

Written Testimony on S.B. 258  
Compensation for Damages Sustained by the Surface Owner When Dealing with Oil or Gas Operation  
By: Fidelity Exploration & Production Company

Fidelity Exploration & Production Company is opposed to Senate Bill 258. Fidelity believes that this legislation is not necessary and that the existing Surface Owner Damage and Disruption statute provides adequate and equitable protection to the surface owner, mineral owner, and the oil and gas operator.

S.B. 258 proposes to amend the current Surface Owner Damage and Disruption statute by changing the notice period, providing a "laundry list" of damages to be considered, and creating a complicated, laborious method of access through the courts. This proposed amendment places an inequitable burden on the mineral estate owner or oil and gas operator; would turn existing case law upside down; and would give the surface owner complete control on oil and gas development through the threat of entering a court process.

The proposed legislation does not exclude federal minerals. Passage of S.B. 258 may violate the Supremacy Clause of the United States Constitution. Montana does not have the authority to pass legislation impeding the rights of the federal mineral estate. The Bureau of Land Management's Onshore Order 1 requires an operator certification that a surface owner agreement has been entered into before it will approve an Application for Permit to Drill. In the event a surface owner agreement cannot be negotiated, BLM has a damage bonding procedure (43 CFR 3814) which is in addition to its reclamation bonds, to protect the surface owner while allowing the oil and gas operator access to conduct operations. BLM sets the 3814 bond amount.

Please find below Fidelity's specific comments to S.B. 258.

Page 2, line 1, "Purpose -- legislative findings":

Subsection (c): "provide expeditious procedures for quantifying the obligations of owners of severed oil and gas estates when agreement cannot be reached." Comment: New section 9 does not provide any "expeditious" procedures. The procedure outlined in section 9 is confusing, dependent on the applicable court docket, and availability of qualified appraisers.

Page 2, lines 10 – 12, "Purpose -- legislative findings":

Comment: This new subsection states "... the purpose of this part can be pursued without impairment of any constitutionally protected rights of owners of severed oil and gas estates..." This legislation effectively places the entire burden to negotiate in good faith on the operator. The surface owner is not held accountable for their participation in access negotiations and compliance. The operator has leased the right for ingress and egress to exercise a valid property right. In order of the mineral estate owner to be able to enjoy his property right, he must have reasonable access to the surface. This

legislation completely takes away the mineral owners' unalienable right to enjoy his property interest.

Page 2, line 27, "Oil or gas operations":

Comment: This definition deletes "and is subsequent to June 1, 1981" which was the effective date of the original Surface Owner Damage and Disruption Act. This deletion would retroactively affect any development operations or surface use agreements that were in effect prior to June 1, 1981. Changing the definition from oil and gas to oil or gas is contrary to customary language addressing oil and gas development; where "oil and gas" refers to all hydrocarbons in the mineral estate.

Page 2, line 30, "Operator":

Comment: This new definition could be interpreted as a deterrent for mineral owners (including the State of Montana) to lease in the first place. This proposed language could arguably make the mineral owner liable to the surface owner for an oil and gas lessee's operations.

Page 3, line 6, "Notice of oil or gas operations":

Comment: The proposed change deletes "drilling" and inserts "oil or gas." This revision changes the previous notice from drilling to operations. This may mean anytime an operator is planning well or facility maintenance, the operator would be required to give the surface owner notice.

Page 3, line 10, "Notice of oil or gas operations":

Comment: Deletes "record" from notice being given to surface owner and any purchaser under contract for deed. While the definition of surface owner includes "...who holds record title to..." the definition continues with "...or has a purchaser's interest in the surface..." It is ambiguous if the "purchaser" has to be of record. An operator should not be obligated to give notice to an unrecorded purchaser under contract for deed. Notice can only be given to owners or purchasers as it is reflected in the county records.

Page 3, line 16, "Notice of oil or gas operations":

Comment: The new text requires that the notice "include an offer to enter into good faith negotiations..." There is no definition of what constitutes good faith. There is not a parallel provision requiring the surface owner to negotiate in good faith. This language could be used as a mechanism to void or renegotiate a surface owner agreement if at a later date another surface owner in the area receives higher compensation. New section 11 "Treble damages" refers back to this section and may make an oil and gas operator liable by a misinterpretation of "good faith" negotiations.

Page 3, line 18, "Notice of oil or gas operations":

Comment: The proposed amendment changes to fewest days in a notice from 10 to 45. The change may be interpreted as a 45-day operations window in which the operator has to commence the applicable oil and gas operations.

Page 3, line 23, “Surface damage mitigation and compensation -- negotiation -- penalty for late payment”:

Comment: After notice, and prior to entry, the operator is required to enter in good faith negotiations with the surface owner. Subsections (a) through (j) describe a laundry list of disturbances that the surface owner agreement is to address. This legislation is dictating the components to be included in a surface owner agreement. What if one of these components is not addressed because of the site-specific situation? List includes “impairment of ground water wells.” There are several environmental influences that may impact ground water wells. Montana already has the Coal Bed Methane Offset Protection Act that provides appropriated water right users with protection.

Page 4, line 11, “Surface damage mitigation and compensation -- negotiation -- penalty for late payment”:

Comment: New language adds “lost use of and access to the surface owner’s land” to the compensation list. If you are already compensating for lost land value, this is a double recovery for the same loss. Also, it may be ultimately considered a legislative taking. The owner of the mineral estate is already entitled to reasonable access to the surface to enjoy their property right. The owner of the surface estate purchased their rights subject to preexisting mineral property rights.

Page 4, line 18, “Surface damage mitigation and compensation -- negotiation -- penalty for late payment”:

Comment: The sentence “The payments contemplated by the subsection (1) may only cover land directly affected by drilling operations and production” is deleted in its entirety. This may make the operator liable for “blue-sky” damages on adjacent lands.

Page 4, lines 22 – 24, “Surface damage mitigation and compensation -- negotiation -- penalty for late payment”:

Comment: This is a new subsection requiring the operator, in the event a surface owner agreement cannot be negotiated, to petition the court in order to determine damages under new section 9. (See below)

Page 5, lines 24-27, NEW SECTION, “Entry for oil or gas operations”:

Comment: Subsection (2) prohibits the operator from access until the “...court enters an order on the appraiser’s written report pursuant to [section 9].” The operator is only granted access at the completion of the court process outlined in new section 9. This is an unreasonable burden on the oil and gas operator and the mineral owner. The mineral estate owner is not able to protect his correlative rights from drainage due to an offsetting well, the surface owner does not have to recognize preexisting rights of the mineral owner for access, and the oil and gas operator may lose a lease because of the lengthy process outline in new section 9.

Page 5, line 29, NEW SECTION, “Offer -- award of litigation expenses”:

Comment: This new section provides that the operator, within 30 days after a petition is filed under [section 9], is to submit a final written offer for damages, including the “accrued necessary expenses of the surface owner.” Accrued necessary expenses is not a defined term, the surface owner is not held accountable for his behavior, and these expenses are not actual damages associated with the operator’s proposed actions.

Page 6, line 10, NEW SECTION, “Determination of damages by court -- petition”:

Comment: This is the new section 9 which is referred to throughout the proposed legislation as the court process governing situations in which the surface owner and the operator cannot reach an agreement. This process favors the surface owner, does not provide an “expeditious procedure” when agreements cannot be reached, and is very laborious. This process adds significant delay in obtaining access. (Notice to surface owner within 10 days after petition is filed; Court has 20 days to appoint appraisers after petition is filed; appraisers have 30 days after their date of appointment to file report; within 10 days after the appraisers file their report, the Court shall forward a copy to each party; any party may file written exceptions within 30 days after the filing of the report; upon a filing of written exceptions, the Court shall hold a hearing to review the report and shall thereafter enter an appropriate order; either party may within 60 days after the filing of the appraisers’ report, file with the Court a written demand for a jury trial.) This process is also vulnerable to the court docket and the availability of qualified appraisers.

Page 8, lines 12-21, NEW SECTION, “Treble Damages”:

Comment: This section allows a court to award treble damages to a surface owner upon showing a preponderance of evidence, that an operator intentionally or negligently began oil or gas operations prior to giving notice and securing the surface owner agreement; or petition the court for appointment of appraisers. This burden is only upon the operator. Legislation should be balanced to provide the operator the right to be awarded treble damages upon a surface owner acting in bad faith, such as locking out an operator who has complied with this legislation.

Fidelity respectfully requests your consideration of the above comments when considering the merits of S.B. 258.