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## Oil and Gas Liens in Oklahoma

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# OIL AND GAS LIENS IN OKLAHOMA

TIMOTHY C. DOWD\*

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### I. Introduction

A discussion of oil and gas liens seems like "deja vu, all over again."<sup>1</sup> The economic downturn of the 1980s led to a number of seminars and written material regarding oil and gas liens and foreclosure of such liens. Since the late 1980s, litigation surrounding oil and gas liens has diminished. While the number of liens (and subsequent bankruptcies) has also diminished, operators of oil and gas wells still have the occasional problem of payment. This paper examines the purpose, procedure and scope of oil and gas liens in Oklahoma.

### II. Statutory Liens

#### A. Mechanics' and Materialmen's Liens

Liens are created either by statute or by contract.<sup>2</sup> A lien is a charge unpaid upon specific property, "by which it is made security for the performance of an act."<sup>3</sup> Mechanics' and materialmen's liens provide a means of enforcing the valid claims of suppliers of materials and labor.<sup>4</sup>

The lien gives secondary protection if the primary contractual rights fail.<sup>5</sup> A mechanics' and materialmen's lien has been compared to a notice of lis pendens.<sup>6</sup> The lien serves as a notice and achieves a priority status to subsequent creditors or purchasers.<sup>7</sup>

Mechanics' and materialmen's liens were not recognized at common law or allowed in a court of equity.<sup>8</sup> Statutory liens, like mechanics' and materialmen's liens, are in derogation of the common law, and therefore, must be strictly construed.<sup>9</sup> Once a lien is properly filed, however, Oklahoma courts have liberally construed the enforcement provisions.<sup>10</sup>

#### 1. Person Entitled to a Lien

Oklahoma, like many other states, has enacted an oil and gas lien statute.<sup>11</sup> The

1. Attributed to Larry "Yogi" Berra, date unknown.

2. See 42 OKLA. STAT. § 6 (1991); *Taylor v. B. B. & G. Oil Co.*, 249 P.2d 430, 433 (Okla. 1952).

3. See 42 OKLA. STAT. § 1 (1991); *Williamson v. Winningham*, 186 P.2d 644, 650 (Okla. 1947).

4. See, e.g., *Riffe Petroleum Co. v. Great Nat'l Corp.*, 614 P.2d 576, 579 (Okla. 1980).

5. See *Gaddis-Walker Elec. Co. v. Phillips Petroleum Co.*, 526 P.2d 964, 967 (Okla. Ct. App. 1974).

6. See *Sawyer v. Shick*, 120 P. 581, 582 (Okla. 1911).

7. See *Cyclone Drilling & Workover v. Woods*, 671 P.2d 688, 690 (Okla. Ct. App. 1983).

8. See *Permian Corp. v. Armcop Steel Corp.*, 508 F.2d 68, 75 (10th Cir. 1974); 2 LEONARD A. JONES, A TREATISE ON THE LAW OF LIENS § 1184, at 177-78 (3d ed. 1914).

9. See *Kratz v. Kratz*, 905 P.2d 753, 758 (Okla. 1995); *Republic Bank & Trust Co. v. Bohman Minerals, Inc.*, 661 P.2d 521, 523 (Okla. 1983).

10. See *Kratz*, 905 P.2d at 758; *Davidson Oil Country Supply v. Pioneer Oil & Gas Equip. Co.*, 689 P.2d 1279, 1280-81 (Okla. 1984).

11. See 42 OKLA. STAT. § 144 (1991). The statute provides:

Any person, corporation, or copartnership who shall, under contract, expressed or implied, with the owner of any leasehold for oil and gas purposes, or the owner of any gas pipeline

statute is designed to protect laborers<sup>12</sup> or materialmen.<sup>13</sup> The Oklahoma statute recites that a lien may be claimed by "any person, corporation, or co-partnership" who performs labor or services, including a geologist or petroleum engineer."<sup>14</sup>

The operator of an oil and gas well is also entitled to claim a mechanics' and materialman's lien. In *Amarex, Inc. v. El Paso Natural Gas Co.*,<sup>15</sup> the Oklahoma Supreme Court responded to a certified question of whether an operator of oil and gas wells may claim an operator's lien by filing a lien in the form of a mechanics' and materialman's lien statement. The court held that a Title 42 oil and gas lien is available to an operator and is enforceable against nonoperators, if the filing complies with the statutory requirements.<sup>16</sup>

The *Amarex* court disagreed with a 1984 bankruptcy court decision holding, based on a 1916 Oklahoma Supreme Court opinion, that an operator was not entitled to a statutory lien on the interest of a nonoperating working interest.<sup>17</sup> In discussing

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or oil pipeline, or with the trustee or agent of such owner, perform labor or services, including written contracts for the services of a geologist or petroleum engineer, or furnish material, machinery, and oil well supplies used in the digging, drilling, torpedoing, completing, operating, or repairing of any oil or gas well, or who shall furnish any oil or gas well supplies, or perform any labor in constructing or putting together any of the machinery used in drilling, torpedoing, operating, completing, or repairing of any gas well, or perform any labor upon any oil well supplies, tools, and other articles used in digging, drilling, torpedoing, operating, completing, or repairing any oil or gas well, shall have a lien upon the whole of such leasehold or oil pipeline, or gas pipeline, or lease for oil and gas purposes, the buildings and appurtenances, the proceeds from the sale of oil or gas produced therefrom inuring to the working interest, exempting, however, any valid, bona fide reservations of oil or gas payments or overriding royalty interests executed in good faith and payable out of such working interest, and upon the material and supplies so furnished, and upon any oil well supplies, tools, and other articles used in digging, drilling, torpedoing, operating, completing, or repairing any oil or gas well, and upon the oil or gas well for which they were furnished, and upon all the other oil or gas well fixtures and appliances used in the operating for oil and gas purposes upon the leasehold for which said material and supplies were furnished or labor or services performed. Such lien shall be preferred to all other liens or encumbrances which may attach to or upon said leasehold for gas and oil purposes and upon any oil or gas pipeline, or such oil and gas wells and the material and machinery so furnished and the leasehold for oil and gas purposes and the fixtures and appliances thereon subsequent to the commencement of or the furnishing or putting up of any such machinery or supplies; and such lien shall follow said property and each and every part thereof, and be enforceable against the said property wherever the same may be found; and compliance with the provisions of this article shall constitute constructive notice of the lien claimant's lien to all purchasers and encumbrancers of said property or any part thereof, subsequent to the date of the furnishing of the first item of material or the date of the performance of the first labor or services.

*Id.*

12. See *Oklahoma Tool & Supply Co. v. Smith*, 246 P. 1090, 1090 (Okla. 1926).

13. See *Davidson Oil*, 689 P.2d at 1280 (affirming award of attorneys fees against competing lien claimant in successful suit by operator against nonoperators).

14. 42 OKLA. STAT. § 144 (1991).

15. 772 P.2d 905 (Okla. 1987).

16. *Accord Ladder Energy Co. v. Intrust Bank, N.A.*, 931 P.2d 83 (Okla. Ct. App. 1996) (affirming award of attorney's fees against competing lien claimant in successful suit by operator against nonoperators); see *Amarex*, 772 P.2d at 909.

17. See *In re George Rodman, Inc.* 38 B.R. 826, 829 (Bankr. W.D. Okla. 1984) (citing Uncle Sam

the 1916 decision in *Uncle Sam v. Richards*,<sup>18</sup> the *Amarex* court did not find any significant distinction between an operator who owns an interest in the lease and one who does not. The court also opined that the statutory language of "[a]ny person, corporation or copartnership" in title 42, section 144 of the Oklahoma Statutes does not indicate that it excludes an owner in the well. In *Amarex*, the Oklahoma Supreme Court overruled *Uncle Sam v. Richards* to the extent that it was inconsistent.<sup>19</sup>

*Amarex* left a related issue undecided: if the lien statute must be interpreted strictly, does the omission of limited liability companies in the statute prevent LLC's from asserting a lien?

### 2. Services Under the Statute

The Oklahoma statute broadly defines the kind of services that claimants may perform to be entitled to a lien. Title 42, section 144 expressly allows a lien to an individual who performs labor or services. The Oklahoma statute also allows a lien to a person who furnishes material, machinery, and oil well supplies used in the digging, drilling, torpedoing, completing, operating or repairing of any oil or gas well.<sup>20</sup> The leasing of drilling equipment, even if it did not include part of a leasehold estate, is a lienable service.<sup>21</sup> Repair of a drilling rig engine off leasehold premises has also been held to be a lienable service.<sup>22</sup>

Oklahoma specifically provides a lien for the services of a geologist or a petroleum engineer.<sup>23</sup> However, the rendering of title opinions does not entitle attorneys to a mechanics' and materialmen's lien, as title opinions are not considered "services" under title 42, section 144 of the Oklahoma Statutes.<sup>24</sup>

### 3. Time to File Lien

Liens are available to contractors and subcontractors. In order for contractors and subcontractors to have a valid oil and gas lien, a lien statement must be filed with the appropriate county clerk. Title 42, section 146 of the Oklahoma Statutes provides that oil and gas well liens must be filed pursuant to the provisions in sections 141 through 143.4, except as to subcontractors.<sup>25</sup> For subcontractors, the lien must be filed within 180 days after the date upon which material, machinery, or supplies were last furnished or labor last performed.<sup>26</sup>

Under title 42, section 142 of the Oklahoma Statutes, contractors must file a lien statement within four months after the last date that labor or material were

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Oil Co. v. Richards, 158 P. 1187 (Okla. 1916).

18. 158 P. 1187 (Okla. 1916).

19. See *Amarex*, 772 P.2d at 910.

20. See 42 OKLA. STAT. § 144 (1991).

21. See *Horton v. Wachtman Drilling Co.*, 385 P.2d 802, 807 (Okla. 1963).

22. See *Nemeroff v. Cornelison Engine Maintenance Co.*, 369 P.2d 604, 607 (Okla. 1962).

23. See 42 OKLA. STAT. § 144 (1991).

24. See *In re Bunker Exploration Co.*, 48 B.R. 708, 710-11 (Bankr. W.D. Okla. 1985).

25. See 42 OKLA. STAT. § 146 (1991).

26. See *id.*

furnished.<sup>27</sup> Lien statements filed within these time periods relate back or attach to the subject property as of the first date that anyone furnished labor, materials, or equipment for the project. The statute requires that the lien be filed within the time period from the date of the last supplying of labor or materials. Thus, an operator could conceivably assert a lien for unpaid joint interest billings years after a well was drilled and producing.<sup>28</sup>

#### 4. The Lien Statement

To perfect a mechanics' and materialmen's lien upon property and material, a lien statement containing the following information must be filed: (1) a statement setting forth the amount claimed and identifying the material or labor supplied; (2) the name of the owner or owners of the property interest against which the lien is claimed; (3) the name of the contractor; (4) the name of the lien claimant; (5) the description of the property subject to the lien; and (6) a verification of the lien by affidavit.<sup>29</sup> Frequently, the lien claimant will attach to the lien statement as an exhibit his itemized statement setting forth the amount claimed and the materials supplied.

The description of the property or well on which a lien is claimed is sufficient if it enables a party to identify with reasonable certainty the property intended to be described.<sup>30</sup> Even an incorrect legal description will suffice if it enables a person to identify the premises with reasonable certainty.<sup>31</sup> The lien statement also requires identification of the material or labor supplied.<sup>32</sup> The lien statement may be amended by attaching an omitted itemized list of labor or materials.<sup>33</sup>

If a claimant provides labor or material on more than one well, a separate lien statement should be filed for each well. In *Exchange National Bank of Tulsa v. Okeya Oil & Gas Co.*,<sup>34</sup> four different wells were drilled under separate contracts, but the contractor filed one lien statement claiming the costs and expenses of the four wells. The court held that the lien statement was null and void because the claimant failed to file separate lien statements under each contract within four months from the date on which the labor was last supplied under the contract.<sup>35</sup> The lien statement may be executed by any officer or agent of the corporation, without the necessity of attestation, seal or acknowledgment.<sup>36</sup>

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27. See 42 OKLA. STAT. § 142 (1991).

28. See *Fourth Nat'l Bank of Tulsa v. Appleby*, 864 P.2d 827, 832-33 (Okla. 1993); *Ladder Energy Co. v. Intrust Bank*, 931 P.2d 83 (Okla. Ct. App. 1996) (stating that Ladder, the operator, assumed its duties in 1993 and filed oil and gas liens against nonoperator in 1994).

29. See 42 OKLA. STAT. § 142.

30. See *Kennedy v. Uhrich*, 62 P.2d 994, 996-97 (Okla. 1936); *Corbitt v. Logan*, 20 P.2d 894, 894-95 (Okla. 1933).

31. See *King v. Long-Bell Lumber Co.*, 105 P.2d 1060, 1061 (Okla. 1940); *Kennedy*, 62 P.2d at 996-97.

32. See 42 OKLA. STAT. § 142.

33. See *Spurrier Lumber Co. v. Montgomery*, 24 P.2d 1005, 1006-07 (Okla. 1933).

34. 229 P. 765 (Okla. 1924).

35. See *id.* at 766.

36. See 42 OKLA. STAT. § 154 (1991); *Davidson Oil Country Supply v. Pioneer Oil & Gas Equip.*

The lien statement must be filed with the county clerk of the county in which the oil and gas well is located.<sup>37</sup> The county clerk is to mail notice to the owners of the property on which the lien attaches.<sup>38</sup> To be effective against a purchaser of proceeds from the sale of oil or gas, the lien statement must also be sent to the purchaser by registered or certified mail.<sup>39</sup>

The lien statement must show the name of the owner of the property against which the lien is to be charged.<sup>40</sup> In an oil and gas situation, the owners are the leasehold owners and not the royalty, production payment, or overriding royalty interest owners.<sup>41</sup> The courts are divided on whether to allow a claimant to amend, change or add omitted parties to a lien statement. The United States Bankruptcy Court for the Western District of Oklahoma held that a party could not amend a lien statement to name additional parties after the time for filing the lien has expired.<sup>42</sup> The court reasoned that to allow an amendment after expiration of the filing period would permit claimants to create and perfect a new lien against these owners, even though the filing period had expired.<sup>43</sup>

This decision is contrary to the 1930 decision of *Whitfield v. Frensley Bros. Lumber Co.*<sup>44</sup> In *Whitfield*, the filed lien statement did not set out the name of the owner or owners of the land. The court held that any lien statement may be amended as to any matter, except the amount claimed, by leave of court in furtherance of justice.<sup>45</sup>

##### 5. Owners Against Whom the Lien Operates

The Oklahoma oil and gas lien statute provides a lien to a claimant who performs labor or provides services "under contract, expressed or implied, with the owner of any leasehold for oil and gas purposes . . . ."<sup>46</sup> In a typical scenario, a claimant will assert a lien against a well operator with whom he contracted. The lien claimant ordinarily does not directly contract with the nonoperating working interest owners. Thus, the strict language of the statute would not allow the lien to be extended to the nonoperators' interests.

A mechanics' and materialmen's lien extends to the leasehold of those leasehold owners included in the lien statement. These owners are liable for material furnished and labor performed in the operation of the well.<sup>47</sup> Generally, no

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Co., 689 P.2d 1279, 1281 (Okla. 1984).

37. See 42 OKLA. STAT. §§ 142, 143, 146 (1991).

38. See *id.* § 143.1.

39. See *id.* § 144.1.

40. See *id.* § 142.

41. See *id.* § 144.

42. See *In re Mahan & Rowsey*, 27 B.R. 883, 887 (Bankr. W.D. Okla. 1983).

43. See *id.* at 887.

44. 283 P. 985 (Okla. 1930).

45. See *id.* at 988.

46. 42 OKLA. STAT. § 144 (1991).

47. See *McAnally v. Cochran*, 46 P.2d 955, 959 (Okla. 1935); *International Supply Co. v. Conn*, 249 P. 900, 901 (Okla. 1926).

personal judgment can be obtained against working interest owners, except for those who contracted for the material and labor.<sup>48</sup>

Third party claimants have used a variety of legal theories to assert a personal judgment against noncontracted leasehold owners. The theory of choice of third party lien claimants is to assert that the operator and the nonoperators entered into a "mining partnership." If the venture is held to be a mining partnership, each partner is jointly and severally liable for the entire claim.<sup>49</sup>

A mining partnership is not a partnership within the general law applying to partnerships. It is a term that refers to the obligations and liabilities incurred by tenants-in-common who jointly develop the common oil and gas property. A mining partnership is to be determined on a case by case basis. The three requirements of a mining partnership are: (1) a joint interest in the property; (2) either an express or implied agreement to share in the profits and losses; and (3) cooperation in the project.<sup>50</sup>

Unless a party is force pooled and participates in a well under a Corporation Commission forced pooling order, the leasehold owners will almost universally execute an American Association of Professional Landmen (AAPL) Model Form Operating Agreement. Article VII(A) of the Model Form Operating Agreement expressly disclaims a mining partnership.<sup>51</sup>

However, the language in the Operating Agreement disclaiming any mineral partnership is not dispositive of the legal relationship between the parties.<sup>52</sup>

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48. See *McAnally*, 46 P.2d at 959; *Anderson v. Keystone Supply Co.*, 220 P. 605, 608-09 (Okla. 1923).

49. See *Sparks Bros. Drilling Co. v. Texas Moran Exploration Co.*, 829 P.2d 951, 952 (Okla. 1991); *Oklahoma Co. v. O'Neil*, 440 P.2d 978, 984 (Okla. 1968).

50. See *Sparks Bros.*, 829 P.2d at 953; *Jenkins v. Pappas*, 383 P.2d 645, 647 (Okla. 1963).

51. Article VII(A) of the AAPL Form 610-1989 provides:

The liability of the parties shall be several, not joint or collective. Each party shall be responsible only for its obligations, and shall be liable only for its proportionate share of the costs of developing and operating the Contract Area. Accordingly, the liens granted among the parties in Article VII.B. are given to secure only the debts of each severally, and no party shall have any liability to third parties hereunder to satisfy the default of any other party in the payment of any expense or obligation hereunder. It is not the intention of the parties to create, nor shall this agreement be construed as creating, a mining or other partnership, joint venture, agency relationship or association, or to render the parties liable as partners, co-venturers, or principals.

MODEL FORM OPERATING AGREEMENT art. VII(A) (Am. Ass'n Prof. Landmen 1989) (Form 610-1989).

Article VII(A) of the AAPL Form 610-1982 provides: "The liability of the parties shall be several, not joint or collective . . . It is not the intention of the parties to create, nor shall this agreement be construed as creating, a mining or other partnership or association, or to render the parties liable as partners." MODEL FORM OPERATING AGREEMENT art. VII(A) (Am. Ass'n Prof. Landmen 1982) (Form 610-1982). Article VII(A) of AAPL Form 610-1977 and section 22 of AAPL Form 610-1956 contain similar stipulations.

52. See *Sparks Bros.*, 829 P.2d at 953 (implied in holding); *Dresser Indus., Inc. v. Crystal Exploration & Prod. Co.*, No. 84-1160, slip op. at 4 n.1 (10th Cir. July 12, 1985) (holding that the declaration of no mining partnership does not preclude litigation of the issue). *But see In re Mahan & Rowsey, Inc.*, 27 B.R. 883, 886 (Bankr. W.D. Okla. 1983) (holding that article VII(A) "precludes a determination that [the operator] was the agent of non-operator owners").



The Oklahoma decision of *Sparks Bros. Drilling Co. v. Texas Moran Exploration Co.*<sup>53</sup> discussed whether joint operation under a joint operating agreement constitutes a mining partnership. The court held that an operating agreement, in itself, does not create a mining partnership.<sup>54</sup> But, a mining partnership can arise from the behavior of the parties.<sup>55</sup> Receiving reports, questioning bills, or hiring a pumper to evaluate the well in contemplation of taking over as operator are not sufficient acts to show cooperation in the drilling of the well, a necessary element for a mining partnership.<sup>56</sup> The court added that because there was no cooperation, no mining partnership existed. The court held that cooperation in a project is "actively joining in the promotion, conduct or management" of the project.<sup>57</sup>

Some lien claimants have sought to characterize the participants in the drilling of a well as acting in a "joint venture." A joint venture is a special undertaking of two or more parties where a profit is jointly sought in a specific venture, without any formal partnership or corporate designation.<sup>58</sup> For a joint venture to exist, there must be: (1) a joint interest in the particular property or project involved, (2) an agreement, either expressed or implied, to share in the profits and losses, and (3) acts or conduct reflecting cooperation in the project.<sup>59</sup>

As the elements of imposing a joint venture and a mining partnership are almost identical, Oklahoma cases have used the terms interchangeably. The remedy is to hold the parties liable as a partnership, rendering them jointly and severally liable.<sup>60</sup>

Another theory asserted by lien claimants is that the operator was acting as the agent of the nonoperator. In the absence of an operating agreement, principals have been held liable where an operator, acting under apparent authority, contracted with outside claimants.<sup>61</sup>

The U.S. Bankruptcy Court for the Western District of Oklahoma held that an operator cannot be the agent for nonoperators where the operating agreement expressly disallows any agency.<sup>62</sup> The court deciding *In re Mahan & Rowsey* relied on an article in the operating agreement to preclude a determination that the operator was the agent of nonoperator owners. The court held that the operator's duties were more akin to that of a contractor.<sup>63</sup>

The ruling in *Mahan & Rowsey* is questionable to rely upon. An unpublished Tenth Circuit decision holds that the parties' declaration in the operating agreement that they are not a mining partnership is not dispositive of the issue. Further, in a case not involving mechanics' and materialmen's liens, the U.S. District Court for

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53. 829 P.2d 951 (Okla. 1991).

54. *See id.* at 953.

55. *See id.*

56. *See id.* at 954.

57. *See id.* at 953 (citing *Jenkins*, 383 P.2d at 647).

58. *See Perry v. Morrison*, 247 P. 1004, 1006 (Okla. 1926).

59. *Cimarron Oil & Gas, Inc. v. Benson-McCown & Co.*, 806 P.2d 83, 84 (Okla. Ct. App. 1989).

60. *See Gragg v. James*, 452 P.2d 579, 586-87 (Okla. 1969).

61. *See Spartan Petroleum Corp. v. Curt Brown Drilling Co.*, 446 P.2d 808, 813-14 (Okla. 1968).

62. *See In re Mahan & Rowsey, Inc.*, 27 B.R. 883, 886-87 (Bankr. W.D. Okla. 1983).

63. *See id.* at 887.

the Western District of Oklahoma held the operator of a unitized waterflood was the agent for the lessees in the unit, unless the operator was acting outside the scope of his authority.<sup>64</sup>

#### 6. Property Subject to Lien

The statutory language provides that a mechanics' and materialmen's lien will attach "upon the whole of such leasehold" and any well supplies, tools, and other articles used in digging, drilling, torpedoing, operating, completing, or repairing any oil and gas well.<sup>65</sup> The lien also attaches to buildings and appurtenances to the property, as well as any proceeds from the property.<sup>66</sup>

The lien attaches to the leasehold.<sup>67</sup> The statute allows the laborer or materialman a lien upon any interest or estate the owner has in the property.<sup>68</sup> An unanswered question is whether the lien will attach to the leasehold and equipment on another well on the lease or in the unit in which the work was performed or labor supplied. The statute is clear that the lien claimant secures a lien upon the entire leasehold. It would follow that the lien would encumber the named party's interest in the entire leasehold, including any other oil and gas wells drilled on the same leasehold. This raises the question of whether the lien would attach to oil and gas wells that are located in an Oklahoma Corporation Commission designated drilling and spacing unit, but not located on the leasehold of the owner. No published decisions deal with this issue.

Even if a lien is allowed to attach *in rem* upon the leasehold of the nonoperators, case law does not suggest that the courts would extend a lien to attach to those noncontracting parties' interests in other wells located on the leasehold or in the unit.<sup>69</sup>

A properly perfected lien secures all material, supplies, tools, the well, and any oil and gas fixtures and appliances used in operating the well.<sup>70</sup> It has been held that the lien attaches to casing, fixtures and equipment,<sup>71</sup> tanks, a pumping unit, and a gas engine brought on the premises but not connected or attached to the leasehold.<sup>72</sup> The lien extends to property on the lease and will follow the property

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64. See *Branch v. Mobil Oil Corp.*, 788 F. Supp. 531, 533 (W.D. Okla. 1991) (citing *Tenneco Oil Co. v. Allen*, 515 P.2d 1391 (Okla. 1973)).

65. See 42 OKLA. STAT. § 144 (1991); *Brewer v. Oil Well Supply Co.*, 258 P. 866, 871 (Okla. 1927).

66. See 42 OKLA. STAT. § 144.

67. See *id.*

68. See *National Gas Co. v. Ada Iron & Metal Co.*, 93 P.2d 529, 530 (Okla. 1939).

69. See *McInnes v. Robinson*, 341 P.2d 577 (Okla. 1959) (reversing trial court decision which impressed lien on wells in Prue sand). *But see* *Hamilton v. Delhi Mining Co.*, 50 P. 378 (Cal. 1897) (stating, in a case involving more than one mine being operated as a unit, that where several claims or locations are owned and operated as one unit, then "the property was being developed as a single mine or claim, and that the improvement or labor thereon, wherever placed, was with the purpose and effect of enhancing the value . . . of each of the several locations embraced therein").

70. See 42 OKLA. STAT. § 144.

71. See *Brewer v. Oil Well Supply Co.*, 258 P. 866, 871 (Okla. 1927).

72. See *Cyclone Drilling & Workover, Inc. v. Woods*, 671 P.2d 688, 691 (Okla. 1983).

even if the property leaves the premises.<sup>73</sup> The lien does not attach to royalty interests or previously reserved bona fide interests payable out of the working interest.<sup>74</sup> Equipment owned by an independent contractor that is brought onto the lease site is not subject to a validly filed lien.<sup>75</sup>

### 7. Enforcement of Lien

The provisions for enforcement of mechanics' and materialmen's liens are found in title 42, sections 171 through 178 of the Oklahoma Statutes. It is important to note that the statute of limitations for foreclosure of a mechanics' and materialmen's lien is one year from the date of the filing of the lien with the county clerk. In foreclosing the lien, all parties who have filed mechanics' and materialmen's liens against the property should be made parties.<sup>76</sup> Furthermore, it is important to join any party claiming an interest in the property, as the foreclosure is done in the same manner as a mortgage foreclosure, including execution and a sheriff's sale. Foreclosing in this manner and joining all such parties should clear title to the property to enable the purchaser at the sheriff's sale to acquire marketable title.

In the event the proceeds of the sale are insufficient to pay all lien claimants in full, the proceeds will be paid on a pro rata basis to all claimants.<sup>77</sup> The prevailing party is also entitled to recover reasonable attorney's fees.<sup>78</sup> The amount of attorney's fees is within the province of the court regardless of the contractual agreement between the parties.<sup>79</sup>

## B. Operator's Lien Under Forced Pooling Statute

### 1. Operator's Rights Under the Statute

Under Oklahoma's forced pooling statute, a respondent in a pooling procedure is given an option to participate in the drilling of the well.<sup>80</sup> The Oklahoma pooling statute gives an operator a lien on the interest of any interest owner who participates under the pooling order.<sup>81</sup> The statute authorizes the Corporation Commission to

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73. See 42 OKLA. STAT. § 144 (1991); *Ketchum v. Reidy*, 312 P.2d 955, 957-58 (Okla. 1957).

74. See 42 OKLA. STAT. § 144.

75. See *Osborn v. Moasco, Inc.*, 73 P.2d 113, 115 (Okla. 1937); *Kissinger v. G.E. Burgher Oil & Gas Co.*, 49 P.2d 1049, 1050 (Okla. 1935).

76. See 42 OKLA. STAT. § 173 (1991).

77. See *id.* § 178; *Fox Rig Co. v. Bell*, 263 P. 119, 120 (Okla. 1928).

78. See *VanCleave v. Kolpak Builders Co.*, 693 P.2d 17, 18 (Okla. Ct. App. 1984); *McGuigan v. Harris*, 440 P.2d 680, 681 (Okla. 1968).

79. See *Security Nat'l Bank of Enid v. Bonnett*, 623 P.2d 1061, 1063 (Okla. Ct. App. 1980).

80. See 52 OKLA. STAT. § 87.1(e) (Supp. 1997).

81. See *id.* The statute provides, in pertinent part:

The operator of such unit, in addition to any other right provided by the pooling order or orders of the Commission, shall have a lien on the mineral leasehold estate or rights owned by the other owners therein and upon their shares of the production from such unit to the extent that costs incurred in the development and operation upon said unit are a charge against such interest by order of the Commission or by operation of law. Such liens shall be separable as to each separate owner within such unit, and shall remain liens until the owner or owners drilling or operating the well have been paid the amount due

provide in its order that production attributable to a nonpaying party's interest may be directed to the payment of his unpaid well costs until such costs are paid in full.<sup>82</sup> The statute providing for the operator's lien is silent on the means of perfecting the lien or the enforcement of the lien.

### 2. Perfection of Lien

The Supreme Court in *Fourth National Bank of Tulsa v. Appleby*<sup>83</sup> dealt with the issue of perfection. In *Fourth National*, a nonoperator (Appleby) elected to participate in four wells, pursuant to a 1980 pooling order. Appleby quit paying his joint interest charges in October 1981. Appleby executed a mortgage to the bank, which filed the mortgage in 1983. The bank sued to foreclose its mortgage in 1986. The operator filed an operator's lien in the county clerk's offices in 1989.

The first issue addressed by the *First National* court was the method of perfection of an operator's lien under title 52, section 87.1(e) of the Oklahoma Statutes. The operator contended that since section 87.1(e) is silent as to a means of perfection, the lien under that statute was perfected upon entry of the forced pooling order. The court disagreed, holding that section 87.1(e) liens must be perfected and enforced in the same way as statutory liens under title 52, section 144 of the Oklahoma Statutes.<sup>84</sup>

### 3. Time to File Lien

After determining the means of perfection of liens under title 52, section 87.1(e) of the Oklahoma Statutes, the *Fourth National* court dealt with the issue of the attachment of an operator's lien. The operator contended that under the mechanics' and materialmen's lien statute, the lien attaches as of the date that labor or materials were first furnished, which the operator contended was 1980. While the court agreed that a lien relates back to the time that services began, it held that the lien can be extinguished by the statute of limitations.<sup>85</sup> The court found that because the operator could have sued Appleby for unpaid sums owed in 1981, all sums due prior to three years before the filing of the lien were barred.<sup>86</sup> Therefore, since the

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under the terms of the pooling order. The Commission is specifically authorized to provide that the owner or owners drilling, or paying for the drilling, or for the operation of a well for the benefit of all shall be entitled to production from such well which would be received by the owner or owners for whose benefit the well was drilled or operated, after payment of royalty, until the owner or owners drilling or operating the well have been paid the amount due under the terms of the pooling order or order settling such dispute. No part of the production or proceeds accruing to any owner of a separate interest in such unit shall be applied toward payment of any cost properly chargeable to any other interest in said unit.

*Id.*

82. *See id.*

83. 864 P.2d 827 (Okla. 1993).

84. *See id.* at 832.

85. *See id.* at 832-33.

86. *See id.* at 833. The court held that the limitations period was three years governing implied contracts and liabilities created by statute. *See id.*

operator perfected its operator's lien in July 1989, any unpaid statements due before July 1986 were barred. In dicta, the court suggested that public policy would not be served by allowing an operator to perfect his lien and relate his lien back to the date labor or materials were first furnished, which could be thirty or forty years prior to the date of filing.<sup>87</sup>

### *C. Oklahoma Oil and Gas Owners' Lien*

Following the numerous bankruptcies of the mid-1980s and several bankruptcy court orders ruling that royalty owners were unsecured creditors, the Oklahoma legislature adopted the Oil and Gas Owners' Lien Act.<sup>88</sup> This Act was designed to give royalty and other interest owners a security interest in unpaid proceeds held by the operator.

#### *1. Persons Entitled to a Lien*

Under the Oil and Gas Owners' Lien Act (the Lien Act), a person owning a whole or fractional interest of any kind in oil or gas at the time it is severed, or who has a right to receive a monetary payment on such oil and gas, shall have a continuing security interest and a lien upon the oil or gas or the proceeds of such sale to the extent of his interest.<sup>89</sup>

#### *2. Time to File*

Under the Lien Act, the interest owner's lien shall be effective against any interest owner, operator, or first purchaser when the notice of the lien has been filed in the office of the county clerk of the county in which the well is located. Upon perfection, the lien will relate back to the date on which the minerals were severed.<sup>90</sup>

The lien must be perfected within ninety days from the time at which payment is due.<sup>91</sup> To be effective against another interest owner, operator, or first purchaser, the notice of the lien must be delivered to such interest owner, operator or first purchaser by registered or certified mail.<sup>92</sup>

#### *3. The Lien Statement*

The Lien Act recites that an interest owner must perfect his security interest and lien by filing a verified notice in substantially the same form provided in the statute.<sup>93</sup>

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87. *See id.* at 834.

88. *See* 52 OKLA. STAT. §§ 548-548.6 (1991).

89. *See id.* § 548.2(A).

90. *See id.* § 548.4(C); *Arkla Exploration Co. v. Northwest Bank*, 948 F.2d 656, 658 (10th Cir. 1991).

91. *See* 52 OKLA. STAT. § 548.4(A) (1991).

92. *See id.* § 548.2(C).

93. *See id.* § 548.4. The statute requires that the lien be substantially in the following form:

NOTICE OF OIL AND GAS OWNER'S LIEN

Notice is hereby given that (name of interest owner for whom notice is filed) whose address is (address of named interest owner) claims an (fractional decimal interest) interest in the oil and/or gas severed or proceeds of sale from the (name of well) operated by (name and address of operator) which well is located on the following described land in

#### 4. *Property Subject to Lien*

The perfected security interest and lien will follow and attach to the oil or gas which was unpaid or the proceeds of such oil or gas, if it has been sold.<sup>94</sup> This gives the interest owner a lien upon the funds in the possession of an operator to the extent of his unpaid royalty.

#### 5. *Enforcement of Lien*

An interest owner who properly perfects his lien must enforce the lien by filing an action within one year after the date of the filing of the notice of lien.<sup>95</sup> In such an action, the prevailing party may be allowed reasonable attorney's fees and costs, including the recording fees for filing the lien.<sup>96</sup>

### III. *Contractual Liens — AAPL Model Form Operating Agreement*

As previously discussed, liens can be statutory or contractual. Contractual liens include any agreement that provides for a lien in the contract. This would include a mortgage or an oil and gas operating agreement.

Virtually all oil and gas operations involving more than one party are conducted pursuant to an operating agreement. Although there are several standard operating agreements, the common form used in Oklahoma is the AAPL Form 610 Model Form Operating Agreement. The AAPL has developed standard forms in 1956, 1977, 1982, and 1989.

#### A. *Person Entitled to a Lien*

Article VII of the 1989 Model Form Operating Agreement grants each party to the agreement a lien and a security interest against each other in the interest in his property to secure the performance of all obligations under the agreement.<sup>97</sup> The 1989 Model Form Agreement is a change from the 1977 and 1982 forms, wherein only the operator was granted a lien.<sup>98</sup>

..... County, Oklahoma:

(description of land)

Oil and/or gas severed from said land has been and is now or may be taken and the above named interest owner has a security interest in and lien upon such oil and/or gas and the proceeds thereof to secure payment under the provisions of the Oil and Gas Owners' Lien Act.

Dated: (date)

\_\_\_\_\_  
(Signature of interest  
owner or operator)

*Id.*

94. *See id.* § 548.6(A).

95. *See id.*

96. *See id.*

97. *See Amarex, Inc. v. El Paso Natural Gas Co.*, 772 P.2d 905, 906 (Okla. 1987).

98. *See MODEL FORM OPERATING AGREEMENT art. VII(B)* (Am. Ass'n Prof. Landmen 1982) (Form 610-1982); *MODEL FORM OPERATING AGREEMENT art. VII(B)* (Am. Ass'n Prof. Landmen 1977) (Form

### B. Obligation Under the Agreement

The AAPL 1989 form provides that each party grants a lien to secure the performance of all obligations under the agreement including, but not limited to (1) the payment of expenses, interest and fees, (2) the proper disbursement of all monies paid hereunder, (3) the assignment or relinquishment of interest in oil and gas leases as required hereunder, and (4) the proper performance of operations. The 1977 and 1982 Model Forms secure only the payment of expenses by the nonoperator.

### C. Property Subject to Lien

The contractual lien granted in the 1989 Model Form encumbers every interest a party owns under the agreement, including (1) the leasehold interest, (2) the working interest, (3) operating rights, (4) the royalty interest, (5) the overriding royalty interest, (6) oil and gas when extracted, (7) equipment, (8) accounts, (9) contract rights, (10) inventory, (11) general intangibles, and (12) all the proceeds and products of the foregoing.<sup>99</sup> The 1982 Model Form Agreement grants a lien on "oil and gas rights," a security interest in oil and/or gas when extracted, and its interest in all equipment.<sup>100</sup> The term "oil and gas rights" is not a defined term in the 1982 agreement.

### D. Perfection of Lien

It has not been a custom and practice in the industry for parties to record the operating agreement. The case of *Amarex, Inc. v. El Paso Natural Gas Co.*<sup>101</sup> examined the issue of perfection of an operating agreement.<sup>102</sup> The *Amarex* court held that the method of perfection of a contractual lien is dependent upon the type of property encumbered. Since an oil and gas lease constitutes an interest in real property, the court held that the procedure to perfect a contractual lien is similar to the procedure for perfecting a mortgage.<sup>103</sup> To perfect a contractual lien against a working interest owner's interest and to serve as constructive notice, the agreement must be executed, acknowledged, and recorded in the land records of the county in which the subject property is located.<sup>104</sup> Although a contractual lien is enforceable between the parties, it is not enforceable without proper acknowledgment and recording.<sup>105</sup>

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610-1977).

99. See MODEL FORM OPERATING AGREEMENT art. VII(B) (Am. Ass'n Prof. Landmen 1989) (Form 610-1989).

100. See MODEL FORM OPERATING AGREEMENT art. VII(B) (Am. Ass'n Prof. Landmen 1982) (Form 610-1982).

101. 772 P.2d 905 (Okla. 1987).

102. See *id.*

103. See *id.* at 906; see also 16 OKLA. STAT. § 15 (1991).

104. See *Amarex*, 772 P.2d at 906.

105. See *id.*

The *Amarex* court instructed that it is imperative that the filed contractual lien statement contain the signature of the owner of the property encumbered.<sup>106</sup> An executed and acknowledged document that is filed in the land records will constitute constructive notice, even if it is not the entire operating agreement.<sup>107</sup> However, the document must be executed by a statutorily authorized agent of the corporation.

In *Amarex*, the lien claimants' operator agreed that a lien statement referencing the operating agreement was sufficient to put third parties on "inquiry notice." The court held that because the lien statement only referred to a "contract," and not an operating agreement, the reference was inadequate.<sup>108</sup>

If the agreement providing for the contractual lien is not recorded, then the avoidance provision of the Bankruptcy Code may allow a trustee or debtor in possession to avoid the contractual lien.<sup>109</sup>

### *E. Enforcement of Lien*

Title 42, section 23 of the Oklahoma Statutes provides that a lien is extinguished by the lapse of time under which an action can be brought upon the principal obligation.<sup>110</sup> In a typical oil and gas situation, the submission of joint interest billings would start the period in which to institute a suit.<sup>111</sup> To foreclose, therefore, an operator must file suit within five years after the breach of the operating agreement.<sup>112</sup>

The operating agreement provides some self-help remedies. Article VII(B) of the 1989 Model Form grants to the parties rights and remedies under the Uniform Commercial Code. It also recites that on default by any party in the payment of its share of the expenses, interest, or fees, or upon the improper use of funds by the operator, all parties have the right to exercise an assignment of proceeds provision found in the agreement. This assignment of proceeds provision authorizes the purchaser of the defaulting party's production to deliver the proceeds from any sale to the claimants. Article VII(B) also contains language regarding waivers of certain rights by the defaulting party.

The 1989 Model Form also grants to each party a power of sale provision as to any property that is subject to the lien and security rights granted. However, this power of sale provision is not adequate under Oklahoma law to allow a nonjudicial foreclosure. Title 46, section 43 of the Oklahoma Statutes requires any mortgage containing a power of sale to state in bold and underlined language the following: "A power of sale has been granted in this mortgage. A power of sale may allow the

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106. *See id.* at 908-09.

107. *See* Alvin C. Harrell & Joseph R. Dancy, *Creditor Lien Rights in Oklahoma and the Impact of Bankruptcy*, 10 OKLA. CITY U. L. REV. 455, 505 (1985). The AAPL has prepared a Form 610 RS (recording supplement) that it recommends be used to perfect the lien.

108. *See Amarex*, 772 P.2d at 906.

109. *See* 11 U.S.C.A. § 544 (West 1993); *see also* *Wilson v. TXO Prod. Corp.*, 69 B.R. 960, 963 (Bankr. N.D. Tex. 1987).

110. *See* 42 OKLA. STAT. § 23 (1991).

111. *See* *Fourth Nat'l Bank of Tulsa v. Appleby*, 864 P.2d 827, 831 (Okla. 1993).

112. *See* 12 OKLA. STAT. § 95(1) (Supp. 1997); *Fourth Nat'l*, 864 P.2d at 931.



mortgagee to take the mortgaged property and sell it without going to court in a foreclosure action upon default under this mortgage."<sup>113</sup>

In the event the parties wish to provide for a nonjudicial power of sale, they would have to add the above language to the operating agreement to comply with Oklahoma law.<sup>114</sup>

#### IV. Priorities Among Claimants

A mechanics' and materialmen's lien that is timely filed refers back and applies from the date the first item of material is furnished to the lease or the date the first labor or services are performed on the lease.<sup>115</sup> Among competing mechanics' and materialmen's lien claimants, the work performed on the leasehold is considered to be one continuous project. Liens for labor and materials furnished attach as of the date of the commencement of the project. All valid lien claimants stand in equal status toward each other.<sup>116</sup> In other words, the lien claimant who supplies material at the end of a drilling well project will be equal in priority to the lien claimant, such as an engineer or surveyor, who provided services prior to the drilling of the well.

A prior recorded mortgage has priority over mechanics' and materialmen's liens subsequently filed, if no labor was performed nor materials supplied prior to the filing of the mortgage.<sup>117</sup> If the construction or drilling was started prior to the recording of a mortgage, the lien of the contractor or subcontractor is superior to that of the mortgagee.<sup>118</sup>

A contract which provides for a lien, if properly executed and filed, will be superior to any mechanics' and materialmen's lien if the contract is filed prior to the time that labor is first commenced or material first supplied.<sup>119</sup> The contractual lien will be superior to a mortgage if properly recorded prior to the filing of the mortgage.<sup>120</sup>

When lending money to an oil and gas owner, a mortgagee must be concerned that any mortgage filed may be subject to a statutory mechanics' and materialmen's lien that has accrued for up to five years, but has not been filed of record.<sup>121</sup>

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113. 46 OKLA. STAT. § 43 (1991).

114. *See id.*

115. *See Cyclone Drilling & Workover, Inc. v. Woods*, 671 P.2d 688, 690 (Okla. Ct. App. 1983); *see also Chickasha Cotton Oil Co. v. Standard Lumber Co.*, 52 P.2d 816, 819-20 (Okla. 1935).

116. *See Industrial Tile Co. v. Home Fed. Sav. & Loan Ass'n*, 331 P.2d 918, 920 (Okla. 1958).

117. *See Karen Myers, Ltd. v. The Law Co.*, 794 P.2d 766, 768 (Okla. Ct. App. 1990).

118. *See Liberty Nat'l Bank & Trust Co. v. Kaibab Indus., Inc.* 591 P.2d 692, 693-64 (Okla. 1978); *see also Ladder Energy Co. v. Intrust Bank, N.A.*, 931 P.2d 83, 84-85 (Okla. Ct. App. 1996).

119. *See Amarex, Inc. v. El Paso Natural Gas Co.*, 772 P.2d 905, 908 (Okla. 1987).

120. *See id.*

121. *See Fourth Nat'l Bank of Tulsa v. Appleby*, 864 P.2d 827, 831-32 (Okla. 1993).