
# ARLINGTON, TEXAS

## AAPL 2021 ANNUAL MEETING

*PROFESSIONAL DEVELOPMENT AND LAND CONFERENCE*

AAPL
Powering The Profession

# Gerald Walrath


AAPL 2021 **ANNUAL MEETING**

AAPL
Powering The Profession

# SO YOU DRILLED A WELL – NOW WHAT?

Gerald W. Walrath

Managing Partner | Kirby, Mathews & Walrath, PLLC


AAPL 2021 **ANNUAL MEETING**

# Property Concept – Estates in Land

The oil and gas lease can generally be considered as a real property interest, with all that entails. See, e.g.

Texas – The oil and gas lease is a fee simple determinable conveyance of minerals to the lessee. *Stephens County v. Mid-Kansas Oil & Gas Co.*, 113 Tex. 160, 254 S.W. 290 (1923); *Natural Gas Pipeline Co. of America v. Pool*, 124 S.W.3d 188, 168 O.&G.R. 199 (Tex. 2003); *In re Devon Energy Production Co.*, 321 S.W.3d 778 (Tex. App.--Tyler 2010).

# Property Concept – Estates in Land (cont.)

Oklahoma – The oil and gas lease is a fee simple determinable conveyance of minerals to the lessee. *Shields v. Moffitt,* 1984 OK42, 683 P.2d 530, 81 O&GR 151; *Mason v. Ladd Petroleum Corp.,* 630 P.2d 1283 (Okla. 1981); *State ex rel. Comm'nrs of the Land Office v. Carter Oil Co.,* 336 P.2d 1086 (1959), 10 O&GR 790. However, there is authority which states that this is not necessarily the case during the secondary term. *Stewart v. Amerada Hess Corp.,* 604 P.2d 854 (Okla. 1980)

North Dakota – Oil and gas leases are interests in real property in North Dakota. *Kittleson v. Grynberg Petroleum Co*., 2016 ND 44, 876 N.W.2d 443.

# Property Concept – Privity of Estate and Contract

- Privity of estate – This is the legal relationship between parties whose estates constitute one estate in law. It also exists when two or more parties hold an interest in the same real property. *Thomson Reuters Practical Law – Glossary*
- Privity of contract – This is the legal relationship that exists between parties to a contract. Only those parties to the contract are bound by the terms of the contract and can enforce the contractual obligations under the contract. A third party that is not a party to the contract does not have privity of contract and cannot enforce the obligations under the contract. *Thomson Reuters Practical Law – Glossary*

# Property Concept – Privity of Estate and Contract (cont.)

Relevance to oil and gas leases –

A lessor and a lessee who owns an interest in the property will be in privity of estate – the lessee's fee simple determinable interest in the property, plus the lessor's retained possibility of reverter, will together constitute the fee interest.

A lessor and a lessee who owns an interest in the property will be in privity of contract by the simple fact of being bound the lease, as the lease contains elements of contract, such as the obligation to pay royalty, or limitations on surface use.

# Co-tenancy – whose provisions to honor?

Fact Pattern I

- A, B, and C each own a 1/3 interest in the surface and minerals of Blackacre.
- A and B execute mirror leases with identical terms. With respect to pipelines, they must be buried below plow depth, the lessee must pay $X.00 per rod to the lessor, and lessee will receive an easement 10’ in width, with the pipeline as the center of the easement.
- C executes a lease on different terms than A and B. With respect to pipelines, they must be buried below plow depth, the lessee must pay $Y.00 per rod to the lessor, and lessee will receive an easement 5’ in width, with the pipeline as the center of the easement.

# Co-tenancy – whose provisions to honor? (cont.)

Fact Pattern I (cont.)

Do you have a problem?

No. The lease terms are not in actual conflict. You may lay your flowlines below plow depth, retaining an easement 5 feet in width. You will pay A and B, and C, their respective rod rates.

# Co-tenancy – whose provisions to honor? (cont.)

Fact Pattern II

- A, B, and C each own a 1/3 interest in the surface and minerals of Blackacre.
- A and B execute mirror leases with identical terms. With respect to pipelines, they must be buried below plow depth, the lessee must pay $X.00 per rod to the lessor, and lessee must lay the pipelines on the shortest route possible to a corner.
- C executes a lease on different terms than A and B. With respect to pipelines, they must be buried below plow depth, the lessee must pay $Y.00 per rod to the lessor, and lessee must lay the pipeline from the wellhead perpendicular to the fence, then along the fence until the pipeline exits the property at a corner.

# Co-tenancy – whose provisions to honor? (cont.)

Fact Pattern II (cont.)

Do you have a problem?

Yes. With respect to the pipeline route, it is not possible to honor both the provisions in the lease executed by A and B – the method described in C's lease will never yield the shortest route.

You must negotiate to amend A and B's lease, amend C's lease, or negotiate a surface use agreement whose pipeline provisions will supersede those enumerated in the lease.

# Co-tenancy – whose provisions to honor? (cont.)

Fact Pattern III

- A owns the surface of Blackacre.
- B owns the minerals of Blackacre
- A executes a surface use agreement. The surface use agreement provides, among its many, many terms, that the tank battery for oil production be limited to 1 acre and contain no more than 4 tanks.
- B executes and oil and gas lease. The lease contains a provision that that the tank battery for oil production be limited to 0.5 acre and contain no more than 2 tanks.

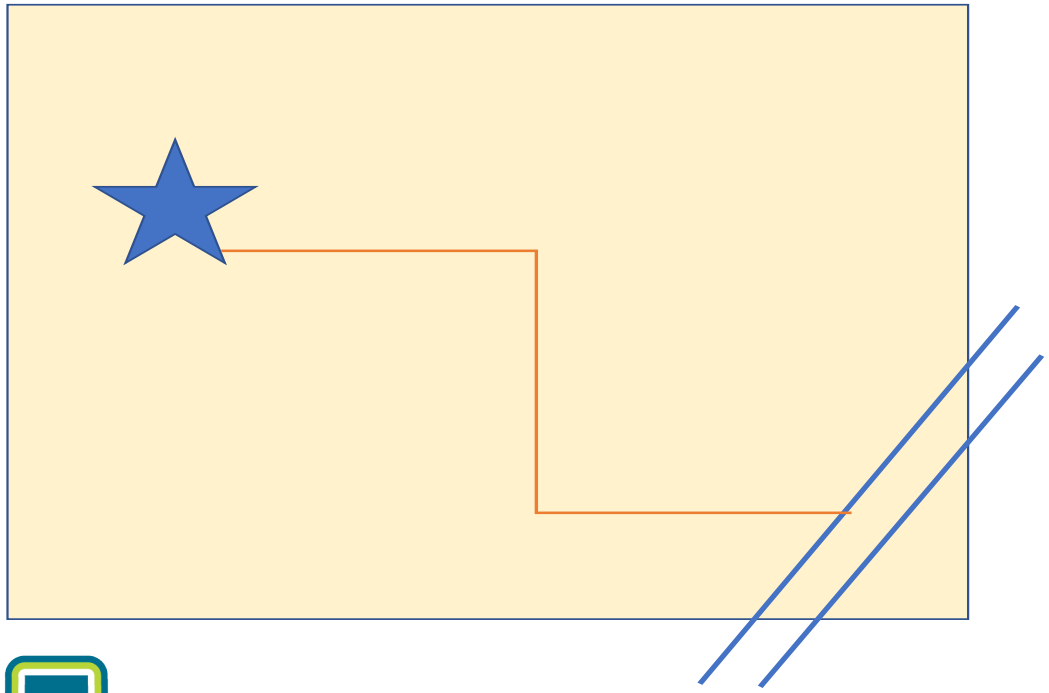
# Co-tenancy – whose provisions to honor? (cont.)

Fact Pattern III (cont.)

Do you have a problem?

No. With respect to the surface estate, B is not in privity of estate with the lessee. Additionally, B has no ability to bind A with respect to the use of the surface, negating privity of contract between B and the lessee.

# Tract Well

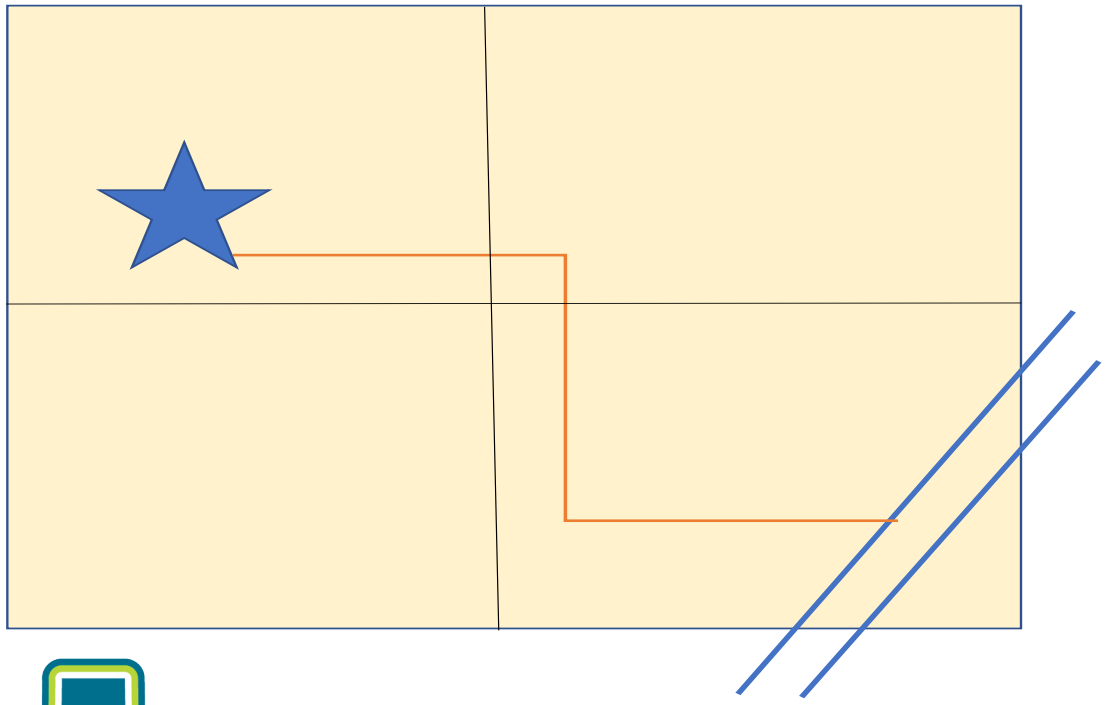


The simplest case.  Everything will be governed by –

a. The lease terms, or

b. The surface use agreement you negotiate

# Unit Well



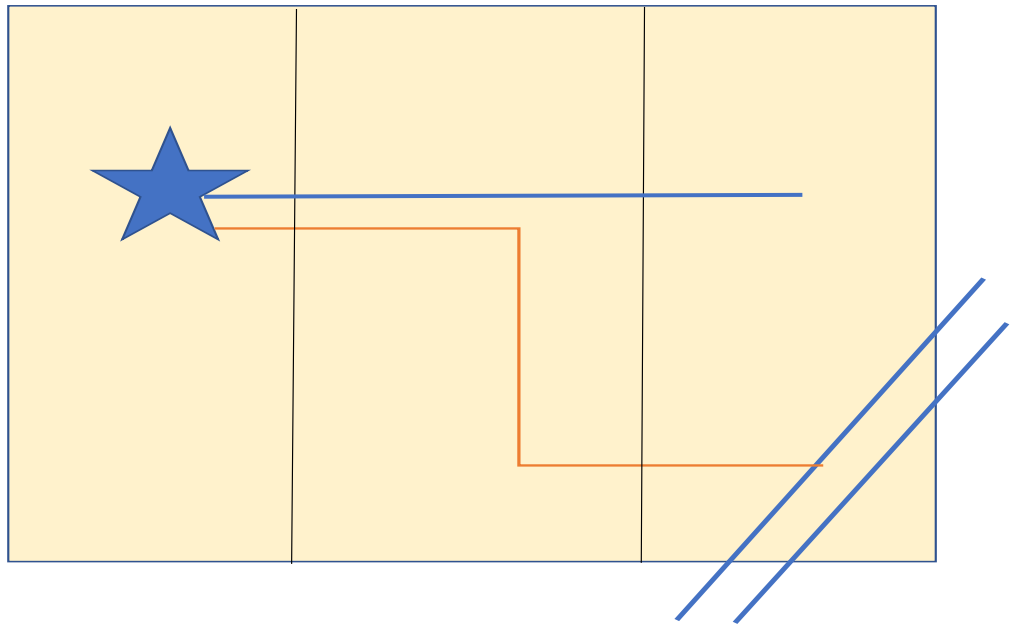
The most common case, whether voluntary or compulsory. You now have more parties in interest, but the basic principles are the same for the unit well as for the tract well.

Everything will be governed by –

a. The lease terms for each tract the flow line crosses or on which the facilities are located, or

b. The surface use agreement you negotiate

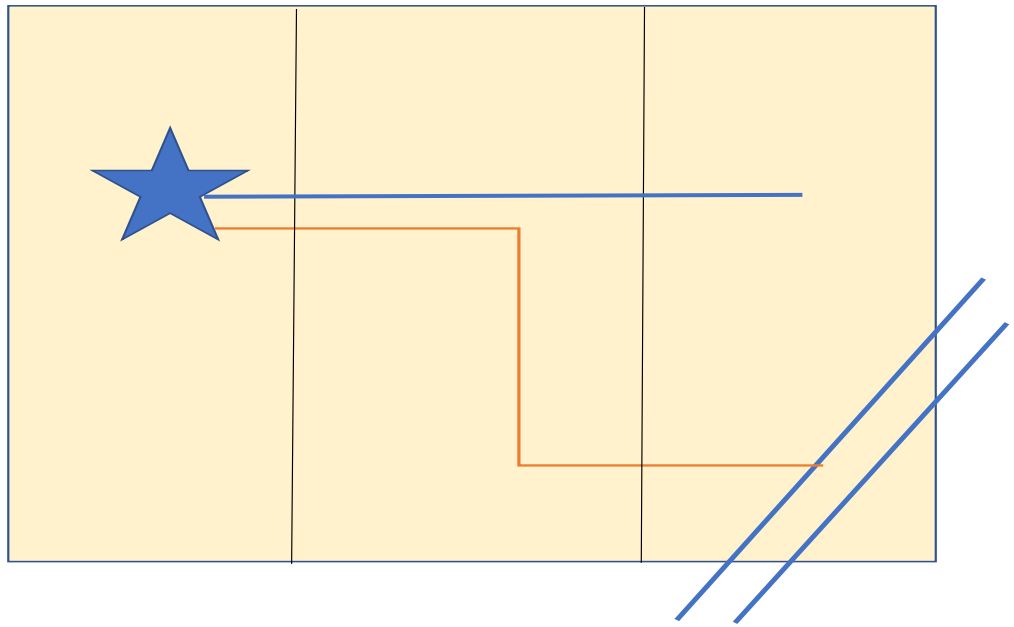
# Allocation Well – Texas Only



"Nothing in the typical mineral lease precludes the lessee from drilling a well horizontally from one border of the Lessor's tract to the other border of the Lessor's tract. This, the lessee who drills such a horizontal well is not purporting to exercise pooling authority and is not slandering the "title" that is the Lessor's right to authorize a cross-conveyance of its royalty interest by pooling."

Ernest E. Smith, Applying Familiar Concepts to New Technology: Under the Traditional Oil and Gas Lease, a Lessee Does Not Need Pooling Authority to Drill a Horizontal Well That Crosses Lease Lines [reprint, first published 2017], 3 Oil & Gas, Nat. Resources & Energy J. 553 (2017), http://digitalcommons.law.ou.edu/onej/vol3/iss2/9

# Allocation Well – Texas Only (cont.)



To paraphrase Professor Smith, the allocation well is no different than a series of horizontal wells; one being located on each tract the lateral crosses.

In terms of necessary agreements, each tract stands on its own, and requires its own agreements, since, in the absence of pooling, you cannot compel one tract to act for the benefit of another tract.

# Pitfalls I, or “Read the Lease”

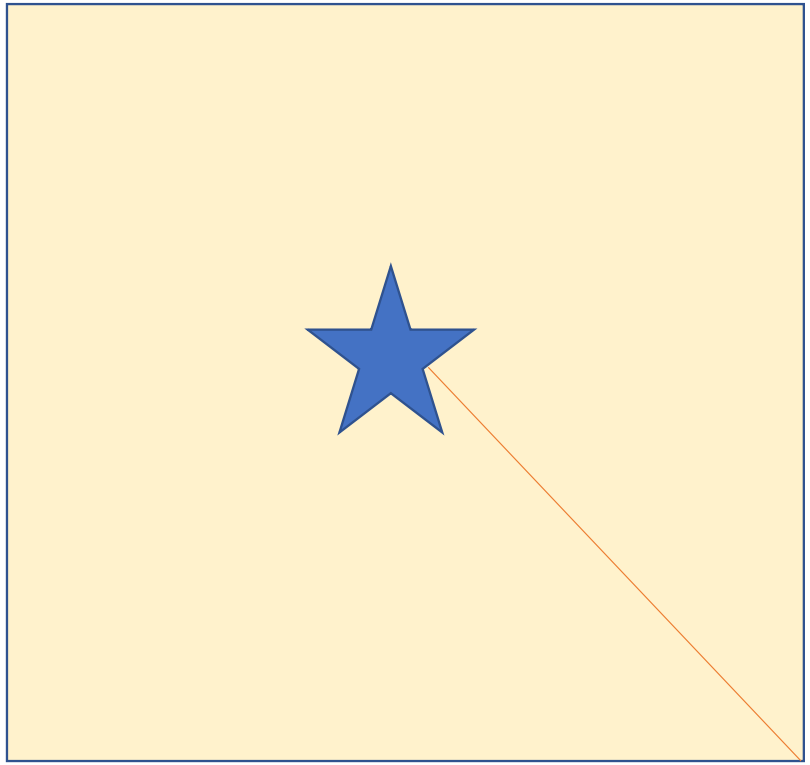
# Pitfalls I, or “Read the Lease” (cont.)

# Pitfalls I, or “Read the Lease” (cont.)

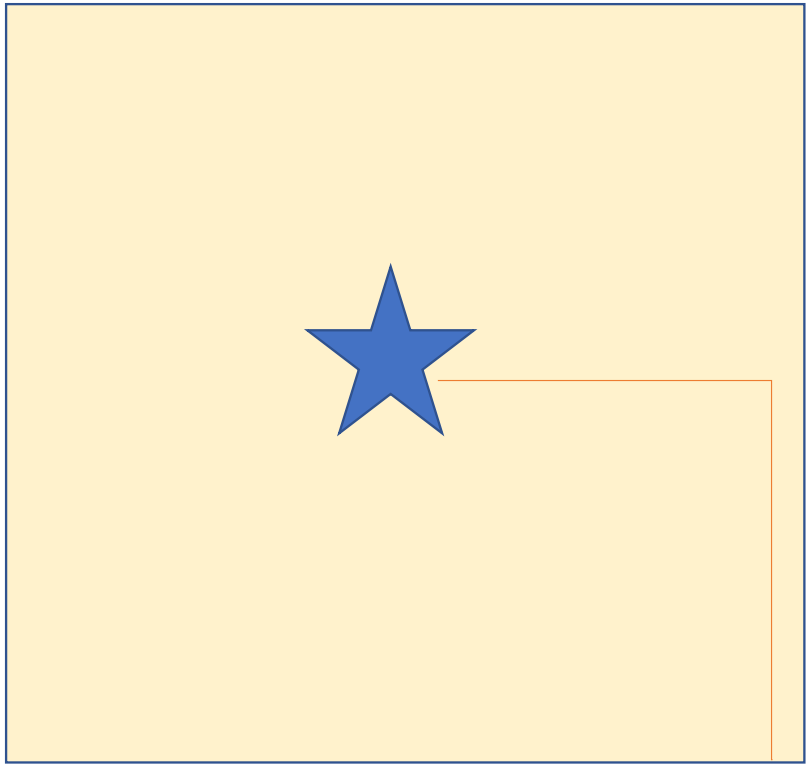
# Pitfalls I, or “Read the Lease” (cont.)

# Pitfalls I, or “Read the Lease” (cont.)

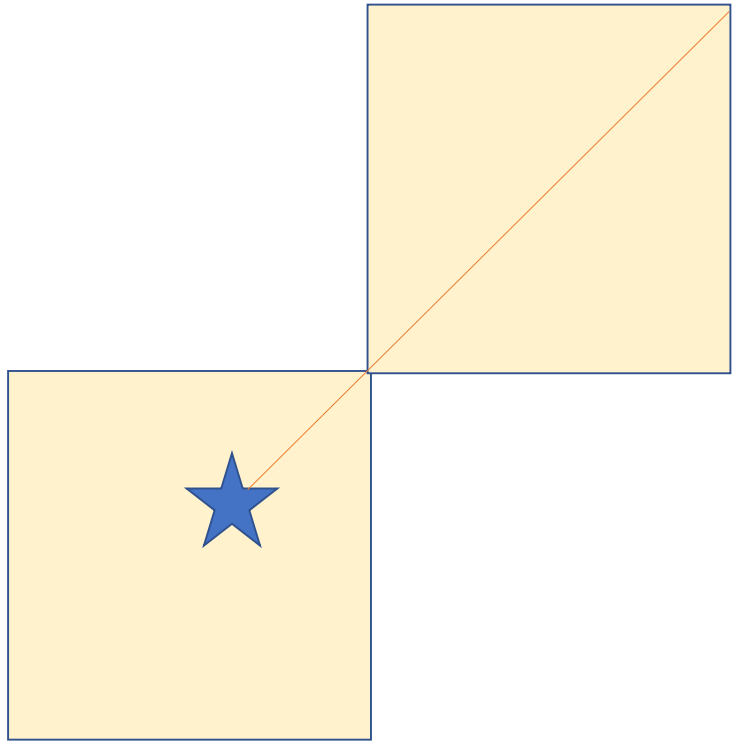
# Pitfalls I, or “Read the Lease” (cont.)



# Pitfalls I, or “Read the Lease” (cont.)



# Pitfalls II, or “Huh?”



# Who are you dealing with?

Property Concept – Co-tenancy

- Co-tenants have the right of equal enjoyment
- This right extends to ALL of the property
- One co-tenant does not have the ability to bind another co-tenant without their consent. *Wilson v. Superior Oil Co.*, 274 S.W.2d 957 (Tex.Civ.App. – Texarkana 1954, writ ref'd n.r.e); *Little v. Williams*, 272 S.W. 2d 409, 413 (Tex.Civ.App. – Austin 1954, writ ref'd n.r.e); 15 Tex.Jur.2d, Co-Tenancy Section 8, p. 163 (1960)

# Who must be a party to the Agreements?

AAPL
Powering The Profession

# Co-Tenants Can Have Conflicting Agendas

# Remedies


WHAT BIG GAME ARE WE STALKING TODAY, MAJOR?
LIBERALS. CHECK AND SEE WHAT THE WILDLIFE GUIDE SAYS ABOUT 'EM.
"THE VANISHING LIBERAL: A BEAST WHICH ONCE THUNDERED ACROSS THE AMERICAN SCENE IN MIGHTY HERDS. RECENTLY HUNTED TO NEAR EXTINCTION."
GOTTA BE ONE LEFT AROUND HERE SOMEWHERES... TRY THE LIBERAL CALL, BOY.
WELFARE! SOLAR POWER! NO NUKES!
RUSTLE RUSTLE
NO NUKES! NO NUKES!
GOTCHA!!
GUN CONTROL! GUN CONTROL!
BLAM!
IT'S A SHAME. THEY'RE MORE FUN THAN BUFFALO.
I THINK I WOUNDED HIM.
OW! SOCIALIZED MEDICINE! SOCIALIZED MEDICINE!

# Remedies (cont.)

If the property is important enough to you, consider voluntary or involuntary partition.

a. Voluntary - contract with a cotenant to fund the legal work for the partition, or buy a co-tenant's share and partition with the other co-tenants.

b. Involuntary - contract with a cotenant to fund the action for partition, or buy a co-tenant's share and sue the other co-tenants for partition.

# The Accommodation Doctrine – Providing a Floor since 1971

## *Getty Oil Co. v. Jones*, 470 S.W.2d 618 (Tex. 1971)

- Issue: Whether a surface use by the lessee was reasonably necessary.
- Facts: John H. Jones, the surface owner, sued for an injunction to restrain Getty Oil Company from using space for pumping units that would prevent him from using an automatic irrigation sprinkler system.
- The surface owner had the burden to show the lessee/operator was unreasonable.

# The Accommodation Doctrine – Providing a Floor since 1971 (cont.)

- Holding: “Where there is an existing use by the surface owner which would otherwise be precluded or impaired, and where under the established practices in the industry there are alternatives available to the lessee whereby the minerals can be recovered, *the rules of reasonable usage of the surface may require the adoption of an alternative by the lessee.*”

# The Accommodation Doctrine – Providing a Floor since 1971 (cont.)

- The Getty Oil case is fairly representative of cases in states in which the accommodation doctrine has been adopted, but have not adopted any form of statutory surface owner protection.
- In light of the dominance of the mineral estate, and now that we know the limits to which we must accommodate the surface use, why make these agreements at all?

# The Accommodation Doctrine – Providing a Floor since 1971 (cont.)

- The purpose of surface use agreements is to limit the operator's liability for its use of the surface. Without the agreements, the operator would be at the mercy of the court to decide whether the use of the surface for post-completion activities, e.g. connections to pipelines, processing facilities and tank batteries, is reasonable.
- Additionally, if an agreement can not be reached, the limit of the temporary restraining order is the reasonable use of the surface.

# Surface Owner Protection Acts

- Certain states have adopted  some form of surface owner protection act. The acts typically provide certain notice requirements, parameters to negotiate surface damages, and if necessary, appraisal and arbitration.
- States which have adopted some form of surface owner protection act include  New Mexico, Oklahoma, Wyoming, North Dakota, Montana, South Dakota, Colorado, Indiana, Illinois, Kentucky, Tennessee, West Virginia. Unsurprisingly, the BLM has their own standard.

# Surface Damages Act - Oklahoma

- Surface Damages Act: §52-318.2 to .9
- Prior to the Surface Damage Act, a surface owner could only recover damages from mineral owner by showing negligence or use greater than reasonably necessary.
- The Surface Damages Act requires an operator to give surface owner written notice of intent to drill before drilling and enter good faith negotiations to determine surface damages.
- If no agreement is reached the operator must petition the court for appointment of appraisers.
- Violation of act exposes operator to treble damages.

# Surface Owner Protection Act - North Dakota

- N.D. Cent. Code 38-11.1-01 to -10
- Similar to other Surface Damage Acts.
  - Notify surface operator -- see N.D.C.C. §38-08.1-04.1
  - Compensate the surface owner -- see N.D.C.C. §38-11.1-04
  - Obligation to plug hole -- see N.D.C.C. §38-08.1-06
- Imposes more responsibilities on the company by requiring that ALL damages to the surface be compensated, not just the unreasonable damages.
- Statute now assures the surface owner is compensated for any damages, whether they are reasonable or unreasonable within the scope of mineral exploration and production.

# Limitations on Surface Owner Protection Acts – the Neuberger case

- *Knife River Coal Mining Co. v. Neuberger*, 466 N.W.2d 606, (ND 1991)
- Fact pattern and procedural posture - The defendants, Dennis and Shirley Neuberger, acting as the personal representatives of the Ella Neuberger Estate, and Dale Neuberger (Neubergers), appealed from the judgment of the District Court for the South Central Judicial District dated July 25, 1990. The district court denied the Neubergers' counterclaims which sought damages from Knife River Coal Mining Company (Knife River) under the Surface Owner Protection Act. The Neubergers asserted that the district court erred in holding that Knife River was not liable for payments under the Surface Owner Protection Act, by allowing parol evidence concerning the interpretation of the two coal leases to be admissible at trial.

# Limitations on Surface Owner Protection Acts – the Neuberger case (cont.)

The North Dakota Supreme Court upheld the decision of the District Court, stating, in pertinent part –

- “Upon reviewing the Act, we note that the purpose of the statute is to protect surface owners from the undesirable effects of development "without their consent." § 38-18-03, N.D.C.C. The language of the statute further provides that the provisions of the Act are to be interpreted to benefit the surface owners "regardless of how the mineral estate was separated from the surface estate." § 38-18-03, N.D.C.C. (emphasis added). We conclude the legislature intended the Act to apply only where the surface owner had not consented to the development.”, and

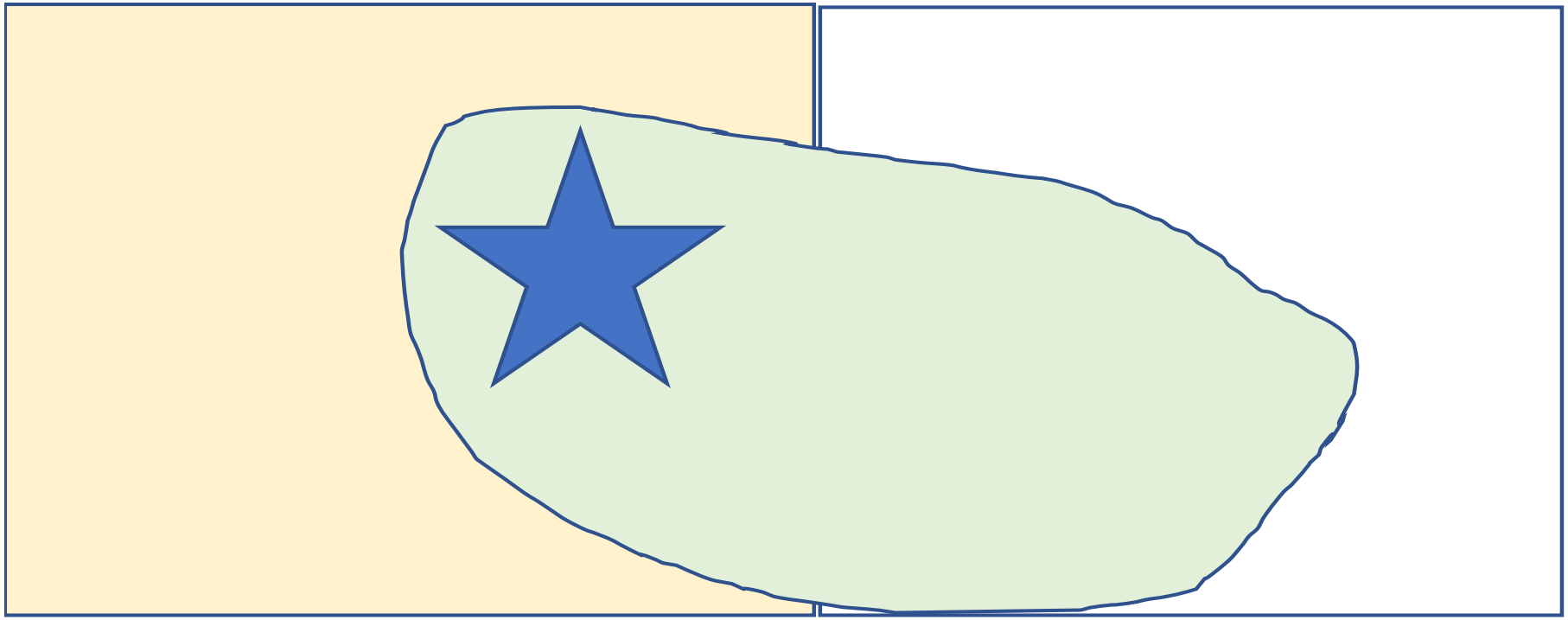
# Limitations on Surface Owner Protection Acts – the Neuberger case (cont.)

- "In the case at hand, Adam and Ella Neuberger were owners of both the surface and mineral interest of the land in question. By entering into the leases, Adam and Ella, the surface owners, consented to the coal mining operations. See § 38-18-06(3). The binding effects of the two leases run with the land and also apply to the subsequent surface owners, the Neubergers. See § 38-8-06, N.D.C.C. Therefore, we conclude that the relief provisions of the Act could not be applied to the case at hand."
- To restate the Court's conclusion, where the surface owners are free to contract for any limitations on the use of the surface via the mineral leasing process, the lease terms will govern.

# Saltwater Disposal Wells – the problem

- There are 180,000 Class II wells in operation in the United States.
- There are 2 billion gallons of fluids injected into these wells every day.
- Most SWD wells are located in Texas, California, Oklahoma, and Kansas

# Saltwater Disposal Wells – the problem (cont.)



# Saltwater Disposal Wells – the problem (cont.)

- Coastal v. Garza may prove instructive on the issue of whether injection is a trespass, although it deals with frac fluids. *Coastal Oil & Gas Corp. v. Garza Energy Trust*, 368 S.W.3d 1 (Tex. 2008)
- However, the FPL cases distinguish the holding in *Garza* as being based on the rule of capture. *Environmental Processing Systems, L.C. v. FPL Farming Ltd*., 457 S.W.3d 414 (Tex. 2015); *FPL Farming Ltd. v. Environmental Processing Systems, L.L.C*., 383 S.W.3d 274 (Tex.App.—Beaumont 2012); *FPL Farming Ltd. v. Environmental Processing Systems, L.L.C.* 351 S.W.3d 306 (Tex. 2011); *FPL Farming LTD. v. Environmental Processing Systems, L.L.C.*, 305 S.W.3d 739 (Tex. App.—Beaumont 2009, pet. granted)

# Saltwater Disposal Wells – the problem (cont.)

- FPL is essentially a comedy in 5 acts, the most recent of which punts on the issue of whether the injection is a trespass. Additionally, FPL concerns Class I injection wells rather than Class II injection wells. Nevertheless, had the Court reached a conclusion, it would have proved instructive.
- Sometimes you can do everything right, and you're still in the wrong.
- The conservative approach would be obtaining agreements with the surface owners overlying the entire aerial extent and pay them proportionately. This would not be popular with the landowner whose land the well is located on.

AAPL
Powering The Profession

# THANK YOU

Thank you very much.

AAPL
Powering The Profession

# Continued Education Component Code

- ARTX-3