

Severing Wind Rights Raises Legal Issues

Recent efforts to create a new estate relating to wind energy could create uncertainties for developers, landowners, banks and title insurers going forward.

BY KATHLEEN D. KAPLA & CRAIG TRUMMEL

Let's start with a hypothetical scenario: Landowner 1 severs the wind rights over his property from his surface estate (i.e., the land). Landowner 1 sells the wind rights to Landowner 2, who then enters an agreement with a wind energy developer for a project on and across all of Landowner 1's property.

Recent attempts to sever the wind rights or wind interests from the surface estate have created uncertainty for wind energy developers, landowners (and those who later buy the land), title insurers and financing parties. As wind-rights severances become more pervasive, the industry may see significant disputes arise among landowners, oil and gas lessees, wind developers and other interested parties until the courts or state legislatures settle the issue of whether wind rights may be severed from the surface estate.

Wind energy is a relatively new legal area, and the land agreements that form the basis of all wind projects are largely creations of contract law combined with real-property law. An agreement between a landowner and a wind energy developer to develop and operate a wind energy project on the land typically involves a term, consideration paid to the landowner and various rights granted to the developer to access the property, construct

and operate wind turbines and related facilities on the property, and use all of the wind resources on the property.

These rights are granted by the landowner because it owns the surface, which must be used and traveled to construct and operate a project. As an incident of surface ownership, the landowner has a right to the air above the land – generally to a reasonable altitude necessary for the landowner's use and enjoyment of its property. The question that has arisen in recent years is whether the landowner may sever its right to the air above its land and, if so, what impact such a severance might have on the landowner's remaining interest, any sub-surface owner or lessee, and the wind developer.

Wind rights are generally not recognized under the law as severable from the surface estate. To date, only one court has upheld the severance of a "wind right" from the fee interest in the underlying property.

In *Contra Costa Water District v. Vaquero Farms*, a California case involving the condemnation of a surface estate, the court analogized the right to develop wind projects to the right to develop oil and gas, and held that the right to generate and transmit electrical energy from wind turbines on the property need not be acquired by a condemnation au-

thority, but could be severed from the surface estate.

On the other hand, in *Romero v. Bernell*, a New Mexico federal court rejected the wind/oil analogy and instead analogized wind to water, holding that wind rights were not capable of a separate valuation because they had no value until reduced to possession. Whether other courts adopt either analogy remains to be seen. Simply put, the legal distinctions among the nature of oil and gas, versus the right to explore for oil and gas, and the nature of oil and gas once severed from the real estate – like the distinctions of water ownership and priority – could become muddled when applied to wind.

Perhaps more importantly, any existing hierarchy or priority of property interests (mineral, surface and pore) under state law could have significant implications for landowners and developers. If courts and legislatures allow the severance of wind rights, they will need to address the priority of the wind interest vis-à-vis the surface-estate owner, any sub-surface-estate owner or lessee, and any pore-estate owner, in addition to the regulatory and developmental practicalities of wind development, the insurability of the wind estate and any leasehold interests granted by the wind interest holder. It may be

A Word About Estates

In the U.S., there are distinct real-property interests that can be severed and sold or transferred. The most common interest severed from land is the mineral estate. One can envision the mineral estate, in its simplest form, as composed of valuable materials under the ground, including oil, gas and hardrock minerals, and the surface estate as being the house and the garden. In some states, the severable estates include sand and gravel, the pore estate and, as discussed, the

wind estate. In the law of minerals, the mineral estate is dominant to the surface estate.

The law recognizes that without use of the surface, you cannot get to the minerals. The law requires that use of the surface by the mineral estate be reasonable, but if you buy a property with the mineral estate in someone else's hands, they could dig up your garden to get out the gold, theoretically.

The ability to dig up the garden is a result of the law establishing

the mineral estate as dominant to the surface estate. The law also may give preferential use of the surface to those who have priority, which means that those who are first have preference in use of their right.

Priority may be an issue with the severance of wind rights and the other estates, because the states and the common law have not ruled on where the wind estate fits, except in Nebraska, North Dakota and South Dakota.

– *Kathleen D. Kapla & Craig Trummel*

for these highly practical and legal reasons that three states (Nebraska, North Dakota and South Dakota) have enacted statutes prohibiting the severance of any wind rights or wind interest from the surface estate. Legislation in Colorado that would have allowed the severance of wind interests was shelved indefinitely during the 2010 session.

With respect to the hierarchy of severable estates, as a general matter, the mineral estate is the dominant estate, and the mineral-estate owner is accorded implied rights to do what is consistent with ordinary custom and usage, such as the right to construct roads, erect storage tanks, and so forth. The priority of a severed wind interest will need to be established, but if a wind estate follows a mineral estate and the surface estate in priority, the right of the wind developer to do what is consistent with ordinary custom and usage may be in conflict with not only the mineral-estate owner's usage, but also those of the surface estate.

Practical wind issues

Any interest received by a wind developer must allow the developer to install turbines, transmission lines and roads, and to keep large areas of adjacent space free of improvements

and vegetation that could impair the flow of wind across the property. If there is a conflict over competing surface use or a non-use – either between the wind developer and the surface owner, or with the owner or lessee of other interests, such as oil and gas – then, in light of their priority, the surface owner's or the subsurface owner's rights may prevail over those of a wind lessee who derived its lease from a wind interest owner, unless the law provides otherwise. As a result, a developer that has an agreement with a wind-rights owner may not have the full scope of rights necessary for the developer's project.

If a wind lease is given by the surface-estate owner, the wind lessee might receive the benefit of the accommodation doctrine, which requires the oil and gas lessee to accommodate existing surface uses where accommodation is reasonably possible, consistent with industry practice and practicable in the confines of the premises. However, it is uncertain whether the accommodation doctrine applies to conflicts of use if the wind lessee's interest is derived from a wind-estate holder who does not also own the surface of the land.

Other open issues arising from the severance and priority of wind rights include the following: Is a

landowner who has priority over the owner of the wind rights bound by a non-interference covenant given to a wind developer? Are hunting lessees, agricultural lessees and other interest holders bound to honor the covenants of such a wind lease? These uncertainties demonstrate that, at present, when a landowner attempts to sever its rights to develop wind from the fee interest in the property – as opposed to granting temporary and defined wind energy leases or easements – there is a risk of diminishing the rights of the surface owner, the wind-estate owner or both, as well as a substantial risk of conflicts among the surface users.

Implications for project permitting

Each state and local permitting authority imposes its own requirements for authorizing a wind project, but, in general, the owner of the land usually must consent to the developer's request for a permit and indicate its consent to the permitting authority.

If the wind rights or wind interests have been severed from the surface estate, a risk arises that the landowner may not only neglect to give its consent to the application, but actually outright oppose it. Again, reconciling the requirements of each permit-

ting regime with the practicalities of a wind-rights severance will be critical for developers and landowners until the courts and legislatures have weighed in on the issue.

Even without the uncertainty of severed wind rights, projects have enough risks, and as with most ventures, parties to a wind project try to minimize risk where possible. One tool for minimizing risk is a title insurance policy.

Insurance and title-review strategies

A title insurance policy provides assurance that the real-property interests secured by the developer are of such a nature to allow the project to operate throughout its lifetime. Assuming that the interest secured by the developer is a leasehold interest, the title company providing the policy determines if the grantors of the lease (i.e., the landowners) have the authority to do so, what encumbrances already affect the property (e.g., liens, easements) and if the lease agreement will create an interest that the title company is willing to insure. Title companies, like all insurance companies, try to minimize risk – risk viewed through a legal lens.

There are exceptions, but generally, as a project progresses through the underwriting process, a property with various competing interests (e.g., oil and gas leases, sand and gravel operations, and a potential wind project) will be viewed as riskier than one without competing interests. If those risks are in the form of interests not born of settled law, such as severed wind rights, the underwriter will demand that the risk be reduced.

One way to ease the underwriter's discomfort is to secure more documentation from the interested parties. More interested parties and greater documentation mean more money. Specifically, the developer will spend more money on legal fees and more time to assure the underwriter that the developer's interest is secure and that the underwriter's risk is minimized. Only with the underwriter's approval is the title insurance policy issued.

Given the uncertainties surrounding the severance of wind rights, developers will want to conduct a careful review of title to the property and all wind energy land agreements. Below are a few recommendations for due-diligence review:

- Review vesting instruments and title exceptions of record;
- Look for terms such as grant or reserve of wind power rights or wind interests;
- Inquire about other parties who may have an interest, of record or not, in the property or its wind development;
- Investigate any pending condemnation or other governmental action relating to the property;
- Review all documents relating to governmental action relating to the property, such as permits and condemnation orders; and
- Analyze all landowner agreements that relate to the granting of any wind rights other than to the wind developer. If wind rights have been severed, the developer should work with counsel to assess the legal, financial and practical risks to the projects. **SNP**

Kathleen D. Kapla is a Seattle-based attorney and the principal and founder of Kapla Law PLLC. She can be reached at kathleen.kapla@kaplalaw.com. Craig Trummel is an attorney based in White Salmon, Wash. He can be reached at craig.trummel@gmail.com.