Rights of the Surface Owner

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Rights of the Surface Owner v. Mineral Owner

• Once mineral rights are severed from the surface estate, the mineral estate becomes the dominant estate and the surface estate becomes the servient estate.

  • This legal principle recognizes that some degree of surface access is necessary in order to develop the mineral estate.

• Because of its dominance, the mineral estate holds an implied easement to use as much of the surface as reasonably necessary for the development of the mineral estate.
Rights of the Surface Owner v. Mineral Owner

• “Reasonable use” extends to a wide variety of oil and gas related activities, including drilling of wells and the building of roads, pipelines, electric lines, as well as storage and processing facilities and the usage of large amounts of water.

• “This right includes the legal privilege to use the surface in a way that interferes with the surface owner’s use of the land and that significantly damages the surface, without the legal obligation to make any compensation whatsoever.”

  — Ernest E. Smith
Are You Truly Protected?

- Increasingly, mineral interest is severed from the surface estate and held by a trust entity or limited partnership.
- While beneficial for taxation and organizational purposes, this may unintentionally create a situation where the surface owner lacks control over the negotiation of leases and surface use agreements.
- Family trusts and partnerships may hold a legal duty to favor mineral production and could be forced to make decisions that are to the detriment of the surface estate.
- This scenario highlights the need for minimum statutory protections for the unprotected surface owner.
Are You Truly Protected?

Many surface owners believe that reserving executive rights associated with the property gives them absolute control over the leasing process and surface use protections.

However, recent case law makes it clear that the duty to non-executives may interfere with the executive’s ability to trade lease benefits for surface use protections.

- Initially, courts punished executives for self-dealing that resulted in disproportionate financial benefits for the executive.
- *Lesley v. Veterans Land Board* demonstrates that executives are also liable when reducing lease benefits in return for surface protection enhancement.

Consider negotiating a separate lease covering the non-executive minerals, then bargain for surface use protections in return for concessions on benefits held only by the executive.
What is a Surface Use Agreement?

• A Surface Use Agreement (SUA) is a contractual agreement between the surface owner and the oil and gas operator, included as a separate exhibit or incorporated into the terms of the oil and gas lease.

• Make sure the SUA runs with the lease and will survive any assignment or sale to a third party.

• The SUA can give the Surface Owner influence over:
  • Location and size of infrastructure and roads
  • Remediation of the surface
  • Use of surface water and groundwater resources
  • Practices designed to minimize disturbance of farming and ranching
  • Monetary damages paid to the Surface Owner
How do I get one on my property?

• The Surface Owner’s power to negotiate and obtain a surface use agreement will depend upon the ownership and leasehold status of the property.
• Perform a baseline evaluation to determine the following:
  • 1. Are the minerals leased or unleased?
  • 2. What portion of the mineral estate is held by the Surface Owner?
  • 3. Who owns severed mineral interest beneath the property?
    • How much does each party own, and how fractured is ownership?
  • 4. Has drilling and/or production of oil and gas already occurred on the property? Is it active?
  • 5. If a lease is in place, what surface protections are outlined in the lease?
The “Preemptive SUA”

- The owner of an interest in the mineral estate is free to enter into a contractual agreement regarding protection of the surface, even if made prior to the severance of minerals and/or the negotiation of an oil and gas lease.

- Prior to the conveyance of minerals into a separate entity, consider agreeing to a covenant outlining minimum surface use protections for future leases.
  - This covenant can include the duty to seek upgrades to existing lease terms when presented with the opportunity.

- If the mineral estate is already severed, negotiate a preemptive surface use agreement to be used by the severed mineral owner in future leasing transactions.
What if the Surface Owner owns little or no mineral interest in the property?

- If there is no lease burdening the property, the surface owner will be reliant upon the severed mineral owners to negotiate surface protections.
  - Consider purchasing mineral rights, and reach out to severed mineral owners to establish a good relationship before the leasing offers start to arrive. Make sure they understand the need for surface protections in future oil and gas leases.
  - Negotiate a “Preemptive SUA” with expected surface protections before development begins.

- If a lease is already in place, look to the terms of the lease for available surface protections.
  - The operator will have no legal obligation to negotiate a SUA with the surface owner in this scenario.
  - The surface owner can only rely upon statutory protections enforced in its particular state.
Damages and Remediation

• Absent an agreement to the contrary, Texas law provides no duty for an operator to reclaim and restore the surface estate of the property once operations conclude.

• Lessee should have an obligation to fully restore and remediate any damage to property at its sole expense, regardless of the fair market value of the property to be restored or remediated.

• Require that the lessee obtain certain levels of insurance protection so that the cost of restoration will be covered under its policies, and have the surface owner named as an additional insured party under the policies.
Indemnity and Environmental Indemnity

• Lessee should indemnify, defend, protect and hold harmless surface owner and associated parties from all liens, claims, demands, costs, expenses, attorneys’ fees, damages, losses and causes of action for injury to persons or property.
  • This indemnification should extend to surface owner’s concurrent or contributory negligence and strict liability.

• Many leases fail to extend the lessee’s indemnity to liability and costs resulting from hazardous materials or the violation of federal environmental laws.
  • The lessee must assume all liability and expenses related to environmental hazards and catastrophic events such as spills or blowouts.
Temporary Damages v. Permanent Damages

• **Temporary Damages** are those which do not last a long time, are not ongoing, are not likely to reoccur, or occur sporadically and unpredictably
  • Damages = cost of repair/remediation

• **Permanent Damages** continue indefinitely or for a very long time, and cannot be repaired/remediated, or are substantially certain to reoccur
  • Damages = loss in fair market value
Temporary Damages v. Permanent Damages

- Keep in mind that damages will be limited to the fair market value of the portion of the property to be restored, not the value of the entire ranch.
- With regard to permanent damages, the fair market value of the property will be fixed at the time of the damage, and the increase in property value will be counted against the landowner when determining damages at trial.
- Landowners also face significant hurdles with respect to the four-year statute of limitations and the limited scope of the discovery rule.
- Perform a baseline appraisal of the property prior to mineral development so that fair market value and damages can be proven in the even of an accident.
Primrose Operating Company, Inc. v. Senn

• Owners of $4M ranch brought suit against operator for soil contamination from salt water leaks and spills on 10 acres of the property

• The jury awarded the cost of removing and replacing the damaged soil, estimated at $2,000,000

• On appeal, the court ruled that restoring the land to its prior condition was “not economically feasible” because it was in excess of the value of the portion of the ranch to be restored

• Therefore, the measure of damages will be the diminution of fair market value when the cost of restoration is not economically feasible
  • This applies even when damages are temporary in nature!
Wheeler v. Enbridge Pipelines, L.P.
449 S.W.3d 474 (Tex. 2014).

• Enbridge cleared a large number of valuable trees in violation of its pipeline easement agreement with Wheeler.

• The jury awarded $300,000 to Wheeler for restoration damages.

• On appeal, the Texas Supreme Court reduced the restoration award to $3,000, based upon the diminution in the fair market value of the damaged property.

• When temporary damages grossly exceed the diminution in market value, the damages are deemed to be permanent and the “economic feasibility” exception will apply.
Lazy R Ranch v. ExxonMobil

• Landowner sued Exxon and sought injunction to prevent further seepage of hydrocarbons and benzene into its groundwater supply

• Trial court determined that the statute of limitations had already elapsed with regard to the landowner’s claims

• Appellate court reversed and remanded, deciding that the statute of limitations did not apply to a request for an injunction to prevent damage from an ongoing nuisance

• What if the cost of complying with the injunction exceeds the fair market value of the property to be restored?

• The Texas Supreme Court has agreed to hear this case
Other Remedies: Texas Railroad Commission

- The Texas Railroad Commission has priority with regard to oversight of damages resulting from oil and gas operations.

- The Memorandum of Understanding (RRC Rule 30) between the TCEQ and the RRC, updated in 2012, gives the RRC jurisdiction over matters that would normally be governed by the TCEQ:
  - This amounts to a special exemption for all oil and gas operations in the State of Texas.

- Railroad Commission remedies often amount to nominal fines and generous deadlines for compliance:
  - Penalties for damage to water resources, livestock and crops will be assessed by an industry-friendly organization.
Other Remedies: The Accommodation Doctrine

• Courts require application of the accommodation doctrine when the surface owner proves “there is an existing use by the surface owner which would otherwise be precluded or impaired, and where under the established practices in the industry there are reasonable alternatives available to the lessee whereby the minerals can be recovered.”

• Courts further require that the Surface Owner prove “there is no reasonable alternative method available to the surface owner by which the [surface owner’s] existing use can be continued.”
Other Remedies: The Accommodation Doctrine

• Courts have ruled that the surface owner’s protected “existing use” can include a planned future use for development or use of the property.

• However, this will require sufficient evidence and paperwork supporting the planned future use.

• Make sure that your future plans for the property are documented and backed by an investment substantial enough to prove your intent in court.
Merriman v. XTO Energy, Inc. 407 S.W.3d 244 (Tex. 2013)

- Surface Owner sought an injunction when XTO began construction of a gas well location on property where the Surface Owner engaged in periodic cattle ranching activities.

- Surface Owner argued the well would interfere with existing locations used for temporary corrals and livestock pens on the property.

- The Texas Supreme Court ruled that the Surface Owner failed to prove he had no reasonable alternative for location of cattle pens on the property.
Surface Damage Statutes

- Almost all states with extensive oil and gas development have adopted some form of legislation to protect and compensate surface owners faced with development on their property.

- These statutes typically prescribe a procedure for contacting and negotiating with surface owners prior to the beginning of operations.
Typical Elements of a Surface Damage Statute:

- Required Notice to Surface Owner
- Good Faith Attempt to Negotiate Damages
- Bonding Requirements
- Payment for Damages to Land and Crops
- Prescribed Method for Determining Damages
- Penalties for Non-compliance with Statute
- Statute of Limitations for Claims
- Possible Payment for Diminution in Value of Property
Surface Damage Statues are compatible with development

- Bakken Shale (North Dakota & Montana)
- Niobrara Shale (Colorado & Wyoming)
- Permian Basin (New Mexico)
- Woodford Shale, Granite Wash (Oklahoma)
- Marcellus Shale (West Virginia, Pennsylvania)

- Statutes protecting surface owners have no demonstrable impact upon mineral development.
Oklahoma Surface Damage Act

• Operator must provide notice to surface owner prior to entry on the property
• The parties must enter into good faith negotiations to determine change in fair market value of the surface that will result from the operator’s planned activities
• If the parties cannot agree, the operator must post a bond and the parties will appoint appraisers
• Jury trial and subsequent appeal is available
• Treble damages awarded for failure by operator to follow prescribed procedure; attorney’s fees available in limited circumstances
New Mexico Surface Owners’ Protection Act

• Operator must provide written notice and a proposed SUA at least 30 days prior to commencement of operations

• Compensable damages include loss in property value, agricultural income, improvements and value of use

• If no agreement is reached after 30 days, operator may post bond and continue with operations

• Surface owner has option to appeal proceeding to state district court for resolution
Texas has no Surface Damage Act!

- Despite its emphasis on private property rights, Texas is the only major oil and gas state without statutory protections for surface owners.

- The operator owes the landowner no compensation unless it engages in unreasonable or negligent use of the surface.

- Application of the accommodation doctrine is rare.

- Without an interest in the mineral estate, the surface owner is generally powerless to negotiate meaningful surface protections with an oil and gas operator.
Surface Protections: Preferred Terms
SUA Provisions: Damages and Performance

• Specify agreed amounts for damage payments for all impacts constructed by operator on the property:
  • Well locations
  • Surface locations, tank batteries and other facilities
  • New roads
  • Pipelines
  • Water lines
  • Electric lines
• The size of damage payments will depend upon the particular property and location
• Seek a contractual lien on the operator’s working interest in order to secure performance of SUA obligations
• Expressly provide that liquidated damage amounts are in addition to all other remedies available to Surface Owner
Surface Use Agreements: Spills
SUA Provisions: Drilling Locations

• Modern technology allows for the drilling of multiple horizontal wells from the same drilling pad, which greatly reduces fractionation of property

• Consider constructing berms or visual screening where drilling locations interfere with open space and views

• Require the operator to reduce the size of the drilling pad once the well is completed or plugged as a dry hole

• In order to encourage smaller and consolidated drilling locations, require payment per acre of land used

• Require a pipe fence or other barrier capable of turning livestock
Multiple Well Drilling Locations:

- Vertical Oil Wells: Up to 16 locations per Section
- Horizontal Oil Wells: 1-2 locations per Section
Drilling Pad
5 acres
SUA Provisions: Frac Ponds

• Limit usage to the storage of fresh water only
  • Prohibit storage of produced water, drilling mud, or any other type of fluid in the impoundment

• Require a design sufficient to be used for livestock and wildlife operations once no longer used for the operator’s activities
  • Reserve the option to elect for reclamation and restoration of the pond area at Surface Owner’s discretion

• Operator must construct and pay for fencing sufficient to prevent livestock and wildlife from entering the pond area
SUA Provisions: Required Coordination and Planning

- Require a quarterly or annual Plan of Operations from the operator:
  - Containing details for all operations planned or contemplated by operator during the next period of operations
  - Approved of in writing by both operator and Surface Owner
  - Including an updated map of the property displaying existing and planned locations, pipeline, roads, electric lines, etc.

- Use “Oil Field Corridors” to consolidate operator’s facilities and access routes along the exterior of the property or other desired area
Oil Field Corridor
SUA Provisions: Access, Gates and Fences

• Allow access to the property only at points of ingress and egress designated by the Surface Owner
• Require that all gates remain locked except for when in active use during entry and exit
  • Can also require that gates be left in condition they are found
• Define the specifications and materials for gates and cattleguards to be installed by operator
  • Give the Surface Owner the option to elect for removal
• Prohibit the operator from accessing portions of the property near homes, livestock operations and hunting areas
SUA Provisions: Roads

- Surface Owner should expressly retain the power to designate access points and existing roads for use by operator
- Require that new roads be limited to one road to each location
  - Require coordination on road construction plans
  - Operator must be made solely responsible for repair, maintenance and erosion control
  - Define preferred construction techniques and materials
  - Limit the width of roads and frequency of vehicle turn-outs
Key Operating & Equipment, Inc. v. Hegar
435 S.W.3d 794 (Tex. 2014)

- Texas Supreme Court ruled that if property is pooled with other tracts to create a pooled well unit, the operator can use one property as a means to access any other property within the pooled unit, unless otherwise prohibited by the lease or SUA.

- The permission of the landowner is not required, and heavy flow-through traffic can result.

- Prohibit the operator, its employees and contractors from entering by one gate and exiting by another gate.
SUA Provisions: Pipelines

- Pipelines are used instead of trucks to transport oil, gas, produced water and fresh water, thereby removing potential traffic from the property.
- Require that the operator and Surface Owner agree on locations prior to the beginning of construction.
- Limit the duration of time for construction and usage of temporary workspace outside of the easement.
- Make the operator use the “double-ditching” technique to preserve topsoil.
- Provide for removal of pipelines by the operator when the lease expires or the lines are no longer in use for a specified period of time.
SUA Provisions: Pipelines

- Be sure to limit easement agreements to one pipeline along a specified route described by metes and bounds and depicted on a plat
- Require inspection and negotiation of damages for trees to be removed from and near the easement
- Define the permitted substances that may be transported through the pipeline
- Limit or prohibit appurtenant surface facilities such as valve sites, pig launchers and compressor sites
- Require sound abatement at locations where operations may produce excessive noise
SUA Provisions: Groundwater Usage

- In Texas, the surface estate owns a real property interest in the groundwater beneath the property.
- This right to pump groundwater may be subject to state regulation through groundwater conservation districts or by other means.
- The surface owner must make provision in the SUA for water sales to the operator; otherwise, the operator will have free access to as much water as desired.
SUA Provisions: Water Wells

- Give the surface owner the option to take over the lessee’s water wells at the conclusion of lessee’s use.

- Beware of taking control of an “exempt” well without first obtaining a permit from the local conservation district for your intended uses, if necessary.

- Require the operator to register and permit water wells in the surface owner’s name.
SUA Provisions: Water Usage

Absent an agreement otherwise, oil and gas operators have the right to use water from water wells and from surface resources free of charge.

- In Texas, this includes the right to completely exhaust certain water resources on the property!
  - *Sun Oil Co. v. Whitaker, 483 S.W.2d 808 (Tex. 1972)*

- Surface protections in the lease must address usage of surface water and groundwater by the lessee.
Coyote Lake Ranch, LLC v. City of Lubbock, 2016 Tex. LEXIS 415 (Tex. 2016)

- The City of Lubbock purchased the severed groundwater rights beneath Coyote Lake Ranch and proposed to drill a number of groundwater wells for its municipal supply.

- Coyote Lake sought an injunction to prevent City of Lubbock’s extensive use of the surface estate.

- The Texas Supreme Court ruled that the accommodation doctrine applies to the owner of the severed groundwater estate.

- This means that the owner of severed groundwater rights holds an expansive right to use the surface in the same manner as an oil and gas operator, unless agreed otherwise.
Priority of Severed Estates

• What are the implications of the Coyote Lake decision with regard to the rights of severed mineral owners?
  • The surface owner has the right to drill water wells for exempt uses such as domestic and livestock purposes.
  • The owner of the severed groundwater estate has the right to reasonable use of the surface for the development of groundwater resources.
  • The mineral lessee holds the right to use as much groundwater as reasonably necessary to develop the minerals beneath the property.

• Are there any conflicting rights in this situation?
  • Which party has priority to groundwater and use of the surface?
Water Usage: Hydraulic Fracture

- Each horizontal well fracture simulation ("stage") is similar to fracture treatment for one vertical well
- The amount of water per frac will depend upon:
  - the total length of the lateral wellbore
  - the number of stages (now up to 40+ per well)
  - Particular characteristics of the shale formation
- This will require millions of gallons of water per horizontal well
Frac Operation
SUA Provisions: Livestock

- Require operator to assume liability for any quarantine or similar government action arising from the operator’s actions or omissions
- Set defined monetary penalties for death or injury to particular type of livestock on the property
  - Should include fair market value of the animal and/or the cost of replacement
- Keep speed limits on all roads no higher than 20-25 MPH
- Require that operator and Surface Owner consider livestock and ranching operations when contemplating development activities
- Provide for a set monetary penalty for each time a gate is found unlocked or unopened
- Make operator responsible for costs resulting from intermingling of livestock
SUA Provisions: Agricultural Operations

• Reserve the right to concurrent use of the surface estate, so long as no unreasonable interference with Lessee’s operations

• Have the Lessee expressly acknowledge that the property is used for agricultural (or ranching, wildlife and hunting) purposes

• Designate active agricultural operation areas as off-limits for oil and gas development and related infrastructure

• Address calculation of damages for harvested crops and loss of potential value of growing crops
SUA Provisions: Reclamation

• Consider the slope and topography of the property in order to prevent runoff and erosion

• Require that all surface locations be restored to their prior condition and original contours within a specified period of time

• Have the operator segregate and stockpile topsoil for usage in later surface reclamation projects
SUA Provisions: Reclamation

• Designate native seed varieties for reseeding of the property
  • If desired, allow Surface Owner to conduct reseeding and be reimbursed by operator
• Use geo-textile materials or wooden drilling mats to lessen the impact of pad construction
• Ban the use of soil sterilization practices
• Designate preferred method for brush control
• Require washing of equipment before entry
Drilling Pad Reclamation:
July 7, 2013
Drilling Pad Reclamation: July 7, 2014

“Reclamation is a process, not a project.”
Wooden Mats
Geotextile Materials

Stockpiling of Topsoil
Reclaimed Drilling Pad
Pipeline Trenching
Pipeline Reclamation: Before
Pipeline Reclamation: After
Consolidation of Operations along Existing Roads
Erosion Mats
Screening Techniques
Monitoring Reclamation
Questions?

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