

Question 10 – July 2019 – Selected Answer 1

(A) Oilco is not entitled to form a pooled unit that includes the south part of Greenacre on July 1, 2016. Whether Oilco may form a pooled unit on the south part of Greenacre depends on whether the lease is still alive as to the south acreage of Greenacre. Generally, the habendum clause of an oil and gas lease determines the duration of the lease. The primary term will be a set number of years and the secondary term will be "so long thereafter as oil and gas is produced in paying quantities." In theory, the secondary term could be perpetual. The oil and gas lease creates a fee simple determinable in the lessee, leaving a possibility of reverter in the lessor in the event the secondary term lapses or ends.

A pooling clause allows the lessee to combine a portion of the lessor's acreage with another tract to form a pooled unit. This is often accomplished to satisfy Railroad Commission minimum acreage requirements, or for convenience of efficiency as judged by the lessee. Once formed, a well can be drilled anywhere on the pooled unit and will keep the entire unit alive (as to non-drill sites and drill sites). However, a lessor friendly clause, the Pugh clause, can be used to restrict a lessor's ability to keep a large tract of land alive with only a portion of the acreage pooled. The Pugh clause releases the un-pooled acreage and states that lessee will need to independently keep that un-pooled acreage alive, either via drilling a well resulting in production or via another savings clause. If the lessee fails to do so, the un-pooled acreage will be released and the lease can terminate as to that acreage upon the end of the primary term.

Here, Greenacre was leased to Oilco for a primary term of one year from June 1, 2015 with a standard secondary term. Oilco pooled the north part of Greenacre with Whiteacre, pursuant to the pooling clause that authorized doing so when it is "necessary or advisable to properly develop the leased acreage." Frank, Greenacre's lessor, included a Pugh clause in his lease. Therefore, when the north portion of Greenacre was pooled, the south (un-pooled) portion was "released" and had to be kept alive through actual drilling and production or some other savings clause. A well was drilled by Oilco on the north acreage in the pooled unit on Greenacre, but the facts do not indicate whether Oilco commenced operations for drilling as to the south acreage. Assuming Oilco made no such effort and there was no production on the south portion, Oilco's lease would have terminated on July 1, 2016, the expiration of the primary term. On July 1, 2016, the day the primary term expired, Oilco attempted to pool the southern portion of Greenacre with the southern portion of Whiteacre. Because Frank's lease states that the lease will only remain in force as to lands within the pooled units where production is occurring by the end of the primary term, Oilco's efforts to pool the southern acreage of Greenacre are not timely. The end of the primary term arrived with no production on that acreage, so the lease terminated and

the southern acreage reverted to Frank, as lessor, automatically. The fee simple determinable does not require Frank take any action to exercise his possibility of reverter, it will be automatic. Oilco still has a valid lease with Frank as to the pooled acreage on the north portion of Greenacre, and the lease will remain in effect so long thereafter as oil and gas is produced in paying quantities on the pooled unit.

(B) Oilco may conduct seismic operations on Whiteacre despite Gwen's objections. When Ellen conveyed Whiteacre to Gwen, she severed the mineral estate from the surface estate, reserving the entire mineral estate in herself and conveying only the surface estate to Gwen. The conveyance of "all oil, gas, and other minerals in and under" operated to reserve the entire mineral estate, and not merely a royalty interest. When the mineral estate is severed, an implied easement arises in favor of the mineral estate, rendering it dominant and the surface estate servient. The mineral estate may use as much of the surface estate as is reasonably necessary to develop the mineral estate. As the mineral owner, Ellen had the right to permit Oilco to conduct seismic operations as part of the oil and gas lease she executed to Oilco. By executing the lease to Oilco, Ellen transferred her rights in the mineral estate to Oilco via a fee simple determinable for the duration of the lease, and likewise transferred the implied easement and the right to use the surface as much as is reasonably necessary to develop the mineral estate. This right includes seismic operations in accordance with Oilco's rights under the lease of Whiteacre.

(C) The accommodation doctrine provides some limits on the mineral estate's use of the surface in developing the oil and gas. The accommodation doctrine requires the surface owner prove pre-existing use on the surface estate that is substantially interfered with by the lessee, and that the lessee has reasonable alternatives on the leased premises. Gwen cannot require Oilco go off the leased premises to accommodate her. The facts do not indicate what pre-existing use Gwen could assert, only that she prefers not to have strangers on her land conduct seismic operations. Unfortunately for Gwen, she purchased only the surface estate from Ellen and therefore her ownership and use is subject to the mineral estate, currently operated by Oilco.

Question 10 – July 2019 – Selected Answer 2

(A) Oil Co cannot form a pooled unit on the south part of Greenacre due to the existence of a Pugh Clause in Frank's lease

The issue here is whether OilCo can form a pooled unit with the south part of Greenacre when the primary term has come to an end.

A habendum clause in an oil and gas lease gives the primary term of the lease and the secondary term. The primary term is usually the time in which oil and gas need not be produced for the lease to remain alive and the secondary term is the amount of time in which oil and gas must be produced in paying quantities. Leases often grant lessees power to pool tracts of land in order to keep leases alive instead of drilling multiple wells, and the RRC also has power to mandate the pooling of wells to prevent against waste and protect interests. A Pugh Clause in an oil and gas lease is a modern trend to protect the lessor from being taken advantage of in terms of pooling. A Pugh Clause will sever pooled tracts upon which production is occurring at the end of the primary term from those upon which nothing is being done in order to leave the lessor free to re-lease these tracts of land.

In this case, the leases grant express power to OilCo to pool certain units. Something which OilCo took advantage of by pooling the northern parts of Greenacre and Whiteacre which were adjacent to one another in order to drill a single well. The well almost immediately began producing in paying quantities (under the Garcia test of the Texas Supreme Court) in September. Although the lease in its final clause suggested that production on a pooled acreage would keep the whole lease alive, Frank's lease also had a Pugh Clause which would prevent this from occurring as it states the lease would remain alive only to the pooled units upon which PPQ was occurring at the end of the primary term thus severing the Northern tract from the Southern Tract. As the primary term of the lease ended on June 1 2016, and OilCo didn't file an instrument regarding the Southern halves of Greenacre and Whiteacre until July 2016, the Pugh Clause will prevent the lease on the southern part being kept alive by pooling. However, as Whiteacre lease did not contain such a clause, Whiteacre lease remains in effect as a whole.

Overall, therefore, the insertion of a Pugh Clause in the lease of Frank prevented the lease on the Southern Tract being kept alive by pooling the Northern tract in July 2015, and as the primary term expired in June 2016 without prior pooling action by OilCo, OilCo can no longer form such a pooled unit.

(B) Gwen will fail in her objections to prevent Oilco from conducting seismic operations on Whiteacre due to the dominance of the mineral estate

The issue here is whether the owner of the surface estate can prevent the owner of the mineral estate or a lessee of the mineral owner from conducting certain operations relating to their corporeal interests and their right to develop the minerals beneath the surface.

Texas law favors the mineral estate. The mineral estate is considered to be the dominant estate in Texas meaning that the owner of the mineral estate has a right to ingress and egress over the surface in order to discover, develop and produce mineral from the ground beneath. This right extends not only to drilling wells, but also to conducting pre-drilling operations to discover the location of oil and gas and to effectively produce those minerals. The owner of the surface estate has little recourse unless the mineral owner (or lessee) is negligent, exceeds the terms of the lease, exceeds what is reasonably necessary to develop, or is vulnerable under the accommodation doctrine.

Here, OilCo is a lessee of the mineral estate from Ellen. The lessee of the minerals in the land is treated as having a 'fee simple determinable' in the minerals and has corporeal interests and the ability to develop these minerals and produce them. OilCo here is trying to conduct seismic operations which are often used to locate oil and other valuable minerals beneath the surface in order to maximize the effectiveness of drilling and discover high pressure and low pressure areas in determining where to place a well. The seismic operations of an oil company are closely related to developing the minerals but also relate to the effectiveness of such development and thus OilCo will be able to conduct seismic operations and use the right of ingress and egress over the land despite Gwen's protest against 'strangers'. As long as they are not negligent and do not interfere with the accommodation doctrine (discussed below), oil and gas seismic operations are a right of a mineral owner and thus Gwen's protests will not be effective.

Overall, therefore, the dominance of the mineral estate and the right to develop the minerals beneath the estate will mean that OilCo can conduct seismic operations over the protests of Gwen. Moreover, there is an express grant in the lease for such seismic operations and the lease language tends to dominate.

(C) The Accommodation Doctrine has three major requirements for a surface owner to satisfy

The final issue here is what must Gwen prove to make use of the accommodation doctrine.

There are three requirements for the accommodation doctrine to apply. Firstly, the use of surface by the mineral lessee must substantially interfere with an existing use of the surface owner. Secondly, there must be reasonable alternatives available for the mineral owner and no reasonable alternatives for the surface owner. Finally, there must be reasonable alternatives available on the tract of land.

Here, Gwen would struggle to prove a substantial interference. OilCo is not drilling in any particular spot or even destroying lands. The dislike of strangers is not enough to amount to a substantial interference. Moreover, seismic operations rarely interfere with surface use in a significant way as it involves sending silent waves into the ground which create computer images. It is a very low-burden operation for a surface owner. Gwen may be able to show that there are reasonable alternatives as such seismic operations can often be conducted on adjacent tracts and sending the waves under and across the land. However, this will fail on the third part that the reasonable alternative must be available on the same tract of land. Here, the only reasonable alternative would be available on Greenacre rather than Whiteacre and therefore, Gwen's use of the accommodation doctrine would fail here.

Overall, therefore, Gwen must establish (1) a substantial interference with existing use; (2) with reasonable alternatives to the oil company and no reasonable alternatives to the surface owner; and (3) alternatives on the same tract of land. She will likely fail on branches (1) and (3), if not all