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Well Site Operations & Surface Damages: Assessing Lieabilities and Calculating Damages

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WELL SITE OPERATIONS AND SURFACE DAMAGES:
ASSESSING LIABILITIES AND CALCULATING DAMAGES

I. Proof of Financial Responsibility:

A. Rule B-2 of the General Rules and Regulations of Arkansas Oil & Gas Commission requires an affidavit of financial responsibility or posting of a bond in the amount of $15,000.00 or an irrevocable letter of credit in that amount to secure against damages.

B. The bond or letter of credit shall remain in effect until the requirements of Act 902 of 1983 "have been properly completed and fully performed." That act requires notice to the surface owner and provides a lien on the operators fixture or equipment and oil, gas, and hydrocarbons produced for payment of damages recoverable under the lease or the laws of the State of Arkansas.

II. Leaseholder Rights:

A. Lease provisions:

1. AAPL Form 680: This lease grants a leasehold interest "For the purpose of carrying on geological, geophysical, and other exploration work, and the drilling and operating for, producing and saving all the oil, gas, and other hydrocarbons...."This form also grants the lessee the right to use gas, oil, and water found on the land, except for well water, free of cost. The

lease requires the lessee to bury pipelines below plow depth and pay "reasonable damages" for injury to growing crops, and requires that the well not be drilled closer than 200 feet to any house or barn or other structure. The form also grants lessee the right to remove its equipment at any time.

B. Producers 88: This lease grants lessee rights "For the sole and only purpose of mining operations for oil and gas, and laying pipe lines, and building tanks, power stations and structures thereon, to produce, save, and take care of said products ...."It contains essentially the same provisions on pipe line depth, distance from structures, and damage to crops as the previous form.

C. There are many versions of oil and gas leases in circulation and most contain an express or clearly contemplated right of the lessee to enter on and use the surface:

1. Some leases will be altered by the parties to prohibit surface operations on subject land. Surface operations in violation of this provision would not be simply a claim for surface damages, but would be trespass.

2. Court Decisions: Completely apart from the lease terminology, when there is a severance of the surface and mineral ownership, the mineral owners

have the right, without the consent of the surface owner, to reasonable use of the surface to drill wells. This includes attendant rights such as the right to build access roads and to take out trees, as well as building the pad, fences, etc. Theoretically, there is no liability to the surface owner for a reasonable use of the surface. Diamond Shamrock Corp. v.Phillips, 256 Ark. 886, 511 SW2d 160 (1964); Koury v. Morgan, 172 Ark. 405, 288 SW 929 (1926); LeCroy v. Barney, 12 F.2d 363 8th Cir. (1926); Larco Drilling Operation v. Lee, 207 So.2d 634 (Miss. 1968). Of course, the surface owner rarely concedes that the mineral owner's use is reasonable or is a right for which the surface owner is not entitled to be paid.

III. Duty to Restore Surface:

A. Statutory Duty:

Many petroleum producing states have statutes requiring surface restoration or payment of damages to the surface owner upon either the completion or abandonment of drilling activities. Illustrative statutes are Okla. Stat. Ann. tit. 52 §§ 318.2-318.9 (West 1987); Kan. Stat. Ann. § 55-132 (a) (1983); and S.D. Codified Laws Ann. §§ 45-5A-1 to 45-5A-11 (1983). The closest any Arkansas Statute comes to creating a statutory duty is Ark. Code Ann. § 15-72-213 (1987), which creates a

lien in favor of the surface owner on the fixtures and equipment and production of the operator to secure payment for damages caused by the surface use.

B. Duty implied at law:

1. Arkansas: A duty to restore the surface was recognized in Bonds v. Sanchez-O'Brien Oil & Gas Co., 289 Ark. 582, 715 SW2d 444 (1986). In that case, the Arkansas Supreme Court found an implied duty on the part of the lessee under an oil and gas lease "to restore the surface of the land, as nearly as practicable, to the same condition as it was prior to drilling," upon cessation of operations. Several specific points are worthing noting:

a. The facts of that case virtually assured the result. The operator plugged then abandoned the well but left water pits, concrete slabs, dams, and other materials on the surface. At least according to the opinion, it appears that the operator made virtually no attempt to voluntarily clean up after itself.

b. The Arkansas Supreme Court limited the deed to restore to "as nearly as practicable," rather than "as nearly as possible." Practicable seems to imply something less than the requirement to take every

conceivable step to restore the surface to its exact predrilling condition without regard to costs or benefits. This is consistent with a duty for "reasonable" use of the surface. Although the Arkansas Supreme Court did not define "practicable" other courts have indicated that the term contains a notion of practical advantage or value or commercial reasonability, as distinguished from anything that is physically or mechanically possible.

3. The Arkansas Supreme Court did not discuss in any detail the terms of the lease, so it is as yet unclear to what extent the Bonds Holding can be modified, qualified, extended or restricted by contract.

C. Some courts have found that failing to restore the surface upon completion or abandonment of a well is actionable as a nuisance. Tenneco Oil Company v. Allen, 515 P.2d 1391 (Okla. 1973).

D. In Texas, if the lessee "exceeds" the rights granted under the lease, the lessee is liable to the surface owner as a trespasser. Brown v. Lundell, 162 Tex. 84, 344 S.W.2d 863, 866 (1961). However, Texas courts have held that there is no implied duty to restore the surface and a lease controls the rights of the parties

in this regard. Warren Petroleum Corporation v. Monzingo, 157 Tex. 479, 304 S.W.2d 362 (1957).

IV. Damages:

A. Arkansas:

1. Bonds v. Sanchez-O'Brien Oil & Gas Co. recognized the existence of a duty but did not discuss calculating damages for breach of the duty.

2. There is some indication that the damages for breach of the duty to restore cannot be grossly disproportionate to the actual injury to the land. For example, Benton Gravel Co. v. Wright, 206 Ark. 930, 175 S.W.2d 208 (1943), the defendant, while blasting with dynamite on its own land, negligently caused a well on the plaintiff's land to go dry. The court recognized the time-honored rule that the measure of damages for permanent injury to the land is "the difference in market value before and after the injury." It had been alleged that the property could have been repaired. The Arkansas Supreme Court concluded that if the cost of restoration is less than the difference in value of the land, then cost of restoration as the proper measure of damages; on the other hand, if the cost of restoration is "much greater" than the injury to the land, then the proper measure of damages is

the difference in value. The Arkansas Supreme Court also noted that if either of two measures of damages will compensate the injured party, then the measure which is the least expensive to the defendant should be adopted.

B. Other Jurisdictions

Support for the rule that loss in value to the land is a correct measure of damages if the cost of repair is grossly disproportionate to the loss in value has found support in mineral cases in other jurisdictions as well. Amico Production Co. v. Carter Farms Co., 103 N.M. 0117, 703 P.2d 894 (1985); Peevyhouse v. Garland Coal & Mining Co. 382 P.2d 109 (Okla. 1963); P. G. Lake v. Sheffield, 438 S.W.2d 952 (Tex. Civ. App.1969). Cases from other states involving fact situations other than hydrocarbon exploration also lend support for capping damages at the loss in value to the land. These jurisdictions include Arizona, Maryland, Nebraska, New York, and Pennsylvania.

C. Any express undertaking regarding repair stated in the parties' lease would be a contractual duty, not one imposed by law, and a landowner-plaintiff theoretically could insist on strict adherence to the contract terms or damages to adequately perform that function himself.

V. Trial Strategy Considerations:

A. Venue.

B. Witnesses.

1. On-site exploration company personnel to explain what was done and why it was necessary and reasonable for drilling and operating the well.
2. Restoration personnel to explain the extent of work.
3. Someone to verify how much money was spent on restoration.
4. A credable-appearing real estate appraiser.
5. Surveyor. (Most plaintiffs overestimate how much land has been affected).
6. Experts in "special" cases: Ground water experts, chemists, engineers, etc.

C. Exhibits

1. The deed.
2. The lease.
3. Photographs (a picture is worth a thousand words).
4. Survey of property and amount of surface used.
5. Real estate appraisal.
6. "Special reports".

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