

EXHIBIT 6
DATE 1.27.05
NO. 298

I. INTRODUCTION

Pursuant to Section 85-2-436(3)(a), MCA, the Montana Department of Fish, Wildlife, and Parks must complete and submit to the Department of Natural Resources and Conservation (DNRC), the Fish and Wildlife Commission (Commission), and the Environmental Quality Council (EQC) an annual water leasing study progress report. The report must include specific information for each lease including:

- (i) **the length of the stream reach and how it is determined;**
- (ii) **technical methods and data used to determine critical streamflow volume needed to preserve fisheries;**
- (iii) **legal standards and technical data used to determine and substantiate the amount of water available for instream flows through leasing of existing rights;**
- (iv) **contractual parameters, conditions, and other steps taken to ensure that each lease in no way harms other appropriators, particularly if the stream is one that experiences natural dewatering; and**
- (v) **methods and technical means used to monitor use of water under each lease.**

FWP completed one new lease agreement (for two leases) in 2004 - on Trail Creek in the Clearwater River basin. The Water Program has prepared the DNRC Change Application for these leases. DNRC also issued a Change Authorization for a lease FWP entered in 2003, on Cedar Creek in the Upper Yellowstone Basin.

The progress report must also contain a summary of stream reaches approved by DNRC for study (pursuant to 85-2-437, MCA), and a summary of leasing activity on all designated streams. If no new leases have been obtained in the reporting year, FWP must "provide compelling justification for that fact" in the report. The remainder of this report has been divided into six sections and associated appendices, described as follows:

- Section II**—background on the creation of the leasing program,
- Section III** – our review of the 2004 leasing year, including new lease agreements, and general issues and opportunities noticed or arising in 2004,
- Section IV** – additional detail on the 2004 leasing activity, including the statutorily required reporting elements for each,
- Section V** – the statutorily-required reporting on the streams designated, so far, for study and potential leasing under FWP's leasing program; and,
- Section VI** – a selection of program goals for 2005.
- Appendix A** lists our leasing objectives, which is what we currently use to evaluate lease offers, and seek additional lease opportunities.
- Appendix B** provides a sample FWP lease evaluation, showing what information FWP needs and uses to evaluate lease offers under the criteria provided in Appendix A.
- Appendix C** provides monitoring information for FWP's existing leases/conversions.

II. WATER RIGHTS AND THE FWP WATER LEASING PROGRAM

Montana's water law has traditionally focused on the rights and procedures associated with diverting water from streams and lakes and putting that water to a beneficial use (e.g., irrigation, fish and wildlife, domestic, mining, etc.) away from the source. Persons who appropriate water from a stream must have a right or permit to do so. A right or permit specifies how much water can be diverted, for what purpose, during what time period, at what point on the stream, the location of the use of the water, and has a priority date assigned to it. The priority date determines who gets the water first; if there isn't enough to go around, the earliest date has the first claim (hence the maxim, "first in time, first in right").

Montana's Water Use Act encourages "*the water resources of the state ... be protected and conserved to assure adequate supplies for public recreational purposes and for the conservation of wildlife and aquatic life*" (85-1-1-1(5), MCA). It also seeks to "*provide for the wise utilization, development, and conservation of the waters of the state for the maximum benefit of its people with the least possible degradation of the natural aquatic ecosystems*" 85-2-101(3), MCA. Except in basins that are closed to new appropriation, the DNRC may issue new permits to divert surface water if the applicant can show (among other things) that water is reasonably available for the use proposed and that there is a means to ensure persons with senior rights can get the water to which they are entitled. There is no flow level where new appropriations are no longer granted. If water is physically available (even 1 in 10 years) and legally available (not claimed by senior water users) a permit can be issued. Generally, the system encourages maximum diversion and use of water from Montana's streams.

In the 1960's conservationists began to advocate for legal mechanisms to keep water instream. The 1969 Legislature passed "Murphy's Law" which allowed FWP to file instream flow claims on 12 blue ribbon trout streams. FWP was later authorized to apply for instream "reservations" to support fishery values. FWP pursued the authority to reserve water, and was granted a series of reservations in the Yellowstone basin (1978 priority date), the Missouri River basin above and below Ft. Peck (1985 priority date), and the Little Missouri basin (1989 priority date). Reservations are a valuable management tool, but due to their late priority dates they do not provide much drought relief.

In 1988, much of Montana suffered severe drought conditions. Low natural flows coupled with normal diversion rates exacted severe tolls on sensitive fisheries. Montana newspapers ran front-page photos of fish kills on dewatered streams. These conditions spurred the 1989 Legislature to consider additional tools and incentives for water users to protect fishery values. One highly controversial idea was to allow FWP to temporarily lease consumptive water rights for instream flows. The idea became a law, and since then FWP has pursued attractive leasing opportunities with willing lessors on seriously dewatered streams with high fishery restoration potential. The water leases are now making major contributions to select fisheries.

FWP's leasing statute was originally set to expire in 1989. It required the agency to prepare a final report of the leasing program to be adopted by the FWP Commission and DNRC. The report was then to be submitted to the EQC for completion by December 1, 1998. The EQC's Water Policy Subcommittee recognized its role in evaluating the leasing program. The EQC included a review of the program and related statutes in its 1997-98 Interim. The Subcommittee

conducted public review of the progress and acceptance of the program. The EQC eventually proposed legislation that would renew FWP's leasing statutes for 10 years, increase the cap on the number of FWP lease streams, increase the maximum lease period for certain leases, require another "final" report in 2008, and allow other leasing programs to lease salvaged water. Though the EQC was encouraged to be more aggressive in proposing changes (i.e., making the program permanent, removing the DNRC study stream approval requirement, etc.), the Council elected to act conservatively to ensure that the whole program wasn't lost. The EQC encouraged others during the 1999 Legislative Session "to use the legislative committee hearing and amendment process to further test the waters on additional changes to the DFWP's water leasing statutes" (EQC, 1998). The bill, as drafted, received overwhelming support in both houses, and was signed by the Governor on March 19, 1999. The EQC deserves credit for its long-term support of this program.

A summary of FWP's leasing history is provided in Figure 1.