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Methods and Challenges in the Credible Valuation of Water Rights in Texas

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*I believe that this is as much about the taking away of a lifestyle as it is about the decrease in the value of land. The Braggs invested their lives, labor and money in a good family farm . . . That life plan has been undermined, and their investment severely devalued.*²

Many Texans, when asked, profess confusion about how to identify their water rights, what government entities regulate those water rights and, of utmost importance, the true market value of the water they own. Everyone believes their water rights have value, but few have experienced the sale of those water rights. There is no Multiple Listing Service or "MLS" available similar to residential property sales markets to allow both buyers and sellers to instantly find true, reliable comparable sales in water transactions. Similarly, there is no "Blue Book" for guidelines on how to value automobiles. To begin the process of valuing a water right for sale or lease, the buyer, seller and/or lender must gain a fundamental understanding of the water rights to be sold or otherwise affected. This process includes the identity of the person or entity who owns the water, what regulations apply, if any, and any other limitations that may impact the ability to transfer the water to the purchaser or lessee, and what process is required to close a sale or lease of the water right. A thorough investigation must be undertaken to determine the credible, defensible fair market value of water. This can be an especially challenging task irrespective of the methodology used.

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² Retired District Judge Thomas Lee, Hondo, Texas, May 7, 2010. From his ruling in *Bragg v. Edwards Aquifer Authority*, May 7, 2010 in *Glenn and JoLynn Bragg v. Edwards Aquifer Authority*; Cause No. 06-11-118170-CV in the 38th District Court of Medina County, Texas

When it comes to water valuation, the commonly heard saying that “water is the next oil” is fundamentally flawed. Unlike oil, which is a truly finite resource that is only renewable over millennia, and is intended to be mined by the highest bidder, water is a renewable resource that can be conserved and, ideally, allocated fairly. Certainly, water has real value; it has been said, “water renders the land its value.”³ This is particularly true especially in most farm and ranch real estate transactions. To begin to discover an answer to what is the credible, defensible valuation of water and/or water rights proposed to be sold or conveyed, it is important to understand some basics about water ownership and applicable regulations.

A Brief Water Primer

Water rights in Texas vary between water flowing on the surface and water percolating underground. They can also vary from regulatory agency to regulatory agency, as well as from place to place, and from time to time. A good example of the “conventional wisdom” that water rights in Texas are convoluted and, at times in the recent past, incomprehensible, is found in a ruling in 1955 made by Federal Judge James V. Allred, a former attorney general and governor of Texas. Allred wrote,

For years it has been a matter of common knowledge that the Texas water laws and decisions are in hopeless confusion; that even if they are clear as some attorneys profess to believe them, their application and administration would be difficult ...⁴

When a well-known jurist such as Judge Allred expresses confusion and frustration with our water laws and decisions, ***in a published decision nonetheless***, it is understandable why the general public may share his feelings. Still today, few Texans understand the wider view of the legal, social, and economic consequences of our State's water rights systems.

Water rights are the most fundamental “stick” in the “bundle of sticks” that determine all the “property rights” and much of the market value of any real property in Texas. Real estate simply sells at higher prices when it is (i) adjacent to surface water, (ii) has access to surface water irrigation diversion rights, and/or groundwater irrigation rights, or (iii) overlies bountiful amounts of fresh potable groundwater. In many instances, the prices for such real estate are many multiples higher than comparable land without adequate water.

Why else is it important to know about water rights in Texas? In addition to the significant impact water rights have on the value of real property, statutory obligations burdening the use of such water resources have created a need to understand water rights because all known defects in real property must be disclosed to any potential purchaser during the time the purchasers are making their decision to buy. This “duty” to disclose any defect known, *including a known defect in a water right*, is shared by sellers, lessors, and their real estate agents. Buyers and lessees should be knowledgeable about the water rights associated with a property they are considering acquiring, and they must know what questions to ask about water rights in general.

The duty to disclose all known defects has become a part of our everyday real estate transactions in Texas and in most parts of the United States. As water becomes scarcer throughout Texas due to population growth and our inevitably recurring droughts, it has become imperative for

³ Letter from George W. Brackenridge to “Brother Tom” [his brother Thomas] recommending Thomas’ land in Junction, Texas should only be sold if it included the section with water on it, “as water render the land its value.” November 19, 1879. Austin History Center, Robert Thomas Brackenridge Papers, La Prella-Brackenridge Papers.

⁴ *Martinez v. Maverick County Water Control & Improvement District No. 1*, 1955, 219 F. 2d 666, 670 (5th Cir. 1955).

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