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Court of Appeals Finds Diversion for Endangered Species To Be Physical Taking

In Casitas Municipal Water District v. United States, Case No. 2007-5153 (Fed. Cir. 2008), the Court of Appeals for the Federal Circuit held that when the government causes water to be diverted from a reclamation project for the benefit of an endangered species, the diversion is a physical taking of property that is per se compensable under the Fifth Amendment of the US Constitution. (See Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 [1982] {when government physically occupies property, a per se taking occurs for which compensation is due}). The Casitas ruling revives the jurisprudence of physical takings with respect to water rights while adding to it a new level of complexity. By bringing the issue of physical takings back into legal relevance, Casitas has the potential to significantly affect federal mandates applicable to water users throughout the United States.

The dispute in Casitas arose out of California’s Ventura River Project, built by the Bureau of Reclamation (BOR) in the 1950s and operated by the Casitas Municipal Water District (CMWD). The project diverted water from the Ventura River to Casitas Lake, among other operations. In 1997, the National Marine Fisheries Service (NMFS) listed the West Coast steelhead trout as an endangered species. In 2003, after consulting with the BOR under section 7 of the Endangered Species Act (ESA), NMFS produced a Biological Opinion that determined the project’s diversion of water from the Ventura River jeopardized the endangered steelhead trout. To avoid a violation of the ESA’s section 9 “take” provision, the BOR mandated that CMWD build a fish ladder and divert up to 3,500 acre-ft of water per year from the project for the ladder. CMWD built the facility and diverted the water, then brought suit against the government in the Federal Court of Claims, claiming both breach of contract and a taking of property in violation of the Fifth Amendment.

The lower court ruled that the mandate on CMWD to divert water from the Ventura River Project to the fish ladder was not a physical taking for which compensation was automatically due. The Court of Appeals overruled the lower court, explaining that the BOR’s mandate “actually caused the physical diversion of water away from the Robles-Casitas Canal—after the water had left the Ventura River and was in the Robles-Casitas Canal—and toward the fish ladder, thus reducing CMWD’s water supply” (Casitas at 26). The court viewed the physical rediversion of water away from the CMWD after the water had been diverted from the river as a critical factor, distinguishing it from a circumstance in which the government simply restricted CMWD’s diversion from the river in the first place. From the court’s perspective, this distinction brought the case under a line of cases in which physical diversions of water by the government were held to be per se physical takings of property, including: International Paper Co. v. United States, 282 U.S. 399 (1931) (United States stopped Interna-
tional Paper from diverting water from the power company's canal for use in its mill); United States v. Gerlach Live Stock Co., 339 U.S. 725 (1950) (United States caused water to be physically diverted from the San Joaquin River, depriving claimants of their rights to its use); and Dugan v. Rank, 372 U.S. 609 (1963) (the United States' storing of water above Friant Dam left insufficient water in the river to supply claimants' water rights).

The government argued that the diversion of water away from Casitas Lake was merely a restriction on use and should be analyzed under the ad hoc balancing test laid out in Penn Central Transportation Co. v. New York City, 438 U.S. 104 (1978). Under that standard, courts look at several factors in determining whether a compensable taking exists, including the economic impact of the regulation on the claimant, the extent to which the regulation has interfered with "distinct investment-backed expectations," and the character of the governmental action (Penn Central, 438 U.S. at 124). The Court of Appeals rejected the government's Penn Central argument, repeatedly stating that unlike a noncompensable regulatory taking, in which the government merely restricts a property owner's use of property, here the government "actively caused water to be physically diverted away from Casitas..." (Casitas at 22, 26, 28, and n.16). As a result, the majority concluded that the Penn Central balancing analysis was not the proper legal test for the circumstances at hand.

Although the result in Casitas may be meritorious, the underlying rationale of the court's opinion raises several questions. The court stated repeatedly that the government's liability arose from its requirement that water be physically diverted from CMWD's facilities. It left open the question of whether a physical taking would arise if the BOR simply forced CMWD to leave water in the river. The lone dissenting judge in the 2–1 ruling seized on this distinction, arguing that the majority's approach elevates form over substance, permitting "self-selected methods of regulatory compliance [that] can be manipulated and negotiated to arrive at preferred Fifth Amendment results" (Casitas at 39). For the dissent, whether water is left in the river or redverted back to the river is immaterial, because the result is the same in both cases and "should not lead to a difference in the characterization of the activity" (Id.).

The issues raised by Casitas are similar to those addressed by Judge John P. Wiese, the trial court judge in Casitas, in an earlier case, Tulare Lake Basin Water Storage District v. United States, 49 Fed. Cl. 313 (2001). In Tulare, Judge Wiese concluded that because water rights by nature are usufructuary rights (i.e., the full scope of the entitlement and their value is in the right to use a given quantity of water), any restriction on water use was a physical, not a regulatory, take. As Judge Wiese explained in Tulare, "[i]n the context of water rights, a mere restriction on use—the hallmark of a regulatory action—completely eviscerates the right itself since plaintiffs' sole entitlement is to the use of the water" (Tulare, 76 Fed. Cl. at 319). Judge Wiese held that the loss of even a portion of the usufructuary right results in a "complete extinction" of the value of that portion of the plaintiff's right, representing an "occupation" of the right to use the water by the government and thus a physical taking (Id.).

In reaching this determination in Tulare, Judge Wiese reasoned that the manner by which the government restricts a right holder's supply is irrelevant, because it is the end result that matters: "whether the government decreased the water to which plaintiffs had access by means of a dam or by means of pumping restrictions amounts to a distinction without a difference" (Id. at 320). In other words, the federal government's elimination of a water right–holder's ability to use a water supply to which it has a right under state law is a taking of that use right, no matter how the restriction is imposed.

Although the Casitas court went to great lengths to distinguish physical diversions by the government and restrictions on the diversions of rights holders, it refused to revisit Tulare and decide whether the character of the government's action creates a meaningful distinction (See Casitas at 28 n.16).
Federal Court of Claims Takes Different Approach Than *Tulare*

A case subsequent to *Tulare* from the Federal Court of Claims—*Klamath Irrigation District v. United States*, 67 Fed. Cl. 504, 538 (2005)—took a different approach than *Tulare*. In *Klamath*, the court determined that the question of whether the government had infringed on the rights holders’ property rights in violation of the US Constitution was not relevant, because the water deliveries were dependent on contractual rights, not property rights. The court found that it was a contract case and that no takings claim could be based on the fact. Because the contracts incorporated the provisions of the Endangered Species Act (ESA), the *Klamath* court concluded that no breach of contract had occurred.

Unlike *Klamath*, underlying water rights were at issue in the *Casitas* case described earlier. The application of the physical takings doctrine to the usufructuary water right is an evolving area of the law. It is questionable whether the distinction identified by the majority in the *Casitas* opinion, which focuses on the manner of the government’s restriction, is the appropriate analysis, rather than an analysis that focuses on the entity imposing the restriction and the legal basis of that restriction.

In general, water rights are created, defined, and regulated by state law. In California, rights to appropriate surface water—like the rights at issue in *Casitas*—are granted by permit (or license) from the State Water Resources Control Board (SWRCB). Modern permits and licenses include conditions that provide that the appropriative right may be reviewed, reduced, or modified to protect public interests, including environmental demands. For example, modern SWRCB permits are conditioned on the demands imposed by Fish and Game Code 5937, which requires that dam operators allow sufficient water to pass through their facilities to keep fish in good condition. The public trust doctrine provides another basis for the state to limit property rights as it balances competing public interests. (See *National Audubon Society v. Superior Court of Alpine County*, 33 Cal.3d 419 [1983]). Moreover, Article X, section 2 of the California Constitution, which requires that the waters of the state “be put to beneficial use to the fullest extent of which they are capable,” also imposes constraints on state-granted water rights.

On these grounds, a strong case may be made that the state, acting through the SWRCB, may restrict usufructuary rights to protect in-stream uses without incurring takings liability so long as the conditions and state laws are applied fairly. However, this was not the case in *Casitas*. The federal government did not seek to have the SWRCB amend the *Casitas* Municipal Water District’s license to divert water from the Ventura River. Instead, it unilaterally required the district to forgo the use of water to which it was entitled under state law. Under such circumstances, a compelling case may be made that the federal government has physically taken an otherwise valid state-granted right and used it for a federal purpose, thereby incurring per se liability pursuant to the physical takings doctrine.

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Founded in 1968, the law firm of Brownstein Hyatt Farber Schreck practices in the areas of real estate, natural resources, public policy, corporate law, and litigation. Although the firm has played an integral role in water issues for the past decade, its recent merger with the California firm of Hatch & Parent has made it a dominant US law firm in the area of water law and policy. For more information about the firm’s water group, contact Mark Mathews at mmathews@bhfs.com or (303) 223-1179 or Stephanie Osler Hastings at shastings@bhfs.com or (805) 882-1412. To visit the firm’s website, go to www.bhfs.com.