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LOUIS F. RACINE (1917-2008)
WILLIAM D. OLSON, OF COUNSEL

May 28, 2008

Director David Tuthill
Idaho Department of Water Resources
P.O. Box 83720
Boise, Idaho 83720-0098

Re: Grand Teton Canal Company pilot project

Dear Director Tuthill:

Thank you for facilitating the Grand Teton Canal Company ("GTCC") pilot project, which seeks to develop an accounting mechanism to enable GTCC shareholders to store water in ponds. Your willingness to consider new means to improve water use and administration is much appreciated. On February 29, 2008 you established a work group that was instructed to define the details of the accounting and reporting procedures to be implemented by the pilot project. Unfortunately, certain IDWR personnel have attempted to take the project in a different direction that we find impractical, resulting in an impasse. The purpose of this letter is to request additional guidance from you as to how the GTCC pilot project will operate so we can move things forward. This letter is joined by Rob Harris and Jerry Rigby who represent various irrigation entities in Eastern Idaho that are very interested in and supportive of developing a solution to the problem addressed by the GTCC pilot project.

The GTCC pilot project was initiated in response to a problem commonly faced by canal company shareholders who want to create ponds on their property for irrigation, recreation, or aesthetic use. IDWR has not recently allowed canal companies to simply amend their water rights to add storage as an authorized nature of use. Instead, IDWR has required canal companies to transfer a discrete portion of their water right from irrigation to storage any time a shareholder desires to create a small pond. While canal companies typically have no problem

allowing shareholders to store water in ponds, they generally refuse to allow transfers of their water rights. The communal nature of canal company water rights makes it impractical to allocate discrete portions to individual shareholders, and the transfer procedure is often viewed as not being worth the hassle. Further, repeated dividing and sub-dividing results in fragmentation of canal company water rights and complicates delivery. As a result, canal companies typically refuse to allow transfers of their water rights which makes water available under canal company shares less flexible and valuable than individually owned water rights and creates significant impediments for persons interested in improving property irrigated under canal company shares.

Our intention with the GTCC pilot project was to create a means whereby shareholders could obtain authorization to use water available under their shares for storage in ponds without having to undertake a transfer of the Company's water rights each time a pond is installed. We believe this can be accomplished via a single transfer proceeding that would add storage for irrigation, recreation and aesthetic use as authorized natures of use of GTCC's water rights. The transfer would create alternate authorized uses of the Company's water rights but would not allow enlargement of use.

In order to protect against enlargement, we proposed that GTCC shareholders be required to dry up acres to offset or mitigate for the development and ongoing maintenance of ponds. GTCC would be required to keep an inventory of ponds created and corresponding acres dried up in order to ensure no enlargement. A complaint procedure would be available within the Company with an option for appeal to IDWR. This accounting and reporting process would enable flexible use of water available under GTCC shares without allowing the Company to increase its diversion or use of water. We understood that from the February 29 meeting that you support this proposal and that we were to work with the GTCC pilot project work group to define the details of the accounting and reporting procedures to be implemented. Enclosed is our letter to the GTCC work group dated March 14, 2008 which further describes the procedure we envisioned.

We have unfortunately reached an impasse with IDWR personnel regarding the design of the pilot project. Mr. Peppersack has informed us that he is unwilling to approve a mechanism of regulating pond development through accounting and reporting procedures. Instead we are told that GTCC will have to transfer some water from irrigation to storage, though Mr. Peppersack has offered to authorize a 5-year transfer process whereby GTCC would attempt to forecast pond development every 5 years at the end of which there would be a permanent transfer of water to storage.

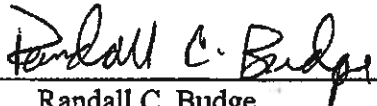
We do not believe that the 5-year transfer process proposed by Mr. Peppersack adequately addresses the problem faced by canal companies and their shareholders and that extended, repeated and often protracted transfer procedures are far less pragmatic than the accounting and reporting procedure we proposed. In short, the canal companies we represent find little if any benefit to the 5-year transfer proposal over the current method and are not interested in continuing the GTCC pilot project on those terms. Our clients remain very interested in developing an accounting and reporting procedure for regulating pond development. GTCC and others who may choose to follow their lead would of course be required to submit a

transfer application to authorize the storage use and add the accounting and reporting procedures as conditions.

Please advise whether we may proceed with developing the accounting and reporting procedures and intended and submitting a transfer application to add storage for irrigation, recreation, and aesthetic purposes as authorized uses of GTCC's water rights. We would be happy to discuss this matter in person or via teleconference at your convenience.

Best Regards,

**RACINE OLSON NYE BUDGE &
BAILEY, CHTD.**

By 
Randall C. Budge

**RIGBY THATCHER ANDRUS RIGBY
KAM & MOELLER, CHTD.**

By /s/
Jerry R. Rigby

**HOLDEN KIDWELL HAHN &
CRAPO, PLLC**

By /s/
Robert L. Harris

Cc: Grand Teton Pilot Project Work Group:
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March 14, 2008

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Re: Grant Teton Canal Company pilot project

Dear Folks:

Thank you for your participation in the IDWR pilot project involving Grand Teton Canal Company ("GTCC"). We represent Blackfoot Farms, LLC, which is a shareholder in GTCC and supports this project. This letter explains the objective of this pilot project and our proposed implementation plan for the project.

The objective of this pilot project is to develop a mechanism to provide flexible use of water by canal company shareholders to allow for irrigation and well as storage in ponds. Canal company water rights typically authorize water use for "irrigation" purposes only. If a shareholder wants to create a pond using water available under his or her shares, IDWR has in the past required the canal company to transfer a portion of its underlying water rights from "irrigation" to "diversion to storage" to reflect the shareholder's pond. Requiring a transfer each time a pond is installed creates administrative burdens and over time results in fragmentation of the canal company water rights from repeated dividing and subdividing.

Canal companies generally have no problem allowing shareholders to store water in ponds so long as other shareholders are not injured by it. In our case, GTCC and Blackfoot Farms entered into an agreement to allow the use of water under Blackfoot Farms' shares for storage in ponds. While canal companies generally have no problem allowing flexible water use by shareholders, companies are often resistant to fragmenting their underlying water rights. Because of the communal nature of canal company water rights, it is impractical to allocate discrete portions of canal company water rights to individual shareholders. The result is that canal companies often refuse to allow a transfer of their water rights to facilitate a shareholder's use of water available under his or her shares to create ponds. This makes water available under canal company shares less flexible and valuable than individually owned water rights and creates significant impediments for persons interested in improving property irrigated under canal company shares.

A solution to this problem is to add "storage" as an additional authorized uses of the canal company water rights without requiring a transfer each time a pond is created which would result in burdensome and unnecessary fragmentation of the water rights. Our proposal is for GTCC to file a single transfer application to simply add storage as an authorized use of the company's water rights without partitioning the quantity between each use. The result is that both irrigation and storage would be authorized under the same rate of diversion. This would not allow the canal company to increase its diversion or use of water; it would simply create flexibility by permitting irrigation and storage as alternate authorized uses of GTCC's water rights.

In order to effectively protect against injury to other water users, procedures must be implemented to account for water use in ponds which will be reported annually to IDWR. The purpose of forming this work group is to develop accounting and reporting procedures that will adequately protect other water users when a GTCC shareholder desires to install a pond using his or her shares. The goal is to ensure that water use during and after implementation of the pond is no greater than water use prior to implementation of the pond. We believe that this can be accomplished via the following procedures.

1. Initial Fill of Pond. The shareholder first determines the volume and location of the proposed pond. During the irrigation season of the initial fill, the shareholder would be required to dry up irrigated acres as necessary to fully offset or "mitigate" the initial fill of the pond. The number of acres to be dried up would be calculated using the consumptive use figures provided on the ET Idaho website for the Driggs station. Appendix A to this letter provides those figures and the formula for calculating acres to be dried up.

For example, if a GTCC shareholder desires to install a pond with a volume of 20 acre-feet, the shareholder would be required to dry up the number of acres necessary to eliminate 20 acre-feet of crop depletion during irrigation season when the pond is initially filled. The number of acres to be dried up depends on what has historically been grown. For instance, if grass hay had historically been raised (depletion of 2.1 ac-ft/ac), approximately 10 acres would need to be dried up to mitigate for the initial 20 ac-ft fill of the pond. The precise number and location acres to be dried up would be pre-determined by the shareholder and reported to GTCC, which would include the identified acres in its annual report to IDWR.

2. Ongoing Maintenance of Pond Volume. Once the pond is filled, water will be depleted from the pond annually through evaporation. Therefore, the shareholder will also be required to permanently dry up the number of acres necessary to offset ongoing pond depletion.

Appendix A shows depletion for shallow water systems, deep water systems, and small stock ponds. You will note that depletion for nearly all crop types is greater than depletion for all pond types. Therefore, if the pond is located on acres previously irrigated then there will likely be no need to dry up acres in addition to those covered by the pond itself. However, if the pond is located on land not previously irrigated, or if the pond type causes greater depletion than the historic crop type (for example, a small stock pond on property historically utilized to grow spring grain), then the shareholder would be required to permanently dry up additional acres as necessary to offset pond depletion.

The precise number and location of acres to be permanently dried up to mitigate for pond depletion would be pre-determined by the shareholder and reported to GTCC, which would include the permanently dried up acres in its annual report to IDWR.

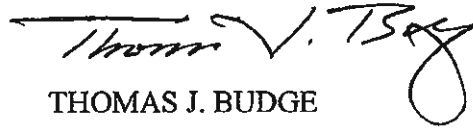
3. Application to GTCC. Any shareholder who desires to install a new pond using GTCC shares would be required to apply to GTCC for authorization. The application must include a map and drawings of the proposed pond with its dimensions, together with a map of the acres to be dried up to mitigate for the initial fill and ongoing maintenance. GTCC can require a reasonable fee for processing the application. GTCC would have discretion to determine whether to allow the use of its water rights for the proposed pond.

4. Annual Report to IDWR. GTCC would be required to submit an annual report to IDWR prior to the irrigation season demonstrating the locations and dimensions of all ponds served by GTCC water rights, together with a map of all acres taken out of production for the irrigation season. We anticipate that the report would identify existing ponds, new ponds to be

brought on line, and acres dried up to mitigation for the initial fill and ongoing maintenance of the pond.

Please review the above procedures and consider additional details that may improve this pilot project. Once the details for the proposed accounting procedure are ironed out, GTCC will file with IDWR an application for transfer to add storage as an authorized use. We would like to schedule a teleconference to discuss this project sometime during the week of March 24-March 28. Please let me know by email when you are available during those dates.

Best Regards,

A handwritten signature in black ink, appearing to read "Thomas J. Budge". The signature is stylized with a large, looping "B" and a long horizontal stroke at the beginning.

THOMAS J. BUDGE

APPENDIX A

GRAND TETON CANAL COMPANY CONSUMPTIVE USE VALUES

Values taken from the ET Idaho website for the Driggs Station
<http://www.kimberly.uidaho.edu/ETIdaho/stninfo.php?station=102676>

CROP TYPE	Consumptive Use (mm)	Consumptive Use (Acre-Feet Per Year)
Alfalfa - peak	785	2.6
Alfalfa - frequent cuttings	679	2.2
Alfalfa - less frequent cuttings	667	2.2
Grass Hay	627	2.1
Spring Grain - Irrigated	542	1.8
Winter Grain - Irrigated	570	1.9
Grass Pasture - high management	629	2.1
Grass Pasture - low management	494	1.6
Grass - Turf (lawns) - Irrigated	583	1.9
Open Water - shallow systems	476	1.6
Open Water - deep systems	130	0.4
Open Water - small stock ponds	621	2.0
POND VOLUME CONVERSION		
Crop Type: Alfalfa - peak		
Proposed Pond Volume (In Acre-feet)	Consumptive Use (Acre-feet Per Year From Table Above)	Acres to Dry Up for Pond Fill (Proposed Pond Volume / Consumptive Use)
20	2.6	7.7