ARIZONA DEPARTMENT OF WATER RESOURCES

Revised Policy Regarding Transfer of Central Arizona Project Municipal and Industrial Water Subcontract Entitlements

February 27, 2006

I. Introduction

A. Scope of Policy.

For clarification purposes, the Arizona Department of Water Resources (Department) revised its 1996 policy regarding transfers of Central Arizona Project (CAP) municipal and industrial (M&I) subcontract entitlements. This policy statement applies to proposed transfers involving CAP allocations that were originally made for M&I purposes to non-Indian subcontractors. This policy is limited to proposed transfers with a term of more than one year, and to transfers within the three-county service area of the Central Arizona Water Conservation District (CAWCD). This service area includes portions of Maricopa, Pinal and Pima counties, and most of the Phoenix, Pinal and Tucson Active Management Areas (AMAs).

In order to receive an initial allocation of CAP water for M&I purposes, M&I entities entered into CAP subcontracts with the CAWCD and the United States Secretary of the Interior (Secretary). Under the terms of these subcontracts, if a subcontractor proposes to transfer its CAP subcontract entitlement, the subcontractor must obtain the prior written approval of both the CAWCD and the Secretary. State law also requires that the subcontractor "cooperate, confer with and obtain the advice of the director" of the Department for a proposed CAP subcontract or a proposed transfer of a CAP subcontract entitlement. A.R.S. § 45-107(D). After review, the Director makes a recommendation to the Secretary regarding the proposed subcontract or transfer. This policy addresses the process for complying with state law when an M&I subcontractor proposes to transfer a CAP subcontract entitlement.

For the purposes of this policy, the term "transfer" means the assignment, conveyance, or relinquishment of a CAP subcontract entitlement. These terms are defined as follows:

(a) A proposed transfer is considered an assignment when a CAP M&I subcontractor proposes to transfer all or a portion of its CAP subcontract entitlement to a successor in interest that will serve the same CAP subcontract service area.

(b) A proposed transfer is considered a conveyance when a CAP M&I subcontractor proposes to transfer all or a portion of its CAP subcontract entitlement to: (1) a replenishment district that will use the CAP subcontract entitlement for replenishment purposes, (2) another entity that is not a successor in interest, such as a county water augmentation authority, that will use the CAP water to directly serve the same CAP subcontract service area, or (3) another entity that will use the CAP water outside the transferring entity's CAP subcontract service area. A replenishment district includes the Central Arizona Groundwater Replenishment District (CAGRD), which is a division of the CAWCD that is responsible for replenishing

groundwater pursuant to A.R.S. § 48-3771 *et seq.* A county water augmentation authority is an authority established pursuant to A.R.S. § 45-1901 *et seq.*

(c) A proposed transfer is considered a relinquishment when a CAP subcontractor proposes to terminate its CAP M&I subcontract without an assignment or a conveyance agreement. This policy statement sets forth the Department's process for reviewing and evaluating these types of proposed transfers.

B. State's Interests.

Because the transfer of a CAP subcontract entitlement may result in a redistribution of the state's water supply, the state has an interest in assuring that transfers are consistent with the intent of the original allocation of CAP water, which was made by the Secretary upon recommendation of the Director. The intent of the original allocations was to reduce or eliminate groundwater overdraft, thereby ensuring the availability of water for the future growth and development planned by counties, cities and towns in central Arizona. CAP water is a major, and sometimes the only, renewable source of water supply for many urban and industrial water demands in central Arizona. Although growth and water use patterns may change during the term of the CAP subcontract, the certainty that water supplies will be available to specific areas helps to ensure that local and regional development will be consistent with long-range plans. Explicit policy and procedures are necessary to assure adequate and consistent evaluations of proposed transfers of CAP subcontract entitlements.

C. Statutory Responsibilities.

The Director is generally responsible for formulating plans and programs for the development, management, conservation and use of surface water and groundwater. A.R.S. § 45-105. The Director also has specific statutory authority and responsibility to "consult, advise and cooperate with the Secretary of the Interior of the United States" regarding allocations of Colorado River water, including proposed transfers of those allocations. A.R.S. § 45-107(A). Consistent with the Director's responsibilities, entities that contemplate transferring their CAP subcontract entitlements are required to cooperate, confer and obtain the advice of the Director, and to submit relevant documents for the Director's review. A.R.S. § 45-107(D) states as follows:

> Individuals, irrigation districts, corporations, state departments, agencies, boards, commissions and political subdivisions of the state shall cooperate, confer with and obtain the advice of the director as to those negotiations, contracts and subcontracts described in subsection C that affect the allocation and use of main stream Colorado river water or the allocation and use of Colorado river water delivered through the central Arizona project. For a proposed contract or subcontract or a proposed amendment of a contract or subcontract that will result in a transfer of an allocation or entitlement of Colorado river water, including central Arizona project water, from a non-Indian Arizona contractor or subcontractor for a term of more than one year, the obligation to cooperate, confer with and obtain the advice of the director shall include the obligation to submit to the director for review the proposed contract or subcontract or the proposed amendment, and all related exhibits and agreements, prior to its execution by the contractor or subcontractor.

After review, the Director makes recommendations to the Secretary regarding the redistribution of the CAP water, which the Secretary fully considers. The purpose of this policy is to describe the process for obtaining the Director's review of, and recommendation on, proposed transfers of CAP subcontract entitlements.

D. General Description of Process.

This policy statement describes the Water Management Objectives, Review Criteria, Decision Guidelines and review and public notice process that the Director will use to evaluate proposed transfers of CAP subcontract entitlements. The Director will review all proposed transfers for consistency with the Water Management Objectives and Review Criteria, which are described in Sections II and III. If two or more entities satisfy the Water Management Objectives and Review Criteria and request the same CAP subcontract entitlement being proposed for transfer, the Director will make a recommendation using the Decision Guidelines described in Section IV. As required by the review and public notice process described in Section V, the transferring and receiving entity must send a written request for review to the Department and must submit supporting documentation. Except for assignments of CAP subcontract entitlements, the Department will provide for, and the Director will consider, public comment regarding the proposed transfer.

II. Water Management Objectives

The criteria for evaluating proposed CAP transfers are based on several Water Management Objectives, which the Department will use to evaluate each proposed transfer. The Water Management Objectives for CAP transfers are:

- To promote transfers of CAP subcontract entitlements that result in the use of CAP water for the benefit of the transferring entity's CAP subcontract service area; or,

- To minimize third party impacts resulting from groundwater pumping by the transferring entity that may occur as a result of the conveyance of a CAP subcontract entitlement; or,

- To promote conveyances of CAP subcontract entitlements that benefit areas outside of the transferring entity's CAP subcontract service area through either (a) near term and direct use of CAP water by a receiving entity to meet existing groundwater demands, or (b) replenishment by a replenishment district to meet the replenishment obligation of the transferring entity or member lands within the transferring entity's service area; or,

- To promote conveyances of CAP subcontract entitlements that benefit areas outside of the transferring entity's CAP subcontract service area through future use of CAP water by a receiving entity, or future use of CAP water by a replenishment district to replenish groundwater; and,

- To promote the management goals of the AMAs (See A.R.S. § 45-562) within the three-county CAWCD service area; and,

- To minimize known environmental, social and economic impacts, that may occur as a result of the transfer of a CAP subcontract; and,

- To ensure that all entities wishing to obtain a CAP allocation demonstrate adequate financial capability to pay costs associated with CAP water use; and,

- To ensure that existing CAP M&I allocations remain available for M&I purposes in the future.

III. Review Criteria

Proposals to transfer CAP subcontract entitlements must be consistent with the Water Management Objectives described above to receive a favorable recommendation from the Director. To determine consistency with these objectives, the Department will evaluate each transfer using the following Review Criteria.

A. Benefits to Transferring Entity's CAP Subcontract Service Area.

This policy favors the transfers of CAP subcontract entitlements that benefit the transferring entity's CAP subcontract service area. This objective may be satisfied through an assignment to a successor in interest. If the proposed transfer does not involve an assignment of a CAP subcontract entitlement to a successor in interest, the Department will consider either: (a) a conveyance to a county water augmentation authority that will use the CAP water to directly serve the CAP subcontract service area of the transferring entity, or (b) a conveyance to a replenishment district to replenish groundwater in the area of impact of the transferring entity's groundwater withdrawals.

B. Minimizing Third Party Impacts.

This policy next favors minimizing any known third party impacts resulting from groundwater pumping by the transferring entity. If a transferring entity intends to meet its water demands by pumping groundwater after the CAP subcontract entitlement is transferred, the Department will evaluate groundwater conditions by analyzing future groundwater level declines and water availability for the transferring entity, and the impact on an entity that requests all or a portion of the CAP subcontract entitlement. The Department may recommend that all or a portion of a CAP subcontract entitlement be conveyed to a requesting entity to mitigate the impacts resulting from the transfer of the entitlement. The recommended allocation will be limited to the average annual loss of groundwater that may have been recoverable by the requesting entity.

C. Near Term and Direct Use of CAP Water, and Replenishment.

This policy next favors conveyances of CAP subcontract entitlements that benefit areas outside of the transferring entity's CAP subcontract service area through either: (1) near term and direct use by the receiving entity to meet existing groundwater demands, or (2) replenishment by a replenishment district to satisfy the replenishment obligation of the transferring entity or member lands within the transferring entity's service area by replenishing groundwater outside the area of impact of the transferring entity's groundwater withdrawals.

Direct use means either: (a) the direct delivery of CAP water, or (b) the storage of water at a groundwater savings facility or underground storage facility and the recovery of the CAP water on an annual basis within the area of impact of the stored water. Storage of CAP water at a groundwater savings facility or an underground storage facility for long-term storage credits will not be considered direct use of CAP water.

D. Future Use of CAP Water, and Replenishment.

This policy next favors conveyances of CAP subcontract entitlements that benefit areas outside of the transferring entity's CAP subcontract service area through future use by the receiving entity, other than a replenishment district, first at a date prior to the year 2035, and then in the year 2035. Next, the Department will consider conveyances to a replenishment district that will use the CAP water to replenish groundwater in the year 2035.

E. AMA Goals.

All proposed transfers must promote the management goals of the AMAs within the three-county CAWCD service area. Most of the Phoenix, Pinal and Tucson AMAs are located within the three-county CAWCD service area. Generally, the management goals for these AMAs are intended to prevent or reduce the overdraft of groundwater within each AMA, which was the intent of the Director's original CAP allocation recommendations.

F. Environmental, Economic, or Social Impacts.

The Department will evaluate any known adverse impacts associated with proposed transfers. Loss of CAP water to an M&I subcontractor may exacerbate local groundwater depletion and any attendant environmental problems. A list of potential impacts caused by groundwater declines includes, but is not limited to:

- Costs incurred by third parties due to groundwater declines and loss of groundwater supplies.
- Migration of groundwater contamination.
- Moratoriums on development due to lack of sufficient water supplies.
- Land subsidence.
- Interference with recovery of stored water.
- Loss of important natural areas.

The Department's recommendation may be conditioned upon mitigation of these impacts.

G. Ability to Pay.

Stable, financially secure M&I entities with adequate water supplies are in the best water management interests of the state. For all proposed transfers, the receiving entities must demonstrate the ability and willingness to pay all costs associated with CAP water use including subcontract costs for the life of the subcontract; construction costs of all necessary infrastructure, treatment and distribution systems to deliver CAP water; and any subcontract holding costs incurred by the transferring entity as determined by the CAWCD.

H. Future Availability of CAP M&I Allocations.

The Secretary made the original allocations of CAP water based upon the recommendation of the Director, who took into consideration the availability of water for future growth and development in the three-county CAWCD service area through the reduction or elimination of groundwater overdraft. When a subcontractor within the three-county CAWCD service area no longer wishes to hold a CAP M&I subcontract, the state has an interest in ensuring that the CAP subcontract entitlement remains available for future use within the three-county CAWCD service area by another CAP M&I subcontractor.

IV. Decision Guidelines

If two or more entities satisfy the Water Management Objectives and Review Criteria stated above, and they request the same CAP subcontract entitlement proposed for transfer, the Director will use the guidelines set forth below. These guidelines establish priorities based on the Water Management Objectives and Review Criteria of this policy. The Department may recommend that a CAP subcontract entitlement be transferred on a pro rata basis between entities with the same priority.

The Department will first consider interested recipients that are located within the same AMA as the transferring entity. Next, the Department will evaluate interested recipients in the other two AMAs in CAWCD's three-county service area. If a CAP M&I subcontractor located within CAWCD's three-county service area, but not within an AMA, proposes to transfer its CAP subcontract entitlement, the Department will consider interested recipients from all three AMAs within CAWCD's three-county service area.

1. First priority will be recommended to an entity that is the successor in interest to the transferring entity, or that can provide sufficient evidence that it will become the successor in interest to the transferring entity in the near future, and that will provide water to the same CAP subcontract service area.

2. Second priority will be recommended to either: (a) a replenishment district that will use the CAP water to replenish groundwater within the area of impact of groundwater withdrawals of the transferring entity, or (b) a county water augmentation authority that will use the CAP water to directly serve the transferring entity's CAP subcontract service area.

3. Third priority will be recommended to an entity that demonstrates adverse impacts on its ability to meet its water demands due to groundwater withdrawals by the transferring entity as a result of the transfer of a CAP subcontract entitlement.

4. Fourth priority will be recommended to either: (a) an entity outside the transferring entity's CAP subcontract service area that will directly use the CAP water in the near term to meet its existing groundwater demands, or (b) a replenishment district that will use the CAP water to satisfy a replenishment obligation of the transferring entity or member lands within the transferring entity's service area by replenishing groundwater outside of the area of impact of the transferring entity's groundwater withdrawals.

5. Fifth priority will be recommended to an entity, other than a replenishment district, that demonstrates the need for the CAP water to meet water demands in the future at a date prior to the year 2035.

6. Sixth priority will be recommended to an entity, other than a replenishment district, that demonstrates the need for CAP water to meet water demands in the year 2035.

7. Seventh priority will be recommended to a replenishment district to replenish groundwater in the year 2035.

V. Review and Public Notice Process

All proposed transfers will be subject to the Water Management Objectives, Review Criteria and Decision Guidelines set forth above. However, as described below, the Department will follow a different review and public notice process for each type of transfer.

A. Assignments.

If a CAP M&I subcontractor proposes to assign its CAP subcontract entitlement, both the transferring entity and the receiving entity shall submit a written request for review to the Department together with the assignment agreement and all related documentation. The Department will provide to the transferring and receiving entities written comments requesting any additional information or documentation that may be required. Because the CAP subcontract entitlement will be used to serve the same CAP subcontract service area, the proposed assignment will not be subject to public review and comment. After receipt of any required information or documentation, the Director will issue a recommendation to the Secretary, with a copy to CAWCD, regarding the proposed assignment.

B. Conveyances.

If a CAP M&I subcontractor proposes to convey its CAP subcontract entitlement to another entity, both the transferring and the receiving entities shall submit a written request to the Department together with the conveyance agreement and all related documentation. Both the receiving entity and the transferring entity must submit water supply development plans that demonstrate how the proposed transfer will meet the Water Management Objectives, Review Criteria and Decision Guidelines stated above in Sections II, III, and IV. At a minimum, these plans shall include approximate quantities of water available to the respective service areas to meet demands, the sources of water, how the CAP water will be used by the receiving entity, and information regarding costs and time frames for implementing the plans. After receipt of submitted documentation, the Department will provide to the transferring and receiving entities written comments requesting any additional information or documentation that may be required. After receipt of all required information, the Department will advertise the proposed conveyance once a week for two consecutive weeks in a newspaper of general circulation in the three-county CAWCD service area. The Department will concurrently advertise the proposed conveyance on its website at www.azwater.gov. The Department will send notice of a proposed conveyance by mail to all persons on the Department's mailing list of entities that have requested notification, as well as to all current CAP M&I subcontractors. The Department will accept public comment on the proposed conveyance for 30 days after the second

newspaper advertisement. If, during the public comment period, another entity requests part or all of a CAP subcontract entitlement involved in a proposed conveyance, the requesting entity must demonstrate that it has the same or a higher priority for the CAP subcontract entitlement.

After the close of the public comment period, the Department will provide to the transferring and receiving entities, and any requesting entity, additional written comments requesting any information or documentation that may be required as a result of public comment and review. After the Department receives any additional information and documentation that may be required, the Director will issue a recommendation to the Secretary, with a copy to CAWCD, regarding the proposed conveyance.

C. Relinquishments.

If a CAP M&I subcontractor proposes to relinquish its CAP subcontract entitlement, but has not entered into an assignment or conveyance agreement, the Director will advertise, after consultation with CAWCD, an "offer to transfer" in a newspaper of general circulation in the three-county CAWCD service area once a week for two consecutive weeks. The Department will concurrently advertise the offer to transfer on its website at www.azwater.gov. The Department will send a notice of any offers to transfer by mail to all persons on the Department's mailing list of entities that have requested notification, as well as to all current CAP M&I subcontractors. Requests for CAP subcontracts and general public comment must be submitted to the Department within 30 days of the second newspaper advertisement.

The Department will review requests for subcontract entitlements pursuant to the Water Management Objectives, Review Criteria and Decision Guidelines in Sections II, III and IV of this policy. After the close of the request and public comment period, the Department will provide to the requesting entities written comment requesting any additional information or documentation that may be required. After receipt of any required information and documentation, the Director will issue a recommendation to the Secretary, with a copy to the CAWCD, regarding a request for a CAP subcontract entitlement.

The Director may modify or revoke this policy at any time.

EFFECTIVE DATE:
February 27, 2006

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Director
Arizona Department of Water Resources