

**American Bar Association
Section of Environment, Energy, and Resources**

**RiverBank:
Water Trusts in the Western United States**

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I. Introduction

It was a crisp fall day and I was heading over Cochetopa Pass from Saguache, Colorado to Gunnison, Colorado. I made the left-hand turn at the “Old Agency” sign, nosed my car south along the dirt road, and stopped. I opened my car door and stepped out, grasshoppers clack-clacking everywhere. I was in a high mountain valley—cattle country—overlooking a wide swath of land irrigated by a few ditches that pull water from a twisting, turning, tightly winding creek well-protected by willows, alders, and brush. And I was on private property.

I was also in the middle of a Colorado Division of Wildlife fishing easement covering approximately eight miles of three tributaries, all of which support wild trout. If you fish and you haven’t been to this area of Colorado, you are missing out. You are also missing out on a microcosmic example of a macrocosmic Colorado water challenge: the competition between consumptive water uses like irrigation and nonconsumptive uses like instream flows.

The State of Colorado has clearly recognized the importance of instream water uses in addition to more traditional water uses. The placement of an instream flow program in the hands of the Colorado Water Conservation Board (“CWCB”) in 1973 was its clearest pronouncement.¹ Yet, the commitment to instream flows is young, as are many of the water rights that the CWCB has secured to protect Colorado’s streamflows.² As a result, more work to balance consumptive uses like irrigation and the needs of aquatic ecosystems must occur. This sentiment—heard

¹ See generally § 37-92-102(3) & -102(4), C.R.S. (2008) (setting out the parameters of Colorado’s instream flow program).

² Jerd Smith, *State’s Money in the Banks*, ROCKY MOUNTAIN NEWS, Sept. 15, 2008, at 5.

around the West a bit louder and more often lately—has fueled the rate at which water trusts are springing up in many prior appropriation states. Most—if not all—water trusts have been formed to protect and enhance streamflows by using market-based, voluntary, cooperative transactions that put older, more defensible water rights back into streams for the benefit of aquatic ecosystems, the flora and fauna that depend on them, and the people who enjoy them.

The topic of this twenty-seventh meeting of the American Bar Association’s water group, *Change in the Midst of Constants: Adapting Water Law to Meet New Demands*, is particularly apropos when discussing the water trust movement. It is a movement premised on the notion that the tools necessary to improve streamflows already exist in the western state-by-state water allocation systems, that “change”—one from an outdated maximizing-diversions paradigm to a newer one of maximum use that includes instream uses such as recreation, piscatorial, and aesthetic uses—can be achieved within the “constants” of western water law.

This paper begins with a description of water trusts generally. It then describes in detail Colorado’s instream flow program, a discussion that necessarily includes a description of the CWCB and the role the Colorado Water Trust (“CWT”) plays in the context of the state’s instream flow program. It then examines the challenges and opportunities facing the effort to improve instream flows statewide. The paper concludes with the idea that, while using water transactions to improve Western streamflows is not a panacea to solving the tension between diversions and aquatic ecosystem needs, working to create an active instream flow transaction market is a step in the right direction—and an important one.

II. What is a Water Trust?

For well over a century, the prior appropriation doctrine has determined how water is allocated in the Western states.³ Based on the principle of “first in time, first in right,” prior appropriation allows the first person who puts water to a beneficial use a right to continue that use without interference from those who began using water later.⁴ The doctrine historically (and arguably, so some say) required that to obtain a defensible water right, one had to remove water from the stream system through a diversion.⁵ Primarily during the summer peak growing season, but also at other times of year, these legal water withdrawals stress the flow levels in

³ JAMES N. CORBRIDGE & TERESA A. RICE, *VRANESH’S COLORADO WATER LAW* at 3-7 (Rev. Ed. 1999) (describing the settlement of the West, the development of prior appropriation as the local custom for water allocation, and the formal adoption of the system in each of the seventeen mainland Western states).

⁴ *See id.* at 7.

⁵ Take, for example, recent and protracted litigation in Colorado over kayak courses (now called Recreational In-Channel Diversions or RICDs), which pushed the debate in Colorado regarding diversions and instream water use to its height. Those who opposed the idea that water rights that remained in the stream to be used for playboating in kayak parks (and other instream benefits) could constitute a defensible water right argued, among a litany of other arguments, that one was required to physically remove water from the stream in order to have a lawful water right. They argued that removal of water from its source as a requirement for a water right was a principle embedded in the prior appropriation doctrine. *See* Glenn E. Porzak et al., *Recreation Water Rights: “The Inside Story”*, 10 U. DENV. WATER L. REV. 209, 216 (2007) (discussing the opposition to Recreational In-Channel Diversions in the application for water rights of the City of Golden, Colorado in Case No. 98CW448 (Colo. Dist. Ct., Water Div. 1)).

stretches of many Western streams and rivers, forcing them to run critically low—and indeed sometimes dry—imperiling aquatic ecosystems.⁶

To mitigate these effects, every Western state maintains some form of instream flow program, a program that entitles water that remains in rivers to the same attributes of a diversionary water right, namely a defined volume, a place of use, a season of use, and a defensible priority.⁷ Some instream flow programs are nascent, some more established, but all seem to be ever-evolving.⁸

In addition to instream flow programs, the use of permanent sales or acquisitions,⁹ leases,¹⁰ soft-management solutions,¹¹ structural solutions,¹² and other incentive-based

⁶ For an example of a diversion structure that dries up a river in Colorado, see the photograph of the San Miguel River in Colorado at <http://www.coloradowatertrust.org/physical-solutions/detail/cccditch/>.

⁷ See, e.g., 1967 Minimum Water Flows and Levels Act, WASH. REV. CODE § 90.22.010 (2008) (“Establishment of minimum water flows or levels--Authorized--Purposes. The department of ecology may establish minimum water flows or levels for streams, lakes or other public waters for the purposes of protecting fish, game, birds or other wildlife resources, or recreational or aesthetic values of said public waters whenever it appears to be in the public interest to establish the same. In addition, the department of ecology shall, when requested by the department of fish and wildlife to protect fish, game or other wildlife resources under the jurisdiction of the requesting state agency, or if the department of ecology finds it necessary to preserve water quality, establish such minimum flows or levels as are required to protect the resource or preserve the water quality described in the request or determination. Any request submitted by the department of fish and wildlife shall include a statement setting forth the need for establishing a minimum flow or level. When the department acts to preserve water quality, it shall include a similar statement with the proposed rule filed with the code reviser. This section shall not apply to waters artificially stored in reservoirs, provided that in the granting of storage permits by the department of ecology in the future, full recognition shall be given to downstream minimum flows, if any there may be, which have theretofore been established hereunder.”); § 37-92-102(3), C.R.S. (2008) (stating that “[f]urther recognizing the need to correlate the activities of mankind with some reasonable preservation of the natural environment, the Colorado water conservation board is hereby vested with the exclusive authority, on behalf of the people of the state of Colorado, to appropriate in a manner consistent with sections 5 and 6 of article XVI of the state constitution, such waters of natural streams and lakes as the board determines may be required for minimum stream flows or for natural surface water levels or volumes for natural lakes to preserve the natural environment to a reasonable degree”).

⁸ For some indication of the range of ages of different Western states’ programs, it is helpful to note that an instream flow program was adopted in Washington as early as 1971, see <http://www.ecy.wa.gov/programs/wr/instream-flows/isfrul.html>, but in Texas not until 2001. See <http://www.twdb.state.tx.us/InstreamFlows/index.html>.

⁹ A sale is a permanent transfer of a water right for change to instream flow use. In Colorado, it requires separation of the water from the land and acceptance of the water by the CWCB. We at CWT can put together funding packages to buy the water, conduct any necessary engineering and other investigations including investigations into title, and will conduct the transaction with the CWCB. In some cases, we will also participate in a water court application to change the use of the acquired water to instream flows.

¹⁰ In Colorado, there are two options for leasing water to the CWCB. These are described in more detail *infra* Part IV. of this paper.

¹¹ These include alternatives such as changes in points of diversion, changes in source (e.g., a surface diversion to a well), and exchanges. Other approaches include innovative agricultural technology

approaches to streamflow enhancement are improving the way streamflows are protected and improved in Western states. These efforts—the everything-but-new-instream-flow-appropriation efforts—are being pursued by water trusts throughout the West. Water trusts, generally nonprofit organizations recognized as public charities under Section 501(c)(3) of the Internal Revenue Code, have been formed to help restore flows for existing habitat while working with water users to maximize the benefits of their water portfolios. They do this by encouraging voluntary, market-based transactions to put more senior, more defensible water back in stressed segments of rivers while offering at the same time an alternative to selling water to, say, municipalities or local development. Although some water trust work requires working within a state’s instream flow program, some does not.¹³ As described above, the tools used are as various as the location of each water right deal.

When considering water trust tools, one would be remiss in failing to mention that water trusts have drawn heavily from the institutional model of the private land conservation movement.¹⁴ Given that, their work is often described in shorthand as using tools that mirror the tools used in land conservation. But this description is, perhaps, too blunt an instrument to do the trick. A discussion about water trusts will wander into land conservation territory, to be sure, but only for a brief moment before moving into and spending most of its time lingering on points pertaining to the intricacies of Western water law and instream flow protection. The reason? The “constants” of Western water law have no analogue in land conservation except for the very obvious: a Western water right and land are real property.¹⁵

Different systems govern the use and allocation of land and water. Practical considerations are at play here as well.¹⁶ To add to the complexity, state-specific water laws and

and retimed storage releases or changes in reservoir management that can provide additional flows. In Colorado, these types of arrangements may have to go through water court, depending upon the plan.

¹² Water-short stream reaches can also benefit from physical solutions such as headgate and delivery-system upgrades and outlet structure and spillway renovation. These solutions may make more water available downstream.

¹³ In Colorado, the use of acquired and leased water for instream flows must occur within the confines of Colorado’s instream flow program. As described above, the CWCB is the only entity in Colorado that may hold water rights for instream flows. § 37-92-102(3), C.R.S. (2008) (stating that “[i]n the adjudication of water rights pursuant to this article and other applicable law, no other person or entity shall be granted a decree adjudicating a right to water or interests in water for instream flows in a stream channel between specific points, or for natural surface water levels or volumes for natural lakes, for any purpose whatsoever”). On the other hand, soft-management solutions, structural solutions, and other incentive-based approaches may not need to involve the instream flow program. Sometimes, a joint approach is warranted. The facts of each deal will determine whether the instream flow program must be used.

¹⁴ Mary Ann King, *Getting Our Feet Wet: An Introduction to Water Trusts*, 28 HARVARD ENVTL. LAW REV. 495, 507-511 (2004). The very success of land trusts encouraged the effort to apply the same kind of transaction- and incentive-based programs to water. Even more intriguing is the cross-pollination that is now occurring between land trusts and water trusts.

¹⁵ Tom Huhnle, *Note: The Federal Income Tax Implications of Water Transfers*, 47 STAN. L. REV. 533 (1995).

¹⁶ For example, land deals do not lend themselves neatly to temporary conservation arrangements. But temporary protection, or even intermittent protection, works well in the water context. Sometimes,

instream flow laws are the major determinants of what a water trust will look like and the programs each will pursue.¹⁷ Thus, even from water trust to water trust, the deals they pursue can and do look rather different.

There is also an element of perception at play here. As Dan Tarlock has noted, “instream flow protection rests on the twin bases of public acceptance and economic rationality.”¹⁸ This idea as it relates to the work of water trusts is best encapsulated in the following quotation from John Wilson, a rancher in Oregon:

*When it comes to water challenges . . . , one thing most folks can agree on is that we'd like to solve them ourselves. I think one of the best ways to make sure water gets where it needs to go is to use the free enterprise system to give property owners some choices. That's what I like about the Columbia Basin Water Transaction Program.*¹⁹

Mr. Wilson has it right on a number of levels. First, he has recognized that balancing consumptive and non-consumptive uses is a challenge, and one that is being taken on state by state. Development of traditional water rights (i.e., rights that divert water from the stream system for consumptive uses) typically came at the expense of healthy streamflows. Over the years, however, people in the West have come to recognize the social, economic, and environmental importance of healthy streamflows. Accordingly, diverters, especially those drying up stream segments, are seeing a lot more pressure to mitigate the damage local aquatic ecosystems suffer as a result of their diversions. Although their diversions are lawful, the consequences to an ecosystem can be dire. Therein lies the challenge that water trusts aim to address every day: how can the needs of both the diverter and the aquatic ecosystem be met?

Second, he recognizes what most people who work at water trusts learn almost immediately: people prefer using free-market solutions to solve environmental issues. The top-down, mandated approach is often seen as offensive; you've probably heard it characterized as failing to recognize the extent to which people believe they are entitled to exercise their private property rights. Where a river system suffers from low flows and local water users' diversions are receiving attention, it becomes clear time and time again that people would rather work on a solution over which they have control as opposed to one that is mandated or imposed.

Lastly, Mr. Wilson has observed that a water transaction program (he refers to the Columbia Basin Water Transaction Program) offers a free-market choice to repairing streamflows. Because water trusts do indeed offer a voluntary solution and a financial benefit—a solution to which many water users are responsive—they are being formed all over the West.

water is needed in a particular system only in dry years. A dry-year lease arrangement is possible. Leasing in general is popular given the flexibility it provides. *See infra* Part IV. of this paper.

¹⁷ See King, *supra* n. 14 at 505-506.

¹⁸ A. Dan Tarlock & Doris K. Nagel, FUTURE ISSUES IN INSTREAM FLOW PROTECTION IN THE WEST 137 (Lawrence J. MacDonnell, Teresa A. Rice, & Steven Shupe eds., 1989).

¹⁹ John Wilson, Wilson Cattle Company, as quoted at <http://www.cbwtp.org/about.htm>.

The first to form was the Oregon Water Trust, which began operations in 1994.²⁰ The Washington Water Trust began operations in 1998.²¹ The Colorado Water Trust and the Montana Water Trust followed, in 2001²² and in 2002,²³ respectively. There are also a number of other water trusts with jurisdictions ranging from the very local to regional, and other organizations whose mission and programs are not tailored exclusively to transacting water deals for streamflow enhancement but who nonetheless work on water transactions as part of their watershed programs.²⁴

III. How Water Trusts Work: A Focus on Colorado's Instream Flow Program, the CWCB, and CWT

Many water trusts must work in collaboration with a state administrative agency. In some cases, the water acquired by a water trust may *only* be held by a state agency if it is to be used for instream flows. For example, as mentioned previously, Colorado's instream flow program is housed within a state agency, the CWCB. There are a number of different sections within the CWCB to manage its various programs.²⁵ The instream flow program is managed by

²⁰ Janet C. Neuman, *The Good, The Bad, and The Ugly: The First Ten Years of the Oregon Water Trust*, 83 NEB. L. REV. 432, 433 (2004). The Oregon Water Trust merged with Oregon Trout this summer. See Memorandum from Joe Whitworth, Executive Director, Oregon Trout and Lynn Youngbar, Interim Executive Director, Oregon Water Trust to Oregon Water Trust & Oregon Trout supporters, members, and partners (re: Upcoming Merger of Oregon Water Trust and Oregon Trout) (June 24, 2008) (available at <http://www.owt.org/Merger%20Announcement.pdf>).

²¹ <http://www.thewatertrust.org/>.

²² <http://www.coloradowatertrust.org/about/>.

²³ <http://www.montanawatertrust.org/about-us/aboutus.html>.

²⁴ See, e.g., the Columbia Basin Water Transactions Program, <http://cbwtp.org/jsp/cbwtp/program.jsp>; the Trans-Pecos Water Trust, <http://www.transpecoswatertrust.com/index.html>; the Deschutes River Conservancy, <http://www.deschutesriver.org/>; the Scott Water Trust, <http://scottwatertrust.org/index.html>; Friends of the Teton River, <http://www.tetonwater.org/>; the Klamath Basin Rangeland Trust, <http://www.kbrt.org/>; The Nature Conservancy, <http://www.nature.org/initiatives/freshwater/>; and Trout Unlimited, <http://www.tu.org/site/c.kkLRJ7MSKtH/b.3022897/k.BF82/Home.htm>.

²⁵ The CWCB is home to the Water Supply Protection section, “responsible for helping to maintain the State’s ability to utilize and develop its entitlements under interstate compacts and equitable apportionment decrees in accordance with state water law,” see <http://cwcb.state.co.us/WaterSupply/>; the Watershed Protection & Flood Mitigation, “directed to prevent flood damages, review and approve floodplain designations prior to adoption by local governmental entities, and provide local jurisdictions with technical assistance and floodplain information,” see <http://cwcb.state.co.us/WatershedProtectionFloodMitigation/>; the Water Supply Planning & Finance section, “responsible for managing the Water Project Loan Program and the Non-Reimbursable Project Investments Program,” see <http://cwcb.state.co.us/Finance/>; the Office of Water Conservation & Drought Planning, which promotes “water use efficiency while providing public information and technical and financial assistance for water conservation planning” and “drought planning by encouraging and assisting communities to prepare and implement drought mitigation plans and by monitoring drought impacts and informing the public, media, and state officials,” see <http://cwcb.state.co.us/Conservation/>; Intrastate Water Management & Development section, which “focuses on helping prepare for and meet Colorado’s future water supply needs,” see <http://cwcb.state.co.us/IWMD/>; and the Stream and Lake Protection section,

the CWCB's Stream and Lake Protection Section. The Stream and Lake Protection Section's mission is "to correlate the activities of mankind with reasonable preservation of the natural environment" and "to preserve or improve the natural environment to a reasonable degree."²⁶ To accomplish the Stream and Lake Protection Section's mission, the CWCB adds water to the instream flow program in two ways. The first is through appropriating new water rights for particular stretches of river.²⁷ Currently, the instream flow program stewards more than 1,400 appropriations protecting nearly 9,000 river miles.²⁸ This is an incredible network of protected streams and rivers. But the CWCB's instream flow appropriations are quite junior. Remember that it was not until 1973 that the Colorado legislature created the instream flow program. As a result, the CWCB's instream flow appropriations are young, with priorities that date only from 1973 to the present. Often when a new, junior water right is obtained, regardless of its decreed use, it may have water available to it only infrequently and in inconsistent amounts. Because the CWCB's appropriated water rights are often quite junior, they cannot prevent the de-watering of stream reaches by senior water rights located above or in the instream flow reach; they can only protect conditions from worsening.²⁹

Of course protection from further decreases in flow for an already stressed segment of river has its benefits, but if *improving* streamflows is part of the plan, another tool must be used. The second arrow in the CWCB's quiver is the acquisitions program.³⁰ Acquisitions are an important mechanism by which the CWCB preserves or improves streamflows in critical areas of the state. It has at least two benefits that are not available to the appropriations program. First, the acquisitions program matches willing sellers (or lessors) with a willing buyer (or lessee). As a result, it represents a market-based approach to protection of streamflows. Second, it provides the CWCB with access to senior water rights.

which "manages and administers the state's Instream Flow Program" and is "responsible for the appropriation, acquisition and protection of instream flow and natural lake level water rights to preserve and improve the natural environment to a reasonable degree." See <http://cwcb.state.co.us/StreamAndLake/>. With programs that encourage maximizing the use of the state's water and provide financing for water construction projects housed within the same agency as a program intended to improve streamflows, there can be mission conflicts.

²⁶ See *supra* n. 25.

²⁷ See *supra* n. 7.

²⁸ See CWCB Stream and Lake Protection Section, TABULATION OF INSTREAM FLOW AND NATURAL LAKE LEVEL WATER RIGHTS at 1 (January 2007).

²⁹ When water *is* available to newer, junior water rights, water is generally available to most water rights in the system and, as a result, to the stream system itself. For all water rights in the West, the times of plenty are not the times of crisis. The times of crisis are the shortages. Added to that challenge are stream reaches where the CWCB could not satisfy one of the elements of a new water right appropriation: water availability. On those reaches, it cannot appropriate a water right at all.

³⁰ See § 37-92-102(3), C.R.S. (2008) (stating that the CWCB "also may acquire, by grant, purchase, donation, bequest, devise, lease, exchange, or other contractual agreement, from or with any person, including any governmental entity, such water, water rights, or interests in water in such amount as the board determines is appropriate for stream flows or for natural surface water levels or volumes for natural lakes to preserve or improve the natural environment to a reasonable degree").

Under the acquisition program, the CWCB can acquire water, water rights, or interests in water to preserve or improve the natural environment to a reasonable degree.³¹ It can acquire absolute direct flow or storage rights on either permanent or temporary bases.³² To determine whether to accept an offered water right, the CWCB evaluates proposed water acquisitions using a public process and established criteria.³³ Among the information it must consider, the CWCB must quantify the amount of water necessary to preserve or improve the natural environment.³⁴ It works closely with the Colorado Division of Wildlife to conduct these analyses.³⁵ Once it has determined to accept a water right into the instream flow program, under almost all circumstances, the CWCB must apply to water court to obtain a decreed right to use the water right for instream flow purposes.³⁶ The water court ensures that no injury will result to other water users from the change.³⁷

³¹ *Id.*

³² See § 37-92-102(3), C.R.S. (2008) (“The board also may acquire, by grant, purchase, donation, bequest, devise, lease, exchange, or other contractual agreement, from or with any person, including any governmental entity, such water, water rights, or interests in water in such amount as the board determines is appropriate for stream flows or for natural surface water levels or volumes for natural lakes to preserve or improve the natural environment to a reasonable degree.”). It is prohibited from acquiring conditional water rights. § 37-92-102(3)(c.5), C.R.S. (2008) (stating that “as to any application filed by the board on or after July 1, 1994, the board may not acquire conditional water rights or change conditional water rights to instream flow uses”).

³³ See generally § 37-92-102(3), C.R.S. (2008). See also 2 COLO. CODE REGS. 408-2 (“ISF Acquisition Rules”). These rules are being revised and a formal rulemaking hearing to consider the revisions is scheduled to occur at the CWCB meeting on January 27, 2009. The revisions incorporate statutory changes in the program made under House Bill 08-1280 and accommodate the funding the CWCB now has available to its acquisition program, discussed in more detail *infra* Part IV. of this paper. Under both the existing and proposed revised rules, the CWCB must consider certain factors in evaluating a proposed acquisition, including: (1) the reach of the stream where acquired water will be used; (2) the historical use and return flow patterns; (3) the natural flow regime; (4) the location of other water rights within and near the reach; (5) the potential for material injury to existing decreed water rights; (6) the natural environment that may be preserved or improved by proposed acquisition; (7) the effect of proposed acquisition on interstate compacts and maximum utilization of the waters of state; (8) whether the water will be available for subsequent use downstream; and (9) costs associated with transaction.

³⁴ § 37-92-102(3)(c), C.R.S. (2008) (“Before initiating a water rights filing, the board shall determine that the natural environment will be preserved to a reasonable degree by the water available for the appropriation to be made; that there is a natural environment that can be preserved the board’s water right, if granted; and that such environment can exist without material injury to water rights.”).

³⁵ See § 37-92-102(3), C.R.S. (2008) (“Prior to the initiation of any such appropriation or acquisition, the board shall request recommendations from the division of wildlife and the division of parks and outdoor recreation.”).

³⁶ 2 COLO. CODE REGS. 408-2 (ISF Acquisition Rule 6I).

³⁷ In Colorado, all changes of water rights must meet the elements of what is called the “no-injury” rule. See *Handy Ditch v. Loudon Irrigating Canal Co.*, 27 Colo. 515, 518, 62 P. 847, 848 (1900). In *Handy*, the Colorado Supreme Court clearly articulated the no-injury rule, stating:

The general rule is that an appropriator of water for any beneficial purpose may change the place of diversion at his pleasure, provided the rights of others are not injuriously affected. . . . [This rule] is peculiarly applicable to subsequent appropriators The rights of a prior appropriator, as against a subsequent appropriator who changed the place

In addition to obtaining fee simple title to a water right, the CWCB has two other options for putting acquired water in the instream flow program. They are both temporary in nature. The first option is the negotiation of a loan under section 37-83-105, C.R.S. (2008) (a “3-in-10 loan”). Water rights placed in 3-in-10 loan may only be used for a period of 120 days in a given year, and only for three (3) years of use over a ten (10) year period.³⁸ A 3-in-10 loan may be used on any stream where the CWCB currently holds an appropriated instream flow right, and in an amount up to the decreed amount of the instream flow.³⁹ One of its most flexible attributes is that a 3-in-10 loan does not require a water court change case; the State and Division Engineers can approve the use of a 3-in-10 loan quickly as long as there will be no injury to other water rights.⁴⁰ The 3-in-10 loan is ideal for use in emergency circumstances such as drought.

The CWCB may also enter into long-term leases. These leases are controlled by section 37-92-102(3), C.R.S. (2008) (“HB 1280 lease”). Although long-term leases are not new to the instream flow program, the Colorado legislature recently established protections for a lessor with the passage of House Bill 08-1280 during the 2008 legislative session. The same process used to determine whether to accept fee simple title to a water right for instream flow purposes is used to evaluate water proposed for use under an HB 1280 lease,⁴¹ in addition to a few additional considerations.⁴² For all HB 1280 leases, the CWCB must file a change of water right application or other application with the water court to obtain a decreed right to use the leased water for ISF purposes.⁴³

of diversion, are already sufficiently safeguarded by the fundamental doctrine of so-called irrigation law: He who is first in time is first in right. A subsequent appropriator has a vested right, as against his senior, to insist upon the stream continuance of the conditions that existed at the time he made his appropriation.

Id.

³⁸ See § 37-83-105(2)(a) (stating that “[a] water right owner may loan water to the Colorado water conservation board for use as instream flows pursuant to a decreed instream flow water right held by the board for a period not to exceed one hundred twenty days”); see also § 37-83-105(2)(a)(IV) (stating that a 3-in-10 loan “shall not be exercised for more than three years in a ten-year period, for which only a single approval by the state engineer is required”).

³⁹ See § 37-83-105(2)(a) (stating that “[a] water right owner may loan water to the Colorado water conservation board for use as instream flows pursuant to a decreed instream flow water right held by the board for a period not to exceed one hundred twenty days”) (emphasis added).

⁴⁰ See § 37-83-105(2)(a)(III), -105(2)(a)(V), & -105(2)(b). The approval process requires the filing of a request for approval with Division Engineer. Written notice of the proposed loan is sent to all parties that have indicated they would like to be notified of such requests. The process includes time for the filing of a protest, and instructions for the circumstances under which Division Engineer can approve.

⁴¹ See *supra* n. 35.

⁴² § 37-92-102(3). To use water under an HB 1280 lease, the CWCB must maintain records of how much water the CWCB uses under the contract each year it is in effect and must install any measuring device(s) deemed necessary by the Division Engineer to administer the lease of water and to measure and record how much water flows out of the reach after use by the Board under the lease.

⁴³ *Id.*

Of the CWCB's two instream flow arrows in its proverbial quiver (appropriations and acquisitions), the acquisitions program is the less utilized.⁴⁴ There seem to be several reasons for this. Running an acquisition from start to finish is a more time-consuming process than the initiation of an appropriation. Among other time-consuming efforts, it requires identifying willing sellers in areas identified as critical stream reaches, conducting an engineering analysis to determine the utility and health of the water right for sale, conducting a title analysis, allowing for the time to negotiate and execute the acquisition, preparing for the CWCB's acceptance process, and running a water rights change application through water court. The CWCB has lacked adequate staff time to target, negotiate, and process transactions. However, although institutional capacity is a factor that contributes to the lack of acquisitions conducted by the CWCB, by far the biggest hurdle is funding. The acquisition program requires money for acquisitions which, until 2008, the CWCB did not have. Until 2008, it relied on donations.

Given the difference in use between the appropriation program and the acquisition program, the institutional and funding issues faced by the CWCB, and the utility of putting solid, senior water rights in the instream flow program, the Colorado Water Trust was formed to hammer out instream flow acquisitions for the CWCB.⁴⁵ In essence, CWT works as a broker of water rights for the CWCB. The relationship between the CWCB and CWT can broadly be described as collaborative governance. CWT relies on and works within the state's program, and the state gains benefits from the work CWT does in the form of increased acquisitions. CWT targets (or responds to offers of) water, negotiates the deals, processes the instream flow water right transactions, raises the funds, puts together an acquisition package, and then contributes the water to the instream flow program.

IV. Challenges and Opportunities in Colorado

The Western states, with unique approaches to the prior appropriation doctrine, present their own, discrete opportunities and challenges for water trusts. This section focuses on Colorado and the challenges and opportunities that affect the efficacy of a working water trust in the state.

A. Opportunities

There are a number of opportunities that are improving the ability to find and acquire water rights for instream flows. These opportunities range from legal to technical to practical to political opportunities.

⁴⁴ Since 1973, the CWCB has completed a few more than twenty water rights acquisitions, *see* <http://cwcb.state.co.us/StreamAndLake/WaterAcquisitions/>, as compared to over 1,400 appropriations. *See supra* n. 29.

⁴⁵ CWT actually has three different program areas it pursues in order to further its mission to protect and enhance streamflows in Colorado. Working in coordination with the agricultural community and other water users, governmental entities, land trusts, watershed groups and other non-profit conservation organizations, CWT pursues and supports the following program areas: (1) conducting water rights acquisitions; (2) implementing physical, structural, and management solutions to improve streamflows; and (3) providing technical support for land trusts with water issues that often arise in connection with their land conservation activities.

1. House Bill 08-1280

House Bill 08-1280 (“HB 1280”) provided two significant new protections for those who enter into long-term leases of water for instream flow purposes with the CWCB. In Colorado, a change of water right almost always requires an analysis of the historical consumptive use.⁴⁶ If a water right is not used for a consumptive purpose in a given year, it receives no credit for consumption and a zero is factored into an analysis of annual diversions for each year the water right is not used consumptively. Rather than penalizing a water user by factoring zeroes into a consumptive use analysis for the time the water right spends in the instream flow program under an instream flow lease (a non-consumptive use), HB 1280 fixes the historical consumptive use at the time the lessor *places* the water right in the instream flow program.⁴⁷ This protection removed the single biggest reason why water users were reluctant to lease water to the instream flow program.

Second, HB 1280 removed abandonment concerns.⁴⁸ Many see this as less consequential than the removal of the historical consumptive use penalty because, under an HB 1280 lease, instream flows must be added as a beneficial use in a change of water rights case in water court. Abandonment occurs only when a water user fails to use his or her water right for its decreed purpose for the statutory period.⁴⁹ With instream flow added as a beneficial use in water court, an abandonment argument would fail. Although a sleeves-from-the-vest-concession to those who requested it, this provision’s inclusion in the statute will prevent an avenue of challenge to use of a water right temporarily in the instream flow program.

The passage of HB 1280 has generated a significant amount of interest in instream flow leasing. The new protections help preserve the value of the water right for the lessor, yet still allow the CWCB to pursue terminable uses of water for instream flow purposes. The end result is greater flexibility for all, and improvement of the instream flow program. Everybody wins.

2. Money: Species Conservation Trust Fund and Construction Fund
Instream Flow Acquisition Funds

The 2008 legislative session secured two different pots of funds for the CWCB’s instream flow acquisition program for the first time in the program’s history. The first pot,

⁴⁶ A change of water right must be approved if it “will not injuriously affect the owner of or person entitled to use water under a vested water right or decreed conditional water right.” § 37-92-305 (3) (2008). A change of water rights does not cause injury if the change of water rights decree maintains the same stream conditions that existed at the time a junior appropriation commenced. *City of Thornton v. Bijou Irrigation Co.*, 926 P.2d 1, 80 (Colo. 1996). The historical use limitation reflects the hard-and-fast rule that application of water to the decreed beneficial use is required to perfect a water right. *Weibert v. Rothe Bros.*, 200 Colo. 310, 317-18, 618 P.2d 1367, 1372 (1980). If the amount used is less than the decreed amount, only the amount used ripens into a water right and is available to change.

⁴⁷ § 37-92-102(3), C.R.S. (2008).

⁴⁸ *Id.*

⁴⁹ See CORBRIDGE & RICE, *supra* n. 3, at 252-57.

contained in House Bill 08-1346 (the annual projects bill for the CWCB), was an appropriation from the Severance Tax Trust Fund Perpetual Base Account in the amount of \$1 million. This money is specifically earmarked for instream flow acquisitions.⁵⁰ The second, Senate Bill 08-168, allocated \$500,000 from the Species Conservation Trust Fund for instream flow acquisitions.⁵¹ This new infusion of \$1.5 million will serve as the heart of the acquisitions program and can ensure its success. With it, the CWCB's instream flow program has become a concrete option for those wanting to place their water rights in a conservation program, keep them in their local communities, and obtain compensation. The decision to allocate the requested money to instream flow acquisitions when that money could have been used in other programs, *e.g.*, for construction projects, showed a commitment to the vitality of the instream flow program never before seen in the history of the program.

3. Changing Use of Western Lands

The changing use of land in the West is also creating opportunities for instream flow water rights acquisitions. The modern population explosion in the West reflects a sustained passion for living in this landscape at the same time it changes that very landscape.⁵² What were formerly working farms and ranches are now exurbs, suburbs, and ranchettes.⁵³ With the decline in the agricultural economy and children no longer interested in running family farm and ranch lands, one of the most common questions farmers and ranchers are now asking themselves is what to do with their land and water. A growing conservation ethic in the West has led to the increase in land conservation; water is finally catching up and becoming part of the conversation. When there is pressure on a farm or ranch to sell to developers, in Colorado, there are viable alternatives. The alternatives allow for maintaining the historical use of the land and water and making some money at the same time: the placement of all or part of the land in a conservation easement, tying some or all of the water to the land through that process, or selling some or all of the water for use in the instream flow program.

4. Other Opportunities

These are only a few of the opportunities available to those conducting water transactions to improve streamflows. Others include the exemption for municipalities from the strict

⁵⁰ See § 37-60-123.7, C.R.S. (2008). These funds are available to pay for the costs of acquiring water, water rights, and interests in water for instream flow use. The primary priority for expenditures of these funds shall be the costs of water right acquisitions for existing or new instream flows. They may be used in limited circumstances for the costs of water acquisitions to (1) preserve the natural environment of species that have been listed as threatened or endangered under state or federal law, or are candidate species or likely to become candidate species; (2) support wild and scenic alternative management plans; or (3) provide federal regulatory certainty. *Id.*

⁵¹ Senate Bill 08-168 was the annual appropriation to the Species Conservation Trust Fund, a fund designed to permit water development to continue by mitigating endangered species and habitat issues. The bill included \$500,000 for instream flow acquisitions.

⁵² William R. Travis et al., *Western Futures: A Look into the Patterns of Land Use and Future Development in the American West* at 3, CENTER OF THE AMERICAN WEST (Report from the Center #6, 2005).

⁵³ *Id.*

application of the anti-speculation doctrine.⁵⁴ The exemption allows a municipality or other water provider to obtain more water than it currently needs. This translates to a surplus that can be placed in a lease for use in the instream flow program. CWT has in fact been contacted by several municipal water suppliers about putting excess water into a HB 1280 lease. These discussions are ongoing.

In general, each opportunity is derived from an increasing conservation/green ethic that is spreading throughout the West. These opportunities have not yet translated into water flooding into Colorado's instream flow programs, but they have certainly increased the opportunities available to put together creative packages and have diversified the options for improving the state's streamflows. Still, though, there are challenges.

B. Challenges

While instream flow water right markets are emerging all over the West, they are in their relative infancy. Thus, they face several challenges, ranging from the difficulty in finding available water to lack of information to lack of standardization in negotiations.

1. Lack of Information

Lack of information is one problem common across all water markets. First of all, finding water for sale is often hard. CWT has been working on water transaction since 2001 and water is certainly available to acquire, but it has been hard to target a stream reach and find readily available water. CWT has found that the "low-hanging fruit" is the most available. For example, water rights that are close to being abandoned are offered fairly regularly. High-volume, senior water in critically water-short stream reaches is hard to find, and harder to afford.

Limited market information to assist in determining price adds to the challenge. For example, CWT is working on a transaction in which an appraisal was necessary because the parties were wildly apart on pricing. Part of the problem was the lack of comparable sales and the difficulty in extrapolating certain comparables to the transaction being pursued. The low end of the comparables for this transaction was water available by contract from a reservoir. Water can be leased from this reservoir for a renewable term for about \$110 per year per acre-foot. Assuming a thirty-year term for repayment, and an interest rate of 5.5%, the present value of annual payments for this water is approximately \$1,566 per acre-foot. In the appraisal at the other end of the spectrum was water that was acquired for \$15,000.00 per acre-foot of firm yield. When you begin talking about the amount of water we were negotiating (about 100 acre-feet), the range of pricing was from \$150,660 to \$1.5 million. Assumed in this scenario, too, is that a temporary contract water can even be used as a comparable for an outright sale. And yet such contracts are available, are often used in lieu of outright acquisitions, and can oftentimes *be* (read: completely occupy) the market. Ultimately, markets may not yet be sufficiently developed for fair market value to be determined if the transaction so requires. This makes negotiations tricky.

2. Contract Terms: What's Fair?

⁵⁴ Under the express terms of Colorado water law, an appropriation is speculative "if the purported appropriator of record does not have either a legally vested interest or a reasonable expectation of procuring such interest in the lands and facilities to be served by such appropriation *unless such appropriator is a governmental agency or an agent in fact for the persons proposed to be benefitted by such appropriation.*" See § 37-92-103(3)(a)(I), C.R.S. (2008) (emphasis added). This is sometimes called the Great and Growing Cities Doctrine.

Another reason water rights deals for instream flows can be challenging is that there are no set standards for the terms of the transfer. The terms are negotiated among the parties. As a result, there are limitless permutations and combinations of contract terms, some that make little difference to the transaction, and others with very real consequences. Take, for example, a deal in which the price of the sale is based on the water right prior to a water court change application, a take-it-or-leave-it proposition where the buyer bears all the risk of the change case but can also gain a benefit if more water is available to change than was initially thought. Then examine the alternative: a transaction where the price is dependent upon how much water is ultimately decreed after a change application is prosecuted. For a water trust, one of the benefits is that it looks and feels just like any other water user except that end use of the water is instream flows. Negotiations occur in the same way as negotiations from one traditional water user to another. The problem, however, is that often with a water trust, public funds are used and risk taking is not part of the model. That can complicate the process.

3. Complexity of the Transactions

As with any water right transfer, instream flow water rights acquisitions require complex analyses to determine: (1) the exact identity of the water right to be transferred, (2) title to the water right, (3) the current validity of the water right from a use perspective, (4) how the water right has been administered, and (5) possible restraints on change.⁵⁵ Unlike a more typical water rights transfer, however, an analysis of the suitability of the water right for instream flow purposes must also be conducted. If there is an existing instream flow on the reach where the acquired water is to be used, the priority date of the instream flow appropriation, the location of the instream flow reach, the amount decreed, the type of natural environment preserved, the water availability to the instream flow, whether there are multiple flow periods or a terminus at a headgate, and whether the decreed amount for the instream flow is already adequate or has been reduced from original biological recommendation based upon a water availability analysis all must be considered to determine the suitability of the acquired water. The offered water right must also be examined for its potential use (i.e., how it will benefit the existing instream flow). Will it firm up the physical supply? Improve the existing instream flow's priority? Increase the level of protection?

Another challenge is the complexity of the process to change a water right to instream flow use. Every water acquisition for instream flow purposes must have the imprimatur of the CWCB in addition to a change of water rights decree that adds instream flow as a beneficial use or permanently changes the use of the water to instream flow. The CWCB has its own rules, required investigations, and procedures for the acceptance of a water right for instream flow. This preliminary process is time-consuming and, if pursued by an individual, could be quite costly.

The next step is water court. With the exception of a 3-in-10 loan, any water use, including HB 1280 leases, must go through water court. The very fact that a water right must go through water court is a significant transaction-inhibitor. Going to water court is perceived, fairly or not, as a complicated, expensive, uncertain, and even risky process. If an entire water right is the subject of a transaction, the fact that it must go through water court may not matter so much. But in the case of partial rights, the entire water right is opened to scrutiny and a standard is set for future changes of the balance of the water right retained by the seller. A number of

⁵⁵ Amy W. Beatie and Arthur R. Kleven, *The Devil in the Details: Water Rights and Title Insurance*, 7 U. DENV. WATER L. REV. 381, 383 (2004).

deals CWT spent time negotiating have been unsuccessful once the interested seller learned that water court would be part of the process. The risk of water court scrutiny in addition to the cost of water court can complicate the process of convincing a possible seller to part with his or her water rights.

4. Dry-up

In Colorado, as previously explained, a change of water rights cannot injure other water users. One way to prevent injury is to distill the water right to its historical consumptive use and allow only the historical consumptive use to be changed. That way, a water user cannot expand his or her previous use to the detriment of other water users in the system. Typically, with irrigation rights, a change of water right will require the dry-up of irrigated land. CWT has found that many people do not understand this concept. They believe that their flow rate will form the basis of a transaction.

Take, for example, the following scenario recently encountered by CWT. In the fall of 2007, CWT was contacted by a watershed advocate about talking to a family that was interested in selling one of their water rights. The water right for sale was decreed to a senior priority ditch that diverts from a severely water-short section of river on the Western slope of Colorado. The initial idea was that the landowners would sell half of the 9.6 c.f.s. water right to us. They irrigated about 260 acres with the water right and the 9.6 c.f.s. was far more water than they could use on the land the particular ditch services. Therein was the problem. The sellers were under the impression that they could sell 4.8 c.f.s. to CWT and not change their irrigation practices at all. CWT had a very difficult time explaining the no-injury rule to them, including why dry-up was necessary. In the end, they did not want to conduct the transaction.

5. Overcoming the Mythology

Part of the problem is a mythology about water rights that people have come to believe, a mythology that is the result of a synergistic effect of two separate beliefs: (1) that a water user can get something for nothing (in the transaction above, obtaining money for selling a water right that would not affect one acre of historical practices); and (2) that a water right is *the* most valuable asset a person owns. That may be true if the water is used in a way that maximizes the historical consumptive use, is very senior, and is in a local market that justifies a high price tag, but it is not so for every locality or every right. The process of disabusing people of the notion, long-held in the family, that their great-great-grandfather's 9.6 c.f.s. water right is worth millions of dollars can be hard, especially when one is the opposing party to a transaction.

6. Other Challenges

These are only some of the challenges faced by those who conduct water transactions to improve streamflows. Others include the difficulty in convincing the seller to obtain a lawyer to help with the transaction if looks as though it will be complicated or if the seller is having trouble understanding the consequences of the deal; financing transactions; financing an organization's day-to-day operations; and the time and resources involved in investigating every lead.

V. Conclusion

Notwithstanding the obstacles and challenges facing the development of an instream flow water market, you now have information to share with your water clients about new options available for diversifying and maximizing the use of their water portfolios: selling or leasing water

for instream flows. These options, while functioning clearly within the prior appropriation system, have the added benefits of: (1) improving local watersheds; (2) keeping water in local communities and within families; (3) maximizing the use of valuable, senior water rights; (4) allowing adaptation to changing circumstances; and (5) in many cases, generating additional income for water users.

Some may believe that the idea that water trusts are satisfied with the prior appropriation system is an overstatement. Perhaps water trusts are simply operating within the existing system—within the “constants” of Western water law—because it is practical and effective even if not ideal. There may also be those who believe that the water trust movement can be a powerful part of the solution to balance the playing field, that it can “be the change.” Whatever a person’s beliefs, water transactions to improve streamflows are likely to neither solve all of the West’s streamflow problems nor fit the needs of every water user. But, as economically rational, equitable, environmentally sound, and sustainable as instream flow water transactions are, they represent a step—and a pretty good one—in the right direction.