# The Institute for Energy Law TEXAS MINERAL TITLE COURSE May 2-3, 2013 Houston, Texas

# IRREGULAR OWNERS – UNLEASED, NONPARTICIPATING, UNPOOLED, OR UNCERTAIN OWNERS AND HOW TO MANAGE THE ISSUES

RICHARD F. BROWN Brown & Fortunato, P.C. 905 S. Fillmore, Suite 400 Amarillo, TX 79101 (806) 345-6300 Telephone (806) 345-6363 Facsimile www.bf-law.com RICHARD F. BROWN Brown & Fortunato, P.C. 905 S. Fillmore, Suite 400 Amarillo, TX 79101 806-345-6300 Telephone 806-345-6363 Facsimile rbrown@bf-law.com www.bf-law.com

#### **BIOGRAPHICAL INFORMATION**

#### **CAREER**

Brown & Fortunato, P.C. (1995 – Present) (President 1995 – Present) Underwood, Wilson, Berry, Stein & Johnson, P.C. (1976 – 1995) (President 1987 – 1989) United States Marine Corps (1969 – 1973) (Captain)

#### AREAS OF PRACTICE

Oil and Gas Litigation Corporate

#### **EDUCATION**

J.D. (1975), Southern Methodist University, Dallas, Texas (Southwestern Law Journal) B.A. in Political Science (1969), Rice University, Houston, Texas

#### **ADMITTED**

U.S. District Court, Western District of Texas – 2001 U.S. District Court, Northern District of Texas – 1980 5th Circuit Court of Appeals – 1976

#### PROFESSIONAL ACTIVITIES

Board Certified in Oil, Gas and Mineral Law, Texas Board of Legal Specialization (1986-Present)

Oil, Gas and Mineral Law Council, State Bar of Texas (Chairman 1996-1997)

Panhandle Producers and Royalty Owners Association (Treasurer 1982-2010)

Texas Independent Producers and Royalty Owners Association (2005 – Present)

Texas Independent Producers Legal Action Association (Treasurer 1983-2003)

Association of International Petroleum Negotiators (2009 – Present)

Texas Bar Foundation (Life Fellow) (1999 – Present)

Amarillo Area Bar Association (1976 – Present)

State Bar of Texas (1976 – Present)

Named to Texas Super Lawyers in Oil and Gas (multiple years)

Planning Committee for more than 25 seminars on oil, gas, and mineral law

Pattern Jury Charge Committee, Oil, Gas and Energy Resources Law Section

#### LAW RELATED PUBLICATIONS

"Recent Texas Oil and Gas Cases," Oil, Gas and Energy Resources Law Section Quarterly Report (2008-Present)

"Case Law Update," Advanced Oil, Gas and Energy Resources Law Course, State Bar of Texas (2007-Present)

"Oil, Gas and Mineral Law, Annual Survey of Texas Law," SMU Law Review (1996-Present)

"Case Law Update," Panhandle Producers and Royalty Owners Association Annual Convention (2009-Present)

Monthly casenote for Panhandle Producers and Royalty Owners Association newsletter "Pipeline" (1987-2010)

"Coal Controversy," Texas Lawyer (December 24, 2007)

"Litigating Land, Title, and Boundary Issues"

Twenty Second Annual Advanced Oil, Gas and Energy Resources Law Course (State Bar of Texas) (2004)

"Nothing is Certain But Death and Maybe Taxes"

Eighteenth Annual Advanced Oil, Gas and Mineral Law Course (State Bar of Texas) (2000)

"Division Orders"

Eighteenth Annual Oil, Gas and Mineral Law Institute (University of Texas and State Bar of Texas) (1992)

"What is Oil/Gas?"

Oil, Gas and Mineral Law Section Report, Vol. 15, No. 6. (1991)

Amarillo Oil Company vs. Energy-Agri Products, Inc.

Seventeenth Annual Oil, Gas and Mineral Law Institute (University of Texas and State Bar of Texas) (1991)

#### CIVIC

Amarillo Local Government Corporation (Vice President 2011 – Present)

Amarillo Tax Increment Reinvestment Zone #1 (Chairman 2007 – Present)

Center City of Amarillo, Inc. (President 1996 – 1998)

Amarillo Economic Development Corporation (President 1990 – 1992)

# TABLE OF CONTENTS

I.	IN	TRODUCTION	1
II.	THE PROSPECT  GENERAL LEASING CONCEPTS		1
III.			2
	A.	Practical Solution for Unleased Owners and	
		Other Causes of Holes in the Prospect	
	B.	Limitations Title and Adverse Possession	6
IV.	OIL AND GAS PROPERTY CONCEPTS		11
	A.	Surface Use and Access Rights	11
	B.	Ownership in Place and the Rule of Capture	
	C.	Community Lease, Non-apportionment Rule, and Entirety Clause	
	D.	Cotenants	
	E.	Good Faith and Bad Faith Trespass	20
V.	NONEXECUTIVE INTERESTS		23
	A.	Types of Interests	23
	B.	Bonus Payments	24
	C.	Ratification and Pooling	27
	D.	Joint Operating Agreements	32
	E.	Examples	34
VI.	LITIGATION		
	A.	MIPA	40
	B.	Receivership	43
	C.	Partition	45
	D.	Trespass to Try Title	46
	E.	Declaratory Judgments	48
	F.	Boundary Disputes	49
	G.	Quiet Title	51
VII.	CONCLUSION		52

### **EXHIBITS**

- A.
- A-1.
- Section 1 Diagram (Prospect)
  Section 1 Diagram (Prospect with Ownership)
  Form Stipulation of Interest and Cross-Conveyance B.
- Form Boundary Agreement and Cross-Conveyance Form Lease Ratification (for a Cotenant) C.
- D.
- Form Lease Ratification (for a Nonparticipating Owner) E.
- Form Designation of Pooled Unit (Gas) F.

# IRREGULAR OWNERS – UNLEASED, NONPARTICIPATING, UNPOOLED, OR UNCERTAIN OWNERS AND HOW TO MANAGE THE ISSUES<sup>1</sup>

#### I. INTRODUCTION

When the well is completed, Management expects to own the production. The Landman has been working for a long time to try and meet that expectation. However, most of the Landman's work was done during the critical lease acquisition stage before drilling commenced. The Landman's work was done without enough time, without enough money, and without enough facts to be sure of the title. Decisions have to be made that are a mix of available information, legal knowledge, legal advice, experience, instinct, and necessity. Leasing the known owners who want to lease is the easy part. Figuring out what to do about everyone else is the hard part. Some can be leased, some can be marginalized, some are risks that can be managed, and some will make the Prospect undrillable.

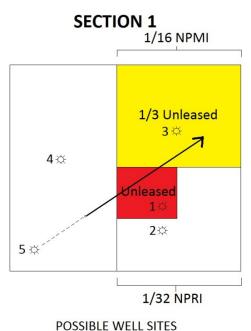
Issues with other working interest owners and regulatory issues may have a material impact on the decisions to be made, but this paper focuses on the leasing issues. It will establish a hypothetical Prospect to illustrate the issues and then suggest the practical steps to be taken to make the issues go away. For the issues that will not just go away, the principal legal issues which must be considered will be reviewed in detail to suggest ways to manage the title and leasing risks. Finally, for when all else fails, the principal legal remedies are reviewed.

#### II. THE PROSPECT

Management has identified a Prospect and intends to drill a well on Section 1. It is unclear whether the well will be a vertical well or a horizontal well, and the production could be

<sup>&</sup>lt;sup>1</sup> The author gratefully acknowledges the assistance of Conrad D. Hester, Natalie K. Mahlberg, and Matthew S. Smith of the firm. Any errors are the author's.

either oil or gas. The geologists and the engineers have not agreed upon the exact location in Section 1, but they are considering five possibilities. An undivided 1/3 interest in the NE/4 is not subject to lease. That is the Yellow Tract. There is also a 1/16 nonparticipating mineral interest that burdens all of the Yellow Tract. All of the NW/4 SE/4 is not subject to lease. That is the Red Tract. There is also a 1/32 nonparticipating royalty interest that burdens all of the SE/4. The diagram below (also attached as Exhibit "A") illustrates the hypothetical scenario on the Prospect.



The topic is too open-ended to cover all scenarios, but the hypothetical will be used to illustrate common issues. The analysis is focused on title, not regulatory issues. How do the Landman and the Title Examiner work together to help Management get this well drilled?

#### III. GENERAL LEASING CONCEPTS

A. Practical Solutions for Unleased Owners and Other Causes of Holes in the Prospect

You cannot fill a hole in your Prospect until you know that there is a hole and can identify the owner who can fill the hole.<sup>2</sup> Doing the take-off or the title work early is important in solving the problem. Knowledge is power. Identify the holes and the owners when there is still a chance to control the development to motivate the unleased owner to lease, or there is at least a chance to minimize risk by controlling development. If the development of the Prospect is too far along when the Landman begins working on the curative, the negotiation leverage may shift to the unleased owner.

First, be sure there is a hole that cannot be filled, because nothing that follows is as simple or as certain as getting the unleased interest leased. You do not get to pick the owner, but you can pick who contacts the owner. Try a different Landman. Try another Lessee. Try a family member, a co-tenant, or a neighbor who has an interest in development. Identify the reason why the unleased owner will not lease and determine if there is a solution. Frequently the issue is just the business terms, and it may not be possible to make a deal. However, you have to consider the limits of your business terms and evaluate whether there is a way to satisfy both Lessor and Lessee. Beyond the usual business terms of bonus, royalty rate, and lease term, sometimes the deal can be done by considering more creative business terms. These could include timing of operations, drilling commitments, limiting locations, defining surface uses, drilling water wells, building ranch roads, etc. If the unleased owner remains recalcitrant, then you must plan around him and/or seek a litigation solution, if one is available and economic.

If the hole in the Prospect is not caused by a recalcitrant owner, but by uncertainty as to the correct owner, at the leasing stage the answer is simple: lease everyone. The only question is cost. If the Prospect can stand the additional cost, then the strategy is to lease everyone, pay

<sup>&</sup>lt;sup>2</sup> See also, Curtis D. Horne, You Don't Know What You Don't Know (May 3, 2013).

everyone, and not worry about identifying the true owner until it is time to pay production royalties. Because Lessees are reluctant to sue Lessors to collect overpaid bonus (assuming that they can collect under the terms of the lease), if the cost of paying extra bonus is too high, then perhaps payment can be deferred until ownership is confirmed, or perhaps bonus can be paid in stages. "Lease everyone" means lease everyone who arguably owns any executive rights in your Prospect. Whatever title issues may be left, those issues can ultimately be resolved and all the minerals will still be under lease.

Unfortunately, in Texas, "lease everyone" also often means get a lease ratification from any possible owner who may not be bound by a lease as executed or by terms included in the lease. As discussed below, for a pooling clause to be binding on a nonparticipating interest, you must get a ratification of every lease executed by the executive rights holder by every nonparticipating owner whose interest is subject to the executive rights controlled by that Lessor.

There are many other circumstances where ownership or the right to lease may be uncertain. For example, who has the power to lease when an estate has not been closed or nothing has been filed to substantiate succession? For example, when there is a life tenancy, who has the power to lease? Identifying the correct Lessor may be complex or uncertain, but if you are on the fly in a competitive area without the time to figure it out, and you can stand the risk and extra cost, lease everyone and be sure your lease has an after-acquired property clause. If the uncertain owner remains "uncertain," then you must plan around him and/or seek a litigation solution, if one is available and economic.

If the hole in your Prospect is not caused by a recalcitrant owner, or uncertainty as to which owner to lease, but rather an inability to find the owner, pursue all of the practical solutions first to confirm that there actually is a hole in your Prospect. Interview all of the

identified family members to locate the missing owner. There are search firms and internet search options which may solve the problem. Often the problem is caused by too many generations or too many gaps in title so that there is just no way to reach a conclusion. If the unleased owner remains "missing," then you must plan around him and/or seek a litigation solution, if one is available and economic.

If the hole is caused by uncertainty as to whether a prior lease has terminated, acquire a release. If a release cannot be acquired, then acquire a top lease with appropriate language to protect your Lessor from claims that Lessor has asserted lease termination and to protect your Lessee from tortious inference or slander of title claims. A top lease does not solve the problem and may provoke litigation, but if done properly, it does fill the hole, if title is finally resolved successfully. Without the top lease, if title is finally resolved successfully, acquiring a new lease may be much more expensive and uncertain than the cost of the top lease.

Simple curative is a simple answer. For example, if the hole in the Prospect is caused by confusion as to ownership interests in a tract or uncertainty as to the location of a boundary, a simple stipulation of interest may cure the problem. Examples of a Stipulation of Interest and Cross-Conveyance and a Boundary Agreement and Cross-Conveyance are included as Exhibits "B" and "C". There are many other examples of curative action which could fill a hole in the Prospect, but the point is that a quick and timely curative step which eliminates the hole in the Prospect is far easier than to plan around the issue or to attempt a cure after the well has been commenced, or worse, completed. No form works all the time, but the most important general considerations for preparing curative documents are to include a correct legal description, all of the possible owners, words of cross-conveyance and grant, and, if applicable, provisions as to after-acquired title.

#### B. Limitations Title and Adverse Possession<sup>3</sup>

Sometimes, Management may choose to rely on limitations title. This may be nothing more than making the practical assumption that the problem, whatever it is, is a problem that is so old, so obscure, or so hard to resolve, that no one will ever do anything about it. It is a practical solution, not a legal solution. It is an assumption of the risk. Limitations title actually means that Management is assuming that if title is challenged, title somehow can be defended on the basis of adverse possession – defensible title.

Title based on adverse possession can be established only in trespass to try title, but such title is often just assumed based on a general knowledge of the facts and the effect of the statutes. Proving title by adverse possession is very complex and challenging. Making reasonable business decisions, or deciding to waive title requirements on the assumption of limitations title, requires a very thorough understanding of the laws of adverse possession.

The general concept behind limitations title can only be summarized here. Adverse possession means actual physical possession of a tract of land, which may, if it lasts for the statutory period of time without interruption, result in the possessor acquiring title to the land. Generally, the possession must be an actual and visible appropriation of real property, commenced and continued under a claim of right that is inconsistent with and hostile to the claim of the true owner. Management is simply assuming that the party in possession has defensible title and will win a title dispute, if the possession has been actual, visible, hostile, and continuous for a long time. Each of these elements has been thoroughly litigated and presents nuances and issues that cannot be addressed here. The Title Examiner, or more correctly, the Landman, faced

<sup>&</sup>lt;sup>3</sup> See also Donald G. Sinex and Scott C. Petry, Adverse Possession, After-Acquired Title and the Rule Against Perpetiuties (May 2, 2013).

<sup>&</sup>lt;sup>4</sup> Rhodes v. Cahill, 802 S.W.2d 643, 645 (Tex. 1990).

with "old" title problems, never has time to fully litigate an adverse possession cause. Decisions as to which parties to lease are frequently driven by conclusions as to reasonable business risk. This usually means some perfunctory analysis or inquiry as to actual, visible, hostile, and continuous, but most of the focus is on "time." As a practical matter time is on the side of the party in possession. It is more unlikely that an old problem will be raised, and more unlikely that an old problem, if raised, can be proven. More importantly, the statute makes it easier for the possessor to win, if the party in possession has been in possession for a long time.

The Texas Civil Practice and Remedies Code outlines the requirements for adverse possession of real property.<sup>5</sup> The adverse possession statutes require different periods of time to perfect title—ranging from three, five, ten, and twenty-five years—depending on the circumstances, such as whether the person in possession of the land has a deed or has paid taxes on the land. Some requirements are common to all situations. Specifically, the appropriation or possession of real property must be: (i) actual and visible, (ii) continued use under a claim of right that is inconsistent with and hostile to the claim of another person, and (iii) continuous and not interrupted.

Actual and visible possession must be such that the true owner is given notice of a hostile claim.<sup>6</sup> If the owner has no actual knowledge of the assertion of claim to the land, the adverse possession must be so open and notorious and manifested by such open or visible act or acts that knowledge on the part of the owner will be presumed.<sup>7</sup> "Mistaken beliefs about ownership do

<sup>5</sup> TEX. CIV. PRAC. & REM. CODE §§ 16.021-28 (1985).

' *Id*. at 787.

<sup>&</sup>lt;sup>6</sup> Orsborn v. Deep Rock Oil Corp., 267 S.W.2d 781, 785–87 (Tex. 1954).

not transfer title until someone acts on them. . . . there must be adverse *possession*, not just adverse *beliefs*."

The claim of right "must be of such character as to indicate unmistakably an assertion of a claim of exclusive ownership in the occupant." "The character of use required to establish adverse possession varies with the nature of the land and with its adaptability to a particular use." Joint use is not enough, because "possession must be of such character as to indicate *unmistakably* an assertion of a claim of exclusive ownership in the occupant." If the possessor admits that "he holds in subordination to the better title, the possession will be regarded as held by consent." Similarly, continued possession after such admissions will fail to mature a title under adverse possession, "until the party has changed the character of his possession either by express declarations or by the exercise of acts of ownership inconsistent with a subordinate character."

The possession must be continuous and uninterrupted by an adverse suit to recover the property.<sup>14</sup> The character of possession cannot be changed or abandoned, and then renewed afterwards at the will and pleasure of the occupant.<sup>15</sup> Gaps in possession may be of sufficient duration to break the required continuity, but a temporary gap in possession for a reasonable period of time will not break the continuity.<sup>16</sup>

\_

<sup>&</sup>lt;sup>8</sup> Tran v. Macha, 213 S.W.3d 913, 914 (Tex. 2006).

<sup>&</sup>lt;sup>9</sup> Rick v. Grubbs, 214 S.W.2d 925, 927 (Tex. 1948).

<sup>&</sup>lt;sup>10</sup> Kazmir v. Benavides, 288 S.W.3d 557, 561 (Tex. App.—Houston [14th Dist.] 2009, no pet.)

<sup>&</sup>lt;sup>11</sup> *Tran*, 213 S.W.3d at 914 (quoting *Rhodes v. Cahill*, 802 S.W.2d 643, 645 (Tex. 1990)).

<sup>&</sup>lt;sup>12</sup> Satterwhite v. Rosser, 61 Tex. 166, 172 (1884).

 $<sup>^{13}</sup>$  Id

<sup>&</sup>lt;sup>14</sup> TEX. CIV. PRAC. & REM. CODE § 16.021(3).

<sup>&</sup>lt;sup>15</sup> Satterwhite, 61 Tex. at 171 (1884).

<sup>16</sup> Balli v. McManus, 311 S.W.2d 933, 935 (Tex. Civ. App.—San Antonio 1958, writ ref'd n.r.e.).
Page 8 of 54

The three-year adverse possession statute requires the adverse possessor to hold real property for at least three years in peaceable and adverse possession under title or color of title.<sup>17</sup> The five-year statute requires the adverse possessor to hold real property for five years in peaceable and adverse possession, and to cultivate, use, or enjoy the property, pay taxes, and claim under a duly registered deed.<sup>18</sup> The ten-year statute requires the adverse possessor to hold real property for ten years in peaceable and adverse possession, and to cultivate, use, or enjoy the property, but does not require the adverse possessor to pay taxes or claim under a duly registered deed or other memorandum of title. The ten year statute only operates as to a maximum of 160 acres, or the acres actually enclosed.<sup>19</sup> The three, five, and ten year statutes will be tolled and will not run during any possession that begins while the true owner is under a legal disability.<sup>20</sup> The twenty-five year statute requires the adverse possessor to hold real property for twenty-five years in peaceable and adverse possession, and to cultivate, use, or enjoy the property," and runs regardless of whether the true owner was under a disability.<sup>21</sup>

The applicable rules for adverse possession of *mineral* interests depend upon whether the surface estate and mineral estate have been severed.<sup>22</sup> The true owner of a mineral estate would not be alerted to a hostile claim on the part of an occupant who takes no steps to penetrate the surface.<sup>23</sup> If the surface estate and the mineral estate have not been severed, adverse possession of the surface extends to the underlying mineral estate.<sup>24</sup> If the surface and mineral estates are

\_

<sup>&</sup>lt;sup>17</sup> TEX. CIV. PRAC. & REM.CODE § 16.024.

<sup>&</sup>lt;sup>18</sup> *Id.* at § 16.025(a).

<sup>&</sup>lt;sup>19</sup> *Id.* at § 16.026(a).

<sup>&</sup>lt;sup>20</sup> *Id.* at § 16.022. A person is under a "legal disability" if the person is: "(i) younger than 18 years of age, regardless of whether the person is married; (ii) of unsound mind; or (iii) serving in the United States Armed Forces during time of war." *Id.* 

<sup>&</sup>lt;sup>21</sup> *Id.* at § 16.027.

<sup>&</sup>lt;sup>22</sup> Natural Gas Pipeline Co. of Am. v. Pool, 124 S.W.3d 188, 193 (Tex. 2003).

<sup>&</sup>lt;sup>23</sup> *Id*.

<sup>&</sup>lt;sup>24</sup> Gulley v. Davis, 321 S.W.3d 213, 220 (Tex. App.—Houston [1st Dist.] 2010, pet. denied).

Page 9 of 54

severed after adverse possession has begun, the limitation title still runs as to both the surface and the mineral estates.<sup>25</sup> If the surface and mineral estates are severed before adverse possession begins, surface occupancy alone is insufficient to establish title by adverse possession to the minerals.<sup>26</sup> An actual, public, notorious, and uninterrupted working of the minerals for the statutory period is generally required to give notice to the true owner.<sup>27</sup> In summary, to adversely possess severed minerals, the minerals must be produced.<sup>28</sup>

Because the possession must be *adverse* to the rights of the actual owner, possession under a lease from the true owner would not amount to adverse possession. That is, the lessor will not lose title to the possibility of reverter in the minerals simply because the lessor's lessee is producing the minerals under a valid lease. However, if the lease has terminated, the minerals have reverted to the lessor, and the lessee may then adversely possess or regain the leasehold by production.<sup>29</sup>

It should be clear that establishing title by adverse possession is complex and difficult.

Assuming that limitations title exists is a big assumption with considerable risk.

If the hole in the Prospect cannot be filled by any of the general concepts discussed above, then the Landman and the Title Examiner have legal and practical issues that are difficult

<sup>&</sup>lt;sup>25</sup> *Id.* (stating "[a]dverse possession commenced prior to limitations will extend to the mineral estate even if the titleholder severs the mineral estate before the limitations period has fully run").

<sup>&</sup>lt;sup>26</sup> *Id.* (stating "possession of the surface estate that commences after a severance of the mineral estate is not sufficient to constitute adverse possession of the mineral estate").

<sup>&</sup>lt;sup>27</sup> XTO Energy Inc. v. Nikolai, 357 S.W.3d 47, 61 (Tex. App.—Fort Worth 2011, pet. filed) (holding property owners could not claim adverse possession of mineral rights in the absence of evidence that they leased the mineral rights or had taken some action to excavate them).

<sup>&</sup>lt;sup>28</sup> The area adversely possessed may depend on which adverse possession statute the adverse possessor claims under. "Peaceable possession of real property held under a duly registered deed or other memorandum of title [(such as an oil and gas lease)] that fixes the boundaries of the possessor's claim extends to the boundaries specified in the instrument." TEX. CIV. PRAC. & REM. CODE § 16.026(c). Under the ten-year statute, "[w]ithout a title instrument, peaceable and adverse possession is limited . . . to 160 acres, including improvements, unless the number of acres actually enclosed exceeds 160. If the number of enclosed acres exceeds 160 acres, peaceable and adverse possession extends to the real property actually enclosed." *Id.* at § 16.026(b).

<sup>&</sup>lt;sup>29</sup> Natural Gas Pipeline Co. of America v. Pool, 124 S.W.3d 188 (2003); Conley v. Comstock Oil & Gas, LP, 356 S.W.3d 755, 768 (Tex. App.—Beaumont 2011, no pet.) (holding adverse possession of a severed mineral estate under the Texas five-year statute of limitations requires both drilling and production).

to forecast and difficult to plan around. To understand the risks, to manage the risks, and to analyze whether the risks assumed are an acceptable business risk begins with an understanding of certain key oil and gas property concepts as they relate to the unleased owner.

#### IV. OIL AND GAS PROPERTY CONCEPTS

A. Surface Use and Access Rights<sup>30</sup>

To promote mineral production, the law has deemed the mineral estate dominant to the surface estate.<sup>31</sup> A mineral estate owner may conduct operations anywhere on a tract of land for which he owns any portion of the mineral rights and is entitled to use as much of the surface as is reasonably necessary to produce the minerals, having due regard for the rights of the owner of the surface estate.<sup>32</sup>

The dominance of the mineral estate gives rise to implied easements for exploration and development, which are appurtenant to the mineral estate for access thereto.<sup>33</sup> Although the mineral estate owner does not commonly exercise the development rights himself because of the expense and risk involved, he may grant these rights by executing an oil and gas lease to a lessee. An oil and gas lessee has the implied right to use such part of the surface as may be necessary to effectuate the purposes of the lease; this right is known as a "lease easement."<sup>34</sup>

The owner of the dominant estate in the minerals is limited to a "reasonable" use of the surface, extending to the use of the lateral surface, the subsurface, and the super-adjacent airspace.<sup>35</sup> The Texas Proposed Pattern Jury Charge on Unreasonable Use asks:

<sup>34</sup> *Id.* at 810.

<sup>&</sup>lt;sup>30</sup> Because Ernest V. Bruchez has covered Surface Access and Use in detail for this seminar, the discussion here will be brief. *See* Ernest V. Bruchez, *Surface Access and Use: Stop, Look and Listen Your Way to the Drill Site* (May 2, 2013).

<sup>&</sup>lt;sup>31</sup> Sun Oil Co. v. Whitaker, 483 S.W.2d 808, 810 (Tex. 1972).

<sup>&</sup>lt;sup>32</sup> *Id.* at 811.

<sup>&</sup>lt;sup>33</sup> *Id*.

<sup>&</sup>lt;sup>35</sup> *Id.* at 817 (citing *Getty Oil Co. v. Jones*, 470 S.W.2d 618, 621 (Tex.1971)).

Did Defendant make a use of the leased premises that was not reasonably necessary?

You are instructed that the lessee under an oil, gas and mineral lease has the right to make such use of the land covered by the leases as is reasonably necessary to carry out the purposes of the lease, having due regard for the rights of the owner of the surface estate....<sup>36</sup>

The Accommodation Doctrine may also limit the use of the surface by the dominant estate owner. When a landowner claims a pre-existing use of the surface estate that would be precluded or impaired by the development of the mineral estate, the surface owner may be able to require the lessee to adopt alternative operations or uses that accommodate the preexisting use of the surface.<sup>37</sup> The Accommodation Doctrine applies when the lessee's operations would preclude or impair the surface owner's preexisting use when the lessee has an acceptable alternative operation or use available that would not impair the use of the surface.<sup>38</sup>

In addition to implied lease easements, a lease may convey whatever express easements the parties choose to include. Generally, easements for surface use and access (roads, pipelines, electric lines, etc.) under a lease cannot be used to benefit off-lease premises—an easement is granted or implied for the benefit of the leased premises, and its use is limited to that land.<sup>39</sup> Where a lease includes both express easements and the authority to pool the leased tract with other lands, the easements may be used to benefit the other pooled lands, as long as the burdened

<sup>&</sup>lt;sup>36</sup> Oil, Gas, & Energy Resource Law Section of the State Bar of Texas, *Oil and Gas Pattern Jury Questions and Instructions*, Question 3.h. "*Surface Use/Accommodation Doctrine Question*" (updated July 7, 2009), available at: http://www.oilgas.org/Content/PDFs/PatternJuryCharges\_20090707.pdf.

<sup>&</sup>lt;sup>37</sup> Getty Oil Co. v. Jones, 470 S.W.2d 618, 621-22 (Tex. 1971).

 $<sup>^{38}</sup>$  *Id*.

<sup>&</sup>lt;sup>39</sup> Robinson v. Robbins Petroleum Corp., 501 SW 2d 865, 868 (Tex. 1973); Bickler v. Bickler, 403 S.W.2d 354, 359 (Tex. 1966).

land is also benefited.<sup>40</sup> A lessee may not use easements across a leased tract to solely benefit other lands within a pool.<sup>41</sup>

Other implied easements may also arise by prescription, necessity, or continued use. A prescriptive easement (similar to adverse possession) requires use of another's land in a manner that is open, notorious, continuous, exclusive, and adverse for the requisite period of time. An easement by necessity may be implied where: (1) there is unity of ownership of the dominant and surface estates prior to the severance; (2) access must be a necessity and not a mere convenience; and (3) the necessity must exist at the time of the severance of the two estates. Similarly, an implied easement appurtenant may be found if: (1) unity of ownership of the dominant and surface estates prior to the severance; (2) the use of the easement was apparent at the time of the grant; (3) the use of the easement must have been continuous so that the parties must have intended that its use pass by the grant; and (4) the use of the easement must be reasonably necessary to the use and enjoyment of the dominant estate. Presumably, any such easements acquired by a lessor would also inure to the benefit of the lessor's lessee.

Applying the basics of surface use and access to the Prospect on Section 1, the Red Tract is the big problem. Management has no surface use or access rights in this tract. Any entry onto the surface is a trespass. Location #1 cannot be drilled. Management cannot cross the Red Tract for any purpose. If existing ranch roads, electrical lines, or pipelines cross the Red Tract, those easements cannot be relied upon, unless they are express easements owned by someone other

<sup>&</sup>lt;sup>40</sup> *Miller v. Crown Cent. Petroleum Corp.*, 309 S.W.2d 876, 879 (Tex. Civ. App.—Eastland 1958, writ dism'd by agr.) (holding that lessee has the right to use an easement burdening lessor's land when such use increased production from lessor's land, as well as production from other lands within a pooled unit).

<sup>41</sup> *Key Operating & Equip., Inc. v. Hegar*, No. 01-10-00350-CV, 2013 WL 103633 (Tex. App.—Houston [1st Dist.]

<sup>&</sup>lt;sup>41</sup> Key Operating & Equip., Inc. v. Hegar, No. 01-10-00350-CV, 2013 WL 103633 (Tex. App.—Houston [1st Dist.] Jan. 7, 2013, no. pet. h.) (holding that lessee had no right to use lessor's surface estate solely to secure production of oil from other tracts).

<sup>&</sup>lt;sup>42</sup> Brooks v. Jones, 578 S.W.2d 669, 673 (Tex. 1979)

<sup>&</sup>lt;sup>43</sup> *Peacock v. Schroeder*, 846 S.W.2d 905, 910 (Tex. App.—San Antonio 1993, no writ)

<sup>&</sup>lt;sup>44</sup> *Id*.

than the owner of the Red Tract, or the easements are easements by prescription, necessity, or continued use which inure to the benefit of lessee on another tract. The Yellow Tract should not be a problem, even though there is an undivided 1/3 unleased interest. The owners of the other 2/3 have the right to develop and therefore their lessee can use the surface of the Yellow Tract. The nonparticipating owners have no possessory rights in the surface and are not relevant for surface use and access questions.

The rest of the Section is leased and the surface can be used. However, the leases on the three leased tracts must be reviewed for pooling clauses. If surface use or access on more than one tract is required, the leases on the tracts used must be pooled, or separate easements must be obtained. For example, if Location #4 is drilled, but the access road and pipeline cross the NE/4, then easements across the NE/4 must be acquired, or the W/2 and NE/4 must be pooled.

All uses are subject to the reasonable use limitation, the Accommodation Doctrine, and, as to the NE/4, the unleased mineral owner may develop and have concurrent rights to surface uses in the NE/4.

#### B. Ownership in Place and the Rule of Capture

To ensure that all of the Prospect is leased and that there are no holes, the Title Examiner and the Landman must start with the basic principles of the ownership of oil and gas under Texas jurisprudence. Texas follows the ownership-in-place theory for minerals, meaning that the mineral estate owner actually owns the minerals as part of the realty before they are produced. Therefore, to lease the oil and gas, the general rule is that you must get a lease from the owner of the mineral estate in that location. If the surface estate and the mineral estate are severed, you must get a lease from the owner of the mineral estate.

<sup>&</sup>lt;sup>45</sup> Elliff v. Texon Drilling Co., 210 S.W.2d 558, 561 (Tex. 1948); Texas Co. v. Daugherty, 176 S.W. 717, 722 (Tex. 1915).

There are five essential attributes of a mineral estate, and the first two are (1) the right to develop (the right of ingress and egress) and (2) the right to lease (the executive right).<sup>46</sup> The landowners may choose to divide up these essential attributes however they may agree, but unless expressly severed, these two attributes remain part of the mineral estate.<sup>47</sup> If the landowners choose to divide up these rights in a different way, *e.g.*, the surface owner retains the right to lease, then you must get a lease from the owner of the surface estate to lease the minerals.

Ownership in place is subject to the Rule of Capture—the mineral owner may acquire title to the oil or gas produced from wells on his land, even though part of the oil or gas has migrated from adjoining lands.<sup>48</sup> Therefore, the general rule is that the owner of the wellsite is entitled to all of the production from the well. It follows that you never want an unleased owner in the wellsite, if there is any way to avoid it.

Applying these concepts to the Prospect on Section 1, Location #1 cannot be drilled. Not only would it be a trespass, but all of the production would belong to the owner of the Red Tract. Locations #2, #3, and #4 can each be drilled and produced. However, there will be a duty to account for 1/3 of production out of Location #3 to the unleased co-tenant, as discussed below. The production from each tract would belong to the owners of that tract with no obligation to share with the owners of the other tracts, unless the leases were pooled.

Location #5 and the horizontal leg present many challenges. The Yellow Tract can be pooled, but the pooling will not be effective as to the unleased owner or as to the owner of the

Page 15 of 54

-

<sup>&</sup>lt;sup>46</sup> Altman v. Blake, 712 S.W.2d 117, 118 (Tex. 1986). A mineral estate consists of the following five rights: (1) the right to develop (the right of ingress and egress), (2) the right to lease (the executive right), (3) the right to receive bonus payments, (4) the right to receive delay rentals, and (5) the right to receive royalty payments. *Id.* 

<sup>&</sup>lt;sup>48</sup> Stephens County v. Mid-Kansas Oil & Gas Co., 254 S.W. 290, 292 (Tex. 1923).

1/16 NPMI in the Yellow Tract. It will be a trespass as to the Red Tract and the 1/32 NPRI in the Red Tract.

The law, under the theory of correlative rights, prevents the mineral estate owner from intentionally wasting or destroying the minerals.<sup>49</sup> Additionally, the Texas Railroad Commission may regulate production by regulating well locations, density, spacing rates of production, and production and completion practices.<sup>50</sup> Regulatory issues may have a significant indirect impact on leasing decisions on the Prospect in Section 1.

#### C. Community Lease, Non-apportionment Rule, and Entirety Clause

The owners of separate tracts may jointly execute a single lease covering both tracts as if the entire area was jointly owned—such a lease is called a community lease. Regardless of where a lessee located the well under a community lease, the lessors will share the royalty proportionately.<sup>51</sup> Any nonparticipating interest owners have the option to ratify the lease and share in the royalty.<sup>52</sup>

When a mineral owner executes a lease for oil and gas and subsequently conveys a divided portion of the oil and gas rights to another (*e.g.*, the NW/4 of the leased lands), and oil and gas is produced from only one portion of the leased lands after the division, only the owner of the particular portion upon which the well is located benefits from production.<sup>53</sup> This is called the Non-Apportionment Rule.

<sup>&</sup>lt;sup>49</sup> Edwards Aguifer Auth. v. Day, 369 S.W.3d 814, 830 (Tex. 2012), reh'g denied (June 8, 2012).

<sup>&</sup>lt;sup>50</sup> Elliff v. Texon Drilling Co., 210 S.W.2d 558 (Tex. 1948).

<sup>&</sup>lt;sup>51</sup> French v. George, 159 S.W.2d 566, 569 (Tex. Civ. App.—Amarillo 1942, writ ref'd) ("It seems to be established as a general rule of law that where several owners of adjoining tracts of land unite in a single lease to a third party for development of oil or gas as a single tract, and provision is made for delivery of the royalty to the lessors, in the absence of an agreement to the contrary, the royalties must be divided among the lessors in the proportion that the area of the tract owned by each bears to the total area covered by the lease, and the ownership of the tract upon which a well may be drilled and from which oil may be produced is a matter of no consequence.").

<sup>&</sup>lt;sup>52</sup> Ruiz v. Martin, 559 S.W.2d 839, 843 (Tex. Civ. App.—San Antonio 1977, writ ref'd n.r.e.)

<sup>&</sup>lt;sup>53</sup> Japhet v. McRae, 276 S.W. 669, 670 (Tex. Comm'n App. 1925).

The parties to an oil and gas lease may avoid the uncertainty of a community lease and the application of the Non-Apportionment Rule by including an entirety clause in the lease.<sup>54</sup> Such a clause generally provides that in the event that the leased premises shall thereafter be owned in severalty or in separate tracts, that the entire leased premises shall be developed and operated as one lease, and that all separate owners will share in production in the proportion that the acreage owned by each separate owner bears to the entire leased premises.<sup>55</sup>

Applying these concepts to Section 1, if the W/2 and NE/4 are under a community lease, or a lease with an entirety clause, the owners of the W/2 and the NE/4 would share proportionately in the royalty, regardless of whether lessee drilled Location #3 or #4. If the lessee drilled Location #3, the owner of the 1/16 NPMI could refuse to ratify the pooling and receive an undiluted share from Location #3. If the lessee drilled Location #4, the owner of the 1/16 NPMI would receive nothing. However, the owner of the 1/16 NPMI could ratify the lease and receive a diluted share. If both locations are drilled, there is some authority that the owner of the 1/16 NPMI could make both elections in his own best interest. The unleased 1/3 owner in the NE/4 could ratify and share proportionately from Locations #3 and #4, or not ratify, and receive a cotenant's share from Location #3.

If the W/2 was leased and then the landowner conveyed the SW/4 to someone else, his assignee would not share in production from Location #4 under the Non-Apportionment Rule. If, however, the lease contained an entirety clause, both assignor and assignee would share in

But see, Montgomery v. Rittersbacher, 424 S.W.2d 210, 212 (Tex. 1968) (holding that the enlargement or diminishment of the rights of a prior nonparticipating royalty owner can be accomplished by the holder of the executive rights executing an oil, gas, and mineral lease which includes either a pooling clause or an entirety clause, provided the nonparticipating owner ratifies such action).
 James E. Key, The Right to Royalty: Pooling and the Capture of Unburdened Interests, 17 Tex. Wesleyan L.

<sup>&</sup>lt;sup>55</sup> James E. Key, *The Right to Royalty: Pooling and the Capture of Unburdened Interests*, 17 TEX. WESLEYAN L. REV. 69, 74 (2010).

production in proportion to their ownership interests, regardless of where the well was located on the W/2.

#### D. Cotenants

Owners of undivided portions of oil and gas rights in and under a single tract of land are cotenants.<sup>56</sup> Each cotenant may enter upon the tract for the purpose of exploring for oil and gas and may drill and develop the premises; however, one cotenant cannot exercise that right to the exclusion of the other, and each may exercise the same right and privilege with reference to the common property.<sup>57</sup> Upon discovery of oil and gas upon the premises, the producing cotenant must account to the nonconsenting or nonproducing cotenant for his pro rata share of the net profits apportioned according to the fractional interest of such cotenant.<sup>58</sup> The net profits are determined by starting with the market value of the oil or gas produced, then deducting the reasonable and necessary expense of developing, extracting, and marketing the minerals.<sup>59</sup> The reasonable and necessary expenses include "the cost of the machinery and appliances and other means necessary and proper to the production. In other words, all reasonable expenses incurred in the production and marketing would have to be deducted from the gross value, before a division of the proceeds between the cotenants."60 However, the underlying concept is that the developing cotenant is benefitting the common estate and is entitled to be reimbursed for the value of the benefit conferred. But if the work done does not benefit the common estate, the developing cotenant cannot recover his cost. For example, if a cotenant drills a dry hole, he does so at his own risk and without right to reimbursement from his cotenant.<sup>61</sup> The general result is

<sup>&</sup>lt;sup>56</sup> White v. Smyth, 214 S.W.2d 967 (Tex. 1948).

<sup>&</sup>lt;sup>57</sup> Willson v. Superior Oil Co., 274 S.W.2d 947, 950 (Tex. Civ. App.—Texarkana 1954, writ ref'd n.r.e.)

<sup>&</sup>lt;sup>59</sup>*Id*..

<sup>&</sup>lt;sup>60</sup> Burnham v. Hardy Oil Co., 147 S.W. 333, 334 (Tex. Civ. App. 1912) aff'd 195 S.W. 1139 (Tex. 1917).

<sup>&</sup>lt;sup>61</sup> Willson, 274 S.W.2d at 950.

that having unleased cotenants is very bad for the developing cotenants. The unleased cotenant requires an entirely separate accounting system, may contest allocation of costs, and may cherry-pick whether to be in or out of wells after riding them down to see the results.

Each cotenant may lease his undivided interest in the property without the consent of the other cotenant.<sup>62</sup> During the period of such a lease, the lessee enjoys the same rights and privileges to enter upon the common premises for the purpose of exploration and development that his lessor had prior to the execution of the lease and is considered a cotenant with the cotenants of his lessors.<sup>63</sup>

In Section 1, the 1/3 owner and the 2/3 owner both own undivided mineral interests in the Yellow Tract; therefore, both have the right to develop the Yellow Tract subject to an accounting to the other, and both have the right to lease their interest without the other's consent. The 1/16 NPMI is nonparticipating with no right to develop the Yellow Tract. Because the 2/3 owner has chosen to lease his interest, the lessee is now a cotenant with the 1/3 owner. If the lessee produces from Location #3, he must pay 2/3 of the royalty specified in the lease to the lessor, less 2/3 of 1/16 payable to the owner of the 1/16 NPMI. After recovering all costs, the lessee must pay to the 1/3 unleased owner 1/3 of the production minus 1/3 of the reasonable and necessary expenses of production, less 1/3 of 1/16 of that share of production payable to the owner of the 1/16 NPMI.

-

<sup>&</sup>lt;sup>62</sup> Burnham, 147 S.W. at 334; Glover v. Union Pacific R. Co., 187 S.W.3d 201, 213 (Tex. App.—Texarkana 2006, pet. denied).

<sup>63</sup> Glover, 187 S.W.3d at 213.

#### E. Good Faith and Bad Faith Trespass

When one develops minerals without any interest in such minerals, he commits trespass and the true owner is entitled to recover damages from the trespassor.<sup>64</sup> The amount of the damages recoverable depends upon whether the trespass was in good faith or bad faith. In the case of a good faith trespass, the true owner may recover the value of the oil at the surface and in the pipeline minus the reasonable costs of drilling, operating, and producing the same.<sup>65</sup> In general, it may be said that to act in good faith in developing a tract of land for oil and gas, one must have both an honest and a reasonable belief in the superiority of his title.<sup>66</sup> Some examples of good faith trespass include tendering delay rentals in good faith, but insufficient quantities to keep the lease alive; drilling operations under a lease that fails because of a lessor's failure of title; and innocent mistake of location of boundary. When a good faith trespasser's reasonable costs of production exceed the value of minerals produced, there are no damages available to the true owner.<sup>67</sup> The result for the good faith trespasser is analogous to the circumstance of an unleased cotenant, but worse. The lessee will never make a dollar. It is at best a wash as to costs, but a loss of time and opportunity.

Bad faith trespassers, on the other hand, are accountable to the true owner for "the value of the things mined at the time of severance without making deduction for the cost of labor and

\_

<sup>&</sup>lt;sup>64</sup> Bender v. Brooks, 127 S.W. 168, 170 (Tex. 1910).

<sup>&</sup>lt;sup>65</sup> *Id.* (holding the measure of damages for taking oil from land through mistake as to ownership would be the value of the oil at the surface, less the reasonable cost of extracting it); *Hunt v. HNG Oil Co.*, 791 S.W.2d 191, 194 (Tex. App.—Corpus Christi 1990, writ denied) (holding that a good faith trespasser may properly deduct expenses incurred while it was a good faith trespasser, such as its completion costs, production taxes, transportation charges, operating expenses, and royalties paid).

<sup>66</sup> Mayfield v. Benavides, 693 S.W.2d 500, 504 (Tex. App.—San Antonio 1985, writ ref'd n.r.e.).

<sup>67</sup> Hunt v. HNG Oil Co., 791 S.W.2d 191, 194 (Tex. App.—Corpus Christi 1990, writ denied).

other expenses incurred in committing the wrongful act . . . or for any value he may have added to the mineral by his labor."<sup>68</sup>

Location #1 cannot be drilled. Anyone drilling on the Red Tract would be liable for trespass, and the owner of the Red Tract would be entitled to damages with the measure of damages depending on whether the trespasser was found to have conducted the operation honestly and with a reasonable belief in the superiority of his title. A trespasser who honestly and reasonably believed he had the right to drill on the Red Tract would be allowed to deduct the reasonable costs of development from the value of the minerals he produced from the Red Tract. Under the facts assumed, the drilling party would almost certainly be a bad faith trespasser. The result is that the well is a gift to the owner of the Red Tract. There is no trespass issue as to Locations #2, #3, and #4. Location #3 has an unleased owner, but the development is not a trespass, because 2/3 of the minerals are leased.

Horizontal wells are initially drilled vertically, and then at a pre-determined point, the drillstem deviates and proceeds horizontally into the targeted formation. A wellbore can extend across several tracts. Each tract traversed by the horizontal wellbore is a drillsite tract, and each production point on the wellbore is a drillsite. Thus, when a wellbore extends under both leased and unleased tracts, even though the well site is located on leased land, a trespass has occurred and the trespassor will be liable to the unleased owner for the portion of oil and gas produced from the unleased tract. There is authority in the context of a failed pooling that the Rule of Capture does not apply to horizontal wells and that the measure of damages payable to the owner of the unpooled tract would be measured by the royalties as specified in the lease,

<sup>68</sup> Mayfield v. Benavides, 693 S.W.2d 500, 506 (Tex. App.—San Antonio 1985, writ ref'd n.r.e.) (citing Cage Bros. v. Whiteman, 163 S.W.2d 638, 642 (Tex. 1942)).

<sup>69</sup> *Browning Oil Co., Inc. v. Luecke*, 38 S.W.3d 625, 634 (Tex. App.—Austin 2000, pet. denied)

<sup>&</sup>lt;sup>70</sup> See id; Owen L. Anderson, Lord Coke, the Restatement, and Modern Subsurface Trespass Law, 6 TEX. J. OIL GAS & ENERGY L. 203, 214 (2011).

compelling a determination of what production can be attributed to the unpooled tract with reasonable probability.<sup>71</sup> However, this case involved a leased tract and the plaintiff was seeking a recovery based on the royalty provisions in the lease. Cases involving slant hole drilling from tract A into tract B have held that the subsurface trespass is a trespass subject to the same rules as a surface trespass. There is no developed case law holding otherwise as to horizontal subsurface trespass. Thus, the damages issue could be serious. Moreover, a trespass, as a continuing tort, may be subject to injunction. That is, it is possible that the production could be shut-in.

As to Section 1, if Management drills the horizontal well at Location #5, presumably the entire section or a unit along the horizontal leg will be pooled. However, the horizontal wellbore traverses both the Red Tract (unleased) and the Yellow Tract (1/3 unleased). Unless the lessee can show he acted in good faith, he will be liable as a bad faith trespasser for the production attributable to the Red Tract without deduction for costs and would have to account to the unleased cotenant in the Yellow Tract for an undiluted 1/3 of production attributable to the Yellow Tract, after deducting beneficial costs. The owner of the 1/32 NPMI in the SE/4 should receive a share of the bad faith trespass payment on the Red Tract, out of the Red Tract owner's share, and if pooled and ratified, a proportionate part out of the share payable to the other owners in the SE/4. The owner of the 1/16 NPMI in the NE/4 should receive an undiluted share of the 1/3 unleased cotenant payout on the Yellow Tract, and if the Yellow Tract lease has not been ratified, an undiluted share out of the 2/3 leased interest, because the pooling clause is not applicable to the NPMI as to those interests.

-

<sup>&</sup>lt;sup>71</sup> Browning Oil Co., Inc., 38 S.W.3d at 647.

#### V. NONEXECUTIVE INTERESTS

## A. Types of Interests<sup>72</sup>

The executive right is one of the sticks in the bundle of property rights that make up the mineral estate. The ist is the "right to make decisions affecting the exploration and development of the mineral estate," but it is known as "the right to lease" because the holder of the executive right has the power to enter into leases on the land for the development and production of oil, gas, or other minerals. Executive rights are frequently severed from other incidents of mineral ownership. Nonexecutive mineral interest owners own the minerals but not the right to lease them, while nonexecutive royalty interest owners are those who own an interest in the royalty after the executive right holder executes a lease on the minerals. Additionally, a nonparticipating royalty interest, or NPRI, has a "well understood meaning" in the industry and "may be defined as an interest in the gross production of oil, gas, and other minerals carved out of the mineral fee estate as a free royalty, which does not carry with it the right to participate in the execution of, the bonus payable for, or the delay rentals to accrue under, oil, gas, and mineral leases executed by the owner of the mineral fee estate. These executive and nonexecutive interests are real rather than personal, and they survive the parties who created them.

-

<sup>&</sup>lt;sup>72</sup> See also Bruce M. Kramer, The Nature of the Mineral Estate (May 2, 2013).

<sup>&</sup>lt;sup>73</sup> Lesley v. Veterans Land Bd. of State, 352 S.W.3d 479, 480-81 (Tex. 2011); see supra, note 45; see also Day & Co. v. Texland Petrol., Inc., 786 S.W.2d 667, 669 (Tex. 1990) (describing the executive right as "an interest in property, an incident and part of the mineral estate like the other attributes such as bonus, royalty and delay rentals.").

<sup>&</sup>lt;sup>74</sup> Lesley, 352 S.W.3d at 487 (quoting Ernest E. Smith, *Implications of a Fiduciary Standard of Conduct for the Holder of the Executive Right*, 64 Tex. L. Rev. 371, 372 (1985)).

<sup>&</sup>lt;sup>75</sup> Mathews v. Sun Oil Co., 425 S.W.2d 330, 333 (Tex. 1968).

<sup>&</sup>lt;sup>76</sup> Lesley, 352 S.W.3d at 487 (quoting Ernest E. Smith, *Implications of a Fiduciary Standard of Conduct for the Holder of the Executive Right*, 64 Tex. L. Rev. 371, 372 (1985)).

<sup>&</sup>lt;sup>78</sup> Plainsman Trading Co. v. Crews, 898 S.W.2d 786, 789-90 (Tex. 1995) (quoting Lee Jones, Nonparticipating Royalty, 26 Tex. L. Rev. 569 (1948)) (emphasis in case).

<sup>&</sup>lt;sup>79</sup> *Lesley*, 352 S.W.3d at 487.

Although the holder of the executive right generally does not have a duty to lease the minerals, the Texas Supreme Court has held that "[i]f the refusal is arbitrary or motivated by self-interest to the non-executive's detriment" then the executive may have breached the fiduciary duty owed to the nonexecutive interest owner.<sup>80</sup>

#### B. Bonus Payments

Generally, both executive mineral owners and nonexecutive mineral owners share in royalty and bonus payments under an oil and gas lease, unless a contrary provision appears in the instrument creating the executive interest.<sup>81</sup> A pure royalty interest is distinguishable because it shares in production only without an interest in bonus or rentals.<sup>82</sup> However, the creating instrument may allocate rights among the parties in whatever fashion desired. The lessee should make bonus and royalty payments to nonexecutive mineral owners absent an agreement between all parties to the contrary, even though there is some Texas case law placing a duty on the executive owner to pay over to the nonexecutive mineral owner the nonexecutive mineral owner share of the payment. Some lessees may attempt to address the problem by including a lease provision wherein royalty and other payments must be paid out of the share of lessor (the executive right holder), but it is not resolved under Texas law whether such a provision is effective.

<sup>&</sup>lt;sup>80</sup> *Id.* at 491.

<sup>81 2-3</sup> Williams & Meyers, Oil and Gas Law § 339, Rights and Duties of the Executive ("The participation in lease benefits by a nonexecutive mineral owner depend on the terms of his deed, but typically such owner shares in bonus, rental and royalty."). Compare with the case of a pure royalty interest owner who is entitled to royalty only with no claim to bonus or delay rentals. 1-3 Williams & Meyers, Oil and Gas Law § 303.2, Consequences: Participation in Bonus and Delay Rentals (2012) (citing State Nat'l Bank of Corpus Christi v. Morgan, 135 Tex. 509, 143 S.W.2d 757 (1940); Schlittler v. Smith, 128 Tex. 628, 101 S.W.2d 543 (1937); Brady v. Security Home Investment Co., 640 S.W.2d 731 (Tex. App.—Houston [14th Dist.] 1982, no writ)).

<sup>&</sup>lt;sup>82</sup> Schlittler, 101 S.W.2d at 544.

The terms of the creating instrument may limit the executive owner's ability to designate how payments under an oil and gas lease should be made. 83 For instance, in *Odstrcil v*. McGlaun, the Eastland Court of Civil Appeals reviewed a deed conveying the executive right for a tract of land that stated any lease executed by the owner of the executive right "shall provide for not less [than] one eighth royalty on oil and provided further that grantors' part of any and all payments, bonus, delay rentals and/or royalties arising by virtue of any such lease and/or leases [must] be paid to grantors . . . . "84 The executive right owner executed a lease on the subject land that provided for delay rentals to be paid to the "lessor," without requiring payments to be made to the grantor. The court observed that the terms of the deed conveying the executive right granted the executive owner full power and authority to execute mineral leases, without joinder of the grantors, upon such terms and conditions and for such length of time as executive owner might deem proper. However, this power was limited by the size of the royalty and the manner of payment to grantors. The court found that the lessee and his assigns had notice of the terms of the deed; the deed was of record and in the lessee's chain of title to their lease. The court therefore held the lease provision requiring payment of rentals to lessor was in violation of the limitation on the executive owner's right to lease, was unauthorized, and therefore the lease was not binding on the grantors.<sup>85</sup>

Absent limitations in the creating instrument, Texas law is unsettled as to the validity of an oil and gas lease designating the executive owner as recipient of all payments under the lease,

-

<sup>&</sup>lt;sup>83</sup> See 2-3 Williams & Meyers, Oil and Gas Law § 330 (stating, "If [the terms of the deed] provide[] that any lease by the executive shall provide for the payment of rentals to the non-executive mineral owner, then lessee's failure to tender the correct amount of rental terminates the lease. If, on the other hand, the language of the deed is less specific, providing . . . that the nonexecutive is to 'receive' the rental, it would be proper to hold that payment of rentals to the executive satisfies the terms of the lease and non-payment to the non-executive will not cause termination of the lease.").

<sup>84 230</sup> S.W.2d 353, 354 (Tex. Civ. App.—Eastland 1950, no writ).

<sup>&</sup>lt;sup>85</sup> *Id.* at 355.

with a duty to account to the nonexecutive owner. "[A] lessee must at present assume that rentals are payable to the non-executive, whatever the terms of the deed may be. Otherwise, by paying the executive, the lessee runs the *risk* of losing part of the lease." Although the executive has the right to execute a lease covering the nonexecutive's mineral interest, as long as he acquires for the nonexecutive every benefit that he exacts for himself, there is no express authority granting the executive the right to accept benefits under a lease on behalf of the nonexecutive owner.

However, if a lessee chooses to make payments to the executive owner, Texas case law at least indicates the executive owner has a duty to provide a nonparticipating royalty owner with his share of the royalty. <sup>87</sup> In *Andretta v. West*, the Texas Supreme Court considered the claim of a nonparticipating royalty interest owner against the executive right owner and the lessee to recover its share of certain payments made by lessee to holders of the executive right. <sup>88</sup> The court analogized the case to situations involving a vendor's duty to account to his vendee for rents collected by the former which rightfully belong to the later as well as situations involving a cotenant's duty to account to the other tenants in common when he receives rent from a third person for use of the entire property. The court held that it was the executive owner's duty, if he knew the name and whereabouts of the royalty owner, to account to him for his share of the

Ω

<sup>&</sup>lt;sup>86</sup> 2-3 Williams & Meyers, Oil and Gas Law § 330 (noting however, "From the viewpoint of social utility, however, much can be said for a decision allowing the lessee to pay all rentals to the executive, at least where the language of the deed does not require a contrary result." Furthermore, while the discussion in this treatise revolved around rentals, the concept of bonus payments is analogous, but the bonus is also likely to be of far greater consequence.) (emphasis added).

Andretta v. West, 415 S.W.2d 638, 641 (Tex. 1967) ("In somewhat analogous situations, it is generally held that a vendor must account to his vendee for rents collected by the former which rightfully belong to the latter."); Friddle v. Fisher, 378 S.W.3d 475, 482 (Tex. App.—Texarkana 2012, pet. filed) (holding that when lessee paid the executive owner the required royalty payments under the lease, the executive owner "had a duty to hold the portion of funds which would be payable to the holder of the NPRI as constructive trustees for the use and benefit of the holder of the NPRI.").

<sup>&</sup>lt;sup>88</sup> *Andretta*, 415 S.W.2d at 641.

payments, and if the name and whereabouts were unknown, to hold the royalty as constructive trustees subject to the demand of the rightful owner.<sup>89</sup>

The safest practice would be to require the executive and nonexecutive owners to sign a division order. 90 In the absence of limitations in the creating instrument, the terms of a division order may govern how payment is distributed.<sup>91</sup> The Texas Division Order Statute defines "payee" as "any person or persons legally entitled to payment from the proceeds derived from the sale of oil or gas from an oil or gas well located in this state."92 The Statute requires that "[t]he proceeds derived from the sale of oil or gas production from an oil or gas well located in this state must be paid to each payee by payor."93 A division order allows the payee to direct the distribution of proceeds from the sale of oil and gas.<sup>94</sup>

# C. Ratification and Pooling<sup>95</sup>

Producing cotenants must account to those mineral owners who are not consenting to lease on the basis of the nonconsenting owner's share of production less costs. 96 Ratification of an oil and gas lease provides the nonconsenting cotenant with the opportunity to become entitled to a proportionate share of the lease royalty (not a share of net profits). 97 If one cotenant signs a lease that purports to cover the entire tract and (1) the lease contains a pooling clause, (2) the

<sup>&</sup>lt;sup>89</sup> *Id*.

<sup>90</sup> Laura H. Burney, The Interaction of the Division Order and the Lease Royalty Clause, 28 St. MARY'S L.J. 353, 356-57 (1997) ("As a rule, once production begins, all interest owners become entitled to their share of production or the proceeds from the sale of that production. However, because of ambiguities in the lease royalty clause and complications in the chain of title, controversies frequently arise regarding the allocation of the production or the proceeds received from the sale of the production. Therefore, to protect themselves against liability for conversion or for failure to account properly, lessees or third-party purchasers historically have implemented an additional document in the payment process: the division order.").

<sup>&</sup>lt;sup>91</sup> TEX. NAT. RES. CODE § 91.401(1)(1991).

<sup>&</sup>lt;sup>92</sup> *Id.* at § 91.401(3).

<sup>&</sup>lt;sup>93</sup> *Id.* at § 91.402.

<sup>&</sup>lt;sup>94</sup> *Id.* at § 91.401(3).

<sup>&</sup>lt;sup>95</sup> See also Charlotte M. Meyer, Pooling Issues for the Title Examiner (May 3, 2013).

<sup>96</sup> Burnham v. Hardy Oil Co., 147 S.W. 330, 334 (Tex. Civ. App.—San Antonio 1912), aff'd, 108 Tex. 555, 195 S.W. 1139 (1917).

<sup>&</sup>lt;sup>97</sup> Tex. & Pac. Coal & Oil Co. v. Kirtley, 288 S.W. 619, 622 (Tex. Civ. App.—Eastland 1926, writ ref'd).

lease covers multiple tracts with differing ownership and contains an entirety clause, or (3) the lease is a community lease, the unleased cotenant can ratify the lease and will receive a royalty share (not a share of net profits) of any pooled production from a well located on the unleased cotenant's tract or *off* the tract but subject to the lease.

Ratification is "the adoption or confirmation by a person, with knowledge of all material facts, of a prior act which did not then legally bind him and which he had the right to repudiate, but which, by the ratification, is given retroactive effect as if originally performed by him." Ratification is accomplished when the nonconsenting mineral owner recognizes the lease, such as by express ratification, <sup>99</sup> executing a division order and thereby claiming a share of the royalty, <sup>100</sup> accepting late payments, <sup>101</sup> or even by filing a lawsuit. <sup>102</sup> An example form ratification for a cotenant is attached to this article as Exhibit D. The unleased cotenant may have more than one lease to choose from when electing to ratify. The prudent unleased cotenant will presumably select the lease with the highest royalty. The working interest owner will want to be clear as to which lease is ratified. Ratifications should be recorded in the county where the land covered by the ratified lease is located.

In Texas, the executive cannot pool nonparticipating royalty interests. <sup>103</sup> If a lease with a pooling clause purports to cover a nonparticipating royalty interest, the nonparticipating royalty

98 Kunkel v. Kunkel, 515 S.W.2d 941, 948 (Tex. Civ. App.—Amarillo 1974, writ ref'd n.r.e.).

<sup>&</sup>lt;sup>99</sup> Gill v. Bennett, 59 S.W.2d 473, 475 (Tex. Civ. App.—El Paso 1933, writ ref'd).

<sup>&</sup>lt;sup>100</sup> Kirtley, 288 S.W. at 622.

<sup>&</sup>lt;sup>101</sup> Day & Co. v. Texland Petrol., Inc., 786 S.W.2d 667, 670 (Tex. 1990).

<sup>&</sup>lt;sup>102</sup> Montgomery v. Rittersbacher, 424 S.W.2d 210 (Tex. 1968); but see Nugent v. Freeman, 306 S.W.2d 167, 170 (Tex. Civ. App.—Eastland 1957, writ ref'd n.r.e.) (holding that filing suit was not sufficient to ratify the lease by the nonexecutive right owner when the owner knew of production for two years).

<sup>&</sup>lt;sup>103</sup> Brown v. Smith, 141 Tex. 425, 174 S.W.2d 43, 46 (1943); Nugent v. Freemen, 306 S.W.2d 167, 170-71 (Tex. Civ. App.—Eastland 1957, writ ref'd n.r.e.); Minchen v. Fields, 162 Tex. 73, 345 S.W.2d 282, 285 (1961) (citing Veal v. Thomason, 138 Tex. 341, 159 S.W.2d 472, 476 (1942)); MCZ, Inc. v. Triolo, 708 S.W.2d 49, 53 (Tex. App.—Houston [1st Dist.] 1986, writ ref'd n.r.e.).

owners have the option to ratify or to refuse to recognize a pooling. 104 Presumably, the same option would apply to a nonparticipating mineral owner. Therefore, in addition to seeking ratifications from unleased cotenants, working interest owners should seek ratifications from every nonparticipating interest owner, because even though the holder of the executive right has the right to grant a lease covering the interests of nonexecutive owners, the executive right owner cannot grant the lessee the right to pool or communitize those interests. 105 Even in the context of a single lease covering multiple tracts with differing royalty ownership, the courts have consistently recognized the right of a nonparticipating royalty owner to ratify the lease and to be paid for production from any tract covered by the lease on a pooled basis. 106 The nonparticipating owner may try to carefully select which lease to ratify, in order to take advantage of the lease with the highest royalty. However, it is unlikely that the unleased nonparticipating owner subject to multiple leases can pick one to ratify as to all of his interest. The nonparticipating owner can exercise the option differently as to different wells, i.e., he can ratify as to a unit well off lease, and refuse to be pooled as to a unit well that, as to him, is a lease well. 107 An example form ratification for a nonparticipating owner is attached to this article as Exhibit E.

Texas courts have drawn a distinction between ratifying *leases* and ratifying *pooled units*. In *MCZ*, *Inc. v. Triolo*, the court held that the nonparticipating royalty owner did not ratify the lease but rather had ratified select pooled units, such that the consent did not apply to the

\_

<sup>&</sup>lt;sup>104</sup> Montgomery v. Rittersbacher, 424 S.W.2d 210, 214-15 (Tex. 1968).

<sup>163</sup> *Id.* at 213.

<sup>&</sup>lt;sup>106</sup> *Id.*; *Ruiz v Martin*, 559 S.W.2d 839, 844 (Tex. App.—San Antonio 1977, writ ref'd n.r.e.).

<sup>&</sup>lt;sup>107</sup> MCZ, Inc. v. Triolo, 708 S.W.2d 49, 53-54 (Tex. App.—Houston [1st Dist.] 1986, writ ref'd n.r.e.).

remainder of the leased lands. <sup>108</sup> Therefore, the nonparticipating royalty owner was not engaging in "partial ratification" of the lease but was instead validly entering into distinct transactions. <sup>109</sup>

In *Ruiz v. Martin*, one party owned a nonparticipating royalty interest in a tract of land called Tract I.<sup>110</sup> Another party, who owned the remaining fee title in Tract I and also owned the unencumbered fee title to Tract II, granted an oil and gas lease covering both Tract I and Tract II, that contained no entirety clause.<sup>111</sup> The lessee completed a gas well on Tract II, and the nonparticipating royalty owner in Tract I then very promptly executed a written ratification of the lease of Tracts I and II and filed the instrument for record.<sup>112</sup> The court held that the ratification of the lease by the owner of an interest in one of the two tracts covered by the lease had the effect of pooling that interest, on an acreage basis, with the other interests in both tracts, so that the nonparticipating royalty owner was, from the ratification date forward, entitled to participate in the royalties on the production from the tract in which he initially had no interest.<sup>113</sup> In effect, the court said that the making of the lease amounted to a proposal or offer to effect a community pooling of interests, which the nonparticipating royalty owner accepted and implemented by his ratification.<sup>114</sup> The effect was the same as if that owner had initially joined in the lease.

The timing of the ratifications creates a tension in these situations between the nonconsenting mineral owner, who would prefer to first observe the drilling activity and then refrain from ratifying the lease if the well is drilled on his tract (and thereby enjoy his royalty undiluted by pooling) or ratify the lease if the well is drilled on the other tract (and thereby

\_

<sup>&</sup>lt;sup>108</sup> 708 S.W.2d at 53.

<sup>109</sup> Id

<sup>110 559</sup> S.W.2d at 840.

<sup>&</sup>lt;sup>111</sup> *Id.* at 840-41.

<sup>&</sup>lt;sup>112</sup> *Id.* at 841.

<sup>113</sup> Id. at 843-44.

<sup>&</sup>lt;sup>114</sup> *Id.* at 844.

participate in the royalty production on a pooled basis), and the working interest owner, who will want to lease up interests early, or exclude those who chose not to ratify until it became profitable to do so. The amount of time a nonconsenting mineral owner may wait before ratification is unsettled. In *Montgomery v. Rittersbacher*, the Texas Supreme Court upheld ratification eight years after the first well was drilled and more than three years from the drilling of a dry hole. In *Ruiz*, the San Antonio Court of Appeals upheld the ratification by nonparticipating royalty owners executed one month after the successful completion of a producing well.

The offer to lease does not extend to ratification by other lessees of unit designations, however. In *Fletcher v. Ricks Exploration*, Fletcher acquired an oil and gas lease on an undivided 1/4 interest in 29.675 acres.<sup>117</sup> Subsequently, Ricks, the operator who had drilled a well, and other working interest owners executed a unit designation creating a 259.47 acre unit, which included the 29.675 acre tract covered by Fletcher's lease.<sup>118</sup> After unsuccessful negotiations to join the unit, Fletcher unilaterally executed and filed for record a ratification of the unit designation, and claimed a pooled interest in production.<sup>119</sup> In rejecting this argument, the court stated: "Fletcher further argues that offer was extended to him by virtue of the inclusion of his 29.675 acre tract in the unit designation, accompanied by the filing of that unit designation . . . we decline to hold that the mere preparation and the filing of a unit designation constitutes an offer to all persons who hold leases on land within the designated acreage to join in the unit."<sup>120</sup> The court further declined to analogize the position of Fletcher to that of an unleased cotenant

<sup>&</sup>lt;sup>115</sup> 424 S.W.2d 210, 212-13 (Tex. 1968).

<sup>&</sup>lt;sup>116</sup> 559 S.W.2d at 843-44.

<sup>&</sup>lt;sup>117</sup> 905 F.2d 890, 891-92 (5th Cir. 1990).

<sup>&</sup>lt;sup>118</sup> *Id*.

<sup>&</sup>lt;sup>119</sup> *Id*.

<sup>&</sup>lt;sup>120</sup> *Id.* at 892.

who attempts to ratify a lease that purports to cover the cotenant's interest. Although Fletcher's lessor, as an unleased cotenant, could have ratified the Ricks lease before leasing to Fletcher, Fletcher, as lessee of a cotenant, could not. This was a federal court applying Texas law, but there is no Texas case directly on point.

A designation of unit is a document filed of record in the county where the land is located that specifies the voluntary joinder of separate ownership interests between working interest owners for drilling purposes. A form Designation of Pooled Unit is attached as Exhibit F.

# D. Joint Operating Agreements<sup>122</sup>

A joint operating agreement ("JOA") is a contract between working interest owners that sets forth the contractual agreement of the parties for the joint operation of oil and gas properties. Generally, the agreement will call for the development of the leases by one of the parties who is designated as the operator, but all parties will share in the costs of the operations and distribute the revenue. The 1982 Model Form Operating Agreement created by the American Association of Professional Landmen will be used herein as an example for its effect on unleased interests.

Exhibit A to the JOA should identify the lands, or the "Contract Area," and contributed leases that are subject to the agreement, detail depth and formation restrictions, and set forth the interests of the parties in the Contract Area. Actual title may form the basis for negotiation, but because Exhibit A is a contractual agreement that allocates costs and production in the Contract Area, actual title is ultimately irrelevant.

The JOA is a risk-spreading contract. Because the risk of the unleased interest can be spread across all of the working interest owners, the JOA, depending upon how it is completed, may serve to reduce the risk to individual working interest owners to a manageable level.

<sup>&</sup>lt;sup>121</sup> *Id*. at 893.

<sup>122</sup> See also H. Martin Gibson, Title Aspects of the Joint Operating Agreement (May 3, 2013).

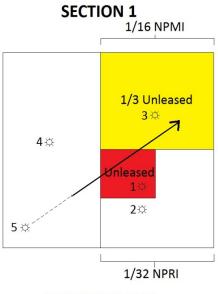
Page 32 of 54

Paragraph III(B) states that the parties' proportions of costs and production are set out in Exhibit A. Generally, the split is derived by assessing the total leasehold mineral acreage position of each party in the Contract Area, giving equal value to each leasehold mineral acre. Although production is shared, revenue is not. Each party owns and must dispose of its share of production appropriately, paying royalties to royalty owners out of its share, "[r]egardless of which party has contributed the lease(s) and/or oil and gas interest(s) hereto on which royalty is due and payable...." However, no party must account to another party's lessor on a price basis higher than the price received by that party. Additionally, Paragraph III(C) states "if the interest of any party in any lease covered hereby is subject to any royalty, overriding royalty, production payment or other burden on production" over the amount set forth in Paragraph III(B) the burdened party bears the excess burden alone. Often a gas balancing agreement will be attached to the JOA in order to correct for imbalances that arise in marketing the production.

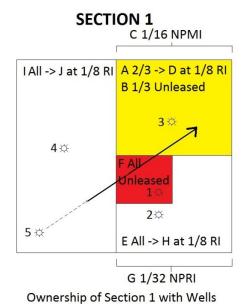
Paragraph IV(B) sets forth the consequences of loss of title under the JOA. Paragraph IV(B)(1) states that the party whose oil and gas lease or interest is affected by a title failure bears alone the entire loss. Similarly, in Paragraph IV(B)(2), a party whose interest or lease terminates through nonpayment of rentals or shut-in or other royalties, solely bears the loss. In contrast to the Individual Loss provisions of Paragraph IV(B)(1) and IV(B)(2), Paragraph IV(B)(3) is a Joint Loss provision, stating that any other loss "shall be borne by all parties in proportion to their interest." Because "joint loss" is usually selected by the parties, the parties spread the legal risks inherent in development with unleased interests so that they become more acceptable.

# E. Examples<sup>123</sup>

To illustrate the allocation of production and some of the risks and issues, the original simple Prospect has been made more complicated by adding some royalty and mineral ownership and lease royalty detail as shown here and in Exhibits A and A-1.



POSSIBLE WELL SITES



<sup>&</sup>lt;sup>123</sup> See also Terry Hogwood, Calculation and Payment of Royalties – Unleased Mineral Owners and Non-Ratified Royalty Owners (May 3, 2013).

Page 34 of 54

Recall that the NE/4 (Yellow Tract) is 2/3 leased, 1/3 unleased, and a 1/16 nonparticipating mineral interest burdens the entire quarter section. A owns 2/3 of the NE/4, subject to 2/3 of the 1/16 NPMI, B owns 1/3 of the NE/4, subject to 1/3 of the 1/16 NPMI, C owns the 1/16 NPMI. A leased to D at a 1/8 royalty.

Recall that in the SE/4, the NW/4 SE/4 (Red Tract) is not subject to lease, while the rest of the quarter section is leased, and a 1/32 nonparticipating royalty interest burdens all of the SE/4. E owns the NE/4 SE/4 and S/2 SE/4, subject to the 1/32 NPRI, F owns the NW/4 SE/4, subject to the 1/32 NPRI, G owns the 1/32 NPRI, E leased to H at a 1/8 royalty.

I owns the W/2. I leased to J at a 1/8 royalty

- 1. Unpooled Net Revenue Interests
  - A) NW/4 SE/4 Location #1
    - F is entitled to all of 8/8 less 1/32, or .96875 NRI
    - G is entitled to royalty of 1/32, or .03125 NRI
    - Note that both interests sum to 1
  - B) NE/4 SE/4 and S/2 SE/4 Location #2
    - E is entitled to royalty of 1/8 less 1/32, or .09375 NRI
    - G is entitled to royalty of 1/32, or .03125 NRI
    - H is entitled to working interest of 7/8, or .875 NRI
    - Note that all three interests sum to 1
  - C) NE/4 Location #3
    - Because the NPMI is nonparticipating, it is leased and unleased in proportion to its ownership by the executives: 2/3 leased, 1/3 unleased
    - A is entitled to royalty of 2/3 of 1/8 less 2/3 of 1/8 of 1/16, or .078125 NRI

- B is entitled to an unleased cotenant share of 1/3 less 1/3 of 1/16, or .3125 NRI
- C is entitled to royalty of 2/3 of 1/8 of 1/16, or .005208 NRI plus an unleased cotenant share of 1/3 of 1/16, or .020833 NRI, for a total NRI of .026042
- D is entitled to working interest of 2/3 of 7/8, or .583333 NRI
- Note that all four interests sum to 1
- If, for instance, a lease covered both the SE/4 and the NE/4, G would be in the enviable position of not having to ratify the lease for Locations #1 and #2 (*i.e.* SE/4) but could ratify the lease for Location #3 (*i.e.*, NE/4)
- D) W/2 Location #4 (not horizontal Location #5)
- I is entitled to royalty of 1/8, or .125 NRI
- J is entitled to working interest of 7/8, or .875 NRI
- Note that both interests sum to 1
- 2. Effect of Pooling
  - A) Location #1
    - Unpooled
      - o F: 8/8 less 1/32
      - o G: 1/32
      - o All others: -0-
    - Section Pooled Invalid
      - o F: 8/8 less 1/32
      - o G: 1/32
      - o All others: -0-

## B) Location #2

- Unpooled
  - E: 1/8 less 1/32
  - o G: 1/32
  - o H: 7/8
  - o All others: -0-
- Section Pooled
  - o A: (160/640 of 2/3 of 1/8) less (160/640 of 2/3 of 1/8 of 1/16)
  - B: -0- or attempt to ratify [who gets 160/640 of 1/3 less 160/640 of 1/3 of 1/16 share if -0-?]
  - C: 160/640 of 2/3 of 1/8 of 1/16 and -0- [who gets 160/640 of 1/3 of 1/16 share if -0-?]
  - o D: 160/640 of 2/3 of 7/8
  - o E: (120/640 of 1/8) less (120/640 of 1/32)
  - o F: -0- [who gets 40/640 less 40/640 of 1/32 share if -0-?]
  - o G: 120/640 of 1/32 and -0- [who gets 40/640 of 1/32 share if -0-?]
  - o H: 120/640 of 7/8
  - o I: 320/640 of 1/8
  - J: 320/640 of 7/8

## C) Location #3

- Unpooled
  - o A: (2/3 of 1/8) less (2/3 of 1/8 of 1/16)
  - o B: 1/3 unleased cotenant share less 1/3 of 1/16

- o C: 2/3 of 1/8 of 1/16 and unleased cotenant share of 1/3 of 1/16
- o D: 2/3 of 7/8
- o All others: -0-

## Section Pooled

- o A: (160/640 of 2/3 of 1/8) less (160/640 of 2/3 of 1/8 of 1/16)
- o B: 1/3 unleased cotenant share less 1/3 of 1/16 [unpooled and undiluted]
- C: (160/640 of 2/3 of 1/8 of 1/16) and 1/3 of 1/16 (unleased cotenant share [unpooled and undiluted])
- o D: 160/640 of 2/3 of 7/8
- o E: (120/640 of 1/8) less (120/640 of 1/32)
- o F: -0- [who gets 40/640 less 40/640 of 1/32 share if -0-?]
- o G: 120/640 of 1/32 and -0- [who gets 40/640 of 1/32 share if -0-?]
- o H: 120/640 of 7/8
- o I: 320/640 of 1/8
- o J: 320/640 of 7/8

## D) Location #4

- Unpooled
  - o I: 1/8
  - o J: 7/8
  - o All others: -0-

## Section Pooled

o A: (160/640 of 2/3 of 1/8) less (160/640 of 2/3 of 1/8 of 1/16)

- B: -0- or attempt to ratify [who gets 160/640 of 1/3 less 160/640 of 1/3 of 1/16 share if -0-?]
- C: 160/640 of 2/3 of 1/16 and -0- [who gets 160/640 of 1/3 of 1/16 share if -0-?]
- o D: 160/640 of 2/3 of 7/8
- o E: (120/640 of 1/8) less (120/640 of 1/32)
- o F: -0- [who gets 40/640 less 40/640 of 1/32 share if -0-?]
- o G: 120/640 of 1/32 and -0- [who gets 40/640 of 1/32 share if -0-?]
- o H: 120/640 of 7/8
- I: 320/640 of 1/8
- o J: 320/640 of 7/8

#### E) Location #5

Location #5 is for a horizontal well with the horizontal surface location in the W/2. The turn from directional into horizontal is also in the W/2, the bold line indicates the existence of the horizontal leg in the production zone, and the terminus of the lateral is in the NE/4. Note the well is producing from the W/2, NW/4 SE/4 (Red Tract), and NE/4 (Yellow Tract).

- Unpooled
  - o Impossible to drill
- Section Pooled (may be impossible to drill)
  - o A: (160/640 of 2/3 of 1/8) less (160/640 of 2/3 of 1/8 of 1/16)
  - o B: 1/3 unleased cotenant share less 1/3 of 1/16 [unpooled and undiluted]
  - o C: (160/640 of 2/3 of 1/8 of 1/16) and (1/3 of 1/16 [unpooled and undiluted])

- o D: 160/640 of 2/3 of 7/8
- o E: (120/640 of 1/8) less (120/640 of 1/32 [assuming ratification by G])
- F: (All? 40/640 of All?) less (1/32? 40/640 of 1/32?) [trespass issues]
- G: (120/640 of 1/32 [assuming ratification of Lease E]) and (1/32? 40/640 of 1/32?) [trespass issues]
- o H: 120/640 of 7/8
- o I: 320/640 of 1/8
- J: 320/640 of 7/8

#### VI. LITIGATION

#### A. MIPA

The Mineral Interest Pooling Act ("MIPA") is a potential solution to the problem posed by unleased or nonconsenting mineral interest owners. <sup>124</sup> In the statute's 45+ year history, only a very small number of force pooling applications have been approved. <sup>125</sup> The reason the MIPA is so infrequently used appears to be partly by design and partly due to inconvenience. The statute is expressly limited to a specific set of circumstances. There are a large number of fields and proposed wells that simply are not subject to the statute. Moreover, the statutory requirements are burdensome and the reward often does not justify the effort. But infrequent use of the statute does not make it irrelevant. The purpose of the MIPA is to encourage voluntary pooling, and the mere existence of a forced pooling statute reduces the need to rely upon it. The existence of the statue has encouraged large tract owners to let small tract owners into the larger unit.

<sup>124</sup> TEX. NAT. RES. CODE § 102.

Scott, Douglas & McConnico, L.L.P., Forced Pooling In Texas: the Mineral Interest Pooling Act, When Can I Use it and How Does it Work?, H-1, Oil & Gas Regulation in Texas Seminar (2011) ("Indeed, only 102 forced pooling applications have been granted in the statute's 44 year history out of the 248 that have been filed through 2010...") (hereafter "Scott, Douglas").

The MIPA is applicable "[w]hen two or more separately owned tracts of land are embraced in a common reservoir of oil or gas for which the commission has established the size and shape of proration units, whether by temporary or permanent field rules, and where there are separately owned interests in oil and gas within an existing or proposed proration unit in the common reservoir and the owners have not agreed to pool their interests, and where at least one of the owners of the right to drill has drilled or has proposed to drill a well on the existing or proposed proration unit to the common reservoir . . . "126 Because the statute requires an existing field, it will never be applicable to a wildcat zone or well. If the existing well proposed for Section 1 is to be completed in an existing field, then it may apply, if the common reservoir extends under two or more separately owned tracts. The statute could not be used to pool the Yellow Tract, because there are not two or more separately owned tracts. If the ownership of the W/2 and the NE/4 is different and the common reservoir extends under both tracts, then the unleased cotenant in the Yellow Tract could be force pooled into a unit consisting of the W/2 and NE/4. Similarly, the SE/4 could be force pooled to include the Red Tract, if the two tracts in the SE/4 are separately owned and the common reservoir extends under both.

The MIPA does not apply to oil and gas fields discovered and produced prior to March 8, 1961, and it does not apply to State lands except with the consent of the State. There are many other reasons why the MIPA does not work very well. There are standing issues, procedural issues, timing issues, proof issues, and cost issues. Some of the bigger issues are the limitation on the risk penalty and the size of the pooled unit. The maximum risk penalty which can be imposed on a nonparticipating owner is 100% over costs. Risk penalties in modern joint operating agreements are frequently 300%, 400%, or even 500%. This is a maximum risk

\_

TEX. NAT. RES. CODE ANN. § 102.011 (emphasis added).

<sup>127</sup> *Id.* at § 102.003.

penalty and the order could impose a nominal amount.<sup>128</sup> The unit must contain the "approximate acreage" of the standard proration unit established by the special field rules.<sup>129</sup> The unit may not exceed 160 acres for an oil well and 640 acres for a gas well, plus a 10% tolerance.<sup>130</sup> The acreage limitations may not work for a horizontal well under Statewide Rule 86.

It is possible the MIPA may now be used in a way that is advantageous to lessees. The statute was originally intended to be a mechanism to allow small tract owners to "muscle-in" to larger tracts. However, in 2008, the Texas Railroad Commission held that a lessee who had leased 90.616 acres of a 96.32 pooled unit could use MIPA to force pool the interests of the remaining unleased 5.704 acres. The commission's rationale was that, in the absence of a force pooling order, the small mineral interest owners could drill a well and produce dramatically more minerals than those underlying their tracts, at the expense of the remaining owners in the pooled unit. This innovative use of the MIPA statute, colloquially known as "reverse MIPA" at the Railroad Commission, is a potential solution for the problem posed by unleased mineral owners. However, terms of the pooling were very favorable for the force pooled owners. The owners of the unleased tracts were pooled as owners of a 1/5 royalty and 4/5 working interest, proportionately reduced, subject to a zero risk penalty. Applying this rationale to Section 1, assuming the statutory requirements are met, Management could force pool the interests of the unleased owners in the SE/4 (Red Tract).

\_

<sup>&</sup>lt;sup>128</sup> *Id.* at § 102.052.

<sup>&</sup>lt;sup>129</sup> *Id.* at § 102.011.

 $<sup>^{130}</sup>$  Id

<sup>&</sup>lt;sup>131</sup> See Finley Resources Inc.'s MIPA Application, Oil & Gas Docket No. 09-0252773.

Scott, Douglas at H-25.

See Final Order Oil & Gas Docket No. 09-0252373.

## B. Receivership

The receivership statute provides a way to fill a hole in the Prospect when there is a missing royalty, mineral, or leasehold owner, or when there is a contingent interest which cannot be leased. Under the statute, a receiver can be appointed on behalf of the missing owners, and the receiver can sign a mineral lease, a ratification of a mineral lease, or an assignment of a mineral lease. Thus, to the extent the Red or Yellow Tracts in Section 1 are unleased due to mineral or royalty interest owners who cannot be found or they are leased to lessees who cannot be found, the receivership statute would be a convenient method for bridging the gap.

The defendant in the proceeding must be not only missing, but must also have paid no taxes on the interest for the preceding five years.<sup>135</sup> Before a Prospective lessee can invoke the statute, he must make a diligent effort to find the missing mineral owner.<sup>136</sup> The precise requirements for locating the owner are not spelled out in the statute or relevant case law, but the search should include, at a minimum, searching social media sites, telephone books, speaking with the grantor under the deeds that conveyed an interest to the grantee, and other such common methods.

After a diligent search has been completed, the prospective lessee should file a verified petition as plaintiff.<sup>137</sup> The petition should be filed in the county where the land lies and should describe with particularity the damage the plaintiff will sustain if the receiver is not appointed, <sup>138</sup>

<sup>&</sup>lt;sup>134</sup> TEX. CIV. PRAC. & REM. CODE ANN. §§ 64.091 – 64.093 (Vernon 2009).

<sup>135</sup> *Id.* at §§ 64.091(b-1)(1); 64.091(b-1)(2) and 64.093(b)(1); 64.093(b)(2).

<sup>136</sup> *Id.* at §§ 64.091(c)(1) and 64.093(c)(1).

<sup>&</sup>lt;sup>137</sup> *Id.* at §§ 64.091(c) and 64.093(c).

<sup>&</sup>lt;sup>138</sup> *Id.* at §§ 64.091(c)(2) and 64.093(c)(2).

as well as the steps taken to find the mineral or royalty owner.<sup>139</sup> The defendant should be served by the ordinary rules applicable to citation by publication.<sup>140</sup>

Prior to a hearing, an attorney *ad litem* will be appointed to represent the defendant (*i.e.*, the missing owner). At the hearing, the plaintiff should offer evidence from a qualified witness that speaks to the efforts made to find the missing defendant, the terms of the proposed lease, and the nature and extent of the damage the lessee will sustain if a receiver is not appointed. The court may then appoint a receiver, who can be the county judge, or a "resident of the county in which the land is located." The order should authorize the receiver to execute leases, ratifications, and pooling and unitization agreements. The plaintiff should ensure that any lease or ratification to be signed by the receiver is fair (contains comparable bonus, royalty and terms as found in other leases in the surrounding area on similar tracts). This will help ensure that the lease is not vulnerable to collateral attack, if the true owner appears. Pooling provisions are limited to 160 acres as to oil and 640 acres as to gas, which may be a problem, particularly as to horizontal wells. 142

There are similar provisions available to fill a hole in the Prospect attributable to a contingent interest, such as interests arising by way of remainder, reversion, possibility of reverter, executory devise, or the occurrence of a condition subsequent or otherwise.<sup>143</sup>

Receivership offers a solution to the problem of missing owners, but it is not without its drawbacks. For instance, because the proceeding is founded on notice by publication and representation by attorney *ad litem*, courts will usually insist on strict compliance with every element of the statute. As a result, receiverships can be tedious, time consuming, and expensive.

Page 44 of 54

<sup>&</sup>lt;sup>139</sup> *Id.* at §§ 64.091(c)(1) and 64.093(c)(1).

<sup>&</sup>lt;sup>140</sup> *Id.* at §§ 64.091(d)(2) and 64.093(d)(2).

<sup>&</sup>lt;sup>141</sup> *Id.* at §§ 64.091(d)(3) and 64.093(d)(3).

<sup>&</sup>lt;sup>142</sup> *Id.* at §§ 64.091(g), 64.092(f) and 64.093(g).

<sup>&</sup>lt;sup>143</sup> *Id.* at § 64.092.

#### C. Partition

In Texas, joint owners of real property, including mineral owners, may compel a partition among the other joint owners.<sup>144</sup> Partition can be by sale or in kind. If the existence of minerals in a tract of land is unknown, courts presume that each portion of the property is equally endowed with minerals, and thus partition in kind is generally preferred. On the other hand, courts prefer partition by sale for property with known minerals, because the possibility of unequal distribution of the minerals creates the risk that partition in kind would be inequitable.<sup>145</sup>

Partition is a potential solution to the problem posed by unleased mineral interest owners in the Prospect, if the partition in kind or by sale occurs at the proper time with a favorable partition. Prior to leasing, the owners of the 2/3 interest in the Yellow Tract could have brought an action against the 1/3 owner, for partition in kind or by sale. If the minerals were then unknown, the result would have been a smaller tract (presumably 2/3 of the NE/4, *e.g.*, west 2/3 of the NE/4) in which the 2/3 owner became the 3/3 owner. This would solve the unleased owner problem as to their now divided estate. However, in the case of Section 1, the owners of the *leased* 2/3 minerals in the NE/4 could not bring an action for partition against the unleased 1/3 interest because they have no possessory interest. The existence of the lease on the Yellow Tract suggests that the existence of the minerals is not unknown, any partition should be by sale, and the lessee of the 2/3 interest in the Yellow Tract probably does not want to sell. Nevertheless, a successful partition suit could render the NE/4 more drillable.

The right to partition is limited to possessory interests. Thus, owners of nonpossessory interests (e.g. royalties) are not entitled to partition. <sup>146</sup> Partition would be unavailable for the

<sup>&</sup>lt;sup>144</sup> TEX. PROP. CODE ANN. § 23.001 et seq (Vernon 1984).

<sup>&</sup>lt;sup>145</sup> Henderson v. Chelsey, 273 S.W. 299, 303 (Tex. Civ. App. 1925, writ denied) aff'd 292 S.W.156 (Tex. 1927).

<sup>146</sup> Douglas v. Butcher, 272 S.W.2d 553, 555 (Tex. Civ. App.—San Antonio 1954, writ ref'd n.r.e.).

Red Tract because there is no joint ownership, except as to the 1/32 NPRI, which is a nonpossessory interest. The 1/16 NPMI is presumably a nonpossessory interest and thus not a necessary party. However, some deeds creating such interests convey access rights and the rights to produce, so the deed creating the interest could be important.

# D. Trespass to Try Title<sup>147</sup>

"A trespass to try title action is a procedure by which rival claims to title or right of possession may be adjudicated." An action in trespass to try title may be used in a wide variety of disputes arising from land title claims, including boundary disputes and cases concerning claims between parties asserting conflicting rights of possession to realty. A trespass to try title action provides a legal remedy for recovering the possession of land unlawfully withheld from an owner with a right to immediate possession.

The plaintiff, to maintain an action in trespass to try title, must recover the strength of his own title, and not on the weakness of the defendant's title. Trespass to try title always puts both title and possession in issue. The defendant is the person in possession or claiming title to the property. The plaintiff has the burden of proving a *prima facie* case, which usually means plaintiff must: (1) prove a regular chain of title from the sovereign; (2) show superior title out of a common source; (3) prove title by limitations; or (4) prove title by prior possession,

For a more detailed article on trespass to try title, declaratory judgments, boundary disputes, and quiet title, *see*, Richard F. Brown, *Litigating Land, Title and Boundary Issues*, Twenty Second Annual Advanced Oil, Gas and Energy Resources Law Course (State Bar of Texas) (2004).

Yoast v. Yoast, 649 S.W.2d 289, 292 (Tex. 1983); TEX. PROP. CODE ANN. § 22.001, et seq.; TEX. R. CIV. P. 783-809.

<sup>&</sup>lt;sup>149</sup> *Martin v. Amerman*, 133 S.W.3d 262, 265 (Tex. 2004).

<sup>&</sup>lt;sup>150</sup> City of Dallas v. Patti, 286 S.W.2d 664, 665 (Civ. App.—Dallas 1956, writ ref'd n.r.e.).

<sup>&</sup>lt;sup>151</sup> Knupp v. Miller, 858 S.W.2d 945, 951 (Tex. App.—Beaumont 1993, no writ).

<sup>&</sup>lt;sup>152</sup> *Martin*, 133 S.W.3d at 264-65.

<sup>&</sup>lt;sup>153</sup> Permian Oil Co. v. Smith, 72 S.W.3d 490, 496 (Tex. 1934).

<sup>154</sup> Kenneshaw Life & Acc. Ins. Co. v. Goss, 694 S.W.2d 115, 118 (Tex. App.—Houston [14th Dist.] 1985, writ ref'd n.r.e.).

which was not abandoned.<sup>155</sup> If the plaintiff fails to meet his burden, a take nothing judgment will place whatever title plaintiff has in the property in defendant.<sup>156</sup> If the plaintiff meets his burden, the burden shifts to the defendant to produce some defensive evidence.<sup>157</sup> If plaintiff prevails, plaintiff will recover title or possession, or both from defendant.<sup>158</sup>

To prove title by a regular chain of conveyances from the sovereign, the plaintiff must establish a land grant or patent from the state or sovereignty showing that the title of the original grantee or patentee passed by successive conveyances to plaintiff.<sup>159</sup>

To prove title from a common source, the plaintiff must trace his title back to a common source by a complete chain of title, trace the defendant's title back to the same source, and prove that the plaintiff's claim or title is superior to the defendant's claim. Once the plaintiff establishes a common source, he then has the burden of proving a title superior to the adverse party's title. The oldest title out of the common source is the better title and is superior to all others.

Proof of title by prior possession requires that plaintiff's possession be prior in time to defendant's, and that there be no proof of title in defendant. Plaintiff can also prove title by adverse possession. 164

<sup>&</sup>lt;sup>155</sup> Rogers v. Ricane Enterprises, Inc., 884 S.W.2d 763, 768 (Tex. 1994).

<sup>&</sup>lt;sup>156</sup> Hejl v. Wirth, 343 S.W.2d 226-27 (Tex. 1961).

<sup>&</sup>lt;sup>157</sup> Walsh v. Austin, 590 S.W.2d 612, 616 (Tex. App.—Houston [1st Dist.] 1979, writ dism'd).

<sup>&</sup>lt;sup>158</sup> TEX. R. CIV. P. 804; *Logan v. First Bank*, 736 S.W.2d 927, 931 (Tex. App.—Beaumont 1987, writ ref'd n.r.e.).

Hunt v. Heaton, 643 S.W.2d 677, 679 (Tex. 1982); Gillum v. Temple, 546 S.W.2d 361, 363-364 (Tex. Civ. App.—Corpus Christi 1976, writ ref'd n.r.e.).

<sup>&</sup>lt;sup>160</sup> Dames v. Strong, 659 S.W.2d 127, 131 (Tex. App.—Houston [14th Dist.] 1983, no writ).

State of Texas v. Noser, 422 S.W.2d 594, 600 (Tex. Civ. App.—Corpus Christi 1968, writ ref'd n.r.e.).

<sup>&</sup>lt;sup>162</sup> Texas Consol. Oils v. Bartels, 270 S.W.2d 708, 712 (Tex. Civ. App.—Eastland 1954, writ ref'd).

<sup>&</sup>lt;sup>163</sup> Spinks v. Estes, 546 S.W.2d 390, 392 (Tex. Civ. App.—Tyler 1977, writ ref'd n.r.e.); Land v. Turner, 377 S.W.2d 181, 183 (Tex. 1964).

Champion Paper & Fiber Co. v. Wooding, 321 S.W.2d 127, 134 (Tex. Civ. App.—Waco 1959, writ ref'd n.r.e.); see supra Section III.B.

## E. Declaratory Judgments

Declaratory judgments in Texas are governed by the Uniform Declaratory Judgments Act ("UDJA"). <sup>165</sup> A person interested under a deed, will, written contract, or other writings constituting a contract or whose rights, status, or other legal relations are affected by a statute, municipal ordinance, contract, or franchise may have determined any question of construction or validity arising under the instrument, statute, ordinance, contract, or franchise and obtain a declaration of rights, status, or other legal relations thereunder. <sup>166</sup> A court of record within its existing jurisdiction has power to declare rights, status, and other legal relations. <sup>167</sup>

Declaratory judgments have been defined as preventative remedies consisting of determinations of legal rights where uncertainties and controversies arise between interested parties. By construing the meaning and effect of instruments included in the chain of title, a declaratory judgment can have a significant effect in resolving issues pertaining to title to real property.

The UDJA requires three basic elements to be present in a claim in order for a party to invoke the UDJA in a title dispute: (1) the parties in the suit must have an interest under a deed, will, or contract; (2) a true controversy must exist between the adverse parties; and (3) the court must be able to fully resolve the controversy. There is a plethora of conflicting precedent regarding what types of writings and what types of interests will satisfy the requirements under § 37.004 regarding the subject matter of relief.

 $<sup>^{165}</sup>$   $\,$  Tex. Civ. Prac. & Rem. Code Ann. § 37.002, et seq. (Vernon 1985).

<sup>&</sup>lt;sup>166</sup> *Id.* at § 37.004(a).

<sup>&</sup>lt;sup>167</sup> *Id.* at § 37.003(a).

Montemayor v. City of San Antonio Fire Dept., 985 S.W.2d 549, 551 (Tex. App.—San Antonio 1998, pet. denied).

TEX. CIV. PRAC. & REM. CODE ANN. §§ 37.004 and 37.008 (Vernon 1985).

The remedy in a suit for a declaratory judgment is a declaration defining the respective rights, duties, and legal status of the parties in the suit.<sup>170</sup> However, any judgment rendered under the UDJA will only affect parties to the suit.<sup>171</sup> An interested party that is not joined in the suit under the UDJA will not be prejudiced by the judgment rendered.<sup>172</sup> One of the biggest benefits of suing under the UDJA is that a party can recover attorney's fees under the Act.<sup>173</sup>

## F. Boundary Disputes

Trespass to try title was once the exclusive remedy by which competing claims to property could be resolved. Prior to the *Martin* case, it was clear that boundary disputes could be tried though trespass to try title, but the court had not addressed whether trespass to try title was the exclusive method for resolving such claims. Moreover, the Texas Supreme Court had held in dicta that "a [declaratory judgment] is certainly one way to resolve a boundary dispute . . . ." This led to some confusion in the lower courts about the proper legal avenue for bringing a boundary dispute.

In the *Martin* case, the Texas Supreme Court explained some of the fundamental distinctions between the principal methods of resolving title issues in Texas. The Court explained that a trespass to try title action is an action to recover possession of land by an owner entitled to immediate possession.<sup>177</sup> On the other hand, the UDJA "provides an efficient vehicle for parties to seek a declaration of rights under certain instruments." The court also

<sup>&</sup>lt;sup>170</sup> *Id.* at § 37.003.

<sup>&</sup>lt;sup>171</sup> *Id.* at § 37.006.

<sup>&</sup>lt;sup>172</sup> Texas Educ. Agency v. Leeper, 893 S.W.2d 432, 446 (Tex. 1994).

<sup>&</sup>lt;sup>173</sup> TEX. CIV. PRAC. & REM. CODE ANN. § 37.009 (Vernon 1985).

<sup>&</sup>lt;sup>174</sup> See Martin v. Amerman, 133 S.W.3d 262, 267 (Tex. 2004).

<sup>&</sup>lt;sup>175</sup> Hunt v. Heaton, 643 S.W.2d 677, 679 (Tex. 1982).

<sup>&</sup>lt;sup>176</sup> Brainard v. State, 12 S.W.3d 6, 29 (Tex. 1999).

<sup>&</sup>lt;sup>177</sup> *Martin*, 133 S.W.3d at 265.

<sup>&</sup>lt;sup>178</sup> *Id*.

emphasized the mandatory language of the trespass to try title statute; "the statute expressly provides that it is 'the method for determining title to . . . real property." 179

While the court's holding was intended to confine boundary dispute claims to trespass to try title, and limit the UDJA to actions to construe the terms of land contracts, the nuance of the court's holding generated confusion among the lower courts, and subsequent decisions struggled to treat the two as mutually exclusive.<sup>180</sup> The confusion appears to be primarily due to the fact that, "construing the terms of land contracts and deeds often implicates the issue of title, whether or not title is awarded in a particular case." Some courts have attempted to reconcile these seemingly overlapping holdings with a rule that, "if resolution of a dispute does not require a determination of which party owned title at a particular time, the dispute could properly be raised in a declaratory judgment action; in other words, if the determination only *prospectively* implicates title, then the dispute does not have to be brought as a trespass-to-try-title action." <sup>182</sup>

After *Martin*, the Texas legislature amended the Civil Practice and Remedies Code to provide:

Notwithstanding Section 22.001, Property Code, [the trespass to try title statute] a person described by Subsection (a) may obtain a determination under this chapter when the sole issue concerning title to real property is the determination of the proper boundary line between adjoining properties.<sup>183</sup>

Accordingly, it now appears that boundary disputes can be brought under the UDJA or trespass to try title.

<sup>183</sup> TEX. CIV. PRAC. & REM. CODE ANN. § 37.004 (Vernon 1985).

<sup>179</sup> Id. at 267 (emphasis in original)(citing Tex. Prop. Code Ann. § 22.002(a)).

See I-10 Colony, Inc. v. Chao Kuan Lee, 14-10-01051-CV, 2012 WL 6965355, at \*4-6 (Tex. App.—Houston [14th Dist.] Dec. 28, 2012, no. pet. h.).

<sup>&</sup>lt;sup>181</sup> *Id.* at \*5.

<sup>182</sup> Id

## G. Quiet Title

A suit in trespass to try title is statutory and accords a legal remedy, while a suit to quiet title is an equitable action.<sup>184</sup> If the quiet title suit is successful, the plaintiff will receive a court decree or declaration that the adverse claim is not valid, which will remove the cloud.<sup>185</sup> A cloud on title has been defined as "[a]ny deed, contract, judgment or other instrument not void on its face which purports to convey any interest in or makes any charge upon the land of a true owner, the invalidity of which would require proof."<sup>186</sup> When such a cloud exists, one option may be a suit to quiet title, also known as a suit to remove a cloud from the title.

The elements of a suit to quiet title are: (1) the plaintiff has an interest in the property; (2) the title to the property is affected by a claim of the defendant's; and (3) the defendant's claim, although facially valid, is actually invalid or unenforceable.<sup>187</sup> The burden of proof for each of these elements is on the plaintiff.<sup>188</sup>

To show that the plaintiff possesses an interest in the property at issue, the plaintiff must allege some right, title, or ownership in the plaintiff with sufficient certainty to enable the court to see that the plaintiff has a right of ownership that will warrant judicial interference. Generally, this element will be met by the plaintiff providing proof of record title to some interest in the property.

Fricks v. Hancock, 45 S.W.3d 322, 327 (Tex. App.—Corpus Christi 2001, no pet.); Katz v. Rodriguez, 563 S.W.2d 627, 629 (Tex. Civ. App.—Corpus Christi 1977, writ ref'd n.r.e).

See, e.g. Southwest Guaranty Trust Co. v. Hardy Rd. 13.4 Joint Venture, 981 S.W.2d 951, 957 (Tex. App.—Houston [1st Dist.] 1998, pet. denied).

In re Stroud Oil Properties, Inc., 110 S.W.3d 18, 26 (Tex. App.—Waco 2002, no pet.).

<sup>&</sup>lt;sup>187</sup> *The Howards v. Davis*, 6 Tex. 174, 185 (1851).

Associated Oil Co. v. Hart, 10 S.W.2d 791, 794 (Tex. Civ. App.—Eastland 1928, writ dism'd w.o.j.).

Wright v. Matthews, 26 S.W.3d 575, 578 (Tex. App.—Beaumont 2000, pet. denied).

But cf. Exploracion De La Estrella Soloataria Incorporacion v. Birdwell, 858 S.W.2d 549, 553 (Tex. App.— El Paso 1993, no writ) (plaintiff does not have to prove title to sovereignty).

The principal issue in a suit to quiet title is the existence of a cloud that equity will remove. The plaintiff must show that an adverse claim to the property exists which is affecting the title to the property. Finally, the plaintiff must show that the adverse claim is invalid or unenforceable, even though it appears valid on its face. To do this, the plaintiff should rely on the substantive law that governs the particular transaction alleged to have created the cloud to establish some fatal flaw or fallacy that will nullify the adverse claim. The principal removes the particular transaction alleged to have created the cloud to establish some fatal flaw or fallacy that will nullify the adverse claim.

If the plaintiff is successful, the court will issue a declaration that the cloud is invalid or unenforceable, which effectively removes the cloud entirely. 193

## VII. CONCLUSION

Acquire your title work as early as possible to create the opportunity to recognize the problems and fix them before it is too late. Lease everyone who arguably has any interest to lease. To lease everyone requires a ratification from nonparticipating owners, if the lease has a pooling clause. Do not be too quick to rely upon limitations title. It is a big assumption of risk and the degree of risk assumed can only be analyzed if you have a good familiarity with the requirements for adverse possession. Remember that severed minerals will never be adversely possessed unless there is actual production.

Analyze the surface use and access issues to connect together the rights you will need to access, drill, produce, and market at the proposed locations. Easements implied or granted in a lease are unreliable. Consider independent easement and surface use agreements.

There is a huge difference between having problems on the wellsite tract and having problems somewhere else on the lease or the unit. Do not assume big risks on the wellsite tract.

<sup>&</sup>lt;sup>191</sup> *In re Stroud*, 110 S.W.3d at 25-26; *Wright*, 26 S.W.3d at 578.

<sup>&</sup>lt;sup>192</sup> See, e.g., Amarillo Oil Co. v. Energy-Agri Products, Inc., 794 S.W.2d 20, 24-25 (Tex. 1990).

<sup>&</sup>lt;sup>193</sup> Ellis v. Waldrop, 656 S.W.2d 902, 905 (Tex. 1983).

Community leases, leases with entirety clauses, and leases with pooling clauses are generally better for the lessee, because the lessee may not figure out until the last minute which acreage and how much needs to be blocked up for the well. Whenever there are nonparticipating interests, this results in additional complications with ratifications, but it is simply the price of keeping some flexibility in the development of the Prospect. Avoid drilling on unleased cotenants. It is very troublesome and very expensive. Never trespass. The only thing good about good faith trespass is that it is not as bad as bad faith trespass.

Payments to nonexecutive owners should be made in accordance with any express provisions in the documents creating the nonexecutive interests. In the absence of express directions it is usually better to make payments directly to those nonexecutives entitled to receive payments. Ratifications by nonparticipating owners must be ratifications of each lease executed by the holders of the executive rights. Ratifications should be acquired before drilling commences to prevent the nonparticipating owners from selectively ratifying. It is usually better to ratify leases with pooling clauses rather than ratifying designations of unit. Designations of unit rarely have the detailed provisions found in a pooling clause and it is better for the owners to be under the same pooling provision.

The JOA may act as a risk-spreading agreement so that the parties can tolerate an unleased owner. If none of the practical suggestions or self-help planning solve the problem, then there are multiple possible legal remedies to resolve title issues. Although the MIPA is clumsy, there is a new-found opportunity to use it to force pool the recalcitrant small owner. Receivership is a very effective tool for resolving the unknown owner problem. Partition can be effective at resolving disputes among lessees under the same lease, but it is generally ineffective at resolving disputes among mineral owners once leasing has begun, unless the lessee chooses to

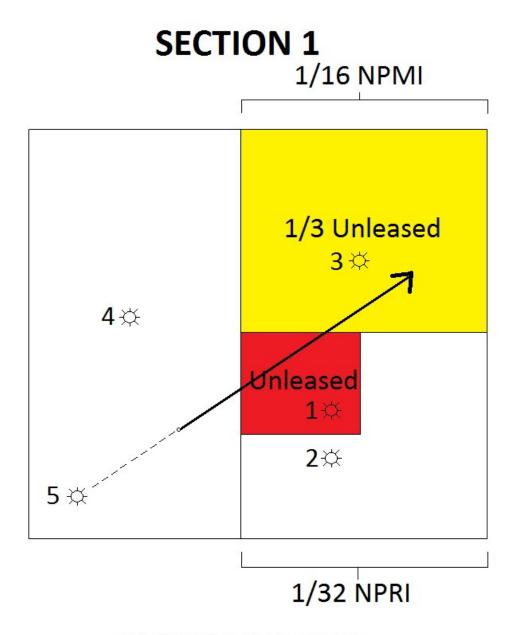
consent to the partition. Trespass to try title is the only way to ultimately resolve real title disputes. It is title litigation. Declaratory judgment actions can be used to resolve limited questions as to determining the construction and effect of particular documents. Boundary disputes can now be resolved in either TTT or a DEC action. Attorney's fees are not recoverable in TTT, but are recoverable in a DEC action. Quiet title is the procedure used when there is some instrument in the chain of title which is somehow raising a question or casting a cloud over the record title.

These are, in summary form, guideposts and suggestions for clearing title during the lease acquisition phase of Prospect development.

F:\DOCS\9999\510\OTHER\240050802.DOCX

## **EXHIBIT A**

# **SECTION 1 DIAGRAM (PROSPECT)**

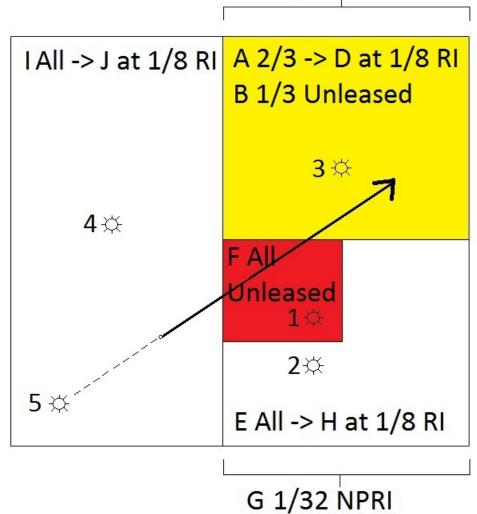


**POSSIBLE WELL SITES** 

## **EXHIBIT A-1**

## SECTION 1 DIAGRAM (PROSPECT WITH OWNERSHIP)

# SECTION 1 C 1/16 NPMI



Ownership of Section 1 with Wells

## **EXHIBIT B**

NOTICE OF CONFIDENTIALITY RIGHTS: IF YOU ARE A NATURAL PERSON, YOU MAY REMOVE OR STRIKE ANY OR ALL OF THE FOLLOWING INFORMATION FROM THIS INSTRUMENT BEFORE IT IS FILED FOR RECORD IN THE PUBLIC RECORDS: YOUR SOCIAL SECURITY NUMBER OR YOUR DRIVER'S LICENSE NUMBER.

# STIPULATION OF INTEREST AND CROSS-CONVEYANCE

This Stipulation of Interest and Cross-Conveyance ("Conveyance") is entered into with respect to the following described lands:

[leg	al description]
in County, Texas, hereinaf	ter referred to as the "Property."
of ownership as between,	ertainty has been asserted as to the rights and powers whose address
whose address is	,, and
whose address is	hereinafter collectively referred
to as the "Parties" and separately as a "Par	(hereinafter collectively referred ty") as to their interests in the Property; and
vest and to accurately reflect the true intere NOW, THEREFORE: The Parties hereto and each of then	re to clarify their title as to the Property and cause it to sts and intent of the Parties hereto;  n agree and stipulate that their interest in the Property
is and shall be owned as follows:	
PARTY	OWNERSHIP INTEREST
as [his/her] sole and separate property	
as [his/her] sole and separate property	
as their community property	

For good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, each of the Parties does hereby GRANT, BARGAIN, SELL, QUITCLAIM, and CONVEY one to the other and among themselves so much of their interest in the Property as is necessary to cause the rights, interests and title to the Property to vest as herein stipulated, to have and to hold forever.

This Conveyance shall not be binding upon any Party until executed by all of the Parties. This Conveyance shall be binding upon the Parties hereto, their respective heirs, devisees, personal representatives, successors, and assigns.

purposes as of the day of	acknowledgments shown below, but effective fo, 20	
	Name:	
	Name:	
	Name:	
	Traine.	
	Name:	
STATE OF		
COUNTY OF §		
This instrument was acknowledged	before me this day of, 20	_ by
	Notary Public, State of	

#### **EXHIBIT C**

NOTICE OF CONFIDENTIALITY RIGHTS: IF YOU ARE A NATURAL PERSON, YOU MAY REMOVE OR STRIKE ANY OR ALL OF THE FOLLOWING INFORMATION FROM THIS INSTRUMENT BEFORE IT IS FILED FOR RECORD IN THE PUBLIC RECORDS: YOUR SOCIAL SECURITY NUMBER OR YOUR DRIVER'S LICENSE NUMBER.

## **BOUNDARY AGREEMENT AND CROSS-CONVEYANCE**

	This Boundary Agreement and Cross-Conveyance ("Conveyance") is between
	whose address is,
and _	whose address is
(here	inafter collectively referred to as the "Parties" and separately as a "Party").
descr	WHEREAS, the Parties own or have equitable interests in adjoining tracts of land ribed as follows:
	Tract 1: [legal description]
	Tract 2: [legal description]
in	County, Texas, hereinafter referred to as the "Properties."
	WHEREAS, the exact location of their common boundary line as described in the records definite and unascertainable by a competent surveyor and cannot be made reasonably certain exceptable surveying efforts.

WHEREAS, the Parties have agreed upon the boundary line between their respective tracts of land to be fixed by a/an [existing fence, marked line, surveyor, etc.]

WHEREAS, the Parties have each in turn viewed this agreed boundary as marked on the ground and accept and desire the same to be the true and correct boundary between them and admit this to be the location as described in their respective deeds.

## NOW, THEREFORE:

For and in consideration of establishing the boundary line between their respective tracts of land, the Parties hereto do agree that the boundary line specifically described on Exhibit A attached hereto and incorporated herein is the true and correct boundary line between their respective tracts of land and the one described in their respective deeds.

For good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, each of the Parties does hereby GRANT, BARGAIN, SELL, QUITCLAIM, and CONVEY one to the other and among themselves so much of their interest in the Properties as is

necessary to cause the title to the Properties to vest as herein stipulated to the Properties to have and to hold forever.

This Conveyance shall not be binding upon any Party until executed by all of the Parties. This Conveyance shall be binding upon the Parties hereto, their respective heirs, devisees, personal representatives, successors, and assigns.

EXECUTED purposes as of the			owledgments shown below, but, 20	effective for all
			Name:	
			Name:	
		0		
STATE OF COUNTY OF		§ §		
This instrument wa		d before n	ne this day of	, 20 by
			Notary Public, State of	
STATE OF COUNTY OF		§ §		
This instrument wa	s acknowledged	d before n	ne this day of	, 20 by
			Notary Public, State of	

# **EXHIBIT "A"**

[Legal Description of Boundary]

#### **EXHIBIT D**

NOTICE OF CONFIDENTIALITY RIGHTS: IF YOU ARE A NATURAL PERSON, YOU MAY REMOVE OR STRIKE ANY OR ALL OF THE FOLLOWING INFORMATION FROM THIS INSTRUMENT BEFORE IT IS FILED FOR RECORD IN THE PUBLIC RECORDS: YOUR SOCIAL SECURITY NUMBER OR YOUR DRIVER'S LICENSE NUMBER.

[Cotenant]

#### LEASE RATIFICATION

REFERENCE is hereby made to the following:

recorded in Volume	at page	neral or oil and gas lease of the Records of as Lessor, to	_ County,	Texas
as Lessee, covering the				
County, Texas (" <b>Property</b>	'"); and			
		ted by instrument dated County, Texas ("U	, as reco	rded in

WHEREAS, the undersigned ("**Ratifying Party**" whether one or more than one) desires to ratify, approve, confirm, and adopt the Lease and the pooling of the Lease into the Unit;

NOW, THEREFORE, for Ten Dollars (\$10.00) and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Ratifying Party does hereby ratify, approve, confirm, and adopt the Lease, including all of its terms and conditions, as to all of the Ratifying Party's interest in the Property, and the Ratifying Party does hereby lease, demise and let the Property unto the current lessee of record exactly as the interest of such lessee(s) now appear, subject to and under all the terms and provisions of the Lease and the Unit, and, as to the Ratifying Party's interest in the Property, the Ratifying Party does hereby agree and declare that the Lease and the Unit are now in full force and effect exactly as if the Lease had been executed by the Ratifying Party.

This Lease Ratification shall not be deemed an offer to pool and shall not create any right, power, or privilege to pool any interest into the Unit, except by lease ratification and the pooling of leases as provided herein.

This Lease Ratification does not limit, hinder, or obstruct in any fashion or manner the lessee's power and right to pool or combine the acreage covered by the Lease or any portion, thereof, or lessee's right to reduce, enlarge, reform, modify, or dissolve any pooled or combined acreage or unit, as provided in the Lease.

This Lease Ratification shall be binding upon each person or party executing the Lease Ratification, regardless of whether it is prepared for execution by one or more than one person or party, and regardless of whether it is executed by less than all of the persons or parties for whom it has been prepared. Upon the execution and delivery of this Lease Ratification to any lessee having an interest in the Unit, or such lessee's agent or employee, such lessee is irrevocably authorized to file this Lease Ratification in the office of the County Clerk of the County in which the Property or any part of the Property is located. This Lease Ratification shall be binding upon the Ratifying Party and the Ratifying Party's heirs, successors, personal representatives, and assigns.

Executed as of purposes as of the		acknowledgments shows, 20	n below, but effect	ctive for all
RATIFYING PARTY:				
Name: Capacity: Address:		Name: Capacity: Address:		
STATE OF	§			
		acknowledged before		day of
		Notary Public	, State of	

#### **EXHIBIT E**

NOTICE OF CONFIDENTIALITY RIGHTS: IF YOU ARE A NATURAL PERSON, YOU MAY REMOVE OR STRIKE ANY OR ALL OF THE FOLLOWING INFORMATION FROM THIS INSTRUMENT BEFORE IT IS FILED FOR RECORD IN THE PUBLIC RECORDS: YOUR SOCIAL SECURITY NUMBER OR YOUR DRIVER'S LICENSE NUMBER.

[Nonparticipating Owner]

#### LEASE RATIFICATION

REFERENCE is hereby made to the following:

- The lease or leases described on Exhibit A attached hereto and incorporated herein ("Leases" whether one or more than one).
   The land described as County
- 2. The land described as \_\_\_\_\_\_, \_\_\_\_County, Texas ("**Property**").

WHEREAS, the undersigned ("**Ratifying Party**" whether one or more than one) desires to ratify, approve, confirm, and adopt the Leases, insofar as the Leases cover and apply to the interests of the Ratifying Party in the Property;

NOW, THEREFORE, for Ten Dollars (\$10.00) and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Ratifying Party does hereby ratify, approve, confirm, and adopt the Leases, including, without limitation, the right to pool, communitize, or unitize the Ratifying Party's interest on the same terms and conditions applicable to the lessor's interest, insofar as the Leases cover the interest of the Ratifying Party in the Property, and the Ratifying Party does hereby lease, demise, and let the interests of the Ratifying Party subject to the Leases unto the current lessee of record exactly as the interest of such lessee(s) now appear, subject to and under all the terms and provisions of such Leases, and, as to the interests of the Ratifying Party in the Property subject to such Leases, the Ratifying Party does hereby agree and declare that such Leases are now in full force and effect exactly as if the Leases had been executed by the Ratifying Party.

If the Ratifying Party owns any additional interest in the Property which is now or later subject to a lease or leases not included in the Leases ("Additional Leases") whether one or more than one), then this Lease Ratification shall extend to and include the interest of the Ratifying Party subject to the Additional Leases, without further action by the Ratifying Party.

This Lease Ratification shall not be deemed an offer to pool and shall not create any right, power, or privilege to pool any interest into any pooled unit, except by lease ratification and the pooling, communitization, or unitization of leases as provided in the Leases and Additional Leases.

This Lease Ratification does not limit, hinder, or obstruct in any fashion or manner the lessee's power and right to pool or combine the acreage covered by the Leases, the Additional Leases, or any portion, thereof, or lessee's right to reduce, enlarge, reform, modify, or dissolve any pooled or combined acreage or unit, as provided in the Leases and the Additional Leases.

This Lease Ratification shall be binding upon each person or party executing the Lease Ratification, regardless of whether it is prepared for execution by one or more than one person or party, and regardless of whether it is executed by less than all of the persons or parties for whom it has been prepared. Upon the execution and delivery of this Lease Ratification to any lessee having an interest in the Property, or such lessee's agent or employee, such lessee is irrevocably authorized to file this Lease Ratification in the Office of the County Clerk of the County in which the Property or any part of the Property is located. This Lease Ratification shall be binding upon the Ratifying Party and the Ratifying Party's heirs, successors, personal representatives, and assigns.

Executed as purposes as of the		he acknowledgmer		w, but effecti	ve for all
RATIFYING PART	Y:				
Name: Capacity: Address:		Name Capa Addr	e: city:		
STATE OF	§				
COUNTY OF					
The foregoin		as acknowledged		n the	_ day of
		Nota	ry Public, State	of	

# **EXHIBIT "A"**

# **LEASES**

## **EXHIBIT F**

NOTICE OF CONFIDENTIALITY RIGHTS: IF YOU ARE A NATURAL PERSON, YOU MAY REMOVE OR STRIKE ANY OR ALL OF THE FOLLOWING INFORMATION FROM THIS INSTRUMENT BEFORE IT IS FILED FOR RECORD IN THE PUBLIC RECORDS: YOUR SOCIAL SECURITY NUMBER OR YOUR DRIVER'S LICENSE NUMBER.

[Gas Unit]

DESIGNATION OF POOLED UNIT ( GAS UNIT)
This Designation of Pooled Unit ("Designation of Unit") is by and between, a company, whose address i
, and, and, company, whose address is
(collectively, "Lessees," whether one or more than one).
REFERENCE is here made to the oil, gas, and mineral leases or oil and gas lease identified on Exhibit A attached hereto and incorporated herein, and as such leases may have been ratified, amended, corrected, or renewed and extended ("Leases").  Lessees collectively own all the interests of the lessees under the Leases. By the authority conferred by the terms of the Leases, Lessees pool, consolidate, combine, and unitize the Leases, insofar as the Leases cover and include all or any part of the Unit Acreage, for the purpose of forming or creating a unit or pooled area to explore, drill, develop, and produce fo gas and gas rights from the Unit Acreage. "Unit Acreage" as used herein includes the following described lands:
,County, Texas, containing acres, more or less.
The Unit formed by this Designation of Unit shall hereafter be known and referred to as the " Gas Unit," and is referred to herein as the "Unit."
The Unit covers all production that is produced from any gas well located on the Unit Acreage. A "gas well" as used herein means a well classified as a gas well by the rules and regulations of the Railroad Commission of Texas. The term "gas and gas rights" refers to all production and products from any gas well (including, without limitation, condensate, distillate

and any liquid hydrocarbons which are produced with or as a part of the gas) that is produced from the Unit Acreage. The Unit shall not apply to or cover production from an oil well as

classified by the rules and regulations of the Railroad Commission of Texas.

The production of gas and gas rights from a gas well on any part of the Unit Acreage shall constitute production of such products from all of the Leases contained in the Unit. Drilling or reworking operations or other operations conducted on the lands or Leases within the Unit for the production of gas and gas rights covered by this Unit shall constitute such operations for the production of gas and gas rights on all lands and Leases included within the Unit.

All gas and gas rights produced from any gas well on the Unit Acreage shall be allocated proportionally among all of the tracts within the Unit in the proportion that the number of surface acres in each of the tracts which are located in the Unit bears to the total number of surface acres in the Unit Acreage, and the share of production to which each interest owner shall be entitled shall be computed on the basis of such owners' respective interest in each tract within the Unit.

It is the intention of the undersigned to include, and they do hereby include in the Unit, all leases and other mineral or royalty interests which the undersigned now own within the Unit and any additional lease or leases or mineral or royalty interests which may be hereinafter acquired by the undersigned, covering all or any part of the Unit Acreage during the time the Unit remains effective. It is the intention of the undersigned to include, and they do hereby include in the Unit, all unpooled interests of persons or parties within the Unit Acreage, who by ratification of one or more of the Leases have the right and by ratification of the Lease(s) elect to be subject to and pooled and included in the Unit on the terms and conditions as provided in such Lease(s). Any person or party having such right and who ratifies any one or more of the Leases and accepts benefits hereunder shall be deemed to have ratified and confirmed each and every Lease(s) binding upon such person or party's interest in the Unit Acreage, regardless of whether all of such Leases are described or described correctly in the ratification. Any person or party who, as an unleased cotenant, is subject to no Lease, but has the right and by ratification of a Lease elects to be leased and to be subject to and pooled and included in the Unit on the same terms and conditions as provided in such Lease, must specify the Lease(s) ratified and the interest subjected to the Lease(s). The interest of any person or party having the right to be included in and subjected to the Unit by ratification shall be included in and subject to the Unit from and after a binding and effective ratification is filed for record in the County where the Unit Acreage is located. As to any well then producing, there shall be no right to share in such production until the first day of the first month following the filing date or the date actual notice is received by the undersigned, whichever is later.

Lessees and their heirs, successors, personal representatives, and assigns reserve the right to amend this Designation of Unit from time to time, and at any time, in order to correct any error herein or to include in this Unit any unleased tract or tracts of land or interest or interests therein located within the boundaries thereof by appropriate amendment or instruments correcting or committing any such outstanding interest to this Unit, and for all other purposes permitted by the Leases. This Designation of Unit shall not be deemed an offer to pool or to create or to extend to any other person or party the right to participate in or join in the Unit, except insofar as such right may already exist and can be exercised by the ratification of one or more of the Leases. No person or party owning a leased interest, other than the undersigned, may join in or ratify this Unit, except with the express written consent of the undersigned.

This Designation of Unit may be executed as one document signed by all Lessees, or in counterparts, or by ratification instrument, with the same effect as if all Lessees executed the same instrument. The failure of any one or more persons owning an interest in the gas and gas rights in and under the Unit Acreage to execute this Designation of Unit or a counterpart or ratification thereof shall not in any manner affect the validity of this Designation of Unit as to the Lessees who do execute this Designation of Unit.

The Unit hereby created shall become effective when a copy of this Designation of Unit is first filed for record in the office of the County Clerk of the County in which the Unit Acreage or any part of the Unit Acreage is located, and, unless sooner terminated or amended by the undersigned, shall remain in force as long as any of the Leases included in the Unit are maintained in force by production, by payment or tender of shut-in gas well royalties, or by other means, in accordance with the terms of the Leases.

This Designation of Unit shall be binding upon the undersigned and their heirs, successors, personal representatives, and assigns.

Executed as of the date of the acknowledgments shown below.

By:		By:	
•	Name:	•	Name:
	Title:		Title:

# **ACKNOWLEDGMENTS**

STATE OF	_				
COUNTY OF	_				
The foregoing in , 20,				ne on the	
behalf of said company.	- J				,
			Notary Public,	State of	
STATE OF	§				
COUNTY OF	_ §				
The foregoing in, 20,				ne on the for	
behalf of said company.	J	,			,
			Notary Public,	State of	

# **EXHIBIT A**

Attached to and made	a part of that certain Designation of Unit	dated	, 20
by and between	and	·	
	<u>LEASES</u>		