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The Top Ten Things Your Momma Never Told You About Oil and Gas Leases

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A. INTRODUCTION TO OIL AND GAS LEASES

An oil and gas lease is not a lease; it is a determinable fee interest in land. See Stephens County v. Mid-Kansas Oil & Gas Co., 254 S.W. 290 (1923). The interest conveyed is considered a determinable fee because the estate may be terminated and returned to the grantor by certain contingencies or failures. Today's oil and gas leases are often referred to as an "unless" lease. The oil and gas leasehold estate terminates unless (i) a delay rental is paid, (ii) there are operations or production within the time specified, or (iii) there is a shut-in gas well and shut-in royalties are paid pursuant to the terms of the lease, depending on what is stated in the lease instrument. Because the execution of an oil and gas lease creates an interest in land, it is subject to the formalities of the Texas laws of conveyancing which are found in Sections 5.001 to 5.043 of the Texas Property Code. Therefore, the lease must be in writing, signed, and acknowledged or sworn to in order to be filed of record. A common practice is to record a memorandum of the oil and gas lease in lieu of recording the actual lease, in which case the memo must be acknowledged and contain the statutory notice of rights on the first page. It also must contain words of conveyance and describe the land with sufficient particularity. In construing a lease, Texas courts follow the “Four Corners Rule” whereby parol and extrinsic evidence are not used to clarify the lease unless there is an ambiguity which cannot be solved within the four corners of the instrument. See Rutherford v. Randall, 593 S.W.2d 949 (Tex. 1980). Except for the implied covenants discussed below, the terms of the lease and the rights of the lessor and lessee spelled out therein, control.

Both the land owner and the oil and gas lessee will benefit from the discovery, production, and sale of oil and gas; however, their interests are not always the same. The lessee, whose interest is solely in minerals, must bear all costs of exploration and development. The lessee traditionally seeks the greatest flexibility possible for its operations under the lease; therefore, it wants the right to drill, but it does not want any obligation to do so. The lessor, who may also be the owner of the surface, has an expense-free interest in the oil and gas, and he

typically wants immediate drilling and rapid development which do not interfere with his current or
prospective surface uses. Most negotiation over the terms of an oil and gas lease centers on these two differing concepts.

There is no such thing as a standard or statutory oil and gas lease. However, a typical producer oriented lease is known as the Producers 88 form (sometimes referred to herein as a "printed form"). There are typically two versions of the Producers 88 – a paid up form and a delay rental form, copies of which are attached hereto, and include examples of the various clauses discussed herein with a producer slant. If representing a landowner or mineral owner (referred to herein as a "mineral owner" or "lessor"), one does not want his client to agree to use a printed form without an addendum providing more favorable provisions, such as a better defined and a more reasonable royalty provision, a vertical and horizontal release provision, a surface use provision (if applicable), a pooling limitation provision and a shut-in royalty limitation provision. For attorneys representing clients with significant mineral interests and in many cases, even for those with smaller interests, one should consider using a lawyer generated lease (referred to herein as a "custom lease"), skipping altogether the Producers 88 form. A producer or lessee may prefer to use the printed form with no lessor generated addendum if possible. While a Producers 88 form is used quite often, there a number of different Producers 88 forms, none of which are by any means standard; and if representing a lessor, one should exercise caution with any such form. Most lawyers representing mineral owners would prefer not to use such forms unless an addendum with terms that are more favorable to landowners is used in conjunction with the form.

I. MINERAL ESTATE VERSUS SURFACE ESTATE

Before reviewing the various clauses of an oil and gas lease, it is important to consider the surface estate and the mineral estate as an oil and gas lease is a severance with a possible reversion to the lessor, thus, a determinable fee. In executing any oil and gas lease, regardless of whether one represents the lessor or the lessee, it should be noted that the mineral estate is dominant to the surface estate, which is subject to an implied easement of surface use by the mineral estate owner to use as much of the surface as is reasonably necessary to carry out the intended purposes for mineral extraction under the lease. See Texaco, Inc. v. Farris, 413 S.W.2d 147 (Tex. Civ. App.—El Paso 1967, writ ref'd n.r.e.). An accommodation doctrine exists in

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