

# Chapter 2

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## Legal Concepts

### Defining Oil and Gas

The oil and gas industry can be segregated into three subdivisions: upstream operations, midstream operations, and downstream operations. The activities that take place during the midstream operations are often included in the downstream category.

**Upstream operations** are most commonly used when referring to the activities involved in searching for, drilling, and producing either oil or natural gas. This can be referred to as the exploration and production phase. Many simply use the term "E&P." Land activities during this phase would include: the title examination, leasing, title curative, surface agreements, exploration contracts, commission work, and lease maintenance.

**Midstream operations** take place after the production phase through the point of sale of the product. Midstream operations are most commonly used when referring to the activities surrounding getting the product to the market place, and begin at the gathering system. The gathering system collects the product from the wellhead and then transports it to a gas processing plant. This gathering system can be a small system, where gas is processed at the wellhead, or a very large system, consisting of thousands of miles of pipe that collect the product from hundreds of wells. Companies that might be involved in midstream operations would include: gathering companies, pipeline developers, trucking companies, rail providers, or barge companies. Midstream operations include the processing, storing, transporting, and marketing of the production.

**Downstream operations** are most commonly used when referring to the refining, selling, and then distributing of the oil and gas products. Those products might include gasoline, diesel fuel, jet fuel, asphalt, lubricants, synthetics, plastics, fertilizers, antifreeze, pesticides, pharmaceuticals, natural gas, and propane. These operations involve refineries, gas processing plants, petrochemical plants, product delivery, utility companies, and retail outlets.

**Hydrocarbon** can be defined as a compound containing both hydrogen and carbon. Hydrocarbons can be found as a solid (coal), or a liquid (crude oil),

or a gas (natural gas).

**Petroleum** can be defined as the generic name for hydrocarbons, including crude oil, natural gas liquids, natural gas, and their products.

**Crude oil** can be defined as the *liquid* petroleum that comes out of the ground. The term crude oil is different from any refined oils that are manufactured out of the crude oil.

**Natural gas** can be defined as the gas that occurs naturally, and is often found in association with, crude oil production.

**Dry Gas** can be defined as the natural gas which is composed mostly of methane with minor amounts of ethane, propane, and butane. Dry gas contains very little, if any, of the heavier hydrocarbons or liquid hydrocarbons.

**Wet gas** can be defined as any natural gas that contains a small amount of liquid. Wet gas contains methane, ethane, propane, butanes, and some higher hydrocarbons, such as pentane and hexane.

**Coal bed methane (CBM)** can be defined as methane gas that is found in coal seams.

**Condensate** can be defined as those hydrocarbons that are found to be in the gas or gas vapor state while under reservoir conditions, but that become a liquid when temperature or pressure is reduced.

## How do states define oil, gas, and related terms?

One of the important differences between states is how each state defines oil, gas, or related terms. Not all states define these terms in the same way. In many cases, understanding the specific definitions as applied in a given state is critical when determining the outcome of a deed or conveyance.

**Arkansas** – In 1941, an Arkansas Supreme Court decided what is now known as the *Strohacker* Doctrine. The Doctrine says that the term “minerals” in a grant or reservation will include only those substances “commonly recognized as minerals” at the time and location of the execution of the deed. The courts determine the intent of the parties through the *Strohacker* Doctrine and the court will determine intent by looking at “the general legal or commercial usage of the word at the time and place of its usage.” *Stegall v. Bugh*, 228 Ark. 632, 310 S.W.2d 251 (1958). *Missouri Pacific Railroad Co. v. Strohacker*, 202 Ark. 645, 152 S.W.2d 557 (1941).

**Colorado** – According to Colorado Revised Statute 34-60-103 (2002), “Gas” means all natural gases and all hydrocarbons not defined as oil.

"Oil" means crude petroleum oil and any other hydrocarbons, regardless of gravities, which are produced at the well in liquid form by ordinary production methods, and which are not the result of condensation of gas before or after it leaves the reservoir.

**Louisiana** – According to Louisiana Revised Statutes 30:3, "Oil" means crude petroleum oil, and other hydrocarbons, regardless of gravity, which are produced at the wellhead in liquid form by ordinary production methods.

"Gas" means all natural gas, including casinghead gas, and all other hydrocarbons not defined as oil above.

**Montana** – According to Montana Code Annotated 82-1-111, "Coal" will be defined as "a combustible carbonaceous rock formed from the compaction and induration of variously altered plant remains. Coal does not include methane gas or any other natural gas that may be found in any coal formation; or oil shale."

"Gas" means all natural gases and all other fluid hydrocarbons, including methane gas or any other natural gas found in any coal formation, as produced at the wellhead and not defined as oil in subsection (3).

"Oil" means crude petroleum oil and other hydrocarbons, regardless of gravity, that are produced at the wellhead in liquid form by ordinary production methods and that are not the result of condensation of gas before or after it leaves the reservoir.

**Mississippi** – According to the Mississippi Code Annotated 53-3-3, "Oil" shall mean crude petroleum oil and all other hydrocarbons, regardless of gravity, which are produced at the well in liquid form by ordinary production methods and which are not the result of condensation of gas.

"Gas" shall mean all natural gas, whether hydrocarbon or nonhydrocarbon or any combination or mixture thereof, including hydrocarbons, hydrogen sulphide, helium, carbon dioxide, nitrogen, hydrogen, casinghead gas, including natural gas from coal seams, compressed air, and all other hydrocarbons not defined as oil above.

**New Mexico** – According to the New Mexico Oil Conservation Division 19.15.2.7 NMAC., "Casinghead gas" means a gas, or vapor, or both gas and vapor, indigenous to and produced from a pool the division classifies as an oil pool. This also includes gas-cap gas produced from such an oil pool.

"Condensate" means the liquid recovered at the surface that results from condensation due to reduced pressure or temperature of petroleum hydrocarbons existing in a gaseous phase in the reservoir.

"Gas," also known as natural gas, means a combustible vapor composed chiefly of hydrocarbons occurring naturally in a pool the division has classified as a gas pool.

"Gas well" means a well producing gas from a gas pool, or a well with a gas-oil ratio in excess of 100,000 cubic feet of gas per barrel of oil producing, from an oil pool.

"Oil" means petroleum hydrocarbon produced from a well in the liquid phase and that existed in a liquid phase in the reservoir. This definition includes crude oil or crude petroleum oil.

"Oil well" means a well capable of producing oil and that is not a gas well as defined above.

**New York** – According to New York Code Rules and Regulations 550.3, "casinghead gas" is defined as gas or vapor, or both gas and vapor, indigenous to an oil stratum and produced from the stratum with oil.

"Gas" is defined as all natural gas, manufactured, mixed, and by-product gas, and all other hydrocarbons not herein defined as oil or condensate.

"Oil" is defined as crude petroleum oil and all other hydrocarbons, regardless of gravity, that are produced at the wellhead in liquid form by ordinary methods and that are not the result of condensation of gas.

**North Dakota** – According to the North Dakota Century Code, "Coal" means all kinds of coal, and includes what is known as lignite coal, unless a contrary intention plainly appears.

"Gas" means all natural gas and other fluid hydrocarbons not herein below defined as oil.

"Natural resources" means coal, oil, gas, and subsurface minerals as defined herein.

"Oil" means crude petroleum oil and other hydrocarbons, regardless of gravity, which are produced at the wellhead in liquid form, and the liquid hydrocarbons known as distillate or condensate recovered or extracted from gas, other than gas produced in association with oil and commonly known as casinghead gas.

"Subsurface minerals" means all naturally occurring elements and their compounds, volcanic ash, precious metals, carbonates, and natural mineral salts of boron, bromine, calcium, fluorine, iodine, lithium, magnesium, phosphorus, potassium, sodium, thorium, uranium, and sulfur, and their compounds, but does not include sand and gravel and rocks crushed for sand and gravel.

**Pennsylvania** – The prevailing law holds that the word “minerals” in a deed would not alone be sufficient to include oil and gas. However, there is a rebuttable presumption and some courts have gone against this rule if clear, convincing evidence points to the intent by the parties to convey oil and gas as part of the “minerals.” Courts have held that the conveyance of “gas” cannot be assumed to also include “oil” or a conveyance of “oil” cannot be assumed to also include “gas.” *Dunham v. Kirkpatrick*, 101 Pa. 36 (1882) and *Bundy v. Myers*, 372 Pa. 583, 94 A.2d 724 (1953).

**Texas** – According to the Texas Natural Resources Code – Section 86.002, “Oil” means crude petroleum oil.

“Gas” means natural gas.

“Gas well” means a well that produces gas not associated or blended with oil at the time of production; a well that produces more than 100,000 cubic feet of gas to each barrel of oil from the same producing horizon; or, a well that produces gas from a formation or producing horizon productive of gas only encountered in a well bore through which oil also is produced through the inside of another string of casing.

“Oil well” means any well that produces one barrel or more of oil to each 100,000 cubic feet of gas.

“Dry gas” means gas produced from a stratum that does not produce oil.

“Casinghead gas” means any gas or vapor indigenous to an oil stratum and produced from the stratum with oil.

“Natural gasoline” means gasoline manufactured from casinghead gas or from any gas.

**Utah** – According to Utah Code Annotated 40-6-2, “Condensate” means hydrocarbons, regardless of gravity, that occur naturally in the gaseous phase in the reservoir and are separated from the natural gas as liquids through the process of condensation either in the reservoir, in the wellbore, or at the surface in field separators.

“Crude oil” means hydrocarbons, regardless of gravity, that occur naturally in the liquid phase in the reservoir and are produced and recovered at the wellhead in liquid form.

“Gas” does not include any gaseous or liquid substance processed from coal, oil shale, or tar sands.

“Natural gas” means hydrocarbons that occur naturally in the gaseous phase in the reservoir and are produced and recovered at the wellhead in gaseous form, except natural gas liquids as defined below and condensate as defined above. “Natural gas” includes coalbed methane gas.

“Natural gas liquids” means hydrocarbons, regardless of gravity, that are separated from natural gas as liquids in gas processing plants through the process of condensation, absorption, adsorption, or other methods.

“Oil” means crude oil, as defined above, condensate, as defined above, or any mixture of them. “Oil” does not include any gaseous or liquid substance processed from coal, oil shale, or tar sands.

**West Virginia** – The term “minerals” would convey oil, gas, and coal. The term “coal and minerals” would convey oil, gas, and coal. The term “coal minerals” would not convey oil and gas. *Bruen v. Thaxton*, 126 W. Va. 330, 28 S.E.2d 59 (1943). “Coalbed methane” has not been defined by the West Virginia Supreme Court as being either coal or gas. Instead, they ruled that coalbed methane belonged to the coal owner if it remained embedded within the coal seam, but if it migrated outside of the coal seam, it could be captured by the owner of gas rights. *Moss*, 591 S.E.2d at 143.

**Wyoming** – According to Wyoming Oil and Gas Conservation statutes, “oil” shall mean crude petroleum oil and any other hydrocarbons, regardless of gravities, which are produced at the well in liquid form by ordinary production methods, and which are not the result of condensation of gas before or after it leaves the reservoir. The word “gas” shall mean all natural gases and all hydrocarbons not defined herein as oil.

The term “oil rights,” used in a reservation of oil only, might also include gas, according to the Wyoming Supreme Court. *Hickman v. Groves*, 71 P.3d 256 (Wyo.2003). Coalbed methane gas has been an area of controversy and in 2002, a Wyoming court was asked to examine a conveyance with the following granting and reservation language:

granting “all coal and minerals commingled with coal that may be mined or extracted in association therewith or in conjunction with such coal operations” reserving “all oil, gas, and other minerals except as set forth above.”

The court ruled that the coalbed methane gas was not granted under the language, but instead was reserved by the grantor. *Newman v. RAG Wyoming Land Co.*, 53 P.3d 908 (Wyo. 2002).

Another court examined the following language whereby the deed granted:

“all coal and all other minerals, metallic and nonmetallic, contained in or associated with coal and which may be mined and produced with coal which grantor owns or holds” reserving “all oil, gas, and other minerals in said lands which grantor now owns, other than those included above in the conveyance to grantee.”

This court also ruled that the coalbed methane gas had been reserved.

McGee v. Caballo Coal Co., 69 P.3d 908 (Wyo.2003).



**Scenario 1:**

Assume that Abe, the owner of a 40-acre tract of land, conveyed the following to Betty:

*"all coal and all other minerals commingled with coal or associated with coal and which may be mined and produced with coal."*

In the deed, Abe reserved the following: *"all oil and natural gas."*

Who might own the *coalbed methane gas* if this scenario happened in Montana, Utah, West Virginia, or in Wyoming?

<p><b>1.</b> Assume that Abe, the owner of a 40-acre tract of land, conveyed the following to Betty:</p>  <p><b>Abe</b>                      <b>Betty</b></p> <p><i>"all coal and all other minerals commingled with coal or associated with coal and which may be mined and produced with coal"</i></p>	<p><b>2.</b> In the deed, Abe reserved the following:</p>  <p><b>Abe</b>                      <b>Betty</b></p> <p><i>"all oil and natural gas."</i></p>
<p><b>3.</b> Who might own the <i>coalbed methane gas</i> if this scenario happened in Montana, Utah, West Virginia or in Wyoming?</p>	<p><b>Montana</b> _____</p> <p><b>Utah</b> _____</p> <p><b>West Virginia</b> _____</p> <p><b>Wyoming</b> _____</p>



ANSWER: The outcome would be different if this language appeared in each of the states. In Montana, "Gas" includes any natural gas found in any coal formation. It would appear that Abe is the owner of the coalbed methane gas. In Utah, coalbed methane gas has been defined as a part of natural gas, and would also appear to belong to Abe. In West Virginia, as long as the coalbed methane remained embedded within the coal seam

beneath the 40 acres, it would seem to belong to Betty. If it migrated outside of the coal seam and under a separate tract of land, it would belong to the owner of the coal under this tract of land. If this scenario happened in Wyoming, the coalbed methane would belong to Abe.

**Scenario 2:**

Assume that Abe, the owner of a 40-acre tract of land, conveyed the described land to Betty. In the deed, Abe reserved the following: *"excepting and reserving unto myself the mineral rights."*

Has Abe reserved the oil and gas minerals if this scenario happened in Pennsylvania or West Virginia?



<p><b>1.</b> Assume that Abe, the owner of a 40-acre tract of land, conveyed the described land to Betty.</p>  <p><b>Abe</b>                      <b>Betty</b></p>	<p><b>2.</b> In the deed, Abe reserved the following:</p>  <p><b>Abe</b>                      <b>Betty</b></p> <p><i>"excepting and reserving unto myself the mineral rights."</i></p>
<p><b>3.</b> Has Abe reserved the oil and gas minerals if this scenario happened in Pennsylvania or West Virginia?</p>	<p><b>Pennsylvania</b> _____</p> <p><b>West Virginia</b> _____</p>

ANSWER: If this happened in Pennsylvania, there is a good chance that the oil and gas minerals were not reserved by Abe if there is no clear, convincing evidence that Abe's intent was to reserve the oil and gas; therefore, Betty would be owner of the oil and gas in Pennsylvania. In West Virginia, the term "minerals" would convey oil, gas, and coal; therefore, Abe would be the owner of the minerals.

**Scenario 3:**

Assume that Abe, the owner of a 40-acre tract of land, conveyed the described land to Betty. In the deed, Abe reserved the following: *"excepting and reserving unto myself all oil rights."*

Has Abe reserved the natural gas minerals if this scenario happened in Colorado or Wyoming?

<p><b>1.</b> Assume that Abe, the owner of a 40-acre tract of land, conveyed the described land to Betty.</p>  <p><b>Abe</b>                      <b>Betty</b></p>	<p><b>2.</b> In the deed, Abe reserved the following:</p>  <p><b>Abe</b>                      <b>Betty</b></p> <p><i>"excepting and reserving unto myself all oil rights."</i></p>
<p><b>3.</b> Has Abe reserved the natural gas minerals if this scenario happened in Colorado or Wyoming?</p>	<p><b>Colorado</b> _____</p> <p><b>Wyoming</b> _____</p>

ANSWER: If this happened in Colorado, there is a good chance that the natural gas minerals were not reserved by Abe, since the state defines gas as all natural gases and all hydrocarbons not defined as oil. Therefore, Betty would own the natural gas. In Wyoming, the term "oil rights" used in a reservation of oil only might also include gas, according to the Wyoming Supreme Court. *Hickman v. Groves*, 71 P.3d 256 (Wyo.2003). Therefore, Abe has reserved the natural gas.

## Minerals and Royalty - Real or Personal Property?

Depending on the state where minerals are located, the minerals and the royalty associated with the mineral interest can be considered real property, personal property, or both. Understanding this can be important for the land professional, especially when a landowner dies and his or her estate is being distributed according to the state's laws of descent and distribution.

Generally, minerals in the ground and leasehold interests are considered real property. Typically, a royalty interest can be defined as real or personal property depending on whether the royalty is accrued or unaccrued royalty. In most states, unaccrued royalties (royalty that are still in the ground) would be considered real property. Accrued royalties (royalty that has been produced) are considered personal property.

**Alabama** – Minerals in the ground are considered real property. Because the value and alienability of a royalty interest is considered to be the same as a severed mineral interest, royalty is considered personal property. *Dauphin Island. Property Owners Assoc. v. Callon Inst. Royalty Investors*, 519 S.2d 948 (Ala. 1988).

**Arkansas** – In Arkansas, royalty is a right to a share of the mineral produced accruing to the owner of the royalty. The royalty interest before production is part of the land and, therefore, subject to conveyance, but becomes personal property when produced. *Shreveport-El Dorado Pipe Line Co. v. Bennett*, 172 Ark. 804, 290 S.W. 929 (1927).

**Colorado** – Minerals in the ground are considered real property. Unaccrued royalty is also considered real property. "Any conveyance, reservation, or devise of a royalty interest in minerals after July 1, 1991, whether of perpetual or limited duration, creates a real property interest." *Colo. Rev. State*. 38-20-107.2 (2007).

**Kansas** – Minerals in the ground are considered real property. Royalty is deemed to be a non-mineral interest and thus, considered personal property. *Magnusson v. Colorado Oil & Gas Corp.*, 331 P.2d 577 (Kan. 1958).

**Louisiana** – In Louisiana, mineral leases, mineral servitudes, and mineral royalties are considered to be real property. While they are in the ground, mineral servitudes and mineral royalty are considered real property. Captured minerals (royalty) are considered personal property. *Succession of Simms*, 250 La. 177, 195 So. 2d 114, 26 O.&G.R. 24 (1965), cert. denied, 389 U.S. 850, 88 S. Ct. 47, 19 L. Ed. 2d 120, rehearing denied, 389 U.S. 964, 88 S. Ct. 320, 19 L. Ed. 2d 380 (1967).

**North Dakota** – Minerals in the ground and royalty interests are both considered to be real property. *Texaro Oil Company v. Mosser*, 299 NW.2d 191 (N.D. 1980).

**Ohio** – Whereas, oil and gas minerals are considered real property, royalty is considered a personal interest.

**Oklahoma** – Minerals in the ground are considered real property. Royalty or “unaccrued royalty” is still a part of the estate and is still in the ground. Unaccrued royalty is considered real property. “Accrued royalty,” or royalty that has come out of the ground, is considered personal property. *McCully v. McCully*, 1939 OK 43, 184 Okla. 264, 86 P.2d 786 (1939).

**Pennsylvania** – Minerals in the ground are considered real property, royalties to be paid under an oil and gas lease are considered personal property. *Smith v. Glen Alden Coal Co.*, 347 Pa. 290, 32 A.2d 227 (1943). Intestate succession laws of Pennsylvania do not make a distinction between real and personal property when it comes to the division of the estate.

**Texas** – Minerals in the ground are considered real property. As a result of classifying ad valorem taxation, royalty is also considered real property. *Sheffield v. Hogg*, 124 Tex. 290, 77 S.W.2d 1021 (1935); *Stephens County v. Mid-Kansas Oil & Gas Co.*, 113 Tex. 160, 254 S.W. 290 (1923). Texas treats the lessor’s royalty, non-participating royalty, overriding royalty, and production payments the same as any interest in real property. The Texas Supreme Court held that the lessor’s royalty is an interest in the land.

**West Virginia** – Oil royalty is considered to be personal property. *Warren v. Boggs* (W.Va.) 97 S.E. 589.

**Wyoming** – Minerals in the ground are considered real property. Unaccrued royalty is also considered real property. *Denver Joint Stock Land Bank v. Dixon*, 122 P.2d 842 (Wyo. 1942).

**Utah** – Minerals in the ground are considered real property. Unaccrued royalty is also considered real property. *Utah Code Ann. 57-1-1(3)* (2007).

**Scenario:** Assume the following events occurred in the states of Texas, Pennsylvania, and Louisiana. Alex and Kim have two children and lived in one of these three states: Texas, Pennsylvania, or Louisiana. Prior to his marriage to Kim, Alex acquired a separate undivided oil and gas mineral interest located in the state in which he lived.

Three years ago, he leased the minerals to your oil and gas company.

Two years ago, Kim, Alex, and their children moved to North Carolina and failed to tell your company.

That same year, your company drilled a producing well on the lands. Since you did not know where to send Alex's royalty checks, his production money has been placed in suspense. To date, just under \$30,000 sits in the account! Several months ago, Alex died without a Last Will and Testament. He is survived by his wife and children.



Alex, Kim and their two children

Assume your company was notified of Alex's death last week. You were given appropriate heirship documentation and you wish to divide his mineral estate among his heirs.

Using the following descent and distribution charts for each of the states, determine two things: first, who should receive Alex's mineral interest? Second, who should receive the \$30,000 royalty?

	<u>Minerals should go to</u>	<u>Royalty should go to</u>
Texas	_____	_____
Pennsylvania	_____	_____
Louisiana	_____	_____

## Texas Intestate Succession after September 1, 1993

Survivors	Division of the Estate
Spouse with children	Spouse receives Life Estate in 1/3 of all <b>real property</b> . Children become the remainder of this interest and take the other 2/3 equally.
Spouse with children	Spouse receives 1/3 in all <b>separate personal property</b> . Children take 2/3 equally.
Spouse, and all children or descendants of a deceased child are also children or grandchildren of the surviving spouse.	Spouse already owns 1/2 of the <b>community property</b> and receives the decedent's 1/2 in <b>real property</b> .

## Pennsylvania – Intestate Succession

Survivors	Division of the Estate
Spouse with children or descendants of the deceased all of whom are children or descendants of the spouse.	Spouse receives the first \$30,000 plus 1/2 of the balance; the balance passes to the decedent's descendants.

## Louisiana Intestate Succession after December 31, 1981

Survivors	Division of the Estate
Spouse with Children	The surviving spouse receives an undivided 1/2 interest in all <b>community property</b> plus a usufruct in the decedent's 1/2 interest in the <b>community property</b> . The children receive the remainder interest in this 1/2 interest in <b>the community property</b> .
Spouse with children	<b>Separate property</b> (real or personal) goes to the children to be divided equally.

ANSWER: Regarding the Minerals:

**Texas** - The widow will receive a Life Estate in 1/3 of real property. Each of the children will receive 1/2 of the 2/3<sup>rd</sup> remaining in the real property and the remainder from their mother.

**Pennsylvania** – Intestate succession laws of Pennsylvania do not make a distinction between real and personal property when it comes to the division

of the estate. The widow will receive 1/2 of the mineral estate and the children will receive a 1/4 interest in the rest of the mineral estate.

**Louisiana** – The widow will receive nothing. Each of the children will receive an undivided 1/2 interest in their father's real separate property.

ANSWER: Regarding the \$30,000 royalty:

**Texas** – Since Texas treats royalty as real property, the royalty should be treated the same as the minerals. From a practical standpoint, creating a life estate in 1/3 of the money would be difficult. It would appear that an appropriate action would be to distribute the money by 1/3 share to each of the heirs.

**Pennsylvania and Louisiana** – This solution is not as easy as it appears. Remember the family moved and are currently living in North Carolina. According to the North Carolina intestate succession laws, "Personal property, whether located in North Carolina or not, is distributed according to the North Carolina's Intestate Succession Laws," with 100% of the personal property going to the widow (if personal property does not exceed \$30,000).

## Fee Simple Absolute Ownership

Fee Simple Absolute refers to ownership that is complete, absolute, and total ownership in real property. Often, the term "fee simple" and fee simple absolute refer to the same type of ownership and owner. This type of ownership is like owning 100% of the "bundle of sticks" of ownership, now and potentially forever. Very often, the conveying language states that the owner has the right "to have and to hold the property *forever*." A fee simple absolute owner has full possession and control over the property. Therefore, there are many options available in how the bundle of sticks is treated. The fee owner can sell 100% of the sticks, sell only certain rights in certain sticks, sell certain sticks for a specified period of time, or allow the entire bundle to pass to his or her heirs.

With few exceptions and in most countries of the world, all minerals including hard minerals and oil and gas are owned by the government. In these areas of the world, no citizen or private organization has the right to mineral ownership. The United States is one of the few exceptions to this rule.

As pioneers moved west, the U.S. government, in most cases, conveyed to the grantee a "fee simple absolute" estate. In other words, settlers received

all rights from the surface to the center of the earth. These rights also included the air above the land.

## Elements of a Mineral Ownership

One of the most important differences between states is related to the nature of ownership of oil and gas minerals. In oil and gas producing states, there are two basic theories on when oil and gas ownership takes place. The first theory is the ownership-in-place theory, and the second is the non-ownership theory.

### Ownership-In-Place Theory

Under this theory, a landowner would own a corporeal possessory interest in the subsurface minerals lying beneath the lands. A possessory interest would be much like owning land in fee simple. The minerals are a part of the land and the owner has the right to occupy, possess, and exercise control over these lands to the exclusion of others. Because oil and gas minerals will move, ownership would be considered a “determinable fee,” which means that ownership can change upon the occurrence of a specified event, such as the minerals moving from beneath the owner’s tract of land to a neighbor’s tract of land. Under the ownership-in-place doctrine, a land owner would be able to claim ownership of oil and gas minerals as long as they were under his or her tract of land. Once they moved beneath a neighbor’s tract of land, the ownership would change. Ownership-in-place is subject to the rule of capture. Most oil and gas producing states seem to adhere to this theory.

### Non-Ownership Theory

Under this theory, ownership of the oil and gas minerals will only take place once they are produced. Although the landowner has a non-possessory interest in the minerals, he has the exclusive right to explore for, search, develop, capture, and produce the minerals. The non-ownership theory can also be referred to as the exclusive-right-to-take theory.

**Alabama** appears to operate under the *non-ownership theory*.

**Arkansas** appears to operate under the *ownership-in-place theory*.

**California** appears to operate under the *non-ownership theory*.

**Colorado** operates under the *ownership-in-place theory*; therefore, a mineral owner has the right to possession of the oil and gas in place, as well as the right to search for, develop, and produce oil and gas from the property. However, because the ownership is a “determinable fee” and the

ownership is based on a present interest, subject to the rule of capture, the mineral owner has no interest once the minerals move.

**Florida** operates under the *ownership-in-place theory*, which says “the owner of a tract of land holds the fee in oil and gas underlying the boundaries of his property even though the oil and gas is not the subject of actual possession until brought to the surface.” *In re Hillsborough Holdings Corp.*, 207 B.R. 299, 303 (Bankr. M.D. Fla. 1997).

**Illinois** appears to operate under the *non-ownership theory*.

**Indiana** appears to operate under the *non-ownership theory*.

**Kansas** appears to operate under the *ownership-in-place theory*.

**Kentucky** appears to operate under the *non-ownership theory*.

**Louisiana** operates under the *non-ownership theory*. According to the Louisiana Mineral Code, ownership of land does not include ownership of oil, gas, and other minerals occurring naturally in liquid or gaseous form. The landowner or the owner of a mineral servitude has the exclusive right to explore and develop the property for the production of such minerals and to reduce them to possession and ownership. *2006 Louisiana Code - RS 31:6 — Right to search for fugitive minerals; elements of ownership of land*.

**Maryland** appears to operate under the *ownership-in-place theory*.

**Michigan** operates under the *ownership-in-place theory*. Michigan laws have established that oil and gas interests are considered real property until they are severed from the estate. *ANR Pipeline Co v 60 Acres of Land*, 418 F Supp 2d 933 (WD Mich 2006).

**Mississippi** follows the *ownership-in-place theory*, in which an oil and gas lease is a conveyance of real property and the transferee obtains a determinable fee in minerals. *Sims v. Inexco Oil Co.*, 618 F. Supp. 183, 187 (S.D. Miss. 1985).

**Montana** operates under the *ownership-in-place theory*. Montana classifies a mineral interest as real property in oil and gas in place. The primary characteristic of the mineral estate is that it is the dominant estate and ownership in that estate carries with it the right to enter the land to explore, drill, and produce the minerals. *Stokes v. Tutvet*, 328 P.2d 1096, 1099, 1100 (MT 1958). “Royalty interests” and an “overriding royal interest” are also considered a real property interest. *Edwards v. Prince*, 719 P2d 422 (MT 1986).

**New Mexico** appears to operate under the *ownership-in-place theory*.

**New York** operates under the *non-ownership theory*. Under common law, the state of New York adheres to the rule of capture. *Wagner v. Mallory*, 169 NY 501. “Title to subsurface oil and gas vests in the party which first brings

it to the surface and reduces it to possession.” *Envirogas, Inc. v. Chu*, 114 AD2d 38, 41, affirmed, 69 NY2d 632, citing *Wagner, supra*.

**North Dakota** operates under the *ownership-in-place theory*. North Dakota classifies a mineral interest as real property in oil and gas in place. The primary characteristic of the mineral estate is that it is the dominant estate and ownership in that estate carries with it the right to enter the land to explore, drill, and produce the minerals. *Texaro Oil Company v Mosser* 299 N.W. 2d 191, 194 (ND 1980). “Royalty interests” and an “overriding royal interest” are also considered a real property interest. *GeoStar Corp. v. Parkway Petroleum, Inc.*, 495 N.W.2d 61, 67 (ND 1993).

**Ohio** appears to operate under the *non-ownership theory*.

**Oklahoma** operates under the *non-ownership theory*. Oklahoma holds that ownership takes place upon the retrieval of the minerals from the ground.

**Pennsylvania** operates under the *ownership-in-place theory*.

**Tennessee** appears to operate under the *ownership-in-place theory*.

**Texas** operates under the *ownership-in-place theory*. Texas holds that minerals are real property and are absolutely owned by the landowner when the minerals are under their tract of land. Once they move beneath another tract of land, the ownership changes. Texas also holds that the landowner can convey or reserve the minerals forever.

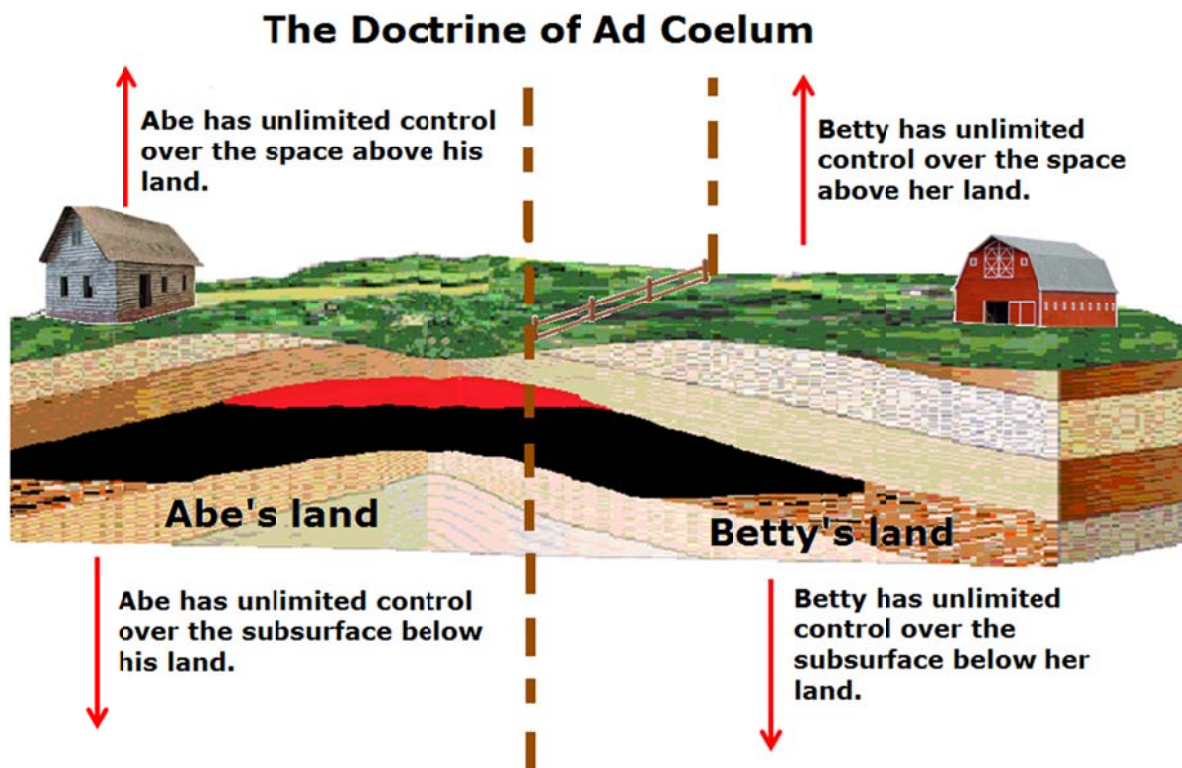
**Washington** appears to operate under the *ownership-in-place theory*.

**West Virginia** operates under the *ownership-in-place theory*. Oil and gas are owned by the owner of the land as long as the minerals are on it or in it, subject to the owner’s control. The ownership would change once the minerals moved beneath a neighboring tract of land. *Energy Dev. Corp. v. Moss*, 214 W. Va. 577, 591 S.E.2d 135, 147 (2003).

**Wyoming** appears to operate under the *non-ownership theory*.

## The Doctrine of Ad Coelum

The doctrine of *ad coelum* dates back to the Roman Empire and the English Common law system, and states that a landowner owns everything above and below the land, up to the heavens and down to hell. The United States adopted the doctrine giving a landowner *unlimited* control over the space above their land and the subsurface below their land. This doctrine worked well for hard rock minerals that were in place; however, issues arose when oil and gas minerals were being extracted from a common reservoir and from beneath a neighboring tract of land. The doctrine does not take into consideration that actions of one landowner in a common reservoir can deplete the reservoir entirely, thus creating loss for the other landowners in the same reservoir. As courts became involved, they realized that the strict application of the doctrine as it applied to hard rock minerals needed to be modified in order to accommodate the characteristics of oil and gas minerals. Since oil or gas reservoirs may stretch beneath many separate tracts of land, and since it is impossible to determine which tract of land the produced product originated from, the doctrine was modified by the rule of capture. In conjunction with the rule of capture, this doctrine implies that a landowner developing oil and gas minerals from this common reservoir could act in such a manner that would adversely affect his neighbor's interest in the same reservoir, but would not be held to any wrongdoing.



## The Doctrine of the Rule of Capture

One of the major differences between oil and gas minerals and hard minerals are their natural ability to move or migrate from high pressure areas to lower pressure areas within a reservoir. Early on in the development of oil production, it was determined that the migration process could move the oil from one owner's tract of land to a neighboring tract of land. Thus, the question arose as to the product's ownership. Under the strict doctrine of the rule of capture, it was determined that a fee simple absolute owner held title to the oil and gas produced from wells drilled on his or her lands, even if the oil or gas had migrated from beneath a neighbor's tract of land. It also established that there was no liability for capturing these minerals, even if they were drained from the neighboring lands.

In 1889, the Pennsylvania Supreme Court compared oil and gas in their natural state to wild animals roaming beneath the earth. The court reasoned that wild animals, and oil and gas, can both wander from one tract of land to another and that oil and gas, while it is beneath a tract of land, belongs to that landowner. If the product migrates beneath a neighboring tract of land and is captured by that owner, title vests in the owner who captures the product. The only protection for a neighbor whose minerals are being drained is to drill and produce wells from his own tract of land. *Westmoreland & Cambria Natural Gas Co. v. De Witt*.

A second ruling by the Supreme Court in *Brown v. Spilman* concluded:

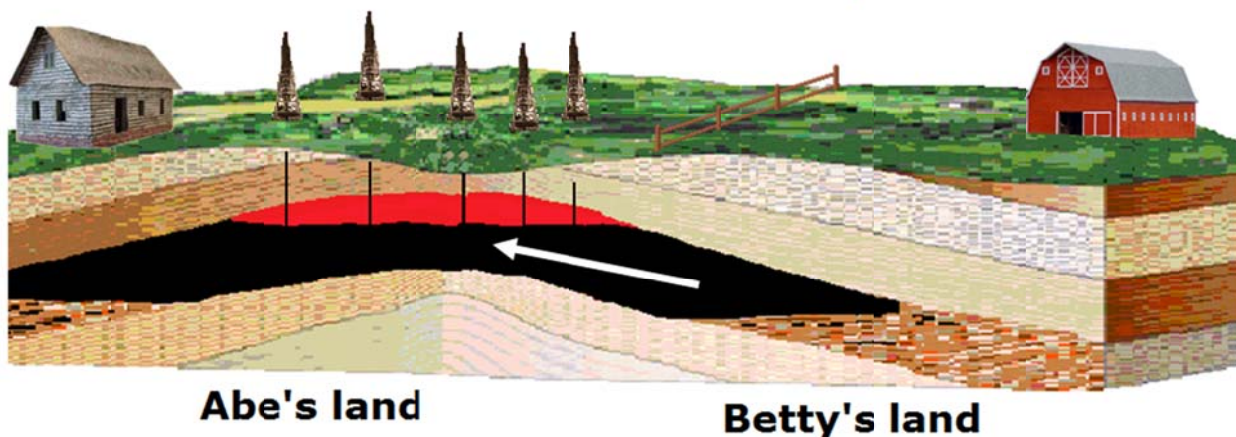
"Petroleum gas and oil are substances of a peculiar character, and decisions in ordinary cases of mining, for coal and other minerals which have a fixed *situs*, cannot be applied to contracts concerning them without some qualifications. They belong to the owner of the land, and are part of it, so long as they are on it or in it, or subject to his control, but when they escape or go into other land, or come under another's control, the title of the former owner is gone. If an adjoining owner drills his own land and taps a deposit of oil or gas extending under his neighbor's field, so that it comes into his well, it becomes his property."

Under the doctrine of the rule of capture, if one party drilled successful wells and began to drain the oil or gas from beneath neighboring tracts of land, courts would not award the drained neighbors any share in the oil or gas production. This left landowners with only two options. Sit idle and watch reservoirs be drained, or drill as many wells, as fast as possible, in order to capture their share of the production. In the early days, there was no limit on the number of wells that could be drilled or no distance regulation from fence lines.

This created, in many parts of the country, a "race to produce" and promoted the philosophy, "Pump as much oil out of the ground as fast as

you can before someone else drills on an adjacent tract of land and beats you to the punch!"

## Doctrine of the Rule of Capture



In order to protect ownership in a common reservoir situation from such actions, the doctrine of correlative rights was developed and began to define ownership in oil and gas in a common reservoir.

Another consequence of the rule of capture, without any government regulations in place, was the loss of reservoir pressure and the premature abandonment of some fields with only 25% of the oil recovered.

Perhaps the greatest example of this can be seen with the events following the famed "Spindletop" Lucas No. 1 well drilled near Beaumont, Texas in January of 1901. Word of the nearly 800,000 barrels of oil being produced in just over a week's time spread across the county like wildfire. Before the end of that year, 440 wells scattered the landscape on the 125-acre hill. By 1904, 1,000 wells had been drilled. The decline rate quickly began and Captain Anthony Lucas, the man who drilled the Lucas No.1 later said, "The cow was milked too hard, and moreover she was not milked intelligently."

## The Doctrine of Correlative Rights

The term "correlative" can be used when two or more parties have a mutual interest in something, when they have an interest in correlation with one another, or their interest is so related that each implies or complements the other. This doctrine is applied when more than one landowner owns the right in oil and gas from a common reservoir.

The doctrine originated in common law from a case where one landowner dug a water well so close to a neighbor's well that it diverted water away from the neighbor's well. The court considered that the two neighbors

owned correlative rights in the water, and that the party digging the new well had the right to dig, but that this party also had an obligation to the other landowner in the common reservoir and did not have absolute and exclusive rights to the water.

In an attempt to help bring into balance the rule of capture and the doctrine of ad coelum, the doctrine of correlative rights established that each landowner in a common reservoir of oil and gas had legal rights and duties to the other landowners. Generally, it states that while each landowner has a legal privilege to take oil and gas through lawful operations on his land, the owner also has an obligation to the other landowners in the common reservoir not to harm the common reservoir or violate the duties owed to his neighbors. Correlative rights establishes the rights of each owner of an oil and gas interest in a common pool or source of supply to have a fair and reasonable opportunity to obtain and produce his just and equitable share of the oil and gas.

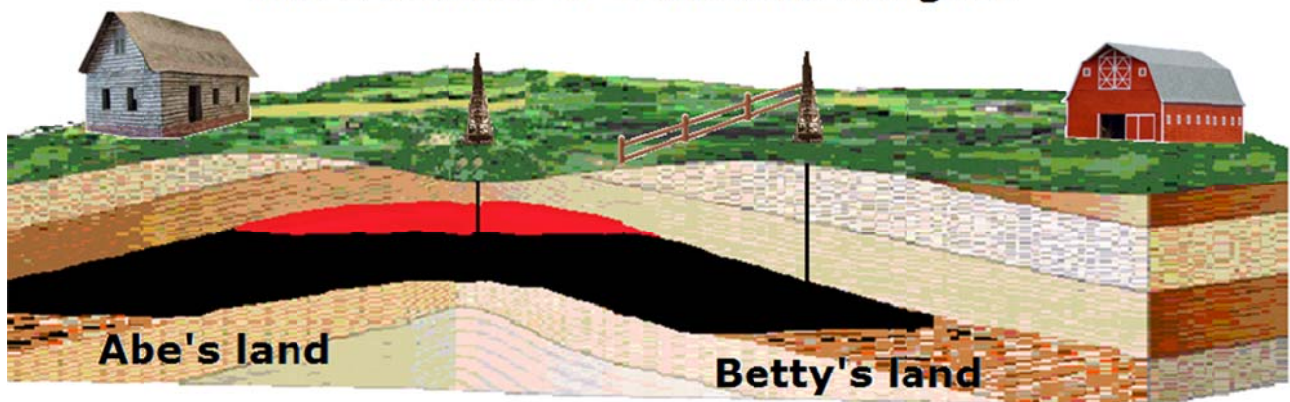
A Texas Supreme Court addressed correlative rights in *Elliff v. Texon Drilling Co.* A well caught fire, cratered, and caused a large amount of oil and gas from a common reservoir to be released into the air, thus causing oil and gas to be drained from neighboring tracts of land. Through the rule of capture, the operator had the right to produce the oil and gas, but through the doctrine of correlative rights, the court found that the operator had a "duty to exercise ordinary care to avoid injury or damage to the property of others." The court also found that the operator had a duty to avoid the negligent waste or destruction of minerals beneath his neighbor's land. The rule of capture did not protect the operator because the drainage was not "reasonable and legitimate."

Today, oil and gas companies are allowed to produce their "proration" of oil and gas from a common reservoir. The term "proration" simply means to divide, distribute, or assess proportionately. Each operator is given the same opportunity to produce their proportionate part of the reserves underlying the same source of supply or reservoir. Proportionate part does not carry with it the same meaning as "equal part." Generally, an operator who has drilled a well with a greater reserve will be allowed to produce at a higher rate than an operator who has drilled a well with a lower reserve. With that being said, if both operators are allowed to produce their proration, both wells should recover their reserves in the same amount of time. One of the primary objectives of proration is to protect a landowner's correlative rights.

In Michigan, an oil company was held liable for drainage of oil that violated a proration order. Sun Oil Company was limited to produce seventy-five barrels of oil per day per well. Instead, they over-produced the well, draining 50,000 barrels of oil from beneath a neighboring tract of land.

Using correlative rights to help define property rights, the court found that the state's conservation order, which limited Sun to seventy-five barrels of oil per day, modified the rule of capture. By not abiding by the proration order, Sun violated the other landowner's right to fairly extract oil and gas from their land, reduced the amount of oil that was available to be produced, and was held liable to the other landowners for damages to the common reservoir through their drainage. The court of appeals held that a violation of a proration order "subjects the violator to liability to all the owners of interests in the pool for conversion of the illegally-obtained oil." *Wronski v. Sun Oil Co.* 279 N.W.2d 564, 570 (Mich. Ct. App. 1979).

## The Doctrine of Correlative Rights



**Both Abe and Betty, owners in a common reservoir, have legal rights and duties to each other.**

**Each have a fair and reasonable opportunity to obtain and produce their equitable share of the oil and gas and are allowed to produce their "proration" of oil and gas from the common reservoir.**

## The Doctrine of Dormant Minerals

In most parts of the United States, the severing of minerals from the surface ownership is common place. Given the nature of this severing over time, severed mineral interests typically become smaller and smaller with each generation of ownership in the interest. The problems that this can pose are several, including an inability to locate owners with tiny fractionalized interests, the loss of revenue for states with tax severed minerals, and an inability to determine the heirs of severed owners when estates have not

been properly probated in the state where the minerals are located.

States that operate under common law rules and have not passed dormant mineral acts hold that a severed mineral estate would not be lost because of non-development or dormancy of those minerals. Other states have adopted statutes that will return severed minerals to the surface owner if those severed minerals sit dormant or unused for a period of time. Other states have made provision whereby, after a statutory period, unclaimed minerals will revert back to the state. There are generally two types of dormant mineral statutes. In some states, the minerals will automatically revert back to the surface owner without any court action, and in others, the minerals will only revert back to the surface owner through a quiet title action.

In areas of the country that are seeing a proliferation of oil and gas exploration, the dormant mineral issue becomes very important. Assume Abe is the surface owner of a tract of land, but owns none of the oil and gas minerals. Every time he goes into town, he sees another neighbor seemingly living the “good life” because of their oil and gas royalty checks.

The state Abe lives in has a dormant mineral statute that joins any severed minerals to his surface ownership if those minerals go unused for 20 years. Potentially, this future revenue could become very significant to Abe.

The one caveat he is wrestling with is that before the minerals will revert to him, the state requires him to make a detailed search for the current addresses of the severed owners and send them notice. The state then requires Abe to report the level of his due diligence in locating proper addresses. If the severed owners receive the notice and properly respond, Abe loses out because their 20 year clock begins all over.

In this scenario, how motivated is Abe to locate current addresses? How tempted might Abe be to make up fictitious addresses and then lie about his due diligence? Assume some of the severed owners are Abe’s cousins. What are the chances that this one issue could escalate into a significant family squabble that would last for years?

## States and Dormant Minerals

**California** – California Civil Code §883.210 et seq. Termination of Dormant Mineral Rights provides for a nonuse period of 20 years in which the owner of the surface land may bring a *judicial action* to terminate severed mineral rights. The severed mineral owner can at any time record a notice of intent to preserve the mineral right.

**Colorado** – Colorado Revised Statutes §38-13-101-103 – Colorado does

not have a dormant mineral statute; however, if production royalties have been unclaimed for a period of five years and are presumed to be abandoned, the royalty is to be paid to the Colorado State Treasurer.

**Connecticut** – Connecticut Code of 2005: The owner of fee simple title, subject to a dormant severed mineral interest for a period of 20 years, may file an action to terminate such mineral interest. The action shall be in the same manner as quiet title. The mineral owner can protect his interest by recording an instrument for the purpose of preserving and keeping the interest.

**Florida** – Florida Statute Ann. 712.01.712.11: Under the provisions of Florida’s Marketable Title Act, a person who has been vested title in land for 30 years or more is deemed to own the estate free and clear, including any dormant mineral interest. The severed mineral owner can preserve their interest by filing of record documented evidence of ownership during the 30 year period.

**Georgia** – Georgia’s Mineral Lapse Statue (O.C.G.A. 44-5-168): “The owner of the real property in fee simple may gain title to such mineral rights by adverse possession if the owner of the mineral rights has neither worked nor attempted to work the mineral rights, nor paid taxes due on them for the seven years immediately preceding the filing of a petition to gain title by adverse possession.” Under the statute, the surface owner may gain title to mineral rights by filing a petition requesting relief. Upon a finding in the surface owner’s favor, a judgment and decree will declare the plaintiff with absolute title to such mineral rights. The filing of a statement of claim does not seem possible under Georgia law.

**Indiana** – Indiana statute IC 32-23-10: A severed owner of coal, oil, gas, or other minerals can lose the minerals if they are unused for a period of 20 years. Once the ownership is extinguished, the severed minerals will revert back to the surface owner. Use of the minerals can include actual production, payment of taxes, operations, payment of rentals or royalties, or the filing of a proper “statement of claim” within the 20-year period or within 60 days after receiving actual knowledge that the 20-year period has expired.

Surface owners can make claim to the unused minerals through filing a proper “lapse of interest” notice, whereby public notice is given in a newspaper and written notice is given to the mineral owner (if a proper address can be found). Once the lapse of interest notice is filed, the county recorder records the filing in a book known as the “dormant mineral interest record.” A second option for the surface owner is to file a “quiet title” suit against the severed mineral.

**Illinois** – Illinois Dormant Mineral Interests Act SB1876: If severed minerals sit unused (no form of production, operations, payment of taxes, a recorded document proving activity, or a proper statement of intent to preserve the mineral interest by the severed mineral owner) for a period of 20 years, the surface owner has a right to claim the minerals through a quiet title action. If multiple mineral owners exist, then activity by one owner would be considered activity by all owners. The Act does not affect the mineral interests of Indian tribes and also doesn't affect water laws.

**Kansas** – Kansas statute requires a 20-year dormancy or unused period before the surface owner can make a claim to the severed minerals. The mineral owner has a 60-day grace period after the publication of notice of dormancy in which he or she can file a statement of claim with the register of deeds.

**Kentucky** – The Dormant Mineral Interests Act provides for unused severed minerals to revert to the surface owner after 15 years of inactivity. A quiet title action is required on the part of the surface owner for the reversion to take place. Use of the minerals can include a proper statement of claim by the mineral owner, or by filing a late notice of interest with the court which will stop the quiet title action.

**Louisiana** – Although Louisiana does not recognize dormant minerals, the state provides for the loss of minerals through a 10-year nonuse prescription period. If a landowner wants to sell the minerals under his land, a mineral servitude is created and the new owner only owns the exclusive right to explore and develop the oil and gas. The term on a mineral servitude is 10 years and under non-use, the interests revert back to the landowner. This is called the doctrine of liberative prescription. *Vincent v. Bullock*. 187 So. 35 (La. 1939); *Wemple v. Nabors Oil & Gas Co.*, 97 So. 666 (La. 1923).

**Maryland** – Dormant Mineral Interest Act of 2010: Surface owners, on or after October 1, 2011, can file an action with the Circuit Court in the county where the property is located to terminate a dormant mineral interest if unused for a period of 20 years. The action shall be in the same manner as quiet title. The mineral owner can protect his interest by recording an instrument that creates, reserves, or evidences a claim of interest.

**Michigan** – The Natural Resources Dormant Mineral Act 554.291 requires any owner of severed minerals to record a valid claim of interest within 20 years of the last sale, lease, mortgage, or transfer, or within 3 years of the date of the act, whichever is later. Any such filing requires "an accurate and full description of all land affected by such notice, which description shall be set forth in particular terms and not by general inclusions." Any severed minerals which are not recorded are treated as abandoned, and they will revert to the surface owner.

**Nebraska** – Nebraska Revised Statute 57-228, et seq., provides for a nonuse period of 23 years in which the surface owner may bring a *judicial action* to terminate the mineral interest. A severed mineral owner has the right to file a verified claim of interest in the county within the twenty-three years prior to the filing of the action.

**North Dakota** – North Dakota adopted a Dormant Mineral Act in 1983, effective July 1, 1985. N.D.C.C. §38-18.1. To encourage mineral development, North Dakota's abandoned mineral statute allows a surface owner to reclaim previously severed mineral interests upon 20 years of non-use by the mineral owner. *This is a quiet title action brought by the surface owner to quiet title to previously severed mineral interests pursuant to North Dakota's abandoned mineral statute.*

N.D.C.C. § 38-18.1-02. Any mineral interest is, **if unused for a period of twenty years**, immediately preceding the first publication of the notice required by section 38-18.1-06, **deemed to be abandoned**, unless a statement of claim is recorded in accordance with section 38-18.1-04. Title to the abandoned mineral interest vests in the owner or owners of the surface estate on the date of abandonment.

If the mineral owner has failed to record a statement of claim and the mineral interest has not been “used” as defined in section 38-18.1-03, above, the surface owner may succeed to the dormant interest by complying with the following provisions:

N.D.C.C. § 38-18.1-06.

1. “Any person intending to succeed to the ownership of a mineral interest upon its lapse, shall give notice of the lapse of the mineral interest by publication.
2. The publication provided for in subsection 1 must be made once each week for three weeks in the official county newspaper of the county in which the mineral interest is located; however, if the address of the mineral interest owner is shown of record or can be determined upon reasonable inquiry, notice must also be made by mailing a copy of the notice to the owner of the mineral interest within ten days after the last publication is made.
3. The notice must state: a. The name of the record owner of the mineral interests; b. A description of the land on which the mineral interest involved is located; and c. The name of the person giving the notice.
4. A copy of the notice and an affidavit of service of the notice must be recorded in the office of the County Recorder of the county in which the mineral interest is located and constitutes prima facie evidence in any legal proceedings that such notice has been given.”

**North Dakota's Last Chance Provision** – Failure to use the minerals or record a Statement of Claim will not cause the interest to be extinguished *if* within sixty days after first publication of the notice provided for in §38-18.1-06, the mineral owner records a statement of claim. N.D.C.C. § 38-18.1-05(3).

N.D.C.C. §38-18.1-03 provides that a mineral interest is deemed to be used if:

1. "There are any minerals produced under that interest;
2. Operations are being conducted for injection, withdrawal, storage, or disposal of water, gas, or other fluid substances;
3. The mineral interest on any tract is subject to a lease, mortgage, assignment, or conveyance of the mineral interest recorded in the office of the recorder in the county in which the mineral interest is located;
5. The mineral interest on any tract is subject to any order or an agreement to pool or unitize, recorded in the office of the recorder in the county in which the mineral interest is located;
6. Taxes are paid on the mineral interest by the owner or the owner's agent;
7. A proper statement of claim is recorded;
8. The owner or lessee utilizes the mineral interest in a manner pursuant to, or authorized by, the instrument creating the mineral interest."

**Ohio** – Ohio Dormant Mineral Act, Ohio Revised Code Section 5301.56: A severed mineral owner can lose the minerals after a period of 20 years of nonuse. Once the ownership is extinguished, the severed minerals will revert back to the surface owner. Use of the minerals can include actual production, a title transaction, mineral use with underground storage, a drilling or mining permit, if a tax parcel number has been assigned to the interest, or the filing of a proper "statement of claim" within the 20-year period or within 60 days after receiving actual knowledge that the 20-year period has expired.

Surface owners can make claim to the unused minerals if a proper *notice* is given (Ohio Rev. Code Ann. 5301.56(E)(1)(West 2010)) and an *affidavit of abandonment* is filed in the County where the property is located. This affidavit must be filed at least 30 days after the notice has been given. The *notice* must be sent certified mail with return receipt requested to the severed mineral owner or their successors. If contact information is not known, notice must be published in the local newspaper where the property is located.

**Oklahoma** – Oklahoma – Uniform Unclaimed Property Stat. Ann. § Act 60-651 and 84-271.1 et seq.: If proceeds from any mineral interest are abandoned for a period of 15 years, as provided for in the Uniform Unclaimed Property Act, then the mineral interest shall not be escheated,

rather the interest is subject to a mandatory judicial sale. Judicial action may be brought by any party who has an interest in either the surface or the mineral rights. This procedure is only available for mineral interests that have produced unclaimed proceeds, either in the form of unclaimed royalties or unclaimed bonus or rentals. Notice is to be provided to the surface owner, who then has an opportunity to acquire the mineral interest at the sale.

**Oregon** – Oregon’s procedure for extinguishing dormant minerals Or. Rev. Stat. § 517.170 et seq; The owner of land subject to a dormant mineral interest for a period of 30 years may extinguish the interest by publishing notice and submitting an affidavit of publication for recording. The mineral owner can protect his interest by recording a statement of claim within the last 30 years. Oregon is a self-executing state whereby the non-used minerals will lapse and revert back to the surface owner.

**Pennsylvania** – In 2006, Pennsylvania adopted a Dormant Oil and Gas Act; however, this legislation does not constitute what we might recognize as a “true” “dormant mineral act.” Some see this as nothing more than a 100% tax on production. The Act permits a trustee to be appointed on behalf of the “dormant” owner. The trustee has the power to execute a lease and then, if the rightful owner does not make a claim on the oil and gas, the trustee will collect the royalties. After deducting the trustee fees, the trustee will then escheat the rest of the royalty to the Commonwealth. This act does not vest dormant severed minerals into the surface owner.

**South Dakota** – A mineral interest shall, if unused for 23 years, be deemed abandoned, unless a statement of claim is recorded. Title to an abandoned mineral interest shall vest in the owner of the surface estate on the date of abandonment. The notice of claim must be filed on or before 23-years from the mineral severance, or on or before July 1, 1958, whichever is later. In 2006, Senate Bill 121 was passed. Section 2 asserts that severed minerals are real property and taxes “shall be assessed in the same manner as any other real nonagricultural property.” Section 3 asserts that the owner of severed minerals shall, no later than November 1, 2007, file for record a verified statement setting forth the correct address, interest, and legal description of the property.

**Tennessee** – Preservation, or extinguishment and reversion of mineral interests 66-5-108:

Any interest in coal, oil and gas, and other minerals shall, if unused for a period of twenty (20) years, be extinguished, unless a statement of claim is filed and the ownership of the mineral interest shall revert to the owner of the surface.

“Use of mineral interest” occurs when minerals are being produced thereunder or when operations are being conducted thereon for injection, withdrawal, storage, or disposal of water, gas, or other fluid substances, or when rentals or royalties are being paid to the owner thereof for the purposes of delaying or enjoying the use or exercise of such rights, or when any such use is being carried out on any tract with which such mineral interest may be unitized or pooled for production purposes, or when taxes are paid on such mineral interest by the owner of the land.

Any person who will succeed to the ownership of any mineral interest upon the lapse thereof may commence such lapse by filing, with the clerk and master of the county in which the mineral interest is located, a complaint of claim of abandoned mineral interest.

If, within sixty (60) days after publication is provided, the mineral interest owner does not file with the clerk and master an answer alleging a claim to the mineral interest, the clerk and master shall so certify to the chancellor who shall enter the following order declaring the mineral interest has lapsed and vesting title to the mineral interest in the owner of the surface estate.

**Washington** – Extinguishment of Unused Mineral Rights 78.22 RCW: Washington provides for a nonuse period of 20 years. If a surface owner files a claim of abandonment and extinguishment, together with a copy of the notice and affidavit of publication in the county auditor's office, then the mineral interest *shall be conclusively presumed to be extinguished* (self-executing). The severed mineral owner must file a statement of claim in the county auditor's office during the 20-year period or the 60-day period after the notice by the mineral owner.

**West Virginia** – West Virginia has no statutory dormant mineral act; however, according to W. Va. Code § 55-12A-7, when a person is unknown, missing, or has abandoned mineral interests, a “special commissioner” will be appointed to receive payment from the royalty. If the rights to the royalty have not been claimed in seven years, the commissioner will convey the minerals back to the surface owner.

**Wisconsin** – Lapse and Reversion of Interest in Minerals Law: Severed minerals can exist as long as the minerals are used during a 20 year period. If a severed mineral estate becomes dormant, the owner of the surface may file a statement of mineral claim and claim ownership of the mineral rights. This creates a 3-year waiting period during which a mineral owner may come forward and contest the surface owner’s claim, by showing that the minerals have been used at some time in the last 20 years.

**Scenario:** Read the following scenario and answer the question.

ANSWER: Given today's date and if this happened in North Dakota, the minerals have sat unused and dormant for over 30 years. However, since



Lawrence



Randall

**1. In 1977, Lawrence, the fee simple owner of land, conveyed an "Undivided 50% of the minerals" to Randall.**

**3. In 2008, Lawrence died. His heir is his son Mitch.**



Mitch

**2. In 2006, Randall died. His heirs are Beverly, his daughter and Matthew, his son.**



Beverly,  
Matthew

**4. The minerals have sat dormant since 1977. Whom should you lease if the lands are located in North Dakota, Oregon or Pennsylvania?**

**Mitch**     **Beverly and Matthew**

North Dakota requires a quiet title action in order for the minerals to revert back to Mitch, it would appear that Beverly and Matthew would be the current owners. Many companies would lease from Beverly and Matthew and also take a protective lease from Mitch. In Oregon, the minerals will automatically revert back to Mitch, but he can only extinguish Beverly and Mitch's interest by publishing notice and submitting an affidavit of publication for recording. In Pennsylvania, it would appear that taking a lease from any of the three would be incorrect. Instead, a trustee must be appointed on behalf of the "dormant" owner. It is this trustee that has the power to execute a lease. In Pennsylvania, make sure that any royalty payments go to the trustee.

## The Doctrine of Mineral Estate Dominance

In the United States, the doctrine of the mineral estate dominance was one of the first common law doctrines generally accepted. In 1893, a Pennsylvania court ruled that the surface estate was servient to the mineral estate. The court addressed the issue this way,

“coal, oil, gas, and iron are absolutely essential to our common comfort and prosperity. To place them beyond the reach of the public would be a great public wrong... the question we are considering becomes of a quasi public character. It is not to be treated as a mere contest between A. and B. over a little corner of each.” *Chartiers Block Coal v. Mellon*, 25 Atl. 597 (S.Ct. Pa. 1893).

The Pennsylvania ruling seemed to base its finding on the importance that coal, oil and gas has for society as a whole. This is just one of the reasons for the doctrine. Another important reason relates to a severed mineral owner’s rights of access to their ownership.

Assume that years ago your grandmother inherited a substantial severed oil and gas mineral interest under a tract of land. You can still remember her saying, “Maybe one day an oil company will lease those minerals and drill a well! If they do, I would travel for the first time in my life and leave something of value to my family.” You could tell that in her mind, she thought the minerals had a considerable potential value.

Also assume that your grandmother who owns the severed mineral interest does not, with that ownership, own a right to access those minerals without the permission of the surface owner. What value do those minerals have to your grandmother now? In essence, they have no value without the signature of the surface owner.

Subsequent to the Pennsylvania case, almost all early cases regarding this subject uniformly recognized the doctrine of mineral estate dominance and the implied grant of access by the severed mineral owner. Consider a North Dakota ruling:

“The mineral estate is dominant in that the law implies, where it is not granted, a legitimate area within which mineral ownership of necessity carries with it inherent surface rights to find and develop the minerals, which must and do involve the surface estate. Without such rights, the mineral estate would be meaningless and worthless.” *Hunt Oil Co. v. Kerbaugh*, 283 N.W.2d 131, 135 (N.D.1979).

The outcome of such cases helped create a doctrine in our country whereby the mineral estate has become the dominant estate, and the owner of the severed mineral estate possesses a reasonable right to access (ingress and egress) their minerals without undue damage to the surface estate.

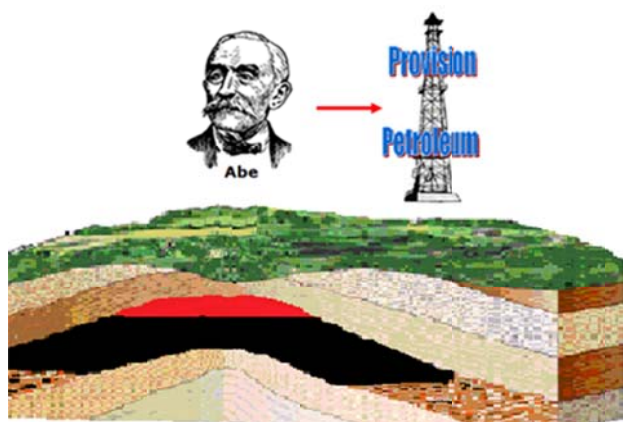
## A Question of Trespass

Because access to the subsurface minerals must occur through the use of surface lands, the question of trespass is always a concern. Trespass can also take place below the surface. Unless an oil company has the rights of access to the subsurface estate, they would be in violation of trespass laws. The following are examples of when trespass might occur and when trespass has not occurred.

### Scenario 1:

Assume that Abe owns both surface and sub-surface rights in a 100-acre tract of land. Abe has granted an oil and gas lease to Provision Petroleum, but has not granted any type of seismic permit. Two weeks ago, Abe planted crops on the land. Last week, Provision accessed the surface lands, laid out their surface seismic equipment on top of the planted field and set off seismic charges beneath the surface. Has trespass taken place?

ANSWER: Even though Provision has not secured any type of seismic permit from Abe, the granting clause in the oil and gas lease has language that gives the oil company permission to conduct seismic activity.



**Abe owns both surface and sub-surface in the pictured land.**

**Abe grants an oil and gas lease to Provision Petroleum. The oil company enters the surface to conduct seismic activity.**

**Has trespass taken place?**

An early West Virginia case concluded, "it is a general rule of law that, when anything is granted, all the means of attaining it and all the fruits and effects of it are also granted."

*Armstrong v. Maryland Coal Co.*, 67 W.Va. 589, 69 S.E. 195, 203 (W.Va. 1910).

Most oil and gas leases would contain some sort of standard surface protection language for Abe. Included in this "boiler plate" language is the phrase that

#### Granting Clause

... 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,

the lessee

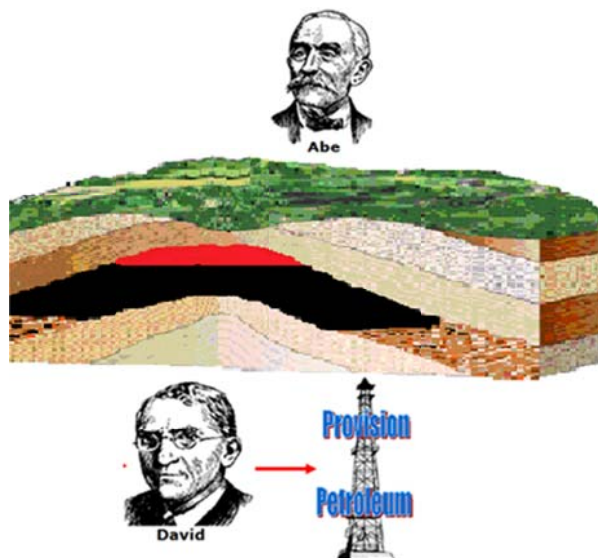
*"shall pay for all damages caused by its operations to growing crops on said land."*

In the scenario, the oil company is bound by this language in the lease and must compensate Abe for the loss of crops. Often a surface/mineral owner will add additional surface protection language to their lease. If Abe has done this, Provision must adhere to this language when conducting its seismic activities.

### Scenario 2:

Assume Abe owns the surface and David owns the sub-surface minerals. Abe has recently planted crops on the land, but has not entered into any type of agreement with Provision Petroleum for seismic operations. David has granted an oil and gas lease to Provision Petroleum. If the oil company accesses the surface lands to conduct seismic activity, has trespass taken place?

ANSWER: In this scenario, David has an unquestionable right to access his minerals, regardless of what Abe's wishes might be. One court concluded that "a grant or reservation of minerals would be wholly worthless if the grantee or reserver could not enter upon the land in order to explore for and extract the minerals granted or reserved." Courts have often ruled that,



**Abe owns the surface lands.**

**David owns the sub-surface lands.  
David grants an oil and gas lease to  
Provision Petroleum. The oil company  
enters the surface to conduct seismic  
activity.**

**Has trespass taken place?**

even though there may not be express language in a granting document, there is an *implied right* to access the minerals. This implied right is then transferred to the lessee through the oil and gas lease.

In our scenario, unless the oil and gas lease contained language that would preclude Provision from access, the oil and gas lease would give the oil company the right to enter the surface and evaluate, through seismic activity, the mineral estate. The oil and gas lease has given Provision an *implied right* to the “reasonable use” of the surface.

Case Law has established “reasonable surface use” as follows:

1. The operator can use salt water produced from the well for operations;
2. The operator can take water necessary for the operations;
3. The operator can house employees on the premises;
4. The operator can construct roads to drill sites;
5. The operator can cut down trees at the site of a well.

In our scenario, Provision Petroleum has obtained, through the lease, an implied right to the “reasonable use” of the surface. Reasonable use can be defined as a right to so much of the surface as is reasonably necessary to explore, develop, and transport the minerals.

Even though the oil company has the right of reasonable surface use, many early court cases determined that surface use must be done with *due regard* for the surface owner’s rights. The “due regard” doctrine requires that excessive and unnecessary uses or damage to the surface be avoided. This doctrine generally concludes that unless an oil company is found to be negligent or excessive, they are only liable for damages to growing crops or improvement to the land. From a practical standpoint, Provision would want to obtain a surface permit agreement from Abe dealing, in advance, with any claims related to surface issues or surface damage issues.

In an early Wyoming case, the court concluded that “In the absence of proof of negligent mining operations... the surface owners... can recover only for damages to agricultural improvements or agricultural crops”. *Holbrook v. Continental Oil Co.*, 73 Wyo. 321, 337, 278 P.2d 798, 804 (Wyo.1955).

Most courts have determined that the right to access the mineral estate through the surface does not give the mineral owner the right to destroy the surface. *Commonwealth v. Fisher*, 364 Pa. 422, 72 A.2d 568 (1950).

In 1883, a Michigan court ruled that,

“mere reservation of minerals... must always respect surface rights of support, and will not, standing alone, permit the surface to be destroyed without some additional statutory or contract authority, and that such statute or contract authority will be construed carefully to prevent the destruction of surface rights.” *Ericson v. Michigan Land and Iron*, 16 N.W. 161, 163 (Michigan 1883)

West Virginia state law requires compensation to surface owners for certain lost income, expenses incurred as a result of being unable to dedicate land

actually occupied by the oil company's operations, the market value of crops destroyed, damage to any water supply, and the cost for repairs of any personal property damaged by operations. W.Va. Code § 22-7-3.

In some states, when drilling a well, Provision has the right to enter the property legally even before any surface agreement is in place. Most states require that the surface owner be contacted prior to the activity, and that a surface agreement has been offered to the surface owner.

Even recently, states have wrestled with or are wrestling with the tensions between surface and subsurface rights. Most courts have consistently ruled on the side of mineral estate dominance but have positioned their laws so that the surface owners are accommodated, where reasonable. The limitations placed on subsurface operations can be generalized as follows:

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

### **Scenario 3:**

Assume Abe and his wife purchased a very scenic 160-acre tract of land where they built their very expensive, "perfect" retirement home. The home sits in the middle of the tract of land. The land cost \$200,000 and the home cost an additional \$300,000 to build. Every morning and afternoon the couple sits outside, somewhere on their wraparound porch, enjoying the views, the sunsets, the sunrises, and the wild animals on the land. Abe and his wife have worked hard their whole lives and they have finally found the "peace" they have longed for.



When Abe and his wife purchased the land, they received no oil or gas mineral rights. An oil company recently leased the minerals from the mineral owner and intends to drill wells on the land. The spacing for the type of wells being drilled is one well on every 10-acres of land. With that being said, the oil company has permission to drill 16 wells on the land. If you were Abe or his wife, what has the potential drilling program of the oil company done to



your “perfect” retirement home? What type of “peace” are you feeling today? What has happened to the value of your property? If you wanted to sell, realistically, what price could you ask for the land and home? If the oil company drills the 16 wells, has any type of trespass taken place?

ANSWER: In this case, trespass still has not taken place. However, several states, including Texas, Utah, North Dakota, Arkansas, New Mexico, and West Virginia have adopted their own doctrine as it relates to surface use. This is widely referred to as the *doctrine of accommodation* or *alternative means* and has, to a certain degree, chipped away at mineral estate dominance. Under this doctrine, although the lessee still has the rights of access, they are required to consider the interests of the surface owner. If there is a pre-existing surface use, the operator is required to accommodate the surface owner if accommodation can be done *easily* and is *reasonable*. The obligation of the operator is to look for reasonable, practical, and alternative means for retrieving the minerals instead of disturbing the split estate surface owner’s land. “Easily” has been determined, through case law, to mean that the cost attributed to the operator’s accommodation does not increase.

Now, lay the doctrine of accommodation and alternative means over the top of Abe and his wife’s scenario. The doctrine *requires* the operator to consider the interests of Abe and his wife. The obligation of the operator is to look for reasonable, practical, and alternative means for retrieving the minerals instead of disturbing the split estate surface owner’s land. With today’s technology, it might be possible to use only one surface pad and still be able to drill the 16 bottom hole locations. Even though the cost would be greater, some operators might choose this option.

## Scenario 4:

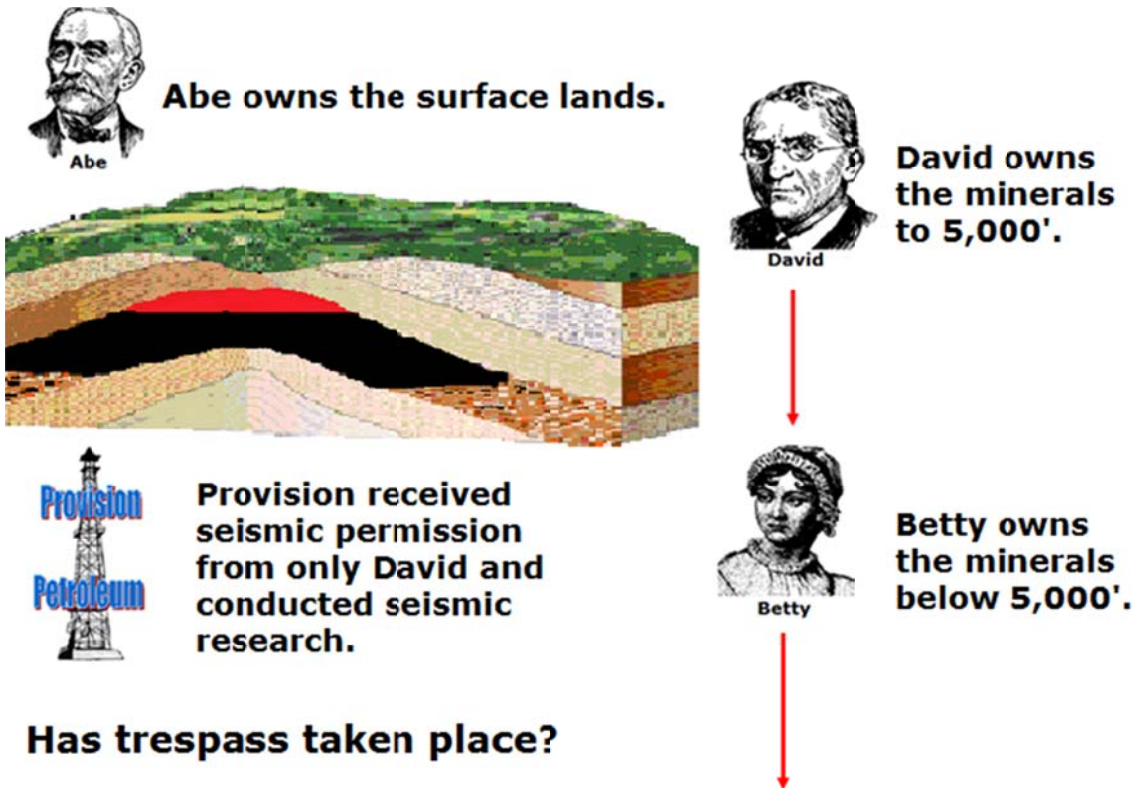
Assume Abe owns the surface but none of the minerals. Eight individuals own undivided interests in the sub-surface minerals. David is the largest undivided mineral owner, owning an undivided 55% of the minerals. If Provision Petroleum acquired a seismic permit from David but acquired no permits from the other mineral owners, and then conducted seismic activity, has trespass taken place?



ANSWER: The question should be asked, "Must consent be acquired from all of the severed mineral owners or would David's consent be sufficient?" In answering this, consider this question. If just one of the other co-tenant owners refused to give their seismic permission, should that keep David from being able to evaluate his interest in the mineral estate? The answer is no. David has the right to evaluate what he owns independently from the others. Therefore, since David owns an undivided 55% of every acre everywhere, with his consent, Provision has obtained access rights to the entire tract of land.

### Scenario 5:

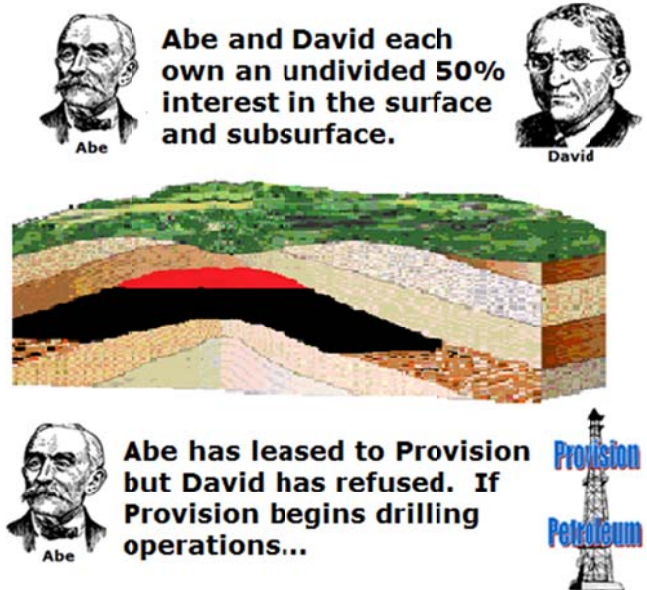
Assume Abe owns the surface but none of the minerals. David owns 100% of the minerals from the surface to 5,000 feet. Betty owns 100% of the minerals below 5,000 feet. Provision Petroleum has been drilling successful shallow wells in the area to a depth of 4,500 feet. However, before drilling on this tract of land, they need seismic data. If Provision received seismic permission from only David and conducted seismic research, would trespass of Betty's minerals have occurred?



ANSWER: Since the drilling activity will be limited to 4,500 feet is David's consent enough? Because the answer to this question is uncertain in many locations, consent should be acquired from all mineral owners at all depths.

## Scenario 6:

Assume Abe and his brother David inherited both the surface and subsurface minerals from their parent's estate. Each owns an undivided 50% interest. Provision Petroleum has approached both Abe and David asking for leases. They want to drill on the tract of land. Abe has consented and signed an oil and gas lease but David has refused. If the oil company drills a well, has trespass taken place on David's 50% mineral interest?



**Has trespass taken place?**

**ANSWER:** In this scenario, because Abe has signed an oil and gas lease, he clearly has given his consent to be pooled with other leases or tracts of land in the vicinity in order to have the well drilled. David has not given his consent to be a part of a pool of leases or tracts of land. Both Abe and David represent two different types of interest that can be pooled in order for the well to be drilled.

Abe represents those parties that have voluntarily agreed to be included in the pool of leases or lands. If all mineral owners would have negotiated and signed oil and gas leases, the unit would be referred to as a voluntary pooled unit.

Since David has refused to sign a lease, he represents those parties that might be *forced* into the pool of leases or lands. The oil company has no power to force David to do anything he does not want to do, but the state regulatory agency that oversees the development of oil and gas does have certain powers over interests that are not leased. Because it is their job to see that oil and gas development takes place in a fair and reasonable fashion, most states will not allow David to stop the development of oil and gas simply because he has refused to sign a lease. It is important to note that not all states recognize or uphold *forced pooling*. If the scenario did take place in a jurisdiction that recognizes forced pooling (some states refer to this as compulsory, statutory pooling or integration), David's unleased interest would not stop the well from being drilled and David's interest would be forced into the drilling unit. Such a unit would be referred to as a forced pooled unit.

## Forced Pooling of an Unleased Mineral Owner

In forced or compulsory pooling jurisdictions, the oil company would file a request for a pooling order. This request must provide a list of all parties that are known to own an oil or gas interest in any tract of land within the proposed unit boundary. All owners who can be located must be notified and advised of the pending pooling action as well as the time and place of the forced pooling hearing. Once the hearing is held, and depending on the results, an order will be issued by the state regarding how David's interest will be treated and what part of revenue, if any, David will receive out of production. As can be seen from the following chart, the interests of an unleased mineral owner can be treated much differently from one state to the next.

	MI	OH	CO	AR	ND	MT	FL	IN	LA	TX	OK	NM	WY	AL	PA	NY	WV
Compulsory Pooling	X											X					X
Mandatory Pooling		X															
Forced Pooling			X		X	X	X	X	X		X		X	X			X
Integration Provision				X										X	X		
Unleased mineral owner receives 1/8th cost free royalty	X	X				X											
Unleased mineral owner can lease with royalty and bonus set by commission				X							X						
Unleased mineral owner can be deemed non-consent (commonly 400%-600%), receiving 1/8th royalty				X													
Unleased mineral owner will receive 1/8th royalty until operator has recovered 7/8th of owners share of 100%-200% payout costs			X														
Unleased mineral owner will receive a cost free royalty equal to the acreage weighted average royalty in unit or 16%					X												
Unleased mineral owner will receive a 300% nonparticipating drill cost penalty							X										
Unleased mineral owner will receive a royalty (equitable share) from production set by the commission								X							X		
Unleased mineral owner will receive no share of production until the operator recoups drilling and associated costs									X					X			
Unleased mineral owner will receive 8/8th of production after payout if interest is undivided and well drilled on his/her tract of land										X		X					
Unleased mineral co-tenant will receive no share of production if the well is not drilled on his/her tract of land										X		X					
Integrated royalty owner receives a royalty equal to the lowest royalty in an existing lease in the spacing unit, but no less than 1/8th																X	
Drilling cannot take place on this tract of land. Terms and conditions as set by the board will be just and equitable - shallow gas wells																	X
Receive a 300% penalty for that portion of the costs for drilling the well.													X				

**Arkansas** – Integration is the term used in Arkansas when dealing with an unleased mineral owner. Integration is provided for in Section 15-72-301 through 324 of the Arkansas Code. The Commission has the power to

integrate the interests of mineral owners if they refuse to execute a lease, pay their prorata share of participation in the unit, or farm their interest out to a third party. If these interests are carried by the operator, Section 15-72-304(b)(2) provides that if the well is productive, the operator may retain the revenue allocated to those non-participating interests until it reaches an amount those parties would have paid for participating, "plus an additional sum to be fixed by the Commission."

**Colorado** – According to Colorado oil and gas code 34-60-116, an unleased mineral owner who has refused a reasonable offer to lease shall receive a landowner's proportionate royalty of 12.5%, until such time as the consenting owners recover, only out of the unleased mineral owner's proportionate 7/8ths share of production from 200% of that portion of the costs and expenses of staking, well site preparation, obtaining right-of-way, rigging up, drilling, reworking, deepening or plugging back, testing, and completing the well, after deducting any cash contribution received by the consenting owners, and 200% of that portion of the cost of equipment in the well, including the wellhead connections.

**Louisiana** – The Louisiana Office of Conservation, Oil, and Gas Division ("LOC") has specific authority to establish drilling units and to force pool the interests of owners, if necessary, in order for the proper development of oil and gas in the state.

Assume a party refuses to sign a lease in Louisiana, or the owner can't be found to lease. There are two options available to the owner. First, they can choose to be treated much like a non-operating oil company in the drilling unit. In other words, they would pay their share of the drilling costs and receive their share of all production. Assume the owner has an interest in 40 acres and the unit size is 640 acres. Assume the drilling costs are estimated to be \$4,500,000. The unleased owner's share of costs would be  $40/640 \times \$4,500,000 = \$281,250$ . It is safe to assume that most unleased owners would not choose this option! Secondly, the owner can be forced pooled. In Louisiana, being forced pooled does not carry with it a greater penalty than the owner's share of well costs. Therefore, during the initial payout period, the forced pooled owner will not receive any royalty from the well. Since the participating oil companies must pay for the unleased owner's share of drilling costs, they are entitled to receive the owner's revenue during the payout period.

After the well pays out, the forced pooled owner will receive their 8/8ths portion of production. As in the example, the owner would receive  $40/640 = 6.25\%$  of all production. After payout, the owner is then responsible to pay their share of costs associated with further operations. In many cases, the owner's share of production is netted against their share of costs.

**Montana** – Once the applicant has made an unsuccessful, good faith attempt to voluntarily pool the interests within the spacing unit, the interest can be force pooled. If the owner of an oil and gas interest is unleased and refuses to pay its share of costs, then it is considered to own a landowner's royalty equal to 1/8th of the owner's proportionate share of production from the well until costs are recovered - 100% of the refusing owner's share of newly acquired surface equipment plus 100% of the refusing owner's share of the cost of operation of the well and 200% of the refusing owner's share of the costs and expenses of drilling, reworking, deepening or plugging back, testing, and completing the well, MCA § 82-11-202.

**New Mexico** – 19.15.13.7: A "pooled working interest" means a working interest or unleased mineral interest that is pooled by division or commission order and not by voluntary agreement of the owner of the interest, except for an unleased mineral interest on federal, state, or tribal lands. Compulsory pooling orders may provide for the recovery, out of the share of production allocable to the working interest of a party that elects not to pay its proportionate share of well costs in advance, in addition to reasonable well costs and costs of supervision and management, of a charge for risk associated with the drilling, completion, or working over and re-completion of each unit well for which the order provides. Unless otherwise ordered pursuant to Subsection D of 19.15.13.8 NMAC, the charge for risk is 200% of well costs. Well costs shall include the reasonable costs of drilling, reworking, diverting, deepening, plugging back, and testing the well; completing the well in a formation pooled by the order; and equipping the well for production.

**New York** – Article 23.Title 9 § 23-0901: The integrated royalty owner shall receive a royalty equal to the lowest royalty in an existing lease in the spacing unit, but no less than one-eighth.

**North Dakota** – North Dakota has a forced pooling statute which permits the operator to force pool any unleased mineral interest after there has been an unsuccessful, good faith attempt to voluntarily pool the interests. According to N.D.C.C. §38-18-08, the unleased mineral owner is entitled to an acreage weighted average royalty interest of the leased tracts within the spacing unit. However, any unleased owner who refuses to participate and pay its proportionate share of the costs is subject to a 100% plus 50% risk penalty.

**Oklahoma** – Before an oil company can propose a well to the Oklahoma Corporation Commission ("OCC"), they must first attempt to reach agreement with all the other owners to either lease their minerals or have them participate in the drilling of the well. Since, owners could potentially stop the drilling of a well by refusing to sign a lease or by refusing to

participate, the OCC has created a method whereby these owners can be forced to become a part of the operations.

The operator must search county records and other sources to determine all appropriate owners. They must attempt to locate correct addresses for these owners. They must file an application naming the owners as respondents and a notice must be mailed and published giving the respondents notice of the time, place, and purpose of the hearing. During the hearing, the Administrative Law Judge (ALJ) will determine if the applicant operator has made a good faith effort to bargain with the respondents and will determine, from testimony, the fair market value of the mineral interests in the unit. This will include bonus amounts paid and royalty negotiated within the unit and the eight surrounding units within the last year. The fair market value will determine both bonus and royalty to be given to a forced pooled owner. Unleased mineral owners are entitled to a statutory one-eighth royalty; however, the fair market value is often greater than a one-eighth royalty. Frequently, the owner will be offered less cash and more overriding royalty.

**Texas** – Force pooling in Texas is not the preferential method of dealing with unleased mineral owners. Even though the state enacted the Mineral Interest Pooling Act in 1965, the Texas Railroad Commission (“TRRC”) rarely uses forced pooling and if the Act is invoked, forced pooling is rarely granted. Instead, the TRRC encourages mineral owners to voluntarily agree to be pooled through a pooling agreement or oil and gas lease.

If a mineral owner can’t be found or refuses to voluntarily agree to be pooled and force pooling is not granted, his or her options are as follows:

An unleased mineral owner who owns an *undivided* mineral interest in the drillsite tract will receive his or her proportionate share of 8/8ths production after payout of the well. Costs associated with payout are land work, drilling, testing, completing, equipping, and operating the unit well. *Cox v. Davison*, 397 S.W.2d 200 (Tex. 1965), 24 O&GR 128.

An unleased mineral co-tenant who owns an undivided mineral interest in a non-drillsite tract which has been pooled with the drillsite tract is not entitled to any part of production. *Superior Oil Co. v. Roberts*, 398 S.W.2d 276 (Tex. 1966), 24 O&GR 77 and *Hunt Oil Co. v. Moore*, 656 S.W.2d 634 (Tex. Civ. App.-Tyler 1983, writ ref’d n.r.e.), 79 O&GR 576.

**West Virginia** – Shallow Gas Wells §22C-8-11. “If no voluntary pooling agreement is reached prior to or during the hearing held pursuant to subsection (b), section ten of this article, then at such hearing the board shall also determine the pooling of interests in the drilling unit. In no event shall drilling be initiated or completed on any tract where the gas underlying such tract has not been severed from the surface thereof by deed, lease or

other title document, without the written consent of the person who owns such tract. Any order of the board pooling the separately owned interests in the gas to be produced from the drilling unit shall be upon terms and conditions which are just and equitable.”

Deep wells §22C-9-7. “When two or more separately owned tracts are embraced within a drilling unit, or when there are separately owned interests in all or a part of a drilling unit, the interested persons may pool their tracts or interests for the development and operation of the drilling unit. In the absence of voluntary pooling and upon application of any operator having an interest in the drilling unit, the commission shall set a hearing and provide notice to all interested parties. After the hearing, the commission shall enter an order pooling all tracts or interests in the drilling unit for the development and operation thereof and for sharing production therefrom. Each such pooling order shall be upon terms and conditions which are just and reasonable and in no event shall drilling be initiated on the tract of an unleased owner without the owner's written consent.”

**Scenario:**



Heath

**Several years ago, Heath inherited both surface and subsurface lands from his father's estate. He owns the land as his sole and separate property. He does not trust "Big Oil" and has refused to sign an oil and gas Lease.**

**In order to pool Heath's interest into a proposed unit, what can be done if this land was located in**

- Louisiana**
- North Dakota**
- West Virginia**

ANSWER: In Louisiana, Heath's options are to participate and pay his share of the drilling costs and receive his share of all production, or to be forced pooled and receive no royalty from the well during the payout period. After the well pays out, Heath would receive his 8/8ths portion of production. In North Dakota, Heath would be entitled to an acreage weighted average royalty interest of the leased tracts within the spacing unit. However, any unleased owner who refuses to participate and pay its proportionate share of the costs is subject to a 100% plus 50% risk penalty. In North Dakota, the unleased mineral owner is entitled to an acreage weighted average royalty interest of the leased tracts within the spacing unit. For deep wells in West Virginia, pooling shall be based on terms and conditions which are just and reasonable, and in no event shall drilling be initiated on the tract of an unleased owner without the owner's written consent.

## Rule Against Perpetuities

The rule against perpetuities is one of the most complicated legal concepts ever developed. It began in England around 1680 in an attempt to keep landowners from controlling the ownership of their property for generations (into perpetuity) after the original owner was dead and buried. This attempt to control ownership can be referred to as controlling the land by the “dead hand.” Prior to the rule being implemented, in an effort to avoid certain death taxes, feudal lords would place their land in trust forever, so that future generations could live off of the land without ever owning the land.

The rule against this perpetual ownership thus established a reasonable time period for the future interest to vest. This time period is “lives in being plus 21.”

There are two keys to understanding how the rule works:

First, one must identify who the “lives in being” is referring to. The “lives in being” do not necessarily refer to the original grantor but rather the last identifiable individual (the “measuring lives”) living at the time the interest was created and places a limit of no greater than 21 years after the death of this person. With this rule, a grantor can convey land to his son, grandson, or great-grandson as long as they are alive at the time of the conveyance. The rule comes in to play when an owner attempts to direct ownership to those who are yet unborn.

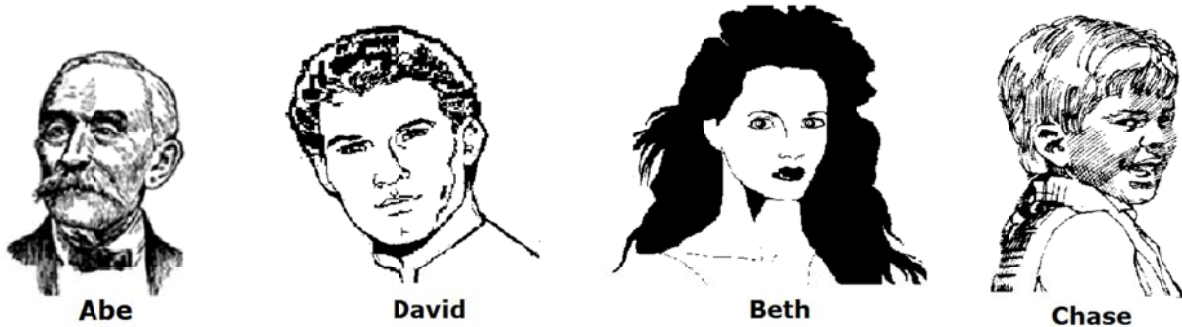
Secondly, determine if there is any limitation on when the person who is holding the future interest can actually vest in the property. (Holding the future interest and vesting in the property are two different events.) If there is a time restriction or limitation on when the future interest can vest, or if the future interest will vest more than 21 years after the death of the “measuring life,” the conveyance violates the rule and becomes void as to those future interests.

**An example of the rule:** Many years ago, a man named Wellington Burt became one of the richest men in American. He died on March 2, 1919. Prior to his death he created a trust, leaving his *children* and *grandchildren* a yearly allowance. Ninety-two years after the creation of the trust, it dissolved because of the rule against perpetuities. On November 21, 1989, Marion Stone Burt Lansill, the last grandchild (the “measuring life”) that was living during Wellington’s life, died. Keep in mind, the rule comes into play “lives in being plus 21 years”; therefore, the trust dissolved in November, 2010, 21 years after Marion’s death. The great-great-great grandchildren became the beneficiaries of the remaining fortune that had been held in trust.

**Example 2:** Assume that Abe created a trust that stated his fortune would go **“to the benefit of my son David for life, then to benefit David’s widow for life, then outright to David’s children.”** A year later, Abe died.

Assume that David met and married Beth, who had been born after the death of her father-in-law, Abe. A few years later, David and Beth have a son named Chase.

Examine the cast of characters.



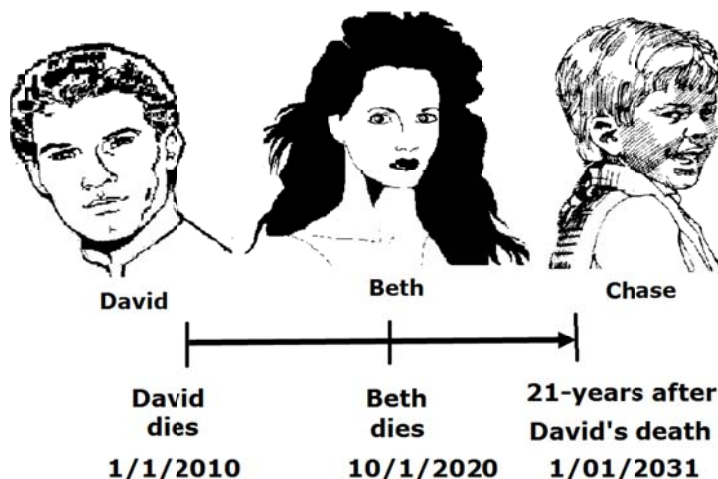
**Circle the party that is the “measuring life?”**

Answer: In this scenario, the measuring life would be David. Beth and Chase are disqualified because they were not living at the time of the creation of the trust. Therefore, the “lives in being plus 21-years” is tied to David.

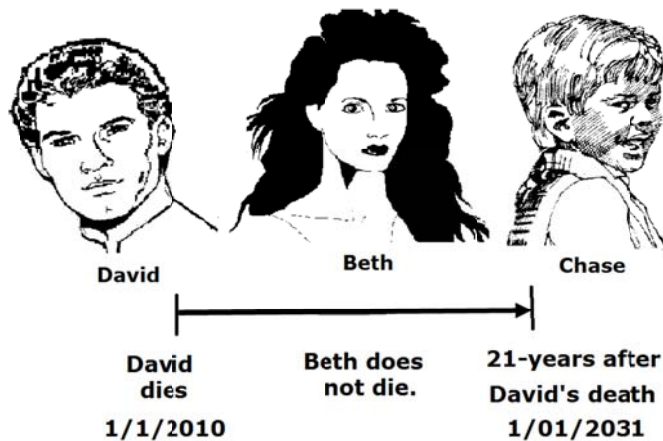
**Example 3:** Next, assume David died and the 21-year clock began to tick. Abe’s trust is to pass first to David, then to David’s wife for her life, then outright to Chase.

Keep in mind, the rule comes into play “lives in being plus 21-years”; therefore, the trust would dissolve 21 years after David’s death.

Question 1: What would be the outcome if Beth died before the 21-year clock went off? \_\_\_\_\_



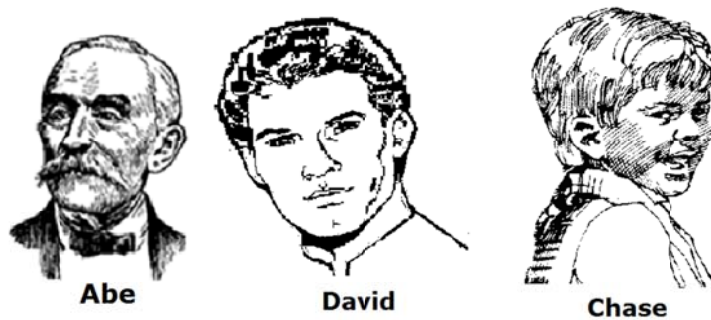
Question 2: What would be the outcome if Beth was still living when the 21-year clock went off? \_\_\_\_\_



ANSWER: If Beth died prior to the 21-year clock going off, the trust would dissolve after Beth's death and Chase, as outlined in the trust, would not receive an interest through the trust. If Beth was living at the end of the 21-year clock, Chase would receive the interest as stated in the trust.

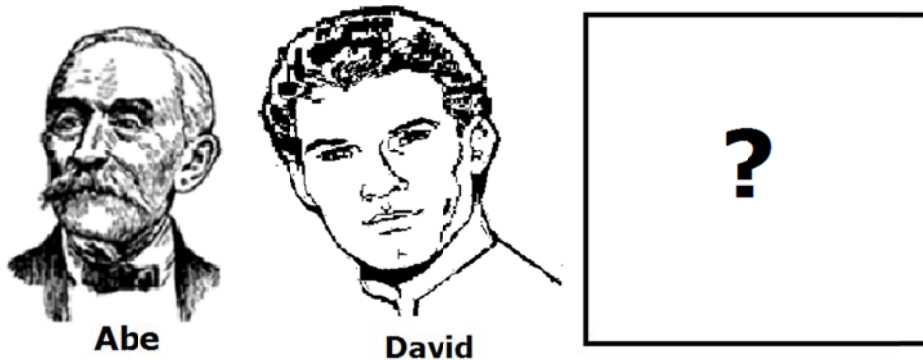
**Read the following scenarios and determine which of the examples would pass under the rule of perpetuity and which would not pass.**

**Scenario 1:** Abe conveyed his property to his son David for life and then to David's child Chase.



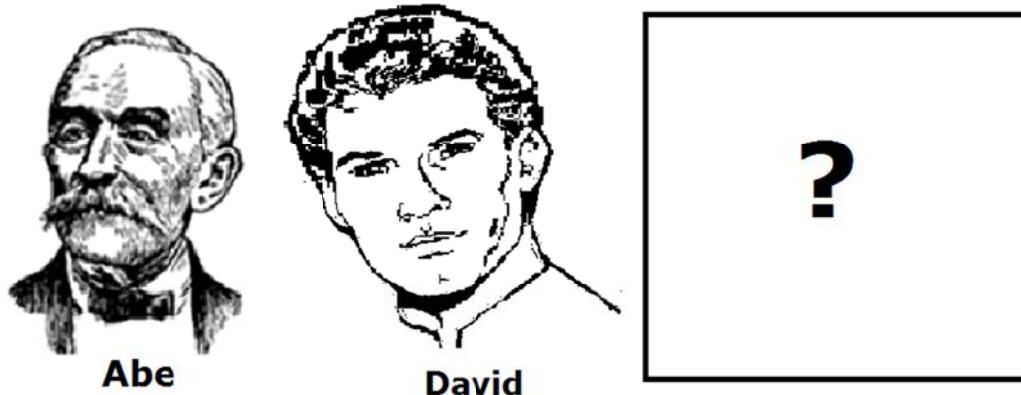
**Abe conveyed his property to his son David for life and then to David's child Chase.**

**Scenario 2:** Abe conveyed his property to his son David for life, and then to David's first child to marry.



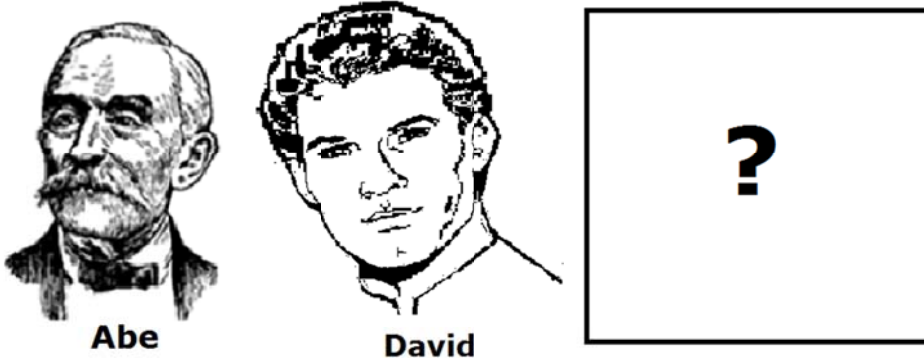
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**Scenario 3:** Abe's living trust states that at his death, David, his son has the right to Abe's property for life. At David's death, the property will vest in David's oldest child.



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ANSWERS:

**Scenario 1** passes the test and is valid under the rule. First, Chase did, in fact, vest in an *interest* to the property at the time the conveyance was created and secondly, because his father David was not the "measuring life," Chase would be the measuring life.

**Scenario 2** would not pass under the rule, but can you determine why? In this example, a condition is set forth that one of David's children must be married in order to receive title to the property. In this example, David would be the measuring life plus 21 years. There is no guarantee that David will ever have children that will marry at least 21 years after his death. Since the conveying language created a condition that might not ever take place, the fact that it could take place would not change the impact of the violation to the rule. In the case of Scenario 2, only the portion of the future grant violated the rule, and only that portion is eliminated from the grant. The grant to David is still legal and effective.

**Scenario 3** would not violate the rule against perpetuities. David is the measuring life plus 21 years. Keep in mind, if David does have a child, the trust states that the oldest child will immediately vest in the property at David's death. They would not have to wait 21-years after David's death. If David has no children, the rule still is not violated. Upon David's death, the property would vest according to David's will, or the laws of descent and distribution.

**Scenario 4** is an example of a situation that would violate the rule. Abe's Last Will and Testament created a future interest, and although David is the measuring life plus 21 years, in this scenario, it is possible that the *vesting* to the land into David's children will occur *more than twenty-one* years after the death of David. Assume David has a child named Chase. Two years later, David is tragically killed. Upon his death, the 21-year clock begins to tick. At the end of the 21-year period, Chase would only be 23 years of age and the will established a vesting age of 25; therefore, the devise of the future interest to David's children is void.

## **Navigable Waters**

The United States Supreme Court ruled that navigable rivers, lakes, and streams have been public since ancient times; that the King of England held such rivers, lakes, and streams for public use during colonial America; that after the Revolutionary War, those colonies took ownership from the British of the land underlying navigable waters, and that under the "Equal Footing Doctrine," any other state entering the Union would have the same ownership rights as the original thirteen states. Therefore, under the equal footing doctrine the Supreme Court ruled that all states received an *implicit grant of all navigable waters*, their shores, beds, and the lands beneath the waters if the waters were navigable at the date of statehood.

This grant extended to the ordinary high-water mark of navigable streams and lakes (commonly referred to as the submerged and submersible land). Navigable waters were not designated at the time of admission. As a result, a critical question of fact always arises as to whether the waters overlying lands in question were navigable at the date of statehood. Ordinarily, the title examiner cannot determine whether or not the waters overlying lands were or were not navigable at statehood. An abstract may show a perfect chain of title from the state, but, if the navigability inquiry is answered in the negative, the state's claim to title is destroyed.

For the land professional, an understanding of this issue can become very important. Ownership of the minerals underlying the rivers, lakes, or streams must be determined. If the waterways are determined to be navigable, the mineral ownership belongs to the state.

### **"Navigable" defined**

In an attempt to determine if rivers, lakes, and streams were navigable at the date of statehood, various federal court cases created the "federal test," a type of template, whereby navigability can be determined.

1. Was the waterway capable of or susceptible to use as a highway for the transportation of people or goods?
2. Was the waterway used for transportation, conducted in customary modes of trade and travel on water?
3. Was the waterway navigable in its natural and ordinary condition?
4. Was the waterway navigable as of the date of statehood?

It is important to note that almost any type of watercraft used or potentially used would be enough to determine navigability. The watercraft's use did not have to occur at statehood, but simply could have occurred.

The National Association for Rivers concludes, "The fact is that even rivers and streams that can be navigated only by small watercraft and logs are still navigable for title purposes, even if they are not navigable for other legal purposes."

**Arkansas** – For many years, a stream was determined to be navigable if it was used for commercial purposes. *Lutesville Sand & Gravel Co. v. McLaughlin*, 181 Ark. 574, 26 S.W.2d 892 (1930). In 1980, the law changed when the State Supreme Court ruled that the Mulberry River was a navigable stream. This river is only used recreationally six months out of a year. During the summer months, the stream dries up. *State v. McElroy*, 268 Ark. 227, 595 S.W.2d 659 (1980). Today, a stream or river can be determined to be navigable whether used for commercial or recreational purposes. If a stream is determined to be non-navigable, then ownership of the land beneath the water belongs to the riparian owner (owner of the land adjoining the stream).

**Colorado** – Colorado acquired title to all lands beneath navigable waters at statehood. *Pollard's Lessee v. Hagan*, 44 U.S. 212 (1845).

**Louisiana** – Louisiana claims ownership to the "historic high water mark of a naturally navigable lake, to the current low water mark of a naturally navigable river or stream, and to all lands in the vicinity of the open gulf directly affected by the ebb and flow of the tides."

**Michigan** – In the state of Michigan, regardless of the navigability of rivers or streams, the riparian owners own to the middle of the stream. *Aalsburg v. Cashion*, 384 Mich 236; 180 NW2d 792 (1970). Except for leases taken prior to April 5, 2002, all drilling for oil and gas beneath the Great Lakes or their connecting waterways has been banned.

**Mississippi** – In Mississippi, the riparian owners adjoining a navigable stream or river own to the deepest point in the channel. *Wilson v. St. Regis Pulp & Paper Corp.* 240 So. 2d 137 (Miss. 1970).

**Montana** – According to state statute, Montana owns all of those lands that lay below the low-water mark; islands and their accretions formed in the riverbeds after statehood; and, abandoned channels formed by avulsion. There are two rivers in Montana that flow through lands that have seen significant oil and gas development. As a result, the state has been very motivated to make a determination as to the ownership of these waterways and has conducted several such studies. In 2010, the state managed 34,706 acres of leased riverbed and island tracts. Oil and gas production from these tracts of land brought in \$1,287,652.

**New York** – "Navigable waters of the state" shall mean all lakes, rivers, streams, and waters within the boundaries of the state and not privately owned, which are navigable in fact or upon which vessels are operated, except all tidewaters bordering on and lying within the boundaries of Nassau and Suffolk counties. NY Code Article 1§2.4.

**North Dakota** – North Dakota title Standard 7-01.1 – "Oil and mineral development in western North Dakota increased the value of subsurface minerals and has made it imperative that a title examiner examine plats and photos, or other evidence, to determine whether the property title to which he is examining has upon it or a portion of it a river, stream, or lake, and to make a determination of whether the same is navigable or non-navigable... absent a legislative determination of navigability, the presumption is in favor of non-navigability. The question of navigability for purposes of title is a federal question to be determined according to federal land and usage. State title to land underlying a navigable river, stream, or lake vests absolutely at the time of its admission to the Union, and after admission is governed by state law. Title to unpatented lands underlying non-navigable waters remained with the United States and is thus subject to patent."

**Oklahoma** – Except for a portion of the Arkansas River between the confluence with the Grand River and the Arkansas state line, all other rivers in the state of Oklahoma have been determined through the courts to be non-navigable. *Vickery v. Yahola Sand and Gravel Co.*, 158 Okla. 120, 12 P.2d 881 (1932).

**Pennsylvania** – The Commonwealth claims title to the "waters of the Commonwealth" in trust for its citizens. *Conneaut Lake Ice Co. v. Quigley*, 225 Pa. 605; 74 A. 648 (1909). It is assumed that this would include all navigable streams and rivers.

**Texas** – All oil and gas minerals that are beneath the Texas coast along the Gulf of Mexico, all land below tidewater, and all the land beneath those river beds that are determined to be navigable, are owned by the state. By statute, all rivers and stream have been deemed to be a "navigable stream" if it is "navigable in fact" or if the average width of the river or stream from

its mouth is more than 30 feet from cutbank to cutbank. *Manry v. Robison*, 122 Tex. 213, 56 S.W.2d 438 (1932), Art. 5302, V.A.T.S., Section 21.001(3), 21.012 and 21.013 (NRC). Texas also claims title to all minerals that are beneath navigable waters found on Permanent School Fund lands.

**Utah** – Navigability is determined as those rivers that “must be regarded as public navigable rivers in law which are navigable in fact. And they are navigable in fact when they are used, or are susceptible of being used, in their ordinary condition, as highways for commerce, over which trade and travel are or may be conducted in the customary modes of trade and travel on water.” *The Daniel Ball*, 10 Wall, 557, 563, 19 L.Ed. 999. Since Utah became a state on January 45, 1896, all bodies of water navigable on that date passed to the state.