

## BOARD OF DIRECTORS

### *Information Summary*

August 6, 2008

#### **Subject**

CAGRDR Revenue Bonding Proposed Legislation

#### **Summary**

In 2007, concerns were raised regarding whether the current funding sources (enrollment fees, activation fees and the infrastructure and water rights component of the annual replenishment assessment/tax) for the Central Arizona Groundwater Replenishment District (CAGRDR) were sufficient to secure the water supplies needed for the CAGRDR to meet its replenishment obligations. Central Arizona Water Conservation District (CAWCD) initiated a stakeholders' process by which to determine how best to secure the funding needed to acquire the supplies needed to meet its replenishment obligations. Recommendations regarding increased fees and assessments were developed. The CAWCD Board of Directors debated these recommendations, but took no action on the proposed fee and assessment increases. The CAWCD Board instructed staff to seek legislation to authorize the CAWCD Board to issue revenue bonds to meet its replenishment obligations.

During the 2008 legislative session, the CAWCD sought legislation that would allow CAWCD to issue revenue bonds for the purpose of securing sufficient water supplies for the CAGRDR. Toward that end, Senators Flake and Aguirre introduced SB 1391 CAP Revenue Bonds.

Provisions of SB 1391:

1. Struck the provision under the powers and duties of the CAWCD Board of Directors of the CAWCD that prohibits the Board from pledging replenishment assessment revenues and replenishment tax to repay revenue bonds, thereby giving them the authority to use such revenues for revenue bond repayment purposes.
2. Current statute limits the amount of bonds that may be issued by the CAWCD to \$250,000,000. SB 1391 would have increased this amount to \$500,000,000.
3. Specifically authorized the CAWCD Board to issue revenue bonds to fund the cost and expenses of CAWCD with respect to replenishment, including the acquisition of water, water rights, and effluent.

4. Authorized the CAWCD Board to charge an annual fee for membership in the CAGR in addition to the fee for excess groundwater use.

Due to the concerns raised by stakeholders, SB 1391 did not move forward. CAWCD committed to meet with stakeholders to identify and attempt to address concerns with the proposed legislation. CAWCD staff worked with stakeholders during meetings held in conjunction with the AMWUA Sustainability Policies Stakeholders.

CAWCD staff is currently meeting with individual stakeholders to address specific concerns and clarify the operation of the bonding mechanism. The issues being discussed address many of the provisions proposed in SB 1391. The CAWCD Board is expected to address the CAGR bonding issue at its August 7 Board Meeting.

### **Considerations**

- If CAWCD is authorized to issue revenue bonds to secure water supplies and to provide a revenue source for other costs associated with its replenishment obligations, its ability to issue revenue bonds for other purposes may be compromised. The costs for non-replenishment related projects could shift to Central Arizona Project (CAP) subcontractors. Existing water users would then be responsible not only for the cost of assuring that their water supplies are secure, but be indirectly responsible for the excess groundwater use by water users who live outside of their communities.
- The ability to use revenue bonds for other projects may not be an option since CAWCD may hit its bonding limitation as a result of meeting its statutorily prescribed replenishment obligations.
- Allowing the CAWCD Board to issue bonds for CAGR purposes may increase the cost of financing CAP-related capital projects.
- The purpose for which AMWUA members join the CAGR for an Assured Water Supply varies significantly from member to member. Some members use the CAGR for replenishment purposes, others may use it as an “insurance policy” to assure that their designations are maintained, but do not intend to use it for replenishment purposes. The assessment of an annual membership fee will impact member service areas in different ways. Creation of an annual membership fee, based on maximum potential use of the CAGR, may work for member lands, but will be complicated by the many reasons that member service areas have enrolled in the CAGR.
- This legislative initiative could have implications for the legislative recommendations of the AMWUA Sustainability Policies Stakeholders Group.

### **Prior Committee Action**

The Board previously has received updates regarding this issue. At its July 30 meeting, the AMWUA Management Board recommended that the AMWUA Board of Directors direct

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AMWUA and members' staff to work with the CAWCD Board and other stakeholders on issues related to sustainability and to work with the CAWCD Board to identify concerns raised regarding proposed legislation.

### **Recommendations**

The AMWUA staff recommends that the AMWUA Board of Directors direct AMWUA and members' staff to work with the CAWCD Board and other stakeholders to balance the interests of the AMWUA Sustainability Policies with the interests of the stakeholders who are supporting the revenue bonding legislation; and that AMWUA staff be directed to work with the CAWCD Board to identify concerns raised regarding proposed legislation.

### **Attachments**

“Position Paper on CAGR Revenue Bonding” Draft of July 28, 2008

**Position Paper on CAGRDR Revenue Bonding  
Draft of July 28, 2008**

Overview of CAGRDR

The Legislature passed the Groundwater Replenishment District Act in 1993, which created a groundwater replenishment authority that is referred to as the Central Arizona Groundwater Replenishment District (CAGRDR). CAGRDR is operated and governed by the Central Arizona Water Conservation District (CAWCD).

While referred to as a “District,” the CAGRDR is not a special purpose district. Legally it is a division within CAWCD responsible for carrying out the statutorily prescribed replenishment obligation of CAWCD. CAGRDR fulfills these replenishment obligations in the CAWCD service area, which encompasses the areas in Maricopa, Pinal, and Pima counties in which the Phoenix, Pinal, and Tucson Active Management Areas (AMAs) are located.

The Assured Water Supply (AWS) Rules are designed to protect groundwater supplies within the AMAs and ensure that future developments have a water supply of adequate quality and quantity for at least 100 years. An assured water supply must be demonstrated before subdivided lots may be sold in an AMA. The AWS Rules limit the amount of groundwater that may be used to demonstrate an AWS. Additionally, an AWS applicant must demonstrate, among other things, that the proposed use of water is consistent with achieving the management goal of the AMA.

For the Phoenix and Tucson AMAs, Arizona water law sets a management goal of safe-yield, which means that the amount of groundwater that is pumped out of the ground does not exceed the amount that returns to the AMA’s aquifers. The Pinal AMA management goal recognizes the necessity to preserve future groundwater supplies for non-irrigation uses. The combination of the AWS program and the management goals for the AMAs has resulted in an increased commitment to use of renewable water supplies and reduced dependence on non-renewable groundwater.

The CAGRDR plays a key role in the Assured Water Supply (AWS) Program and membership in CAGRDR provides a means by which an AWS applicant can meet the AWS requirements. There are two classes of membership in the CAGRDR – member lands and member service areas. If the owner of subdivided land joins the CAGRDR, the parcels within that subdivision are classified as “member lands”. If a municipal water provider joins the CAGRDR, the municipal water provider is considered a “member service area”. Both member lands and member service areas are allowed to rely on more groundwater to demonstrate an AWS than would otherwise be allowed under the AWS Rules. Groundwater use, termed “excess groundwater,” is allowed as long as the Arizona Department of Water Resources (ADWR) determines that the excess groundwater is physically available for 100 years and the landowner or municipal provider pays CAGRDR to replenish the excess groundwater within three calendar years of the time it is withdrawn. CAGRDR must replenish the excess groundwater in the same AMA in which it is withdrawn.

At the present time, CAGR D relies on excess CAP water and a CAP Municipal and Industrial (M&I) subcontract acquired by the CAGR D as its principal water supplies to meet replenishment obligations. Additional sources used by the CAGR D include short-term CAP leases, effluent and acquisition of long-term storage credits. However, as CAP supplies become fully utilized, additional water supplies must be developed to fulfill CAGR D's replenishment obligations. The cost to acquire future water supplies is expected to be higher than the cost incurred to acquire existing water supplies.

CAGR D funds water rights acquisitions and development of related infrastructure through three revenue sources: 1) enrollment fees; 2) activation fees; and 3) the water rights and infrastructure component in the CAGR D's annual replenishment assessment and annual replenishment tax.

For member lands, the enrollment fee is a one-time, per unit fee assessed on the owner of subdivided land seeking enrollment in CAGR D. The enrollment fee, currently set at \$74.00 per housing unit, is typically paid by the developer. For member service areas, the enrollment fee is a one-time fee of \$5,000 per service area, which is levied to cover the administrative cost associated with the enrollment. Five AMWUA cities have enrolled as member service areas in the last 15 years.

The activation fee is a one-time fee based on the number of housing units in a subdivision and must be paid to CAGR D before issuance of a public report by the Arizona Department of Real Estate and prior to the sale of any parcels in the subdivision. For member service areas of CAGR D, the activation fee may be paid by the water provider or the fee may be passed through to the developer. The developer typically pays the activation fee for developments joining CAGR D as member lands. This fee is currently set at \$72.00 per housing unit.

The Water Rights and Infrastructure Component of CAGR D's annual replenishment assessment and annual replenishment tax is currently set at \$90 per acre-foot. The total assessment rate for the Phoenix AMA for tax year 2008-2009 is set by the CAWCD Board at \$290 per acre-foot. CAGR D's replenishment assessment is levied against the actual volume of excess groundwater used by its members. Member lands, i.e. individual homeowners, pay assessments as part of their property tax bills. Municipal providers enrolled as member service areas pay an annual replenishment tax based on the replenishment obligation incurred in the service area during the year.

#### Problem Statement

The current CAGR D Plan of Operation estimated that CAGR D would need to spend more than \$260 million through 2027 for future water rights acquisition and infrastructure development to meet the projected replenishment obligations identified in the plan. CAGR D estimated its ultimate replenishment obligation for current members and potential members expected to enroll through 2015 would be 226,800 acre-feet per year.

Currently, CAGR D estimates that about 70% of the water development program will be paid for through annual replenishment assessments and taxes, 18% will come from activation fees, 3% will come from enrollment fees, and 9% will come from interest generated from these revenues.

The revenues collected from enrollment fees, activation fees and the water rights and infrastructure component of the assessments and taxes, are not expected to be sufficient to finance future water rights acquisitions and related infrastructure development without significant increases from the rates established for tax year 2007-2008.

The CAWCD Board of Directors is exploring options to ensure that adequate and equitably generated revenues are available to finance water development necessitated by the growing demands placed on CAGR. Initially, the CAWCD proposed increasing the activation and enrollment fees, but these increases were opposed by some members of the development community. As part of the subsequent discussion, the CAWCD Board is exploring the feasibility of seeking legislation allowing it to issue revenue bonds to help finance water development for CAGR. Discussion has centered on the appropriate balance of cost allocation for future water supplies. The key issue is the amount that member service areas and homeowners should pay through annual assessments and taxes versus the amount that developers should pay up front when they first join the CAGR and receive a Certificate of AWS from ADWR.

#### Existing Statutory Authority

Title 48, Chapter 22, Article 4 of the Arizona Revised Statutes (ARS) describes the replenishment functions of CAWCD.

ARS §48-3712.A.6 prohibits repayment of CAWCD revenue bonds using money received from “replenishment assessment revenues and replenishment tax.”

ARS §48-3772.A.3 establishes the authority for the CAWCD Board to levy an annual replenishment property tax assessment against each parcel of land for member lands and an annual replenishment tax against each member service area.

ARS §48-3772.A.7 establishes the requirement that CAWCD levy an activation fee.

ARS §48-3772.B provides the authority for CAWCD to develop water supplies for the benefit of CAGR member lands and member service areas.

ARS §48-3762 limits CAWCD’s aggregate revenue bonding capacity to \$250 million.

#### Policy Statements

1. CAGR must have adequate funds to finance water rights acquisition and infrastructure development to meet its replenishment obligations and to ensure that the CAGR Plan of Operation complies with statutory requirements.
2. Funds available for CAGR must be adequate when water acquisition is needed.
3. Funds used for CAGR water development must be equitably generated.

4. Financing water development for CAGR D purposes must not impact the CAP's ability to finance projects that benefit M&I CAP customers.
5. CAGR D water development funding must not impact the ability of member service areas to develop water supplies independent of CAGR D or to de-enroll if a member service area no longer needs to rely upon CAGR D.
6. Since Water Availability Status members provide their own water for replenishment, these members should not pay CAGR D for additional water rights acquisition (currently Scottsdale is the only Water Availability Status member).
7. CAP M&I customers' bonding authority must not be directly or indirectly impacted by CAGR D bonding.
8. The CAWCD Board of Directors must be prohibited from pledging or identifying current or future CAP M&I revenues as a source of repayment of CAGR D obligations.
9. Revenue streams must meet bond repayment obligations including:
  - a. Adequate times-coverage of Maximum Annual Debt Service for both outstanding and proposed obligations.
  - b. Funding of any required bond reserve or replacement and extension account.
  - c. Cost of insurance of proceeds, including surety bonds, purchased in lieu of a reserve or replacement account.
10. Member service areas must not bear the cost of new member lands development.

#### Criteria for a Solution

1. If bonding is used to fund CAGR D water development, adequate protections must be established to ensure that financing of CAP related capital projects will not be impacted.
2. Non-CAGR D related revenues must be prohibited from being used to repay CAGR D related bonds.
3. Protections must be in place to ensure that CAP financial health will not be directly or indirectly the basis for obtaining CAGR D related bonds.
4. Adequate revenues must be generated from activation and enrollment fees to ensure that, as future water supplies are acquired, existing CAGR D members are not paying disproportionately increased water costs.
5. Revenues generated from member service areas must be in proportion to the actual dependence of each member service area on CAGR D for water supplies and meeting assured water supply requirements.

6. Revenues generated from member service areas must not subsidize service to member lands.
7. Bonding authority would be restricted so that the extent that bonds may be issued is based on future revenue streams generated only by usage, and shall not be secured by the value of property upon which assessments or taxes are based.
8. Assessments and taxes must be levied in accordance with a long-term plan to ensure that adequate funds are in place and that it is possible for members to project impacts of assessments and taxes.

#### Strategic Considerations

1. What is AMWUA's position regarding potential linkages between the sustainability legislation, the revenue bonding legislation and the ADD Water process?
2. Given state budget issues, is it a good time to discuss CAWCD financial provisions at the legislature?
3. How will the discussion of CAGRDR bonding authority impact future proposals for direct delivery of CAGRDR water to Member Service Areas?
4. What are the impacts of raising the CAP bonding capacity limitation for CAGRDR purposes if additional CAP bonding is necessary?

#### CAWCD Proposal

CAWCD has been hosting a series of stakeholder meetings. At these meetings, a proposal has been evolving. The current CAGRDR staff proposal consists of:

1. Removing the prohibition on using bonding authority and allowing the use of replenishment assessment revenues and replenishment taxes to repay bonds.
2. Doubling the existing aggregate bonding limit to \$500 million.
3. Establishing an annual "membership fee" to be collected from all members whether they use excess groundwater or not. Revenues from the membership fee must be used for acquisition of water rights and development of infrastructure, including paying bond debt.
4. Specifying that the annual membership fee be divided between member lands and member service areas based on the replenishment obligation incurred for each member class.
  - a. Membership fees for member lands would be based on the replenishment obligation projected for the lands at build-out.

- b. Membership fees for member service areas would be based on the total obligation identified in member service agreements between the provider and the CAGRDR or based on the amount of excess groundwater specified in the provider's designation of assured water supply.
5. Providing that enrollment fees, activation fees, and the water rights and infrastructure component of CAGRDR's replenishment assessments and taxes must be levied so as to generate at least twice the projected revenues from the membership fees.

#### AMWUA Position

AMWUA will not support legislation that does not address the concerns raised in the "Policy Statements" and "Criteria for Solution" sections of this position paper.

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