

# MEMORANDUM



**To:** AWBA Commission Members  
**From:** Virginia O'Connell  
**Subject:** Summary of Distribution of AWBA Long-term Storage Credits Meeting dated May 17, 2011  
**Date:** June 9, 2011

AUTHORITY MEMBERS  
Sandra Fabritz-Whitney, Chairman  
Maureen R. George, Vice-Chairman  
Tom Buschatzke, Secretary  
John Mawhinney  
Lisa Atkins

EX OFFICIO MEMBERS  
Senator Steve Pierce  
Representative Andy Tobin

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As requested by the AWBA Commission members at the March 30, 2011 meeting, AWBA staff held a meeting to initiate discussion regarding the development of policies and procedures associated with the transfer of AWBA long-term storage credits during declared shortages. As this was the first meeting with interested parties, the primary goal was to solicit input, particularly with respect to issue identification. A draft discussion paper was distributed prior to the meeting to assist in facilitating the discussion. The draft discussion paper is attached.

The meeting was attended by 43 entities and included representatives from ADWR, CAWCD, the Bureau of Reclamation, AMWUA, Indian tribes, CAP M&I subcontract holders, irrigation districts, Maricopa and Pinal counties, and consultants. The meeting attendance list is attached.

The following are the salient points from the discussion, not in any priority order:

1. It is recognized that some issues are more administrative in nature while others are more policy oriented. Additionally, the issues are different when discussing credits that were developed using 4- cent *ad valorem* tax revenues versus withdrawal fees, and even more so when discussing the use of withdrawal fee credits for Indian firming purposes. AWBA, CAWCD, and AWBA staff are currently discussing concepts regarding the use of withdrawal fee credits for Indian firming purposes. Until the outcome of these discussions is known, it is premature to discuss issues associated with the distribution of withdrawal fee credits. Therefore, the consensus of the group was that initial discussions should focus on the issues associated with credits developed using 4- cent *ad valorem* tax revenues.

It is also recognized that some policy issues are solely the AWBA's and some are solely CAWCD's, however, some need to be addressed cooperatively by the AWBA, CAWCD, ADWR and, to some extent, Bureau of Reclamation (Reclamation).

2. AWBA and ADWR staff recommend that long-term storage credits be distributed (or assigned) to CAWCD at the end of the year or after the recovery has already been completed for improved efficiency and accuracy. CAWCD staff noted that there is a need for CAWCD to have certainty that the credits will be transferred because of the costs associated with the recovery of the credits. It was noted that AWBA staff works

cooperatively with CAP staff to develop its Annual Plan of Operation (Plan) for the following year, which is approved in December. As part of the Plan, the AWBA must project the amount of long-term storage credits that will be distributed the following year for shortage purposes. CAP staff noted that they had anticipated the credits would be transferred beforehand to provide certainty and assurance regarding the AWBA's commitment. An alternative suggested was that the AWBA could potentially set aside the number of credits identified in the Plan for the shortage year by resolution and then assign the credits at the end of the year based on actual use.

Regardless of the timing of the distribution of credits, a reconciliation process will need to be developed to determine the final amount of credits needed. This process should also allow reconciliation in the longer-term (two or more years) because of unintentional reporting errors that may be found in that time frame. Depending on the procedure developed, it may require statutory change. The statutes governing the assignment of credits and recovery are recharge statutes, not AWBA statutes.

Potential Action: Determine/develop process that provides CAWCD security regarding distribution of credits.

3. There are questions regarding the amount of water the AWBA will firm during shortages i.e. in any shortage year, what volume will M&I subcontractors actually receive from the AWBA? This question has been raised because the statute is vague and merely states "to the extent necessary to meet the demands of M&I subcontractors". This is one of the primary policy questions that will need to be answered. It was suggested that AWBA, CAWCD and ADWR staff have further discussions to determine who should be responsible for making this determination and developing any potential policies. The policies should then be developed with input from M&I subcontractors.

The question of volume is directly tied to the length of time that the credits will be available for distribution. There are a finite number of credits and the underlying policy question is how many and for what purpose will the credits be distributed. The policy that is developed will determine how quickly the credits are utilized and how long they will last.

There was a statement regarding credits being a "common good" and the idea that there is some concern about eroding the benefit of the collective. Modeling results would be helpful to define the impact to the greater good, i.e. what is the actual scale/extent of the problem. It was also stated that the potential for unintended consequences needed to be taken into consideration in all discussions regarding the distribution of the credits.

4. Should accruing additional long-term storage credits by M&I subcontractors during times of shortage be a demand that is met by the AWBA?

It was noted that there are sometimes water management reasons for recharging water and that those would exist even during times of shortage. The City of Scottsdale's water gradient issue was described as an example. They also noted that they use

recharge to mitigate potential subsidence issues with the CAP canal. It is recognized that these situations do exist. The first test of whether storage is actually for a water management purpose would likely be location, i.e. is the storage actually taking place within the service area in a location that provides water management benefits. Protecting the physical availability of groundwater was also discussed.

Philosophy and politics were noted to be of high importance. From the philosophical viewpoint, it is recognized that at this level of shortage, many individuals will have had cuts to their CAP supplies and it will be difficult for some to justify the delivery of water for recharge purposes when others are going without water, potentially for direct uses. With respect to politics, it was noted that it is a reality that by the time this condition is reached, that water users are going to be curtailing water uses. There are too many in-state and interstate political ramifications for curtailment to not occur.

5. Is the CAP water that was stored and then recovered actually CAP M&I subcontract or Project water? This is a CAWCD policy decision that must be made. If it is not subcontract water, then CAP has a great deal of discretion. If it is subcontract water, then decisions need to be made in consultation with the M&I subcontract holders. Reclamation is currently also developing a position on whether recovered CAP credits are Project water. They are planning to have discussions with CAWCD once consensus within Reclamation is reached.

6. Developing these types of policies will be difficult because no two water service areas have the same supplies, distribution systems, treatment facilities, capacity for storage, canals, etc.

7. Should the AWBA be concerned about an equitable distribution of credits? For example, if some subcontractors have more access to non-CAP supplies, should they be required to use those first? Discussion primarily seemed to be opposed to this because the statement was made that it actually penalizes those that developed alternative supplies. Additionally, as noted above, it will be difficult to evaluate equity when all service areas are so different.

8. The issues associated with Indian firming are very different. There are many components of the settlements that must be incorporated into the discussion, including how CAP delivers water to Indian contracts. For these reasons it was suggested that Indian firming be addressed separately. Reclamation recommended having the Indian firming discussions after the M&I firming issues have been addressed.

At the end of the meeting it was decided that the AWBA would meet with CAWCD, ADWR, and Reclamation staff to reach clarity on some definitions and to resolve some of the issues regarding authorities and responsibilities. AWBA staff committed to schedule another stakeholder meeting following these meetings and the June 15<sup>th</sup> AWBA meeting. Interested parties that had additional issues, questions, or concerns were asked to submit those in writing to AWBA staff.

Subsequent, to the meeting one letter of comment was received and it is attached.

## Arizona Water Banking Authority

### Discussion Paper for Distributing Long-term Storage Credits for CAP M&I Firming

#### Background

The Intergovernmental Agreement (IGA) among ADWR, AWBA, and CAWCD identifies certain cooperative activities and joint planning processes that the parties must participate in periodically. These activities include developing a coordinated and cooperative planning process that addresses issues such as: 1) the future distribution and use of water stored by the AWBA, and 2) the recovery of water stored by the AWBA and CAWCD for water management objectives set forth in Title 45, Chapter 2, Arizona Revised Statutes.

CAWCD has a good understanding of the physical aspects of recovering credits and delivering water during shortages. However, during its recovery planning process, which has focused more on the location, timing, and purpose of recovering credits, several process and policy questions have been raised. AWBA staff identified these questions in a preliminary draft on *Potential Policies Regarding Distribution of Long-Term Storage Credits for M&I Firming*, which was provided at the AWBA Commission meeting on March 30, 2011. AWBA, CAWCD, and ADWR staff have since had initial discussions on these questions, which differ with regard to the source of funding the AWBA used to accrue the credits.

Some of these questions concern the “use” of AWBA credits. Pursuant to A.R.S. § 45-2457(D), except for the distribution of four-cent tax credits for M&I firming and agreements entered into by the Authority, the decision to distribute or extinguish AWBA credits is at the complete discretion of the Authority. Some of these questions will need to be answered, if the Authority is to develop guidelines on the distribution of its credits.

#### Four- Cent Tax Credits

The AWBA’s role is fairly specific concerning the distribution of credits accrued with the four-cent tax. However, additional discussion is needed regarding the appropriate use of these credits during Colorado River shortage operations.

...shall distribute long-term storage credits accrued with monies deposited in the fund in accordance with section 48-3715.03, subsection B only for the benefit of the county in which the monies were collected. The authority shall distribute these long-term storage credits to CAWCD to the extent necessary to meet the demands of CAWCD's municipal and industrial subcontractors during times in which CAWCD's diversions from the Colorado River have been or will be disrupted by shortages on the Colorado River or by disruptions in operation of the central Arizona project.

Based on the plain reading of the statute, several of the questions identified in the preliminary draft paper discussed above can be resolved fairly easily since they are administrative in nature:

***When are the credits distributed (assigned) to CAWCD?***

CAWCD will have estimates in October of the amount of CAP water that will be available for delivery in the following shortage year and the amount of M&I demand it has for that water. Based on this information, CAWCD can estimate the amount of credits that will need to be recovered in order for CAWCD to meet its CAP M&I subcontract demands during the shortage year. CAWCD could provide these estimates to the AWBA so that they can be included in the AWBA's Annual Plan of Operation as required by statute. After the shortage year end, CAWCD can determine the number of credits necessary to cover the M&I shortage volume that will be reported to ADWR for recovery well permits held by CAWCD, as well as its recovery partners, along with any credits that will be needed for credit exchange. Based on the CAWCD year end report, the AWBA would request that ADWR assign the appropriate credits to CAWCD.

***Are credits returned to the AWBA if CAWCD did not actually need them or do they stay with CAWCD until they are needed?***

By requesting that ADWR assign credits at the end of the calendar year based on actual recovery, there is no need for CAWCD or recovering agents to return credits because only those credits that were used would be assigned. However, a mechanism for credit reconciliation would need to be established to address reporting errors that are not discovered until the following year.

***What accounting is required for the AWBA to be sure the credits are used for the benefit of the county where the money is collected?***

Likewise, by waiting to assign credits at the end of the calendar year, CAWCD can base its notification on the actual amount of credits recovered and water delivered to its customers. The wells from which those credits were recovered must be reported to ADWR as part of the annual reporting requirements. Furthermore, under current ADWR reporting requirements, the place of use of those credits can be verified if they were recovered by an M&I subcontractor pursuant to an agreement with CAWCD and used within that M&I subcontractor's service area or if that subcontractor delivered the recovered water to another M&I subcontractor.

***Does the AWBA retain any control over the credits once distributed to CAWCD?***

The AWBA would be assigning credits to CAWCD based on end-of-year reporting. ADWR can verify the recovery of these credits as part of its annual reporting review.

The following questions are related more towards policy and require additional discussion. The AWBA is seeking stakeholder input prior to resolving these questions. There may also be a need for additional AWBA policies before a procedure can be implemented. Points for discussion have been included under each question.

***Should credits be distributed for water that is requested for the purpose of accruing long-term storage credits?***

- The AWBA is required by statute to distribute four-cent tax credits to CAWCD "to the extent necessary" to meet M&I demand during shortages. Should the accrual of long-term storage (LTS) credits be considered "necessary" during times of shortage?

- Should direct use demand be met first before future water needs are considered? [Annual storage and recovery is considered a direct use]
- A leading rationale for establishing M&I firming goals was to assist in protecting a water provider's Designation of Assured Water Supply during shortages. Pursuant to the AWS rules, when a provider's surface water supply falls below the drought volume (80% of normal), a provider can apply to ADWR to qualify for a drought exemption. If approved, the provider's groundwater use would be considered consistent with the management goal of the AMA. Thus the firming goal was estimated to provide a replacement water supply up to 20% of CAP M&I supplies during shortages.
  - If shortages are equal to or greater than 20%, would it be reasonable to distribute credits for long-term storage if groundwater is also being pumped? Would there still be some subcontractors that are storing their subcontract water for LTS credits at this point?
  - There is an additional benefit associated with the distribution of AWBA's credits for accruing LTS credits because they could be sold to other entities. Should the AWBA allow its credits to be used for this purpose?
- If credits are distributed for the purpose of accruing LTS credits, would the AWBA distribute 5% less to account for the cut to the aquifer? Would there be an additional cut to account for losses? If so, how would the losses be calculated?
- Distributing credits for the purpose of accruing LTS credits could increase the pace at which four-cent tax credits are utilized. Does this also create issues concerning the equitable distribution of credits?

***Should the AWBA be concerned about an equitable distribution of the credits within the county?***

- Some M&I subcontractors may not need the full use of their subcontract at the time a shortage is declared because they either have access to other sources of water, have reduced their demand through drought planning, or do not have the demand to make full use of their subcontract.
  - If credits are distributed on a first come, first served basis, will credits be available to those providers in the future when they do make use of their full subcontract?
  - Likewise, if credits are distributed for the purpose of accruing LTS credits early, will credits be available in the future to meet direct use demands?
- How would the AWBA distribute credits to CAWCD to insure that there is equal/fair access to the credits? Would this reduce CAWCD's flexibility in meeting the demand of its M&I subcontractors?
- Does it matter if credits are distributed equitably as long as demand is being met?

### Withdrawal Fee Credits

The Authority's role is not as specific in the distribution of the credits accrued with the withdrawal fees:

...shall distribute or extinguish long-term storage credits accrued with monies collected in accordance with section 45-611, subsection C, paragraph 3 only for the benefit of the active management area in which the monies were collected. The authority may distribute or extinguish these long-term storage credits to the extent necessary to meet the demands of CAWCD's municipal and industrial subcontractors during times in which CAWCD's diversions from the Colorado river have been or will be disrupted by shortages on the Colorado river or by disruptions in operation of the central Arizona project, to implement the settlement of water right claims by Indian communities in this state or, on request from the director, to meet the other water management objectives set forth in chapter 2 of this title.

What is clear is that withdrawal fee credits can be used for M&I firming and Indian settlements. The AWBA is currently participating in discussions with CAWCD and ADWR concerning the firming of Indian and CAP M&I Priority water. The following questions pertain to the concepts being discussed as part of this process:

#### ***Should the AWBA establish a priority for the use of withdrawal fee credits?***

Absent the availability of general appropriation funds for the development of Indian firming credits, withdrawal fee credits remain the AWBA's only alternative for meeting its Indian settlement obligations, including Indian leases that have a CAP NIA Priority water firming requirement.

- If Indian firming is identified as the highest priority for the use of withdrawal fee credits, should there be a specific amount of credits identified before credits can be used for other water management goals?
- Withdrawal fee credits in the Pinal AMA may also be needed to meet a replenishment obligation in the southside protection zones.

#### ***Should the AWBA reserve a quantity of withdrawal fee credits that will be available for M&I firming?***

- How would the quantity of reserved credits be determined?
- Should credits be reserved to meet other water management goals?
- If credits are reserved for M&I firming or other water management goals there could be a risk that they may be needed to meet the Indian settlement obligations.

#### ***Should the AWBA wait until there is an actual demand for the credits before they are dedicated for a specific use?***

- Given that withdrawal fees are the only credits available to the AWBA for meeting its Indian firming obligations, is it necessary for the AWBA to formally prioritize the use of these credits?

- Would such prioritization provide comfort (to the legislature, settlement participants and/or CAP subcontractors) that the State can meet (has met) its Indian firming obligations?

***Does the AWBA distribute withdrawal fee credits for M&I firming in conjunction with the use of the four-cent tax credits or wait until the four-cent tax credits are fully utilized?***

The conditions and restrictions regarding use of four-cent tax credits have been identified in statute. Would it make sense to fully utilize those credits for M&I firming before withdrawal fee credits are used for the same purpose since withdrawal fee credits can be used for other purposes and are the only credits currently available for meeting Indian settlement obligations?

***If withdrawal fee credits are dedicated, who does the AWBA distribute those credits to?***

This would depend on what the credits are used for:

- There would be no need to distribute credits if they are extinguished to meet certain Indian settlement obligations and/or water management goals.
- Credits recovered for Indian firming purposes could be distributed to an entity (including, but not limited to, CAWCD) that has agreed to recover the credits and deliver the water or is accepting the credits pursuant to an exchange.
- If the credits are dedicated for M&I firming, should they be distributed in the same manner as four-cent tax credits are distributed?

***Should the AWBA treat withdrawal fee credits similar to the four-cent tax credits and distribute to CAWCD?***

If the credits are being used for M&I firming purposes it might be reasonable to follow the same procedure for distributing four-cent tax credits, which may include the assignment of credits directly to a subcontractor that has entered into an agreement with CAWCD.

The following questions are administrative in nature and can be addressed using procedures similar to those identified under the distribution of four-cent tax credits:

***Once distributed for M&I firming, how does the AWBA insure the credits are used for the benefit of the Active Management Area where the fees are collected?***

By requesting that ADWR assign AWBA credits at the end of the calendar year, the entity receiving the credits can notify the AWBA of the actual amount of credits recovered and used. The wells from which those credits were recovered must be reported to ADWR as part of the annual reporting requirements. Under current ADWR reporting requirements, the place of use of those credits can be verified if they were recovered by an M&I provider and used within that provider's service area.

***How are credits returned to the AWBA if they are not fully utilized by the entity that received the credits?***

By requesting that ADWR assign credits at the end of the calendar year based on actual recovery, there would be no need to return credits.

Distribution of Credits Meeting

May 17, 2011

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Distribution of Credits Meeting

May 17, 2011

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## Gerry L. Wildeman

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**From:** Virginia Oconnell  
**Sent:** Wednesday, June 01, 2011 1:06 PM  
**To:** Tim J. Henley; Gerry L. Wildeman  
**Subject:** FW: Policy questions regarding distribution of AWBA credits

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**From:** Miller, Elizabeth [<mailto:EMiller@scottsdaleaz.gov>]  
**Sent:** Wednesday, June 01, 2011 1:14 PM  
**To:** Virginia Oconnell  
**Subject:** Policy questions regarding distribution of AWBA credits

Virginia –

I'm glad you had the meeting on the 17<sup>th</sup> – it's good to get things moving forward a little faster. At the end of the meeting, you asked for written comments from the stakeholders in attendance to further document the discussion at the meeting. I've put together some quick thoughts/comments on the stuff that was discussed @ the meeting on the 17<sup>th</sup>. I hope that they will be helpful. Please let me know if you'd rather have them show up as some kind of formal letter. It seemed more straightforward just sending them to you via email. Also, if you would pls forward to Gerry and Tim. I can't find either of their emails in my contact list. Thanks!

I'm concerned mainly about the question of whether it is appropriate to distribute credits for water that is requested for accruing long-term storage credits. Scottsdale believes that there may be circumstances where this may be appropriate. However, the baseline decision that must be made before it is possible to answer this question is the degree to which we want to 'save' the ad valorem credits for future M&I firming needs. In order to have enough information to make that decision, we need to know how often M&I shortage is expected, and how long the AWBA credits can be expected to last given that shortage level. The AWBA Supply and Demand Analysis that is currently underway will be invaluable in helping to answer this threshold question. I would hope that no final policy decisions are made re the distribution of credits until this study is completed.

There may be circumstances where underground storage of AWBA credits may be determined to be "necessary" to meet certain water management objectives. For example, a municipal provider might want to store water to protect the physical availability of its groundwater against the increased groundwater pumping that would likely result in times of shortage. Scottsdale is particularly interested in preserving our ability to store water, due to our location at the topmost end of the hydrologic gradient in the ESRV basin. Increased groundwater pumping in any situation would result in an increase in the hydrologic gradient and therefore an increase in the rate that groundwater flows away from the City of Scottsdale. Being able to recharge water in strategic locations will help stabilize water levels at a level where we will be able to pump if it is necessary.

The hydrologic conditions within the northern part of our service area also make it very unlikely that we would be in a position to increase our groundwater pumping pursuant to ADWR's assured water supply drought exemption. Your discussion paper raises the question of whether it is appropriate to distribute AWBA credits for storage if a provider is also pumping (or is legally allowed to pump?) groundwater pursuant to their assured water supply drought exemption. I urge you to not apply a blanket prohibition on distribution

of recovered AWBA credits to all water providers that would be considered eligible for the drought exemption, since some of us may not be in a position to make use of it.

Our hydrologic situation also limits the ways that we would be able to take delivery of recovered AWBA credits. We simply would not be able to pump the credits and maintain physical availability should they be assigned to us for recovery from our own wells. Scottsdale's need is for direct delivery of AWBA credits through the CAP canal system to our surface water treatment plant.

These comments are my initial thoughts on some of the policy issues raised in your discussion paper and at the meeting on May 17<sup>th</sup>. I'm glad that Tim committed at the end of the meeting to work with CAP and ADWR to begin to clarify the relative roles of the various agencies. I'm sure that the policy framework (perhaps a 'straw man') that comes out of those discussions will help focus our discussions toward that resolution.

Again, thanks for the chance to comment. I look forward to working with the AWBA, CAP, and other stakeholders to discuss and resolve the many issues associated with planning for the distribution and use of AWBA's stored water.

Please let me know if you have any questions or would like clarification re these comments.

Beth M.