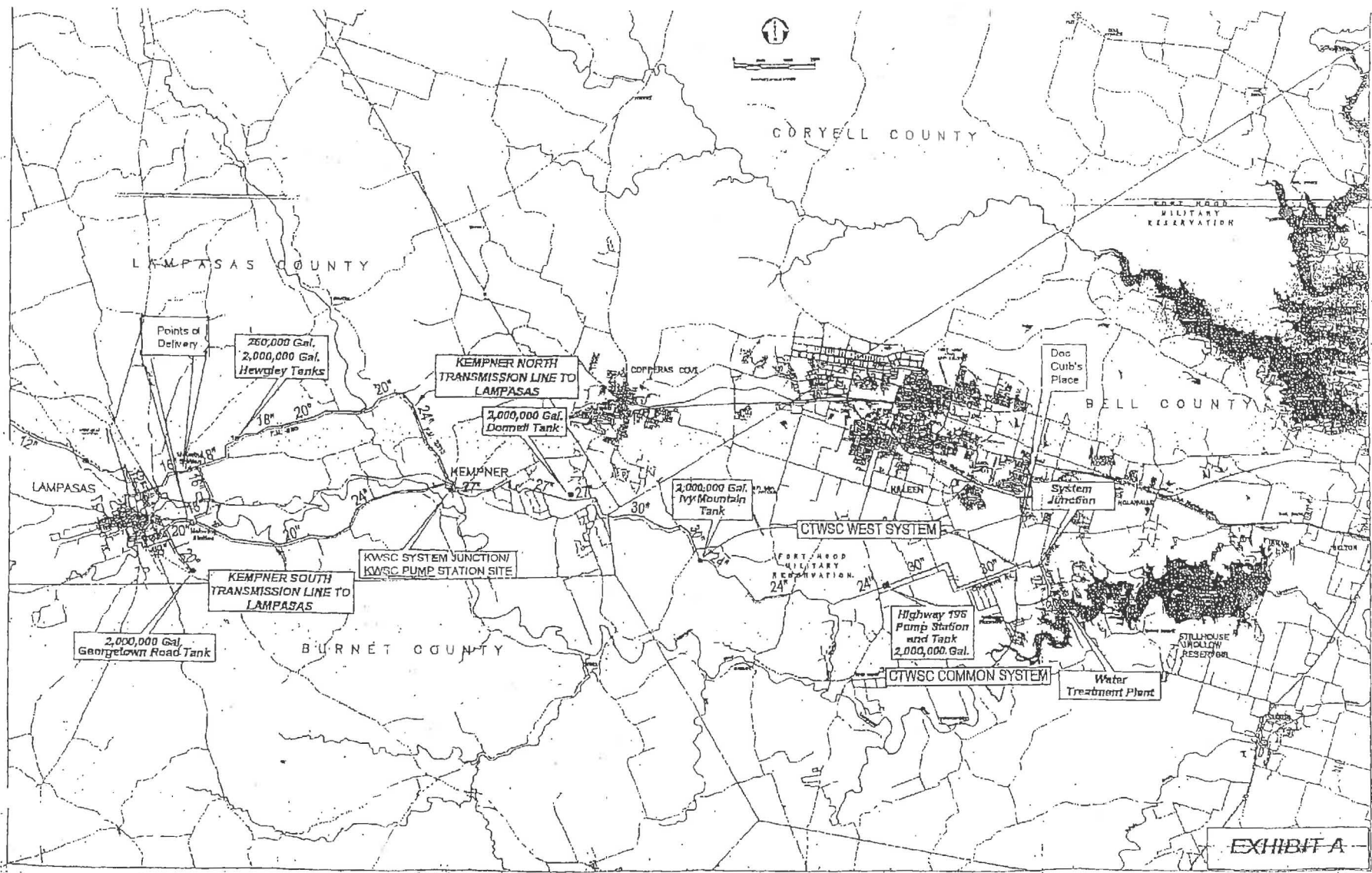


EXHIBIT A

EXHIBIT A
System Map

EXHIBIT B
Kallman Estimate

PROJECT COST ESTIMATE

Conceptual
 Preliminary
 Final

Prepared by: Steven D. Kallman, P.E., R.P.L.S. Date: October 6, 2004

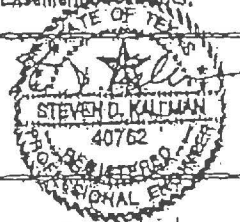
PROJECT: Contract Mediation with Kempner WSC
 LOCATION: Harker Heights, Bell County, Texas
 TYPE OF IMPROVEMENTS: Water Distribution System
 CLIENT NAME: Central Texas WSC
 CLIENT ADDRESS: 4020 Lakewood Drive, Harker Heights, Texas 76548-8607
 CLIENT PHONE: (254) 698-2779
 CLIENT FAX: (254) 698-4105

#	Description	Amount
1.	200,000 Gallon Ground Storage Tank, 880 Foot Overflow on 0.442 Acre Tract Adjacent to Hwy. 185 Pump Station Site	\$ 175,000.00
2.	Booster Pump Station on Same Site Above Water Line and Gravel Access Road to Same Site Above; Purchase 4,023' x 30' Strip of Land Adjacent to and East of Hwy. 185 Pump Station Site from Chaparral Road to Pump Station Site	\$ 1,167,077.00
3.	18" Water Line Paralleling Existing 24" Water Line along West Side of Sillhouse Lake Road in Private Easements yet to be Acquired	\$ 500,000.00
4.	2 - 2000 GPM, 800 HP High Service Pumps, Starters, Piping, Valves and Related Items at Existing Water Treatment Plant site to Increase Firm Pumping Capacity from 8,050 GPM (14.03 MGD) to Minimum 14,692 GPM (16.17 MGD)	\$ 312,600.00
5.	Relocate 2 West Bell Meters from Hwy. 185 Pump Station Site to 0.442 Acre Site	\$ 25,000.00
6.	Remove West Bell Meter and Plug Water Line at Fort Hood Site; Replace 1,400 L.F. of 8" Water Line	\$ 50,000.00
7.	Relocate Kempner WSC Meter from Ivy Mountain Tank Site to Hwy. 185 Pump Station Site at Inlet to Tank	\$ 25,000.00
TOTAL		\$ 2,264,677.00

Notes:

1. Item Nos. 1, 2, 4, 5, 6 and 7 include 10% Construction Contingency, 10% Engineering and 5% for Special Items such as Surveying, Geotechnical and Environmental Services.
2. Item No. 3 includes 10% Contingency and \$22,500. Engineering to Complete Project. No Costs are included in Item No. 3 to Purchase Easements or for Legal Fees to Prepare Easement Documents.

S.D. KALLMAN, L.P.
 ENGINEERS AND ENVIRONMENTAL CONSULTANTS
 1108 South Meys, Suite 100
 Round Rock, Texas 78684
 Phone: (512) 218-4404 Fax: (512) 218-1686



10-06-09

PROJECT COST ESTIMATE

_ Conceptual X Preliminary _ Final

Prepared by: Steven D. Kellman, P.E., R.P.L.S. Date: October 5, 2004

PROJECT: Chaparal Pump Station to replace Hwy. 195 Pump Station
 LOCATION: Adjacent to and north of Hwy. 195 Pump Station on 0.442 Acre Site
 TYPE OF IMPROVEMENTS: High Service Pump Station, Water Line and Access Road
 CLIENT NAME: Central Texas WSC
 CLIENT ADDRESS: 4020 Lakeliff Drive, Harker Heights, Texas 76548-8607
 CLIENT PHONE: (254) 698-2778
 CLIENT FAX: (254) 698-4105

1	Bond and Mobilization	L.S.	\$ 20,000.00	1	\$ 20,000.00
2	Excavation	L.S.	\$ 28,000.00	1	\$ 28,000.00
3	Concrete	L.S.	\$ 42,000.00	1	\$ 42,000.00
4	Piping, Valves, Meters and Meter Vaults	L.S.	\$ 366,000.00	1	\$ 366,000.00
5	Vault Covers and Grating	L.S.	\$ 27,000.00	1	\$ 27,000.00
6	1600 Square Foot Building	L.S.	\$ 80,000.00	1	\$ 80,000.00
7	1500 GPM, 150 HP High Service Pump and Can	EA.	\$ 35,000.00	2	\$ 70,000.00
8	Electrical	L.S.	\$ 150,000.00	1	\$ 150,000.00
9	Trench Safety	L.S.	\$ 1,000.00	1	\$ 1,000.00
10	Chain Link Gorse Fence; Access Road Fence; Three Gates	L.S.	\$ 3,600.00	1	\$ 3,600.00
11	30" x 16" Tapping Sleeve and Valve	L.S.	\$ 7,500.00	1	\$ 7,500.00
12	16" PVC, C-905-CL, 150 Water Line	L.F.	\$ 40.00	350	\$ 14,000.00
13	Silt Fence	L.F.	\$ 2.00	640	\$ 1,280.00
14	Restoration and Revegetation	S.Y.	\$ 1.00	3,360	\$ 3,360.00
15	All Weather Access Road and Parking	S.Y.	\$ 6.00	910	\$ 7,260.00
16	18" CGMP Driveway Culvert	L.F.	\$ 36.00	32	\$ 1,152.00
17	Headwalls for Culvert	EA.	\$ 1,500.00	2	\$ 3,000.00
18	12" Modulating Valve and Vault Feeding 200,000 Gallon Ground Storage Tank	L.S.	\$ 15,000.00	1	\$ 15,000.00
19	350 KW Emergency Generator	EA.	\$ 93,500.00	1	\$ 93,500.00
PRELIMINARY ESTIMATED CONSTRUCTION COST					\$ 933,682.00
10% CONTINGENCY					\$ 83,368.00
10% ENGINEERING					\$ 83,368.00
6% FOR SITE ACQUISITION FOR 30 FOOT WIDE ACCESS TO SITE AND SURVEYING GEOTECHNICAL AND ENVIRONMENTAL SERVICES					\$ 46,683.00
ESTIMATED TOTAL PROJECT COST					\$1,167,077.00



 STATE OF TEXAS
 PROFESSIONAL ENGINEER
 Steven D. Kellman
 No. 10205

EXHIBIT C
Amortization Schedules

EXHIBIT D
CTWSC O&M Calculation Examples

CTWSC O&M EXAMPLES – Section 3.5

Definitions for purposes of the examples:

“City Percentage” is the percentage calculated as set forth in Section 3.5.C.1 (metered flow of treated water into the City at City Points of Delivery by metered pump discharge flow from State Highway 195 Pump Station, including any flow from KWSC New Facilities; or City Use divided by City Use + KWSC Use + KWSC New).

“City Use” means water delivered to City Points of Delivery.

“KWSC Take” means all water delivered to KWSC from CTWSC.

“KWSC Volume Percentage” means KWSC Take divided by Total CTWSC Sales.

“KWSC Use” means KWSC Take, less City Use

“KWSC New” means water From KWSC New Facilities.

“Total CTWSC Sales” means all water delivered to CTWSC customers.

“Volume Bill” means the amount CTWSC bills to KWSC monthly for O&M, **absent** application of a “floor.” The Volume Bill is calculated by multiplying the CTWSC O&M on the Existing System (“CTWSC O&M”) by the percentage calculated by dividing the volume of treated water delivered to KWSC by the total volume of treated water delivered to all customers of CTWSC and multiplying by 100 (KWSC Take divided by Total CTWSC Sales x 100).

“Floor Bill” means the amount CTWSC bills to KWSC monthly for O&M in the event that a floor applies. The Floor Bill is calculated by multiplying CTWSC O&M by the floor calculated pursuant to Section 3.5.B.1.

1. As information, City Use, KWSC Use, and Total CWSC Sales figures are from the December 2005 CTWSC bill.
City Use 31,718,000
KWSC Use 53,106,000
KWSC Take = 84,824,000.
KWSC New = 0.
KWSC Volume Percentage = 53%.
City Percentage = 31,718,000 divided by 84,824,000 = 37%.
CTWSC Total Sales = 159,848,746
Assume CTWSC O&M = \$100,000

Volume Bill = \$100,000 x [KWSC Volume Percentage, i.e., KWSC Take 84,824,000 divided by Total CTWSC Sales 159,848,746 x 100 = 53%] = \$53,000
No floor applies (53% exceeds 42%).

CALCULATION:

City Bill = CTWSC O&M x KWSC Volume Percentage x City Percentage = \$100,000 x 53% x 37% = \$19,610.

KWSC Bill = \$33,390.

2. Same assumptions as 1, but KWSC Use is 25,000,000 and KWSC New is 28,106,000.
City Percentage remains 37%. (City Use-31,718,000, divided by 84,824,000, or City Use + KWSC Use 25,000,000 + KWSC New 28,106,000).
Assume CTWSC Total Sales = 131,742,746 (decreased by lost sales of KWSC New of 28,106,000).
KWSC Take (City Use 31,718,000 + KWSC Use 25,000,000 = 56,718,000) divided by CTWSC Total (131,742,746) = 43.052%, KWSC Volume Percentage.
No floor applies (43.052% exceeds 42%).
Assume CTWSC Total O&M = \$100,000.
Volume Bill = \$43,052.
City Percentage = 37%. City pays \$15,929.24, KWSC pays \$27,122.76.
3. Same assumptions as 1, but KWSC Use is 0 and KWSC New is 53,106,000.
City Percentage remains 37% (City Use divided by City Use +KWSC Use plus KWSC New is same percentage as in Example 2).
Assume CTWSC Total = 106,742,746 (decreased by lost sales of KWSC New of 53,106,000).
KWSC Take (City Use 31,718,000 + KWSC Use 0) = 31,718,000, divided by CTWSC Total 106,742,746 = 29.7%, KWSC Volume Percentage.
Floor applies (29.7% is less than 42%).
Assume CTWSC Total O&M = \$100,000.
Volume Bill without floor would be \$29,700.
City Bill without floor would be 37% x \$29,700 = **\$10,989**, and KWSC would pay **\$18,711**.
Floor Bill = \$42,000, for an increment of an additional \$12,300.
 - a. Assume KWSC is still using 1.06 MGD of City water treatment capacity so that City:KWSC capacity ratio is 49:51, not 63:37, for purpose of "floor increment" calculation.

Applying this 49:51 ratio to the "floor increment," City would pay 49% of \$12,300, or an additional \$6027. KWSC would pay 51% of \$12,300, or an additional \$6273.

Total City Bill: $\$10,989 + \$6027 = \$17,016$.
Total KWSC Bill: $\$18,711 + \$6273 = \$24,984$.

b. Same assumptions as in 3.a., but KWSC has restored the 1.06 MGD to the City and now the City:KWSC capacity ratio is 63:37.

Applying this 63:37 capacity ratio to this "floor increment," City would pay 63% of $\$12,300$, or an additional $\$7749$. KWSC would pay 37% of the increment, or an additional $\$4551$.

Total City Bill: $\$10,989 + 7749 = \$18,738$.
Total KWSC Bill: $\$18,711 + \$4551 = \$23,262$.

4. Same assumptions as 3, but assume KWSC reduces its share of CTWSC WTP capacity by 10% without the City acquiring that capacity, resulting in a floor of 37.8% under the CTWSC Wholesale Contract.

City Percentage remains 37% (City Use + KWSC Use plus KWSC New is same as in Example 2 and 3).

Assume CTWSC Total = 106,742,746 (decreased by KWSC New of 53,106,000).
KWSC Take (City Use 31,718,000 + KWSC Use 0) = 31,718,000, divided by
CTWSC Total 106,742,746 = 29.7%.

Floor applies (29.7% is less than 37.8%).

Assume CTWSC Total O&M = $\$100,000$.

Volume Bill without floor would be $\$29,700$.

City Bill without floor would be $37\% \times \$29,700 = \$10,989$, and KWSC would pay $\$18,711$.

Floor Bill would be $37.8\% \times \$100,000 = \$37,800$, for an additional increment of $\$8100$. Applying the 63:37 capacity ratio to the increment (since the City did not acquire KWSC's capacity, the ratio remains unchanged), the City would pay $63\% \times \$8100$ or an additional $\$5103$. KWSC would pay $37\% \times \$8100$ or an additional $\$2997$.

Total City Bill: $\$10,989$ plus $\$5103 = \$16,092$.

Total KWSC Bill: $\$18,711 + \$2997 = \$21,708$.

5. Assume KWSC reduces its capacity completely, the floor becomes 26.5%.

City does not acquire KWSC capacity. Assume City use drops to 18,000,000.

Otherwise same assumptions as in 4.

City Percentage = $18,000,000$ divided by $18,000,000 + 53,106,000 + 0 =$
 $18,000,000$ divided by $71,106,000 = 25.31\%$.

Assume CTWSC Total Sales = $100,000,000$.

KWSC Take (City Use 18,000,000 + KWSC Use 0) = 18,000,000, divided by
CTWSC Total 100,000,000 = 18%, KWSC Volume Percentage.

Floor applies (18% is less than 26.5%).

Assume CTWSC Total O&M = \$100,000.

Volume Bill would be \$18,000 (18% x 100,000).

City Bill without floor would be 25.31% x \$18,000 = \$4555.80, and KWSC would pay \$13,444.20.

Floor Bill would be \$26,500 (26.5% x 100,000),

With floor of 26.5%, KWSC Bill = \$26,500, for an additional increment of \$8500.

Applying 63:37 ratio: City would pay an additional \$5355 and KWSC would pay an additional \$3145.

Total City Bill: \$4555.80 + \$5355 = \$9910.80.

Total KWSC Bill: \$13,444.20 + \$3145 = \$16,589.20.6. Under Section

3.1.B, City has right to acquire up to 2.06 MGD of additional capacity, on a volume-only O&M basis. Floor does not apply to and City will not pay floor on CTWSC O&M on this amount of additional capacity.

7. Same assumptions as 5, but (i) City has acquired relinquished KWSC capacity (i.e., in addition to or other than the volume-only 2.06 MGD referenced in Section 3.1.B) so that floor remains 42%, and (ii) despite KWSC Use being 0, CTWSC Total Sales have increased to 180,000,000.

City Percentage remains 25.31%.

KWSC Take = (18,000,000 + KWSC Use 0 = 18,000,000, divided by CTWSC Total Sales 180,000,00 = 10%, KWSC Volume Percentage.

Floor applies (10% is less than 42%).

Assume CTWSC O&M = \$100,000.

Volume Bill would be \$10,000 (10% x \$100,000).

City bill without floor would be 25.31% x \$10,000 = \$2531, and KWSC would pay \$7469.

Floor Bill would be 42% x \$100,000 or \$42,000, for an additional increment of \$32,000.

If City has acquired 100% of KWSC relinquished CTWSC WTP capacity (leaving City with 7.68 MGD), then City would pay \$2531 + 32,000 = \$34,531. KWSC would pay \$7469.

EXHIBIT E
Tank Assessment

TANK MAINTENANCE ANNUAL PAYMENT

INITIAL PAYMENT:

The Hewgley Tank is the first tank scheduled to have maintenance in 2007 and the estimate for maintenance is \$300,000. The plan is to bid the project in July-August 2007, draw the tank down in September to perform the work and have the work complete by December 2007. The proposed initial payment schedule for year one is calculated by using \$325,000 as a base amount, with the first payment by both parties to be made in November 2006. KWSC has provided a break down that would take into consideration that we are now three months into the contract time period and the time frame for when work on the first tank needs to commence. The total initial payment would be **\$81,250** with the City's portion being **\$29,193.94** and KWSC portion **\$52,056.06**, based on the average monthly percentage as used for the monthly water billing, for December 2005 through August 2006 (.35931). The last payment for the first tank would be made on or about August 1, 2007, so that work on the Hewgley Tank can be complete by December 2007. The first payment would be due in November 2006. Future payments would be based on the monthly percentage as calculated in Section 3.5.C.1.

TEN-YEAR MONTHLY REVOLVING PAYMENT SCHEDULE (TO BE REVISED IN YEAR 5 AND REVIEWED AND ADJUSTED EVERY YEAR AT THE ANNUAL MEETING):

There are four tanks identified that need to have maintenance performed as follows:

2007 – Hewgley Tank #2 - \$300,000
2008 – Georgetown Tank - \$325,000
2009 – Donnell Tank - \$350,000
2010 – Hewgley Tank #1 - \$100,000

The City is not responsible for maintenance to the Donnell Tank, which is scheduled for maintenance in 2009 (Section 3.5.E.1, page 27 of agreement). The total estimated amount of repair for the Hewgley Tank #2, Georgetown Tank and the Hewgley #1 Tank is \$725,000. KWSC would be responsible for the Donnell Tank at \$350,000.

ADDITIONAL COMMENTS:

Every year at the Annual Meeting, the parties can adjust the Annual Tank Payment to be sure it is still accurate (Section 3.5.E.2, page 27 of agreement). The City pays the City's Percentage of the Annual Tank Payment, which can fluctuate. KWSC will pay the City on a quarterly basis the interest rate accrued on the City's portion of the funds on deposit.

In addition to the tanks listed above there will be future maintenance/repair costs associated with the Ivy Mountain Tank and the State Highway Tank, which is not currently included in the Ten-Year Rolling Schedule as proposed.

PROPOSED TANK MAINTENANCE TEN-YEAR ROLLING SCHEDULE

CITY	KWSC																																																				
<u>\$325,000.00</u>																																																					
Year 1:	\$325,000.00 / 12 months equals \$27,083.33																																																				
	Total - Initial Payment will be \$81,250.00 breakdown is as follows:																																																				
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**this percentage was calculated as an average for the City from Dec. 05 thru Aug 06.

Year 2: (\$300,000)	\$25,000 x City's monthly%	KWSC's %
Year 3: (\$350,000)	\$29,166.67 x 0	KWSC 100% (Donnell Tank)
Year 4: (\$100,000)	\$8,333.33 x City's monthly %	KWSC's %
Year 5: (\$150,000)	\$12,500 x City's monthly %	KWSC's %
Year 5 reevaluate and reestablish the maintenance schedule and Annual Tank Payment.		
Year 6: (\$150,000)	\$12,500 x City's monthly %	KWSC's %
Year 7: (\$150,000)	\$12,500 x City's monthly %	KWSC's %
Year 8: (\$150,000)	\$12,500 x City's monthly %	KWSC's %
Year 9: (\$175,000)	\$14,583.33 x City's monthly %	KWSC's %
Year 10: (\$200,000)	\$16,666.67 x City's monthly %	KWSC's %

11/9/2006 Tank Maintenance Annual Payment

CAUSE NO. 207,477

KEMPNER WATER SUPPLY CORPORATION	§	IN THE DISTRICT COURT
	§	
	§	
VS.	§	169TH JUDICIAL DISTRICT
	§	
CENTRAL TEXAS WATER SUPPLY CORPORATION	§	
	§	BELL COUNTY, TEXAS

AMENDED SETTLEMENT, COMPROMISE, RELEASE AND TOLLING AGREEMENT

This Amended Settlement, Compromise, Release and Tolling Agreement (“Agreement”) is entered into by and between KEMPNER WATER SUPPLY CORPORATION (“KWSC”) and THE CITY OF LAMPASAS, TEXAS (the “City”) on the last date written herein. KWSC and the City may hereafter be collectively referred to as “Parties.” The Parties agree as follows:

WHEREAS, KWSC is a Texas non-profit corporation, organized and established under Chapter 67, Texas Water Code (formerly Article 1434a, R.C.S. of Texas 1924, as amended), and KWSC independently owns and operates its potable water distribution system in order to provide potable water to its customers; and

WHEREAS, the City is a Texas municipal corporation chartered under Article XI, § 5 of the Texas Constitution, and the City independently owns and operates its potable water distribution system in order to provide potable water to its customers; and

WHEREAS, as part of settlement of litigation between KWSC and the City in 2001, the Parties agreed that prior contracts between them needed to be amended,

modified and completely replaced by the Wholesale Water Supply Contract entered into as of September 13, 2001 (the "2001 Contract"); and

WHEREAS, KWSC and the City have operated pursuant to the 2001 Contract to this date; and

WHEREAS, disputes have arisen between and among KWSC, the City, and Central Texas Water Supply Corporation ("CTWSC"), resulting in litigation brought by KWSC in Cause No. 15,419, *Kempner Water Supply Corporation vs. Central Texas Water Supply Corporation*, 27th Judicial District Court of Lampasas County, Texas, said lawsuit having been transferred to Bell County and now referred to as Cause No. 207,477 C, *Kempner Water Supply Corporation vs. Central Texas Water Supply Corporation*, 169th Judicial District Court of Bell County, Texas ("Lawsuit"); and

WHEREAS, on February 21, 2006, the City and KWSC agreed to a 2006 Wholesale Water Supply Contract which was submitted to the United States Department of Agriculture-Rural Development ("USDA-RD") for its concurrence; and

WHEREAS, on February 21, 2006, the City and KWSC also agreed to a Settlement, Compromise, and Release Agreement which was also submitted to USDA-RD for its concurrence; and

WHEREAS, in response to the comments of USDA-RD, the City and KWSC have agreed to and submitted to USDA-RD certain amendments to the 2006 Wholesale Water Supply Contract (the "2006 Contract" herein means and includes agreed amendments

thereto) (a copy of the 2006 Contract is attached hereto as Exhibit A), which 2006 Contract shall be effective upon written concurrence from USDA-RD in the form attached hereto or as it may be modified in future by agreement of the Parties in order to gain the concurrence of USDA-RD; and

WHEREAS, KWSC has obtained a commitment for approximately \$33 million in loan funds from the Texas Water Development Board ("TWDB") in order to acquire additional water treatment, storage and transmission facilities, through construction and through purchase, and to pay off all KWSC indebtedness to USDA-RD ("TWDB Loans" as defined in the 2006 Contract); and

WHEREAS, the Parties have determined that it is in their mutual best interests and in the best interests of their respective members and customers to provide for the 2006 Contract to become effective in the event that KWSC repays all of its indebtedness to USDA-RD before USDA-RD provides its concurrence in the 2006 Contract, or, if those events do not occur by September 1, 2006, to provide for interim operation with a tolling agreement and nonsuit pending the 2006 Contract becoming effective, and further to provide a means to fully settle and resolve all claims and counterclaims between them that have been asserted and/or which might have been asserted in the above-styled and numbered clause, and to amend the February 21, 2006 Settlement, Compromise and Release Agreement to address the matters herein; and

NOW, THEREFORE, for the consideration herein expressed, the Parties agree as follows:

1. Superseding Amendment. This Amended Settlement, Compromise, Release and Tolling Agreement supersedes and replaces the February 21, 2006 Settlement, Compromise, and Release Agreement executed by the Parties.

2. Condition Precedent and Effective Date. A condition precedent to the effectiveness of paragraphs 6, 7 and 8 of this Agreement is that the 2006 Contract has become effective. The effective date of paragraphs 6, 7 and 8 of this Agreement ("Effective Date") shall be the date, or earlier date, upon which the 2006 Contract becomes fully effective under either or both of 2.a. or 2.b. below (i.e., not merely in interim operation). The remaining covenants of this Agreement shall become effective upon execution of this Agreement by the Parties. The 2006 Contract shall become effective (the "Effective Date" of the 2006 Contract as defined therein) on the earliest to occur of the following:

a. Concurrence by USDA-RD to the 2006 Contract. KWSC and the City have been notified by letter dated August 22, 2006, from Bryan Daniel, State Director of USDA-RD, that USDA-RD has concurred in the 2006 Contract, conditioned only upon the payoff by KWSC of USDA-RD Loans 91-06 and 91-07 to KWSC, as evidenced by the security agreements and promissory notes relating thereto. Therefore, upon the date that KWSC warrants to the City that it has

caused to be tendered the amount demanded by USDA-RD in discharge of KWSC indebtedness to USDA-RD for USDA-RD Loans 91-06 and 91-07, the 2006 Contract shall become effective, and paragraphs 6, 7 and 8 of this Agreement shall become effective, irrevocable and fully binding and enforceable between the Parties.

b. Repayment by KWSC of All Indebtedness to USDA-RD. "KWSC Indebtedness" shall mean USDA-RD loans 91-01, 91-02, 91-06 and 91-07 to KWSC as evidenced by the security agreements and promissory notes relating thereto. The Parties agree that upon the date that KWSC warrants to the City that it has caused to be tendered the amount demanded by USDA-RD in discharge of all KWSC Indebtedness to USDA-RD, the 2006 Contract shall become effective between the Parties as if USDA-RD had concurred therein, and paragraphs 6, 7 and 8 of this Agreement shall become effective, irrevocable and fully binding and enforceable between the Parties. KWSC agrees promptly to provide to the City copies of documents confirming such tender to USDA-RD of the amount designated by USDA-RD,

3. Interim Operation/Tolling Agreement/September 1, 2006. If USDA-RD's unconditional concurrence ("2.a" above) or KWSC payoff of KWSC Indebtedness ("2.b" above) has not occurred by September 1, 2006, the Parties shall operate under the Interim

Operation/Tolling Agreement set forth in this paragraph 3 until the 2006 Contract becomes effective.

a. Beginning September 1, 2006, and until the occurrence of "2.a." or "2.b." above, or until the Parties mutually agree otherwise in a duly executed written instrument, the Parties agree to operate on an interim basis under all terms of the 2006 Contract as if fully effective.

b. For purposes of interim operation under the 2006 Contract, the Parties agree that "Effective Date" in the 2006 Contract shall mean September 1, 2006. For example, for purposes of the Effective Date Adjustments in Section 4.9 of the 2006 Contract, "Effective Date" shall be September 1, 2006.

c. USDA-RD. During interim operation under the 2006 Contract, the Parties agree to work diligently and in good faith to take prompt and reasonably necessary steps to secure (i) USDA-RD's unconditional concurrence in the 2006 Contract, including submittal to USDA-RD of any mutually agreed modifications to the 2006 Contract and (if required) settlement agreement, and (ii) KWSC's warranty to the City that it has caused to be tendered the amount demanded by USDA-RD in discharge of all KWSC Indebtedness.

d. Nonsuit and Tolling.

(1) The City and KWSC agree that within 10 calendar days after September 1, 2006, if the 2006 Contract and this Agreement have not

already become effective under "2.a." or "2.b." above, the Parties shall each file a notice of nonsuit without prejudice of all currently pending claims against the other in the lawsuit.

(2) The Parties expressly agree that, provided (i) KWSC is in compliance with this Agreement and the Parties are operating under the 2006 Contract on an interim basis as provided herein, and (ii) KWSC is diligently pursuing funding of TWDB Loans described in the 2006 Contract and still has outstanding unfunded loan commitments from TWDB for the TWDB Loans described in the 2006 Contract, the City will not refile its claims against KWSC. The foregoing notwithstanding, the Parties further agree that (i) unless the 2006 Contract (in its current form or as it may be modified by agreement of the Parties) has become effective pursuant to "2.a." or "2.b." above, the City may re-file these claims at any time after September 1, 2007, and (ii) in the event of such re-filing, KWSC shall not assert Timing Defenses with respect to the Tolling Period (both as defined below). Nothing herein shall constitute any acknowledgment by KWSC as to the validity or merit of any of the City's claims tolled hereunder.

(3) Tolling.

i. The Tolling Period means the period which extends from March 30, 2004 until the earlier of 90 days after September 1,

2007, or such earlier date (if any) of re-filing of the Lawsuit pursuant to paragraph 3.b above with respect to KWSC. The Tolling Period may be extended by written agreement of the Parties.

ii. The Parties agree that all time periods governing any Timing Defenses shall be tolled during the Tolling Period. "Timing Defenses" shall mean any affirmative defenses based on statute(s) of limitation, statute(s) of repose, laches or the passage of time to any claims, known or unknown, that the City may have against KWSC, or to any claims, known or unknown, that KWSC may have against the City. This Agreement shall not revive any claim that is barred before March 30, 2004 by any Timing Defense. Any lawsuit filed pursuant to this subparagraph 3.d shall be deemed by the Parties to be treated as if it were filed on March 30, 2004, so that no prejudice will have occurred by the nonsuit contemplated herein.

4. TWDB Loans. KWSC represents and warrants to the City that, to the best of KWSC's knowledge, information and belief, TWDB does not and will not require review, approval, or any change to the 2006 Contract as a condition of funding the TWDB Loans, as reflected by the TWDB letter attached as Exhibit B.

5. Agreement to Cooperate. In consideration of the undertakings herein, and assuming TWDB seeks no changes to the 2006 Contract, upon the Parties' execution of

this Agreement the City will cooperate with KWSC in seeking the closing of the TWDB Loans, as further set forth in Section 4.6 of the 2006 Contract.

6. City Releases. Effective as of the Effective Date of this Agreement, for and in consideration of the execution by KWSC of the 2006 Contract, and in the further consideration of the releases herein made, sufficiency of which consideration is hereby acknowledged, the City does for itself and its Council Members, agents, employees and assigns, hereby and forever release and discharge KWSC, its members, representatives, employees, agents and assigns, whether specifically mentioned or not, of and from any and all known and unknown liability, actions, causes of action, claims, demands, damages, costs, expenses, claims for contribution or indemnity, and/or compensation of any kind whatsoever arising out of or allegedly relating to any of the following:

(a) the Settlement Agreement executed by the Parties on or about September 13, 2001, in connection with Cause No. 14,130 filed in the 27th Judicial District Court of Lampasas County, Texas ("2001 Settlement Agreement"), together with the Judgment entered in said cause;

(b) the 2001 Contract;

(c) any alleged breach by KWSC of the 2001 Settlement Agreement or the 2001 Contract, or of any prior agreement between the Parties;

(d) any alleged failure of KWSC to comply with any provision of the 2001 Settlement Agreement or 2001 Contract, or of any prior agreement between the Parties;

(e) any alleged conversion by KWSC of any property or property right owned or claimed by the City including (without limitation) rights to raw or treated water or capacity to treat water from CTWSC's water treatment plant and any water storage and transmission capacity in any facilities owned by CTWSC or KWSC;

(f) any alleged failure of KWSC to provide water or water storage or transmission capacity to the City in quantities and/or at rates allegedly required by any contract, including the 2001 Contract and the 2001 Settlement Agreement, at any time up to the effective date hereof;

(g) any claim or action asserted or alleged by the City against KWSC and CTWSC relating to the 2000 Contract, the 2001 Contract, the 2001 Settlement Agreement or to the sale, production, treatment, provision or transmission of water by or from either of the Parties;

(h) any alleged entitlement to attorney's fees or costs by the City relating to the above-listed causes;

(i) any claim for declaratory relief, damages, unjust enrichment, constructive trust, attorneys' fees, costs of suit, interest and other or further relief asserted or which could have been asserted by the City in the Lawsuit, including, without limitation, claims for accounting, over-billing, failure to pay or allow credit for interest on escrow and/or reserve accounts maintained by or for the benefit of KWSC and/or the City;

(j) any and all other claims and/or causes of action which the City has or may have by reasons of the transactions and occurrences described more fully in the pleading identified as the First Amended Petition in Intervention of City of Lampasas, Texas, or any other petition or pleading filed by the City in the Lawsuit, including any alleged entitlement to attorney's fees or costs by the City relating to any of the above or foregoing causes;

PROVIDED, HOWEVER, the foregoing does not release any claims based upon requests by the City for correction of billing errors since January 2006 and Billing Adjustments under Section 4.9B of the 2006 Contract.

7. KWSC Releases. Effective as of the Effective Date of this Agreement, for and in consideration of the execution by the City of the 2006 Contract and of the releases herein made, the sufficiency of which consideration is hereby acknowledged, KWSC does by these presents, for itself, its Board of Directors, its members, employees and assigns, hereby and forever release and discharge the City, its Council Members, representatives, employees, agents and assigns, whether specifically mentioned or not, of and from any and all known and unknown liability, actions, causes of action, claims, demands, damages, costs, expenses, claims for contribution or indemnity, and/or compensation of any kind whatsoever arising out of or allegedly relating to any of the following:

(a) the 2001 Settlement Agreement;

- (b) the 2001 Contract;
- (c) any alleged breach of the 2001 Settlement Agreement or the 2001 Contract by the City, or of any prior agreement between the Parties;
- (d) any alleged failure of the City to comply with any provision of the 2001 Settlement Agreement or 2001 Contract, or of any prior agreement between the Parties;
- (e) any claim or action asserted or alleged by KWSC against the City relating to the 2000 Contract, the 2001 Contract, the 2001 Settlement Agreement or to the sale, production, treatment, provision or transmission of water by or from either of the Parties;
- (f) any alleged entitlement to attorney's fees or costs by KWSC relating to the above listed causes;
- (g) any claim for declaratory relief, damages, unjust enrichment, constructive trust, attorneys' fees, costs of suit, interest and other or further relief asserted or which could have been asserted by KWSC in the Lawsuit, including, without limitation, claims for accounting, over-billing, failure to pay or allow credit for interest on escrow and/or reserve accounts maintained by or for the benefit of KWSC and/or the City;
- (h) any and all other claims and/or causes of action which KWSC has or may have by reasons of the transactions and occurrences described more fully in the pleading identified as Kempner's First Amended Petition and Cross-Action, or any other petition or pleading filed by any party in the Lawsuit, including any alleged entitlement to attorney's fees or costs by KWSC relating to any of the above or foregoing causes;

PROVIDED, HOWEVER, the foregoing does not release any claims based upon requests by KWSC for correction of billing errors since January 2006 and Billing Adjustments under Section 4.9B of the 2006 Contract.

8. Dismissal of Claims. In the event any lawsuit between the Parties is on file at such date as the 2006 Contract becomes effective, then, within ten days after the 2006 Contract becomes effective under paragraph 2.a or 2.b above, the Parties will dismiss with prejudice all claims asserted by them against each other which relate to any of the matters released herein. More particularly, (i) if, at such date, a notice of nonsuit has not been previously filed, then the Parties will dismiss with prejudice all claims asserted against each other in the lawsuit, and (ii) if at such date a re-filing under paragraph 3.d(2) above has occurred, then the Parties will dismiss with prejudice all claims asserted against each other in the new lawsuit contemplated under paragraph 3.d(2) above.

9. Warranty of Authority. KWSC warrants and acknowledges that the Board of Directors of KWSC has approved this Agreement and that the person signing on behalf of KWSC has full authority to execute this Agreement on behalf of KWSC.

10. Warranty of Authority. The City warrants and acknowledges that the City Council of the City has approved this Agreement and that the person signing on behalf of the City has full authority to execute this Agreement on behalf of the City.

11. Doubtful Claims. It is agreed and understood by the Parties that this is a settlement of doubtful and disputed claims and that this settlement is not to be construed

as an admission of liability on the part of the City, KWSC, or any person, entity or corporation hereby released, by all of whom liability is expressly denied.

12. Review of Agreement. It is further acknowledged that the undersigned and the respective Board of Directors and Council Members of the Parties have directed that the undersigned persons execute the same based wholly upon their own judgment and knowledge of the claims, liability questions and alleged damages involved herein.

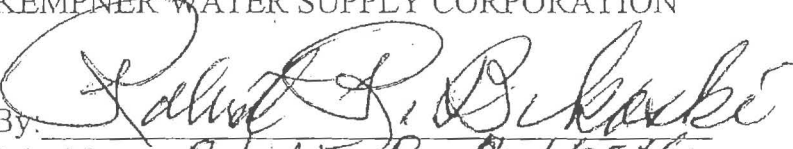
13. Counterparts. This Agreement may be executed in multiple originals. Properly executed signature pages, whether they constitute original signature pages, copied signature pages, or facsimile copied signature pages, may be attached to the original Amended Settlement, Compromise, Release and Tolling Agreement. Any such copied signature page or facsimile copied signature page attached to the original Amended Settlement, Compromise, Release and Tolling Agreement will have the same force and effect as an original signature page.

14. Severability. In the event that, at the behest of USDA-RD or other state or federal agency, any provision contained in this Agreement (including the provision for interim operation, or any aspect thereof, under the 2006 Contract) shall be held to be invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability of such provision shall not affect any other provision of this Agreement, and this Agreement shall be construed (i) as if such invalid, illegal or unenforceable provision had never been contained herein, and (ii) notwithstanding the foregoing, and to

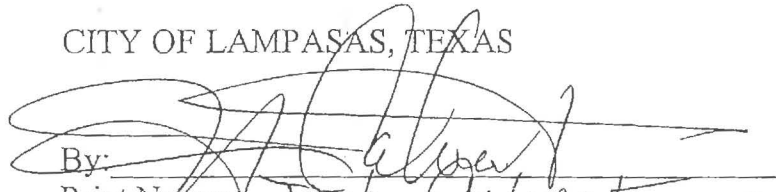
the maximum extent possible, to effectuate the intent of the Parties as set forth in this Agreement and in the 2006 Contract..

WITNESS OUR HANDS on this the 28th day of August,
2006.

KEMPNER WATER SUPPLY CORPORATION

By: 
Print Name: ROBERT R. MIKOSKI
Title: PRESIDENT, RWSC B.O.D.

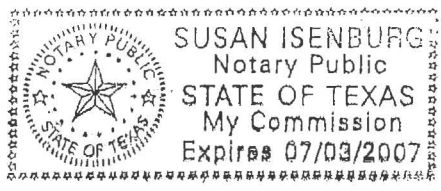
CITY OF LAMPASAS, TEXAS

By: 
Print Name: JACK CALVERT
Title: MAYOR

THE STATE OF TEXAS §
 §
COUNTY OF Lampasas §

BEFORE ME, the undersigned authority, on this day personally appeared Robert R. Bikaski, known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged to me that he/she is authorized to execute this Agreement on behalf of KEMPNER WATER SUPPLY CORPORATION, that he/she understood the same and executed the same for the purposes and consideration therein expressed.

GIVEN UNDER MY HAND and seal of office this the 28th day of August, 2006.

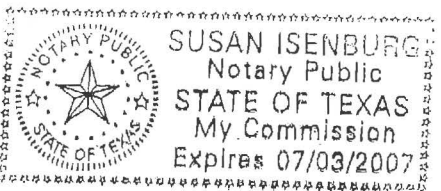


Susan Isenburg
NOTARY PUBLIC, STATE OF TEXAS

THE STATE OF TEXAS §
 §
COUNTY OF Lampasas §

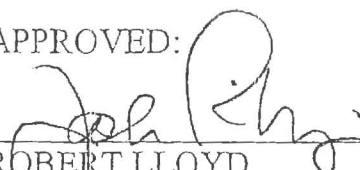
BEFORE ME, the undersigned authority, on this day personally appeared Jack Culvert, known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged to me that he/she is authorized to execute this Agreement on behalf of THE CITY OF LAMPASAS, TEXAS, that he/she understood the same and executed the same for the purposes and consideration therein expressed.

GIVEN UNDER MY HAND and seal of office this the 28th day of August, 2006.

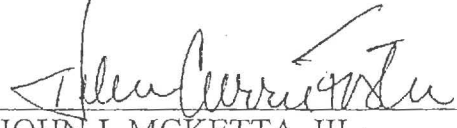


Susan Isenburg
NOTARY PUBLIC, STATE OF TEXAS

APPROVED:



ROBERT LLOYD
JAMES CHRISMAN PHILLIPS
Attorney for Kempner Water Supply Corporation



JOHN J. MCKETTA, III
HELEN CURRIE FOSTER
Attorney for the City of Lampasas

CAUSE NO. 207,477

KEMPNER WATER SUPPLY
CORPORATION

§
§
§
§
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§
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IN THE DISTRICT COURT

VS.

169TH JUDICIAL DISTRICT

CENTRAL TEXAS WATER
SUPPLY CORPORATION

BELL COUNTY, TEXAS

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WHEREAS, in response to the comments of USDA-RD, the City and KWSC have agreed to and submitted to USDA-RD certain amendments to the 2006 Wholesale Water Supply Contract (the "2006 Contract" herein means and includes agreed amendments

thereto) (a copy of the 2006 Contract is attached hereto as Exhibit A), which 2006 Contract shall be effective upon written concurrence from USDA-RD in the form attached hereto or as it may be modified in future by agreement of the Parties in order to gain the concurrence of USDA-RD; and

WHEREAS, KWSC has obtained a commitment for approximately \$33 million in loan funds from the Texas Water Development Board ("TWDB") in order to acquire additional water treatment, storage and transmission facilities, through construction and through purchase, and to pay off all KWSC indebtedness to USDA-RD ("TWDB Loans" as defined in the 2006 Contract); and

WHEREAS, the Parties have determined that it is in their mutual best interests and in the best interests of their respective members and customers to provide for the 2006 Contract to become effective in the event that KWSC repays all of its indebtedness to USDA-RD before USDA-RD provides its concurrence in the 2006 Contract, or, if those events do not occur by September 1, 2006, to provide for interim operation with a tolling agreement and nonsuit pending the 2006 Contract becoming effective, and further to provide a means to fully settle and resolve all claims and counterclaims between them that have been asserted and/or which might have been asserted in the above-styled and numbered clause, and to amend the February 21, 2006 Settlement, Compromise and Release Agreement to address the matters herein; and

NOW, THEREFORE, for the consideration herein expressed, the Parties agree as follows:

1. Superseding Amendment. This Amended Settlement, Compromise, Release and Tolling Agreement supersedes and replaces the February 21, 2006 Settlement, Compromise, and Release Agreement executed by the Parties.

2. Condition Precedent and Effective Date. A condition precedent to the effectiveness of paragraphs 6, 7 and 8 of this Agreement is that the 2006 Contract has become effective. The effective date of paragraphs 6, 7 and 8 of this Agreement ("Effective Date") shall be the date, or earlier date, upon which the 2006 Contract becomes fully effective under either or both of 2.a. or 2.b. below (i.e., not merely in interim operation). The remaining covenants of this Agreement shall become effective upon execution of this Agreement by the Parties. The 2006 Contract shall become effective (the "Effective Date" of the 2006 Contract as defined therein) on the earliest to occur of the following:

a. Concurrence by USDA-RD to the 2006 Contract. KWSC and the City have been notified by letter dated August 22, 2006, from Bryan Daniel, State Director of USDA-RD, that USDA-RD has concurred in the 2006 Contract, conditioned only upon the payoff by KWSC of USDA-RD Loans 91-06 and 91-07 to KWSC, as evidenced by the security agreements and promissory notes relating thereto. Therefore, upon the date that KWSC warrants to the City that it has

caused to be tendered the amount demanded by USDA-RD in discharge of KWSC indebtedness to USDA-RD for USDA-RD Loans 91-06 and 91-07, the 2006 Contract shall become effective, and paragraphs 6, 7 and 8 of this Agreement shall become effective, irrevocable and fully binding and enforceable between the Parties.

b. Repayment by KWSC of All Indebtedness to USDA-RD. "KWSC Indebtedness" shall mean USDA-RD loans 91-01, 91-02, 91-06 and 91-07 to KWSC as evidenced by the security agreements and promissory notes relating thereto. The Parties agree that upon the date that KWSC warrants to the City that it has caused to be tendered the amount demanded by USDA-RD in discharge of all KWSC Indebtedness to USDA-RD, the 2006 Contract shall become effective between the Parties as if USDA-RD had concurred therein, and paragraphs 6, 7 and 8 of this Agreement shall become effective, irrevocable and fully binding and enforceable between the Parties. KWSC agrees promptly to provide to the City copies of documents confirming such tender to USDA-RD of the amount designated by USDA-RD,

3. Interim Operation/Tolling Agreement/September 1, 2006. If USDA-RD's unconditional concurrence ("2.a" above) or KWSC payoff of KWSC Indebtedness ("2.b" above) has not occurred by September 1, 2006, the Parties shall operate under the Interim

Operation/Tolling Agreement set forth in this paragraph 3 until the 2006 Contract becomes effective.

a. Beginning September 1, 2006, and until the occurrence of "2.a." or "2.b." above, or until the Parties mutually agree otherwise in a duly executed written instrument, the Parties agree to operate on an interim basis under all terms of the 2006 Contract as if fully effective.

b. For purposes of interim operation under the 2006 Contract, the Parties agree that "Effective Date" in the 2006 Contract shall mean September 1, 2006. For example, for purposes of the Effective Date Adjustments in Section 4.9 of the 2006 Contract, "Effective Date" shall be September 1, 2006.

c. USDA-RD. During interim operation under the 2006 Contract, the Parties agree to work diligently and in good faith to take prompt and reasonably necessary steps to secure (i) USDA-RD's unconditional concurrence in the 2006 Contract, including submittal to USDA-RD of any mutually agreed modifications to the 2006 Contract and (if required) settlement agreement, and (ii) KWSC's warranty to the City that it has caused to be tendered the amount demanded by USDA-RD in discharge of all KWSC Indebtedness.

d. Nonsuit and Tolling.

(1) The City and KWSC agree that within 10 calendar days after September 1, 2006, if the 2006 Contract and this Agreement have not

already become effective under "2.a." or "2.b." above, the Parties shall each file a notice of nonsuit without prejudice of all currently pending claims against the other in the lawsuit.

(2) The Parties expressly agree that, provided (i) KWSC is in compliance with this Agreement and the Parties are operating under the 2006 Contract on an interim basis as provided herein, and (ii) KWSC is diligently pursuing funding of TWDB Loans described in the 2006 Contract and still has outstanding unfunded loan commitments from TWDB for the TWDB Loans described in the 2006 Contract, the City will not refile its claims against KWSC. The foregoing notwithstanding, the Parties further agree that (i) unless the 2006 Contract (in its current form or as it may be modified by agreement of the Parties) has become effective pursuant to "2.a." or "2.b." above, the City may re-file these claims at any time after September 1, 2007, and (ii) in the event of such re-filing, KWSC shall not assert Timing Defenses with respect to the Tolling Period (both as defined below). Nothing herein shall constitute any acknowledgment by KWSC as to the validity or merit of any of the City's claims tolled hereunder.

(3) Tolling.

i. The Tolling Period means the period which extends from March 30, 2004 until the earlier of 90 days after September 1,

2007, or such earlier date (if any) of re-filing of the Lawsuit pursuant to paragraph 3,b above with respect to KWSC. The Tolling Period may be extended by written agreement of the Parties.

ii. The Parties agree that all time periods governing any Timing Defenses shall be tolled during the Tolling Period. "Timing Defenses" shall mean any affirmative defenses based on statute(s) of limitation, statute(s) of repose, laches or the passage of time to any claims, known or unknown, that the City may have against KWSC, or to any claims, known or unknown, that KWSC may have against the City. This Agreement shall not revive any claim that is barred before March 30, 2004 by any Timing Defense. Any lawsuit filed pursuant to this subparagraph 3.d shall be deemed by the Parties to be treated as if it were filed on March 30, 2004, so that no prejudice will have occurred by the nonsuit contemplated herein.

4. TWDB Loans. KWSC represents and warrants to the City that, to the best of KWSC's knowledge, information and belief, TWDB does not and will not require review, approval, or any change to the 2006 Contract as a condition of funding the TWDB Loans, as reflected by the TWDB letter attached as Exhibit B.

5. Agreement to Cooperate. In consideration of the undertakings herein, and assuming TWDB seeks no changes to the 2006 Contract, upon the Parties' execution of

this Agreement the City will cooperate with KWSC in seeking the closing of the TWDB Loans, as further set forth in Section 4.6 of the 2006 Contract.

6. City Releases. Effective as of the Effective Date of this Agreement, for and in consideration of the execution by KWSC of the 2006 Contract, and in the further consideration of the releases herein made, sufficiency of which consideration is hereby acknowledged, the City does for itself and its Council Members, agents, employees and assigns, hereby and forever release and discharge KWSC, its members, representatives, employees, agents and assigns, whether specifically mentioned or not, of and from any and all known and unknown liability, actions, causes of action, claims, demands, damages, costs, expenses, claims for contribution or indemnity, and/or compensation of any kind whatsoever arising out of or allegedly relating to any of the following:

(a) the Settlement Agreement executed by the Parties on or about September 13, 2001, in connection with Cause No. 14,130 filed in the 27th Judicial District Court of Lampasas County, Texas ("2001 Settlement Agreement"), together with the Judgment entered in said cause;

(b) the 2001 Contract;

(c) any alleged breach by KWSC of the 2001 Settlement Agreement or the 2001 Contract, or of any prior agreement between the Parties;

(d) any alleged failure of KWSC to comply with any provision of the 2001 Settlement Agreement or 2001 Contract, or of any prior agreement between the Parties;

(e) any alleged conversion by KWSC of any property or property right owned or claimed by the City including (without limitation) rights to raw or treated water or capacity to treat water from CTWSC's water treatment plant and any water storage and transmission capacity in any facilities owned by CTWSC or KWSC;

(f) any alleged failure of KWSC to provide water or water storage or transmission capacity to the City in quantities and/or at rates allegedly required by any contract, including the 2001 Contract and the 2001 Settlement Agreement, at any time up to the effective date hereof;

(g) any claim or action asserted or alleged by the City against KWSC and CTWSC relating to the 2000 Contract, the 2001 Contract, the 2001 Settlement Agreement or to the sale, production, treatment, provision or transmission of water by or from either of the Parties;

(h) any alleged entitlement to attorney's fees or costs by the City relating to the above-listed causes;

(i) any claim for declaratory relief, damages, unjust enrichment, constructive trust, attorneys' fees, costs of suit, interest and other or further relief asserted or which could have been asserted by the City in the Lawsuit, including, without limitation, claims for accounting, over-billing, failure to pay or allow credit for interest on escrow and/or reserve accounts maintained by or for the benefit of KWSC and/or the City;

(j) any and all other claims and/or causes of action which the City has or may have by reasons of the transactions and occurrences described more fully in the pleading identified as the First Amended Petition in Intervention of City of Lampasas, Texas, or any other petition or pleading filed by the City in the Lawsuit, including any alleged entitlement to attorney's fees or costs by the City, relating to any of the above or foregoing causes;

PROVIDED, HOWEVER, the foregoing does not release any claims based upon requests by the City for correction of billing errors since January 2006 and Billing Adjustments under Section 4.9B of the 2006 Contract.

7. KWSC Releases. Effective as of the Effective Date of this Agreement, for and in consideration of the execution by the City of the 2006 Contract and of the releases herein made, the sufficiency of which consideration is hereby acknowledged, KWSC does by these presents, for itself, its Board of Directors, its members, employees and assigns, hereby and forever release and discharge the City, its Council Members, representatives, employees, agents and assigns, whether specifically mentioned or not, of and from any and all known and unknown liability, actions, causes of action, claims, demands, damages, costs, expenses, claims for contribution or indemnity, and/or compensation of any kind whatsoever arising out of or allegedly relating to any of the following:

(a) the 2001 Settlement Agreement;

- (b) the 2001 Contract;
- (c) any alleged breach of the 2001 Settlement Agreement or the 2001 Contract by the City, or of any prior agreement between the Parties;
- (d) any alleged failure of the City to comply with any provision of the 2001 Settlement Agreement or 2001 Contract, or of any prior agreement between the Parties;
- (e) any claim or action asserted or alleged by KWSC against the City relating to the 2000 Contract, the 2001 Contract, the 2001 Settlement Agreement or to the sale, production, treatment, provision or transmission of water by or from either of the Parties;
- (f) any alleged entitlement to attorney's fees or costs by KWSC relating to the above listed causes;
- (g) any claim for declaratory relief, damages, unjust enrichment, constructive trust, attorneys' fees, costs of suit, interest and other or further relief asserted or which could have been asserted by KWSC in the Lawsuit, including, without limitation, claims for accounting, over-billing, failure to pay or allow credit for interest on escrow and/or reserve accounts maintained by or for the benefit of KWSC and/or the City;
- (h) any and all other claims and/or causes of action which KWSC has or may have by reasons of the transactions and occurrences described more fully in the pleading identified as Kempner's First Amended Petition and Cross-Action, or any other petition or pleading filed by any party in the Lawsuit, including any alleged entitlement to attorney's fees or costs by KWSC relating to any of the above or foregoing causes;

PROVIDED, HOWEVER, the foregoing does not release any claims based upon requests by KWSC for correction of billing errors since January 2006 and Billing Adjustments under Section 4.9B of the 2006 Contract.

8. Dismissal of Claims. In the event any lawsuit between the Parties is on file at such date as the 2006 Contract becomes effective, then, within ten days after the 2006 Contract becomes effective under paragraph 2.a or 2.b above, the Parties will dismiss with prejudice all claims asserted by them against each other which relate to any of the matters released herein. More particularly, (i) if, at such date, a notice of nonsuit has not been previously filed, then the Parties will dismiss with prejudice all claims asserted against each other in the lawsuit, and (ii) if at such date a re-filing under paragraph 3.d(2) above has occurred, then the Parties will dismiss with prejudice all claims asserted against each other in the new lawsuit contemplated under paragraph 3.d(2) above.

9. Warranty of Authority. KWSC warrants and acknowledges that the Board of Directors of KWSC has approved this Agreement and that the person signing on behalf of KWSC has full authority to execute this Agreement on behalf of KWSC.

10. Warranty of Authority. The City warrants and acknowledges that the City Council of the City has approved this Agreement and that the person signing on behalf of the City has full authority to execute this Agreement on behalf of the City.

11. Doubtful Claims. It is agreed and understood by the Parties that this is a settlement of doubtful and disputed claims and that this settlement is not to be construed

as an admission of liability on the part of the City, KWSC, or any person, entity or corporation hereby released, by all of whom liability is expressly denied.

12. Review of Agreement. It is further acknowledged that the undersigned and the respective Board of Directors and Council Members of the Parties have directed that the undersigned persons execute the same based wholly upon their own judgment and knowledge of the claims, liability questions and alleged damages involved herein.

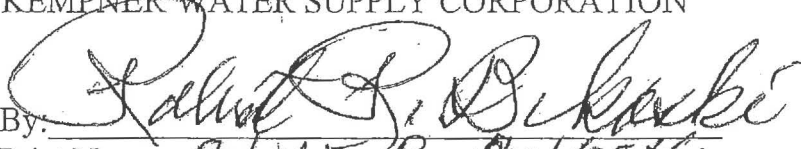
13. Counterparts. This Agreement may be executed in multiple originals. Properly executed signature pages, whether they constitute original signature pages, copied signature pages, or facsimile copied signature pages, may be attached to the original Amended Settlement, Compromise, Release and Tolling Agreement. Any such copied signature page or facsimile copied signature page attached to the original Amended Settlement, Compromise, Release and Tolling Agreement will have the same force and effect as an original signature page.

14. Severability. In the event that, at the behest of USDA-RD or other state or federal agency, any provision contained in this Agreement (including the provision for interim operation, or any aspect thereof, under the 2006 Contract) shall be held to be invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability of such provision shall not affect any other provision of this Agreement, and this Agreement shall be construed (i) as if such invalid, illegal or unenforceable provision had never been contained herein, and (ii) notwithstanding the foregoing, and to

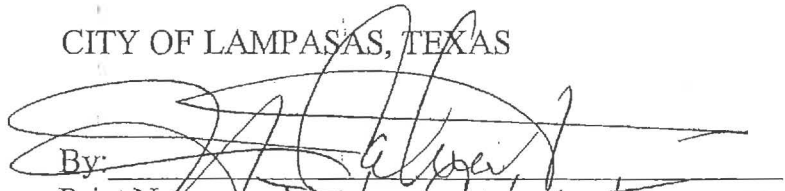
the maximum extent possible, to effectuate the intent of the Parties as set forth in this Agreement and in the 2006 Contract.

WITNESS OUR HANDS on this the 28th day of August,
2006.

KEMPNER WATER SUPPLY CORPORATION

By: 
Print Name: ROBERT R. MIKOSKI
Title: PRESIDENT, KWSU B.O.D.

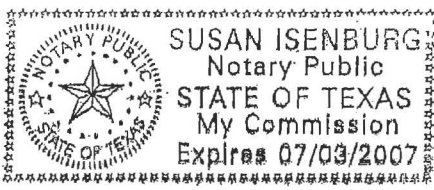
CITY OF LAMPASAS, TEXAS

By: 
Print Name: JACK CALVERT
Title: MAYOR

THE STATE OF TEXAS §
 §
COUNTY OF Lampasas §

BEFORE ME, the undersigned authority, on this day personally appeared Robert R. Bikaski, known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged to me that he/she is authorized to execute this Agreement on behalf of KEMPNER WATER SUPPLY CORPORATION, that he/she understood the same and executed the same for the purposes and consideration therein expressed.

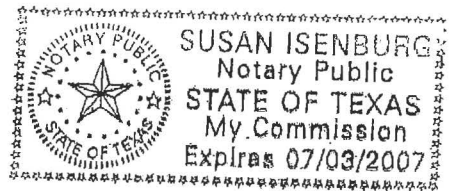
GIVEN UNDER MY HAND and seal of office this the 28th day of August, 2006.

 Susan Isenburg
NOTARY PUBLIC, STATE OF TEXAS

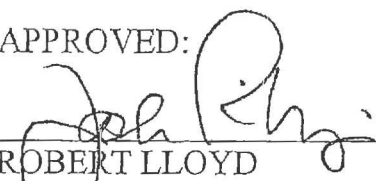
THE STATE OF TEXAS §
 §
COUNTY OF Lampasas §

BEFORE ME, the undersigned authority, on this day personally appeared Jack Calvert, known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged to me that he/she is authorized to execute this Agreement on behalf of THE CITY OF LAMPASAS, TEXAS, that he/she understood the same and executed the same for the purposes and consideration therein expressed.

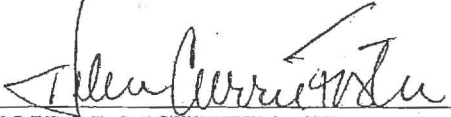
GIVEN UNDER MY HAND and seal of office this the 28th day of August, 2006.

 Susan Isenburg
NOTARY PUBLIC, STATE OF TEXAS

APPROVED:



ROBERT LLOYD
JAMES CHRISMAN PHILLIPS
Attorney for Kempner Water Supply Corporation



JOHN J. MCKETTA, III
HELEN CURRIE FOSTER
Attorney for the City of Lampasas

