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Chapter 2 – What is a Title Opinion?

Costs associated with drilling oil or gas wells can be considerable and any company planning to invest these large amounts of money in such a project would want assurances that their leasehold investments are sound. The customary method in receiving these assurances is through an examination of the public records by a qualified title attorney. The task of the attorney is to accurately examine all title documents, legal instruments, and contracts tied to the tract or tracts of land and then to render a summary of title in the form of a title opinion. This examination and opinion would become the essential link between the public records and the company that acquired and is seeking to develop the oil and gas interests.

After an examination of the chain of title has been completed, a title attorney will submit an official account or report setting forth his or her opinion of the ownership of the tract or tracts of land and accurately calculating the surface, mineral, or leasehold interests of those identified. A very important part of this report will include a list of title issues or title defects and the requirements necessary to satisfy or cure those issues.

Many land professionals have an inaccurate view of why the title opinion is rendered in the first place. Some see its main function as setting forth the leasehold ownership in a given area, establishing what lessees hold what leases, and how costs will be split amount the parties. Others believe it is to set forth and calculate the division of interest so all owners are paid correctly out of production. Although each of the cited reasons are addressed in title opinions, the main purpose of a title opinion is to advise the client of title defects and irregularities that might impair the marketability of title, or might expose the client to litigation, and then to suggest how those defects and irregularities might be cured.

Once the title opinion is rendered, land professionals are given the task of examining and curing those title defects or clouds on title. In order to accomplish this task in an appropriate manner, each of the title requirements should be ranked in a priority status, setting forth what problems might expose the client to the biggest risks. Land professionals should then set about finding the most effective way to solve the defects.

A Drilling Title Opinion

Prior to drilling an oil and gas well, an oil company will have a drilling title opinion prepared. This can also be referred to as an Original Title Opinion or a Base Title Opinion. This report can be prepared from a review of an abstract of title or may be rendered after an examination from the instruments of record that affect the given tract or tracts of land. The latter would be referred to as a "stand up" opinion. The title opinion identifies who would have an interest in the oil, gas, and other minerals in the lands upon which a well is to be drilled. It will identify problems or any issues in each owner's title and make requirements specifying the issues, and will discuss easy to understand solutions so the oil company can be assured that it has the right to drill and produce oil and gas from the lands.

This opinion will generally:

1. summarize the title history of the land, paying special attention to surface ownership, rights-of-way, and surface use issues,
2. analyze the leases covering the land,
3. provide each working interest owner with the percentage of production they will be entitled to receive and their share of costs for operations, and
4. list any requirements that should be satisfied.

The precise interests of royalty and/or overriding royalty owners may or may not be set forth in the drilling title opinion.

A Supplemental Title Opinion

A supplemental title opinion is often rendered, based upon an updated title examination of items that were not originally examined by the attorney, in order to reflect any changes to ownership or to respond to title requirements set out in the original title opinion that have been satisfied by curative items.

If asked to render a supplemental opinion, the curative that resulted in the satisfaction of a requirement should be described. A supplemental opinion which is filled with nothing more than "Requirement Satisfied" comments is of little value to the client if the opinion is needed for additional work at a later date.

Acquisition Opinions

Acquisition opinions are prepared for someone who is intending to purchase oil and gas properties. These opinions are more limited and enable the purchaser to understand what they are purchasing and confirm the seller's title. Many times the scope of these opinions are fashioned according to the

nature of the properties being purchased and are prepared in connection with the design and implementation of a due diligence program to identify the quality and quantity of the properties being acquired.

A Division Order Title Opinion

In the event the oil company finds producible oil or gas on the property, a division order title opinion may be prepared. This opinion is usually based on the prior title opinion, includes an updated record check, and focuses on the persons or entities that are entitled to proceeds from the sale of production from the well and the percentage each is entitled to receive. Again, the opinion identifies problems or issues in each owner's title and makes requirements concerning how to correct those issues, so that those persons can be correctly and accurately paid. The opinion can propose that proceeds attributed to certain owners be held in suspense until title requirements pertaining to those interests be cured.

The division order title opinion is rendered after production has been established, and will:

1. reflect additional changes of ownership and make requirements based on these changes,
2. note previous requirements that have been satisfied, and
3. express the division of royalty, overriding royalty, production payments, net profits interest, and net revenue interest based on a unit basis, if a unit is to be established.

This opinion will analyze agreements that affect a pooled area such as a joint operating agreement, farmouts, joint venture agreements, area of mutual interest agreements, and/or commoditization agreements.

Contents of a Standard Division Order Title Opinion

1. Date that the title opinion was issued
2. Name and address of recipient
3. Legal description of subject property
4. Date through which title is certified
5. Materials examined
6. Ownership of all surface, mineral rights, leasehold interests
7. Comments including the tabulation of leases, tabulation of assignments, easements, encumbrances, and taxes
8. Recapitulation of prior opinions' title requirements and status
9. New title requirements

Lender's Opinions or Security Opinions

Lender's opinions are prepared and addressed to a bank or institution who is lending money secured by a mortgage or other security instrument. The construction of this opinion will differ from the opinions previously cited in that the lender's opinion will be limited to the interest of the borrower, confirm that the lender is acquiring the security for their loan, and will validate that the lender would be able to proceed against the properties in the event of default on the loan. Comments or title requirements found in the lender's opinion will restrict themselves to title related to the interests of the borrower. The opinion will set forth all current oil and gas leases, royalty and other interests that burden the borrower including any liens or encumbrances, the borrower's net revenue interest, and all personal property such as fixtures or production owned by the borrower that is directly tied to the property involved. Also noted will be any agreements or contracts including letter agreements, farmout agreements, operating agreements, joint venture agreements, area of mutual interest agreements, pooling agreements, and unit agreements that would have an effect on the interest.

The Ideal Title Opinion - Anonymous

A New Orleans Lawyer sought an F.H.A. loan for a client. He was told the loan would be granted if he could prove satisfactory title to a parcel of property being offered as collateral. The title to the property dated back to 1803, which took the lawyer three months to track down. After sending the information to the F.H.A., he received the following reply (actual letter):

"Upon review of your letter adjoining your client's loan application, we note that the request is supported by an Abstract of Title. While we compliment the able manner in which you have prepared and presented the application, we must point out that you have only cleared title to the proposed collateral property back to 1803. Before final approval can be accorded, it will be necessary to clear the title back to its origin."

Annoyed, the lawyer responded as follows (actual letter):

"Your letter regarding title in Case No. 189156 has been received. I note that you wish to have title extended further than the 194 years covered by the present application. I was unaware that any educated person in this country, particularly those working in the property area, would not know that Louisiana was purchased by the U.S. from France in 1803, the year of origin identified in our application.

For the edification of uninformed F.H.A. bureaucrats, the title to the

land prior to U.S. ownership was obtained from France, which had acquired it by Right of Conquest from Spain. The land came into possession of Spain by Right of Discovery made in the year 1492 by a sea captain named Christopher Columbus, who had been granted the privilege of seeking a new route to India by the then reigning monarch, Isabella. The good queen, being a pious woman and careful about titles, almost as much as the F.H.A., took the precaution of securing the blessing of the Pope before she sold her jewels to fund Columbus' expedition.

Now the Pope, as I'm sure you know, is the emissary of Jesus Christ, The Son of God. And God, it is commonly accepted, created this world. Therefore, I believe it is safe to presume that He also made that part of the World called Louisiana. He, therefore, would be the owner of origin. I hope you find His original claim to be satisfactory. Now, May we have our loan?"

The loan was granted!

What is Title Opinion Curative?

The word "cure" is most often associated with health. A person is diagnosed with an ailment and the examining physician sets forth the steps needed for the person to be cured from the issue. The steps needed to cure the patient would vary depending on what was going on. If the patient's ailment was minor, the treatment might simply be to drink lots of water and get a lot of rest. A different malady might require a medication along with water and rest. Other ailments might be more serious and require a minor surgery. Some illnesses would be so serious that the attending physician would not have the skill or resources needed to cure the patient. The patient would be send to a specialist or to a hospital for treatment.

Curing defective or unmarketable title is much the same as what would happen in a doctor's office or a hospital. The examining title attorney is acting much the same as an attending physician giving a patient a physical examination. In an attempt to diagnose any problems, he or she would make an initial examination of all title. If ailments in title exist, the attorney would list them in the title opinion, along with a detailed plan for how each item should be cured. A handful of the title defects might be such minor issues that time itself would take care of the ailment. Others might require some action on the part of the land professional. Others might be more serious and take more time to cure with greater attention given to the defect. Others would be so grave that no title attorney or land professional could cure the issue. Instead, the only cure would be the court.

Three Actions or Remedies to Satisfy Title Defects

Usually, curing title defects can take place in one of three manners.

First, title statutes that are in place can cure some title defects. The examining attorney will identify those title defects solved by a title statute and will normally state that no further action is required as to those defects.

Secondly, the procurement of certain curative documents may be necessary in order to certain cure title defects. It is safe to assume that the majority of title defects will be resolved through this method. The documents needed to cure these types of defects are varied and normally referred to as title curative documents. They range from items needed to cure minor issues to those that would be considered more major in status. When approaching these defects, the land professional will use what is known as a “business risk” standard in order to determine which defects are most critical to address and which might be waived.

Lastly, there are some title defects that the land professional cannot cure. Judicial action would be required.

GENERAL RULE

There are three general actions or remedies possible to satisfy title defects. They are:

1. title statutes,
2. judicial action, and
3. the procurement of curative documents.

Once the opinion is rendered, it becomes the responsibility of the landman, land technician, division order analyst, or lease administrator to determine what actions will be taken to cure title.

Business Risk Classification of Title Requirements

Gaining an understanding of how to evaluate the “business risk” of each requirement is as important as knowing how to cure the issue. Many title requirements can be cured in more than one way. As the requirement is assessed, the land professional must examine two aspects of the requirement. First, the item must be given a rating of importance. A category of 1-4 is suggested below. Category 4 would have the greatest degree of importance. Secondly, thought must be given to the way in which the item can be cured. Remember, many title requirements can be cured in more than one way. The higher degree of importance placed on having the item cured might dictate the way in which the item is to be cured.

The Decree of Importance in Having the Item Cured

Category 4	
Category 3	
Category 2	
Category 1	

Method used to Cure item

Result

Method used to Cure item	Result
Method 1 Waive Item costing no time	Item still uncured
Method 2 Acquire Minor Curative possibly costing little time	Item could be fixed but not totally cured
Method 3 Acquire Solid Curative possibly costing greater time	Item is cured

Using the chart, place the following items in a category of importance and then determine which method should be used to cure the item.

Scenario 1: Your Oil Company has acquired a lease on a tract of land. Courthouse records show an older unreleased lease on the same tract of land. It appears that the lease expired 7 years ago. The mineral owner claims that no drilling has ever occurred on the lands. Assume that the signing bonus your company paid to the owner was \$25 per acre and the leased lands are known to be in a marginally productive area.

What category of importance would you rate this item? _____

What method of curing would seem appropriate? _____

(In a case like this, the unreleased lease may, in fact, be holding the land by production. The land professional would clearly want to investigate this matter further. An affidavit of non-production or non-development would be in order. Also an investigation from the state regulatory commission should be done to confirm that no production has been reported from the older lease. This may become determined to be a Category 3 item. Method 2 may be used in an attempt to address the business risk.)

Scenario 2: Assume the same circumstances as found in Scenario 1 except the signing bonus your company paid was \$2,500 per acre and the leased lands are known to be a drill site.

What category of importance would you rate this item? _____

What method of curing would seem appropriate? _____

(In a case like this, a higher degree of risk is at stake and a higher degree of curative would be in order. This clearly would be a Category 4 requirement. An affidavit of non-production or non-development with an investigation from the state regulatory commission that no drilling or production has taken place would be in order. Because of the added risk factor a release on the older lease would also be advisable.)

Scenario 3: Assume Your Oil Company wishes to lease and drill a well on a tract of land that contains an unreleased oil and gas lease. The land is in a very competitive area. According to the primary term of the unreleased

lease, the lease will not expire for eighteen months; however the mineral owner claims that the lease was terminated because the lessee failed to make delay rental payments. You are willing to pay the mineral owner \$2,500 per acre and, if the older lease has terminated, you wish to drill the well in six months.

What category of importance would you rate this item? _____

What method of curing would seem appropriate? _____

(In a case like this, an even higher degree of risk is at stake. An affidavit of non-production or non-development would be in order along with an investigation from the state regulatory commission, but because of the added risk factor a release on the older lease would also be advisable. There is a good chance that this release cannot be secured. Because of the potential risk, if this cannot be accomplished, a court proceeding may be the only available method of curing this title issue.)

Scenario 4: Assume a mineral owner has recently died. They have been receiving monthly royalty checks that average \$25.00 per month from a well that your company operates. Your company was notified of the person's death by the decedent's surviving spouse. There is a last will and testament whereby all of the decedent's estate is to pass to the surviving spouse. The spouse is not going to probate the estate because of cost.

What category of importance would you rate this item? _____

What method of curing would seem appropriate? _____

(In a case like this, because the average monthly royalty associated with the interest is so low the business risk for the company is not extreme. This may be ranked as a Category 2 item. Many companies would allow the interest to be transferred to the appropriate heirs through an affidavit of death and heirship. This method of curing title falls in the Method 2 category.)

Caution

If a requirement carries a high business risk but is deemed as having little or no business risk, the consequence can become significant.

Scenario 5: Assume the same circumstances as found in Scenario 3 except the monthly royalty checks average \$2,000 per month. Would the item move up in its degree of important to be cured? Would the method used to

cure the item change? Assume the monthly checks average \$50 but you know your company is drilling new and very successful wells in new horizons in the area. Would the item move up in its degree of important to be cured? Would the method used to cure the item change?

Scenario 6: In Texas, when a given tract of land is burdened by a non-participating royalty interest, that interest cannot be pooled without the consent of the NPRI owner. A ratification of the oil and gas lease containing pooling provisions or of the unit declaration, or a document granting consent to pool, should be obtained from the owner of the NPRI and filed of record. If not, the outcome can be significant.

Mattax Oil and Gas has recently secured a lease from Harriet Parsons covering Tract B from the following plat.

The following is an order of events surrounding the issue:

1. 100% of the minerals under Tract B are owned by Harriet Parsons. At the time of leasing, Harriet Parsons negotiated a 3/16th lease royalty.
2. Prior to leasing, Harriet Parsons had conveyed, through a Royalty Conveyance, an 18.75% non-participating royalty to her daughter, Marilyn Parsons.
3. Because Mattax wishes to begin drilling operations within the next 4 months, a drilling title opinion was rendered. The title attorney has established the following title requirement:

Tract A: 160-acres Lease owned by ABC Oil Company	Tract B: 160-acres Lease owned by Mattax Oil
Tract C: 160-acres Lease owned by Oilco, Inc	Tract D: 160-acres Lease owned by Petras, Inc

Unit boundary in this Texas well = 640-acres

Requirement: There are four mineral owners within the unit. Harriet Parsons owns all (100%) of the mineral interest in the NE4 and leased same to Mattax Oil and Gas on May 10, 2012, negotiating a 3/16th royalty interest. At entry 4 of Abstract 33246 in a 1999 deed recorded in Book 45, Page 378, Harriet Parsons conveyed an 18.75% non-participating royalty interest to her daughter Marilyn Parsons. The Parsons' property is the location of the drillsite. Since Mattax Oil and Gas owns 25% of the unit they will be responsible to pay 25% of the costs for drilling the well. If the well is drilled and completed in the NE/4 of the section, Mattax's payment of NPRI to Marilyn Parsons would be a full 18.75%. We require that Marilyn Parsons either ratify the lease or sign a unit designation in order for Mattax to reduce

Marilyn's 18.75% NPRI proportionately within the unit. Once the ratification or consent to pool has been obtained, Marilyn Parsons' unit net revenue will be proportionately reduced to 4.6875%.

Consider the business risk in this scenario. As can be seen, the business risk for Mattax to proceed without first obtaining the required curative items would be significant.

Classification of Requirements

In a title opinion, each requirement should include an indication of the severity of the business risk and the importance of it being satisfied. The title attorney will also make suggestions as to how the defect can be satisfied. If more than one curative action can be taken, the various options might be suggested. As already stated, not all title defects are as severe as one another. Therefore, each title requirement will fall within one of four general categories. Because title defects are often based on someone's opinion, the category in which a defect might be placed is often subjective.

1. **Critical Requirements** – These requirements "*must be*" resolved. If not, the consequences could be critical. If uncured, an operator might face severe liability issues, including trespass; suit based on incorrect payments out of production; or, perceived illegal actions on the part of the operator.
2. **Necessary Requirements** – These requirements, although important, would not fall into the "*must be*" category but rather in the "*should be*" resolved category and should be fixed before operations take place. The curative documents can be procured in light of the time and expense needed to cure the items.
3. **Temporarily Waivable Requirements** – A temporarily waivable requirement might seem as critical as those cited in the first instance; however, these requirements can wait to be cured pending the outcome of the proposed operation. Once the drilling operation is successful and before payments go out the door, the title issue should be cured.
4. **Waivable Requirements** – These requirements would constitute little or no risk to the operator, thus could be waived with no action necessary on the part of the land professional.

Once the land professional has placed each of the title requirements in the appropriate category, appropriate steps of action coupled with appropriate curative documents should be used in an attempt to cure the title defects.

In What General Category would each of these Requirements Fall?

Review each of the following five title requirements, placing each in one of the four categories. Keep in mind that the answers could become debatable because placing a given requirement in a category can become subjective. However, in your opinion, in which of the four categories would you place each of these requirements?

Requirement #1:

Rodney D. Rose acquired his interest in Lot 6 and NE/4NE/4, by two deeds from John Meagher. The Deed dated December 17, 2005, had a defective acknowledgment as it did not contain a statement as to the residence of Mary Marshall, the Notary Public.

In which category would you place this requirement?

- Critical
- Necessary
- Temporarily Waivable
- Waivable

ANSWER: The title attorney went on to say, "The deed *should be* properly re-acknowledged and re-recorded."

Notice the words "should be." It appears that the title attorney is placing this in the necessary category. Although the effect of a defective acknowledgment varies from state to state, in some states, the instrument is not entitled to recording and is not constructive notice to parties outside the instrument. What this means is that even though the instrument has been recorded, it is as if it does not appear in the courthouse records. Statutes of a number of states will grandfather in defective acknowledgments after they have been of record for a specified number of years, or if they were recorded prior to a certain date.

Requirement #2:

Holly Otis, by and through her attorney in fact, Jason Otis, by Warranty Deed dated November 10, 2002, recorded in Volume 125, page 756, Deed Records, conveyed a 1/8th interest in the surface and a 1/8th mineral interest in Section 18 to Tom Curtis. No power of attorney from Holly Otis to Jason Otis appears in the material examined.

In which category would you place this requirement?

- Critical
- Necessary
- Temporarily Waivable
- Waivable

ANSWER: The title attorney went on to say, "We *should be* furnished with a certified copy of the power of attorney from Holly Otis to Jason Otis." It appears that this falls in the necessary category.

Requirement #3:

A Conveyance from Dolly Edmonds to Jimmy Fox dated March 24, 1999, Volume 655, page 7 references a conveyance dated April 1, 1975, recorded in Volume 555, page 2, Deed Records from Aztec Oil to Dolly Edmonds conveying a 110/640 mineral interest. At the time of the conveyance to Dolly Edmonds, Aztec only owned a 55/640 mineral interest. Through the conveyance to Jimmy Fox, Dolly Edmonds is purportedly conveying more interest to Fox that she received from the Aztec conveyance.

In which category would you place this requirement?

- Critical
- Necessary
- Temporarily Waivable
- Waivable

ANSWER: The title attorney went on to say, "*In the event of production*, Aztec, Dolly Edmonds, and Jimmy Fox should enter into a Stipulation of Interest which reflects what each claims in and to the interests originally conveyed by Aztec to Edmonds." With the words, "in the event of production" it appears that the title attorney is placing this in the third category or the temporarily waivable category.

Requirement #4:

A surface investigation of the captioned lands should be made to determine if there are any claims to title which would adversely affect the interests shown herein and which would not be reflected from the records examined.

In which category would you place this requirement?

- Critical
- Necessary

- Temporarily Waivable
- Waivable

ANSWER: The title attorney went on to say, "This inspection *must* include an investigation relative to the existence or nonexistence of any highway or railroad right-of-way, schools, cemeteries, placer and lode mining locations, if any, located at any time on the captioned lands and *must* take place prior to any operations on said lands." Notice the word "must." Because of the liability issues surrounding trespass, adverse possession, wetlands, burial grounds, endangered species lands, this requirement must be met and it appears that the title attorney places this in the highest category or the critical category. Keep in mind, none of these issues can be determined from the courthouse records.

Requirement #5:

In preparation of this Division Order Title Opinion, we have assumed that Oil and Gas Lease No. 1 is being properly maintained by production.

In which category would you place this requirement?

- Critical
- Necessary
- Temporarily Waivable
- Waivable

ANSWER: The title attorney went on to say, "We recommend that you verify with the Minerals Management Service that the lease account for Oil and Gas Lease No. 1 is in good standing to effectively maintain the oil and gas lease." Although there is no direct indication in which category the title attorney is placing this issue, it appears to be of some significance and should probably be placed in the critical arena, being taken care prior to any type of operations.

Comments or Advisory Requirements

Many title opinions will contain an area that lists "comments" or "advisory requirements" separately from actual title requirements. Those listed comments are there to discuss elements that affect the quality of title or help in interpreting the title. Comments do not set forth any given title defect that must receive curative attention.

The value of reading each comment is to gain a fuller understanding of the

issues that surround the title requirements. They may help the reader understand how interests are calculated, the distribution of burdens, assumptions concerning payout elections, and the interests covered by reason of past curative documents.

There are times when comments are included in the requirement section of a title opinion, making it difficult, at times, to distinguish a comment from an actual requirement.

Examples of Comments:

1. In calculating interests herein, we have used the following acreage amounts in the respective tracts, as shown by references in the abstracts and files: Tract 1 = 23.657 acres, Tract 2 - 55.77 acres.
2. It appears that all delay rental payments have been properly paid through the commencement of drilling the McGregor 1-36 well. The effect is that all leases will be extended by the production from the unit well.
3. Completion Report indicates that the Cherokee is spaced as a 640 acre unit by Order No. 185364.
4. Mortgage:

Dated: May 15, 2007

Recorded: Book 1337, Page 125

Mortgagor: Gale Harrison

Mortgagee: Paul Reynolds

Description: SW/4 of Section 13, T13N, R22W

Comment: The above mortgage constitutes a lien on the mineral interest shown owned herein by George Harrison, Wallace Harrison, Rose Harrison, and Violet Carl. In connection with the above unreleased mortgage, a Lis Pendens Notice appears filed of record which is a mortgage foreclosure suite foreclosing the above mortgage. Please refer to Objection and Requirement in regards thereto.