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SFA**BILL ANALYSIS**

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House Bill 4280 (as reported without amendment)
House Bill 4281 (Substitute H-1 as reported without amendment)
Sponsor: Representative Larry DeVuyst
House Committee: Conservation and Outdoor Recreation
Senate Committee: Natural Resources and Environmental Affairs

CONTENT

The bills would amend Part 615 of the Natural Resources and Environmental Protection Act (NREPA), which pertains to the regulation of oil and gas wells, to describe the postproduction costs that could be deducted from a lessor's royalties; to specify the provisions of a division order for the payment of royalties under a lease; and to impose penalties on a person who violated House Bill 4281 or Public Act 127 of 1998.

House Bill 4281 (H-1) provides that a person who entered into a gas lease as a lessee after the bill's effective date, could not deduct from the lessor's royalty any portion of postproduction costs unless specifically allowed by the lease. If a lease explicitly provided for this deduction, the lessee could deduct postproduction costs only for the following items, unless the lease explicitly and specifically provided for the deduction of other items:

- Removal of carbon dioxide, hydrogen sulfide, molecular nitrogen, or other constituents, except water, whose removal would enhance the value of the gas.
- Transportation after the point of entry into a pipeline system (as described in the bill).

The bill also would prohibit a lessee from charging postproduction costs incurred on gas produced from one drilling unit, pooled or communitized area, or unit area, against a lessor's royalty for gas produced from another drilling unit, pooled or communitized area, or unit area.

A person who entered into a gas lease as a lessee before or after the bill's effective date, and who charged the lessor for any portion of postproduction costs, would have to give the lessor written notice of the availability of a specific itemized explanation of all postproduction costs to be assessed. If the lessor requested this information, the lessee would have to provide it.

A division order or other document from a lessee that stipulated how production proceeds were distributed could not alter or define the terms of a lease, unless it was voluntarily agreed to by both parties. As a condition for the payment of royalties, a lessee or other payor would be entitled to a signed division order from the payee containing only provisions specified in the bill, unless both parties had voluntarily agreed to other provisions.

The bill would repeal the tie-bar provision of Public Act 127 of 1998. The Act proposed to add Section 61503a to the NREPA to require the lessee on a gas production lease to provide the lessor with monthly revenue statements itemizing deductions taken from the lessor's royalties and listing the unit price received by the lessee for gas sold, and to have an annual financial audit of the lessee's operations. The Act was tie-barred to House Bill 4259, which was not enacted. As a result, Public Act 127 has not taken effect.

House Bill 4280 provides that a person who knowingly violated Section 61503a (the section created by Public Act 127 of 1998) or House Bill 4281 would be subject to a civil fine of up to \$1,000. A default in the payment of a civil fine or costs ordered under this provision, or an installment of the fine or costs, could be remedied by any means authorized under the Revised Judicature Act. The Attorney General or the lessor of a gas lease could bring an action in circuit court for injunctive relief or damages, or both, against a violator.

Further, if a person who had entered into a gas lease as a lessee violated Section 61503a or House Bill 4281, each day the violation continued would constitute a separate offense for five days only; each day thereafter, it would not constitute a separate offense. If a lessee's violation would affect more than one lessor having an interest in the same well, pooled unit, or unitized area, the violation as to all lessors would constitute only one offense.

If a court found that a lessee had deducted postproduction costs from a lessor's royalty contrary to House Bill 4281, the lessor could recover as damages the amount deducted contrary to House Bill 4281. In addition, a party who prevailed in litigation could recover reasonable attorney fees that were incurred in bringing an action if the court found that the position taken by the nonprevailing party was frivolous.

A person could not bring a court action unless the person had first given the lessee written notice of the alleged violation of Section 61503a or House Bill 4281, with reasonably comprehensive details, and allowed a period of at least 30 days for the lessee to cure the alleged violation.

The bills would take effect 90 days after their enactment and are tie-barred to each other.

Proposed MCL 324.61503b (H.B. 4281)
Proposed MCL 324.61503c (H.B. 4280)

Legislative Analyst: N. Nagata

FISCAL IMPACT

The bills would have no fiscal impact on State or local government.

Date Completed: 12-2-99

Fiscal Analyst: P. Graham

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.