CHAPTER 17

Ambiguities in Deeds, Leases, and Assignments

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§ 17.01. Introduction.

The oil and gas lease is the basic instrument under which oil and gas exploration and development is ordinarily conducted. The modern oil and gas lease is a very complex instrument which is the product of many years of rapid evolution. The length as well as the complexity of the instrument has increased considerably since the time of the first reported oil and gas lease.\(^1\)

To understand fully the evolution of the oil and gas lease, we will begin by examining the first reported lease:

Agreed this fourth day of July, A.D. 1853, with J.D. Angier of Cherrytree Township, in the County of Venango, Pas., that he will repair up and keep in order, the old oil spring on land in said Cherrytree Township, or dig and make new springs, and the expenses to be deducted out of the proceeds of the oil, and the balance, if any, to be equally divided, the one-half to J.D. Angier and the other half to Brewer, Watson & Co., for the full term of five years from this date. If profitable.

Brewer, Watson & Co.

J.D. Angier\(^2\)

As one can ascertain, this simplistic lease allows for many controversies between the two parties. How a court is to deal with the controversies which result from the construction of the instrument is the subject of this Chapter. By understanding how a court will likely interpret an agreement, the parties to the agreement can take steps to circumvent the need for judicial intervention by their initial wording of the agreement. Controversy concerning the agreement can be prevented by familiarity with judicial interpretation.

As Professor Kuntz has observed:

Although the oil and gas lease appears in many forms and there is no standard oil and gas lease, there is sufficient similarity among leases and the objectives sought by the parties thereto that it is possible to refer to the oil and gas lease as a special type of instrument.\(^3\)

Due to the specialized nature of the oil and gas lease, one must look to a court's methods of interpreting the oil and gas lease. We will begin by examining the general considerations utilized by courts in attempting to resolve ambiguities. Next, we will look at these general considerations as they relate to oil and gas leases. Finally, we will look at specific problems with deeds, leases, and assignments in the oil and gas industry.

§ 17.02. General Considerations of the Established Rules of Construction.

The established rules of construction are used only when the instrument is not clear, is ambiguous, or is
uncertain. Rules of construction always look to "the intention of the parties" and particularly to the intention of the grantor or assignor where that can be determined.

[1]--Intent of the Parties.

The court will usually begin to determine the intention of the parties by the terms used in the instrument. If the intention is still doubtful, the court will then likely use construction aids, or rules of construction, to ascertain the parties' objective intent. If the instrument is ambiguous, the court may allow parol or other extrinsic evidence to be considered, such as the circumstances leading to execution of the instrument, the situation of the parties, and the subject matter. Parol evidence, however, may be completely excluded under many circumstances.

[a]--Language of the Instrument.

The language of an instrument will be the controlling factor in its interpretation. If proper language is used, the meaning of that language will apply. Courts are generally not concerned with what the parties meant to say but with what they did say – the language of the instrument. In *Campbell v. Campbell*,(4) the court addressed a waiver of surface support. The court determined "such a conveyance or waiver should not be implied unless the language of the instrument of conveyance is appropriate therefor and clearly indicates such to be the intention of the parties . . ."(5)

Courts will generally find that words are to be given their ordinary meaning. Technical words do not necessarily need to be interpreted in their technical sense, and "strict or literal meaning of the language used will not be applied if it would frustrate the apparent intention of the parties as deduced from the entire instrument."(6) In *Hammet Oil Co. v. Gypsy Oil Co.*, (7) the court stated "[w]ords in a contract are to be understood in their ordinary and popular sense, unless there is something to indicate that the parties used the words in a technical sense."(8)

Explanatory words or parenthetical explanations will usually be considered secondary to the written language of an instrument.(9) In *Knox v. Krueger*,(10) the court looked at a parenthetical clause of assignment of oil and gas royalties which stated "one and one-fourth per cent (1¼% of all the) royalty of all the oil and of all the gas produced and saved" from land under an oil and gas lease reserving one-eighth of production to lessor. The court found the parenthetical to be repugnant to the written words of the contract. Therefore, the written words took precedence and 1¼% of all oil and gas produced was conveyed and not 1¼% of of the oil and gas produced on the premises.(11) One needs to take great care when choosing the language to be used in an instrument.

[b]--Four Corners Rule.

Instruments are viewed as a whole. All clauses of an instrument will be examined to determine the parties' intent. "The court will presume that the parties to a gas and oil lease worded it so as to express the actual contract which they intended to make, and will not fractionalize a lease or divide it into separate sections."(12) In *Townsend v. Cable*,(13) the court stated "[t]he basic principle followed in construction of deeds is to determine the intention of the grantor as gathered from the four corners of the instrument."(14) In *Paddock v. Vasquez*,(15) the court stated: "The intention of the parties is to be gained from a consideration of the entire instrument though the immediate objective of the inquiry is the meaning of an isolated clause, taking into consideration every provision, clause, and word, whether of grant, or description, or of qualification, exception, or explanation."(16)
A common source of controversy arises when the drafter places a heading or label on the instrument with the intention of describing the instrument's contents. The parties usually are not sufficiently familiar with the phraseology to understand fully the meanings of the provisions used. Therefore, the parties tend to place an unfounded amount of trust in the label despite the possibility of its inaccuracy. While the label itself has no controlling force in an instrument, there is a difference among jurisdictions as to the weight which is to be given the label. Under Louisiana law, the label affixed to an instrument may have some bearing upon the court's interpretation of it. In Melancon v. Cheramie, the court looked to the caption "ROYALTY DEED" at the top of a deed as a factor in determining that it was intended to be a royalty deed. Under Kansas law, the court is "not governed by the name or title affixed to a document." However, the label is considered an expression of intention, and the "contents of the instrument must make it clear that it is something else than what its title indicates." In Oklahoma, the court will not recognize the label as a manifestation of intention to any degree. In Colonial Royalties Co. v. Keener, the court stated: "That the instrument is labeled `Royalty Deed' has no bearing upon the intention of the parties, expressed in the body of the instrument."

Another issue related to the "four corners rule" is the problem which can arise when more than one instrument is involved. Generally, when more than one instrument is involved, and all are part of the same transaction, both instruments will be construed as one. In Empire Gas & Fuel Co. v. Stern, the court was looking at a contract, draft, and lease. The court stated: "In the eye of the law they are one instrument. They will be read and construed together, as if they were one in form as they are in substance." However, it is not essential for the separate instruments to refer to one another. The only prerequisite is that the instruments be a part of the same transaction.

A difficulty can arise when the separate instruments are inconsistent with each other. In this case, usually the instrument created last will be the controlling instrument. In Willeke v. Bailey, the court stated: "[I]t is quite evident that the terms of the one agreement are so inconsistent with those of the other that the two cannot subsist together. In that situation the rule is that the one made first is conclusively presumed to have been superseded by the other."

It is also necessary always to keep in mind that every part of an instrument is important. Therefore, a portion which is certain will control over a portion which is uncertain.

[c]--General Rules.

Generally, the validity of an instrument is favored. This is due to the court's lack of desire to restrict the ownership of land. In Whitehall Oil Co. v. Heard, the court said, "where the instrument could be reasonably interpreted either way, the proper interpretation is that which least restricts the ownership of the land conveyed . . ." However, the court may struggle to find an instrument valid, especially where there are inconsistent clauses which both enforce and cancel the instrument. If one expression cancels and another puts the instrument in force, generally, the latter will control.

[i]--Written Portions vs. Printed Portions.

Both printed matter and handwritten or typewritten matter are equally binding. However, a controversy in an instrument may occur when the printed matter is inconsistent with the written matter. When this problem occurs, generally, the written portions will control over the printed portions. The reason for this general rule is that "the written words are the immediate language and terms selected by the parties themselves for the expression of their meaning, while the printed form is intended for general use without reference to
particular objects and aims."(34) However, this general rule is not always followed. In *Bennett v. Henderson*,(35) the court examined a situation in which words were handwritten in the margin of a deed. The handwritten portion was inconsistent with the printed portions. The court stated: "The deed is not at all ambiguous. It needs no construction. Whether the marginal notations are attempted wills or something else, they are mere surplusage. We need not define the intention of the grantor when there is no reasonable basis for questioning the words of the deed."(36)

In many instances, unitization clauses setting forth the number of acres that can be unitized are left in a lease. Courts in these cases often find the written portions nullify the printed form, and the written portion controls.

[ii]--First Clauses vs. Later Clauses.

When there appears to be a conflict between two clauses in an instrument, under common law, the first clause would control. However, "the provisions of the granting clause are given great weight and ordinarily will control in the event of an irreconcilable conflict with other provisions, or if the other provisions are too indefinite to be given any meaning."(37) Courts have generally found that, notwithstanding a general granting clause, the habendum clause will control where limitations have been placed on the full grant. However, in *Brungardt v. Smith*,(38) the court addressed this philosophy by stating that "the ancient rule that the habendum clause controls has lost much of its former force and the deed should be construed by considering all of its language with a view to ascertaining the intent of the grantor."(39)

[iii]--Sweep Clauses (Ejusdem Generis).

In the construction of laws, wills, and other instruments, the "ejusdem generis rule" is that where general words follow an enumeration of persons or things, by words of a particular and specific meaning, such general words are not to be construed in their widest extent, but are to be held as applying only to persons or things of the same general kind of class as those specifically mentioned.(40)

Sweep clauses are those clauses where a list of rights or items are set forth followed by a sweeping generality, such as "etc." General words following specific words are limited to things of the same kind or classes as those specifically stated. For example, a reservation of "oil, gas, and other minerals" reserves other minerals like oil and gas. In *Bundy v. Myers*,(41) the court found that "[a] reservation of oil, coal, fire clay, and minerals of every kind and character does not include natural gas, in absence of clear intent by parties to so include it."(42)

One of the major controversies which arise concerning this subject involves whether oil and gas are included within the term "mineral." The majority rule states "that oil and gas are included within the term `minerals' when used alone, unless there is a demonstrated intention to the contrary."(43) The minority rule states that "oil and gas are not included within the terms `minerals' when used alone, unless there is some demonstration of intention to include them."(44) The majority view is followed in Illinois, Kansas, Kentucky, Michigan, Oklahoma, Texas, Utah, Virginia, West Virginia, and conceivably in Louisiana and Mississippi and probably in Ohio.(45)

Most oil and gas leases contain a so-called "Mother Hubbard Clause." This clause usually states that the lease covers all property owned by the grantor in a certain township. One of the main purposes of this type of clause is to collect into the description of the leased land small strips whose descriptions are not available and are dependent on a survey.(46) It is my opinion that courts in general will limit the Mother Hubbard Clause to gores, strips, and appurtenances only. I also believe that the specific description may be found to
An important rule of construction that must be taken into consideration is that the words used may be construed against whoever chose them. Since the grantor usually chooses the words, courts attempt to find the grantor's intention. However, an ambiguity will be construed against the party who chose the ambiguous language, usually the grantor. In *Jones v. Johnson*, the court stated: "Furthermore, it is an established rule of construction that where there is ambiguity or a question in construing a deed, the deed should be construed most favorably to the grantee as against the grantor." In *Corbin v. Moser*, the court recognized the rule:

The general rule is well settled that if there is any ambiguity in a deed so that it is capable of two possible constructions, one of which will be more favorable to the grantee, the other of which will be more favorable to the grantor, that method of construction which will be more favorable to the grantee will be selected and the deed will be construed against the grantor. All doubts, therefore, are to be resolved against the grantor. This rule is statutory in some jurisdictions. The rule is predicated upon the reasoning that since a grant is expressed in words of the grantor's own selection, it is, prima facie, an expression of his intention, and he is therefore chargeable with the language used. If, therefore, the deed can inure in different ways, the grantee, it is said, may take it in such way as will be most to his advantage.

In *Gelfius v. Chapman*, the court looked at a subsequent description of access rights following a grant of land subject to the grantors' specific reservation of a gas and oil interest. The court found that the subsequent description did not modify the grant and reservation because it might have been copied into the deed without attention to its terms.

However, while it is the general rule that an instrument will be construed against the grantor, one needs to bear in mind that certain circumstances may supercede this rule. In *Turner v. McBroom*, the court found that the rule of deeds being construed against the grantor did not apply because there was "no evidence concerning circumstances surrounding execution and delivery of deed in question or any indication which party drafted the deed." In *Clark v. Carter*, the court did not construe the wording of the instrument against the grantors because the grantors could neither read nor write.

The words "subject to," "reserving," and "excepting" in instruments create many interpretation problems. Generally, when you "except" something, you retain it. When you use the words "subject to," you are conveying subject to an existing encumbrance but not retaining any interest yourself. Courts, however, have construed these words almost any way they see fit, particularly if there is other language that may explain the use of the terms.

The actions of the parties contemporaneous with or subsequent to the conveyance may be considered to establish the intention of the parties. "If the deed or other instrument under consideration is ambiguous, then extrinsic evidence may be admitted to show the facts and circumstances surrounding the parties and the execution of the instruments for the purpose of arriving at the true meaning of the instrument and the intention of the parties." "If, however, the deed or other instrument is not ambiguous, then such extrinsic evidence is not admissible." In *Paddock v. Vasquez*, the court stated: "Where the terms of a deed are plain and unambiguous the construction given it by the parties is ordinarily immaterial and, in the absence of fraud, accident, or mistake, parol evidence is not admissible to vary its terms." However, the court
held that parol evidence could not be admitted since the deed was clear, definite, certain, and unambiguous.\(^{(61)}\)

[vi]--Summary.

In summary, all factors must be considered and no one factor is determinative to establish the intention of the parties to create a particular interest. However, in the event a specific statement of intention is set forth in the granting clause or in a clause immediately following it, that statement will probably be given more weight than the other factor, including the words of the grant.\(^{(62)}\) Also, let me emphasize that, although courts often do not mention equities, they are always important in assisting the court in determining the "intention of the parties."

§ 17.03. Special Considerations in the Interpretation of Oil and Gas Leases.

[1]--Preparation by Lessee.

Oil and gas leases are generally prepared by the lessee. The general rule in the construction of oil and gas leases is that the instrument is to be construed against the lessee and in favor of the lessor.\(^{(63)}\) This is an established rule of construction even though it is contrary to the rule that conveyances are to be construed against the grantor. In *Schumacher v. Cole*,\(^{(64)}\) the court said that "it is a recognized doctrine in this court that oil and gas leases are to be construed liberally in favor of the lessor and strictly against the lessee."\(^{(65)}\) In *State ex rel. Commissioners of Land Office v. Couch*,\(^{(66)}\) the court stated: "At the outset we recognize that oil and gas leases are construed most strongly against the lessee and in favor of the lessor . . .."\(^{(67)}\)

Courts have fashioned this rule in the interest of promoting development and preventing delay. They looked at various factors to aid in constructing this rule. First, was the desire to secure to the lessor some type of consideration for conveyance.\(^{(68)}\) Second, was the fear that oil and gas could migrate voluntarily from one tract to the other.\(^{(69)}\) Third, was the concern that, since oil and gas was of no value in the ground, it should be developed as quickly as possible.\(^{(70)}\) Some jurisdictions are finding that this rule of construction is outdated and should not be applied.\(^{(71)}\) In *Freeland v. Edwards*,\(^{(72)}\) the court stated:

While other jurisdictions have announced doctrines of construction especially applicable to oil-and-gas leases, such rules appear to be mere ad hoc application of generally accepted principles of the construction of contracts. (2 Summers, The Law of Oil and Gas §§ 371-372.) This court has consistently applied the same rules of construction and interpretation to such leases as to other contracts.\(^{(73)}\)

Therefore, it may be that, as the reasons for this rule of construction become more and more outdated, more jurisdictions will discontinue its use.

[2]--Implied Covenants.

This Chapter discusses implied covenants because they are, in effect, a form of ambiguity in that they are matters not stated in the agreement and are subject to interpretation by the courts.

When a lessor and lessee enter into an oil and gas lease, it is under the presumption that each party is willing to do whatever is necessary to lead to the financial success of the venture. Each party is expected to undertake whatever is "reasonably" necessary for the financial success of the undertaking and to avoid
actions that would detract from its success. The duties expected on the part of the lessor are not as extensive as those imposed on the lessee. In *Kokomo Natural Gas & Oil Co. v. Albright*,(75) the court found that there was no implied covenant on the part of the lessor that natural gas would be found on the leased premises. The court determined that, if the lessee wanted assurance of natural gas on the property, it should have expressly so stated in the contract.(76) The general duties or implied covenants of the lessor may be classified as duty regarding title, duty not to obstruct lessee's operations, and duty to cooperate by consenting to prudent operations.(77) Since the duties imposed upon the lessor tend to gravitate toward basic non-interference with the lessee, we will concentrate on the duties impliedly imposed on the lessee.

Although there are many classifications concerning the implied covenants imposed upon the lessee, we will use the following classification:

The classification of implied covenants adopted in this Treatise, with a brief comment on each covenant, follows: (1) The covenant to drill an initial exploratory well . . .. (2) The covenant to protect the leasehold from drainage . . .. (3) The covenant to reasonably develop the premises . . .. (4) The covenant to explore further . . .. (5) The covenant to market the product . . .. (6) The covenant to conduct with reasonable care and due diligence all operations on the leasehold that affect the lessor's royalty interest . . ..(78)

However, you must remembered that the implied covenant must be able to coexist with the express provisions of a lease. In *Swiss Oil Corp. v. Riggbsy*,(79) the court stated "The rule applies only where the express and the asserted implied provisions relate to the same subject matter or some particular part thereof, and there is a conflict, in which case the express agreement would supersede the implied one. It is otherwise when there is no conflict."(80) In *Linn v. Wehrle*(81) the court stated: "The law seems well settled in Ohio that there can be no implied covenant in a contract in relation to any matter that is specifically covered by the written terms of the contract itself."(82) And in *Hartman Ranch Co. v. Associated Oil Co.*,(83) the court stated: "Where express covenants do not cover completely all phases of the lessee's obligation in regard to exploration, development, and protection, implied covenants may coexist with express covenants."(84)

The first implied duty we will examine is the duty to drill an exploratory well. The general rule is that there is an implied covenant in an oil and gas lease requiring the lessee to begin development within a reasonable time.(85) In *Mansfield Gas Co. v. Alexander*,(86) the court determined that there was an "implied covenant" on the part of the lessee to "make the exploration and search for the minerals in a proper manner and with reasonable diligence . . .."(87) However, one must be conscious of express provisions that would supercede the implied covenant. In *New Harmony Realty Corp. v. Superior Oil Co.*,,(88) the court found there was no implied covenant to drill an exploratory well where there was an express provision in which "the contracting parties declared that no implied covenants should affect or be effective to interpret, change or restrict such plain expressions of agreement."(89)

One such express provision that courts have declared supercedes the implied covenant to drill an exploratory well is the "drilling clause." "In a majority of jurisdictions with decisions on the point, this objective has been achieved. According to this majority view, the drilling clause specifically covers the subject of drilling an exploratory well, and the lessor has agreed to accept rentals in lieu of drilling."(90) While the majority may cling to this philosophy, there is a minority view which states "the principal objective of the lease is the development of the property for oil and gas, and in order to effectuate such purpose, the lessor is privileged to refuse to accept delay rentals and demand a well."(91)

The main question to be answered concerns the standard to which a lessee is to be held when determining if there was a breach of the implied covenant to drill an exploratory well. Many courts have held the standard
to be one of ordinary diligence. In *Mansfield Gas Co. v. Alexander*, the court found that the lessee "must prosecute the work in the manner in which the business is ordinarily carried on, and with ordinary diligence until the search for oil and gas is ended, either by finding it and thereafter operating the premises, or by demonstrating that there is no oil or gas and surrendering the lease." (93)

The next implied covenant we will look to is that imposing the duty to drill additional developmental wells. Once oil and gas have been discovered in paying quantities, there is an implied duty on the part of the lessee to continue to develop the premises (94) "This duty may be described in the traditional manner as a duty to such additional development wells as may be required for full development of the leased premises. . . . The duty has also been described as being sufficiently broad to include a duty to engage in further exploration." (95)

Some courts are more likely to find that this implied covenant exists where the consideration for the lease is a royalty to be paid to the lessor. In *George v. Jones*, (96) the court found that "if the consideration for the lease is a royalty to be paid to the lessor on the product of the mine, there is an implied covenant that the work of prospecting and development shall be prosecuted . . .." (97)

One must also remember that, being an implied covenant, this duty may be affected by express provisions in the instrument:

The specific provision regarding development wells is likely to fall in one of several possible categories: (1) it may be descriptive of existing duty, (2) it may prescribe the number of wells to be drilled, (3) it may provide that further drilling is at the discretion of the lessee, or (4) it may provide that there shall be no implied obligation of further development. (98)

In order to determine if there has been a breach of this implied duty, a court must determine the standard of care to be demonstrated by the lessee. The most common standard is the prudent operator standard. In *Sun Oil Co. v. Frantz*, (99) the court stated:

[T]he prudent operator rule applies and imposes on the lessee the implied duty to do whatever in the circumstances would be reasonably expected of a prudent operator of a particular lease, having a rightful regard for the interest of both the lessor and the lessee. Each case stands on its own facts and the cardinal principles that govern the mutual duty of fair play must be applied. (100)

The next implied duty to be examined is the duty of diligent and proper operation. "The lessee's duty of diligent and proper operation is a broad duty to perform certain operations such as the testing, completing, operating, reconditioning, and plugging of wells. It is a broad duty to perform those operations and all others in a diligent manner." (101) This duty is broad and its adequate performance may be difficult to ascertain. While different standards may be applied, some tend to be more prevalent than others. In *Warfield Natural Gas Co. v. Allen*, (102) the court applied the standard of "good faith and sound discretion." The court stated:

[T]he law will imply an agreement to do and perform those things that according to reason and justice the parties should do in order to carry out the purpose for which the contract was made . . . among them is the obligation that the lessee would test and develop the property in good faith, . . .." (103)

Another standard that may be applied is the prudent operator rule. In *Chenoweth v. Pan American Petroleum Corp.*, (104) the court stated "As the term suggests, it imposes upon the lessee the implied duty to do whatever in the circumstances would be reasonably expected of a prudent operator of a particular lease,
having a rightful regard for the interest of both the lessor and lessee."

Another implied covenant applied to oil and gas leases is the duty to market production. Professor Kuntz has said:

It should be recognized at the outset that the requirement of marketing by the lessee of oil, gas, or other substances produced under the terms of the oil and gas lease is a complex requirement in that it may operate as a special limitation, as part of an express covenant, or as an implied affirmative obligation.\(^{106}\)

Although there is an implied duty to market production, the parties must be aware of express provisions in the lease which supercede any implied duty. One provision would be a shut-in gas royalty clause: \(^{107}\)

Depending upon the wording of the clause, it may relieve the lessee of the duty to market gas for a specified period of time, establish a period of time within which the lessee must market the product, or have no effect on the diligence required of the lessee in seeking a market for the gas. . . . Other clauses which may have an effect on the implied duty to market the product are the forfeiture, the non-forfeiture, notice, and judicial ascertainment clauses. \(^{108}\)

Professor Kuntz has further observed:

The standard of performance uniformly required of the lessee to comply with his implied duty to market oil or gas is the prudent operator standard under which the lessee is required to exercise reasonable diligence or the degree of diligence that would be exercised by an ordinary prudent operator having regard for the interests of both the lessor and lessee. \(^{109}\)

However, while the lessee will be held to the prudent operator standard in the majority of jurisdictions, the lessee will probably not be held to the high standards of a fiduciary. \(^{110}\)

Where the lessee has not abandoned the lease, its failure to market the product has been regarded as a passive breach. As a result, the lessor must place the lessee in default by making demand before seeking cancellation or forfeiture. Demand is not required if the lease has expired or the lessee has abandoned it. \(^{111}\)

Another implied duty imposed upon the lessee is the duty to protect against drainage. In *Indian Territory Illuminating Oil Co. v. Rosamond*, \(^{112}\) the court stated: "The implied covenant of the lease, that the lessee will protect the land from drainage by adjoining wells so long as the drilling of a protection well or wells will . . . be a profitable undertaking." \(^{113}\) Again, however, one must be aware of the express provisions that may exist in the lease:

Specific provisions which relate to the lessee's duty to protect against drainage range from provisions which are descriptive of the existing duty, though provisions which eliminate the duty entirely and provisions which modify the duty by substituting either a minimum requirement or a maximum requirement, to provisions which serve other purposes but may or may not have a concurrent effect on the lessee's duty to protect against drainage. \(^{114}\)

The standard imposed on the lessee may vary depending on the jurisdiction. However, the most common standard is the prudent operator standard, under which "the lessee must drill a well to protect the leased premises from drainage if a prudent operator would do so." \(^{115}\) In *Central Kentucky Natural Gas Co. v. Williams*, \(^{116}\) the court stated "the lessee or the owner of the lease must act in good faith, and as an ordinarily prudent operator." \(^{117}\)
The final implied covenant which may be recognized is the duty of further exploration. This duty is not recognized in all jurisdictions. A Texas court recognized it in *Willingham v. Bryson*. However, the Texas Supreme Court rejected the idea of an implied duty of further exploration in *Clifton v. Koontz*.

In *Fox Petroleum Co. v. Booker*, the court found that an implied duty of further exploration existed. It also found that the covenant operated during and after the fixed term of the lease once oil or gas had been discovered. Once a court has determined this implied duty exists, it must determine if it is superceded by express provisions in the lease:

A specific provision regarding further exploration is likely to fall into one of several categories: (1) it may describe the circumstances under which further exploration is required, (2) it may be descriptive of existing duty, (3) it may provide for a specific drilling obligation, (4) it may provide against a duty of further exploration, or (5) it may be in the form of a modification of some standard clause in the lease.

Many courts have used the prudent operator standard to evaluate a lessee's further exploration actions. In *Trust Co. of Chicago v. Samedan Oil Corp.* the court stated "it imposes upon the lessee the implied duty to do whatever in the circumstances would be reasonably expected of a prudent operator of a particular lease, having a rightful regard for the interest of both the lessor and lessee."

[3]--Other Lease Clauses.

[a]--Lesser Interest Clause.

A lesser interest clause may also be called a proportionate reduction clause, a reduction clause, or a lesser estate clause. A lesser interest clause ordinarily provides "that if the lessor's interest in the leased premises is less than the entire and undivided fee simple estate therein, the royalties and rentals called for by the lease are to be paid to the lessor only in the proportion that his interest bears to the whole undivided fee." We sometimes see the so-called "Lesser Interest Clause" deleted. For example, the lease provides that the lessor will receive a royalty payment. After title is examined, it is found that the lessor only owns a one-half interest in the property. If the lesser interest clause has been deleted, it would appear that you now must pay the lessor the full interest. Courts have determined that this is not always the case. They have determined that the written portion controls over the printed portion. In one instance where a bonus clause was provided, the court determined that it was not affected by the lesser interest clause. Therefore, if you provide any rights in the written matter as opposed to the printed matter, you should be extremely careful to provide that any such right would be limited by the lesser interest clause. Also, if the lease clearly states that the lessor owns only a one-half interest and a royalty interest is provided, the lesser interest clause will not affect the lessor, and the lessor will receive a royalty, notwithstanding the fact that the lessor only owns a one-half interest.

[b]--Conduct of the Parties.

While the construction of the instrument is usually the controlling factor to determine intent, it is not given the same degree of importance in all jurisdictions. In *Harbert v. Hope Natural Gas*, the West Virginia court stated:

Consumption of the gas not being confined to a dwelling house on the leased premises, by the terms of the lease, the place of consumption is one of intention, to be determined by the facts and circumstances relating to the subject matter of contract, known to the parties at the time, and by their subsequent conduct in the execution thereof, indicating such intention.
In other words, your practices may overrule the express wording of the lease.

[c]--Producing Well.

It should be noted that discovery without production is generally not considered to be a producing well. One interesting case involved a lease which stated that a "Pugh clause" should be included. No specific clause was inserted.

The term "Pugh" Clause has reference to a lease provision to the effect that, notwithstanding any provision of the lease to the contrary, drilling operations on or production from a pooled unit established under the lease, embracing a part of the lessor's lands and other lands, will serve to maintain the lease in force and effect only as to the lands in the unit, and that the lease may be maintained as to the remainder of the land only by doing so in a manner specified in the lease; and if it is to be done by delay rental payments, rentals shall be payable on the number of acres not included in the unit.

Pugh Clauses vary. However, generally they provide that only the unitized portion of the lease will be held if the lease is unitized. In the case we are discussing, the landowner stated that the intention of the Pugh Clause was to limit the held acreage only to the drilling units even though there was no unitization. This issue was never litigated due to its eventual settlement.

[d]--Forfeiture Provisions.

Forfeiture provisions appear to be favored by courts in oil and gas leases. An "unless" type lease is "[a]n oil and gas lease which provides that the lease will be rendered null and void and the lessee will automatically be relieved from liability, upon failure to commence operations or to pay rent." It must be expressly stipulated in the lease that the lease shall become null and void at a certain time unless the lessee begins operations or pays the rentals stipulated. In the cases of an "unless" type lease, courts have declared forfeiture for failure to pay rentals. For the most part, in oil and gas leases, equity does not abhor forfeiture.

§ 17.04. Specific Problems Regarding Ambiguities as They Relate to Oil and Gas.

[1]--Mineral Exceptions in Deeds.

Courts have generally held that, after discovery of oil and gas and, if oil and gas was known in the area, a deed excepting "coal and all other minerals" would be deemed to include oil and gas in the exception absent any express words of limitation or other words indicating a contrary intent.

Courts, however, have been quick to reach an opposite conclusion where words have been placed in the instrument indicating that only the removal of coal and clay was intended. For instance, the reservation of the right to use the surface referred to only items that would be utilized in the removal of coal and clay. In Detlor v. Holland, a conveyance stated:

do hereby grant, bargain, sell and convey to the said Michael L. Deaver, his heirs and assigns forever, all the coal of every variety and all the iron ore, fire clay and other valuable minerals in, on, or under the following described premises . . . together with the right in perpetuity to the said Michael L. Deaver, or his assigns, of mining and removing such coal, ore or other minerals, and the said Michael L. Deaver, or his assigns, shall also have the right to the use of so much of the surface of the land as may be necessary for pits, shafts, platforms, drains, railroads, switches, sidetracks, etc., to facilitate the mining and removal of
such coal, ore, or other minerals and no more.

The court held that the deed did not convey the oil and gas on the premises.\(^{(134)}\)

To some degree, Ohio courts have made a full turn on this matter. In *Myrtle Muffley v. M.B. Operating Co., Inc.*,\(^{(135)}\) the court stated:

The instant deed of conveyance was executed in 1960. It is beyond dispute that in that year oil and gas drilling had been conducted in Tuscarawas County for decades. Thus, the absence of a specific oil and gas reservation must be construed in favor of appellee as was accomplished by the trial court.

Thus, the courts have departed from their original interpretation that a reservation of coal and all other minerals will include oil and gas if it was known in the area. Thus, the law now may be that, if a reservation was made after 1860 when oil and gas was known and oil and gas activities were common in the area, the absence of a specific reservation of oil and gas will be deemed to limit the reservation to minerals other than oil and gas. In one case, the court, in seeking the intention of the parties, looked to the Charter of the grantor corporation. This provided only for the development of coal and clay. Therefore the court determined that it was not the intention of the grantor to reserve oil and gas. Courts find the "intention of the parties" in strange places.

[2]--Merger of Title.

Whether there is a merger of title depends on the intention of the parties and the equities of the case. In many instances, a landowner acquires an oil and gas lease on his farm and the question then arises as to whether there is a merger of title. Does the oil and gas lease continue to exist after the landowner conveys the premises?

The doctrine of merger of title often arises in mortgage cases. For example, A mortgaged to B and also gave a second mortgage to C. B then acquired the property (B usually being a bank), and then C claimed that the first mortgage merged into the title and the second mortgage is now the superior lien. However, courts have found that this is not true. This problem was addressed in *Colopy v. Wilson*.\(^{(136)}\) The landowner, Mr. Colopy, acquired the oil and gas lease and later sold a portion of the property to his son, retaining a second mortgage. The gas well was on the son's property; however, the father continued to use gas from the well. The bank foreclosed the first mortgage and named the father as a party to that proceeding. Mr. Wilson acquired the property at the foreclosure proceeding. At no time was the oil and gas lease mentioned. Mr. Wilson shut off Mr. Colopy's gas, claiming that the lease had merged and that Colopy had no right to take free gas. The trial court found in favor of Mr. Colopy. However, the appellate court found it necessary to determine whether there had been a merger of title and remanded. This matter is still pending. In the meantime, Mr. Colopy's family is still taking free gas, and Mr. Colopy is now deceased. This matter was complicated by the fact that Mr. Colopy hit Mr. Wilson across the head with a wrench.

The best way to resolve this question in Ohio is to file a Certificate of Merger.

[3]--Deed vs. Lease.

A question can arise as to whether the instrument of conveyance is a deed or a lease. Minerals can be severed with a proper instrument. A court will attempt to determine the intention of the parties involved. However, it is often times difficult to tell the intention of parties as to whether there has been a severance or a lease. While calling the instrument a "deed" or a "lease" may be examined in the determination, it is not a controlling factor. Controlling factors include: (1) Is there a stated time? (2) is the payment based on removal? (3) Was the price paid adequate?
[4]--Reservations of a Royalty Interest in a Deed.

When dealing with reservations of a royalty interest in a deed, the first question is whether this is a participating or a non-participating interest. In the case of a participating interest, the party reserving the royalty must sign the oil and gas lease. Generally, reservation of royalty will be considered the reservation of a non-participating interest unless further rights are stated. The second question is whether there has been a prior reservation of a royalty or of minerals. For example, A conveys to B, reserving a one-half interest in the minerals. There has been a previous reservation of a one-half interest in the minerals. The general rule, subject to a determination of the intention of the parties, is that the one-half is conveyed by A to B. Therefore, it is necessary that the previous reservation be set forth if you intend to retain the other half.

In Texas, the court has fashioned a rule referred to as the "Duhig Rule." The court found that a granted interest takes priority over a reserved interest to the extent possible. However, the "Duhig Rule" is not followed if it can be shown that the grantee had actual notice of previously reserved interests.

[5]--Assignment of Leases.

The examination of the assignment of leases is a source of vast confusion. To begin, it should be understood that the Working Interest is 8/8 of something. The Working Interest is the operating interest under an oil and gas lease. An Overriding Royalty is a royalty interest carved out of the Working Interest created by an oil and gas lease. Assuming a landowner's royalty is the traditional, and there are no Overriding Royalty Interests, the Working Interest is 8/8ths of . In many instances, assignments transfer the "Working Interest." Thus the question which needs to be addressed is whether or not the assignor reserved a ths Working Interest. In order to avoid judicial interpretation, assignments should be specific. For instance, if there is a 1/16 of Overriding Royalty Interest outstanding, it should be designated that the Working Interest is 8/8 of 15/16 of . It is also quite helpful to utilize a statement known as the Net Revenue Interest.

Another problem that may arise is with the reservation of an Overriding Royalty Interest. Often we see a reservation of a 1/16 Overriding Royalty Interest. Many times, the parties feel that this should be 1/16 of 8/8. Courts will find that, if the landowner's royalty is , it is 1/16 of unless stated specifically to the contrary. One major point of confusion is where the assignor assigns one-half of the Working Interest to B, subject to a 1/16 Overriding Royalty Interest. The question then is whether the one-half Working Interest should bear the entire 1/16 Overriding Royalty Interest or should it be apportioned. If it is not so stated that it is proportional, courts generally find that the assigned interest will bear the entire burden of the override.

Another difficulty may arise in the use of decimal equivalents. Most Division Orders are stated in decimal equivalents. However, many people use these and then place a percentage sign after them. This, of course, creates an extremely minor interest in a property when a more substantial interest was intended.

§ 17.05. Conclusion.

We have discussed general rules of construction and how they apply to oil and gas leases. We have considered specific matters where ambiguities arise in the oil and gas industry. The most important thing to keep in mind is that, in the case of uncertainty, the "intention of the parties controls." The intention is whatever a court decides it to be. Decisions can be found almost going any way you want. In reviewing the many cases on this subject, it appears that the courts have attempted to resolve uncertainties by reaching an equitable result. Lawyers who copy previous deeds without giving thought to what their language means create many of the problems regarding minerals. As always, careful drafting can avoid most ambiguity.
problems.


2. 2. *Henry's History of Petroleum*, p. 60.


5. 2. *Id.* at 933.


7. 4. 218 P. 501 (Okla. 1921).

8. 5. *Id.* at 502.


10. 7. 145 N.W.2d 904 (N.D. 1966).

11. 8. *Id.* at 908.


13. 10. 378 S.W.2d 806 (Ky. 1964).

14. 11. *Id.* at 808.


16. 13. *Id.* at 124.


18. 15. *Id.* at 477.


20. 17. *Id.* at 144.


23. 20. 266 P.2d 467 (Okla. 1953).

24. 21. *Id.* at 470.


26. 23. 15 F.2d 323 (8th Cir. 1926).
27. 24. *Id.* at 326.

28. 25. See, *e.g.*, Wm. Lindeke Land Co. v. Kalman, 252 N.W. 650 (Minn. 1934).

29. 26. 189 S.W.2d 477 (Tex. 1945).

30. 27. *Id.* at 479.

31. 28. 197 So. 2d 672 (La. 1967).

32. 29. *Id.* at 678.


34. 31. Dale v. Case, 64 So. 2d 344 (Miss. 1953).

35. 32. 663 S.W.2d 180 (Ark. 1984).

36. 33. *Id.* at 182.


38. 35. 290 P.2d 1039 (Kan. 1955).

39. 36. *Id.* at 1044.


41. 38. 94 A.2d 724 (Pa. 1953).

42. 39. *Id.* at 725.


44. 41. *Id.* at 375.

45. 42. *Id.* Also see text, *infra*, at § 17.04[1]. [For elaboration on this subject, see Carpenter, "Interpreting Grants and Reservations of `Minerals' and `Other Minerals': When Is a Mineral Not a `Mineral'?," 5 *Eastern Min. L. Inst.* ch. 10 (1984) – *Ed.*]

46. 43. Continental Oil Co. v. Walker, 117 So. 2d 333 (Miss. 1960).


48. 45. *Id.* at 225.

49. 46. 403 P.2d 800 (Kan. 1965).

50. 47. *Id.* at 805.


52. 49. *Id.* at 1048.

54. 51. Id. at 46.

55. 52. 351 So. 2d 1333 (Miss. 1977).

56. 53. Id. at 1334.


58. 55. Id. at 479.


60. 57. Id. at 128.

61. 58. Id.


64. 2. 309 P.2d 311 (Mont. 1957).

65. 3. Id. at 314.

66. 4. 298 P.2d 452 (Okla. 1956).

67. 5. Id. at 453.


69. 7. Id. at 500.

70. 8. Id.

71. 9. Id.

72. 10. 142 N.E.2d 701 (Ill. 1957).

73. 11. Id. at 703.


76. 14. Id. at 684.


78. 16. 5 H. Williams & C. Meyers, Oil & Gas Law § 804 (1964).

79. 17. 67 S.W.2d 30 (Ky. 1933).
80. 18. *Id.* at 34.


82. 20. *Id.* at 289.

83. 21. 73 P.2d 1163 (Cal. 1937).

84. 22. *Id.* at 1166.


86. 24. 133 S.W. 837 (Ark. 1911).

87. 25. *Id.* at 838.


89. 27. *Id.* at 677.


91. 29. *Id.*

92. 30. 133 S.W. 837 (Ark. 1911).

93. 31. *Id.* at 840.


96. 34. 95 N.W.2d 609 (Neb. 1959).

97. 35. *Id.* at 616.


99. 37. 291 F.2d 52 (10th Cir. 1961).

100. 38. *Id.* at 54.


102. 40. 59 S.W.2d 534 (Ky. 1933).

103. 41. *Id.* at 536.

104. 42. 314 F.2d 63 (10th Cir. 1963).

105. 43. *Id.* at 66.

106. 44. 5 E.O. Kuntz, *The Law of Oil & Gas* § 60.1 (1987).


Id. at § 60.3.

Craig v. Champlin Petroleum Co., 435 F.2d 933 (10th Cir. 1971).


120 P.2d 349 (Okla. 1941).

Id. at 352.


Id. at § 61.3.

60 S.W.2d 580 (Ky. 1933).

Id. at 584.


325 S.W.2d 684 (Tex. 1959).

253 P. 33 (Okla. 1926).

Id. at 34.


192 F.2d 282 (10th Cir. 1951).

Id. at 284.


84 S.E. 770 (W. Va. 1915).

Id. at 770.


Id. at 1378.

49 N.E. 690 (Ohio 1898).
2. *Id.* at 690.

134. 3. *Id.*


138. 7. Duhig v. Peavy-Moore Lumber Co., 144 S.W.2d 878 (Tex. 1940).

139. 8. *Id.* at 879.


144. 13. La Laguna Ranch Co. v. Dodge, 114 P.2d 351 (Cal. 1941).