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Contractual Interpretations, Ambiguities, and Litigation Difficulties Presented in the Context of Oil and Gas Leases as a Result of the Texas Supreme Court's Decision in *Murphy Exploration & Prod. Co.-USA v. Adams*, 560 S.W.3d 105 (Tex. 2018)

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ONE J

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CONTRACTUAL INTERPRETATIONS,
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AND GAS LEASES AS A RESULT OF THE TEXAS
SUPREME COURT'S DECISION IN *MURPHY
EXPLORATION & PROD. CO.-USA v. ADAMS*,
560 S.W.3D 105 (TEX. 2018)

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I. Introduction

The landmark case, *Murphy Exploration & Prod. Co.-USA v. Adams*, heard by the Texas Supreme Court in 2018, considered a lessee's obligation to drill an offset well in an oil and gas lease when an adjacent well commenced near the lessor's land.¹ The decision turned largely on the court's contractual interpretation of the definition of an "offset well in an oil and gas lease."² The majority opinion, articulated by Justice Lehrman, ruled that clauses involving a lessee's obligation for offset leases must be construed in light of the "context" and circumstances" occurring during the execution of the lease.³ This contractual analysis, known as "the

* I would like to extend my deepest gratitude to Professor James David Hampton for everything that he has helped me with throughout this paper. He is a wonderful mentor, role-model, and friend. I would also like to thank Bill & Kay Stiles for their tremendous and unfailing support of my academic endeavors.

1. *Murphy Expl. & Prod. Co.-USA v. Adams*, 560 S.W.3d 105 (Tex. 2018) [hereinafter *Murphy*].

2. *Id.* at 113.

surrounding circumstance doctrine” has broad implications for future oil and gas cases in Texas.

Most importantly, this case may ultimately take away from the purpose and intentions of lessors executing private contracts in oil and gas leases because it injects an area of uncertainty between the lessor and lessee as to what obligations must be sustained by the lessee with regard to an offset lease provision. Furthermore, it delegates a higher deal of responsibility for lessors to include a greater level of detail and explicit provisions in oil and gas contracts. This is to ensure that there are no misunderstandings or misconstructions of the provisions because of a potential court-interjected interpretation of the lease. Finally, the application of the surrounding circumstances doctrine may be a difficult standard to apply in order to ascertain parties’ intent in an oil and gas lease because of changes in technology, unforeseen circumstances, and because of the expansion of terms and definitions incorporated in leases.

II. A Summary of “Murphy”

Murphy Exploration & Production Company entered into a lease with two landowners for a tract of land that covered two contiguous 302 acre tracts in Attascosa County.³ The leases provided Murphy with three different alternative actions that could be pursued if a well was completed within 467 feet on the land adjacent to the leased tract.⁴ Murphy had the option to:

- (1) [C]ommence drilling operations on the lased acreage and thereafter continue the drilling of such offset well or wells with due diligence to a depth adequate to test the same formation from which the well or wells are producing from [sic] on the adjacent acreage; or
- (2) Pay the lessor royalties as provided for in this lease as if an equivalent amount of production of oil and/or gas were being obtained from the off-set location on these leased premises as that which is being produced from the adjacent well or wells; or
- (3) Release an amount of acreage sufficient to constitute a spacing unit equivalent in size to the spacing unit that would be allocated under

3. *Id.* at 107.

4. *Id.*

this lease to such well or wells on the adjacent lands, as to the zones or strata producing in such adjacent well.⁵

Comstock Oil & Gas drilled a producing horizontal well (The Lucas Well) that was on an adjacent track 350 feet away from the tracts covered by the lease.⁶ The Lucas Well triggered the offset provision included in the aforementioned lease agreement, and Murphy decided to exercise the option of drilling an offset well.⁷

The offset, horizontal well that Murphy commenced complied with the provisions of the lease insofar as the drilling commenced within 120 days of the Lucas Well's completion, and that it reached "a depth adequate to test the same formation" that the Lucas well was producing.⁸ However, the new well commenced by Murphy was undertaken approximately 1,800 feet from the pertinent lease line—causing the lessors to bring action because they believed that this location would not protect their land against drainage.⁹

Herbst (lessor), argued that the offset well drilled on his lease was too far away from the lease boundary line to qualify as an offset well.¹⁰ However, Murphy (lessee) countered and argued that the provision imposed no location or minimum spacing requirement for the offset well; it only required that the well be drilled "on leased acreage" and "to a depth adequate to test the same formation from which the well or wells are producing from on the adjacent acreage."¹¹ Murphy also argued that the provision was drafted with horizontal shale wells in mind and only required the lessee to counterbalance (or offset) production from the shale formation—recognizing that there is little to no drainage in the Eagle Ford shale, and therefore no reason to locate the offset well near the lease line.¹²

Procedurally, the trial court agreed that Murphy had satisfied the provisions of the offset lease and rendered a final judgment in favor of that

5. *Id.* (Because this case largely turns on contract interpretation, it is necessary to display the entirety of the lease in order to demonstrate how the court utilized interpretive means to achieve the holding of this case).

6. *Id.*

7. *Id.*

8. *Id.*

9. *Id.*

10. *Id.*

11. *Id.* at 108 (emphasis added to highlight the pertinent provision of the lease in dispute).

12. *Id.*

determination.¹³ However, the court of appeals reversed and remanded the trial court's ruling, reasoning that Murphy did not conclusively show that it complied with the offset provision.¹⁴

The Texas Supreme Court held that Murphy had satisfied the offset lease provision. First, the court recognized that the provision's only specific requirement with respect to where to drill "such off-set well" is that it be "on the leased acreage" and "to a depth adequate to test the same formation" from which the triggering well is producing.¹⁵ Next, the court distinguished the lessee's duty in this case, where the lease was drafted "with horizontal shale drilling in mind," versus what the lessee's duty would have been had the lease been drafted with vertical drilling in mind.¹⁶ This distinguishing feature became a paramount part of this argument because of the court's employment of the contractual obligation to "consult the facts and circumstances surrounding a negotiated contract's execution to aid the interpretation of its language" and to "inform [the court's] construction of the lease language."¹⁷

Because the offset well in this case was a horizontal well, the court reasoned that "[t]he locations of both the vertical portion of a horizontal well and the nonperforated portions of the horizontal wellbore are essentially irrelevant for production purposes."¹⁸ The court further noted that the perforated portions of the horizontal wellbore are the "points at which oil and gas is drained and produced from the surrounding rocks" and that "the tight reservoirs developed by horizontal drilling...are not susceptible to migration in the same fashion as found in formations traditionally targeted by vertical drilling."¹⁹ Finally, the court reasoned that "if the parties had intended the offset well to protect against drainage, the provision would presumably have included requirements regarding the direction and placement of the perforated portions of the horizontal wellbore."²⁰ The fact that the leases specified exactly what is to be done once the offset provision is triggered without mentioning proximity is

13. *Id.*

14. *Id.* The Texas Court of Appeals reasoned that Murphy did not satisfy the offset well provision because the well did not fit the "commonly understood meaning" of the term "offset well." Moreover, the appellate court went on to note that an offset well is generally recognized as *a well that protects against drainage*.

15. *Id.* at 110.

16. *Id.*

17. *Id.* at 111.

18. *Id.*

19. *Id.*

20. *Id.* at 112.

significant in the lease. The court interpreted this provision only to require Murphy to drill a well in accordance with the explicit terms of the lease and nothing more.²¹

The dissenting justices in this case, voting with Justice Johnson, cited two problems with the Court's position.²² First, the dissent contended that the leases must have been based on what a "reasonable premise" would have been, irrespective of what the lessors actually intended when they entered into the lease.²³ Second, the justices noted that the express language in the leases seemed to contemplate both vertical and horizontal drilling, and authorized no special treatment with respect to either type of well.²⁴

Next, the dissenting justices analyzed the context and definition of "offset wells" at the time the lease was commenced in August 2009, and found that it was contrary to what the majority established in the case. More fundamentally, the dissenters argued that the majority ignored "the consistent, longstanding industry use of the word in regard to wells."²⁵ As support for this contention, the dissenting justices referenced another Texas Supreme Court case which provides that: "[T]rade usage can illuminate the meaning of contract language because 'the meaning to which a certain term or phrase is most reasonably susceptible is the one which [is] so regularly observed in place, vocation, trade or industry so "as to justify an expectation that it will be observed with respect to a particular agreement."'"²⁶ Finally, in an effort to emphasize this important point, the Justices cited dictionaries and other supplemental, academic sources to support their reasoning that the well drilled did not constitute an offset well by traditional definition.²⁷ Traditionally, offset well is defined as "[a]n oil well dug for the specific purpose of preventing drainage of oil to the adjoining property."²⁸

21. *Id.* at 113.

22. *Id.* at 117 (Johnson, J., Dissenting).

23. *Id.*

24. *Id.*

25. *Id.*

26. *Id.*; see also *URI, Inc. v. Kleberg Cty.*, 543 S.W.3d 755, 768 (Tex. 2018) (quoting *Nat'l Union Fire Ins. Co. of Pittsburgh, PA v. CBI Industries, Inc.*, 907 S.W.2d 517, 521 (Tex. 1995)).

27. *Id.* at 121–23.

28. *Id.* at 121.

*III. Texas Oil and Gas Contract Legal Applications
and Interpretive Guidelines*

Understanding the standards and terms applied in *Murphy* is important for the subsequent discussion of its effect on oil and gas leases in Texas. Below, are the pertinent authorities utilized to inform, construct, and direct the court's holding in *Murphy*. However, these interpretive guidelines are also responsible for difficulties and ambiguities in construing oil and gas leases in the future because of *Murphy's* holding and the Justice's application of them.

In construing an oil and gas lease, as with any contract, the task is to "ascertain the true intentions of the parties as expressed in the writing itself."²⁹ Moreover, it is necessary to consider the entire writing of a contract so to "harmonize and give effect to all the provisions of the contract so that none will be rendered meaningless."³⁰ Further, a court in interpreting an oil and gas contract should "give terms their plain, ordinary, and generally accepted meaning unless the instrument shows that the parties used them in a technical or different sense."³¹ Perhaps most importantly, in considering an oil and gas lease, where the lease "expressly defines a duty, [a court] [shall] not impose a more stringent obligation *unless it is clear that the parties intended to do so.*"³²

When an oil and gas lease is ambiguous, a court may "consult the facts and circumstances surrounding a negotiated contract's execution to aid the interpretation of its language."³³ However, there is a limitation that is imposed when considering the surrounding circumstances of an oil and gas lease insofar as "[C]ourts may not rely on evidence of surrounding circumstances to make the language say what it unambiguously does not say."³⁴

29. *Italian Cowboy Partners, Ltd. v. Prudential Ins. Co. of Am.*, 341 S.W.3d 323, 333 (Tex. 2011).

30. *Seagull Energy E & P, Inc. v. Eland Energy*, 207 S.W.3d 342, 345 (Tex. 2006).

31. *Heritage Res., Inc. v. NationsBank*, 939 S.W.2d 118, 121 (Tex. 1996).

32. *Exxon Corp. v. Emerald Oil & Gas Co.*, 348 S.W.3d 194, 215 (Tex. 2011).

33. *URI, Inc.*, 543 S.W.3d at 768.

34. *First Bank v. Brumitt*, 519 S.W.3d 95, 110 (Tex. 2017).

IV. Distinguishing Bell v. Chesapeake Energy Corp., 2019 Tex. App. LEXIS 1978 from Murphy: Considering Express Language in Oil and Gas Leases and the Application of the “surrounding circumstances doctrine.”

In *Bell*—a seminal case in the interpretation of oil and gas leases—the language employed in the lease contained spacing requirements that compelled the lessee to drill an offset well if a producing well was drilled on an adjacent property.³⁵ Moreover, under the *Bell* lease, Chesapeake (the defendant) agreed “(1) to drill such offset wells which is *reasonably designed to protect the Leased Premises from drainage*, or at the option of Lessee, shall (2) pay to Lessor the Compensatory Royalties set forth below, or (3) execute and deliver to Lessor a recordable form releasing acreage to drill an offset well to the formation of such Adjacent Well.”³⁶ Chesapeake contended that its obligations under the lease were qualified by the reasonably prudent operator standard, which provides that an operator need not drill an offset well to protect the leased premises from drainage unless there is proof of “(1) substantial drainage of the lessor’s land, and (2) that a reasonably prudent operator would have acted to prevent substantial drainage from the lessor’s land.”³⁷ Unlike the lease in *Murphy*, the *Bell* Lease contained language demonstrating that the parties intended for the offset clause to operate in the context of drainage.³⁸ This proved to be a pertinent, distinguishing factor between the two cases. The provision that Chesapeake drill “such offset wells which is reasonably designed to protect the leased premises from drainage” demonstrated that there was an intent by the writers of the lease that the offset well should be drilled in proximity to the adjacent well on the property.³⁹

This has been the strongest deviation from the court’s ruling in *Murphy*. The deviation illustrates that it is now imperative for drafters of oil and gas leases to include some provision referencing “drainage” in order to effectuate his/her offset well being drilled in a proximate location to the adjacent land. The deviation also reflects the care and diligence that is needed to draft any new oil and gas lease because of the courts need for clarity regarding terms, such as “offset”—which traditionally had drainage implications—to expressly confirm the purpose of the well in the lease if

35. *Bell v. Chesapeake Energy Corp.*, 2019 WL 1139584, No. 04-18-00129-CV, (Mar. 13, 2019).

36. *Bell*, 2019 WL 1139584, at 4. (emphasis added).

37. *Id.* (quoting *Amoco Prod. Co. v. Alexander*, 622 S.W.2d 563, 568 (Tex. 1981)).

38. *Id.* at 12.

39. *Id.*

the condition is triggered. Finally, Murphy's decision may carry grim implications for older leases that relied on the traditional definitions and interpretations of oil and gas leases before *Murphy* was decided.

The oil and gas industry is constantly evolving in the realm of technology and in many other facets. Such developments may alter or transform common definitions associated with the industry that may result in ambiguity in construing a lease. This notion is especially true when considering the surrounding circumstances doctrine relied on in *Murphy*. As a result, one's private contractual ability may be rendered null with regard to a term that would have been expressly understood, before *Murphy* was decided in 2018. It is important to consider that the lease in *Murphy* was drafted in August of 2009, with litigation over the issue occurring nearly a decade later. The original drafters, without including the term "drainage" or any other aiding term for the court to construe this otherwise unambiguous term, were not aware that such a term would be called into question. This casts a shadow of uncertainty over contractual intent in oil and gas leases going both backwards and forward in time.

V. The Interpretation of the Term "Offset" as it applies to Oil and Gas Leases and Why the Majority Got It Wrong in Murphy

The majority's application of the surrounding circumstances doctrine should not have been so strictly applied to the geographical and physical considerations of the leased property. The doctrine should have been applied more relatively to the surrounding contexts and circumstances of the terms and provisions of the contract itself, based on industry standards and usage. Because the majority focused on the leases surrounding the property, instead of the parties' original intentions, the surrounding circumstances doctrine did not align with the requirement that contract terms be given their "plain, ordinary, and generally accepted meaning", and the court's duty to "ascertain the true intentions of the parties"⁴⁰ For instance, in evaluating the term "offset," the Texas Supreme Court used the definition provided by Webster's Dictionary—taking the word's definition to mean that to be an offset well it must "counterbalance" or "compensate" for the adjacent well's production.⁴¹ In reaching this conclusion, the court only looked to the word "offset," which can be utilized in a variety of

40. See *supra* note 1, at 108 (quoting *Heritage Res., Inc. v. NationsBank*, 939 S.W. 2d 118, 121 (Tex. 1996)); see also *Italian Cowboy Partners, Ltd. v. Prudential Ins. Co. of Am.*, 341 S.W.3d 323, 333 (Tex. 2011).

41. *Id.* (citing *Offset*, WEBSTER'S INT'L DICTIONARY (3d ed. 2002)).

different contexts.⁴² As a result, the majority ignored the actual plain meaning of the entirety of the term “offset well” which has been interpreted by scholars to mean the following: “[A] well drilled on one tract of land to prevent the drainage of oil or gas to an adjoining tract of land, on which a well is being drilled or is already in production.”⁴³ In an effort to emphasize this key point, Justice Johnson in his dissenting opinion cited over two pages in the reporter of definitions for the term “offset well”, to demonstrate that the way the majority applied the term in its analysis was incorrect because of its nonconformity with industry custom.⁴⁴

Moreover, in *Valence Operating Co. v. Dorsett*, a 2005 Texas Supreme Court case that interpreted notice provisions in an oil and gas operating agreement, the Court utilized a standard of review requiring that “[C]ontract terms are given plain, ordinary, and generally accepted meanings unless the contract itself shows them to be used in a technical or different sense.”⁴⁵ Naturally, Texas courts have interpreted this language to mean that “[i]f a lease term has a generally accepted meaning in the oil and gas industry, we [the court] use its generally accepted meaning.”⁴⁶ The dissenting Justices again noted that there have been several instances and cases considered by the Court in which there seemed to be no need to demonstrate or interpret the application of the term or explain its meaning because it presumptively carried weight and understanding as an industry term.⁴⁷ Moreover, the concept of an offset well is by no means a novel term in the industry and has been recognized by the Texas Supreme Court as early as 1928.⁴⁸ Several Texas Supreme Court cases have since discussed the implications of offset clauses in oil and gas leases—making it difficult to understand just how the majority arrived at this result if they were truly

42. For instance, a google search of the definition of the word “offset” provides a variety of different areas in which the word has been used in different contexts such as in the fields of surveying, electronics, finances, and architecture. Conducting a basic search of the term “offset” curiously did not pull up any offset well definitions or references.

43. PATRICK H. MARTIN & BRUCE M. KRAMER, *WILLIAMS & MEYERS, OIL AND GAS LAW*, 689 (Matthew Bender ed., LexisNexis 2019).

44. *See supra* note 1, at 121-23 (Johnson, J., dissenting).

45. *Valence Operating Co. v. Dorsett*, 164 S.W.3d 656 (Tex. 2005).

46. *PNP Petroleum I, LP v. Taylor*, 438 S.W.3d 723 (Tex. App. 2014).

47. *See supra* note 1, at 124 (Johnson, J., dissenting); *see* *Hooks v. Samson Lone Star, Ltd.*, 457 S.W.3d 52, 67-8 (Tex.2015); *Lesley v. Veterans Land Bd.*, 352 S.W.3d 479, 488 (Tex. 2011).

48. *Texas Pacific Coal & Oil Co. v. Barker*, 6 S.W.2d 1031 (Tex. 1928).

abiding by the required mandates set forth in interpretive precedent on the issue.⁴⁹

VI. The Development of Future Technology in the Oil Industry and How it May Affect Lease Interpretation Under the Surrounding Circumstance Doctrine

The interpretation of an oil and gas lease requires that the court consider the circumstances present at the execution of the lease.⁵⁰ However, these circumstances can change or can be ambiguous in themselves with the oil industry because it is constantly evolving and changing in response to drilling technology and other innovations for the production of energy. Consequently, a lessor may not be aware of the ever-changing circumstances or recent developments at the time a lease is executed with the production company/lessee. Therefore, the surrounding circumstance doctrine may cause more ambiguity and disarray instead of guiding the court to a reasonable answer as to the parties' intent. In order to understand how important this notion is with regard to contract interpretation, one must comprehend just how much the United States relies on the oil and gas industry, and the amount of resources that are incorporated for the funding of the industry.

The United States utilizes fossil fuels as its primary source of energy, with fossil fuels accounting for approximately 82% of the energy consumed in America.⁵¹ Moreover, on a much larger scale, the United States' reliance on hydrocarbons for energy carries with it a large implication and impact on the global economy.⁵² Because of this impact, there is a natural incentive to continuously revolutionize the industry to be as efficient and as profitable as possible—leaving a need for technological development to effectuate this process.

This technological development has largely taken place in three pertinent areas in the oil and gas industry: horizontal drilling, extension, and

49. See *Shell Oil Co. v. Stansbury*, 410 S.W.2d 187 (Tex. 1966); *Commonwealth of Massachusetts v. Davis*, 168 S.W.2d 216, 223 (Tex. 1942).

50. *Nat'l Union Fire Ins. Co. of Pittsburgh v. CBI Indus., Inc.*, 907 S.W.2d 517 (Tex. 1995) (reasoning that in order to determine whether a contract is ambiguous one must look to the circumstances present when the contract was entered).

51. *Advancing Systems and Technologies to Produce Cleaner Fuels, Oil and Gas Technologies: Subsurface Science, Technology, and Engineering*, U.S. DEPT. OF ENERGY (2015), <https://www.energy.gov/sites/prod/files/2016/05/f32/Ch.7-SI-Oil-and-Gas-Technologies.pdf>.

52. *Id.* at 2.

hydraulic fracturing.⁵³ For instance, there are over 1 million hydraulically fractured wells in the United States; this number is expected to rise and may account for approximately 70% of natural gas production in the United States.⁵⁴ The topic and development of horizontal wells has been increasingly necessary in the United States for producers to utilize in important geographic areas to extract hydrocarbons by exploiting shale plays from regions all across America; and largely throughout Texas.⁵⁵

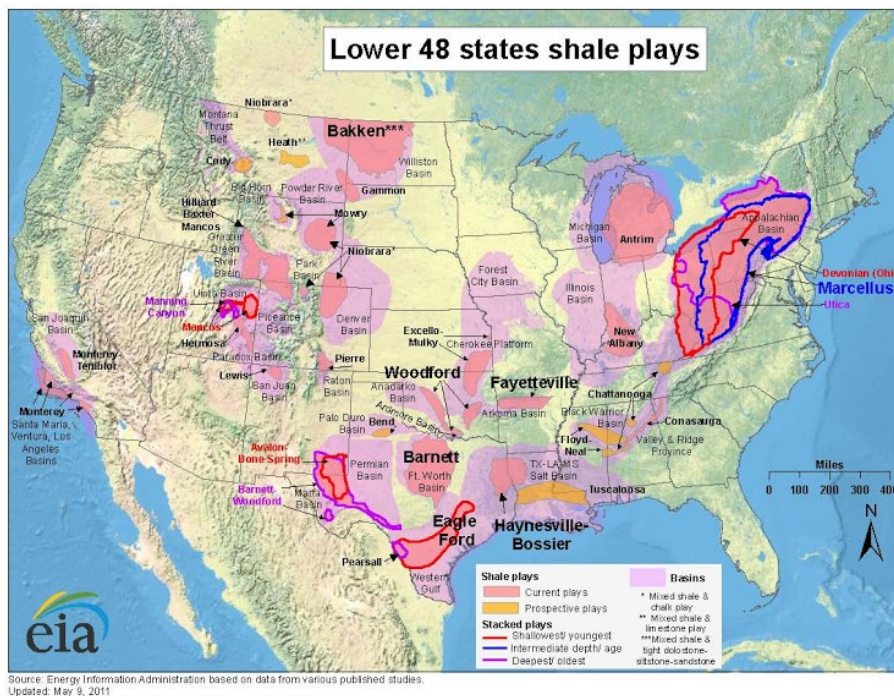


Image by the U.S. Energy Information Administration: Hydraulic Fracturing, The Strauss Center (2014), <https://www.strausscenter.org/energy-and-security/hydraulic-fracturing.html> (last visited Jan 1, 2020).

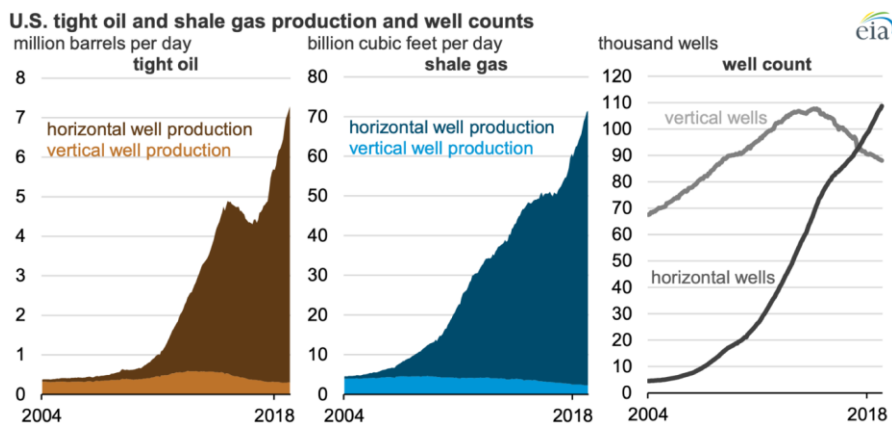
Moreover, with the availability of new technology, producing companies are able to target considerably more geographic areas in order to extract

53. *Id.*

54. Hydraulic Fracturing, THE STRAUSS CENTER (2014), <https://www.strausscenter.org/energy-and-security/hydraulic-fracturing.html> (last visited Jan 1, 2020).

55. *Id.*

hydrocarbons, such as shale plays. Shale plays are different from a traditional reservoir because the shale acts as “both the source *and* the reservoir of the natural gas.”⁵⁶ Scholars have noted that “[w]hile older shale gas or oil wells were usually vertical, more recent shale gas and oil wells often take advantage of advances in directional drilling technology to achieve a horizontal drainhole to extract from the target shale or other formation.”⁵⁷ For example, some formations in the Permian Basin, a dominant producing area of West Texas, were historically drilled with vertical wells (accounting for 96% of production in the area); however, over the course of 14 years, the industry reported that vertical wells accounted for only 4% of production for those same formations, noting that the industry had turned to the utilization of horizontal wells to produce.⁵⁸



In furtherance of the need to develop technology, there have been significant funds imposed to aid in the development of oil and gas technology. One example of this tremendous expenditure into the industry was a 39-million-dollar amount announced by the Department of Energy for oil and gas research projects.⁵⁹ Rick Perry, U.S. Secretary of Energy, stated: “The United States is projected to become a net energy exporter by

56. JOHN S. LOWE ET AL., CASES AND MATERIAL ON OIL AND GAS LAW (7th ed. 2018).

57. *Id.* at 19.

58. *Horizontally Drilled Wells Dominate U.S. Tight Formation Production*, U.S. ENERGY INFO. ADMIN. (June 6, 2019), <https://www.eia.gov/todayinenergy/detail.php?id=39752>.

59. *Department of Energy Announces \$39 Million for Oil and Natural Gas R&D Projects*, U.S. DEPT. OF ENERGY (April 16, 2019), <https://www.energy.gov/articles/department-energy-announces-39-million-oil-and-natural-gas-rd-projects>.

2022, and by improving technologies that enhance the efficiency of producing and recovering oil and natural gas, we can be sure to achieve that title.”⁶⁰

All of the technological developments that have occurred in the oil industry, and that will continue to occur, may have an adverse impact on oil and gas leases because of their contractual nature.⁶¹ Texas law mandates that contractual interpretation be done by “giv[ing] words and phrases their *generally accepted meaning* reading them in context and in light of the rules of grammar and *common usage*.”⁶² Because lessors and operating companies alike can not foresee technological developments in the industry, especially under circumstances such as in *Murphy* where the lease may be around a decade old before its terms are contested, the interpretation of a contract may become increasingly difficult with the application of the holding in *Murphy*. For instance, the changes that occurred in the Permian Basin from 2004-2018 with respect to the shift of reliance to horizontal wells rather than vertical wells because of the development of technology in the industry would likely change what the lessor’s had originally understood as to what rights and protections their leases encompassed.

Furthermore, because there are two primary goals that a lessee has with regard to the purpose of the lease and lease formation: (1) “seek[ing] the rights to explore, drill, develop, and produce for an initial term without obligations to do so; and (2) if production is obtained the lessee wants the right to maintain the lease for as long as it makes business sense to do so”—the lessee may try to avail himself of older understood contractual terms so as to avoid expending a considerably higher amount of resources on the most current technology.

In conclusion, no party to a contract is able to foresee the changes in circumstances that may occur, especially in an industry as complicated and technologically advanced as the oil and natural gas industry. A reliance on terms that may become archaic may detract from what a lessor intends or hopes to implicate in the contract with regard to the obligations and duties of a lessor. Under *Murphy*, it is apparent that a lessor should make terms explicit in what he/she expects from a lessee in crucial areas regarding issues such as drainage, and the protection of other interests that the lessor can’t protect herself.

60. *Id.*

61. See LOWE ET AL., *supra* note 56, at 189 (noting that a lease is a contract because it is burdened with certain express and implied promises).

62. Penn Ins. and Annuity Co. v. Kuriger, 495 S.W. 3d, 540, 546 (Tex. App. 2016).

*VII. The Expansion of Terms and Definitions In the Oil and Gas Industry
Make It Important For Courts to Interpret Terms According to Industry
Custom*

Historically, the oil and gas industry has “not been terribly responsive to judicial opinions, changes in industry custom and practice, or common sense” in the realm of development and use of written agreements.⁶³ Moreover, as technology continues to advance and terms for new innovations become a central part of the industry, the definitions for those provisions and terms become increasingly important to interpret according to their plain meaning—derived from industry custom. The expansion of terms and definitions in the industry has become vast. Professor Bruce Kramer noted, “the Manual of Oil and Gas Terms [at its 14th edition] covers over 1,500 pages” of terms and definitions that have arisen because of the industry’s progress.⁶⁴ Similarly, Professor Anderson stated that the expansion of oil and gas exploration has imposed a great impact on terms and definitions in the industry, and has reinforced the notion that in some cases “what is good for the oil and gas lessee is not necessarily good for the oil and gas lessor.”⁶⁵ In addition to his statement, Anderson placed an emphasis on giving terms their ordinary meaning, noting that “in order to negotiate effectively a lease or otherwise represent a lessor or surface owner, lawyers must know the vocabulary.”⁶⁶

Although it is clear that oil and gas leases differ with regard to each specific lease, the general structure that a lease creates between a lessor and lessee are normally very similar.⁶⁷ This similarity amongst leases has created a number of oil and gas clauses, generally with analogous language, which typically sets out the obligations of the lessee in order to provide a beneficial relationship between the parties.⁶⁸ Lessor’s rely on these

63. Bruce M. Kramer, *Keeping Leases Alive in the Era of Horizontal Drilling and Hydraulic Fracturing: Are the Old Workhorses (Shut-in, Continuous Operations, and Pooling Provisions) Up to the Task?*, 49 WASHBURN L.J., 283 (Winter 2010).

64. *Id.* See also PATRICK H. MARTIN & BRUCE M. KRAMER, WILLIAMS & MEYERS: MANUAL OF OIL AND GAS TERMS (14th ed. 2009).

65. Owen L. Anderson, *David v. Goliath: Negotiating the “Lessor’s 88’ and Representing Lessors and Surface Owners in Oil and Gas Plays*, 27 ROCKY MT. MIN. L. INST. 2 (1982).

66. *Id.*

67. David E. Pierce, 22 TULSA L.J. 445, 446 (Summer 1987).

68. *Id.* at 447. These provisions include the granting clause, savings clause, habendum clause, and continuous production clause, among others.

provisions and terms in order to protect their respective mineral rights from the developer, who generally provides the contract.⁶⁹

Even when there are no express provisions in an oil and gas contact, courts have recognized a need to protect the lessor under certain circumstances; these circumstances are manifested in the six major oil and gas implied covenants.⁷⁰ These covenants are also significant because “the lessors and lessees cannot anticipate all of the particular circumstances that will exist when production is realized.”⁷¹

Taken together, the expansion and development of new terms in the oil and gas industry may create costly uncertainty in the interpretation of typical lease agreements when they are not interpreted according to their industry definition. This is most evident in the inconsistent decisions handed down by courts attempting to properly apply the surrounding circumstance doctrine. For instance, in determining what surrounding circumstances were appropriate to incorporate when attempting to ascertain the terms and definitions of a contract, one Texas court aired their frustration: “What [] surrounding circumstances [are] to one court is parol evidence to another . . . case law on this issue is less than consistent at times.”⁷²

Moreover, the inconsistency and uncertainty regarding the application of the surrounding circumstances doctrine is clearly evidenced by the Texas Supreme Court’s 5-4 decision in *Murphy*—effectively showing that even the state’s highest court has had trouble discerning what a relevant circumstance is, and to which circumstances appropriately “inform [the court’s] construction of the lease language.” As a result, utilizing an oil and gas term’s common industry meaning in order to ascertain a party’s intent

69. *Id.*

70. Slate Olmstead, *Frac Sand, Hydraulic Fracturing, and Implied Covenants: The Potential for Liability*, 3 OIL & GAS, NAT. RESOURCES & ENERGY JOURNAL, 1395 (2018). The six major oil and gas covenants include: (1) the implied duty to develop; (2) the implied duty to explore; (3) the implied duty to protect against drainage; (4) the implied duty to market; (5) the implied duty to accommodate; and (6) the implied duty of prudent operation for the mutual benefit of the lessor and lessee. *See also* John Burritt McArthur, *U.S. Oil and Gas Implied Covenants and Their Functions: “As Much a Part of the Contract—Is as Effectually One of Its Terms—As if Had Been Plainly Expressed,”* 61 ROCKY MT. MIN. L. INST. 29-1, 7 (2015).

71. James C. Wright, Brian J. Pulito, & Cheryl L. Davis, *Implied Covenants in Oil and Gas Leases in the Appalachian Basin*, 19 TEX. WESLEYAN L. REV 121, 122 (2012).

72. *Lind v. Int’l Paper Co.*, No. A-13-CV-249-DAE, 2014 U.S. Dist. Lexis 116412 (W.D. Tex. 2014).

under an oil and gas contract should be given the greatest weight in the context of applying the surrounding circumstances doctrine.

VIII. Oil Booms: Unexpected Circumstances and Their Potential Effect on the Application of the Surrounding Circumstances Doctrine

Throughout Texas' history and other large oil-producing states, many areas of land have had unforeseeable developments in the oil and gas industry. Such unexpected changes could present problems going forward with the surrounding circumstance doctrine applied in *Murphy*. This is because there may be areas in which the discovery of oil is so novel that there may be no other wells or surrounding circumstances for which the court could interpret the parties' intentions.

The presence of oil in Texas, first discovered in 1543, has long been a prevalent factor in the societal and economical welfare of the state.⁷³ Throughout the history of Texas, many unexpected oil booms have occurred and have surprised landowners.⁷⁴ On January 10, 1901, "Spindletop" an enormous geyser of oil in Jefferson County, exploded and created the origin for the Texas oil industry; many major oil and gas corporations found their beginning here.⁷⁵ Oil discoveries in North Texas began to occur between 1902 and 1910 throughout areas such as Wichita Falls, Brownwood, and Petrolia⁷⁶ prompting the discovery of oil in East Texas in the 1930's, which became the "biggest oil field in the world."⁷⁷

73. Mary G. Ramos, *Oil and Texas: A Cultural History*, TEXAS ALMANAC (2017), <https://texasalmanac.com/topics/business/oil-and-texas-cultural-history> (last visited Jan 26, 2020). Spanish Explorers in 1543, led by Luis de Moscoso Alvarado, were among the first Europeans to discover oil in Texas. They made this discovery by seeing oil floating on the surface of the water and subsequently used it to caulk their boats.

74. *Id.* The Texas Almanac has compiled a chart listing the major chronological oil and gas discoveries in Texas. This list includes over 100 different field discoveries ranging vastly across different counties and areas of the state. Moreover, these major discoveries occur over a period of 60 years (1894-1954). Almanac for reference: <https://texasalmanac.com/sites/default/files/images/other/oil10.pdf>

75. *Spindletop*, HISTORY.COM (June 10, 2019), <https://www.history.com/topics/landmarks/spindletop>. Some of titan corporations in the field of oil and gas began around the Spindletop area as a result of the discovery of this enormous Geyser. These companies included Gulf Oil, Texaco, and Exxon.

76. *See* Ramos, *supra* note 73. These discoveries were often made by farmers who were attempting to create water wells in order to provide for their livestock.

77. Van Craddock, *Way back in 1915, an oil well had been drilled near Kilgore. It was a dry hole.*, LONGVIEW NEWS JOURNAL (Oct. 1, 2016), https://www.news-journal.com/news/local/way-back-in-an-oil-well-had-been-drilled-near/article_b8c0472c-eb16-5aec-84a9-1e768818ea44.html. This oil discovery provided important economic benefits not only for

Since then, the Texas oil industry has encountered a dynamic history of “booms and busts.”⁷⁸ Most notably, these booms have occurred in the 1970’s, 1980’s and in the mid 2000’s.⁷⁹ However, despite the many busts that have occurred throughout the period, Texas remains the world’s top oil producer.⁸⁰

In some cases, particularly those dealing with shale formations, many Texas landowners in the past were not aware of their legal rights, which left them unable to effectively negotiate favorable contractual provisions for their own leases for fear of “missing out” on a deal with a production company.⁸¹ For example, in 2006, citizens around Fort Worth experienced an incredible oil boom that resulted in more than 6,600 natural-gas wells in the area the following year; producing 2.6 trillion cubic feet of natural gas annually ever since.⁸² Due to the tremendous influx of wells in an urban area, naturally, many citizens and attorneys in the area were unprepared when signing and interpreting the provisions of their leases, leaving questions as to whether many of those contracts should be deemed unconscionable—meaning an unfair bargaining power between parties.⁸³

Moreover, scholars have noted that “in the second decade of the twenty-first century, oil and gas lessees, with easier access to information, tend to be more sophisticated” granting them “much greater bargaining power than they enjoyed a generation ago.”⁸⁴ This seemed to occur early in the aforementioned Barnett Shale boom during which early signers of oil and gas leases were offered a substantially lower amount of compensation per acreage and royalty percentage as compared to the offers that were

Texas, but also for the entire nation because of the Depression and an unprecedented two-year drought for many landowners in the area. As of 2016, the East Texas Field which housed the famous well “Daisy Bradford #3” has produced approximately 5.3 billion barrels of oil.

78. Spencer Salmon, *Booms and Busts: Preserving Mother Nature While Staring Into the Abyss Of Bankruptcy*, 16 TEX. TECH. ADMIN L.J. 465 (2015).

79. *Id.*

80. *Id.* See also Robert Rapier, *The Permian Basin Is Now The World's Top Oil Producer*, FORBES (Apr. 5, 2019), <https://www.forbes.com/sites/rrapier/2019/04/05/the-permian-basin-is-now-the-worlds-top-oil-producer/#73501b653eff>.

81. Zach J. Burt, *Playing the Wild Card in the High Stakes Game of Urban Drilling: Unconscionability in the Early Barnett Shale Gas Leases*, 15 TEX. WESLEYAN L. REV. 1.

82. *Id.* at 6.

83. See *id.* at 1, 3.

84. Byron C. Keeling, *In the New Era of Oil and Gas Royalty Accounting: Drafting A Royalty Clause That Actually Says What the Parties Intend It to Mean*, 69 BAYLOR L. REV. 516, 517 (Fall, 2017).

presented to some landowners only a little bit later.⁸⁵ This prompted the notion that “the only difference between a good lease and a bad lease can be a substantial amount of money.”⁸⁶

With lease agreements varying so substantially in common areas such as the Barnett Shale formation, the surrounding circumstance doctrine could be very difficult to apply. This is especially true here, in a context where many lessees are unaware of how other leases may be governed, interpreted, applied, and even construed with regard to the production companies that they signed with. Because each lease in geographic area could potentially differ drastically in the context of another oil boom, the Texas Supreme Court should have relied on common terms, such as the “offset well provision” applied in *Murphy* to stay true to its common industry meaning—just as the dissent argued.

The history of Texas suggests that the oil industry will continue to have booms and busts as long as there is a petroleum need in the United States. By not applying the common terms associated with the industry and instead looking to other leases and wells in the area in order to apply the surrounding circumstance doctrine set forth in *Murphy*, lessees will continue to be disadvantaged in the face of new oil and gas discoveries and booms that will continue to occur because of better technology and an evolving society that will continue to incorporate oil and gas into its everyday uses and needs.

IX. Conclusion

In conclusion, the *Murphy* case is largely problematic for parties to a lease that have not provided express and clear-cut definitions regarding what constitutes an offset lease. Consequently, this may lead to unclear obligations for lessees as to what is required of them by the lease. Moreover, the *Murphy* holding may interfere with lessor’s ability to effectuate his or her goals in a private contract. One of the principle foundations of a contract is to effectuate the parties’ intent either by way of traditional canons, or by other means. Here, this extra duty to explicitly

85. Brian J. Steinocher *Regulate or Be Regulated: Why Professional Landmen Should Be Proactive in Protecting the Integrity of Their Occupation*, 4 TEX. A&M. J. PROP L. 383, 389 (2018). This article noted that lease offers ranged between \$300 to \$400 dollars per residential lot, with royalties between 12.5% and 18.5% and subsequently rose to offers as high as 18,250 per acre with up to a 27.5% royalty.

86. *Id.* at 388.

include terms and provisions that used to be established clearly via industry standards may affect both past and present leases.

Furthermore, the expansion of the industry both technologically, and in terms of new definitions that may be used in oil and gas leases in the future, make it necessary that an oil and gas term's commonly understood industry meaning be given the most weight in applying the surrounding circumstance doctrine. By applying the law in this way, Texas courts will be able to interpret contracts in a way that better gives effect to the party's intent, and will greatly resolve the ambiguity and uncertainty that will come as a result of the ruling in *Murphy*.