



Long-Term Drought Lease Pilot Program

Introduction and Background

The Washington Legislature amended chapter 43.83B RCW in 2020 to improve the state's resilience to future drought conditions and directing Ecology to conduct a pilot study of long-term lease agreements for leasing water rights during drought:

(1) The department shall initiate a pilot program in a selected basin or basins to explore the cost, feasibility, and benefits of entering into long-term water right lease agreements. The purpose of the agreements is to alleviate water supply conditions that may affect public health and safety, drinking water supplies, agricultural activities, or fish and wildlife survival. Under this program, the department is authorized to negotiate and enter into contractual agreements before a drought emergency is declared under RCW 43.83B.405(2) that identify projects, measures, sources of water, and other resources that may be accessed during times of water shortage. Water right changes executed under agreement under this section are subject to the requirements of RCW 90.03.380.

(2) The department shall submit a report to the legislature by December 31, 2024, on the results of the pilot program. The department shall include a summary of the contracts entered into pursuant to this section and recommendations to the legislature.

Long-term lease agreements are a novel approach to improving water supply resilience. These agreements allow water right holders to continue using their water as usual until the agreement is activated by a drought declaration or other trigger. Once activated, Ecology would pay for the water right holder to forgo irrigation. The unused water then remains available to support other instream or out-of-stream needs. Once the low flow conditions end, the water right reverts back to the water right holder. This process could then be repeated as needed over the length of the agreement.

Agreements of this kind are useful because they allow Ecology to identify sources of water to support instream flows well in advance of an actual drought emergency. Once a drought does occur, it provides certainty that an alternate water supply is available to boost streamflows or address other water supply needs. This tool is more responsive than a single season drought lease because it can reduce the delays created by needing to find potential water right holders willing to lease their water rights and developing lease agreements during a drought.

This report presents the summary of project work and findings of Ecology's Water Resources Program for future applications of long-term drought lease agreements.

Approach

Ecology identified two types of long-term contractual structures applicable to this project:

- A **contingent contract** is a long-term agreement for the lease of water during individual water years based on a triggering condition or conditions. This triggering condition could be based on real-time factors (such as real-time streamflow gauging), regional water supply forecasts (e.g., the contract is triggered when water supply is forecast to be below 70% of normal for that year), or Ecology's declaration of a drought emergency. For the purposes of this pilot program, we decided that watershed-level water supply forecasting for low-flow periods would likely provide the most useful contingency threshold.
- An **option contract** is a long-term agreement for the lease of water during individual water years based on an opt-in by one or both parties to the contract. Each year, the contracting parties with options must decide by an agreed-upon deadline whether they intend to exercise their option for the use of the water. For the purposes of drought leases, where reliability of the contracted water for lease availability is paramount, the preferred option contract approach was a lessee (Ecology) option, where Ecology would decide whether to exercise the option each year.

Payment structures for contingent and option lease contracts vary, but typically would involve two types of payments. Ecology, as the party paying for the use of the water, is considered the *lessee*. The water right holder receiving payment for Ecology to use the water is the *lessor*.

- First, Ecology would offer the lessor a premium payment to sign the contract. This is known as an *option consideration* in option contracts. This premium could be paid either as a one-time payment or annually, depending on the lessor's preference.
- Ecology would then pay an additional fee to the lessor when the option or contingency to execute a single-season lease is exercised.

For the purposes of this pilot program, we decided that development of option contracts would be simpler and more attractive to water right holders. Ecology contracted with a non-profit organization, Trout Unlimited, to implement the option contract pilot project.

Outreach

In order to conduct pilot program outreach, Ecology partnered with Trout Unlimited to use their ground-level relationships with water right holders. Trout Unlimited staff developed a template option contract for drought leases for use in negotiations and conducted outreach with agricultural water right holders in 2020 (See Appendix A for the template agreement). Outreach focused on holders of senior agricultural water rights to maximize the benefit to instream resources from foregoing diversions.

The project team identified two watersheds with existing outreach resources to conduct the study:

- The Yakima River basin was selected due to existing local relationships with water right holders and regional interest in creative water solutions. It has existing instream flow management that would protect leased water for instream use. Additionally, we anticipated that the large amount of water right leases already occurring in the area could lead to greater interest in a new approach to leasing.
- The Methow River basin was also selected due to existing local relationships with water right holders. Like the Yakima River basin, it has existing instream flow management that would protect leased water for instream use. Finally, given the severity of low-flow conditions in the Methow watershed, we anticipated that any additional drought leases could provide substantial benefit to aquatic habitat.

Findings

Ecology struggled to identify any water right holders interested in leasing their water rights through a long-term lease agreement due to two factors:

1. Direct outreach and development of long-term lease agreements stalled in 2020 due to the Covid-19 epidemic and never recovered. Social distancing requirements and pandemic anxiety made it difficult to engage with water right holders during much of the period of this program.
2. Ecology declared droughts in 2021, 2023, and 2024, which diverted focus from drought lease options to drought emergency response.

In addition to limitations on outreach imposed by the Covid-19 pandemic, project outreach failed to generate interest among water right holders for several reasons:

- Many water right holders did not want to commit to a long-term agreement that would intermittently interrupt their own use of their water rights. Feedback indicated that water right holders prefer to lease their water rights outright (e.g., a five-year continuous lease of water rather than a five-year option lease where water *may* be leased for shorter periods of time).
- Variability of payment structures made it difficult to communicate the potential benefits of contingent and option contracts relative to standard lease payment structures. Water right holders preferred the certainty of up-front payment to the uncertain potential for additional payments over the term of the agreement.
- Senior water right holders expected to be able lease their water rights on a year-by-year basis for greater value than through a long-term contract.

Ecology and Trout Unlimited believed that these issues could be overcome through continued outreach, relationship-building, and education about the possible benefits of option or contingent leases. Negotiations for water right transactions are complicated and generally require years of development. As a result, there may be future opportunities to apply this tactic.

We also struggled to identify a suitable operational structure for an agreement due to irreconcilable timing factors. Irrigators need to make decisions about their agricultural operations in January or February. However, water supply forecasts are generally unreliable before April. As a result, we would not be able to make an informed decision to exercise an option early enough in the water year. A significant advance in the predictive power of water supply forecasts is likely needed to develop a usable option agreement in either of the study basins.

In specific circumstances, long-term water right lease agreements may be more viable where late season leases would provide benefits to water supply conditions. For example, an irrigator may agree to forgo irrigation after mid-summer and accept a reduced number of hay cuttings. Recent work on short-term leases of this kind in the Dungeness River basin has indicated that this type of arrangement has the potential to be suitable for longer-term agreements. Overall, this tool would be most useful where the timeline needed by irrigators to make business decisions aligns more closely with certainty in the water supply outlook.

Conclusion

The drought lease pilot program did not lead to the execution of any long-term drought lease agreements during the duration of the pilot program. This type of lease structure was not found to be appealing to agricultural water right holders in the watersheds studied by this project.

However, negotiations for water right transactions are complicated and generally require years of development. As a result, there may be future opportunities to apply this tactic. Therefore, Ecology intends to continue exploring possible applications of long-term drought lease agreements as part of our broader development of drought response activities.

Appendix A – Template Long-Term Drought Lease Agreement

OPTION AGREEMENT FOR DROUGHT-YEAR LEASE OF WATER RIGHT

THIS OPTION AGREEMENT FOR DROUGHT-YEAR LEASE OF WATER RIGHT (hereinafter “this Option Agreement”) is made and entered into this ____ day of _____, 20__ (“the Effective Date”), by and between the Washington Department of Ecology, (hereinafter referred to as “Ecology”) and _____ (hereinafter collectively referred to as “Water Right Owner”).

RECITALS

A. WHEREAS, Ecology, pursuant to RCW 43.83B.450(1), has the authority to enter into long-term water lease agreements with water users in select basins prior to drought to access water during water shortages; and

B. WHEREAS, Water Right Owner is the owner a legally established water right, more fully described in Exhibit A attached hereto and incorporated by this reference (the “Water Right”);

C. WHEREAS, the Water Right authorizes use of water from the _____ River under Water Right Certificate Number _____; and

D. WHEREAS, the Water Right was confirmed for irrigation of __ acres of land from _____ through _____ annually at a diversion rate of __ cubic feet per second (“cfs”) and __ acre-feet per year (“af/y”). The Water Right has a priority date of _____, ____; and

E. WHEREAS, the authorized point of diversion for the Water Right is located _____; and

F. WHEREAS, the Water Right is appurtenant to real property in _____ County, more specifically described as _____ County parcel number _____ (“the Property”), and more fully described in Exhibit B attached hereto and incorporated by this reference; and

G. WHEREAS, Ecology wishes to secure the ability to lease the Water Right from the Water Right Owner in years when certain drought conditions are present; and

H. WHEREAS, Water Right Owner wishes to provide Ecology with the option to lease the Water Right when certain drought conditions are present.

Agreement

NOW, THEREFORE, in consideration of Ten Dollars (\$10.00) and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Ecology and Water Right Owner agree as follows:

1. **Option.** Water Right Owner grants to Ecology an exclusive and irrevocable option to lease the Water Right upon the terms and conditions set forth in this Option Agreement (the “Option”).

2. **Term.** The term of the Option shall commence on the Effective Date and continue through _____, 20__ (“Option Term”).

3. **Option Consideration.** *[What is your option consideration going to be? Are you going to pay a nominal amount to secure the option and pay the lease amount if and when you exercise the option, or are you going to pay a larger amount to entice the water right owner to consider this transaction approach?]*

4. **Contingency to Exercise -- Change Application.** In order for Ecology to use the Water Rights for Ecology's intended purposes, the Water Rights must be changed to include instream flow as purpose of use for the Water Rights for years that Ecology exercises its Option and leases the Water Right. Ecology and Water Right Owner agree that changing the Water Right to allow for Ecology's intended must be completed prior to Ecology being able to exercise its Option. To accomplish these changes, within fifteen (15) days of the Effective Date, Ecology will prepare and deliver to Water Right Owner one or more counterpart applications (collectively, "the Change Application"), in the form prescribed by Ecology, for the change the Water Rights pursuant to this Agreement. Within fifteen (15) days of receipt of the Change Application, Water Right Owner shall duly sign all counterparts of the Change Application and deliver to Ecology all of the original signed counterparts of the Change Application.

4.1 Cooperation on Change Application. Water Right Owner and Ecology agree to provide to each other, when requested, any and all documents, records, or other information they each may need to facilitate and accomplish the Change Application when requested by the other party.

4.2 Costs Associated with Application Process. Water Right Owner is not required to pay any costs associated with the Change Application or its approval by Ecology. However, Water Right Owner will cooperate with Ecology in all aspects of the Change Application process and will allow Ecology to defend any objections. If the change decision issued by Ecology is appealed by a third party, Water Right Owner has the right to terminate this Option Agreement, but Water Right Owner shall provide Ecology written notice of Water Right Owner's termination within ten (10) days of receiving notice of a third-party appeal.

4.3. Ecology Responsible for Completion of Application Process. The Change Application and all matters necessary for final approval and satisfactory resolution of all appeals of the Change Application shall be at Ecology's control; provided, however, Water Right Owner shall cooperate with Ecology or assigns, and shall not object to the Change Application.

4.4 Ecology Not a Guarantor of the Water Rights. Water Right Owner recognizes that part of the Change Application process requires Ecology to make a tentative determination of the extent and validity of the Water Right. Water Right Owner also recognizes that Ecology, in processing the Change Application, will follow certain statutes and administrative code provisions. In addition, Water Right Owner recognizes that in applying the statutes and administrative code provisions, Ecology interprets the statutes and administrative code provisions in a manner that is subject to certain statutory and administrative appeal rights. Ecology's processing of the Change Application may result in all or part of the Water Right being determined to be relinquished. Water Right Owner agrees to assume the risk of all or part of the Water Right being determined to be relinquished and agrees to hold the Ecology harmless from any and all damages, including but not limited to loss of water or property rights, which may occur as result of the transfer process.

4.5 Contingency Deadline. Ecology and Water Right Owner agree that the contingency described in paragraph 4 shall be satisfied, removed or waived as provided herein on or before *[April 1, 2021]*, or this Option Agreement shall become null and void.

4.6 Refund of Option Consideration. *[Need to decide whether Ecology wants a refund of Option Consideration if the contingency isn't satisfied in time. In my opinion that decision is most likely based on whether the Option Consideration is nominal or substantial, with Ecology seeking a refund if it is substantial.]*

5. Trust Water Right Program During Lease. *[Need to determine the mechanism for "holding" the Water Right in TWRP during lease period. While the Change Application would authorize instream flow and as an additional beneficial use, Ecology Policy 1210 says that ACQ doesn't apply when instream is the beneficial use and Ecology "holds [the leased Water Right] in the Trust Water Rights Program (TWRP) for the purposes of enhancing instream flows." Since the water right won't be used for instream flow or in the TWRP during the years that Ecology doesn't exercise the option, Ecology needs to create a mechanism to hold the water right in the TWRP during the years in which it does exercise the option. One pathway is to have a Trust Water Right Agreement signed that lays all of this out and covers the entire Option Term. Another is to have Ecology issue a letter that the water right is being held in the TWRP when Ecology exercises the Option.]*

6. Exercise of Option. Ecology's goal in securing the Option is have the right to lease the Water Right from Water Right Owner for Ecology's drought relief purposes in any year during the Option Term when the following drought conditions exist: *[(a) a year, or a portion thereof, when the water supply for the Yakima River Basin is below seventy-five percent of normal, as confirmed by the Bureau of Reclamation, and "junior" (post-1905 priority) water rights are pro-rationed or curtailed, or (b) a year in which the State of Washington declares a drought in all or part of the Yakima River Basin pursuant to WAC 173-166-060.]* Once the contingency in paragraph 4 has been satisfied, removed, or waived, exercise the Option, Ecology must provide the Water Right with written notice of their intent to exercise the Option in accordance with the provisions of Paragraph 12 hereof within the time periods specified in Paragraph 2 above ("Notice of Exercise"), no later than *[March 15]*.

7. Rolling Option. Ecology's exercise or non-exercise of the Option during any one year of the Option Term does not affect Ecology's ability to exercise the Option in a future year during the Option Term and the Option shall remain valid throughout the Option Term. Ecology shall have the sole discretion and right to exercise the Option during any year of the Option Term.

8. Lease Payment. If Ecology exercises the Option, Ecology will pay Water Right Owner _____ Dollars (\$ __.00) per acre or a total of _____ Dollars (\$ _____00) (\$xxx.00 per acre times __acres) ("Lease Payment") in each year that Ecology exercises the Option during the Option. The Lease Payment is payable in cash within fifteen (15) days of *[Notice of Exercise, proof of non-use at the end of season, or other trigger.]*

9. No Relinquishment or Abandonment. To the best of Water Right Owner's knowledge, the entire Water Right has been put to beneficial use during at least one of the last five years preceding the Effective Date and no period of five consecutive

years of partial or total nonuse of the Water Right in the past five (5) years. Furthermore, to the best of Water Right Owner's knowledge, no portion of the Water Rights has been intentionally unused sufficient to constitute abandonment under Washington Law.

10. Agreement Not To Divert and Not Irrigate. If Ecology exercises the Option, Water Right Owner hereby agrees to not divert any water under the Water Right and to not irrigate the Property during the years in which Ecology exercises the Option and leases the Water Right.

11. Temporary Easement for Monitoring. Water Right Owner hereby grants and conveys to Ecology, its employees, agents, and successors, at all times during the Option Term, access to the diversion point for the Water Right and the Property. Access will be used solely for the purpose of allowing Ecology to monitor and enforce the covenants contained in this Option Agreement regarding the cessation of the diversion and fallowing of the Property during the years Ecology exercises the Option in the Option Term. Ecology will provide Water Right Owner with reasonable notice prior to accessing the diversion point or the Property.

12. Execution of All Documents. Ecology and Water Right Owner, individually and severally, hereby acknowledge that the execution of all documents associated with this transaction will substantially affect their legal rights and that each has the opportunity to obtain and consult with independent legal counsel for the purposes of this transaction and matters relating thereto.

13. Attorneys' Fees. If either party hereto is required to retain an attorney to enforce any provision of this Option Agreement, whether or not a legal proceeding is commenced, the substantially prevailing party shall be entitled to reasonable attorneys' fees regardless of whether at trial, on appeal, in any bankruptcy proceeding, arbitration matter or without resort to suit.

14. Governing Law and Venue. This Option Agreement shall be interpreted, construed and enforced according to the laws of the State of Washington and venue shall be in _____ County, Washington.

15. Notices. Subject to the requirements of any applicable statute, any notices required or permitted by law or under this Option Agreement shall be in writing and shall be (i) personally delivered, (ii) sent by first class certified or registered mail, return receipt requested, with postage prepaid, or (iii) dispatched by facsimile transmission (accompanied with reasonable evidence of receipt of transmission and with a confirmation copy mailed no later than the day after transmission) to the parties' addresses set forth above. Either party may change such address for notice. All notices which are so addressed and paid for shall be deemed effective when personally delivered, or, if mailed, on the earlier of receipt or two (2) days after deposit thereof in the U.S. mail.

Any notice or communication required by this Agreement between Ecology and Water Right Owner shall be given to the addresses set forth below:

Ecology:

Water Right Owner:

16. **Section Headings.** The word or words appearing at the commencement of sections and subsections of this Option Agreement are included only as a guide to the contents thereof and are not to be considered as controlling, enlarging or restricting the language or meaning of those sections or subsections.

17. **Invalidity.** In the event any portion of this Option Agreement should be held to be invalid by any court of competent jurisdiction, such holding shall not affect the remaining provisions hereof unless the court's ruling includes a determination that the principal purpose and intent of this Option Agreement are thereby defeated.

18. **Legal Relationships.** The parties to this Option Agreement execute the same solely as a lessor and optionee. No partnership, joint venture or joint undertaking shall be construed from these presents, and except as herein specifically provided, neither party shall have the right to make any representation for, act on behalf of, or be liable for the debts of the other. All terms, covenants and conditions to be observed and performed by either of the parties hereto shall be joint and several if entered into by more than one person on behalf of such party, and a default by any one or more of such persons shall be deemed a default on the part of the party with whom said person or persons are identified. No third party is intended to be benefited by this Option Agreement. Any married person executing this Option Agreement hereby pledges his or her separate property and such person's and his or her spouse's marital communities in satisfaction hereof.

19. **Assignment; Successors.** Neither Ecology or Water Right Owner may sell, transfer, assign, pledge or encumber its interest in this Option Agreement without the prior written consent of the other party, which consent shall not be unreasonably withheld. A purported sale, transfer, assignment, pledge or encumbrance without prior written consent of the other party shall be null and void and of no force or effect. Subject to the restrictions contained herein, the rights and obligations of Ecology and Water Right Owner shall inure to the benefit of and be binding upon their respective estates, heirs, executors, administrators, successors, successors-in-trust and assigns.

20. **Entire Agreement.** All understandings and agreements previously existing between the parties, if any, are merged into this Option Agreement, which alone fully and completely expresses their agreement, and the same is entered into after full investigation, neither party relying upon any statement or representation made by the other not embodied herein. This Option Agreement may be modified only by a written amendment executed by all parties.

21. **Interpretation.** This Option Agreement has been reviewed by both parties and each party has had the opportunity to consult with independent counsel with respect to the terms hereof and has done so to the extent that such party desired. No stricter construction or interpretation of the terms hereof shall be applied against either party as the drafter hereof.

22. **Counterparts.** This Option Agreement may be executed in counterparts, each of which shall be deemed to be an original instrument. All such counterparts together shall constitute a fully executed Agreement. Facsimile transmission of this

Option Agreement and retransmission of any signed facsimile transmission shall be the same as delivery of an original.

23. Amendment. This Option Agreement may not be modified or amended except by the written agreement of the parties.

IN WITNESS WHEREOF the parties have signed and delivered this Option Agreement as of the Effective Date.

ECOLOGY:

WATER RIGHT OWNER:

By:

By:

Title: _____

Title: _____

Date: _____

Date: _____

ACKNOWLEDGEMENTS

State of Washington

County of _____

I certify that I know or have satisfactory evidence that _____ is the person who appeared before me, and said person acknowledged that she signed this instrument, on oath stated her authority to execute the instrument as the authorized agent for Ecology, to be the free and voluntary act of such entity for the uses and purposes mentioned in the instrument.

Dated: _____

Name: _____

NOTARY PUBLIC for the State of _____,

residing at _____

My appointment expires: _____

State of Washington

County of _____

I certify that I know or have satisfactory evidence that _____ is the person who appeared before me, and said person acknowledged that they signed this instrument and acknowledged it to be their free and voluntary act, for the uses and purposes mentioned in the instrument.

Dated: _____

Name: _____

NOTARY PUBLIC for the State of _____,

residing at _____

My appointment expires: _____

Exhibit A: Water Rights

Exhibit B: Property