LETTER OPINION
2007-L-07

March 13, 2007

Mr. Lynn D. Helms
Director, Oil and Gas Division
North Dakota Industrial Commission
600 East Boulevard Avenue
Bismarck, ND 58505

Dear Mr. Helms:

Thank you for your letter in which you ask about N.D.C.C. § 38-11.1-04. Chapter 38-11.1, N.D.C.C., provides protections to the surface owners of land burdened by oil and gas exploration and development activities. It is my opinion that damages related to drilling a well must be paid in a single payment; damages incurred thereafter may be compensated by annual payments. It is my further opinion that the law does not require that damage payments be the same to every surface owner in a unit; rather, it requires just compensation. Differing circumstances from tract to tract may require "non-uniform" payments.

Your questions concern N.D.C.C. § 38-11.1-04, which requires oil and gas companies to compensate surface owners for damage and disruptions caused by oil and gas activities. The statute provides in part:

> When determining damages, consideration must be given to the period of time during which the loss occurs and the surface owner may elect to be paid damages in annual installments over a period of time; except that the surface owner must be compensated for harm caused by exploration only by a single sum payment.

You state that oil and gas companies typically refuse to make annual payments, telling landowners that the law requires a single payment. You ask whether N.D.C.C. § 38-11.1-04 requires a single payment in all situations.[1]

The statute provides that when damages are assessed, consideration must be given to the time period during which the loss occurs, "and the surface owner may elect to be paid damages in annual installments." Clearly, the statute does not restrict

[1] Chapter 38-11.1, N.D.C.C., has been challenged, but the attack failed. Murphy v. Amoco Prod. Co., 729 F.2d 552 (8th Cir. 1984) (addressing the due process, equal protection, contract, and taking clauses of the United States Constitution and article I, sections 21 (privileges and immunities) and 22 (special laws) of the North Dakota Constitution).

compensation to one-time payments. It expressly recognizes annual payments and expressly allows the landowner to "elect . . . annual installments."

The statute, after expressing the possibility of annual payments, adds: "except that the surface owner must be compensated for harm caused by exploration only by a single sum payment." The Legislature did not define "exploration," but I understand from your agency that in the oil and gas industry "exploration" typically refers to drilling a well. If minerals are not discovered in paying quantities, the well is plugged. But if drilling is successful, the well is completed and mineral production can continue for decades. In light of the language that "the surface owner must be compensated for harm caused by exploration only by a single sum payment," damages related to exploration, that is, drilling, must be paid in a single payment. Damages that will be incurred thereafter, however, could be compensated by annual payments. Of course, the landowner could choose to accept a single payment for post-exploration damages.

Even though the statute's express language does not require resorting to a secondary source, the legislative history supports the above analysis. A conference committee report states that "except for exploration operations, the bill gives the surface owner the option to receive compensation in annual installments over the life of a well."[2] This distinguishes damages incurred during exploration -- compensable only with a one-time payment -- from post-exploration damages -- compensable by annual payments at the landowner's option. A memorandum in the legislative history states that the bill "gives the surface owner the option to demand annual installments," but that "damages caused by exploration will be compensated for by a lump sum payment."[3]

Dissatisfaction about one-time payments was a reason the bill was introduced.

> [The oil and gas company] usually but not always . . . makes a one time offer to the surface owner for actual surface damage. In the event of a dry hole the compensation may be fair . . . but in the event of production, which may be for 20 or 30 years of (sic) more, the surface owner gets no consideration unless the producer volunteers or the surface owner has to sue in each instance and prove his claim. . . .
>
> We are reluctant to be operating under present practices where the surface owner has to sue in every instance where he feels he has been damaged, and must prove his claim. . . .
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> The trouble with a one time settlement is that there is no way to determine years in advance what actual damage, let alone intangible damages might

[2] Conference Committee Report, HB 1198, 1979 N.D. Leg. (undated).
[3] Memo from Owen Anderson to Sen. Garvin Jacobson, 1979 N.D. Leg. (undated).

> be. For instance, odor in the air, management practices, working around oil equipment, danger to health of humans and livestock, loss of water wells and springs. Then too, salt and oil spills, corrosion on metal buildings, machinery and wire by hydrogen sulfide gas, loss of use of surface, cattle passes, roads, pipelines and traffic, flair (sic) outs, fires, pollution, trespassing and depreciated value of surface.[4]

Your second question concerns payments for damage caused by unit activities. According to your agency, units are not usually established until some years after a field has been producing and the reservoir pressure, and hence mineral production, has decreased but can be revitalized by artificially re-pressuring the reservoir. Injecting water is often used to re-pressure a reservoir and stimulate production. Units, which can cover tens of thousands of acres, provide for the joint operation of all wells and other facilities in the unit area.

You ask whether N.D.C.C. § 38-11.1-04 requires unit operators to pay the same damages to each surface owner in the unit. For example, the operator might conclude that a certain sum is adequate compensation for the presence of a well and propose that each person owning land burdened by a well should be paid that sum. Or the operator might calculate road damages on a per-rod basis and offer compensation on this basis to all landowners. Such a method assumes that all landowners suffer the same injuries, that the characteristics and circumstances of each parcel and each landowner are the same, or nearly so. While such an approach to compensation could theoretically satisfy the statute, it is possible, and even likely that, from parcel to parcel, there are differences in the land and the uses to which it is put. I understand that the Cedar Hills South Unit in Bowman County covers about 55,000 acres and currently has 121 producing wells and 128 water injection wells. It would seem unlikely that all unit wells and other facilities have the same consequences for the tracts they burden.

Nothing in N.D.C.C. § 38-11.1-04, or any other part of N.D.C.C. ch. 38-11.1, requires that a unit operator make the same damage payments to all landowners. The statute requires operators to pay a sum "equal to the amount of damages sustained," an amount to be determined "by any formula mutually agreeable" to the operator and landowner. How the operator carries out the duty to pay "damages sustained" is initially its prerogative. Uniform payments could be acceptable provided each landowner receives adequate compensation for whatever damage he sustains. But the law does not require that damage payments to every surface owner in a unit be the same. What is required is that they be "justly compensated."[5]

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[4] Hearing on H.B. 1198 Before the House Comm. on Natural Resources, 1979 N.D. Leg. (Jan. 18) (Statement of Rep. Murphy). See also id. (Statement of Joyce Byerly, McKenzie County Grazing Association).

[5] N.D.C.C. § 38-11.1-01(3).

Sincerely,

Wayne Stenehjem
Attorney General

cmc/pg

This opinion is issued pursuant to N.D.C.C. § 54-12-01. It governs the actions of public officials until such time as the question presented is decided by the courts.[6]

[6] See State ex rel. Johnson v. Baker, 21 N.W.2d 355 (N.D. 1946).