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PERFECTION IN THE OILFIELD

A General Discussion Regarding Perfection of Your Client's Interest or Lien in Oil, Gas and Other Minerals

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TABLE OF CONTENTS

Page

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I. INTRODUCTION[1]

Regardless of the state in which he or she practices, an energy lawyer will need to be familiar with perfection of titles to and liens on myriad properties, including (but certainly not limited to) oil, gas and other minerals in the ground; the minerals severed from the ground; proceeds of sales of the minerals; accounts and general intangibles arising out of minerals transactions; the minerals as they are transported from the wellhead to the processing plant; the minerals as they are processed and marketed; the equipment used to produce, transport and process the minerals (such as the platform itself if the production site is in the water; equipment on the well; motor vehicles and boats; communications equipment; computer hardware as well as software used; intellectual property derived from seismic surveys; proprietary information that may be subject to disclosure to agencies under various laws; structures used for offices and crew housing; and contracts to which his or her client is a party.

This paper will provide a general overview of the principles of Texas law regarding perfection of titles and liens in oil, gas and other minerals. The focus will be on real property, not personal property.

A. Distinction Between a Perfected Title and a Marketable Title

Under Texas law, an instrument that is properly recorded in the proper county is notice to all persons of the existence of the instrument.[2] Conversely, a conveyance of real property or an interest in real property or a mortgage or deed of trust is void as to a creditor or to a subsequent purchaser for a valuable consideration without notice unless the instrument has been acknowledged, sworn to or proved and filed for record as required by law.[3] For purposes of this paper, "perfected title" or "perfection of title" will mean a document relating to oil or gas, or an interest therein, as real property that has been properly executed, acknowledged or sworn to, and properly recorded in the proper county.

On the other hand, "marketable title" is a record title that is free from reasonable doubt such that a prudent person, with knowledge of all salient facts and circumstances and their legal significance would be willing to accept it. To be marketable, a title need not be absolutely free from every possible suspicion. The mere possibility of a defect that has no probable basis does not show an unmarketable title.[4] Matters that may make a title unmarketable include: interests

[1] The author acknowledges with gratitude the invaluable assistance and sharp eye of his long-standing (and long-suffering) assistant, Mary S. Lee, and Joe Martin of the BakerHostetler IT department.
[2] Texas Property Code § 13.002.
[3] *Id.* § 13.001(a).
[4] Texas Title Examination Standard 2.10.

acquired by limitation title; land acquired by accretion; outstanding oil and gas leases, royalty interests, covenants, or easements; or mortgages, judgment liens, or tax liens.[5]

In sum, the owner's title may be *perfected* but it may not be *marketable* within the standards set out above; the converse is also true, *i.e.*, the owner's title may be *marketable*, but it may not be *perfect*. For instance, an oil and gas lease that is outside its primary term cannot be determined to be in force and effect simply by examining the records of the county in which the leased lands are located; review of records other than the county records must be made to determine whether production was obtained during the primary term, and whether the well on the lease is producing hydrocarbons in paying quantities on the date of inquiry. Also, there may be recorded (and unrecorded) exceptions to title that a buyer or lender is willing to accept, which, but for his or her agreement to accept them, would cause the title to be deemed imperfect or unmarketable, or both. It is for these reasons that in a purchase and sale transaction most lawyers will negotiate a definition of marketable title as well as standards for permitted encumbrances or permitted exceptions that will not cause the seller's title to be less than marketable. For the same reason, it would be prudent for the borrower's lawyer to consider similar revisions in any deed of trust or mortgage where the borrower is warranting title to the mortgaged real property.

II. WHY RECORD?

In general, there are three types of recording statutes recognized in the United States: race; race-notice; and notice. A "race" statute provides that a purchaser or lienholder who is second in time of conveyance prevails if he or she records first, regardless of whether that person has notice of other unrecorded interests. Under a "race-notice" statute, the subsequent purchaser or lienholder must acquire an interest without notice of the prior unrecorded interest and also must file for record before recordation of the prior unrecorded interest. A "notice" statute protects a subsequent purchaser or lienholder who acquires an interest without notice of a prior unrecorded conveyance or lien, regardless of when the subsequent purchaser's deed or subsequent lienholder's security instrument is recorded.[6]

Texas is a notice recordation state.

Our courts have said time and again that the recording laws in Texas are meant to protect good faith purchasers and creditors without notice of prior transfers from being injured or prejudiced by their lack of knowledge of the competing claim;[7] that the intention of our recording laws is to compel every person receiving conveyances of real property to place such an instrument of record, not only that he or she may protect their own rights, but also those of all others who may afterwards seek to acquire an interest in the same property;[8] and that the purpose

[5] Comments to Texas Title Examination Standard 2.10 and cases cited therein.
[6] Comments to Texas Title Examination Standard 4.40 and cases cited therein.
[7] *de Toca v. Wise*, 748 S.W.2d 449, (Tex 1998); *Sanchez v. Telles*, 960 S.W.2d 762 (Tex. App. – El Paso 1997, pet. denied).
[8] *Sanchez v. Telles*, 960 S.W.2d 762 (Tex. App. – El Paso 1997, pet. denied).

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