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THE NORTH DAKOTA FARMER/RANCHER AND SEVERED MINERAL RIGHTS

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Julie A. Krenz, Owen Anderson, and Jerome E. Johnson*

Severed mineral interests create recurring problems of great importance to many farmers and ranchers in North Dakota. Historically, development of mineral resources was seen as a critical need and economic boon that took priority over ownership rights in the surface of the land. Hence, the mineral estate generally was referred to as the "dominant" estate. Mineral developers were allowed unrestricted use of as much of the surface as was reasonably necessary for their operations. The surface estate became known as the "servient" estate because the mineral estate owner could use as much of the surface as was reasonably necessary to produce the minerals. The increasing competition for use of the surface is causing a judicial and legislative re-examination of the traditional relationship between the mineral estate and the surface estate. The impacts of increasing mineral development give rise to conflicts between the mineral owner and the surface owner for competing uses of the same land.

This report presents the rights and liabilities of the mineral owner and the surface owner when the mineral interest in oil and gas has been severed from the surface estate. It does not cover the rights of surface owners with regard to the mining of coal.

It considers applicable North Dakota laws, some interpretations of them, and how they affect North Dakota farmers and ranchers. Many aspects of the law remain unclear at this time, either because there never have been answers or because the laws are changing. Courts and future legislatures will decide many of the legal questions; until then, the legal rights of the parties will remain in doubt to some degree.

Reservation and Grant of Mineral Rights

A fee simple ownership of the land includes both the surface rights and the mineral rights, but in many cases these two rights have been separated. Once divided, the mineral rights and the surface rights form two distinct estates--each separate from the other and each can be sold, leased, or inherited without relation to the other. The surface owner and the mineral owner each enjoy corresponding and reciprocal rights and obligations which impose limitations on each other.

The surface and mineral estates are separated by either of two methods: a reservation or a grant. A reservation occurs when the owner of both the surface and mineral estates transfers ownership of the surface while retaining ownership of all or a portion of the mineral estate. A grant takes place when

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the owner of both the surface and mineral estates transfers ownership of the mineral estate while retaining ownership of the surface. Generally, the same legal principles apply to grants as to reservations.

Severed ownership also can include joint mineral ownership by several persons in the same land. For example, two or more people may own all the minerals under 160 acres of land. Each person has a right to a proportionate share of the various benefits. Several people also can own separate minerals. One person may own coal while another may own uranium and another may own oil and gas. Even different layers of minerals in the same land can be owned by different parties.

Reservation

The United States government, the state of North Dakota, and private parties have retained certain mineral interests by reservation.

By the United States Government

The federal government retained nearly 5,000,000 acres of mineral rights in North Dakota through reservations in patents. The intent of Congress is important to establish the rights each owner has in these lands. Congress has passed a number of acts dealing with the reservations of minerals.

The 1862 Homestead Act did not reserve minerals to the government. Ownership of both the surface and mineral estate, known as a fee simple interest, passed to the homesteader. The lands were patented as agricultural lands, which were thought to be nonmineral in nature. Later Congress opened "mineral lands"--land considered valuable for mineral development--to homesteading and settlement but reserved certain minerals. The first congressional acts opening mineral land in North Dakota were passed in 1909-10 and reserved coal; most of the federal government's severed mineral rights in North Dakota reserve only coal. Two important congressional acts which issued patents with reservations or exceptions of oil, gas, or other minerals were the 1914 Agricultural Entry Act and the 1916 Stock Raising Homestead Act. The 1914 Act specifically reserved oil and gas, but the 1916 Act stated "all the coal and other minerals." The term "other minerals" includes oil, gas, and many other minerals, including gravel.

The acts provide that any person who acquires mineral rights to the lands may enter and occupy as much of the surface as needed in the mining and removal of the minerals. Use of the surface for drill sites, pumps, tanks, roads, pipelines, waterlines, and the use of heavy machinery are a few of the many operations conducted by the lessee causing extensive surface damage for which the surface owner is not compensated. Congress provided that the surface owner was to recover for any damages due to the mining operations. Congress limited damages to such things as destroying crops or agricultural improvements. Improvements include wells, fences, buildings, corrals, silos, and other things to improve the land for stock raising purposes.

Congress passed an act in 1949 which provides that any person mining by open pit or strip mining methods shall be liable for damages to crops or improvements of the homesteader plus damages to grazing lands. The reference to open pit and strip mining may mean that the developer will be liable for damage caused by those activities and will not be liable for damages caused by oil and gas operations.

By the State of North Dakota

The state of North Dakota is a large owner of severed mineral interests. The original 1939 state reservation was 5 percent of all "oil, natural gas, or minerals." The legislature increased the reservation of oil, natural gas, or minerals in any transfer of state lands to 50 percent in 1941. The North Dakota Constitution has provided since June 28, 1960 that in sales of all school lands

> "All minerals therein, including but not limited to oil, gas, coal, cement materials, sodium sulphate, sand and gravel, road material, building stone, chemical substances, metallic ores, uranium ores, or colloidal or other clays, shall be reserved and excepted to the state of North Dakota..."

State-owned school lands are lands originally granted to the state by the United States under legislation creating the state in 1889. The Constitutional provision applies to original school lands, and by reason of a special statute enacted in 1977, to all land under the control of the Board of University and School Lands. The 50 percent reservation still applies to the sale of other state lands. The North Dakota Supreme Court interpreted the 1941 statute such that the term "minerals" includes coal but does not include sand and gravel. There is some doubt as to whether the reservation includes uranium. The statute applies to all transfers of land held by the state. The state reserves 50 percent of the mineral rights, no more or less, of land acquired from the state, and the buyer gets the remaining 50 percent of the mineral rights. The 1960 reservation is much broader than the 1941 reservation. It includes sand, gravel, uranium, and many other minerals specified by name.

By Other Owners

Commercial banks, land banks, insurance companies, and other credit agencies that acquired farms by mortgage foreclosure own mineral interests in North Dakota. The institutions frequently reserved half or more of the mineral rights when they resold the lands to farm operators. For example, the Federal Land Bank owns many severed mineral interests throughout North Dakota.

Railroad companies also are owners of many mineral rights in North Dakota. Congress made large land grants to the Northern Pacific Railroad Company. The railroad companies used the land as collateral for loans or would sell the land directly to raise funds for constructing the railroad. The deed to the land first sold by the railroad companies reserved coal and iron. Later on, the deeds conveying the surface reserved coal, iron, and

other minerals. Courts generally interpret the term minerals to include oil and natural gas.

By Private Individuals

Private individuals often separate the surface and mineral estates. Here, the document severing the estates must be examined to determine the intent of the parties and the resulting rights and obligations of the two estate owners.

The Mineral Deed

Mineral right owners generally use a mineral deed to transfer ownership of mineral rights.

One question causing legal problems is, "What minerals are included in the deed?" Many documents of grant or reservation refer to "any oil, gas, and other minerals in and under the described land." There is frequently an issue as to ownership of gravel, clay, granite, sandstone, coal, lignite, iron ore, and more recently, uranium and fissionable materials. The minerals not conveyed or reserved remain with the surface estate.

Courts examine the language of the deed closely for the facts and circumstances existing at the time of the transaction to determine the intent of the parties. Absent a special action to reform the terms of a deed, the intent of the parties as stated in the deed controls their respective rights and not the intentions which they may have had but failed to include in the deed. If the language in the deed is clear, the court will interpret that language by its ordinary meaning. If the language is not clear, courts may look at:

1. Common mining practices in use at the time the deed was drawn up. For example, local knowledge that coal existed as an extractable mineral at the time the instrument was executed would indicate that the parties most likely intended it to be included within the meaning of the term mineral. This is true even if the grantee has to use part of the surface to extract the coal.

2. Which party drew up the deed, because some courts interpret ambiguous parts of a deed against the party that drew it up.

3. The surface use and kind of land proposed to be mined. Gravel and sand would probably not be included in the meaning of the word mineral because they are part of the soil and mining them would destroy the surface.

The North Dakota Supreme Court considering if the term "minerals" included coal, stated:

> "We have found no cases holding that coal is not a mineral. Whenever the question has been considered, the courts have construed the term 'mineral' to include coal."

The conclusion is that the word "mineral" taken in its ordinary meaning always includes coal. Thus, the presumption is that any deed in North Dakota which conveys rights to "minerals" has transferred the coal rights.

The legislature passed a law in 1955 specifying what minerals were included in the term "minerals" when it was used in leases and conveyances. Because of this law, the question of what minerals are included in a conveyance of "minerals" usually arises in instruments dated before July 1, 1955. The 1955 law stated that no interest in gravel, coal, clay, or uranium would pass in a lease or conveyance unless the intent to convey that interest was specifically and separately set forth in the instrument.

The legislature passed a law in 1957 that dealt separately with leases and conveyances. The law remained basically the same for conveyances. As to leases, however, the law provided that "no lease of mineral rights will pass any interest in any minerals except those minerals specifically set forth by name in the lease." This law regarding leases is still in effect today and applies even if the phrase "all other minerals" is used in the lease.

The North Dakota Supreme Court held that this law did not apply in the case of a reservation or exception of mineral interests. So, the legislature enacted a new statute in 1975. It provided that in deeds reserving or excepting the minerals, only those minerals specifically named in the deed would be reserved. If O sold land to A and reserved "oil, gas, and other minerals" O would own only oil and gas, A would own all other minerals including coal.

The 1983 legislature revised the laws on mineral conveyances and reservations. Effective July 1, 1983, a conveyance of "minerals" includes all minerals of any nature, including compounds and byproducts, but the conveyance does not include gravel, clay, or scoria unless those minerals are specifically included in the conveyance. Prior to this law, a conveyance of mineral rights did not include gravel, coal, clay, or uranium unless the intent to convey such interest was specifically set forth in the conveyance. For example, if X conveyed "oil, gas, and all other minerals" to Y before July 1, 1983, X would retain ownership of gravel, coal, clay, and uranium. Y would own oil, gas, scoria, and all other minerals. On the other hand, if X conveyed "oil, gas, and all other minerals" to Y after July 1, 1983, X would retain ownership of gravel, clay, and scoria. Y would own oil, gas, coal, uranium, and all other minerals.

Also effective July 1, 1983, a conveyance which includes a reservation of "minerals" shall mean that all minerals of any nature, except for gravel, clay, and scoria, will be transferred with the surface estate unless those minerals are specifically reserved by name in the conveyance. Prior to July 1, 1983, a conveyance which included a reservation of "minerals" reserved only those minerals specifically named. For example, if X conveyed land to Y and reserved "oil, gas, and all other minerals" before July 1, 1983, only oil and gas would be reserved because those were the only minerals specifically named in the conveyance. Y would own all minerals except for oil and gas.

If X conveys land after July 1, 1983, and reserves "oil, gas, and all other minerals," the reservation of minerals includes all minerals of every nature except gravel, clay, and scoria. X no longer has to specifically name every mineral he wants reserved in the conveyance.

The Mineral Lease

Courts that deal with mineral leases will generally examine the intentions of the parties in determining the rights of the parties. The description and definition of minerals that can be transferred by a lease is dealt with in a specific North Dakota statute. In part, the statute states:

> No lease of mineral rights in this state shall be construed as passing any interest to any minerals except those minerals specially included and set forth by name in the lease.

This statute causes the wording of a lease to be interpreted different from a deed. The term "specially included" means that the word "minerals" would include only those minerals specifically named in the lease. Thus, a transfer of a mineral lease which purports to lease "all oil, gas, and other minerals" would not include coal since coal was not specifically mentioned.

Rights of Mineral Lessees

The owner of the mineral estate has the inherent right to enter the land and conduct operations to develop the mineral estate. The high costs of development and technical skills needed often causes the mineral owner to convey his right to mineral development to someone else by an oil and gas lease.

Leasing mineral rights sharply differs from the sale of those rights. A lease is not the sale of the minerals but is only a right to mine and remove the minerals specified in the lease agreement. The minerals become the property of the lessee as they are mined. If they are never mined and the lease expires, the minerals remain the property of the mineral owner. The lease agreement states the rights and obligations of the parties to it. The lease results in three separate estates: the surface estate, the mineral estate, and the leasehold estate. The surface owner retains all rights to the use and enjoyment of the surface, except those granted to the lessee for the purpose of locating and removing the minerals. Mineral leases may be assigned by the mineral lessee to another party who has all the rights and obligations specified in the original lease.

Generally the mineral owner (lessor) and the mineral developer (lessee) share in the profits. The usual lease has the developer bear the costs of exploration, development, and production. The mineral owner/lessor and lessee usually agree to the following:

1. The lessee receives exclusive right to explore for and develop a certain mineral. The lessee can assign this right to others for the term of the lease.

2. The duration of the lease is usually for a term of years (commonly 3, 5, or 10 years) and so long thereafter as oil and gas are produced in paying quantities.

3. The lessee usually gives the mineral lessor a cash payment, called a bonus, for the execution of the lease.

4. The lessee keeps the lease in force by paying delay rentals. Delay rentals are annual payments by the lessee to the mineral owner to keep the lease in effect prior to the discovery and production of oil and gas.

5. In the event of production, the lessee promises to pay the lessor a royalty, which is a share of the profits. Typical royalty shares in North Dakota are a 1/8 or 1/6 interest.

6. In the event of discovery of gas that cannot be readily marketed, the lessee promises to pay the lessor a shut-in-royalty. This is a dollar amount agreed on in the lease.

If oil and gas are produced or the well is shut-in, the lease will remain in force as long as the lessee produces oil and gas or pays shut-in royalty payments.

The rights in the lease can never be greater than those granted in the mineral deed. For example, assume that O sold a farm to A, reserving an undivided share of the mineral estate, and also reserving the power to control the leasing of the entire mineral estate. A, while he owns an undivided interest in the mineral estate, would be unable to lease his interest because O reserved this right. If A sells his interest to B, B would also be unable to lease. If there is mineral production on the land, however, A or B would receive a share of the royalty payments. Also, depending upon the exact nature of their interest, A or B may be entitled to receive a share of the lease bonus and rentals.

Creation of Conflicts

The landowner who owns both the surface estate and the mineral estate can control mineral development and allow it on his terms. He may lease the land for a bonus and usually will receive annual delay rentals from the lessee for the number of years specified in the agreement granting the lease. The landowner also receives royalty payments if there is mineral production from the land. The owner, in entering the lease, is said to have impliedly authorized the lessee to use as much of the surface as is reasonably necessary to conduct operations.

When the two estates are separated, the surface owner cannot control the mineral owner's access to his land and generally cannot prevent oil and gas development. Also, the mineral owner can lease his mineral rights to whoever he pleases. The surface owner receives no financial benefit from the minerals. The surface owner may try to restrict the mineral development or seek surface damage compensation. The mineral owner usually has no agreement with the surface owner, which becomes apparent when the issue of surface damages arises. The relationship between the surface owner and the owner of severed mineral interests in North Dakota rests upon an analysis of the legally recognized and protected rights of each and the corresponding duties and restrictions placed upon each.

Rights of the Mineral Owner

Historical Setting

The need for mineral resources encouraged mineral owners to develop their natural resources. The early encouragement of mineral development gave rise to the practice of treating mineral estates as dominant over the surface estate. The mineral owner generally has been able to enter and use as much of the surface as is reasonably necessary to develop the minerals. However, recent legislation and court decisions indicate that the law no longer favors the mineral owner as it did in the past.

Two kinds of rights may be granted to the mineral owner. Express rights are those listed in the document severing the mineral estate from the surface estate. An example of an express right would be a clause which specifically gives the mineral owner the right to use water from wells belonging to the surface owner. Implied rights are provided by law, such as the right of entry on the land, the right to build or use roads to enter and leave the property, and to generally employ all means reasonably needed to mine the minerals. Implied rights are not actually specified in the transfer document, but are implied by law. The courts reason that when a person is given mineral rights, the parties must have intended that he would have access to remove and enjoy those minerals. Without implied rights, the interest might be inaccessible and the mineral estate would be worthless. However, the mineral owner is limited to methods reasonably necessary to mine and can be liable for any negligent and unreasonable operations.

The main issue in past disputes between surface and mineral owners was whether the use of the surface was reasonable and necessary to explore and develop the oil and gas. The mineral owner usually transfers (leases) his right to explore or develop oil and gas on the property in which he owns a mineral interest to a mineral lessee. A conflict arises when some surface damage occurs. The mineral owner is usually a bystander. The issue becomes whether the surface owner must bear the damages caused by drilling operations of the mineral lessee, or whether the lessee must compensate the surface owner for damages.

Under the lease, the lessee may not be liable for any injury or damages resulting from his actions if a court decided that his use of the surface was reasonable and necessary. However, the lessee will be liable for damages if the lease or a statute prohibits the acts and provides for damages, or if the acts were performed in a negligent or unreasonable manner.

It is necessary to look at what happened at the time the lease was created to understand how an oil and gas lease gave the lessee those rights. The typical lease form contains a granting clause that usually provides:

> Lessor...grants, leases and lets exclusively to the lessee the land described before for the purposes of investigating, exploring for, drilling for, producing, saving, owning, handling, storing, treating and transporting oil and gas together with all rights, privileges and easements useful for lessee's operations on said land and on lands in the same

field with a common oil and gas reservoir, including but not limited to the rights to lay pipelines, build roads, construct tanks, pump and power stations, power and communication lines, houses for its employees, and other structures and facilities and drill for, produce, and use fresh water.

The lessee obtains these rights, so he does not have to pay for damages resulting from authorized conduct as long as the use was reasonably necessary for the exploration, drilling, or production of oil and gas.

A particular type of use may be expressly authorized by the lease or there may be no question as to whether a use was necessary to effectuate the purpose of the lease, but the lessee's conduct in making that use may have been improper. For example, a lease may expressly grant the right to install an oil storage tank. Installing a leaky tank makes the lessee liable to the surface owner for damages. Also, the lessee would be liable to the surface owner if he used more land than was reasonably necessary for a well-site.

In the past, the lessee did not have to compensate the surface owner for surface damage that was reasonably necessary to explore for and produce oil and gas. Recent legislation has changed this. North Dakota law now requires the mineral lessee to compensate the surface owner for all damages the lessee causes, even if they are reasonable and necessary.

Location Damages

Society has shown broadened concerns for the rights of the surface owner, but the mineral estate retains important attributes of its dominant status. One important right is that, unless there is a statutory (which North Dakota now has) or contractual obligation, a mineral developer has no duty to compensate the surface owner for surface damages or to reclaim the land if his mineral operations are performed in a reasonably necessary manner. The reasonable necessary standard recently has come to mean that the mineral developer must reasonably accommodate the surface owner where such actions would not unreasonably burden the mineral developer.

Reasonably necessary uses by the lessee, a legally protected right, cannot serve as the basis for a valid compensable damage claim. Some surface damage inevitably results from reasonable oil and gas operations. The parties severing the minerals, whether by lease or mineral deed, are deemed to have had this in mind when they made their bargain.

Although the lessee is not legally required to do so, the practice of compensating the surface owner for damages has developed in the oil industry. Damages are generally paid because mineral developers want to establish and maintain good working relationships with the surface owner, or because mineral developers realize that it is less expensive to pay damages than become involved in costly litigation. Generally, when damages are paid, the surface owner will sign a form releasing or discharging the mineral developer from any claim that the surface use is unreasonable. Mineral developers may still be liable for damages caused by their negligence or for violating a statute or regulation.

The most common form releases the mineral lessee for liability with regard to a particular well. Be sure it is read and reviewed by an attorney.

WARNING--There is no legal basis for the surface owner to deny a mineral owner or mineral lessee access to the estate, unless there is a contractual agreement between the mineral lessee and the surface owner. The lessee may get an injunction or a restraining order from a court forbidding the surface owner from interfering with oil and gas operations.

One mineral lessee brought action to stop a surface owner from interfering with the lessee's operations. The surface owner refused to let the developer on his land until he agreed to pay the surface owner $6,500 in initial damages, $1,500 annually, and other damages for road construction. The lessee had no legal obligation to pay damages. The court awarded the lessee $10,912.00 damages for being denied access and for delaying development operations. The court also fined the surface owner $1,000 as a penalty for interfering with the mineral development.

A surface owner who prevents a lessee from developing minerals may be liable for damages in the hundreds of thousands of dollars. Liability insurance probably would not protect the surface owner because his acts were intentional and clearly illegal. An attorney should be contacted immediately if there is a conflict between the surface owner and the mineral developer.

The Accommodation Doctrine and the Conflict of Due Regard for the Surface Owner

The mineral developer has the right to use as much of the surface as is reasonably necessary to produce oil or gas, but court decisions have stated that these rights must be exercised with due regard for the interests of the surface owner. In other words, the mineral developer must make reasonable accommodations to the surface owner. The early years of mineral development was a period when the need for energy resources took priority over ownership rights in the surface. Courts have recently begun limiting the rights of mineral lessees. The North Dakota Supreme Court continues to recognize the mineral lessee's right to develop minerals but has questioned the social desirability of a rule that allows the damage and destruction of a surface estate, that may be of equal or greater value than the value of the mineral being extracted, without any compensation for the surface owners.

The 1979 North Dakota Oil and Gas Production Damage Compensation statute continues the trend of limiting mineral lessee's rights. Here the legislature recognized the importance of agriculture to the public welfare of the state of North Dakota.

The legislature felt that exploration for and development of oil and gas interfered with the agricultural or other uses of the surface. This law provides compensation to surface owners for damages caused by this interference. This law and its effect is explained further below.

It is still generally held that the oil and gas estate is the dominant estate so that the mineral lessee can use as much of the surface as is reasonably necessary to produce and remove the minerals. The concept of due

regard, however, is that the reasonableness of a lessee's surface use is determined by considering the needs of both the surface owner and the mineral lessee.

It is not clear how much the concept of due regard will limit the mineral lessee's use of the surface. Two recent court decisions have limited the oil and gas lessees use of the surface by requiring them to consider alternative methods of developing and operating.

A Texas court held that the concept of due regard means the accommodation of conflicting interests in the use of the surface. North Dakota adopted this view, which involves a consideration of the surface owner's position or surface usage as well as that of the mineral lessee's.

The "accommodation doctrine" was first applied in a Texas case. There, a surface owner drilled water wells and installed center pivot irrigation systems. Later, the mineral lessee drilled two wells under a lease granted by the mineral owner. The oil pumping equipment was taller than the center pivot irrigation booms so the irrigation equipment could not work. The court held that when the mineral owner's or lessee's rights impair existing surface uses, the mineral owner or lessee must accommodate the surface uses if he has a reasonable alternative. The court found that the oil company should have placed its pumping units below the surface to avoid interference with the surface owner's irrigation operation.

The court stated that if there is only one manner of use of the surface in which the mineral lessee can develop and produce the minerals, then the lessee has the right to use this manner, regardless of surface damage.

The accommodation doctrine considers three factors:

1. There must be an existing surface use. This was center pivot irrigation in the Texas case.

2. The proposed use must substantially interfere with the existing surface use. The installation of pumps by the lessee prevented further irrigation operations.

3. The lessee must have reasonable alternatives available. The Texas lessees could have placed the pumps below the surface so that the center pivot irrigation equipment could pass over the oil wells.

One reason for this doctrine is that when the mineral rights have been severed from the surface, both the mineral owner/lessee and the surface owner have valuable estates that benefit a state's economy. Hence, the mineral lessee should be required to accommodate the surface owner's use whenever accommodation is reasonably possible.

The surface owner has the burden of proving that the lessee's use of the surface is unreasonable. The surface owner must prove that the mineral lessee has a reasonable and feasible alternate way to develop his interest. If successful mineral development requires a particular use of the surface that cannot be reconciled with the surface owner's use, the mineral owner's or lessee's estate is still the dominant one and will prevail. This can be

demonstrated by a Texas case where the lessee was allowed to deplete the surface owner's ground water reserves even though water could have been purchased inexpensively from a nearby river. The court stated that to be a reasonable alternative to the lessee, the alternative must be available to the lessee on the leased premises.

The mineral estate is still the dominant estate in North Dakota, which gives its owner the right to use as much surface as is reasonably necessary to develop and produce the minerals. The North Dakota Supreme Court has adopted the accommodation doctrine. If the surface owner can show that reasonable alternatives exist, then the goals of the mineral developer will be balanced against the inconveniences to the surface owner. It must first be proven that reasonable alternatives exist before the interests of the surface owner and mineral owner will be balanced. The mineral lessee will prevail on the absence of reasonable alternatives.

Reasonably Necessary Uses

Examples follow of surface uses that courts have found to be reasonably necessary for oil and gas development. Some limitations placed on those uses are discussed. The list is not inclusive. Whether a court will find a specific use reasonably necessary to develop oil and gas may depend on the facts and circumstances of that particular case.

Exploration for Oil and Gas

The mineral lessee has the right to enter land to conduct geophysical operations to discover oil and gas. This involves the use of explosive devices and sensitive measuring equipment. Prior to June 30, 1983, the lessee was not required to pay damages for surface injuries as long as the exploration activity was reasonably necessary.

The 1983 amendment to the North Dakota Oil and Gas Production Compensation Act requires mineral developers to compensate the surface owner for harm caused to the surface by exploration. Surface owner is defined by statute as the person who has possession of the surface of the land either as an owner or as a tenant.

Location and Time of Drilling

The mineral developer has the right to locate and construct the oil well and drilling rig as desired and to remove trees and vegetation to clear a drilling site. He has the right to maintain well sites, slush and waste pits, drainage ditches and ponds for impounding salt water, storage tanks, reservoirs, and pickup stations. The North Dakota Supreme Court stated that a lease provision granting the lessee "all other rights and privileges necessary...for economic operation or production" expressly gave the lessee the right to construct a second salt water disposal pit.

Most leases provide that no well will be drilled within 200 feet of any residence or barn unless the surface owner consents. The mineral developer

probably will not be allowed to drill a well where it would jeopardize the lives of the surface owners. For example, one mineral developer constructed a pit designed to permit the escape of flammable and explosive gases. The court held that it was not reasonably necessary to drill a well next to this pit because of the probability of an explosion.

An Oklahoma court held that the mineral developer was not liable for injuries to or loss of cattle caused by drinking oil and gas refuse from slush pits and ditches. It found that the excavation and maintenance of unfenced slush pits was a reasonably necessary use of the surface by the mineral developer. But a mineral developer was liable for harm caused to cattle that drank water from an "emergency pit." Emergency pits catch fluids in case of an accident. The court found that these pits were not reasonably necessary for the production of oil and gas. There may be a very fine distinction between what is "reasonable" and "not reasonable" to a court.

Roads--Ingress and Egress

The lessee has the right to construct, maintain, and utilize roads to locate, produce, and market oil and gas. This includes the operation of heavy construction equipment and trucks on roads leading to and from the well site. The lessee is usually allowed to use materials found on the leased premises to construct the roads.

The mineral lessee who builds a road to a well site but fails to drill may be held liable for the surface damages. The lessee may be liable if he constructs roads used for transit to wells on other lands. The lessee should use a route to gain access to the minerals that minimizes surface damage rather than one which is merely more convenient. Where both a public and private road provide access to the leased premises, the lessee may have to use the public road.

Pipe and Pipelines

The mineral developer has the right to install and use pipelines to transport hydrocarbons or waste on or off the premises. Pipelines must be installed and operated in a non-negligent manner without occupying an unnecessarily large area of surface.

Most leases require the lessee to bury pipes below plow depth when requested by the lessor. Some leases only require pipes to be buried below plow depth if the land is cultivated.

The mineral developer will be strictly liable if stored salt water escapes. He must prevent oil and poisonous waste from accumulating in open pits near the well. He may be liable if he does not properly guard against gas escaping due to pipeline breakage.

Water

The lessee has a right to use water located on the premises free of charge, even if it limits irrigation water for the surface owner. He cannot

use water from the surface owner's own wells or private ponds, or extract water to use on other tracts of land.

Buildings and Structures

The lessee has the right to construct and maintain buildings if they are reasonably necessary. Courts have found that dwellings are reasonably necessary for employers who would guard, protect, and preserve the property and regulate production of oil.

Buildings cannot be constructed merely for the convenience of the mineral developer. One court found that the construction of a warehouse and tool shed was not reasonably necessary to the production of the oil and gas.

Fences

The mineral developer has no duty to fence off pits or operating areas. Cattle or other animals straying in these areas are trespassers. Conservation regulations require a developer to fence off storage pits which are present for an excessive period of time or are unreasonably large.

The surface owner has the right to fence the land, including access roads, to keep his livestock out of operating areas or pits. This is so even if the mineral developer is inconvenienced.

Restoration of the Surface

Historically, the mineral developer had no duty to restore the surface after he had completed operations in the development of oil and gas. An oil and gas lease or deed may have included an express provision requiring the mineral developer to restore the premises after his operations stopped. But these provisions often were not included in leases and deeds until recently. Many leases now have a clause requiring restoration of the premises. Also, modern conservation regulations require the mineral lessee to restore the well sites.

The mineral developer who is required to restore the premises must do so within a reasonable time. If the lessee has the right to remove buildings, restoration of the premises does not include replacing the buildings.

The 1979 North Dakota law greatly modified the law on surface damages. Previously the mineral developer was not liable for surface damages that were reasonably necessary to the production of oil and gas. The 1979 Oil and Gas Production Damage Compensation Act requires the mineral lessee to compensate the surface owner for all surface damage even when the damage was caused by activities reasonably necessary to develop the minerals. It is discussed further below.

Legal Rights of the Surface Owner

The surface owner has the right to enjoy his land free from annoyance, except as reasonably arises from the mineral owner and his mining activities. For example, the mineral owner has no right to use the surface owner's buildings or machinery unless expressly provided for. Anything other than reasonably necessary use by the mineral owner would be an invasion of the surface owner's rights.

Lease Provisions

Surface Use Provision

The granting clause in a lease form, usually written by the mineral lessee, grants many rights to the lessee. A carefully written lease can control the use of the surface by placing restrictions on the lessee's surface rights or by providing for compensation to the surface owner for certain acts of the lessee. The surface owner can only add these provisions if he owns an interest in the mineral rights. He can add these provisions to the lease if he owns an interest, but the lessee may be reluctant to accept any which would limit these broad surface rights.

Free Use of Gas

Some lease forms now have a clause which grants the lessor the right to use gas not needed for mineral operations from any gas well on the leased premises. The lessor usually must assume the risk and expense of piping the gas to his buildings.

Usually the gas can only be used for stoves and inside lights in the principal dwelling. Some courts have stated that "principal dwelling" includes a cluster of buildings, such as a garage, outhouse, and tool shop.

The lease grants the use of gas to the lessor, but questions have arisen as to whether this benefit extends to the surface owner if he does not own any mineral rights. That the gas is to be used for a dwelling "on the premises" to the benefit of the surface occupant would suggest that the surface owner would be able to use the free gas. Courts have gone both ways on this issue.

Notifying Surface Owner Prior to Operations

Previously the mineral developer did not have to give notice to the surface owner or tenant of his intent to begin mineral operations. Surface owners argued that with prior notice they could arrange to move livestock to another pasture or to harvest growing crops in the area.

North Dakota law now requires mineral developers to give notice to the land operator at least three days prior to any exploration activity. The notice must include the approximate time and location of the scheduled

activity. The mineral developer must give the surface owner written notice at least twenty days prior to the commencement of drilling activities. The notice should disclose the plan of work and operations sufficiently so that the surface owner can evaluate the effect of the operations. This will give him an opportunity to remove livestock or crops.

Causes of Action for Surface Damage

Liability does not necessarily arise if some surface damage occurs. But a mineral owner/lessee may be found liable under theories of negligence, trespass, nuisance, excessive use of the surface, and the duty not to damage the surface intentionally or recklessly. A mineral lessee may be liable for surface damages when there is a breach of lease terms. Liability based on breach of lease terms may not help the surface owner where his interest has been severed from the minerals. However, many leases now provide that the lessee will bury pipelines installed on the leased premises and pay for damages to growing crops.

Liability may be based on breach of a statutory duty or violation of an administrative rule or regulation. This is known as strict liability. The mineral developer may be found liable based on any of the above actions. Often these theories of liability overlap; excessive use of the surface may constitute trespass or nuisance, or negligence may not be separable from trespass or nuisance. Liability is most frequently based on negligence, though it may be based on excessive use of the surface, trespass, or nuisance.

Negligence

A cause of action for negligence holds the mineral lessee to the standard of care of a reasonably prudent operator. Some examples of negligent or unnecessary damage to the surface owner's land include overflow from salt water disposal pits, failure to warn the surface owner about imminent drilling operations so he can take steps to prevent injury to livestock, the presence of open tanks or other impoundments of poisonous materials which might injure livestock, failure to protect against the escape of gas or other substances from the well, breaking of salt water disposal lines, or leading and accumulation of oil in pools near storage tanks. The traditional dominant status of the mineral estate prevails even if the lessee causes substantial damage and interferes with the surface owner's land use if the lessee is using only reasonable methods to produce the minerals.

Nuisance

A mineral lessee's operations that cause unreasonable interference with the peaceful occupation and enjoyment of the surface owner may make him liable for nuisance even though the operations are lawful and carried on without negligence. While nuisance is a possible basis for liability, it is often combined with the theory of excessive use or some other theory. The nuisance concept is used by adjacent land owners as a basis for recovery.

Trespass

Trespass is a direct infringement by the mineral lessee of the property rights of the surface owner. The lessee has the right of ingress and egress so trespass may arise when the mineral developer uses more of the surface than he is entitled to.

Use of More Surface Than is Reasonably Necessary

Every oil and gas lease implies the right to use as much of the surface as is reasonably necessary to produce the minerals. The mineral lessee is not liable to the surface owner for damages reasonably necessary to the operation unless there are express lease provisions. A lessee who goes outside these boundaries may be liable for damages. The lessee should use all reasonable and practicable alternatives to minimize damage to the surface. Some examples of excessive use include construction of roads in excess of the reasonable needs of the lease, occupation of more surface than necessary to enjoy the minerals, use of water in excess of the amount authorized, and use of surface in connection with operations on other premises.

Strict Liability

A mineral owner can be held strictly liable for damages by his operations on the land. Strict liability most often arises in cases of the adjacent landowner versus the mineral lessee rather than the surface estate versus the mineral estate. This doctrine has mainly applied to seismic operations. For example, a mineral lessee conducts seismic operations by exploding dynamite on the surface owner's land with his permission, but may be liable for the damages to neighboring property caused by vibrations.

Often strict liability in surface damage cases is based on a violation of a statutory duty or administrative regulation. This occurs most often in the case of surface pollution. For example, the mineral developer has the implied or express duty to maintain salt water disposal pits. The mineral lessee will be strictly liable for damages if there is a statute or regulation prohibiting overflow of salt water overflow pits with subsequent pollution of the surrounding surface.

Contract Liability--Provisions in the Lease

Parties to a lease can create provisions in anticipation of problems that may arise. The parties can define the rights and liabilities of each party under the lease.

Courts confronted with a problem about the meaning of contract provisions usually attempt to establish the intent of the parties at the time of entering the contract. For example, an oil and gas lease will not include the right to mine hard minerals, especially when the parties intended to limit the lease to production of oil, gas, and related minerals.

If the surface estate and mineral estate have been severed and the surface owner is not a party to the lease, he may still be able to enforce the contract provision in the lease as a third party beneficiary.

One common provision in modern leases provides that the lessee will pay for damages to growing crops resulting from his operation. Growing crops does not include pastureland used for grazing unless provided for in the lease. The lessee will be liable for any damage to the crops because this express clause negates the implied right to even reasonable and necessary use. However, this provision may be used as a limitation, impliedly excluding the lessee from other types of surface damages.

Statutory Provisions for Surface Damages

The legislature enacted the North Dakota Oil and Gas Production Damage Compensation Act in 1979. It directly addresses the surface damage issue and defines recoverable damages. The legislative assembly found that the State of North Dakota is largely dependent on agriculture and that the exploration for development of oil and gas interferes with the agricultural use of the surface. This statute was enacted to compensate surface owners for injury to and interference with the use of their property, to protect the public welfare of North Dakota, and to protect the economic well-being of individuals engaged in agricultural production.

This act provides that the mineral developer must pay the surface owner damages for loss of agricultural production and income. The surface owner has possession of the surface either as an owner or as a tenant. Agricultural production includes the production of farm animals, grass or crops, whether or not they are raised for commercial purposes. The mineral developer also must compensate the surface owner for lost land value, lost use of and access to the surface owner's land, and lost value of improvements caused by drilling operations, including surface damages caused by seismic activities.

In addition to compensating the surface owner for damages caused by reasonably necessary use of the surface, the mineral developer is required to compensate for all damages to person or property, real or personal, resulting from the lack of ordinary care and for damages resulting from a nuisance created by the drilling operation.

The mineral developer is required to compensate the surface owner even if the surface and mineral estates have not been severed. The statute expressly provides that the surface damage payments may not be waived regardless of whether the two estates have been severed.

The amount of damages is determined under this statute by any formula agreeable to the surface owner and the mineral developer. The surface owner may sue the developer if he is unwilling to accept the compensation offered. The surface owner is entitled to costs and reasonable attorney fees if the court awards him more than the developer offered. The fees and costs provision creates a clear incentive for the developer to offer the surface owner a fair settlement.

The act provides surface owners and others with the maximum amount of constitutionally permissible protection from damage caused by the exploration and development of oil and gas reserves. The requirement that mineral developers compensate surface owners for damage they cause may serve as an incentive for developers not to drill where drilling is not likely to yield enough oil and gas to justify the loss from the payments for disruption of the surface. The compensation requirement also may be an incentive for developers to minimize surface damages and to remedy damages they cause.

This law took effect on July 1, 1979 and was amended in 1983. It allows compensation to surface owners even if the mineral estate was leased before July 1, 1979, as long as the development occurred after the effective date. The common law mentioned above applies for harm done prior to July 1, 1979, to recover surface damages.

The mineral developer will not be liable for surface damages caused by reasonably necessary uses of the surface that occurred prior to July 1, 1979. In order to find the developer liable, a cause of action will have to be based on negligence, trespass, nuisance, excessive use of the surface or, the duty not to damage the surface intentionally or recklessly. The mineral developer also may be liable if he did not comply with provisions in the lease or if he did not comply with administrative or statutory rules and regulations.

Measure of Damages

The question of the measure of damages arises if the mineral owner or developer is found liable.

Land or Buildings

There are two basic measures of damage used when the land itself or structures on it are injured.

The first measure is the diminution measure. Here the surface owner is entitled to recover the difference in the value of his property immediately before and immediately after the injury to it. This is the amount the property has been diminished in value as a result of the injury. The other measure of recovery awards the plaintiff the reasonable cost of restoring or repairing the damage. Courts usually award the measure that reasonably and fully compensates the surface owner.

Courts usually will award damages based on the diminution test if the injury is permanent. Courts will allow recovery for the cost of repair or replacement when the injury is one that is reasonably repairable. Repair cost is usually allowed when buildings have been damaged or where debris has been deposited on the land and can be removed. Damages for temporary injuries to land are measured by the loss of rental value.

The measure of damages is based on the diminution test rather than the cost of repair if restoring the land or a building costs more than the value of the land or building. Courts usually will not allow recovery of repair

costs if they would provide the surface owner with property or a building more valuable than he had before.

Livestock

The mineral developer has no duty to fence his operations to keep out livestock. The livestock owner usually can not recover damages if livestock are injured in the wellsite, ditches, and slush pits areas.

The developer is more likely to be found liable when harm occurs outside of the area which is reasonably necessary to maintain the wellsite, ditches, and pits. Courts have held mineral developers liable for harm caused by a defective cattle guard and for harm caused by poisonous substances from a pasture, hole, stream, fresh water pond, or the like which had been polluted by the mineral lessee. Damages often are recoverable where an upstream oil and gas operator allows oil, saltwater, or other refuse to enter a creek or stream and flow through the premises of the surface owner.

The measure of damages is the market value of the livestock at the time of injury where they are killed. The measure of damages is the loss of market value where the injury to the livestock is not fatal. Damages for veterinarian expenses to treat the injured livestock, or loss of milk also can be recovered. Damages for the value of unborn livestock usually are not recoverable. Their loss can be considered measured as the difference in the value of the dam immediately before and after losing the young.

Crops

The measure for damages for crops is the market value of the lost portion. The value is determined at maturity of the crop. Some courts deduct the estimated cost of harvesting and marketing from its market value. The cost of reseeding may be adequate compensation if the damage takes place early in the season.

Other Relief

A surface owner may be entitled to a preliminary injunction to stop the operations of a mineral lessee who does not maintain his operations properly and either causes or threatens to cause extreme damage to the surface. A court may cancel the lease where a mineral lessee fails to protect the surface by not properly drilling a disposal well as required by state regulations.

Section 38-11.1-04 of the North Dakota Century Code requires the mineral developer to pay the surface owner damages for loss of agricultural production and income, lost land value, lost use of and access to the surface owner's land and lost value of improvements caused by drilling operations. The amount of damages is to be determined by any formula that both the surface owner and mineral developer agree upon.