

Drafting Groundwater Transfer Agreements

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Success occurs when opportunity meets preparation!

You have to be very careful if you don't know where you are going – because you might not get there!

Yogi Berra

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Purpose of Outline –
To Address the Transfer of Groundwater Rights

First - What are we trying to transfer?

- Groundwater Rights
- Necessary Access Rights

Next - What issues typically arise between a buyer and seller and how might we address these issues in transfer documents?

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Groundwater

Texas Water Code - “water percolating below the surface of the earth”. Distinguished from surface water which is owned by the state. Groundwater is a part of the surface estate of the land.

Who Owns it?

In 1904 the Texas Supreme Court adopted the “Rule of Capture” making clear the landowner was free to capture from his land and use as much groundwater as could be put to beneficial use. - Rule of the Bigger Pump

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Regulation of Use

- ✓ Under authority granted by the Texas Constitution, the State retains the authority to regulate the conservation of our groundwater resources.
- ✓ As a part of this regulatory scheme groundwater districts can and have been created to allow local regulation of this groundwater for “conservation” purposes.
- ✓ The number of groundwater districts in Texas has more than doubled in the last ten years.

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Cracks in the System! - New Authority of Groundwater Districts

SB-1 and SB-2 – authorized:

- ✓ A groundwater district's regulation of the production of groundwater
- ✓ A groundwater district's authority to regulate transfers of groundwater: and
- ✓ A groundwater district's ability to regulate transfers of groundwater out of the groundwater district.

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A Warning Shot –

In Sipriano v. Great Springs Waters of America, Inc. – the Texas Supreme Court commented:

In Senate Bill 1, the Legislature has chosen a regulatory solution and a democratic process to address groundwater issues - “It would be improper for courts to intercede at this time... It is more prudent to wait and see if Senate Bill 1 will have its desired effect, and to save for another day the determination of whether further revising the common law is an appropriate prerequisite to preserve Texas’ natural resources and protect property owners’ interests.”

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What is the nature and character of these Groundwater Rights we are attempting to transfer?

- Real Property?
- Personal Property?
- Vested or Unvested Rights?

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What are we trying to transfer?

Case Law:

- ✓ Groundwater is a part of the surface estate of the land (not the mineral estate);
- ✓ The owner of land has the exclusive property rights to the groundwater to be used at their will; and
- ✓ The rights to this groundwater include all rights that they might have for any other species of property.

A Vested Right!!

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How do we sell and how do we buy – groundwater??

Most Common Forms:

- ✓ Buy the land and get the groundwater as a part of the bundle of sticks (not covered in this outline)
- ✓ Purchase of groundwater in fee simple absolute
- ✓ Transfer of groundwater for a period of time
 - ✦ Fee simple determinable
 - ✦ Lease
- ✓ License
- ✓ Water supply agreements

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START WITH THE OUTRIGHT PURCHASE

Not dissimilar to a real estate sales transaction – as a starting point – **however**, there are notable differences:

Legal Description:

- ✓ What groundwater is being conveyed? – geological description;
- ✓ Determine if exclusive or non-exclusive right to develop and use groundwater; and
- ✓ If less than all of the groundwater is conveyed - determine the priority between the two estates for access and other purposes.

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Outright Purchase

Also Will Need Use of Appurtenant Surface Estate:

- ✓ The right to use the surface estate for the exploration and development of the groundwater estate on an exclusive or non-exclusive basis;
- ✓ The right to place infrastructure on the surface estate (through a fee interest, lease or easement); and
- ✓ The right of ingress and egress to construct, operate and repair a water collection system.
- ✓ Implied easement of necessity?

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Limitations on Use of Surface Estate:

- ✓ Operating covenants or behavioral covenants relating to the groundwater owner's use of the surface estate;
- ✓ Operating covenants or behavioral covenants relating to the landowner's use of the surface estate; and
 - ✦ Sanitary control easements and environmental covenants and indemnities
- ✓ Insurance requirements relating to joint use of surface estate.

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Review of Title:

- ✓ Determine that no prior severance has occurred;
- ✓ Review title for effect of prior liens and encumbrances. Remember, security instruments may encumber the groundwater estate; and
- ✓ Review mineral interests which may have a claim on the water rights. Mineral estate owners may own implied surface easements and rights to use groundwater in exploration.

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Feasibility Period Issues:

- ✓ Investigate groundwater hydrology and geology;
- ✓ Investigate water quality;
- ✓ Determine infrastructure needs and costs (wells, pipelines, etc.);
- ✓ Determine the limitations on withdrawal and transfer of groundwater set by the groundwater district or other regulatory body, if any; and
- ✓ Determine baseline environmental condition of the real property through an environmental site assessment.

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Required Closing Documents:

- ✓ Groundwater warranty deed (see attached);
- ✓ Bill of sale to convey groundwater and personal property interests associated with groundwater;
- ✓ Assignment of permit rights;
- ✓ Transfer documentation required by the groundwater district;
- ✓ Easements, leases or other documents necessary to address use and access issues.

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Required Closing Documents:

- ✓ Seller's reservation of groundwater and permit rights;
- ✓ Subordination or release of mineral interest owner's surface easement rights to use groundwater; and
- ✓ Subordination or release of deed of trust liens or other liens and security interests which encumber the groundwater.

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Other Special Issues:

- ✓ Proration of permitting fees and groundwater district fees;
- ✓ Adjustments for loss of groundwater rights after purchase; and
 - ✦ Loss to be borne by seller or purchaser?
 - ✦ Cause of reduction (seller, purchaser or systemic)?
 - ✦ Manner in which any recovery for loss is to be shared?
- ✓ Further assurances clause.

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Next - Transfer of Groundwater for a Period of Time

- ✓ **Fee Simple Determinable** - absolute title - but sometimes difficult to obtain – not as flexible as a lease unless accompanied by operating agreement
- ✓ **Lease** - Only a **possessory right** - subject to the conditions set out in the lease and the landowner's fee ownership interests, but allows for a great deal of flexibility
- ✓ **License** - A license to use groundwater is not a grant of a real property interest in the groundwater - only a personal privilege

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Transfer Of Groundwater For A Period Of Time

Special Issues: Because the groundwater is returned to the original owner at the end of the term:

- ✓ Describe the term of use; and
- ✓ Describe the condition on which the estate will terminate.

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Transfer of Groundwater for a Period of Time

Consideration:

- ✓ Will the consideration will be paid in periodic payments?
 - ❖ Address the method measuring the payment amounts, such as quantity of water withdrawn.
 - ❖ Address any “growth rate escalator” on deferred payments (PPI/CPI or others).
 - ❖ Determine if there will be minimum or guaranteed payments.

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Transfer of Groundwater for a Period of Time

Consideration:

- ✓ Determine if there will be a duty to produce all or a minimum amount of the water yield;
- ✓ Where minimum water payments are to be made, address credits for excess water payments; and

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Transfer of Groundwater for a Period of Time

Termination of Rights to Use Groundwater:

- ✓ Ownership of groundwater and facilities after termination;
- ✓ Condition of groundwater and facilities after termination;
- ✓ Return and maintenance of permits; and
- ✓ Plugging of wells upon termination.

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Transfer of Groundwater for a Period of Time

Encumbrances, Casualty, Condemnation and Indemnity:

- ✓ With Leases and Licenses – non-disturbance and attornment agreement;
- ✓ Casualty/Condemnation; and
 - ❖ Representation in connection with settlement of claims.
 - ❖ Allocations of recovery.
- ✓ Mutual indemnity.

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Water Supply Contracts

There are a myriad of ways to buy and sell water

- ✓ At one end, a lease, license or fee simple/determinable transfer of groundwater with use of additional portions of the surface estate;
- ✓ At the other end, the owner of the land produces the groundwater and provides it to a purchaser - no transfer of title;

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Water Supply Contracts

Outline of Significant Issues:

- ✓ Groundwater Designation - define area from which the groundwater will be produced - assess the groundwater commitment under drought conditions, etc.;
- ✓ Guaranteed Minimum Supply - define the minimum *quantity* of the groundwater to be delivered;
- ✓ Groundwater Quality - define the minimum *quality* of the groundwater to be delivered;
- ✓ Delivery Rates - define maximum and minimum delivery rate obligations.

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Outline of Significant Issues:

- ✓ Development Responsibility - determine who will develop and who will provide capital investment;
- ✓ Clawback of Capital Investment - in connection with delivery or quality failures;
- ✓ Allocation of Operational Responsibility - day-to-day operations, repair and maintenance, pumping, collection and delivery, treatment, storage;

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Water Supply Contracts

Outline of Significant Issues:

- ✓ Exclusive or Non-Exclusive Use - If non-exclusive, address priority of delivery rights;
- ✓ Casualty/Condemnation rights and obligations:
 - ✦ Duty to restore
 - ✦ Sharing of consideration
- ✓ Prior Encumbrances - protect priority of rights;

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Outline of Significant Issues:

- ✓ Governmental Compliance - delivery of the groundwater in compliance with all applicable laws;
- ✓ Contract with governmental entities; and
- ✓ Force majeure - issues in dealing with governmental entities;

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It ain't over till it's over!!

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