Groundwater Transfers in Nebraska: Obstacles and Opportunities to Buying and Selling Groundwater Rights

by Daniel L. Lindstrom

If you practice law in farm country (and let's face it, whether you realize it or not, if you are in Nebraska, you are in farm country), you will sooner or later become aware of a new and growing market for groundwater. In Greater Nebraska, it is not uncommon to hear radio advertising or see written advertising indicating that some agricultural land realtor has water rights listed for sale. We can sell water in Nebraska, you ask? Well, yes and no.

Some Background

Despite the opinions of early explorers that the area encompassing Nebraska was a vast wasteland, referred to in the early nineteenth century as the "Great American Desert[1]," our state is blessed with incredible, but not unlimited, underground water resources. While many aquifers underlie portions of Nebraska, the most notable and important to human activity is the "High Plains" or "Ogallala" Aquifer. As one of eight states sitting atop the Ogallala Aquifer, the size of the Nebraska portion considerably dwarfs that of the other seven states.[2]

Daniel L. Lindstrom

Daniel J. Lindstrom is a shareholder with Jacobsen Orr Lindstrom & Holbrook, PC, LLO and has practiced law with the firm since 1986. His practice includes litigation of insurance, business, agricultural, water, zoning, annexation and other matters. Mr. Lindstrom also represents clients in business and corporate matters. In addition to his litigation and business practice, he has been actively involved in representing and consulting with clients, including Kearney and other Nebraska communities, on issues relating to economic and community development, including Tax Increment Financing (TIF).

As of October 1, 2013, Nebraska had approximately 209,442 groundwater wells. These wells are used for a variety of domestic, irrigation, and municipal purposes.[3] Like the topography, geology, and weather of Nebraska, our underground water resources are highly variable. In some places the aquifer recharges at a rate that roughly keeps up with, or exceeds, pumping demand. In many other places, however, it does not. In many places, the volume of stream flow is directly connected to the quantity of underground water in adjacent aquifers, but in other places the relationship between surface water resources and groundwater resources is negligible at best. These relationships are complicated and they affect the regulatory and legal rules pertaining to water use in Nebraska in ways that we can only superficially discuss in this article.[4]

Some Basics

The Public Owns the Water In Nebraska

The concept of public ownership of water in Nebraska is sometimes confusing to clients. For example, I can convey my real estate to you, and retain the right to ownership of any minerals lying beneath the surface of that property, thereby severing that right before granting the property to you. I cannot, however, do the same thing with the water under my land. This is because, rather than being treated like a mineral right that is a severable property right,[5] the surface water of Nebraska is dedicated to the people by the Nebraska Constitution.[6] Likewise both the Supreme Court[7] and the Legislature have

also determined that the ground water underlying the land in Nebraska belongs to the public.[8] So if it is owned by the public, and therefore ownership of the water itself cannot be severed from the real estate, how can it be sold or otherwise conveyed apart from conveyance of the real estate? Read on.

Groundwater Property Rights Are Limited Rights to Use

Ground water is "that water which occurs or moves, seeps, filters, or percolates through the ground under the surface of the land."[9] In Nebraska, a landowner acquires the right to use groundwater, subject to regulation, by virtue of the ownership of the overlying land.[10] The development of case law in the state has long recognized the right of a landowner to withdraw groundwater for a reasonable and beneficial use.[11] However, this right to withdraw and use is limited by statute and administrative regulations.

With the passage of the Groundwater Management and Protection Act ("GWMPA"),[12] and subsequent amendments, the Legislature updated and built upon prior water management statutes, such as those creating Natural Resource Districts within the state.[13] The Legislature granted broad authority for each Natural Resource District ("NRD") to create rules regulating groundwater use and transfers within its boundaries, subject to certain rulemaking and oversight by the Nebraska Department of Natural Resources ("DNR"). An important component of the GWMPA is the requirement that basins be periodically evaluated by the DNR to determine whether they are fully appropriated or over appropriated.[14] If an area is determined to be fully or over appropriated, certain steps must be taken to limit new and existing uses of water, including the adoption of an integrated management plan ("IMP") by the affected NRD, in conjunction with the DNR. The IMP is implemented with the goal of managing both surface and groundwater uses in a manner that incrementally results in a balance between water use and supply. This IMP process often results in imposition of restrictions and conditions upon the development and use of groundwater resources for irrigation, and it can be the source of some controversy—sometimes resulting in litigation. Moreover, these IMP restrictions (as well as regulation of surface water resources by DNR) often result in creating two classes of irrigators: those who have access to groundwater or surface water for irrigating crops, and those who wish that they had such access.

The Genesis of a Water Market

In many cases, the "have-nots" simply lose the use of water for irrigation, either temporarily or for the long term, as the result of NRD or DNR regulation. However, some NRDs have adopted rules that make it possible to transfer rights to

KANSAS CITY ESTATE PLANNING SYMPOSIUM

National Speakers
at a Midwest Price

* $349 with electronic book
or $398 with hard copy book
One day pricing is also available.

Featuring a special **Elder Law Segment**

Latest, Most Advanced Information
on **Estate, Tax** and **Business Planning**

Thurs., May 1 – Fri., May 2, 2014

Overland Park Convention Center
6000 College Blvd., Overland Park, KS

www.kceps.org

*Continuing Education Credit available for Attorneys, Certified Financial Planners (CFP®s), Certified Public Accountants (CPAs) and Insurance Professionals.

Register now at www.kceps.org

withdraw and use groundwater from an existing property to another property.[15] As a result, the "have-nots" in those NRDs may still be able to develop irrigation on acres that would otherwise have been relegated to dry land farming only.

In some cases NRDs have taken creative steps to incent irrigators to reduce water use and to retire land from irrigation, including the use of "water banks" or "depletion offset accounts" to facilitate temporary or permanent acquisition and retirement of irrigation uses.[16] Additionally, some NRDs have begun to purchase groundwater and surface water rights in an effort to augment stream flow and to meet their goals for achieving a favorable balance of supplies and demand for use under their respective IMPs.[17]

In exchange for adequate consideration, landowners who wish to retire irrigation uses on marginal or difficult-to-irrigate properties are often happy to participate in these NRD programs, or to simply sell their right and transfer it to another irrigator who desires it, when rules permit such a transfer. These recent developments have created a market that didn't exist prior to passage of LB 962 in 2004.[18]

Practical Considerations for Completing the Groundwater Transfer

If your client is retiring a water right while in the course of working with an NRD that is acquiring the water right, you may simply find the forms that have been developed by the NRD to adequately document the deal and protect the rights of your seller/transferor. The overriding interest of the seller/transferor is, of course, to be paid the compensation expected and agreed upon. However, be sure to insist on reviewing these documents, as some NRDs are less experienced or sophisticated about documenting transfers. Sometimes conditions to the transfer can be problematic and will require interpretation or negotiation.

Often NRDs will use conservation easements as the means of transfer and you will want to ensure that the terms of the conservation easement are reasonable. While an NRD, like other political subdivisions and non-profits, can hold a conservation easement, if you are representing parties in a transfer of water rights between private individuals, be aware that private landowners cannot hold a conservation easement.[19]

Valuation of the interest to be transferred can be unpredictable. What appears to be happening is that the market price either runs with the NRD's stated price per acre, or acre-foot, for water banking, or it is calculated to approximate the difference in fair market value of farmland with irrigation versus dry farmland.

As mentioned above, a number of realtors have been active in representing sellers of water rights in NRDs in which transfers of groundwater rights are permitted. After having represented buyers in these transactions and having reviewed a number of form-based purchase agreements utilized by real estate agents, I cannot emphasize enough that you should not permit your client who is a buyer to simply accept and rely upon the realtor's form. It will likely be wholly inadequate in terms of protecting the interests of the buyer of water rights. When tens or hundreds of thousands of dollars are involved, your client will want some contractual promises in place that will provide the client with as many remedies as possible if the deal goes sour. Nonetheless, despite loud and repeated protests, sometimes you cannot convince your client that using a detailed purchase agreement will do anything other than chill the negotiations. Sometimes the seller or seller's agent will simply refuse to use your well-crafted purchase agreement. In either case, make sure that you have a letter in your file to your buyer client that advises your buyer that:

• While the NRD will take some steps to facilitate the transaction according to its rules and certain statutory requirements, it will not and cannot provide the buyer with any assurances or any remedy if the transaction does not go as expected or if the water right obtained is worthless.

- The NRD will do what it needs to do to assure that the transfer will comply with its rules for depletion allowance calculations and it will do a simple lien search to comply with the statute[20] before it approves the transfer, but those steps are not intended to protect the buyer.

- Nothing in the form agreement gives the buyer a specific remedy if the seller of the right:

  • Does not own the overlying real property from which the transfer arises;

  • Succeeds in "selling" the same right to more than one buyer;

  • Fails to comply with NRD rules concerning retirement of the water right on the property from which it is sourced.

While intentions are good and expectations are high, these transactions for the transfer of groundwater rights have yet to take on a uniform and predictable course. Proceed with due caution.

Endnotes

1 The 1820 Army Engineers expedition lead by Maj. Stephen H. Long made its way through what later became Nebraska. Major Long's report concluded that the area was "almost wholly unfit for cultivation" and his cartographer is credited with placing the term "The Great American Desert" on the expedition's map of the area. Earlier exploration by Zebulon Pike (1806) and Lewis and Clark (1802-06) resulted in similarly uncomplimentary reports about the area's natural resources—especially its water resources. James C. Olson & Ronald C. Naugle, *History of Nebraska* 1-4 (3d ed. 1997).

2 *See An Atlas of the Sand Hills* 67-122 (Ann Bleed & Charles

Flowerday eds., 2d Ed.1990); William Ashworth, *Ogallala Blue: Water and Life on the High Plains* 9-21 (2007).

3 State of Nebraska, Department of Natural Resources, Quarterly Report (Oct. 1, 2013) available at http://www.dnr.ne.gov/GroundWater/PDF_Files/SummaryAllWellsRegisteredThridQuarter2013County.pdf (summarizing all wells registered in Nebraska by county).

4 *See* Richard S. Harnsberger & Norman W. Thorson, Nebraska Water Law and Administration (1984) [hereinafter Harnsberger]; J. David Aiken, *Hydrologically-Connected Groundwater, Section 858, and the Spear T Ranch Decision*, 84 Neb. L. Rev. 962 (2006).

5 *Fawn Lake Ranch Co. v. Cumbow*, 1025 Neb. 288, 167 N.W. 75, 76 (1918). See also 58 C.J.S. Mines and Minerals § 192 (West 2013).

6 N.E. Const. Art. XIV, § 5: "The use of the *water of every natural stream within the State of Nebraska is hereby dedicated to the people* of the state for beneficial purposes . . . ." (emphasis added).

7 *State v. Sporhase*, 208 Neb. 703, 706, 305 N.W.2d 614, 617 (1981), *rev'd. on other grounds Sporhase v. Nebraska*, 458 U.S. 941 (1982).

8 "The Legislature finds that *ownership of water is held by the state for the benefit of its citizens*, that ground water is one of the most valuable natural resources in the state . . . ." Neb Rev. Stat. § 46-702 (Reissue 2010) (emphasis added).

9 Neb. Rev. Stat. § 46-635 (Reissue 2010).

10 *See* Harnsberger *supra note* 4, at 214.

11 *Prather v. Eisenmann*, 200 Neb. 1, 5, 261 N.W.2d 766, 769 (1978); *Spear T Ranch v. Knaub*, 269 Neb. 177, 187 691 N.W. 2d 116, 128 (2005).

12 Neb. Rev. Stat. §§ 46-701 through 46-753 (Reissue 2010).

13 There are currently 23 NRDs in Nebraska. *See* NU Water-Related Research by Natural Resources District, *available at* http://watercenter.unl.edu/researchdb/nrds/nrdDB.asp.

14 These determinations have resulted in significant portions of basins in the western half of Nebraska becoming subject to integrated management plans. Currently, all of the Platte River west of Chapman has been designated as either fully or over appropriated, nearly all of the Republican River basin has been designated fully appropriated, and the far western portion of the Niobrara River basin has been designated fully appropriated. For a map of these areas, *see* Fully Appropriated and Overappropriated Surface Water in Nebraska (Sept. 9, 2011) available at http://dnr.ne.gov/SurfaceWater/FullyOverAppropriatedAreaStatewide_0911.pdf.

15 *See, e.g.*, Ground Water Management Plan, Rules and Regulations, Rule 7 *available at* http://www.cpnrd.org/2013%20GW%20Management%20Plan.pdf.

16 See, e.g., Central Platte NRD's website *available at* http://www.cpnrd.org/Water_Bank.html; Tri-Basin Natural Resources District Rules and Regulations for Management and Protection of Land and Water Resources, Rules 9.6, 9.7 *available at* http://www.tribasinnrd.org/documents/GMARules0613.pdf.

17 Importantly, compliance with the Interstate Compact involving the Republican River basin, and the need to offset depletions pursuant to the Platte River Recovery Implementation Program in the Platte River basin, are also drivers of both IMP provisions and the desire of some NRDs in those basins to participate in such purchases.

18 Neb. Rev. Stat. § 46-739 (Reissue 2010).

19 Neb. Rev. Stat. § 76-2,111(3) (Reissue 2009).

20 Neb. Rev. Stat. § 46-739.01 requires the NRD to obtain a title search for purposes of determining whether a lien exists on the property from which the water right is transferred. This provision is not designed to protect the purchaser of a water right, it is instead designed to protect lenders and the value of their security interests.