

Fiscal impact reports (FIRs) are prepared by the Legislative Finance Committee (LFC) for standing finance committees of the NM Legislature. The LFC does not assume responsibility for the accuracy of these reports if they are used for other purposes.

Current FIRs (in HTML & Adobe PDF formats) are available on the NM Legislative Website (legis.state.nm.us). Adobe PDF versions include all attachments, whereas HTML versions may not. Previously issued FIRs and attachments may be obtained from the LFC in Suite 101 of the State Capitol Building North.

FISCAL IMPACT REPORT

ORIGINAL DATE 2/14/2007
 LAST UPDATED 2/26/2007 HB 827/aHHGAC/aHENRC

SPONSOR Nunez

SHORT TITLE Surface Owners Protection Act SB _____

ANALYST Schuss

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY07	FY08		
	NFI		

(Parenthesis () Indicate Expenditure Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From

Department of Agriculture (DOA)

Attorney General's Office (AOG)

Energy, Mineral and Natural Resources Department (EMNRD)

Department of Environment (DOE)

SUMMARY

Synopsis of HENRC Amendment

The House Energy and Natural Resources Committee amendment does the following:

- redefines "surface owner" to read, a person who holds legal or equitable title, as shown in the records of the county clerk, to the surface of the real property on which *the operator has the legal right to conduct oil and gas operations;*
- clarifies compensation of damages to the surface owner to include, *damages sustained by the surface owner, as applicable, for loss of agriculture production and income, lost land value, lost use of and lost access to the surface owner's land and lost value of improvements caused by oil and gas operations. The payments contemplated by this section only cover land affected by oil and gas operations.*
- adds a new Subsection to Section 4 to read, *the operator and the surface owner may enter into a mutually acceptable agreement that sets forth the rights and obligations of the parties with respect to the surface activities conducted by the operator.*

Synopsis of HHGAC Amendment

The Health and Government Affairs Committee proposed amendment to HB 827 adds a new Section to make the Surface Owners Protection Act applicable to private fee surface land; and leasehold interests in any land on which oil and gas operations are conducted when the tenant incurs damages to leasehold improvements as a result of oil and gas operations.

The amendment also removes the section that provides for a statute of limitations. The statute of limitations was six years in the original bill.

Synopsis of Original Bill

House Bill 827 creates the “Surface Owners Protection Act”, which establishes the duties and requirements to which oil and gas operators and surface landowners must adhere to negotiate surface access agreements and determine compensation for property damages from oil and gas operations. HB 827 provides for oil and gas operator bonding in certain circumstances and provisions limiting the applicability of the Surface Owners Protection Act for maintenance and ongoing production activities related to an existing oil or gas well and for oil and gas operations conducted within the scope of a surface access agreement entered into prior to July 1, 2007. HB 827 also contains provisions for attorney’s fees and costs for prevailing parties in court actions and treble damages if the court finds actions to be knowing and willful.

FISCAL IMPLICATIONS

HB 827 would apply to the state as a surface owner, it is possible that the state would receive additional revenues in the form of compensation for surface use and surface damages from oil and gas operation on state lands where the minerals are owned by the United States or private parties.

SIGNIFICANT ISSUES

HB 827 would set out a process under state law requiring:

- Oil and gas operators to compensate surface landowners for the use of a surface landowner’s property and any damages sustained as a result of oil and gas operations.
- Oil and gas operators to compensate tenants of surface landowners for any leasehold improvements by repairing or replacing the improvements damaged as a result of oil and gas operations.
- Oil and gas operators to reclaim all surface lands directly affected as a result of oil and gas operations.
- Oil and gas operators to notify landowners in advance of contemplated oil and gas operations, provide specific information about the proposed operations and make an offer of compensation for the use of and damages to the surface resulting from the oil and gas operations.
- Specific timelines for surface landowners to take action on an oil and gas operator’s proposed surface use and compensation agreement.

- A mechanism for oil and gas operators to enter a surface landowners property without a surface use and compensation agreement if a surety bond, letter of credit, cash or certificate of deposit is posted with a surety company or banking institution. The surety bond, letter of credit, cash or certificate of deposit shall be for the benefit of and readily payable to the surface landowner for \$10,000 per well location or a \$25,000 blanket amount.
- A mechanism for providing attorney's fees and costs to surface owners in civil actions if the court finds that an oil and gas operator conducted operations without providing notice, outside of a surface use and compensation agreement without posting bonding or other surety, or operated outside the scope of an existing surface use and compensation agreement. Surface owners would also be liable for an oil and gas operators' attorney's fees and costs if they failed to exercise good faith in complying with the provisions of the Act or the terms of a surface use and compensation agreement. The court would also be able to assess treble damages if either the oil and gas operators or the surface owner's actions were knowing and willful.
- A statute of limitations for a surface owner to bring an action pursuant to the Surface Owners Protection Act within six years after the damage has been discovered, or should have been discovered, through due diligence, by the surface owner.
- Limits on the applicability of the Surface Owners Protection Act for maintenance and ongoing production activities related to an existing oil or gas well and for oil and gas operations conducted within the scope of a surface access agreement entered into prior to July 1, 2007.

ENMRD has included the following issues in their analysis:

Under common law (accustomed practice typically applied by courts in the absence of a statute), an owner or lessee of oil and gas has a right to use as much of the surface of the land as is necessary to explore for and produce minerals. The surface owner, absent a contrary agreement, is not entitled to compensation for loss of use of the portion of the surface necessary for mineral operations, nor for any diminution in the value of the surface due to such operations. The oil and gas producer is liable only for damages to the surface caused by its negligence, or by unreasonable or excessive use of the surface.

State law does not presently require prior notice of operations to the surface owner, or require security from the operator for damages that may accrue to the surface owner. Where, however, the mineral estate is owned by the United State, the United States Bureau of Land Management requires oil and gas producers give notice to the surface owner and either obtain a surface use agreement or post security prior to commencement of operations. BLM requires that an oil and gas operator file a statement that it has an agreement with the surface owner, or a bond, with BLM at the time the operator files its application for permit to drill. The bond amount is determined by BLM on a case by base basis and is usually from \$1,000 to \$5,000 per well location. Oil and gas producers in New Mexico typically pay surface damage settlements to surface owners prior to operations. There is, however, no legal requirement to do so.

HB 827 would put New Mexico in company with nine other states (Illinois, Kentucky, Montana, North Dakota, Oklahoma, South Dakota, Tennessee, West Virginia and Wyoming) that have modified the common law concerning an oil and gas operator's liability to surface owners by statute. The Act follows the general pattern of other states by providing surface owners a

right to compensation while allowing oil and gas operators access on prescribed conditions. Under the Act, the oil and gas operator could obtain immediate access by posting of a bond or other security in the amount provided, if the surface owner does not respond to the operator's proposal, or if negotiations are not successful.

Since the Act would apply to lands where the United States owned the minerals as well as to lands in State or private mineral ownership, an oil and gas operator drilling on federal mineral lands would, if it failed to secure a surface use agreement, have to comply with the bonding requirements of the Act as well as the existing BLM requirements described above.

TECHNICAL ISSUES

AGO states that Page 5, line 6: although the phrase “operator indemnification for injury to persons caused by the operator” can be presumed to require indemnification of the surface owner, it could be clarified to expressly so state.

ENMRD notes that the provision for notice to the surface owner to be sent to the address "shown by the records of the county clerk" [Page 5, lines 12 and 13] should be changed to the "records of the county tax assessor", since the tax office would ordinarily have more current and complete information regarding surface owner addresses. This change would be particularly important to surface owners since notice is deemed received under the Act five days after mailing, and the surface owner's time to accept a proposed surface use and compensation agreement runs from the date of deemed receipt. If notice were sent to an old address in a deed given at the time the surface owner acquired the property, the surface owner might not receive notice in time to take advantage of the offer, or might not receive the notice at all.

The bill requires the oil and gas operator to reclaim lands affected by its operations, but does not provide the measure of damages that the surface owner may recover if the operator fails to reclaim. Under general legal principles, if someone damages property, the property owner can recover no more than the value of the property prior to the damage, whereas if someone enters into a contract to reclaim property and does not do so, the property owner can recover the cost of reclamation, even if that cost exceeds the value of the reclaimed land. Since the act does not prescribe what amount a surface owner can recover, presumably this issue is left for the courts to resolve.

DOE states that the \$10,000 bonding in Subsection A of Section 5 is required for surface entry without an agreement by an oil and gas operator to an individual well location. However, there is not a clear purpose listed for the posting of a \$25,000 blanket bond in Subsection B of Section 5. The purpose of blanket bonding by the New Mexico Oil Conservation Division is to cover plugging and abandonment of multiple wells. It would appear that the blanket bond in this case may also be for bonding of multiple well sites of an oil and gas operator. The purpose of this subsection should be clarified and the language modified accordingly.

DUPLICATION

Duplicates SB 960

OTHER SUBSTANTIVE ISSUES

According to ENMRD, under the act, if an operator had posted a bond to secure access, and later

became insolvent, leaving the land unreclaimed, the surface owner could recover the proceeds of the security, and would not be obligated to apply those proceeds to actual reclamation of the property. OCD would recommend that the bill be amended to require the proceeds of the bond (if the property has not been reclaimed) to be applied first to reclamation of the surface, with any surplus to be paid to the surface owner.

EMNRD reports that threats to surface lands and quality of life are becoming increasingly significant concerns as the state's population continues to grow. HB 827 would provide new mechanisms to provide equity between oil and gas operators and surface owners in the development of surface use agreements, and would allow for a fair negotiation process to encourage the resolution of disputes. This will allow operators to pursue additional oil and gas developments and to continue current operations in a manner that is beneficial to and in the interests of oil and gas operators and the citizens of the State of New Mexico.

BS/nt