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# Oil and Gas: Top Leasing After *Voiles v. Santa Fe Minerals* — Unethical Claim-jumping or Prudent Business Practice?\*

## I. Introduction

A top lease is a "subsequent oil and gas lease which covers one or more mineral interests that are subject to a valid, subsisting prior lease."<sup>1</sup> Generally, parties word a top lease so that it becomes effective upon the expiration or termination of the prior lease, known as the base or bottom lease.<sup>2</sup> Top leasing has existed in the oil and gas industry for several years, but the propriety and legality of the practice have long been matters of debate, especially in Oklahoma.<sup>3</sup> Although the industry and the courts at one time viewed top leasing as immoral and illegal, Oklahoma courts and the Oklahoma oil and gas industry now view top leasing as a useful business practice.<sup>4</sup> *Voiles v. Santa Fe Minerals*,<sup>5</sup> in particular, focused on the economic realities of business competition rather than on the ethics of top leasing. As a result, the court implicitly accepted top leasing as a favorable method of insuring that mineral lessees continue oil and gas production and pay competitive prices to mineral lessors.<sup>6</sup> By recognizing top leasing as an established practice in Oklahoma,<sup>7</sup> *Voiles* has resolved the confusion found in earlier Oklahoma case law dealing with top leases.

This note will describe the different types of top leases, chronicle how the status of top leasing in Oklahoma and in other oil and gas jurisdictions has changed over the decades, and discuss the various legal problems associated with executing a top lease. Next, it will explain what steps top lessees should take to ensure the safety of their investments and how top lessees may protect themselves from liability to bottom lessees. Finally, this note will demonstrate how top leasing serves the interests of both mineral lessors and mineral lessees, thus providing Oklahoma with economic benefits.

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\* Winning note, Oklahoma Bar Association Mineral Law Section Writing Award for 1998.

1. Michael L. Brown, *Effect of Top Leases: Obstruction of Title and Related Considerations*, 30 BAYLOR L. REV. 213, 213 (1978).

2. See Michael E. Jackson & Margaret L. Weissbrod, *Top Leasing in the Appalachian Basin*, 6 E. MIN. L. FOUND. 12-1, 12-5 (1985).

3. See Max H. Ernest, III, *Top Leasing — Legality v. Morality*, 26 ROCKY MTN. MIN. L. INST. 957, 958-59 (1980).

4. See *Voiles v. Santa Fe Minerals*, 911 P.2d 1205, 1209 (Okla. 1996).

5. 911 P.2d 1205 (Okla. 1996).

6. See *id.* at 1212.

7. See *id.* at 1209.

## II. Types of Top Leases

There are two basic types of top leases: the common-lessee (or two party) top lease and the divergent-lessee (or three party) top lease.<sup>8</sup> In a common-lessee top lease, the same lessee holds both the top and the bottom lease.<sup>9</sup> The lessee secures a second (top) lease, which covers part or all of the same mineral interest, while the original (bottom) lease is still effective, typically prior to the termination or expiration of the bottom lease.<sup>10</sup> For example: *R* (the mineral owner and lessor) leases his mineral interests to *E* (the lessee) for a primary term of five years beginning June 1, 1994. On April 1, 1999 (two months before the end of the primary term), *R* executes a new lease (the top lease) with *E*, covering the same mineral interest as in the original lease (the bottom lease).<sup>11</sup>

The second and more common type of top lease is the divergent-lessee top lease.<sup>12</sup> The divergent-lessee top lease involves the original lessor (or the lessor's successor in interest) and a new lessee.<sup>13</sup> The original lessee is not a party to the top lease. For example: *R* (the mineral owner and lessor) leases his mineral interests to *B* (the bottom lessee) for a primary term of five years beginning June 1, 1994. On April 1, 1999 (two months before the end of the primary term), *R* executes a lease (the top lease) with *T* (the top lessee), a stranger to the first lease.<sup>14</sup>

The divergent-lessee top lease has produced the most amount of litigation.<sup>15</sup> Suits involve conflicts such as: (1) who owns the leasehold;<sup>16</sup> (2) whether the lessor has repudiated the bottom lease by executing a top lease;<sup>17</sup> (3) whether the

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8. See Brown, *supra* note 1, at 213-14; see also Ernest, *supra* note 3, at 958; Jackson & Weissbrod, *supra* note 2, at 12-5; J. Hovey Kemp, *Top Leasing for Oil and Gas: The Legal Perspective*, 59 DENV. L.J. 641, 642 (1982); J. Clayton Johnson, *The Top Lease — No Longer a Stranger in the Lease Block*, 34 INST. ON OIL & GAS L. & TAX'N 201, 203 (1983).

9. See Brown, *supra* note 1, at 214; Ernest, *supra* note 3, at 958; Jackson & Weissbrod, *supra* note 2, at 12-5.

10. See Brown, *supra* note 1, at 214. Top leasing by the same lessee may appear to be a "substituted contract" or "novation." If viewed as a substituted contract or novation, the top lease would supersede the bottom lease. See Johnson, *supra* note 8, at 210. Determining whether the top lease is indeed a novation of the prior lease often involves analyzing the language of the new lease. If the new lease is silent on the existence of the prior lease, courts will presume that the parties intended to supersede the prior lease with the new lease. See *id.* at 211. If a top lease includes some sort of subordinating language, such as the word "subject to," then it is clear that the top lease will take effect only after the bottom lease has expired or terminated, and thus would not be considered a novation. See *infra* text accompanying notes 154-60.

11. For similar examples, see Brown, *supra* note 1, at 213; Ernest, *supra* note 3, at 958; Jackson & Weissbrod, *supra* note 2, at 12-5.

12. See Jackson & Weissbrod, *supra* note 2, at 12-5.

13. See *id.*

14. For similar examples, see Brown, *supra* note 1, at 213; Ernest, *supra* note 3, at 958; Jackson & Weissbrod, *supra* note 2, at 12-5.

15. See Jackson & Weissbrod, *supra* note 2, at 12-5.

16. See *id.*; see also Kemp, *supra* note 8, at 642-43.

17. See Brown, *supra* note 1, at 218 n.37 and accompanying text.

top lessee has slandered the bottom lessee's title by taking a top lease;<sup>18</sup> (4) whether a top lessee should be liable for champerty and maintenance if he encourages the lessor to bring a lease cancellation suit against the bottom lessee;<sup>19</sup> (5) whether a top lease violates the rule against perpetuities;<sup>20</sup> and (6) whether the top lessee should be liable for tortious interference with contract for taking a top lease.<sup>21</sup> *Voiles v. Santa Fe Minerals*<sup>22</sup> addresses many of these issues, helps to solidify the validity of top leases, and erases any residual concerns of the effect and status of top leasing.

### III. Law Prior to *Voiles v. Santa Fe Minerals*

To appreciate fully the *Voiles* decision and how it lays to rest any residual concerns about the illegality and impropriety of top leasing, a discussion of early case law on top leasing is required. Indeed, Oklahoma cases varied in their results and reasoning to such an extent that the effect of top leasing remained debatable for several years.

#### A. Cases Upholding the Validity of a Top Lease

In 1923, the Oklahoma Supreme Court held in *Rorex v. Karcher*<sup>23</sup> that a top lease is valid, provided that top lessees take their top leases subject to the rights of bottom lessees.<sup>24</sup> The *Rorex* court reached this conclusion by reasoning that, as title owners of the property in fee simple absolute, landowners may carve from the fee as many estates as they desire.<sup>25</sup> Executing a second oil and gas lease during the existence of the first lease falls well within the landowners' rights and prerogatives.<sup>26</sup> However, if they have already executed a top lease on the property, landowners are not free to extend the term of the bottom lease in derogation of the top lessee's rights.<sup>27</sup> Such an extension, the court concluded, would damage the top lessee's rights under his top lease.<sup>28</sup>

Three years later, the Oklahoma Supreme Court decided a similar case, *Gypsy Oil Co. v. Marsh*.<sup>29</sup> In *Gypsy*, the principal issue was whether the bottom lease had expired at the end of its primary term.<sup>30</sup> The top lessee sued the bottom lessee,

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18. See Jackson & Weissbrod, *supra* note 2, at 12-5; Kemp, *supra* note 8, at 642-43; see also *infra* notes 84-92, 134-37 and accompanying text.

19. See, e.g., Mitchell v. Amerada Hess Corp., 638 P.2d 441 (Okla. 1981); Voiles v. Santa Fe Minerals, 911 P.2d 1205 (Okla. 1996).

20. See, e.g., Stoltz, Wagner & Brown v. Duncan, 417 F. Supp. 552 (W.D. Okla. 1976).

21. See, e.g., James Energy Co. v. HCG Energy Corp., 847 P.2d 333 (Okla. 1992); Voiles v. Santa Fe Minerals, 911 P.2d 1205 (Okla. 1996).

22. 911 P.2d 1205 (Okla. 1996).

23. 224 P. 696 (Okla. 1923).

24. See *id.* at 697.

25. See *id.*

26. See *id.*

27. See *id.* at 697-98.

28. See *id.*

29. 248 P. 329 (Okla. 1926).

30. See *id.* at 331.

seeking the cancellation of the bottom lease and thus quieting title in the top lessee.<sup>31</sup> The *Gypsy* court rejected the bottom lessee's claim that the existence of a top lease constituted a defense to the suit.<sup>32</sup> Instead, it affirmed the trial court's decision to cancel the bottom lease because the bottom lessee failed to produce oil in paying quantities.<sup>33</sup>

*Jennings v. Elliot*<sup>34</sup> is another case that appears to uphold the validity of top leases. The Oklahoma Supreme Court found that landowners have a right to execute a top lease.<sup>35</sup> Executing a top lease, the court concluded, would "in no way interfere" with defendants' rights under the bottom lease.<sup>36</sup>

Four decades after it decided *Jennings*, the Oklahoma Supreme Court, in *Mitchell v. Amerada Hess Corp.*,<sup>37</sup> confronted the issue of whether a top lessee who aids a lessor in suing to cancel a bottom lease is engaged in champerty and maintenance.<sup>38</sup> The facts of *Mitchell* are very similar to the facts in *Voiles v. Santa Fe Minerals, Inc.*<sup>39</sup> In *Mitchell*, the top lessees sought a contract from the mineral owners to become the owners' agent for the purposes of obtaining a cancellation and release of the bottom leases.<sup>40</sup> The *Mitchell* court noted that "any interest whatever in the subject matter of the suit, [w]hether great or small, vested or contingent, certain or uncertain," will be sufficient to defeat a charge of champerty.<sup>41</sup> Possession of some top leases respecting the land involved in the suit was sufficient to exempt the top lessees from a charge of champerty and maintenance.<sup>42</sup> Thus, the court affirmed the top leases' validity.<sup>43</sup>

Nebraska case law is in accord with these early Oklahoma cases. In *Willan v. Farrar*,<sup>44</sup> the Nebraska Supreme Court cited approvingly to *Rorex* and found that lessors have no power to waive a defective rental payment by a bottom lessee as

31. *See id.*

32. *See id.* at 334. Furthermore, the *Gypsy* court questioned the ethics of the top lease. "[The top lessee] took his lease at a time when the oil company's lease was in force . . . and at a time when he knew that it was claiming an estate in the premises because of [an oil] discovery, and [knew] that he was purchasing litigation." *Id.* Because the bottom lessee drilled a shallow well in bad faith in order to gain more time to drill another well in deeper sand, the court refused to "plac[e] its protecting arm around either party." *Id.*

33. *See id.*

34. 97 P.2d 67 (Okla. 1939).

35. *See id.* at 70-71.

36. *See id.* at 71.

37. 638 P.2d 441 (Okla. 1981).

38. *Worrel v. Roxana Petroleum Corp.*, 291 P. 47, 48-49 (Okla. 1930) defined champerty and maintenance as "officious intermeddling in a suit which in no way belongs to one, by maintaining or assisting either party with money or otherwise to prosecute or defend it."

39. 911 P.2d 1205 (Okla. 1996).

40. *See Mitchell*, 638 P.2d at 442.

41. *Id.* at 444 (quoting *Worrel v. Roxanna Petroleum Corp.*, 291 P. 47, 48-49 (Okla. 1930)).

42. *See id.* at 445.

43. *See id.* at 446.

44. 124 N.W.2d 699 (Neb. 1963).

against a top lessee.<sup>45</sup> Once lessors issue the top leases to a top lessee, lessors owe an implied duty not to render the top leases ineffective.<sup>46</sup>

### *B. Cases Rejecting the Validity of a Top Lease*

In contrast to the above-cited cases is *Simons v. McDaniel*,<sup>47</sup> a 1932 Oklahoma Supreme Court decision wherein the court held that acts of lessors in executing and delivering a top lease constitute an outright declaration that a bottom lease is terminated.<sup>48</sup> The court further held that executing and delivering a top lease obstructs the exercise of a bottom lessee's rights under the terms of the bottom lease, thus clouding the bottom lessee's title.<sup>49</sup>

Oklahoma is not the only jurisdiction to hold that the mere existence of a top lease constitutes a cloud on the bottom lessee's title. For example, Kansas case law is consistent with *Simons*. In *Robinson v. Continental Oil Co.*,<sup>50</sup> the United States District Court for the District of Kansas held that the mere existence of a top lease constitutes an attack upon a bottom lessee's title.<sup>51</sup> The court concluded that while a bottom lessee's title is under attack, the bottom lessee has no obligation to carry out any express or implied conditions of the lease.<sup>52</sup>

### *C. Unsettled Status of Top Leasing*

Although the Oklahoma Supreme Court decided *Simons* subsequent to *Rorex* and *Gypsy*, it failed to cite to either of those cases.<sup>53</sup> Moreover, *Jennings*, decided six years after *Simons*, made no mention of *Simons* or *Rorex*, despite the inconsistency of the cases.<sup>54</sup> Furthering the confusion, approximately thirty years after *Rorex* and *Simons*, the United States Court of Appeals for the Tenth Circuit decided based on Oklahoma law<sup>55</sup> that "topleasing has the same invidious characteristics as claim-jumping."<sup>56</sup>

Given the varying results and conclusions reached in these cases, top lessees receive little comfort. Because parties rely on court decisions when deciding whether to enter into an oil and gas leasing agreement, the oil and gas industry

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45. *See id.* at 703-04.

46. *See id.*

47. 7 P.2d 419 (Okla. 1932).

48. *See id.* at 420.

49. *See id.* A cloud on title is "an outstanding claim or encumbrance which, if valid, would affect or impair the title of the owner of a particular estate." BLACK'S LAW DICTIONARY 255 (6th ed. 1991).

50. 255 F. Supp. 61 (D. Kan. 1966).

51. *See id.* at 63. The opinion does not indicate whether the top lease contained any "subject to" language. *See infra* notes 154-56 concerning the use of "subject to" language.

52. *See Robinson*, 225 F. Supp. at 63.

53. *Simons v. McDaniel*, 7 P.2d 419 (Okla. 1932).

54. *Jennings v. Elliott*, 97 P.2d 67 (Okla. 1939).

55. *See Frankfort Oil Co. v. Snakard*, 279 F.2d 436 (10th Cir. 1960).

56. *Id.* at 445 n.23. Snakard contended that Frankfort purposely failed to meet its drilling obligations in order to top lease Snakard's leases after Snakard's interests were extinguished. *See id.* at 444-45. Holding that Frankfort had the right but not the obligation to drill, the court rejected Snakard's contention and found that Frankfort did not acquire any interest in Snakard's expired leases. *See id.* at 440, 445.

would benefit from consistent case law on top leasing. In *Voiles v. Santa Fe Minerals*,<sup>57</sup> Oklahoma has finally provided sound precedent on which parties may rely. *Voiles* confirms that top leasing is a valid oil and gas industry practice.

#### IV. *Voiles v. Santa Fe Minerals*

##### A. Facts

Plaintiffs mineral lessors [collectively "Voiles"] executed several oil and gas leases (the bottom leases) to Defendant Santa Fe Minerals (the bottom lessee).<sup>58</sup> Plaintiff Oklahoma Hugoton Corporation ["Hugoton"] paid Voiles for top leases of the area already leased by Santa Fe Minerals.<sup>59</sup> In the process of obtaining the top leases, Hugoton entered into a separate agreement with Voiles.<sup>60</sup> This separate agreement authorized Hugoton to bring suit to judicially terminate Santa Fe Minerals' bottom leases.<sup>61</sup>

##### B. Procedural History

Subsequently, Voiles and Hugoton brought suit to quiet title to their mineral interests and to cancel the bottom leases owned by Santa Fe Minerals.<sup>62</sup> The essence of the suit was that Santa Fe Minerals violated the "cessation of production" clause<sup>63</sup> of their bottom leases by failing to have a well capable of producing in paying quantities for more than sixty days without commencing drilling operations.<sup>64</sup> Santa Fe Minerals counter-claimed to quiet title to its bottom leases.<sup>65</sup> Santa Fe Minerals also filed a third-party claim against Hugoton, alleging tortious interference with contract,<sup>66</sup> slander of title,<sup>67</sup> and champerty and maintenance.<sup>68</sup>

The trial court rejected Voiles' and Hugoton's argument that the cessation of production clause terminated the bottom leases.<sup>69</sup> It found Santa Fe Minerals'

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57. 911 P.2d 1205 (Okla. 1996).

58. *See id.* at 1207

59. *See id.*

60. *See id.* at 1207-08.

61. *See id.*

62. *See id.* at 1208.

63. This clause allows a lessee to maintain a lease that has ceased to produce, usually by requiring the lessee to commence drilling operations on a new well. *See Pack v. Santa Fe Minerals*, 869 P.2d 323, 327 (Okla. 1994); *see also infra* notes 75-83, 120-32 and accompanying text.

64. *See Voiles*, 911 P.2d at 1208.

65. *See id.*

66. *See infra* notes 98-113, 138-43 and accompanying text.

67. *See infra* notes 84-92, 134-37 and accompanying text.

68. *See supra* notes 37-43 and accompanying text; *see infra* notes 114-18, 144-53 and accompanying text.

69. *See Voiles*, 911 P.2d at 1208.

bottom leases to be the "presently existing" leases.<sup>70</sup> The trial court also canceled and set aside the top leases.<sup>71</sup>

Concerning Santa Fe Minerals' claims against Hugoton for slander of title and for champerty and maintenance, the court rendered judgment in favor of Hugoton.<sup>72</sup> However, Santa Fe Minerals' claim for tortious interference with contract was successful.<sup>73</sup> All parties' appeals were consolidated.<sup>74</sup>

### C. Decision

#### 1. Cessation of Production Clause

The first issue the Oklahoma Supreme Court decided concerned the cessation of production clause. The bottom leases were executed between 1937 and 1950.<sup>75</sup> Thus, by the time Voiles and Hugoton brought the lease cancellation suit, the ten year primary term of each lease had expired, and only production of the minerals could keep the leases from being terminated.<sup>76</sup> The bottom leases' habendum clause provided for a primary term of ten years and "as long thereafter as oil, gas, casinghead gas or any of them is produced."<sup>77</sup> Voiles and Hugoton argued that the sixty-day cessation of production clause controlled the habendum clause.<sup>78</sup> Therefore, because Santa Fe Minerals had failed to produce for more than sixty days without commencing drilling operations, Plaintiffs claimed that the bottom leases should be canceled.<sup>79</sup>

The Oklahoma Supreme Court, relying primarily on *Pack v. Santa Fe Minerals*,<sup>80</sup> held that a lease in its secondary term will not terminate under the terms of the habendum clause when a well is at all times *capable* of producing in paying quantities.<sup>81</sup> Only if a lessee fails to comply with the implied covenant to market may the lease be canceled.<sup>82</sup> Despite Plaintiffs' request to do so, the court refused to overrule *Pack*.<sup>83</sup>

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70. *See id.*

71. *See id.*

72. *See id.*

73. *See id.*

74. *See id.*

75. *See id.* at 1207.

76. *See id.*

77. *Id.* at 1208.

78. The habendum clause, also known as the term clause, sets the lease duration and usually consists of two sub-parts: the primary term and the secondary term. The primary term is a fixed term of years during which the lessee has the right, without the obligation, to explore for oil and gas or to drill for oil and gas on the premises. The secondary term starts after the primary term when production is being obtained. *See* EUGENE O. KUNTZ ET AL., *CASES AND MATERIALS ON OIL AND GAS LAW* 159 (2d ed. 1993).

79. *See Voiles*, 911 P.2d at 1208.

80. 869 P.2d 323 (Okla. 1994).

81. *See Voiles*, 911 P.2d at 1208.

82. *See id.*

83. *See id.* at 1208-09.



## 2. Slander of Title

The Oklahoma Supreme Court also considered the trial court's denial of Santa Fe Minerals' slander of title claim.<sup>84</sup> Hugoton defended by arguing that, if the trial court found the bottom leases to be valid, then the top leases could simply be disregarded.<sup>85</sup> Hugoton also argued that it had brought suit in good faith to remove a cloud on Voiles' mineral interest, that is, the allegedly expired leases belonging to Santa Fe Minerals.<sup>86</sup> Because malice is an essential element of a slander of title action,<sup>87</sup> the Oklahoma Supreme Court had to decide whether Hugoton acted in good faith or bad faith when it sued to cancel Santa Fe Minerals' bottom leases. A showing of good faith indicates a lack of malice.<sup>88</sup>

Hugoton argued that it showed good faith in bringing the suit only after a trial court judgment against Santa Fe Minerals in a similar suit.<sup>89</sup> Hugoton also argued that it had a good faith belief that Santa Fe Minerals' bottom leases constituted a cloud on Voiles' mineral interests.<sup>90</sup> These two arguments combined to form the impression that Voiles had a colorable claim against Santa Fe Minerals.<sup>91</sup>

The Oklahoma Supreme Court affirmed the trial court's judgment denying Santa Fe Minerals' slander of title claims against Hugoton.<sup>92</sup> The court reasoned that Hugoton had not acted in bad faith or without probable cause when it sued to cancel Santa Fe Minerals' bottom leases because "a party is entitled to litigate a matter of first impression."<sup>93</sup> In *Pack v. Santa Fe Minerals*,<sup>94</sup> the Oklahoma Supreme Court granted certiorari to consider the first impression question of "whether a lease, held by a gas well which is capable of producing in paying quantities but is shut-in for a period in excess of sixty (60) days but less than one year due to a marketing decision made by the producer, expires of its own terms under the 'cessation of production' clause unless shut-in royalty payments are made."<sup>95</sup> This question of first impression was very similar to the one in *Voiles*,<sup>96</sup> but *Pack* had not been

84. *See id.* at 1209.

85. *See id.*

86. *See id.*

87. *See* Denis Binder, *Slander of Title and Assorted Slings and Arrows of the Property Bar*, 13 E. MIN. L. FOUND. § 13.02 [5][b] (1992).

88. "Considered together, the Oklahoma cases appear to give the term 'malice' this meaning: that the defendant acted deliberately in asserting a claim without reasonable grounds for believing in its validity." Eugene O. Kuntz, *Discussion Notes*, 12 OIL & GAS REP. 912-13 (1994).

89. *See Voiles*, 911 P.2d at 1209.

90. *See id.*

91. *See id.* at 1210.

92. *See id.*

93. *Id.* (quoting *Dotson v. Rainbolt*, 894 P.2d 1109, 1115 (Okla. 1995)).

94. 869 P.2d 323 (Okla. 1994).

95. *Id.* at 325.

96. The *Voiles* court stated:

The primary issue in this appeal is the application of the sixty-day cessation of production clause, and whether it controls the habendum clause in the lease . . . . The cessation of production clause in the base lease provided for cessation of the lease after the expiration of the primary term if production . . . failed, unless the lessee resumed operations for a

decided until after Hugoton and Voiles had brought their appeal.<sup>97</sup> Thus, Voiles' and Hugoton's suit still involved a question of first impression.

### 3. *Tortious Interference with Contract*

A third issue which confronted the *Voiles* court was tortious interference with contract.<sup>98</sup> This tort arises when one who is not a party to a contract interferes with that contract by encouraging one of the contracting parties to breach its terms.<sup>99</sup> In a top leasing situation, a bottom lessee might assert this tort when the top lessee encourages the lessor to seek cancellation of the bottom lease.<sup>100</sup>

At trial, the judge found that Hugoton intentionally interfered with the leases between Voiles and Santa Fe Minerals.<sup>101</sup> However, the trial judge also found that Hugoton performed an important service for Voiles by helping Voiles to revisit their contractual relationship with Santa Fe Minerals.<sup>102</sup> Thus, only nominal damages were awarded.<sup>103</sup>

The Oklahoma Supreme Court reversed the judgment, finding that Hugoton had not intentionally interfered with Santa Fe Minerals' contracts and business relations.<sup>104</sup> The court noted that those who are not parties to a contract (or lease) can be held liable for tortious interference.<sup>105</sup> If Hugoton was acting as Voiles' agent when it sued Santa Fe Minerals, then Hugoton would not be liable for wrongfully interfering with the bottom lease between Voiles and Santa Fe Minerals.<sup>106</sup>

Pointing to trial testimony of two mineral owners, Santa Fe Minerals, on appeal, claimed that Hugoton filed suit without the express authorization of the owners.<sup>107</sup> However, the Oklahoma Supreme Court found that this testimony was not sufficient to affect Hugoton's status as Voiles' agent.<sup>108</sup> The court examined in detail a letter which appointed Hugoton as Voiles' special agent having "full and complete power

well within sixty days of the cessation . . . This precise issue was resolved in *Pack v. Santa Fe Minerals*.

*Voiles*, 911 P.2d at 1208 (citation omitted).

97. *See id.* at 1208-09.

98. The elements of tortious interference with contract (also known as malicious interference with contract) are: (1) that [the plaintiff] had a business or contractual relationship that was interfered with; (2) that the interference was malicious and wrongful, and that such interference was neither justified, privileged, nor excusable; and (3) that damage was proximately sustained as a result of the complained of interference. *James Energy Corp. v. HCG Energy Corp.*, 847 P.2d 333, 340 (Okla. 1992) (citing *Mac Adjustment, Inc. v. Property Loss Research*, 595 P.2d 427, 428 (Okla. 1979)).

99. *See Voiles*, 911 P.2d at 1211.

100. *See id.* at 1209.

101. *See id.* at 1210.

102. *See id.* at 1211.

103. *See id.* at 1210.

104. *See id.*

105. *See id.* at 1211.

106. *See id.*

107. *See id.* at 1210.

108. *See id.*

to take all necessary steps to obtain a release and judicial termination of the [bottom leases]."<sup>109</sup> Each of the mineral owners received and signed the letter.<sup>110</sup>

This fact heavily influenced the supreme court to conclude that Hugoton acted as Voiles' agent.<sup>111</sup> However, there was plenty of testimony demonstrating that the mineral owners either ignored the agency provisions in the letter or did not understand that a suit would be filed on their behalf.<sup>112</sup> Furthermore, some mineral owners testified that they would not have filed suit if Hugoton had not approached them with an offer to take a top lease and to pay their litigation costs for suing to cancel the bottom leases.<sup>113</sup> This latter testimony is important for resolving the next issue presented to the court, champerty.

#### 4. Champerty and Maintenance

The final issue the *Voiles* court analyzed involved the old legal doctrines of champerty and maintenance.<sup>114</sup> The court framed the issue succinctly: "Is it champerty for the mineral lessee to assist the lessor with a quiet title proceeding?"<sup>115</sup> Citing *Mitchell v. Amerada Hess Corp.*,<sup>116</sup> the court answered in the negative.<sup>117</sup> Because top leases are "characteristic of the industry" and because Voiles lacked funds to maintain litigation against Santa Fe Minerals, the court reasoned that advancing funds to Voiles did not violate any principle of law or public policy.<sup>118</sup>

### V. Case Analysis

*Voiles* is a part of a long line of Oklahoma decisions which clarify the meaning of the word "production" in oil and gas leases.<sup>119</sup> As part of this history, *Voiles* offers stability and valuable precedent to parties engaging in oil and gas transactions. *Voiles* also represents the view that business realities rather than ethical considerations should govern these transactions.

#### A. Cessation of Production Clause

##### 1. History of the Term "Production"

The major issue in *Voiles* concerned the cessation of production clause.<sup>120</sup> In accord with the minority view, the Oklahoma definition of the terms "produced" or

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109. *Id.* at 1211.

110. *See id.*

111. *See id.*

112. *See id.*

113. *See id.*

114. *See supra* note 38 and accompanying text.

115. *Voiles*, 911 P.2d at 1212.

116. 638 P.2d 441 (Okla. 1981).

117. *See Voiles*, 911 P.2d at 1212.

118. *Id.* (citing *Lott v. Kees*, 165 So. 2d 106, 111 (Ala. 1964)).

119. *See infra* notes 120-28.

120. *See Voiles*, 911 P.2d at 1208.

"production" has changed over the years from "production in paying quantities"<sup>121</sup> (when referring to production during both the primary and secondary terms of the habendum clause) to "capability of production in paying quantities"<sup>122</sup> (when referring to production in the primary term of the habendum clause). "Produced" or "production," as used in the secondary term of the habendum clause<sup>123</sup> and as used in the cessation of production clause,<sup>124</sup> also mean "capable of being produced in paying quantities."

If a lessee has completed a well *capable* of producing oil or gas in paying quantities, the lease remains in force throughout the secondary term, allowing the lessee to have a reasonable amount of time to market production diligently.<sup>125</sup> *Actual* production, as required by the majority of oil and gas producing states, is not necessary to keep the lease in force in Oklahoma.<sup>126</sup>

Because Oklahoma classifies the nature of an oil and gas lease in its secondary term as a *profit a prendre* whose duration is that of a *fee simple* on condition subsequent,<sup>127</sup> the grantor (or in this case the lessor) must bring an action to cause forfeiture.<sup>128</sup> The lease will not automatically terminate once oil or gas is capable of being produced.

## 2. Cessation of Production Clause in Voiles

Relying primarily on *Pack v. Santa Fe Minerals*,<sup>129</sup> the *Voiles* court reiterated that a lease in its secondary term will not terminate under the terms of the habendum clause when a well is at all times *capable* of producing in paying quantities.<sup>130</sup> The requirement of mere capability to produce in paying quantities allows the lessee voluntarily to cease removal of gas for a reasonable time without forfeiting his lease.<sup>131</sup> During this time of cessation of production, the lessee may

121. *Henry v. Clay*, 274 P.2d 545 (Okla. 1954) ("Oklahoma is committed to the doctrine that when an oil and gas lease provides that it shall remain in force and effect for a certain term and so long thereafter as oil or gas is produced, the term 'produced' means produced in paying quantities.") The opinion does not make clear whether actual production was necessary or whether capability of production was sufficient to hold a lease.

122. *State ex rel. Comm'rs of Land Office v. Carter Oil Co.*, 336 P.2d 1086, 1095 (Okla. 1958) ("In the absence of a specific clause requiring marketing within the primary term . . . the completion of a well . . . capable of producing oil or gas in paying quantities will extend such term . . . provided that within a reasonable time . . . a market is obtained.") This decision makes clear that *capability* of production will suffice to hold a lease; *actual* production is not required.

123. *See Gard v. Kaiser*, 582 P.2d 1311 (Okla. 1978).

124. *See Pack v. Santa Fe Minerals*, 869 P.2d 323 (Okla. 1994); *Danne v. Texaco Exploration & Prod. Inc.*, 883 P.2d 210 (Okla. Ct. App. 1994).

125. *See Danne*, 883 P.2d at 214.

126. *See Pack*, 869 P.2d at 328.

127. *See Danne*, 883 P.2d at 214. A "profit a prendre" is an incorporeal right to enter upon another's land and to extract substances. 1 EUGENE O. KUNTZ, A TREATISE ON THE LAW OF OIL AND GAS §3.1 (1987) [hereinafter KUNTZ, TREATISE].

128. *See Danne*, 883 P.2d at 213.

129. 869 P.2d 323, 327 (Okla. 1994).

130. *See Voiles v. Santa Fe Minerals*, 911 P.2d 1205, 1208 (Okla. 1996).

131. *See Pack*, 869 P.2d at 331.

diligently seek markets which offer higher prices. Only if a lessee fails to comply with the implied covenant to market may the lease be canceled.<sup>132</sup>

Professor Owen L. Anderson of the University of Oklahoma characterizes the *Pack* decision as an "excellent discussion of Oklahoma law [which] correctly interprets case law precedent."<sup>133</sup> Because *Voiles* relied heavily upon *Pack*, *Voiles* represents a continuation of the Oklahoma view on "capability of production in paying quantities." Consistent with prior case law on the subject, *Voiles* provides stability — valuable precedent on which parties may rely when considering whether to take legal action or whether to enter into an oil and gas lease.

### *B. Slander of Title*

When a top lessee joins a mineral lessor in a suit to cancel the bottom lease, the bottom lessee might defend against the suit by asserting that his title has been slandered. To buttress this argument, the bottom lessee might assert that the execution of an oil and gas lease, despite the continued validity of his prior lease, constitutes slander of his title.<sup>134</sup> However, the largest hurdle the bottom lessee faces in proving that his title has been slandered is showing that the top lessee acted with malice. If the top lessee has a valid interest, the fact that the lessor executed the top lease does not show that either party has acted in bad faith or with lack of probable cause.<sup>135</sup>

The *Voiles* court found that Hugoton had a good faith belief that the allegedly expired bottom leases owned by Santa Fe Minerals constituted a cloud on *Voiles*' mineral interests.<sup>136</sup> The fact that the court found that Hugoton acted without malice in bringing the lease cancellation suit is important because it strikes a proper balance between two competing public policies. The first policy is that a person should be able to assert his property rights without fear of being sued if it turns out that his title is bad. The second policy is that a person should be able to enjoy his property and should be free of others asserting claims that impair the merchantability and value of his title.<sup>137</sup> By requiring Santa Fe Minerals to prove that Hugoton acted with malice, the *Voiles* court furthered both of these goals.

### *C. Tortious Interference with Contract*

Similarly, tortious interference with contract requires that the top lessee act in bad faith or without probable cause in bringing a lease cancellation suit against a bottom lessee.<sup>138</sup> The primary factor which led the Oklahoma Supreme Court to conclude that there was no bad faith was the letter which appointed Hugoton as *Voiles*'

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132. See *Voiles*, 911 P.2d at 1208.

133. *Discussion Notes to Pack v. Santa Fe Minerals*, 128 OIL & GAS REP. 565, 565 (1994).

134. See *Petroleum Energy Inc. v. Mid America Petroleum, Inc.*, 775 F. Supp. 1420, 1428 (D. Kan. 1991).

135. See *supra* note 88.

136. See *Voiles*, 911 P.2d at 1209-10.

137. See KUNTZ, TREATISE, *supra* note 127, § 12.1.

138. See *supra* note 98.

agent.<sup>139</sup> Authorizing Hugoton to act on Voiles' behalf to bring a lease cancellation suit against the bottom lessees, this separate agreement established Hugoton's status as a representative of a party to the lease.<sup>140</sup> As a representative of a party to the lease, Hugoton could not be liable for tortious interference.<sup>141</sup> The supreme court noted that without Hugoton's help, many of the mineral owners would not have been able to pay litigation expenses.<sup>142</sup> By finding that Hugoton had not interfered with the bottom leases when Hugoton sued on Voiles' behalf, the court laudably aided Voiles in enforcing their contractual rights. Furthermore, by allowing Hugoton to help Voiles enforce their contractual rights, the court aided Voiles in obtaining additional drilling, more production, and larger royalties.<sup>143</sup>

#### *D. Champerty and Maintenance*

When a top lessee aids or encourages the mineral lessor to bring a lease cancellation suit against the bottom lessee, the bottom lessee may try to defend against the suit by claiming that the mineral lessor and top lessee are engaging in champertous conduct.<sup>144</sup> Because the doctrines of champerty and maintenance are based on the principle that only parties who have an actual interest in the matter may engage in a lawsuit, bottom lessees who try to use the doctrine as a defense to a lease cancellation suit are, in essence, asserting that top lessees have no legitimate interest in the matter. In this situation, a bottom lessee might charge that the top lessee is "stirring up" needless litigation.<sup>145</sup>

Regarding this issue, the Oklahoma Supreme Court in *Mitchell v. Amerada Hess Corp.*<sup>146</sup> held that a top lessee indeed has a legitimate interest sufficient to defeat a champerty defense — possession of a top lease.<sup>147</sup> The *Voiles* court relied upon *Mitchell* when it concluded that Hugoton did not engage in champertous conduct.<sup>148</sup> However, it did not state that Hugoton's possession of the top leases constituted an "interest in the subject matter of the suit." Rather, the court focused on the "benefits" that Hugoton provided Voiles by "policing oil companies [and] keeping them honest" in their dealings with mineral owners.<sup>149</sup>

The Oklahoma Supreme Court emphatically stated that it would not "prohibit mineral owners from obtaining litigation assistance from top lessees in challenges to the continued validity of base leases."<sup>150</sup> It arrived at this decision despite the testimony of some mineral owners that they would not have sued Santa Fe Minerals

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139. See *Voiles*, 911 P.2d at 1211.

140. See *id.*

141. See *id.*

142. See *id.*

143. See *id.*

144. See, e.g., *Mitchell v. Amerada Hess Corp.*, 638 P.2d 441 (Okla. 1981).

145. See Susan Lorde Martin, *Syndicated Lawsuits: Illegal Champerty or New Business Opportunity?*, 30 AM. BUS. L.J. 485, 485 (1992).

146. 638 P.2d 441 (Okla. 1981).

147. See *id.* at 445.

148. See *Voiles*, 911 P.2d at 1211.

149. *Id.*

150. *Id.* at 1212.

if Hugoton had not approached them with an offer to take a top lease and to pay their litigation costs for suing to cancel the bottom leases.<sup>151</sup> According to the court, "[p]olicing oil companies [and] keeping them honest"<sup>152</sup> is more important than discouraging "unnecessary" litigation and increased costs to mineral lessees<sup>153</sup> because of the important services the mineral owners received.

#### E. "Subject to" Language

Ordinarily, the inclusion of some sort of subordinating language, such as the words "subject to," makes it clear that a top lease will take effect only after the bottom lease has expired or is terminated.<sup>154</sup> In fact, some commentators have explained *Simons v. McDaniel*<sup>155</sup> not as an outright rejection of top leasing, but rather as an example of how the lack of subordinating language will cause the execution of a top lease to appear as an act of repudiation of the bottom lease by the lessor and as an act of slander of title of the bottom lessee's title by the top lessee.<sup>156</sup>

Because "subject to" language in the top lease explicitly recognizes the validity of the bottom leases, inclusion of this language would resolve problems associated with top leasing, such as claims of slander of title and tortious interference with contract. Yet, the *Voiles* court made no mention of whether the Hugoton top leases contained any subordinating language.<sup>157</sup> The court could have quickly resolved the issues presented by the parties by determining if the lease contained "subject to" language. Instead, the court focused on each claim separately. By taking this methodical approach, the court, whether inadvertently or not, emphasized the attractive attributes of top leasing: it allowed mineral owners to revisit their contractual relationship with their bottom lessees;<sup>158</sup> it allowed mineral owners to

151. *See id.* at 1211.

152. *Id.* at 1212.

153. *See Martin, supra* note 145, at 485.

154. *See Kemp, supra* note 8, at 659 n.100 and accompanying text; Jackson & Weissbrod, *supra* note 2, at 12-7 n.3 and accompanying text; Brown, *supra* note 1, at 219; Johnson, *supra* note 8, at 216-17.

155. 7 P.2d 419 (Okla. 1932).

156. *See Brown, supra* note 1, at 218.

157. The *Voiles* court stated:

The top lease states that it vests in the top lessee the mineral owner's reversionary interest under the base lease. It further states that possession under the top lease shall vest upon release of the base lease or upon a final and unappealable judgment that the base lease has terminated. The top lease also states that if this possession does not vest then the reversionary interest and top lease granted would terminate "within ten (10) years from the date of this Agreement."

*Voiles v. Santa Fe Minerals*, 911 P.2d 1205, 1209 (Okla. 1996). Note that the wording of this lease does not violate the rule against perpetuities, for it vests, if at all, well within twenty-one years following a life or lives in being at the creation of the interest. For cases involving top leases or top deeds and the rule against perpetuities, see *Stoltz, Wagner & Brown v. Duncan*, 417 F. Supp. 552 (W.D. Okla. 1976); *Peveto v. Starkey*, 645 S.W.2d 770 (Tex. 1983); *Nant v. Puckett Energy Co.*, 382 N.W.2d 655 (N.D. 1986).

158. *See Voiles*, 911 P.2d at 1211.

obtain additional drilling and more production (and thus a larger royalty);<sup>159</sup> and it policed oil companies and kept them honest.<sup>160</sup>

#### *F. Acceptance of Top Leasing Despite Cancellation*

Although the Oklahoma Supreme Court found no slander of title, no tortious interference with contract, and no champerty, it affirmed the trial court's judgment canceling the top leases. The supreme court affirmed the judgment because none of the parties asked it to let the top leases survive its declaration of the bottom leases' validity.<sup>161</sup> Despite its affirmation of the top leases' cancellation, the court went on to characterize top leasing as a common and accepted industry practice.<sup>162</sup> It noted that trial testimony established that "[top leases] are accepted, they are frequent, and they are simply considered to be a legitimate form of business competition in the oil business."<sup>163</sup> Moreover, the court recognized that "in the oil and gas industry there are people who take top leases and fund litigation attacking the base lease."<sup>164</sup> While once considered to be a form of "claim jumping,"<sup>165</sup> top leasing has now become a "useful and widespread business practice in the oil and gas industry."<sup>166</sup>

### *VI. Implications*

#### *A. Advice to Top Lessees*

*Voiles* provides three major pieces of advice to those considering taking a top lease. First, if a person takes a top lease in order to extinguish the bottom lease, he should make sure to bring a lease cancellation suit under the implied covenant to market, not under the cessation of production clause. A bottom lessee's failure to comply with the implied covenant to market, but not its ceasing production, could result in cancellation of its lease.<sup>167</sup> Second, the top lessee should make sure that the top lease states that it is "subject to" the bottom lease in order to avoid a slander of title suit.<sup>168</sup> Finally, the top lessee should enter into a separate agreement with the lessor. This agreement should authorize the top lessee to act on behalf of the lessor when bringing a lease cancellation suit. Having this agreement will protect the top lessee against a tortious interference with contract action by the bottom lessee.<sup>169</sup>

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159. *See id.*

160. *See id.* at 1212.

161. *See id.* at 1209.

162. *See id.*

163. *Id.*

164. *Id.*

165. *Frankfort Oil Co. v. Snakard*, 279 F.2d 436, 445 n.23 (10th Cir. 1960).

166. *Voiles*, 911 P.2d at 1209 (citing *Nantt v. Puckett Energy Co.*, 382 N.W.2d 655, 659 (N.D. 1986)).

167. *See Voiles*, 911 P.2d at 1208.

168. *See supra* notes 154-60 and accompanying text.

169. *See supra* notes 98-113, 138-43 and accompanying text.



### B. Increased Drilling and Production

*Voiles* has implicitly accepted that top leasing is a proper method of insuring that mineral lessees continue oil and gas production and pay competitive prices to mineral lessors. By treating top leasing as an established business practice in Oklahoma, the *Voiles* court has resolved the confusion found in earlier case law, especially between *Rorex* (stating that landowners may carve out as many estates from their fee simples as they see fit, including top leases)<sup>170</sup> and *Simons* (stating that a top lease is an obstruction of the bottom lessee's exercise of his rights).<sup>171</sup>

The implications of accepting top leasing as a valid and useful practice extend far, because top leasing can be an effective tool for obtaining acreage in tightly leased areas. At a time when the United States land drilling industry expects a dramatic increase in drilling operations over the next five to ten years, a variety of factors — industry consolidation, land rig attrition, the evaporation of used pipe and spare parts, and a shortage of qualified crews — has reduced the number of operationally-capable land rigs in the United States.<sup>172</sup> No longer will oil and gas companies worry about the legality or impropriety of top leasing, since *Voiles* has erased any residual concerns of the effect and status of top leasing.

Certainly, top leasing benefits top lessees by allowing them to gain footholds in heavily leased areas. However, top leasing also benefits mineral lessors by allowing them to obtain increased production and thus larger royalty payments.<sup>173</sup> Without the fear of being top leased, a bottom lessee faces less pressure to begin drilling operations.<sup>174</sup> Thus, top leases provide big benefits to mineral owners.

An increase in top leasing could impact Oklahoma's economy in another way. Years ago when rig rates were lower and drilling work was sporadic, qualified and experienced people who ran the rigs left the industry.<sup>175</sup> Any remaining experienced rig workers were being flown out of Oklahoma to work in Latin America and the Gulf of Mexico.<sup>176</sup> By increasing the practice of top leasing, thus increasing drilling and providing steady work, experienced and qualified rig workers may remain in Oklahoma.

### VII. Conclusion

At one time a party who acquired a top lease was considered to be a "claim jumper."<sup>177</sup> After the *Voiles* decision, such is no longer the case. The economic reality of business competition, rather than the ethics of top leasing, is now the major concern of the oil and gas industry and of the courts. As one *Voiles* witness

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170. See *Rorex v. Kercher*, 224 P. 696, 697 (Okla. 1923).

171. See *Simons v. McDaniel*, 7 P.2d 419, 420 (Okla. 1932).

172. See Brian A. Toal, *U.S. Land Drillers Trip Out of Hole*, OIL & GAS INVESTOR, Aug. 1997, at 22, 22.

173. See *Voiles v. Santa Fe Minerals*, 911 P.2d 1205, 1211 (Okla. 1996).

174. See Brown, *supra* note 1, at 242.

175. See Toal, *supra* note 172, at 25.

176. See *id.*

177. *Frankfort Oil Co. v. Snakard*, 279 F.2d 436, 445 n.23 (10th Cir. 1960).

testified, "[top leases] are accepted, they are frequent, and they are simply considered to be a legitimate form of business competition in the oil business."<sup>178</sup> Now that Oklahoma has essentially endorsed the practice of top leasing, it seems that top leasing is here to stay.

*Marichiel Lewis*

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178. *Voiles*, 911 P.2d at 1209.

