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STATE OF CALIFORNIA
State Lands Commission
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STATE OF CALIFORNIA
STATE LANDS COMMISSION

AMENDMENT OF LEASE PRC 8727.1

WHEREAS, the State of California, acting through the State Lands Commission, hereinafter called Lessor, and, Cabrillo Power I LLC, hereinafter called Cabrillo, have heretofore entered into an agreement designated as Lease PRC 8727.1, authorized by the Lessor on May 10, 2007 and executed August 14, 2007, whereby the Lessor granted to said Lessee a General Lease – Industrial Use covering certain State Land situated in San Diego County, hereinafter referred to as Lease Premises (“Lease Premises”); and

WHEREAS, Section 4, Paragraph 15(e) provides that the Lease may be terminated and its terms, covenants and conditions amended, revised or supplemented only by mutual written agreement of the parties; and

WHEREAS, Cabrillo and Poseidon (Channelside) LLC, hereafter referred to as Poseidon, have entered into an Agreement dated July 11, 2003; and

WHEREAS, the Agreement between the Cabrillo and Poseidon provides for a use of the Lease Premises that is not allowed under current provisions contained in the Lease; and

WHEREAS, Poseidon has applied to the Lessor to use the Lease Premises for desalination purposes; and

WHEREAS, by reason of the foregoing, it is now the desire of the parties to amend the foregoing Agreement.

NOW THEREFORE, the parties hereto agree as follows:

SECTION 1 – BASIC PROVISIONS and MAILING ADDRESS is amended to include Poseidon as a Co-Lessee, whose mailing address is 501 W. Broadway, Suite 1260, San Diego, CA 92101. Any reference to “Lessee” in this lease shall refer to both Cabrillo and Poseidon as Co-Lessees.

SECTION 1 – LAND USE OR PURPOSE is amended to include desalination use of the existing improvements by Poseidon.

SECTION 2 – SPECIAL PROVISIONS shall be amended to include the following amendment to paragraph 8 (which replaces the prior paragraph 8) and to add paragraphs 10 through 23 as separate obligations of Poseidon:

8. Authorized Uses:

It is the intent of the parties to this lease that the improvements and activities authorized herein are for the exclusive use of the Co-Lessees, Cabrillo and Poseidon, in conjunction with Cabrillo's existing power plant cooling water system involving the intake of sea water and the commingling of brine water discharge from Poseidon's desalination facility. The test desalination facility shall cease operation prior to the operation of the Poseidon desalination facility.

10. Poseidon shall, at all times during the term of the Lease, comply with the Energy Minimization and Greenhouse Gas Reduction Plan (the GHG Plan), as adopted by the California Coastal Commission on August 6, 2008, except that, notwithstanding the provisions of that Plan:

- a) In addition to Poseidon's offset requirements under the GHG Plan, Poseidon shall be deemed to have fully offset construction and operational impacts of the desalination facility by obtaining an additional 25,000 tons of carbon offsets/Renewable Energy Certificates (RECs), subject to the verification procedures in the GHG Plan, as a one-time obligation, to be purchased prior to operation of the desalination facility;
- b) The provisions of Section III(E) of the Energy Minimization and Greenhouse Gas Reduction Plan (the GHG Plan), as adopted by the California Coastal Commission on August 6, 2008, entitled, "Contingency if No GHG Reduction Projects are Reasonably Available," shall apply to Poseidon's lease, except that if:
 - i) offsets in an amount necessary to mitigate the Project's GHG emissions are not reasonably available; ii) the "market price" for carbon offsets or RECs is not reasonably discernable; (iii) the market for offsets or RECs is suffering from significant market disruptions or instability; or (iv) the market price has escalated to a level that renders the purchase of offsets/RECs economically infeasible to the Project, then: Poseidon may delay or postpone acquisition of carbon offsets or RECs required under this lease for a period of up to three years from the date acquisition of the offset is due, provided that: i) Poseidon shall bank the minimum purchase price of \$10 per ton of carbon required to be offset per year during the market disruption as required under Section III(E) of the GHG Plan; and ii) that within three years from the date that acquisition of the annual offset would otherwise be due, Poseidon shall acquire those carbon offsets or RECs as required under this lease for that annual offset, regardless of cost per ton of carbon offsets required.
- c) This sub-paragraph was intentionally left blank.
- d) This sub-paragraph was intentionally left blank.

11. a) Poseidon shall, at all times during the term of the Lease, comply with the Marine Life Mitigation Plan, as adopted by the California Coastal Commission on August 6, 2008. Poseidon will provide copies of all reports that are required to be

provided to the California Coastal Commission to the Lessor's Executive Officer at the time any such reports are required to be submitted to the California Coastal Commission. The restoration project shall require up to 55.4 acres of wetlands restoration to be implemented in two Phases, with the first Phase (Phase I) comprising not less than 37 acres of wetlands restoration, and the second Phase (Phase II) comprising up to an additional 18.4 acres. Obligations for Phase II of the wetland mitigation comprise 18.4 acres, but may be proportionally reduced by the California Coastal Commission if it finds that Poseidon has reduced marine life impacts caused by entrainment and impingement.

- b) The provisions of the Marine Life Mitigation Plan notwithstanding, Poseidon shall request an amendment to Lease PRC 8727.1 if Poseidon desires to receive mitigation credits for direct benefits to marine life from dredging that would otherwise be required pursuant to compliance with the Marine Life Mitigation Plan.
 - c) Poseidon shall at all times during the term of the Lease, comply with the post restoration monitoring and remediation requirements set forth in the Marine Life Mitigation Plan Section 5.4 for ensuring the success of the wetlands restoration site(s), provided that the standards include success criteria from four existing relatively undisturbed sites and that Poseidon achieve a 95% confidence level of success for the restoration required. Should the Coastal Commission amend Section 5.4 at any time, Poseidon shall request amendment of this Lease.
12. Poseidon, without interference with, or interruption of, powerplant scheduled operations and at its sole cost and expense, shall use the best available design, technology, and mitigation measures at all times during which this Lease is in effect to minimize the intake (impingement and entrainment) and mortality of all forms of marine life associated with the operation of the desalination facility as determined by the San Diego Regional Water Quality Control Board or any other federal, state, or local entity having applicable jurisdiction.
 13. As reasonably determined by the Lessor, the monitoring, maintenance, and operation of the wetland restoration site(s) and the reference site(s) may be modified to conform with equivalent or superior standards and requirements developed by the San Diego Regional Water Quality Control Board or the California Coastal Commission or any other federal, state, or local entity having applicable jurisdiction.
 14. Within ten years from the effective date of this Amendment, or upon such earlier time as agreed to by the Lessor, or upon notice by Cabrillo that it will no longer require the use of the Lease Premises for the purposes of generating electrical power, Lessor will undertake an environmental review of the ongoing impacts of operation of the desalination facility to determine if additional requirements pursuant to Special Provision paragraph number 12, above, are required. Lessor, at its sole discretion, may hire a qualified independent environmental consultant, at the sole expense of Poseidon, with the intent to analyze all environmental effects of facility operations and alternative technologies that may reduce any impacts found. Lessor may require, and Poseidon shall comply with, such additional requirements as are reasonable and as are consistent with applicable state and federal laws and regulations and as Lessor determines are appropriate in light of the environmental review.

15. Poseidon shall provide copies of all regulatory monitoring and compliance reports pertaining to the operation of its desalination facility to Lessor at the time of submitting such reports with any regulatory agency.
16. a) Poseidon shall provide Lessor with
 - i) a non-cancelable operational performance deposit in the amount of \$1,000,000, prior to commencement of construction, but not more than one year from the effective date of the Lease Amendment. At any time during the term of the Lease, Lessor may require an increase in the amount of the performance deposit to reflect economic inflation or to cover any additionally authorized improvements, alterations, or purposes or any modification of rental.
 - and-**
 - ii) a non-cancelable wetland performance deposit in the amount of \$3,700,000 prior to commencement of operation of the desalination facility to ensure the implementation of compensatory mitigation, monitoring and maintenance as described in the approved plan. Fifty percent (50%) of the wetland performance deposit shall be released when the Lessor's Executive Officer determines that construction has been completed in conformance with the plans approved by the California Coastal Commission. The remainder of the wetland performance deposit for Phase I of the restoration project shall be proportionally and incrementally released based upon the productivity of the wetlands as determined by Lessor's Executive Officer, based upon the performance standards as outlined in the Marine Life Mitigation Plan, as adopted by the California Coastal Commission on August 6, 2008, provided that any further modification to the performance standards in Marine Life Mitigation Plan Section 5.4, shall require amendment of Lease PRC 8727.1.
- b) The performance deposit may take one of the forms set out below or some other form acceptable to Lessor, and shall guarantee Poseidon's full and faithful performance of all the terms, covenants, and conditions of this Lease;
 - (i) Cash;
 - (ii) A renewable Time Certificate of Deposit from a financial institution authorized to do business in the State of California, wherein the principal sum is made payable to the State or order and both the financial institution and the form of the certificate are approved by the Lessor's Staff;
 - (iii) A Non-Cancelable Bond issued by a responsible surety company authorized to do business in California, as approved by the Lessor's Staff, provided:
 - (A) The Bond is automatically renewable and any alteration of the bond shall first require 30 days' prior written notice to Lessor, and
 - (B) The Bond shall guarantee payment in cash to Lessor of the performance deposit amount upon receipt of written demand from Lessor.

- (iv) An irrevocable Standby Letter of Credit in a form acceptable to the Lessor's staff.
 - c) Regardless of the form in which Poseidon elects to make said performance deposit(s), all or any portion of the principal sum shall be available unconditionally to Lessor for correcting any default or breach of this lease by Poseidon, its successors or assigns or for payment of reasonable and actual expenses incurred by Lessor as a result of the failure of Poseidon, its successors or assigns, to perform faithfully any and all of the terms, covenants, and conditions of this Lease. The wetland performance deposit referenced in subsection (a)(ii) above shall only be available to cure defaults related to section 11 of this lease. The performance deposit referenced in subsection (a)(i) above shall be available to cure all other defaults under the lease.
 - d) Should Poseidon elect to assign or provide a Time Certificate of Deposit to fulfill the performance deposit requirements of this Lease, the agreement entered into by Poseidon with a financial institution to establish a deposit necessary to permit assignment or issuance of a certificate may allow the payment to Poseidon or order of interest accruing on account of said deposit.
 - e) Should the entire performance deposit or any portion thereof be appropriated and applied by Lessor for the payment of overdue rent or any such other sum due and payable to Lessor by Poseidon, then Poseidon, within 30 days after written demand by Lessor, restore said performance deposit to the required amount. This Paragraph D is only applicable to the performance deposit and shall not be applicable to the wetland performance deposit.
 - f) Poseidon shall maintain the required performance deposit throughout the Lease term. Failure to do so shall be deemed a default and shall be grounds for immediate termination of this Lease Amendment as the same relates to the additional use approved by this Lease Amendment.
 - g) The performance deposit shall be rebated, reassigned, released, or endorsed to Poseidon or order, as Poseidon may direct at such time as Poseidon has vacated the premises, is not in default and has no further obligation under the Lease. Interest on the performance deposit required hereunder shall accrue for the benefit of Poseidon and shall be made available to Poseidon from time to time except as the same is required to remedy or cure any default by Poseidon; provided, however, that if the performance deposit is given in the form of cash then Poseidon shall not be entitled to any interest thereon.
17. Poseidon shall, as a separate obligation, provide to Lessor, prior to commencement of construction, in the form attached to this Lease Amendment as Exhibit A, or in a form approved by Lessor's staff, an unconditional guarantee by parent company Poseidon Water LLC for full performance by Poseidon of all the obligations under the Lease.
18. Poseidon shall, prior to the use of the Lease Premises for desalination purposes, provide to Lessor a detailed report of compliance with Order No. R9-2006-0065, NPDES No. CA0109223, adopted by the San Diego Regional Water Quality Control Board, on August 16, 2006, and became effective on October 1, 2006, and any subsequent amendments thereto.

19. Poseidon shall provide a written report to the Lessor for use at a public hearing to be conducted by Lessor within five years of the effective date of this lease amendment in order to publicly review and evaluate Poseidon's compliance with the terms of the lease as provided for in Section 4, Paragraph 6 including, but not limited to, compliance with the federal Clean Water Act, and California's Porter-Cologne Water Quality Control Act.
20. In the event that Poseidon fails to comply with any or all of its separate obligations under this Lease, Lessor may terminate Poseidon's rights under this Lease Amendment. Such termination shall not affect any or all of Cabrillo's rights or obligations under this Lease. Additionally, assuming that Cabrillo is not otherwise in default of any of its separate obligations under this Lease, no default by Poseidon of any or all of its separate obligations under this Lease will give Lessor the right to terminate any of Cabrillo's rights under this Lease.
21. Poseidon shall not make any changes in use or operation of the intake channels and jetties without prior authorization by Lessor.
22. Poseidon shall be responsible for reimbursing all of Lessor's reasonable staff expenses incurred by Lessor and its Staff to monitor compliance by Poseidon of all of its reservations, terms, covenants and conditions of the Lease for the term of the Lease. Upon execution of the Lease Amendment, Poseidon shall execute a Reimbursement Agreement with the Lessor specifying the mechanism by which all actual costs by Lessor shall be reimbursed. An expense deposit of \$25,000 shall be paid to and held by the Lessor as a cash surety to ensure performance of this paragraph.
23. Poseidon acknowledges that it is responsible for Section 4 General Provisions of Lease PRC 8727.1, except as otherwise noted below.

SECTION 2 – SPECIAL PROVISIONS shall be amended to include the following paragraph 24 as a separate obligation of Cabrillo:

24. Cabrillo shall notify Lessor in writing prior to discontinuing its use of the Lease Premises in connection with the production of electricity. Upon receipt of notification by Lessor, Cabrillo may apply to Lessor for approval of an assignment of its obligations under the lease to Poseidon. In considering Cabrillo's application for approval of an assignment, Lessor will take into account Poseidon's past performance and the likelihood that Poseidon could and would carry out all obligations under the lease as sole lessee. In the event that Lessor finds that there is a substantial probability that Poseidon would not or could not carry out all such obligations, then Lessor may disapprove the assignment, in which case, at Cabrillo's option, the lease would terminate or Cabrillo would remain as Co-Lessee.

SECTION 2 – SPECIAL PROVISIONS shall be amended to include the following paragraph 25:

25. Cabrillo and Poseidon shall be jointly and severally liable for all provisions of this Lease except for those provisions that specify a separate obligation of one or the other.

SECTION 4 – GENERAL PROVISIONS is amended as follows:

Paragraph 11, Default and Remedies, (a) Default, Paragraph (4) is hereby deleted in its entirety and is replaced with the following:

- (4) Co-Lessees' failure to obtain, maintain and comply with all necessary governmental permits or other entitlements;

The effective date of this amendment to the aforesaid Agreement shall be August 22, 2008. This Amendment, consisting of seven pages together with Exhibit A, consisting of four pages, is a portion of document number PRC 8727.1, with a beginning date of December 14, 2006, consisting of four sections with a total of fourteen pages. All other terms and conditions of this lease shall remain in full force and effect. This Agreement will become binding on the Lessor only when duly executed on behalf of the State Lands Commission of the State of California.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date hereafter affixed.

CO-LESSEES:

*CABRILLO POWER I, LLC

LESSOR:

STATE OF CALIFORNIA
STATE LANDS COMMISSION

By: *me* Keith Richards

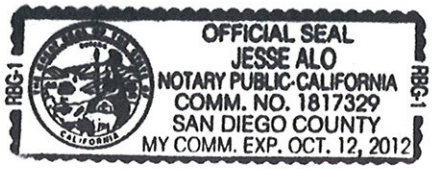
By: _____

Title: PRESIDENT

Date: _____

Date: NOVEMBER 24, 2008

*POSEIDON RESOURCES (CHANNELSIDE), LLC



By: Peter MacLaggan

State of California
County of San Diego
On November 24, 2008 before me, Jesse Alo, Notary Public,
personally appeared Keith S Richards and Peter MacLaggan
who proved to me on the basis of satisfactory evidence to be the person(s)
whose name(s) is/are subscribed to the within instrument and acknowledged
to me that he/she/they executed the same in his/her/their authorized capacity(ies),
and that by his/her/their signature(s) on the instrument the person(s), or the entity
upon behalf of which the person(s) acted, executed the instrument.
I certify under PENALTY OF PERJURY under the laws of the State of California that the
foregoing paragraph is true and correct.

Title: VICE PRESIDENT

Date: NOVEMBER 24, 2008

WITNESS my hand and official seal. [Signature]

*All signatures must be acknowledged

This Lease was authorized by the California State Lands Commission on _____

EXHIBIT A
PRC 8727.1 LEASE AMENDMENT

GUARANTY

1. **Poseidon Water LLC, a Delaware limited liability company** (“Guarantor”), owns **Poseidon Carlsbad LLC**, which in turn owns **Poseidon Resources (Channelside) LLC** (Poseidon Resources). POSEIDON RESOURCES is a Co-Lessee under General Lease – Industrial Use Lease No. PRC 8727.1 (the “Lease”) granted by the State of California acting by and through the State Lands Commission (“Lessor”). For valuable consideration, the receipt and sufficiency of which are hereby acknowledged by the undersigned, Guarantor hereby unconditionally guarantees performance of all the terms, covenants, conditions, agreements, and obligations of POSEIDON RESOURCES under the Lease in the same manner and to the same extent as though Guarantor were the co-lessee thereunder (the “Obligation”).
2. This is a continuing and absolute Guaranty relating to the Obligation, irrespective of any release of, or granting of time or any other forbearance or indulgence to POSEIDON RESOURCES. Modifications of or alterations or changes which may be made in the Lease, or in the terms, duties and obligations imposed thereunder shall not in any way release the Guarantor, either in whole or in part, from any liability arising under this Guaranty. Notice to the Guarantor of any such modifications, alterations, changes, extensions or forbearance is hereby waived.
3. If, during the term this Guaranty is in effect, POSEIDON RESOURCES fails to timely perform any Obligation including without limitation, any obligation of POSEIDON

RESOURCES to make any monetary payment provided for thereunder, and fails to cure any such failure in the manner and within the period of time provided within the Lease, Guarantor will tender performance of such obligation directly for Lessor's benefit promptly upon Lessor's demand therefor, and without Lessor having to make prior demand upon POSEIDON RESOURCES. Notwithstanding the preceding sentence, the obligations of the Guarantor hereunder are independent of the obligations of POSEIDON RESOURCES, and a separate action or actions may be brought and prosecuted against the Guarantor whether an action is brought against POSEIDON RESOURCES or whether POSEIDON RESOURCES is joined in any such action or actions.

4. The Guarantor waives: (a) any right to require the Lessor to (i) proceed against POSEIDON RESOURCES; (ii) proceed against or exhaust any security or other guarantor; or (iii) pursue any other remedy in Lessor's power whatsoever; and (b) notice of acceptance of this Guaranty.

5. The Guarantor represents and warrants to Lessor that (a) all authorizations, approvals, notices, filings and other action required by the internal documents governing the Guarantor and the regulatory authorities having jurisdiction over the Guarantor in connection with the due authorization, execution and delivery of this Guaranty has been duly obtained or made and are in full force and effect; and (b) this Guaranty has been duly executed and delivered by the Guarantor and constitutes the legal, valid and binding obligation of the Guarantor enforceable against the Guarantor in accordance with its terms.

6. THIS GUARANTY SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAW OF THE STATE OF CALIFORNIA WITHOUT REGARD TO PRINCIPLES OF CONFLICTS OF LAWS. The Guarantor, by its execution of this Guaranty, hereby submits to the non-exclusive jurisdiction of the courts of the State of California and of the United States of America in connection with any action or proceeding relating to this Guaranty and hereby consents to service of process or other summons in any such action or proceeding brought by Lessor against it in any such court by means of registered mail to the last known address of the Guarantor. Nothing herein, however, shall prevent service of process by any other means permitted by law or the bringing of any such action or proceeding in any other jurisdiction.

7. None of the terms or provisions hereof may be waived, altered, modified or amended except by a writing duly signed by the Lessor and by the undersigned. If any term hereof shall be held to be invalid, illegal or unenforceable in any jurisdiction, the validity of all other terms shall in no way be affected thereby in that jurisdiction, and the unenforceability in that jurisdiction shall in no way affect the validity or enforceability of that or any other terms hereof in any other jurisdiction.

8. This Guaranty shall be binding on the Guarantor and its successors and assigns and shall inure to the benefit of the Lessor. This Guaranty shall not be deemed to benefit any person except POSEIDON RESOURCES and Lessor.

In witness whereof, the Guarantor has caused this Guaranty to be executed on its behalf by its duly authorized representative, as of this _____ day of August, 2008.

POSEIDON WATER LLC

By: _____

Name: _____

Title: _____

(Attach Notary of Authorized Signature)

(Attach Delegation of Authority of Signatory)