

BOARD OF WATER SUPPLY
COUNTY OF MAUI
200 SOUTH HIGH STREET
WAILUKU, MAUI, HAWAII 96793
www.mauicounty.gov/water

January 6, 2022

Honorable Michael P. Victorino
Mayor, County of Maui
200 South High Street
Wailuku, Hawaii 96793

Dear Mayor Victorino:

**SUBJECT: MAUI COUNTY BOARD OF WATER SUPPLY SUPPORT OF THE
COUNTY OF MAUI ACQUIRING THE LONG-TERM WATER LEASES
FOR THE NĀHIKU, KE'ANAE, HONOMANŪ, AND HUELO LICENSE
AREAS**


On December 16, 2021, the Board of Water Supply (BWS) received extensive testimony from the public, as well as presentations from Maui County Managing Director Sandy Baz and Maui County Council Agriculture and Public Trust Committee Chair Shane Sinenci. Following the presentations and testimonies, and per the agenda, the BWS discussed Recommended Immediate Actions (page 81) and the Recommended Near-Term Actions (page 82) from the Board of Water Supply Temporary Investigative Group (TIG) Report, which was approved unanimously by the Board of Water Supply on December 19, 2019.

The Board subsequently approved by unanimous vote, submitting this letter of support to the Mayor and the Maui County Council, encouraging the County of Maui to pursue the feasibility of acquiring the leases for the Nāhiku, Ke'anae, Honomanū, and Huelo license areas through an intergovernmental agreement with the Department of Land and Natural Resources (DLNR), as recommended in our 2019 TIG Report. To this effect, the Board recommends contacting DLNR as soon as possible to determine next steps for doing so.

"By Water All Things Find Life"

Thank you very much for your time and consideration in this matter.

Sincerely,



Dean K. Frampton
Chair, Maui County Board of Water Supply

cc: Sandy Baz, Managing Director
Maui County Council Members
Jeffrey T. Pearson, Director
Helene Kau, Deputy Director

Maui County Board of Water Supply
330 South High Street
West Maui, Hawaii 96753
Phone: (808) 243-2100
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MAUI COUNTY BOARD OF WATER SUPPLY
COUNTY OF MAUI ACQUIRING THE LONG-TERM WATER RIGHTS
FOR THE MAUI KAU KAUAHONOHONO AND FIELD LUNDS
AREA

On October 26, 2011, the Board of Water Supply (BWS) received a letter from the public as well as presentations from Maui County. The letter was received from the Maui County Council and Public Trust Commission. The letter requested that the Board of Water Supply (BWS) consider the acquisition of the long-term water rights for the Maui Kau KaUAHONOHONO and Field Lunds area. The BWS is currently reviewing the presentation and will provide a response to the letter by the end of the month.

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DAVID Y. IGE
GOVERNOR
STATE OF HAWAII



TYLER I. GOMES
DEPUTY TO THE CHAIRMAN

JOSH GREEN
LT. GOVERNOR
STATE OF HAWAII

STATE OF HAWAII
DEPARTMENT OF HAWAIIAN HOME LANDS

P. O. BOX 1879
HONOLULU, HAWAII 96805

TESTIMONY OF WILLIAM J. AILA, JR, CHAIRMAN
HAWAIIAN HOMES COMMISSION
BEFORE THE MAUI COUNTY COUNCIL
MEETING ON JANUARY 7, 2022 AT 9:00 AM

RESOLUTION NO. 22-4 (2022)

Aloha Chair Lee, Vice Chair Rawlins-Fernandez, and Members of the County Council:

The Department of Hawaiian Home Lands (DHHL) submits testimony **offering comments on and support for** this resolution.

The availability of water is one of the key barriers DHHL faces in the development and delivery of homesteads across Hawai'i. In acknowledgement of that reality, the Legislature has included a number of provisions in various statutes to help address that challenge. All of these provisions are intended to ensure that the purposes of the Hawaiian Homes Commission Act (HHCA), including "Providing adequate amounts of water and supporting infrastructure, so that homestead lands will always be usable and accessible" (HHCA 101(b)(4)) will be fulfilled.

One of those provisions relates to the issuance of state water leases and licenses, which includes the East Maui waters addressed by this resolution. Hawai'i Revised Statutes 171-58(g) requires that prior to the issuance of any long-term water lease, "After consultation with affected beneficiaries, these departments shall jointly develop a reservation of water rights sufficient to support current and future homestead needs. Any lease of water rights or renewal shall be subject to the rights of the department of Hawaiian home lands as provided by section 221 of the Hawaiian Homes Commission Act."

To fulfill this requirement, in December 2020 DHHL, after beneficiary consultation and approval by the Hawaiian Homes Commission, has submitted a request to the Commission on Water Resources Management (CWRM) for such a reservations We have requested CWRM to approve a reservation of 11,177,500 gallons per day originating from the watershed of, and tributaries to, the East Maui streams diverted by the East Maui Irrigation system for non-potable water use in Pūlehunui and Kēōkea-Waiohuli Hawaiian Home Lands.

It is also helpful in relationship to this resolution to share that to further ensure that adequate water will be provided for Hawaiian Home Lands, the Hawai'i Supreme Court has explicitly included that reservations of water for, and uses of water by, the

DHHL for homesteading purposes are one of the four "public trust" uses of water that are to be provided for and protected. This status is described in the same decisions that this resolution references, the Waiāhole water case and the Kaua'i Springs case (In re Water Use Permit Applications, 94 Hawaii 97 (2000), and Kauai Springs, Inc. v. Planning Commission of County of Kauai, 133 Hawaii 141(2014)).

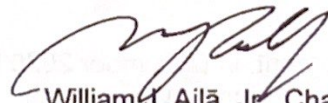
As a municipal government agency, the County of Maui has an obligation to uphold not only the public trust doctrine, but also the legal obligations outlined in the Hawaiian Homes Commission Act, a Constitutional mandate and a condition of statehood. DLNR also holds those mandates and must require of any potential water lessee or assignee to fulfill these duties as a condition of any lease or license. We note that the current owners of EMI participated in our beneficiary consultation process and have done nothing to indicate that they oppose the granting of our reservation and cooperation in the provision of water to our beneficiaries.

However, DHHL notes that the obligations of the County of Maui are unambiguous in regard to its duties to the HHCA. Hence DHHL recognizes the benefits that would accrue to its beneficiaries if this resolution were passed and its actions contemplated were adopted.

Finally, we note that in separate constitutional and statutory provisions, DHHL is to receive, in addition to any reserved water, 30% of the revenues generated by water lease and license payments. Thus we are grateful for and support the provisions of this resolution acknowledging that lease payments would still be made to the State.

We would be happy to answer any questions. Thank you for your consideration of our testimony.

Me ke aloha,



William J. Ailā, Jr., Chairman
Hawaiian Homes Commission

AMENDED

STATE OF HAWAII
DEPARTMENT OF LAND AND NATURAL RESOURCES
Land Division
Honolulu, Hawaii 96813

October 22, 2021

Board of Land and Natural Resources
State of Hawaii
Honolulu, Hawaii

STATEWIDE

Adoption of Guidance to Appraisers for the Determination of the Upset Rent for Public Auctions for Water Leases for Consumptive Use Purposes Pursuant to Section 171-58, Hawaii Revised Statutes.

BACKGROUND

Through efforts to establish a process for issuing water leases pursuant to Section 171-58, Hawaii Revised Statutes (HRS), the most significant challenge encountered by staff has been the valuation of the upset rent for the use of water. Under most circumstances, HRS 171-58 requires water leases to be issued via public auction. The public auction process, with its requirements codified in multiple sections throughout HRS Chapter 171, is an extensive, time consuming process. As required in HRS 171-17, the upset price for all public auctions shall be determined by appraisal, the result being the fair market value of the interest to be disposed.

This requirement has created an incongruity when considering the nature of water in Hawaii, which is a public trust resource. Unlike other markets in the country where water can be held and disposed as other private property interests, water rights in Hawaii are held by the State for the benefit of the public. This has posed a challenge for appraisers to determine a market value of an interest for which there is no market. Similar to the valuation of submerged lands and geothermal resources, other types of public trust resources entirely held by the State, guidance for the valuation of water rights needs to be developed by the State.

In researching historical water leases, staff determined that it would not be appropriate to adopt valuation methodologies that were used at the time. Such methodologies may not be appropriate as they were developed at a time when the current requirements in HRS 171-58 did not yet exist, less emphasis was given to resource management and sustainability, and the public trust obligations with respect to water use were not as clearly defined in law. Therefore, staff developed guidance for an appraiser to consider when determining the value of water that addresses the aforementioned priorities. Staff also determined that the guidance should be incorporated into HRS 171-58 and drafted proposed legislation to achieve that purpose.¹

¹ In addition to the valuation guidance, the proposed legislation included a process to allow water leases to be awarded by direct negotiation and other amendments to clarify the water leasing process.

as amended
APPROVED BY THE BOARD OF
LAND AND NATURAL RESOURCES
AT ITS MEETING HELD ON
October 22, 2021 *go.*

The proposed legislation was included in the administrative package for both the 2020 and 2021 legislative sessions but failed to pass each time.² Although the Department intends to submit legislation for the 2022 session, staff believes that bringing this issue before the Board for their consideration and approval is appropriate. In the event the legislation fails to pass, provided that the Board approves this item, staff will be able to proceed in working with appraisers to determine the value of water without further delay. Given the significance of this issue, staff believes that the process of the valuation of water should be decided directly by the Board rather than left to staff discretion.

DISCUSSION

Proposed Guidance

Staff developed the following guidance consisting of multiple factors that could be used by an appraiser to determine the value of water. Acknowledging that this guidance is largely conceptual in nature, staff believes it would be appropriate to use the current revocable permit rent as a starting value, as it serves as an indication of the value of water for a particular disposition. The revocable permit rent would then be subject to adjustment via consideration of the factors discussed below. Staff notes that the guidance grants deference to an appraiser to exercise their professional expertise and judgment as to which factors may be applicable and how much weight should be accorded to each factor, based on the individual circumstances of prospective lessees.

The factors are not intended to serve as a strict formula to be applied unilaterally in all situations. The guidance is intended to apply primarily to consumptive uses of water. Certain non-consumptive uses, such as hydropower, may be valued using alternative methods that are limited to that particular use. However, the factors may be modified to apply to non-consumptive use if determined appropriate by an appraiser.

The first is the amount of water diverted or extracted, as allowed by the Commission on Water Resource Management (CWRM), and proposed use of water allowed under the lease. The greater the amount of water used and the private benefit the lessee receives from its use would increase the value of the water. For example, a lease that allows a use such as bottling water for commercial resale should be valued higher than a lease for hydropower.

The second is the amount of water diverted or extracted in proportion to the amount of water available from the surface or ground water source, the greater of which would increase the value of the water. As an example, a water lease that allows the lessee to use most or all the available water in excess of the instream flow standard would have a greater value than a lease that provides for a much smaller amount of the excess above the instream flow standard or sustainable yield.

The third is the cost of delivery. For example, the appraisal would consider the cost of maintenance and upgrades to mitigate system losses, the greater of which would decrease the

² For reference, House Bill 2357 and Senate Bill 2913 were introduced in the 2020 legislative session, and House Bill 1015 and Senate Bill 1169 were introduced in the 2021 legislative session.

value of water. Staff believes that this could provide the lessee incentive to include a commitment to maintain and upgrade the delivery system as part of the lease.

The fourth is the avoided cost to the lessee of obtaining water from practicable alternative water sources, the greater of which would increase the value of water. This would essentially be an analysis of replacement costs in the event no water lease was awarded. For example, a smaller agricultural water user could have relatively low replacement costs by transitioning to county service, implementing a catchment system or trucking in water. A higher volume user may need to resort to drilling one or more wells at a higher cost.

The fifth is the net economic benefit to the lessee, the greater of which would increase the value of water. This would be similar to the income approach analysis done in traditional appraisals. Staff believes that if the water use results in significant profits for a lessee, then the value of the water should reflect that accordingly. Conversely, if the water is used for a purpose that is not economically lucrative, then that should also be considered in the valuation.

The sixth is the value contributed by the lessee for watershed management pursuant to HRS 171-58(e), the greater of which would decrease the value of water. Staff believes that as the contribution by the lessee to the implementation of a watershed management plan is separate from the water lease rent, the amount of the contribution should be considered in the valuation. Staff does not envision this as a specific “dollar for dollar” adjustment but rather one of multiple factors in determining value. Staff believes that this could provide an incentive for the Department and the lessee to reach an agreement on the appropriate contribution for the watershed management plan implementation.

The seventh and final is the public benefit provided from the use of water. Such benefits include purposes such as domestic uses, traditional and customary practices such as taro cultivation, aquaculture uses, irrigation and other agricultural uses, power development, and commercial and industrial uses. Staff believes that it is appropriate for the valuation to consider public benefits or public purposes where water used for those purposes should not be valued as highly as purely commercial uses. The most significant priority with greater weight and accordingly a larger reduction in value should be given when public trust uses are included in the lease such as domestic use and activities such as taro cultivation. Secondary priorities would be uses of water that are consistent with State policies such as food sustainability and renewable energy. Finally, uses that primarily support economic development would receive minimal to no reduction in value.

Alternatives Considered

In developing the guidance, staff had numerous discussions with the CWRM and the Department of Hawaiian Home Lands (DHHL). DHHL has favored a valuation approach that would utilize a percentage of the avoided cost to the lessee of obtaining water from practicable alternative water sources. DHHL has justified this method as providing the most clarity and certainty in the appraisal process, which is lacking in staff’s proposed guidance. While staff appreciates DHHL’s position and the extensive time and effort DHHL staff contributed to addressing this issue, staff does not believe that the DHHL favored methodology is appropriate.

Staff believes that the DHHL methodology is more so a formula that is overly narrow and restricts an appraiser from relying on their knowledge and expertise in their determination of value. Additionally, applying such a strict, narrow criteria may result in significantly different valuations for similar uses of water. It is foreseeable that there could be parties that use equivalent amounts of water for similar purposes but have different alternative water sources due to a reliance on external factors that are not related to the actual use of water. For example, one user may be able to obtain water from a catchment system or by truck delivery while another user may have no option to drill a well, which would result in very different values for a similar water use.

DHHL has noted that a lessee could recoup costs by passing them on to consumers. Staff believes that this would negatively impact efforts to progress in priorities such as food sustainability and renewable energy. Smaller agricultural users with a limited customer base may exit the market if their customers opt not to pay a higher price for their products. Additionally, due to regulatory requirements, hydropower projects may not be able to simply pass the higher costs to ratepayers.

Another alternative staff considered was to establish a value for water that is consistent with other markets in the United States. This would require the Department to contract for the services of an appraisal firm outside of Hawaii with experience in the valuation of water rights in the mainland United States. During staff's preliminary research, it appears that the most active market for water is in the western United States, particularly California, as determined by the volume of water rights transactions. This has led to the establishment of the Nasdaq Veles Water Index, which sets a price for water in California as a commodity, independent of delivery costs. Aside from market transaction data, the index also considers conditions that affect supply. For example, drought conditions may result in raising the index price.

However, while this may be the most economically defensible alternative, implementing a similar approach in Hawaii may be problematic, as water is a public trust resource and not a private property interest subject to market conditions. Although the intent of HRS 171-58 may be to treat water as an economic unit for the purpose of a lease, there are public trust obligations and regulatory requirements that prohibit complete commodification as in other markets. Furthermore, the current index price for water, which is set per acre foot, is \$860.69, or approximately equivalent to \$2,641.36 per million gallons.³ This would likely price most if not all water users out of the market and require a statutory fix, resulting in an indefinite delay to staff's efforts to convert revocable permits to water leases.

In conclusion, staff believes that valuing water by considering multiple factors would provide the appraiser the flexibility to address the unique circumstances of a particular water use. While that may not provide the level of certainty and predictability favored by DHHL, staff's position is that this is the most comprehensive approach to valuing water that addresses obtaining a fair return to the State for the use of a public trust resource, supporting policy priorities and achieving sustainable resource management.

³ One acre foot is equal to 325,851 gallons.

RECOMMENDATION:

That the Board:

1. Approve staff's proposed guidelines to appraisers to determine the appropriate public actions for water fees for consumption or purposes pursuant to Section 171-58, Hawaii Revised Statutes.

Respectfully submitted,



Ian Hirokawa
Special Projects Coordinator

APPROVED FOR SUBMITTAL:



Suzanne D. Case, Chairperson *et*

Land Board Meeting: October 22, 2021; D-8: Approved as amended.

Approved as amended. The Board amended the submittal: (i) on page 2, second full paragraph by rephrasing the statement that says "it would be appropriate to use the current renewable permit rent as a starting value" to "the appraiser may consider using the current renewable permit rent in its valuation and analysis"; and (2) striking the 7th factor of public benefit in the appraisal analysis.