Draft Findings and Potential Policy Tools – for Meeting 6

Advisory Group on Water Trust, Banking, and Transfers

DRAFT; July 13 2020

Notes

This paper is a draft document. Concepts included have not been approved by Ecology leadership. They are reflective of the current thinking of Ecology Water Resources staff after completion of the Advisory Group on Water Trust, Banking, and Transfers; they should not be interpreted as a commitment to pursue (or not pursue) specific policy actions.

In this document, we present draft findings and potential policy tools for each of the four topics discussed. The draft findings reflect our central takeaways from the Advisory Group meetings. There are then three categories of potential policy tools presented.

- *Potential Ecology Recommendations and Actions* – These are policy concepts that Ecology is considering for recommendation to the Legislature. This category also includes actions that Ecology can implement within our existing authority and which we currently plan to act upon.
- *For Future Legislative Evaluation* – These are policy concepts that Ecology is not recommending, but we believe merit further evaluation by the Legislature. Policy concepts in this category are worthy of continued discussion despite not currently being ripe for implementation or because the concept implicates actions for other state agencies or local governments, and thus would need broader legislative discussions.
- *Considered but not Recommended* – These are policies that Ecology considered and discussed with the Advisory Group and does not recommend for legislative consideration.

Topic 1: Out-of-basin transfers

Findings

F.1.1 Downstream out-of-basin transfers can be a valuable tool for providing water for new uses while also boosting instream flows (in those cases where the water in the intervening reach is not subject to withdrawal for other out-of-stream uses). Often, these transfers provide much needed flexibility for water management**.**

F.1.2 The needs of each basin are unique – it will be difficult (and likely unwise) to seek one solution that fits all basins. For example, some basins could see greater ecological or economic impacts of water moving downstream than other basins. Management considerations are also often basin-specific, such as whether instream flows are met in the basin-of-origin or whether the basin-of-origin is closed to new appropriation.

F.1.3 If water rights transferred downstream cannot be transferred back upstream, out-of-basin transfers may foreclose the potential for new out-of-stream uses in the basin of origin, which limits the capacity for future economic growth. Some participants expressed that

limiting downstream, out-of-basin transfers could prevent these economic losses. Others argued, however, that most downstream, out-of-basin transfers are driven by greater macro-economic factors, such as commercial agricultural enterprises outcompeting traditional family farms, and that limitations on the downstream sale of water rights are an inappropriate response. They voiced concern that limitations on agricultural water marketing would place an undue burden on farmers seeking to capitalize on a major asset.

F.1.4 Economic realities may make it difficult for communities in headwater basins to compete in an open marketplace for available water rights. In these basins, meeting long-term goals to keep water rights from being transferred downstream out-of-basin may require outside or state-level investment in local water banking programs or partnerships to level the playing field.

Policy Tools – Potential Ecology Recommendations and Actions

P.1.1 Create an administrative tool or implement a process or procedure such that a water right transferred downstream may be moved back upstream without a finding of impairment to intervening users. Ecology would still not approve a transfer that would cause impairment to an existing water right beyond what would have occurred in absence of the original downstream transfer. **Note, we are consulting with our attorneys on whether this could be implemented through existing authority or whether additional statutory authority would be necessary, and on whether it would face legal barriers.**

Objective: Create greater flexibility such that downstream, out-of-basin transfers are no longer "permanent" and may be transferred back upstream	
Pro's	**Con's**
Increased flexibility to move water rights back upstream after they have been transferred downstream	Could be costly, time consuming, and complicated to implement
Potential impacts on the local economy due to downstream transfers could become reversible	Moving a right back upstream after an extended period of time may result in ecological impacts, especially given the impacts of climate change
	This may not help resolve the issue if water is more valuable downstream, and thus the headwater basins still are negatively affected by downstream out-of-basin transfers
	Water rights in the affected reach issued after the downstream transfer may be subject to interruption if the subsequent upstream transfer would otherwise impair senior rights, including instream flows

P.1.2 Authorize "conservation easements" on water rights to limit their use to the basin-of-origin. An entity could purchase the easement, which would have the effect of limiting transfer of the water right so it could not be transferred out of the basin-of-origin for future

consumptive uses. **Note, we are consulting with our attorneys on whether this could be implemented through existing authority or whether additional statutory authority would be necessary, and on whether it would face legal barriers.**

Objective: Provide a non-regulatory tool to keep water rights in the basin-of-origin	
Pro's	**Con's**
Provides a mechanism to keep water rights in the basin of origin	

Policy Tools – For Future Legislative Evaluation

P.1.3 Establish that before a water right may be sold for transfer out of the basin of origin, state, local, and tribal governments, and non-profits would be provided a "right of first refusal." Parties would have a set duration of time to make an offer.

Objective: Increase the opportunity for water rights to stay in the basin of origin	
Pro's	**Con's**
Provides a mechanism to keep water rights in the basin of origin	Such a tool could be an unconstitutional taking of property rights
Increases local control	Disclosure of the sale before the sale is final could complicate or derail the transaction
Could maintain economic benefits in the local community	Lengthens the processing time for out-of-basin transfers
Does not prevent the marketing and sales of water rights	Requires a new source of funding to implement. Without funding this could create process with no result

P.1.4 Require that before the place of use of a water right may be transferred downstream out-of-basin, Ecology must determine that the change will not be detrimental to the public interest.

Objective: Prevent downstream out-of-basin transfers that would be detrimental to the public interest	
Pro's	**Con's**
Can be an effective way to evaluate the impacts of a downstream out-of-basin transfer and provide a mechanism to prevent it	Public interest is largely undefined and subjective
A requirement for a public interest review is not a novel idea in Washington water law (see, RCW 90.42.040; 90.44.100; 90.03.290; and 90.44.540)	It is unclear at what geographic scale would be appropriate to measure the impacts – at a county level, regional, or statewide?
A public interest test already exists for new water rights and for changes to most groundwater rights	Using a public interest test could start to value some beneficial uses over others, which many participants thought was unwise

	The core issue may be the loss of economic opportunities for farming in upstream communities – and preventing a water right from moving downstream will not incentivize people to keep farming; thus, the policy tool is misplaced

P.1.5 Create a revolving loan fund or grant program to fund purchases water rights for use in the basin of origin.

Objective: Assist tribes, local governments, and nonprofits in acquiring water rights to keep in the basin of origin	
Pro's	**Con's**
Creates a funding source to help tribes, local governments, and nonprofits to participate in the water market	The unavailability of water rights for sale may be more of a limiting factor than funding
	Could be administratively costly to establish and operate

Policy Tools – Considered but not Recommended

P.1.6 Authorize Ecology to "close" a basin (or subbasin) to out-of-basin transfers through rulemaking.

Reasoning: Incentive and market-based solutions provide a more effective mechanism to keep water in a basin. Ecology also has concerns with closing a basin through rulemaking, even if specific statutory authority were provided to do so. We would need clear criteria for what would justify this rulemaking, which could be difficult to articulate and/or measure. In addition, even with authority to adopt rules with this standard, rulemaking requires that the benefits outweigh the costs and it's unclear whether that would be the case. Lastly, rulemaking is costly and time consuming for the agency. With other rulemaking priorities, it is unclear when Ecology will have resources to undertake this rulemaking in the near term.

P.1.7 Restrict the number of water rights that may be transferred for use out-of-basin from any one WRIA.

Reasoning: It is unclear how Ecology would determine the appropriate number of water rights (or the quantity of water) that can be transferred.

Topic 2: Transparency in water right sales

Findings

F.2.1 There was general sentiment among participants that the public notice requirements of sales and transfers are not the problem. Instead, Ecology should be concerned that online postings of transfer applications are not sufficiently accessible to the general public.

F.2.2 Increased knowledge of sales and prices could help to develop a more robust marketplace for trading water rights.

F.2.3 The statutory requirement to post notice of water right transfers in the newspaper is outdated. However, local newspapers may still provide a useful medium for public notice in some rural areas with limited internet access.

F.2.4 There was common agreement that limiting who can buy a water right (such as prohibiting out-of-state entities) is unwise. Differentiating between in-state and out-of-state buyers of water rights is likely to be problematic (and potentially unconstitutional). See P.2.4 for details.

Policy Tools – Potential Ecology Recommendations and Actions

P.2.1 Modernize the requirement that notice of water right transfers is published in local newspapers. Amend RCW 90.03.380 to allow Ecology to publish notice electronically.

Objective: Improve transparency	
Pro's	**Con's**
Newspaper posting is archaic, costly and reaches a limited audience	Particularly in rural areas, newspapers still provide the only notice to many people and the advertising supports local papers
Cost savings for the agency	
Modern means of communication will reach a broader audience	

P.2.2 Make water right transfer application information more accessible to the public through administrative improvements. Post water right change applications in an integrated, publicly-accessible GIS interface. Note, Ecology can implement this within existing authority. We have begun work on this project and anticipate completion by 2022.

Objective: Improve transparency	
Pro's	**Con's**
Improves access to information about water right transfers	Requires some administrative resources to implement

Policy Tools – For Future Legislative Evaluation

P.2.3 Align disclosure laws for water rights sold separately from land with the laws for land sales. Require that water right sales (including prices) are reported to the state and made publically available.[1]

[1] This could potentially tie to the Real Estate Excise Tax, which is collected on water right sales. Though collected, our current understanding is that this information is not currently tracked or published in publically-available, searchable database.

Objective: Improve transparency	
Pro's	**Con's**
Improves market transparency	Administratively costly for both the state and local governments
Could make more water rights available with knowledge of prices	Might increase the price of water, including the cost of water right acquisitions
In the event that trading of water rights in transactions distinct from the appurtenant land becomes common, such recording would simplify tracking ownership of water rights and create greater certainty of ownership	Unclear that the need for this information outweighs the cost of the undertaking

Policy Tools – Considered but not Recommended

P.2.4 Limit who can buy a Washington water right.

Reasoning: This policy option would have significant negative implications because out-of-state entities, like the Bureau of Reclamation, play an important role in water management in Washington. Implementation could hinder water management in interstate basins.

In addition, such a regulation limiting out-of-state entities would have easy workarounds and loopholes. Any entity can buy land in Washington, and it would be incongruent to restrict who can buy water.

P.2.5 Provide advance public notice of sales including price disclosure.

Reasoning: This could set the expectation that Ecology or local governments could prevent a sale from happening, which they would not have authority to do. This also has high potential to disrupt sales. In addition, participants noted that we do not require advance public notice of land sales and that water rights should not be treated any differently.

P.2.6 Require that any water right sale be reported to county commissioners.

Reasoning: It is unclear what benefit would come from reporting all sales. It could also set the expectation that local governments could prevent a sale from happening, which they would not have authority to do.

Topic 3: Private investment & marketing of water rights – Use of the Trust Water Rights Program (TWRP)

Findings

F.3.1 There is lack of consensus and common understanding of basic terminology of the trust program, including terms such as *temporary donation* and *transfer into trust*. The most important distinction between "types" of trust water rights is the intended end use of that

water right – or more precisely, the role that Ecology will play in managing the right. This is not clear in statute.

F.3.2 Lack of clarity in chapter 90.42 RCW promotes confusion and disagreement on terms, standards, and processes, which could result in use of the Trust Statutes in ways not intended by the legislature or impairment to existing water rights.

F.3.3 The flexibility of the TWRP is one of its greatest assets. Limiting its flexibility by clarifying certain definitions and processes could hamper creative water solutions. Several participants expressed opinions that the value of flexibility outweighs any potential concerns over "abuse" of the TWRP.

F.3.4 There is broad agreement that a water right being used for mitigation should first undergo a tentative determination of extent and validity. There was general sentiment (but not consensus) that Ecology already has the statutory authority to require this condition.

F.3.5 There was no consensus whether or not the TWRP enables speculation in water rights and, if so, whether this activity constitutes a significant problem. Moreover, there was no common definition for "speculation" accepted by the group. To some, the non-consumptive beneficial use of the right for instream flow is comparable to any other beneficial use, shielding it from classification as speculation. To others, this non-consumptive use is simply legal cover for "speculative" behavior.

F.3.6 Many participants were not concerned over use of the TWRP in ways that yield private profit. They contend that private use rights are inherently intended to drive public benefits through efficient use of the resource through private incentives, and that the intentions of the owner should not matter as long as rights are being beneficially used in accordance with the Water Code. Therefore, water right owners are allowed to profit from instream uses just as from out-of-stream uses. Moreover, the ongoing streamflow benefits of trust water rights provide the opportunity for a "win-win" scenario to both public and private interests.

F.3.7 Some participants, however, voiced concern over the scenario whereby a person buys a water right with no plan to put it to beneficial use themselves (other than instream flows), but rather with the express intent of simply reselling the water right at a later time for a higher price. They view this activity as speculative and therefore abusive.

Policy Tools – Potential Ecology Recommendations and Actions

Note that statewide, the Trust Water Rights Program is governed by chapter 90.42 RCW. Trust water is also governed by chapter 90.38 RCW, which is strictly applied to the Yakima Basin. Ecology is not currently considering any changes to chapter 90.38 RCW.

P.3.1. Differentiate between water rights that are placed in trust for the purpose of instream flow enhancement and protection from relinquishment versus water rights that are placed in trust to be used as mitigation. Clarify terminology such that there is a common definition for widely used terms. Note, Ecology is currently evaluating whether to pursue these changes in

statute, rule, or policy. If such clarification were pursued through statutory amendment, we anticipate it would require substantial changes to chapter 90.42 RCW, if not a near-complete rewrite.

Objective: Create two categories of trust water rights to clearly differentiate their end use	
Pro's	**Con's**
Clarifies both Ecology's administrative role and the water right holder's long-term intentions for use, reducing potential speculation	Lack of consensus on terminology and proper distinctions indicates this could be a difficult and potentially lengthy process
Provides clarity on administrative processes	Clarity could reduce flexibility for water right holders when their future plans are uncertain
Ensures that use of trust water rights will not impair existing rights	

P.3.2. Amend chapter 90.42 RCW to clarify that any water right being used for long-term[2] or permanent mitigation must first undergo a tentative determination of extent and validity. Because temporary donations to the TWRP generally do not undergo a tentative determination of extent and validity, this policy would clarify that temporary donations may not be used to mitigate for long-term or permanent uses.[3] Note, we believe this could be accomplished through a surgical, brief amendment to chapter 90.42 RCW (as opposed to P.3.1, which would necessitate a more comprehensive amendment).

Objective: Ensure that new mitigated uses will not impair existing water users or instream flows	
Pro's	**Con's**
Added clarity from the Legislature will increase certainty and reduce legal risk	Unclear whether this is necessary – existing statutory authority may be sufficient
Ensures that use of trust water rights will not impair existing rights	Limits flexibility – although the use of donations for mitigation is often inadvisable, it may be appropriate in some unique circumstances
This distinction would help to keep track of which rights can be used for mitigation	
Helps to prevent the scenario whereby a permanent use is mitigated by a temporary trust right	

P.3.3. Update the Trust Water Guidance document as to clarify administrative processes for trust water and water banking. Note, Ecology can pursue this under existing authorities. We have begun this work and anticipate completion by Summer 2021.

[2] Long term could be defined as more than 5 years in the same way chapter 90.42 RCW establishes different processes and standards for leases shorter than five years versus longer than 5 years.
[3] Note, there could be provision to grandfather any donations that are actively being used as mitigation.

Objective: Clarify administrative practices	
Pro's	**Con's**
Increased clarity and consistency	

Policy Tools – For Future Legislative Evaluation

None.

Policy Tools – Considered but not Recommended

P.3.4. Limit use of the TWRP such that that individuals who buy a water right must plan to put the water to beneficial use themselves.

Reasoning: Placing a right into the TWRP inherently constitutes putting the water to beneficial use, and it is within a water right owner's prerogative to dedicate a right to non-consumptive beneficial use while determining future out-of-stream use. Therefore this restriction would have no effect. However, if this restriction is applied so that the purchaser must plan for out-of-stream use, it would functionally give priority to out-of-stream uses over instream uses.

P.3.5. Limit the number of trust water rights that can be removed from trust in any given year.

Reasoning: We have not seen that water being withdrawn from trust has caused streamflow problems. Also, it would be difficult to determine the appropriate number of water rights that could be removed. If the limit were based on geographic distribution, it would be difficult to track administratively.

P.3.6. Restrict how long a temporarily donated water right may remain in trust.

Reasoning: Data shows that most rights are in the TWRP for 5 years or shorter, so any limit above that timeframe would have limited utility. In addition, there can be significant streamflow benefits to water rights being left in the TWRP. We see little utility in mandating removal from trust after a specified duration. Also, it is unclear what limitations Ecology would then be able to place on that right to either remove it from trust or prevent its re-donation for another 10-year period.

Topic 4: Private investment & marketing of water rights – Water banking

Findings

F.4.1 Water banks play a critical role in reallocating water between beneficial uses, including instream flows. Both public and private water banks play an important role.

F.4.2 There was general agreement among participants that it can be concerning when a bank that provides water to meet basic health needs gains disproportionate market power or becomes a monopoly. However, participants debated whether the appropriate remedy is through carrots (incentivizing competition) or through sticks (increased regulation).

- Some participants expressed that there should be greater government regulation of water banks providing water for public health and safety (like in-home use). Though there was no clear recommendation on what that that regulation should entail, some participants recommend learning lessons from oversight of public utilities.

- Other participants argued that while monopolistic behavior can be worrisome, increased regulation is not warranted. They expressed that the solution to monopolies would be to reduce barriers to entry as to increase bank competition. They expressed that rather than regulating the marketplace, Ecology should be positioned to support more banks.

F.4.3 Many participants expressed that rather than expanding the regulation of water banking, Ecology should focus on how the state can better support banking where it can play a critical role in addressing public health and safety and other water supply challenges. Every basin is unique, and so are the conditions that drive the need for water banks.

F.4.4 It is important to recognize the role that Ecology's regulatory actions have played in driving banking activity, both positive and negative. When writing instream flow rules, Ecology should consider how the regulation may enable or hinder market conditions conducive to water banking and/or speculative or monopolistic activity.

F.4.5 Many participants expressed that transparency in water banks helps to ensure equity and fairness, especially regarding prices that banks charge customers. It was noted that the bill passed in 2016 (SB 6179) requiring that banks disclose their costs and fees for mitigation resulted in significant improvement.

F.4.6 Many participants thought it would be appropriate for water banks to pay the full administrative cost of bank establishment.

F.4.7 Staffing and capacity limitations at Ecology sometimes results in lengthy processing times for water bank agreements and related water right change applications. It may also contribute to inconsistent practices that create uncertainty for clients. Additional resources for implementation of the TWRP would benefit state water management.

Policy Tools – Potential Ecology Recommendations and Actions

P.4.1. Require that prospective bankers submit a "water banking prospectus" in which they outline their business plan.[4] The prospectus would be made available for public comment. Ecology would use the comments received to inform the trust water right agreement (or water banking agreement) negotiated with the banker. Note, this proposal would be tied to P.4.2, Cost Recovery. The legislature could consider adding specific elements to be addressed in

[4] Information such as intended uses and customers, and the suitability of the mitigating water right to meet those uses.

the prospectus. If P.4.2 were not pursued, we could implement this policy under current authority.

Objective: Increase transparency on water banking activity	
Pro's	**Con's**
Requires bankers to engage with Ecology early in the process	If not paired with cost recovery in P.4.2, this would create new administrative costs on Ecology
Clarity about the purpose of a water bank at the onset would serve the public's interest in understanding how the public's water resources are being managed, and to understand potential impacts on the state	There is no cut-and-dry delineation of what constitutes a water bank. There could be confusion on when a prospectus is required
Public comment could inform the terms and conditions of the water banking agreement	
Formalizes and standardizes the process for creating a water bank	

P.4.2. Authorize Ecology to recover the administrative costs of developing water banking agreements. Amend chapter 90.42 RCW to establish a fee for reviewing and processing the water banking prospectus.[5] Also establish that Ecology may require that applicants use the cost reimbursement process for associated water right change applications that are submitted to Ecology.

Objective: Minimizes the public resources that are spent towards an activity that mostly results in private benefits	
Pro's	**Con's**
User pays; the burden is on the banker	The cost could be burdensome for non-profits or local governments seeking to water bank
Will fund additional resources for Ecology to help with permitting, which will allow Ecology to process applications more quickly and build more capacity and consistency among staff	

P.4.3. Clarify Ecology's authority to require water banks to address issues beyond ensuring that there is no impairment to senior water rights. This could include requirements to create enhanced stream flow benefits, or other stipulations for additional consumer or environmental protection. **Note, we are consulting with our attorneys on whether this could be implemented through existing authority or whether additional statutory authority would be necessary, and on whether it would face legal barriers.**

Objective: Provide greater consumer or environmental protections in banking agreements

[5] This could be a flat fee or based upon a fee schedule. The fee will be based upon the amount of staff time Ecology spends in working with potential bankers on developing a trust water right agreement or water banking agreement.

Pro's	Con's
Provides clear authority for more specific provisions in water banking agreements that address environmental enhancement and/or level of service and operational issues	Oversight of these provisions would require additional resources at Ecology
Provides a way to address unique issues in each water bank development with lower legal risk of being arbitrary and capricious	If specific authorities are not detailed in statute, would require Ecology rulemaking. Rulemaking is costly and time consuming for the agency. With other rulemaking priorities, it is unclear when Ecology will have resources to undertake this rulemaking in the near term

P.4.4. Require that draft water banking agreements are posted for public comment before being finalized. Ecology will consider public comment before finalizing terms of the agreement. Note, Ecology plans to pursue this under current authorities. No statutory changes are needed.

Objective: Increase transparency and opportunity for public comment	
Pro's	**Con's**
Increased transparency. Under the current system, it's difficult for the general public to know what's in these agreements	Will lengthen the time it takes to develop water banking agreements
May give the public greater input on the terms and conditions placed on a water bank	Related to P.4.3, certain comments may require conditions for water banking agreements that are outside Ecology's current authority

Policy Tools – For Future Legislative Evaluation

None.

Policy Tools – Considered but not Recommended

P.4.5. Amend chapter 90.42 RCW to establish that water banks must define their service area and then have a "duty to serve" within that area.[6]

Reasoning: Ecology originally considered this policy as a way to prevent price discrimination and ensure that a customer is not denied service based upon who they are. There was also hope that this could decrease the number of banks established to serve the same customers. However, this policy option could result in reduced competition and increased cost to consumers. In addition, this could create an expectation that water will be available in a given area and lead to increased development pressure.

[6] Meaning that the bank could not deny providing mitigation to any customer in their defined service area.

P.4.6. Amend chapter 90.42 RCW to establish that Ecology may prioritize working on water banks serving the greatest public need (such as public health and safety or creating a new water supply solutions).

Reasoning: Prioritizing "public health and safety" might be seen as endorsing a priority for domestic water use, which is contrary to the Water Code. This policy option would contribute to the perception that Ecology would be "picking winners and losers" in water banking. And, if Ecology deprioritized an application, it may be years before we process it. Instead of pursing this, we believe it is preferable to authorize cost recovery as to provide Ecology with the resources to process trust water agreements and banking proposals in a timely manner.

P.4.7. Clarify in statute that Ecology may deny a proposal to establish a new water bank.

Reasoning: This policy option would result in the perception that Ecology would be "picking winners and losers" for new water banks.