

ADD WATER PROGRAM PROPOSAL

(CAP Staff Proposal as Modified by AFTER¹ HIOG-2)

STAKEHOLDER COALITION² COMMENTS

08-18-11

(Comments are shown in ALL CAPS and stricken text; for ease of reference, shaded text shows CAWCD new language from previous CAP Staff Proposal)

[COMMENT: THE STAKEHOLDER COALITION NOTES THAT THE CAP STAFF PROPOSAL DOES NOT ADDRESS ALL OF THE ADD WATER ISSUES. THE STAKEHOLDER COALITION IS COMMENTING ON ONLY THOSE ISSUES CONTAINED IN THIS PROPOSAL.]

WATER SUPPLY

Phased Approach

1. The ADD Water and Just Water Programs will be structured as a series of "phases."
2. CAWCD will initiate new phases at regular intervals, not expected to exceed five years.

[COMMENT: ADD NEW BOX TO READ: "ALTERNATIVE OFFERED BY STAKEHOLDER COALITION: CAWCD WILL INITIATE NEW PHASES AS NECESSARY, AS FURTHER DESCRIBED IN ATTACHMENT A."]

¹ HIOG-2 HAS NOT AGREED TO ALL OF THE MODIFICATIONS.

² THE MEMBERS OF THE STAKEHOLDER COALITION ARE REPRESENTATIVES OF RESOLUTION COPPER, SALT RIVER PROJECT, CENTRAL ARIZONA IRRIGATION AND DRAINAGE DISTRICT, HOHOKAM IRRIGATION AND DRAINAGE DISTRICT, POTENTIAL WATER SUPPLIERS, THE CITY OF TUCSON, THE SOUTHERN ARIZONA WATER USERS ASSOCIATION, AND AMWUA AND ITS MEMBER MUNICIPALITIES. THE STAKEHOLDER COALITION IS NOT COMMENTING ON THE ALTERNATIVES OFFERED BY THE ARIZONA MINING ASSOCIATION.

3. In each phase, CAWCD will acquire/develop new water supplies for the ADD Water Program, a portion of which will be dedicated to CAGR. CAWCD will also acquire new water supplies for the Just Water Program in each phase.

- a. CAWCD, in consultation with potential ADD Water contractors, will determine the target volume to be acquired for the Long-Term ADD Portfolio and for the Short-Term ADD Portfolio for non-CAGR contractors for each phase during a "pre-launch" planning process that will evaluate the potential demand for ADD Water.

[COMMENT: THE SHADED TEXT HAS NOT BEEN DISCUSSED BY THE HIOG-2. THE STAKEHOLDER COALITION CONTINUES TO BELIEVE THAT THE CONCEPT OF A SINGLE PORTFOLIO OF LONG-TERM WATER SUPPLIES AND A SINGLE PORTFOLIO OF SHORT-TERM SUPPLIES IS IMPRACTICAL AND INFEASIBLE, AND THAT ADD WATER SUPPLIES FOR EACH PHASE MUST BE MANAGED SEPARATELY. WE PROPOSE THAT THE HIGHLIGHTED LANGUAGE IN SECTION 3a AND 3b BE DELETED. DELETING THIS LANGUAGE WILL ALLOW CAP STAFF AND ALL STAKEHOLDERS TO DISCUSS THIS CONCEPT AT THE APPROPRIATE TIME.]

- b. CAWCD will determine the target volume to be acquired for the Long-Term ADD Portfolio and for the Short-Term ADD Portfolio for CAGR in each phase.
 - c. CAWCD, in consultation with potential Just Water contractors, will determine the target volume to be acquired for the Just Water Program in each phase.
4. Phases will continue until the ADD Water Program target volume of 300,000 acre-feet and the Just Water Program target volume of 50,000 acre-feet have been acquired/developed or until CAWCD determines that no additional ADD Water or Just Water supplies are available, whichever occurs first.

Alternative offered by ARIZONA MINING ASSOCIATION: CAP would offer long term (permanent) Colorado River (CR) water supplies in each phase that would qualify for Assured Water Supply (AWS). The volume of the first phase would be increased to 35,000 AF to accommodate industrial users. There would be no separate set aside for industrial users, who would compete for the general pool consistent with sharing criteria applicable to all users. A separate industrial pool would be developed outside the phases for "Other Water", i.e., non-permanent (i.e., short term supplies, or supplies available for 50 years or less), and non-CR permanent supplies. The size of the pool would be determined by demand, based on input from the prospective industrial contractors. Outside phase water would be considered ADD Water subject to the same priority and access to the canal as supplies secured within phases.

Phase 1

1. For Phase 1, CAWCD will acquire 30,000 acre-feet as follows:
 - a. CAWCD will acquire 20,000 acre-feet of ADD Water for potential contractors other than the CAGR. Distribution between the Long-Term ADD Portfolio and the Short-Term ADD Portfolio is yet to be determined.

[COMMENT: THE SHADED TEXT IN THIS PHASE 1 SECTION HAS NOT BEEN DISCUSSED BY THE HIOG-2. THE STAKEHOLDER COALITION PROPOSES THAT THIS LANGUAGE BE DELETED. THE CONCEPT REQUIRES DISCUSSION AND IS UNNECESSARY TO THIS DRAFT.]
 - b. CAWCD will acquire 6,700 acre-feet of ADD Water for CAGR. Distribution between the Long-Term ADD Portfolio and the Short-Term ADD Portfolio is yet to be determined.
 - c. CAWCD will acquire 3,300 acre-feet for the Just Water Program.

ADD Water Use of CAP Canal Capacity

1. Conditions for taking delivery of ADD water will be incorporated into contracts or statutes as appropriate.
2. ADD Water contractors may be subject to monthly delivery limitations (e.g. 11% of annual entitlement).
3. Deliveries of CAP Project Water, including CAP Excess Water, shall have priority to use of CAP system capacity over deliveries of ADD Water, which is non-Project Water. CAWCD will acquire new water supplies for all ADD Water. CAWCD will divert and deliver all water available from the Colorado River up to the full capacity of the CAP system, including improvements to that system. CAWCD will begin improvements to expand canal capacity at the start of the ADD Water Program. Deliveries of ADD Water will have priority to use the increased canal capacity paid for by ADD Water contractors.
4. Any ADD Water contractor may also enter into a special CAP Excess Water (ADD Replacement) contract that will be applicable only in a year in which the availability of surplus³ Colorado River water prevents CAP from delivering some or all of the contractor's ADD Water entitlement—i.e., when the ADD Water has been displaced in the system by surplus Colorado River water. In a surplus year, CAWCD would offer the contractor holding an ADD Replacement Contract an amount of CAP Excess Water up to the contractor's ADD Water contract amount

³ A surplus year occurs when the Secretary of the Interior declares a surplus and Arizona is entitled to more than 2.8 million acre feet of Colorado River Water.

that could not be delivered because it was displaced by surplus Colorado River water, after first providing for:

- a. Rights to CAP water, including CAP Excess Water, as required by the Arizona Water Settlements Act and the Revised Stipulation.
 - b. The ability of CAP M&I subcontractors under their CAP subcontracts to receive greater than 11% of their maximum entitlement in any month if such increased delivery is compatible with the overall delivery of Project Water to other subcontractors.
 - c. As specified by the Revised Stipulation, ADD Replacement contracts would not give rise to a right in any subsequent year to receive CAP Excess Water.
5. ADD water contractors would pay the regular ADD Water delivery rate for all water delivered under the CAP Excess Water (ADD Replacement) contract.

Types of ADD Water Supplies

1. Types of water supplies that may be acquired for the ADD Water Program include:
 - a. Colorado River water. In conformance with state and federal law, CAWCD may acquire rights to Colorado River water held under contract pursuant to §5 of the Boulder Canyon Project Act.
 - i. Most likely these will be priority 3 or higher water rights—i.e., senior to CAP’s Colorado River entitlement.
 - ii. CAWCD may consider priority 4 water rights—equal to CAP priority—on a case-by-case basis.
 - iii. This may entail obtaining rights to water that is currently unused by the existing contract holder, but such acquisitions must not harm CAP contractors and subcontractors.
 - b. Imported Groundwater. CAWCD, directly or in conjunction with other authorized entities, may acquire the groundwater that is available for transport into an initial AMA, and transport that water, subject to state law governing transportation of groundwater to an AMA.

Alternative offered by ARIZONA MINING ASSOCIATION: CAP would also acquire Other Water (non-permanent and non-CR River permanent supplies) outside of phases for industrial purposes. If groundwater basin water is included in Other Water, it may be necessary to seek minor modifications to the transportation statutes to allow for the use of these supplies for this purpose.

- i. A portion of the groundwater resource would be used to meet long-term ADD Water contract demands.
 - ii. The remainder of the groundwater resource could be used as a drought supply or to complement other water supplies.
 - c. Brackish groundwater. Desalination of brackish groundwater may be considered on a case-by-case basis for the ADD Water Program if the costs of developing (capital) and producing (OM&R) that supply are comparable to the costs of other ADD Water supplies, and if the use of brackish groundwater does not adversely affect the water supplies of other groundwater users or impede the ability to reach the management goal of an AMA (e.g., safe-yield).
2. Ocean Desalination Not Included. At present, the cost of ocean desalination—particularly annual OM&R cost—is far greater than the expected cost of the supplies identified above. Therefore, CAWCD will not develop ocean desalination as a water supply for the initial ADD Water Program.
- a. If there is still a demand for additional water supplies when no additional water supplies of the type identified above are available, CAWCD will work with stakeholders to develop ocean desalination.
 - b. Ocean desalination would have its own operating rules, financial structure, etc.

ADD Water Supply Portfolios

1. CAWCD will create and maintain two ADD Water supply portfolios:
 - a. Long-Term ADD Portfolio. This portfolio shall consist solely of permanent (100 years or longer) water rights and supplies. CAWCD will acquire water supplies for the Long-Term ADD Portfolio from multiple sources at various times, but will manage those water supplies as a single portfolio that increases in size over time.
 - b. Short-Term ADD Portfolio. This portfolio shall consist of water rights and supplies with a term of less than 100 years. CAWCD will acquire water supplies for the Short-Term ADD Portfolio from multiple sources at various times, but will manage those water supplies as a single portfolio. CAWCD will

Alternative offered by stakeholders
STAKEHOLDER COALITION: Isolate supplies purchased in a particular phase to that phase BY TYPE OF CONTRACT, including all risks and benefits OF THOSE SUPPLIES. This differs from the language here CAP STAFF PROPOSAL WHERE ~~in that~~ with each phase the supply portfolio grows and the risks and benefits are shared across phases.

acquire replacement supplies from time to time as needed to insure that the Short-Term ADD Portfolio is sufficient to satisfy all delivery obligations under Short-Term ADD Water contracts.

[COMMENT: THE STAKEHOLDER COALITION STRONGLY BELIEVES THAT CAWCD SHOULD NOT OFFER CONTRACTS FOR MORE ADD WATER SUPPLIES THAN CAWCD HAS ACTUALLY ACQUIRED. RELIANCE BY WATER USERS ON "REPLACEMENT WATER" THAT HAS NOT YET BEEN ACQUIRED COULD HAVE SIGNIFICANT ADVERSE CONSEQUENCES. CAWCD MUST RECONCILE THE DEMAND FOR SHORT-TERM SUPPLIES IN A PHASE WITH THE AMOUNT OF SHORT-TERM SUPPLIES IT IS ACTUALLY ABLE TO ACQUIRE IN THAT PHASE. THIS CAN BE DONE THROUGH THE TWO-STAGE CONTRACTING PROCESS RECOMMENDED BY THE STAKEHOLDER COALITION, AS FURTHER EXPLAINED IN ATTACHMENT A. IF A SHORT-TERM CONTRACTOR NEEDS MORE WATER THAN CAWCD IS ABLE TO ACQUIRE IN A PHASE, THE CONTRACTOR MAY CONTRACT FOR ADDITIONAL WATER IN A SUBSEQUENT PHASE. AS RECOMMENDED BY THE STAKEHOLDER COALITION AND FURTHER EXPLAINED IN ATTACHMENT A, A NEW PHASE COULD BEGIN AS SOON AS THE CONTRACTING PERIOD FOR THE CURRENT PHASE CLOSES. WE PROPOSE THAT THE NEW LANGUAGE REGARDING REPLACEMENT SUPPLIES BE DELETED.]

2. ADD Water contracts will provide for delivery of water from either the Long-Term ADD Portfolio or the Short-Term ADD Portfolio, but not from any specific source within either portfolio.

[COMMENT: AS NOTED ABOVE, THE STAKEHOLDER COALITION BELIEVES THAT IT IS IMPRACTICAL AND INFEASIBLE TO MANAGE ADD WATER SUPPLIES ACQUIRED FOR ONE PHASE AS PART OF A SINGLE PORTFOLIO OF WATER SUPPLIES COVERING ALL PHASES. WE PROPOSE THAT THE NEW LANGUAGE REGARDING LONG-TERM AND SHORT-TERM PORTFOLIOS BE DELETED.]

3. M&I providers may wish to use ADD Water contract entitlements to qualify for Assured Water Supply purposes under existing ADWR rules.
 - a. Each municipal provider or developer will remain responsible for demonstrating that it has an assured water supply.
 - b. CAWCD will provide all necessary information on ADD Water supplies to ADWR. The assured water supply

Alternative offered by ARIZONA MINING ASSOCIATION: Other Water supplies could be acquired outside of the phases for industrial purposes. These supplies would not need to be AWS qualified.

eligibility of water supplies under an ADD Water contract will be determined by ADWR.

- c. The ADD Water program is intended to be compatible with the current Assured Water Supply program and that program's underlying policy objectives.

CONTRACTS

Eligibility to Contract for ADD Water

1. Any municipal, industrial, agricultural or Indian water user within CAWCD's three-county service area is eligible to obtain a water service contract for ADD Water. Municipal and industrial water user includes the CAGR and landowners.
2. CAWCD, acting in its capacity as CAGR, will have the same privileges, obligations and rights as other ADD Water contractors.
3. AWBA is not eligible to enter into a long-term water contract for ADD Water, but may purchase ~~unused~~ ADD Water under a ~~spot-market~~ SHORT-TERM contract and may partner with an ADD Water contractor to use water available under an ADD Water contract.

[COMMENT: SINCE THERE IS NO LONGER ANY SPOT-MARKET WATER, THE STAKEHOLDER COALITION PROPOSES THAT AWBA BE ELIGIBLE TO ENTER INTO SHORT-TERM CONTRACTS.]

4. An entity whose primary business purpose is to purchase or store water for future resale ("remarketer") cannot obtain an ADD Water contract.
 - a. This provision does not prevent a group of eligible parties (e.g., landowners) from forming an entity to purchase an ADD Water contract for assignment to the individual parties ~~between phases~~.

[COMMENT: THE STAKEHOLDER COALITION RECOMMENDS THAT THE STRICKEN LANGUAGE BE DELETED BECAUSE IT MAY IMPLY THAT THERE WILL BE ADD WATER PURCHASES BETWEEN PHASES. BETWEEN PHASE CONTRACTS ARE NOT NECESSARY UNDER THE STAKEHOLDER COALITION PROPOSAL, AS FURTHER DESCRIBED IN ATTACHMENT A, BECAUSE A NEW PHASE MAY BEGIN AS SOON AS THE CONTRACTING PERIOD FOR THE PREVIOUS PHASE ENDS.]

- b. This provision is not intended to prevent eligible contractors from making private financing arrangements for purchasing ADD Water.

Classes of ADD Water Contracts

1. CAWCD will offer two classes of ADD Water contracts: Long-Term and Short-Term.
2. Long-Term contracts will be for permanent service and are intended to meet assured water supply requirements. Water to be delivered under Long-Term contracts will be from the Long-Term ADD Portfolio.

Alternative offered by ARIZONA MINING ASSOCIATION: *Long-term contracts referred to above would be AWS qualified contracts, and only AWS qualified water would support them. In addition, CAP would offer Other Water contracts, that could be short-term or permanent, but the water supply backing them would be Other Water.*

[COMMENT: AS NOTED ABOVE, THE STAKEHOLDER COALITION BELIEVES THAT IT IS IMPRACTICAL AND INFEASIBLE TO MANAGE WATER SUPPLIES ACQUIRED FOR ONE PHASE AS PART OF A SINGLE PORTFOLIO COVERING ALL PHASES. WE PROPOSE THAT THE NEW LANGUAGE REGARDING DELIVERY FROM PORTFOLIOS IN PARAGRAPHS 2 AND 3 BE DELETED.]

3. Short-Term contracts will be for a specific term of service less than 100 years, as defined in each such contract. Water to be delivered under Short-Term contracts will be from the Short-Term ADD Portfolio.

Assignments

1. "Assignment" means the permanent transfer of an ADD Water Contract entitlement to a third party.
2. An ADD Water contractor may assign all or part of its ADD Water contract entitlement to another eligible entity, subject to the following:
 - a. The assignment of an ADD Water contract that includes Colorado River water will be subject to any required review or approval by ADWR, the Secretary or CAWCD.
 - b. The assignment of an ADD Water contract that includes groundwater will be subject to state law on groundwater transportation, and to any required review or approval by CAWCD or ADWR.
3. CAWCD may impose operational requirements, as necessary and appropriate, to prevent harm to CAP contractors, ADD Water contractors or CAGR– e.g., if the assignment would move the point of delivery downstream on the CAP system and thereby impair CAWCD's ability to make other deliveries. To the extent possible under state and federal law, the following priorities (in order) shall apply for assuming ADD Water contracts held by those other than CAGR:

- a. An entity assuming or that has responsibility to deliver water within the assigning contractor's service area or development area.
 - b. CAGRDR, if it must replenish excess groundwater delivered within the assigning contractor's service area or development area.
 - c. Any other ADD water contractor.
 - d. Any non-ADD water contractor that wants to enter into a new ADD water contract.
4. To the extent possible under state and federal law, the following priorities (in order) shall apply for assuming ADD Water contracts held by CAGRDR:
- a. Water providers serving CAGRDR member lands and member service areas, if the assigned water will be substituted for excess ground water pumping and will reduce CAGRDR's replenishment obligations.
 - b. Any other ADD Water contractor.
 - c. Any non-ADD Water contractor that wants to enter into a new ADD Water contract.
5. CAWCD will prepare the necessary assignment documents to effectuate the assignment.

Alternative offered by ARIZONA MINING ASSOCIATION: Because of the unique nature of the "outside phase" acquisitions PROPOSED BY THE MINING COMPANIES, which will be tailored for industrial delivery and use, industrial contractors outside the phases should have greater flexibility on assignments to allow for cost recovery, subject to BOR and ADWR review.

Leases

1. "Lease" means an agreement for the temporary transfer of an ADD Water Contract entitlement to a third party.
2. An ADD Water contractor may lease all or part of its ADD Water contract entitlement, subject to the following:
 - a. The lease of an ADD Water contract entitlement that includes Colorado River water will be subject to any required review or approval by ADWR, the Secretary or CAWCD.
 - b. The lease of an ADD Water contract entitlement that includes groundwater will be subject to state law on groundwater transportation, and to any required review or approval by CAWCD or ADWR.

Alternative offered by ARIZONA MINING ASSOCIATION: Same as for an assignment, contractors should have greater flexibility in leasing their ADD Water contract, subject to BOR's and ADWR's normal approval process and CAP's operational limits.

- c. CAWCD may impose operational requirements, as necessary and appropriate, to prevent harm to CAP contractors, ADD Water contractors or CAGR– e.g., if the lease would move the point of delivery downstream on the CAP system and thereby impair CAWCD's ability to make other deliveries.

Alternative offered by ARIZONA MINING ASSOCIATION: *ADD Water should permit exchanges of ADD Water, so long as the exchange is allowed under current law. This concept would allow a participant to exchange a water supply with CAP for an ADD Water contract, or allow a participant to exchange an ADD Water contract for another water supply, or finance an ADD Water contract in exchange for another water supply, if the law on exchanges is satisfied.*

3. Contractual provisions relating to scheduling and payment for ADD Water deliveries and other provisions will be required to be included in the ADD Water Contract lease.

Conditions on Use of ADD Water Supply

1. The ADD Water supply can be used for any legal purposes under applicable state and federal law, including underground storage and recovery. The supply may be used within the service area and, subject to certain conditions, in areas located outside the service area.
2. In general, long-term storage credits generated through the storage of ADD Water may not be sold at a profit unless such profit is returned to the ADD Water Program. (Profit needs to be defined.)
3. With the following limited exceptions, ADD Water may be used only within the CAP service area.
 - a. If the ADD Water contractor is a municipal provider⁴:
 - i. 100% of the municipal provider's service area⁵ was located within the CAP service area as of January 1, 2009;
 - ii. The area the municipal provider proposes to serve with ADD Water that is outside the CAP service area is contiguous to the CAP service area and the municipal provider's service area located within the CAP service area and does not exceed 10% of the municipal provider's service area that is within the CAP service area; and
 - iii. The municipal provider will take delivery of the ADD Water within the CAP service area.
 - b. If the ADD Water contractor is not a municipal provider:

⁴ Municipal provider means a city, town or private water company.

⁵ The municipal provider's service area is the area of land actually being served water by the municipal provider and any additions to that area containing an operating distribution system owned by the municipal provider.

- i. And the ADD Water contractor is an electrical energy service provider that will use the ADD Water for electrical generation:
 1. As of January 1, 2009, one or more partners of the electrical energy service provider served Arizona customers within the CAP service area;
 2. The electrical energy that will be generated from the use of ADD water will be used in whole or in part within the CAP service area; and
 3. The ADD Water contractor will take delivery of the ADD water within Arizona from the CAP canal or other ADD Water infrastructure.
 - ii. And the ADD Water contractor is a mining company that will use the ADD water for mineral extraction and metallurgical processing:
 1. The ore body is located wholly or partially within the CAP service area;
 2. The use of ADD Water will be **in lieu of** groundwater that could otherwise be pumped by the mining company within the CAP service area; and
 3. The ADD Water contractor will take delivery of the ADD Water within the CAP service area.
 - c. Any other proposed use of ADD Water outside the CAP service area will be considered on a case-by-case basis and must be consistent with the following principles:
 - i. The proposed use of the ADD Water will significantly contribute to the economy of the CAP service area or the operation of the CAP Project; and
 - ii. The ADD Water contractor will take delivery of the ADD Water within the CAP service area.
 - d. ADD Water used outside of the CAP service area will be subject to the same financial requirements, rates and charges as ADD Water used inside the CAP service area plus an additional fee to the extent the CAP project works are used. Revenues from the additional fee will be used for CAP Project purposes as determined by the Board.
4. During an outage event, ADD Water contractors, to the degree operationally possible, will be treated the same as CAP customers. After consultation with ADD Water contractors, CAP could temporarily discontinue or reduce the quantity of water to be furnished to ADD Water contractors for the purposes of investigation, inspection, maintenance, repair, or replacement of any facilities

Alternative offered by ARIZONA MINING ASSOCIATION: *ADD Water should be allowed anywhere so long as the mining company has operations within the three-County area. Also, the limitation on reducing groundwater simply refers to the fact that mining companies can, as an alternative, seek a mineral extraction permit to secure groundwater so securing an ADD Water contract limits the need to seek additional pumping authority under a mineral extraction permit.*

(CAP or ADD Water related) or any part thereof necessary for the furnishing of water. So far as feasible, CAP should coordinate any such discontinuance or reduction with ADD Water contracts and give due notice in advance of such temporary discontinuance or reduction, except in case of emergency, in which case no notice need be given. Neither CAP, its officers, agents and employees, shall be liable for damages when, for any reason whatsoever, any such temporary discontinuance or reduction in delivery of water occurs. If any such discontinuance or temporary reduction results in deliveries to the ADD Water contractor of less water than what has been paid for in advance, the contractor shall be entitled to be reimbursed for the appropriate proportion of such advance payments prior to the date of the contractor's next payment of water service charges or the contractor may be given credit toward the next payment of water charges if the contractor should so desire.

Priorities During Shortage

1. All ADD Water contracts share the same priority and are subject to the following in the event of a shortage in ADD Water supplies:
 - a. ADD water contractors will be asked to submit schedules that incorporate voluntary reductions.
 - b. If all requests cannot be met, CAP will consult with ADD water contractors to determine the best way to fulfill all delivery requests to the greatest extent possible.
2. CAP may develop a firming program that could involve acquiring additional water supplies or storing unscheduled ADD water to either offset shortages or to firm ADD Water supplies.

[COMMENT: THE WORD "ADD" IS MISSING FROM THIS SECTION. THE STAKEHOLDER COALITION PROPOSES DELETING THE LANGUAGE DEALING WITH STORING UNSCHEDULED ADD WATER BECAUSE UNSCHEDULED ADD WATER THAT IS COLORADO RIVER WATER WILL BECOME EXCESS CAP WATER.]

Alternative offered by stakeholders STAKEHOLDER COALITION: *Priorities of water sources purchased in a phase would be isolated to that phase before any other priority system is imposed. AN ADD WATER CONTRACT WOULD RETAIN THE PRIORITY OF THE SOURCE OF WATER THAT IS THE BASIS OF THE CONTRACT. SHORTAGES AMONG CONTRACTS FOR THE SAME SOURCE OF WATER WITH THE SAME PRIORITY WOULD BE SHARED.*

Allocation Process

1. The Allocation Process is a process in which potential contractors attempt to reach agreement among themselves about how to allocate the volume of ADD Water available in a phase (e.g., 20,000 acre-feet in Phase 1).

Alternative offered by stakeholders STAKEHOLDER COALITION: *The allocation process would be managed through a bifurcated contract consisting of a planning stage and an implementation stage. The details of this proposal are included IN Attachment A.*

2. During the allocation process, the potential contractors shall consult with ADWR regarding its Policy and Procedures for Transferring an Entitlement of Colorado River water.
3. The Allocation Process is described below:
 - a. Potential contractors must submit a statement of interest including a requested volume to ADWR by an established deadline. Statements of interest received after this date will be held for subsequent phases.
 - b. ADWR will be responsible for pre-qualifying potential contractors. Those who pre-qualify will be allowed to participate in the Allocation Process.
 - c. Potential contractors, who have been pre-qualified, will participate in the allocation process and attempt to reach agreement on how to allocate the ADD Water supply available in that phase.
 - d. Before finalization of the allocation process for each phase, CAWCD will notify potential contractors of the cost per acre-foot for ADD water supplies, based on information gathered during its water supply acquisition activities.
 - e. ADWR will certify that an allocation agreement was reached among the potential contractors and will submit the results of that agreement to CAWCD.
 - f. If ADWR cannot certify that an allocation agreement was reached among potential contractors, then the "equal shares" method will be applied— i.e., the total volume of ADD Water available in the phase will be divided by the number of potential contractors that have requested water in that phase, with each participant being allocated an equal share. If the volume allocated by the equal share method is greater than the volume requested by any potential contractor, the excess volume shall be reallocated equally among the remaining potential contractors.

Alternative offered by ARIZONA MINING ASSOCIATION: *The sharing mechanisms described above would apply within phases. Outside the phases, CAP would secure Other Water and the volume and timing would be determined by the participants. If there is insufficient water available to meet industrial demands, then the participants will determine sharing arrangements. ADWR would not serve in an allocation role.*

Use of Unscheduled Supplies

1. Unused ADD Water that is Colorado River water will automatically become Excess CAP Water and will be disposed of by CAWCD in the same manner as other Excess CAP Water.

Alternative offered by ARIZONA MINING ASSOCIATION: *Consistent with provisions above on leases and assignments, this discussion of unused water does not impose restrictions on leasing or assignments beyond those discussed previously. If an industrial user anticipates not being able to utilize its full contract share, it may lease that volume.*

2. Groundwater supplies, including brackish groundwater, not used to meet scheduled ADD Water deliveries in any year will be left in place for future use.

FINANCES⁶

Pre-Launch Costs

1. CAWCD will have to incur some costs before the start of each phase of the ADD Water Program. Such pre-launch costs may include fees for consultants retained to identify and evaluate water supplies, costs to obtain water rights or options to acquire water rights and basic administrative costs. CAWCD would not expect to pay the full cost of acquiring water supplies using pre-launch funding, but may do so if appropriate opportunities are presented and if sufficient pre-launch funding is available.
 - a. CAWCD will establish an accounting fund to capture ADD Water costs on an ongoing basis beginning January 2012, which coincides with the start of CAWCD's next budget cycle.
 - b. After the ADD Water accounting fund is established, CAWCD may identify and capture pre-2012 expenses that should be charged to the ADD Water Program.
2. Phase 1 will be unique due to the fact that there have been no previous phases. Consequently, there may be certain pre-launch costs that will be incurred only in Phase 1. Other types of pre-launch costs may be incurred in multiple phases. Certain financing mechanisms may only be appropriate or available for a single phase, others may be appropriate or available for multiple phases, and still others may only be appropriate or available once the ADD Water Program is operational (i.e., after Phase 1).
3. The CAWCD Board may choose from the following options to fund pre-launch costs:
 - a. Use of existing, but currently unused, taxing authority. Funds collected from this source could be used to cover pre-launch costs solely for Phase 1 or to establish a revolving fund that would be available to pay pre-launch costs for Phase 1 as well as subsequent phases of ADD Water.

Alternative offered by stakeholders STAKEHOLDER COALITION: Do not use any sources of revenue for ADD except the following: payment by potential ADD Water contractors or CAWCD borrowing money from a commercial lender. To the extent CAWCD borrows money from a commercial lender, interest will only be charged to those relying on this mechanism and CAWCD may not use its reserve funds as collateral and such loans cannot adversely impact CAP rates, CAP subcontractors or CAGR members.

⁶ SEC categories covered in this section include: Capital Costs – Supply (Q17-18); Capital Costs – Infrastructure (Q19-21); and Operation Maintenance and Repair (OM&R) (Q22-24).

- i. CAWCD has the authority to levy an ad valorem tax of up to 10¢ per \$100 of assessed valuation. That tax may be used for any purpose for which CAWCD is organized. CAWCD is currently levying only 6¢ of that taxing authority.
 - ii. CAWCD could generate funding for ADD Water by temporarily increasing its general ad valorem tax for some period of time.⁷
 - iii. The currently unused taxing authority would only be available for ADD Water if and to the extent it was not needed for CAP purposes. If at any point during the collection period CAWCD determined that the temporary ad valorem tax revenues were needed for CAP purposes, then those revenues would immediately be available for CAP.
- b. Borrowing. CAWCD could borrow funds to cover pre-launch costs. Borrowing may entail added cost. Borrowing would not create a revolving fund, so each phase of the ADD Water Program would have to obtain its own separate financing. Any amounts borrowed to finance the pre-launch costs for a particular phase would be repaid by those obtaining ADD Water contracts in that phase.
- i. Loan from CAWCD reserves. CAWCD reserves could be used for this purpose only if and to the extent that actual reserves exceed CAWCD's reserve target. The ADD Water Program would repay the loan to CAWCD reserves, with interest.
 - ii. Funding from a third-party.
 1. Contributions by potential ADD Water contractors. Potential ADD Water contractors could contribute funds to CAWCD to cover pre-launch costs. If the contributor does not ultimately execute an ADD Water contract, they would be reimbursed the full amount of the contribution. If the contributor executes an ADD Water contract, the amount of the contribution would be applied against costs due at the time of contracting.
 2. Secured conventional loan from a commercial lender. Loan security could take the form of contracts for water options, backed up by CAGR assets if the ADD Water Program is not implemented.

⁷ At present valuations, a 1¢ increase in the ad valorem tax rate would generate around \$6 million.

3. Loan from private investor. Terms and requirements cannot be predicted at this point.
- c. ADD Water Self-Funding. After the launch of Phase 1, the ADD Water Program may have its own reserve accounts (e.g., Working Capital, Big R, etc.) that may be available temporarily for purposes of funding pre-launch costs (i.e., until the launch of the next phase, at which time they would be repaid by new ADD Water contractors). The cost of such self-funding would be the interest earnings that would be foregone.
- d. Other funding mechanisms. For example, unique business arrangements, such as with a power generator that might agree to contribute funds in exchange for a purchase power agreement with the ADD Water Program. .

Costs Due at Time of Contracting

1. Water supply acquisition costs WILL BE determined for each phase, including pre-launch costs not already paid by the contractor, AND are due at the time of contracting for ADD Water.

[COMMENT: THE STAKEHOLDER COALITION PROPOSES THE ABOVE CHANGES TO MAKE CLEAR THAT THE COSTS OF ADD WATER WILL BE DETERMINED SEPARATELY FOR EACH PHASE AS WAS AGREED UPON BY THE HIOG-2.]

2. A financing mechanism should be available to help those with limited ability to pay for an ADD Water contract, such as ACC-regulated and small MUNICIPAL utilities. CAWCD cannot provide that financing mechanism at this time.

[COMMENT: THIS CHANGE IS NECESSARY FOR CLARITY.]

3. Public-private partnerships may be used to finance the cost of obtaining an ADD Water contract.

Phase 1

1. The cost of acquiring water supplies and associated infrastructure for Phase 1 of the ADD Water Program will be substantial. CAWCD cannot demonstrate the creditworthiness or security that would be required to obtain sufficient financing without pledging existing CAP reserves, revenue streams and taxing authorities for the ADD Water Program. Therefore, it is not realistic at this time for CAWCD to finance the cost of water supply acquisition for Phase 1 on behalf of ADD Water contractors.

2. For Phase 1, ADD Water contractors will be required to provide 100% of the water acquisition charge at the time of contracting. ADD Water contractors will be responsible for arranging their own financing as needed.
3. If CAWCD is able to negotiate flexible payment terms with those selling water supplies to the ADD Water Program for Phase 1, CAWCD may be able to offer some payment flexibility to ADD Water contractors.

Subsequent Phases

1. For subsequent phases, CAWCD may be able to offer ADD Water contractors more financial flexibility. Such flexibility may come from any of the following sources (or others):
 - a. Financing mechanisms that may become available to CAWCD once the ADD Water Program has established an operating history.
 - b. Flexible payment terms CAWCD may be able to negotiate with those selling water supplies to the ADD Water Program.
 - c. A revolving fund established for that purpose. Initial funding to establish the revolving fund could come from a single infusion or a committed revenue stream.
2. In all cases, the amount CAWCD receives each year from ADD Water contractors must equal or exceed the amount that CAWCD must pay for water supply acquisition in that year.

Capital Costs for Improvements to CAP Canal Capacity

1. An infrastructure improvement capital charge will be computed based on the cost of increasing annual CAP canal capacity to 2.1 million acre-feet divided by 300,000 acre-feet (the target size of the ADD Water Program).
2. Currently the cost of canal improvements is estimated at around \$100 million, but that estimate will be updated before implementation of the ADD Water Program.
3. The capital charge will be levelized over the phases and paid over a specified period of time for each phase (e.g., \$333/acre-foot, paid over 10 years).

OM&R Costs

Fixed OM&R

1. ADD water contractors will pay two fixed, postage stamp OM&R rates:

- a. A fixed OM&R rate designed to cover OM&R costs tied to clearly separable and identifiable ADD water assets.
 - b. A share of the existing CAP fixed OM&R rate. Any fixed OM&R costs that are not based on clearly separable and identifiable ADD Water assets will be incorporated into the existing CAP fixed OM&R rate and paid by both existing CAP customers and ADD Water contractors.
2. ADD Water contractors will be required to pay fixed OM&R costs (both ADD-specific and CAP) for water scheduled for delivery whether taken or not. The contractor would be relieved of this obligation only to the extent that CAP, or the contractor, is able to find another customer for any unused water.
 3. The annual reconciliation for ADD Water contractors will involve no additional billing or refunds. CAP will develop and incorporate an acceptable annual rate stabilization mechanism. This will not change in any way the annual reconciliations performed under existing CAP contracts.

Variable OM&R (Energy)

1. Energy costs for existing CAP customers and ADD Water contractors will be kept completely separate. ADD Water contractors will pay a pumping energy rate designed to cover the energy costs for ADD Water.
2. Power supplies used to deliver ADD water will be pooled and ADD Water contractors would pay a single postage stamp rate for energy, but the rate could be "hedged" or protected against disproportionate increases in the cost of those power supplies in relation to overall operation and maintenance costs. How the rate would be "hedged" against disproportionate increases in energy costs will require additional work by stakeholders in the future.

ADD Water Replacement Costs

1. Costs associated with replacing infrastructure will be incorporated into a "Big R" component of fixed OM&R.
2. Costs associated with addressing contingencies for water supplies in the Long-Term ADD portfolio will be incorporated into a "Big W" delivery rate component for Long-Term ADD Water contracts.
3. Costs associated with replacing water supplies in the Short-Term ADD Portfolio will be incorporated into a "Big W" delivery rate component for Short-Term ADD Water contracts.

Other Rate Components

1. ADD Water delivery rates may also include, but are not limited to, the following components as appropriate:
 - a. Peak capacity surcharge. This charge would be designed to discourage extensive use of CAP delivery capacity during the peak delivery periods.
 - b. Conservation charge. If there is consensus for such a program, CAWCD could collect funds through a conservation charge and then make those funds available to ADD Water contractors to promote local efforts that reduce demand for ADD Water, thereby potentially reducing the volume of new/replacement supplies that must be acquired and lowering cost to all ADD Water contractors.

[COMMENT: ADD NEW BOX TO READ: "ALTERNATIVE OFFERED BY STAKEHOLDER COALITION: CONSERVATION PROGRAMS ARE THE PREROGATIVE OF ADWR AND THE INDIVIDUAL CONTRACTORS. THIS CONCEPT OF A CONSERVATION CHARGE IS BEYOND THE SCOPE OF THE ADD WATER PROGRAM.]

Reserves

1. CAWCD may establish and maintain reasonable ADD Water reserve funds by including additional rate components, as necessary, for working capital needs, environmental, and other costs.

CAGRD AND THE ADD WATER PROGRAM

1. CAGRD may enter into Long-Term and/or Short-Term ADD Water contracts.
2. CAGRD may also acquire non-ADD Water supplies outside of the ADD Water Program. Such supplies may include, but are not limited to:
 - a. Effluent or other water supplies that will not be transported through the CAP.
 - b. Project water supplies—e.g., leases of CAP Indian priority water.
 - c. Non-Project water supplies that do not otherwise meet the requirements for inclusion in either the Long-Term ADD Portfolio or the Short-Term ADD Portfolio. These supplies may rely on the CAGRD interim set-aside.

[COMMENT: THE HIOG-2 SPENT MANY MEETINGS DISCUSSING ISSUES RELATED TO CAGRD AND THE USE OF ADD WATER, BUT WAS NOT ABLE TO RESOLVE THESE ISSUES. IT IS IMPORTANT THAT THIS DOCUMENT REFLECT

THIS FACT. THE STAKEHOLDER COALITION PROPOSES THAT THE FOLLOWING LANGUAGE BE ADDED HERE:

"MANY ISSUES RELATED TO CAGRD AND THE USE OF ADD WATER REMAIN TO BE RESOLVED, INCLUDING:

- WHETHER WATER SUPPLIES MUST BE PURCHASED IN ADVANCE OF NEW ENROLLMENT IN CAGRD.
- WHETHER WATER SUPPLIES WILL BECOME A CAP ON NEW ENROLLMENT.
- WHETHER THE VOLUME OF ADD WATER IN A PHASE FOR CAGRD WILL BE LIMITED TO A PERCENTAGE OF THAT PHASE.
- WHETHER CAWCD MUST USE A PORTION OF ADD WATER ACQUIRED FOR CAGRD TO SATISFY PRE-ADD ENROLLMENT REPLENISHMENT OBLIGATIONS."]

CAP STAFF JUST WATER PROGRAM PROPOSAL

WATER SUPPLY

1. In conjunction with each phase of ADD Water, CAWCD will also acquire water supplies for the Just Water Program.
2. A target volume for Just Water acquisitions will be established for each phase, up to a cumulative total of 50,000 AF.
3. Just Water supplies will be available for delivery from the Colorado River.

WATER RIGHTS

1. CAWCD will assign the water rights it acquires for the Just Water Program to the appropriate regional or statewide entity upon payment to CAWCD of its costs in acquiring those water rights.
2. The appropriate regional or statewide entity will hold Just Water rights in trust until contracted to individual entities outside CAWCD's three-county service area.

FINANCES

If the appropriate regional or statewide entity does not pay or provide for payment to CAWCD for Just Water supplies within a reasonable time period following CAWCD's acquisition of those supplies, then CAWCD may, in its sole discretion:

1. Allow options for water rights to expire.
2. Exercise options for water rights and make that water a part of the next ADD Water phase, selling the water under ADD Water spot market contracts in the meantime.
3. Sell the water rights to CAGR D.
4. Other disposition.

WATER ALLOCATION

1. ADWR (or other appropriate regional or statewide entity) will determine how to distribute/allocate available Just Water supplies, subject to any required approval by the Secretary of the Interior.

ATTACHMENT A

Alternative Offered by Stakeholders STAKEHOLDER COALITION⁸

(referenced on page 40 1 of proposal)

1. CAWCD, in consultation with potential ADD Water Contractors and other interested stakeholders (e.g., ADWR, Bureau of Reclamation, etc.), would develop a standard form ADD Water contract for approval by the CAWCD Board of Directors. There may need to be some different terms for different types of ADD Water contracts (e.g., long-term, special). The standard form ADD Water contract would be a bifurcated contract consisting of two contractual stages as follows:
 - A "planning stage" during which any required review and approval by ADWR and the Secretary would be initiated and ADD Water would be allocated within that phase.
 - An "implementation stage" during which supply acquisition, final approvals, infrastructure construction, and actual water delivery would occur.
2. At the appropriate time, CAWCD would open a phase of the ADD Water Program and interested parties could execute the standard form ADD Water contract with CAWCD.
 - Any party wishing to participate in the phase must execute the standard form ADD Water contract before the closing date of the phase. The closing date would be six months after the date CAWCD opens the phase.
 - CAWCD may accept contracts for the phase after the closing date only as a "back up" in the event contractors in the phase opt out or reduce their requests for ADD Water in that phase (see below), or more water is actually acquired than needed by those contractors.
3. ADD Water contractors will determine their own needs and what they are willing and able to pay.
 - The total volume of ADD Water acquired for the initial phase will be based on the volume of water requested by those who sign contracts prior to the closing date of that phase, but will not exceed 26,700 acre-feet. CAWCD will not be required to acquire the full 26,700 acre-feet for that phase if the demand in that phase is

⁸ THE MEMBERS OF THE STAKEHOLDER COALITION ARE REPRESENTATIVES OF RESOLUTION COPPER, SALT RIVER PROJECT, CENTRAL ARIZONA IRRIGATION AND DRAINAGE DISTRICT, HOHOKAM IRRIGATION AND DRAINAGE DISTRICT, POTENTIAL WATER SUPPLIERS, THE CITY OF TUCSON, THE SOUTHERN ARIZONA WATER USERS ASSOCIATION, AND AMWUA AND ITS MEMBER MUNICIPALITIES.

less or sufficient supplies are not available at a cost or of a type that meets the needs of the contractors in that phase.

- Based on the demand of the initial phase and other relevant factors, CAWCD could adjust the size of a subsequent phase.
 - If the requested demand by ADD Water contractors who sign contracts prior to the closing date exceeds 26,700 acre-feet for the initial phase, or the size of the phase for a subsequent phase, or a lesser amount that is actually acquired, the supplies would be shared (among types of contracts) by agreement among the contractors. If the contractors cannot agree on how to share the supplies, the supplies would be shared equally by the contractors up to the amount requested in the contract or the reduced amount requested by a contractor (see paragraph 5 below).⁹
4. All contractors in a phase would share the costs of the planning stage (i.e., planning, negotiating, pre-acquisition and options) in proportion to the amount of water finally allocated to each contractor.
 - The planning stage costs would initially be allocated to each contractor based on the amount of water requested.
 - As more contracts are signed prior to the closing date, the proportionate shares of the costs would be modified.
 - The final shares of the planning stage costs would be reconciled at the end of the planning stage based on the amount of water actually allocated to each contractor so that each contractor pays the same cost per acre-foot.
 - Payments of planning stage costs would be made during the planning stage according to a schedule developed by CAWCD.
 5. Prior to the payment during the planning stage of options for ADD Water supplies in a phase, an ADD Water contractor could opt out of the contract for that phase and would incur no further financial responsibility in that phase. A contractor could also reduce its request for ADD Water in that phase.
 6. During the implementation stage, if more water supplies are acquired than are needed by existing contractors and parties who signed back-up contracts, other parties may opt in by signing an ADD Water contract and paying their proportionate share of the planning costs. All other contractors, including those who opted out prior to the payment of options for ADD Water, will be reimbursed proportionately to the extent revenues exceed planning stage costs.

⁹ While this appears to be the preferred method of most HIOG-2 members for sharing supplies, some HIOG-2 members believe that supplies should be shared pro-rata based on the amount requested in the contract. Concerns were expressed that the preferred method might work to the disadvantage of CAGR and other contractors who need a larger supply at one time.

7. After the closing date of a phase, CAWCD would open a new phase as soon as practicable, but not before all supplies are earmarked for the previous phase.
8. CAWCD would be responsible for water supply acquisition and all regulatory clearances (e.g., NEPA review and ADWR transfer policy) associated with the acquisition of water supplies. Contractors would not dictate to CAWCD any process for or terms of water supply acquisition. However, CAWCD must make known the specific supplies to be acquired and the costs and terms of acquiring such supplies prior to entering into binding obligations so that contractors may decide whether to opt-out of the phase.
9. An important function of the planning stage would be to match contractors' needs to supplies that may be available.