STATE OF NEW MEXICO
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
OIL CONSERVATION COMMISSION

APPLICATION OF THE NEW MEXICO OIL CONSERVATION DIVISION FOR REPEAL OF EXISTING RULE 50 CONCERNING PITS AND BELOW GRADE TANKS AND ADOPTION OF A NEW RULE GOVERNING PITS, BELOW GRADE TANKS, CLOSED LOOP SYSTEMS AND OTHER ALTERNATIVE METHODS TO THE FOREGOING, AND AMENDING OTHER RULES TO MAKE CONFORMING CHANGES; STATEWIDE.

CASE NO. 14015

OIL CONSERVATION DIVISION'S TRIAL BRIEF

The Oil Conservation Commission (the Commission), by Order R-12819-A, issued on October 25, 2007, as modified by Order R-12819-B, issued on November 1, 2007, directed the parties to brief certain legal issues pertinent to this case. The Oil Conservation Division (the Division) submits this brief in response to the Commission's orders.

Surface Owner Consent Requirement

Section 19.15.17.F(1)(c) requires written consent from the surface owner as a prerequisite to onsite closure of any pit or drying pad. Briefing has been requested concerning:

> whether [this provision] violates the subsurface owners [sic] right to reasonable use of the surface and whether the Oil Conservation Commission has the authority to require surface owner consent.

The first of these questions is easily answered as to lands to which the Surface Owner Protection Act [NMSA 1978, Sections 70-12-1 through 70-12-10 (2007) (the SOPA)] applies. As to such lands, a mineral owner has a mandatory, statutory duty to restore the surface, and accordingly, doe not have a right to permanently bury waste on site except pursuant to an agreement with the surface owner.

A. The subsurface, except for the actual minerals, is part of the surface estate. Accordingly, a mineral owner or oil and gas lessee has no right to bury waste on leased premises, except pursuant to an implied right to use the surface for oil and gas operations.

An oil and gas operator's statutory obligation to reclaim the surface applies to the area beneath the literal surface of the ground where waste might be buried. This is because the subsurface is legally part of the "surface estate," conveyed to or retained by the surface owner when a mineral estate is severed by patent, deed or oil and gas lease. The mineral reservation or grant does not vest a mineral owner with title to the subsurface. It merely gives the mineral owner title to the minerals that are in the subsurface, together with the right to use so much of the "surface estate" (ground surface and/or subsurface) as are reasonably necessary for extraction of the minerals.

The clear majority of jurisdictions that have addressed the issue have held that the mineral estate includes only the oil and gas native to the formation, unless the conveyance or severance of the mineral estate explicitly states otherwise, and therefore the surface owner retains possession of the subsurface pore space, including the sole right to store substances, such as non-native gas or produced water, in the vacated space, after the mineral estate has been removed.

The mineral interest retains the right to access the minerals as long as there remain minerals to extract, but the surface owner has the residual right to the subsurface. *Westerman v. Pennsylvania Salt Mfg. Co*, 260 Pa. 140, 146 (1918); accord *Tate v. United Fuel Gas Co.*, 137 W.Va. 272, 71 S.E.2d 65 (1952). In *Westerman*, the Supreme Court of Pennsylvania held that the coal mining interest had "no perpetual right of way" through the land and that "its right will cease when the coal therein is exhausted or abandoned." Westerman, 260 Pa. 140, 146. Years

later, the West Virginia Supreme Court of Appeals ruled in accordance with Pennsylvania, holding that the vacated space following mineral extraction remains the property of the surface owner. *Tate*, 137 W.Va. 272, 282, 71 S.E.2d 65, 72 (1952).

In the leading case of *Emeny v. United States*, 188 Ct.Cl. 1024, 412 F.2d 1319 (1969), the Court of Claims held that the surface owner retains ownership of the pore space, observing that "[t]he surface of the leased lands and everything in such lands, except the oil and gas deposits covered by the leases," were still the property of the respective landowners. This included the geological structures beneath the surface, including any such structure that might be suitable for the underground storage of 'foreign' or 'extraneous' substances produced elsewhere. *Emeny*, 412 F.2d 1319, 1323. See also *Ellis v. Arkansas Louisiana Gas Co.*, 450 F.Supp. 412 (E.D. Okla. 1978) *aff'd* 609 F.2d 436 (10th Cir. 1979) (holding that it is the surface owner's privilege to grant storage rights, and that it is "the American view is that the cavern is owned by surface owners"); *Department of Transportation v. Goike*, 560 N.W.2d 365, 365-366 (Mich. Ct. App. 1997) (holding that subterranean storage space, once it has been evacuated of the minerals and gas, belongs to the surface owner, and that a mineral right is a right to the minerals themselves, not to the land surrounding the minerals); *Pomposini v. T.W. Phillips Gas & Oil Co.*, 580 A.2d 776 (Pa. Super. 1990) *aff'd sub nom. Keppel v. Fairman Drilling Co.*, 615 A.2d 1298 (Pa. 1992) ("the right to extract gas did not include the right to use the cavernous spaces owned by the lessor for the storage of gas in the absence of an express agreement therefore"); M.J. Harvey, Jr., 109 IBLA 31 at 33, GFS (O&G) 1989-75 (May 25, 1989) (to the extent that no valuable minerals underlay the tract in question, the owner of the surface estate rather than the owner of the mineral estate owned the non-mineral strata); and Phillips Petroleum Co., 105 IBLA 345, GFS (O&G) 1989-9 (Nov. 17, 1988) (operator who had consent of surface owner, but not of mineral owner,

was entitled to use a dry hole as a salt water injection well).

This right of the surface owner to the subsurface is somewhat tempered by the continuing rights of the mineral estate as long as there remain minerals to extract. *International Salt Co. v. Geostow,* 878 F.2d 570, 575 (2nd Cir. 1989) (the surface owners were precluded from executing a waste storage contract with a third party to use the excavated space created by the salt mining activities as there still remained minerals in place, and International Salt Co. was using the previously mined sections as a means of access to the un-mined portions of their property). In the *Goike, supra,* the Michigan Court of Appeals clarified the distinction between these rights, holding that:

> [a] surface owner possesses the right to the storage space created after the evacuation of underground minerals or gas, but mineral estate holder may 'store' any fluid minerals or gas native to the chamber that has not yet been extracted, they cannot introduce any foreign or extraneous minerals or gas into the chamber. Only the surface owner possesses the right to use the cavern for storage of foreign minerals or gas, and then only after defendants have extracted the native gas from the cavern. *Goike*, 560 N.W.2d 365, at 366.

While we have not found a New Mexico case that directly ownership of subsurface space, the Court of Appeals opinion in *McNeill v. Rice Engineering & Operating , Inc.,* 133 N.M. 804, 811, 70 P.3d 794 indicates acceptance of the proposition explicated in authorities from other states that an oil and gas lessee's rights to the subsurface exists only to the extent that it is reasonably necessary for the production of oil or gas from the lease.

B. The New Mexico Surface Owner Protection Act prohibits permanent burial of waste on land without agreement of the surface owner.

Prior to enactment of the SOPA, a mineral owner or oil and gas lessee could argue that it had a right to permanently bury production waste underneath the surface if it could establish that such action was a reasonably necessary for production of the minerals. The New Mexico Supreme Court so held in *Amoco Production Co. v. Carter Farms Co.,* 103 NM 117, 703

P2d 894 (1985) (which dealt with waste spread on the surface) so held, and treated the question whether such disposition was reasonably necessary as a fact issue.

The SOPA, however, changes all that. It limits and qualifies the mineral owners' rights to use the surface by imposing a mandatory duty to reclaim the surface so used. There is nothing in the SOPA to indicate that "the surface" is used in that Act in any sense or meaning different from its established common law meaning, which includes the subsurface. Thus, although an oil and gas operator likely has the right to store production wastes on site temporarily as part of the production process, it must eventually remove the wastes as part of its duty to reclaim the surface, unless the surface owner otherwise agrees in writing.

NMSA 1978 Section 70-12-4.C requires that, [a]n operator shall reclaim all the surface affected by the operator's oil and gas operations." Section 70-12-3.C defines "reclaim" as:

> to substantially restore the surface affected by oil and gas operations to the condition that existed prior to oil and gas operations, or as otherwise agreed to in writing by the operator and surface owner[.]

Clearly the permanent placement of wastes on the land in a location where there were no wastes prior to the commencement of oil and gas operations is incompatible with an operator's statutory duty to reclaim. The operator thus only has a legal right to do leave waste on the premises (regardless of any environmental regulation) "as . . . agreed to in writing by the operator and the surface owner."

C. The requirement that an applicant for onsite disposal of waste furnish evidence of surface owner consent is a necessary and reasonable incident of the Oil Conservation Commission's power to establish a permitting regime for waste disposal.

The second question, of course, is, does the Commission have power, as part of a rule establishing a permitting regime governing the permanent disposition of waste, to require an operator seeking a permit for on-site disposal to furnish proof that it has satisfied the prerequisite

(required by the SOPA) to enable it to lawfully implement the disposal method for which it is seeking a permit.

The Commission has the power, pursuant to NMSA 1978 Section 70-2-12.B(21) and (22) to adopt rules regulating the disposition of wastes resulting from oil and gas operations for the protection of fresh water, public health and the environment. Presumably the Commission can exercise this power by requiring permits for disposition of such wastes in particular ways. The Division has presented evidence in this case that such a permitting regime is necessary for effective protection of fresh water, public health and the environment. A logical and reasonable requirement to impose in connection with such a permitting regime is a requirement that the operator seeking a permit present appropriate proof that it has the right, under applicable property laws, to implement the plan for which it seeks a permit. In the case of on site disposition on fee surface lands, the applicable property law is the SOPA which requires written agreement with the surface owner for any plan of reclamation that does not entail restoration of the surface to its original condition.

The Commission has had experience with the difficulties that can arise when the Division issues a permit to an operator to do something it does not otherwise have a legal right to do. Case No. 13942, *Application of Samson Resources Company, etc.,* involved a situation where an operator drilled a well pursuant to a Division-approve Application for Permit to Drill (APD) at a location where the operator had no property right to enter or drill. *See* Order No. R-12343-E, issued March 16, 2007. That Order cites and discusses prior cases involving approval of APDs where the operator's property rights were contested or non-existent, including Case No. 13153, *Application of Pride Energy Company, etc.* and Case No. 12731 [Order No. 12108-C, issued

December 9, 2004] and *Application of TMBR/Sharp Drilling, Inc. etc* [Order No. 11700-B, issued April 26,2002]. In Order No. R-12343-E, the Commission admonished that:

> the Commission approves of the language of Division Form C-102, field 17, [requiring an applicant for a permit to drill to certify that it has a property or contractual right to drill at the specified location] and asks the Division to continue its use and to notify the Commission if it plans to discontinue its use.

The Commission's experience with these cases provides ample demonstration of the reasonableness and necessity of including in a permitting rule a requirement that the permit applicant provide proof to the Division that it has the right to do the act for which it seeks a permit. The power to adopt rules for permitting the disposition of waste necessarily includes the power to adopt reasonable and necessary provisions for administering a permitting regime.

D. State and Federal Lands.

The SOPA does not apply to lands where the surface is federal public domain or State trust lands. The right of an oil and gas lessee to use the surface of such lands for any purpose, including waste disposal, would depend, in the former case upon the federal Mineral Lands Leasing Act, 30 USC Section 181 *et seq.*, United States Bureau of Land Management rules and lease stipulations, and in the latter case, upon applicable provisions of NMSA 1978 Chapter 19 and State Land Office rules. In dealing with such lands, however, the Commission and the Division are entitled to rely upon the legal presumption that a public official will do his or her duty, and, accordingly, if an oil and gas lessee has a right to bury waste on lands of the United States or the State of New Mexico, the management agency having jurisdiction of those lands will execute the requisite acknowledgement of that right. If the applicable agency contests the lessee's right to bury waste on such lands, the same reasons exist for the Commission to require

deferral of issuance of a permit until the controversy is resolved as exists in the case of private lands.

In either case, the Commission, by adopting the proposed rule, will not be delegating its power to regulate the disposition of waste to a private person or another agency, nor undertaking to decide who has a property right to control the use of subsurface repositories. It will simply be providing an orderly means for the Division to be assured that it does not license a trespass or a breach of a legal duty mandated by the SOPA or other State or federal laws or rules.

The 100-Mile Radius Provision and the Dormant Commerce Clause

Section 19.15.13.F(1)(a) of the proposed rule requires that an operator proposing on-site closure of a pit or drying pad demonstrate that there is not an available division-approved disposal facility or an available out-of-state disposal facility within a 100-mile radius of the site. This provision in no way infringes upon the so-called "dormant commerce clause" of the federal Constitution.

The "dormant commerce clause" is a doctrine developed by the United States Supreme Court. Under that doctrine, the Court has held that the constitutional grant (U.S. Const. Art. I, Section 8) to Congress of the power to regulate commerce among the several states prohibits states from adopting commercial rules that discriminate against or interfere with interstate commerce even in the absence of applicable federal laws.

The United States Supreme Court has applied the dormant commerce clause to invalidate state solid waste management laws in two distinct situations. First, a state may not prohibit, or discriminatorily tax, disposition of waste originating out of state at a disposal facility within its jurisdiction. *Philadelphia v. New Jersey*, 437 US 617 (1978) (invalidating N.J. law prohibiting

importation of municipal waste into the state for disposal); *Oregon Waste Systems, Inc. v. Dep't of Environmental Quality*, 511 U.S. 93 (1994) (invalidating Ore. law imposing a discriminatory "surcharge" upon disposal of waste generated out of state at an Oregon disposal facility). Second, a state may not require than in-state generated waste be processed at a private, in-state facility. *C&A Carbone, Inc. v. Town of Clarkstown,* 511 U.S. 383 (1994).

The proposed rule is not in any way analogous to provisions invalidated in any of these decisions. It does not prohibit or affect in any way disposal in New Mexico of waste originating in other states. Nor does it require disposal of New Mexico waste in a New Mexico facility in preference to an out-of-state facility.

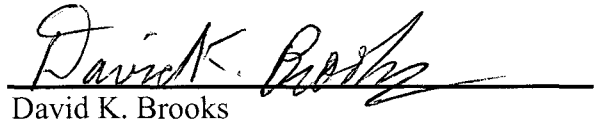
The Division has not found any case invalidating that a state law that *requires*, as distinguished from one that *prohibits,* the disposal of local wastes outside the state. Assuming, however, that such a provision might have dormant commerce clause implications, the proposed rule is not such a provision. The availability of an out-of-state disposal facility within the 100-mile radius may preclude an operator, absent an exception, from disposing of waste on-site, but it does not require that the operator utilize the out-of-state facility. The operator remains free to utilize a permitted in-state facility regardless of the availability of a closer out-of-state facility, and neither the proposed rule, nor Commission Rule 19.15.36 (regarding surface waste management facilities) imposes any restriction on the location of new in-state disposal facilities that are in any way tied to the proximity or availability of out-of-state facilities.

It is true that a state may not impose commerce restricting requirements based on a radius, or other geographical restricted area, that have the effect of limiting interstate commerce, even if the restriction applies equally to in-state business. Thus, in *Fort Gratiot Landfill v. Michigan Dep't of Natural Resources,* 504 US 353 (1992), the Court struck down a Michigan

law that prohibited a disposal facility from accepting out-of-county wastes, even though it applied in the same manner to wastes from other counties in Michigan as it did to out-of-state waste, and in *Dean Milk Co. v. Madison*, 340 US 349 (1951), it similarly struck down a local ordinance that prohibited sale in a town of milk unless it was Pasteurized within a five-mile radius of the town. The laws invalidated in these cases, however, were laws that inhibited intestate commerce, and the cases only stand for the proposition that a state cannot justify a law inhibiting interstate commerce merely because it also inhibits some intrastate commerce. The proposed rule is not such a law. There is no situation in which the proposed rule requires an operator to dispose of waste in-state rather than at a licensed out-of-state facility, and it has no application whatever to disposal of out-of-state waste.

The federal constitutional doctrine dormant commerce clause does not impact the proposed rule.

RESPECTFULLY SUBMITTED,



David K. Brooks
Assistant General Counsel
Energy, Minerals and Natural Resources
Department of the State of New Mexico
1220 S. St. Francis Drive
Santa Fe, NM 87505
david.brooks@state.nm.us
Phone: (505)-476-3450
FAX: (505)-476-3462

Attorney for The New Mexico Oil
Conservation Division