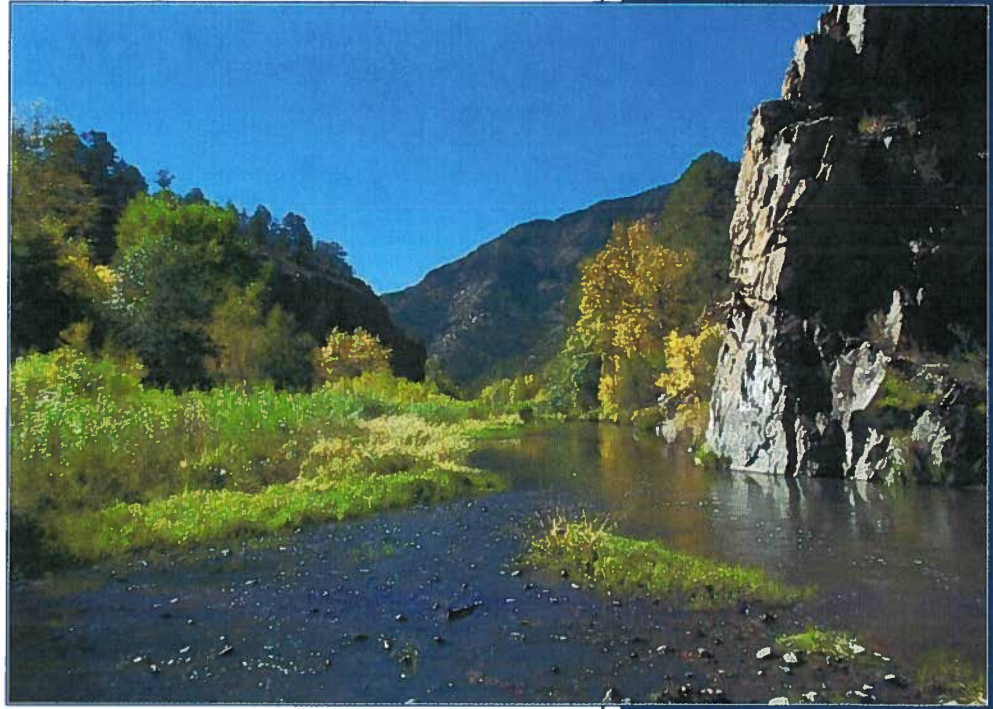


2017



NEW MEXICO UNIT FUND

Report to the New Mexico
Legislative Finance Committee and Interim
Water and Natural Resources Committee



New Mexico Interstate
Stream Commission

November 2017

New Mexico Unit Fund: Report to the
New Mexico Legislative Finance Committee and
Interim Water and Natural Resources Committee

New Mexico Interstate Stream Commission

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November 2017

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ABBREVIATIONS AND ACRONYMS

AWSA	Arizona Water Settlements Act of 2004
CAP	Central Arizona Project
CRBPA	Colorado River Basin Project Act of 1968
CUFA	New Mexico Consumptive Use and Forbearance Agreement
DFA	Department of Finance and Administration
EIS	Environmental Impact Statement
GSFCC	Gila San Francisco Coordinating Committee
ICIP	Infrastructure Capital Improvement Plan
ISC	New Mexico Interstate Stream Commission
JPA	Joint Powers Agreement
NEPA	National Environmental Policy Act
NOI	Notice of Intent
OM&R	Operation, Maintenance and Repair (or Replacement)
SIC	New Mexico State Investment Council
SWNMSG	Southwest New Mexico Stakeholders Group

EXECUTIVE SUMMARY

The New Mexico Unit Fund (“NM Unit Fund” or “Fund”) is a fund in the New Mexico treasury created by the NM Unit Fund Act, NMSA 1978, § 72-14-45, consisting primarily of deposits from the U.S. Bureau of Reclamation (“Reclamation”) pursuant to the federal Arizona Water Settlements Act of 2004 (“AWSA”). The NM Unit Fund Act requires that the Interstate Stream Commission (“ISC or Commission”) report to the Legislative Finance Committee and the Interim Water and Natural Resources Committee every year by November 15 on the following three items:

- 1) the status of the NM Unit Fund;
- 2) the distribution of money from the NM Unit Fund to implement the purpose of the Fund pursuant to the Act; and
- 3) proposed uses and levels of funding projected for the upcoming fiscal year.

The AWSA provides New Mexico with up to an annual average of 14,000 acre-feet of water per year from the Gila and San Francisco Rivers above and beyond the amount decreed to New Mexico by the U.S. Supreme Court in *Arizona v. California*, 376 U.S. 340 (1964). In addition, the AWSA provides \$66 million (adjusted for inflation to \$90.4 million) for construction of a New Mexico Unit (“NM Unit”) or other water utilization projects in the counties of Catron, Grant, Hidalgo, and Luna.

The \$66 million provided to New Mexico is being deposited into the NM Unit Fund in ten annual installments. New Mexico has received six annual payments of \$9.04 million totaling \$54.24 million. Expenditures total \$12.93 million as of October 23, 2017. An increase in Market Value of investments on the Fund is \$3.26 million. The current balance in the Fund is \$44.6 million.

The FY2018 budget breaks down as follows:

1. The ISC’s FY2018 Gila/AWSA operating budget is \$315,000.
2. The ISC’s FY2018 Gila/AWSA Work Plan as approved by the Commission is \$2,611,500.
3. More funds will be expended from a total of \$9.1 million allocated by the ISC for the Non-NM Unit projects. The exact amount of expenditures is currently unknown because it depends on progress made on those projects individually.
4. The NM CAP Entity’s FY2018 budget as approved by the Commission is \$1,354,685.
5. Reclamation’s budget for environmental compliance activities related to the NM Unit for the period of January through September 2017 as approved by the Commission is \$4,413,000. This amount has been advanced to Reclamation. Reclamation will use the monies remaining from this amount to fund its activities through June 2018.

In addition, the FY2019 budget will break down as follows:

1. The appropriation request for the ISC’s FY2019 Gila/AWSA operating budget of \$315,000.
2. The ISC’s FY2019 Gila/AWSA Work Plan may include engineering; environmental compliance; and legal services. The specifics of those costs are currently unknown.
3. More funds will be expended from a total of \$9.1 million allocated by the ISC for the Non-NM Unit projects. The exact amount of those expenditures is currently unknown because it depends on progress made on those projects individually.
4. The NM CAP Entity’s FY2019 budget is \$1,409,686.
5. Reclamation’s budget for the period of October 2017 through June 2019 as approved by the Commission is \$3,255,000. Funds will be advanced to Reclamation out of this budget. The exact amount of expenditures is currently unknown.

I. INTRODUCTION

During the 2011 Legislative Session, the New Mexico Legislature passed H.B. 301 (“the Act”) creating the NM Unit Fund in the State Treasury. The Act is codified as 2011 NM Laws, Ch. 99, NMSA 1978, § 72-14-45 (2011). The Fund consists of money distributed to the State pursuant to Paragraphs (2)(D)(i) and (ii) of Section 403(f) of the Colorado River Basin Project Act of 1968 (“CRBPA”), codified at 43 U.S.C § 1524(f), as amended by Section 107(a) of the AWSA. Pursuant to the Act, the Fund can also consist of appropriations, grants, and donations or bequests to the Fund.

Income from the Fund is credited back to the Fund. Balances do not revert to the general fund.

Money in the NM Unit Fund is administered by, and appropriated to, the ISC. The Act requires the ISC to report to the Legislative Finance Committee and the Interim Water and Natural Resources Committee every year by November 15 on the following three items:

- 1) the status of the NM Unit Fund;
- 2) the distribution of money from the NM Unit Fund to implement the purpose of the Fund pursuant to the Act; and
- 3) proposed uses and levels of funding projected for the upcoming fiscal year.

This report includes these three items. In addition, this report provides a general update on issues and activities arising from the AWSA.

II. BACKGROUND

The federal CRBPA directed the U.S. Secretary of the Interior (“Secretary”) to offer to contract with water users in New Mexico for water from the Gila River, its tributaries, and underground water sources in amounts to permit consumptive use of water in New Mexico not to exceed an annual average in any period of ten consecutive years of 18,000 acre-feet over and above consumptive uses provided by Article IV of the Decree of the Supreme Court of the United States in *Arizona v. California*, 376 U.S. 340 (1964).

The federal AWSA amended the CRBPA by directing the Secretary to offer to contract with water users in New Mexico, with the approval of the ISC, or with the State of New Mexico through the ISC, for water from the Gila River, its tributaries and underground water sources in amounts that permit consumptive use not to exceed an annual average of 14,000 acre-feet in any 10-year period. This consumptive use is in addition to New Mexico’s decreed right in *Arizona v. California*.

Should New Mexico divert and consumptively use the additional AWSA water, the Secretary must deliver “exchange water” from the Central Arizona Project (“CAP”) to downstream, forbearing Gila River water users in Arizona.

The AWSA further provides \$66 million, adjusted for inflation since January 1, 2004, in ten annual payments to the NM Unit Fund beginning with year 2012. Withdrawals from the NM Unit Fund are for the purpose of paying costs of the NM Unit¹ or other water utilization alternatives to meet water supply demands in Catron, Grant, Hidalgo, and Luna Counties as determined by the ISC in consultation with the Southwest New Mexico Water Study Group (“SWNMSG”) or its successor². The AWSA mandates that costs associated with planning, environmental compliance, and environmental mitigation and restoration, among others, be paid with withdrawals from the NM Unit Fund.

The AWSA allows an additional amount of \$34 million, adjusted for inflation since January 1, 2004, for construction of the NM Unit, provided that certain conditions listed in the AWSA are met. Moreover, if the rate of return on carryover funds in the federal Lower Colorado Basin Development Fund exceeds an average annual rate of four percent for the period beginning with the AWSA’s enactment through the date of initiation of construction of the NM Unit, an additional amount up to \$28 million shall be made available for construction. Thus, a maximum additional \$62 million may be available for construction of the NM Unit. Earnings in the Lower Colorado Basin Development Fund to date do not support the additional \$28 million.

¹ New Mexico Unit of the Central Arizona Project (“NM Unit”): Physical facilities to be used to divert, store, and deliver the additional water under the AWSA

² This group was succeeded by the Gila-San Francisco Water Commission. The NM CAP Entity is the successor to the Gila-San Francisco Water Commission.

III. ISC PLANNING AND ADMINISTRATION

The AWSA was signed into law in December 2004. In early 2005, the ISC formed the Gila San Francisco Coordinating Committee (“GSFCC”), in an attempt to build consensus among regional stakeholders. The GSFCC was composed of one representative each from the ISC, the U.S. Bureau of Reclamation (“Reclamation”), the U.S. Fish and Wildlife Service, the Office of the Governor, and the Gila San Francisco Water Commission (representing local governments). The GSFCC convened a Technical Committee composed of representatives from local water users, environmental groups, and state and federal agencies.

The task of the GSFCC’s Technical Committee was to determine the studies necessary to evaluate the environmental effects of potential water withdrawals under the AWSA. After literature reviews, science forums, and initial baseline studies, the Technical Committee agreed on a suite of 13 additional studies and surveys needed, with a total projected cost of \$945,000. The 2006 Legislature appropriated the full amount of funding, but the appropriation was vetoed.

In 2007, the ISC formed the SWNMSG. The task of the SWNMSG was to reach consensus among all stakeholders on a small suite of projects to be funded from AWSA monies. By November 2010, the SWNMSG’s suite consisted of 70 different projects. In February 2011, after a request by the ISC to reach consensus on a much smaller set of projects, the SWNMSG could only reduce the number of projects to 50.

As a consequence of these failed efforts, the ISC developed its own process to solicit and evaluate proposals. The ISC, with input from regional stakeholders, initiated a two-tiered evaluation process for selection of projects to be funded from the NM Unit Fund.

During Tier-1 of the process, the ISC received 45 project proposals from stakeholders, which were evaluated by a panel consisting of representatives from the ISC; the New Mexico Department of Game and Fish; the New Mexico Environment Department; the Energy, Minerals, and Natural Resources Department; and the Office of the State Engineer. Twenty proposals met the Tier-1 criteria and passed to the Tier-2 ranking process. On February 29, 2012, the ISC selected 16 of the 20 Tier-2 projects for further assessment, refinement, or combination. In 2013, one proponent withdrew its proposal from consideration.

After extensive evaluation of the 15 proposals’ technical feasibility, legal feasibility, costs, water supply, benefits, and environmental impacts, the Commission voted at its November 24, 2014 meeting to send a written notice to the Secretary that New Mexico intended to build a NM Unit. The Commission also voted to fund non-NM Unit projects³ (with some modifications made by the ISC at its February 26, 2015, meeting), at a total cost of \$9.1 million. Those projects and their respective allocations are listed in Table 1.

³ Also known as non-diversion projects, or other water utilization alternatives

Table 1. Non-NM Unit projects and their awards as approved by the Commission

	Project	ISC Award (\$)	
1	Town of Hurley Regional Water Project ⁴	2,100,000	
2	Gila Basin Irrigation Commission Diversion Structure	1,250,000	
3	1892 Luna Irrigation Ditch Association Diversion Structure	100,000	
4	Pleasanton East-Side Ditch Improvement	200,000	
5	New Model Canal Improvement ⁵	200,000	
6	Catron County Ditches Diversion Structure	500,000	
7	City of Deming Effluent Reuse	1,750,000	
8	Municipal Water Conservation Fund (\$3M)	City of Deming Effluent Reuse	596,000
9		Bayard Effluent Reuse	1,171,048
10		Lordsburg Meter Replacement	242,950
11		Rodeo Meter Replacement	14,000
12		Santa Clara Effluent Reuse	100,000
13		Silver City Park Irrigation Upgrade	18,157
14		Silver City Meter Replacement	500,000
15		Bayard/Cobre Schools Effluent Reuse	176,295
16		Hurley Meter Replacement	181,550
Total		9,100,000	

Prior to final design and construction of a NM Unit, an Environmental Impact Statement (“EIS”) must be prepared, in accordance with the National Environmental Policy Act (“NEPA”). The Secretary must issue a Record of Decision, upon the completion of the EIS.

The AWSA directs Reclamation to be the lead agency for environmental compliance pursuant to NEPA. The AWSA also provides for the State of New Mexico, through the ISC, at its option, to be joint lead agency for environmental compliance. On February 26, 2015, the ISC voted to be joint lead agency and transmitted its intent to the Secretary on February 27, 2015.

On November 17, 2016, the Commission approved an MOU between the ISC and Reclamation that outlines both agencies’ duties and responsibilities as NEPA joint leads with respect to environmental compliance and the preparation of the EIS for the NM Unit. At the same meeting, the Commission also approved a Funding Agreement between the ISC, Reclamation, and the Entity, as the project proponent, to fund Reclamation’s work on this EIS, including staff hours and contractors.

⁴ Formerly known as Grant County Water Commission Wellfield and Pipeline Project

⁵ The initial allocation was for both Sunset and New Model Canals in the Virden Valley. However, the Sunset Canal subsequently decided not to pursue its project. Upon request from the New Model Canal, the ISC re-allocated the full amount of the AWSA grant to the New Model Canal.

In the meantime, the ISC hired a financial adviser to determine an appropriate asset allocation strategy for investment of the NM Unit Fund in the pooled funds offered by the NM State Investment Council (“SIC”). At its June 22, 2016, meeting, the Commission approved the staff’s recommendations for the NM Unit Fund asset allocation strategy. The asset allocation and targets are listed in Table 2.

Table 2. Asset allocation and targets

Asset Class	Implementation Choice ⁶	Minimum	Target	Maximum
Large Cap U.S. Equity	Passive	22%	25%	28%
Small/Mid Cap U.S. Equity	Active	6.5%	8%	9.5%
Non-U.S. Developed Equity	Passive	15%	17%	19%
Non-U.S. Emerging Markets Equity	Active	4%	5%	6%
Core (Plus) Fixed Income Bonds	Active	40%	45%	50%

Pursuant to the Joint Powers Agreement between the ISC and the SIC, a total of \$37 million has been invested out of the NM Unit Fund since November 2016. An increase in Market Value of investments is \$3.26 million⁷ as of September 30, 2017.

⁶ The two implementation choices are actively or passively managed investment pools. Actively-managed strategies strive to outperform a relevant broad market benchmark, albeit at higher fees, whereas passively-managed strategies seek to meet the return of the relevant broad-market benchmark at substantially lower fees.

⁷ A total of \$43,468 has been charged in investment costs as of September 30, 2017. It should be noted, however, that those costs for managing the pool are charged to each investment pool. Costs are allocated to each investor as a percentage of their ownership of units in the pool and it makes up part of the Market Value of investments at the end of each month. There are no direct costs for investing funds with the SIC.

IV. NM CAP ENTITY AND PROJECT SELECTION

The AWSA also provides for the creation of the New Mexico CAP Entity (“CAP Entity”), an entity formed or designated by the State of New Mexico, through the ISC, to enter into the NM Unit Agreement with the Secretary. In addition, the AWSA states that the CAP Entity shall own and hold title to all portions of the NM Unit. Following construction of the NM Unit, the CAP Entity will be responsible for reimbursing the Secretary for operation, maintenance, and repair (“OM&R”) costs attendant to delivery of the exchange water.

Furthermore, the Secretary is authorized to design, build, operate, and maintain the NM Unit. Upon request by the CAP Entity, the Secretary shall transfer to the CAP Entity those responsibilities, or any combination thereof. In April 2016, the CAP Entity requested transfer of the design responsibility from the Secretary to the CAP Entity.

The CAP Entity was formed under a Joint Powers Agreement (“JPA”) approved by the Department of Finance and Administration (“DFA”) in July 2015, and amended in October 2017. The CAP Entity is currently composed of fourteen local governments from Southwest New Mexico. They are as follows:

1. Upper Gila Irrigation Association
2. Fort West Irrigation Association
3. Gila Farm Irrigation Association
4. Gila Hot Springs Irrigation Association
5. Catron County
6. Grant County
7. Luna County
8. Village of Santa Clara
9. Hidalgo Soil and Water Conservation District
10. Hidalgo County
11. City of Deming
12. San Francisco Soil and Water Conservation District
13. City of Lordsburg
14. Grant Soil and Water Conservation District⁸

In addition, the ISC signed the JPA and is a non-voting member of the Entity. The ISC is also the CAP Entity’s first fiscal agent. The City of Deming is the second fiscal agent.

As soon as it was formed, the CAP Entity began negotiations with Reclamation for supplemental terms that the Department of Interior wanted added to the NM Unit Agreement⁹. The Secretary

⁸ Joined the Entity through the JPA amendment in October 2017

⁹ The text of the NM Unit Agreement was drafted in 2004, attached to the AWSA as an appendix, and ratified by Congress when it passed the AWSA.

of the Interior signed the NM Unit Agreement on November 23, 2015, thus meeting the deadline set by the AWSA.

For the purpose of preparing the EIS, the NM Unit needs to be designed to a level sufficient to allow the public and interested parties to make meaningful comments and to determine what physical, socio-economic, and environmental impacts might result from implementation of the NM Unit. On November 24, 2015, the CAP Entity voted to allow the ISC to negotiate and award a contract for up to 30-percent engineering design services for the NM Unit, to be used in coordination with the CAP Entity to obtain information to help the Entity make decisions as it moves forward with this process.

Following the CAP Entity's approval, the ISC hired an engineering firm to work with the CAP Entity to develop a conceptual design and identify a Proposed Action. The work was completed, and the NM CAP Entity submitted its proposal to Reclamation on July 15, 2016.

On February 7, 2017 the CAP Entity's Executive Director participated in a meeting with The Nature Conservancy and the New Mexico Department of Energy, Minerals and Natural Resources, at which they indicated they would not allow the NM Unit proposed by the Entity to be built on the lands they jointly own.

Following this outcome, the CAP Entity approved a new scope of work for the design engineer to explore other options and help amend its Proposed Action. This phase of work was completed in October 2017. The CAP Entity voted on a project at its October 30, 2017 meeting, and directed its staff to draft a revised Proposed Action letter for submittal to the Joint Leads in the NEPA process.

When the revised Proposed Action has been formally submitted, Reclamation will publish in the Federal Register a Notice of Intent ("NOI") to prepare an EIS for the NM Unit. This will officially begin the NEPA process. The Joint Leads anticipate that the NOI will be published in Winter 2017/2018.

V. NEW MEXICO UNIT FUND

The NM Unit Fund and NMSA 1978, § 72-14-45 are described in the Introduction, and the descriptions are not repeated here.

STATUS

The \$66 million provided to New Mexico by the AWSA is being deposited into the NM Unit Fund in ten annual installments of \$9.04 million, adjusted for inflation. The sixth annual deposit from Reclamation occurred in January 2017.

Status as of October 23, 2017:

- Total received since January 2012: \$54.24 million
- Cumulative total expenditures for FY12-18: \$12.93 million (*see Table 3 for breakdown*)
- Increase in Market Value of investments: \$3.26 million (*as of September 30, 2017*)¹⁰
- Current Balance: \$44.6 million

DISTRIBUTION OF MONEY TO IMPLEMENT THE PURPOSES OF THE FUND

The expenditures to date of \$12.93 million have been for the purposes of paying the following: ISC's Full-Time Equivalents ("FTEs") dedicated to Gila/AWSA work and their support costs; engineering and scientific investigations and reports; website development and maintenance and facilitators for public meetings; legal support; advances to Reclamation for NEPA; and the CAP Entity's budget. The breakdown of the expenditures is listed in Table 3.

Table 3: FY2012-18 Expenditures Breakdown as of October 23, 2017

Budget Item (FY2012-18)		Expenditure (\$)
ISC AWSA operating budget		1,443,166
ISC contractual Services	NM Unit engineering	837,063
	Studies	3,795,906
	Legal	476,359
	Facilitation, website, other	106,304
Advances to Reclamation for NEPA		4,413,000 ¹¹
Non-NM Unit projects		1,123,991 ¹²
CAP Entity budget (FY2016-18)		734,487
Cumulative Total as of October 23, 2017		12,930,276

¹⁰ At the time this report was being prepared, the ISC had not yet received the investment report for October 2017.

¹¹ \$2,411,587 (55%) has been obligated/expended by Reclamation as of September 30, 2017.

¹² Out of a total of \$9.1 million that has been allocated by the Commission

USES AND LEVELS OF FUNDING PROJECTED FOR THE CURRENT FISCAL YEAR (2018)

1. ISC's Gila/AWSA Operating Budget: The appropriated FY2018 operating budget for ISC Gila staff is \$315,000 which includes 3 FTEs¹³ and support costs.
2. ISC's Gila/AWSA Work Plan: At its June 20, 2017 meeting, the ISC approved the FY2018 Gila/AWSA Work Plan¹⁴ in the amount of \$2,611,500 for the purposes of funding up to 30-percent design of the NM Unit on behalf of the CAP Entity; NEPA and related services; public outreach; and legal services.
3. ISC's Non-NM Unit Projects: As noted above, \$1,123,991 out of \$9.1 million has been expended on these projects to date. It is anticipated that more funds will be expended before the end of the current fiscal year. The exact amount of expenditures is currently unknown because it depends on progress made on those projects individually.
4. CAP Entity's Budget: At present, the CAP Entity's expenses are paid from the NM Unit Fund pursuant to Paragraph V(m) of the JPA. The ISC approved the CAP Entity's FY2018 budget of \$1,354,685 on April 21, 2016. The NM CAP Entity's budget includes operational expenses, salary of the executive director, consultants' fees, legal services, and other contractual services.
5. Advances to Reclamation for NEPA: At its November 17, 2016 meeting, the ISC approved Reclamation's Interim Project Plan, as defined in the Funding Agreement, for the period of January 1, 2017 through September 30, 2017 in the amount of \$4,413,000. This initial disbursement was made to Reclamation in December 2016, and received by Reclamation in January 2017. As of September 30, 2017, there is a balance of \$2,001,413 remaining from the advances related to the Interim Project Plan. This balance will be enough to fund Reclamation's planned internal costs and contracts until the end of the current fiscal year. Reclamation has informed the ISC that it will adjust the Schedule of Advances based on the remaining balance from the Interim Project Plan. Reclamation will not request any further payments until July 2018, the start of the 2019 fiscal year. Therefore, there will not be any further disbursements to Reclamation out of the NM Unit Fund in the current fiscal year.

USES AND LEVELS OF FUNDING PROJECTED FOR THE UPCOMING FISCAL YEAR (2019)

1. ISC's Gila/AWSA Operating Budget: The ISC FY2019 appropriation request for the Gila/AWSA operating budget is \$315,000 for 3 FTEs and support costs.
2. ISC's Gila/AWSA Work Plan: The FY2019 Gila/AWSA Work Plan may include engineering; environmental compliance; and legal services. The specifics of those costs will be determined based on the ISC's Joint Lead Agency work activity needs¹⁵, and will be proposed to the Commission.

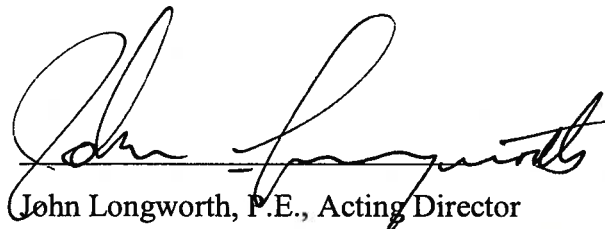
¹³ Two of those positions are currently filled and it is anticipated that a third position will be filled soon.

¹⁴ This Work Plan does not include elements that were separately considered and approved by the Commission, i.e. Reclamation's Project Plans and Non-NM Unit grants.

3. ISC's Non-NM Unit Projects: It is anticipated that more funds will be expended on these projects in FY2019. The exact amount of expenditures is currently unknown because it depends on progress made on those projects individually.
4. CAP Entity's Budget: The CAP Entity's FY2019 budget request in the amount of \$1,409,686 was approved by the ISC on July 20, 2017 and submitted with the ISC's FY2019 appropriation request. The CAP Entity's budget includes operational expenses, salary of the executive director, consultants' fees, legal services, and other contractual services.
5. Advances to Reclamation for NEPA: At its May 18, 2017 meeting, the ISC also approved Reclamation's 2018-2019 Bi-Annual Project Plan for the period of October 1, 2017 through June 30, 2019 in the amount of \$3,255,000. As noted above, there will not be any disbursements to Reclamation between October 2017 and June 2018. Additional disbursements will be made to Reclamation in FY2019. The exact amount of expenditures is currently unknown.

Therefore, the ISC anticipates FY2018 and FY2019 expenditures to include FTEs and support costs, engineering, additional advances to Reclamation, federal environmental compliance, the CAP Entity's budget, legal services, and the funding for the Non-NM Unit projects.

NM INTERSTATE STREAM COMMISSION

 11/15/17
John Longworth, P.E., Acting Director