Oil and Gas Production from a Unitized Area - The Nonjoining Owner

William T. Carlisle

reason arising out of the subject matter or the circumstances,[48] the court refused to preclude review. The decision demonstrates that, "the true architects of reviewability are the courts."[49]

Leeds & Northrup and *Scofield* recognize that a charging party has vital rights in a Board proceeding. Although the rights in each case are of a different nature, they are both private rights which are to be recognized and enforced by the courts. The Second Circuit's refusal[50] to recognize private rights is in direct conflict with this reasoning. And the Board's merely affording the objecting party its reasons for the settlement, in lieu of a hearing,[51] would also seem to conflict with *Scofield* due to the fact that this is an incomplete recognition of the charging party's administrative rights. The current trend is a proper one. Although the Board should be given discretionary powers in certain proceedings, often the right to a hearing outweighs the value of absolute administrative expediency. Perhaps to compensate for this trend, the Board will slow down its complaint-issuing process, preferring to exhaust all opportunities for settlement prior to issuing a complaint. Nevertheless, once a complaint has issued the charging party's right to a hearing has been reinforced by the *Leeds & Northrup* decision.

George E. Seay, Jr.

Oil and Gas Production From a Unitized Area — The Nonjoining Owner

The plaintiff, Roberts, owned an undivided half interest in a one and one-half acre tract of land. James Craven and Estella Todd owned the other half interest in the tract. Superior Oil Company attempted to get all three cotenants to join a "Unitization and Unit Operating Agreement" for a unitized area consisting of several hundred acres. Roberts refused, but Craven and Todd executed separate oil and gas leases to Superior, each lease purporting to cover all of the tract. Although it drilled no wells on the one and one-half acre tract, Superior did obtain production from the unit. For some reason, not apparent from the opinion, Superior considered the Craven and Todd leases as representing one and one-half acres, instead of one-half of

[48] JAFFE, JUDICIAL CONTROL OF ADMINISTRATIVE ACTION 339 (abr. student ed. 1965).
[49] *Ibid.*
[50] See notes 28-31 *supra* and accompanying text.
[51] See notes 26-27 *supra* and accompanying text.

one and one-half acres, and paid royalty on unit production accordingly.[1]

Roberts still refused to ratify the lease but instead sued to recover one-half of the unit production[2] allocated to the one and one-half acre tract, less reasonable expenses.[3] The court of civil appeals affirmed the trial court's finding that since Superior had allocated to itself the entire tracts pro rata share of production from the unit, it held Roberts' share in trust and was required to account for the production, less expenses attributable to Roberts' land.[4] *Held, reversed and rendered:* the nonjoining cotenant has no right to production from another tract in a unitized area since there is neither actual production from his land nor a contractual relationship with the unit. *Superior Oil Co. v. Roberts,* 398 S.W.2d 276 (Tex. 1966).

I. A Cotenant's Interest: The Effect of a Unitization Agreement

Texas law recognizes absolute ownership of oil and gas in place, subject to the rule of capture.[5] The owner of property acquires title not only to the surface land but also to all oil and gas which he produces from wells drilled and bottomed on his land, even to such minerals which have migrated from the adjoining lands.[6] And where

[1] Superior Oil Co. v. Roberts, 398 S.W.2d 276 (Tex. 1966).

[2] The Texas Supreme Court spoke in terms of "working interest," when the court actually meant to say "production." See the court of civil appeals decision, 390 S.W.2d 550 (1965).

[3] Roberts sued for an accounting between cotenants, on the theory that by accepting leases from Craven and Todd, Superior became a tenant in common in the mineral estate underlying the one and one-half acre tract. Roberts equated the pooling of such tract and the obtaining of production from the unit with actual production from the tract in question. Had Superior produced from Roberts' tract, it would have had to account to Roberts for its share (an undivided one-half) of the minerals produced less the necessary and reasonable cost of production and marketing. Cox v. Davison, 397 S.W.2d 200 (Tex. 1965); White v. Smyth, 147 Tex. 272, 214 S.W.2d 967, 5 A.L.R.2d 1348 (1948). See text accompanying notes 8, 9, 16 and 27 *infra.*

[4] Superior Oil Co. v. Roberts, 390 S.W.2d 550 (Tex. Civ. App. 1965).

[5] Ryan Consol. Petroleum Corp. v. Pickens, 155 Tex. 221, 285 S.W.2d 201 (1955); Brown v. Humble Oil & Ref. Co., 126 Tex. 296, 83 S.W.2d 935 (1935). See also Elliff v. Texon Drilling Co., 146 Tex. 575, 210 S.W.2d 558, 561 (1948), where the court stated:

> [T]he so-called rule or law of capture . . . is that the owner of a tract of land acquires title to the oil or gas which he produces from wells on his land, though part of the oil or gas may have migrated from adjoining lands. He may thus appropriate the oil and gas that have flowed from adjacent lands without the consent of the owner of those lands, and without incurring liability to him for drainage. The non-liability is based upon the theory that after the drainage the title or property interest of the former owner is gone . . . under the law of capture there is no liability for reasonable and legitimate drainage from the common pool.

However, in *Elliff* the rule of capture did not relieve the party from liability to the adjacent owner for *negligence* in allowing a well to blow-out.

[6] Ryan Consol. Petroleum Corp. v. Pickens, 155 Tex. 221, 285 S.W.2d 201 (1955).

such owner leases his land for the production of oil and gas, the lessor and lessee own all the oil and gas that they bring to the surface.[7]

The owner of an undivided mineral interest, even without the consent of his cotenants, may drill wells on common property; but he must not exclude his cotenants from also drilling, and he must account to his cotenants to the extent of their interest.[8] In the recent decision of *Cox v. Davison*,[9] the Texas Supreme Court held that where a well is drilled on common property, the nonjoining cotenant is entitled to his proportionate share of the market value of the oil and gas, less reasonable expenses, with no allowance for interest.

A pooling or field-wide unitization agreement arises when two or more owners of separate tracts either grant oil and gas leases with provisions allowing pooling (which leases are subsequently pooled) or grant oil and gas leases and later enter into a separate unitization agreement, pooling the tracts for production purposes. Their royalty interests under the leases are pooled for the period of the leases, with the royalties usually being apportioned among the lessors in the ratio of their respective acreage contributions to the unit. Texas courts allow a cotenant both to lease his undivided interest and to include it in a unitized area without the consent or joinder of his cotenant.[10] Of course, the cotenant's actions bind only his undivided interest, and his unitization agreements do not restrict the nonjoining party from developing his mineral interest within the regulations imposed by the Railroad Commission.[11]

In a fact situation like *Roberts*, involving both a nonjoining cotenant and a unitization agreement, the court must first determine the contractual relationships of the parties. Since a cotenant's actions bind only his undivided interest, the nonjoining party can neither receive the benefits of unit production occurring off his property nor collect damages for injury to his property as a result of the operation of that unit.[12] He may be permitted to ratify the lease, if he does so

[7] The rule of capture applies to the production of oil and gas as between owners of adjacent tracts. However, the rule of capture has no application between cotenants, since as between cotenants there is no question of drainage where the well is drilled and bottomed on common land.

[8] Prairie Oil & Gas Co. v. Allen, 2 F.2d 566 (8th Cir. 1924); White v. Smyth, 147 Tex. 272, 214 S.W.2d (1948). See also Humble Oil & Ref. Co. v. Kishi, 276 S.W. 190 (Tex. Comm. App. 1925).

[9] 397 S.W.2d 200 (Tex. 1965).

[10] Whelan v. Placid Oil Co., 274 S.W.2d 125 (Tex. Civ. App. 1954).

[11] Title 102, Oil and Gas, VERNON'S ANN. CIV. STAT.; Dobson v. Arkansas Oil & Gas Co., 218 Ark. 160, 235 S.W.2d 33 (1950).

[12] Tide Water Associated Oil Co. v. Scott, 159 F.2d 174 (5th Cir. 1964).

promptly.[13] However, in the absence of compulsory pooling statutes,[14] courts look with disfavor upon a nonjoining owner's waiting until the unit achieves production and then either seeking more favorable lease terms or defeating the purposes of the unit by drilling his own well which drains the unit field.[15]

Secondly, the court must consider both actual production and constructive production. Where there is actual production from a well bottomed on the nonjoining cotenant's tract, the rule of *Cox v. Davison*[16] entitles the nonjoining cotenant to his proportionate share of the market value of the oil or gas, less reasonable expenses (with no allowance for interest). Where production is from a well on another tract, courts have often applied the theory of constructive production to allow recovery. The theory is based on the clause in the unitization agreement whereby production from any tract within the unit constitutes production from all tracts in the unit. In *Spradley v. Finley*,[17] for example, a cotenant leased his undivided mineral interest for a term of fifteen years "and so long thereafter" as oil or gas was produced, and such lease was later pooled under a unitization agreement containing a constructive production clause.[18] The court held that production from another tract within the unit served to extend the lease beyond the primary term, *i.e.*, that production from the unit constituted production from the tract in question under the terms of the lease agreements. The concept of constructive production, however, applies only to those parties who were privy to the unitization agreement.[19]

II. BOGGESS V. MILAM[20] AND CALIFORNIA CO. V. BRITT[21]

In two cases prior to *Superior Oil v. Roberts*, courts in other states held that the owner who refuses to join a unitization agreement has

[13] Texas courts will not allow the non-joining royalty owner to wait an unreasonable time after the development of the lease before ratifying, nor will the courts permit the non-joining royalty owner to act in bad faith in ratifying the lease. Furthermore, the court will not require that the lessee hold open his ratification offer for an unlimited or unreasonable length of time. Nugent v. Freeman, 306 S.W.2d 167 (Tex. Civ. App. 1957) *error ref. n.r.e.* Ward v. Gohlke, 279 S.W.2d 422 (Tex. Civ. App. 1955) *error ref.*; Texas & Pac. Coal & Oil Co. v. Kirtley, 288 S.W. 619 (Tex. Civ. App. 1926) *error ref.*

[14] TEX. REV. CIV. STAT. ANN. art. 6008c (1965).

[15] Corley v. Mississippi State Oil & Gas Bd., 234 Miss. 199, 105 So. 2d 633 (1958).

[16] 397 S.W.2d 200 (Tex. 1965); see text accompanying note 9 *supra*.

[17] 157 Tex. 260, 302 S.W.2d 409 (1957).

[18] "If production is found on the pooled acreage it shall be treated as if production is had from this lease, whether the well or wells be located on the premises covered by this lease or not." Spradley v. Finley, 157 Tex. 260, 302 S.W.2d 409 (1957).

[19] Note 11 *supra*.

[20] 127 W. Va. 654, 34 S.E.2d 267 (1945).

[21] 247 Miss. 718, 154 So. 2d 144 (1963).

no right to production obtained from another tract within the unit.[22]

In *Boggess v. Milam*,[23] a West Virginia decision, the complainant, W. W. Boggess, owned an undivided one-tenth interest in a 116-acre tract. The cotenants, owning five-sixths of the remaining undivided interest, unitized the 116-acre tract with an adjoining 53-acre tract. Boggess expressly refused to join such lease and unitization agreements. Shortly after the signing of the agreements, a gas well was drilled and bottomed on the adjoining 53-acre tract. The plaintiff sued to recover his alleged proportionate interest in the net value of the entire production obtained from the well on the adjoining 53-acre tract. Boggess, claiming to be a tenant in common with the other owners in the unit, contended that the unitization agreement destroyed the separate identities of the two tracts, thus merging the tracts into one for operating purposes.

The West Virginia Supreme Court concluded that the lessee was not liable, in the absence of a contractual obligation, to the owner of land adjoining a tract upon which the lessee had a producing oil or gas well. Since Boggess had refused to join both the lease of the 116-acre tract and the unitization agreement, he acquired no contractual rights; nor did either instrument affect his interest, favorably or unfavorably. The court reasoned that nonjoining cotenants should not be allowed to prevent or impair the development of unitized tracts where they had been given a fair and equal opportunity to join the unitization agreement.

In *California Co. v. Britt*[24] the Mississippi Supreme Court followed the *Boggess* decision. With substantially the same fact situation as *Boggess*, Britt, the nonjoining cotenant, brought a claim for drainage of the oil beneath his tract against California Company, the operator of the unitized field. The supreme court reversed the lower court decision and held that California Company incurred no liability for drainage.[25]

III. Adherence to the Rules in Texas

The court of civil appeals in *Roberts*,[26] in effect, attempted to extend the concept of constructive production to allow the nonjoining

[22] California Co. v. Britt, 247 Miss. 718, 154 So. 2d 144, 148 (1963).
[23] 127 W. Va. 654, 34 S.E.2d 267 (1945).
[24] 247 Miss. 718, 154 So. 2d 144 (1963).
[25] *Id.* at 147. There was dicta in this case to the effect that if Britt had not been offered a fair and reasonable opportunity to enter the unitization agreement on equal terms with the other parties in the unit, then Britt could have recovered equity. As to what constitutes a "fair and reasonable" offer to voluntarily pool, see the new Texas Compulsory Pooling Act, Tex. Rev. Civ. Stat. Ann. art. 6008c (1965).
[26] 390 S.W.2d 550 (Tex. Civ. App. 1965).

cotenant to recover a pro rata share of unit production when his cotenant purported to convey a full interest in the tract. It held that although the lease and unitization agreements executed by Craven and Todd conveyed only their interests, and not Roberts' share, Roberts became a cotenant with Superior. The court cited a former case[27] for the rule that where a cotenant severs oil or gas from the mineral estate without the consent of the other cotenants, he must pay the other cotenants their proportionate share of the production, less reasonable expenses. The Texas Supreme Court[28] cited *Boggess v. Milam*[29] and *California Co. v. Britt*[30] for authority that the unitization agreement does not effect a merger of title but merely consolidates the contractual interests under the leases. The court concluded by saying that Superior's accounting methods—paying the full one-eighth royalty on one and one-half acres to Craven and Todd—gave Roberts no basis on which to recover from Superior. However, Roberts might have been able to maintain a suit for slander of title if he could have shown first, malice—the bad faith purchase of Roberts' title for the purpose of asserting a claim against the land and a repudiation of Roberts' title—and, second, that he suffered special damages.[31]

IV. Conclusion

The Texas Supreme Court was correct in following the *Boggess* and *Britt* cases and applying them to the situation where a cotenant purports to unitize the full interest in a tract where there is a nonjoining cotenant. The purpose of the unit is to maintain fieldwide pressure and achieve maximum efficiency in production. The nonjoining owner should not be allowed to defeat this purpose by waiting until production is obtained and then claiming an accounting as to production instead of a royalty interest. In fact, if the nonjoining owner has been offered a reasonable opportunity to join or ratify the unit agreement, the operator should not be compelled to continue

[27] White v. Smyth, 147 Tex. 272, 214 S.W.2d 967 (1948); see note 3 *supra* and text accompanying note 8 *supra*.

[28] Superior Oil Co. v. Roberts, 398 S.W.2d 276, 278 (Tex. 1966).

[29] 127 W. Va. 654, 34 S.E.2d 267 (1945).

[30] 247 Miss. 718, 154 So. 2d 144 (1963).

[31] Kidd v. Hoggett, 331 S.W.2d 515 (Tex. Civ. App. 1959) *error ref. n.r.e.* See also Reaugh v. McCollum Exploration Co., 139 Tex. 685, 163 S.W.2d 620 (1942); *cf.*, Shield v. Shield, 286 S.W.2d 252 (Tex. Civ. App. 1955) *error ref. n.r.e.*, a concurrent owner who executes an oil and gas lease on the subject property and receives the bonuses, rentals, or royalties payable under the lease is in the same position as a concurrent owner who himself develops and operates the property, and is personally liable to account to his cotenants for all sums so received by him.