

0034

cc. Jim
Stowell
LJ
9/13/94 Bam
Bond file
07 07
TELEPHONE
(801) 363-4300
FACSIMILE
(801) 363-4378

PARSONS, DAVIES, KINGHORN & PETERS

A PROFESSIONAL CORPORATION
ATTORNEYS AT LAW

310 SOUTH MAIN STREET
SUITE 1100
SALT LAKE CITY, UTAH 84101

September 12, 1994

JOHN PARSONS
GLEN E. DAVIES
GERALD H. KINGHORN
BILL THOMAS PETERS
LANGDON T. OWEN, JR.
R. L. KNUTH
GREGORY L. PROBST
KEN P. JONES
DAVID W. SCOFIELD
JOSEPH T. DUNBECK, JR.
STUART W. HINCKLEY
RONALD F. PRICE

HAND-DELIVERED

Thomas A. Mitchell
Assistant Attorney General
Utah Division of Oil, Gas & Mining
3 Triad Center, Suite 350
Salt Lake City, Utah 84180-1203

Re: In re Sunnyside Coal Company
Sunnyside City and East Carbon City

Dear Tom:

During last Friday's meeting with Mr. Burnham and Ms. Dragoo, you asked for a letter explaining the claims of our clients, Sunnyside City and East Carbon City, to surface water rights of Grassy Trail Creek. We have three theories which establish our clients' ownership of the Grassy Trail Creek water rights.

First, under the Memorandum Agreement dated September 17, 1951, Geneva Steel Company and Kaiser Steel Corporation agreed to jointly construct and operate the reservoir on Grassy Trail Creek and to use it to store and distribute the parties' surface water rights. The recitals to the Memorandum Agreement state, in part:

WHEREAS, the parties desire to jointly build, own, maintain, repair and operate a storage reservoir and appurtenant works on Grassy Trail Creek and to improve, repair, maintain and operate certain existing facilities of Kaiser on Range Creek to the end that the water available for use under the water rights hereinafter more particularly described of Geneva, Kaiser, Galbreath, and K&F shall be utilized without regard to ownership or priority date to meet present and increasing demands for domestic water in the East

Thomas A. Mitchell,
Assistant Attorney General
September 12, 1994
Page 2

Carbon County Area and to provide for the allocation of water during periods of shortage on a fair and equitable basis,

Of particular note is Article 4 which dedicates the use of the parties' water to common use:

The parties hereto agree that all water rights subjected to this Agreement will remain the separate property of the owner contributing the same, but all water which accrues during the life of this Agreement under any or all of said water rights will be available for joint use as provided herein. All such water will be reserved for use in and utilized to supply the Domestic Use of the East Carbon County Area including the mines, plants, commercial establishments or other facilities of Kaiser, Geneva, K&F and Galbreath, in East Carbon County and Emery County. . . .

Although Article 15 of the Memorandum Agreement specifies that Geneva shall own a 61.2% undivided interest in the reservoir and appurtenant works and that Kaiser will own the remaining 38.8%, Article 7 of the places all of the Grassy Trail Creek facilities of both Kaiser and Geneva under their joint control. Article 16 provides that the Grassy Trail Creek facilities will be jointly used until one of the parties cancels it on thirty days' written notice. However, if the Memorandum Agreement is so cancelled,

. . . the party terminating this Agreement shall be conclusively deemed to have abandoned any ownership or interest in the reservoir and appurtenant works on Grassy Trail Creek and in all water stored therein, without further act of the parties, but the party so terminating shall at the request of the other party execute an appropriate instrument quitclaiming its interest therein to the other party. After such termination, the party so terminating shall have no right to use said reservoir and appurtenant works, except as herein in this Article 16 otherwise provided. (Emphasis supplied).

Likewise, the parties agreed, in Article 2, that any after-acquired direct-flow or storage rights in Grassy Trail Creek would also be subject to the provisions of the Memorandum Agreement. Article 2 further provides that

PARSONS. DAVIES. KINGHORN & PETERS

Thomas A. Mitchell,
Assistant Attorney General
September 12, 1994
Page 3

In the event of termination of this Agreement as provided in Article 16 hereof, any water rights on Grassy Trail Creek, other than the water rights of Galbreath and K&F set forth in Article 1 hereof, acquired in any fashion after the date of execution of this Agreement by the party terminating this Agreement shall, at the option of the remaining party, be sold to said remaining party at the cost of the acquisition of the same.

Finally, Article 20 of the Memorandum Agreement makes the agreement binding on the parties' successors and assigns.

The Memorandum Agreement was supplemented by a second Memorandum Agreement, dated January 3, 1952 between Kaiser Steel and Kaiser & Frazier Parts Corporation (K&F). Under this second agreement, K&F agreed to store its direct flow rights in Grassy Trail Creek in the reservoir for distribution according to the terms of the September 17, 1951 Memorandum Agreement.

In the early 1980's, the City of East Carbon obtained title to the Geneva rights, which are the most senior rights on Grassy Trail Creek, rights 91-360 and 91-363 and several more junior rights. As successor to Geneva, all these rights East Carbon acquired are subject to the Memorandum Agreement of September 17, 1951.

Our position is that the 1951 Memorandum Agreement burdens the Grassy Trail Creek water rights of Kaiser and Geneva, that the agreement binds their successors, and that it has never been terminated. Contrary to Ms. Dragoo's recollection, the February 27, 1989 order of the bankruptcy court in the Kaiser bankruptcy which permitted Sunnyside Reclamation to purchase Kaiser's water rights, specifically approved the purchase of Kaiser's rights under the Memorandum Agreement. Accordingly, the Memorandum Agreement survived the Kaiser bankruptcy.

The Memorandum Agreement was recorded and so, under Utah law, gives constructive notice to all, including Sunnyside Coal and the State of Utah when the water rights were pledged as collateral for the reclamation obligation. The Memorandum Agreement created a separate interest in these water rights and the debtor's title to the water rights cannot be improved by the mere fact of transfer and cannot pass to a bona fide purchaser free of the servitude, whether it be the State or a purchaser from Sunnyside

Thomas A. Mitchell,
Assistant Attorney General
September 12, 1994
Page 4

Coal's estate. These rights must continue to be available for use by the Cities jointly with the other water users in the area, wherever legal title might reside.

Any cancellation of the Memorandum Agreement automatically results in loss of the water rights to the other party or its successor, now East Carbon City. Sunnyside Coal has expressly repudiated the Memorandum Agreement, has ceased to use the reservoir or the water rights and the cities have long ago assumed sole responsibility for operating the reservoir and the water rights it stores, and East Carbon asserts that it is already vested with full ownership of the reservoir, the diversion works and the water rights by operation of Article 16.

Second, Sunnyside asserts its ownership by estoppel. After the bankruptcy of Kaiser Coal Company and the sale of the mine to Sunnyside Coal's predecessor, Sunnyside Reclamation and Salvage, the mine operator repeatedly promised to donate sufficient water rights to operate Sunnyside City's municipal system. In an April 4, 1989 letter from W. P. Balaz to the mayor of Sunnyside City Sunnyside Reclamation promised to donate 415 acre-feet per year to Sunnyside City, an amount calculated to be sufficient for the City's present municipal needs, with some left over for modest growth. SR&S valued the water at \$150.00 per acre-foot, a total of only \$62,250.00.

In reliance on that promise, Sunnyside City specifically cancelled a request for a block grant which would have enabled it to condemn those same water rights at the price Sunnyside Reclamation placed on them. After repeated assurances that the donation would be made, and after cancellation of the block grant on March 5, 1992, Mr. Balaz's successor wrote to the Mayor of Sunnyside and repudiated the promise to donate. As stated in that letter, SR&S's water rights had been included in the Trust Deed and Security Agreement, dated March 9, 1989, the security for Sunnyside Coal's reclamation obligations to the State of Utah. Trusting in the promise to deed the water rights to the City, Sunnyside made a number of concessions to the coal operations which it would not have made in the absence of the promise. Sunnyside City also exercised forbearance in moving to condemn the water rights, and in foregoing an opportunity to acquire a community development grant for this purpose. Sunnyside suffered detriment as a result of its justifiable reliance on Sunnyside Coal's promise when that source of funding subsequently became unavailable.

When the Division learned of the promised dedication of water rights to Sunnyside City, Sunnyside Coal persuaded the mayor of Sunnyside to send a letter to the Division, (dated May 10, 1993), acknowledging that the water is encumbered by the State's trust deed

Thomas A. Mitchell,
Assistant Attorney General
September 12, 1994
Page 5

and expressing the City's interest in acquiring the water; Mayor Wakefield was apparently told that without such a disclaimer from the City, the mine, upon which the City so heavily depended, would be shut down. That "repudiation" was invalid for reasons which will be discussed below.

Third, when Kaiser conveyed away the homes and other land in Sunnyside City in the late 1970's, it did not include any reservation of water rights in the deeds to either Sunnyside City or the individual homeowners. In Utah, a water right which has historically been used to benefit land becomes an appurtenance to the land, passing to the grantee in the absence of an express reservation in the instrument of conveyance. Roberts v. Roberts, 584 P.2d 378, 379-80 (Utah 1978). This common law rule was embodied in Utah Code Ann. Section 73-1-11, which states:

"A right to the use of water appurtenant to land shall pass to the grantee of such land . . . ; provided, that any such right to the use of water, or any part thereof, may be reserved by the grantee in any such conveyance by making such reservation in express terms in such conveyance, or it may be separately conveyed."

Thus, a deed such as those Kaiser gave to the City of Sunnyside and the people who purchased their homes from the company conveys, along with the land, whatever right the grantor has to water which has become appurtenant to that land. Anderson v. Hamson, 167 Pac. 254 (Utah 1917). As a result, when the property passed to the various householders and to Sunnyside City, they received a proportionate share of the Grassy Trail Creek water historically serving that land. Those water rights have been in open and notorious use since the property was conveyed away without reservation.

Finally, we have been told that the debtor and the State rely on the letter from Sunnyside's mayor as an acknowledgment that the City has "repudiated" any claim of an interest in the debtor's water rights. This contention overlooks the express provisions of Article XI, Section 6 of the Constitution of Utah:

"No municipal corporation, shall directly or indirectly, lease, sell, alien or dispose of any waterworks, water rights, or sources of water supply now owned or hereafter to be owned or controlled by it; but all such . . . shall be preserved, maintained and operated by it for supplying its inhabitants with water at reasonable charges: . . ."

PARSONS, DAVIES, KINGHORN & PETERS

Thomas A. Mitchell,
Assistant Attorney General
September 12, 1994
Page 6

Our Supreme Court has interpreted this constitutional provision to invalidate any voluntary alienation, direct or otherwise, of a city's water rights. Nephi City v. Hanson, 779 P.2d 673 (Utah 1989). Even assuming that the May 10, 1993 letter from Sunnyside's mayor was authorized by the City Council (which it was not), any attempt by the City to give away an interest in a water right would be ineffective and both the debtor and the State were on notice of the constitutional proscription.

I hope the foregoing has adequately explained our clients' position. As we stated in our meeting last week, the Cities must litigate this issue as far as will be necessary, since a failure to prevail would leave the Cities with little or no water supply to serve their inhabitants, an untenable result.

Kindest regards,

PARSONS, DAVIES, KINGHORN & PETERS



R. L. Knuth

RLK:rf

Enc.

cc: Mayor Grant McDonald
Mayor Paul Clark
Denise A. Dragoo,
Attorney at Law