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# ONE J

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## CURATIVE POOLING WHEN THE VALIDITY OF AN OIL AND GAS LEASE IS CHALLENGED (FORCE POOLING THE TOP LESSEE)

MATT ALLEN<sup>\*</sup>

### *Introduction*

To say the least, significant exploration and development is occurring in the STACK and SCOOP plays of Oklahoma. The favorable reservoir economics of the STACK and SCOOP, coupled with a seemingly sturdy (albeit unglamorous) price of oil, have resulted in a highly competitive environment from the land perspective. A familiar scenario has developed: a few acres of leasehold in the right place, at the right time, can result in a financial windfall. With money to be made and available leasehold in proven areas becoming scarce, the top lease offers an enticing and cheap method to acquire valuable leasehold in promising areas (if your top lease vests, that is).

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Top leases within these competitive areas is a challenge to address from the operator's standpoint. Often, the operator owns leasehold in the unit that is held by production by a marginal well. The operator would like to commence operations on a new well to preserve the existing base leases. Top leases are taken by opportunistic players. The top lease is like a time bomb, but without the informative Mission Impossible style digital clock ticking down to let the operator know just when to take cover. Should the top lease vest by a court adjudication, the top lease might be determined to be effective at a point in the past. That could result in a significant amount of leasehold being carried in the well, with the operator taking all of the risk of the well costs attributable to the top lease. Yet, until the top lease is clearly vested, the top lessee might not own any drilling rights at all.

The operator is stuck. Should the operator enter into a joint operating agreement with a party who is not currently in title, and may never be? Can the operator ask the Corporation Commission to force pool top lessees? What we do know is that the operator will not want to, and should not have to, take on all the risk of drilling a well with acreage potentially outstanding. This paper addresses the force pooling of owners of top leases as "curative" parties before the Oklahoma Corporation Commission.

#### *The Commission's Origins and Jurisdiction to Force Pool*

The Oklahoma Corporation Commission was created by the Oklahoma Constitution. The Commission does not have any independent plenary power over conservation matters. All of the Commission's authority in conservation matters is derived from legislative delegation. Therefore, any Commission order in a conservation matter must be authorized explicitly by statute or through necessary implication from statute. The Commission does not have the authority or jurisdiction to enter any order that is outside the authority or jurisdiction granted by the Legislature.<sup>1</sup> An order that exceeds the jurisdiction or authority delegated by the Oklahoma Legislature cannot stand.<sup>2</sup> Importantly,

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1. *Kingwood Oil Co. v. Hall-Jones Oil Co.*, 1964 OK 231, 396 P.2d 510, 513. ("It is well settled that the Corporation Commission is a tribunal of limited jurisdiction, and that it has only such jurisdiction and authority as is expressly or by necessary implication conferred upon it by the constitution and statutes of this state.")

2. *See e.g., Inexco Oil Co. v. Okla. Corp. Comm'n*, 1988 OK 78, 767 P.2d 404, 406.

### 1. What is a “top lease”?

First things first: what’s a top lease? A top lease is a “lease granted by a [mineral owner] during the existence of a recorded mineral lease which is to become effective if and when the existing lease expires or is terminated.”<sup>3</sup> Top leases historically were considered to be “invidious” and as distasteful as “claim jumping.”<sup>4</sup> Currently, top leases are considered a legitimate, if annoying, contractual arrangement.

A top lease vests by operation of law when the underlying base lease terminates, thereby placing the drilling rights associated with the subject mineral tract into the top lessee’s ownership without need for a new lease from the mineral owner. A base lease typically terminates under its own terms (whether in the primary or secondary term) but can also be terminated voluntarily by the lessee releasing the lease of record. The most common scenario is that the base lease has been perpetuated into its secondary term by production, a top lease is executed by the mineral owner, and then the production from the well holding the base lease becomes questionably economic, casting the continuing effectiveness of the base lease into doubt and therefore, possibly causing the top lease to vest. If a base lease possibly has terminated for lack of production, and the base lessee refuses to release the lease, the top lessee may bring an action in district court to cancel the base lease. Based on the facts presented, the court may adjudicate the base lease to be effective, or alternatively decide that the base lease terminated at some point in the past, thereby vesting the top lease at that same point in the past. Until the top lease vests, in theory and depending on the language within the top lease, a top lessee probably holds a reversionary interest held by the mineral owner.<sup>5</sup>

The district court is empowered to determine that the top lease vested at some point certain in the past because that is the moment the base lease terminated, causing the top lease to vest. Before that adjudication occurs, the top lessee does not have any clearly vested drilling rights but could potentially own drilling rights. The difficult issue here is that before there is an adjudication as to the effectiveness of the base and top leases, no one

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3. *Harding & Shelton v. Prospective Inv. and Trading Co.*, 2005 OK CIV APP 88, 123 P.3d 56, 59 n. 2 (hereinafter referred to as “*PITCO*”) (citing 8 Williams & Meyers, *Oil and Gas Law*, 1115 (2004)).

4. *Frankfort Oil Co. v. Snakard*, 279 F.2d 436, 445 n. 23 (10th Cir. 1960), *cert. denied* 364 U.S. 920 (1960).

5. *Voiles v. Santa Fe Minerals, Inc.*, 1996 OK 13, 911 P.2d 1205, 1209.

knows whether the top lease is effective for certain, and if so, when it became effective.

This stymies development because any operator proposing a well does not know whether the top lessee owns any drilling rights. If the operator ignores the top lessee and commences operations on a new well, the operator is taking on a significant risk that the top lessee will later be adjudicated as an owner of drilling rights. The operator will have sustained all the top lessee's risk in the new drilling endeavor. If the operator treats the top lessee as an actual owner in order to foreclose this risk, the operator may be inadvertently admitting the base leases have terminated. A solution is to have the Commission force pool the top lessee while maintaining the operator's stance that the base leases are still in full force and effect. But can the Commission force pool a top lessee?

## 2. *What type of owner can the Commission force pool?*

The Oklahoma Supreme Court in *O'Neill v. American Quasar Petroleum Co.*<sup>6</sup> defined who and what type of interest may be made subject to a force pooling order of the Commission. In *O'Neill*, a leasehold owner carved out overriding royalty interests from its working interest and granted them to several grantees.<sup>7</sup> Some, but not all, of those grants also contained a provision whereby the override would be convertible to working interest upon payout of the unit well.<sup>8</sup> American Quasar Petroleum Company ("American Quasar") informed the leasehold owner that American Quasar intended to drill a well on the leasehold premises. American Quasar filed a pooling application, joining the leasehold owner and the grantees (who owned only the overriding royalty interest and no drilling rights or working interest) in the pooling.<sup>9</sup> The Commission entered an order pooling all of the parties. The order required the owners of overriding royalty interests to pay their proportionate share of well costs, or instead "To receive in addition to the normal 1/8th royalty an override of 1/16th of 7/8ths on oil and 1/8th of 7/8ths on natural gas."<sup>10</sup> The owners of the overriding royalty interest appealed from the Commission's order arguing, inter alia, that the Commission did not have the statutory authority to force pool owners of overriding royalty interests.<sup>11</sup>

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6. 1980 OK 2, 617 P.2d 181 (Okla. 1980).

7. *Id.* at 182.

8. *Id.*

9. *Id.*

10. *Id.*

11. *Id.*

The Oklahoma Supreme Court agreed with the appellants. The court first reviewed the pooling statute, which reads:

When two or more separately owned tracts of land are embraced within an established spacing unit, or where there are undivided interests separately owned, or both such separately owned tracts and undivided interests embraced within such established spacing unit, the **owners** thereof may validly pool their interests and develop their lands as a unit. Where, however, **such owners** have not agreed to pool their interests and where one such separate owner has drilled or proposes to drill a well on the unit to the common source of supply, the Commission, to avoid the drilling of unnecessary wells, or to protect correlative rights, shall, upon a proper application therefor and a hearing thereon, require such owners to pool and develop their lands in the spacing unit as a unit.<sup>12</sup>

The “owner” referenced in the pooling statute is defined as follows in 52 O.S. § 86.1 (4):

4. "Owner" means a person who has the right to drill into and to produce from any common source of supply and to appropriate the production, either for that person or for that person and others;

In analyzing these two provisions, the court noted that the owner of an overriding royalty interest has no assertible right in the oil and gas leasehold.<sup>13</sup> The court then determined that the owner of an overriding royalty interest cannot be an “owner” as defined by § 86.1 because the owner does not own a right to drill.<sup>14</sup> The court concluded that the Commission does not have the requisite jurisdiction to enter a pooling order requiring the owner of an overriding royalty interest to make an election between participation or an alternative.<sup>15</sup> The court therefore reversed the Commission’s order.

We learn from *O’Neill* that the owner of a right to drill<sup>16</sup> is an appropriate party to force pool and the Commission does not have the

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12. OKLA. STAT. ANN. tit. 25 § 87.1(e) (emphasis added) (West 2018).

13. *O’Neill*, 617 P.2d at 184.

14. *Id.*

15. *Id.* at 185.

16. The phrases “right to drill” or “drilling rights” are commonly understood to mean “working interest,” which is the operating interest under an oil and gas lease giving the party

jurisdiction to force pool owners of overriding royalty interest. By extension, the court's holding in *O'Neill* should apply to any portion of the fee mineral interest that is not the "right to drill." This point of law has been confirmed a number of times and is well-settled law.<sup>17</sup>

Critically, the *O'Neill* court found the Commission does not have the requisite statutory jurisdiction to force pool any type of interest other than drilling rights. Therefore, any order attempting to force pool interests other than drilling rights would fail *for lack of jurisdiction*. This complicates the issue. The order will appear effective on its face as to all of the parties set forth on the respondent list appended to the order, even if the Commission's jurisdiction failed as to a party; but any pooling order that purports to covers any type of interest other than drilling rights would be void ab initio as to that interest. A cursory review of the order will not review the fatal defect.

In theory, the Commission would not have had jurisdiction to force pool that owner and that interest at any time. Whether the owner of an overriding royalty interest objects to the Commission's attempt to force pool matters not — the defect is jurisdictional from the onset of the proceeding. The Commission never had any authority to force pool the interest or owner. It should not matter what the Commission attempted to do — if the defect is jurisdictional, the order must fail at least as to that interest and party.<sup>18</sup> The Commission has no authority to enter an order that would affect the owner

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the right to explore for hydrocarbons and reduce them to possession. H.R. Williams & C.J. Meyers, *MANUAL OF OIL AND GAS TERMS* (15th ed. 2012).

17. *BP Am. Prod. Co. v. Lo Yare, L.P.*, No. 104,680, 2008 WL 9876064, at 3 (Okla. Civ. App. July 11, 2008) ("Given this statutory definition of owners applicable in the context of pooling, the Commission's statutory authority in its issuance of a pooling order is limited to the forced pooling of only those owners with a right to drill."); *O'Neill v. America Quasar Petroleum Co.*, 617 P.2d 181, 184 (Okla. 1980) (citing Okla. Stat. Ann. tit. 52, § 86.1(d) (West 2018), 87.1(d) (West 2018); *Grace Petroleum Corp. v. Corporation Comm'n of State of Okla.*, 841 P.2d 1172, 1174 (Okla. Civ. App. 1992); *Alliance Oil & Gas Co. v. Chesapeake Expl. Ltd. P'ship*, No. CIV-04-1779-W, 2006 WL 8436211, at \*5 (W.D. Okla. Jan. 18, 2006) (citing *O'Neill v. America Quasar Petroleum Co.*, 617 P.2d 181, 184) ("Oklahoma law clearly establishes that the OCC has no authority to require owners of an overriding royalty interest to pool those interests.").

18. An analogous situation is when the Oklahoma Supreme Court determined in 1986 that the Commission did not have the jurisdictional authority under the force pooling statute to pool by the wellbore. *See Amoco Prod. Co. v. Corp. Comm'n of State of Oklahoma*, 1986 OK CIV APP 16, 751 P.2d 203. The Commission had entered countless pooling orders that were intended to and explicitly force pooled by the wellbore. Upon challenge by Amoco, the court ruled that the Commission did not have, and never had, the jurisdiction to force pool by the wellbore because the statute intended for pooling to be by the unit.

(although it is always a good idea to appear and protect yourself instead of hoping the case law supports your appeal).<sup>19</sup> The Commission has primary jurisdiction to review its own jurisdiction in a Commission proceeding.<sup>20</sup> Only upon a challenge of the Commission's lack of jurisdiction<sup>21</sup> would it become clear whether the order was not effective as to the party and interest.

### 3. *Pooling a party as a "curative" matter.*

At the moment the pooling application is filed, the top lessee is not a clearly vested owner of drilling rights. By requesting a pooling, the applicant is alleging implicitly (or perhaps explicitly) that the parties named are all appropriate parties to be force pooled, thereby ostensibly admitting that the top lessee is an owner of drilling rights. At the same time, the operator is likely asserting in district court that the top lessee does not own any drilling rights. Can this top lessee be force pooled? How does the operator/applicant protect its legal position?

The Commission recognizes and allows the pooling of a party for "curative" purposes when the title to drilling rights may be uncertain. That said, there is no official definition of "curative" to be found in relation to a force pooling. A single mention of "curative" pooling exists in the Commission's Rules of Practice:

(f) Exhibit list of respondents. A pooling order shall contain an attached exhibit listing all respondents or interests in the following manner:

- (1) Known respondents. List all known respondents by name and address.

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19. See e.g., *Alliance*, No. CIV-04-1779-W, 2006 WL 8436211, at \*5 ("Chesapeake attempts to distinguish *O'Neill* on the ground that the owner of the overriding royalty interest there in dispute objected to and then appealed the OCC's pooling order, whereas Alliance did neither. The Court finds this distinction to be of no consequence. As the OCC had absolutely no power to pool Alliance's overriding royalty interest, Alliance's silence in the face of the pooling proceeding can in no way be construed as a forfeiture of its rights as the issue goes to the heart of the OCC's jurisdiction.").

20. *Arkla Exploration Co. v. Shadid*, 1985 OK CIV APP 40, 710 P.2d 126, 128, (quoting *Harding & Shelton, Inc. v. Prospective Inv. & Trading Co.*, 2005 OK CIV APP 88, 123 P.3d 56, 62).

21. This is a permitted collateral attack, as challenges to the Commission's jurisdiction may be raised at any time. See e.g., *Inexco Oil Co. v. Okla. Corp. Comm'n*, 1988 OK 78, 767 P.2d 404, 406.

- (2) Unknown and/or unlocatable respondents. List all respondents, with last known address if available, or if there are none so state under this section of the exhibit.
- (3) Respondents listed for curative reasons only. List all respondents or if none so state under this section of the exhibit.<sup>22</sup>

Without an established legal definition, we are left to our own devices to describe or define what constitutes a “curative” party in a pooling.

Helpfully, the Oklahoma Court of Civil Appeals has taken judicial notice of the “curative” pooling and did not determine that curative pooling is inappropriate (at least insofar as an operator and mineral owner are concerned). In *Steinkuehler v. Hawkins Oil and Gas, Inc.*, mineral owners granted a lease to an entity who in turn farmed out the interest to operator Hawkins Oil and Gas, Inc (“Hawkins”).<sup>23</sup> Hawkins timely commenced operations on the Steinkuehler No. 1-15 Well under the lease but encountered significant drilling problems in the well and was forced to plug and abandon the hole.<sup>24</sup> With dispatch, Hawkins then skidded the rig to continue drilling operations by drilling a new hole. Hawkins broke earth on the second hole after the date of expiration of the primary term of the oil and gas lease. Hawkins drilled and completed the well as a producer through the second hole (the Steinkuehler No. 1-15A Well). The lessors then informed Hawkins that the lessors planned to file suit to cancel the lease. In response, Hawkins filed a “curative” pooling at the Commission to protect Hawkins’ position in the event the lease was canceled in district court. Lessors made an election under the curative pooling order<sup>25</sup> whereby the lessors were entitled to receive a 1/4<sup>th</sup> total royalty.<sup>26</sup>

Concurrently, the lessors did file the threatened lease cancellation suit.<sup>27</sup> Lessors argued that the lease had terminated when Hawkins plugged and abandoned the Steinkuehler No. 1-15 Well after the exploration of the primary term of the lease. Hawkins argued that the operations were continuous, and the lease was perpetuated under the terms thereof. In

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22. OAC 165:5-15-3 (2017).

23. 1986 OK CIV APP 9, 728 P.2d 520, 524, *cert. denied* Nov. 12, 1986.

24. *Id.* at 521.

25. Commission Order No. 236757.

26. *Hawkins*, 728 P.2d at 521.

27. *Id.*

reaching its decision, the trial court analyzed whether the above-described drilling operations should be considered one continuous drilling operation (commenced prior to the end of the primary term of the lease) or two separate drilling operations (with the first operation having commenced and concluded with the plugging of the first hole, the second hole constituting a “new” and separate operation that was begun after the primary term of the lease). The trial court found in favor of the lessors and canceled the lease. In reaching this conclusion the trial court noted that Hawkins’ own actions suggested that the second hole was a separate and distinct, non-continuous drilling operation. The actions the court relied upon were that (i) Hawkins plugged the first hole and submitted paperwork to the Commission regarding such plugging (suggesting the operations were separate), and (ii) Hawkins filed a curative pooling action (suggesting Hawkins considered the lease to have terminated).<sup>28</sup> Hawkins appealed the ruling.

The appellate court overturned the trial court determination and remanded with instructions to enter judgment in favor of Hawkins, preserving the lease. Relevant here, the appellate court noted that Hawkins filed the curative pooling in response to the lessor’s threat to file the lease cancellation action.<sup>29</sup> The court noted that the curative pooling was not indicative of Hawkins’ belief regarding the status of the wells or wells, but was instead “an obvious safeguard procedure to protect [Applicant’s] interest in the well in the event the leases were cancelled.”<sup>30</sup> The court then noted that Hawkins’ curative pooling might indicate Hawkins’ lack of confidence in Hawkins’ current legal position vis-à-vis the lease cancellation suit, but “could not be indicative of Hawkins’ earlier intent when it skidded the rig a short distance and continued drilling through a new bore hole.”<sup>31</sup>

*Steinkuehler* is a tacit recognition by the Oklahoma Court of Civil Appeals that curative poolings are an appropriate function of the Commission. Moreover, Hawkins ultimately prevailed in the lease cancellation matter, which suggests that the filing of a curative pooling action was not a *per se* admission that the leases in question had terminated,

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28. *Id.* at 524–25.

29. *Id.* at 524.

30. *Id.*

31. *Id.* This finding was important to show Hawkins had not abandoned any operations under the lease.

but instead may constitute an “obvious safeguard.”<sup>32</sup> Although we should be cautious not to read too much into *Steinkuehler*, the case also suggests that under those facts, either the subject lease was still in effect or the pooling order would be effective.

Clearly, this case is helpful to operators seeking to pool parties for curative purposes, particularly in the face of a lease cancellation suit. However, the opinion would be strong authority had it been rendered by the Oklahoma Supreme Court. Further, the tacit recognitions within the opinion would be stronger if explicit. That said, this author believes these recognitions and concepts in *Steinkuehler* likely would apply to the top lessee as well as a mineral owner, particularly since top lessees commonly employ mineral owners in their lease cancellation suits. The following case discussion does review a pooling proceeding involving a top lessee and base lessee at the same time.

*4. The PITCO case – A pooling proceeding covering a top lessee and a base lessee at the same time.*

In *Harding & Shelton, Inc. v. Prospective Inv. and Trading Co., Ltd.* (“PITCO”),<sup>33</sup> the Oklahoma Court of Civil Appeals analyzed whether the Commission may enter a force pooling order where the top lessee filed the application and, if so, the order’s effectiveness on a base lessee. In that litigation, the “Base Lessee” obtained leases covering two mineral tracts in 1996.<sup>34</sup> Those tracts contained a producing well, which ceased to produce in 1997, casting doubt on the validity of the base leases. A different company became the “Operator” of the mineral tracts, and then a different “Top Lessee” acquired top leases from the mineral owners in March of 1999. The Base Lessee found itself pitted against the Operator and Top Lessee.

The mineral owners (with Operator’s backing) sued to terminate the base leases for lack of production.<sup>35</sup> While that lawsuit was pending, Top Lessee filed a pooling application with the Commission, with the proposed initial operations thereunder being a workover of the existing well. While both the first suit and the pooling proceeding were pending, Base Lessee filed another suit to force Top Lessee and Operator to offer Base Lessee an

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32. The designation of a respondent as “curative” in the pooling perhaps has no meaningful impact on the Commission’s jurisdiction but may help to preserve the operator’s legal position that an underlying lease has not terminated.

33. 2005 OK CIV APP 88, 123 P.3d 56.

34. *Id.* at 59.

35. *Id.* at 60.

interest in the top leases on the grounds they were renewals of the base leases.

The Commission entered a pooling order in February of 2001, covering the workover of the existing well, including a deepening and recompletion of the existing well. Base Lessee appeared before the Commission in such cause. Base Lessee filed a motion to reopen and “correct” the pooling order to allow for “deferred payment of cost for formations currently behind pipe in the...well.”<sup>36</sup> Base Lessee desired to participate in the recompletion aspect of the operations, but not in the deepening of the well to other formations. Base Lessee withdrew its request after entering into a letter agreement dated April 4, 2001, with Top Lessee and Operator. Under the letter agreement, Base Lessee would be allowed to defer prepayment of well costs under the pooling order until Operator and Top Lessee were ready to complete the well in the shallower zones. The letter agreement further stipulated that Operator and Top Lessee did not admit the validity of the base leases or that the Base Lessee owned any interest at all. Base Lessee elected to participate under the pooling order, as supplemented by the obligations of the letter agreement.<sup>37</sup>

The first suit resulted in a judgment declaring the base leases cancelled. On May 29, 2001, Base Lessee tendered its share of recompletion costs, attempting to condition that payment as follows:

As [Operator and Top Lessee] are also claiming the interest shown above and per the terms of the OCC order as amended by letter agreement dated April 4, 2001, we expect one of these companies to match these funds in the escrow account. Evidence supporting the deposit of like funds by [Operator and Top Lessee] should be included in the escrow account information provided to PITCO. Should the dispute regarding ownership in the Metzler be dismissed by action of the court or by PITCO the funds submitted herewith shall be returned to PITCO within forty-eight (48) hours of written notice....<sup>38</sup>

Base Lessee was attempting to hedge its bet after losing the lease cancellation suit, whereby if the Base Lessee decided to stop prosecuting the suit to force Top Lessee and Operator to give some of the interest in the top leases, then Base Lessee could move forward claiming no drilling rights

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36. *Id.*

37. *Id.*

38. *Id.*

(and therefore no obligation to pay well costs) and receive back its own prepayment of well costs. Top Lessee and Operator refused to accept Base Lessee's attempt to so condition its prepayment of well costs.<sup>39</sup>

In 2002, it became apparent to all parties that the workover attempt yielded disappointing results at a higher than estimated cost. Not surprisingly, the desires of the parties suddenly changed. Top Lessee and Operator capitulated to Base Lessee's demands in the second suit, offering interests in the top leases upon the payment by Base Lessee of excess costs and \$75.00 per acre. Base Lessee dismissed its own suit (the second suit seeking interest in the top leases) and demanded a return of the "conditional" prepayment.<sup>40</sup>

The Operator then filed a third lawsuit, seeking a judgment for the Base Lessee's share of the cost overruns and to foreclose on its statutory lien<sup>41</sup> upon Base Lessee's interest. Base Lessee filed counterclaims against Operator and Top Lessee for return of the prepayment of well costs.<sup>42</sup> The court found in favor of Operator and Top Lessee, finding that Base Lessee had elected to participate in the workover under the pooling order and therefore had obligated itself to certain costs. This was the appealed-from decision, which necessarily included a finding that Base Lessee had participated under the pooling order and therefore the Base Lessee would owe a participant's well costs.

On appeal to the Oklahoma Court of Civil Appeals, Base Lessee argued that there was no legal basis for the payment obligation recognized by the trial court, and that the Commission lacked jurisdiction over Base Lessee to compel the payment of workover costs because Base Lessee never held record title.<sup>43</sup> The court rejected Base Lessee's arguments. First, the court recognized that the Commission had subject matter jurisdiction to entertain Operator's and Top Lessee's force pooling application under § 87.1. Next, the court determined that the Commission had primary jurisdiction to determine whether an election is effective and noted that once the "option period" under a valid pooling order ends, the interests vest and can no longer be extinguished unless there is a vitiating infirmity in the order.<sup>44</sup>

The court then addressed Base Lessee's argument that the Commission did not have personal jurisdiction over Base Lessee because Base Lessee

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39. *Id.*

40. *Id.* at 61.

41. Okla. Stat Ann. tit. 42 § 2001 (West 2018).

42. *PITCO*, 123 P.3d at 61.

43. *Id.* at 61–62.

44. *Id.* at 62.

eventually was found to not be in title at the time of the pooling order, and therefore the Commission could not “compel” Base Lessee to do anything at all. Importantly, at the time of the pooling, **Base Lessee was claiming an interest** (much like a top lessee might in a similar circumstance) by defending against the lease cancellation suit and by filing another suit seeking an interest in the new top leases as renewals of the base leases. The court noted that the order did not “compel” any payment at all, but instead allowed owners of drilling rights to elect to participate by making a payment. Base Lessee had even appeared at the pooling hearing in protest and sought to modify the pooling order. The court found that Base Lessee chose to avail itself of the option to participate under the pooling order, based on its assertion of ownership.

Under these facts, the court found that the Base Lessee waived any objection to the Commission’s jurisdiction by voluntarily appearing and seeking affirmative relief, and then electing to participate. The court also found that even if the pooling order were defective for failure to address the uncertain nature of Base Lessee’s interest, Base Lessee had standing as “a person affected by” the order to appeal or seek a modification to clarify the ownership status. Base lessee failed to do so.<sup>45</sup> The challenge to personal jurisdiction failed, even though it was possible that Base Lessee owned no interest at the relevant time.<sup>46</sup>

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45. *Id.*

46. “Personal jurisdiction” may be a somewhat misleading phrase to use given the Commission’s unique jurisdiction over both the party and the ownership interest. A non-owner could theoretically appear before the Commission and voluntarily submit to jurisdiction, thereby establishing what is commonly understood to be “personal jurisdiction.” However, should that party not own any type of oil and gas interest in the relevant common source(s) of supply covered by the Commission matter, then there would not be any interest within the Commission’s jurisdiction to be covered or impacted by an order, rendering any established “personal jurisdiction” moot. This supports the notion that the Commission exercises quasi in rem jurisdiction, and not personal jurisdiction, in a force pooling. This concept is further supported by the fact that publication service performed on unknown parties, or other known parties who cannot be located, is sufficient for the Commission to enter an order affecting such a party’s property. *See also* *Harding & Shelton, Inc. v. Sundown Energy, Inc.*, 2006 OK CIV APP 12, 130 P.3d 776 (wherein the appellate court departed from the then-common understanding that the Commission’s jurisdiction in a pooling was primarily personal jurisdiction, and any party who was not personally made subject to a pooling by being properly named and served notice could not be subject to the pooling order to issue; instead, the court found that drilling rights that are made subject to a pooling order must be considered to remain subject to the pooling order, even if those rights transfer to another party after the entry of the order and the recipient was not covered by the

The court then addressed various equitable arguments. Relevant to this paper, the court outlined the elements of judicial estoppel:

This doctrine provides a party who knowingly assumed a particular position dealing with matters of fact is estopped from assuming an inconsistent position to the prejudice of the adverse party. This rule ordinarily applies to inconsistent positions assumed in the course of the same judicial proceeding or in subsequent proceedings where the parties and questions are identical. *Capshaw v. Gulf Ins. Co.*, 2005 OK 5, n. 28, 107 P.3d 595, 602.<sup>47</sup>

The court noted that a court's equitable jurisdiction does not require specific authority, with the purpose of equity to be to promote and achieve justice with some degree of flexibility.<sup>48</sup> Then, the opinion reads as follows:

At its most basic, “[e]quitable estoppel is employed to prevent one party from taking a legal position inconsistent with an earlier action that places the other party at a disadvantage.” *Merritt*, 2003 OK 68 at ¶ 15, 73 P.3d at 883. It “holds a person to a representation made, or a position assumed, where otherwise inequitable consequences would result to another, who has in good faith, relied upon that representation or position.” *Id.* (citing *Oxley v. Gen. Atl. Res., Inc.*, 1997 OK 46, ¶ 20, 936 P.2d 943, 947).

The court discussed, but did not dispositively rely upon, these concepts of equitable or judicial estoppel in reaching its decision in *PITCO* other than to say that equitable principles did not support Base Lessee under the facts to the point of overturning the appealed decision.

An interesting takeaway from *PITCO* is that Base Lessee was found ultimately to be subject to the pooling order even though the base lease had been canceled. Base Lessee probably did not own any working interest with which to participate in the well. If Base Lessee did not own any working interest, then how could the Commission exercise jurisdiction over Base Lessee within the pooling? The case does not address any *O'Neill* issues. The court relies upon concepts of personal jurisdiction and, evidently, estoppel to find Commission jurisdiction over Base Lessee. Perhaps Base

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order. “Quasi in rem,” rather than “personal,” better describes the Commission’s jurisdiction.).

47. *PITCO*, 123 P.3d at 64.

48. *Id.* (citing *Merritt v. Merritt*, 2003 OK 68, ¶ 13, 73 P.3d 878, 883).

Lessee would have succeeded in asserting the Commission never had statutory jurisdiction over Base Lessee as a non-owner, but that argument does not appear to have been asserted.

5. *Applying what we know: practical considerations in pooling top lessees.*

The overarching concern in naming a top lessee as a respondent in a force pooling is the questionable nature of its ownership and whether the Commission can establish jurisdiction over the party under the standard set in *O'Neill*. Because the ownership requirement under *O'Neill* is jurisdictional in nature, and because jurisdiction may be challenged at any time, the risk that the Commission did not establish jurisdiction over a party with questionable ownership will hang over the operator's head into the future. That said, *Steinkuehler* may have blessed the concept of pooling a party for curative purposes when that party threatened a law suit, even when the pooling applicant does not believe the party to own a vested interest. *PITCO* may show that a non-owner may be held subject to a pooling order, which is of course contrary to *O'Neill*.

It is not that the case law is confused, exactly, but that it is unconnected. The authors of one opinion may not contemplate the ramifications of their holding in one case. This is likely due to the appellate courts' attempt to limit decisions to as few issues as possible.

Whether a top lessee may be force pooled under the *O'Neill* standard is likely to be a fact-driven analysis. The practicing bar is left to its own devices in analyzing the Commission's authority to force pool curative parties under the *O'Neill* standard, or when it applies at all. The following hypothetical fact patterns may help illustrate.

*Presumption 1: The top lessee has taken a passive stance, merely holding its top lease without asserting vested ownership.*

Under these facts, the party owns no vested rights, only the legal possibility of acquiring the drilling rights. The party has not asserted current vested ownership as the lessor did in *Steinkuehler* and has not filed suit to cancel the base leases. Under *O'Neill*, the party is not an "owner" in fact, nor has claimed any ownership, and the Commission probably does not have the statutory jurisdiction to pool this party.

A difficult situation arises when the base leases are questionably effective due to middling production, but the top lessee does not force the issue. The operator may be concerned that the base leases could have terminated but may not yet see fit to admit the base leases have terminated and file a release of record. The operator may want to force pool the top lessee out of an abundance of caution. But under these facts, if the top

lessee protests the pooling and demands to be dismissed, the Commission probably ought to do so under *O'Neill*. If this occurs, the top lessee may be admitting the base leases are in effect, which is helpful to the operator.

If the party does not attempt to protest, or is not successful in a protest, then the Commission would enter an order ostensibly pooling the top lessee. Should the top lease never vest, then the party never owned any interest to be pooled anyway and the pooling order should be considered ineffective as to that party.<sup>49</sup> The operator loses nothing other than the time and expense of the pooling proceeding, although the top lessee may desire an order of the Commission affirmatively terminating the pooling order as to the top lessee so as to not cloud title.

If an order is entered covering the top lessee's interest, and later the top lease is adjudicated to have vested at a point **prior** to the entry of the order, then the operator has a strong argument that the Commission's order was effective on the top lessee's interest. Even though at the time of the entry of the order the top lessee did not appear to own the requisite interest and did not assert ownership, the subsequent adjudication of ownership creates a "new" fact that the top lessee did indeed own the requisite interest at the requisite time, even if the party appeared at the Commission to contest jurisdiction.

If an order is entered covering the top lessee's interest, and later the top lease is adjudicated to have vested at a point **after** the entry of the order, then the pooling order most likely would not be effective as to the top lessee. Under this scenario, the top lessee never asserted an interest nor actually owned an interest during any point of the pooling process. There is no strong argument that the top lessee should be subject to the pooling order.

*Presumption 2: The top lessee has taken a moderate stance, asserting ownership of vested rights through the top lease, but not yet taking a legal position before any tribunal.*

This analysis is similar to presumption 1, but with the helpful benefit of the top lessee actually representing ownership of drilling rights. That representation could amount to taking a legal position (discussed in Presumption 3, below). Presume that such representation, however, does not quite amount to a legal position before a court. The Commission should be much more comfortable entering a pooling order covering a top lessee as

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49. This could cause confusion in record title should the top lessee later acquire drilling rights in the unit. The top lessee would appear to be subject to a pooling order, although the pooling order probably was not effective as to the top lessee at the time of entry.

a “curative” party if the applicant can present evidence that the party represents ownership, particularly given the finding in *Steinkuehler* that a curative pooling in response to a threatened lease cancellation suit is an “obvious safeguard.”

Perhaps the top lessee would decide to appear at the Commission to attempt to evade the Commission’s jurisdiction because the top leases have not vested. The top lessee would have two choices: (1) represent to the Commission that the top lessee currently owns drilling rights (but is not in clear title) thereby probably admitting that the top lessee is a proper party to force pool, or (2) represent that the top lessee does not currently own any drilling rights and is not a proper party to force pool. Under choice (1), the operator and Commission should be able to rely on the party’s assertion of ownership as a submission to the Commission’s jurisdiction, resulting in a reliable pooling order covering the top lessee. This is a logical conclusion and follows the analyses in *Steinkuehler* and also *PITCO*, where the Base Lessee was determined to be subject to the order even though the base leases later were canceled by the district court. Under choice (2), perhaps the entry of a pooling order covering the top lessee would be inappropriate, but the operator walks away from the Commission with an admission on the record that the base leases are currently in effect: a win. This admission would be helpful in negotiations and also in district court should the top lessee later file suit to cancel the base leases.

*Presumption 3: The top lessee has taken an aggressive stance, asserting ownership of vested rights through the top lease and filing a suit to cancel the base leases.*

Under this presumption, the top lessee represents ownership of drilling rights and has taken a legal position in court that the top lessee is a current owner of drilling rights. The analysis above in Presumption 2 should be applicable here as well.

Further, the operator would have additional protection under the doctrine of judicial or equitable estoppel, described above in the review of *PITCO*, should the top lessee attempt any argument that the Commission cannot establish jurisdiction on the top lessee because the top leases have not yet vested. The Commission should find that the top lessee is estopped from asserting in district court that the top leases have vested, while at the same time asserting that the Commission does not have jurisdiction to force pool the top lessee because the top lessee is not in title to drilling rights. Further, under the same principle, the top lessee should be precluded from asserting at any point in the future, after the order is entered, that the Commission did not and could not establish jurisdiction over the top lessee when it will be

clear to all parties that the top lessee previously asserted a legal position that the base leases had terminated.<sup>50</sup> The Oil and Gas Appellate Referee of the Commission recently recommended that in the face of a lease cancellation suit, an operator should be allowed to pool the interests of “possible” owners (including a lessor).<sup>51</sup> No final determination in that matter has been rendered by the Commission.

**Regardless of any of the foregoing**, *PITCO* and other case law<sup>52</sup> suggest that if a party participates in the pooling process and takes a benefit under the pooling order, then that party will be held subject to the pooling order later should the party argue that the order is ineffective as to the party’s interest. This rule of law helps to foreclose the risk of failure of Commission jurisdiction over the top lessee. Either the top lessee will appear and challenge jurisdiction at the pooling hearing, so the operator knows early on what the risk may be, or the top lessee does not protest and takes a benefit of the order shortly after its entry, thereby committing itself to the pooling order at an early point in time and minimizing the risk of a successful challenge to the order.

*Presumption 4: The top lessee is the pooling applicant.*

In *PITCO*, the pooling action was filed by Top Lessee prior to any vesting of drilling rights. In theory and depending on the language within the top lease, all that Top Lessee had vested at the time of the pooling was the reversionary interest held by the mineral owner.<sup>53</sup> Under the scenarios involved here, our archetypical top lessee does not hold vested drilling rights. The question is begged: if only an owner of drilling rights is an appropriate party to join in a pooling so as to invoke the Commission’s jurisdiction, must the pooling applicant be an owner of vested drilling rights to invoke the Commission’s jurisdiction? The author contends that “yes” is the answer, under the relevant portion of the statute:

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50. *Morgan, Baldwin & Co. v. Kanola Oil & Ref. Co.*, 1924 OK 523, 102 Okla. 26, 226 P. 335, 337 (“It cannot, consistently claim to be the owner of property, or of a contract, the title to which it recognizes to be in another. With two inconsistent courses from which to select, it cannot elect to stand first upon one and then upon another. It could elect but once, and having made that election, the polls closed. It must not blow hot and cold. It cannot avoid the burdens and claim the benefits.”).

51. Report of the Oil and Gas Appellate Referee, Cause CD No. 201707810-T, filed September 7, 2018.

52. *Grand River Dam Authority v. Eaton*, 1990 OK 133, 803 P.2d 705, 708 (discussing *Tara Oil Co. v. Kennedy & Mitchell, Inc.*, 622 P.2d 1076 (Okla. 1981)) (“The real rule in *Tara* is that a party cannot at the same time accept the benefits of a judgment and attack it on appeal . . .”).

53. *See Voiles*, 1996 OK 13, 911 P.2d 1205, 1209.

When two or more separately owned tracts of land are embraced within an established spacing unit, or where there are undivided interests separately owned, or both such separately owned tracts and undivided interests embraced within such established spacing unit, **the owners thereof** may validly pool their interests and develop their lands as a unit. Where, however, **such owners** have not agreed to pool their interests and where one such separate owner has drilled or proposes to drill a well on the unit to the common source of supply, the Commission, to avoid the drilling of unnecessary wells, or to protect correlative rights, shall, upon a proper application therefor and a hearing thereon, require such owners to pool and develop their lands in the spacing unit as a unit.<sup>54</sup>

The statute contemplates that all of the parties to a pooling proceeding be “owners,” which includes all of applicant and the respondents. The strict interpretation is that the pooling applicant must be an “owner.” An “owner” must be a party who owns drilling rights. If a top lessee does not own vested drilling rights, then perhaps that party cannot invoke the Commission’s jurisdiction by filing a pooling application.

In *PITCO*, Top Lessee filed the pooling application. The court did not address whether Top Lessee’s ownership was sufficient to invoke the Commission’s jurisdiction under § 87.1, apparently presuming that Top Lessee’s application was appropriate and effective. Perhaps the court did not address the issue since the base leases, in that case, were canceled eventually, placing Top Lessee in vested title presumably at the time of filing of the application. Perhaps the court in *PITCO* did not address whether Top Lessee’s ownership was sufficient to invoke the Commission’s jurisdiction simply because no party raised that argument in earlier proceedings. Nevertheless, there is a lingering, minor suggestion under *PITCO* that a top lessee owns a sufficient interest (whatever that may be) to invoke the Commission’s jurisdiction in a pooling proceeding.

To argue the other side, an unvested top lessee likely is able to represent only “color of title.”<sup>55</sup> The Oklahoma Court of Civil Appeals has previously determined that “color of title” in an applicant is insufficient to

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54. OKLA. STAT. ANN. tit. 52 § 87.1(e) (emphasis added) (West 2018).

55. If the top lessee could show more than “color of title,” then there probably is not any ambiguity as to the top lessee’s ownership, and there is no question to be answered about who should be pooling whom.

invoke the Commission's jurisdiction. In *Samson Resources Co. v. Okla. Corp. Comm'n*, the court found as follows:

52 O.S.1991, § 87.1 requires the applicant to "own" an interest in the minerals or to have a right to drill. This section of law does not use the phrase "color of title". The phrase "color of title" has been defined by the Oklahoma Supreme Court as follows:

"Any instrument having a grantor and grantee, and containing a description of the lands intended to be conveyed, and apt words for their conveyance, gives color of title to the lands described. Such an instrument purports to be a conveyance of title; and, because it does not, for some reason, have the effect, it passes only color, or the semblance, of title. It makes no difference whether the instrument fails to pass an absolute title because the grantor had none to convey."

*Adams v. Parks*, 435 P.2d 122, 125 (Okla.1967). Blacks Law Dictionary, Sixth Edition, further provides color of title is "that which is a semblance or appearance of title, but is not title in fact or in law." **If an applicant need only show "color of title" under § 87.1, then that would mean an applicant would not have to own any minerals or have a right to drill but just present evidence that they might. In light of the general purposes of the statute, we cannot conclude the Legislature intended such a result.** This is not to say, however, that an Applicant before the Commission could not invoke the jurisdiction of that body based on "color of title." The determination of ownership of minerals or the right to drill is a finding of fact to be made by the Commission, whose findings must be supported by substantial evidence.<sup>56</sup>

The holding in *Samson* should apply to any type of application filed under § 87.1, including poolings. When upholding the Commission's order that dismissed four different proceedings in *Samson*, the court did not

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56. *Samson Res. Co. v. Okla. Corp. Comm'n*, 1993 OK CIV APP 67, 859 P.2d 1118, 1121 (emphasis added).

distinguish among different applications seeking various types of relief.<sup>57</sup> Very likely, a top lessee does not have the appropriate ownership to invoke the Commission's jurisdiction in a pooling but the adverse party ought to appear to contest jurisdiction before the order is entered, and let the Commission make an affirmative determination on the issue.

While color of title is insufficient to invoke the Commission's jurisdiction, the *Samson* court notes that "The determination of ownership of minerals or the right to drill is a finding of fact to be made by the Commission, whose findings must be supported by substantial evidence."<sup>58</sup> In other words, the court believes the Commission should determine whether a party is a proper owner by reviewing evidence. This sounds a bit like "trying title," which is not something the Commission is willing to do, notwithstanding *Samson*. The Commission will not review whether a top lease has vested based on cessation of production. That is not a controversy that the Commission has statutory authority to adjudicate, even if the Commission has the authority to assess its own jurisdiction by reviewing the ownership of the parties in a proceeding.

#### *Conclusion*

The apparent benefits of pooling of top lessees as curative parties should outweigh the risks. Depending on the facts, the potential outcomes when attempting to force pool a top lessee are:

- Be denied outright by the Commission (and know where you stand, early in the process).
- The top lessee makes no appearance, but the pooling order later is found to be ineffective to the interest (same position you would be in if you made no attempt to pool, just bear in mind that there is risk).
- The top lessee makes no appearance but later takes a benefit under the pooling order, becoming subject to the order without regard to whether the top leases vested.
- The top lessee makes no appearance, and the pooling order later is found to be effective to the interest.

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57. The appealed-from order is Order No. 362056, granting motions to dismiss Cause CD Nos. 156357-T (increased density), 156358-T (increased allowable), 156374-T (clarification of pooling Order no. 231222) and 156454-T (well location exception).

58. *Samson*, 859 P.2d at 1121.

- The top lessee argues that he owns no interest (thus confirming the effectiveness of the base lessee, a good outcome), but be denied by the Commission.
- The top lessee argues that he owns the interest (thus establishing a legal position and committing himself to the Commission's jurisdiction in the pooling), and the Commission will very likely grant the pooling that should be upheld.

Pooling top lessee as curative parties makes sense. Even if some twist of facts or law results in a pooling order being ineffective as to a party, that is still the same position that operator would be in had there been no attempt made at all. That said, take precautions to protect your legal position at all times:

- Be explicit in any proposal letter or negotiations that the top leases have not vested, but the operator is moving forward in a "curative" sense.
- Be very explicit in the pooling application that the parties are curative in nature.
- In order to protect legal position, isolate top lessees in separate curative pooling. Do not commingle "standard" pooling respondents with top lessees.
- Be explicit in the record of the pooling proceeding about the nature of the respondent's interest.
- Be explicit in the pooling order concerning which parties are curative in nature.
- Be consistent throughout the various legal proceedings to avoid judicial estoppel.
- Escrow any monies becoming due, and have curative participant escrow well costs, pending the outcome of any district court action.

With these considerations in mind and remembering that the only certain thing in the oil patch is uncertainty, the operator should be able to have top lessees force pooled while mitigating risk as much as reasonably possible.