

## **Conflict Looms Over Federal and State Regulation of Access to Federal Oil & Gas Leases on Split-Estate Lands<sup>1</sup>**

Large areas of the Rocky Mountain West were settled under federal laws that transferred ownership of surface lands, but which retained the rights to the subsurface mineral estate, including ownership of oil and gas deposits, in the United States. Lands in which such dual ownership exists are known as a “split-estates” and as a result of such divided ownership the interests of the holders of the surface estate have sometimes been in opposition to individuals seeking to develop the mineral interests. This conflict has been perhaps most evident in the development of federally owned coalbed natural gas which can have significant implications for both estates due to the production of significant amounts of water at the surface.

In response to the tension between the interests of owners of split-estates, new and potentially incompatible efforts to regulate the development of oil and gas reserves on split-estate lands are being pursued at both the federal and state level. In the federal arena, the Bureau of Land Management (BLM) and the Forest Service recently published proposed joint revisions to “Onshore Oil and Gas Order No. 1,” which governs the approval of operations under a federal lease. 70 Fed.Reg. 43349 (July 27, 2005). Among the changes to Order No. 1, which was last revised more than twenty years ago, are regulations pertaining to the development of federal oil and gas leases on split-estate lands. Although public comment on the federal regulations closed on October 25, 2005, and the regulations are yet to be finalized, in their current form they require a lease operator to certify to the BLM that an access agreement with the surface owner has been reached or, in the absence of such an agreement, that a good faith effort to reach such an

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<sup>1</sup>By Richard W. Goeken, J.D. ©2005, all rights reserved. The author is a partner in the Washington, D.C.-based law firm of Saltman & Stevens, P.C. and concentrates his practice on advising clients about contracting for natural resources with the federal government. The author can be reached at (202) 452-2140 or by e-mail at: [rgoeken@saltmanandstevens.com](mailto:rgoeken@saltmanandstevens.com). This article is intended for informational purposes only and does not constitute legal advice.

agreement has failed. If no agreement is reached, the operator must also provide a bond to the BLM for the benefit of the surface owner in the minimum amount of \$1,000. The proposed regulations also specify that:

- Surface owners have the right to appeal the amount of the bond; and
- BLM will carefully consider the views of the surface owner and the effect on the surface landowner's use of the surface before implementing mitigation measures.

Even though the proposed federal regulation is more deferential to surface owners than current federal regulations, the new provisions still have the potential to conflict with a recently enacted Wyoming state statute which provides a different scheme for dealing with conflicts between surface owners and oil and gas developers. See Wyoming Statutes, §§ 30-5-401 through 30-5-410. The Wyoming law, which went into effect on July 1, 2005, provides higher minimum bond amounts than the proposed federal regulation and an elaborate system under state law procedures for determining and providing compensation to aggrieved surface estate holders for a wider range of economic injuries.

Although the new state law would clearly apply to situations where the mineral estate and the surface estate are held by two non-federal owners, a question not squarely answered by the new Wyoming statute, however, is its applicability to split-estates where ownership of the mineral interest is held by the federal government. By its terms the statute appears to apply broadly to any oil and gas operator having the right to "any oil or gas underlying the surface of land." (Emphasis added). In fact, both the Wyoming Attorney General and spokesmen for the Governor have been quoted in the press stating their belief that the statute applies to split-estates involving federal oil and gas ownership. Moreover, the Wyoming Oil and Gas Commission is

also of the view that the statute applies to federal oil and gas interests and is presently pursuing regulations to that effect.

In response to the position of the Wyoming officials, the Director of the BLM submitted comments to the Wyoming Oil and Gas Conservation Commission that clearly expressed BLM's opposition to the application of the statute, and any regulations promulgated under it, to federal oil and gas interests:

The recent Wyoming statute and the proposed regulations would impose additional financial requirements that would burden the federal mineral estate, e.g., liability for loss of production and income, liability for loss of land value and duplicative bonding requirements to both the United States and the Wyoming OGCC. The statute and regulations could also impose potential delays in approval of operations on federal leases. . . . In light of the legal concerns posed by application of [the Wyoming statute] **we believe that the statute and regulations implementing the statute are limited in application to [the] state and private mineral estate.**

(Emphasis added). Letter dated June 13, 2005, from Kathleen Clarke, Director, BLM to Don J. Likwartz, Wyoming Oil and Gas Supervisor. Among the legal concerns specifically identified by the BLM, was the state's "improper" attempt to impose new economic burdens on existing interests of federal leaseholders.

Despite BLM's strong opposition to Wyoming's attempts to regulate access to federally owned oil and gas deposits on split-estate lands, other states in the Rocky Mountain West are also considering legislation to address split-estate issues. For example, in April of 2005, Montana passed H.B. 790, which required the Montana Environmental Quality Council to conduct a study of split-estate lands. The study is to address the issues of bonding requirements, the reclamation of surface property affected by coalbed methane development as well as the relationship between federal law and state law with regard to split-estates. The study, which is presently on-going, is to be completed by September 15, 2006, at which time the

Environmental Quality Council is to report back to the legislature regarding its findings and recommendations, including any recommendations for legislation. The committee tasked with performing the study recently held a meeting in Sheridan in an effort to better understand Wyoming's approach to and experience with split-estate legislation. As was the case with the Wyoming statute, it is quite likely that any attempt by Montana to regulate access to federally owned oil and gas deposits will again be met with strong opposition by the BLM.

In an apparent effort to head-off direct conflict in Wyoming, Montana, and elsewhere, Congress, as part of the Energy Policy Act of 2005, directed the Secretary of the Interior to review the current policies and practices with respect to management of federal subsurface oil and gas development and their effects on private owners of surface rights. The Secretary, who directs the activities of the BLM, is to report her findings to Congress by February 26, 2006, including making recommendations for administrative or legislative action necessary to facilitate reasonable access to federal oil and gas leases while also addressing surface owners concerns and minimizing impacts to private surface owners. Toward this end, BLM has named a national ombudsman for split-estate issues and has directed each of the state offices in the Rocky Mountain energy-producing states (i.e., Montana, Wyoming, Colorado, Utah and New Mexico) to establish points of contact for split-estate issues, with the goal of developing a strategy for identifying and resolving split-estate issues.

It remains to be determined whether or not a compromise can be found for the looming conflict between the various approaches to split-estate ownership currently being pursued by federal and state authorities. Generally speaking, however, in the event of a direct showdown between incompatible federal and state laws, the state law is typically required to yield and the federal law is declared to be the law of the land. Of course, determining precisely when such

incompatibility exists and, when it does, the extent to which all or just a part of the state law is to be supplanted can present difficult legal questions. In the meantime, owners of federal leases on split-estate lands are left with many unsettled issues regarding how best to proceed with development.