

Well Share Agreements – the Good, the Bad, and the Ugly

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ABSTRACT:

In order to meet the demand for new homes at an affordable price, a common mini-development plan in place today consists of purchasing a 5 to 10 acre parcel of land and splitting it up into several smaller lots. The small time developers who are promoting these home sites will then have one “Exempt” domestic water well drilled to serve all the lots in the split. The total number of lot splits can vary, however it's usually intended to be less than the maximum number of lots that can be served without the water system coming under the ADEQ's regulation. The mini-developer then dedicates the water well and all equipment to the new lot owners. The resulting water service system then becomes a loose knit association of people sharing a single exempt water well, managed by one of the lot owners. The water system manager, typically elected by default, has little to no experience managing water systems. As a result, somewhere down the road well maintenance is required on the system and the collective well share parties are not prepared for the problems, or the expenses. If there is not a properly written and recorded well share agreement in place to manage the issues that can arise during the life of the well system, then the little house of cards begins to crumble. This presentation will illustrate with real world examples what triggers these collapses and exposes weaknesses in some well share agreements.

EXPERIENCE HAS SHOWN THAT:

From my earlier experiences as a water well & pump contractor, and now as a water well inspector for real estate transfers, I have seen quite a few well share agreements. Some agreements I would describe as pretty good documents, some as bad, and some as just outright ugly. The strength or weakness of the well share agreement depends on the details of the wording within it. The addition or omission of just a few words in a well share agreement can make a big difference in the effectiveness of the document.

I have held two very different perspectives when working within the terms of these agreements. The first was from the perspective of a well and pump contractor who performed work on the shared water system. As a contractor, I needed to know who had the authority to authorize my services, and most importantly, who would make the payment after the work has been completed. As a water well inspector representing the buyer, I look for, and note, what words and clauses might be a cause for concern as they invest in this property, and become subject to the well share agreement.

AUTHORIZED WATER SYSTEM MANAGER

A good well share agreement document names the association's manager, and defines his or hers authority, and responsibilities. A good document also spells out the duration of the manager's office, list his or hers contact information, and even defines how replacements are to be elected. There should also be an individual who is second in command if the manager is unreachable or not able to perform the designated duties.

A good well share agreement also names the treasurer, or money handler, for the association. It also defines the treasurer's authority to open a checking account deposit the monthly incomes. A well written well share agreement also sets out the instructions on how to manage the association's funds. It should also prescribe the Treasurer's authority for payment of invoices that have been authorized and approved by the system's manager. Experience has shown that it seldom works out this way?

In the past I would receive a telephone call from a member of the system reporting a water outage. Typically the caller was a stay at home mom who had a sick child in the house and horses in the back yard. She had to have water, and she had to have it soon. If I had not worked on this system before, I would ask for the name and phone number of the water system manager. I might get a phone number, but I would either get no answer or find out the manager was out of town for the week. Who's the next in command with the authority to authorize repairs to the system, I would ask? That was often the trigger in a poorly written well share agreement. No one with authority to authorize repairs was reachable when major problems develop, and it dramatically delays the well and pump contractor getting started on making repairs.

In the real world situation, I would typically go ahead and do the repair work, put the mom, kids, and horses back in water, and then ask the question, who's got the check book to make the payment for our services? Always in the back of my mind was a question, "does the Co-Op have sufficient funds to cover the expense of these repairs"? This may not

sound like an issue to everyone, but to the contactor who performs the work it certainly is. So if there are no provisions in the agreement to name the manger, and an emergency back-up manger, then from my perspective that well share agreement can only be described as “Bad.”

Secondly, if the Co-Op bank account has insufficient funds to cover the total cost of the essential repairs, then who was going to make up the balance? From what I saw, deficiencies in Co-Op banking accounts were most frequently caused by members who hadn't been paying their fair share in past months? A contractor should not have to wait for his payment for services until these members are current. A good well share agreement has provisions for dealing with tardy and absentee member nonpayment in order to keep the Co-Op in good health. An even better one has a specified plan for covering expenses in excess of currently available funds. If the contractor isn't paid within a reasonable amount of time, he can begin the Contractor's Lien filing process against the Co-Op.

WELL LOCATION IS CRITICAL:

A critical item of note for me as a water well inspector representing a buyer is: whether or not the well is located on one of the well share owner's land, or is it located on a separate parcel of land, belonging to all parties involved. Obviously the preferred arrangement is for the water well, storage tank, booster pump and all the associated equipment to be located on a separate parcel of land that all lot owners share an equal and undivided interest in.

On this separate parcel of land should be located a separate electrical power meter in the name of the well share Co-Op. Too many times I have seen where the electrical service meter is in the name of the first person to purchase a lot in the wild cat development and in some cases, it services their house as well. I have seen where disputes arise over how much of the electrical bill is for the shared water plant, and how much is the responsibility of the home owner with the power meter. Nothing good comes of such arrangements when one person has the responsibility of dividing up the power bill and separating out their personal use from that of the Co-Op's.

If the water well is located inside the property boundaries of one of the parties to the well, then there must be dedicated easements for ingress and egress for each of the others. Without an easement of record, other parties to the agreement would have no right to trespass onto the land where the well is located.

I ran into one of these situations while performing an inspection for a buyer of one home on a shared well. I was caught on site by the land owner while inspecting the water well. He informed me that he owned the land, and the well, and only provided water to the other properties for a monthly consideration. He explained that no one had a right to enter his property and inspect, or service, the well except him. He didn't realize it but at that moment he had just declared that he was operating a private water company, and selling water, not sharing a well. That's just exactly what I reported to the buyer. I should have reported him to the ADEQ, but I didn't. The water sharing agreement he had with the other lot owners has to be described as "Ugly".

SHARING THE COSTS

I have seen well share agreements where splitting the cost of operating the water system among several home owners was done on a monthly flat rate basis. This is an operating system where each member pays the same amount for their water, regardless of how much they use. This form of billing system is necessary because the well share members are not metered individually and billed for the actual amount of water use. This cost saving system design is a major oversight made by small time developers during the original system construction. The small cost savings leads to mini water wars later on. Properly prepared well share agreements have explicit wording in them to designate a separate co-owned well site, a separate power meter for operating the water plant, and individual water meters for each member.

This is an essential consideration that must be contained in the original water system construction arrangement. The wording of the well share agreement must define this arrangement and designate one of the lot owners as the responsible party to read the water meters monthly and generate individual water bills based upon consumption of water, and pro-rated electrical service, plus any maintenance cost incurred during the past month, i.e. weed control, water quality testing, equipment servicing etc.

Probably the most sensitive trigger for members of the shared water well system is the issue of just and appropriate payment. No one wants to pay for something they didn't get, nor do they want to pay for someone else's water service. I investigated and repaired

one situation where a particular home owner left the water running for a week while he went on vacation. The system was drained and a booster pump was burned up due to running dry. This triggered the question, was it fair to ask for all the well share owners to split the costs of this unnecessary repair bill? If the well share agreement document isn't structured to handle situations such as this, then perhaps they should have regular meetings and allow members an opportunity to express their views and resolve issues surrounding billing procedures.

PROVIDING QUALITY WATER

At present, water system with more than 15 connections, and/or 25 individuals being served water for more than 60 consecutive days are technically subject to the authority of the Arizona Department of Environmental Quality. Most of the systems referred to in this paper and presentation could fall under ADEQ's authority, however, they are not presently registered with them. They do not have an ADEQ Certified Water Plant Operator taking care of their system who is taking periodic water quality samples. What liability this presents to the designated Co-Op manager is an issue for other presenters in this seminar to address. From my perspective I would not want to be the default manager of a water system that is not monitoring water quality on a regular basis.

I can attest to the fact that water quality is becoming an increasingly important issue with today's buyers. The media has indoctrinated us with countless stories of the horrible consequences of drinking contaminated water. The result has been increased

awareness of buyers to water quality, and institutional lenders who have specified certain water quality tests prior to funding. When it comes time for one well share owner to sell his well share the lender often requests a water quality sample. The question arises after I collect and have the sample analyzed, should this information be shared with the other share owners? What if the results indicate that there is a potential problem with the well's water quality. Do the other members have a right to be informed of the results? Or, should the Co-Op have already had this water quality information on file and make it available for all new well share owners? These are triggers to issues that are not typically covered in most well share agreements today. I anticipate that they will become bigger issues in the future as water quality becomes everyone's concern.

LESS THAN ADEQUATE SERVICE

I have found that most of these split lot shared water well systems are living with little or no legal claim to adequate water services into the future. The well share document that buyers are given, or sometimes not given but just referenced during a transfer of a vacant lot, give the buyer the impression that adequate water service will be available for them forever. In the real world, this will not always be the case.

As stated in my opening remark, in order to meet the demand for new homes at an affordable price, 5 to 10 acre parcels of land were often splitting it up into several smaller lots. Meeting the demand for affordable land is what drives the small time developer to initiate the sequence of events that brings us to these issues of well share agreements. The

prospect that each purchaser of an original split lot can further divide his or her lot and reap the same benefits that that the mini developer will reap is a carrot that is often dangled in front of each buyer. This carrot has some serious consequences if eaten, however.

If each buyer has the right to further subdivide his lot and obtain the same well share water rights, then the total number of well shares can expand exponentially. A well share agreement document should clearly define whether or not a buyer has the rights to further subdivide. But long before this right is granted there should be some serious consideration as to whether the well, or more correctly the aquifer, can support future demands.

The “Assured and Adequate” water supply designations as required by Arizona law for platted subdivisions served by a public water system in Arizona do not apply to the type and size of Co-Op well share systems being discussed. This situation is leading to a number of well share Co-Op systems that are running out of adequate water for the total number of homes that end up on the system. When constructing the original well share agreements these mini-developers tried hard not to create any explicit or implied warranties as to the life of the well, or the aquifer. Lacking specific wording to the contrary, a badly worded well share agreement could, however, trigger future claims against the developer, the well driller, the pump installer, the home builder, and the Realtor.

An example of what I see happening today is that as the built-out condition of the mini developments are being reached, the last share holders to build a home are finding

that the system cannot support the additional demands. What worked fine for the first few home owners now falls short of meeting the collective demands. More well shares were authorized than the system and/or the aquifer can support. Some shortages can be cured with additional water system equipment like bigger storage tanks and additional booster pumps, others cannot.

The original water system equipment was probably purchased based upon the sole criteria of “lowest bidder”. Hence, the mechanical water system can meet only a fraction of the total peak demand of all share holders. The mechanical parts of the system were never engineered to meet peak demands. Almost as certainly the aquifer was never fully evaluated to see if it would meet the sustained demands of the mini-development. No one ever thought during the establishment of the well share arrangement that the aquifer may not support the total demand of the collective home owners for even twenty years.

What guaranteed rights to water service do the individual lot owners of any well share agreement have? This question is seldom considered in the reading of a well share agreement by a purchaser. Another question is when the Co-Op can no longer deliver adequate water service, is it the responsibility of the collective owners to step up and invest in expanding the system to accommodate the newest member? If the inability to meet the demand is a depleted aquifer due to past demands on this system, plus the demands of the neighboring systems, plus the lack of recharge, than the necessity to drill deeper looms as a very expensive trigger.

FEWER OPTIONS IN THE FUTURE

There will be countless well share Co-Ops where drilling the existing well deeper may not be an option. Many of the “Exempt” water wells that were drilled to form these mini- developments were drilled and cased with 4 ½ to 5-inch diameter PVC well casing set in a nominal 8-inch diameter borehole. Most water well drill pipe today measures 4 ½-inches in outside diameter and therefore cannot be used to drill inside these well casings. A new borehole must be drilled and a replacement well must be constructed.

The problem will be that the original document provided for only a thirty foot by thirty foot well site for the original water well and all related equipment. There is no room left on the original well site for the drilling a replacement well. When drafting the original well share agreements, mini-developers don’t anticipated how much room modern well drilling equipment needs to construct a well twenty years in the future. This is a common problem that was created in the past that has simply been deferred to the future well share owners.

Another reason that drilling deeper may not be a solution to ultimate peak water demands could be a hydro-geologic reason. Not all aquifers have infinite depths. The location of the particular Co-Op that shares a given well determines whether or not more water can be found at a greater depth. I can foresee where in the not so distant future a number of well share Co-Ops will be faced with little or no options to maintain their water supply. The expense of obtaining a new or replenishment water source will likely trigger claims against the developers and builders of these systems.

HEAD OFF FUTURE PROBLEMS BEFORE THEY START

Avoiding the pitfalls that make a well share agreement ugly begins with the conceptual model used by the original developer. It's important for the developer to set up the ownership of the water system to be self sustaining. In order to do this, an essential component of the design is to establish a name for a not-for-profit well share association. Once named and formed, it is essential that the powers of the managing parties be clearly defined. Substitute and permanent replacements for authority positions should also be spelled out in the original document. A separate well site property, apart from the individual lot owners should be dedicated for the placement of the well and all associated pumping equipment. In areas where the aquifer may not meet the demands of the collective owners for at least fifty years, a separate parcel of land, should be set aside and dedicated for the drilling a future, and much deeper well.

Bills are being introduced in our state's legislature to amend the laws that allow mini developers to put home buyers in these situations with poorly formulated well share agreements and without adequate water supplies. Municipalities and counties in Arizona will be being given the authority to evaluate building plans to assure that the impact of the new growth will not adversely affect the groundwater resource. If fully implemented, these changes will have the same impact as the ADWR designation of having an "Adequate Water Supply" now has. These changes may apply to any property being split into as few as three lots.

Anyone who buys into an existing Co-Op well share system should ask what sort of guarantee is there that the system will continue to operate well into the future. Once one purchases their way into a Co-Op system, and typically the Co-Op water supply is the sole source of water for their property, then there are few options left to get out of a bad situation. If the aquifer can no longer support the demands placed on the system, and drilling deeper is not an option, then a well share owner can see their investment, and their equity, vanish.

The laws in place today regarding real estate sales and transfers with a private, or shared water supply, require that the seller disclose all issues related to their property. If there have been problems with the shared well then this fact must be disclosed. Most buyers today are doing their due diligence and investigating all aspects of shared water systems, including quantity and quality. And finally, provisions for amending a bad well share agreement should be incorporated into all documents that they might be transformed into a good one as various real world situations evolve.

SUMMARY

Well share agreements have been a way of life for many years, and many of them have worked quite well. There is no assurance that they will work well in the future. And the looming question may be: who will be held responsible for water shortages, and unacceptable water quality under the terms of the well share agreement?