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STATE WATER RESOURCE ADMINISTRATION IN THE FREE TRADE AGREEMENT ERA: AS STRONG AS EVER

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I. INTRODUCTION

Water, in its various forms, is the United States' most precious natural resource.¹ Despite a joint statement by the United States, Mexico and Canada that the North American Free Trade Agreement ("NAFTA") does not apply to water resources, some interest groups continue to raise concerns that international trade agreements, such as NAFTA and the General Agreement on Trade and Tariffs ("GATT"), may impair customary state regulation of water resources within the United States, leading to dangerous exploitation of its water resources.² The perceived dan-

1. NATIONAL WATER COMMISSION, WATER POLICIES FOR THE FUTURE ix (Water Information Center Inc. 1973).

2. See, e.g., Christopher Scott Maravilla, *The Canadian Bulk Moratorium and Its Implications For NAFTA*, 10 CURRENTS: INT'L TRADE L.J. 29, 33-34 (2001); Maude Barlow, *The Threat of International Trade and Investment Agreements*, International Forum on Globalization, available at <http://www.thirdworldtraveler.com> (accessed from homepage by selecting "Water page" and then selecting "Blue Gold – the global water crisis and the commodification of the world's water supply" and then selecting "The Threat of International Trade and Investment Agreements.") (last visited Oct. 30, 2007); Mel Clark, *Treason in Canada*, Nesara International, available at <http://nesara.insights2.org> (accessed from homepage by selecting "The Canada Page" and then selecting "Canada's Water Given to the US") (last visited Oct. 30, 2007); Christine Elwell, *NAFTA Effects on Water: Testing for NAFTA Effects in the Great Lakes Basin*, Sierra Club of Canada, available at <http://www.sierraclub.ca> (accessed from homepage by selecting "Transition to a Sustainable Economy" from the "Program Areas" drop down menu, then selecting "Trade and Environment" and then selecting "NAFTA Effects on Water – The Great Lakes Basin and Free Trade.") (last visited Oct. 30, 2007); Richard C. Booking, *NAFTA and Privatization*, available at <http://www.h2o.net/magazine/>

ger arises out of two fundamental suppositions. First, if water is a “good” or a “product,” once it is captured and placed into commerce it will be subject to protection under the trade protections set forth in NAFTA and GATT.³ As a consequence, some argue that the floodgates will open and state governments will lose the ability to control water removals of any size or by any method.⁴

The second position is grounded in the allegation that NAFTA’s Chapter Eleven, which sets forth foreign investment protections, will jeopardize existing and proposed state and local water resource management.⁵ Some argue that NAFTA arbitration tribunals, acting in closed, non-public proceedings, may award significant arbitration damages to foreign investors against the United States arising from state-based water resources management decisions, and that these awards will deter legitimate state laws designed to ensure sustainable use of water resources and environmental protection.⁶

As this article explains, these concerns are misplaced because they are premised on an incomplete and flawed understanding of the nature of property interests in water, the history and character of contemporary state water resource regulation, and the limits of these trade laws in the context of water resource management.⁷

The theory that NAFTA and GATT will “open the floodgates” to unbounded exports and consequential damages is founded upon the notion that the states’ right to regulate water is subordinate to the NAFTA and GATT mandates regarding free trade for identified tariff items—referred to as “products” (e.g., bottled water, beer, ethanol, produce, etc.).⁸ It is true that once water is bottled, it is in fact a product and a

urgences/enjeux/politiques/amerique_nord/canada/francais/bocking_1.htm (last visited Oct. 31, 2007).

3. See Part V(B), (C) *infra*, discussing the applicability of NAFTA and GATT to water in its natural state versus water that has been captured, packaged, and transformed into an article of commerce.

4. See, e.g., Cynthia Baumann, *Water Wars: Canada’s Upstream Battle to Ban Bulk Water Export*, 10 MINN. J. GLOBAL TRADE 109, 119-23 (2001); Clark, *supra* note 2.

5. See Jamie W. Boyd, *Canada’s Position Regarding an Emerging International Fresh Water Market with Respect to the North American Free Trade Agreement*, 5 NAFTA L. & BUS. REV. AM. 325, 335-36 (2005); See also MAUDE BARLOW & TONY CLARKE, *BLUE GOLD: THE FIGHT TO STOP THE CORPORATE THEFT OF THE WORLD’S WATER* 165-80 (Earthscan Publications 2003) (arguing that WTO trade panels uphold commerce issues over the environment).

6. See, e.g., Barlow, *supra* note 2; Booking, *supra* note 2; Clark, *supra* note 2; Elwell, *supra* note 2.

7. GEORGE A. GOULD, *WATER RIGHTS SYSTEMS: WATER RIGHTS OF THE EASTERN UNITED STATES* 8-10 (Kenneth Wright ed., American Water Works Assn. 1998) (“The law must necessarily reflect the nature of the legal problem to be resolved. Usually, the more complex the problem, the more complex must be the legal system. The allocation of water resources — the legal problem of water law — is quite complex.”).

8. See Plaintiffs’ Motion For Summary Disposition—Brief In Support of Motion, *Michigan Citizens for Water Conservation v. Great Springs Water of America, Inc.*, No. 01-14563-CE, (Mich. Cir. Ct. June 5, 2002), available at <http://www.savemewater.org>

good to which trade laws apply, indiscernible from other products.⁹ However, while water in a beer bottle may be a good, *water rights* are

(accessed from homepage by selecting “Water Court Case” and then “Motion for Summary Disposition – Brief in Support of Motion”) (last visited Nov. 1, 2007) (stating that if a water company is allowed to “sever and claim groundwater for itself to sell for private profit, wholly disconnected from the land or for that matter the State of Michigan, then nothing will stand in the way of the private exploitation or privatization of Michigan’s water resources by others. At that point the commerce clause or international trade agreements, like Chapter 11 of NAFTA or Section 10 of the World Trade Organization agreement, will chill or deprive the State of Michigan and citizens of any public ownership or control, subjecting the State to untold exorbitant losses.”); James M. Olson, *Finding the Gradient of Water Law: Michigan Citizens v. Nestle Waters North America, Inc.*, ST. B. MICH., ENV’T L. SEC. 25 (June 18, 2004); Cynthia Baumann, *Water Wars: Canada’s Upstream Battle to ban Bulk Water Export*, 10 MINN. J. GLOBAL TRADE 109, 127 (2001); Clean Water Action, *Don’t Privatize the Water: Keeping Michigan’s Water in Public Hands* 8 (Oct. 2005), available at www.cleanwateraction.org/mi/DontPrivatizeWaterHiRes.pdf (last visited Dec. 1, 2007).

9. See, e.g., *Sprinklets Water Center Inc. v. McKesson Corp.*, 806 F. Supp. 656 (E.D. Mich. 1992) (acknowledging that bottled water is treated as a refined product with a valuable commercial identity); *Quill Natural Spring Water Ltd. v. Quill Corp.*, No. 91 C 8071, 1994 WL 559237 (N.D. Ill. Oct. 7, 1994) (involving a trademark dispute concerning bottled water, and referring to such as a product); *Saratoga Vichy Spring Co. v. Lehman*, 625 F.2d 1037 (2d Cir., 1980) (acknowledging bottled mineral water as a product within trademark action); *Eniva Corp. v. Global Water Solutions, Inc.*, 440 F. Supp. 2d 1042 (D. Minn., 2006) (acknowledging bottled mineral water as a product); *Zepp v. Mayor & Council of Athens*, 348 S.E.2d 673 (Ga. 1986) (holding water distributed to customers is a good within the meaning of the Uniform Commercial Code); *Apani Southwest, Inc. v. Coca-Cola Enter. Inc.*, 300 F.3d 620; (5th Cir., 2002) (acknowledging bottled water as a product within an antitrust action); *Fisher v. Coca-Cola Bottling Co. of Los Angeles*, No. CV 78 0479-F (C.D. CA. 1979) (concerning an antitrust action relating to bottled water product identity); *Mayor of Jersey City v. Town of Harrison*, 71 N.J.L. 69 (1904) (comparing the sale of water by a municipality to that of a private vendor selling bottled water, and holding that since the bottled water sales were a sale of goods, it must follow that municipal water sales through a series of water works also constituted a sale of goods). Bottled water is regulated by the U.S. Food and Drug Administration (FDA) as a food product. See Federal Food, Drug, and Cosmetic Act, 21 U.S.C. §§ 301-97 (1996). As a product, the FDA regulates bottled water standards of identity and quality, as well as manufacturing processes. See 21 C.F.R. §§ 129, 165.110 (2006). Bottled water is also subject to the federal Fair Packaging and Labeling Act. 15 U.S.C. § 1451-61. (2007). Most state provisions regulating bottled water as a food product mirror the federal standards. In Michigan, the Michigan Food Law of 2000 adopts by reference the federal “food code.” MICH. COMP. LAWS ANN. § 289.6101(1) (West 2000). Section 7109 of the Michigan Food Law adopts the federal standards for the processing and bottling of bottled drinking water. MICH. COMP. LAWS ANN. § 289.7109 (West Supp. 2000). Section 7107 of the Michigan Food Law also sets forth the food quality standards for bottled water. MICH. COMP. LAWS ANN. § 289.7107 (West Supp. 2000). The Illinois Food, Drug and Cosmetic Act adopts the federal food standard regulations for bottled water. 410 ILL. COMP. STAT. ANN. 620/1 - 620/26 (West 1967). In Ohio, bottled water is included within the scope of the Ohio statutes regulating other food products such as soft drinks and nonalcoholic beverages. OHIO REV. CODE ANN. §§ 913.22-24 (West Supp. 2007). As a further example, in New York, the terms “food” and “food products” include “all articles of food, drink, confectionery or condiment, whether simple, mixed or compound, used or intended for use by man or animals and shall also include all substances or ingredients to be added to food for any purpose.” N.Y. AGRIC. &

not.¹⁰ Whether considered as an incident of land ownership¹¹ or an independent property interest arising from the application of water to a beneficial use, water rights are an interest in real property to which trade laws do not apply.¹² As I explain *infra*, the entire fabric of water law within the United States reflects the state's role in authorizing the acquisition of real property interests under the organic law of the state, in the interrelationships among the real property interests, and in the public regulation of those property interests,¹³ to which all but NAFTA's Chapter Eleven are inapplicable.

As for fears that NAFTA's Chapter Eleven will supersede state regulations, it must be noted that investor protections apply only to *investments* by foreigners.¹⁴ Rights to use water resources originate almost entirely under state law, subject to a few notable exceptions associated

MKTS. LAW § 2 (McKinney 2004). For a discussion of water as a product in the municipal context, see *Canavan v. Mechanicville*, 128 N.E. 882, 883 (N.Y. 1920); *McKeesport Municipal Water Authority v. McClosky*, 690 A.2d 766 (Pa. Commw. Ct. 1997); *Miller v. McKeesport Municipal Water Authority*, 555 A.2d 790 (Pa. 1989); *Mulberry-Fairplains Water Assn., v. Town of North Wilkesboro*, 412 S.E.2d 910, 915 (N.C. Ct. App. 1992); *Sternberg v. New York Water Service*, 155 A.D.2d 658, 659 (N.Y. App. Div. 1989); see also discussion of coverage of water within the Harmonized Commodity Description and Coding System at Part V(B) *infra*, notes 126-29.

10. See *Sullivan v. City of Ulysses*, 932 P.2d 456, 506 (Kan. Ct. App. 1977); *Cortella v. Salt Lake City*, 72 P.2d 630, 635 (Utah 1937); *Madison v. McNeal*, 19 P.2d 97, 98-101 (Wash. 1933); *Stanislaus Water Co. v. Bachman*, 93 P. 858, 862-63 (1908); see, e.g., SAMUEL WIEL, *WATER RIGHTS IN THE WESTERN STATES*, 83, 89 (Bancroft-Whitney 1905) (distinguishing between ownership of a water right and personalty).

11. See RESTATEMENT (SECOND) OF TORTS § 858, cmt. b (1979). Riparian rights have been characterized as part and parcel of the land itself, corporeal hereditaments, incorporeal hereditaments, easements, appurtenances and as tenancies in common in the stream. See, e.g., *Village of Tequesta v. Jupiter Inlet Corp.*, 371 So.2d 663 (Fla. 1979); John K. Bennett, *Some Uncertainties in the Law of Water Rights*, 21 S. CAL. L. REV. 344 (1948); John K. Bennett, *Some Fundamentals of Legal Interests in Water Supplies*, 22 S. CAL. L. REV. (1948).

12. See *infra* Part III(A); Charles J. Myers, *A Historical and Functional Analysis of the Appropriation System*, National Water Commission, Legal Study No. 5, 3-6 (1971) (stating that "[a] property right in the use of water is created by diversion of the water from a stream (or lake) and its application to beneficial use. Water can be used at any location, without regard to the position of place of use in relation to the stream."); Frank J. Trelease, *Federal-State Relations in Water Law*, National Water Commission, Legal Study No. 5, 5-6 (1971); George A. Gould, *Conversion of Agricultural Water Rights to Industrial Use*, 27 ROCKY MTN. MIN. L. INST. 1791, 1801 (1982).

13. Trelease, *supra* note 12, at 2-8 (stating that "[l]ike other laws governing scarce things the institutional framework of American water law is a combination of interacting property rights, economic forces and public regulation.").

14. North American Free Trade Agreement, art. 1139, Can.-Mex.-U.S., Dec. 8-17, 1992, 32 I.L.M. 289 (1993) [hereinafter NAFTA], also available at <http://www.nafta-sec-alena.org> (accessed from homepage by selecting "English" then "Legal Texts" and then "View the North American Free Trade Agreement (NAFTA)") (last visited Nov. 1, 2007).

with federal reservations.¹⁵ As such, *water rights* are acquired under and governed by state law. These laws acknowledge the existence of common law rights and ensure that the acquired rights comport with state notions of the public interest, and that the subsequent exercise of these rights is consistent with the initial authorization.¹⁶

State law and regulations establish rules that govern the origin of title to a water right and establish the terms under which a water right may be obtained and ultimately may vest against governmental takings.¹⁷ A state may comprehensively regulate all facets of the water right to foster economically productive, resource efficient and environmentally sound capture, storage, conveyance and distribution of water.¹⁸ Consequently, any investment in water made by a foreign investor is taken subject to the same regulatory conditions that prevail within the state and apply to all persons.¹⁹ Simply put, no water right can be obtained, nor investments made, in rights that exceed what is available under the applicable state property law.²⁰

The United States, therefore, will not be held liable under the Chapter Eleven investor protections for regulations relating to the acquisition and use of water resources so long as the regulations are non-discriminatory, are not applied arbitrarily, and due process of law is afforded to water resource regulation, like that afforded to any common land use regulation.²¹ These basic standards for government regulation

15. See Parts III(B) and IV(A) and (B) for a discussion of the various legal approaches to water resource allocation through the states. The principle notable exception to state regulation of water resource use is the doctrine of federal reserve rights, which prohibits a state from exercising its water allocation powers in a manner that deprives federal reserved lands of the water required to satisfy the primary or principle purposes of the federally reserved land. *Arizona v. California*, 373 U.S. 546, 601 (1963); *Winters v. United States*, 207 U.S. 564 (1908).

16. Frank J. Trelease, *New Water Legislation: Drafting for Development, Efficient Allocation and Environmental Protection*, 12 LAND & WATER L. REV. 385, 408-10 (1977); Trelease, *supra* note 12 at 5-6.

17. Trelease, *supra* note 12, at 5-6. See *infra* Part VI(D).

18. See *infra* Part IV. See, e.g., *Village of Tequesta*, 371 So.2d at 672 (analogizing water regulation to zoning laws).

19. *State v. Apfelbacher*, 167 N.W. 244, 246 (Wis. 1918) (stating that “the conveyance . . . to the state confers no greater right with reference to these flowing waters than [he] himself had. The condition of reasonable use attached to it before he conveyed it, and remained with it after such conveyance. The state stands in no better position with reference to its exercise than did or would the defendant . . .”).

20. See *Village of Tequesta*, 371 So.2d at 670-72 (holding that no property right is conferred until the potential user complies with applicable law); *Apfelbacher*, 167 N.W. at 245-46; see also, *Kennebunkport & Wells Water Dist. v. Maine Turnpike Auth.*, 71 A.2d 520 (Me. 1950); *Roberts v. Martin*, 77 S.E. 535 (W.Va. 1913).

21. *Village of Tequesta*, 371 So.2d at 667-69; see also *Allegretti & Co. v. County of Imperial*, 42 Cal. Rptr.3d 122 (Cal. Ct. App. 2006); *Baldwin v. County of Tehama*, 36 Cal. Rptr.2d 886 (Cal. Ct. App. 1994); *infra* Part VI(D).

and due process requirements are expected by most Americans.²² Chapter Eleven simply emulates these basic protections in the NAFTA context.

To date, the final awards issued by the NAFTA arbitration tribunals have denied claims for liability under Chapter Eleven investor-state arbitrations where a foreign investor is injured by a non-discriminatory environmental law that is applied with due process and in a non-arbitrary manner.²³ The NAFTA tribunals have distinguished trade-protective and arbitrary state actions, for which liability will be found, from non-discriminatory, fairly applied resource protection laws, which are permissible.²⁴ The final award in the recent Methanex decision is an apt example.²⁵

My analysis begins in Part II with a brief overview of NAFTA and GATT and their relation to water resources. Part III provides an introduction to the laws governing the use of water, and the interplay of water rights law and NAFTA and GATT. Part IV discusses the role of the public interest and the police power in authorizing water use and in regulating water uses. Part V discusses the protections afforded to trade in goods under NAFTA and GATT, and why these provisions will not impair legitimate water resource management. Part VI examines the application of NAFTA's Chapter Eleven investor protections to water management laws, including the resolution of NAFTA investor-state arbitration claims. Part VII sets forth my thoughts on the essential elements of water resource management planning that will survive challenges under NAFTA and GATT, and then considers the Great Lakes-St. Lawrence River Basin Water Resources Compact ("Compact") as a contextual example of the state's role in the administration of water resources in the trade agreement era.

22. See B. F. Wright, *American Interpretation of Natural Law* (Russell and Russell 1962) (1931); L. Strauss, *Natural Right and History* (Univ. of Chicago Press 1957); Julius Stone, *Human Law and Human Justice* (Stanford Univ. Press 1965); Richard Tuck, *Natural Rights Theories* (Cambridge Univ. Press 1982); Lloyd L. Weinreb, *Natural Law and Justice* (Harvard Univ. Press 1987); Russell Hittinger, *A Critique of the New Natural Law Theory* (Univ. of Notre Dame Press 1988); Universal Declaration of Human Rights, art. I, G.A. Res. 217A, U.N. GAOR 3d Sess., 1st plen. Mtg., U.N. Doc. A/810 (Dec. 10, 1948).

23. See *infra* Parts VI(C), (D).

24. *Methanex Corp. v. United States*, Final Award, ¶ 1 (2005), [hereinafter *Methanex I*], available at <http://www.state.gov> (accessed from homepage by entering "Methanex 51052" into search window and selecting hyperlink) (last visited Nov. 1, 2007).

25. *Id.*

II. NAFTA AND GATT—BRIEF REVIEW OF THE TREATIES AND THEIR RELATION TO WATER RESOURCES

GATT was first signed in 1947.²⁶ The agreement was designed to provide an international forum that encouraged free trade between member states by regulating and reducing tariffs on traded goods and by providing a common mechanism for resolving trade disputes.²⁷ GATT membership includes more than 151 countries as of July, 2007.²⁸ In 1994, as a result of eight years of trade negotiations, commonly referred to as the Uruguay Round, the World Trade Organization (“WTO”) replaced GATT as an international organization to govern trade.²⁹ However, GATT still exists as the “WTO’s umbrella treaty for trade in goods,”³⁰ updated as a result of the Uruguay Round negotiations.³¹

NAFTA is a separate agreement entered into between the United States, Canada, and Mexico, which became effective on January 1, 1994.³² NAFTA creates a free-trade bloc between the three countries through the elimination of barriers so that goods and services can flow freely throughout the continent.³³ The agreement sets forth provisions to eliminate trade barriers, resolve disputes, promote fair competition, and increase investment opportunities throughout the three countries.³⁴ NAFTA is a successor trade agreement to the GATT in relation to trade between these nations.³⁵

Of particular relevance here are Articles III and XI of GATT, which require national treatment of goods and prohibit quantitative re-

26. World Trade Organization, Understanding the WTO - The GATT Years: from Havana to Marrakesh, *available at* <http://www.wto.org> (accessed from homepage by searching for “the GATT years” and selecting “Understanding the WTO – The GATT Years: from Havana to Marrakesh”) (last visited Nov. 1, 2007).

27. World Trade Organization, Understanding the WTO - What is the World Trade Organization?, *available at* <http://www.wto.org> (accessed from homepage by selecting “Introduction”) (last visited Nov. 1, 2007).

28. World Trade Organization, Understanding the WTO - The Organization: Members and Observers, *available at* <http://www.wto.org> (accessed from homepage by selecting “Introduction” then expanding “The organization” menu and selecting “Members List”) (last visited Nov. 1, 2007).

29. World Trade Organization, Understanding the WTO - What is the World Trade Organization?, *available at* <http://www.wto.org> (accessed from homepage by selecting “The Basics”) (last visited Nov. 1, 2007).

30. Antonio Alice Badway, *Controlling the Export of Dual-Use Technology in a Post-9/11 World*, 18 *TRANSNAT’L L.* 431, 440 (2005).

31. *Id.*

32. NAFTA, Frequently Asked Questions, *available at* <http://www.nafta-sec-alena.org> (accessed from homepage by selecting “Frequently Asked Questions”) (last visited Nov. 1, 2007).

33. Boyd, *supra* note 5, at 331.

34. NAFTA, *supra* note 14, art. 102. For a general description of NAFTA, *see also* NAFTA, *supra* note 32.

35. Rafael Leal-Arcas, *Choice of Jurisdiction in International Trade Disputes: Going Regional or Global?*, 16 *MINN. J. INT’L L.* 1, 8, 14-17 (2007).

strictions on imports or exports of products.³⁶ Some fear that in the event that water is traded internationally, Article XI's prohibition on import/export restrictions will require the continued trading of water resources in bulk even if the export were damaging to the environment.³⁷

NAFTA's Chapter Three governs "national treatment" and market access for goods, including import and export restrictions.³⁸ Like the concerns expressed in relation to GATT's Article XI, some allege that the protections for trade in goods set forth in Chapter Three will prevent a nation from imposing restrictions on the capture and export of water resources, resulting in harm to the resource, environment and the local populace's water supply needs.³⁹ Some commentators also note that water as a commodity is not exempted from Chapter Three, which expressly exempts other products from NAFTA's trade protections such as raw fish and logs exported from Quebec, and on this basis allege that NAFTA applies to limit water resource laws.⁴⁰ I explain in Part V why these concerns are misguided.

The concern expressed by some that allowing exports of bottled water or other water-laden products now will create exposure to the

36. General Agreement on Tariffs and Trade, art. III, Oct. 30, 1947, 55 U.N.T.S. 194 [hereinafter GATT]. The GATT parties adopted GATT again in 1994, with minor changes, as part of the agreement creating the WTO. Agreement Establishing the World Trade Organization, art. I, Apr. 15, 1994, 33 I.L.M. 1125, 1144 (1994). When it is necessary to distinguish the two, they are called "GATT 1947" and "GATT 1994." See, e.g., General Agreement on Tariffs and Trade: Multilateral Trade Negotiations Final Act Embodying the Results of the Uruguay Round of Trade Negotiations, Introductory Note, 33 I.L.M. 1125, 1127 (1994). GATT Article III provides, "[t]he products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products." GATT art. III. GATT Article XI provides:

No prohibitions or restrictions other than duties, taxes, or other charges, whether made effective through quotas, import or export licenses or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party.

Id. at art. XI.

37. Robert J. Girouard, *Water Export Restrictions: A Case Study of WTO Dispute Settlement Strategies and Outcomes*, 15 GEO. INT'L ENVTL. L. REV. 247, 252 (2002).

38. NAFTA, *supra* note 14, at ch. 3.

39. See, e.g., Baumann, *supra* note 4; J. Owen Saunders, *Trade Agreements and Environmental Sovereignty: Case Studies from Canada*, 35 SANTA CLARA L. REV. 1171 (1995); Sanford E. Gaines, *Fresh Water: Environment or Trade?*, 28 CAN.-U.S. L.J. 157 (2002); Marcia Valiante, *Harmonization of Great Lakes Water Management in the Shadow of NAFTA*, 81 U. DET. MERCY L. REV. 525, 544 (2004).

40. See Maravilla, *supra* note 2, at 32-34; Ruth Walker, *Water Lawsuit Tests NAFTA First for Profit*, CHRISTIAN SCI. MONITOR, Dec. 16, 1998, at 7; see also *infra* Part V(C), explaining that water in its natural state is inherently not a good governed by NAFTA, and NAFTA's trade protections do not apply to water resource management laws. Therefore, NAFTA need not exempt water from NAFTA's trade protections. This point has also been made by Canada's former trade minister. See *infra* note 148.

United States under NAFTA and GATT if states attempt to place subsequent limitations on bulk transfers,⁴¹ is also misguided. The bottled water industry is, and has been for years, a robust interstate, national, even international, industry.⁴² An effort for its own sake to unwind the transportation of water in small containers would be a fool's errand, as the industry represents such a small fraction of consumptive water uses.⁴³

41. See *supra* note 8.

42. Claudia H. Deutsch, *For Fiji Water, a Big List of Green Goals*, N.Y. TIMES, Nov. 7, 2007, available at <http://query.nytimes.com/gst/fullpage.html?res=9E05EEDF103AF934A35752C1A9619C8B63&n=Top/Reference/Times%20Topics/People/D/Deutsch,%20Claudia%20H> (last visited Dec. 12, 2007).

43. Fresh water withdrawals for bottled water are literally a drop in the bucket when considered in the context of other consumptive uses. For example, irrigated agriculture withdraws 150 million acre-feet per year, 91 million acre-feet of which are applied to consumptive uses. United States Department of Agriculture – Economic Research Service, *Irrigation and Water Use: Questions and Answers*, available at <http://www.ers.usda.gov> (accessed from homepage by selecting “Briefing Rooms” from the horizontal menu, then selecting “Irrigation and Water Use” then selecting “Water Allocation, Water Conservation, and Water Management” within the Overview paragraph, then selecting “How much does irrigated agriculture use?”) (last visited Nov. 1, 2007). To emphasize the point, in a typical year, a single Colorado River contractor, the Imperial Irrigation District, historically diverted approximately 3 million acre-feet for agricultural irrigation, or roughly 120 times the amount of water withdrawn by the entire national bottled water industry. The Border Environment Cooperation Commission, *Imperial Irrigation District Water Conservation Project*, available at <http://www.cocef.org> (accessed from homepage by selecting “English,” then expanding the “Projects” menu, then selecting “Certified Projects,” selecting “CA,” then selecting “Imperial, California – Water Conservation (ID-405)”) (last visited Nov. 14, 2007); International Bottled Water Association, *the 2005 Stats*, available at <http://www.bottledwater.org> (accessed from homepage by selecting “Beverage Marketing’s 2006 Market Report Findings”) (last visited Nov. 1, 2007). A single watermelon requires 100 gallons of freshwater to produce; a single serving of chicken requires 408 gallons; a single serving of steak requires 2,607 gallons. International Bottled Water Association, “How Much Water Do We Use?”, available at <http://www.bottledwater.org> (accessed from home page by selecting “Site Map” then selecting “Fact Sheets and Q&A’s” then selecting “How Much Water Do We Use?”) (last visited Nov. 14, 2007). Even within the beverage sector alone, bottled water is not an extraordinarily large use. According to data from the International Bottled Water Association, Americans consumed 25,472 acre-feet of bottled water in 2006, or about 28.3 gallons per person. International Bottled Water Association, *The 2005 Stats*, available at <http://www.bottledwater.org> (accessed from homepage by selecting “Beverage Marketing’s 2006 Market Report Findings”) (last visited Nov. 1, 2007). This is a small fraction of the total freshwater use in America. American breweries produced 18,666 acre-feet of beer in 2004-2005. See Barth-Haas Group, *World Beer Production 2004/2005*, available at <http://www.barthhaasgroup.com> (accessible from homepage by selecting “News & Reports” then selecting “The Barth Report – 2006/2007” and then selecting “English” adjacent to “2005-2006 Barth Report also available”) (last visited Nov. 1, 2007). Additionally, the top ten soft drink companies produced 70,703 acre-feet of soft drinks in 2006. Beverage Digest, *Data & Statistics*, available at <http://www.beverage-digest.com> (accessible from homepage by selecting “Data” and then selecting “2005 top-10 data”) (last visited Nov. 1, 2007); Moreover, concerns regarding exports of water to faraway lands are also mitigated by the practical limitations of such exports. See J.W. Buckley, S.J. Wright & D. Wright, *Preliminary Study of the*

Further, the United States Supreme Court has already declared that water is in fact an article of commerce,⁴⁴ and that a state may not enact a facially discriminatory ban on the export of groundwater to another state.⁴⁵

Nevertheless, because commentators continue to express concerns that NAFTA and GATT are a threat to the integrity of state water resource management plans, I will address the legal contentions on their merits. In summary, the argument that a failure to limit exportation of bottled water has implications for water resource management⁴⁶ completely mischaracterizes the proper inquiry and thus begs a misleading answer.

Regulation of water in a bottle has almost nothing to do with a water right or the state's administration of its water resources. Bottled water is a product created from water that has been extracted and placed in a container, and is no different from soda or beer. While the corpus of the water may in some cases constitute personalty or a good, the water right itself remains realty.⁴⁷ That water exists in a bottle is merely evidence that the state has authorized, by common law, statute, or both, a public or private proprietor to obtain a *water right* that will permit the use of water in a manufacturing process where water is captured for subsequent human hydration.

Conversely, *water rights*—as opposed to products containing water—are interests in real property.⁴⁸ They are not goods or products.⁴⁹ They are acquired in accordance with state law and reflect public interest considerations while they are managed in accordance with the police power.⁵⁰ They embody the state's authorization for the taking of water and its application to a beneficial use.⁵¹ Until the water is separated from the land and joins commerce as a good or as a product, it remains an

Diversion from Lake Superior to the Missouri River Basin, 68 J. HYDROLOGY 461, 469 (1968); Robert Haskell Abrams, *Setting Regional Policy on Diverting Great Lakes Water to the Arid West: Scaling Down the Myths*, THE WAYNE LAWYER, Sep. 22, 1982, at 6. Shipping United States water by tanker to a foreign country may not constitute the best water augmentation strategy for potentially thirsty buyers. *Id.* Any country that has the capability of receiving water by tanker has access to desalinated water, which will likely be considerably less expensive and provide greater control and reliability. *Id.* Likewise, land routes for exporting water over long distances are also likely not cost-effective in most situations given the radical escalation of construction costs for large volume conveyance facilities in recent years. See Robert Glennon, *Water Scarcity, Marketing, and Privatization*, 83 TEX. L. REV. 1873 (2005).

44. *Sporhase v. Nebraska ex rel. Douglas*, 458 U.S. 941, 941 (1982).

45. *City of El Paso v. Reynolds*, 563 F. Supp. 379, 388 (D.N.M. 1983).

46. See *supra*, note 8.

47. See *supra*, note 10.

48. See *infra*, note 65.

49. *Id.*

50. See *State of California v. Superior Ct. of Riverside County*, 93 Cal. Rptr.2d 276, 285 (Cal. Ct. App. 2000); *Hawley v. Kansas Dept. of Agriculture*, 132 P.3d 870, 881 (Kan. 2006).

51. *Riverside County*, 93 Cal. Rptr.2d at 280-82; *Hawley*, 132 P.3d at 882.

interest in real property.⁵² A state remains free to regulate interests in real property, including the acquisition and use of water rights as a matter of its state laws applicable to private property rights. Accordingly, Chapter Three of NAFTA and Articles III and XI of GATT do not limit the customary exercise of state water resource management.⁵³

Chapter Eleven of NAFTA governs the treatment and protection of foreign investors and foreign investments made within the territory of NAFTA co-signers.⁵⁴ The Chapter contains several key investor protection provisions that NAFTA critics allege may be used to challenge the application of state water laws: national treatment (Article 1102), minimum standard of treatment (Article 1105), and compensation for investment expropriations (directly or indirectly) (Article 1110).⁵⁵ Articles 1116 and 1117 of NAFTA allow for an investor, as opposed to solely a nation state, to submit a dispute under Chapter Eleven for arbitration of alleged violations of Chapter Eleven's investor protections.⁵⁶

Some allege that these investor protections will result in claims for substantial damages against host nations arising out of legitimate water resource management laws, and that the resulting arbitration awards will cause a chilling effect upon necessary water resource regulation by the host nation's political subdivisions.⁵⁷ I will explain in Part VI why these concerns merely reflect a continuation of the critical misunderstanding of water resource management within the United States - an admittedly arcane body of law - and are dramatically overstated.

III. THE NATURE OF PROPERTY RIGHTS IN WATER

A. *Water Rights are an Interest in Real Property*

Water rights in the United States are important and revered property rights.⁵⁸ Land without water in the arid West is comparatively

52. See *infra*, note 58. Water may constitute an "article of commerce" for purposes of the dormant Commerce Clause. See *Sporhase*, 458 U.S. at 941. The point at which the corpus of the water is severed from the real property and becomes "personalty" is subject to a division of authority among the states. *Stanislaus Water Company*, 93 P. at 862; *Turley v. Furman*, 114 P. 278, 279 (N.M. 1911).

53. See *infra*, Part V.

54. See e.g. NAFTA, *supra* note 14.

55. See NAFTA, *supra* note 14, arts. 1102, 1105, and 1110.

56. See NAFTA, *supra* note 14, arts. 1116 and 1117.

57. See, e.g., NATIONAL WATER COMMISSION, *supra* note 1, at ix.

58. *Dugan v. Rank*, 372 U.S. 609, 625 (1963); *Ivanhoe Irrigation Dist. v. McCracken*, 357 U.S. 275 (1958); *United States v. Gerlach Live Stock Co.*, 339 U.S. 725, 733-36 (1950) (considering whether compensation was due from the U.S. Bureau of Reclamation for the destruction of riparian water rights incident to the construction of the Central Valley Project ("CVP"). The court expressly addressed the right to take water *in the future*. Relying on the fact that "Congress has recognized the property status of water rights vested under California law" within the provisions of the Reclamation Act, the Court held that compensation was due.); *International Paper Co. v. United States*, 282

worthless.⁵⁹ Even in the East, where rainfall is more plentiful, water rights are an important limiting factor on growth and economic productivity.⁶⁰ In-stream flow requirements and other ecological needs for water further limit the remaining supply available for competing users.⁶¹ Despite the enormous importance of water to our society's well being, water law remains obscure and frequently misunderstood.⁶²

In the United States, the authority to permit the accrual of water rights and the responsibility for management of water resources has been retained primarily by the states.⁶³ Likewise, each state has laws that reflect the resource policies of the state and, in some cases, implement federal standards such as the Clean Water Act.⁶⁴

U.S. 399, 407 (1931) (considering the diversion of water that otherwise supplied plaintiff's water rights, which were used in its paper mill operation. The court held that "the petitioner's right was to the use of water; and when all the water that it used was withdrawn from the petitioner's mill and turned elsewhere by government requisition for the production of power it is hard to see what more the Government could do to take that use." Accordingly, the Supreme Court awarded compensation for the loss of the right to take water in the future.); *see also* Nevada v. United States, 463 U.S. 110, 123 (1983); State of Arizona v. State of California, 460 U.S. 605, 620 (1983); *Sullivan*, 932 P.2d at 506; *Cortella*, 72 P.2d at 635; *Riverside County*, 93 Cal. Rptr.2d at 276; *Schimmel v. Martin*, 213 P. 33, 34 (Cal. 1923); *Washoe County Nevada v. United States*, 319 F.3d 1320, 1322 (Fed. Cir. 2003) (holding that "a water right is property subject to constitutional protection"); SCOTT SLATER, CALIFORNIA WATER LAW AND POLICY § 1-11 (MICHIE PARKER PUBLICATIONS DIV. 2006). Moreover, the statute of frauds applies to conveyances of water rights. *Waterford Irrigation Dist. v. Stanislaus County*, 228 P.2d 341, 345 (Cal. Ct. App. 1951). Likewise, the statute of limitations concerning land *e.g.* apply to water rights as well. *See, e.g.*, *Staats v. Newman*, 988 P.2d 439, 441 (Or. Ct. App. 1999) (citing OR. REV. STAT. § 540.610.1).

59. *See* *City of El Paso v. Reynolds*, 563 F. Supp. 379, 381 (D.N.M. 1983); *The Bureau of Reclamation, A Very Brief History*, available at <http://www.usbr.gov/history/borhist.html> (last visited Nov. 22, 2007).

60. For example, Georgia, Florida, and Alabama have been locked in a three-way legal battle over water rights for almost two decades. Atlanta's rapid growth has strained water supplies, especially during the current drought. *Short-Term Water Fix Proposed in Southeast*, Associated Press, Nov. 1, 2007, available at <http://www.msnbc.msn.com/id/21584661/>. (last visited Nov. 14, 2007).

61. *See* *Public Utility Dist. No. 1 of Pend Oreille County v. State Dept. of Ecology*, 51 P.3d 744, 770 (Wash. 2002) (holding that "[m]inimum instream flows constitute an appropriation affecting competing claims to the same water."); *Alliance to Save the Mattaponi v. Commonwealth, Dept. of Environmental Quality ex rel. State Water Control Bd.*, 621 S.E.2d 78, 88-89 (Va. 2005); *Columbus & Franklin County Metropolitan Park Dist. v. Shank*, 600 N.E.2d 1042, 1053-54 (Ohio 1992).

62. DAVID H. GETCHES, *WATER LAW IN A NUTSHELL* 2-3 (3d ed. 1997).

63. *Idaho Power Co. v. State, By and Through Dept. of Water Resources*, 661 P.2d 741, 755 (Idaho 1983) (holding that "[u]nder] Section 27 of the Federal Power Act, 16 U.S.C. § 821, all state water law is preserved 'relating to the control appropriation, use, or distribution of water.'"); *see also* *Solid Waste Agency of Northern Cook County v. U.S. Army Corps of Eng'rs*, 531 U.S. 159, 174 (2001).

64. *Public Utility Dist. No. 1 of Pend Oreille County*, 51 P.3d at 759 (holding that "[u]nder the Clean Water Act, the state is required to enforce water quality standards on intrastate waters."); *Building Indus. Ass'n of San Diego County v. State Water Resources Control Bd.*, 22 Cal. Rptr.3d 128, 133 (Cal. Ct. App. 2004).

Two fundamental aspects of water rights in the United States are critical to understanding this body of law. First, water rights are real property interests.⁶⁵ Second, whether water rights are derived as an incident of land ownership or by compliance with common law or statutory requirements, they are usufructuary property rights in a shared public resource⁶⁶ and vest only to make use of the common supply and, even

65. *See, e.g.*, *Federal Land Bank of Spokane v. Union Cent. Life Ins. Co.*, 29 P.2d 1009, 1011 (Idaho 1934) (holding that “a water right is real property and may be sold and transferred separately from the land upon which it has been used, the same as any other real property.”); *King v. White*, 499 P.2d 585, 588 (Wyo. 1972) (holding that “a water right is a ‘property right of high order,’ with ‘none of the characteristics of personal property,’ and it is real property.”); *Northern Ohio Traction & Light Co. v. Quaker Oats Co.*, 114 Ohio St. 685, 696 (1926) (holding that “a water right is a species of property in and of itself . . .”). Water rights are separately assessed by the tax assessor. *See CALIFORNIA STATE BOARD OF EQUALIZATION, ASSESSORS’ HANDBOOK* § 542, *ASSESSMENT OF WATER COMPANIES AND WATER RIGHT, PART II: ASSESSMENT OF WATER RIGHTS* (Dec. 2000); *In re Assessment of Taxes of C.W. Booth*, 1904 WL 1285, 1 (Haw. 1904) (holding that “[i]f land with water rights appurtenant thereto and used solely in connection therewith, is assessed in full . . . such water rights cannot be further assessed apart from the land . . .”). Water rights may be exchanged for real property and then back again for water rights in accordance with Internal Revenue Code § 1031, as “like kind” interests in real property. *Rev. Rul. 55-749*, 1955-2 C.B. 295, *distinguished by Rev. Rul. 67-255*, 1967-2 CB 270. The same statutes that countenance adverse possession and prescription of other real property interests apply equally to water rights. *See Ebell v. City of Baker*, 299 P. 313, 317-18 (Or. 1931) (holding that “a city can lose its water rights by adverse possession and user by another, amounting to prescription”); *Kountz v. Olson*, 29 P.2d 627, 629-30 (Colo. 1934); *In re Drainage Area of Bear River in Rich County*, 361 P.2d 407, 408-09 (Utah 1961). When expropriated, just compensation is required under the Fifth Amendment of the United States Constitution. U.S. CONST. amend. V. Even civil remedies to redress an unauthorized private interference with one’s water right sound in trespass and nuisance; not conversion, replevin or trover. *Viestenz v. Arthur Township*, 54 N.W.2d 572, 578 (N.D. 1952) (holding that “a wrongful interference with waters or water rights . . . may constitute a nuisance”); *Trelease, supra* note 12, at 2-8 (holding that “[t]he allocation of property rights in water resources follows the pattern set for other resources like minerals or like land itself”).

66. *Eddy v. Simpson*, 3 Cal. 249, 252-53 (1853) (holding that “[t]he right of property in water is usufructuary, and consists not so much of the fluid itself as the advantage of its use”); *RESTATEMENT (SECOND) OF TORTS* § 858, cmt. B (1979); 1 *WELLS A. HUTCHINS, WATER RIGHTS LAWS IN NINETEEN WESTERN STATES* 151 (U.S. Dept. Agric. 1971). A water right, by definition, concerns the right to take water from its source, not a right to a particular molecule of water. *See Riverside County*, 93 Cal. Rptr.2d at 286-87; *Akron Canal & Hydraulic Co. v. Fontaine*, 50 N.E.2d 897, 901 (Ohio Ct. App. 1943) (holding that “[i]t is not an ownership in the water but a right to its flow for the various lawful uses to which it may be subjected”); *Town of Chino Valley v. City of Prescott*, 638 P.2d 1324, 1328 (Ariz. 1981) (holding that “[t]he right of the owner to groundwater underlying his land is to the usufruct of the water and not the water itself”); *In the Matter of the Rights to the Use of the Gila River*, 830 P.2d 442, 447 (Ariz. 1992) (holding that “[w]ater rights are property rights”); *Hammond v. Johnson*, 66 P.2d 894, 898 (Utah 1937) (holding that “‘water rights,’ as acquired by private persons or companies, includes or means the right to the use thereof, and does not, except under certain limited conditions, vest any title to the corpus of the water in the appropriator or user”); *Rock Creek Ditch & Flume Co. v. Miller*, 17 P.2d 1074, 1076-77 (Mont. 1933) (holding that “[t]he so-called ‘ownership’ of water differs from that of personal property capable of corporeal

then, not without regard to the impact of one's use upon others⁶⁷ and the environment.⁶⁸ It is these oft-overlooked nuances of property law that collectively serve to insulate state water and resource protection laws from NAFTA and GATT challenges.

possession. Neither the appropriator of water nor one to which a right is decreed owns the corpus of any part of the flow of the stream”).

67. RESTATEMENT (SECOND) OF TORTS § 850A (1979); *see also* Bernard v. City of St. Louis 189 N.W. 898, 893 (Mich. 1922) (holding that the defendant should only be required “not to interfere with an adequate supply of water for the plaintiffs’ reasonable use”); Maerz v. US Steel Corp., 323 N.W.2d 524 (Mich. Ct. App. 1981); East Bench Irrigation Co. v. Deseret Irrigation Co., 271 P.2d 449, 455 (Utah 1954) (holding that “a change in place of diversion or the place or nature of use or a combination of such changes cannot be made if the lower users, whether prior or subsequent to the rights of the parties making the change will thereby be deprived of the use of water which they would have had under the use which the upper appropriators made before the change”).

68. *See, e.g.*, ALASKA STAT. § 46.15.080(b)(1)-(8) (1989); ARIZ. REV. STAT. ANN. § 45-153 (1987); CAL. WATER CODE §§ 1253, 1255, 1257, and 1257.5 (West 1971) (requiring California State Water Resources Control Board to weigh impacts on instream uses and environmental effects of permitting water appropriations); COLO. REV. STAT. § 37-92-102(3) (2004) (vesting Colorado Water Conservation Board with authority to appropriate water rights in accordance with principles of environmental protection); HAW. REV. STAT. § 174C-49(a)(4) (1991); IDAHO CODE ANN. §§ 42-203A, 203C (2003); MONT. CODE ANN. §§ 85-2-302-311(2) (2007); NEV. REV. STAT. §§ 533.325, .370(3), and 534.050(1) (2005); N.M. STAT. ANN. §§ 72-5-1, -6, -7, 72-12-3(e) (West 1985); N.D. Cent. Code §§ 61-04-02, -06 (West 1985); OR. REV. STAT. § 537.460 (2003) (indicating that public interest consideration covers water quality); OR. REV. STAT. §§ 537.130, .170(4) (2003); S.D. CODIFIED LAWS §§ 46-1-15, -2a-9, -5-10, -6-3 (1988); TEX. WATER CODE ANN. §§ 11.121, .134(3), .134(4), .147, .150, .152, .1271, and .1331 (Vernon 1995); UTAH CODE ANN. §§ 73-3-1, -8(1) (2007); WASH. REV. CODE §§ 90.03.250, 03.290, .44.050, and .44.060 (2004); WYO. STAT. ANN. §§ 41-4-503, 41-3-930 -931, and -932 (1977 & Supp. 1990); Shokal v. Dunn, 707 P.2d 441, 448-49 (Idaho 1985) (citing IDAHO CODE § 42-1501 and requiring Director of Water Resources to consider factors such as “protection of fish and wildlife habitat, aquatic life . . . aesthetic beauty . . . and water quality” in assessing an application for water rights); Stempel v. Department of Water Resources, 508 P.2d 166, 172 (Wash. 1973) (citing REV. CODE OF WASH. § 90.54.020(3) in holding that issuance of water use permit must be conditioned on the protection of the quality of the natural environment); *see also* Craig Bell and Norma Johnson, *State Water Laws and Federal Water Uses: The History of Conflict, The Prospects for Accommodation*, 21 LEWIS & CLARK ENV'T'L L.J. 1, 8-16 (1991); John C. Peck, *Property Rights in Groundwater--Some Lessons from the Kansas Experience*, 12 KAN. J. L. & PUB. POL'Y 493, 507 (2003). It should also be noted that although the states possess broad discretion as to whether an application for a new water right is consistent with the public interest and the environment, the state's authority may be constrained by takings problems in the event vested water rights are taken for public benefit in the future. *See, e.g.*, *Gerlach Live Stock Co.*, 339 U.S. at 733-36; *Tulare Lake Basin Water Storage Dist. v. U.S.*, 49 Fed.Cl. 313 (2001); *but see* *Klamath Irrigation Dist. v. United States*, 67 Fed.Cl. 504 (2005). However, takings concerns associated with reallocation of water after private rights have vested can largely be avoided when the state reserves its property in the public interest. Public parks such as Yellowstone National Park have long been reserved without alienation into private ownership and the state may make similar reservations in the public interest with regard to water resources. *See* Frank J. Trelease, *The Model Water Code, the Wise Administrator and the Goddam Bureaucrat*, 14 NAT. RESOURCES J. 207, 213 (1974).

B. Property Rights in a Shared Resource

Water rights regimes vary throughout the United States. With regard to surface water, some states follow a riparian rights regime, derived from the original English common law, which may impose reciprocal rights and obligations upon landowners abutting a body of surface water, whereby they receive the right to withdraw water for their reasonable use.⁶⁹ Among the states that recognize riparian rights there are considerable divisions as to the definition of “riparian use” and the limitations on the place of beneficial use.⁷⁰ Other states follow the doctrine of prior appropriation, originating from the mining camps in the 19th Century West. The doctrine of prior appropriation does not limit use to riparian lands nor to particular purposes, but instead provides that rights are obtained by historical usage and are prioritized based upon the date of initial appropriation.⁷¹ This system accords the first appropriator a paramount claim to water where there is insufficient water to meet the needs

69. *See, e.g.*, *United States v. Willow River Power*, 324 U.S. 499 (1945) (stating that “each riparian proprietor has an equal right to make a reasonable use of waters of the stream subject to the equal right of the other riparian proprietors to make a reasonable use.”); *Carlsbad Mut. Water Co. v. San Luis Rey Development Co.*, 178 P.2d 844, 851 (Cal. Ct. App. 1947) (stating that “[s]uch riparian owner, by reason of the situation of his land on the stream, has the right to make any reasonable and beneficial use to himself on the riparian land.”); *Harris v. Brooks*, 288 S.W.2d 129 (Ark. 1955); *see also*, *Thompson v. Enz*, 154 N.W.2d 473, 483-84 (Mich. 1967); JOSEPH W. DELLAPENNA, *AMERICAN SOCIETY OF ENGINEERS, THE REGULATED RIPARIAN MODE WATER CODE* (ASCE Publications 1997); Joseph W. Dellapenna, *Owning Surface Water in the Eastern United States*, 6 PROC. E. MIN. L. ROUND. 102, 133-134 (1985); 78 Am. Jur. 2d Waters § 49 (2002).

70. There is a division of authorities regarding the enjoyment of riparian rights and whether water use must be limited to the riparian tract. Some states limit the use of riparian water rights. *See, e.g.*, *Harrell v. City of Conway*, 211 SW.2d 924 (Ark. 1954); *Town of Purcellville v. Potts* 19 S.E.2d 700 (Va. 1942); *McBryde Sugar Company, Ltd., v. Robinson* 504 P.2d 1330 (Haw. 1973). Some states limit water use to the smallest riparian tract within the chain of title (the “source of title” or “smallest tract” rule) and others allow a riparian to aggregate land to expand the reach of the right (the “unity of title” rule). JOSEPH SAX, BARTON THOMPSON, JR., JOHN LESHY & ROBERT ABRAMS, *LEGAL CONTROL OF WATER RESOURCES* 23, (West Group 2000). Other states avoid the problem entirely by applying a rule of reasonable use that does not exclude off-tract uses *per se*. *See, e.g.*, *Smith v. Stanolind Oil & Gas Co.* 172 P.2d 1002 (Okla. 1946); *Michigan Citizens for Water Conservation v. Nestle Waters North America, Inc.*, 709 N.W.2d 174 (Mich. Ct. App. 2005), *rev'd in part*, 737 N.W.2d 447 (Mich. 2007); *Texas Co. v. Burkett* 296 S.W. 273 (Tex. 1927); RESTATEMENT (SECOND) OF TORTS §§ 850, 850A (1979).

71. *See Carson v. Gentner*, 52 P. 506, 508 (Or. 1898); *Pleasant Valley Canal Co. v. Borrer*, 72 Cal. Rptr.2d 1, 8 (Cal. Ct. App. 1998) (reasoning that “[i]n 1872, the state Legislature added provisions to the Civil Code—essentially a codification of the rules that had grown up in the mining camps—creating a statutory procedure for securing appropriative water rights”).

of all.⁷² Still other states use a hybrid system in which both riparian and prior appropriative rights are recognized.⁷³

Groundwater law presents a similar set of common law rights and administrative regulation. Groundwater rights may be acquired as overlying rights (the analog to the riparian right), prior appropriation rights, or pursuant to a state licensing scheme.

Regardless of its type of water rights regime, each state recognizes a right *to use* water and sets forth the terms and conditions under which rights may be obtained.⁷⁴ While water rights throughout the United States are an interest in real property,⁷⁵ they attach to a non-stationary and shared public resource.⁷⁶ Thus, although water rights may be acquired by private parties in a manner provided by state law, in most cases this does not confer ownership of the physical corpus of the water.⁷⁷ Each state sets forth the manner in which a water right may be ob-

72. The United States Supreme Court has explained that “the doctrine of prior appropriation, the prevailing law in the Western States, is itself largely a product of the compelling need for certainty in the holding and use of water rights.” *State of Arizona* 460 U.S. at 620; *see also*, *Empire Lodge Homeowners’ Ass’n v. Moyer*, 39 P.3d 1139, 1148 (Colo. 2001); *American Falls Reservoir Dist. No. 2 v. Idaho Dept. of Water Resources*, 154 P.3d 433, 438 (Idaho 2007) (holding that “[p]riority of appropriations shall give the better right as between those using the water’ of the state. IDAHO CONST. art XV, §3. ‘As between appropriators, the first in time is first in right.’ IDAHO CODE § 42-106.”).

73. *See Lux v. Haggin*, 10 P. 674, 675 (Cal. 1886); *People v. Shirokow*, 605 P.2d 859, 864 (Cal. 1980).

74. *See, e.g.*, ARK. CODE ANN. §§ 15-22-201 to -622 (2003); DEL. CODE ANN. tit. 7, §§ 6001-6031 (2001 & Supp. 2002); IOWA CODE §§ 455B.261 to .281 (1997 & Supp. 2003); KY. REV. STAT. ANN. §§ 151.010 to .600, 151.990 (Michie 2001 & Supp. 2003); MD. CODE ANN., ENVIR. §§ 5-501 to -514 (West 1996 & Supp. 2003); N.J. STAT. ANN. §§ 58:1A-1 to -17 (West 1992 & Supp. 2003); N.C. GEN. STAT. §§ 143-215.11 to .22K (2003); WIS. STAT. §§ 30.18, .28, .292 to .298, 281.35 (1998 & Supp. 2003); JOSEPH W. DELLAPENNA, *WATER AND WATER RIGHTS*, CH. 9 (Robert E. Beck ed., 1991); George W. Sherk, *Eastern Water Law: Trends in State Legislation*, 9 VA. ENVTL. L. J. 287 (1990).

75. *See supra*, notes 10 and 65; Norman K. Johnson & Charles T. DuMars, *A Survey of the Evolution of Western Water Law in Response to Changing Economic and Public Interest Demands*, 29 NAT. RESOURCES J. 347, 351 (1989) (stating that “[a]n appropriative water right, once vested, became a constitutionally protected property interest. It could be sold, leased, or transferred in other ways. It was a usufructuary right, or a right to use, and was protected as a property right.”).

76. Trelease, *supra* note 12, at 2-8.

77. *See Nestlé Waters*, 709 N.W. 2d at 221 (holding that “this state has long recognized that private persons obtain private property rights in water on the basis of their ownership of land.” The court went on to hold that “water, while a resource common to all Michigan citizens, is neither owned by the state nor subject to the public trust absent a determination that the body of water in question is navigable.”); *see also*, *Village of Tequesta*, 371 So.2d at 667; *City of Barstow v. Mojave Water Agency*, 5 P.3d 858, 860 n.7 (Cal. 2000); *Shirokow*, 605 P.2d at 864. California statutes limit property ownership to the right to use. CAL. WATER CODE § 102 (1971) (providing that “[a]ll water within the State is the property of the people of the State, but the right to the use of water may be acquired by appropriation in the manner provided by law.”). California courts have since explained that the state’s property interest in water is not an ownership

tained, and in doing so governs the circumstances (duration, manner, place and purpose) under which the holder of the right may enjoy the privilege of having secured the perennial right to use the state's water.⁷⁸

While water rights are a form of property right, no water right is absolute. Multiple water rights may attach to a given supply, and the right of any individual must be exercised with regard to the effects on other users or the environment.⁷⁹ This fundamental precept pertains to virtually all water rights throughout the United States. Whether the right is based on prior appropriation, riparianism or an administrative licensing scheme, where one right begins and another ends is dependent upon a number of considerations that originate from the property laws of the state jurisdiction.⁸⁰ Thus, while water rights constitute an interest in real property, they cannot be viewed in isolation from the rights of others in the shared resource or from public interest concerns.⁸¹

For example, states that acknowledge riparian rights may follow a natural flow,⁸² reasonable use,⁸³ modified reasonable use,⁸⁴ the Restatement (Second) of Torts⁸⁵ or a hybrid system.⁸⁶ In almost all cases, the manner in which the right may be exercised is governed by the spe-

interest, but rather a nonproprietary, regulatory one. *Riverside County*, 93 Cal. Rptr.2d at 285. The state has no right to possess and use water to the exclusion of others, and the state may only acquire water rights pursuant to the same regulatory framework applied to others. *Mojave*, 5 P.3d at 860, n.7; *Riverside County*, 93 Cal. Rptr.2d at 276; *Turlock Irrigation District v. Zanker*, 45 Cal. Rptr.3d 167, 170, n.2 (Cal. Ct. App. 2006) (holding that "water itself is not subject to ownership in California by private parties. Instead, a party can own the right to use water. That right is subject to a requirement that the use be reasonable or beneficial.").

78. See *supra*, note 74; *Village of Tequesta*, 371 So.2d at 666-67 (holding that "[w]ithout a permit Jupiter has no such property right to the use of water . . .").

79. See RESTATEMENT (SECOND) OF TORTS § 850A(b) cmt. b (1979) (determining the reasonableness of a use of water depends on consideration of multiple factors, including the "suitability of the use to the watercourse or lake," which requires balancing economic benefits of water extraction against potential environmental costs such as reduced minimum stream flows and lower pond water levels).

80. See *supra*, Parts III & IV.

81. See HUTCHINS, *supra* note 66, at 8-19.

82. See, e.g., *Collens v. New Canaan Water Co.*, 234 A.2d 825, 831 (Conn. 1967); *Hatmaker v. Gripe*, 84 P.2d 418, 419 (Okla. 1937); *Eva Morreale Hanks*, *The Law of Water in New Jersey*, 22 RUTGERS L. REV. 621, 628-29 (1968).

83. See, e.g., *Romney v. Landers*, 392 N.W.2d 415, 420 (S.D. 1986); *Bassett v. Salisbury Mfg. Co.*, 1862 WL 1466, (N.H. 1862); *Rothrauff v. Sinking Spring Water Co.*, 14 A.2d 87, 90 (Pa. 1940); *Nashville C. & St. L. Ry. v. Rickert*, 89 S.W.2d 889, 896 (Tenn. Ct. App. 1935); *Richard C. Ausness*, *Water Rights Legislation in the East: A Program for Reform*, 24 WM. & MARY L. REV. 547, 549 (1983).

84. See, e.g., *Beaunit Corp. v. Alabama Power Co.*, 370 F.Supp. 1044 (N.D. Ala. 1973); *Nestle Waters*, 709 N.W.2d at 201-02.

85. RESTATEMENT (SECOND) OF TORTS § 850A (1979); see also *Cline v. American Aggregates Corp.*, 474 N.E.2d 324, 328 (Ohio 1984); *State v. Michels Pipeline Constr., Inc.*, 217 N.W.2d 339, 350 (Wis. 1974).

86. See *Harris*, 283 S.W.2d at 133-34; *Katz v. Walkinshaw*, 74 P. 766, 771 (Cal. 1903); 78 Am. Jur. 2d Waters § 49 (2002).

cific features of the right under state law. The nuances of each state's common law or administrative overlay may influence whether water may be used for off-tract uses, transferred or enjoyed by a municipality.⁸⁷

Likewise, in prior appropriation states, an appropriative right does not confer absolute ownership or guarantee a fixed quantity of water. Rather, the appropriator is only authorized to take up the extent of his or her right, and then only if water is available after the withdrawals taken by more senior appropriators.⁸⁸ An appropriator cannot change the method, manner, place of withdrawal, or place of use if the change will result in an injury to the rights of others, or will substantially harm the environment.⁸⁹

Groundwater rights are also property rights and are generally subject to similar legal considerations as those that govern the acquisition of surface water rights and standards of use.⁹⁰ Indeed, the modern view is that groundwater rights should be managed in coordination with surface water rights.⁹¹

IV. THE PUBLIC INTEREST AND THE POLICE POWER

There is no one approach used by the states to manage water resources. Some states rely heavily upon a state administrator, such as a state engineer, department of water resources, department of ecology,

87. *See* Pyle v. Gilbert, 265 S.E.2d 584, 589 (Ga. 1980) (authorizing use of water by riparian owners on non-riparian land whether by grant or condemnation); Gillis v. Chase, 31 A. 18 (N.H. 1891); Thurston v. Portsmouth, 140 S.E.2d 678 (Va. 1965); RESTATEMENT (SECOND) OF TORTS § 855 (1979).

88. *See supra* notes 71, and 72.

89. *See* Farmers Highline Canal & Reservoir Co. v. City of Golden, 272 P.2d 629, 635 (Colo. 1954) (holding that "where it appears that the change sought to be made will result in depletion to the source of supply and result in injury to junior appropriators therefrom, the decree should contain such conditions as are proper to counteract the loss, and should be denied only in such instances as where it is impossible to impose reasonable conditions to effectuate this purpose"); *see also* Barnes v. Hussa, 39 Cal. Rptr.3d 659 (Cal. Ct. App. 2006).

90. *Cline*, 474 N.E.2d at 327-28 (Holmes, J., concurring); *Maerz*, 323 N.W.2d at 530; *Michels Pipeline*, 217 N.W.2d at 345.

91. *See, e.g.*, ALA. CODE § 9-10B-3(3) (1979); ALASKA STAT. § 46.15.030 (1980); CONN. GEN. STAT. §§ 22a-367(9), 22a-368 (1995); DEL. CODE ANN. tit. 7, §§ 6003(a)(3), (b)(4) (2000), FLA. STAT. §§ 373.019(17), 373.023(1) (2005); HAW. REV. STAT. §§ 174C-3, 174C-4(a) (1987); IOWA CODE §§ 455B.264, 455B.268(1)(a) (2004); KY. REV. STAT. ANN. § 151.150(2) (West 1966); MD. CODE ANN. ENVIR. §§ 5-101(l)(1), 5-501(a); 5-102(a) (West. 1995); MASS. GEN. LAWS ch 21G, §§ 2, 7 (2002); MINN. STAT. §§ 103G.005(17), 103G.271(1) (1997); MISS. CODE ANN. §§ 51-3-1, 51-3-5 (West 1985); N.J. STAT. ANN. § 58:1A-3(g) (West 2006); N.C. GEN. STAT. § 143-215.21(3), (5) (2007); S.D. CODIFIED LAWS, §§ 46-1-1 (1960); UTAH CODE ANN. § 73-1-1 (West. 1935). *See also* Spear T Ranch, Inc. v. Knaub, 691 N.W.2d 116; (Neb. 2005); *Nestle Waters*, 269 Mich. App. at 67-8; NATIONAL WATER COMMISSION, *supra* note 1, at 233; RESTATEMENT (SECOND) OF TORTS § 858 (1979).

etc.,⁹² to issue permits or licenses to authorize the acquisition of water. Others rely more heavily on common law principles applied by the courts to control withdrawals from water resources.⁹³ Still others decentralize water management to various local entities, including water management districts.⁹⁴ Moreover, in many states, state agencies, local agencies and courts divide, and often share, authority for water management decisions.⁹⁵

While state water laws vary and some are far more advanced than others in their comprehensive approaches, each state employs some legal methodology and venue to (a) divide limited water resources between competing water users; (b) provide for consideration of environmental water needs; and (c) ensure generally that the public interest is advanced in relation to the state's water resources.⁹⁶ Virtually all states prohibit waste and unreasonable use in one form or another.⁹⁷ Typically, the right to continued use of water is secured by compliance with state laws, including those conditions imposed upon the issuance of a license

92. See, e.g., *Maryland Aggregates Ass'n, Inc. v. State*, 655 A.2d 886, 888 (Md. 1995) (holding that "[a]ny individual, business, or governmental entity in Maryland 'which may appropriate or use any waters of the State, whether surface water or groundwater,' must first obtain a water appropriation permit from the Department of Natural Resources"); *Vineyard Land & Stock Co. v. District Court of Fourth Judicial Dist. of the State of Nevada in and for Elko*, 171 P. 166, 169 (Nev. 1918) (holding that "in Nevada the Constitution (article 6, § 1) limits the judicial authority to certain designated courts, whereas the water law undertakes to confer judicial authority upon the state engineer").

93. See, e.g., Julia R. Wilder, *The Great Lakes as a Water Resource: Questions of Ownership and Control*, 59 IND. L. REV. 463 (1984).

94. For example, the California Water Code appendix provides for several special district acts that create groundwater management districts. See, e.g., CAL. WATER CODE §§ 40-1 (Orange County Water District), 121-1 (Fox Canyon Groundwater Management Agency), 131-1 (Ojai Basin Groundwater Management Agency), and Surprise Valley Groundwater Basin Act, 137-1. Likewise, Texas has established local groundwater conservation districts to manage groundwater. TEX. WATER CODE ANN. § 36.0015 (Vernon 2001).

95. See, e.g., FLA. STAT. § 373.1961 (2006); MICH. COMP. LAWS ANN. § 324.32701 - .3278. (West 2006); *Village of Tequesta*, 371 So.2d at 665-67. In California, "[t]here are two principal state agency actors affecting water resources in California: the Department of Water Resources ('DWR') and the State Water Resources Control Board ('SWRCB'). The DWR manages the State Water Project ('SWP'), and has general statewide water planning and advisory functions. The SWRCB administers the State's appropriative surface water rights and water quality regulatory programs." Barbara T. Andrews & Sally K. Fairfax, *Groundwater and Intergovernmental Relations in the Southern San Joaquin Valley of California: What Are All These Cooks Doing to the Broth?*, 55 U. COLO. L. REV. 145, 233 (1984); see also, *supra* note 58.

96. See Bell and Johnson, *supra* note 68, at 8-10. See, e.g., Mark Tader, *Reallocating Western Water: Beneficial Use, Property, and Politics*, 1986 U. ILL. L. REV. 277 (1986).

97. See, e.g., *Elmore v. Imperial Irrigation Dist.*, 205 Cal. Rptr 438, 439 (Cal. Ct. App. 1984) (holding that "Article X, section 2 of the California Constitution requires 'the water resources of the State be put to beneficial use to the fullest extent of which they are capable, and that the waste or unreasonable use or unreasonable method of use of water be prevented'")

or permit, or arising under the common law right, such as the method and timing of withdrawals, storage, distribution, use and discharge.⁹⁸

A. Establishment and Acknowledgement of Water Rights: The Public Interest

As was noted at the outset of this article, water is a precious and valuable resource. It fuels the nation's economy, and is an essential component of our natural environment. And while water use must be sustainable, the public interest is promoted by maximizing the efficient and beneficial use of water.⁹⁹ It is important to clarify that "[w]hat is to be maximized is welfare from water use, not water use itself."¹⁰⁰ Thus, courts have found it axiomatic that an application to take water that is not bona fide - that is, one that does not demonstrate a credible intention to promptly apply water to beneficial use within the time constraints arising under applicable law—constitutes "speculation" that does not comport with the public interest.¹⁰¹ Moreover, in states with permitting or licensing systems, the issuance of a permit or license to capture and use water does not alone create a property right. Rather, only where there has been actual use in conformity with the terms of the permit or license will a water right vest as "property."¹⁰²

98. See, e.g., TEX. WATER CODE ANN. § 11.002 (Vernon 2001); Wilder, *supra* note 93. For a discussion of required procedures to obtain a water right permit in Washington State, see also Darryl V. Wareham, *Washington Water Rights Based on Actual Use or on Delivery System Capacity? Department of Ecology v. Theodoratus*, 24 SEATTLE U. L. REV. 187, 192 (2000); Virginia Houston v. Town of Waitsfield 648 A.2d 864, 866 (Vt. 1994) (applying zoning law to prohibit bottled water facility as incompatible with agricultural use designation).

99. Trelease, *supra* note 12, at 5-6. Beneficial use is the basis, measurement and limit of a water right in the prior appropriation system. See CAL. CONST. article X, § 2; N.M. CONST. art. 16 § 3; ARIZ. REV. STAT. ANN. § 45-131 (1998); NEV. REV. STAT. § 533.035; N.M. STAT. ANN. § 72-1-2 (1978); N.D. CENT. CODE § 61-01-01.2 (2005); S.D. CODIFIED LAWS § 46-1-8 (1955 & supp. 1960); WYO. STAT. § 41-3-101 (1981). For a discussion of the public interest and the police power as manifest in water allocation and water management decisions see Bell & Johnson, *supra* note 68; see also George A. Gould, *A Westerner Looks at Eastern Water Law: Reconsideration of Prior Appropriation in the East*, 25 U. ARK. LITTLE ROCK L. REV. 89 (2005), Teresa N. Lukas; *Article And Comment: When The Well Runs Dry: A Proposal for Change in The Common Law of Ground Water Rights in Massachusetts*, 32 B.C. ENVTL. AFF. L. REV. 37 (1982); Ronald B. Robie, *The Public Interest in Water Rights Administration*, 23 ROCKY MTN. MIN. L. INST. 917, 935-938 (1977).

100. Frank J. Trelease, *Policies for Water Law: Property Rights, Economic Forces, and Public Regulation*, 5 NAT. RESOURCES J. 1, 3-4 (1965).

101. See, e.g., Department of Ecology v. Theodoratus, 957 P.2d 1241 (Wash. 1998); Lake Shore Duck Club v. Lake View Duck Club, 166 P. 309, 310-11 (Utah 1917); Colorado River Water Conservation District v. Vidler Tunnel Water Co., 594 P.2d 566 (Colo. 1979); City of Thornton v. Bijou Irrigation Co., 926 P.2d 1 (Colo. 1996).

102. *Village of Tequesta*, 371 So.2d at 667; California Trout, Inc. v. State Water Resources Control Bd., 255 Cal. Rptr. 184, 199 (Cal. Ct. App. 1989) (holding that "[t]he right then vests when the water is actually diverted and placed to beneficial use."); Walsh

Moreover, the states acting through their water resource administration and state engineers possess broad discretion in evaluating applications to initiate new uses or change in existing ones.¹⁰³ In all jurisdictions, when, where, and how water is withdrawn and put to beneficial use are essential elements of the underlying property right in water that afford the state substantial control to ensure that the public interest is maximized.¹⁰⁴ In many jurisdictions, this discretion is exercised through an administrative process that is accompanied by a full review of the environmental consequences of the proposed action.¹⁰⁵ This discretion almost always includes the express or implied right to determine whether the application conforms to the public interest and to select among competing applications.¹⁰⁶ In prior appropriation states and others with an

v. Wallace, 67 P. 914, 917 (Nev. 1902) (holding “[t]o constitute a valid appropriation of water . . . there must be an actual diversion of the same, with intent to apply it to a beneficial use, followed by an application to such use in a reasonable time”); Washington Dept. of Ecology v. Grimes, 852 P.2d 1044, 1054-55 (Wash. 1993) (indicating that because a vested property right could exist only to the extent of beneficial use, limitation on water rights does not constitute a taking); Green v. Wheeler, 458 P.2d 938, 941 (Ore. 1969) (stating that a water right vests only when the statutory requirements are met and the appropriation has been perfected to the satisfaction of the State Engineer); *Virginia Houston*, 648 A.2d at 866 (finding that a proposed bottling plant did not comport with agricultural land use designation).

103. See, e.g., CAL. WATER CODE § 1253-1257 (West 1971); *Shokal*, 707 P.2d at 450; Ko’olau Agr. Co. v. Comm’n of Water Resource Mgmt., 927 P.2d 1367, 1373 (Haw. 1996) (holding “[t]he Commission’s discretion under the designation scheme is broad.”); City of San Antonio v. Texas Water Commission, 407 S.W.2d 752 (Tex. 1966); *Shirokow*, 605 P.2d at 865; *Alliance to Save the Mattaponi*, 621 S.E.2d at 92 (holding that the State Water Control Board acted within its discretion when it determined that it could not protect affected archaeological sites while, at the same time, preserve in-stream flows of the river and satisfying water supply needs of the city’s reservoir project.); Trelease, *supra* note 12, at 30; Robert H. Abram, *Water Allocation by Comprehensive Permit Systems in the Eastern United States: Considering a Move Away from Orthodoxy*, 9 VA. ENVTL. L. J. 255, 261-65 (1990).

104. See, e.g., ARIZ. REV. STAT. ANN. § 45-153(B) (1987 & supp. 1998); CAL. WATER CODE §§ 1260, 1375, 1381 (West. 1971); IDAHO CODE ANN. § 42-202 (1973 & supp. 1996); KAN. STAT. ANN. § 82a-709 (1997); see also WIEL, *supra*, note 10.

105. See *supra*, note 74.

106. See *Young & Norton v Hinderlider*, 110 P. 1045, 1049 (N.M. 1910); *Shokal*, 707 P.2d at 448 (noting that the director of water resources has an affirmative duty to assess and protect the public interest when ruling on an application for appropriation); Robie, *supra* note 99, at 935-938; Trelease, *supra* note 100; *The Milagro Beanfield War Revisited in Ensenada Land and Water Associated v. Sleeper: Public Welfare Defies Transfer of Water Rights*, 29 NAT. RESOURCES J. 861 (1989); Trelease, *supra* note 12, at 5-6 (arguing that “water law should follow and implement a wise policy of resource allocation, one that will insure the use of the resource to produce the maximum benefits for man and for society as a whole”). A Minnesota statute provides that, “The state, to the extent provided by law, shall control the appropriation and use of waters of the state.” MINN. STAT. § 103A.201. Under this statute, the state water commissioner must “contemplate the conservation, allocation and development of all the waters of the state, surface and underground, for the best interests of the people.” *Id.* at § 105.39(1). Furthermore, the commissioner shall have administration over the use, allocation and control of public waters, the establishment, maintenance and control of lake levels. *Id.* at

administrative licensing system, the extensive discretion reserved to the state has led to the prevailing view that an applicant has no property right in the success of a pending application, regardless of whether water is physically available to appropriate.¹⁰⁷

In the course of the administrative process, the state customarily provides due process to the applicant as well as other interested stakeholders.¹⁰⁸ After a consideration of the proposed application, the state can fairly evaluate a wide variety of factors, including the economic or social benefits of the proposed use, any adverse impacts of the use on other users or the environment, and impacts to the water supply of the area of origin.¹⁰⁹ Accordingly, an application can be denied, largely without legal recourse by the applicant,¹¹⁰ where there is insufficient water available to satisfy a pending request, or where the permit or license, if granted, would cause an unreasonable impact on existing water users or the environment.¹¹¹

Riparian jurisdictions also afford significant state control of water resource use. It is noteworthy that common law riparianism is rapidly giving way to regulated riparianism.¹¹² In other words, government regulation of water in the form of administrative permits systems is replacing traditional riparian rights,¹¹³ with some states adopting permit systems, while others have supplemented their common law with other types of regulation for surface water, groundwater, or both.¹¹⁴

§ 105.39(3). “The commissioner shall establish and maintain a state-wide system to gather, process and disseminate information on the availability, distribution . . . and use of waters of the state.” *Id.* at § 105.39(6); *see also*, Joseph W. Dellapenna, *Adapting Riparian Rights to the Twenty-First Century*, 106 W. VA. LAW. REV. 539, 586-87 (2004).

107. *See Village of Tequesta*, 371 So.2d at 667 (acknowledging that there is no property right in a potential use). *See e.g.*, *In re Applications A-16027 et al.*, 495 N.W.2d 23 (Neb. 1993); *In re Applications A-15145 et al.*, 433 N.W.2d 161 (Neb. 1988) (holding that a water right applicant has no property right in a mere application for water rights); *California Trout*, 255 Cal. Rptr. at 199 (holding that “[t]he right then vests when the water is actually diverted and placed to beneficial use.”); *Virginia Houston*, 648 A.2d at 866 (finding that a proposed bottling plant did not comport with agricultural land use designation and thus finding no interference with a water right).

108. *See, e.g. Goldberg v. Kelly* 397 U.S. 254 (1970); *Mathews v. Eldridge* 424 U.S. 319 (1976).

109. *See* COLO. REV. STAT. § 37-45-118(i)(b)(iv) (1989 Supp.); *supra* notes 66-68; Ronald B. Robie & Russell R. Kletzing, *Area of Origin Statutes — The California Experience*, 15 IDAHO L. REV. 419, 426-431 (1979); Dean E. Mann, *Interbasin Water Transfers: Political Institutional Analysis*, National Water Commission (Report No. NWG-SBS-72-037).

110. The administrative agency must, however, comply with due process. *See supra*, note 108.

111. *See supra*, notes 99-103.

112. *See* Dellapenna, *supra*, note 106, at 584 (explaining that regulated riparianism has replaced common law riparianism in most eastern states).

113. *See id.* Robert H. Abrams, *Replacing Riparianism in the Twenty-First Century*, 36 WAYNE L.REV. 93, 124 (1989).

114. *See* Wilder, *supra*, note 93, at 501.

Many riparian states have also established regulations to allow non-riparian use.¹¹⁵ There are now vested commissions or existing natural resource departments in riparian rights jurisdictions that possess the authority and discretion to issue certificates, permits, or licenses, or to register water withdrawals and to make allocations among water users in times of shortage.¹¹⁶

Environmental protection also plays a central role in water rights administration in virtually all states, whether through compliance with traditional public interest review,¹¹⁷ public trust responsibilities,¹¹⁸ the

115. Richard J. Moen, Bruce A. Machmeier, & John L. Sullivan, *A Proposal for Regulating Water Use in Minnesota*, 7 HAMLIN L. REV. 207, 232-34 (1984); see also, R.I. GEN. LAWS § 46-15-2 (1990 & supp. 1995); Hudson River Fisherman's Ass'n v. Williams, 531 N.Y.S.2d 379 (N.Y. App. Div. 1988). Historically, cities were granted powers to procure water supplies by special legislation. See *Adams v. Greenwich Water Co.*, 83 A.2d 177, 181-82 (1951). Currently, the power to acquire rights is granted by general statutes that are broadly applicable to municipalities. WATERS AND WATER RIGHTS § 7.05(c)(1) (Robert E. Beck ed., 2001).

116. See, e.g., FLA. STAT. § 373.1961 (1971); MICH. COMP. LAWS § 324.32701 - .32728 (West 2006); see also *Village of Tequesta*, 371 So.2d at 666-67 (holding that "[w]ithout a permit Jupiter has no such property right to the use of water beneath its land for which, upon deprivation, it must be compensated through inverse condemnation"); *Somerset v. Dighton Water Dist.*, 200 N.E.2d 237, 239 (Mass. 1964) (construing the right to appropriate water from any stream "not already appropriated and used for the purpose of public water supply."); *Syracuse v. Gibbs*, 28 N.E.2d 835 (N.Y. 1940) (holding that the city may not contest properly imposed conditions on appropriation). In Wisconsin, a person is required to obtain an individual permit to divert water from a stream. WIS. STAT. ANN. § 30.18. The Department of Natural Resources will only approve a permit if it determines that "the proposed diversion will not injure any public rights in navigable waters" and "the water to be diverted is surplus water, or if it is not surplus water, that all riparians who may be adversely affected by the diversion have consented to the proposed diversion. *Id.* The Minnesota Department of Natural Resources has the authority to issue or deny a permit to use water and may issue permits with or without conditions. MINN. STAT. §§ 103G.305, .315 (1997).

117. See, e.g., *ABKA Ltd. Partnership v. Wisconsin Dept. of Natural Resources*, 635 N.W.2d 168, 177 (Wis. Ct. App. 2001) (holding that "[s]uch public interest concerns also include maintaining the safe and healthful condition of the water, protecting spawning grounds and aquatic life, controlling the placement of structures and land uses, preserving shore cover and natural beauty, and promoting the general attractiveness and character of the community environment"); *Wisconsin v. Bleck*, 338 N.W.2d 492, 498 (Wis. 1983) (holding that rights of riparian owners are qualified, subordinate, and "subject to the public's paramount interest of the state and the paramount rights of the public in navigable waters"); *Matter of Eigenheer*, 453 N.W.2d 349, 354 (Minn. Ct. App. 1990) (holding that "[i]n 1937, the [Minnesota] legislature assigned to the Commissioner of Conservation (now the Department of Resources) the task of supervising a permit system for the use and appropriation of the state's waters, thereby conserving this valuable resource"); *Diack v. City of Portland*, 759 P.2d 1070, 1078 (Or. 1988) (holding that "[i]n determining whether the proposed use would impair or be detrimental to the public interest, the Water Resources Commission shall consider . . . The prevention of wasteful, uneconomic, impracticable or unreasonable use of the waters involved").

118. The consideration of environmental values is often expressly provided by state statute. See *supra*, note 68. The state's general public interest evaluation of new uses may be further buttressed in some jurisdictions and to different degrees by the public trust

reasonable use doctrine,¹¹⁹ or environmental stewardship. States with permitting or licensing systems commonly include specific permit or license conditions to require that the water right holder satisfy in-stream flow requirements for fish, wildlife, and other environmental purposes.¹²⁰ Further, because adaptive management is often required to address changed ecological circumstances, or an evolving understanding of the environmental impacts resulting from a specific water withdrawal, a water right may be conditioned to yield to evolving environmental considerations, including reductions in the scope, method, or timing of withdrawals to accommodate environmental objectives.¹²¹

doctrine of the specific state. *Parks*, 676 N.W.2d at 823. The public trust doctrine has traditionally been limited to public ownership of submerged land under tidal or navigable waters. See e.g., *Illinois Cent. R.R. Co. v. State of Illinois*, 146 U.S. 387, 452-53 (1892) (holding that the public trust authorized Chicago to revoke grant of fee interest in waterfront to railroad company). However, some state courts have expanded the public trust doctrine to determine whether a new water use application is in the public interest. For example, the Supreme Court of South Dakota recently examined statutes and precedent from other states when determining whether the public trust doctrine may have potential application to water resources. *Parks*, 676 N.W.2d at 823. The court concluded “that the State of South Dakota retains the right to use, control, and develop the water in these lakes as a separate asset in trust for the public. Accordingly, we align ourselves with the Idaho, Iowa, Minnesota, New Mexico, Montana, North Dakota, Oregon, Utah, and Wyoming decisions that have recognized the public trust doctrine’s applicability to water, independent of bed ownership.” *Id.* at 838. Hawaii and California appear to go further, extending the doctrine to impose a duty independent from express statutory considerations in relation to the administration of *water rights* in navigable waters. *National Audubon Society v. Superior Court*, 658 P.2d 709 (Cal. 709); *In re Water Use Permit Applications*, 9 P.3d 409, 460 (Haw. 2000). Only Hawaii has extended the doctrine in the water rights context to non-navigable waters and groundwater. Compare *In re Water Use Permit*, 9 P.3d at 409 with *Golden Feather Community Ass’n v. Thermalito Irrigation Dist.*, 257 Cal. Rptr. 836, 842 (1989).

119. See *United States v. State Water Resources Control Bd.*, 227 Cal. Rptr. 161, 187 (Cal. Ct. App. 1986) (holding that “[b]oard was authorized to modify the permit terms under its power to prevent waste or unreasonable use or methods of diversion of water. All water rights, including appropriative, are subject to the overriding constitutional limitation that water use must be reasonable”).

120. See *Nebraska Game & Parks Commission v. The 25 Corporation, Inc.*, 463 N.W.2d 591, 604 (Neb. 1990) (“Nebraska’s constitutional right to appropriate can and must be limited by the demands of the public interest”); *El Dorado Irrigation Dist. v. State Water Resources Control Bd.*, 48 Cal. Rptr.3d 468, 480 (Cal. Ct. App. 2006) (approving the permit “subject to appropriate conditions to protect the counties of [f] origin, public interest and the environment”).

121. See *Alliance to Save the Mattaponi*, 621 S.E.2d at 90-91 (including a condition in the permit that requires the City to develop a plan for monitoring salinity levels). In California, a water right, whether it predates or postdates 1914 is not exempt from reasonable regulation. See *State Water Res. Control Bd.*, 227 Cal. Rptr. at 168-69. A real property owner does not have an unfettered right to develop property in any manner he or she sees fit. See *Rutherford v. State of California*, 233 Cal. Rptr. 781, 791 (Cal. Ct. App. 1987); *People v. Murrison*, 124 Cal. Rptr.2d 68, 76-77 (Cal. Ct. App. 2002); *Allegretti & Co. v. County of Imperial*, 42 Cal. Rptr.3d. 122, 136 (Cal. Ct. App. 2006). Likewise, a water right holder cannot legitimately object to restrictions imposed upon the use of a water right granted by the state.

B. Regulation of Water Rights: The Police Power

Even after permission for the initiation of a new use has been granted by a state and a water right has been obtained and accorded fully vested status as a real property interest under state law, the right remains subject to reasonable applications of the police power.¹²² Just as landowners must comply with reasonable zoning requirements, as proper expressions of the state police power, the holder of a water right must accept reasonable regulations that ensure that water is applied to beneficial purposes under reasonable means.¹²³

In the abstract, a water right might be likened to a continuing covenant with the state whereby a water right holder enjoys the right to use a portion of a public resource but only in a manner consistent with common, prevailing or legislated standards of efficiency and reasonableness. Today a reasonable use requirement applies to all water withdrawals in most states.¹²⁴ The taking and use of water in an unreasonable manner is prohibited.¹²⁵

There are, however, legal limitations to a state's ability to retroactively adjust or alter a vested use that is largely being exercised consistent with the state water rights regime.¹²⁶ In essence, water rights reflect a

122. See *Gin Chow v. City of Santa Barbara*, 22 P.2d 5, 16 (Cal. 1933); *Hardy v. Higginson*, 849 P.2d 946, 948 (Idaho 1993) (holding that amendments to water rights permits are subject to public interest determinations); *Knight v. Grimes*, 127 N.W.2d 708, 713 (S.D. 1964).

123. Trelease, *supra* note 68.

124. See, e.g., *Imperial Irrigation Dist. v. State Water Resources Control Bd.*, 275 Cal. Rptr. 250 (Cal. Ct. App. 1990); *Girouard*, *supra* note 37.

125. See *Village of Tequesta*, 371 So.2d at 668 (stating that state courts or administrative agencies, depending upon the state regime, can restrict or enjoin a use of water that is deemed wasteful or unreasonable); *State Water Res. Control Bd.*, 227 Cal. Rptr.3d at 201-02 (holding that the California Water Board could modify permits in order to protect fish and wildlife from pollution); Trelease, *supra* note 68. In California, the state's authority to regulate water rights to protect environmental values and other public-interest goals has also been expressed as an aspect of the public trust doctrine, that is, the state may not allow the exercise of water rights to harm public trust interests. See *National Audubon Society*, 658 P.2d at 712. The California Supreme Court's reliance on the "public trust" to support environmental protection in *National Audubon Society* was largely unnecessary given the State's reserved jurisdiction to restrict existing water rights, which arises from the usufructuary character of water rights, and the reasonableness requirement imposed by the California Constitution, Article X, Section 2. See Roderick E. Walston, *The Public Trust Doctrine in the Water Rights Context: The Environmental Wrong Remedy* (1982), 22 SANTA CLARA L. REV. 63, 88-90; Clifford W. Schulz & Gregory S. Weber, *Changing Judicial Attitudes Towards Property Rights in California Water Resources: From Vested Rights to Utilitarian Reallocation*, 19 PAC. L.J. 1031, 1093-99 (1988). Moreover, in actual practice, the California State Water Resources Control Board has applied the doctrine in a manner that has e.g. not threatened vested water rights. See Gregory S. Weber, *Articulating the Public Trust: Text, Near-Text and Context*, 27 ARIZ. ST. L.J. 1155 (1995).

126. See *Colorado v. New Mexico*, 459 U.S. 176, 192 (1982) (holding that "the extent of the duty to conserve that may be placed upon the user is limited to measures that are

balancing of the concurrent public rights in water¹²⁷ and the state's administration of private rights as may be consistent with the police power.¹²⁸ Nonetheless, this limit to state authority does not detract from the underlying point that the state typically possesses considerable discretion to regulate water rights well after they have vested to ensure that they are exercised in a manner consistent with the scope of their initial creation or authorization under the organic law of the state.¹²⁹

V. NAFTA AND GATT TRADE PROTECTIONS DO NOT IMPAIR LEGITIMATE WATER MANAGEMENT LAWS AND REGULATIONS

A. Overview

The federal government long ago acquiesced in the administration of water resources by the states.¹³⁰ Over the last several decades the degree of state involvement has continuously broadened and deepened.¹³¹ As noted above, states have customarily reserved discretion in authorizing the issuance of new rights in the public interest and regulating existing water rights to obtain the desired efficiencies and protection against harm to other users and the environment. Whether states have been uniformly or even largely successful in achieving their stated objectives is a subject too vast to be addressed here.

What is relevant here is that the states' role in governing the origin of title to a water right, as an interest in real property, has important

'financially and physically feasible and 'within practicable' limits") (O'Connor, J., Concurring); *Public Utility Dist. No. 1 of Pend Oreille County*, 51 P.3d at 773 (holding that "[a] governmental abrogation of a preexisting, vested water right is an appropriation of that enhanced minimum flow to a public use and therefore is a taking encompassed in the Fifth and Fourteenth Amendments no matter how minimal the intrusion may be"); *Int'l Paper Co.* 282 U.S. 399; *Dugan*, 372 U.S. 609.

127. ; see also *Muench v. Public Service Commission*, 55 N.W.2d 40, 43 (Wis. 1952); *Riverside County*, 93 Cal. Rptr.2d at 280.

128. See *Village of Tequesta*, 371 So.2d at 666-67.

129. See *supra* note 125; Steven J. Shupe, *Waste in Western Water Law: A Blueprint for Change*, 61 OR. L. REV. 483, 521 (1982); WIEL, *supra* note 10, at 89 (stating that "[a] water right of appropriation is spoken of as a privilege, license or franchise. This franchise is conditioned on a beneficial use of water; a failure of this condition causes a loss of the right"); *Gin Chow*, 22 P.2d at 5; *People ex rel. State Water Resources Control Board v. Forni*, 126 Cal. Rptr. 851 (Cal. Ct. App. 1976). However, a utilitarian effort to reprioritize water rights masquerading as the police power may not redefine vested water rights and the court must give due regard for long-standing state water rights laws when apportioning resources. See *Mojave Water Agency*, 5 P.3d at 869-70. Certain infringements of vested water rights or water supply contracts may also result in a taking. Compare *Gerlach Live Stock*, 339 U.S. 725; *Int'l Paper Co.* 282 U.S. 399; *Tulare Lake Basin Water Storage Dist.*, 49 Fed.Cl. 31; *Romey v. Landers*, 392 N.W.2d 415, 420 (S.D. 1986); *Klamath Irrigation Dist.*, 67 Fed.Cl. 504 (2005).

130. GOULD, *supra* note 7.

131. See, e.g. Charles J. Wilkinson, *Western Water Law in Transition*, 56 U. COLO. L. REV. 317 (1985).

implications for evaluating the reach of NAFTA and GATT, and whether they have any potential to interfere with state water administration. As the foregoing discussion illustrates, a water right holder, whether public or private, possesses the right to capture and beneficially use a portion of the resource so long as it is captured and used in the manner proscribed by law and subject to the state's regulatory oversight.¹³²

These principles are relevant to my analysis in several regards. The fundamental nature of water rights as an interest in real property, rather than a good or product (i.e., personal property), excludes water rights and the laws applied to water rights by the states from the trade protections of Articles III and XI of GATT and Chapter Three of NAFTA. On their face, these trade protections only apply to trade in goods and products; they do not apply to interests in real property or the processes whereby real property rights are acquired or regulated.

As I explain *infra* in Part VI, even Chapter Eleven's investment protections, which extend to all investments—not just those made in products and goods—present very little threat to ongoing water resource administration. This is because investments in water resources are inherently conditioned upon the state's water rights management system, which typically includes a multitude of factors to promote the public interest and protect environmental values. As long as the state's water rights administration process is fairly applied, Chapter Eleven should pose no threat to water resource administration.

B. Trade Protection Provisions and Water Resources

NAFTA and GATT both prohibit the erection of trade barriers. Specifically, GATT Article XI prohibits a nation from imposing quantitative restrictions on imports or exports of products.¹³³ GATT Article III prohibits a country from subjecting imported goods to taxes or charges that are in excess of those applied to like domestic products.¹³⁴

NAFTA provides similar protections in Chapter Three.¹³⁵ Article 301's "national treatment" requires that a nation treat the other nation's competitive or substitutable goods no less favorably than the most favorable treatment accorded by that nation to its own goods.¹³⁶ The article incorporates by reference Article III of GATT relating to the national

132. *Public Utility Dist. No. 1 of Pend Oreille County*, 51 P.3d at 769-70.

133. GATT Article XI provides: "No prohibitions or restrictions other than duties, taxes, or other charges, whether made effective through quotas, import or export licenses or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party." GATT, *supra* note 36, art. XI.

134. GATT, *supra* note 36, art. III(2).

135. NAFTA, *supra* note 14, ch. III, art. 302.

136. *Id.* at art. 301.

treatment of goods.¹³⁷ Article 309 prohibits a host nation from maintaining any prohibition or restriction on the importation of any good of another nation or on the exportation or sale for export of any good destined for the territory of another nation.¹³⁸

The first axiomatic observation to an evaluation of the effect of these trade protections on water resource management is that Articles III and XI of GATT and Chapter Three of NAFTA only apply to products and goods as understood under NAFTA and GATT. Goods are defined in Article 201 of NAFTA as “domestic products as these are understood in the *General Agreement on Tariffs and Trade* or such goods as the Parties may agree.”¹³⁹ GATT does not specifically define the term “product.” However, contracting parties to GATT, who are also contracting parties to the International Convention on the Harmonized Commodity Description and Coding System, use an international coding system (HS Code) to describe products for tariff purposes.¹⁴⁰ Countries use this system as a basis for trade negotiations and to classify goods.¹⁴¹ This coding system includes product descriptions for water. It defines water as: “waters, including natural or artificial waters and aerated waters, not containing added sugar or other sweetening matter nor flavouring; ice and snow.”¹⁴² The official GATT explanatory note for this tariff heading states that it “covers ordinary natural water of all kinds (other than sea water). Moreover, ordinary natural water remains in this heading whether or not it is clarified or purified.”¹⁴³

GATT’s inclusion of “natural” water within the tariff heading on water has led some commentators to conclude that NAFTA and GATT cover all fresh water in whatever form.¹⁴⁴ Thus, some allege that if water is traded internationally in any form, protections for the trade in goods will require the continued trading of water resources, including bulk ex-

137. *Id.*

138. *Id.* at art. 309.

139. *Id.* at ch. 2, art. 201 (emphasis in original).

140. ANWARUL HODA, *TARIFF NEGOTIATIONS AND RENEGOTIATIONS UNDER THE GATT AND THE WTO: PROCEDURES AND PRACTICES* 270 (Cambridge 2001). The Harmonized Commodity Description and Coding System (HS) of tariff nomenclature is developed and maintained by the World Customs Organization. *Id.*

141. *Id.*

142. Universal Postal Union, Harmonized Commodity Description and Coding System Code § 22.01, available at www.upu.int (accessed from homepage by searching for “Harmonized Commodity Description” and selecting “Country List”) (last visited Nov. 2, 2007).

143. Although the HS coding system defines water as “ordinary natural water of all kinds,” an explanatory note says that the heading extends to “water whether or not it is clarified or purified.” The reference to “clarification or purification” suggests a human process that occurs after the water is captured and separated from its natural state. Thus, this illustrates that the focus of the tariff heading is natural water (purified or not) that has been separated from its natural state (i.e., water in a product form, as personal property, not as real property).

144. Boyd, *supra* note 5, at 334.

ports, even if the trade in water is damaging to the environment.¹⁴⁵ As I explain *infra* in Part V(C), these concerns are misplaced because they derive from a fundamental misunderstanding of (a) the nature of water rights within the United States as interests in real property; and (b) the state regulations that governs the acquisition and use of water rights.

Other commentators have explained that NAFTA and GATT do not apply to water resources while in their natural state largely based upon (a) the intentions of the approving nations; (b) interpretations of the terms “good” and “product” as used in NAFTA and GATT respectively to not cover water within its natural state, and (c) the understanding that the specific treatment accorded to harvesting natural resources should be applicable to water.¹⁴⁶ While I largely agree with these commentators, my focus is on the more fundamental questions arising from the law of property in the context of water rights. Specifically, I emphasize the character of water rights as an interest in real property, and the dominant role of the states in acknowledging and authorizing title to water rights and subsequently regulating water rights and water resources through the state’s police power.

C. NAFTA and GATT Do Not Apply to Water Within its Natural State

Neither GATT nor NAFTA’s trade protections apply to water rights or other interests in real property because GATT’s Articles III and XI and NAFTA’s Chapter Three are limited to “goods” and “products.” Water rights are not goods or products; they are interests in real property,¹⁴⁷ regardless of whether the jurisdiction treats the right as appurtenant, non-appurtenant or part and parcel of the land.¹⁴⁸ Likewise, the

145. See Girouard, *supra* note 37.

146. See Scott Philip Little, *Canada’s Capacity to Control the Flow: Water Export and the North American Free Trade Agreement*, 8 PACE INT’L L. REV. 127, 139-44 (1996); see also JON R. JOHNSON, *THE NORTH AMERICAN FREE TRADE AGREEMENT: A COMPREHENSIVE GUIDE* 109 (Canada Law Book Inc. 1995) (stating that “[t]he key to determining the scope of [the NAFTA and GATT] provisions is the use of the word ‘product.’ As the GATT does not define ‘product,’ the meaning of this word is its ordinary meaning, which is ‘something that is produced.’ For a thing to be produced, something must be done to it. It must be extracted, harvested, collected, stored, graded, transported, refined, processed, assembled, packaged, or somehow transformed into an article of commerce. Unexploited resources such as oil or gas in the ground or water in lakes, rivers or aquifers are not ‘products’ and therefore are not subject to these or any other NAFTA provisions”); Boyd, *supra* note 5, at 334.

147. See *supra* note 38.

148. Water in its natural state, whether in streams, lakes, or ponds, or percolating through the soil, is part of the land, and therefore real property. See *King*, 499 P.2d at 588 (Wyo. 1972) (holding that “[a] water right is a ‘property right of high order,’ with ‘none of the characteristics of personal property,’ and it is real property”); *Stanislaus Water*, 93 P. at 862; *Smith v. Mun. Court*, 245 Cal. Rptr. 300 (Cal. Ct. App. 1988) (holding that water does not become personal property or a “product” until it is severed from the property); *Copeland v. Fairview Land Etc. Co.*, 131 P. 119, 121 (Cal. 1913);

administration of water rights in each state is an application of the police power over a real property interest, analogous to numerous other police power regulations of real property, such as property-related laws concerning zoning, building permits, nuisance avoidance, endangered species, wetland protection, toxic substances, pollution, and so on.¹⁴⁹

Nothing in NAFTA or GATT purports to preempt, modify or affect traditional notions of real property. Moreover, there appears to be no arbitration decision that has imposed such a far-reaching conclusion. Such a result would require a quantum leap from existing United States jurisprudence and deviate substantially from the focus of these trade protection laws—that being the uninhibited trade in goods or products. Nowhere has it been logically maintained that these laws create exceptions to domestic laws that govern real property interests. Such an absurd premise would impair the power of local governments to enact zoning and other land use measures, as well as the ability of the Bureau of Land Management and the U.S. Forest Service to administer licenses for grazing, mineral extractions, timber harvesting and the like on public lands, and would result in a myriad of other outlandish detriments to the public welfare.

Similarly, application of Chapter Three of NAFTA and Articles III and XI of GATT to state laws regulating the exercise of rights to use water resources would frustrate water resource management. For these reasons, I conclude that this proposition is uncontestable: NAFTA and GATT's trade laws do not apply to a state's administration of the acquisition and use of the state's water resources.

The implications of this conclusion are that a state may regulate the withdrawal and use of water, free from liability from the trade protections set forth in NAFTA and GATT. Fears that NAFTA and GATT will "open the floodgate"—that allowing any water to be captured and placed into commerce will cause governments to lose the ability to control water removals—are fundamentally misplaced.

Through its law and regulation, the state ensures that the water is captured, conveyed, stored, and used consistent with state policy, and can condition the future right to use as needed to protect the public interest,¹⁵⁰ within constitutional limitations. The fact that the state allowed

Murphy v. Kerr, 296 F. 536, 546 (D.N.M. 1923); Skinner v. Jordan Valley Irrigation Dist., 300 P. 499, 501 (Or. 1931); Edinburg Irrigation. Co. v. Paschen, 235 S.W. 1088, 1090 (Tex. Comm'n. App. 1922).

149. See, e.g. Meg Stevenson, *Aesthetic Regulations: A History*, 35 REAL. EST. L. J. 519 (2007) (discussing building and construction regulations); American Law Institute, *The Condemnation Landscape Across the Country Post-Kelo*, SM006 A.L.I.-A.B.A. 433 (2007) (discussing zoning regulation under the police power); Richard A. Epstein, *How to Create—Or Destroy—Wealth in Real Property*, 58 ALA. L. REV. 741, 761 (2007) (discussing use of police power to regulate real property to protect environmental concerns).

150. See, e.g., Heldermon v. Wright, 152 P.3d 855 (Okla. 2006); Delta Wetlands Props. v. County of San Joaquin, 15 Cal. Rptr.3d 672 (Cal. Ct. App. 2004); Parks v.

withdrawals and use by one user from a specific water body for a particular use does not obligate the state under NAFTA or GATT to allow any other withdrawals.¹⁵¹ As noted above, in prior appropriation states and other permitting or licensing systems, the prevailing view is that an applicant has no property right in the success of a pending application. Further, as discussed, the state is generally free, under any type of water rights regime, to impose conditions and qualifications upon the right to future use to accommodate changed circumstances and to ensure that the public interest in the use of the state's water is maintained.¹⁵² Again, NAFTA and GATT trade protections have no application to restrict or limit the actions taken by the states in this regard because water rights are an interest in real property that fall outside of protections for trade in goods and products set forth in these treaties.

There is a critical distinction between regulation of usufructuary water rights and regulation of goods and products created with water. The latter unquestionably falls within NAFTA and GATT's respective protections for trade in goods and prohibition of trade barriers. For example, a regulation that banned or restricted imports or exports of particular products simply because the product was manufactured with water (whether it be fruits and vegetables, bottled water or other beverage, fuel or chemicals, or any other product containing water) would undoubtedly fall within the direct coverage of the protections afforded by Chapter Three of NAFTA and Articles III and XI of GATT. Such a regulation would violate these trade protections unless an exception is afforded by GATT's Article XX or NAFTA's Article 2101, discussed *infra*.

There is also a concern alleged by some that the export of bottled water is equivalent to countenancing bulk export of water (e.g., by pipeline or tanker).¹⁵³ However, this concern is rooted in the confusion over the difference between the state's power to manage its water resources, and its power to regulate trade in a product that is generated through the beneficial use of a water right.

Although the states may differ on the point at which they may declare water has become sufficiently separated from the natural source that it ceases to be realty, and instead becomes personal property, all states hold that water rights are interests in real property, and they remain

Cooper, 676 N.W.2d 823 (S.D. 2004); *Chatfield East Well Co., Ltd. v. Chatfield E. Prop. Owners Ass'n*, 956 P.2d 1260 (Colo. 1998); *In re Hitchcock and Red Willow Irrigation Dist.*, 410 N.W.2d 101 (Neb. 1987).

151. See *Temescal Water Company v. Dept. of Public Works*, 280 P.2d 1 (Cal. 1955); *United States v. State Water Res. Control Bd.*, 227 Cal. Rptr. at 169; *City of Albuquerque v. Reynolds*, 379 P.2d 73 (N.M. 1963); *Beach v. Superior Ct.*, 173 P.2d 79 (Ariz. 1946); *Anita Ditch Co. v. Turner*, 389 P.2d 1018 (Wyo. 1964).

152. See *infra* Part IV.

153. See *supra* note 8.

subject to state administration and police power-based regulation.¹⁵⁴ Therefore, the state's authority to control the activity is at its zenith when it manages and regulates the water right under which a person or entity may subsequently reduce the water to possession and apply it to a beneficial use.¹⁵⁵

Moreover, there is no legal authority to support a characterization of commerce in bottled water as an "export" of water. To be sure, bottled water, like water delivered to a customer's tap by a municipality,¹⁵⁶ is a product.¹⁵⁷ Therefore, the bottled water market is simply commerce in one type of product produced with, and containing water. Like other beverages, the water is beneficially used at the moment of the product's creation at the bottling plant. Its place of use is not determined by where it is consumed or its quantity measured by the quantity actually ingested.

Likewise, distribution of bottled water cannot be characterized as a "diversion" of water. A "diversion" has been consistently defined among the states as the removal of water from its natural channel to transport it through pipes, conduits, ditches or canals.¹⁵⁸ In the case of bottled water, the use occurs at the time the water is separated from the natural water source prior to the water ever being processed through the bottling plant, just as occurs when water is extracted for use in making beer, soft drinks, or any other water-laden product. The subsequent shipment of bottled water in a national (or international) market is no more a "diversion" than the shipment of any other of these beverages and products.

In states where the right to make a beneficial manufacturing use arises from common law, the state may regulate the right in accordance with the police power. Typically this means ensuring that the withdrawal of water from the natural water course or groundwater basin does not injure the environment or other users.¹⁵⁹ In states maintaining a licensing or permitting system, the state retains all of its public interest authority as

154. See *supra* notes 10, 58, 74, and 75.

155. See *supra* Part IV.

156. See, e.g., *McKeesport*, 690 A.2d 766; *Miller*, 55 A.2d at 790; *Mulberry-Fairplains*, 412 S.E.2d at 915; *Sternberg*, 155 A.2d at 689; *Coast Laundry, Inc. v. Lincoln City* 497 P.2d 1224 (Or. 1972); *Zepp, v. Mayor & Council of Athens* 348 S.E.2d 673 (Ga. 1986) (holding that water distributed to customers is a good within the meaning of the Uniform Commercial Code).

157. See discussion, *supra* note 9.

158. N.Y. ENVTL. CONSERV. LAW § 15-1505 (McKinney 1973 & supp. 1983-1984); Cynthia L. Koehler, *Water Rights and the Public Trust Doctrine: Resolution of the Mono Lake Controversy*, 22 ECOLOGY L. Q. 541 (1995); Wilder, *supra* note 93 at 501; *United States v. State Water Res. Control Bd.* 227 Cal. Rptr. at 170; BLACK'S LAW DICTIONARY (5th ed.); ARIZONA REV. STAT. § 37-1101 (1994); ALASKA STAT. ANN. § 46.15.260 (1996).

159. See *supra* notes 93, 98, and 111.

to whether to grant a license or permit to make beneficial use of the supply for the designated manufacturing purpose.¹⁶⁰

A case can certainly be made that bulk export of water by tanker is sufficiently similar to a pipe or conduit that it can be construed as a diversion and a means of conveyance rather than a product, as the water held in the tanker has not yet been applied to any specific beneficial use. The tanker in such case is part of the process of removal. If the bulk export by tanker is indeed the functional equivalent of diversion by pipeline or conduit, the state is fully vested with the power to regulate the method of conveyance as an appurtenance to the water right.¹⁶¹

I accept that drawing the line between products (e.g., bottled water) and means of diversion and conveyance (e.g., water in a tanker) may

160. *See supra* Part IV.

161. The method of withdrawal and conveyance is part of the water right owner's bundle of property rights and will support legal action to redress unreasonable interference. *See, e.g.,* McNamara v. City of Rittman, 838 N.E.2d 640, 645 (Ohio 2005); United States v. Orr Water Ditch Co., 256 F.3d 935, 942 (9th Cir. 2001); Parker v. Wallentine, 650 P.2d 648, 654 (Idaho 1982); State Ex Rel. Crowley v. Dist. Court, 88 P.2d 23, 29-30 (Mont. 1939); Current Creek Irrigation Co. v. Andrews, 344 P.2d 528, 531 (Utah 1959); Colorado Springs v. Bender, 366 P.2d 552, 556 (Colo. 1961); *see also* Prather v. Eisenmann, 261 N.W.2d 766, 771-72 (Neb. 1978); MacArtor v. Graylyn Crest III Swim Club, 187 A.2d 417, 420 (Del. Ch. 1963). The owner's property right encompasses the right to divert, withdraw, and convey water under reasonably efficient means without undue waste. *See, e.g.,* Doherty v. Pratt, 124 P. 574, 576 (Nev. 1912); Warner Valley Stock Co. v. Lynch, 336 P.2d 884, 890 (Or. 1959); *Erickson v. Queen Valley Ranch Co.*, 99 Cal. Rptr. 446, 449-50 (Cal. Ct. App. 1971). The state plays several prominent roles in ensuring that the methods of diversion, withdrawal, and conveyance remain reasonably efficient and not wasteful. First, the state may approve the means of diversion/withdrawal and conveyance in the granting of the water right and in authorizing changes to existing uses to ensure that proposed methods are reasonable. *See, e.g.,* ARIZ. REV. STAT. § 45-152(A)(4) (2005) (requiring every permit for an application to appropriate water to describe the location, point of diversion and description of the proposed works by which the water is to be put to beneficial use); CAL. WATER CODE ANN. § 1260(d) (West 2006) (requiring every application for a permit to appropriate water to include the location and description of the proposed headworks, ditch canal, and other works); IDAHO CODE ANN. § 42-202(1)(d) (West. 2005) (requiring an application to appropriate water to include a description of the proposed ditch, channel, well or other work); KANSAS STAT. ANN. § 82a-709(d) (West. 2005) (requiring all applications to appropriate water to describe the location of the works or proposed works for the diversion and use of the water); MD. CODE ANN. ENVIR. § 5-507(b)(1) (West 2007) (reserving to the state the power to impose any condition, term, or reservation concerning the character, amount, means, and manner of the appropriation of water); MONTANA CODE ANN. § 85-2-311(1)(c) (West. 2005) (requiring applications to appropriate water to specify the proposed means of diversion, construction, and operation of the appropriation works are adequate). Second, the state may act pursuant to its reserved police power to ensure that the water right holder continues to divert/withdraw and convey water for a beneficial use with reasonable efficiency in accordance with the custom, standards, and habit prevailing among similarly situated users exercising best management practices. *See, e.g.,* CAL. CONST. Art. 10 § 2; CAL. WATER CODE § 275; *Am. Falls Reservoir Dist. v. Idaho Department of Water Resources* 154 P.3d at 447; *Imperial Irrigation Dist.*, 237 Cal. Rptr. 283, 288; *Imperial Irrigation Dist.* 275 Cal. Rptr. at 258; *In re Water Rights of Escalante Val. Drainage Area*, 348 P.2d 679, 682 (Utah 1960).

not necessarily be easy. However, this determination is unrelated to the state's undiminished authority to regulate the water right, including the method of diversion, up until the moment a product is created.¹⁶² The state's authority to grant permission to use water and to regulate its use as a right in real property is as strong after the NAFTA and GATT as it ever was.

D. State Proclamations and Assertions

The foregoing conclusion—that water rights are not subject to NAFTA and GATT—is also supported by the joint statement issued by Canada, the United States, and Mexico in 1993, a year prior to the adoption of NAFTA. The statement provides:

*Unless water, in any form, has entered into commerce and becomes a good or product, it is not covered by the provisions of any trade agreement, including the NAFTA. And nothing in the NAFTA would oblige any NAFTA Party to either exploit its water for commercial use, or to begin exporting water in any form. Water in its natural state in lakes, rivers, reservoirs, aquifers, water basins and the like is not a good or product, is not traded, and therefore is not and never has been subject to the terms of any trade agreement.*¹⁶³

The joint statement is just one of multiple assertions by the NAFTA signatory parties that water within its natural state is not a good covered by NAFTA. Canada, in particular, has repeatedly and continually stated as much both before and after NAFTA's execution, in large part as a response to domestic concern that NAFTA will force large scale bulk export of water from Canada to the United States. These repeated assertions are well reported in an article prepared for the Canadian Depository Service Program, Law and Government Division, by David Johansen.¹⁶⁴

162. See *supra* Part IV. There is no property right in a future use of water. *Hollister Park Investment Co. v. Goleta Water Dist.*, 147 Cal. Rptr. 91 (Cal. Ct. App. 1978); *Bank of America Nat'l Trust & Savings Ass'n v. Summerland County Water District*, 767 F.2d 544 (9th Cir. 1985); *Lockary v. Kayfetz* 908 F.2d 543 (9th Cir. 1990).

163. Joint Statement by the Governments of Canada, Mexico and the United States Concerning NAFTA and Water (1993) [hereinafter Joint Statement] (emphasis added) Government of Canada, Office of the Prime Minister, Prime Minister Announces NAFTA Improvements; Canada To Proceed With Agreement (Dec. 2, 1993).

164. David Johansen, *Water Exports and the NAFTA*, Law and Government Division, available at <http://dsp-psd.pwgsc.gc.ca> (accessed from homepage by selecting "English" then searching for "Water Exports" and selecting "Water Exports and the NAFTA (PRB 99-5E)") (last visited Nov. 2, 2007). Instances in addition to the Joint Statement in which the Canadian government or Canadian officials have made these assertions, as reported by Mr. Johnson's article, include:

E. Resource Exceptions within NAFTA and GATT Likely Also Allow for Water Resource Management Laws and Regulations

In addition to the fact that NAFTA and GATT do not apply to laws governing water rights because they are an interest in real property, NAFTA and GATT include exceptions to their respective prohibitions on trade restrictions for laws relating to health and safety measures and exhaustible natural resources. These exceptions provide independent and powerful support for the conclusion that NAFTA's and GATT's trade

1) *The NAFTA Manual*, issued by the Canadian federal government in 1992 before NAFTA's adoption, which states that "Like the Canada-U.S. Free Trade Agreement (FTA), the NAFTA does not apply to large scale exports of water. As in the FTA, only water packaged as a beverage or in tanks is covered in the NAFTA. Water was not discussed during the NAFTA negotiations with the United States and Mexico. Large-scale exports of water, either by inter-basin transfer or diversion, are contrary to the 1987 federal water policy. THE NAFTA WILL NOT AFFECT WATER EXPORTS. Canada's legislation to implement the FTA already states clearly that the FTA does not apply to water, except in the case of water packaged as a beverage or in tanks. Similar provisions will be included in the NAFTA implementing legislation. There never has been, nor will there be, any negotiation or provision for large-scale exports of water to another country." *Id.*

2) Appearance in 1993 before the House of Commons Legislative Committee on Bill C-115 (NAFTA implementation) by Mr. Konrad von Finkenstein, then the Assistant Deputy Attorney General, Department of Justice (stating that "if you trade water in its natural state you put in tanks, or bottles, or something and sell me fresh water that you've taken out of a well or something like that, then you are indeed trading in water and it's then a good and is covered by the GATT, by the FTA, or by the NAFTA. But that's a good you're trading . . . Water is no different from any other resource. Take a forest, for instance. There's nothing in the NAFTA, the FTA, or the GATT that forces us to cut our trees down, etc. . . . And the same applies with water, you don't have to trade or anything with it"). *Id.*

3) Canada's *North American Free Trade Agreement Implementation Act*. It provides at Section 7(1) that "[f]or greater certainty, nothing in this Act or the Agreement, except Article 302 of the Agreement, applies to water." Section 7(2) states, "In this section, 'water' means natural surface and ground water in liquid, gaseous or solid state, but does not include water packaged as a beverage or in tanks." *Id.*

4) Editorial response by the Canadian Trade Minister on May 2, 1993 within the *Victoria Times-Colonist* to an earlier editorial claiming that water will be treated as a "good," subject to the same rules as the other "goods and services" under the FTA and the NAFTA. The Trade Minister's rebuttal stated, "Water in its natural state is not covered by the NAFTA, the FTA, the GATT, or any other trade agreement. Lakes, rivers, or aquifers are simply not goods or products, any more than are the fish swimming in them or the oil and gas trapped under them. Trade agreements only cover water as a 'good,' that is, only when water has entered into commerce as a product. . . There is absolutely nothing in the NAFTA or any other trade agreement that forces Canada to either exploit its water for commercial use, or to export its water. . . The bottom line is that Canadian governments, both now and under the NAFTA, have the freedom of action required to regulate the exploitation of our water resources. And until it is exploited and entered into commerce as a good, water is not covered by the NAFTA or any other trade agreement." *Id.*

protections do not impair water rights administration.¹⁶⁵ Importantly, these exceptions may also exempt other laws that manage water resources, which fall outside of water rights administration, such as laws applicable to drought-period allocations of water already in the possession of a water purveyor.¹⁶⁶

Article XX of GATT sets forth exceptions to GATT's trade protections for certain environmental regulations. Subsection (b) establishes an exception for regulation "necessary to protect human, animal and/or plant life or health."¹⁶⁷ Subsection (g) creates an exception for regulation "relating to the conservation of exhaustible natural resources, if such measures are made effective in conjunction with restrictions on domestic production or consumption."¹⁶⁸ A third provision, subsection (j), excepts

165. These exceptions are not necessary to reach this conclusion because NAFTA's and GATT's trade protections do not apply to water rights administration. *See* discussion, *supra* Part V(B).

166. *See, e.g.*, CAL. WATER CODE §§ 350-359, 71640-71644 (West 2007); CONN. GEN. STAT. ANN. §§ 25-32 (West 2007); DEL. CODE ANN. tit. 20, §§ 3132-3133 (1985); FLA. STAT. ANN. § 373.175 (2007); HAW. REV. STAT. § 174C-62 (2007); MASS. ANN. LAWS ch. 21G, §§ 15-17 (2007); NEV. REV. STAT. ANN. § 416.060 (2007); OR. REV. STAT. §§ 536.700-.780 (1989); TENN. CODE ANN. § 68-13-705(10) (West 2007); WASH. REV. CODE ANN. §§ 43.83B.400-.83B.425.

167. (West 2007); GATT, *supra* note 36, at art. XX(b) (stating that nothing in the Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures "necessary to protect human, animal or plant life or health") (emphasis added).

168. GATT, *supra* note 36, at art. XX(g) (stating that nothing in the Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures "relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption"). Article XX(g) of GATT has recently been interpreted by the WTO Appellate Body in the Shrimp-Turtle case, in which the Appellate Body examined whether the United States' restriction on shrimp, which was enacted to protect sea turtles, was allowed under the "conservation exceptions." Appellate Body Report, *United States — Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, VII 2755 (Oct. 12, 1998). Here, the Appellate Body employed a two-step analysis to answer this question: (1) Whether the regulation related to the "conservation of exhaustible natural resources;" and (2) whether the measure was arbitrary or constituted unjustifiable discrimination. *Id.* Though the first part of the test was answered in the affirmative, the Appellate Body held that the measure was arbitrary because it was applied inconsistently to countries that had similar policies as the United States. *Id.* at ¶ 177. In addition, the Body held that instead of attempting to protect the species via international agreement, the U.S. instead imposed a unilateral blanket import prohibition. *Id.* at ¶ 169-72. In response to this decision, the United States revised its regulation to allow imports of shrimp from countries that had comparable harvesting methods that effectively protected sea turtles. Revised Guidelines for the Implementation of Section 609 of Public Law 101-162 Relating to the Protection of Sea Turtles in Shrimp Trawl Fishing Operations, 64 Red. Reg. 130, 36946 (July 8, 1999). Further, the United States attempted to negotiate a multilateral agreement to protect sea turtles. World Trade Organization, *United States — Import Prohibition of Certain Shrimp and Shrimp Products, Recourse to Art. 21.5 of the DSU by Malaysia*, ¶ 31-32, WT/DS58/AB/RW (Oct. 22, 2001). In turn, the Appellate Body held that these new measures were allowable under the conservation exception and were not arbitrary. *Id.* at ¶ 134, 152. The Shrimp-Turtle case is instructive in that it suggests that regulations

measures “essential to the acquisition or distribution of products in general or local short supply.”¹⁶⁹

States and local governments have a rich history of applying the police power to regulate the use and distribution of water during shortages and to ensure health and safety.¹⁷⁰ Perhaps there is no better example of the state’s paramount authority to regulate water as a commodity than in the area of drought or supply shortages.¹⁷¹ There are legions of cases sustaining governmental authority to restrict the deliveries of water during drought or other conditions that are required for public health, safety and welfare.¹⁷² Accordingly, to the extent a state or municipality sought not to regulate the withdrawal of water from its natural source, but rather to focus its attention on the downstream distribution of the water to protect human safety or the environment, such an action is relatively routine under state law and expressly contemplated as an exception from GATT set forth in Article XX, subsection (j) - measures relating to products in general or local short supply.

Moreover, the same police power-based regulation referenced in Part IV above as a feature of water rights administration is a further exception from the coverage of GATT as a legitimate health and safety matter, set forth in GATT Article XX, subsection (b). The states’ interest in promoting sustainable use and sustainable development has already prompted legislation throughout the states to place conditions on the

that are narrowly focused on a conservation objective and do not simply restrict all exports, but instead regulate in a fair and even-handed manner, will be upheld.

169. GATT, *supra* note 36, at art. XX(j) (stating that nothing in the Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures “essential to the acquisition or distribution of products in general or local short supply; Provided that any such measures shall be consistent with the principle that all contracting parties are entitled to an equitable share of the international supply of such products, and that any such measures, which are inconsistent with the other provisions of this Agreement shall be discontinued as soon as the conditions giving rise to them have ceased to exist”).

170. *See infra* note 172.

171. *See infra* note 172.

172. *See, e.g.,* Barshop v. Medina County Underground Water Conservation, 925 S.W.2d 618, 635 (Tex. 1996); Matter of Water Supply Critical Area No. 2,558 A.2d 1321, 1324 (N.J. Super. Ct. App. Div. 1989); City of Golden v. Simpson, 83 P.3d 87, 92 (Colo. 2004); Gilbert v. State of California, 266 Cal. Rptr. 891, 896 (Cal. Ct. App 1990); Butte County Water Users’ Ass’n v. R.R. Comm’n of Cal., 196 P. 265, 269-70 (Cal. 1921) (holding that there is authority to restrict access when supplies are limited in order to ensure that there is enough water to serve existing users); San Diego County Water Auth. v. Metro. Water, 11 Cal. Rptr.3d 446, 457-58 (Cal. Ct. App. 2004). Additionally, many states grant water providers express statutory authority to curtail service when there is a bona fide water shortage. *See* Janet C. Neuman, *Drought Proofing Water Law*, 7 U. DENV. WATER L. REV. 92, 100-02 (2003). *See also* Henderson Co. v. Thompson, 300 U.S. 258, 266 (1937) (stating that police power regulations dealing with physical things such as land or natural resources could have incidental effects on contracts if the power was exercised in the interest of the public welfare).

withdrawal of water, promote conservation and create efficiencies.¹⁷³ Thus, evenly applied police power regulation as described in Article XX subsection (b)—regulation to protect human, animal and or plant life or health—is expressly exempt from GATT’s coverage regardless of whether it affects real property rights or goods.¹⁷⁴

Some have debated whether water resources meet the definition of “exhaustible natural resources” to qualify for yet another exception pursuant to Article XX subsection (g)—conservation of exhaustible natural resources. The resolution of this question turns on whether water resources are considered as “exhaustible” or are “renewable.”¹⁷⁵

Unfortunately, there is no clear-cut answer. By their nature, water resources may be considered renewable. But water in its various forms and at specific locations may not be. Fresh water supplies are in a condition of increasing scarcity world wide.¹⁷⁶ Indeed, water rights laws, at their core, are frequently focused upon allocating supplies among water users during conditions of scarcity. Moreover, some courts have held that a non-sustainable use is akin to use of a non-renewable resource.¹⁷⁷ Large volumes of groundwater within the United States are indeed completely non-renewable and are being mined to exhaustion.¹⁷⁸ Although this exception is hardly required to find that NAFTA and GATT place few constraints on state resource management, it is yet another basis to support the conclusion.

NAFTA selectively incorporates GATT’s Article XX provisions to except resource-based laws from many of NAFTA trade protection provisions, including Chapter Two (trade in goods) and Chapter Three (trade barriers), provided that those laws are non-discriminatory.¹⁷⁹ However, NAFTA does not incorporate GATT’s Article XX exceptions in relation to several of NAFTA’s investor protection provisions set forth in Chapter Eleven. I will address the lack of extension of these exceptions to the Chapter Eleven provision in Part VI *infra*.

173. See *supra* note 68.

174. GATT, *supra* note 36, at art. XX(b).

175. *Id.* at art. XX(g). For an interpretation of the terms “exhaustible” and “renewable” under GATT, see J. Patrick Kelly, *The Seduction of the Appellate Body: Shrimp/Sea Turtle I and II and the Proper Role of States in WTO Governance*, 38 CORNELL INT’L L.J. 459, 477-82 (2005).

176. See Jane M. Cohen, *Of Water Banks, Piggybanks, and Bankruptcy: Changing Directions in Water Law*, 83 TEX. L.REV. 1809, 1823 (2005); Glennon, *supra* note 161, at 1873.

177. See, e.g. Trelease, *supra* note 12.

178. WILLIAM ASHWORTH, *NOR ANY DROP TO DRINK* 1-3 (Summit Books 1982).

179. NAFTA, *supra* note 14, at art. 2101. The law may not be “applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade.” GATT, *supra* note 36, at art. XX. Thus, like the U.S.’s dormant commerce clause, the exceptions cannot be used as a façade for purely protectionist measures. For example, conditions on the export of an exhaustible resource can only be imposed if there is a similar restriction imposed on production of that resource domestically.

VI. CHAPTER ELEVEN'S INVESTMENT PROTECTIONS DO NOT CREATE LIABILITY IN RELATION TO LEGITIMATE LAWS AND REGULATIONS TO PROTECT WATER RESOURCES

Chapter Eleven of NAFTA defines the treatment that a host nation must extend to investors and investments from other NAFTA nations.¹⁸⁰ Unlike Chapter Three, which does not apply to water resource management laws for the reasons discussed *supra*, Chapter Eleven does apply in the context of domestic water laws because it protects foreign investments.¹⁸¹ There are three primary provisions by which Chapter Eleven requires NAFTA governments (and their political subdivisions) to protect foreign investors: National Treatment (Article 1102), Minimum Standard of Treatment (Article 1105), and Expropriation and Compensation (Article 1110), each of which is discussed *infra*. Chapter Eleven also allows the foreign investor itself, not just its nation state, to bring a claim for damages against the host nation.¹⁸²

180. NAFTA, *supra* note 14, at art. 1102 (providing that “[e]ach Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments”).

181. NAFTA defines the term “investment” quite broadly to include enterprise and real estate or other property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes. NAFTA, *supra* note 14, at art. 1139. NAFTA tribunal decisions have expanded the definition to include access to markets. See *Pope & Talbot, Inc v. Canada*, ¶ 96 (2001) [hereinafter *Pope & Talbot I*], available at <http://www.appletonlaw.com> (accessed from homepage by selecting “Cases”, then “Pope & Talbot v. Canada” then “Page 2” then “Interim Award by Arbitral Tribunal – June 26, 2000”) (last visited Nov. 2, 2007) (holding that claimant’s access to the U.S. lumber market is a property interest subject to protection under Article 1110); but see *Methanex I*, *supra* note 24 (holding that market share constitutes an element of the value of the enterprise, but not an independent property interest).

182. See NAFTA, *supra* note 14, at arts. 1116-17. Complaints brought under Chapter Eleven are resolved by arbitration, based on the arbitration rules of the United Nations Commission on International Trade Law (UNCITRAL) and the International Center for the Settlement of Investment Disputes (ICSID). *Id.* Of note, decisions reached by a NAFTA arbitration tribunal have no precedential effect on future tribunals, although the tribunals do look to the reasoning within prior awards. NAFTA, *supra*, note 14, at art. 1136(1) (providing that, “[a]n award made by a Tribunal shall have no binding force except between the disputing parties and in respect of the particular case”); see also Kenneth J. Pippin, *An Examination of the Developments in Chapter 19 Antidumping Decisions under the North American Free Trade Agreement (NAFTA): The Implications and Suggestions for Reform for the Next Century Based on the Experience of NAFTA after the First Five Years*, 21 MICH. J. INT’L L. 101, 117 (1999) (explaining that despite the lack of binding precedential authority, NAFTA panels often cite prior decisions when ruling on a case). Should the complainant succeed, the federal government of the host nation is liable for all awarded damages even if it is a state or local law that has caused the actionable expropriation NAFTA, *supra*, note 14, at art. 105; see also Ari Afilalo, *Towards a Common Law of International Investment: How NAFTA Chapter 11 Panels Should Solve Their Legitimacy Crisis*, 17 GEO. INT’L ENVTL. L. REV. 51, 62 (2004).

Chapter Eleven's investor and investment protections are excluded from Article 2101's exemptions for environmental regulations. Instead, Article 1114 states that NAFTA governments are encouraged to adopt regulations that ensure investment activities are "undertaken in a manner sensitive to environmental concerns," but *only* if those measures are otherwise consistent with the obligations set forth in Chapter Eleven.¹⁸³ The "otherwise consistent" qualification poses this question: if a domestic law enacted to protect water resources reduces the value of a foreign investment, will it create a cause of action in the foreign investor against the host nation? For the reasons set forth below, non-discriminatory water resource regulations do not create Chapter Eleven liability.

A. North American Agreement on Environmental Cooperation

The North American Agreement on Environmental Cooperation (NAAEC) is a side agreement concerning environmental management that was enacted concurrently with NAFTA.¹⁸⁴ NAFTA arbitration tribunals should look to the NAAEC when interpreting any of NAFTA's Chapter Eleven investment provisions that may result in environmental implications because "[i]nterpretation of an international treaty begins with the language itself unless it effects a result inconsistent with the parties' intentions."¹⁸⁵ The NAAEC demonstrates the intent of the NAFTA nations to promote domestic environmental protection measures that will not subject them to liability under NAFTA's investor protection measures. Specifically, Article 3 of NAAEC obligates the parties as follows:

Recognizing the right of each Party to establish its own levels of domestic environmental protection and environmental development policies and priorities, and to adopt or modify accordingly its environmental laws and regulations, each Party shall ensure

183. NAFTA, *supra* note 14, at art. 1114.

184. See North American Agreement on Environmental Cooperation, Can.-Mex.-U.S., Sept. 8-14, 1993, 32 I.L.M. 1480. [hereinafter NAAEC]. The NAAEC's objectives are, *inter alia*, to (a) foster the protection and improvement of the environment in the territories of the Parties for the well-being of present and future generations; (b) promote sustainable development based on cooperation and mutually supportive environmental and economic policies; (c) increase cooperation between the Parties to better conserve, protect, and enhance the environment, including wild flora and fauna; (d) support the environmental goals and objectives of the NAFTA; . . . and (g) enhance compliance with, and enforcement of, environmental laws and regulations . . ." *Id.* at art. 1.

185. *In re Gambino*, 421 F.Supp.2d 283, 299 (D. Mass. 2006) (holding that the "clear import of treaty language controls unless 'application of the words of the treaty according to their obvious meaning effects a result inconsistent with the intent or expectations of its signatories'" (citing *Sumitomo Shoji America, Inc. v. Avagliano*, 457 U.S. 176, 180 (1982))).

that its laws and regulations provide for high levels of environmental protection and shall strive to continue to improve those laws and regulations.¹⁸⁶

If investors were able to claim that legitimate environmental regulations result in expropriation, the environmental goals of NAAEC would be compromised. Thus, Chapter Eleven's investment protections should be interpreted to avoid adverse environmental results in the context of affording investment protections. As discussed *infra*, the final awards issued by the NAFTA tribunals are in accord with the NAAEC because they have not found liability in relation to non-discriminatory resource protections laws adopted and applied with appropriate due process protections.¹⁸⁷

B. The Nature of State Water Management Regimes and Investments in Water Resource Preclude Chapter Eleven Liability

As explained in Part VI, concerns that NAFTA's Chapter Eleven investor protection provisions could "chill" the enactment or enforcement of legitimate water management laws are misplaced because an investor cannot claim to have made an investment in water unless and until that investor has secured a water right under state water law. Again, state legal regimes establish the terms and conditions pursuant to which a water right may be acquired¹⁸⁸ and to which exercise of that right is subject. Each state typically applies multiple conditions to the acquisition and maintenance of a water right to ensure that water withdrawals are made consistent with the public interest.¹⁸⁹ Therefore, each state's legal regime necessarily conditions "investments" in water, and limits the scope of claims that may be brought pursuant to Chapter Eleven.

The implications of this analysis are that conditions imposed upon the acquisition of water rights and on the use of water to protect the public's interest in water resources should not be held to violate NAFTA's Chapter Eleven investment protection provisions, so long as they are applied even-handedly in a fair and transparent manner. Specifically, such resource regulations will not violate NAFTA's Article 1102

186. NAAEC, *supra* note 184 at art. 3.

187. See *Pope & Talbot I*, *supra* note 181, at ¶ 96; *S.D. Myers, Inc. v. Canada*, 40 I.L.M. 1408, ¶¶ 246-48, 250 (2000) [hereinafter *S.D. Myers I*] available at <http://naftaclaims.com> (accessed from homepage by selecting "The Disputes" then "Canada" then "S.D. Myers" and then "Partial Award on the Merits, 13 November 2000") (last visited Nov. 3, 2007); *Metalclad Corp. v. United Mexican States*, Final Award, 5 ICSID REV.: FOREIGN INVESTMENT L. J. 209, 230-31 (2000) [hereinafter *Metalclad I*] available at <http://naftaclaims.com> (accessed from homepage by selecting "The Disputes" then "Mexico" then "Metalclad" and then "Final Award, 2 September 2000") (last visited Nov. 3, 2007); *Methanex I*, *supra* note 24, at ¶ 1.

188. See discussion, *supra* Part III.

189. See discussion, *supra* Part IV(A).

equal treatment requirements so long as the conditions and restrictions are applied equally to all parties seeking to withdraw and use water within the state.¹⁹⁰ The same may be said in relation to NAFTA's Article 1105 ("minimum standard of treatment") so long as the regulatory regime is governed by due process standards equally applied to all individuals and entities, foreign or domestic.¹⁹¹ Finally, because investments in water resources are inherently limited by the conditions imposed under the state's water management laws, no expropriation should be found under Article 1110 where the state has simply enforced those conditions.¹⁹² In other words, a foreign investor can secure no greater rights than arise under state law. Accordingly, there is no basis for a foreign investor to assert discriminatory treatment where it has acquired rights conditioned and limited by the character of the rights themselves, the public interest, and the state's reserved police power. As discussed next, additional insight and support for these conclusions can be gained from a closer consideration of the three primary Chapter Eleven investment protections and the NAFTA tribunal decisions that have applied these provisions.

C. Chapter Eleven's Investor Protections: Articles 1102 (National Treatment) and 1105 (Minimum Standard of Treatment)

1. NAFTA Article 1102: National Treatment

Article 1102 is NAFTA's "non-discrimination" provision. It requires the host nation to accord to foreign investors and investments "treatment no less favorable than it accords, in like circumstances, to those of its own investors."¹⁹³ To show a violation of this Article, a foreign claimant must demonstrate that a host nation's regulation has caused the foreign investor or investment to receive less favorable treatment than a domestic competitor.¹⁹⁴ If a foreign claimant can demonstrate that

190. See discussion, *supra* Part VI(C)(1).

191. See discussion, *supra* Part VI(C)(2).

192. Marvin Feldman v. Mexico, 18 ICSID REV.: FOREIGN INVESTMENT L.J. 488, ¶¶ 102-03 (2002) (stating that expropriation does not result from bona fide regulation: a state is not required to compensate an investment for any loss sustained by the imposition of a non-discriminatory, regulatory measure protecting legitimate public welfare objectives). Furthermore, the Preamble of NAFTA states that NAFTA Parties have preserved "their flexibility to safeguard the public welfare," showing the Parties had no intention of diminishing the scope of the police power that exists under international law. NAFTA, *supra* note 14, at preamble.

193. NAFTA, *supra* note 13, at art. 1102(1).

194. See Pope & Talbot, Inc. v. Canada, Award on Merits, Phase Two, 122 I.L.R. 336, ¶¶ 78-79 (2001), [hereinafter Pope & Talbot II], available at <http://www.appletonlaw.com> (accessed from homepage by selecting "Cases", then "Pope & Talbot v. Canada" then "Page 2" then "Merits Award, April 10, 2001") (last visited Nov. 2, 2007).

the treatment it received was less than the best treatment afforded to a competing investment or investor in "like circumstances," the host nation bears the burden of justifying the difference in treatment.¹⁹⁵ Such difference in treatment may be excused, however, where the host government can show that it has "a reasonable nexus to rational government policies that (1) do not distinguish, on their face or *de facto*, between foreign-owned and domestic companies, and (2) do not otherwise unduly undermine the investment liberalizing objectives of NAFTA."¹⁹⁶

This analysis of Article 1102 is strikingly similar to the manner in which the United States Supreme Court has analyzed restrictions on interstate trade under the dormant Commerce Clause. If a state law treats in-state and out-of-state economic interests differently, to the benefit of in-state interests, it is "virtually *per se* invalid."¹⁹⁷ Under such circumstances, the regulation will only be upheld if it is found to achieve a legitimate local purpose that cannot be adequately served by non-discriminatory alternatives. On the other hand, if a restriction is found to be non-discriminatory, and it "regulates even-handedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits."¹⁹⁸

As the record of NAFTA decisions demonstrates, the tribunals' analysis of Article 1102 claims closely tracks the United States Supreme Court's dormant Commerce Clause jurisprudence. As a result, a domestic water law enacted to protect the resource and applied in a non-discriminatory manner should be upheld under Article 1102's national treatment provisions *even though* it may disproportionately affect a foreign investor or investment.

Critics of NAFTA have pointed to the NAFTA arbitration in *Ethyl Corporation v. Canada*¹⁹⁹ as an example of the dangers posed by Chapter Eleven because a foreign investor was able to force a host government to rescind a law that it could not have challenged in its own home country.²⁰⁰ The arbitration concerned a Canadian ban on the impor-

195. Todd Weiler, *The Treatment of SPS Measures Under NAFTA Chapter 11: Preliminary Answers to an Open-Ended Question*, 26 B.C. INT'L & COMP. L. REV. 229, 241-242 (2003).

196. *Pope & Talbot II*, *supra* note 194, at ¶ 78.

197. *Oregon Waste Systems, Inc. v. Dep't of Env'tl. Quality of State of Oregon*, 511 U.S. 93, 99 (1994).

198. *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970).

199. *Ethyl Corp. v. Government of Canada*, Award on Jurisdiction 38 I.L.M. 708 (1998) [hereinafter *Ethyl I*] available at <http://www.naftaclaims.com> (accessible from homepage by selecting "The Disputes" then "Canada" then "Ethyl Corp." and then "Award on Jurisdiction, 24 June 1998") (last visited Nov. 2, 2007).

200. See H. Hamner Hill, *NAFTA and Environmental Protection: The First Ten Years*, 200 J. INST. JUST. INT'L STUD. 157, 161 (2006).

tation of substances containing manganese,²⁰¹ including MMT, a widely used fuel additive.²⁰² Ethyl Corporation, a U.S. company that imports and distributes MMT in Canada, filed a Chapter Eleven claim alleging that such regulatory interference with its investment in the MMT business constituted a denial of equal “national treatment” under Article 1102 and an expropriation requiring compensation under Article 1110.²⁰³ Following a ruling by a Canadian court that the ban on MMT violated Canada’s own Agreement on Internal Trade, the Canadian government settled Ethyl Corporation’s NAFTA claim for \$13 million in damages and revoked the manganese ban. While NAFTA critics contend the result illustrates the danger that Chapter Eleven poses to domestic environmental protection, the Canadian manganese ban bears little resemblance to a true non-discriminatory environmental regulation, which should not violate Article 1102. Although the ban was ostensibly enacted to protect the health of Canadians, it only prohibited the importation and inter-provincial trade in MMT, not the domestic production of MMT or its use in gasoline. It was this intrinsic discrimination against outsiders that made the MMT ban suspect.²⁰⁴ By contrast, had Canada issued a comprehensive ban on all substances containing manganese based upon public health concerns, such a ban would not have constituted a violation of Article 1102’s national treatment standard.²⁰⁵

Indeed, where NAFTA tribunals have decided Article 1102 claims on their merits, they apply the “like circumstances” test, men-

201. Manganese-based Fuel Additives Act (MBFAA), S.C. 1997, c. 11 (Can.).

202. Canada enacted the ban following the release of a study concerning the health dangers of manganese. The study, Environmental Health Directorate, Health Canada, Risk Assessment for the Combustion Products of Methylcyclopentadienyl Manganese Tricarbonyl (MMT) in Gasoline (Dec. 6, 1994), is available at <http://www.hc-sc.gc.ca> (accessed from homepage by selecting “English” then “Environmental & Workplace Health” then “Air Quality” “Publications” and then “Risk Assessment for the Combustion Products of Methylcyclopentadienyl Manganese Tricarbonyl (MMT) in Gasoline”) (last visited Nov. 2, 2007)..

203. Ethyl Corp. v Government of Canada, Notice of Arbitration at 7-12 (1997) [hereinafter Ethyl II] available at <http://www.naftaclaims.com> (accessible from homepage by selecting “The Disputes” then “Canada” then “Ethyl Corp.” and then “Notice of Arbitration, 14 April 1997”) (last visited Nov. 2, 2007).

204. Ethyl Corp. v. Government of Canada, Statement of Claim at ¶ 35 (1997) [hereinafter Ethyl III], available at <http://www.naftaclaims.com> (accessible from homepage by selecting “The Disputes” then “Canada” then “Ethyl Corp.” and then “Statement of Claim, 2 October 1997”) (last visited Nov. 2, 2007). An analogous state law within the United States banning the importation of a particular substance into the state, but not restricting the intrastate production or trade of that same product, would almost certainly be struck down under the dormant Commerce Clause. See *Hughes v. Oklahoma*, 441 U.S. 322 (1979) (striking down Oklahoma statute which placed no limits on numbers of minnows that could be taken by licensed minnow dealers and did not limit in any way how such minnows might be disposed of within the state, but which forbade transportation of any commercially significant number of natural minnows out of state for sale).

205. See *Methanex I*, *supra* note 24, at ¶¶ 21-22.

tioned above, to determine whether the different treatment of investors in like circumstances “is justified by legitimate public policy measures that are pursued in a reasonable manner.”²⁰⁶ In the *S.D. Myers v. Canada* arbitration, the claimant, a U.S. corporation specializing in PCB waste remediation with many Canadian clients, filed a claim against Canada after Canada banned the exportation of PCB waste to the United States.²⁰⁷ The NAFTA Tribunal’s final award found that Canada’s PCB export ban amounted to a discriminatory and protectionist measure, crafted to favor domestic waste processors over those like *S.D. Myers* that sought to process PCB waste within the United States.²⁰⁸ The Tribunal, therefore, found that Canada had breached Article 1102’s national treatment requirements.²⁰⁹ However, the Tribunal did not disparage Canada’s desire to cultivate domestic waste-processing capability, but rather highlighted its failure to do so without breaching Article 1102.²¹⁰ The final award explained that international environmental principles expressed in the NAAEC²¹¹ suggest the need for a balanced approach to environmental measures even if that may have the effect of distorting trade and development.²¹²

The Tribunal considers that the interpretation of the phrase “like circumstances” in Article 1102 must take into account the general principles that emerge from the legal context of the NAFTA, including both its concern with the environment and the need to avoid trade distortions that are not justified by environmental concerns. The assessment of “like circumstances” must also take into account circumstances that would justify governmental regulations that treat them differently in order to protect the public interest.²¹³

In essence, the Tribunal read into Article 1102’s “like circumstances” test the exceptions for environmental regulation that exist in GATT Article XX, which were incorporated by NAFTA Article 2101, but which the text of NAFTA does *not* extend to Chapter Eleven investor

206. *S.D. Myers*, *supra* note 187 at ¶ 246; *Pope & Talbot II*, *supra* note 194, at ¶ 78.

207. *S.D. Myers, Inc. v. Government of Canada*, Statement of Claim (1998) [hereinafter *S.D. Myers II*] available at <http://www.naftaclaims.com> (accessible from homepage by selecting “The Disputes” then “Canada” then “S.D. Myers” and then “Statement of Claim, 30 October 1998”) (last visited Nov. 2, 2007)

208. *S.D. Myers I*, *supra* note 187, at ¶¶ 252-55.

209. *Id.* at ¶ 256.

210. *Id.* at ¶ 255.

211. These principles include: 1) States have the right to establish high levels of environmental protection, and are not obligated to compromise their standards merely to satisfy the political or economic interests of another state; 2) States should avoid creating distortions of trade; and 3) environmental protection and economic development can and should be mutually supportive. *Id.* at ¶ 247.

212. *Id.* at ¶¶ 246-48, 250.

213. *Id.* at ¶ 250.

protections.²¹⁴ S.D. Myers was awarded \$9 million in damages for being temporarily shut out of the Canadian market for PCB remediation because Canada's regulation was clearly protectionist.²¹⁵ However, the Tribunal's discussion of the interplay between Article 1102 and environmental goals suggests deference to non-discriminatory environmental regulation, even if such regulation results in unequal impacts upon foreign investors when applied.

The final award issued in *Pope & Talbot v. Canada* further supports this premise.²¹⁶ That arbitration arose out of Canadian restrictions on lumber exports to the United States enacted pursuant to the Softwood Lumber Agreement between the two nations, which was drafted to prevent "dumping" of Canadian lumber into U.S. markets.²¹⁷ Although the domestic regulation was not environmental in nature, the final award is instructive as to when Article 1102 liability will and will not arise. The Tribunal found that Canada's export control regime did not violate Article 1102, even though it subjected the foreign claimant to worse treatment than its domestic competitors, because the non-discriminatory restrictions bore a reasonable relation to Canada's legitimate goal of meeting its trade treaty obligations to the United States.²¹⁸ The decision in *Pope & Talbot* demonstrates that NAFTA will accommodate unequal regulatory treatment of foreign investment or investors where "there is a reasonable nexus between the [regulation] and a rational, non-discriminatory government policy."²¹⁹

Water rights regulations that bear a "reasonable nexus" to non-discriminatory water resource management objectives should be similarly upheld. In the context of dormant Commerce Clause jurisprudence,

214. Weiler, *supra* note 195, at 242. GATT's Article XX, incorporated into NAFTA by Article 2101, provides that certain environmental regulations, such as those relating to the conservation of exhaustible natural resources, may be enacted even if they conflict with trade protection provisions. *See* discussion, *supra* Part V(C).

215. As explained by the tribunal, Canada excluded the American claimant because it wanted to ensure strength of the Canadian PCB remediation industry. *S.D. Myers I*, *supra* note 187, at ¶¶ 252, 255. This was a legitimate goal for the Canadian government to pursue, but the method they chose — excluding all foreign competitors — was inconsistent with the requirements of Article 1102. *Id.* The tribunal suggested that Canada could have achieved the same goal through less discriminatory means such as government subsidies — an analysis which closely parallels U.S. dormant Commerce Clause jurisprudence. *Id.*; *see also Hughes*, 441 U.S. at 337.

216. *See Pope & Talbot II*, *supra* note 194.

217. *Pope & Talbot v. Canada*, Statement of Claim at ¶ 14-15 (1999) [hereinafter *Pope & Talbot III*], available at <http://www.appletonlaw.com> (accessed from homepage by selecting "Cases", then "Pope & Talbot v. Canada" then "Page 4" then "Statement of Claim, March 25, 1999") (last visited Nov. 2, 2007).

218. *Pope & Talbot II*, *supra* note 194, at ¶ 103-04.

219. *Pope Talbot II*, *supra* note 194, at ¶ 81; *see also Methanex I*, *supra* note 24, at ¶ 21-22 (holding that an environmental regulation banning MTBE in California was applied uniformly and without discrimination, and was therefore in accordance with Article 1102).

the applicable test is whether the regulation is “narrowly tailored” to the public policy it promotes. In *Sporhase v. Nebraska*, for example, the Supreme Court struck down a Nebraska state statute prohibiting the export of water to any state that forbade the transfer of its own water into Nebraska.²²⁰ The portion of the statute requiring reciprocity for water transfers was held to be facially discriminatory against out-of-state interests, and in violation of the dormant Commerce Clause, because the law was not narrowly tailored to the conservation and preservation rationale asserted by the state.²²¹

The Court did, however, uphold that portion of the statute requiring that any export of groundwater be for a reasonable purpose, not contrary to the goals of conservation and preservation of groundwater, and not detrimental to the public welfare.²²² These are customary considerations that are evaluated by water rights administrators when granting a right to water or evaluating a change in existing use. Because Article 1102 of NAFTA and the U.S. dormant Commerce Clause serve similar goals of prohibiting disparate treatment of insider and outsider investment activity, it is reasonable to surmise that a NAFTA Tribunal might apply similar reasoning as set forth by the U.S. Supreme Court in *Sporhase*. Although the analysis in *Sporhase* suggests that a comprehensive ban on water exports would violate Article 1102, the *Sporhase* analysis would allow a state to condition water exports on a showing of compliance with beneficial use, sustainable use, and conservation requirements that are narrowly tailored to achieve their purpose.²²³ Regulation of exports, carefully drafted to protect a public purpose, such as protecting a region’s ecology, should be upheld.²²⁴ The latter approach is already the approach commonly applied among the states because it more clearly reflects the states’ interest in ensuring beneficial use, preserving the resource and avoiding harm to the environment, rather than arbitrarily restricting commerce.²²⁵

2. NAFTA Article 1105: Minimum Standard of Treatment

Article 1105 is NAFTA’s “due process” provision. It requires that each nation provide a “minimum standard of treatment” to investors

220. *Sporhase*, 458 U.S. at 957.

221. *Id.* at 957-58 (hypothesizing that for such a comprehensive ban to succeed, Nebraska would have to show that (1) the state as a whole has a water shortage, (2) intrastate water transfer from areas with a surplus to areas of need is feasible, and (3) the importation of water from adjoining states would compensate for any exportation).

222. *Id.* at 955-56.

223. See Carl P.A. Nelson, *Sporhase v. Nebraska Ex Rel. Douglas: A Call for New Approaches to Water Resource Management*, 11 HASTINGS CONST. L.Q. 283, 312-15 (1983-1984).

224. Chris A. Shafer, *Great Lakes Diversions Revisited: Legal Constraints and Opportunities for State Regulation*, 17 T.M. COOLEY L. REV. 461, 482-83 (2000).

225. See *supra*, Part IV.

and investments from either of the other two nations, and that the treatment must be “in accordance with international law, including fair and equitable treatment and full protection and security.”²²⁶ “Fair and equitable treatment” under Article 1105 requires governments to act in a transparent manner, to provide investors with a fair hearing, to not make decisions on the basis of irrelevant factors or with insufficient evidence, and to not frustrate the legitimate expectations of investors, when those expectations develop as a result of government conduct.²²⁷ Similarly, Article 1105’s “full protection and security” provision obligates governments to protect investments against losses suffered as a result of misadministration or enforcement failures.²²⁸

The minimum standard of treatment due under Article 1105 is quite similar to the guarantees of procedural and substantive due process afforded by the Fourteenth Amendment of the United States Constitution. Procedural due process requires that a state proceeding which results in a deprivation of property be fair, while substantive due process insures that such state action not be arbitrary and capricious.²²⁹ For example, an administrative agency may not apply disparate or inconsistent treatment or standards to similarly situated parties in comparable situations.²³⁰ Before a person is deprived of property by administrative rule, due process also requires that the person be afforded notice, an opportunity to be heard, and a written statement of findings.²³¹

The NAFTA tribunals have addressed several Article 1105 claims related to environmental regulation. In *S.D. Myers*, discussed *supra*, the claimant asserted that Canada’s ban on PCB waste exports was enacted in a discriminatory and unfair manner in violation of basic requirements of international law for due process and good faith.²³² As noted, *supra*, the NAFTA Tribunal found that Canada had implemented the legislation specifically for the purpose of protecting Canadian industry.²³³ The ban was enacted contrary to the recommendation of its own Department of Environment experts, and despite the knowledge that the United States Environmental Protection Agency was willing to cooperate on a “technically and environmentally sound solution” to the PCB problem.²³⁴ Although the Canadian law was transparently protectionist,²³⁵ the

226. NAFTA, *supra* note 14, art. at 1105(1).

227. See *Metalclad I*, *supra* note 187, at ¶¶ 51-52, 80, 88, 91-92.

228. See Todd Weiler, *A First Look at the Interim Merits Award in S.D. Myers, Inc. v. Canada: It is Possible to Balance Legitimate Environmental Concerns With Investment Protection*, 24 HASTINGS INT’L & COMP. L. REV. 173, 184 (2001).

229. See *Licari v. Ferruzzi*, 22 F.3d 344, 347 (1st Cir. 1994).

230. *Sunrise Manor Nursing Home v. Axelrod*, 135 A.D.2d 293, 297-98 (N.Y. App. Div. 1988).

231. U.S. CONST. amend. XIV; *Michigan Elec. Co-op. v. Michigan Public Service Comm’n.*, 705 N.W.2d 709 (Mich. 2005).

232. *S.D. Myers I*, *supra* note 187, at ¶ 40-42.

233. *Id.* at ¶¶ 164-88.

234. *Id.* at ¶ 173.

Tribunal was less concerned with the Canadian government's goal of propping up its domestic industry than with Canada's failure to grant proper due process protections to those foreign corporations affected by the export ban.²³⁶ As the Tribunal noted, the violations of the Article 1105 requirements for fair and equitable treatment were "unacceptable from an international perspective . . . [even] in light of the high measure of deference that international law extends to the right of domestic authorities to regulate matters within their own borders."²³⁷

The final award issued in *Metalclad v. Mexico* also found a violation of the minimum standard of treatment required by Article 1105.²³⁸ The arbitration arose after the claimant, a U.S. company, purchased a Mexican waste disposal company, in part based upon assurances by the federal government of Mexico that the Mexican company had all the necessary permits to operate a landfill in Guadalcazar.²³⁹ In actuality, Metalclad was forced to seek construction permits from municipal authorities for the landfill. The local government eventually denied Metalclad the necessary construction permits at a municipal meeting of which Metalclad received no notice and at which Metalclad was given no opportunity to appear.²⁴⁰ Moreover, the denial of the construction permit was not predicated upon any alleged defect in the construction of the landfill, but simply local opposition to the project.²⁴¹ After the municipality signaled its intent to derail the project, the state issued a decree that "effectively and permanently prevented the use by Metalclad of its investment."²⁴² The Tribunal found that Mexico had failed to afford Metalclad the standard of treatment required by Article 1105 because (i) the Mexican federal government falsely portrayed the Mexican waste disposal company's permit status, (ii) the municipal authorities denied its

235. *Id.* at ¶ 255.

236. According to the factual background outlined in the *S.D. Myers I*, the Canadian ban was not based on sound evidence, and was enacted for trade protection reasons that had no connection to the health risks cited as the justification for the ban. *Id.* at ¶¶ 161-95.

237. *Id.* at ¶ 263.

238. *Metalclad I*, *supra* note 187, at ¶¶ 74-101.

239. *Metalclad Corp. v. United Mexican States, Investor Memorial*, 3 (1997) [hereinafter *Metalclad II*] available at <http://naftaclaims.com> (accessed from homepage by selecting "The Disputes" then "Mexico" then "Metalclad" and then "Investor Memorial, 13 October 1997") (last visited Nov. 3, 2007).

240. *Metalclad I*, *supra* note 187, at ¶¶ 86, 91.

241. *Id.* at ¶ 92. I do not address here the merits of the local population's objections to the landfill, whether they were grounded in environmental concerns, cultural conflicts, or any other basis. I simply point out that the scope of a construction permit is limited to the adequacy of the construction quality of the project. Thus, the liability in *Metalclad* resulted, in part, from the Mexican government's improper denial of the construction permit based on concerns unrelated to construction quality.

242. *Id.* at ¶ 96.

permits without due process, and (iii) the state government issued an arbitrary decree.²⁴³

Although NAFTA critics portray *Metalclad* as an example of a corporation preventing the adoption of domestic environmental regulations,²⁴⁴ the final award simply illustrates Article 1105's requirement that NAFTA signatory nations and their political subdivisions follow "due process" requirements when regulating, including clear rules and established practices and procedures.²⁴⁵ By comparison to the unpredictable treatment applied to *Metalclad* by the local Mexican authorities, water resource management regulations in place throughout the United States are clear, predictable rules for the establishment of an investment in water resources. As such, they should not face liability under Article 1105.

The final award issued in *Methanex Corp. v. U.S.A.* supports this conclusion. In this arbitration, the Tribunal rejected Methanex's claim that California's ban on MTBE deprived it of equitable treatment under Article 1105.²⁴⁶ Methanex alleged that the Governor of California had banned MTBE as a political favor to the Archer Daniels Midland Company, which manufactured ethanol, a competing product.²⁴⁷ The final award found, however, that Governor Davis's approval of the ban was a largely ministerial action.²⁴⁸ In fact, the ban had been passed by the California legislature during the previous governor's tenure, and its implementation was contingent upon scientific findings followed by public hearings, testimony, and peer review.²⁴⁹ In short, the MTBE ban was enacted through a transparent democratic process, Methanex was on notice of the impending ban for some time before it was enacted, and it was applied in a non-discriminatory manner. Thus, the final award found no violation of Article 1105 because the MTBE ban was applied with all the fair and equitable treatment required by Article 1105.²⁵⁰

In light of the *Methanex* decision, a federal, state, or local law directed at the protection of water resources (e.g., water rights administration or water quality protection) should not incur liability under Article 1105 so long as the law is enacted and applied in a manner that ensures fair and equitable treatment. Again, the standard of appropriate treatment under Article 1105, as described by the NAFTA Tribunal, is similar to the procedural and substantive due process requirements of the Fourteenth Amendment: notice and opportunity to be heard, regulation based

243. *Id.* at ¶¶ 88, 97, 100.

244. See Halil Hasic, *Article 110 of NAFTA: Investment Barriers to Upward Harmonization of Environmental Standards*, 12 SW. J. L. & TRADE AM. 137, 151 (2005).

245. *Metalclad I*, *supra* note 187, at ¶ 88.

246. *Methanex I*, *supra* note 24, at Part IV, c. C, ¶ 26.

247. *Id.* at Part IV, c. C, ¶ 8.

248. *Id.* at Part III, c. B, ¶ 54.

249. *Id.*

250. *Id.* at Part IV, c. C, ¶ 26.

on factual findings, and consistent treatment for similarly situated parties.

D. Chapter Eleven's Investor Protections: Article 1110 (Expropriation Compensation)

Whereas Articles 1102 and 1105 protect foreign investors from discriminatory, arbitrary and unfair treatment, Article 1110 protects foreign investments from expropriation without compensation.²⁵¹ Article 1110 provides that a host nation shall compensate an injured party for expropriation of any investment by the host nation, including its political subdivisions (i.e., including state and local government).²⁵² Specifically, the article forbids expropriations affecting another nation's investors except (a) for a public purpose; (b) on a non-discriminatory basis; (c) in accordance with due process of law and Article 1105(1); and (d) on payment of compensation.²⁵³ For compensation to be due, the investment interference must meet the threshold of "substantial."²⁵⁴

Article 1110 potentially presents conflict between an investor deprived of the fundamental right to continue operating or owning its investment, and a sovereign nation's fundamental right to protect its citizens and natural resources. It is this underlying tension that has infused certain NAFTA arbitration awards regarding Article 1110 with perhaps more controversy and significance than they merit. For example, the expropriation award in *Metalclad Corporation v. Mexico* is often cited by NAFTA critics as an example of an investor's use of Article 1110 to force the public at large to pay for resource protection laws that interfere with foreign investments.²⁵⁵ As I have explained, however, Mexico's liability arose not from the application of resource protection laws, but from Mexico's arbitrary treatment of *Metalclad* and denial of permits for the construction of the landfill without the fair and equitable treatment required by Article 1105.²⁵⁶

251. See NAFTA, *supra* note 14, at art. 1110.

252. *Id.* at arts. 105, 1110.

253. *Id.* at art. 1110. It should be noted that the conjunctive "and" precedes the compensation element of Article 1110. At least one scholar has argued that the logical consequence of this construction is that, unlike U.S. regulatory takings jurisprudence which only requires compensation when a regulatory taking deprives property of a certain percentage of its value, Article 1110 requires compensation whenever an expropriation occurs, even if it the expropriation only reduces a portion of an investment's value. See Jessica Lawrence, *Chicken Little Revisited: NAFTA Regulatory Expropriations After Methanex*, 41 GA. L. REV. 261 (2006).

254. See *Pope & Talbot I*, *supra* note 181, at ¶ 102.

255. See Hasic, *supra* note 244, at 151; Terra Lawson-Remer, *Values Under Siege: NAFTA, GATS, and the Propertization of Resources*, 14 N.Y.U. ENVTL. L.J. 481, 504-08 (2006).

256. See discussion, *supra* Part VI(C)(2).

Non-discriminatory water resource management laws applied with appropriate due process protections should not be found to be expropriative under Article 1110. As I explained in Part III, *supra*, virtually all rights to capture and use water are acquired subject to state laws governing water rights, as interests in real property. The restrictions imposed by these laws are inherent qualifications of the right and are part and parcel to any “investment” made in the resource.²⁵⁷ Application of the state water resource management laws, therefore, cannot result in an expropriation because the foreign investor cannot possess an investment free of the restrictions arising under the organic state law and inherent in the relevant water right.²⁵⁸

Moreover, the final awards issued to date in Article 1110 cases have demonstrated that non-discriminatory resource protection laws fairly applied are not cases found to be expropriatory even if the application of the laws disproportionately harms a foreign investment. A recent example is the final award in the recent Methanex Corp. v. U.S.A. arbitration.²⁵⁹ As noted above, the arbitration involved California’s ban on the gasoline additive MTBE, which reduced Methanex’s sales of methanol, an MTBE component. In addition to its Article 1102 and Article 1105 claims, Methanex alleged under Article 1110 that the ban was “tantamount to an expropriation” because “the measure constitute[d] a substantial taking” of Methanex’s business, investment, and economic

257. See discussion, *supra* Part III.

258. Consider, for example, a riparian jurisdiction in which the riparian right is initially limited by law to use only upon the riparian property (i.e., appurtenant use). A purchaser of the right may only liberate the water for a non-appurtenant use by complying with the applicable state law regarding grant, transfer or licensing. See Michael D. Rosen & Richard J. Sexton, *Irrigation Districts and Water Markets: An Application of Cooperative Decision-Making Theory*, 69 LAND ECON. 1, 39-53 (1993). This is true even if the state was the purchaser of the right. See *Apfelbacher*, 167 N.W. 244, 246 (holding that “[t]he conveyance . . . to the state confers no greater right with reference to these flowing waters than [he] himself had”); *Riverside County*, 93 Cal. Rptr.2d at 283 (concluding that the state only possesses such riparian or appropriative rights as it may otherwise obtain by law). It is of no real consequence whether the state common law or administrative system authorizes riparians to make off-tract beneficial use or to convey the right to third parties by grant or condemnation. The point is that the extent of the riparian’s respective right as well as that of its grantee are determined by the states, as real property rights arising under state law. See *supra*, note 70. In a prior appropriation state, the ability of an applicant to initiate a new use or for an existing user to change to a new use is traditionally dependent upon avoiding injury to another vested right. U.S. Dept. of the Interior, Bureau of Land Management, Western States Water Laws: Water Appropriation Systems, available at <http://www.blm.gov/nstc/WaterLaws/appsystems.html>. (last visited Nov. 14, 2007). In such cases, the vested rights of another user interact with and provide a limitation on the rights of a potential investor. Again, the point is the scope of the right is limited by limitations imposed by the state’s water rights management regime. See *supra*, notes 71 and 72. A foreign investor in the right cannot claim an expropriation where the state simply enforces those limitations; see also discussion, *supra* Part III.

259. *Methanex I*, *supra* note 24.

value.²⁶⁰ The Tribunal's final award explained that the MTBE ban was a non-discriminatory law enacted for a legitimate public purpose, with appropriate due process, and thus did not constitute a compensable expropriation under Article 1110.²⁶¹ Although the matter was decided on jurisdictional grounds, the Tribunal addressed the Article 1110 claim, stating that "as a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and which affects, inter alia, a foreign investor or investment is not deemed expropriatory and compensable."²⁶²

The transparent MTBE regulation in *Methanex* contrasts sharply with the Mexican government's action that was held to cause an expropriation in *Metalclad*, discussed *supra*. In that case, the actions of the state and local authorities were executed without due process, specifically discriminated against *Metalclad*, and destroyed 100% of its investment in the landfill.²⁶³ Accordingly, the Tribunal found Mexico had violated Article 1110 by indirectly expropriating *Metalclad*'s investment.²⁶⁴

It is instructive to consider expropriation liability under Article 1110 in relation to U.S. regulatory takings jurisprudence,²⁶⁵ as the two legal principles are somewhat analogous.²⁶⁶ In the words of Supreme Court Justice Oliver Wendell Holmes in the landmark decision of *Pennsylvania Coal v. Mahon*, "while property may be regulated to a certain extent, if the regulation goes too far, it will be recognized as a taking."²⁶⁷ To determine whether a regulation has gone too far, the U.S. Supreme Court has articulated a balancing test consisting of three considerations: 1) the economic impact of the regulation on the claimant,²⁶⁸ 2) the extent

260. *Methanex Corp. v. U.S.A.*, Statement of Claim (1999) [hereinafter *Methanex II*] available at <http://www.naftaclaims.com> (accessible from homepage by selecting "The Disputes" then "USA" then "Methanex" and then "Statement of claim, 3 December 1999") (last visited Nov. 3, 2007).

261. *Methanex I*, *supra* note 24, at Part IV, c. D, ¶ 15.

262. *Id.* at ¶ 7. The tribunal found that although *Methanex* experienced a loss of a valuable market for its product, *Methanex*'s business had not been expropriated because "the regulatory action [had] not deprived the claimant of control of his company, . . . interfered directly in the internal operations . . . or displaced the claimant as the controlling shareholder." *Id.* at ¶ 16. The tribunal also explicitly rejected the argument that the loss of intangibles such as customer base and market share constitutes "investments" subject to expropriation and compensation, stating that they are merely elements useful for calculating the value of a comprehensive expropriation. *Id.* at ¶ 17.

263. *Metalclad I*, *supra* note 187, at ¶ 102-12.

264. *Id.* at ¶ 112.

265. The "takings clause" of the Fifth Amendment to the United States Constitution provides that property shall not be taken for a public use, without just compensation. U.S. CONST. amend. V. The restriction is made applicable to the States by the Fourteenth Amendment. U.S. CONST. amend. XIV.

266. See Gregory M. Starner, *Taking a Constitutional Look: NAFTA Chapter 11 As an Extension of Member States' Constitutional Protection of Property*, 33 LAW & POL'Y INT'L BUS. 405, 427-28 (2002).

267. *Penn. Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922).

268. *Penn Cent. Transp. Co. v. New York City*, 438 U.S. 104, 113-14 (1978).

to which the regulation interferes with the landowner's "reasonable investment backed expectations,"²⁶⁹ and 3) the overall character of the government action.²⁷⁰ The Court also acknowledged that each case depends largely on the "particular circumstances [in that] case"²⁷¹ and on "essentially ad hoc, factual inquiries."²⁷² There are also instances, however, in which a regulation results in a *per se* "total" taking for which compensation is due; specifically, when the regulation deprives a landowner of all economically viable use of his or her property.²⁷³

It is also important to emphasize that "regulatory takings" analysis is qualified by a "nuisance exception." The courts have recognized that "some values are enjoyed under an implied limitation and must yield to the police power."²⁷⁴ Thus, a regulatory taking does not occur if the contested regulation is itself grounded in a state's "background principles" of nuisance and property law, because there can be no taking where the property owner never had the right to use the property in a manner contrary to the regulation.²⁷⁵ Applied to water resource management, this principle supports the conclusion that an entity cannot claim a regulatory taking under U.S. jurisprudence, nor an expropriation under Article 1110, where the state restricts the entity from withdrawing or using water in a manner contrary to the state's water management regime.²⁷⁶

While non-discriminatory water resource laws enacted with the customary due process should not yield liability as an expropriation under Article 1110, the converse is equally true; laws that patently discriminate against foreign investors, that are enacted without due process, or which confiscate or substantially interfere with a water right outside of the normal state regulatory scheme, may constitute a compensable expropriation under Article 1110. Again, United States takings law is instructive. A taking may occur where state or federal regulation "goes too far" and effectively eliminates an otherwise lawfully exercisable water

269. *Id.* at 124.

270. *Id.*

271. *Id.* (substitution in original).

272. *Id.* at 130-31.

273. *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1019 (1992).

274. *Pennsylvania Coal*, 260 U.S. at 413.

275. *Lucas*, 505 U.S. at 1004 (holding that "no compensation is owed in this setting as with all takings claims if the State's affirmative decree simply makes explicit what already inheres in the title itself, in the restrictions that background principles of the State's law of property and nuisance already place upon land ownership"); *see also Tahoe-Sierra Pres. Council, Inc. v. Tahoe Regional Planning Agency*, 535 U.S. 302, 351 (2002).

276. *Fallini v. Hodel*, 725 F.Supp. 1113, 1122-23 (D.Nev. 1989), *aff'd.*, 963 F.2d 275 (9th Cir. 1992) (holding that "[w]hile the Fifth Amendment's just compensation provision is designed to bar government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole, this principle is inapplicable to cases in which losses sustained by the plaintiffs are the incidental result of reasonable regulation in the public interest"); *see also* discussion, *supra* Part III.

right.²⁷⁷ For example, the United States courts have found compensable takings where a party's riparian water rights were completely extinguished by the construction of a federal aqueduct,²⁷⁸ where an entire diversionary right was requisitioned by the government for the purpose of generating power,²⁷⁹ and where the federal government issued an order that essentially divested an appropriator of its state water right, to provide wildlife access to the supply.²⁸⁰

Water rights are usufructuary rights and, as discussed *supra* in Part III.B, are generally limited to the beneficial use of that water. A *non-beneficial* use of water is not part of the bundle of property rights comprising a water right. A prohibition against a water right holder applying water to a non-beneficial use is not a taking of his water right, because he or she never had the right to make an unreasonable or non-beneficial use in the first instance.²⁸¹ Government regulation that prevents a water right holder from using his water in a non-beneficial manner may reduce or even extinguish that use without constituting a taking, because that action was merely an enforcement of the background regulatory environment in place at the time of the acquisition of the water right.²⁸² Accordingly, ongoing government regulation of the water resource may limit the uses to which water rights are applied without giving rise to a takings claim.²⁸³

It is also noteworthy that, although the text of Article 1110 putatively requires compensation for all expropriations, the text may also allow a tribunal to consider adverse environmental externalities when computing any damages due for an expropriation. Among other traditional valuation concepts, Article 1110 instructs that "other criteria" should be considered in determining the amount of compensation due as a result of an expropriation of an investment. If the investment activity is environmentally harmful, the negative value of those externalities should arguably be deducted from the calculation of fair market value of the

277. See *Fallini*, 725 F.Supp. at 1122.

278. *Gerlach*, 339 U.S. 725.

279. See *International Paper*, 282 U.S. 399.

280. *Fallini*, 725 F.Supp. at 1122-23 (holding that "[c]onsumption by wild horses of practically *all* of the Deep Well water . . . cannot be characterized as an 'incidental' result of reasonable regulation").

281. See James H. Davenport & Craig Bell, *Governmental Interference with the Use of Water: When do Unconstitutional "Takings" Occur?*, 9 U. DENV. L. REV. 1, 32-33 (2005). See, e.g., *Gin Chow*, 22 P.2d 5; *Joslin v. Marin Mun. Water Dist.*, 429 P.2d 889 (Cal. 1967).

282. See Davenport & Bell, *supra* note 281, at 33 (citing *Lucas*, 505 U.S. at 1031).

283. See, e.g., *State Water Res. Control Bd. (Racanelli Decision)*, 227 Cal. Rptr. 161; see also Clifford Schultz & Gregory Weber, *Changing Public Attitudes Toward Property Rights in California Water Resources: From Vested Rights to Utilitarian Reallocations*, 19 PAC. L.J. 1031, 1110 (1988); Brian E. Gray, *The Property Right in Water*, 9 HASTINGS W.-NW. J. ENVTL. L. & POL'Y 1 (2002); Julia Muedeking, *Taking the Heart of the Klamath Basin: Is it Free?*, 8 DRAKE J. AGRIC. L. 217 (2003).

injured investment.²⁸⁴ Thus, if a domestic water law, adopted to prevent the negative externalities of over-exploiting or contaminating a water source, were to substantially interfere with a foreign investment, the avoided negative externalities should be deducted from any compensation due to a foreign investor as a result of the law's interference with the investor's investment. Under this approach, the actual compensation may be *de minimis* depending on the circumstances at hand.

VII. DESIGNING VALID WATER RESOURCE MANAGEMENT LAWS

Based upon the forgoing analysis, this part presents a practical discussion of how states may structure water resource laws to withstand potential challenge based upon NAFTA and GATT. As noted above, although NAFTA's Chapter Eleven investment protections may extend to water resource laws, these provisions parallel several domestic laws within the United States, notably Due Process protections,²⁸⁵ dormant Commerce Clause jurisprudence,²⁸⁶ and the regulatory takings doctrine.²⁸⁷ Thus, resource management laws adopted to comport with these domestic legal principles should also satisfy the requirements of Chapter Eleven's investor protection laws, and vice versa. As an overarching statement, water resource laws should be directed at protection of the resource and administered with due process, and in a non-discriminatory and non-arbitrary manner. Laws that adhere to this fundamental precept should not invoke any liability under GATT or NAFTA.

A. Focus on Protection of the Resource

As discussed in Part V, *supra*, the protections for trade in goods set forth in NAFTA's Chapter Three and GATT's Articles III and XI will not apply to laws directed at protecting the quantity and quality of water

284. Weiler, *A First Look*, *supra* note 228, at 187 (stating that "[w]hereas NAFTA Article 1110(1) obviously enshrines a strong preference for the protection of investment (by promising compensation for all measures that substantially interfere with it), Article 1110(2) includes an open-ended definition of the criteria that may be used in the valuation of the compensation to be paid for such interference. If the economic activity undertaken by an investment leads to externalities that are so damaging to the environment that a government must take regulatory steps that substantially interfere with that investment, the appropriate level of compensation for such interference should take into account the negative value of those externalities. While professional business valuers may puzzle at the thought of adding 'negative environmental externalities' to a list of criteria that is supposed to be used to determine the 'fair market value' of an investment, it is incumbent upon treaty interpreters to arrive at a meaning of 'other criteria, as appropriate,' in Article 1110(2), that balances the NAFTA right of investment protection with the fundamental need to protect human, plant and animal life or health, and the environment *e.g.*").

285. See *Licari*, 22 F.3d at 344.

286. See *Bruce Church*, 397 U.S. at 142.

287. See *Lucas*, 505 U.S. at 1019.

resources existing within their natural state (i.e., before being withdrawn and incorporated into a product).²⁸⁸ The trade protection laws only apply to goods and products, not domestic regulation of real property, or the means of gaining access to a natural resource such as water.²⁸⁹ Thus, governments should focus their laws, as virtually all now do, on the administration of water rights and resource protection (e.g., restrictions on discharge of contaminants), rather than on restriction of trade in goods or products made with water resources. Laws of this type will be excluded from the trade protections set forth in NAFTA and GATT, while laws aimed at restricting trade in goods and products produced with water will fall under NAFTA and GATT.

B. Design and Administer Water Resource Laws to be Non-Discriminatory and Non-Arbitrary; Administration Should Afford Due Process

It is also important that the state's water rights administration and resource protection laws be administered fairly with respect to foreign investors so to avoid liability under Chapter Eleven, as well as U.S. due process requirements, the dormant Commerce Clause, and regulatory takings challenges. In application, this means that the laws should (a) be adopted and applied in a nondiscriminatory manner to avoid violations of NAFTA's Article 1102 (national treatment); (b) be administered in a non-arbitrary manner with ample due process to avoid violations of NAFTA's Article 1105 (minimal standard of treatment); and (c) avoid direct expropriations to evade liability under Article 1110 (expropriation compensation)

Specifically, to comport with these principles in relation to water resource regulations, the state should:

- establish an objective environmental or other public policy basis for the regulation (e.g. sustainable use, safe yield, flow regimes, riparian habitat, fishery index, satisfaction of competing in-state water needs, etc.);

- declare priorities and methodologies for the administration of the regulation;

- acknowledge and protect vested property rights so long as the property rights are exercised consistent with state laws and priorities;

- provide due process in the adoption of the regulations, including ample hearing and public input opportunities and written findings and reports to illustrate the rational public policy bases for the regulation; and

288. *See supra* Part V.

289. *See Id.*

provide ample due process protections in relation to the application of the regulations, including notice of hearings, open hearings, opportunities for protests and a means to resolve competing claims, and issuance of written findings of facts the rational basis justifying the determinations made.

Conversely, the state should avoid:

formulating water regulations that treat similarly situated foreign and domestic prospective users of water differently;

issuing a complete prohibition on foreign exports of water while permitting domestic water transfers or exports that would result in the same effect upon the public interest in water resources;

discriminating against foreign transfers by (i) charging a higher fee to transfer water across borders than is charged for transfers or use within the country unless such fees are cost justified; (ii) requiring legislative approval for transfers of water out of the country (where no legislative approval is required for domestic transfers); or (iii) taxing foreign transfers (where no tax is levied on in-state transfers or domestic transfers), unless the tax is justified on a cost basis; and

imposing restrictions upon the production and commerce in specific products that include water resources (e.g., bottled water and other beverages), unless it is shown in written findings that the production or commerce in the specific product presents a unique harm to the public interest that other products do not.

Because these considerations are also relevant to the validity of the state's water management laws under domestic United States law (e.g., due process protection, dormant Commerce Clause jurisprudence and the regulatory takings doctrine), most water resource management systems throughout the country already adhere to these principles, and thus should be immune from liability under Chapter Eleven's investor protections.

In point of fact, one NAFTA Chapter Eleven arbitration claim has been brought by an American company, Sun Belt Water, Inc. ("Sun Belt"), challenging a Canadian ban on certain bulk water exports from Canada.²⁹⁰ While the allegations of impropriety were significant, the claim was never actively prosecuted and appears to have been abandoned.²⁹¹ The claim arose from a competitive bidding process promoted by British Columbia and the Canadian federal government in 1991,

290. Sun Belt, Inc. v. Canada, Notice Intent to Submit a Claim for Arbitration (1999) [hereinafter Sun Belt] available at <http://www.naftaclaims.com> (accessible from homepage by selecting "The Disputes" then "Canada" then "Sun Belt" and then "Notice of Intent to Submit a Claim for Arbitration, 27 November 1998") (last visited Nov. 3, 2007).

291. There have been no filings in this case since October 12, 1999.

whereby Sun Belt was initially awarded a license to export water from British Columbia to California via marine tankers.²⁹² Sun Belt's complaint alleged that four days after Sun Belt was awarded the license, without notice the government of British Columbia announced a temporary moratorium on the export of water by marine transport vessel, and eventually the federal Canadian government imposed a permanent ban to the same effect.²⁹³ As a result, Sun Belt filed a NAFTA claim in 1998 alleging that the Canadian government had violated Articles 1102, 1103, 1104, 1105, and 1110.²⁹⁴

While the claim was never prosecuted beyond the filing of a Notice of Claim with the NAFTA tribunal, the allegations were that the initial moratorium on water exports was imposed by the Canadian government with the *specific intent* of benefiting a Canadian company at the expense of Sun Belt, and that Sun Belt was denied redress by the Canadian courts.²⁹⁵ Sun Belt further alleged that Canada's failure to compensate Sun Belt, despite its compensation of a similarly situated Canadian partner, constituted a breach of the national treatment provisions of Art. 1102.²⁹⁶

Most important for our purposes here, at no time did the case implicate the legality of Canadian resource management laws. Rather Sun Belt sought relief from what it alleged were patently discriminatory preferences for a Canadian company under Article XI. Thus, had the case been prosecuted to completion and had Sun Belt prevailed, the case would not have suggested any deviation from the point here: that non-discriminatory water resource management laws implemented with appropriate due process will not result in any liability under NAFTA.

C. A Present Day Example: The Great Lakes Agreement and Compact

As a present example of regulatory approaches that are aimed at protecting water resources against exploitation, consider the Great Lakes-St. Lawrence River Basin Sustainable Water Resources Agreement ("Agreement") and the Great Lakes-St. Lawrence River Basin Water Resources Compact ("Compact"), which were signed by Great Lakes Governors and Canadian Premiers on December 13, 2005.²⁹⁷ The

292. *Sun Belt*, *supra* note 290 at II. ¶ 15.

293. *Id.* at II. ¶ 16.

294. *Id.* at I. A.

295. *Id.* at II. ¶¶ 25-34.

296. *Id.*

297. Great Lakes-St. Lawrence River Basin Sustainable Water Resources Agreement, Dec. 13, 2005, [hereinafter Agreement], available at <http://www.cglg.org> (accessed from homepage by selecting "Projects" then "Great Lakes Water Management" then "Great Lakes-St. Lawrence River Water Resources Regional Body" then "Agreement" and then "English") (last visited Nov. 3, 2007); Great Lakes-St. Lawrence River Basin Water Resources Compact, Dec. 13, 2005, [hereinafter Compact], available at <http://www.cglg.org> (accessed from homepage by selecting "Projects" then "Great Lakes

Agreement represents an effort by the Great Lakes States, Ontario and Québec to address common water resource management challenges. The Agreement is to be implemented in Ontario and Québec through Provincial laws, and in the United States, through the Compact, an agreement among the Great Lakes States that is proposed for enactment as an interstate compact.²⁹⁸ The Compact is now being considered for adoption by the respective legislatures of the member states.²⁹⁹

Collectively, the Agreement and Compact detail how the States and Provinces intend to manage and protect the Great Lakes-St. Lawrence River Basin (“Basin”) from exploitation and provide a framework for each State and Province to enact laws protecting the Basin.³⁰⁰ Among other things, the Agreement and Compact (i) ban new diversions of water from the Basin, subject to limited exceptions, (ii) set forth consistent standards that the States and Provinces will use to review proposed diversions of Great Lakes water for intra-Basin use; (iii) provide for the collection and sharing of technical data to improve decision-making by the governments; and (iv) set forth regional goals and objectives for water conservation and efficiency programs that will be adopted by the States and Provinces.³⁰¹

Much of the Agreement and Compact is focused on developing resource-based protections to ensure the sustainable use of the resource. For example, the Agreement and Compact require that each Province and State adopt a program for the management and regulation of new or expanded water withdrawals and use to ensure that such withdrawals and use do not cause significant harm to the Basin’s waters or related natural resources.³⁰² These management and regulation programs will likely take the form of water rights management laws, which are well within the states’ reserved authority in recognizing and regulating water rights in accordance with the police power.³⁰³ Again I emphasize that water rights management laws are not affected by NAFTA’s and GATT’s trade protections laws because such laws govern the use of an interest in real property and not a product.³⁰⁴ Accordingly, there should be no risk in the

Water Management” then “Great Lakes Agreement and Compact” then “Agreement and Compact” and then “English”) (last visited Nov. 3, 2007).

298. See, e.g. Agreement, *supra* note 297; Compact *supra* note 297.

299. As of November 2007, only Minnesota and Illinois had enacted the compact. Legislation to enact the Compact was introduced in Michigan, Illinois, Ohio and Indiana. For status of enactments see <http://www.csg.org/programs/ncic/GreatLakes-St.LawrenceRiverBasinWaterResourcesCompact.aspx> (last visited Nov. 10, 2007).

300. See, e.g. Agreement, *supra* note 297; Compact, *supra* note 297.

301. See Summary of Agreement and Compact available at <http://www.cglg.org> (accessed from homepage by selecting “Projects” then “Great Lakes Water Management” then “One Page Overview”) (last visited Nov. 3, 2007).

302. Agreement, *supra* note 297, at art. 206; Compact, *supra* note 297, at § 4.10.

303. See *supra* Part IV(B).

304. See *supra* Part III(A).

adoption of fairly-applied implementing regulations that provide the customary protections for the management of a state's water resources.

One of the more publicized features of the Agreement and Compact is the prohibition on bulk water diversions from the Great Lakes Basin in containers larger than 5.7 gallons.³⁰⁵ States are free to treat withdrawals in smaller containers as they see fit.³⁰⁶ Regulations prohibiting diversions of water from the Great Lakes Basin through pipelines are exempt from the trade protections of NAFTA and GATT because such regulations simply govern withdrawal and conveyance of water, which are fundamental features of water rights. Again, because water rights management laws govern interests in real property rather than goods and products, NAFTA's and GATT's trade protection provisions, by definition, do not apply.³⁰⁷

Efforts to prohibit exports of water in "containers" presents a more complex inquiry in relation to NAFTA and GATT's applicability, one that will largely depend upon whether the water and container are a "product" or "good," or whether the container instead functions only as a physical means of conveyance of the water. As I have noted *supra*, a shipment of water through large tankers may be viewed as simply another means of diversion and conveyance, no different than a pipeline conveying water to its end beneficial use.³⁰⁸ In such a case, the diversion and conveyance by tanker are not a "product" or "good," but rather, means of conveyance. As such, they are subject to the state's reserved power to grant permission in accordance with the public interest, and to regulate water rights as interests in real property.

Bottled water and other beverages, by comparison, are undisputedly goods and products under NAFTA and GATT.³⁰⁹ Because NAFTA and GATT expressly prohibit the imposition of restrictions on the export of products,³¹⁰ a ban of water exports in any container that constitutes a product would constitute a ban on trade in a "product" to which these trade protections apply.³¹¹ In such cases, whether a ban on an export of a particular product is permissible turns not on the state's authority to manage its water resources, but on whether the ban qualifies for one of the stated exceptions under GATT Chapter XX, subsections (b), (g) and (j), respectively.³¹² Whether such a defense would be successful would

305. Agreement, *supra* note 297, at art. 207, ¶ 9; Compact, *supra* note 297, at §§ 4.8, 4.12.10. Exceptions to this general prohibition are set forth in § 4.9.

306. Agreement, *supra* note 297, at art. 207, ¶ 9; Compact, *supra* note 297, at § 4.12.10.

307. See *supra* Part III(A).

308. See *supra* Part V(D).

309. See *supra* notes 9 and 158.

310. NAFTA, *supra* note 14, at art. 309; GATT, *supra* note 36, at art. XI; see *supra* Part V(B).

311. See Harmonized Commodity and Coding System Code, *supra* note 142; at § 22.01.09 (listing bottled water as a product).

312. See *supra* Part V(D).

likely depend on the factual showing regarding whether the measure was appropriately tailored to the protection of health and safety during a condition of low supply, an effort to protect an exhaustible resource, or to preserve a product in a condition of scarcity.³¹³

It should be noted that the Agreement and Compact exclude from the definition of diversion “Water that is used in the Basin or a Great Lake watershed to manufacture or produce a Product that is then transferred out of the Basin or watershed.”³¹⁴ Thus, products manufactured with water (including bottled water³¹⁵) are excluded from the Agreement and the Compact’s bans on diversion regardless of whether the product includes a container greater than 5.7 gallons.

Although the Agreement and Compact do not ban exports of bottled water from the Great Lakes Basin, some critics of the 5.7-gallon or less exception within the Agreement and Compact—the so called “bottled water exception”³¹⁶—have urged the legislatures within their respective states to go further and ban exports of bottled water, regardless of bottle size.³¹⁷ However, such an action would actually serve to weaken a state’s potential defenses available under NAFTA and GATT by eliminating any argument that the regulation properly considered obvious differences arising from the size of the container and the volumetric impact associated with the withdrawal on the resource. It would also surrender the argument that the 5.7-gallon or less exception was a reasonable effort to draw the line between the characterization of certain containers as products, subject to NAFTA and GATT, and other larger con-

313. *See supra* Part V(E).

314. Agreement, *supra* note 297, at art. 103; Compact, *supra* note 297, at § 1.2. Both the Agreement and Compact define diversions as “a transfer of Water from the Basin into another watershed, or from the watershed of one of the Great Lakes into that of another by any means of transfer, including but not limited to a pipeline, canal, tunnel, aqueduct, channel, modification of the direction of a water course, a tanker ship, tanker truck or rail tanker but does not apply to Water that is used in the Basin or a Great Lake watershed to manufacture or produce a Product that is then transferred out of the Basin or watershed.” *Id.*

315. *See* discussion, *supra* notes 9 and 158.

316. The so called “bottled water exception” is not truly an exception because bottled water, which is a product, is not covered by definition of “diversion” within the Agreement and Compact. *See supra* note 314.

317. *See, e.g.*, Memorandum from Jodi Habush Sinykin, Of Counsel, Midwest Environmental Advocates, to John Stolzenberg and Rachel Letzing, Wisconsin Special Committee on the Great Lakes Compact, Recommendations Regarding Treatment of Bulk Water Transfers and Bottled Water for Inclusion in a Legislative Council Option (Dec. 6, 2006), available at <http://www.legis.state.wis.us> (accessed from homepage by holding the mouse over “Joint Legislative Committees” and selecting “Joint Legislative Council” then holding the mouse over “Committees” then holding the mouse over “Study Committee” then selecting “2006 Interim” then “Great Lakes Water Resources Compact” and then “Recommendations Regarding Treatment of Bulk Water Transfers and Bottled Water for Inclusion in a Legislative Council Memo”) (last visited Nov. 3, 2007); PETER ANNIN, THE GREAT LAKES WATER WARS 235-37 (Island Press 2006).

tainers that are only a means of diversion and conveyance, not subject to NAFTA and GATT.³¹⁸

Even if a ban on export of bottled water could pass muster as a proper police power measure exempt from NAFTA Chapter Three and GATT Articles III and XI, such a ban would still be subject to scrutiny under Chapter Eleven of NAFTA.³¹⁹ For example, the ban could run afoul of Articles 1102 and 1105 of NAFTA, which respectively mandate national treatment (i.e., non discrimination) and minimum standards of treatment of foreign investments.³²⁰ This is not an insignificant challenge. Distinguishing between containers of 5.7 gallons or less and larger containers *might* be explained as an impact-based regulation. However, once again, the total ban suggested by the critics would effectively undercut this defense as well.

In application, the amount of water bottled and exported may have virtually no detectable impact upon the water resource at issue.³²¹ Thus, a blanket export prohibition of water in all containers, purportedly as a measure to protect water resources, could be found to be an arbitrary law in that it does not rationally relate to the public purpose cited as the basis for the law.³²² The exemption for smaller containers is an implicit recognition that resource protection can be compatible with low-impact uses such as bottled water, and may be an attempt to distinguish them from methods of bulk diversion and conveyance.

Similarly, a complete ban could also be deemed discriminatory, in violation of Articles 1102 and 1105 of NAFTA, if it were to only govern the export of bottled water but not the export of other water-containing beverages. From a resource-protection standpoint, a law that restricts exports of bottled water, but not soda and other flavored water, beer, wine, etc. would almost surely be deemed discriminatory and arbitrary.³²³ Obviously, depending upon size, location and other circumstances, a soda or beer manufacturing business may bottle far greater quantities of water and cause far greater resource and environmental impacts, than a bottled water plant. Thus, such a ban, which applies to pure water in a bottle but not water with sweetening and coloring in a bottle (e.g., soda), would likely be considered arbitrary and discriminatory in

318. Agreement, *supra* note 297, at art. 207, ¶ 9; Compact, *supra* note 268, at § 4.12.10.

319. This statement assumes a foreign investor would be impacted.

320. NAFTA, *supra* note 14, at arts. 1102, 1105. *See infra* Part VI.

321. *See* general discussion, *supra* note 43.

322. *See supra* Part V(D); *Shrimp-Turtle*, *supra* note 168. *See, e.g.*, GATT Panel, *United States — Restrictions on Imports of Tuna*, 30 ILM 1594 (1991) (holding that US ban on Mexican tuna violated the “primarily aimed at such a conservation” condition set out by a former Panel decision when interpreting the “relating to” condition in Art. XX (g) GATT, because of the discriminatory manner in which the United States implemented the measure).

323. GATT, *supra* note 36, at art. XX; NAFTA, *supra* note 14, at arts. 1102, 1105.

that it discriminates between manufacturers of similar products without any apparent public purposes for such discrimination.³²⁴

In sum, under any formulation, a state's prospects of surviving challenges under NAFTA and GATT would become worse, not better, if the state were to regulate beyond the Agreement and the Compact, and ban exports of water in all containers of any size. Such a complete ban would overtly burden trade and commerce, and would not be "narrowly tailored" to promote the public policy it seeks to promote. Consequently, a state would be far better served to direct its focus to formulating water rights management laws that are tailored to protect the Basin's waters and related natural resources consistent with the Agreement and Compact.³²⁵

VIII. CONCLUSION

As explained in this article, NAFTA and GATT do not threaten to undermine water resource management, as alleged by some. The trade protections set forth in Article III and XI of GATT and Chapter Three of NAFTA apply only to products and goods, and have no application to water rights, which are a form of real property interest, or water within its natural states, which is part of the land and a common public resource. Water resource management, which is largely the province of state authority, is not threatened by NAFTA or GATT. In fact, the state's power to grant permission to use its resources, recognize property rights in water and to regulate that use in accordance with the police power is largely undiminished in the free trade agreement era.

Each state remains free to apply even-handed water management laws as it deems appropriate. The scrutiny applied to water withdrawal and use will continue to stem from the water management system employed by each state. While some states largely depend on common law water rights regimes, enforced principally by the courts, others have opted for permitting programs that include individual and specific review of each proposed withdrawal and use.

NAFTA's Chapter Eleven does set forth provisions that protect individual investors and investments, including those that may be made in water resources. However, as explained, these protections generally track similar protections already afforded under United States law, notably due process protections, dormant Commerce Clause prohibitions on restraints of interstate trade, and regulatory takings jurisprudence. Thus, water resource laws that comport with domestic law within the United States should not yield liability under NAFTA's Chapter Eleven.

As I have sought to explain in Part VII above, designing and applying valid water resource laws that will sustain a Chapter Eleven chal-

324. See GATT, *supra* note 36, at art. XX.

325. See *supra* Part VII(C).

lenge is not difficult and is rather intuitive from a fairness perspective. Laws should focus on protection of water resources, rather than arbitrarily discriminating against certain products made with water. Laws should be adopted and applied with due process protections (e.g., proper notices, hearings, fact-based decision-making, etc.) Likewise, laws cannot be applied arbitrarily and must treat domestic and foreign entities alike (i.e., cannot discriminate), although disparate effects of an evenly applied resource protection law will be allowed. Again, these parameters are largely the same as those already required by United States law.

Thus, policy makers should not fear that NAFTA, GATT, or any other trade or commerce protection law will jeopardize water resource laws which are administered fairly upon all participants. Legislative efforts should focus on the adoption and application of even-handed laws that will ensure the protection and sustainable use of this critical resource.