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BY HAND DELIVERY

October 23, 2014

Gerald L. Deming  
Supervisor, Town of York  
2668 Main Street  
York, NY 14592

*Re: Local Law #1, 2014<sup>1</sup> permitting HVHF in the Town of York*

Dear Supervisor Deming and Members of the Board,

I represent York residents David Rose and Molly Cummings, and submit the following comments in opposition to the above proposed zoning amendment which would permit High Volume Hydraulic Fracturing (HVHF) as a special use within York's Agricultural and Industrial Districts.

The Town of York cannot proceed to adopt proposed Local Law No. 1 (LL1) due to the state's ongoing environmental review, LL1's inconsistency with the Town's Comprehensive Plan and other reasons specified below.

**I. New York's Moratorium on HVHF and DEC's SEQRA Review**

Procedurally, adoption of LL1 is premature given the state's moratorium<sup>2</sup> on the natural gas drilling technique HVHF. As the Board is aware, the state is engaged in an ongoing review of the environmental impacts of HVHF pursuant to the State Environmental Quality Review Act (SEQRA). The New York State Department of Environmental Conservation (DEC) issued a draft Supplemental Generic Environmental Impact Statement (dSGEIS) in 2009 and issued a revised

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<sup>1</sup> "A Local Law to amend and supersede as applicable the zoning map of the Town of York as officially adopted and The Zoning Ordinance of the Town of York, Livingston County, New York to modify various definitions and substantive sections throughout the entirety of The Zoning Ordinance of the Town of York."

<sup>2</sup> Executive Order No. 41, Governor Paterson (12/13/10), extended by Governor Cuomo.

dSGEIS in 2011. HVHF is extremely controversial as DEC received 13,000 public comments on the initial dSGEIS and an additional 60,000 public comments on the revised dSGEIS.

DEC has been the lead agency in examining the potentially significant impacts of HVHF as it has “the principal responsibility for carrying out or approving” the action in question. ECL§8-0111(6).

SEQRA provides that once a lead agency is established to examine the environmental impacts of an action – with no objections from any other agency - then no other agency may take priority in issuing findings concerning that action. Thus, it is DEC’s sole responsibility to assess HVHF’s potential impacts and choose among alternatives to ensure that adverse environmental impacts are minimized to the maximum extent practicable. 6 NYCRR §617.11(d)(5).

Here, the Town has proposed adopting LL1 to permit HVHF in its Agricultural and Industrial Districts.

However, the Town is not authorized by DEC’s regulations to conduct and complete its own competing SEQRA review of HVHF at this time. Indeed, no other agency, including the Town of York, may usurp DEC’s role as lead agency and issue findings prior to DEC’s issuance of SEQRA findings.

Moreover, as a practical matter there are no DEC regulations that permit HVHF and the state’s moratorium remains in effect. Though DEC proposed new HVHF rules and regulations on September 28, 2011, the rulemaking time period expired on February 27, 2013 with no new rules adopted. Thus, HVHF will not be permitted until after the state lifts its moratorium and republishes a new notice of rulemaking in the New York State Register and completes rulemaking.

Should the Town proceed to enact LL1 it will be an empty exercise subject to judicial reversal.

## **II. HVHF’s Inconsistency with the Town’s Comprehensive Plan**

New York’s zoning enabling statutes (the state statutes which give cities, towns and villages the power to enact local zoning laws) all require that zoning

laws be adopted in accordance with a comprehensive plan. The comprehensive plan provides the backbone for the local zoning law. Town Law §263.<sup>3</sup>

[Z]oning changes must indeed be consonant with a total planning strategy, reflecting consideration of the needs of the community.... What is mandated is that there be comprehensiveness of planning, rather than special interest, irrational *ad hocery*.

*Town of Bedford v Village of Mount Kisco* 33 NY2d 178 (1973).

Here, York's inexplicable decision to move ahead and enact a new zoning law to allow HVHF has no basis in the Town's Comprehensive Plan (2006 Update). Though a number of gas wells have been drilled in York gradually over a long period of time, neither HVHF or any gas drilling is mentioned in the Comprehensive Plan or in the Town's Code. Indeed, it appears York has never categorized or quantified potential impacts of drilling practices.

Regarding the Comprehensive Plan's identification of industrial uses it states:

Efforts will be undertaken to attract new industrial employers to sites in Piffard and Retsof in order to broaden the Town's property tax base, with particular emphasis in the area covered by the Empire Zone.

The Town's industrial development program will include the infilling of existing industrial areas as well as the identification and promotion of new sites for industrial development, with emphasis on supporting and marketing the Empire Zone. The purpose of the Town's industrial development program will be to provide opportunities for local employment and to strengthen the tax base without compromising the quality of the Town's residential character. (At pgs. 6-8).

Industrial uses are so limited in York (1.4% of the Town's area) that the Comprehensive Plan suggests rezoning industrial areas to other uses – rather than a blanket expansion of industrial uses - as there “is an abundance of land zoned for

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<sup>3</sup> See New York State Department of State publication “Zoning and the Comprehensive Plan” James A. Coon Local Government Technical Series (2009).



industrial (1,086 acres) but only about a third (417 acres) are currently being used as industrial. (At pg. 17).

Indeed, the Plan envisions limited placement of industrial uses: “Light industrial and industrial activities are appropriately placed near rail lines and in areas with existing industrial activity.” (At pg. 21). The Plan further provides:

Given the proximity of the industrial and light industrial districts to sensitive community uses such as residential areas and the school facilities, the Town should adopt site plan development standards to minimize the potential adverse impacts of new industrial uses on neighboring land uses. Among other things, the standards should address such concerns as access controls both to and from major roads and within industrial parks, as well as buffers to protect non-industrial neighbors.

The Plan recommends working “with County Industrial Development Agency to market industrial land, particularly in the Empire Zone and other areas where appropriate zoning and infrastructure exists” and “[r]equir[ing] buffers between new industrial developments and adjacent residential and public uses to minimize conflicts and negative impacts.”

By contrast, LL1 would allow HVHF in the Agricultural District which comprises approximately two-thirds of York’s land area (not including LL1’s proposed aquifer protection overlay district).

York’s Zoning Code describes the purpose of the Town’s Agricultural District as “provid[ing] for uses compatible with and supportive of agriculture, while limiting residential and non-agricultural development to minimize conflicts between agricultural and non-agricultural uses.” (Id. at §400[A]).

Tellingly, potential conflicts from industrial uses are not even contemplated as extending heavy industry uses throughout the Agricultural District is an entirely foreign concept. The proposed LL1 flatly contradicts York’s Zoning Code and the Comprehensive Plan’s plain language prohibiting the introduction of heavy industrial uses throughout a majority of the Town.

And, HVHF’s claimed beneficial purposes contained in the preamble of LL1 are flatly contradicted by established facts. Specifically, LL1 list five areas



where HVHF is claimed to be beneficial to the Town. The following examines each of these statements.

First, LL1 claims its purpose is to:

*Balance various forms of development that are desirable by the public while protecting the rural character of the Town.*

However, as shown by the public hearing held September 24, 2014, HVHF is not a form of development desired by the public. In fact, LL1 fails to provide any background, logic or geological context in support of its purposes.

Because the law fails to identify which subsurface formations are to be targeted it is important to note that, according to the oil and gas industry, drilling and utilizing hydraulic fracturing to extract natural gas from the Marcellus Shale beneath the Town of York is not considered economically viable.

For example, John Holko, Chief Executive Officer of Lenape Resources who “manages or owns 139 hydraulically fractured natural gas wells in Livingston County, as well as about 350 more in other places”<sup>4</sup> offered his opinion on bringing HVHF to Livingston County:

Truthfully, the likelihood of this type of drilling being above the southern point of Livingston County is pretty limited. If it comes to Livingston County at all it will be the southern edge, and it’s definitely not going to start there. The New York counties which are the focus areas are Chemung, Tioga and Broome. The typical industry map doesn’t have Livingston County on it. Could there be Utica Shale development even deeper? Maybe, but it’s not going to happen today.

In fact, the Marcellus Shale maps show its depth to be less than 1000 feet and therefore considered “uneconomical.” (See Attached Map). Therefore, prior to enacting any zoning to allow HVHF, the Town must address what formations this law is intended to apply to and whether there is a purpose and need for HVHF in York.

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<sup>4</sup> See interview published on a website maintained by the Dryden Safe Energy Coalition, available at <http://drydensec.org/node/141>.

Regarding impacts to community character, DEC has already concluded that based upon experiences in Pennsylvania and West Virginia HVHF may irrevocably alter the character of rural Towns such as York. DEC's revised dSGEIS (pg. 6-317) clearly states:

High-volume hydraulic fracturing operations could potentially have a significant impact on the character of communities where drilling and production activities would occur. Both short-term and long-term, impacts could result if this potentially large-scale industry were to start operations. Experiences in Pennsylvania and West Virginia show that wholesale development of the low-permeable shale reserves could lead to changes in the economic, demographic, and social characteristics of the affected communities.

Second, LL1 claims its purpose is to:

*Protect and encourage farming and agriculture, which is the dominant land use in York.*

The Town of York includes dairy farms including Noblehurst Farms which recently embarked on a \$12 million project, to build a new facility. As Empire State Development President, CEO & Commissioner Kenneth Adams recently stated: "Agribusiness is an important sector of the Upstate New York economy and with WNY Enterprise LLC's dairy processing facility coming online soon we'll be well positioned to access new markets."<sup>5</sup> Noblehurst Farms is within the Agricultural District and therefore maybe negatively impacted by HVHF operations.

As noted by Susan Christopherson, Ph.D. in her comments on the revised dSGEIS:

Recent evidence from Pennsylvania indicates that agriculture and particularly dairy farming may be significantly affected by drilling activity. For example: "(Bradford) county's dairy herd has decreased over the last decade from 30,000 head in 2002 to just under 20,000 head today. Another 15 dairies have been sold since the beginning of the year (2011.)" (Tomes 2011). Although evidence from

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<sup>5</sup> See: <http://regionalcouncils.ny.gov/western-new-york/092013/livingston-dairy-processing-facility>.

Pennsylvania is anecdotal, there is sufficient information to indicate that one of New York's major industries will be negatively affected by HVHF gas drilling...

There are also land use impacts affecting farmers, including impacts not only from the well pads but also from the ancillary industrial facilities, such as "laydown yards" (operations and storage sites), pipelines, and compressor stations. (Tomes 2011).

The American Farmland Trust (2011) has submitted comments on the RDSGEIS that summarize its expert assessment of the impact on agricultural production in New York State:

...the DEC's analysis of the impacts of drilling and hydraulic fracturing to agricultural land is inadequate and encourages specific analysis of the likely impacts of such activities to agricultural land resources. The SGEIS analysis should consider the scale of farmland likely to be converted by both direct drilling activities and the off-site drilling support services and other types of residential and commercial development that is anticipated as a result of natural gas drilling. In addition, it should consider the impacts of such activities to agricultural land values and on the ability of New York farmers to maintain their competitiveness in a global economy.

Thus, LL1 may negatively impact local farms and the impacts upon this critical resource must be addressed by York prior to enacting any law permitting HVHF.

Third, LL1 claims its intent is to:

*Encourage new development in the existing hamlets in the Town to protect and promote their social and economic well-being.*

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Again, DEC's revised dSGEIS includes an economic assessment which is not favorable. Its conclusion states, in part:

In addition to the positive fiscal impacts discussed above, local governments would also experience some significant negative fiscal



impacts as a result of the development of natural gas reserves in the low-permeability shale. As described in previous sections, the use of high-volume hydraulic-fracturing drilling techniques would increase the demand for governmental services and thus increase the total expenditures of local government entities. Additional road construction, improvement, and repair expenditures would be required as a result of the increased truck traffic that would occur. Additional expenditures on emergency services such as fire, police, and first aid would be expected as a result of the increased traffic and construction and production activities. Also, additional expenditures on public water supply systems may be required. Finally, if substantial in-migration occurs in the region as a result of high-volume hydraulic fracturing operations, local governments would be required to increase expenditures on other services, such as education, housing, health and welfare, recreation, and solid waste management to serve the additional population.

Socioeconomics, three possible development scenarios are being assessed in this SGEIS to reflect the uncertainties associated with the future development of natural gas reserves in the Marcellus and Utica Shales – a high, medium and low development scenario.<sup>6</sup>

Here, York cannot proceed to enact LL1 without considering HVHF's impacts upon York's local economy, housing market and infrastructure.

Fourth, LL1 claims its intent is to:

*Protect property values by prohibiting uses, buildings and structures that are incompatible with the character of the Town and each of its zoning districts.*

LL1 accomplishes this by prohibiting HVHF in every zone except for York's Agricultural and Industrial Districts. LL1 gives absolutely no reason why HVHF is incompatible with almost every other use in York except for agricultural uses.

Studies show that HVHF is incompatible with virtually every existing use. For example, regarding noise the revised dSGEIS states that:

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<sup>6</sup> Socio-economic Impact Analysis Report, Ecology and Environment, P.C. (E & E) available at: <http://www.dec.ny.gov/energy/75370.html>.

Ambient noise levels in the communities would likely increase as a direct result of drilling and additional traffic at the well pads, and as a result of increased development in the region (see Section 2.4.13). Aesthetic resources and viewsheds could be at least temporarily impacted and changed during well pad construction and development (see Section 2.4.12). *Id.* at 319.

Moreover, HVHF will not protect property values. Devaluation will occur regardless of its zoning classification.<sup>7</sup> HVHF's negative economic consequences have been well-documented. For example:

Title Companies will generally not insure a residential homebuyer from negative impacts arising as a result of underground encroachments unless a recorded agreement, such as a lease, allows for that encroachment. An underground encroachment, such as a wellbore entering a homeowner's subsurface without their consent, would be considered a cloud on title affecting the property's insurability and marketability.<sup>8</sup>

Gregory May, a Senior Vice President for Residential Mortgage Lending with Tompkins Trust Company concurs with this analysis. He authored a "White Paper" in 2011 setting forth a number of basic conflicts caused by using residential properties for industrial uses such as oil and gas drilling. (See Attached "White Paper").

Among Mr. May's findings are:

- Surface or sub surface [oil or gas] rights within 200 feet of a residential structure would not be acceptable for conventional financing in the Secondary market.
- NYS title insurance gas endorsements specifically void title insurance coverage if the premises are used for any commercial venture.
- Lenders are responsible to warrant several items to the investor in the Secondary market that can not be done leaving lenders with significant liability.

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<sup>7</sup> See property value analysis of HVHF at: <http://www.dec.ny.gov/energy/75370.html>.

<sup>8</sup> Statement reviewed and approved by Lee Rhinehart, President of Hudson Valley Abstract, Inc. on March 10, 2014.

- Surface or sub surface [oil or gas] rights within 300 feet of a residential structure or within 300 feet of property boundary lines would not be acceptable for FHA (Department of HUD) financing. Id.

Also in 2011, the New York State Bar Association Journal<sup>9</sup> examined the issue of oil and gas lease impacts upon homeowner's property interests. The article quoted Mr. May in stating:

Even before the drilling commences, many upstate New York homeowners with gas leases cannot obtain mortgages. Bank of America, Wells Fargo, Provident Funding, GMAC, FNCB, Fidelity and First Liberty, First Place Bank, Solvay Bank, Tompkins Trust Company, CFCU Community Credit Union and others are either imposing large buffer zones (too large for many borrowers) around the home as a condition to the loan or not granting a mortgage at all.

Mr. May's reports have been submitted during hearings before the New York State Assembly and the State Senate. Attached herewith is Mr. May's report presented to State Senator Avella on February 4, 2014 as part of the Senate's inquiry into the economics of oil and gas drilling.

May's 2014 report concludes that oil or gas drilling is in direct conflict with most financing options:

These conflicts with commonly accepted lending standards would appear to prohibit any residential property with a gas lease or drilling activity from securing traditional mortgage financing.

The report reiterates financing prohibitions on "surface or sub-surface entry within 200 feet of the residential structure." (Freddie Mac requirements in section 39.4[i].) Id. at pg. 2.

Further, the report indicates the standard NYS mortgage document (Fannie Mae/Freddie Mac form 3033) "adopted by virtually all lenders in New York" prohibits storage or disposal of hazardous substances on residential property. (Section #21 of the standard NYS mortgage document.) Id. at pg. 3.

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<sup>9</sup> "Homeowners and Gas Drilling: Boon or Bust? Elisabeth N. Radow, Esq. (November/December 2011).



Therefore, oil and gas drilling fluids are not authorized under the terms of a standard residential mortgage to be discharged into a property's subsurface.

Also, the 2014 report identifies that homeowner's insurance policies prohibit oil and gas drilling. It identifies that large nationwide insurance companies such as Nationwide and State Farm have clearly stated they do not provide coverage for any losses associated with gas drilling. Were drilling to occur these companies would not renew insurance coverage. The report concludes that "[t]his leaves the home owner and the lender without adequate protection." *Id.* at pg. 4.

As a result, York should not proceed to enact LL1 prior to examining its economic impacts upon York residents.

Fifth, LL1 claims its intent is to:

*Lessen and avoid congestion on Town roads.*

However, permitting HVHF in the Town on two-thirds of its land area will cause significant increases in traffic and congestion. DEC's revised dSGEIS states that one single HVHF well will result in 6,790 one way trips by heavy and light trucks. See revised dSGEIS Table 6.62 - Estimated Truck Volumes for Horizontal Wells Compared to Vertical Wells (New August 2011).

And, the impacts to Town roads are acute:

On collectors and minor arterials, there is a potential for greater impacts from this activity [HVHF] because these routes were often built to lower standards, and thus, heavy trucks would have a much greater impact than other types of traffic. As a result, actual contribution of heavy trucks to road and bridge deterioration would be greater than suggested by their proportion to total traffic. Revised Draft SGEIS 2011, Page 6-314.

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Concerning the impact to York, the Town must examine its infrastructure and the maintenance and repair costs that will be borne by taxpayers should HVHF be approved.

Thus, there is nothing to support the five claims made in the preamble of LL1. Indeed, all the science, studies, experiences in other states and environmental

data either flatly refute or seriously call into question LL1's conclusory claims of HVHF's impacts.

Considering the above, adoption of LL1 would be legally void. That result is precisely what occurred in *Eggert v Town Board of the Town of Westfield*, 217 AD2d 975, 977 (4th Dept, 1995) where the relevant zoning amendment was struck down for failure to comply with the comprehensive plan requirement with the explanation that, "[t]he record does not contain any detailed explanation by the Town Board for changing the permitted uses in the district."

Of additional concern, two members of the Board that may cast votes to enact LL1, David Deuel and Norman Gates, hold gas leases on significant tracts of lands in York and thus maintain a specific pecuniary interest in the Town's adoption of the new zoning permitting HVHF on their lands. Thus, pursuant to General Municipal Law §806 these Board members must recuse themselves from any vote on LL1. (See *Zagoreos v Conklin*, 109 AD2d 281, 286-287 [2d Dept 1985] where decision annulled because decisive votes in favor of zoning application were cast by two ZBA members who were employed by applicant.) See also: Op. Atty. Gen. (Inf.) 92-59 "[m]embers of the city council, who owned multiple parcels of property and who would benefit economically from proposed legislation seeking to amend the city's electrical and plumbing codes, should recuse themselves from participating in the proposed legislation given apparent conflicts of interests."

Moreover, conflicts of interest are not limited to only those specified in General Municipal Law §806. (See *Matter of Tuxedo Conservation & Taxpayers Assn. v Town Bd. of Town of Tuxedo*, 69 AD2d 320, [2d Dep't 1979] where the court held an officer of an advertising firm could not vote on a zoning application by a subsidiary of one of his firm's clients, despite the absence of any interest specifically forbidden by the provisions of the General Municipal Law.)

### **III. The Town of York's Ultimate SEQRA Responsibilities**

Even if DEC eventually issues SEQRA findings on HVHF and issues regulations for the administration of HVHF, the Town would need conduct its own thorough SEQRA review of HVHF's impacts upon the Town of York because "[n]o agency involved in an action may undertake, fund or approve the action until it has complied with the provisions of SEQR. 6 NYCRR §617.3(a).



SEQRA's criteria in determining the significance of an action requires inquiry into whether a project creates "a material conflict with a community's current plans or goals as officially approved or adopted."<sup>10</sup>

Here, as above, analysis of York's Zoning Code and its Comprehensive Plan shows that the heavy industrial use of HVHF is entirely inconsistent with York's land use plans. Moreover, the zoning map of York shows that a majority of the Town is zoned for Agricultural use. Thus, adoption of LL1 would constitute a Type 1 action as defined by SEQRA as it proposes to change the allowable uses in the Town's agricultural District, which comprises more than 25 acres. 6 NYCRR §617.4(b)(2).

Any plan to rezone to allow HVHF would require York to complete an EIS. That EIS would need to examine all environmental impacts that are unique to including consistency with existing land uses, impacts upon infrastructure and the issues discussed in DEC's revised dSGEIS and any other future SEQRA documents including DEC's ultimate SEQRA findings.

And, York's SEQRA review must consider whether enacting LL1 will encourage violation of landowners' rights contrary to the State Constitution and contrary to the policy of New York's Oil, Gas, and Solution Mining Law (OGSML). That policy cautions that natural gas drilling in New York be conducted in a manner that protects the public as well as all landowners' rights.

In this regard, the OGSML assumes a single vertical well<sup>11</sup> would be drilled in each spacing unit to harmlessly drain the migratory minerals beneath all properties within a spacing unit following the common law rule of capture. Under the "correlative rights" theory, all owners within the spacing unit receive a share in the royalties satisfying their economic interest in the drained fluids. However, the Legislature never intended that the establishment of a spacing unit would transfer an owner's *in situ* minerals to a neighboring driller.

In violation of the common law, DEC has implemented a policy interpreting ECL §23-0501 as allowing a wellbore to trespass upon property within the spacing unit by penetrating the subsurface of any property integrated into a well spacing unit pursuant to ECL §23-0901. That policy is triggered by the

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<sup>10</sup> 6 NYCRR §617.7(c)(1)(iv).

<sup>11</sup> DEC's 1992 GEIS relating to oil and gas drilling refers only to vertically drilled wells.



filing of a spacing unit which is established as a matter of law if it conforms with DEC's well spacing criteria.

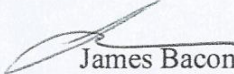
Consequently, any future SEQRA review conducted by the Town must examine the economic impact of HVHF upon owners that do not consent to being placed into a spacing unit and whom should not be subjected to trespass and the taking of their fixed minerals.

In sum, for all of the above reasons, the Town of York must table Local Law No. 1 until:

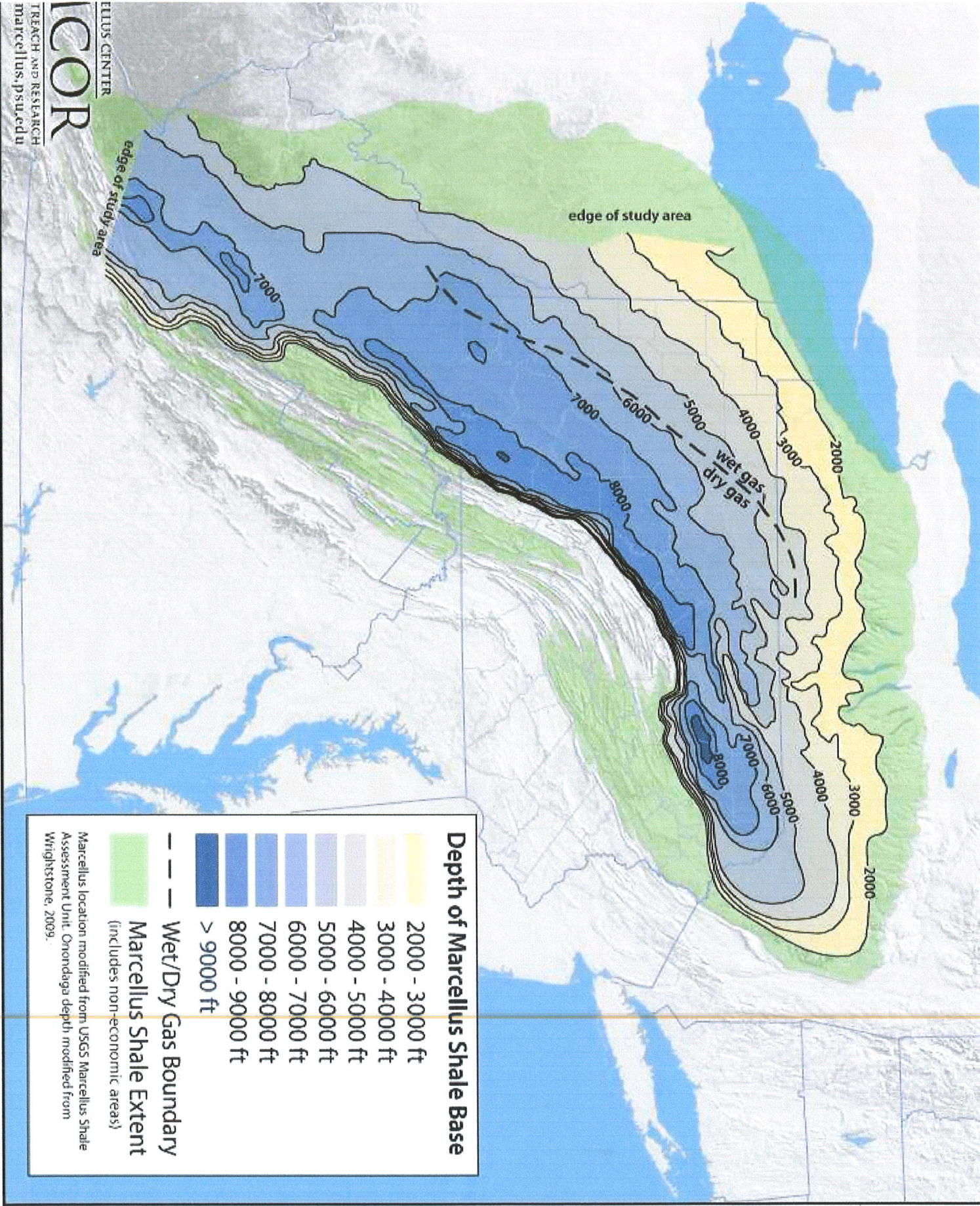
- 1) the state lifts its moratorium on HVHF;
- 2) DEC completes its environmental analysis of HVHF;
- 3) DEC completes its rulemaking process and issues HVHF regulations;
- 4) York revises its Comprehensive Plan to address HVHF;
- 5) York completes a SEQRA review of any proposed HVHF rezoning, and;
- 6) The Town Board members casting votes in favor of HVHF rezoning have no conflicts of interest.

Should the Town proceed to enact Local Law No. 1 prior to completion of the above, its decision on its face will be arbitrary, capricious and an abuse of discretion as defined by CPLR Article 78. And, any petitioner challenging the law would likely request costs and attorneys fees considering the Town has now been placed on notice that adopting LL1 would be a legally baseless act.

Respectfully submitted,

  
James Bacon





**Depth of Marcellus Shale Base**

- 2000 - 3000 ft
- 3000 - 4000 ft
- 4000 - 5000 ft
- 5000 - 6000 ft
- 6000 - 7000 ft
- 7000 - 8000 ft
- 8000 - 9000 ft
- > 9000 ft

--- Wet/Dry Gas Boundary

Marcellus Shale Extent  
(includes non-economic areas)

Marcellus location modified from USGS Marcellus Shale Assessment Unit, Onondaga depth modified from Wrightstone, 2009.



**Gas and Oil Leases**  
**Impact on Residential Lending**  
by Greg May  
VP – Residential Mortgage Lending Tompkins Trust Company

March 24, 2011

**NOTICE**

**The information in this presentation is general in nature and is to be used only for informational purposes.**

**Consult with a Real Estate Attorney to address specific issues as they relate to a specific property or lease.**

**No opinion is being expressed or implied on the practice of leasing mineral rights, environmental impact or regulations surrounding gas and oil leases.**

**Summary Points**

- 1) There is not a cost effective or reliable way to determine if a residential property has a gas lease to allow an Appraiser to establish an appraised value. Title examinations of each property would add significant cost to each transaction in NYS.
- 2) Surface or sub surface rights within 200 feet of a residential structure would not be acceptable for conventional financing in the Secondary market.
- 3) NYS title insurance gas endorsements specifically void title insurance coverage if the premises are used for any commercial venture.
- 4) Lenders are responsible to warrant several items to the investor in the Secondary market that can not be done leaving lenders with significant liability.
- 5) NYS licensed Appraisers are not able to consider the impact on value if a gas lease exists as noted in item #1 above and hence their Appraisals would not meet Secondary market requirements.
- 6) Surface or sub surface rights within 300 feet of a residential structure OR within 300 feet of property boundary lines would not be acceptable for FHA (Department of HUD) financing.



Summary Points  
Gas and Oil Leases as they relate to Residential Lending  
Greg May, VP, Residential Mortgage Lending – Tompkins Trust Company  
March 24, 2011

For purposes of this discussion, I will utilize the word “lender” or “bank” to refer to traditional banks as well as credit unions and mortgage bankers.

In general terms, banking regulators on a federal and state level monitor how much a bank has in lending compared to deposits and assets. The regulators also establish certain requirements for bank liquidity, funds not loaned or pledged in some fashion, in an effort to provide for a sound financial system. The same holds true for credit unions and their regulators.

In an effort to provide a steady and potentially unlimited source of funding for residential mortgage loans, the secondary market was established and remains one of the only consistent methods for lenders to provide affordable and consistent funding for residential mortgage lending. Most lenders utilize secondary market standards for underwriting and property review. These standards allow a lender to sell loans to Fannie Mae, Freddie Mac or other investors because of the known and accepted standards and a track record of performance.

In addition, to secure the FHA Insurance or VA Guarantee, these government programs have established similar underwriting and minimum property standards that are required to be followed.

Without the mortgage secondary market, banks would only be able to lend based on the assets (or deposits) they have available. Once those assets are fully loaned, they would not be able to lend additional funds until one of the current loans were paid in full. With the secondary market, banks are able to lend, sell the mortgage to Fannie Mae, Freddie Mac or another investor and then relend those same funds to another borrower. This process provides for a consistent, equitable and affordable method for borrowers to purchase homes.

The issue of leased land to gas or oil companies creates challenges for banks. Below is a summary of those challenges linked to the numbers noted on page one:

- 1) Secondary market requirements establish property value for residential properties by comparable sales (similar properties that have sold within a short time and distance from the subject). Since there is not a reliable mapping system to identify properties with gas leases, the appraiser is not able to identify potential comparable properties. In addition, many gas leases only have a memorandum of lease recorded which do not provide the necessary details to compare leases.

- 2) Secondary market requirements state (Freddie Mac guide 39.4 (i)):
  - a. Exceptions for outstanding oil, gas, water or mineral rights are **acceptable if commonly granted** by private institutional Mortgage investors in the area where the Mortgaged Premises are located, and:
    - i) The exercise of such rights will not result in damage to the Mortgaged Premises or impairment of the use or marketability of the Mortgaged Premises for residential purposes and **there is no right of surface or subsurface entry within 200 feet of the residential structure**, or
    - ii) There is a comprehensive endorsement to the title insurance policy that affirmatively insures the lender against damage or loss due to the exercise of such rights
  
- 3) A title insurance comprehensive endorsement in NYS contains the following restrictions which would likely result in the title insurance coverage being void if they occurred. Typical gas leases allow gas companies to perform these activities. The loss or inability to provide title insurance would restrict lending on properties with gas leases if title insurance was not available.
  - a. No structure shall be erected on the premises which exceeds three (3) stories or thirty five (35) feet in height...
  - b. The premises shall not be used for the storage of any material, machinery, equipment or supplies of any kind...
  - c. The premises shall not be used for any commercial purpose of any kind...
  
- 4) Secondary Market requirements state (Freddie Mac guide 39.4 (m)) that lenders must warrant the following, each of which would not be possible with gas/oil leases in place. These leases restrict use of the property by the borrower and there is not reliable data to support what impact a gas lease has on value or marketability:
  - a. ...must not interfere with the use and enjoyment of any present or proposed improvements on the mortgaged premises or with the use and enjoyment of the balance of the Mortgage Premises not occupied by improvements.
  - b. ...must not affect the marketability of the Mortgaged Premises
  - c. ...must have no or minimal effect on the value of the Mortgaged Premises
  - d. ...must be commonly acceptable to private institutional Mortgage investors in the area...

Banks could not warrant any of these issues due to lack of comparable sales and details regarding gas leases attached to other properties.

- 5) Secondary market requirements state (Freddie Mac guide 44.3 (d)) regarding any detrimental conditions such as underground mines... "The Appraiser must also consider the effect of such conditions in estimating the subject property's market value and/or marketability." Since there is not any way to determine if other gas/oil leases exist, the Appraiser can not fulfill this requirement.
  
- 6) FHA requirements are similar in all forms to the above with the exception that FHA requires **there is no right of surface or subsurface entry within 300 feet of the residential structure OR within 300 feet of the property boundary lines**



## CONCLUSION:

While the secondary market and FHA do not specifically prohibit gas and/or oil leases, the following items, as addressed above, cause a high level of concern for prudent banks and lenders.

1) Comparable sales, subject to gas/oil leases, are not able to be documented reliably at this time by NYS licensed appraisers. Many of the leases are recorded only in memorandum form so it is impossible for the appraiser to be able to review comparable leases and perform the duties and responsibilities of the Appraisal standards.

2) Historical data to support value and marketability is not able to be documented reliably at this time by NYS licensed appraisers. Tax roles, assessment roles, multiple listing databases and other forms of determining property sales have not and currently do not track the existence or terms of gas/oil leases. Therefore, the impact, either positive or negative, on value and marketability is not able to be documented reliably at this time by NYS licensed appraisers.

3) Since the appraisers can not supply the comparable sales, historical data and conclusive impact on value and/or marketability, the appraisal report they produce would not meet secondary market minimum standards, banking regulatory standards or NYS Appraisal standards. That would leave the lender with exceptional liability to warrant for value and marketability that the appraiser has not documented with data as being supported by comparable sales, historical data, etc.

4) Gas/oil leases are generally NOT accepted by lenders such as Wells, First Place Bank, Provident Funding, GMAC, FNCFB, Fidelity, FHA, First Liberty or Bank of America. It would be difficult, if not impossible, to meet the "acceptable if commonly granted" rule.

5) The set back of 200 feet noted above means 200 feet each direction for a lot size of at least 440 x 440 or 193,600 sf or 4.48 acres...to account for the house, well, septic size...hence the need to release 5 acres from all lease rights. 1 acre = 43,264sf. 5 acres = 216,320 sf.

6) FHA loans are more commonly utilized by lower income borrowers and lower valued properties. For FHA, the set back of 300 feet noted above means 300 feet each direction for a lot size of at least 640 x 640 or 409,600 sf or 9.47 acres...to account for the house, well, septic size...hence the need to release 10 acres from all lease rights. 1 acre = 43,264sf. 10 acres = 432,640 sf. This does not address the 300 feet from property boundary lines issue and will related to #7 below.

7) If the property is set closer to the road or a property boundary than the 200 or 300 ft setback, a neighboring property that has a gas lease may prevent the un-leased property from being able to be financed. A central reporting database on all gas leases mapped is needed to allow appraisers to determine if a neighboring property has a gas lease. Currently the only method to determine if a gas lease exists is to have an attorney do a title review on surrounding properties that would add significant expense and time delays to each residential transaction.

## Gas and Oil Leases

Impact on residential mortgage lending

Greg May, Senior VP , Residential Mortgage Lending, Tompkins Trust Company

**NOTE: Should these comments, in part or in full, be utilized, and quoted or attributed to the above named person, the following must also be included.**

**"No opinion is being expressed or implied by the author on the practice of leasing mineral rights surrounding gas and/or oil leases (referred to as gas leases, leases or fracking hereafter) by these comments. The comments provided are summarized to highlight potential conflicts for residential mortgage lending in an effort to facilitate education about and consideration of these issues for home owners and potential home buyers."**

### COMMENTS:

There are several critical issues associated with traditional mortgage lending that are in direct conflict with the Proposed SGEIS and the Revised Express Terms 6 NYCRR Parts 550 through 556 and 560 (the revised regulations). The lending standards followed by the vast majority of lenders are those of the secondary market agencies, specifically Fannie Mae, Freddie Mac, FHA and VA and in New York State, SONYMA. These conflicts with commonly accepted lending standards would appear to prohibit any residential property with a gas lease or drilling activity from securing traditional mortgage financing.

1) Residential real estate ownership is most commonly transferred in "fee simple" ownership, which by definition represents all rights to both the surface and sub-surface real estate and property. Property value is established by a NYS licensed Appraiser that compares similar property sales that traditionally transfer ownership with all these "fee simple" rights as a bundle. Should some of those rights not be transferred or have an encumbrance attached, then the NYS licensed Appraiser cannot provide a reliable and accurate estimate of value (an Appraisal) that would meet traditional mortgage lending or secondary market (Fannie Mae, Freddie Mac, FHA, VA, USDA and SONYMA) requirements. To accurately determine if some of those "fee simple" rights were transferred or



encumbered would require a legal title search, which is costly and outside the responsibility and skills of a NYS licensed Appraiser. Without an acceptable Appraisal, the property is not eligible for traditional secondary market mortgage financing.

2) Fannie Mae and Freddie Mac (as well as SONYMA which adopted these standards) have long standing requirements regarding both surface and sub-surface set back distances. For example, the Freddie Mac requirements in section 39.4 (i) states:

“...and there is no surface **or sub-surface** (bold and underlined to stress the point) entry within 200 feet of the residential structure...”.

The recent DEC revised regulations provide for a setback of 500 feet from an occupied dwelling, but with horizontal drilling proposed by HVHF the sub-surface activity is not addressed. Any regulation regarding setback must also protect “fee simple” ownership of sub-surface rights.

3) FHAVA also has specific restrictions regarding gas leases and wells. Section 4150.2d of the HUD Minimum Property Standards states:

“Operating and abandoned oil and gas wells pose potential hazards to housing, including potential fire, explosion, spray and other pollution.

1. Existing Construction: No existing dwelling may be located closer than 300 feet from an **active or planned** (bold and underlined to stress the point) drilling site. ”

Any regulation regarding setback must also protect “fee simple” ownership for an adequate distance surrounding any well site.

4) The standard NYS mortgage document (Fannie Mae/Freddie Mac form 3033) has been in use since the last revision in 2001. It has been adopted by virtually all lenders in NYS. Section #18 of that document states:

“Lender may require Immediate Payment in Full of all Sums Secured by this Security Instrument if all or any part of the Property, or if any right in the Property, is sold or transferred without Lender’s prior written permission.”

Most gas leases executed have been done by home owners without prior written consent of the lender and are now in technical default under the terms of their mortgage loan.

5) Section #21 of the standard NYS mortgage document states:

“...There are other substances that are considered hazardous for purposes of this Section 21.” It continues: “...These substances are ”...**gasoline**.



**kerosene, other flammable or toxic petroleum products, toxic pesticides and herbicides, volatile solvents, materials containing asbestos or formaldehyde, and radioactive materials.**" (bold and underlined to stress the point)

It further states:

**"I (borrower) will not cause or permit Hazardous Substances to be present on the Property. I will not use or store Hazardous Substances on the Property. I also will not dispose of Hazardous Substances on the Property, or release any Hazardous Substance on the Property, and I will not allow anyone else to do so."** (bold and underlined to stress the point)

A gas lease grants all these and many other rights that are specifically not authorized or allowed under the terms of a standard residential mortgage. Again, most leases that have been executed are in technical default under the terms of their mortgage.

6) Most Hazard Insurance policies for residential homes (commonly referred to as homeowners insurance) have specific prohibitions for activities granted and undertaken by a gas lease. Several large nationwide Insurance Companies such as Nationwide and State Farm have clearly stated they do not provide coverage for any losses associated with gas leases or drilling. In dialog with many other New York State regional Insurance Companies, most stated that they will not insure losses as a result of gas leases or drilling and most stated that if they became aware that a lease or drilling was in effect, they would not renew insurance coverage. This leaves the home owner and the lender without adequate protection and would result in a default under the terms of a standard mortgage.

As summarized, a gas lease or active fracking is in conflict with many items deemed prudent, necessary and required for traditional mortgage financing. It is my sincere hope that the issues highlighted have provided insight into this issue for home owners, potential home buyers and others with a vested interest in the residential home market in New York State. Thank you.

Quotes from Times Online from February 27, 2013:

"(Fracking is) deemed an exclusion in the same way earthquake or earth movement is," said Mike Barry, vice president of media relations at the Insurance Information Institute, a nonprofit institute funded by the insurance industry.



“We would recommend that the homeowners check their homeowner’s or farm insurance before signing any leases,” said Roseanne Placey, spokeswoman for the Pennsylvania Insurance Department. “Check to see if they (the homeowners or farmers) would be at risk. These are commercial wells. You may need a commercial liability policy. “As a landowner, do you want to bear the liability risk? And if you do, do you have the proper coverage?”

Dave Phillips, a spokesman for State Farm Insurance Co. reported that State Farm has set specific guidelines regarding hydro-fracking operations. The company does not write commercial insurance for businesses conducting hydro-fracking operations or for commercial properties where fracking is taking place. State Farm does not have a fracking endorsement for private residences, but does have earthquake, earth-movement and sinkhole endorsements available in most areas, Phillips said. “But there needs to be a conversation as to whether fracking would be covered under that, if at all,” Phillips said. The endorsements don’t guarantee that fracking-related damage will always be covered.

“Our longstanding underwriting guideline is that we do not insure the oil and gas business,” Nancy Smeltzer, a Nationwide spokeswoman, said.

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