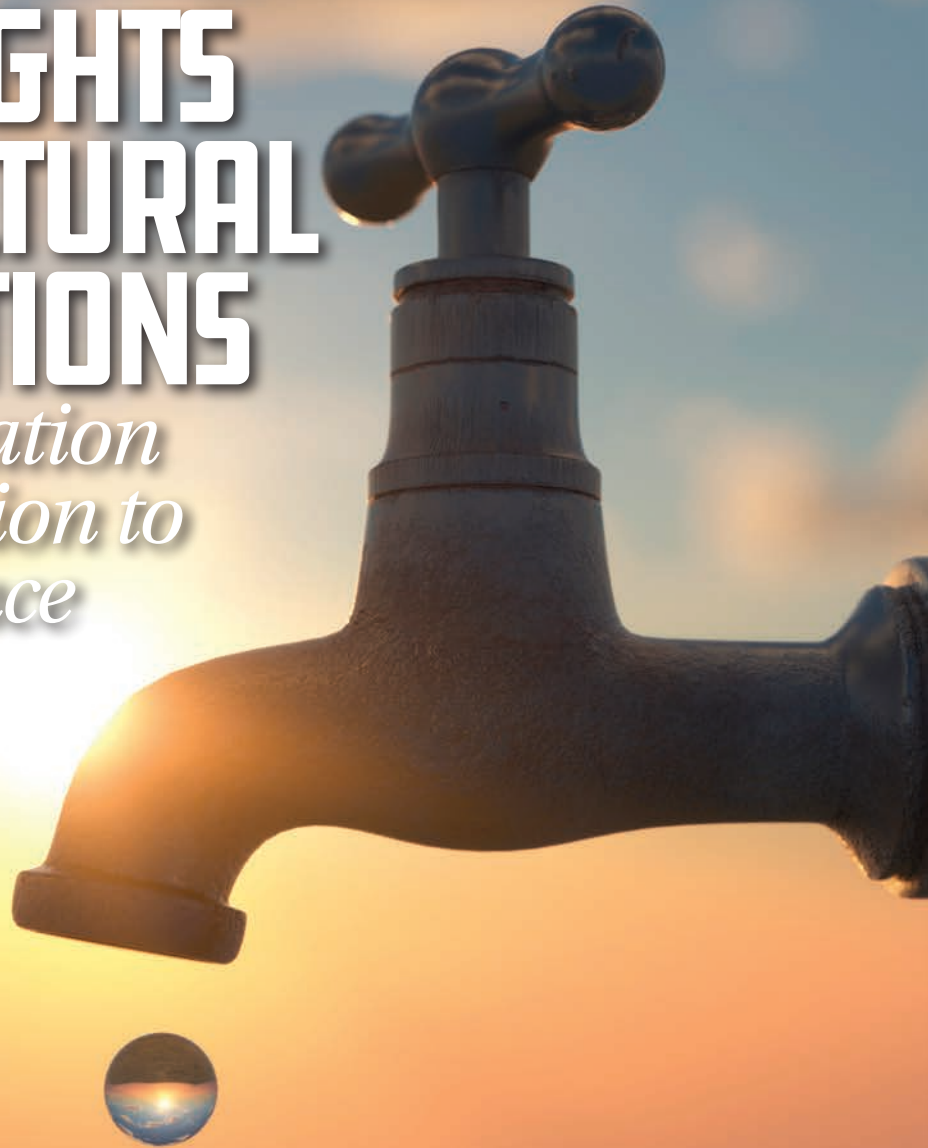


WATER RIGHTS IN AGRICULTURAL TRANSACTIONS

*From Evaluation
and Verification to
Conveyance*



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Water rights can make, or break, an agricultural real estate transaction. Irrigation rights alone were appraised at over \$24 million in a deal this article's authors helped to close. Even in transactions in which water rights are not separately valued, water availability can dictate the land's worth. Without secure water rights, cropland that requires irrigation may become nearly worthless.

Buyers, sellers, and lenders dealing in

agricultural real estate thus need to understand and account for the status of water rights in their transactions. Below are best practices for due diligence associated with water rights.

"PAPER" WATER RIGHTS

Due diligence begins with a focus on "paper" water rights. A "paper" water right states who has the legal right to use water,

in what manner, and when. Put differently, what do public records document about the water at issue? Does the seller have any permits or deeded water interests? Are those documents dispositive, or has a state-based permitting regime overridden them?

To begin, determine how water rights are administered locally. State laws govern most water rights, and those laws principally consist of two schemes.

First is the riparian doctrine, which developed in the water-abundant eastern states. It confers water rights based on land-ownership adjacent to a watercourse or on the land overlying a groundwater source. See *Tyler v. Wilkinson*, 24 F. Cas. 472, No. 14312 (C.C.D. R.I. 1827). The absolute-dominion, reasonable-use and correlative-rights rules are groundwater offshoots of the riparian doctrine.

Second is prior appropriation, which originated in the arid west. Appropriative rights do not depend on proximate land ownership but on the date on which water was first beneficially used. An appropriator has a right from the moment that they intended to apply water to a beneficial use, diverted the water from its natural course, and applied the water to a beneficial use. See *Irwin v. Phillips*, 5 Cal. 140 (1855).

Complicating this picture is the fact that these schemes stem from a combination of common-law and statutory authorities. Some states also use different regimes to regulate surface water and groundwater. See e.g., *Spear T Ranch, Inc. v. Knaub*, 691 N.W.2d 116, 125 (Neb. 2005). Most states and even some local regulators have further added a permitting-scheme overlay. See e.g. Or. Rev. Stat. § 537.140.

In this way, the manner of due diligence will depend on the local legal source of water rights. Whether from the land recording system or another state or local regulator, request copies of any permits, licenses, or other “paper” water rights, and evaluate how much water they allow and whether they are tied to specific parcels or times of irrigation.

“WET” WATER RIGHTS

While a “paper” water-rights review is essential, it alone is insufficient. Due diligence turns next to the difficult task of analyzing the “wet” water itself. At issue is whether the paper right confers as much actual water as it says, or at least enough to make the transaction economical.

The first potential risk is internal: Has the seller actually perfected and maintained their right? Or, if the buyer intends to acquire new rights, does the buyer meet the requirements? In a riparian jurisdiction, ensure that the land abuts the watercourse and that the seller currently holds or the buyer is eligible for any necessary permits. Consult surveys, public records and any historical data.

Alternatively, in a prior-appropriation jurisdiction, verify when the appropriator first made the beneficial use and if they have continued to do so in an adequate amount. Most jurisdictions enforce relin-

quishment, forfeiture, and prescription if a water right goes unused for a certain time. See e.g., *Twin Creeks Farm & Ranch, LLC v. Petrolia Irrigation Dist.*, 461 P.3d 91, 95 (Mont. 2020). Analyze public records showing crop productivity and request pumping data and other water-use records from the seller. Left unchecked, these internal risks can make a water right worthless, no matter its strength on paper.

External factors can also threaten “wet” water rights. Is a moratorium in place? Or, even without a declared moratorium, will competing rightsholders make the contemplated irrigation impractical? A riparian jurisdiction, in times of shortage, typically allocates a limited water body either in proportion to ownership of adjacent or overlying land or according to a reasonableness analysis. See *Holm v. Kodat*, 211 N.E.3d 310, 316 (Ill. 2022). Reasonableness, in some jurisdictions, incorporates a preference for domestic and municipal uses over irrigation. See e.g., Neb. Rev. Stat. § 46-613.

During times of shortage, an appropriative jurisdiction, by contrast, will generally permit senior appropriators to issue calls forcing junior appropriators to stop pumping. See *Kelly v. Teton Prairie LLC*, 2376 P.3d 143, 146 (Mont. 2016). Is there any evidence that has already occurred or will soon occur? It is imperative to understand not only the extent of “paper” water rights at hand but also what the actual chances are that those rights will yield “wet” water when desired.

A “wet” water-rights review cannot rest on public records alone. Some jurisdictions gather and publish data about a water source’s use and availability. See e.g., S.D. Codified Laws § 46-2-11. That is a good place to start. Buyers and lenders should also consult climatic and water-use data. In some cases, third-party hydrologists, economists, and other consultants will additionally be necessary to evaluate the “wet” water rights.

CONVEYANCE INSTRUMENTS

The final step, after due diligence, is to convey the water rights. Like land, water is often treated as a property right. See *Clawson v. State, Dep’t of Agric., Div. of Water Res.*, 315 P.3d 896, 904 (Kan. App. 2013). But, unlike land, water rights are “usufructuary,” meaning deeds and other instruments can, at most, convey a right to use the water but not ownership of the water itself. *Farmers Reservoir & Irrigation Co. v. Pub. Serv. Co. of Colorado*, 526 P.3d 161, 170 (Colo. 2022).

Also, unlike land, water rights depend on the correlative rights of others. Neighbors consequently may have good reason to oppose a conveyance if it affects their hydrologically connected rights. *Vill.*

of Four Seasons Ass’n, Inc. v. Elk Mountain Ski Resort, Inc., 103 A.3d 814, 820 (Pa. 2014).

Each jurisdiction has a different procedure for transferring water rights. Some riparian states imply a water conveyance any time the adjacent or overlying land transfers title. See e.g., *Sanders v. Plant*, 204 S.W.2d 323, 324 (Ark. 1947). Others require the deed to separately identify any riparian rights it intends to convey. See *Movrich v. Lobermeier*, 905 N.W.2d 807, 818 (Wis. 2018).

Prior-appropriation jurisdictions typically permit water rights to be conveyed separately from land. See e.g., *Salt Lake City Corp. v. Big Ditch Irr. Co.*, 258 P.3d 539, 547 (Ut. 2011). That said, statutes may limit this, for instance, by prohibiting severing the water rights from land to which the water was originally applied or protecting the interests of third parties. See Okla. Stat. § 105.22; Utah Code § 73-3-14. In states with a permitting overlay, the buyer and seller may need to notify regulators or even apply for permission to complete the transfer. See Tex. Water Code § 11.084.

CONCLUSION

Water rights can, and should, form a linchpin of many agricultural land transactions. To protect themselves, landowners and lenders should take care to evaluate the “paper” and “wet” water rights at issue and follow local rules to effectively convey those rights. This article provides only a general overview of that process and is not a substitute for state-specific, and in some cases federal, analysis of water rights. That should involve experienced local counsel. Consultants may also be necessary to quantify water rights and evaluate their relationship with other local uses.



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