Chapter 2

The

Granting Portion

of the

Oil and Gas Lease

THE GRANTING PORTION OF THE LEASE

The first portion of the oil and gas lease would be considered the granting portion of the lease. Several important items encompass this area including the:

- The date of the lease
- The parties entering into the lease contract
- The consideration
- The granting clause
- The legal description
- The Mother Hubbard clause or cover all clause

THE DATE OF THE LEASE

The lease date becomes a very important part of the oil and gas agreement. It not only identifies the exact effective date but also becomes the focal point around which other lease obligations must take place. It becomes the birthday of the lease and acts in a similar fashion as a person's birthday. On the anniversary date of that birthday, certain activities tied directly to the person might take place. In a similar way on or before the anniversary date of the oil and gas lease certain activities might be required to take place.

The Date and the Parties Entering the Lease Agreement

OIL, GAS AND MINERAL LEASE

AGREEMENT, Made and entered into this 10th day of July 2007, by and between Jack Johnson and Jessica Johnson, husband and wife , hereinafter called "Lessor" and whose address is 250 South Medlock Place, Casper, Wyoming and Your Oil and Gas Company , hereinafter called "Lessee" and whose address is 125 NE Saint Street, Suite 500 Houston, TX .

From time to time a lease will be signed and notarized but, through negligence, will be left undated. Although this date is very important the fact that the date is missing from the top of the lease does not render the lease invalid. In cases like this the valid date of the lease becomes the date of execution found at the bottom of the lease.

PARTIES ENTERING THE LEASE AGREEMENT

A lease involves two (2) parties, a "Lessor" and a "Lessee". The "lessor" is the owner of all or part of the minerals located in the described lands of the lease. The "Lessee" is the party wishing to lease the minerals and is responsible for all terms and conditions of the lease.

Unlike the date portion of the lease, the exact and correct names of the parties entering the lease agreement are vitally important. Some states, such as Louisiana, even require indication of the lessor's marital status.

It is not uncommon to have a lessor whose legal name is different than the common name used by the lessor. For instance, *Nicholas Timothy Wilkins* might use any of the following names:

Nicholas T. Wilkins, a/k/a
N.T. Wilkins, a/k/a
Timothy Wilkins, a/k/a
Tim Wilkins, a/k/a
Nick Wilkins

- Nicholas T. Wilkins
- N.T. Wilkins
- Timothy Wilkins
- Tim Wilkins
- Nick Wilkins

In a case like this, which is the proper name to use on the oil and gas lease? To answer this question one must simply go to the vesting deed whereby the person acquired title. If the conveyance vested title into *Nicholas Wilkins,* that is how his name should appear on the oil and gas lease. If the conveyance vested title into *Tim Wilkins,* that is how his name should appear on the lease.

On the other hand, it is possible that different conveying instruments show more than one name for the same person. In a case like this, the lease should contain both names such as:

Nicholas T. Wilkins, also known as Timothy Wilkins.
The lease should be signed as Nicholas T. Wilkins.

If two conveying instruments showed title vesting in both Nicholas T. Wilkins and N.T. Wilkins the lease should be styled:

Nicholas T. Wilkins, also known as N.T, Wilkins.
The lease should be signed as Nicholas T. Wilkins.

If a conveying instrument showed title vesting into a *Nancy Johnson,* but it was determined that at the time of signing the lease she was married with a last name of Jenkins, the lease should be styled:

Nancy Jenkins, a married woman, formerly known as Nancy Johnson.

If two conveying instruments showed title vesting into a *Nancy Johnson* and also into a *Nancy Isaac's* but it was determined that at the time of signing the lease she was one and the same person and was now re-married with the name Nancy Jenkins, the lease should be styled:

Nancy Jenkins, a married woman, formerly known as Nancy Isaacs, formerly known as Nancy Johnson.

It is also recommended that if a person uses a different name than their given name, both names should appear on the lease.

ISSUES CONCERNING MARRIED COUPLES

Statues vary from state to state. Some states have community property laws, other states have tenancy by the entirety laws, and other states recognize homestead exemptions. Each of these laws affects how a married person can sell, convey or lease property.

COMMUNITY PROPERTY

Most states that have adopted community property rules were first colonized by Spain or France. In the United States, there are nine community property states:

Arizona	California	Idaho
Louisiana	Nevada	New Mexico
Texas	Washington	
Wisconsin		

(Wisconsin is not really a true community property state; however, its laws bear a strong resemblance to the laws of the other community property states.)

Property in Alaska can also be considered community property if a married couple signs an agreement to that effect.

In community property states, property accumulated during the course of the marriage, any earnings, profits, income and or assets would be owned jointly by both spouses. This *joint ownership* or community property should be automatically presumed unless there is some specific evidence that would indicate it to be separate property. Although community property laws vary from state to state, generally, community property cannot be conveyed separately. In other words, both parties would need to sign an oil and gas lease.

TENANCY BY THE ENTIRETY

Tenancy by the entirety is a type of ownership between husband and wife whereby the property is co-owned by the two while they are married. When one or the other party dies, the property will automatically pass to the surviving spouse. While they are living the property cannot be conveyed separately by only one of the parties.

Tenancy by the entirety is based on an old common law view that saw both husband and wife as one person for purposes of owning property. As such, while they are still living, neither can separately sell, lease, mortgage or place a lien against the property. In the United States there are 17 states and the District of Columbia that have tenancy by the entirety. They are:

Common Law saw both husband and wife as one person for the purposes of owning property

Alaska	Arkansas	Delaware	
Florida	Hawaii	Maryland	
Missouri	Oklahoma	Vermont	
Mississippi	Virginia	District of Columbia	
New Jersey	Wyoming	Massachusetts	Pennsylvania
Rhode Island	Tennessee		

States that allow tenancy by the entirety for real estate only:

Illinois	Indiana	Kentucky	Michigan
New York	North Carolina	Ohio	Oregon

If your company wanted to lease a 160-acre tract of land in Wyoming from Ronald and Catherine Perkins, husband and wife and co-owners of the land, but only received Ronald's signature because Catherine was out of town, would you have a valid lease? If Ronald died prior to Catherine's return, what portion, if any, of the property would your company own under lease?

Unfortunately, because Wyoming is a tenancy by entirety state your company's lease would be no good. At the time of Ronald's death title would automatically vest into Catherine who would own 100% of the property. Since she didn't sign the lease and since the lease signed by Ronald was not valid without Catherine's signature, your company would own no leased lands.

HOMESTEAD EXEMPTION LAWS

"The homestead exemption amounts essentially to a right which married couples may establish in real estate which thereafter may not be effectively conveyed or dealt with by one spouse without the consent of the other."[1] In other words, in any state that has homestead exemption laws, both husband and wife should appear on the oil and gas lease.

TENANTS IN COMMON

Tenancy in common is the most common type of joint ownership in real property in the United States. Unless stated otherwise, a *tenancy in common* would occur when two or more parties receive title to a piece of property.

JOINT TENANTS WITH RIGHTS OF SURVIVORSHIP

Taking title to a piece of property as *joint tenants with the rights of survivorship* is very different from taking title as *tenants in common or tenants by the entirety*.

Most states would recognize a joint tenancy with the right of survivorship if the deed simply read, *"To Norris Beal and Madge Beal, husband and wife, as joint tenants."* However, Texas is an exception to the rule and requires the additional language, *"with right of survivorship".*

The Four Unities

In order for a JTWROS to be produced, those wishing to be the joint tenants must share in what is known as the *"four unities."*

1. Time - the property must be acquired at the same time.
2. Title – all joint tenants must have the same title to the property
3. Interest - all tenants must possess the exact same interest
4. Possession – all must have 100% rights to the property.

A joint tenancy would be invalid if any one of these four unities were missing. In cases like this, the ownership becomes a tenancy in common.

Dissolving a joint tenancy with right of survivorship

Once a joint tenancy with the right of survivorship is created, in most states, one of the joint tenants interest can be dissolved as to its right of survivorship status if the joint tenant conveys his or her interest to another party.

In English common law, one joint tenant could not break the joint tenancy without a third party being involved. This third party was referred to as a *straw man*. A straw man was a party that purchased the interest from the co-tenant at a token price. The straw man would then sell the interest back to the same co-tenant at the same price, thus creating a tenant in common ownership with this interest.

Most states allow the joint tenancy to be broken without the use of a straw man and without the knowledge or consent of the other joint tenants.

California and Texas hold that a joint tenancy cannot be broken unless consent is obtained from all the other joint tenants or there is a partition of the property from the courts.

New York holds that a joint tenant can sell his interest to a third party without the consent or knowledge of the other joint tenants; however, the power to extinguish the right of survivorship of the joint tenant does not take effect until the deed is recorded. Why?

Problems with this approach:

Three brothers named Justin, Kevin, and Larry own a track of land as joint tenants with the right of survivor. Larry does not want his interest in the property to pass to his two brothers when he dies; therefore he breaks his joint tenancy by executing a conveyance to a straw man who immediately conveys the property back to Larry as a tenant in common.

Larry does not tell his other brothers and does not have the document recorded. Instead of Larry dying, his brother, Justin dies. Larry does not mention the previous conveyance to his other brother. Without the knowledge of this, Justin's interest automatically passes in equal portions to the two surviving brothers – Kevin and Larry.

Determining ownership

In a situation where there are there or more owners, and one of the owners breaks the joint tenancy, the other joint tenant's rights are still in tact. The interest that was broken becomes a tenancy in common interest.

Rules Regarding:

Tenants in Common	Tenants by Entirety	Joint Tenants
1. Two or more parties can take title as TIC	**1. Only a husband and wfie can take tiltle as TBE**	**1. Two or more parties can take title as JTWROS**
2. Each TIC own a separate undivided interest in the property. The interest can be either equal or unequal.	**2. The two own the property as if they were one person**	**2. Each JTWROS owns an *equal* undivided interest in the property. JT's cannot own unequal interests.**
3. Upon death, the deceased person's ownership would be distributed as specified in the Last Will and Testament or according the laws of descent and distribution.	**3. When one or the other party dies, the property will automatically pass to the surviving spouse.**	**3. Regardless of any provisions set forth in a will, the heirs are not entitled to any portion of the joint tenant estate.**
4. Each TIC has the right to possession of the whole property; however, individually, they have the right to deal with their undivided interest independently from the spouse or other TIC.	**4. While they are living, the property cannot be conveyed separately by only one of the parties.**	**4. Each JTWROS has the right of possession of the whole property; however, individually, they have the right to deal with their interest independently from the spouse or other JT.**

THE STYLING FOR OTHER ENTITIES

The following are examples of how other entities should appear on the lease:

1. In the case of an estate that has not yet been resolved:

   Nathan Johns, Personal Representative of the estate of Norris Johns, deceased.

2. When there is a guardian or a conservator:

   Nathan Johns, Guardian of the estate of Norris Johns, a minor

3. When there is a trust:

   Nathan Johns, as Trustee under the Nathan Johns Revocable Trust, dated March 3, 2005.

4. When there is a corporation:

   Johns Family, Inc., a Colorado Corporation

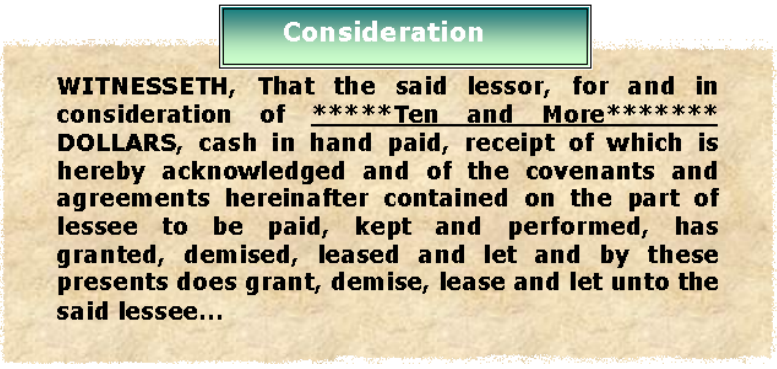
5. When there is a general partnership:

   Nathan Johns, Partner and Norris Johns, Partner, for Johns Family Farms, a General Partnership

6. When there is a Life Tenant and Remaindermen

   When a life estate exists with both a life tenant and remainderman, both are necessary to execute a lease.

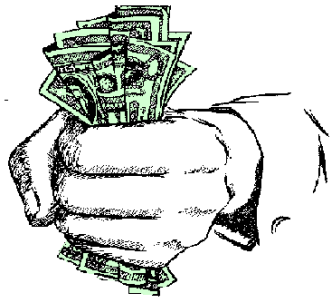
CONSIDERATION



In order for a contract to become a valid contract, consideration must take place; therefore, consideration is a vital element in the law of contracts and becomes a vital part of the oil and gas lease contract. Without consideration the lease would become unenforceable.[2]

Consideration must have value, such as monetary value, and is offered to the lessor in exchange for the granting of the leased premises to the lessee. Just as the money given to the lessor has value, so the granting of the lease has value to the lessee.

Generally, oil companies wish to hide the total amount of consideration offered to the lessor. Therefore, the phrase, *"Ten and more"* Dollars appears on the lease. What this means is that the lessee has paid the lessor at least ten dollars and probably much more.



The amount of money paid to the lessor in exchange for the lease is called a *signing bonus* and is based on two factors. First, it involves the number of net mineral acres the lessor owns on the lease. Secondly, it involves the negotiated dollar amount the lessee is willing to pay per acre. If the lessor owned 78 net mineral acres and the negotiated dollar amount per acre was $75, the bonus consideration would be 78 X $75 = $5,580.00.

THE GRANTING CLAUSE

The first paragraph of most oil and gas leases contains the granting clause. It is here where the lessor sets out and defines what exactly is being granted to the lessee in the oil and gas lease. Within the granting clause, one would find the legal description clause and the Mother Hubbard or cover all clause.

The purpose of the granting clause is to define certain items necessary for both the lessor and lessee. The five aspects of the granting clause are as follows:

Granting Clause

WITNESSETH, That the said lessor, for and in consideration of _*******Ten and More*******_ DOLLARS, cash in hand paid, receipt of which is hereby acknowledged and of the covenants and agreements hereinafter contained on the part of lessee to be paid, kept and performed, has granted, demised, leased and let and by these presents does grant, demise, lease and let unto the said lessee, for the sole and only purpose of exploring by geophysical and other methods, mining and operating for oil (including but not limited to distillate and condensate), gas (including casinghead gas and all other constituents), and all other hydrocarbons, and for laying pipe lines, and building tanks, power stations and structures thereon, to produce, save and take care of said products, all that certain tract of land, together with any reversionary rights therein, situated in the County of _Dewey_, State of _Montana_, described as follows, to-wit:

Township 16 South, Range 16 West
Section 14: SW/4NW/4, W/2SW/4

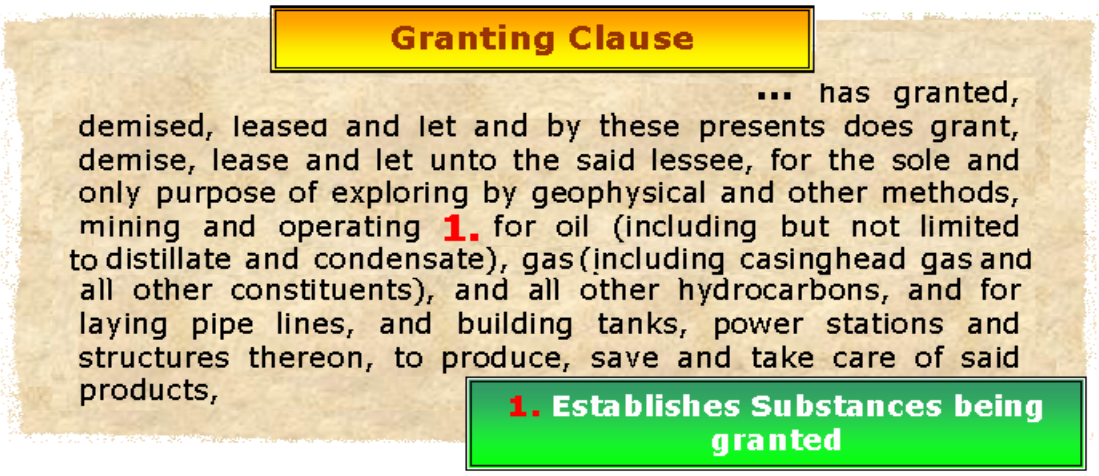
Legal Description Clause

of Section _14_, Township _16 South_, Range _16 West_, and containing _120.00_ acres, more or less,

together with all strips, parcels of land, accretion and riparian rights adjoining or contiguous to the above described tract of land, attaching to and forming a part of said land whether properly or specifically described or not and owned or claimed by Lessor.

Mother Hubbard Clause

1. THE GRANTING CLAUSE WILL ESTABLISH THE SUBSTANCES THAT ARE BEING GRANTED.



In this lease, the language specifies *"oil (including but not limited to distillate and condensate), gas (including casinghead gas and all other constituents), and all other hydrocarbons".* Not all leases have this particular granting language. Many leases simply state, *"all oil and gas"* or *"all oil, gas and other minerals."* That type of granting language is very *general* in nature. Often courts have been asked to step in and interpret what constitutes *"other minerals".* To add to the confusion, states differ on their interpretation of what constitutes *"oil, gas or other minerals"*.

Specific words followed by general words are limited to the same kind as the specific words. For instance, if the granting language stated, "Oil, gas and other minerals," the "other minerals" would mean other minerals like oil and gas.

If the granting language stated, "Coal and other minerals," the other minerals would mean other minerals like coal.

If the lease uses this general language but later describes specific substances, the general statement becomes limited in nature to the specific substances described.

Example:

The Granting Clause of an oil and gas lease granted "*oil, gas and kindred minerals."* The lease then *specified* the substances as to *"all of the oil, gas, casing-head gas and other liquid semi-solid and solid minerals."*

When drilling a well, the oil company discovered gypsum and asked a Kansas court to rule if gypsum was granted under the *"kindred mineral"* language of the lease. In Keller v. Ely, the court found that "the *general terms* contained in the reservation must be deemed to embrace and include only those things similar in nature to those previously *specifically* enumerated."[3] Since the specific minerals mentioned did not include gypsum, the oil company could not consider gypsum under the "kindred mineral" language.

In most cases, defining *oil* or *gas* is not an issue. Oil companies take leases because they are strictly interested in finding and producing oil and gas. And in most cases, the substances found are oil and gas. If a company was interested in coal or silver, they would most likely use something other than an oil and gas lease. However, there are times that a company, in the process of drilling an oil or gas well, has discovered some other type of mineral. In those cases, company employees find themselves asking the question, "Just what substances are covered under our lease?"

WHAT SUBSTANCES ARE COVERED?

To answer that question one must read the entire lease. Let's say the granting language was the general type and simply read, *"oil and gas".* The granting language did not even mention *"other minerals."* Would this lease cover coal? The simple answer would be a resounding, "No". The more complex answer is, "What does the entire lease say?" As we have seen previously, the simplified granting language may be more specifically defined in other parts of the lease. This includes the royalty clause."[4]

The royalty clause may make specific reference to the types of minerals being granted. "In a number of leases, there are *three* provisions for the payment of royalties on production: one covers royalties on oil, a second covers royalties on gas, and the third covers royalties on *other substances*, frequently adding specific provisions concerning certain substances such as coal, potash or sulfur."[5]

If such a lease had the provision to pay the lessor a royalty on coal, the lease would most likely cover coal, even if the granting language was limited to "oil and gas".

Individual state statutes will also determine what substances might be covered. The state of West Virginia in Energy Development Corp. v. Moss, No 31,238,2993 WL 22762066 (W.Wa. Nov. 20, 2003) ruled that

the oil and gas lease does not cover coalbed methane. The particular lease language used in this case reads:

"all of the oil and gas and all the constituents of either in and under the land hereinafter described in all possible productive formations therein…."

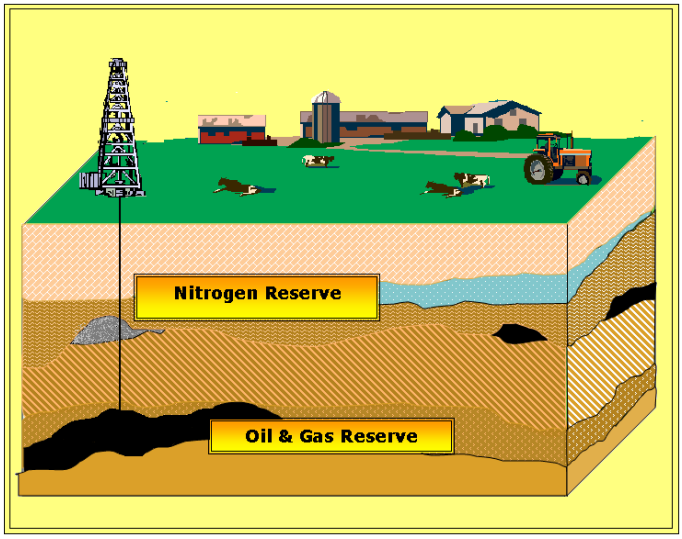
In several of the western states such language would allow the lessee to develop the coalbed methane but the West Virginia Court ruled that an *oil and gas* lease does not give the lessee the right to drill into the lessor's coal seam in order to produce coalbed methane.

WHAT SUBSTANCES CONSTITUTE GAS?

The question regarding what constitutes gas becomes an even bigger issue. Gas, as we know it, is a *hydrocarbon*. Read the granting language again in our lease. The language specifically states, "*gas (including casinghead gas and all other constituents), and all other hydrocarbons".*

Certain gases, such as nitrogen, carbon dioxide and helium, are not hydrocarbon gases. Would they be covered under our lease?

In Northern Natural Gas Company v. Grounds, the court had to determine whether a lease, whose granting language simply covered "oil and gas", included helium, which was being extracted from the gas stream. The Court found, "absent specific reservations, the grant of gas by the leases covered all components of the gas, including helium."[6] It appears that the court's findings were not based on a strict interpretation of the definition of hydrocarbons rather on the fact that separating the helium from the gas stream would have been impossible.[7]



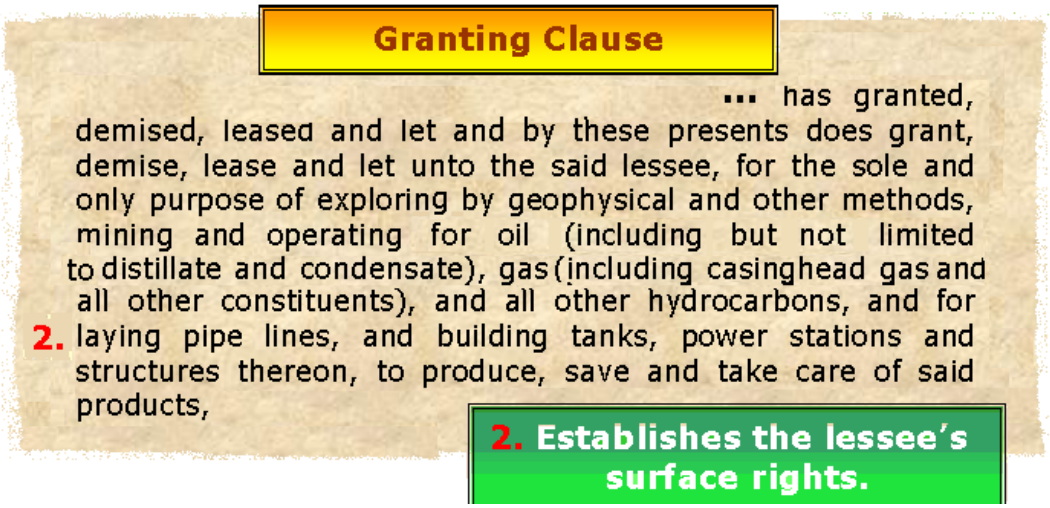
Conversely, if your company was drilling a well on the same lease and discovered a very valuable nitrogen reserve located several hundred feet above your target zone, could

your company claim the nitrogen under the "oil and gas" granting language?

In all likelihood, since the nitrogen is not a part of the oil or gas stream and since the nitrogen is not a hydrocarbon it would not be covered under the granting clause.

Federal oil and gas leases become even more ridged. They are specific in nature to only oil and gas minerals and specifically exclude helium.[8]

2. THE GRANTING CLAUSE WILL ESTABLISH THE LESSEE'S SURFACE RIGHTS.



In this lease the surface rights are limited to laying pipe line, building tanks, power stations and structures thereon in order to produce, save and take care of said products. Other lease language might include:

- Facilities for storing oil
- Building power stations
- Constructing telephone lines
- Housing for caring for employees

In many cases, a lessor might own the mineral rights in and under a surface tract of land but they do not own any of the surface lands. For example, let's say that your company has taken a lease from Douglas McDougal who owns 100% of the minerals; however, he does not own any of the surface land. That land is owned by Charles Nelson. In cases like this the question must be asked, can Douglas McDougal grant surface

rights (as listed above) to your company? Wouldn't Charles Nelson be the only party able to grant such surface rights?

In order to understand the answer to this question, one must understand the following principal:

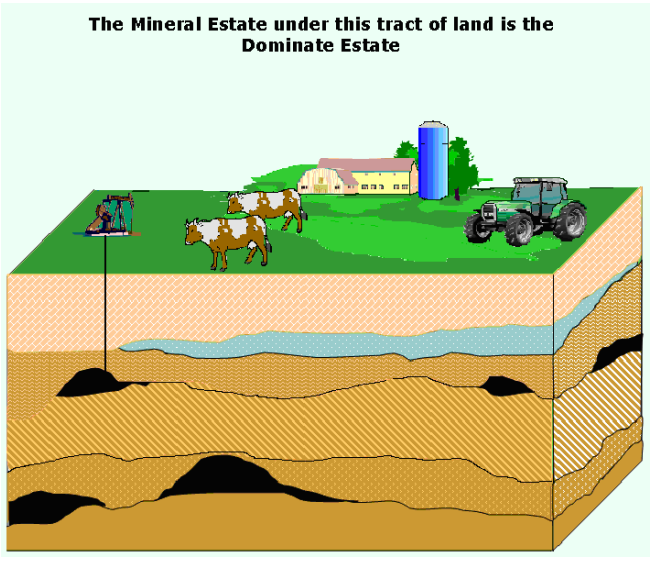
THE MINERAL ESTATE IS THE DOMINATE ESTATE

When a mineral estate is severed from the surface estate, the mineral estate is regarded as the *dominate* estate.[9] This means that Douglas McDougal, the *mineral* owner, has the right to use so much of the surface as is *reasonably necessary* for the use and development of the minerals and he has the right to grant these rights (such as laying pipe line, building tanks, power stations and structures) to your company.

This might appear unfair or unjust because, after all, Charles Nelson, the surface owner, makes his living by growing crops on the surface. In a case like this, are there limitations and why would the *mineral estate* be the *dominate estate*?

The reason is simple: If the *surface estate* were the *dominate estate* and the surface owner owned no minerals, then that owner could prevent the minerals from ever being developed.

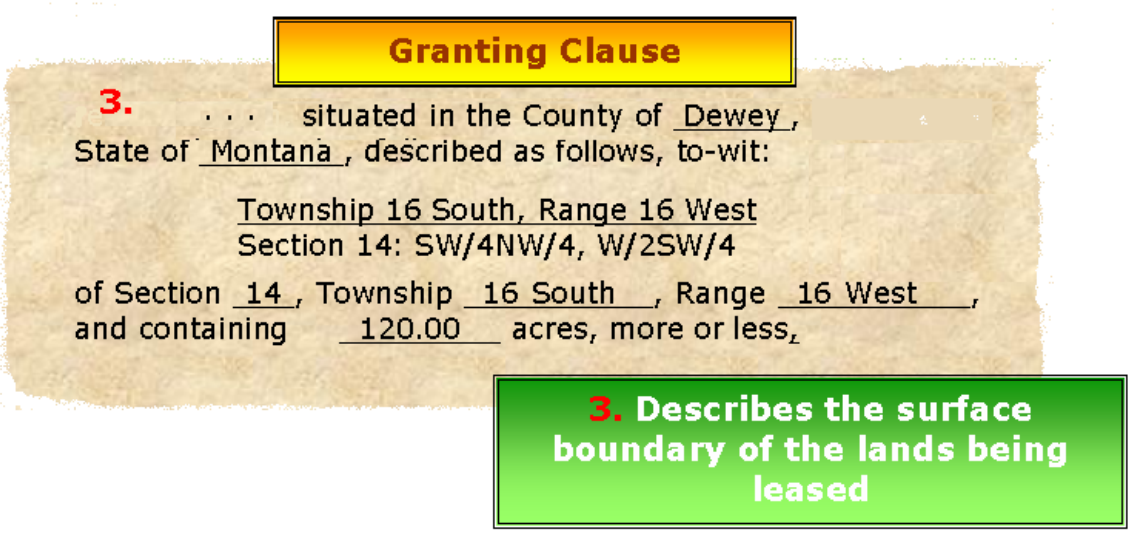
> "If the lease merely grants the right to develop oil and gas, without addressing surface access rights to conduct operations, lessee has an implied right to make reasonable use of the surface to facilitate operations."[10]



Three limitations on mineral estate dominance

- The surface area is limited to what is reasonably necessary for the development of minerals.
- Subsurface operations must occur in a genuine and faithful manner.
- Subsurface operations must occur with due regard for the surface owner and must accommodate the surface owner if reasonable.[11]

3. THE GRANTING CLAUSE WILL DESCRIBE THE SURFACE BOUNDARY OF THE LANDS BEING LEASED.



In our example, the lands are being described by what is known as "The Rectangular Survey System". This survey system was developed by our forefathers in order to describe the western lands granted to early settlers and will be more fully explained in the following lesson.

Not all lands are described in such a manner. Several parts of our country use metes and bounds legal descriptions. In Texas, legal descriptions might be described by the use of surveys, abstracts or Spanish land measurements. These will also be more fully explained in the following lesson.

Having knowledge and understanding of each and how the lands are described becomes vital for land and land administration personnel.

4. THE GRANTING CLAUSE WILL CONTAIN MOTHER HUBBARD OR COVER-ALL LANGUAGE.

Picture the dresses worn by the ladies in the "Little House on the Prairie" television series. They covered everything from the neck of the woman to the base of her ankles – thus the term *Mother Hubbard*. Her dress covered everything.

For oil and gas purposes, it was often necessary to rely on such a concept when property was being described. Early survey methods were often inaccurate. Where metes and bounds descriptions were used, precise ownership was often confusing. Where tracts of land bordering rivers or streams were being leased, the riverbed could change. Oil companies needed a lease that would cover everything including the lands described on the lease and any other acreage that was identified later through resurvey, or the small bits and pieces of land contiguous and adjacent to the land described in the lease.

Directly connected to the legal description is language that can be referred to as the "Mother Hubbard Clause" or the "Cover all Clause" or the "Entirety Clause." This clause will provide that the lease will cover all land contiguous and adjacent to the tract described in the lease.

Granting Clause

4. together with all strips, parcels of land, accretion and riparian rights adjoining or contiguous to the above described tract of land, attaching to and forming a part of said land whether properly or specifically described or not and owned or claimed by Lessor.

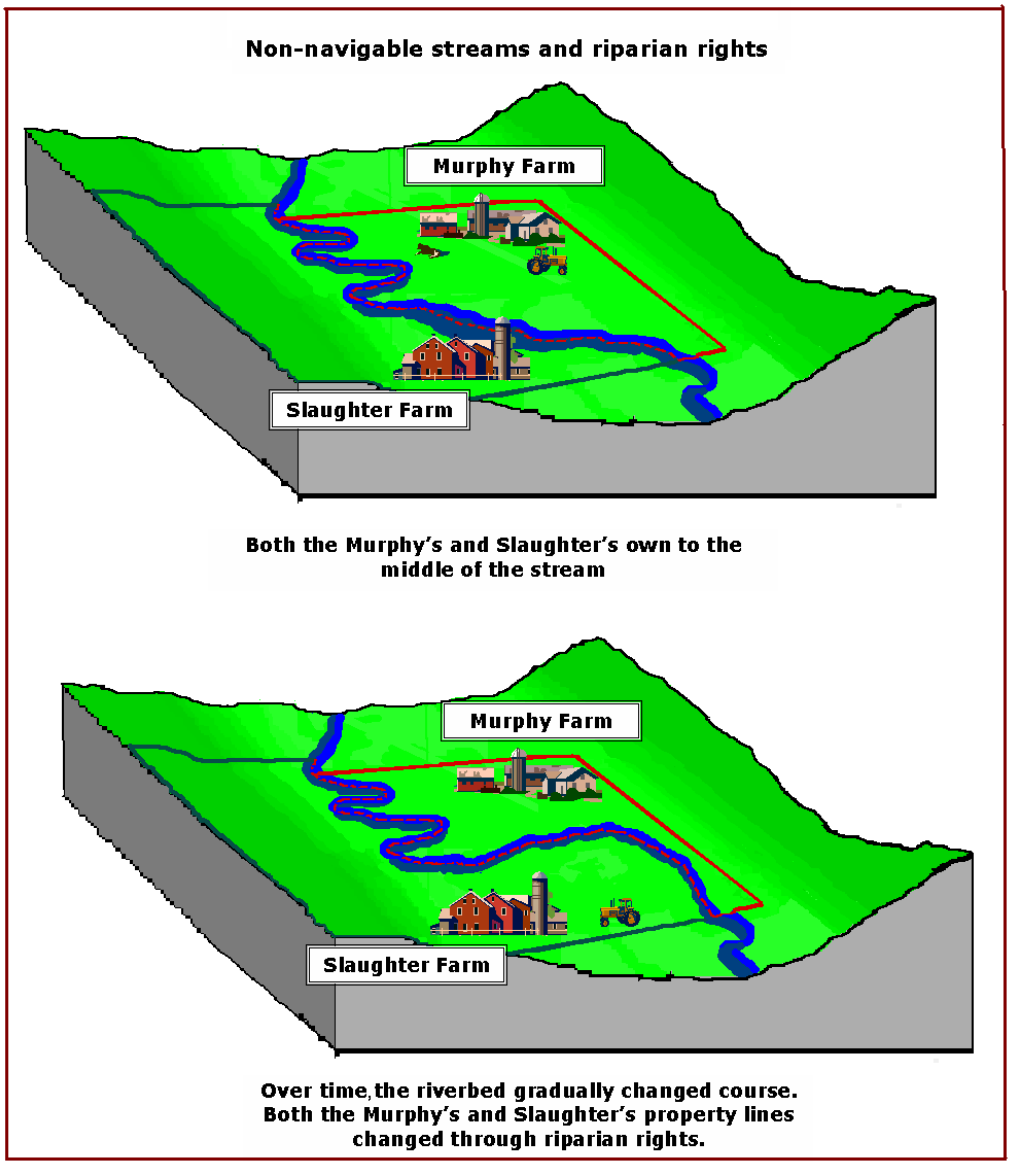
4. Mother Hubbard Clause

For example, the lease might describe 432.16 acres more or less. When a title opinion is rendered, it might be discovered that the tract of land actually contained 432.46 acres.

Generally when this occurs, the oil company is not obligated to go back and pay the lessor an additional bonus for the non-described acreage. However, if a producing unit was formed and a well was drilled, the lessor should be paid his or her proportionate part of all production based on the total 432.46 acres owned under lease.

MOTHER HUBBARD AND RIPARIAN RIGHTS

Generally, non-navigable streams or rivers are owned by the adjacent property owners – each owning to the middle of the stream or river. Over time, riverbeds gradually change as the natural flow of the water changes its course. When this happens, the property owner's rights to the river change with the natural flow of the water. This is called riparian rights.



Notice that the language in the lease example covers *riparian rights*. If

your company had taken a lease on the Slaughter farm lands, because of the change in the riverbed, your company's acreage position would have changed dramatically.

Not all Mother Hubbard language is the same. The following language does not mention the word riparian; however, a provision for "all accretion attaching to … said land" is specified. This language would have the same outcome as in the previous example.

All land owned by Lessor in the above mentioned Section or Sections, all property acquired by prescription and all accretion attaching to and forming a part of said land are included herein, whether properly or specifically described or not.

AVULSION RIGHTS

Avulsion is the sudden change in the course of a river or stream caused by such things as a flood or by man. Generally, avulsion will not change the ownership to the land and the original boundary ownership remains the same.

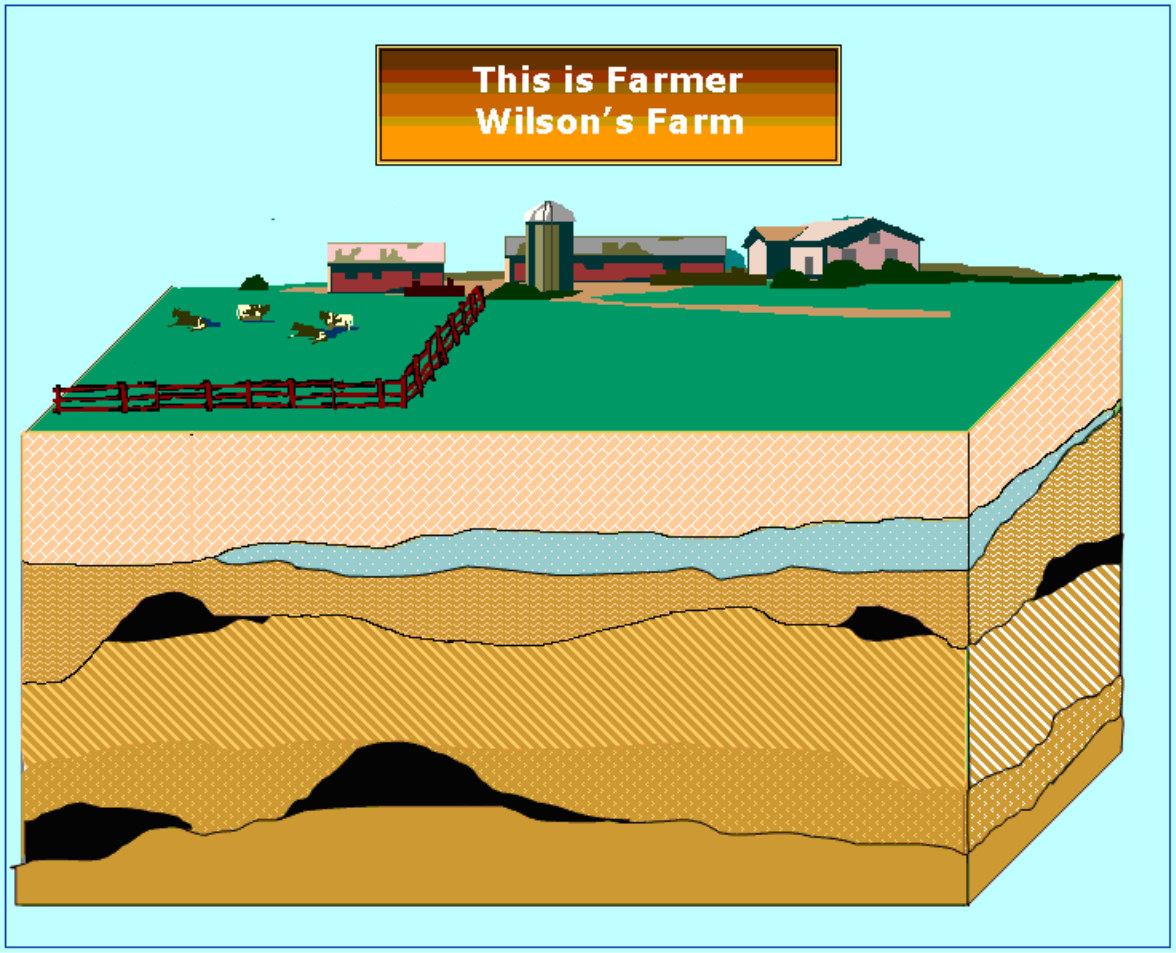
SOME LIMITATIONS FOR THE MOTHER HUBBARD CLAUSE

Some courts have limited the scope of the Mother Hubbard Clause to cover only strips of land that were *unknown* at the time of the oil and gas lease. The rational for this is simple: if, at the time of the lease, all of the lands were *known* but only a portion of the land was described on the lease, then the non-described tract of land was considered to be a separate tract of land.

Example:

Farmer Wilson leased all of the lands shown to your company *excluding the fenced lands*. It is clear that those lands were known at the time of the lease. He considered them a separate tract of land.

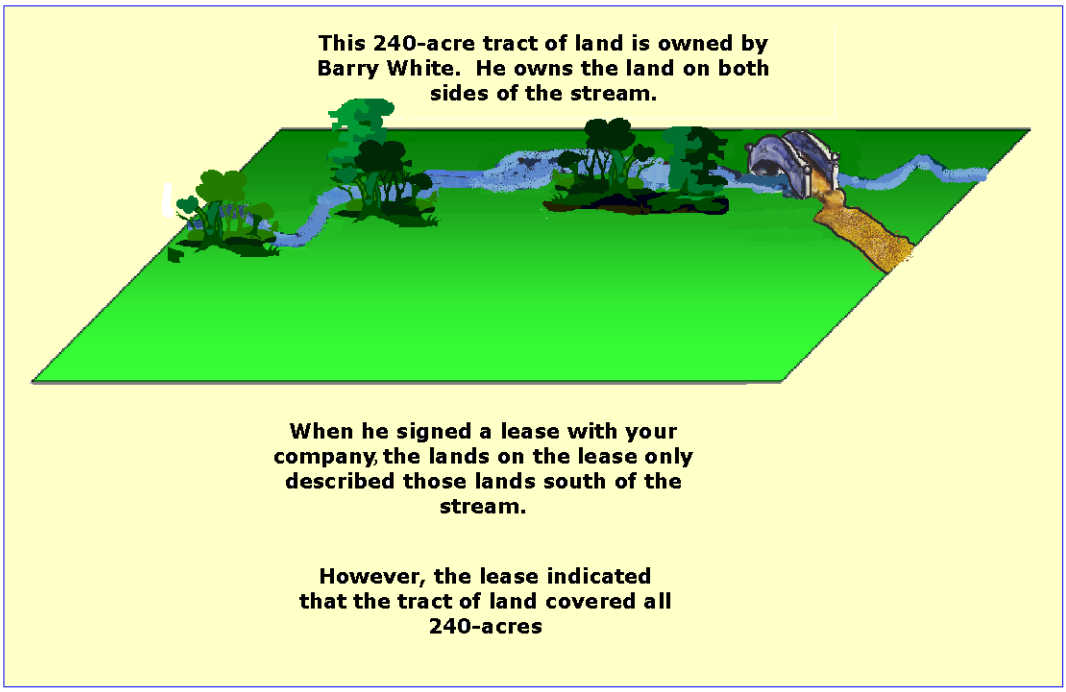
Even though they are contiguous and adjacent to the tract of land found on the lease, your company could not claim them under the Mother Hubbard Clause.



Courts have also ruled that certain errors made on the part of the lessor cannot be resolved through the Mother Hubbard Clause.

Example:

Barry White leased with your company. The legal description only referenced those lands south of the stream. Those lands contain 195-acres. Together the lands south of the stream and north of the stream total 240-acres. The lease referenced 240-acres.



In cases like this where an obvious mistake has taken place on the lease form, courts generally will not allow the Mother Hubbard Clause to remedy the error.

5. THE GRANTING CLAUSE CAN CONTAIN DEPTH LIMITATIONS.

Granting Clause

. . . situated in the County of Dewey,
State of Montana, described as follows, to-wit:

Township 16 South, Range 16 West
Section 14: SW/4NW/4, W/2SW/4

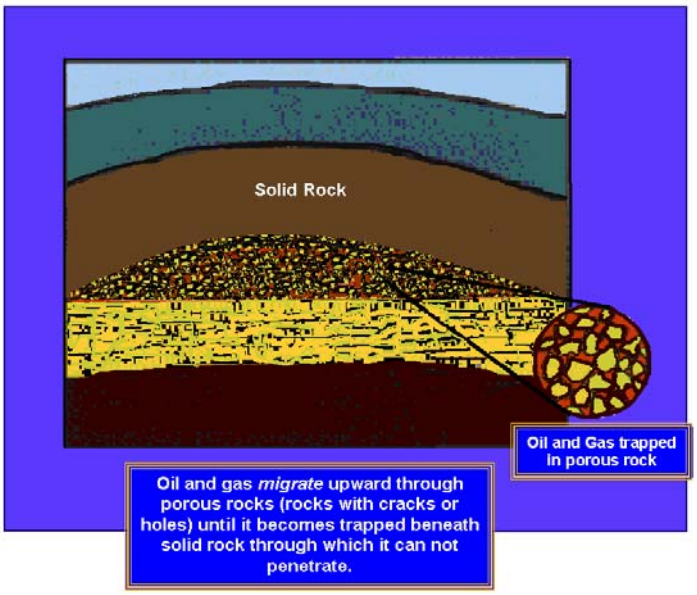
5. Limited from the surface of the earth to 9,355 feet.

of Section 14, Township 16 South, Range 16 West,
and containing 120.00 acres, more or less,

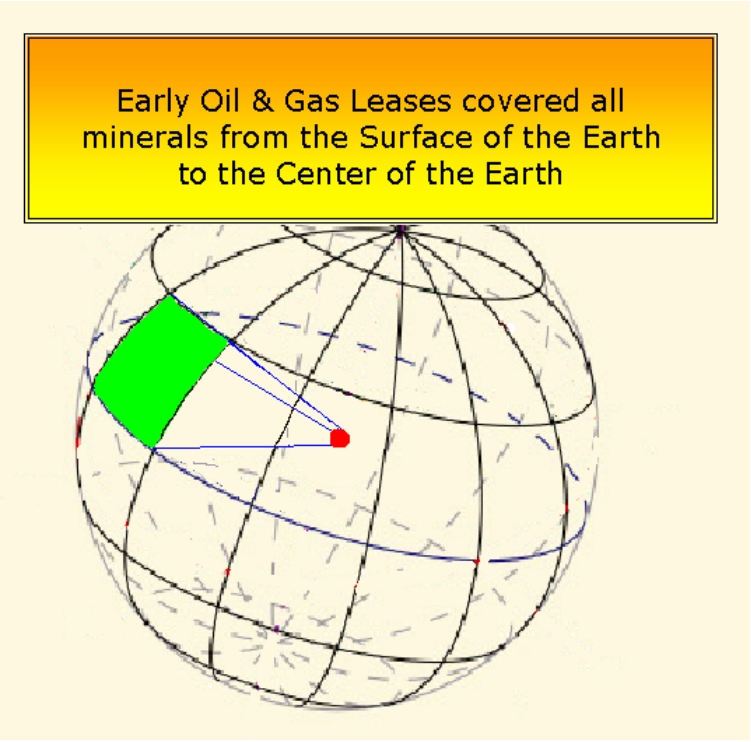
5. Granting Clause with Depth Limitations

Subsurface reservoirs of oil and gas are not found in underground caves or caverns rather they exist in porous rocks (rocks like sandstone that have holes). Since oil and gas travel or migrate through these types of rocks, they travel upward until they are trapped beneath a formation of solid rocks that contain no cracks or holes.

Finding these trapped reserves can be tricky. They are not always at the same depth. In one location, oil and gas might migrate upward to a depth of 3,000 feet before it becomes trapped. In another location, the oil and gas might become trapped beneath a deeper formation of solid rock located at 8,000 feet.



As the oil and gas industry began to mature, both lessor and lessee became more educated about oil reserves. In the early days, the oil and gas lease would cover the minerals from the surface of the earth to the center of the earth. In such a case, any and all reservoirs were covered under the one oil and gas lease. If the company taking the lease only wanted to drill shallow wells at a depth of 3,000 feet, any reserves deeper than 3,000 feet would sit for decades without any attempt to produce the oil and gas minerals.



This issue produced oil and gas leases that contained depth limitations. These depth restrictions would limit the company from producing any reservoirs either above or below the depths covered in the oil and gas lease.

Leases containing depth restrictions can be styled in several ways. Often the limitation is referenced with the words, "the stratigraphic equivalent of" followed by a certain depth or a reference to a certain geologic formation. Often selecting a formation in order to define a depth is avoided if the formation is not easily identifiable. In cases like this and in order to identify a specific formation, a lessor may use the name of a certain well located near the lease.

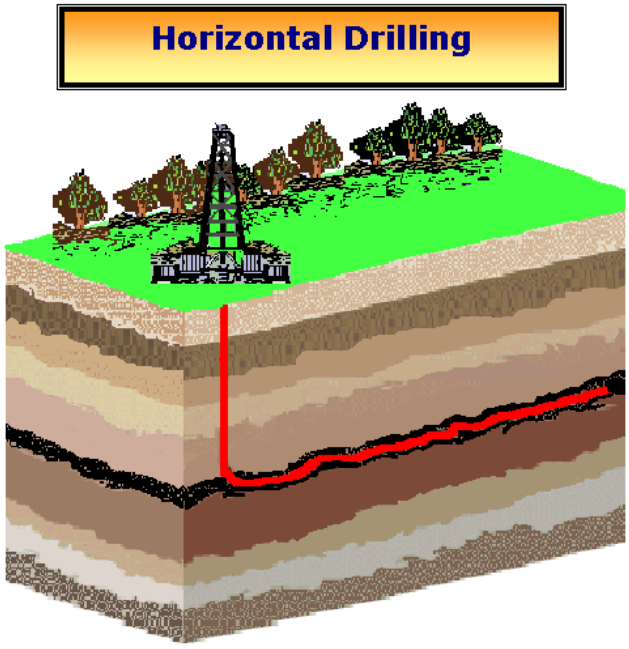
In some parts of the country reservoirs may be wide but very thin. A discovery well might hit a producing zone that is only 25 feet thick. You can imagine that drilling such a well could be very expensive, risky and not have a lot of upside in regards to production.

Once the oil from such a wellbore location is produced, the porous rocks sit empty until the other oil from this wide reservoir begins to seep toward the well. But oil seeps very slowly. A few years ago the only way to produce such a field was by drilling as many wells as was allowed into the same reservoir.[12]

Today, the entire concept has changed. The depth restriction found on the lease for this type of zone might read:

"limited in depth from 9,225 feet to a depth of 9,250 feet.

Even though the lease would cover only 25 feet of minerals located at a depth just over 9,000 feet, technology has changed and a company would have the ability, through horizontal drilling, to produce this zone with only one or two well bores.

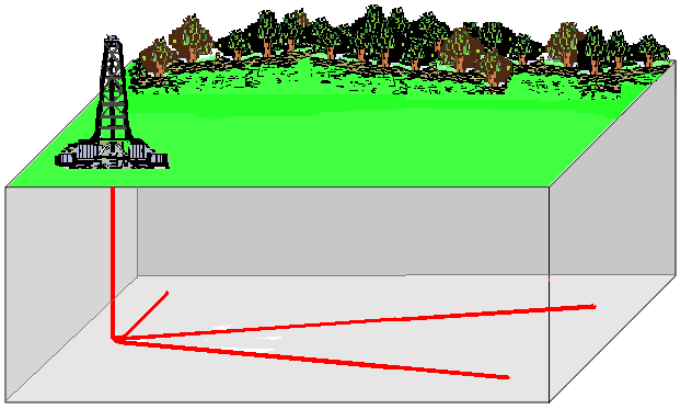


With horizontal drilling a company can capture greater productivity from such a zone.

The concept begins with bending the pipe. "Because the pipe that drives oil wells is surprisingly flexible, a horizontal well can snake around to reach isolated pockets or follow a reservoir that meanders across the terrain." [13]

From one drill site location, a company can drill to the target zone and then bend the pipe, drilling several horizontal legs, each capturing the 25 foot zone under the tract of land.

Today, it is estimated that 3,000 to 4,000 horizontal wells are drilled annually. The longest horizontal well on record was drilled in southern England, in the Wytch Farm oil field. The hole travels almost 7 miles in a horizontal direction. [14]



FOOTNOTES

[1]Landman's Legal Handbook, A Practical Guide to Mineral Leasing, third edition, Rocky Mountain Mineral Law Foundation, F.H. Gower, 1977.

[2]www.dictionary.law.com/definition.

[3] Keller v. Ely, 192 Kan. 698, 702, 391 P.2d 132, 135 (1964).

[4] The Oil & Gas Lease part eleven: The Granting Clause: Substances covered by the lease, Lewis Mosburg's Internet Oil & Gas Newsletter, 1999, www.mosburgoil-gas.com .

[5]Ibid.

[6]An Introduction to Kansas Oil & Gas Law, David E. Pierce, Washburn University School of Law, 1988.

[7]Ibid.

[8] blm.gov/nhp/facts/acres.

[9]reyeslaw.com/case_mountainlakesranch.asp.

[10]An Introduction to Kansas Oil & Gas Law, David E. Pierce, Washburn University School of Law, 1988, p.13.

[11]G. Alan Perkins, "Rights and Conflicts among Surface Owners, Mineral Owners, and Lessees in Arkansas," *American Association of Professional Landmen, (February,* 2006).

[12]The Department of Geology and Geophysics, University of Wisconsin-Madison, A Crude Story, More Bright Ideas www.geology.wisc.edu/courses/g115/oil.

[13]Ibid.

[14]Ibid.