Water as a Public Resource: Emerging Rights and Obligations (Summer Conference, June 1-3) 1987

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Public Interest Review of Water Right Allocation and Transfer in the West: Recognition of Public Values

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I. Introduction

A. The appropriation doctrine is the major water right system in the West. See 3 W. Hutchins, Water Rights Laws in the Nineteen Western States 141-649 (1977).

B. The states have responded in various ways to growing concern about public values in water such as scenic beauty, recreational use, and fish and wildlife habitat. The range of responses is covered by various presentations at this conference. One response, and the subject of my presentation, builds on an appropriation doctrine statutory tradition requiring review of proposed appropriations for conformity with the public interest.

C. Earlier discussions of public interest review include E. Clyde & D. Jensen, Administrative Allocation of Water (Nat'l Water Comm'n Legal Study No. 3, 1971); Clyde, Allocation of Water for Resource Development, 14 Nat. Res. Law. 519 (1981); Robie, The Public Interest in Water Rights Administration, 23 Rocky Mt. Min. L. Inst. 917 (1977).

II. States with Public Interest Review

A. Sixteen western states by statute mandate public interest review of initial water right allocation. The statutes require a permit from an administrative agency to appropriate water and typically allow a permit to issue only if the proposed appropriation conforms to the public interest or public welfare. Alaska Stat. §§ 46.15.040, -.080(a) (1984 &

Supp. 1986); Ariz. Rev. Stat. Ann. §§ 45-142, -143 (Supp. 1986); Cal. Water Code §§ 1225, 1255 (West 1971 & Supp. 1987); Idaho Code §§ 42-201, -203A, -203C (Supp. 1986); Kan. Stat. §§ 82a-705, -711 (1984); Mont. Code Ann. §§ 85-2-302, 311(2) (1985) (does not use typical "public interest" or "public welfare" phrasing but a permit can issue for larger appropriations only if the proposed use is "a reasonable use," which is defined in terms of typical public interest criteria); Neb. Rev. Stat. §§ 46-233, -234, -2,116 (1984); Nev. Rev. Stat. §§ 533.325, -.370(3), 534.050(1) (1985); N.M. Stat. Ann. §§ 72-5-1, -6, -7, 72-12-3, -3.E (1985); N.D. Cent. Code §§ 61-04-02, -06 (1985); Or. Rev. Stat. §§ 537.130, -170(4) (1985); S.D. Comp. Laws Ann. §§ 46-1-15, -5-10, -6-3, -2A-9 (1983); Tex. Water Code Ann. §§ 11.121, -.134(3) (Vernon Supp. 1987); Utah Code Ann. §§ 73-3-1, -8(1) (1980 & Supp. 1986); Wash. Rev. Code Ann. §§ 90.03.250, -.290, -44.050, -44.060 (1962); Wyo. Stat. §§ 41-4-503, -3-930 to -932 (1977 & Supp. 1986).

B. Public interest review for water right transfers has a shorter history and less, but growing, acceptance.

1. Most states by statute require a permit for transfers that entail a change in point of diversion, place of use, nature of use, or time of use of a water right.

2. A water law text published in 1971 reported only one state with a statute listing detriment to the public interest as a ground for denial of a permit. 1 W. Hutchins, supra, at 641-44 (1971). Today, such statutes exist in eight states.

Idaho Code § 42-222(1) (Supp. 1986); Kan. Stat. § 82a-708b (Supp. 1986); Mont. Code Ann. § 85-2-402(3) (1985) (does not use the phrases "public interest" or "public welfare," but a permit to change larger rights can issue only if the proposed change is "a reasonable use," which is defined in terms of typical public interest criteria); Neb. Rev. Stat. § 46-290, -294 (1984); Nev. Rev. Stat. § 533.370(3) (1985); N.M. Stat.

Ann. § 72-5-23, -5-23, -12-7, -12B-1 (1985 & Supp. 1986); N.D. Cent. Code § 61-04-15.1 (1985); S.D. Comp. Laws § 46-2A-12 (1983).

3. Two more states by statute require consideration of certain public effects of proposed transfers, namely, impact on instream beneficial uses, Cal. Water Code §§ 1725 (temporary change), 1735 (trial transfer), 1738 (long-term transfer) (West Supp. 1987), and economic effect on the community, Wyo. Stat. § 41-3-104 (1977).

4. Furthermore, public interest review of transfers might not require express statutory authority.

   a. At least two courts have held public interest review was implicitly required by various water code provisions. In re Howard Sleeper, Rio Arriba County Cause No. RA 84-53(C), letter to counsel, at 5-6 (April 16, 1985) (case arose before New Mexico enacted a statute expressly requiring public interest review), appeal docketed Ensenada Land & Water Ass'n v. Sleeper, No. 8720/8830 (Ct. App. N.M. 1985); Clark v. Briscoe Irr. Co., 200 S.W.2d 674 (Tex.Civ.App. 1947).

   b. Alaska has no express statutory public interest review requirement, but an administrative rule requires it. 11 Alaska Admin. Code § 93.930(c) (1983).

III. Historical Perspective

A. In 1890, Wyoming enacted the first permit system for

appropriating water. The legislation authorized the state engineer to reject proposed appropriations that would be detrimental to the public interest, but it did not in any way define the public interest. As other states adopted permit systems, their statutes followed the pattern of not defining the public interest. Office of Experiment Stations, U.S. Department of Agriculture, State Engineer and His Relation to Irrigation 96 (Bulletin 168, 1906).

B. Four cases decided between 1910 and 1915 helped shape the new and amorphous public interest concept. Young & Norton v. Hinderlider, 15 N.M. 666, 110 P. 1045 (1910); Cookinham v. Lewis, 58 Or. 484, 114 P. 88 (1911), reh'g denied 58 Or. 484, 115 P. 342 (1911); In re Commonwealth Power Co., 94 Neb. 613, 143 N.W. 937 (1913); Big Horn Power Co. v. State, 23 Wyo. 271, 148 P. 1110 (1915) (report of state engineer's action on a permit application that was not appealed). A common thread runs through these cases: Economic development is in the public interest, and a project that will impede maximum development is detrimental to the public interest.

C. The half century following the initial group of cases was characterized by quiescence. Applications to appropriate evidently generated little controversy, probably because nearly all proposed beneficial uses were viewed as serving the public interest.

1. The most notable legislative development was a

1929 Oregon law that said in determining the public interest, "the state reclamation commission shall have due regard for conserving the highest use of . . . water for any and all purposes, including [among others] public recreation and the protection of commercial and game fishing or any other beneficial use to which the water may be applied." Act of Feb. 28, 1929, ch. 245, § 1, 1929 Or. Laws 252-53.

2. The major public interest review case during this period was Tanner v. Bacon, 103 Utah 494, 136 P.2d 957 (1943), where the court upheld a decision by the state engineer to subordinate an application for power use that would interfere with a junior application for domestic and irrigation purposes in addition to power use. The court reasoned that the greater beneficial use of the latter project would better serve the public interest. A common law use preference for domestic and agricultural uses also appears to have figured into the decision.

D. A striking theme emerges from Tanner and the earlier cases: Public interest review meant little if anything beyond assessing whether a proposed appropriation would conform to the goal of maximizing economic development. No attention was given to the effect of a proposed appropriation on public values such as scenic beauty, recreational use, and

fish and wildlife habitat.

IV. Content of Modern Public Interest Review

A. Relevant Factors

1. Modern statutes on water right allocation and transfer vary in how much guidance they give administrative officials about potentially relevant factors in public interest review.

   a. Permit statutes in three states comprehensively define the public interest and include public values. Alaska Stat. § 46.15.080(b) (1984); N.D. Cent. Code § 61-04-06 (1985); Or. Rev. Stat. § 537.170(5) (1985). The Alaska statute, for example, enumerates eight factors bearing on the public interest, including "(3) the effect on fish and game resources and on public recreational opportunities; (4) the effect on public health; . . . [and] (8) the effect upon access to navigable or public waters."

   b. Some permit statutes lack comprehensive definition of the public interest but still give significant guidance on relevant factors and expressly include some public values in the calculus. For example, in California a series of statutes governing new appropriations requires consideration of the state water plan; the relative benefit from various beneficial uses of the water

concerned including, among others, preservation and enhancement of fish and wildlife and recreation; streamflow requirements proposed for fish and wildlife purposes under other legislation; water quality control plans established under other legislation; and a state goal of providing a decent home and suitable living environment for every Californian. Cal. Water Code §§ 1256-59 (West 1971 & Supp. 1987).

c. Finally, other permit statutes give little or no specific guidance about public interest review or the role of public values therein. E.g., Nev. Rev. Stat. § 533.370(3) (1985); N.M. Stat. Ann. §§ 72-5-6, -5-23, -12-3.E, -12-7 (1985 & Supp. 1986); Wash. Rev. Code Ann. §§ 90.03.290, -.44.060 (1962).

2. The Washington and Idaho courts have construed statutes that lack specific guidance on relevant factors.

a. Stempel v. Department of Water Resources, 82 Wash.2d 109, 508 P.2d 166 (1973), arose under a statute that prohibits appropriations detrimental to the public welfare but says nothing about relevant factors. The department argued that it did not have to consider the water quality effects of a

proposed appropriation because (1) other state agencies had authority to regulate pollution and (2) the statutory public welfare criterion for water permits dated back to 1917 and in historical context was unrelated to pollution concerns. The court rejected both arguments, relying on two recent pieces of legislation to supplement the vacuous permit statute. The State Environmental Policy Act of 1971 made environmental protection a mandate of every state agency for major actions significantly affecting the environment, and the Water Resources Act of 1971 declared a policy of protecting and enhancing the natural environment. These acts, said the court, obligated the department to consider the total environmental and ecological factors of proposed appropriations.

b. Shokal v. Dunn, 109 Idaho 330, 707 P.2d 441 (1985), involved a statute that prohibits appropriations detrimental to the local public interest and defines that phrase vaguely as "the affairs of the people in the area directly affected by the proposed use." Idaho, unlike, Washington has no state environmental policy act or broad water resource policy act. However, the court

found other legislative guidance that showed public values were an important component of the local public interest.

The Idaho legislature did not add a public interest clause to the permit statute until March 29, 1978; and on the same day it also enacted minimum streamflow legislation expressly designed to protect fish and wildlife habitat, aquatic life, recreation, aesthetic beauty, transportation and navigation values, and water quality. The court concluded that the legislature must have intended the local public interest in the contemporaneous water permit statute to include the same elements. Furthermore, the court said that common sense suggests the local public interest includes the comprehensive list of factors enumerated in the Alaska permit statute, plus such specifics as discouraging waste and encouraging conservation. It summed up by saying that the legislature intended to include any locally important factor impacted by proposed appropriations.

3. Related to the statutory construction question just discussed is the administrative law doctrine of nondelegation, which limits the delegation of legislative or judicial powers to

an administrative agency. A common formulation of the doctrine says a delegation is invalid unless limited by standards to guide administrative discretion and enable judicial review to determine whether the agency followed the standards. See 1 F. Cooper, State Administrative Law 54-61 (1965).

a. The doctrine was argued without success in several older water permit cases. East Bay Mun. Util. Dist. v. Dep't of Public Works, 1 Cal.2d 476, 35 P.2d 1027 (1934); Clark v. Briscoe Irr. Co., supra; Tanner v. Bacon, supra.

b. Dictum in a recent case suggests a different approach. The Oregon permit statute for new appropriations comprehensively enumerates factors that bear on the public interest. But the court hinted that if this were not the case, it "might" require the permit agency to adopt rules establishing more definite standards before acting on permit applications. Steamboaters v. Winchester Water Control District, 69 Or. 596, 688 P.2d 92 (1984).

B. Weighing the Factors

1. Even the permit statutes that provide considerable guidance about relevant factors typically give little help on how to weigh them.

2. This is true of the Alaska permit statute, and that is no accident. Alaska's water use act is based on a proposed water code the state employed Frank J. Trelease to draft. In his report to the state setting forth and explaining the code, Trelease commented on public interest review of permit applications: "Making decisions . . . will be difficult. No law can make them, they must be made by people. . . . [T]he balancing of benefits against cost must be performed by the exercise of judgment." F. Trelease, A Water Code for Alaska, A Report to the State of Alaska 14-17 (1962), excerpted in F. Trelease & G. Gould, Cases and Materials on Water Law 138-40 (4th ed. 1986).

3. Some states have statutes that appear quite specific about certain aspects of the public interest, such as detailed use preference or area-of-origin protection statutes. E.g., Ariz. Rev. Stat. Ann. § 45-147 (Supp. 1986) (use preference); N.D. Cent. Code § 61-04-06.1 (use preference); MacDonnell & Howe, Area-of-Origin Protection in Transbasin Water Diversions: An Evaluation of Alternative Approaches, 57 U.Colo. Rev. 527 (1986) (comprehensive coverage of area-of-origin legislation).

Nonetheless, under at least some of these statutes a flexible or balancing approach might

still apply. See, e.g., East Bay Mun. Util. Dist. v. Dep't of Pub. Works, supra, 35 P.2d at 1029 (hinting that a preference in issuing permits for domestic use and then for irrigation over other uses might be invocable only "[w]here the facts justify the action"); City of San Antonio v. Texas Water Commission, 407 S.W.2d 752 (Tex. 1966) (area-of-origin statute barring transport to another watershed to the "prejudice" of anyone in the source watershed must be construed in light of another statute calling for maximum use of water; therefore, "prejudice" can be found only if the benefits of transbasin use would be less than the detriment to the source watershed.)

4. The Shokal case, supra, from Idaho addressed how to weigh the relevant factors:

> The relevant elements and their relative weights will vary with local needs, circumstances, and interests. For example, in an area heavily dependent on recreation and tourism or specifically devoted to preservation in its natural state, [the Department of] Water Resources may give great consideration to the aesthetic and environmental ramifications of granting a permit which calls for substantial modification of the landscape or the stream.

109 Idaho at 339, 707 P.2d 450. This does not mean that all public interest elements are flexible. The court also said the department should not issue a permit for a proposed

facility that would violate mandatory water quality standards, even though a different state agency has the primary responsibility for water quality. Apart from that, however, the court said that the determination of "what the public interest requires, is committed to Water Resources' sound discretion." 109 Idaho at 339, 707 P.2d at 450.

5. The exercise of administrative discretion is subject to judicial review. The scope of review varies among the states.

   a. One approach is a trial de novo, in which the court hears new evidence and makes a new decision with no deference to the administrative determination. E.g., Utah Code Ann. § 73-3-15 (1980).

   b. More commonly, review is on the administrative record with the courts applying various tests depending on the jurisdiction and the issue on appeal. The courts generally use standard administrative law jargon such as error of law, lack of substantial evidence for factual findings, clearly erroneous, arbitrary or capricious, and abuse of discretion.

   c. Bank of America National Trust & Savings Ass'n v. State Water Resources Control Board,42 Cal.App.3d 198, 116 Cal.Rptr. 770

(1974), illustrates the limits of agency discretion under the substantial evidence standard. The board had issued permits to a land developer to store water in offstream reservoirs, subject to the condition that certain reservoirs on the developer's land be kept open to the public for recreational use. It concluded the condition was in the public interest because the developer's diversions would reduce the streamflow, and public access to the reservoirs would compensate the public for diminished recreational opportunities on the stream and possible adverse effects on fish.

On appeal, the court acknowledged the board had power to impose a public access condition if supported by substantial evidence in the record. However, the court decided that the record failed to support the board's fears about diminished recreational opportunities and effects on fish life, so it struck down the public access condition.

C. Two Recent Decisions

1. In re Application for Water Permit No. 4580A-3, Findings of Fact, Conclusions of Law, and Final Decision of South Dakota Water Management Board (Oct. 29, 1986), dealt with unpleasant odor as a

relevant factor. A permit applicant sought to appropriate groundwater for a large hog farm to be located a couple miles from two recreation areas on the Missouri River. The state water management board found that nearly 127,000 people visited the recreation areas annually and that the value of the recreational use was $2.5 million per year. It said that the occasional presence of unpleasant odors from the hog farm at the recreation areas was a significant public interest concern. However, it concluded that the probable difficulties with odors were outweighed by the probable benefits from economic development of the hog farm, which would employ six people, use 200,000 bushels of locally grown corn annually, and purchase significant amounts of other materials in the area.

2. In re Howard Sleeper, supra, a New Mexico trial court decision now on appeal, considered public interest factors in a water right transfer. The applicable permit statute failed even to mention the public interest, let alone define it. The trial court ruled, however, that as a matter of common sense detriment to the public interest was an implicit barrier to transfer. It concluded that the proposed transfer would be detrimental to the public interest.

a. More specifically, the Sleeper court on de novo review overturned the state engineer's approval of an application to transfer about fourteen acre feet of water annually from irrigated agriculture in northern New Mexico to create an artificial lake at a planned resort complex. The court focused on two factors in finding detriment to the public interest. First, although the proposed resort would aid economic development of the area, the poverty-stricken local residents would receive little economic benefit because they would end up in menial jobs such as waiters and maids. Second, northern New Mexicans have a fierce pride in their culture, and ties to the land and water are central to that culture. Although the proposed transfer involved a small quantity of water, the court feared the resort development represented the first step toward destruction of the local culture. In sum, the court took a broad view of public interest factors, treating as relevant both the distribution of economic benefits and cultural values not measurable in dollars.

b. Furthermore, the court did not mince words in weighing the factors. The trial judge said: "I am persuaded that to transfer water

rights, devoted for more than a century to agricultural purposes, in order to construct a playground for those who can pay is a poor trade, indeed." Letter to counsel, at 7 (April 16, 1985).

V. Function of Public Interest Review

A. The content of public interest review has clearly changed over the years. To focus only on change, however, can be misleading. This section undertakes to show that despite changing content, the essential function of public interest review has remained constant.

B. Administrative regulation of economic activities is typically based on a perceived failure of market forces to deal adequately with particular structural problems. S. Breyer, Regulation and Its Reform 15 (1982). With water resources, the key structural problem is externalities.

1. An externality exists when an appropriator's water use affects others, negatively or positively, but the appropriator does not take those effects into account. In other words, some of the costs or benefits of the appropriator's water use are external to the his or her calculations in deciding whether to make the use.

2. The problem with externalities is that they tend to cause resource misallocation. For example,

if an irrigator of sugar beets does not have to take into account the loss of downstream recreational opportunities associated with his water diversion, the result might well be the production of too many sugar beets (or at least the use of too much water in their production) and too little downstream recreation.

C. Externality theory underlies modern public interest review. See Trelease, Policies for Water Law: Property Rights, Economic Forces, and Public Regulation, 5 Nat. Res. J. 1 (1965). The Alaska water permit statute's elaborate definition of public interest factors reads like a catalog of potential negative and positive water use externalities. Although Idaho's permit statute lacks a detailed definition of the public interest, externality theory almost leaps out from its definition of the "local public interest" as "the affairs of the people in the area directly affected by the proposed use." The Idaho court in Shokal did not use the technical language of externality theory, but it embraced the essence of that theory when it said "the legislature intended to include any locally important factor impacted by proposed appropriations."

D. A closer look at the history of public interest review reveals that from very the beginning the courts were instinctively applying externality

theory.

1. Young & Norton v. Hinderlider, supra, said it would be detrimental to the public interest to grant a permit for a large irrigation project if the water supply is insufficient because failed projects scare away potential investors in future irrigation development. Similarly, In re Commonwealth Power Co., supra, said it would be detrimental to the public interest to grant a permit for conflicting power projects because the resulting interference and litigation would scare away investors. Loss of investor confidence represents an external cost of failed projects and conflicting projects.

2. Young & Norton also said it would be detrimental to the public interest to grant a permit for a small irrigation project that would seriously interfere with an otherwise feasible larger irrigation project for which a competing application is pending. Cookinham v. Lewis, supra, applied the same reasoning to an application for a small project that would seriously interfere with Carey Act development of a large area. Big Horn Power Co. v. State, supra, reported a decision by the state engineer that it would be detrimental to the public interest to grant a permit for a small hydroelectric project in mining country without reducing the

height of the proposed dam to avoid interference with use of the canyon for a railroad bed. Cheap rail transportation was thought necessary to promote large scale mineral development in the region. These decisions all recognize that an external cost of a small water project might be the lost opportunity for greater economic development.

E. The essential function of public interest review, then, has always been to regulate externalities to maximize benefits. The content of public interest review has changed, but that simply reflects a broader modern view of the kinds of benefits to be maximized.

1. The concept of relevant externalities illuminates the relationship between constant function and changing content. Almost any activity involves external costs or benefits. Only some externalities, however, are relevant: "An externality becomes relevant whenever the affected party is not indifferent to it." A. Randall, Resource Economics: An Economic Approach to Natural Resource and Environmental Policy 157 (1981).

2. In the early years of the West, the dominant if not the only goal of the appropriation doctrine was maximum economic development. Consequently, relevant external costs involved concerns such

as loss of investor confidence and little projects rendering big projects infeasible. Today, the objective of water management in probably all states is broader than economic development. To borrow a phrase from the National Water Commission, the objective now is "greater productivity, in both monetary and nonmonetary terms, from existing supplies." National Water Commission, Water Policies for the Future 227 (1973). With the broader objective, more externalities become relevant. As public values increasingly are a part of the maximization goal, the effects new appropriations will have on public values increasingly are relevant externalities.

3. The concept of relevant externalities also helps explain the growing popularity of public interest review for water right transfers. The historical basis for regulating transfer externalities is the rule that a transfer must not injure any other water right, including junior rights. The no injury rule forces a transferor to take into account costs the transfer will impose on other appropriators due to reduced streamflow. Its major purpose historically was to promote water development by improving the security of supply for junior appropriators. An external cost of allowing

unregulated transfers would have been loss of enthusiasm for investment in new water use projects, and this was a relevant externality given the goal of maximum economic development. Modern public interest review of transfers is thus firmly anchored in appropriation doctrine tradition. It is simply a tool, like the time-honored no injury rule, for dealing with (now) relevant transfer externalities.

VI. An Assessment of Public Interest Review

A. Criticisms

1. While constancy of function may give modern public interest review of water right allocation and transfer a certain historical legitimacy, that does not make it immune from criticism.
2. Administrative agencies have long allocated a variety of scarce resources under public interest standards. E.g., the Civil Aeronautics Board used to allocate airline routes under a public interest standard, the Federal Communications Commission allocates radio and television broadcast frequencies under a public interest standard, and the Corps of Engineers issues permits to dredge and fill navigable waters under that standard.
3. Regardless of the agency involved or the resource allocated, public interest review tends to draw the same criticisms: costly and time

consuming proceedings, lack of coherent standards, and (because of that) corrupt and inconsistent decisions. Breyer, supra, at 78-89.

4. Not surprisingly, the deregulation movement of the last decade has reached some forms of public interest review. E.g., airline route allocation has been deregulated, and the allocation of radio and television broadcast frequencies has been partially deregulated. But public interest review of water right allocation and transfer has been in the ascendancy during the same period. The question naturally arises of whether this is incongruous or whether there are sound reasons for the difference.

5. Unless one is willing to take the extreme, and today untenable, position that public values in water should never count for anything, the real issue is not whether modern public interest regulation is imperfect but whether there are better ways to accommodate public values. Three alternatives are examined below.

B. Better Standards

1. More detailed statutory enumeration of potentially relevant public interest factors might help applicants and protestants prepare their cases before the agency. However, that would barely touch the problem of a lack of coherent

standards.

> The effect of many standards . . . is virtually the same as having none at all. There is no clear indication of which standards are more important, how they are to be individually applied, or how varying degrees of conformity are to be balanced. The existence of so many standards effectively allows the agency near-total discretion in making a selection.

S. Breyer, supra, at 79. Thus, the solution does not lie in greater enumeration of relevant factors.

2. One approach to better standards inheres in the Shokal statement that a permit should not issue if a proposed facility will violate mandatory water quality rules. Stated more broadly, the idea would be to develop some quite specific minimum standards by statute, administrative regulation, or state water plan provision. An example might be administrative guidelines on minimum conservation requirements for various categories of projects. Greater use of detailed minimum standards could streamline the permit process by quickly weeding out certain applications.

3. However, the minimum standards approach cannot solve all, or perhaps even many, water right allocation and transfer disputes. Ultimately, the effort to develop better standards clashes with the overall objective of greater productivity, in both monetary and nonmonetary terms,

from existing water supplies. That objective in reality has multiple, conflicting and vague components that cannot be reduced completely to per se rules or mechanical standards. The multiple, conflicting, and vague factors relevant to public interest review simply mirror the complexity of the overall goal and the impossibility of prior consensus about what it should mean in widely diverse and not always foreseeable fact patterns.

C. Reliance on Other Regulatory Tools

1. It might be argued that water permit agencies should minimize or ignore public values in public interest review because the legislature through water pollution, land use, and minimum streamflow reservation or appropriation legislation has created other tools to protect such values. The contention, for example, might be that rules developed under the other regulatory tools should preclude the water permit agency, as a matter of sound policy if not legality, from applying more stringent standards in public interest review.

2. The South Dakota hog farm case provides an illustration. A commentator on the case has said: "One might argue that a decision on whether a potentially odor-causing facility should be allowed is better handled in a zoning

proceeding. Indeed, the local zoning board was confronted by the same issue with regard to this company at about the same time." Rocky Mt. Min. L. Fdn., Guhin, XIX Water Law Newsletter No. 3, at 6 (1986) If local zoning allowed a hog farm at the proposed site, should that have precluded the state water management board from considering the effect of hog odor on the recreation areas along the Missouri River?

3. Though not directly in point, experience under the National Environmental Policy Act (NEPA) illuminates the issue. The Atomic Energy Commission's initial rules on environmental impact statements prohibited its hearing board from independently evaluating and balancing certain environmental factors if other responsible agencies had already certified that their own environmental standards were satisfied by a proposed project. Calvert Cliffs' Coordinating Comm. v. United States Atomic Energy Comm'n, 449 F.2d 1109, 1123 (D.C.Cir. 1971), rejected that approach for the following reason:

> The point of the individualized balancing analysis is to ensure that . . . the optimally beneficial action is finally taken.
>
> Certification by another agency that its own environmental standards are satisfied involves an entirely different kind of judgment. Such agencies, without overall responsibility for the particular federal action in question,

> attend only to one aspect of the problem: the magnitude of certain environmental costs. . . . [T]here may be significant environmental damage (e.g., water pollution), but not quite enough to violate applicable (e.g., water quality) standards. Certifying agencies do not attempt to weigh that damage against the opposing benefits. Thus the balancing analysis remains to be done. It may be that the environmental costs, though passing prescribed standards, are nonetheless great enough to outweigh the particular economic and technical benefits involved in the planned action.

The court ruled that the Commission could demand stricter water pollution controls from its licensees than required by the water quality standards of the certifying agency. Congress later overturned this specific ruling. Clean Water Act § 511(c)(2), 33 U.S.C. § 1371(c)(2) (1982). Whether the congressional action also bars federal agencies from weighing water quality impacts in their overall balancing of costs and benefits under NEPA is unclear. D. Mandelker, NEPA Law and Litigation § 2:17 (1984). But with other environmental impacts, the logic of Calvert Cliffs' still applies. Southern Oregon Citizens v. Clark, 720 F.2d 1475 (9th Cir. 1983) (herbicide registration); Oregon Environmental Council v. Kunzman, 714 F.2d 901 (9th Cir. 1983) (pesticide registration).

4. To apply the NEPA experience to public interest review of water permit applications, suppose a

proposed appropriation or transfer will adversely affect water quality but will not violate any applicable effluent limitation or water quality rule. If that will be the only adverse effect, maybe the water permit agency should defer to the announced state water pollution policy, as established by perhaps a different agency, and not condition a permit on compliance with stricter effluent limitations. But even if that is so, a different case arguably would be presented by a proposed appropriation or transfer that will have a combination of adverse consequences, none of which violate any individual water quality, land use, or minimum streamflow standards, but which cumulatively mean the costs exceed the benefits. With responsibility for water pollution control, land use regulation, and minimum streamflow reservations or appropriations, typically divided among different agencies or entities, public interest review of water permit applications is perhaps the only feasible mechanism for an overall balancing of costs against benefits for specific projects.

D. Reliance on Well-Defined, Marketable Property Rights

1. Some commentators have argued that externality problems with water resource use can be solved better by redefining property rights than by

administrative regulation. E.g., T. Anderson, Water Crisis: Ending the Policy Drought (1983); J. Hirshleifer, J. De Haven & J. Milliman, Water Supply: Economics, Technology, and Policy chs. 3-4 (1970); Gardner, The Untried Market Approach to Water Allocation in New Courses for the Colorado River 155 (G. Weatherford & F. Brown, eds. 1986); Williams, The Law of Prior Appropriation: Possible Lessons for Hawaii, 25 Nat. Res. J. 911, 924-28 (1985).

2. They propose a property rights system for the resource characterized by rights that are well-defined, enforced, and transferable. For example, suppose an appropriator has a right to divert a certain quantity of water to irrigate sugar beets, but the water or part of it would be more valuable if left in the river to provide downstream recreation. Since the benefits downstream are external to the appropriator's calculus, he will have no incentive to leave the water in the stream. However, the market would reallocate the use from irrigation to recreation if (1) the law were changed to allow an entrepreneur to hold an instream appropriation for recreational use, (2) the entrepreneur could enforce that right by charging recreational users a fee, and (3) the irrigator's right were freely transferable. The entrepreneur would

then make a purchase offer to the irrigator that would bring the downstream values into the irrigator's calculus. The externality would disappear.

3. Critics of the property rights approach raise various objections. First, it would often be difficult if not impossible to enforce property rights in public value water uses by excluding those who do not pay. Second, water rights are not always sufficiently well-defined for the market to work as a reallocator. Without well-defined rights, bargaining is hampered because potential purchasers are unsure of what they would be buying. Third, unregulated appropriation of water under the rule that "first in time is first" would award rights based on a race to use water, and the resulting initial allocation would not likely maximize benefits from the resource. Even if market forces could later reallocate water rights to the more valuable uses, market transactions entail costs to gather information and negotiate bargains. Public interest review of new appropriations would promote efficiency by achieving a better initial allocation that would reduce the need for later transaction costs. Fourth, even if market forces would adequately reflect public values at present, it is doubtful they would do so for

future generations because the private sector is likely to use too high a discount rate in making investment decisions and thus value future benefits too low. See, e.g., A. Randall, supra, at 187-88; Scarce Water and Institutional Change 10-11, (K. Frederick ed. 1986); Runge, An Economist's Critique of Privatization 71, in Public Lands and the U.S. Economy (G. Johnston & P. Emerson, eds. 1984); Gould, Water Use and the Prior Appropriation Doctrine 21, paper presented at Western Water: Expanding Uses/Finite Supplies Conference (Natural Resources Law Center, University of Colorado, June 2-4, 1986).

4. The more thoughtful property rights advocates acknowledge that these criticisms have at least some validity. They respond that despite its imperfections, the property rights approach is more likely than administrative regulation to approximate an optimal allocation of water. In other words, they say the risk of market failure is less than the risk of government failure.

5. Regardless of the merits of the debate about market failure versus government failure, the property rights approach faces two serious obstacles.

   a. First, it is far from clear that people really want to treat water as purely a market commodity. A natural resource

economist has observed:

> All societies identify some goods, services, amenities, and resources that, it is thought, ought to be beyond the reach of commerce. There are many different ways of expressing this idea: "the best things in life are free"; "some things ought not to be bought and sold, but should be considered everyone's birthright"; and "some things are too important to be left to the market." Different cultures have entirely different notions as to which goods, amenities, and resources ought to be immune from market influences, and some societies place many more items in that category than do others. In the United States, natural environments, wild rivers, and historical sites are often considered to be in that category.

A. Randall, supra, at 187.

b. Second, reliance on public interest review to deal with the externalities of water use has deep roots in appropriation doctrine history. Recent expansion of the concept of relevant externalities to keep pace with evolving water management goals constitutes no change in essential function and no more than incremental change in content. The property rights approach, in contrast, would represent more radical change. Radical change is difficult to achieve because of what some might condemn as inertia and others might praise as institutional stability. The kind of radical change that

the property rights approach represents is unlikely to occur absent widespread and intense dissatisfaction with the public interest review approach to externalities. There is little present evidence of that kind of dissatisfaction with the way public interest review has been evolving.

VII. Conclusion

A. In 1914, Roscoe Pound described how the law was beginning to impose social limitations on the use of property. About water, he wrote:

> Recently a strong tendency has arisen to regard running water and wild game as res publicae, to hold that they are owned by the state, or better, that they are assets of society which are not capable of private appropriation or ownership except under regulations that protect the general social interest. It is too early to say just how far this tendency will go. But it is changing the whole water law of the western states.

Pound, The End of Law as Developed in Legal Rules and Doctrines, 27 Harv. L. Rev. 195, 234 (1914). In 1971, a report prepared for the National Water Commission on administrative allocation of water commented that "the noted 'strong tendency' has been slow to develop." E. Clyde & D. Jensen, supra, at 5. Two years later, the Commission itself concluded: "State laws in many instances are inadequate to protect important social uses of water." National Water Commission, Water Policies for the Future 278 (1973).

B. Since then, state laws have changed in various ways to become more adequate, and evolving public interest review has contributed toward that effort. There is now a strong if not irresistible trend in the statutes and cases to treat public values as relevant factors in public interest review. It is harder to generalize about the weight of public values in the balancing part of public interest review. The reported balancing cases are too few and the issues too fact specific. Putting aside the New Mexico resort complex decision, which did not involve public values in the usual sense and which may or may not survive appeal, the cases do not reveal great boldness in weighing public values. On the balancing question, a paraphrase of part of Roscoe Pound's nearly three-quarter century old observation is still appropriate: It is too early to say just how far this tendency will go. But it is changing the whole water law of the western states, not radically but incrementally.

C. Over the years, some elements of the public interest have crystallized into more or less specific rules, such as use preferences and minimum standards. But the public interest will never be fully reducible to mechanical rules. There will always be hard questions of judgment. Public interest review enables reasoned debate about those questions. Though public interest review is not a marketplace

in the sense desired by advocates of the property rights approach, it constitutes a marketplace for ideas about what to value.