

1-1-2012

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Johna Varty, Case Note, Pawnee Well Users v. Wolfe: The Natural Successor to Vance v. Wolfe, 15 U. Denv. Water L. Rev. 469 (2012).

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CASE NOTES

PAWNEE WELL USERS V. WOLFE: THE NATURAL SUCCESSOR TO VANCE V. WOLFE

JOHNA VARTY*

I. INTRODUCTION

In 2009, the Colorado Supreme Court created a stir in the energy and water communities when it issued its decision in *Vance v. Wolfe*. In *Vance*, the court held that water produced during the coalbed methane (“CBM”) extraction process constituted a “beneficial use” of that water, thus subjecting it to administration by the Colorado State engineer (“SEO” or “state engineer”).¹ While the underlying facts in *Vance* related to methane gas produced from coal seams, the resulting rulemaking process had implications for oil and natural gas producers throughout the state.² As a result, the oil and gas industry saw the decision as an additional regulatory hurdle that would significantly increase the costs and uncertainty of both CBM and conventional forms of oil and gas production (“conventional development”).³⁴ Landowners and water right holders concerned with water quality and the security of their water rights applauded the court’s decision as an appropriate step toward further protecting their water interests.⁵

Following the *Vance* decision, the SEO faced the staggering reality that that thousands of oil and gas wells in the State would require permitting determinations.⁶ The Colorado Legislature (“Legislature”) stepped in to provide a streamlined process by which the SEO could proceed with

* With thanks to Jason Turner, Colorado River Water Conservation District, for his review and commentary.

1. *Vance v. Wolfe*, 205 P.3d 1165, 1169 (Colo. 2009).

2. Cody Doig, *Vance v. Wolfe: “Beneficial Use” or “Beneficial Byproduct?”— An Analysis of Produced Water in Colorado*, 13 U. DENV. WATER L. REV. 163, 173 (2009).

3. For the purposes of this Note, I will use “conventional development” to mean all forms of non-conventional oil and gas production other than CBM. These type of production include, but are not limited to, conventional associated gas, gas-rich shale, and conventional non-associated gas.

4. *Id.*

5. Neal Joseph Valorz, *The Need for Codification of Wyoming’s Coal Bed Methane Produced Groundwater Laws*, 10 WYO. L. REV. 115, 124 (2010).

6. Kristin H. Mosely, *Produced Water Associated with Shale Gas Development*, *1, *4 (Feb. 24, 2012)(unpublished comment, on file with the University of Denver Water Law Review).

making these determinations.⁷ The resulting legislation provided a process by which the SEO could make basin-wide determinations over whether the water being produced was tributary or nontributary in nature.⁸ The legislation further clarified that for both CBM and conventional development, any tributary groundwater produced would require a permit, and if taken from an over-appropriated stream system, require a court-approved augmentation plan.⁹ The Legislature further declared that for conventional production, groundwater extracted from nontributary sources would not require a permit unless that water was being put to a beneficial use.¹⁰ CBM production of nontributary groundwater stayed true to *Vance*, and required a permit.¹¹ See Figure 1.0 for a general breakdown of how each type of well is now administered.

Type of Well	Permit Required?	Augmentation Plan?
Nontributary CBM	Yes	No
Nontributary Conventional	No (unless put to beneficial use as defined by § 37- 90-137(7))	No
Tributary CBM	Yes	Yes (if over-appropriated)
Tributary Con- ventional	Yes	Yes (if over-appropriated)

Figure 1.0¹²

Opponents of oil and gas development, concerned landowners including the plaintiffs in *Vance*, and environmental groups opposed the basin-wide determinations and challenged the laws in court. The resulting case, *Pawnee Well Users v. Wolfe*, challenged the scope of the SEO's administrative authority and process, claiming that the Legislature did not grant the SEO the authority to make basin-wide determinations, and that the public was not given sufficient due process.¹³

7. 2009 CO H.B. 1303; 2010 CO S.B. 165.

8. COLO. REV. STAT. § 37-90-137 (2011); *see also* COLO. REV. STAT. § 37-90-137(4) (granting the state engineer authority to issue permits for non-tributary wells); COLO. REV. STAT. § 37-90-103(10.5) (defining "nontributary").

9. *Id.*

10. *Id.*

11. *Id.*

12. Kent Holsinger, Produced Water from Oil and Gas: The Legal and Regulatory Framework, presentation (powerpoint at 138) (on file with author).

13. *Pawnee Well Users v. Wolfe*, No. 2010CW98 (Water Div. 1 2011).

This Note examines *Pawnee* as an inevitable outgrowth of *Vance*. The first section will discuss the basic geology and hydrology associated with CBM development and the differences between it and conventional production. Second, this Note will analyze the *Vance* decision. Third, this Note will address the changes the Legislature made to the regulatory scheme both during after *Vance* in order to incorporate the *Vance* decision into the SEO's rulemaking jurisdiction and streamline the resulting process. Fourth, this Note will look at *Pawnee* as the inevitable result of the *Vance* decision and the Legislature's actions. Last, this Note will discuss some future policy implication of the *Vance* and *Pawnee* decisions.

II. WHAT IS CBM AND HOW IS IT DIFFERENT FROM CONVENTIONAL OIL AND GAS DEVELOPMENT?

CBM is quite different from conventional development and results in different extraction techniques. CBM is found in shallow underground seams, generally at depths between 1,000 and 3,000 feet.¹⁴ Comparatively, conventional oil and gas, while occasionally just as shallow as CBM, is commonly much deeper—with some wells over 8,000 feet below the surface.¹⁵ Biological processes in these coal seams generate methane gas that is held in place by the hydrostatic pressure of naturally occurring groundwater also found within the coal seams.¹⁶ Therefore, in order to release the methane, producers must first dewater the coal formation.¹⁷ Once the water is removed, the methane is no longer trapped by hydrostatic pressure and can be extracted.¹⁸ The water produced is then disposed of in a variety of ways including stored in lined storage tanks followed by re-injection, stock watering, irrigation, stock watering, or release into dry stream channels.¹⁹ While there has been a trend towards recycling this water, it is often more cost efficient to re-inject the water into geologically isolated formations well below the surface and any aquifers containing usable water supplies.²⁰ The Colorado Oil and Gas Conservation Commission ("COGCC") regulates access to and activities in these formations, as well as the reinjection process, and the storage and recycling process.²¹

While there are formations where conventional oil and gas can be extracted much closer to the surface, generally, the comparatively shallower

14. Joseph Michael Evers, *Coalbed Methane: Intermountain Oil and Gas BMP Project*, Nat. Res. Law Center, University of Colorado Law School, available at <http://www.oilandgasbmpps.org/resources/cbm.php>.

15. *Id.*

16. *Id.*

17. *Id.*

18. *Id.*

19. *Vance*, 205 P.3d at 1167.

20. Mosely, *supra* note 6 at *3-4.

21. *Vance*, 205 P.3d at 1167.

depth of CBM production is more likely to pump tributary groundwater than conventional production.²² See e.g. Figure 2.0.

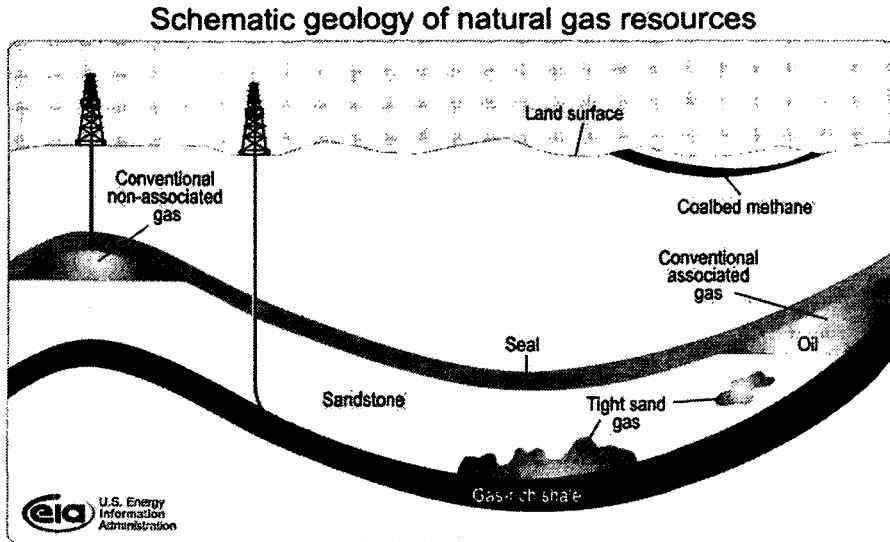


Figure 2.0²³

In the case of conventional deposits, there are often intermediate layers of nonporous rock, which serves to “seal-in” oil and gas and thereby separate it from other groundwater aquifers.²⁴ In addition, deeper groundwater aquifers located in or near the formations that contain conventional oil and gas, are less likely to be hydraulically connected to tributary surface water merely as a result of their depths.²⁵ Moreover, even if these deep aquifers are hydraulically connected, water at such a depth is likely to satisfy Colorado’s statutory definition of nontributary groundwater, which requires that the groundwater “withdrawal . . . will not, within one hundred years of continuous withdrawal, deplete the flow of a natural stream . . . at an annual rate greater than one-tenth of one percent of the annual rate of withdrawal.”²⁶ Due to this deep groundwater’s slow migration speeds, on average about a foot per day, it is more

22. See Edwin D. Gutentag, et al., *Geohydrology of the High Plains Aquifer in Parts of Colorado, Kansas, Nebraska, New Mexico, Oklahoma, South Dakota, Texas and Wyoming: U.S. Geological Survey Professional Paper, 1400-B*, High Plains RASA Project, available at <http://pubs.usgs.gov/pp/1400b/report.pdf>.

23. U.S. ENERGY INFORMATION ADMINISTRATION, NATURAL GAS: SCHEMATIC GEOLOGY OF NATURAL GAS RESOURCES, (Jan. 27, 2010) available at http://www.eia.gov/oil_gas/natural_gas/special/ngresources/ngresources.html.

24. *Id.*

25. See Gutentag, *supra* note 23.

26. COLO. REV. STAT. § 37-90-103 (10.5) (2010).

likely that the statute will deem the water produced during conventional development “nontributary.”²⁷

Conventional development is also different from CBM because the removal of groundwater is not inextricably tied to the extraction process.²⁸ Unlike CBM production, oil and gas is extracted by drilling a well into an oil or gas bearing formation, and relying on the natural pressure of the oil or gas at depth to push the oil or gas to the surface.²⁹ In conventional development, water removal is not necessary for production and is only produced in large quantities towards the end of the life of the well.³⁰

A. VANCE V. WOLFE

In *Vance*, two ranching families, the Fitzgeralds and the Vances (referred to collectively as “Ranchers”), brought a declaratory judgment action in Colorado District Court, Water Division 7 (“water court”) to determine the legal obligations of the SEO and the Division 7 Engineer for well permits and augmentation plans associated with water produced during CBM operations.³¹ The Ranchers wanted CBM wells to be subject to permitting administration by the SEO and argued that the withdrawal of groundwater during CBM extraction constituted a beneficial use of that water under the Water Right Determination and Administration Act of 1969 (“1969 Act”) and Colorado Ground Water Management Act (“GWA”).³² The Ranchers were concerned that the SEO’s abdication of this obligation resulted in harm to their senior water rights.³³ The water court agreed with the Ranchers that CBM extraction constituted a beneficial use of groundwater and the extraction by CBM producers was an out of priority withdrawal.³⁴ Defendants appealed the water court’s finding of beneficial use to the Colorado Supreme Court. The Colorado Supreme Court upheld the water court’s decision, agreeing with the Ranchers, and *Vance v. Wolfe* quickly became another of a long history of hotly debated water cases.³⁵

The Appellants, the SEO and BP America Production Company (“Appellants”) presented a three-pronged argument in their appeal.³⁶ Appellants first argued that water produced during CBM extraction was

27. R. W. Buddemeier & J. A. Schloss, Groundwater Storage and Flow, KANSAS GEOLOGICAL SURVEY (2000) available at <http://www.kgs.ku.edu/HighPlains/atlas/apgengw.htm>.

28. Evers, *supra* note 14.

29. *Id.*

30. *Id.*

31. *Vance*, 205 P.3d at 1166-67.

32. COLO. REV. STAT. § 37-92-502; COLO. REV. STAT. § 37-90-137; *Vance*, 205 P.3d at 1166-67.

33. *Vance*, 205 P.3d at 1166-67.

34. *Id.*

35. *Vance*, 205 P.3d at 1167.

36. *Id.* at 1166-68.

actually "produced water" and therefore a mere waste product incidental to the actual goal of mining for methane.³⁷ Appellants argued that with no intent to put water to beneficial use, the withdrawal of such water would not trigger either the 1969 Act or GWA.³⁸ In response, Ranchers argued that because extracting the methane required the withdrawal of water, and because water is instrumental in keeping methane trapped in coal seams, the extraction of water constituted beneficial use.³⁹

The Court agreed and held that the production of water was not an incidental waste, but rather an essential component of producing methane gas; the Court further held that this beneficial use triggered the 1969 Act and the GWA.⁴⁰ This "beneficial use" gave rise to appropriative rights and required the SEO to prohibit out-of-priority withdrawals without an approved augmentation plan.⁴¹ Relying on its past decisions regarding the beneficial use of water associated with gravel extraction, the Court reasoned that the interpretation in those cases coupled with statutory construction resulted in the determination that the withdrawal of groundwater in the CBM process was an "integral component" to the CBM process, and thus a beneficial use.⁴²

In *Three Bells Ranch Assoc. v. Cache La Poudre Water Users Ass'n* and *Zigan Sand & Gravel, Inc. v. Cache La Poudre Water Users Ass'n*, commonly referred to as the "gravel cases," the claims centered on the question of whether the water collected in pits after the extraction of sand and gravel constituted a beneficial.⁴³ In the gravel cases, the Court held that because the producers used the water collected in the pits for a later beneficial use including land reclamation and dust suppression, that use gave rise to an appropriative right.⁴⁴ Hoping to distinguish the gravel cases from the case at hand, Appellants in *Vance* argued that the fact that the water was applied to a *later* use is what gave rise to the beneficial use, where in CBM production, the contentious use happened at the time of extraction.⁴⁵ The Court disagreed, holding that the temporal difference between finding beneficial use at the time of extraction in *Vance* rather than the later use in the gravel cases was not relevant.⁴⁶

The Court discussed at length the fact that Colorado water law proceeds from the presumption that all groundwater is tributary unless proven to be non-tributary and the parties in *Vance* did not challenge that

37. *Id.* at 1168.

38. *Id.*; COLO. REV. STAT. § 37-92-502; COLO. REV. STAT. § 37-90-137.

39. *Vance*, 205 P3d at 1168.

40. *Id.*; COLO. REV. STAT. § 37-92-502; COLO. REV. STAT. § 37-90-137.

41. *Vance*, 205 P3d at 1168.

42. *Id.* at 1170.

43. *See generally*, *Three Bells Ranch Assocs. v. Cache La Poudre Water Users Ass'n*, 758 P.2d 164 (Colo. 1988); *Zigan Sand & Gravel, Inc. v. Cache La Poudre Water Users Ass'n*, 758 P.2d 175 (Colo. 1988).

44. *Three Bells Ranch Assocs.* 758 P.2d at 166; *Zigan Sand & Gravel, Inc.* 758 P.2d 181.

45. *Vance*, 205 P3d at 1170 (*emphasis added*).

46. *Id.*

presumption.⁴⁷ Pursuant to the 1969 Act, the state engineer has the affirmative duty to protect existing water rights against injury by curtailing injurious out-of-priority diversions of tributary ground water that are not replaced under an augmentation plan or substitute water supply plan.⁴⁸ If a court finds an “appropriation” and a “well” under the GWA and the 1969 Act, *and* the presumption of the tributariness of that water source is not overcome, then the use of that water is subject to the priority system to be administered by the SEO.⁴⁹ In this case, the court did not need to address whether the water was tributary because neither party contested the presumption.⁵⁰

The 1969 Act defines an “appropriation” as, “the application of a specified portion of the waters of the state to a beneficial use,” and a “well” as, “any structure or device used for the purpose of or with the effect of obtaining ground water for a beneficial use from an aquifer.”⁵¹ The fact that Appellants constructed CBM wells with the intent to extract ground water was also uncontested; the definition of “well” and “appropriation” thus hinged on whether the use of the extracted water was a “beneficial use.”⁵² Had the court found that the use was a beneficial use but that the water was not tributary, the SEO would still have had to assert its jurisdiction over the water.⁵³ The burden of this intervention would be less onerous however, because the producer’s use of the water would not give rise to an appropriative right that could trigger a costly augmentation plan if the stream-system was already over-appropriated.⁵⁴ Rather, because the GWA does not require nontributary water to be administered under the priority system, the Appellants would simply need to obtain a permit from the SEO in order to conduct CBM operations.⁵⁵ After holding that the extraction of water in CBM mining constituted a “beneficial use” of that water, the court next addressed the SEO’s two remaining arguments.

Appellants next argued that, as an administrative agency, the SEO was entitled to deference in its definition of beneficial use because the term was ambiguous.⁵⁶ The court disagreed, holding that the SEO’s determination that extraction of water during CBM development did not constitute beneficial use was contrary to the plain meaning of the 1969 Act and therefore unreasonable.⁵⁷ The 1969 Act defines “beneficial use” as, “the use of that amount of water that is reasonable and appropriate under reasonably efficient practices to accomplish without waste the purpose for

47. *Id.* at 1168.

48. COLO. REV. STAT. § 37-92-502.

49. Vance, 205 P.3d at 1168-69.

50. *Id.*

51. COLO. REV. STAT. § 37-93-103(3)(a); COLO. REV. STAT. § 37-93-103(14)(a).

52. Vance, 205 P.3d at 1169.

53. *Id.* at 1171.

54. *Id.*

55. *Id.*

56. *Id.* at 1172.

57. *Id.*

which the appropriation is lawfully made.”⁵⁸ While this is a broad and ambiguous definition of the term, and acknowledging that the SEO was entitled to some deference, the court nevertheless held that the SEO’s claim that water produced during CBM development did not fall within the definition conflicted with the plain meaning of the statute.⁵⁹

Third, Appellants argued that the Colorado Oil and Gas Conservation Commission (“COGCC”) had exclusive regulatory authority over water produced during CBM extraction.⁶⁰ To support their argument, Appellants offered evidence that the COGCC had been granted broad regulatory authority.⁶¹ While it acknowledged the powers granted to the COGCC, the court ultimately held that the COGCC did not have exclusive regulatory authority because Appellants failed to produce evidence of a specific provision of the Oil and Gas Conservation Act that exempted oil and gas production from the 1969 Act or the GWA.⁶² Because of the absence of such evidence, the court held that the appellant’s argument was in direct conflict with the plain language of the Ground Water Act and the 1969 Act.⁶³ Accordingly, the court interpreted the language of the 1969 Act and the GWA to hold that water produced by appellant’s CBM wells constituted beneficial use, did not overcome the presumption of tributaryness, and gave rise to an appropriative right.⁶⁴

By holding that water produced during CBM development constituted a beneficial use, the court surprised the oil and gas industry by demonstrating that they did not have an exemption for their groundwater withdrawals. The court also emphasized that when making the determination, the issue was very fact specific. Finally, its extensive examination of the presumption that all groundwater is tributary seemed to hint to the Legislature that this would be the next step in the incorporation of water law into oil and gas development.

B. THE AFTERMATH OF VANCE

The *Vance* decision triggered powerful reactions from both the water and oil and gas communities, and led the Legislature and SEO to take action. Many analysts were quick to extrapolate from the decision its application to the oil and gas industry as a whole.⁶⁵ Many also wondered if conventional oil and gas wells would now be administered under the

58. COLO. REV. STAT. § 37-92-502.

59. *Vance*, 205 P.3d at 1172.

60. *Id.*

61. *Id.* at 1173.

62. *Id.*

63. *Id.*

64. *Id.* at 1171.

65. See Ken Wonstolen, *Vance Decision Throws Oil and Gas Into Uncharted Waters*, ENERGY NEWS ALERT, Beatty & Wozniak, P.C. (2009) available at <http://www.bwenergylaw.com/News/documents/VanceDecisionThrowsOilandGasIntoUnchartedWaters.pdf>.

prior appropriation system.⁶⁶ The oil and gas industry argued that forcing producers to buy water rights or adjudicate costly augmentation plans could make drilling in Colorado prohibitively expensive for producers.⁶⁷ The existence of the presumption of tributariness only served to strengthen the oil and gas industry's trepidation.⁶⁸ As a result of these concerns, and anticipating the increased burden that regulating groundwater produced during oil and gas development would place on the SEO, the Legislature began reacting to *Vance* even before the decision was handed down by proposing House Bill 1303, which passed just days after the court issued its opinion in *Vance*.⁶⁹ The Legislature attempted not only to create an efficient framework for the SEO, but also incorporate the court's ruling about the beneficial use of water produced during CBM development.

C. HOUSE BILL 09-1303 AND SENATE BILL 165

Recognizing both that CBM development is unique and that *Vance* necessitated a comprehensive framework for dealing with water issues in oil and gas development, the Legislature passed several bills to streamline the administration of CBM wells and extend the SEO's authority to all oil and gas wells.⁷⁰ The Legislature first adopted House Bill 09-1303 ("HB 09-1303"), which created specific timelines for when producers are expected to acquire permits and augmentation plans for tributary wells, and granted the SEO authority to administer the withdrawal of nontributary groundwater for oil and gas development.^{71 72}

The Legislature also adopted Senate Bill 165, which amended COLO. REV. STAT. § 37-90-137 to address the *Vance* decision and provide guidelines for the State engineer to determine when a permit is not required.⁷³ These guidelines are codified in § 37-90-137(7) and state that no permit is required for nontributary groundwater produced in oil and gas development, with the exception of CBM development, if the water is not beneficially used.⁷⁴ The statute further states that nontributary water produced in oil and gas development, excluding CBM-produced water, is not beneficially used if it is extracted for the purpose of facilitating oil and gas production and it is disposed of in the same geologic basin from

66. Mosely, *supra* note 18 at *4-5.

67. Doig, *supra* note 2, at 173-4.

68. *Vance v. Wolfe Case Summary*, HOLLAND & HART LLP: WESTERN WATER LAW, available at www.westernwaterlaw.com/Vance_v_Wolfe.html.

69. 2009 CO H.B. 1303.

70. Produced Nontributary Ground Water Rules, 2 COLO. CODE REGS. § 402-17, Statement of Basis and Purpose.

71. COLO. REV. STAT. § 37-90-137(7)(c).

72. *H.B. 09-1303: Admin Mineral Development Water Wells*, COYOTEGULCH (Apr. 28, 2009) available at <http://coyotegulch.wordpress.com/2009/04/28/hb-09-1303-admin-mineral-development-water-wells-3/>.

73. 2010 CO S.B. 165.

74. COLO. REV. STAT. § 37-90-137(7).

which it was removed.⁷⁵ The Bill goes on to require that this disposal comply with all other relevant statutes and regulations and must be one of the enumerated methods of dealing with the water.⁷⁶ Some of the enumerated methods include reinjection, road spreading, and reuse.⁷⁷ This essentially means that nontributary water produced during oil and gas development, other than CBM development, does not require a permit as long as it is disposed of in the same basin from which it was taken in a manner that satisfies one of the above-enumerated methods. Water produced during CBM development is considered beneficially used at extraction and thus requires a permit for the withdrawal of nontributary water.

COLO. REV. STAT. § 37-90-137, as amended by the two bills discussed above, also provides for review under the Colorado Administrative Procedure Act of the SEO's determination as to whether energy producers need a permit.⁷⁸ The combination of HB 09-1303 and Senate Bill 165 thus created a framework for the SEO to administer groundwater produced during oil and gas development that both acknowledges the differences between CBM extraction and other forms of oil and gas development, and allows for the integration of water law into the oil and gas regulatory scheme (refer to Figure 1.0 for a chart that explains this framework). These two actions by the Legislature allowed it to create an exception for conventional development that produces nontributary water.⁷⁹ This exception is justified by the complex hydrology and geology associated with oil and gas development in Colorado and speaks to the true concerns of water right holders.

Water right owners are inevitably concerned with oil and gas development harming the quality and quantity of their water supplies. Whether the water produced as a result of energy production is a "beneficial use" of that water does not necessarily speak to this concern. The Legislature's focus on the "tributary"/"nontributary" distinction effectively addresses their concerns in that nontributary ground water will, by definition, not impact the water rights holders on surrounding streams, where withdrawals of tributary groundwater will impact these water rights holders.⁸⁰ Had the Legislature acted, as industry feared it would, and defined beneficial use as any water extracted to facilitate oil and gas production, the SEO may have needed to administer water rights for groundwater produced more than a mile below the surface that was in no way hydrau-

75. *Id.*

76. *Id.*

77. *Id.*

78. *Id.*

79. Amy Mowry & Ken Wonstolen, *Vance v. Wolfe Adds Water Considerations for Colorado Oil and Gas Producers*, DENVER ASSOCIATION OF PETROLEUM LAWYERS NEWSLETTER (Oct. 2009) available at http://www.cobar.org/repository/Inside_Bar/Water%20Law/November%2012,%202009/Produced%20Water%20Article%20_00132482_.pdf.

80. COLO. REV. STAT. § 37-90-103.

lically connected to water used by water right owners.⁸¹ This could considerably increase the cost of oil and gas development without protecting water right users.⁸² Therefore, in fully addressing the produced water issue by regulating only tributary groundwater in conventional development, the Legislature created a functional exception that allayed the fears of the oil and gas industry while also protecting existing water rights.

In *Vance*, the debate did not revolve around whether or not the water produced was tributary because the Court relied on the un rebutted presumption that all groundwater is tributary.⁸³ During the water court evidentiary proceedings, plaintiffs submitted engineering reports indicating that not only was the water tributary, but that the withdrawal of such water by CBM producers constituted an injury to their senior water rights.⁸⁴ Therefore, the presumption that groundwater was tributary was supported by facts in the *Vance*. Moreover, such a presumption generally applies to CBM wells, because CBM production regularly occurs at shallower depths.⁸⁵ But conventional oil and gas producers argue that the same facts are not likely to apply for most conventional wells.⁸⁶

D. STATE ENGINEER'S "PRODUCED NONTRIBUTARY GROUNDWATER RULES"

Under its delegated authority to administer groundwater produced during oil and gas development, the SEO promulgated the "Produced Nontributary Ground Water Rules" ("Rulemaking" and "Rules," respectively).⁸⁷ The Rules acknowledged the rebuttable presumption that all groundwater is tributary, and the difficulty of a case-by-case determination for the thousands of oil and gas wells already in existence in Colorado.⁸⁸ Thus, the SEO determined by rule, that certain geologic formations within the State were nontributary, thereby avoiding the necessity of conventional producers to rebut that presumption for each individual well operating in certain formations.⁸⁹

During the Rulemaking, the SEO reviewed evidence from many interested parties including complex modeling, to determine areas where the water produced by oil and gas wells is nontributary for purposes of the SEO's administration of such water.⁹⁰ If the water in the oil and gas-producing formation satisfied the statutory definition of nontributary, the formation was officially delineated as nontributary in a Basin Specific

81. *Id.*

82. Doig, *supra* note 2 at 176.

83. *Vance*, 205 P.3d at 1168.

84. Mowry, *supra* note 78.

85. *Id.*

86. Evers, *supra* note 14.

87. Produced Nontributary Ground Water Rules, *supra* note 70.

88. *Id.*

89. *Id.*

90. *Id.*

Rule.⁹¹ This means conventional oil and gas producers would not need to obtain a permit in such delineated basins provided the water was not beneficially used in accordance with COLO. REV. STAT. § 37-90-137(7). See Figure 3.0 for the list of basins delineated as nontributary by the Basin Specific Rules.

Basin/Field (Name)	Formation (Name)	Rule Dictating Nontributary Designation	Area Designated As Nontributary
Piceance Basin	Mesaverde Formation	Rule 17.7.D.1	Cameo and South Canyon Coal Groups (in the Muddy Creek Drainage North of Paonia Reservoir in Delta and Gunnison Counties)
	Neslen Formation		All Neslen Formation within Piceance Basin in Garfield and Rio Blanco Counties
	Shallow Formations		Undifferentiated Wasatch Formation, middle and lower Wasatch Formation, Iles Formation of the Mesaverde Group, Williams Fork Formation of the Mesaverde Group, and undifferentiated Mesaverde Group, within certain delineated areas in Rio Blanco, Garfield, Mesa, Delta, and Pitkin Counties.
	Weber Formation		Rangely Oil Field in Rio Blanco County
	Morrison and Entrada Sundance Formations		Wilson Creek Oil Field in Rio Blanco County

91. *Id.*

Basin/Field (Name)	Formation (Name)	Rule Dictating Nontributary Designation	Area Designated As Nontributary
Northern San Juan Basin	Fruitland Formation	Rule 17.7.D.2	All Fruitland Formation
	A Pictured Cliff, Cliff House, Menefee, Point Lookout, and Dakota Formations		Within delineated areas in Southwestern Colorado
Paradox Basin	Paradox Formation		Hovenweep Shale, Gothic Shale, and Desert Creek Members within Mesa, Montrose, San Miguel, Dolores, and Montezuma Counties
Sand Wash Basin	From Fort Union Formation, Lance Formation, Lewis Shale, Meseverde Group, Baxter Shale, Frontier Formation		Mowry Shale, Dakota Sandstone, Nugget Sandstone, and Hiawatha Member of the main body of the Wasatch Formation in Moffat County.
	Wasatch Formation		Hiawatha and West Hiawatha Gas Fields
Denver—Julesburg Basin	Pierre Shale Formation, Lower Pierre Shall Formation, the Niobrara Formation, the Carlile Formation, the Greenhorn Formation, the Graneros Formation, the Dakota Group, and the Lyons Formation		Parkman, Sussex, and Shannon Members of Pierre Shale Formation; within certain delineated areas in northeastern Colorado.

*Figure 3.0*⁹²

92. Burr, Watson, & Huffman, Presentation at the University of Denver Water Law Review Annual Symposium (April 13, 2012) (on file with author).

The state engineer's ability to conduct this analysis on a basin wide level rather than on a well-by-well basis streamlined the process and will likely reduce the considerable cost and time associated with conducting with well-by-well determinations. The Rules also created a process for administrative appeal and provide for appellate review of the SEO's determinations of groundwater produced by energy developers by the water court and ultimately the Colorado Supreme Court.⁹³

E. HOUSE BILL 1286

Recognizing that the Rules promoted efficiencies in the permitting process, the Colorado Legislature passed House Bill 1286 ("Bill") in order to clarify and strengthen the SEO's position with regards to the Rules.⁹⁴ The Bill clarified that the SEO had the specific authority to determine groundwater basins as tributary or nontributary.⁹⁵ Further, the Bill granted the SEO both rulemaking and adjudicatory authority to administer this process.⁹⁶ Of relevance is the fact that the Legislature enacted the Bill while the *Pawnee Well Users v. Wolfe* case (discussed in detail below) was pending.

1. *Pawnee Well Users v. Wolfe*

The SEO adopted the Final Rules in December 2009 and the Basin-Specific Rules were incorporated in early 2010.⁹⁷ On March 1, 2010, a group of water users and water right holders including the plaintiffs in *Vance*, filed complaints in water divisions 1, 2, 4, 6, and 7, which were consolidated into one proceeding in Colorado District Court, Water Division No. 1 ("water court"), captioned *Pawnee Well Uses v. Wolfe*.⁹⁸ In their complaint, plaintiffs challenged the Final Rules and the Basin-Specific Rules, claiming that the SEO exceeded its statutory authority and that there was insufficient public notice of the rulemaking and related procedures.⁹⁹

The water court reviewed both sets of rules using the "arbitrary and capricious" standard specified in the Colorado Administrative Procedure Act ("APA"), which provides that a court will defer to an agency decision unless the agency's actions were arbitrary and capricious.¹⁰⁰ To be found arbitrary or capricious, the agency action must deny a statutory right, commit an action contrary to a constitutional right, exceed statutory jurisdiction, or commit an action that is clearly erroneous on the facts of the

93. Produced Nontributary Ground Water Rules, *supra* note 70.

94. 2011 CO H.B. 1286.

95. *Id.*

96. *Id.*

97. *Id.* at *3.

98. *Pawnee Well Users* at *3.

99. *Id.* at *4.

100. COLO. REV. STAT. § 24-4-106.

whole record.¹⁰¹ If the agency's action is not arbitrary or capricious, the water court will defer to the agency and uphold the agency's decision.¹⁰² This deference is premised on the idea that agencies are the entities best equipped to interpret statutes directed at them.¹⁰³ Courts are reluctant to impose their own interpretation of statutes over an agency's interpretation of its statutory authority.¹⁰⁴ The APA, therefore, instructs courts to defer to agency discretion except in the enumerated instances.¹⁰⁵

Plaintiffs' primary argument consisted of three parts. First, plaintiffs argued that the SEO did not have the rulemaking authority to make general basin wide determinations as to whether the groundwater being produced was tributary or nontributary in lieu of conducting a traditional well-by-well analysis because House Bill 1303 and Senate Bill 165 only granted the SEO the authority over water produced during energy development, rather than entire basins.¹⁰⁶ Second, plaintiffs argued that the SEO did not have the statutory authority to conduct adjudications that make nontributary determinations.¹⁰⁷ Third, plaintiffs argued that the SEO did not have the authority to make determinations in areas where there is currently no oil and gas development.¹⁰⁸ Concerning the first part of plaintiffs primary argument, the water court held that COLO. REV. STAT. § 37-90-137(7)(c) as amended by House Bill 1303 expressly granted the SEO authority to adopt rules to assist in administering groundwater because to hold otherwise would render subsection 137(7)(c) superfluous.¹⁰⁹

Turning to the second part of plaintiffs main argument, the water court held that notwithstanding its acknowledgment that House Bill 1303 and Senate Bill 165 did not granted the SEO the explicit authority to conduct adjudications, the water court held that the legislation granted the state engineer "implied and incidental" powers to effectuate the legislative mandate and that these implied powers included adjudications.¹¹⁰ Further, when the Legislature passed House Bill 1286, it made both the SEO's authority to delineate entire basins and its adjudicatory authority explicit.¹¹¹ Accordingly, the water court held that the SEO had the implied power to adjudicate claims associated with such delineations.

The water court then addressed plaintiffs' third claim that the SEO lacked authority to make nontributary determinations in areas where there are no current or proposed oil and gas wells because COLO. REV. STAT. § 37-90-103(10.5) requires that nontributary determinations be

101. *Id.*

102. *Id.*

103. *Id.*

104. *Id.*

105. *Id.*

106. Pawnee Well Users at *8.

107. *Id.*

108. *Id.*

109. COLO. REV. STAT. § 37-90-137(7)(c).

110. Pawnee Well Users at *9.

111. *Id.*

made on existing aquifer conditions the time of permitting, and not before.¹¹² The water court found that §103(10.5) does not specifically conflict with § 137(7)(c) because the SEO could conduct further analysis at the time a permit is sought as required by § 103(10.5) and yet still designate the basin earlier pursuant to § 137(7)(c).¹¹³

The water court next addressed plaintiffs' claims that they did not receive sufficient due process under the U.S. and Colorado constitutions and the APA. Analyzing the U.S. and Colorado procedural due process claims, the water court applied the three-part *Olson* test.¹¹⁴ The test states that a court must consider (i) whether a property right has been identified; (ii) whether governmental action with respect to that property amounts to a deprivation; and (iii) whether the deprivation, if one is found, occurred without due process of law.¹¹⁵ The fact that the plaintiffs were water right owners easily satisfied the first part of the test because water rights are property rights.¹¹⁶ The water court held, however, that part (ii) was not satisfied because plaintiffs were not sufficiently able to prove that the SEO's actions actually deprived them of a right.¹¹⁷ Rather, the water court found that any deprivation would be merely incidental because no injury yet existed, and would only result upon the SEO's potential erroneous determination at some point in the future.¹¹⁸ Therefore, the water court held that the Plaintiffs had sufficient procedural due process under both the U.S. and Colorado constitutions.¹¹⁹

Plaintiffs next claimed that the SEO's Notice of Proposed Rulemaking ("Notice") was not consistent with the subject matter of the notice and therefore the Rules should be overturned for lack of procedural due process.¹²⁰ Had plaintiffs succeed on this claim, the Rules would have been overturned for lack of adequate procedural due process. However, the water court found that, contrary to plaintiffs' assertions, the manner in which the SEO promulgated the Rules provided sufficient notice because specific passages of the Notice mentioned that the rulemaking was designed to "identify certain areas or formations with the State as non-tributary or tributary."¹²¹

In related APA claims, plaintiffs next asserted they were deprived of procedural due process because they were not given sufficient time to conduct cross-examination witnesses during the rulemaking proceedings.¹²² The water court disagreed because plaintiffs made no showing of

112. COLO. REV. STAT. § 37-90-103(10.5).

113. *Pawnee Well Users* at *12.

114. *Hillside Community Church v. Olson*, 58 P.3d 1021, 1025 (Colo. 2002).

115. *Id.*

116. *Pawnee Well Users*, No. 10CW89WL at *14.

117. *Id.*

118. *Id.*

119. *Id.* at *15.

120. *Id.*

121. Record at 23-24, *Pawnee Well Users v. Wolfe*, No. 10CW89WL *1 (2011) (No. 2012SA13).

122. *Pawnee Well Users*, No. 10CW89WL at *16.

facts that they would have presented had they been given more time to prepare.¹²³ Finally, the water court denied plaintiff's claim that the SEO's cost-benefit analysis was insufficient.¹²⁴ In so doing, the water court found that while the SEO presented a multitude of facts concerning the cost-benefit analysis, plaintiffs articulated no specific facts for why the cost-benefit analysis was insufficient.¹²⁵

The water court next examined whether it could consider House Bill 1286 in determining whether the SEO exceeded its statutory authority. Plaintiffs argued that because the Bill was enacted after the SEO initiated the rulemaking, applying the legislation to grant retroactive authority to the SEO would be unconstitutionally retrospective because it could injure owners of water rights.¹²⁶ The water court underwent a three-step analysis. First, it looked at whether it could consider legislation enacted while a case was pending. The water court quickly determined that it could as long as the legislation was not retrospective. Second, the water court determined that the 1286 was not retroactive because it merely clarified the authority granted in House Bill 1303. In reaching this conclusion, the water court began with the rebuttable presumption that when the Legislature amends a statute, it intends to change the law and as such, is retroactive.¹²⁷ This presumption can be rebutted with evidence that the Legislature merely intended to clarify the law and not create a new law.¹²⁸ In making this determination, the water court applied the three-part *Academy of Charter Schools Test*, which examines (i) whether the statute was ambiguous before it was amended; (ii) the plain language of the amendment; and (iii) the legislative history of the amendment.¹²⁹

As to the first part of the *Academy of Charter Schools Test*, the water court held that House Bill 1303, the Bill House Bill 1286 sought to amend, was ambiguous.¹³⁰ Nowhere in Bill 1303 did it say how the SEO could administer permits.¹³¹ Had the bill been unambiguous, then House Bill 1286 would be retroactive, and the water court would then need to examine whether the legislation was also unconstitutionally retrospective.¹³² However, because House Bill 1303 did not specify how the SEO could administer permits, it was ambiguous and House Bill 1286 was necessary to clarify 1303's ambiguity.¹³³ The water court also held that the second part of the *Academy of Charter Schools Test* was satisfied because the plain language of House Bill 1286 made clear that the Legis-

123. *Id.*

124. *Id.*

125. *Id.*

126. *Id.* at *16-17.

127. *Id.* at *17.

128. *Id.*

129. *Acad. of Charter Schools v. Adams County School Dist. No. 12*, 32 P.2d 119, 125 (Colo. 1995).

130. *Pawnee Well Users* at *18.

131. CO H.B. 1303.

132. *Pawnee Well Users* at *18.

133. *Id.*

lature's intent in passing the Bill was to delegate authority to the SEO to make nontributary designations as well as to conduct adjudications concerning these designations.¹³⁴ Finally, the water court held that the legislative history also supported this finding.¹³⁵ Thus the court held that House Bill 1286 was not new legislation, but merely clarified House Bill 1303.¹³⁶

Third, notwithstanding its holding that HB 1286 was not retroactive, the water court held that even if HB 1286 was retroactive, it was not unconstitutional because it was not retrospective. Retroactive legislation is only unconstitutional if it is retrospective.¹³⁷ Retrospective legislation is legislation that both applies retroactively *and* divests an individual of a vested right.¹³⁸ The water court held that none of the plaintiffs had been deprived of a vested right because the right they asserted was a right to an administrative rulemaking process, which is only an inchoate right.¹³⁹ Because this right was only inchoate, rather than vested the bill was not retrospective and was therefore constitutional.¹⁴⁰ Thus the water court held that HB 1286 was not retroactive because it merely intended to clarify the statute, and even if it was retroactive, it was not unconstitutionally retrospective because it only divested individuals of an inchoate rather than vested right.¹⁴¹

The water court then examined the validity SEO's "Fruitland Rule" ("FR"). The FR delineated a groundwater basin called the "Fruitland Formation" situated beneath the Southern Ute Reservation as nontributary.¹⁴² However the SEO, in a stipulation with the Southern Ute Indian Tribe, declined to decide whether he had jurisdiction to administer nontributary water originating on the reservation, codified in the Rules under 17.3.F.¹⁴³ Analyzing the FR and 17.3.F ("Tribe Rule"), the water court held that the State engineer could not promulgate a rule for an area where his jurisdiction had not been established and overturned the FR.¹⁴⁴ The Tribe Rule establish that the Rules shall not be construed to establish the jurisdiction of any party.¹⁴⁵ Therefore, the water court held that, because the SEO could not determine its jurisdiction, the determination that the Fruitland Formation was nontributary constituted an advisory opinion under the Rules, which the SEO did not have authority to make

134. *Id.*

135. Sonnenberg Testimony before the House Agriculture Committee discussion of HB 1286, March 21, 2011.

136. Pawnee Well Users at *20.

137. *Id.* at *19.

138. *Id.*

139. *Id.*

140. *Id.*

141. *Id.* at *17-20.

142. 2 COLO. CODE REGS. § 402-17.7.D.2.

143. Pawnee Well Users at *21.

144. *Id.*

145. 2 COLO. CODE REGS. § 402-17.3.F.

under the APA.¹⁴⁶ At the time of this writing, the SEO is appealing the water court's holding on this issue to the Colorado Supreme Court.¹⁴⁷

Finally, the water court looked at the legal effect of the rules. Plaintiffs argued that the SEO's determinations regarding the tributary nature of the water should have no effect in water court proceedings, unless C.R.S. § 37-92-305(6) applies.¹⁴⁸ This statute gives the SEO explicit authority to make binding legal decisions regarding permitting of wells.¹⁴⁹ However, it does not grant the SEO authority to make basin-wide decisions.¹⁵⁰ The water court held that the SEO's basin-wide determinations did not have any independent legal effect, but were limited to the SEO's duties to administer the dewatering of geological formations by facilitating or permitting the mining of minerals pursuant to C.R.S. § 37-90-137(7).¹⁵¹ Further, the water court found that the SEO's determinations were afforded the rebuttable presumption of validity. This ultimately means that a water court is not restrained from determining the tributary nature of the water if an oil and gas producer seeks to adjudicate its rights to this water, but the SEO's determination is given significant weight.

The ultimate effect of *Pawnee* is that the SEO has the authority to make basin-wide, nontributary groundwater determinations to facilitate the administration of groundwater associated with the mining of minerals. These determinations provide an exemption for a large number of non-CBM oil and gas wells to avoid the permitting process. The only portion of the SEO Rules the water court overturned was the Fruitland Rule and this is currently being appealed to the Colorado Supreme Court.¹⁵²

III. FUTURE POLICY IMPLICATIONS

The oil and gas industry was clearly worried about the potential result of the Court's decision in *Vance* and therefore sought to calm their fears in the Legislature even before they were sure about the end result in *Vance*. The actions of the Legislature and the upholding of the SEO's Rules in *Pawnee* do much to allay the fears of oil and gas producers. The Legislature and SEO have built on the *Vance* decision by both regulating gas development in Colorado and by carving out an exception for conventional development by specifically defining what does not constitute beneficial use and by conducting complex, basin-by-basin analysis of groundwater formations. While an increase in litigation and permitting costs to oil and gas producers in the State seems inevitable after these

146. *Id.*

147. Colorado State Engineer's Notice of Appeal from the Water Court Review of an Agency Action at *2, *Pawnee Well Users v. Wolfe*, No. 10CW89WL *1 (2011) (No. 2012SA13).

148. COLO. REV. STAT. § 37-92-305(6).

149. *Id.*

150. *Id.*

151. *Pawnee Well Users* at *23.

152. No. 2012SA13 *supra* note 147.

rules are implemented, these costs are not likely to be nearly as damaging to the industry as feared after the *Vance* decision.

These rules also created a legal distinction between CBM development, which is far more likely to affect tributary water supplies, and other forms of oil and gas development. By requiring that the SEO administer groundwater produced during oil and gas development, the *Vance* decision added significantly to the workload of the SEO. But the Legislature's actions reduced this burden when it worked closely with the SEO to create a streamlined regulatory framework. Thus, it is likely that oil and gas industry will not see the catastrophic cost increases it feared would occur after *Vance*. Further, now water rights owners have added legal protections over their groundwater rights.

Finally, the Legislature's recent decisions and actions have raised questions concerning the ownership of nontributary groundwater. Under Colorado law, landowners own the nontributary water beneath their land, as opposed to tributary groundwater, which is a separate right subject to the prior appropriations doctrine. Does this distinction give landowners more control over oil and gas development on their land in areas that are delineated as nontributary or less? Will this force more producers to deal directly with landowners in addition to regulatory agencies? Only time will tell.