

**RECENT REGULATORY ACTIONS
AFFECTING AGRICULTURAL WATER SUPPLIES
IN CALIFORNIA**

Prepared by
Gary W. Sawyers, Esq.

Set forth below are summaries of recent regulatory actions affecting agricultural water supplies in California.

Water Rights Fees

In connection with the State's budget crisis, legislation was enacted in 2003 stripping funding for the State Water Resources Control Board's Division of Water Rights, effectively shifting funding for the Division to fees to be collected from water rights holders. As directed by that legislation, the Board hurriedly established a fee schedule to fund the Division of Water Rights in the Fall and Winter of 2003. These new fees are substantial, and add to the cost of irrigation water supplies.

- Among the myriad issues raised by the Board's approach, (i) the fees appear to be a tax rather than a user fee, and therefore may be illegal, (ii) the Board's approach imposes fees on pre-1914 and riparian water rights covered by Board-issued permits and licenses, even though the Board has no jurisdiction over those senior water rights, (iii) the Board elected to simply take the "face value" of all permits and licenses as the basis for fees, rather than actual diversions or water supplies, thereby significantly "over-counting" the amount of water on which fees will be paid, and (iv) the Board assumed a significant non-payment rate and required water rights holders making payments to absorb the cost of those non-payments.
- In January 2004, the Board delivered its first Notices of Determination based on the fee schedule it had adopted. Most water rights holders objected but paid under protest. Virtually all of those protests were rejected by the Board. Discussions over restructuring the Board's water rights fee regulations floundered, but Board staff revising the methodology for the determination of fees in September 2004. The revised regulations are very similar to the original regulations used to impose water rights fees in January 2004. Commencing in October 2004, the Board began to forward new Notices of Determination based on its revised fee schedule. Again, most water rights holders filed petitions for reconsideration, and most were denied.
- In December 2004 Senator Florez introduced SB 31, a bill designed to significantly reduce the amount of funding obtained by the Board through water rights fees. It is unclear whether Senator Florez can be successful in his efforts.
- Litigation brought by the Central Valley Project Water Association and Northern California Water Association, and a separate suit brought by the California Farm Bureau Federation, challenge the fees as illegal taxes. A decision should be rendered soon.

Water Quality Issues

Although State and federal water quality statutes have always regulated California agriculture and irrigation water purveyors, until recently the impacts of those statutes had been overshadowed by restrictions imposed by the public trust doctrine and numerous species-related laws. However, commencing in 1999, a series of court decisions and legislative enactments coupled with several highly-energized environmental groups focused on water quality have given rise to a host of new restrictions and threats that could significantly impact growers throughout the State.

Among other water quality-related developments in the past few years of interest to the agricultural community are as follows:

- The Ninth Circuit Court of Appeals ruled in the *Talent Irrigation District* case that the use of aquatic herbicides by irrigation water purveyors can require an NPDES permit under the federal Clean Water Act, even if the herbicide was applied in accordance with a label approved by the Environmental Protection Agency. As a result, an interim general permit that imposed significant additional restrictions and reporting requirements on water purveyors was developed by the State Water Resources Control Board. The interim general permit expired in early 2004, prompting the State Water Resources Control Board to issue a longer term general permit stating the conditions to be met by water agencies in the application for aquatic herbicides in order to comply with the Ninth Circuit's ruling. As expected, the terms of the long-term general permit were more onerous than the terms of the interim general permit, but they may be workable for agricultural water purveyors. Although the Federal Environmental Protection Agency has issued a directive indicating that it does not believe the *Talent Irrigation District* decision is correct, and that the EPA will not engage in enforcement activities with respect to that decision, the State of California continues to enforce the *Talent Irrigation District* decision.
- The Ninth Circuit ruled that aerial spraying of pesticides could constitute an activity requiring an NPDES permit if any part of the chemical reaches "waters of the United States."
- The longstanding waiver from permitting requirements under California's Porter-Cologne Water Quality Act for irrigation water run-off and storm water run-off from irrigated fields was rescinded by statute effective December 31, 2002. In the absence of that waiver, each farmer that has tailwater or storm water run-off that leaves the farmer's property could potentially be subject to permitting.
- In April 2003, the Ninth Circuit Court of Appeals issued a decision in *Northern Plains Resource Council v. Fidelity Exploration and Development Company* that groundwater extracted as part of natural gas production operation can be a "pollutant" under the Clean Water Act. If that water is discharged into the waters of United States by placing it into a river or other water body that is degraded as a result, an NPDES permit is required.
- In *Washington Toxics Coalition v. Environmental Protection Agency*, the United States District Court for Central Washington ordered the imposition of "buffer zones" around critical habitat for a variety of endangered or threatened salmon populations, including the Central Valley steelhead. Fifty-four pesticides are now prohibited within these buffer zones.

nes until the EPA issues a “no effect” determination or completes a consultation process for each of the pesticides. The buffer zones are 20 feet for ground application and 100 feet for aerial application.

- The United States Court of Appeals for the Second Circuit ruled that citizens may file lawsuits alleging violations of the Clean Water Act relative to the application of pesticides, even if the application is not in violation of the pesticide label approved by the Environmental Protection Agency. In a case entitled *No Spray Coalition v. City of New York*, the lower court dismissed a challenge by environmental groups because the Federal Insecticide, Fungicide and Rodenticide Act does not allow citizens to file environmental lawsuits. However, the Clean Water Act does include a citizen suit provision, and the appellate court held that the absence of citizen suit authority in FIFRA does not affect the exercise of the citizen suit authority to enforce the Clean Water Act. The Second Circuit expressly declined to consider whether application of a pesticide in a manner consistent with FIFRA must be deemed compliant with the Clean Water Act as well, and remanded that determination to the lower court.
- The Corps of Engineers entered into a settlement agreement in a Washington state case in which the Corps has agreed that water flowing in irrigation and drainage ditches will constitute “water of the United States” for purposes of imposing Clean Water Act jurisdiction. The Corps reportedly is considering changing nationwide policy to be consistent with the settlement. If water in irrigation and drainage ditches were to be considered water of the United States for purposes of the Clean Water Act, significant new requirements would be imposed on all ditch operators.
- Over the past few years, several federal appellate courts have issued rulings holding that the diversion of water from one watershed into another is a “discharge” under the Clean Water Act requiring the issuance of an NPDES permit. One such case from Florida was recently argued before the United States Supreme Court, but the Court deflected the principal issue and remanded the case for further factual findings. Accordingly, the only federal precedent in existence today holds that NPDES permits are, in fact, required for diversions of water from one watershed to another. However, no such case has yet been litigated in the Ninth Circuit, which has jurisdiction over California. That may be changing; recently, fishery groups filed a notice of intent to sue PG&E over diversions PG&E has been making for a century from the Eel River into the Russian River. If the case proceeds, the issue of permitting of diversions from one watershed to another in California will be determined. If permitting is required, virtually every large water project in the State (including the CVP and the SWP) will be subjected to an additional round of regulation through NPDES permitting. This case therefore has enormous importance for even routine water management, since diversions between watersheds are a common practice.
- The State and Regional Water Quality Control Boards are establishing “total maximum daily loads” for streams throughout California. Those TMDLs will drive water allocations and farming practices, as they impose firm limits on the amounts of covered constituents that can be allowed in the affected water way.

Endangered Species Act

The federal Endangered Species Act continues to play an important role in the allocation of irrigation water in California. In addition to its omnipresent impacts on Delta water supplies, other recent ESA-related developments include the following:

- In September 2004 the United States Fish and Wildlife Service listed the Central California population of the California tiger salamander as a threatened species. In October 2004, the Fish and Wildlife Services designated critical habitat for the California tiger salamander. There are two discreet regions of the San Joaquin Valley containing populations of the tiger salamander. One region encompasses San Benito, western Merced, northwestern Madera and western Fresno counties. The other region encompasses portions of central Madera and Fresno counties, and northern Tulare and Kings counties. Most of the remaining tiger salamander habitat is rangeland. The tiger salamander lives in rodent burrows in the upland grassland and oak savannah areas around the vernal pools and stockpounds in which they breed. This listing will have significant consequences for land use, water supplies and routine operations. Anyone with tiger salamanders or potential tiger salamander habitat on their property should therefore review the listing, critical habitat and the restrictions placed upon the use of land on which tiger salamanders are present or potentially present.
- Environmental groups in Oregon filed an action in federal court in Portland seeking to require the United State Fish and Wildlife Service to list effectively all species of lamprey as either endangered or threatened under the federal Endangered Species Act. Among the species called out in the suit is the Kern brook lamprey, which is believed to inhabit many rivers and streams in the Central Valley.

State Activities

- Questions persist as to whether the State Water Resources Control Board and/or Regional Water Quality Control Boards will remain in existence following implementation of the Governor's California Performance Review; substantial changes in the manner in which water is administered in California could result.
- Senator Sheila Kuehl has introduced Senate Bill 820, by which she seeks to dramatically alter water management and planning in California. The bill provides that, commencing January 1, 2011, a "rebuttable presumption of waste" would arise with respect to water use whenever any person fails to implement "cost-effective water conservation practices." As a result, failing to implement such practices could result in the loss of water rights (since water users who waste water can lose their rights to that water). The bill defines "conservation" as practices which reduce diversions or extractions "while maintaining the current social and economic benefits" of "current uses of water." The bill would thus shift the burden of proof to water users. The bill would also require every person, including water districts, pumping more than 25 acre-feet of groundwater annually to file a notice of extraction with the State Water Resources Control Board. Most likely a prelude to ground

water regulation, this provision of the bill could increase costs for farmers pumping groundwater due to the SWRCB's costly filing fees. It could also necessitate a large-scale staff increase by the SWRCB, to be funded by fees. The failure to file the required notice would be deemed non-use of water for the year in which no filing occurs, significantly impacting landowners' claims to groundwater rights. Failure to file would also render a groundwater user ineligible to receive State funding. SB 820 would make any willful misstatement in a filing required by the bill to be a crime punishable by up to 6 months in jail or \$ 1,000 in fines or both. In addition, civil liability could be imposed. SB 820 would also make filing a statement of diversion with the SWRCB for pre-1914 water mandatory or the underlying right could be lost in a proceeding before the SWRCB in which it is alleged that an appropriative right has ceased for lack of beneficial use. This proposal would create regulatory and administrative burdens that have not previously existed for pre-1914 water rights holders. Finally, the bill would require districts that have adopted groundwater management plans to update them before December 31, 2008, and every five years thereafter. Failure to do so would render a district ineligible for certain State funding. Currently, once a groundwater management plan is in place there is no need to update it. SB 820 would also significantly increase the requirements for a groundwater management plan to qualify as a lawful plan.

- Two bills now before the Legislature would eliminate landowner voting in water agencies and drop the requirement that irrigation district directors own land in the district. These bills, which are driven by civil rights concern, would radically change the voting in many water agencies and turn control over to residents rather than landowners.

Sales of Water Supplies and Water Rights

There is little doubt that a more vibrant water market is emerging in California. Short term (i.e., one year) transfers have been commonplace in California for decades as water management tools, and California's large water projects are effectively all "water transfers" in the sense that water has been reallocated from its place of origin to areas of need. However, California has been generally resistant to long-term water transfers as a means of addressing new demands. While many other arid Western states have adopted a more market-driven approach to water allocation, California has lagged behind.

That is now changing, due to a largely static water supply (resulting from a lack of new water development projects, see below) and rapidly growing demand in two sectors: urban and environmental. Both urban and environmental water users can afford significantly higher prices for water than most of agriculture, and agriculture holds the rights to a substantial portion of the state's developed water supply. As a result, irrigation water supplies are seen by many as a "reservoir" to be tapped to meet new and better funded needs. In turn, many farmers – particularly those with marginal land or in financial distress – see their water supply as their most valuable asset and are willing to consider converting at least a part of it into cash.

The Central Valley Project Improvement Act became law in October 1992, and included sweeping provisions that allowed for transfers of Central Valley Project water supplies. It was anticipated that the CVPIA by the catalyst for a water market in California. That did not occur. In the thirteen years since the passage of the law, there has yet to be a single long-term water tran

sfer approved under the CVPIA transfer provisions. Efforts at omnibus State water transfer legislation have also failed. It appears that a water market cannot be legislated, and that a water market requires willing buyers and willing sellers, coupled with lowered legal barriers to transfers.

While numerous political and legal impediments to transfers remain, numerous examples of long-term transfers can now be cited. For example:

- Environmental Water Account. Created as a feature of CalFed (see below), the EWA seeks to purchase irrigation water supplies for environmental uses. Over the past few years, the EWA has purchased significant amounts of water, often at above market prices, and it is now pursuing long-term acquisitions.
- “Monterey Amendments” to the State Water Project water supply contracts. These amendments permitted the permanent transfer from the Kern County Water Agency of 130,000 acre feet of SWP irrigation water entitlement to urban uses. All but 16,000 acre feet of that entitlement have been transferred.
- Water stacking and intra-district transfers. Many water agencies, and particularly those experiencing conversion from agricultural use to urban development, are allowing (and even requiring) water entitlement to be “stripped” from land and “stacked” on other land to increase the entitlement of the recipient property in order to ensure adequate water for development. The “stripped” land is typically fallowed, and sometimes used for environmental mitigation. A variation on this approach is the large-scale land retirement program being pursued by the Westlands Water District to “concentrate” supplies on non-drainage impacted land.
- Broadview Water District. The Westlands Water District has purchased virtually all of the land in the Broadview Water District in order to acquire the Broadview water supply.
- CVP Contract assignments. Some small CVP contractors have already permanently assigned their water service contracts to other agencies, effectively transferring their water entitlements.
- One of the least acknowledged issues raised by transfers is the impact on secured lending. Recently, lenders have become interested in water transfers because of potential adverse impacts on real property collateral from which water has been transferred; efforts are underway to accommodate lenders to ensure that lenders remain comfortable and will continue to extend credit in the agricultural sector. Nevertheless, careful preparation of loan documents and due diligence will be essential for lenders in light of changes in transfer legislation. Analysis of water assets will also be critical in bankruptcy and similar settings, as the source of an agricultural debtor’s financial woes (water) may turn out to be the debtor’s most significant asset.

CalFed and the Potential for New Water Supply Projects

The Bay-Delta Estuary is the key to California’s water supply. Two thirds of the State’s surface water flows to or through the Delta. It is also an extraordinarily fragile ecosystem that has

s been impacted by drought, invasive foreign species, water development projects and a host of other factors. Commencing in the late 1980s, Delta pumping restrictions to address environmental and water quality concerns were imposed that resulted in drastic reductions in water supplies, particularly to agricultural interests on the West side of the San Joaquin Valley. In connection with the efforts that lead to a Water Quality Control Plan for the Delta in 1995, a new process referred to as "CalFed" was initiated to develop a list of alternatives for addressing environmental issues in the Bay-Delta Estuary. The CalFed process involved the cooperative effort of all "stakeholders" and conducted numerous public hearings throughout the State to develop information.

- In February 1996, the CalFed process produced a list of 20 alternative projects for addressing Bay-Delta environmental issues. From that list, alternatives were selected and further studied, after which environmental documentation was prepared and a final "record of decision" developed describing a broad range of goals and activities to be pursued to address Bay-Delta and related issues. The CalFed Bay-Delta Program was thus developed as a means of coordinating State and federal efforts to address the myriad regulatory, physical and political issues that create a bottleneck in the Delta.
- CalFed has itself become mired in political disagreements and controversy, and funding has stalled. Federal bills providing both authorizations and appropriations have been blocked for the past several years; it remains unclear if Congress will be willing or able to provide the billions of dollars needed to fund the federal portion of CalFed. Of even greater concern is the State's ability to participate given its current financial condition.
- However, there are ongoing efforts to achieve federal legislation to fund CalFed, and the recently passed Proposition 50 in California would provide at least a portion of the State money required. In addition, the CalFed process has generated numerous "off shoot" programs and agreements such as the Environmental Water Account, storage investigations and the recent "Napa Accord" that carry the promise of significant improvements in water supplies and environmental conditions.
- Congress recently passed a pared back version of CalFed, providing reliable federal funding (albeit at a much reduced level) for the first time. The State is now considering whether and how to pay for its share of CalFed.

Water Storage and Delivery - Restrictions and Outlook

California is expected to have an annual water supply deficit of five million acre feet or more by 2025. Of all the water that falls on California as precipitation, roughly one third is controlled and utilized, one third is permanently dedicated to the environment, and one third is theoretically available but politically and practically (at least at present) off limits. The State is thus critically water short.

- With the exception of recently completed Diamond Valley Lake in Southern California, there have been no significant water storage projects constructed in California in more than a quarter century. Environmental opposition to new surface storage projects is intense, and regulatory impediments and permitting requirements for surface storage offer opponents of any storage project substantial opportunities to delay or scuttle the project. No ne

w reservoirs are even close to construction as of this writing, and it will easily be at least another decade or two before any other new storage can be brought on line.

- The attendant regulatory and environmental costs of any new reservoir would make the water extremely expensive. It is unlikely that the yield from a new reservoir would cost less than \$300 to \$400 per acre foot – or more – pricing it beyond the means of virtually all farmers. Nevertheless, most water managers believe new storage is critical to California's water future. As a result, new approaches to storage are being developed.
- The most widely implemented is groundwater storage, in which water that would otherwise have been lost to flood releases is captured and recharged into the underground rather than stored on the surface. Large and successful groundwater storage projects have been conducted in the Kern County Water Bank, Semitropic Water Storage District and Arvin-Edison Water Storage District. A number of other banks are either under construction or being pursued. The cost of water derived from groundwater banking is still significant (often in the range of \$100 to \$200 per acre foot), and a substantial investment is required in both land and recovery facilities. Moreover, energy requirements for extractions are problematic. Nevertheless, until surface water storage can be again constructed, storage below ground may become the only viable alternative.

Groundwater and Possible Pumping Regulation

Unlike the law governing rights to surface water and true underground streams (which is largely statutory), there is no comprehensive, statewide regulatory scheme governing the extraction or use of groundwater in California. Therefore, a great many aspects of groundwater law remain unclear or subject to interpretation.

- There has been a recent effort by California counties to regulate groundwater by virtue of their general municipal police powers. While counties have generally not attempted to regulate groundwater extraction, except with respect to well drilling standards and health and safety concerns, demands of groundwater during the recent drought inspired counties to become more proactive in the groundwater arena. A California court held that groundwater regulation is within a county's police powers and is not otherwise preempted by general State law. As a result of this case, many counties have adopted sweeping groundwater ordinances. In particular, counties are concerned with potential mining of groundwater resources for use outside the county.
- Since 1993, local agencies (e.g., local water districts, cities, and counties) have been empowered to adopt "AB 3030" programs to manage groundwater. Many local agencies have adopted such plans. However, AB 3030 allows local agencies to impose "pump taxes" and restrictions on groundwater extractions only under very limited circumstances. As a result, many AB 3030 plans do not include regulatory elements, but are instead focused on monitoring, recharge opportunities and addressing contamination. They have been criticized as ineffective.
- Efforts are pending in the Legislature to put more "teeth" into AB 3030 plans, and/or to move towards regional or statewide regulation of groundwater.

