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Chapter 3

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Determining the Legal Ramifications of Express Oil and Gas Lease Provisions: Do the Rules of Document Interpretation Provide Predictability?

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Synopsis

§ 3.01. Introduction.

The oil and gas lease has served as the basic contract for the petroleum industry since before "Colonel" Edwin Drake struck oil in Titusville, Pennsylvania in 1859.[1] In fact, the first recorded lease, dated the fourth day of July 1853, and filed in the county of Venango, Pennsylvania, contained only 10 lines and ended with the prophetic statement: "If profitable."[2] Running twice as long as this first lease, the Drake lease, signed four years later in 1857, featured familiar clauses such as a provision for a 1/8th royalty, termination conditions, and an initial 15-year term.[3]

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1 Daniel Yergin, *The Prize: The Epic Quest for Oil, Money and Power* 26 (1991). E.L. Drake assumed the title "Colonel" in an effort to impress the locals. *Id*. at 26. Early oil and gas leases were adapted from forms used in the salt industry in Pennsylvania, as oil and gas were discovered as a result of borings for salt water. The salt industry leases had evolved from the leases used for solid minerals. From the beginning, oil and gas leases were used rather than outright land purchases because the owners of the land seldom "had the money or the faith to test the productivity of their holdings." Thus the lease developed to grant to those with such resources, but with little interest in ownership of the land, the privilege of exploration and production. Leslie Moses, "The Evolution and Development of the Oil and Gas Lease," 2 *Inst. on Oil & Gas L. & Tax'n*, 1, 10 (1951).

2 Leslie Moses, "The Evolution and Development of the Oil and Gas Lease," 2 *Inst. on Oil & Gas L. & Tax'n*, 1, 6 (1951).

3 *Id*. at 7.

Dated December 30, 1857
Deed Book P, p. 357
$1 in hand.
Pennsylvania Rock Oil Company to E.B. Bonditch and E.L. Drake

"Demise and Let all the lands owned or held under lease by said company in this County of Vanango, State of Pennsylvania, 'To bore, dig, mine, search for and obtain oil, salt water, coal, and all materials existing in and upon said

By the end of the century, as the industry evolved and geological knowledge expanded, other clauses considered "typical" by today's standards began appearing in oil and gas leases, including the habendum clause, bonus payment and delay rental provisions, and drilling and savings clauses. And by 1920 these and other "standard" clauses could be found in several variations of the popular "Producers 88" form.[4]

Throughout the decades, the "typical" oil and gas lease clauses have been developed and revised in response to judicial decisions. As Professor A.W. Walker noted nearly 50 years ago, "The clauses in the modern oil and gas lease [have evolved] through many years of trial and error and after a great amount of litigation and judicial construction."[5] And, as he predicted, that evolutionary process has continued. To provide an update on that process, this chapter reviews selected court decisions construing lease clauses. The cases discussed include recent decisions and older cases providing unique lessons about particular lease clauses. In order to better evaluate these court decisions, the chapter begins with a description of the general rules of document interpretation which courts purport to follow when scrutinizing an oil and gas lease clause. The next sections provide a basic description of the wording and purposes of various clauses, followed by a discussion of cases which demonstrate the effect of those provisions.

> lands, and take, remove and sell such, etc., for their own exclusive use and benefit, for the term of 15 years, with the privilege of renewal for the same term. Rental, one-eighth of all oil as collected from the springs in barrels furnished and paid for by lessees. . . . Lessees agree to prosecute operations as early in the spring of 1858 as the season will permit, and if they fail to work the property for an unreasonable length of time, or fail to pay rent more than 60 days, the lease will be null and void.'" *Id*. at 7.

4 However, while these forms contain many "typical" clauses, one version can vary substantially from another; therefore, the Producers 88 label does not suggest a "standard" lease form. These variations caused an early Texas court to determine that the caption "Producers 88" was "incapable of definite application." Fagg v. Texas Co., 57 S.W.2d 87 (Tex. Com. App. 1933). For a description of the history behind the "Producers 88" form *see* Leslie Moses, *supra* note 2, at 27; A.W. Walker, Jr., "Defects and Ambiguities in Oil and Gas Leases," 28 *Tex. L. Rev.* 895, 896-97 (1950).

5 A.W. Walker, *supra* note 4, at 909 (1950).

6 The scope of this chapter is limited to the legal implications of express lease provisions. The effect of implied obligations, through the doctrine of implied covenants, will not be discussed.