ARIZONA Auditor General
Making a Positive Difference

REPORT HIGHLIGHTS
Special Audit
December 2017

Central Arizona Water Conservation District

CONCLUSION: The Office of the Auditor General has completed a special audit of the Central Arizona Water Conservation District (District) pursuant to Laws 2017, Ch. 305, §129. We found that the District collects and spends revenues in accordance with legal requirements and/or policies the District's Board of Directors (Board) established. The District has also established and maintains various financial reserves to meet contractual obligations and prepare for large or unusual costs that may arise. Further, the District operates the Central Arizona Groundwater Replenishment District (CAGRD), which the Legislature established to conserve groundwater supplies and facilitate land development.

District delivers Colorado River water to central and southern Arizona

The District is a multicounty water conservation district formed under state law that delivers Colorado River water to entities in Maricopa, Pima, and Pinal Counties (the District's service area). This water is delivered via a 336-mile aqueduct system called the Central Arizona Project (CAP). The District's formation was authorized in 1971 to contract with the U.S. Secretary of the Interior to repay the federal government for a portion of the CAP construction costs. The District also operates the CAGRD, which is responsible for replenishing groundwater pumped by its members.

District collects and spends revenues in accordance with requirements and/or policies

Revenues collected in accordance with legal requirements and/or board policies—The District is authorized to collect revenues from water delivery charges, two property taxes, and surplus energy sales and surcharges and does so in accordance with laws, contracts, regulations, and/or board policies. Specifically, the District charges some or all customers annual water delivery rates in accordance with their contracts, including rates based on its cost to operate, maintain, and replace the CAP (OM&R), the pumping energy costs to deliver water, and a capital charge for the annual repayment of CAP construction costs. In addition, the District is legally authorized to annually levy and collect two property taxes on the assessed valuation of homes within its three-county service area. The two taxes are a general ad valorem tax and a water storage tax. Finally, through contractual agreements, the District receives revenues from (1) the sale of surplus energy produced by the Navajo Generating Station (NGS) that is not needed for the District's water pumping needs, and (2) surcharges collected on energy sold in Arizona from the Hoover Power Plant and the Parker-Davis Project.

Revenues spent in accordance with legal requirements and/or board policies—The District's expenses include its obligation to repay CAP construction costs, general OM&R costs, and energy costs:

- **CAP construction costs—**The District's repayment obligation for CAP construction costs is approximately $1.6 billion, plus interest. The District is responsible for making annual installment payments to the U.S. Bureau of Reclamation (Reclamation) until 2046. On average, the District's annual repayment obligation is approximately $55 million per year for 2017 through 2032 but drops to approximately $45 million annually for 2033 through 2043. The remaining three payments drop to $10.6 million until paid in 2046.

- **Annual OM&R costs—**The District incurs annual OM&R costs, such as salaries and benefits, maintenance, capital projects, and lobbying. The District offers its employees a generous compensation package, including above-average base pay and a 401(k) plan with partial match. The District is also a member of the Arizona State Retirement System and covers the full pension costs for its employees. From 2014 through 2016, the District spent $57.2 million to $60.4 million per year in salary and benefit costs for its employees. During this same period, maintenance costs averaged $27.6 million annually, and capital expenditures averaged $36.7 million annually.

- **Pumping power—**In 2014 to 2016, the District spent an average of $93.3 million per year on power to pump water through the CAP. Most of these costs were for power purchased from the NGS, which supplies the majority of the District's power. However, the NGS is scheduled to close at the end of 2019, and the District reported that it is exploring its future energy options.

District collects various groundwater replenishment revenues to administer the CAGRD—As it is legally authorized to do, the District levies and collects one-time enrollment and activation fees, annual membership dues, and annual replenishment tax assessments from CAGRD members to finance the CAGRD's groundwater replenishment activities.

District has established and maintains various reserves

The District, through its Board, has established and maintains various financial reserves to meet contractual obligations and prepare for large costs that may arise. Statute gives the Board the authority to establish and maintain reserves. Some reserves are required by contracts with Reclamation. For example, the 1988 Master Repayment Agreement with Reclamation requires the District to maintain a $40 million repayment reserve to help ensure payments are made to Reclamation for the District's share of CAP construction costs. The Board authorized other reserves to accomplish the District's purposes or pursuant to state law. Altogether, the District's reserves totaled nearly $490.6 million as of December 31, 2016.

The District's reserves have been established to meet operating needs, capital projects, CAGRD operations, or other purposes. For example, the District anticipates using reserves to pay its share of the NGS decommissioning costs, which it estimates will be between $109.3 million and $161.4 million. According to a contract between the Western Area Power Administration, Reclamation, and the District, the District is entitled to 24.3 percent of the power generated by the NGS but is also responsible for a corresponding portion of the costs to decommission the NGS.

CAGRD acquires water supplies to replenish groundwater

CAGRD is a district department charged with replenishing groundwater—The Legislature established the CAGRD within the District to help ensure land development did not overdraw groundwater supplies. The CAGRD provides a mechanism for developers to meet the Arizona Department of Water Resources' (ADWR) Assured Water Supply Rules, which require developers to demonstrate the land they wish to develop has a 100-year water supply. Developers who are unable to meet this requirement would not be approved to develop land unless they join the CAGRD. The CAGRD must replenish any groundwater its members use beyond a certain limit, and it charges its members fees, dues, and assessments to pay for its groundwater replenishment costs.

ADWR provides some CAGRD oversight—The CAGRD is statutorily required to provide reports and other information for ADWR review so it can determine if the CAGRD is meeting its groundwater replenishment obligations. Specifically, the CAGRD must submit a plan of operation every 10 years that describes how it will meet its future groundwater replenishment obligations. The plan identifies potential water sources the CAGRD could acquire. The CAGRD also submits annual reports to the ADWR that detail the CAGRD's replenishment obligations and actual replenishment activities for the previous year.

CAGRD has relied on excess CAP water but will need additional water supplies—Historically, there has been enough excess CAP water to meet the demand of any entity wishing to purchase it, including the CAGRD to meet its groundwater replenishment obligations. However, entities that are entitled to CAP water began to order more of their entitlement, which has gradually reduced the amount of excess CAP water available to entities such as the CAGRD. Therefore, the Board has limited excess CAP water allocations available to nonagricultural users to only the CAGRD, the Arizona Water Banking Authority (which stores unused Colorado River water for use in times of shortage), and Reclamation. Even with this measure, the CAGRD acknowledged that excess CAP water alone will not be not sufficient to meet its future obligations. Thus, the CAGRD has acquired, is working to acquire, or is considering acquiring additional water sources, such as leasing water, purchasing long-term storage credits (i.e., the right to use stored water in the future), or obtaining a CAP water allocation. In the future, alternative water sources for the CAGRD could be costly and difficult to obtain.