

# **REGULATORY OVERVIEW OF FERC - STATE JURISDICTION OVER WATER USE AND “WATER RIGHTS”**

## **INTRODUCTION AND SUMMARY**

At the Socioeconomic TWG meeting held on May 22, 2002 to discuss a draft Water Rights Study Plan, there was some confusion reflected in the comments of those attending as to the meaning and scope of “water rights” and the relationship of that subject to FERC relicensing. It was suggested that it might be helpful if a “regulatory overview” were prepared by SMUD, El Dorado County Water Agency, and the City of Sacramento (the City) to help explain the relationship of the water rights area to the FERC relicensing process to assist in better framing and organizing the written concerns, comments, and position statements that the members of the Socioeconomic TWG may wish to submit regarding water issues. This document presents a high level overview of the regulatory framework for that purpose. At the City’s request, it was not a co-preparer of the document; rather, the City may participate as a commenting party.

The important relationship to keep in mind is the interplay between FERC’s responsibility and authority to determine the best mix of project uses of water and the State’s authority to actually grant the water rights for such uses. It is FERC’s statutory responsibility to determine whether the plans of an initial license or relicense applicant represent the most comprehensive plan for development of the waterway for all beneficial public uses within the meaning of Section 10(a) of the Federal Power Act. FERC’s determination of what constitutes the most comprehensive plan of use, in turn, determines the license conditions the licensee must implement to fulfill the most comprehensive plan of beneficial public uses. The authority under the FERC license allows a water rights applicant to demonstrate that it can put the rights applied for to “beneficial use,” as it must under state water law.

It should also be kept in mind that the Master Memorandum of Understanding (MMOU) executed by SMUD, El Dorado County Water Agency (on behalf of itself and other entities it represents) and El Dorado Irrigation District establishes the manner in which issues relating to water rights and supply will be treated in SMUD’s relicensing. That is, issues relating to future needs, supply, and/or storage for El Dorado County entities will be dealt with outside relicensing under the MMOU. Per the terms of the MMOU, the issue of reoperation of the UARP to enhance current or existing water and storage rights is within the ambit of relicensing. Thus, the focus of the Socioeconomic TWG is confined solely to those matters within the relicensing, namely reoperation of the UARP to enhance current or existing water rights.

As agreed at the Socioeconomic TWG meeting, this statement represents a framework agreed upon by the drafters. This paper is solely intended to provide a general background discussion and not to memorialize the legal position of any party. Other stakeholders views may differ and for purposes of creating the record, those stakeholders may submit position statements.

## **SUMMARY OF LAW APPLICABLE TO UARP**

Following is the statutory framework of the relationship of water uses and water rights in the relicensing context.

### **Federal Law**

#### **Federal Power Act (FPA)**

The primary provisions of the FPA that frame the relationship between FERC's authority to determine project uses and the State's authority to grant the water rights for such uses are found in FPA Sections 4, 9, 10 and 27.

Section 4(e) of the FPA sets out the Commission's jurisdictional authority to issue licenses for projects located on Federal lands, navigable waters of the U. S., or those affecting interstate commerce. It also provides in relevant part:

In deciding whether to issue any license under this Part for any project, the Commission, in addition to the power and development purposes for which licenses are issued, shall give equal consideration to the purposes of energy conservation, the protection, mitigation of damage to, and enhancement of fish and wildlife (including related spawning grounds and habitat), the protection of recreational opportunities, and the preservation of other aspects of environmental quality.

Section 9(a)(2) of the FPA requires a license or relicense applicant to submit to FERC:

Satisfactory evidence that the applicant has complied with the requirements of the laws of the State or States within which the proposed project is to be located with respect to bed and banks and to the appropriation, diversion, and use of water for power purposes and with respect to the right to engage in the business of developing, transmitting, and distributing power, and in any other business necessary to effect the purposes of a license under this chapter.

Section 10(a) (1) of the FPA requires that the Commission license the project that represents the most "comprehensive plan" for developing the waterway for all beneficial public uses. Section 10 requires that all licenses issued shall be on the following conditions:

That the project adopted, including the maps, plans, and specifications, shall be such as in the judgment of the Commission will be best adapted to a comprehensive plan for improving or developing a waterway or waterways for the use or benefit of interstate or foreign commerce, for the improvement and utilization of water-power development, for the adequate protection, mitigation, and enhancement of fish and wildlife (including related spawning grounds and habitat), and for other beneficial public uses, including irrigation, flood control, water supply, and recreational and other purposes referred to in section 797(e) [4(e)] of this title; and if necessary in order to secure such plan the Commission shall have authority to require the modification of any project and of the plans and specifications of the project works before approval.

Finally, Section 27 of the FPA reserves state jurisdiction over “proprietary” water rights:

Nothing contained in this chapter shall be construed as affecting or intending to affect or in any way to interfere with the laws of the respective States relating to the control, appropriation, use, or distribution of water used in irrigation or for municipal or other uses, or any vested right acquired therein.

### **Section 401 of the Clean Water Act (CWA)**

Section 401 of the Clean Water Act requires any applicant for a federal permit or license for an activity which may result in any discharge of a pollutant into navigable waters to provide the federal agency with a certification from the appropriate state agency (in California, the SWRCB) that the discharge will comply with specified provisions of the Act. This requirement, however, is waived if the state agency does not act on the applicant’s certification request within one year. The section also authorizes the state agency to include in any certification any effluent and other limitations and monitoring requirements to assure that the applicant will comply with specified Clean Water Act limitations and standards and with any other appropriate requirement of state law. These must become conditions on the federal permit or license.

### **State Law**

#### **Water Rights Law**

In California, water quality permitting, section 401 certification, and water rights permitting authority is under the same agency umbrella, the State Water Resources Control Board (SWRCB).

River and other surface water may be diverted, stored, and used only under a valid water right. Two types of rights exist in California: riparian rights and appropriative rights. Riparian rights are an incident of ownership of land riparian (adjacent) to the river; they do not allow storage, must be used on the riparian land, and do not require a permit.

Appropriative rights are of two types: pre-1914 appropriative rights, which must have been perfected by mid-1914 and must have been used essentially continuously since then, and post-1914 appropriative rights, which require a permit (or license based on a permit) granted by the SWRCB. Because appropriative rights are based on seniority (first in time, first in right), the Board will consider an application for a permit only if there is unappropriated water in the stream available for appropriation (the Board has declared the American River to be fully appropriated from July 1 to October 31 ). Water rights are required whether the use is consumptive (e.g., irrigation or municipal supply) or non-consumptive (e.g., power generation). Water rights within each category also further specify the types of use that are authorized, the place of use, the place of storage (if any), and the place where water may be diverted. These limitations may be changed by action of the board, but only if the change does not adversely affect any water right holder, senior or junior.

## **Applicable Area of Origin Statutes**

Although California has several “area of origin” statutes, only two have any application to the upper American River. The Watershed Protection Act (Water Code section 11460) protects the watershed of origin from exports associated with the State Water Project and the federal Central Valley Project; this law is not implicated by the UARP re-licensing. The other is the so-called “county of origin law” (Water Code section 10505), which in essence subordinates the state’s rights under water right applications filed in the 1930’s to the needs of the county in which the water originates. These applications are held by the SWRCB.

## **Instream Flow Protection**

Instream values can be protected in California in several ways. Among them are Water Code section 1243, which provides that “use of water for recreation and preservation and enhancement of fish and wildlife resources is a beneficial use of water” that must be considered when the SWRCB acts on applications for other uses. Water may be appropriated for such purposes so long as a diversion or impoundment of water is involved. The SWRCB may include terms and conditions in appropriative rights to maintain bypass flows and may modify these requirements if it has retained appropriate jurisdiction. Fish and Game Code section 5937 authorizes the SWRCB to require the operator of a dam to release water if necessary to keep fish below the dam in good condition.

## **SMUD’s WATER RIGHTS AND WATER RIGHT AGREEMENTS**

### **SMUD’s UARP Water Rights**

During the 1940’s and early 50’s, SMUD filed five applications for water rights for the UARP. Three were for non-consumptive power uses, including two that provided for storage at Union Valley, Ice House, and Loon Lake Reservoirs. Two were for consumptive municipal water supply uses. The SWRCB issued permits to SMUD for the three power applications on April 30, 1957 (licenses were issued in 1975 and 1980). SMUD has two other water rights for the UARP, issued under applications filed in 1965 and 1981. One of these provides additional storage at Ice House. The two original storage rights also provide that no diversion or use of water by SMUD may be made which will interfere with diversion or use of water for irrigation or domestic purposes under water rights that are senior or junior to SMUD’s, and the Ice House storage right is subordinate to future upstream domestic and stockwatering uses and to other future uses in the watershed if the SWRCB determines SMUD’s use is unreasonable in light of the proposed other use. SMUD’s other large reservoirs are regulating reservoirs and storage for more than 30 days is not permitted.

### **SMUD’s Agreement with the City of Sacramento**

On June 28, 1957, SMUD assigned its two consumptive use applications for municipal water supply to the City of Sacramento. That agreement specified that, as between SMUD and Sacramento, the City’s rights under the assigned applications and “any other rights City may acquire in water conserved by [SMUD’s] Upper American River Project” are subordinate to SMUD’s rights under its three power (non-consumptive) water rights.

## **SMUD's Agreement with El Dorado County**

On July 11th, 1957, SMUD and El Dorado County signed an agreement (supplemented in December 1961) which gives El Dorado County or a public agency assignee the right to use SMUD's Slab Creek Reservoir and White Rock Penstock to divert up to 40,000 afy (with some exceptions). The agreement specifies that it "relates only to the use of [SMUD's] facilities by County" and that El Dorado's diversions must occur "by virtue of permits issued to it by the State Water Rights Board." In exchange, El Dorado must pay SMUD for the replacement cost of its lost power generation.

## **QUESTIONS RAISED BY THE SOCIOECONOMIC TWG**

At the Socioeconomic TWG meeting held on May 22, 2002, SMUD provided its initial responses to three questions before the group:

57. To what extent does the City of Sacramento's (all claimed water rights in the in the Project area) consumptive water rights affect UARP operations?
58. To what extent would reassignment of SMUD's still-held, Project related consumptive water rights affect UARP operations?
59. To what extent do all consumptive water rights and other contractual obligations affect the Project's operation?

In summary, SMUD's responses to those questions, respectively, were that the City of Sacramento's consumptive rights are subordinate to SMUD's power generation rights; the UARP does not hold any consumptive rights; and that UARP has no reasonable potential to have a substantial impact on existing water rights.

## **ISSUES FOR THE MASTER MEMORANDUM OF UNDERSTANDING**

The SMUD/EDCWA/EID MMOU proposes to study changes in UARP operation, and to identify possible modifications to existing UARP facilities such as reservoir expansion or development of new facilities, which could benefit water supply and power generation purposes. Changes in UARP operation may be possible to benefit El Dorado's water supply needs. These operational changes may be possible without adversely affecting SMUD's power generation rights or revenues and such changes may, or may not, necessitate a change in El Dorado's consumptive rights in terms of its points of storage and diversion. For instance, El Dorado believes that a multi-party transfer agreement might enable El Dorado to utilize releases from UARP storage at Folsom Reservoir at times when El Dorado is restricted from diverting its own water from its own storage facilities located further upstream, in exchange for relinquishing El Dorado releases at other times.

## **GENERAL DISCUSSION**

### **FERC Authority**

Stakeholders and governmental agencies participating in the UARP relicensing proceeding may be seeking changes in Project flow patterns to benefit particular beneficial uses, e.g., requests for changes in release schedules to benefit rafting or for fish and wildlife enhancement. FERC project relicensings have typically resulted in a reduction of power generation as a result of increased stream flow requirements to benefit fish and wildlife and operational changes related to recreation and other public purposes. Changes in release schedules to accommodate rafting interests could result in a loss of power generation, or power value, by increasing water releases in off-peak periods. These changes, if required by FERC, would shift the water use from a power generation or “developmental” purpose, to a “non-developmental” purpose, but still under the existing state water right for the project.

FERC’s licensing authority extends beyond the mere ability to require changes among or affecting just non-consumptive or instream uses. Under FPA section 10(a), upon relicensing the FERC has the authority to require the license applicant to modify its proposed plans of development to satisfy the statutory requirement that it license the most comprehensive plan for all beneficial public uses. The U.S. Supreme Court has construed section 10(a) as creating a “public interest test.”<sup>1</sup> While the local and regional need for power is relevant to the public interest, “[t]he test is whether the project will be in the public interest. And that determination can be made only after a full exploration of all issues relevant to the ‘public interest,’ including future power demand and supply, alternative sources of power, and public interest in preserving reaches of wild rivers and wilderness areas, the preservation of anadromous fish for commercial and recreational purposes, and protection of wildlife.”<sup>2</sup>

Particularly in the context of a project relicensing, it is important to recognize that section 10(a)’s mandate is dynamic, not static. “Comprehensive development is a concept that evolves over time, reflecting different era’s technical options, economic realities, and resource use priorities.”<sup>3</sup> The Commission’s determination of the project best adapted to a comprehensive plan will dictate the nature and scope of the license conditions necessary to carry out such a plan. All FERC licenses contain a Standard License Article that requires that a licensee obtain and maintain all necessary property rights, including water rights, necessary to carry out project purposes.

### **Tension between FERC and State Authority**

Since enactment of the FPA in 1920, judicial holdings have interpreted the reach of Sections 9 and 27. The early cases confirmed the legislative determination to avoid unconstitutional invasion of state jurisdiction, and recognized a dual system of control with each jurisdiction having final authority within its own jurisdiction. However, those cases found the Commission to have the superior right to regulate interstate and foreign commerce and thus held that a licensee could not be precluded from operating a hydroelectric project for failure to obtain a conflicting state permit.<sup>4</sup>

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<sup>1</sup> *Udall v. FPC*, 387 U.S. 428, 450 (1967).

<sup>2</sup> *Id.*

<sup>3</sup> *City of Fort Smith, Arkansas*, 44 FERC ¶ 61,160 (1980).

<sup>4</sup> *First Iowa Hydro Electric Cooperative v. Federal Power Commission*, 328 U.S. 152 (1946).

In later cases, the U.S. Supreme Court stated: 1) that the FPA was not intended to abolish, or eliminate, without just compensation, any existing proprietary rights to use water for power production, and 2) that the only purpose of Section 27 was to preserve to holders of state-conferred water rights a right to compensation if those rights were taken or destroyed as incident to exercise by another of a license granted by FERC, and that the intent was not to give a state power to veto FERC action.<sup>5</sup> Thus, the U.S. Supreme Court denied an attempt by the State of California to prevent issuance of a license based on the applicant's failure to comply with the State's instream flow demands.<sup>6</sup>

These cases, however, did not address the Clean Water Act (CWA), which the U.S. Supreme Court has since interpreted as giving state water quality permitting authorities broad conditioning authority over water quality and quantity for FERC licensees.<sup>7</sup> Consequently, FERC's determination of the best mix of beneficial project uses may end up being challenged in the state water rights forum or, more likely, in the state water quality regulatory forum, both of which in California are the SWRCB.

There are unanswered questions as to the outcome of a situation whereby FERC orders a project operational regime necessitating the licensee's use of the Federal power of eminent domain (condemnation) to acquire the necessary water rights for such an operation. We are unaware of any FERC or court decisions that have involved the attempt of a FERC license applicant to acquire by eminent domain water rights needed to carry out FERC-mandated purposes that conflict with existing water rights. FERC is likely to be deferential to such state water rights permitting authority and will probably do what it can to avoid such a situation. Furthermore, it is more likely, that a FERC-mandated operation regime would be challenged in the water quality certification arena, rather than the water rights permitting arena, and as previously noted, the U.S. Supreme Court case held that States can determine the quantity of water flows for water quality and other non-water quality purposes.<sup>8</sup>

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<sup>5</sup> *Federal Power Commission v. Niagara Mohawk*, 347 U.S. 239 (1954) and *Scenic Hudson Preservation Conference v. Federal Power Commission*, 453 F. 2d 463 (C.A.N.Y. 1971), *certiorari denied* 407 U.S. 926. However, the Court in *Niagara Mohawk* was not construing the scope and effect of Section 27. Moreover, the court in *Scenic Hudson* found that no party's water rights were impaired by the proposed project.

<sup>6</sup> *California v. FERC*, 495 U.S. 490 (1990); see also *Sayles Hydro Associates v. Maughn*, 985 F. 2d 451 (C.A. 9<sup>th</sup> 1993). Those cases held that the Section 27 savings clause only protected from supersedure state laws that relate to the distribution of water used in irrigation or for municipal or other uses, but did not apply to the state's minimum stream flow requirements designed to protect fish.

<sup>7</sup> In *PUD No. 1 of Jefferson County v. Washington Department of Ecology*, 114 S. Ct. 1900 (1994), the U.S. Supreme Court sustained the authority of state water quality permitting agencies to impose broad environmental conditions on federally licensed activities involving discharges into waterways and wetlands under the authority of Section 401 of the CWA. The state agency had conditioned the City of Tacoma's Section 401 certification on maintenance of certain minimum instream flows for fish habitat, which Tacoma asserted were unnecessarily high, would make the project economically infeasible, and exceeded the agency's certification authority. The dissent argued that the majority's holding gave the states exactly the veto power over hydroelectric projects which previous Supreme Court holdings in *California v. FERC* and *First Iowa* expressly held they did not possess.

<sup>8</sup> Other cases of interest are summarized below.

*National Wildlife Federation v. FERC*, 912 F.2d 1471 (D.C. Cir. 1990). Holding: Under section 4(e) of the FPA, the benefit of a secure and increased water supply may be considered as a development benefit or purpose to be weighed against environmental detriments from a proposed project. It further stated that pursuant to section 10(a)(1) of the FPA the Commission "must ensure that proposed projects are best adapted to serve a number of beneficial public uses 'including . . . water supply'" . . . and "[g]iven that the Commission is explicitly directed to consider the water-supply benefits of a proposed project in deciding what modifications, if any, to require of a proposal, it makes sense that the Commission is also empowered to consider those benefits in deciding whether to grant a license at all."

## **Issues Under the SMUD/El Dorado Contract**

Should El Dorado choose to exercise its rights under the contract, issues raised include what and whose water rights might be used to implement that contractual right and what impacts such a diversion would have on UARP's power generation. Compensation for negative economic impacts on UARP power generation would be required per the terms of the contract.

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Boise Cascade Corp., 36 FERC ¶61,135 (1986), Holding: State water rights are subordinate to a licensee's right to use water. FERC denied a request that a license be conditioned to prevent the licensee from obtaining water rights that would interfere with water rights under state law. The Idaho Department of Water Resources (IDWR) complained that FERC's decision presumed to vest ultimate control over future upstream diversions in FERC rather than in the states. FERC offered the following concession: "[W]e can require the licensee to reasonably reduce its use of water for generation to coincide with reductions in flows caused by future upstream diversions if we . . . conclude that it would be in the public interest to accommodate such upstream diversions. IDWR can petition [FERC] at any time to have us exercise our authority." FERC determined that the record evidence did not support inclusion of a license condition requiring subordination. FERC went further: "Moreover, by reserving the right to permit unlimited diversion upstream of the project, IDWR's condition would in essence vest in it, rather than [FERC], ultimate control over operation and continued viability of the project. Indeed, it would enable IDWR to nullify key rights Boise has under the license. We do not believe this would be consistent with Congress' intent in enacting the Act." [citing *First Iowa, supra*].

Boise-Kuna Irrigation District, 53 FERC ¶61,328 (1990) Holding: FERC included an article in the license providing that the project may not reduce or impair delivery of water for irrigation purposes pursuant to any state grant of a right to use natural river flows. FERC stated that although the operation requirements for the Federal Reclamation dam where Boise-Kuna's hydro plant was located adequately provided for protection of existing natural flow rights, the Commission nevertheless added a new protective license condition "in the interest of providing clearer assurance that existing water rights will be protected."

Rancho Riata Hydropower, 54 FERC ¶61,176 at 61,134 (1991). Holding: FERC held that the standard reservation of authority can be used to subordinate project water use to specific other uses, including irrigation, but denied to do so on the facts in before it. However, FERC made clear its authority to address the project's impact on water rights if it needed to in the future. FERC noted that a Standard License article protected its right to reopen and modify the license as necessary to address the use, storage and discharge from storage of waters affected by the license and it could under that authority insert in the license a clause subordinating project water use to specific other water uses. However it stated that was not indicative of whether future conflicts between project water use and other water rights would justify imposing a subordination clause, only that persons may pursue such a remedy if a real conflict developed. In 59 FERC ¶61152 (1992), FERC determined that there were inadequate flows to both meet downstream consumptive demands and upstream power production; it requested additional flow release data from all the parties: In 63 FERC ¶61221 (1993), FERC determined that the licensee would have to increase minimum flows and that it appeared that would result in the project operation being uneconomic. On August 10, 1995 FERC issued its "Order Accepting Surrender of License" for the Project.