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UNIFORM COMMERCIAL CODE—§ 9-401— PERFECTION OF SECURITY INTERESTS IN MINERALS, INCLUDING OIL AND GAS, REQUIRES REAL ESTATE FILING IN OKLAHOMA

The 1972 amendments to the Uniform Commercial Code recently passed in Oklahoma¹ clarify and simplify procedures for perfecting security interests in oil-and-gas-related collateral. Historically, the procedures for perfecting security interests in such collateral, which typically includes both real and personal property, have gone through three phases. Before the enactment of the Code in 1961,² because of the dual nature of the collateral, perfection of oil and gas security interests was governed by both real estate³ and chattel mortgage laws.⁴ The enactment of Article 9 of the Uniform Commercial Code in 1961⁵ repealed the chattel mortgage statutes⁶ and required perfection of interests in both tangible and intangible personalty by filing in the state central filing office without the formalities of execution and acknowledgment.⁷ The Code, however, did not change the laws requiring interests

1. Commercial Code—Modifications—Transitional Provisions, ch. 194, 1981 Okla. Sess. Laws (to be codified in scattered sections of OKLA. STAT. tit. 12A).

2. U.C.C., ch. 1, 1961 Okla. Sess. Laws (codified at OKLA. STAT. tit. 12A, §§ 1-101 to 10-104 (1971)).

3. A mortgage of real estate is created whenever an instrument conveys an interest in real estate for security purposes. OKLA. STAT. tit. 46, § 1 (1971). For procedural requirements governing perfection of interests in real estate, see OKLA. STAT. tit. 16, §§ 15, 16; tit. 19, §§ 287, 291, 298; tit. 46, §§ 1, 3, 6, 8, 10 (1971).

4. See R. HEMINGWAY, *THE LAW OF OIL AND GAS* 444 (1971); Ryan, *Effect of the Uniform Commercial Code on Oil and Gas Transactions*, EIGHTEENTH ANN. INST. ON OIL AND GAS L. & TAX. 365, 409 (1967) [hereinafter cited as Ryan]; Vagts, *The Impact of the Uniform Commercial Code on the Oil and Gas Mortgage*, 43 TEX. L. REV. 825, 842 (1965). The Oklahoma chattel mortgage statutes were found at OKLA. STAT. tit. 46, §§ 51-75, 91-94 (1951) (repealed 1961).

5. U.C.C., ch. 1, 1961 Okla. Sess. Laws (codified at OKLA. STAT. tit. 12A, §§ 9-101 to -507 (1971)).

6. OKLA. STAT. tit. 12A, § 10-102 (1971); OKLA. STAT. ANN. tit. 12A, app. at 453 (West 1963).

The repealer statutes of Article 10, however, were themselves repealed. General Repealer, ch. 68, § 1, 1980 Okla. Sess. Laws. Nevertheless, the effect of the repealer statutes of Article 10 remains: "Whenever any act of the legislature is repealed, which repealed a former Act, such former Act shall not thereby be revived, unless it be expressly so provided, and the act revived be set out in full." OKLA. STAT. tit. 25, § 32 (1971).

7. Okla. Stat. tit. 12A, § 9-401 (1971). See Ryan, *supra* note 4, at 390.

in realty to be perfected in accordance with the real estate mortgage statutes.⁸ Thus, two types of filing continued to be necessary where oil-and-gas-related collateral were involved.

The 1972 Code amendments eliminate the necessity of dual filing to perfect security interests in collateral related to oil and gas production⁹ as was required during both the pre-Code and the 1961 Code period. In effect, the recent amendments permit perfection of mortgages covering security interests in collateral characterized as both real and personal property by a single filing in the office of the county clerk where the land is situated.¹⁰

The recent amendments are significant because they clarify an area of law which formerly was a source of confusion. The two most important types of collateral used in oil and gas financing are the oil and gas lease¹¹ and the assignment of production,¹² both of which have

8. OKLA. STAT. tit. 12A, § 9-104(j) (1971) specifies that transactions in real estate are excluded from Article 9 ("except to the extent that provision is made for fixtures in section 9-313, to the creation or transfer of an interest in or lien on real estate, including a lease or rents thereunder").

9. Commercial Code—Modifications—Transitional Provisions, ch. 194, §§ 26, 27, 1981 Okla. Sess. Laws (to be codified at OKLA. STAT. tit. 12A, §§ 9-401, -402 (1981)). The Oklahoma Constitution states that "No act shall take effect until ninety days after the adjournment of the session at which it was passed . . . unless, in case of emergency, to be expressed in the act, the Legislature . . . so directs." OKLA. CONST. art. 5, § 58. Since the act amending the Code contained no emergency clause, the effective date of the amendments would be ninety days after July 20, 1981, or October 19, 1981.

10. See notes 28 & 29 *infra* and accompanying text.

11. Since Oklahoma adheres to the non-ownership theory of oil and gas, the oil and gas lease represents an exclusive non-possessory right to explore for and produce the oil and gas. The nature of the rights in an oil and gas lease has been described in *Rich v. Doneghey*, 71 Okla. 204, 206-07, 177 P. 86, 89 (1891):

[Owners in fee simple have] no absolute right or title to the oil or gas which might permeate the strata underlying the surface of their land, as in the case of coal or other solid minerals fixed in, and forming a part of, the soil itself.

But with respect to such oil and gas, they [the owners] had certain rights designated by the same courts as a qualified ownership thereof, but which may be more accurately stated as exclusive right, subject to legislative control against waste and the like, to erect structures on the surface of their land, and explore therefor by drilling wells through the underlying strata, and to take therefrom and reduce to possession, and thus acquire absolute title as personal property to such as might be found and obtained thereby. This right is the proper subject of sale, and may be granted or reserved. The right so granted or reserved, and held separate and apart from the possession of the land itself, is an incorporeal hereditament; or more specifically, as designated in the ancient French, a profit a prendre, analogous to a profit to hunt and fish on the land of another. Considered with respect to duration, if the grant be to one and his heirs and assigns forever, it is of an interest in fee. An interest of less duration may be granted, and that for a term of years has been denominated by this court a chattel real. Such right is an interest in land.

Id. (citations omitted).

12. By mortgaging an assignment of production or its proceeds the "borrower assigns to the lender the oil, gas, and other minerals produced, saved, and sold from the mortgaged property and authorizes and directs any purchaser of such production to pay to the lender the amounts due to

been characterized in Oklahoma as personalty.¹³ Before the adoption of the 1961 Code, although the oil and gas mortgage secured collateral characterized as personal property, the Oklahoma courts interpreted the real estate mortgage statutes to require such security interests to be recorded as mortgages of real estate.¹⁴ The courts reasoned that both the oil and gas lease and the assignment of production fell within the scope of statutes requiring "interests in" or instruments "relating to" real estate to be recorded as real estate.¹⁵ Apart from the oil and gas

be paid for such production." Johnson, *Legal Aspects of Oil and Gas Financing*, NINTH ANN. INST. ON OIL AND GAS L. & TAX. 141, 158 (1958). The importance of the assignment of production lies in the fact that upon production the mortgagee can amortize the debt while his security interest is being depleted. See Vagts, *supra* note 4, at 832. Commonly, the lender receives all of the production but before default returns a portion of the production to the borrower to cover his operating expenses. Johnson, *supra*, at 159. For a form for a mortgage of an assignment of production, see Hoagland, *A Form of Mortgage and Assignment of Oil and Gas Production*, 34 DICTA 226 (1957).

13. At common law the distinction between personalty and realty in relation to interests in land turned on duration. 1 H. WILLIAMS & C. MEYERS, OIL AND GAS LAW § 212 (1980). Since a leasehold estate is not a freehold estate but an estate of limited duration, a leasehold estate was classified at personalty under the common law. R. BROWN, THE LAW OF PERSONAL PROPERTY § 1.7, at 10-11 (1975). In accordance with the common law, Oklahoma cases, with some exceptions, have treated interests in minerals as personalty. See, e.g., Continental Supply Co. v. Marshall, 152 F.2d 300, 307 (10th Cir. 1945), *cert. denied*, 327 U.S. 803 (1946) (mortgage of assignments of production was on personal property not yet acquired and, therefore, a chattel mortgage to the extent it covered after acquired personal property although it must be recorded under a real estate mortgage statute); State v. Kirchner, 185 Okla. 129, 130, 90 P.2d 1055, 1056 (1939) (oil and gas leases are not real property for the purpose of real property ad valorem taxation); Pluto Oil and Gas Co. v. Land, 151 Okla. 117, 121-22, 2 P.2d 945, 949 (1931) (since oil and gas lease is personalty, the guardian of a minor does not have to conform to the conveyancing requirements of the probate code when conveying an oil and gas lease); Clark v. Mercer Oil Co., 139 Okla. 48, 50, 281 P. 283, 285 (1929) (oil and gas lease is not real property within statute regulating partition of real property although courts of equity can order the partition of personalty where division in kind is impractical); First Nat'l Bank of Headlton v. Dunlap, 122 Okla. 288, 289-90, 254 P. 729, 731-32 (1927) (oil and gas lease does not fall within the scope of statute providing that recorded judgments are liens on the debtor's real estate). But see McCully v. McCully, 184 Okla. 264, 266-67, 86 P.2d 786, 788-89 (1939) (pledge of unaccrued royalty is a pledge of an interest in real estate); Cuff v. Koslosky, 165 Okla. 135, 137, 25 P.2d 290, 294 (1933) (mineral interest is within meaning of statute requiring appraisal of lands and tenements prior to sale by execution); Woodworth v. Franklin, 85 Okla. 27, 33, 204 P. 452, 458 (1921) (oil and gas leases create interest in real estate and fall within the statute of frauds). For a discussion of the classification of mineral interest in Oklahoma see 1 H. WILLIAMS & C. MEYERS, *supra*, at § 214.2.

14. See Continental Supply Co. v. Marshall, 152 F.2d 300 (10th Cir. 1945), *cert. denied*, 327 U.S. 803 (1946); Stone v. Wright, 75 F.2d 457 (10th Cir. 1935), *cert. denied*, 295 U.S. 754; Davis v. Lewis, 187 Okla. 91, 100 P.2d 994 (1940); McCully v. McCully, 184 Okla. 264, 86 P.2d 786 (1939).

15. The trial court in Continental Supply Co. v. Marshall, 52 F. Supp. 717 (W.D. Okla. 1943), *rev'd*, 152 F.2d 300 (10th Cir. 1945), *cert. denied*, 327 U.S. 803 (1946), found that a mortgage of an oil and gas lease fell within Oklahoma's mortgage statute which provided that "[e]very instrument purporting to be an absolute or qualified conveyance of real estate or any interest therein, but intended to be defeasible or as security for the payment of money, shall be deemed a mortgage and must be recorded and foreclosed as such." *Id.* at 721 (quoting from OKLA. STAT. tit. 46, § 1 (1941) which is still in effect today) (emphasis added). On appeal, the Tenth Circuit

lease and the assignment of production, however, oil and gas financing often required perfection of security interests in other collateral such as equipment, extracted oil and gas, contract rights, and accounts receivable.¹⁶ Security interests in these kinds of collateral had to be perfected under statutes relating to accounts receivable and chattel mortgages.¹⁷

The Uniform Commercial Code, adopted by Oklahoma in 1961, disclaimed any effect on security interests in real property¹⁸ but expressly governed the perfection of security interests in tangible and intangible personalty, including contract rights and accounts receivable.¹⁹ Although prior to the Code the Oklahoma courts had interpreted real estate statutes to encompass assignments of production and production payments,²⁰ the express language of the code raised questions about the continued validity of the court's classification.²¹ Because it was unclear whether security interests in assignments of production and pro-

affirmed this portion of the trial court's finding although it appeared to base its conclusion on OKLA. STAT. tit. 16, § 15 (1941) which states in pertinent part that "no deed, mortgage, contract, bond, lease or other instrument relating to real estate other than a lease for a period not exceeding one year and accompanied by actual possession, shall be valid as against third parties unless acknowledged as herein provided" (emphasis added) (this statute remains effective). The court found that under this statute a mortgage of an oil and gas lease must be recorded as a real estate mortgage to impart notice to third parties. 152 F.2d at 306. Similarly, in an earlier case, *Stone v. Wright*, 75 F.2d 457 (10th Cir. 1935), cert. denied, 295 U.S. 754, the court found that an assignment of ten thousand dollars which was to be paid out of the proceeds from an undivided working interest, although not a conveyance of an interest in real estate, was so related to real estate as to be a proper instrument for recording under OKLA. STAT. § 9672 (1931) (now OKLA. STAT. tit. 16, § 15 (1971)). 75 F.2d at 460. These holdings conform to the Oklahoma Supreme Court's holding in *Davis v. Lewis*, 187 Okla. 91, 100 P.2d 994 (1940) that an assignment of proceeds of a working interest was an "instrument relating to real estate" and was required to be acknowledged and recorded in order to be valid as to third persons under the law on the subject of recording." *Id.* at 94, 100 P.2d at 997.

16. See Ryan, *supra* note 4, at 409-11; Vagts, *supra* note 4.

17. See Ryan, *supra* note 4, at 409.

18. OKLA. STAT. tit. 12A, § 9-104(j) (1971).

19. As enacted in 1961, OKLA. STAT. tit. 12A, § 9-102(1) provided in part that Article 9 applies "(a) to any transaction (regardless of its form) which is intended to create a security interest in personal property or fixtures including goods, documents, instruments, general intangibles, chattel paper or accounts or contract rights; and also (b) to any sale on accounts, contract rights or chattel paper" (emphasis added).

Under the 1972 amendments, contract rights have been eliminated from Article 9, so that the new section states that Article 9 applies (a) to any transaction, regardless of its form, which is intended to create a security interest in personal property or fixtures including goods, documents, instruments, general intangibles, chattel paper or accounts; and also (b) to any sale of accounts or chattel paper. Commercial Code – Modifications – Transitional Provisions, ch. 194, § 6, 1981 Okla. Sess. Laws (to be codified at OKLA. STAT. tit. 12A, § 9-102 (1981)).

20. The holder of a production payment has a "right to receive some money which will be earned by future sales of production from the property described in the instrument defining the production payment" Ryan, *supra* note 4, at 416.

21. *Davis v. Lewis*, 187 Okla. 91, 94, 100 P.2d 994, 997 (1940). See notes 13-15 *supra* and accompanying text.

duction payments should be filed according to the Code²² or the real estate mortgage laws,²³ a practical solution was to file a combined mortgage and financing statement in both the county clerk's office and the state central filing office.²⁴ Perhaps because of this practice, no Oklahoma court ever addressed the issue of whether assignments of production and production payments were governed by the Code.²⁵

Another difficulty that arose under the 1961 Code was the requirement that accounts and contract rights be perfected according to the laws of the state where the borrower keeps his account records.²⁶ Whenever accounts and contract rights served as collateral, the lender had to ascertain the place where the borrower kept the records, and if in another state, perfect his security interest in accordance with the laws of that state. The requirement for out of state filing created many problems, especially where borrowers from several states were involved.²⁷

The 1972 amendments to the Code resolve these difficulties. The amended Code provides that the proper place to file is where a real estate mortgage would be filed "when the collateral is timber to be cut or is minerals or the like, including oil and gas, or accounts subject to subsection (5) of Section 7 of this act."²⁸ The Code further provides:

When a writing constituting a mortgage upon lands, or interests in lands such as oil and gas leasehold estates, also covers minerals to be severed from such lands, equipment used in mining, storing, treating and marketing such minerals and the accounts and proceeds to be derived from disposition of such minerals contains a legal description of such lands

22. See Ryan, *supra* note 4, at 417-18. Even prior to the adoption of the Code, it appears that many lawyers made chattel mortgage filings to perfect security interests in production payments. See Vagts, *supra* note 4, at 842. But see McKinnis, *The Exclusion of Oklahoma Realty Rights from Section 9 of the Uniform Commercial Code*, 36 OKLA. B.J. 513 (1965) (mortgages of assignments of production and its proceeds are not governed by the Code).

23. Ryan, *supra* note 4, at 418; Vagts, *supra* note 4, at 842.

24. See Ryan, *supra* note 4, at 417-18; Vagts, *supra* note 4, at 844-45.

25. The only case which appears to have considered the effect of the 1961 Code on oil and gas financing is *Ingram v. Ingram*, 521 P.2d 254, 260 (Kan. 1974) (mortgages of oil and gas leases are excluded from the provisions of the Code and are to be treated as real estate mortgages).

26. OKLA. STAT. tit. 12A, § 9-103(1) (1971) provides:

If the office where the assignor of accounts or contract rights keeps his records concerning them is in this state, the validity and perfection of a security interest therein and the possibility and effect of proper filing is governed by this Article; otherwise by the law (including the conflict of laws rule) of the jurisdiction where such office is located.

27. See R. HENSON, *HANDBOOK ON SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE* 346 (1979).

28. U.C.C. ch. 194, § 26, 1981 Okla. Sess. Laws (to be codified at OKLA STAT. tit. 12A, § 9-401(1)(b) (1981)).

sufficient to comply with Sections 287, 291 and 298 of Title 19 of the Oklahoma Statutes [of 1971], as amended, has been validly executed, acknowledged and recorded in the office of the County Clerk for the county in which such lands are located, such mortgage shall constitute a financing statement covering such collateral and no other filing or recording shall be required to perfect the security interests in such collateral covered by the mortgage. The mortgage shall remain effective to perfect such security interests until it shall be released or satisfied of record or its effectiveness as to lands or other interests in lands described therein shall be otherwise effectively terminated.²⁹

Under this section a mortgage on realty interests can also secure intangible and tangible personal property such as extracted oil and gas, accounts receivable, equipment, and the like.³⁰ Thus, even though the mortgage covers personalty formerly perfected as chattels, no central filing is required, and a filing of a single document in the real estate records is enough to perfect security interests in the various collateral.³¹ Furthermore, even when the lease itself does not serve as collateral, but the loan is secured by purely intangible personal property, such as accounts arising from the sale of oil and gas, the lender must still file a financing statement in the office of real estate records.³² Finally, since security interests in accounts must be perfected under the law of the state where the wellhead is located,³³ no out of state filing is required to perfect an interest in accounts arising from the sale of oil and gas.³⁴

Under the current provisions of the Code, the financing statement must contain a description of the collateral, the name and address of

29. *Id.* § 27 (to be codified at OKLA. STAT. tit. 12A, § 9-402(5) (1981)).

30. *Id.*

31. *Id.*

32. *Id.* § 26 (to be codified at OKLA. STAT. tit. 12A, § 9-401(1)(b) (1981)):

[W]hen the collateral is timber to be cut or is minerals or the like, including oil and gas, or accounts subject to subsection (5) of Section 7 of this act, or when the financing statement is filed as a fixture filing (Section 9-313) and the collateral is goods which are or are to become fixtures, then in the office where a mortgage on the real estate would be filed or recorded.

33. *Id.* § 7 (to be codified at OKLA. STAT. tit. 12A, § 9-103.1(5) (1981)):

Perfection and the effect of perfection or non-perfection of a security interest which is created by a debtor who has an interest in minerals or the like, including oil and gas, before extraction and which attaches thereto as extracted, or which attaches to an account resulting from the sale thereof at the wellhead or minehead are governed by the law, including the conflict of laws rules, of the jurisdiction wherein the wellhead or minehead is located.

34. See generally R. HENSON, HANDBOOK ON SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE 346 (1979); J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE 991 (2nd ed. 1980).

both borrower and lender, and the borrower's signature.³⁵ Moreover, the financing statement must contain a tract index description of the land and be validly executed, acknowledged and recorded.³⁶ The new provisions change prior law by adding the requirements of a tract index description of land, valid execution and acknowledgement, and by eliminating the requirement of the lender's signature.³⁷ The inclusion of the description of land in the financing statement eliminates the former requirement of a land description in the security agreement.³⁸

Oklahoma joins several other states by requiring real estate filing for perfection of security interests in minerals, including oil and gas.³⁹ The Oklahoma amendments are unique, however, in that a single document can perfect security interests in the various collateral involved in oil and gas financing.⁴⁰ The amendments to the Code are a welcome change.⁴¹ Certainly, they will simplify oil and gas financing in Oklahoma.

Ali M.M. Mojdehi

35. U.C.C. ch. 194, § 27, 1981 Okla. Sess. Laws (to be codified at OKLA. STAT. tit. 12A, § 9-402(1) (1981)).

36. *Id.*

37. *Id.* (to be codified at OKLA. STAT. tit. 12A, § 9-402(5) (1981)).

38. Compare OKLA. STAT. tit. 12A, § 9-203(1)(b) (1971) with the amended version, U.C.C., ch. 194, § 12, 1981 Okla. Sess. Laws (to be codified at OKLA. STAT. tit. 12A, § 9-203(1)(b) (1981)).

39. The 1972 version has been adopted by: Arizona, Arkansas, California, Colorado, Connecticut, Florida, Georgia, Hawaii, Idaho, Illinois, Iowa, Kansas, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Nevada, New Hampshire, New York, North Carolina, North Dakota, Ohio, Oregon, Rhode Island, Texas, Utah, Virginia, West Virginia and Wisconsin. 6A BENDER'S UNIFORM COMMERCIAL CODE SERVICE, § 9-401, at 1-974.112 (1981).

40. No other state appears to allow a single filing to perfect security interests in as many types of collateral as Oklahoma. Iowa and Texas, however, appear to allow the mortgage of real estate to cover accounts and fixtures. 6A BENDER'S UNIFORM COMMERCIAL CODE SERVICE, § 9-402, at 1-974.186, 1-974.213 to .214 (1981).

41. Article 11 governs the effect of the 1972 amendments on security interests perfected under the 1961 Code. Commercial Code — Modifications — Transitional Provisions, ch. 194, §§ 40-45, 1981 Okla. Sess. Laws (to be codified at OKLA. STAT. tit. 12A, §§ 11-102 to -107 (1981)). Filings made under the former Code are effective for any existing collateral until the date formerly specified, but not less than five years after filing. *Id.* § 42 (to be codified at OKLA. STAT. tit. 12A, § 11-104(1) (1981)). However, if the debtor acquires oil and gas related collateral after the effective date of the amendments, a financing statement must be filed in the office of the county clerk. *Id.* (to be codified at OKLA. STAT. tit. 12A, § 11-104(2) (1981)). A continuation statement will not continue perfection of existing oil and gas related collateral since the place of filing has changed. Instead, a new financing statement must be filed in the place required by the new amendments. *Id.* (to be codified at OKLA. STAT. tit. 12A, § 11-104(3) (1981)). The new financing statement can be filed at any time during the six months before a perfected security interest lapses. The financing statement can be signed by either the debtor or the secured party. It must identify the security agreement, state the place and date of the last filing, any book, page and filing number, and that the security agreement entered into prior to the adoption of the amendments is still effective. Once filed in the office of the county clerk, a financing statement may thereafter be extended by the filing of a continuation statement. *Id.* § 43 (to be codified at OKLA. STAT. tit. 12A, § 11-104(4) (1981)).

