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Pitfalls In Developing Lands Burdened By Non-Participating Royalty: Calculating the Royalty Share and the Duty Owed to the Non-Participating Royalty Owner by the Holder of the Executive Right

Phillip Norvell

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PITFALLS IN DEVELOPING LANDS BURDENED BY NON-PARTICIPATING ROYALTY: CALCULATING THE ROYALTY SHARE AND THE DUTY OWED TO THE NON-PARTICIPATING ROYALTY OWNER BY THE HOLDER OF THE EXECUTIVE RIGHT.

PHILLIP E. NORVELL is a Professor of Law at the University of Arkansas School of Law. He specializes in Oil and Gas, Water and Antitrust Law. He received his BA degree and J.D. degree from the University of Oklahoma. He was a trial attorney for the Federal Trade Commission from 1973-75 where he was primarily involved in antitrust litigation involving the petroleum industry. He has been a speaker at numerous Arkansas Natural Resources Law Institutes, Institute on Oil and Gas Law and Taxation, and the Mississippi Institute on Oil and Gas. Also he is a member of the Arkansas Oil and Gas Commission.
Pitfalls in Developing Lands Burdened by Non-Participating Royalty

Calculating the Royalty Share and Coexisting with the Duty Owed to the Non-Participating Royalty Owner by the Executive Interest

by

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Pitfalls in Developing Lands Burdened by Non-Participating Royalty

Calculating the Royalty Share and Coexisting with the Duty Owed to the Non-Participating Royalty Owner by the Executive Interest

I.

Introduction

Non-Participating Royalty may be severed\(^1\) from the mineral estate,\(^2\) and when severed, only entitles the owner to its prescribed share of production, cost-free. The non-participating royalty owner does not participate in the executive right, the right to execute oil and gas leases, or in bonus or delay rental payments.\(^3\) Conveyances of non-participating royalty must be interpreted to determine the share of gross production that is conveyed or reserved. Central in determining the share of gross production conveyed is whether the interest created is a fractional share royalty or a fraction of royalty.

The difference between a non-participating fractional share royalty and a fraction of royalty is simple, yet illusive. First, a fractional share royalty entitles the owner to only that specified fractional quantum of gross production stated in the deed. In essence, the effect of a fractional share conveyance of royalty is to transfer "a fraction or percentage of gross production that stands as a free royalty."\(^4\) The share of gross production that the fractional share is entitled to is fixed by the fractional size of the interest conveyed by the deed, regardless of the amount of royalty contained in a subsequent oil and gas lease.\(^5\) For example, the language conveying "an undivided 1/16th of all of the oil, gas, and other minerals produced and saved," entitles the royalty owner to a 1/16th share of gross production regardless of the fact the landowner's royalty reserved in the oil and gas lease is a 1/8th, 3/16th or 1/4th royalty.\(^6\) A fractional share royalty interest does not participate in any overriding royalty reserved in an oil and gas lease, that is, in addition to the landowner's royalty.\(^7\)

Conversely, a non-participating fraction of royalty conveys that fractional share of royalty that is contained in the oil and gas lease.\(^8\) For example, a 1/2 of non-participating royalty, with an oil and gas lease providing for a 1/8th royalty, is entitled to a 1/16 part of gross production. Likewise, if the oil and gas lease provides for a 3/16th of royalty, a 1/2 of non-participating royalty is entitled to 3/32nds of gross production. In effect, the fraction of the non-participating royalty's share...
of production is not "fixed," but "floats" in accordance with the size of the landowner's royalty contained in the lease. In addition to the landowner's royalty, the fraction of non-participating royalty also shares proportionally in any overriding royalty interest reserved in the oil and gas lease, if the interest is a royalty. Because the holder of the executive right negotiates the landowner's royalty share in the oil and gas lease, and thus, determines the quantum of royalty that the fraction of non-participating royalty owner receives, the executive owner owes a duty of care to the non-participating royalty owner in establishing the landowner's royalty.

Determining whether a non-participating royalty conveyance creates a fractional share or a fraction of royalty involves an issue of construction teeming with complications which increase the perplexity of the question. Looming large in the confusion is the fact that the standard landowner's royalty in the oil and gas lease for approximately 50 years was a 1/8th share. That customary 1/8th share furnished the background in which non-participating royalty interests were created during that era. Thus, one wanting to reserve a share of the landowner's 1/8th royalty as, for example, 1/2 of that interest, could express it in either one of two ways. The reservation could be expressed as a fraction of royalty, i.e., 1/2 of the royalty, entitling them to 1/16th share of gross production, or as a straight fractional share, a 1/16th share of gross production, both of which reserved the same quantum of production. Thus, for many years, as a practical matter, a fractional share and a fraction of royalty were synonymous. In fact, as will be seen, many non-participating royalty interests were created by instruments that utilized both a fractional share and a fraction of royalty. One expression may be found in one clause of the deed, such as the granting clause, while the alternative expression will appear in either a "subject to" or a "future leasing" clause.

Over the last twenty years the landowner's royalty in the oil and gas lease has increased to a greater fractional share, such as a 3/16th or 1/4th. Consequently, a fractional share or a fraction of royalty are no longer synonymous, but yield different shares of gross production. The fraction of designation, created during the era in which the 1/8th landowner's royalty was all but universal and was the background for the transaction, yields a greater share of production than its historic counterpart, the fractional share designation.

To complicate matters, some laypersons, particularly during the old days when less of the populace was educated, had difficulty with fractions in general. Moreover, the distinction between these two different royalty designations is often slight and some laypersons, as well as lawyers, simply fail to comprehend the difference.
Delineating the Difference

The distinction between fractional share royalty interests and fraction of royalty interests may best be illustrated by examples from the case law. A common example of a fractional share non-participating royalty is the grant of a fraction of gross production or its equivalent. For example, "an undivided 1/24 of all of the oil, gas, and other minerals produced, saved and made available for market" conveyed a fractional share royalty interest entitled the grantee to a 1/24th share of gross production.11

The fractional share conveyance may also utilize a fraction in reference to "royalty" as a synonym for gross production. Thus, a reservation of "a 1/16th royalty from any oil and gas produced" entitles the grantor to a 1/16th share of gross production.12 Similarly, a grant of "a fee royalty of 1/32 of the oil and gas" created a fractional share 1/32 interest in gross production.13

Conversely, the common example of a fraction of non-participating royalty is grant of a "1/2 of royalty."14 The quantum of gross production is the specified fraction of the amount of the oil and gas lease royalty. As has long been observed, the "fraction of royalty" designation is equivalent to a mathematical formula that determines the quantum of gross production involved.15 The term "of" that follows the fraction (1/2) and precedes the term "royalty" means "times" and requires the fraction to be multiplied by the lease royalty to determine the quantum of gross production. Thus, when the lease royalty is 1/8th, 1/2 of royalty equals 1/16th of gross production. Yet that same fraction of royalty equals 3/32 of gross production when the lease royalty is 3/16ths.

A fraction of royalty has also been expressed by language that indicates the fraction is an interest in the royalty. For example, a grant of a "one-half (1/2) interest in all royalties" conveys "one-half (1/2) of the royalty" reserved in the mining lease.16 Also, a deed reserving "one-half (1/2) interest in and to the royalty rights" reserved 1/2 of the royalty to be paid under any existing or future lease.17 Similarly, a reservation of "an equal one-eighth (1/8th) of any royalty of all oil, gas, *** developed on or received from said land" reserved a 1/8th of royalty, which due to the royalty in the lease being 1/8th, reserved a 1/8th of 1/8th, or a 1/64th, share of gross production.18
Some Problem Areas

A. A Fraction of a 1/8th Royalty

Some non-participating royalty conveyances have utilized a fraction of a 1/8th royalty to fix the quantum of the royalty share. The effect is to create a fractional share royalty. For example, a grant of "1/2 of the 1/8th royalty (same being 1/16th of total production)" conveys a 1/16th share of gross production despite the fact that the lease royalty may be in excess of a 1/8th share.\textsuperscript{19} The plain meaning of the specific language utilized dictates the fractional share construction. After all, 1/2 of 1/8th equals a 1/16th share. The specific language of the grant or reservation precludes a construction of anything other than a fractional share of gross production. Thus, the courts give a literal interpretation to the fraction of 1/8th non-participating royalty which results in a fractional share construction.

That result, however, has not gone unquestioned. Dean Ernest Smith has observed that the general intent of the parties to the conveyance or reservation of a fraction of a 1/8th royalty was to convey or reserve a fraction of whatever royalty share that is subsequently provided for in the lease.\textsuperscript{20}

In essence, under Smith's theory, the 1/8th fraction appearing in the formula was not only synonymous with the oil and gas lease royalty share but signified the lease royalty share, whatever that share may subsequently become. Thus, a 1/4th of 1/8th royalty would be construed as a 1/4th of royalty, i.e., a fraction of royalty, entitling the royalty owner to share in lease royalty in excess of 1/8th. The hypothesis for Smith's general intent for a fraction of royalty construction is the historical ubiquity of the oil and gas lease royalty as a 1/8th share and the probability that the parties never considered the possibility of a lease providing for a greater royalty share. Smith recognizes, however, that the specificity as to the quantum of the share of royalty inherent in the fraction of 1/8th royalty conveyance, i.e., the specific intent, precludes any contradiction of such terms by a general intent based on historical facts or assumptions.\textsuperscript{21} Thus, despite his qualms, Smith recognizes that the fractional share of construction will prevail as the fraction of 1/8th royalty formula.

Nevertheless, cases exist dealing with deeds or reservations of a fractional share of 1/8th royalty that bear the suspicion that Smith's general intent theory is not far off the mark. One such case is \textit{Canter v. Lindsey},\textsuperscript{22} a Texas Civil Court of Appeals case. In that case, Dora Roberts owned the fee mineral estate to 17,712 acres of land. In 1935, she conveyed to M C. Lindsey as follows:
"... one fourth of one eighth (1/4 of 1/8) of all the oil, gas, and other minerals produced from the following described land ... the interest herein conveyed being an equal one fourth of one eighth (1/4 of 1/8) part of all of the oil, gas, and other minerals when same has been produced from said land, and to such extent, such part of any and all future productions of such is hereby conveyed."

The deed also reserved to the grantor the right to all bonuses, delay rentals and executive rights.

Thereafter, in 1941, Roberts executed the following deed to J.E. Mabee:

"That I, Dora Roberts, ... do GRANT, SELL, and CONVEY unto the said J. E. Mabee, ..., a three-fourths (3/4) interest, undivided, in and to all of the oil, gas and other minerals, on, in, and under the certain tracts, parcels and pieces of land ..."

The next clause of the deed conveyed to Mabee all the rights to the executive, bonuses and delay rentals, "as well as all other benefits accruing thereunder," to the remaining 1/4th interest.

That clause continued as follows:

"save and except the royalty payable under any such lease covering such 1/4th interest, all royalty accruing under any such lease on such 1/4th interest being payable to M. C. Lindsey, his heirs and assigns, who owns an undivided one-fourth (1/4) non-participating royalty interest in the oil, gas and other minerals in said land."

The deed then recited that Lindsey did not own any rights to the executive, bonus or rentals, such rights having been retained by Roberts in Lindsey's deed and repeated that such rights were conveyed to Mabee who would then solely own all executive, bonus and delay rental rights. As to royalty, the instrument concluded by stating that Mabee would own:

"the right to receive only three-fourths (3/4) of the royalty accruing under any such lease, or leases, the remaining one-fourth (1/4) interest in such royalty being owned by M. C. Lindsey, his heirs and assigns."

In 1973, an oil and gas lease covering part of the land was executed that provided for a 3/16ths royalty and production was established on the lease.
A declaratory judgment action was then instituted to determine the ownership of the 1/16 lease royalty share attributable to the 1/4th of royalty interest reserved in the Mabee deed that was in excess of the 1/8th royalty share. Predictably, all of the parties to the original conveyances were deceased but their heirs and successors-in-interest of Lindsey, Mabee and Roberts sought to recover the 1/16th royalty share.

Lindsey argued that he acquired the excess 1/16th royalty share by virtue of the 1935 deed. Lindsey argued, in part, that the deed conveyed a 1/4th of 3/16th, i.e., a 3/64th, royalty share in production from the 1973 lease. Lindsey prevailed at the trial court, but the Court of Civil Appeals reversed. First, the Court held the deed unambiguous and construed the scope of the conveyance to encompass only a 1/32nd fractional share non-participating royalty. In effect, Lindsey was conveyed a fractional share 1/32nd royalty, not a 1/4th fraction of royalty. Thus, Lindsey was only entitled to a 1/32nd share of gross production regardless of the size of the landowner's royalty contained in the 1973 lease. The Court observed:

"The Plaintiff became entitled to a 1/32nd royalty interest, but no more. That interest was established in 1935 and was absolute and independent of any royalty reserved in any future lease by the then holder of the executive rights."25

In effect, the Court in Canter literally interpreted the 1/4th of 1/8th royalty deed to convey a fractional share 1/32nd interest.

In addition to the 1935 deed, Lindsey also claimed that the recitals in the 1941 Mabee deed that described, albeit erroneously, his royalty share as a 1/4th of royalty established his right to a 1/4th share of the 1973 lease royalty. The Court rejected this argument for the following reasons. First, the recitals in the Mabee deed that described his royalty as a 1/4th share did not operate as a grant to Lindsey of that interest because of the lack of words of conveyance. Also, because the recitals in the Mabee deed as to Lindsey's title were erroneous they could not supply a basis for an exception from the grant that would operate as a conveyance of an interest.26 Finally, both of the Lindsey theories relating to the 1941 Mabee deed would also fail for contravening the rule that a reservation in favor of a stranger to the title is void.

Mabee, the grantee to the 1941 deed, claimed the excess royalty at issue on the theory that Roberts had conveyed to him everything which she owned and had not previously conveyed to Lindsey. The Court rejected this argument noting that even though Roberts was mistaken as to Lindsey's interest under the
1935 deed, believing he owned a 1/4th of royalty when he in fact owned a 1/32nd royalty, the 1943 deed clearly and unambiguously reserved a 1/4th of the royalty from the conveyance to Mabee. In effect, Roberts retained that portion of the reserved interest that was not outstanding in another.27 Thus, as only 1/32 was outstanding in Lindsey, entitling him to 2/64th of the gross lease production, and Roberts reserved a 1/4 of royalty, being a 1/4th of 3/16ths, or 3/64ths of such production, she owned the difference, being a 1/64 share of gross production.

When Canter v. Lindsey is considered in relation to Dean Smith's general intent theory, one wonders if Dora Roberts believed that a 1/4th of 1/8th royalty was identical to a 1/4th of royalty when she executed the two deeds? The Court admitted that she was mistaken when she executed the 1945 deed as to the effect of the 1935 deed. Was she also mistaken in forgetting that a 1/4th of 1/8th royalty was conveyed to Lindsey, as opposed to a 1/4th of royalty? Or, did she simply not believe that there was a distinction between the two? Did she think that the different formulas were synonymous and conveyed the equivalent share in production from a future lease? She, as well as Lindsey and Mabee, may have labored under that delusion. In any event, despite however convincing one might find Smith's theory, the literal interpretation that results in a fractional share construction of a fraction of 1/8th royalty prevails, absent additional language or circumstances dictating a different result.28 The plain language of the formula evidencing the specific intent cannot be overridden by a general intent derived from the historical background of the universality of the 1/8th lease royalty and a general assumption that the fraction 1/8th was intended to encompass any fraction of lease royalty.

2.

The Inconsistent Granting Clause:
A Fraction Of and the Minimum Royalty Provision

Brown v. Havard29 involved the construction of the following royalty reservation contained in a 1963 warranty deed:

"Grantors reserve ... in perpetuity an undivided one-half non-participating royalty (Being equal to, not less than an undivided 1/16th) ... ."

Brown, the defendant, executed the deed in favor of the successors-in-interest, Havard, et al. (Havard). The land was then subject to an oil and gas lease providing for a 1/8th royalty that was held during the secondary term by payment of shut-in-gas royalties on a gas well, the Gill No. 1. Havard, in 1973, executed an oil and gas lease covering the entire tract.
except for the Gill No. 1 gas unit to M-Tex that provided for a 3/8th lease royalty. M-Tex drilled four producing wells on the new lease. Havard then brought a declaratory judgment action contending that Brown only reserved a 1/16th royalty in the M-Tex wells. Havard argued, inter alia, that the deed was ambiguous and that extrinsic evidence revealed that the parties only intended a reservation of a 1/16th royalty. Brown contended that deed was unambiguous and reserved 1/2 of royalty, entitling him to 1/2 of the 3/8ths lease royalty. The case was tried to a jury which found, based on extrinsic evidence, that Brown was only entitled to a 1/16th share of gross production. The trial judge, finding the deed was not ambiguous and reserved a 1/2 of royalty, entered a judgment notwithstanding the verdict (JNOV), awarding Brown an undivided 1/2 of the lease royalty, being 3/16ths of gross production. The Court of Civil Appeals reversed, finding the deed ambiguous, and the evidence sustaining the jury's determination that the parties intended only a reservation of a 1/16th royalty. The Supreme Court of Texas, in a divided opinion, affirmed the Court of Appeals.

The majority of the Texas Supreme Court held the deed was ambiguous which permits the admission of extrinsic evidence to ascertain the intent of the parties. The test to determine whether there is an ambiguity is that after applying established rules of interpretation, the deed remains susceptible to more than one interpretation, it is ambiguous; but if only one meaning is clearly evident, the deed is not ambiguous.

The majority predicated its decision that the reservation was ambiguous on the following construction. The deed provided

"Grantors reserve ... in perpetuity an undivided one-half non-participating royalty ... ."

The majority determined this language would reserve a 1/2 royalty, being 1/2 of gross production, and not 1/2 of the royalty. However, the parenthetical phrase "Being equal to, not less than an undivided 1/16th," had "reference to a reservation of royalty."

The ambiguity was contained in the parenthetical phrase. One interpretation of "Being equal to, not less than an undivided 1/16th" is that it reserved a 1/16th fractional share royalty. In effect, the parties intended to reserve a 1/2 of the conventional 1/8th royalty, "being equal to" a 1/16th royalty. Under this interpretation, the language "not less than an undivided 1/16th" merely provided for the contingency that if the lease royalty were ever reduced, the 1/16th share would be received, insuring the reservation was a 1/2 of 1/8th royalty.

The parenthetical phrase also supported an alternative interpretation of a reservation of 1/2 of royalties contained in
future leases with a proviso that such share could not be less than 1/16th. This was the argument advanced by Brown. However, the opinion cryptically noted that the presence of the "comma" between the phrase "Being equal to" and "not less than an undivided 1/16th" must be ignored to permit this latter construction. In other words, in the view of the majority, the presence of the "comma" in the parenthetical phrase grammatically precludes a construction of that language as intending to convey a 1/2 of royalties in future leases but not less than a 1/16th share. To achieve that construction based on that language, the comma, i.e., the grammatical construction, must be ignored.\(^3\) After reviewing the extrinsic evidence admitted by the trial court, the majority affirmed the Court of Appeals determination that Brown intended to reserve a 1/16th royalty share.

The dissenting opinion found the deed unambiguous and reserved to Brown 1/2 of royalties with a minimum royalty set at 1/16th. The dissent interpreted the parenthetical language as referring to the lease in existence at the time the deed was executed as well as to future leases. Under the existing lease, which had a 1/8th royalty clause, a reservation of 1/2 of royalties would be equivalent to a 1/16th royalty. The inclusion of the words "not less than an undivided 1/16th" only indicated that Brown contemplated future leases on the property after the existing lease expired. In the event a future lease provided for less than a 1/8th royalty, Brown, under the parenthetical clause, would still be entitled to a 1/16th royalty. If the future lease provided in excess of a 1/8th royalty, Brown was to share in 1/2 of that royalty. In effect, the draftsman was merely exercising caution to guarantee a certain minimum royalty.

Finally, the dissent differed on the effect of the "comma" in the parenthetical phrase. The dissent noted:

"There is no language anywhere in the reservation clause to indicate that the Browns' royalty was to be limited to a maximum of 1/16th; there is no language to the effect that 1/2 of royalties is to be equal to not more than 1/16th. The reservation does, however, unambiguously state that the Browns' royalty interest is to be not less than 1/16th. Describing a variable amount as being equal to not less than 1/16 has the same result as describing it as equal to or greater than 1/16. The absence of a comma between the words "equal to" and "not less than" does not change this meaning. The deed reserves 1/2 of royalties, and the explanatory parenthetical sets a minimum of 1/16. The specific fractional equivalent to 1/2 of royalties may vary according to the lease so long as the Browns received their 1/16 minimum."\(^3\)

Brown v. Havard illustrates some of the perplexing problems
of construing mineral or royalty conveyances for lawyers and landpersons. First, one must be able to see the potential for an ambiguity in the deed or reservation clause, i.e., the susceptibility to different interpretations. However, as noted by the majority opinion, even if it is susceptible to two constructions, it is not ambiguous if one construction clearly predominates.

More importantly, the conclusion that the reservation was ambiguous may be plausible but not irresistible. After all, the grantor's reservation specifically specified a 1/2 non-participating royalty, which was intended as a 1/2 of royalty reservation (Brown never argued otherwise), which was followed by the parenthetical phrase where the majority found the ambiguity. When the reservation was created, an oil and gas lease with a 1/8th royalty was in existence and the grantor could have intended to reserve a perpetual non-participating royalty, mindful that future leasing of the tract may occur. The intent appears evident: the language of the parenthetical phrase was to insure that no less than a 1/16th lease royalty would ever devalue his perpetual royalty interest. Did he also intend the language "Being equal to" to confine his royalty share to a 1/16th? What would your answer be if you did not know that the jury had found that the parties intended the reservation of a 1/16th share of production?

If in fact Brown's intent was to reserve a 1/2 of royalty interest with the parenthetical phrase only being added to insure that his royalty under any future lease would be a minimum of 1/16 share, then the drafting of the minimum royalty provision that was designed to protect, in actuality, led to ruination. Although minimum royalty provisions may be a desirable addition to the fraction of royalty grant or reservation to protect the royalty owner from a low lease royalty negotiated by the executive owner, Havard points out the necessity that such clauses be clearly and unambiguously drafted so that the conveyance is to a fraction of royalty with a minimum royalty limitation. Otherwise, as may have been the case in Havard, that which was intended to help may in fact harm.

3. The Horrors of the Double Fraction

In Palmer v. Lide, the Arkansas Supreme Court was construing a 1927 non-participating royalty deed that granted as follows:

"do hereby grant, bargain, sell and convey ... an undivided one-eighth of one-eighth (1/8) interest in
and to all of the oil gas and other mineral royalty ... ."

Oil production was subsequently established on the land under a lease providing for a 1/8th landowner's royalty. Division orders were prepared which reflected that the deed conveyed a 1/8th of 1/8th royalty, a 1/64th share of gross production. The successors-in-interest of both the grantors (plaintiffs) and the grantees (defendants) executed the division orders and royalty was distributed to the parties on that basis until the operator suspended the amount subsequently disputed. Plaintiffs then sued to recover the suspended royalties and to determine their proper share of future royalties.

Plaintiffs argued that the deed conveyed a 1/8th of 1/8th of royalty, with the latter being fixed by the lease at 1/8th. Thus, according to the plaintiffs, the deed conveyed 1/8 of 1/8 of 1/8, being a 1/512 share of gross production. The defendants argued that the deed, as reflected in the original division orders, conveyed 1/8th of 1/8th royalty, being a 1/64 production share. The Supreme Court, affirming the trial court, interpreted the deed as conveying 1/8th of 1/8th of the royalty, which under the facts was a 1/512 share of gross production. Predictably, the Court gave effect to the plain language of the grant. The language unequivocally conveyed a fraction (1/8) of a fraction (1/8) of a fraction (of royalty, being a 1/8th share). The Court observed that it simply "is not possible to interpret the unmistakably clear language of the deed to mean 1/8th of 1/8th of the total production."35

The defendants, who had been enjoying the royalty overpayment occasioned by misinterpretation of the deed in the preparation of the division orders, also argued vainly that the plaintiffs were barred from claiming that the defendants were only entitled to receive a 1/512 production share by adverse possession, laches, limitations or estoppel. The Court, following Warmack v. Cross Co.,36 held that the overpaid royalty owner does not acquire title by adverse possession or acquiescence to the interest attributed to his ownership by mistake by the party disbursing the proceeds of production. Additionally, the Court held that one who erroneously receives and keeps overpayment for several years is not in equity entitled to a continuation of the error.

One cannot quarrel with the construction of the "double fraction" formula by the Arkansas Supreme Court in Lide and by other courts.37

The specific intent of the parties arising from the plain language of the formula is unmistakable. However, one is haunted by the fear that the "horrors of the double fraction" may be the result of an error based simply on the parties' selection of the
wrong royalty deed form. Intending only to convey a 1/8th of 1/8th royalty, or a 1/64th share of gross production, the parties mistakenly selected a printed form to convey a fraction of royalty and inserted in the blank, which is followed in the form by the salient of royalty language, the fraction, 1/8 of 1/8. Had the printed form selected been for a fractional share conveyance, no mistake would have occurred and their intent would have been effectuated. Obviously, that one simple and single word "of," succeeded by the term "royalty," is paramount in establishing the quantum of the royalty share conveyed. Yet that simple distinction was probably lost on a lot of landowners, particularly in the early days of mineral conveyancing. That common error, like the Duhig rule of mineral conveyancing, has likely occasioned the loss of fortunes in oil and gas royalties.

4. The Large Fractional Share

Fractional share non-participating royalties are peculiarly worthy of caution. The illustrative case is Gavenda v. Strata Energy, Inc., a Texas Supreme Court case, wherein the Gavenda family reserved a 15-year non-participating royalty interest in a 1967 deed. The relevant part of the deed provided:

"an undivided one-half (1/2) non-participating royalty of all of the oil and gas in, to and under that [sic] produced ... ."

Subsequently, in 1978, the predecessor-in-interest to the grantee, who owned the executive right to the Gavendas' non-participating royalty, executed an oil and gas lease providing for a 1/8th landowner's royalty. Thereafter, Strata Energy, Inc., and others, acquired the oil and gas lease by assignment and drilled two producing wells on the tract.

Strata then hired an attorney to prepare a division order title opinion. The examining attorney erroneously interpreted the reservation in the 1967 deed as entitling the Gavenda family to a 1/16th royalty share, as opposed to a 1/2 royalty share. Obviously, the attorney erroneously construed the reservation as a 1/2 of royalty, which would accrue 1/2 of the landowner's royalty which equals a 1/16th of gross production. Instead, the deed reserved a 1/2 royalty which entitled the Gavendas' to a 1/2 of gross production.

Based on the title opinion, Strata prepared division orders, which the Gavendas' executed, that provided for the disbursement of their share of the proceeds on a 1/16th royalty share. Thereafter, when some of the Gavendas died and the royalty
ownership changed, transfer orders were prepared and executed reflecting the 1/16th royalty ownership.

Apparently, during the administration of one of the estates, the error was discovered. The Gavendas revoked their division and transfer orders two days before the term interest expired. Thereafter, the Gavendas' sued to recover the unpaid 7/16th royalty share, amounting to more than $2.4 million in unpaid royalties. In the litigation, the defendant lessees did not dispute that the deed reserved a 1/2 royalty interest, being a 1/2 share of gross production. Instead, they argued that the stipulation of ownership interest contained in the division orders estopped the plaintiffs from claiming any royalty in excess of the 1/16th interest.

The Supreme Court of Texas, reversing the trial court and the intermediate appellate court, held that the defendants were liable for the unpaid royalties prior to the revocation of the division orders. Historically, estoppel had been applied based on the stipulation of ownership interest contained in the division order. Such estoppel precluded the underpaid interest owner from recovering the deficiency from the operator who relied on the division order to distribute the proceeds of production. The Court reasoned, however, that estoppel is not applicable when the operator made the mistake because a contrary result would allow the operator to profit unjustly from its own mistake.

The opinion recognized that the attorney who misconstrued the royalty reservation was being sued for malpractice but, as the attorney was the agent of the defendants, his negligence was imputed to them.

5.

Inconsistency in the Granting, Subject To and Future Leasing Clauses

Early non-participating royalty deed forms, and occasionally formally drafted royalty reservations, paralleling early mineral deeds, often contained multiple clauses in which different fractions could be inserted. The granting clause designates the quantum of the estate conveyed in the deed. The "subject to" clause recites that the interest conveyed was subject to an outstanding oil and gas lease and specifies the lease benefits that are covered and included in the grant. The "future-lease" clause specifies the ownership interests conveyed under future leases after the existing lease has expired.

The practice of specifying the interests conveyed under existing and future leases in the "subject to" and "future-lease"
clauses is attributed to an early ill-fated Texas case. Caruthers v. Leonard\textsuperscript{44} held that the grantee of a fractional interest in a mineral estate that was subject to a pre-existing oil and gas lease did not receive a right to his proportionate share of the benefits under the lease. Caruthers was obviously bad law; its holding was inconsistent with the basic common law principle of conveyancing, namely that which is not specifically reserved from the grant is conveyed. Eventually, some forty years later Caruthers was overruled.\textsuperscript{45} In the absence of Caruthers, a "subject to" clause is only required to prevent the grantor from breaching the covenants of title when the mineral estate conveyed is burdened by a pre-existing oil and gas lease.

Deeds drafted to require the parties to fill in separate clauses, some of which relate to the different incidents of mineral ownership, such as the "subject to" and "future-lease" provisions, are obviously susceptible to errors that present perplexing issues of judicial interpretation. The focus of our inquiry is the problem which occurs when the clauses utilize both a fractional share and a fraction of royalty. However, the resolution of this issue has been intertwined with the most common problem of construction involving inconsistencies between the "subject to" and "future lease" clauses and granting clauses, the dilemma of disparate fractions relating to mineral and royalty interests.

The problem of construction of these multiple provision deeds is attributable to the misconception of the parties, particularly as to early conveyances, as to the whether a mineral or royalty estate is being conveyed. Rooted in the problem was the widespread confusion relating to the difference between mineral and royalty fractional shares as they relate to the share of production attributable to such fractional interests. For example, a 1/16th of a mineral estate only entitled the grantee to a 1/16th of the conventional 1/8th lease royalty, being a 1/128 production share; while a 1/2 mineral estate entitled the grantee to a 1/2 of the 1/8th royalty, being a 1/16th royalty share. Failing to fully understand this distinction, the parties intending to convey a 1/2 mineral estate, focusing on the 1/16th share of royalty, may have erroneously inserted the 1/16th fraction in the granting clause drafted to convey a mineral estate, while inserting the 1/2 fraction in the subject to or future lease clause.\textsuperscript{46}

A. The Texas Cases: The Decline, Fall and Resurrection of the Multiple Grant Construction

The legacy of some early and highly criticized Texas cases\textsuperscript{47} that construed deeds as effectuating "two grants," or more, continues to play a prominent, yet equivocal role, in the Texas case law which deals with inconsistencies between the granting, "subject to," and "future lease" clauses in mineral and royalty

\textsuperscript{14}
deeds. The "two grant" approach is that if the benefits conferred on the grantee in the "subject to" clause or the "future lease" clause differ from the benefits derived from the interest conveyed in the granting clause, then the former clause is construed as conveying, along with but independent of the latter clause, the benefits conferred therein. In effect, such a deed conveys not one, but two or more grants.

If the "two grant" construction prevails, then a royalty deed with a granting clause conveying a "1/32nd of the oil and gas in and under and that may be produced and saved" and a "future lease" clause that recites that the grantee owns a "1/4th of the royalties" under "future leases" conveys two separate and distinct interests; a 1/32nd fractional share royalty applicable to the existing lease and a "1/4th of royalties" under subsequent leases. The "1/4th of royalties" clause entitles the grantee to its proportionate share of royalties in the future lease in excess of the conventional 1/8th landowner's royalty.

Although some early Texas cases applied the "two grant" theory in some oil and gas deed construction cases, the theory was not applied to cases involving conflicting fractions in mineral or royalty deeds. The traditional "four corners" rule of construction, involving conventional rules of interpretation to ascertain the intent, was utilized.

However, in Farmers Canal Co. v. Potthast, a 1979 Texas Civil Appeals Court case, was decided under the "four corners" standard, and hindsight reveals that the decision was a harbinger of what was to come. The case dealt with the construction of a 1945 non-participating royalty deed in which the granting clause conveyed "a 1/4th interest in and to all of the ... oil royalty, gas royalty, ... ." A "future lease" clause also recited:

"It is distinctly understood and herein stipulated and agreed . . . that Grantee shall only receive one-fourth (1/4th) of the money royalty on sulphur ... and one-fourth (1/4th) of the one-eighth (1/8th) royalty on oil, gas and all other minerals provided for in such lease or leases; and in the event Grantors, their heirs, or assigns, in the status of the fee owners of the minerals shall operate and develop the minerals therein, Grantee, his heirs and assigns, shall own and be entitled to receive as a free royalty an undivided one-thirty-second (1/32nd) of all of the sulphur, oil, gas and other minerals produced, saved and sold off the premises;"

Apparently the land was not leased until 1972, when plaintiffs, successors-in-interest to the grantors, executed an oil and gas lease that provided for a 1/6th royalty on oil and gas. Production was established on the lease.
Plaintiffs sought a construction of the deed to determine that the deed only conveyed a 1/4th of 1/8th royalty. Naturally, the defendants, the successors-in-interest of the grantees, argued that the deed conveyed a 1/4th of royalty which entitled them to 1/4th of a 1/6th royalty share. The court held that the grantees were conveyed a 1/4th of royalty and the defendants were entitled to a 1/24th share of gross production.

In so holding, the Court recited the standard rule of deed construction, the "four corners" rule, seeking the intention of the parties by considering all language appearing therein, and harmonizing, if possible, those provisions which appear to conflict. The Court, however, also recited and applied other rules of deed construction: construing the deed against the grantor if doubt exists as to the intention of the parties; and, if there is a "necessary repugnance" of clauses in the conveyance, the granting clause prevails. Thus, since the granting clause specified a grant of 1/4th of royalty, while the future leasing clause restricted the royalty to 1/4th of 1/8th, the granting clause prevailed, and the deed conveyed a 1/4th of royalty.

Subsequently, in 1984, the Supreme Court in Alford v. Krum adopted the "repugnancy to the grant" theory to resolve inconsistencies between the granting, subject to, and future lease clauses. The case involved the construction of a 1929 deed in which the granting clause conveyed a 1/2 of 1/8th mineral interest, the "subject to" clause provided for a 1/16th of royalty under the existing lease, and the "future lease" clause provided:

"in the event that the said above described lease for any reason becomes cancelled or forfeited, ... the lease interests and all future rentals on said land, for oil, gas and mineral privileges shall be owned jointly by ...[Grantors and Grantees] ... each owning a one-half interest in all oil, gas and other minerals in and upon said land, together with one-half interest in all future rents." (Emphasis added.)

The lease in effect at the time the deed was executed had expired.

The trial court construed the deed as conveying a 1/16th mineral estate (1/2 of 1/8th). The Court of Appeals, emphasizing the language of the future leasing clause, reversed the trial court, holding that the deed conveyed a 1/2 mineral estate. In a divided opinion, the Supreme Court, reversing the Court of Appeals, held that the deed conveyed a 1/16th mineral estate.

The holding of the majority was premised on the rule of construction that when irreconcilable conflict between the granting clause and other clauses in the deed exists, the granting clause prevails. The majority reasoned that when an irreconcilable conflict precludes a harmonization of internally inconsistent
expressions of intent, the granting clause, which contains the
"controlling language" and the "key expression of intent,"
prevails. Further, the majority observed that the "well
established" purpose of the future lease clause is to "explain or
restate" the operative effect of the grant contained in the
granting clause when the present lease terminates and future leases
are executed. Finally, the majority emphasized that the language
of the granting clause was clear and specific while the language of
the future lease clause was unclear.

The dissent, by Chief Justice Pope, offered the following
analysis of the deed. The granting clause first conveyed a 1/2 of
1/8th or a 1/16th mineral estate. The "subject to" clause then
recognized the existence of an outstanding oil and gas lease and
expressly subjected the 1/16th conveyance to the outstanding lease.
The dissent then noted that the majority had also held that the
deed presently conveyed the "possibility of reverter" to that
1/16th interest upon termination of the lease. Up to this point in
this analysis, the dissent noted that there was no disagreement
with the majority.

The disagreement related to the "future lease" clause which
the dissent viewed as conveying a "different and a greater estate"
upon termination of the outstanding lease. According to the
dissent, "the ridgepole that divides the rights conveyed before
reverter from those conveyed after reversion" was the language that
upon cancellation of the outstanding lease "the lease interests and
all future rentals on the land shall be owned jointly ...[by the
grantors and grantees] ... each owning a one-half interest in the
oil, gas and other minerals ... ." The dissent further noted that
there is no ambiguity in a deed that grants a 1/16th mineral estate
so long as there is an outstanding lease and a 1/2 mineral estate
upon the lease's termination. The fractions are different, the
dissent stated, for a good reason.52

Even though the deed was construed to contain "multiple
grants," the dissent also emphasized the applicability of the "four
corners" rule of construction.53. More importantly, the multiple
grants recognized by the dissent involve first the conveyance of
a mineral estate, which fluctuates in size according to time, and
secondly the grant of an undivided 1/16th interest when the land
was burdened by an outstanding lease, and, thirdly, a subsequent
grant of an undivided 1/2 interest when the lease expired.54

Two points emerge from Alford. One is that the majority's
adoption of the rule "repugnant to the grant" construction. This
rule provides that the granting clause prevails over the "subject
to" and "future lease" provisions when an irreconcilable conflict
between former and latter clauses exists. This rule has some
advantages; namely simplicity of application and certainty of
title. Many deeds with disparate fractions as to mineral or
royalty interests arising from the inclusion of a "subject to" or
"future lease" clause do present irreconcilable conflicts, impossible of internal harmonization, with the granting clause. Thus, a title examiner can often determine the scope of the conveyance without resort to litigation.

The disadvantage of this reasoning is that it is an arbitrary rule of construction that may not reflect the intent of the parties because it exalts the physical location of one clause over another clause that may be more expressive of intent. However, the reign of Alford was short-lived. In 1991, the Texas Supreme Court in Luckel v. White, another divided opinion, reversed the "repugnancy to the grant" rule of construction, specifically overturning Alford.

Luckel involved the construction of a 1935 royalty deed. Mayes, the grantor, conveyed a royalty interest to Luckel by a deed in which the granting, habendum, and warranty clauses recited that a 1/32nd fractional share royalty was conveyed. The "subject to" and "future lease" clauses stated that the grantee was entitled to receive "1/4th of any and all royalties." When the deed was executed, the land was subject to an oil and gas lease providing for a 1/8th royalty that had subsequently expired. Many years later, the land was subject to numerous leases, some of which provided for a 1/6th royalty. A declaratory judgment action was brought to determine if the successors-in-interest of the grantee, Luckel, were entitled to a 1/32nd or a 1/4th of 1/6th share of gross production from the excess royalty clauses.

The majority opinion applied the "four corners" rule of construction, which ascertains the intent of the parties by attempting to harmonize all parts of the deed, only striking down a part of the deed when an irreconcilable conflict with another part of the instrument destroys its effect. The majority ascertained the intent of the parties by harmonizing the conflict between the granting clause and the "future lease" clause as follows: the granting clause conveyed a 1/32nd interest (or 1/4th of the royalty under the existing lease) until the existing lease expired; and, the "future lease" clause presently conveyed the possibility of reverter as to 1/4th of royalties. Thus, as to future leases, the latter clause conveyed a 1/4th of the total reserved royalty. Since the harmonization of the Mayes-Luckel deed conflicted with the construction of the deed in Alford, the latter case was expressly overruled. The Court further held that the outright grant of an 1/32nd fixed royalty in the granting clause did set the minimum of the royalty for the 1/4th royalty conveyed pursuant to the "future lease" clause.

Luckel v. White resurrected the "two grant" doctrine in Texas deed construction. Although the language of the "four corners" rule of construction, harmonizing all clauses of the instrument, if possible, is present, the recognition of, as well as the emphasis on, the two separate and distinct grants emerging from the granting
clause and the "future lease" clause is inescapable. Also, as the granting clause conveyed a 1/32nd fractional royalty share under the exiting lease and the "future lease" clause conveyed a 1/4th of royalty as to the "possibility of reverter" which would become possessory, apparently, upon the execution of the future lease, a conveyance of simultaneous interests, which are differing only as to the quantum of the share conveyed and the time in which the interests become possessory. That is a rather sophisticated theory as to the subject matter of the parties to a 1935 royalty deed. The criticism of Luckel v. White, which is the enduring criticism of the "two grant" theory, is that its unlikely the parties intended two separate grants in the deed. As stated by the dissenting opinion:

"The oft-repeated expression that a grantor has the power to convey by one instrument different interests in the possibility of reverter and under the subsisting lease should not obscure the fact that very few grantors really intend to convey interests of different magnitude."

If flawed theory of Luckel does not necessarily make the result wrong. The result is the same as if the deed had been construed against the grantor. However, the dissent disagreed with the result as well as the "two grant" rationale. The dissent would have taken judicial notice of the fact that the standard lease royalty in 1935 was a 1/8th share. The parties did not then contemplate that a 1/4th of royalties might not always equal a 1/32nd production share. The granting clause intended to convey a permanent grant of a 1/32nd royalty interest. The "future lease" clause's "1/4th of royalties" was only used to extend the 1/32nd production share to future leases.

Despite the lack of enthusiasm of the resurrection of the "two grant" doctrine to mineral and royalty conveyances, no one mourned the loss of Alford except, of course, title examiners who determined ownership on the basis of the "repugnancy to the grant theory" and their clients who made investments in mineral and royalty titles in reliance on Alford.

B. The Arkansas Cases

Barret v. Kuhn, is the first Arkansas Supreme Court case construing a non-participating royalty deed that contained both a fractional share and a fraction of royalty. The royalty deeds at issue were executed in the 1940's when there was no production on the land. The deeds were entitled "Royalty Deeds" and underneath was printed the term "non-participating." The granting clause provided:

"do hereby grant ... an undivided one sixty-fourth (1/64)
interest in and to all of the oil, gas and other
minerals, in, under and upon the following described
lands . . . "

Following the granting clause was a "minimum royalty" clause that the Court referred to a "royalty" clause:

"Provided, that the grantors herein expressly covenants with the grantee that no oil and gas mining lease shall ever be executed covering the above land, or any part thereof, that shall reserve to the grantors herein, their heirs and assigns, as royalty, less than one-eighth of all of the oil and gas produced and saved from said land and this covenant shall be deemed a covenant running with the land."

Following the "minimum royalty" clause was an "intention" clause which the court also treated as part of the "royalty" clause:

"It is the intention of the parties hereto that the grantee herein, its successors or assigns, shall be entitled to receive hereunder one-eighth of all oil and/or gas run to the credit of the royalty interest reserved under and by virtue of any oil and gas mining lease now in force and effect . . . , and under any oil and gas mining lease hereafter executed . . . ." (Emphasis added.)

Additionally, after the royalty clause was a "production" clause:

"and in any event, the grantee herein, its successors or assigns, shall be deemed the owner of and shall be entitled to receive 1/64th of all oil and gas produced and saved from the said land . . . ."

Thereafter, the plaintiffs, successors-in-interest to the grantors, and owners of the executive right, executed oil and gas leases that provided for overriding royalties of either 1/8th or 1/16th in addition to a 1/8th landowner's royalty. After production was established on the land, division orders were prepared that provided for the owners of the non-participating royalty, the grantees, to share in the overriding royalty as well as the lease royalty. Litigation ensued to determine the proper division of the royalty and overriding royalties between the plaintiffs and defendants.

The Arkansas Supreme Court, affirming the decision of the Chancellor, held that the nonparticipating royalty owners were only entitled to a 1/64th share of production which precluded their participation in the overriding royalty. The Court reasoned that
the granting clause, as further evidenced by the language of the "production clause," conveyed only a 1/64th interest in the oil, gas and minerals produced. This interpretation clearly limited the claim of the nonparticipating royalty owners because if they were to participate in the overriding royalty interest, they would receive more than a 1/64th interest. In effect, the Court construed the deed as granting a fractional royalty interest.

The rationale for this result can be premised on the applicability of the rule of construction that the granting clause, specifying the fractional share, controls over the inconsistent "royalty clause," with its fraction of royalty language. In effect, the "repugnancy to the grant" rule of construction was applied. But the case can also be read as holding that the fraction of language in the "royalty clause" was only intended by the parties to permit the royalty owners only to participate in the 1/8th lease royalty.63

Anadarko Petroleum Co. v. Venable,64 a 1993 Arkansas Supreme Court case, also involved the construction of non-participating royalty deeds containing conflicting fractional share and fraction of royalty clauses. Because the deeds are identical in form, differing only as to the fractional shares conveyed, the discussion will focus exclusively on one deed, the "Royal" deed.

The deed was executed in 1939 when the lands were then subject to an existing oil and gas lease, the Tissue lease, that provided for a one-eighth royalty. The deed contained the following granting clause

"the grantee shall at all time subsequent to the execution of this instrument, receive a 13/1920ths part of all oil, gas and other minerals produced and saved from the above described land, ... which provision and agreement is a covenant which shall run with the land.... ."

The deed then contained the following subject to clause which the Court described as a "second" granting clause:

"It is understood that this land is encumbered with an oil and gas lease, executed by J.G. Tissue, a widower, as Lessors, to Record Owners as Lessee, on _____, which lease is recorded in Book _____, at Page _____, ... .

And for the same consideration the Grantors do hereby bargain, grant, sell, convey and set over onto the Grantee an undivided 13/240ths part of all royalties on oil or gas produced from the above described lands during the term of said lease, or any extension thereof." (Emphasis added).
Thereafter, in the 1980's, sometime after the expiration of the Tissue lease, the mineral owners executed oil and gas leases that provided for a 3/16th royalty (with 1/16th of that share apparently being an overriding royalty). The defendant, Anadarko Petroleum Co., the lessee, drilled producing wells on the leased lands. In 1983, the plaintiffs, the successors-in-interest of the grantees, executed division orders in favor of the defendant. The defendant was disbursing the proceeds from production and had calculated their royalty share as a straight 13/1920th share of production which was equivalent to payment on a 1/8th royalty basis.

In 1991, the plaintiffs sued the defendant in Chancery Court to establish their right to participate in the royalty on a 3/16th basis. The Arkansas Supreme Court, affirming the holding of the Chancellor below, interpreted the 1939 deed as granting a fraction of royalty which permitted the plaintiffs to share in the royalty on a 3/16ths basis.

The Court's holding was premised on two bases. First, the quantum of royalty granted in the deed had to be determined by reading the straight fractional share grant of the "first" granting clause in conjunction with the "second" granting clause's grant of a fraction of royalty. In so doing, the Court rejected the defendant's argument that the fraction of royalty contained in the second granting clause was merely "explanatory" of the scope of the fractional share conveyed in the first granting clause. The Court reasoned that the language of the second granting clause "utilized all the terms of art of conveyance," i.e., words of grant, and granted an "additional fractional one-eighth of" that initially conveyed in the lease.

Additionally, the defendant argued that the language of the second granting clause, "during the term of said lease or any extension thereof," indicated that the parties did not contemplate that clause being applicable to "future leases." The Court rejected that argument, affirming the Chancellor's finding that the subsequently executed oil and gas leases were an "extension" of the previously expired Tissue lease. Therefore, subject to the second granting clause, the grant of a fraction of royalty, required payment of royalties on the 3/16th basis.

Despite the fact that the deed contained two granting clauses (the Court emphasized and interpreted the second granting clause as intending to effectuate a conveyance), the case does not follow the "two grant" theory of Luckel v. White. In effect, applying the "four corners" rule of construction, the Court found that the parties to the conveyance intended the latter fraction of "royalty clause" to control over the former fractional share clause.

Moreover, the Court held that the plaintiff's execution of the division order, which calculated their royalty share on a 1/8th
basis, did not preclude recovery from the defendant for the underpayment occasioned by the failure to pay royalty on the 3/16th basis. Although the Court recognized the general rule that the purchaser of production may rely on the division order in making payment to the interest owners and not be liable in tort or contract for underpayment, it refused to apply the rule. The Court refused to apply the rule for three reasons. First, the division order did not specifically indicate plaintiff's ratification or waiver of the right to challenge the calculation of his ownership share. Second, plaintiff's lack of knowledge of the 1980 leases, providing for the 3/16th royalty share, prior to filing suit precluded applicability of the doctrine of estoppel and laches. And thirdly, the record was devoid of any evidence regarding any payments made by Anadarko that interjected the rights of innocent third parties.

The rationale and holding as to the failure of the division order to protect an operator paying royalty pursuant to its terms are difficult to determine from the opinion. One would assume from the facts that Anadarko was making the excess royalty share payment, a 1/16th share, to the owners of the mineral estate who were burdened by the plaintiff's non-participating royalty interest. If so, pursuant to Gavenda, the operator was not unjustly enriched, and according to traditional theory, should not have been liable for the period prior to plaintiff's revocation of the division order.

II.

The Duty of Care the Executive Right Owes to the Non-Participating Royalty Owner

The problem that peculiarly haunt non-participating royalty interests to a fraction of royalty is that the owners of such interests do not participate in the leasing of the land which determines the quantum of lease royalty that they will receive from production. The owner of the executive right to the mineral estate negotiates and executes the oil and gas lease which fixes the amount of bonus, delay rentals and royalty to be paid under the lease. Thus, absent a judicial standard regulating the conduct owed by the owner of the executive right to the non-participating royalty owner, the latter would be at the mercy of the former as to the share of royalty he will receive under the lease.

Typically, but not always, the owner of the mineral estate burdened by the non-participating royalty interest owns the executive right, as well as the right to the bonus and delay rental payments. Additionally, the mineral owner may also own
the remaining share of royalty, if any, which has not been severed by prior non-participating royalty conveyances. An inherent conflict will exist between the mineral owner who owns no interest, or a partial interest in the royalty and the non-participating royalty owner over the negotiation of the lease terms. The non-participating royalty owner wants the maximum lease royalty. The mineral owner, however, has the incentive to negotiate for a reduced lease royalty to maximize bonus and delay rental payments. Likewise, looking for a future leasing opportunity and an additional bonus, the mineral owner may bargain for a lower royalty to obtain a shorter primary term. Finally, if the mineral owner also owns the surface, the lease royalty may be sacrificed for surface damage or non-development clauses.

The protection of the non-participating royalty owner lies in the standard of care imposed on the owner of the executive interest in negotiating lease benefits on behalf of the executive and non-executive interests. The evolution of that standard has not been uniform or without controversy. The prevailing standards have been the traditional "utmost fair dealing," sometimes referred to as the "prudent landowner" standard, and the "fiduciary standard" originating in the 1985 Texas case of Manges v. Guerra.

A. The Utmost Fair Dealing Standard

The "utmost fair dealing" standard measures the duty the mineral owner owes to the non-participating royalty owner in executing the oil and gas lease. This standard is what a "reasonable prudent landowner" owning the full mineral fee, and not burdened by the outstanding non-participating royalty interest, would have done under the circumstances. The "utmost fair dealing" standard has traditionally been viewed as an intermediate standard between an unduly high fiduciary duty and an insufficiently low duty of good faith. The "utmost fair dealing" standard is premised on an implied covenant in the deed that severs the non-participating royalty interest from the mineral estate.

The standard implicitly recognizes that a mineral owner burdened by a fraction of non-participating royalty is entitled to pursue his self-interest in negotiating the bonus, delay rentals and other advantageous lease terms. The mineral owner is not obliged to subordinate his interest to the interest of the non-participating royalty owner. However, the mineral owner cannot unduly benefit at the expense of the non-participating royalty owner in exercising the executive right.

The extent that the mineral owner can act in pursuing his
self-interest at the expense of the non-participating royalty owner is limited by the "prudent landowner" standard. If the reasonable prudent landowner, not burdened by the outstanding interest, would have negotiated the same deal that the mineral owner negotiated, the mineral owner bears no liability. However, if that reasonable prudent landowner negotiates a deal more favorable to the royalty owner, the mineral owner is liable.79

In sum, the "utmost fair dealing" standard examines the fairness of the lease royalty share to the non-participating royalty owner in relation to the other lease benefits obtained by the mineral owner. This standard is what an objective reasonable "prudent landowner," owning the full mineral fee, would have bargained for.80

The "utmost fair dealing" standard is criticized for failing to provide adequate guidance and predictability in determining whether the mineral owner in rejecting or accepting a lease proposal will violate the standard. For example, assume that a mineral owner who owns no royalty is offered two lease proposals. The first is an offer to lease for a $500 dollar per acre bonus and a 1/8th royalty. The second lease offer is for a $250 per acre bonus and a 3/16th royalty. The nearest production is one mile away and two dry holes have been drilled on the tract over 30 years ago. The well logs on the old dry holes are missing, if they ever existed. Seismic operations have been conducted in the area but the data is confidential to the proprietor and unavailable to the mineral owner. What's an objective "prudent landowner" owning the full mineral fee to do? How does a lawyer advise the mineral owner who desires to make the right decision, i.e., take the $500 per acre bonus, but who also wants to avoid the reasonable likelihood of litigation and, more importantly, the possibility of liability?

A commonly expressed view is that if the lease royalty negotiated by the executive is equal to the going royalty rate in the area, no violation of the "utmost fair dealing" standard will likely occur.81 Conversely, a lease royalty of less than the going rate in the area portends a violation of the standard. Under these circumstances, the "utmost fair dealing" standard may reflect reality if all influences on leaseg terms in the area are equal, i.e., the primary term offered, the desirability and availability of surface damage or non-development clauses, and if all lands in the area are reasonably in equal proximity to drilling operations or production. Any change in any of the above facts may affect the royalty bargained for by an executive as to any particular tract. Thus, th royalty share negotiated by landowners in the area is not dispositive, nor necessarily relevant, to the royalty share that the "prudent landowner" would have bargained for. Perhaps, the more accurate statement of conventional wisdom is that a lease royalty that is less than the going lease royalty rate should foreshadow litigation.
Another criticism of the prudent landowner standard is that it is inherently inconsistent. The standard permits the executive to pursue his self interest, however, in pursuing that self interest he cannot benefit himself at the expense of the non-executive. Even though the apparent inconsistency may render the standard difficult to apply, the reason the standard emphasizes both the mineral owner's self interest and protection of the non-executive, is simple to explain. The mineral owner owns the right to the bonus, and like any other rational property owner, he should be free to secure the maximum return obtainable from his property. However, he also negotiates the lease royalty share for the non-participating royalty owner. Thus, some limitation on the mineral owner's right to pursue his self interest to the detriment of the non-participating royalty owner in the exercise of the executive right is required. The "prudent landowner" standard, i.e., the "utmost fair dealing" standard, attempts to balance the irreconcilable interests of the mineral owner and the non-participating royalty owner.

Finally, the standard is viewed by some as being insufficient to protect the interests of the non-executive owner from the rapacity, or lack of altruism, of the owner of the executive interest. The executive owner controls the interests of the non-executive and determines their share in the lease benefits. Therefore, a more stringent standard of care than that reflected in the "utmost fair dealing" standard should be imposed on the executive, regardless of the whatever proprietary interest the latter may also have in the mineral estate.

B. The Fiduciary Duty

Manges v. Guerra held that the owner of the executive right to a non-participating mineral interest, who also owned a share of the mineral estate, owed a fiduciary duty to the non-executive interests. Manges, the executive, violated the fiduciary duty by leasing in excess of 25,000 acres to himself for a ten year primary term, at a nominal bonus ($5 inclusive), $2 per acre annual delay rentals and a 1/8th royalty. By the lease, Manges acquired the 7/8ths working interests. Shortly thereafter, Manges farmed-out the lease to a third-party, retaining a 50% of the working interest, cost-free.

The fiduciary duty recognized in Manges is specifically based on the relationship of the parties, and not on a contract implied in the deed. The fiduciary duty imposed in Manges required the executive to acquire for the non-executive every benefit that he exacts for himself. Manges through his self-dealing, gained "special benefits." The 7/8 working interest from the Manges to Manges lease and the 1/2 cost-free working interest
from the farm out were not shared with his non-executives. In addition to actual damages, the non-participating mineral owners were entitled to cancellation of the Manges to Manges lease and exemplary damages. However, their election to sue for damages precluded the remedy of cancellation of Manges' executive right.

The extent to which Manges elevated the standard of care owed by the executive to the non-executive in the management of the mineral estate is unclear. A fiduciary duty implies a more stringent standard than exists under the "utmost fair dealing" standard. The fiduciary standard implicitly suggests that the executive's right to pursue his own self interest is limited or proscribed.

However, the fiduciary duty was imposed in Manges under circumstances in which a cotenancy existed in the mineral estate between the executive and non-executive interests. Manges owned an undivided 1/2 mineral estate and the executive right to the 1/2 non-participating mineral estate. The fiduciary duty required the executive to acquire for the non-executive every benefit that he exacted for himself. The procurement of benefits that profit only the executive interest incurs liability. The pursuit of self interest by the executive at the expense of the non-executive is actionable. But, a fiduciary duty requiring participation on a proportionate ownership basis in all the lease benefits is appropriate when the executive and non-executive interests share a cotenancy relationship in the mineral estate. There is no necessity to recognize or protect the pursuit of self interest that results in a division of lease benefits unrelated to the proportional ownership interests.

When a mineral owner burdened by a fraction of non-participating royalty interest exercises the executive right, both parties do not share on a proportional ownership basis in all the lease benefits. The relationship is unlike the cotenancy relationship in Manges. The mineral owner is entitled to the bonus, delay rental payments and only a partial share, if any, of the lease royalty. The non-participating royalty owner participates only in his share of lease royalty. Thus, the mandate of the fiduciary duty in Manges, the acquisition of identical benefits for the non-executive when the executive negotiates the lease, cannot be applied when the non-executive is a non-participating royalty owner.

That does not mean, however, that Manges has not raised the standard of care that the mineral owner owes to the non-participating royalty owner. Rather than the contractual basis as the source of the duty owed, it is now the relationship of the parties from which the duty arises. The remedies, such as exemplary damages and lease cancellation, that accompany the fiduciary standard, and that were applied in Manges, are more
drastic. The exact standard the fiduciary duty imposes on the mineral owner exercising the executive right to the non-participating royalty interest has been the subject of some speculation. One view is that the fiduciary duty prohibits the executive from "acting against the non-executive's interest" and requires him to "act affirmatively to protect the non-executive's interest." Another view is that the executive is analogous to a "trustee" who is also the "life beneficiary" of the trust, "who can take his own interest into account in making decisions when administering the trust... but cannot take unfair advantage... by making decisions that... substantially disadvantage or effectively destroy the remainder interest." Under the latter view, the executive would be entitled to take his own interest into account, the right to bonus and delay rentals, so long as his decisions were in good faith and did not substantially disadvantage the royalty owner.

Hopefully, if Manges elevated the standard of care that the mineral owner owes to the fraction of non-participating royalty interest in the exercise of the executive right, the new standard will not unduly limit or proscribe the mineral owner's self interest in negotiating the lease bonus, delay rentals and other lease benefits, such as a surface damages. Requiring the mineral owner to subordinate his interest to a reasonable bonus or surface damage protection will diminish his property interest and violate the intent of the parties to the deed of severance.

Despite the uncertainty that lingers as to the effect of Manges on the standard of care, no one doubts that the case has obviously expanded the remedies available to the non-executive, including the non-participating royalty owner. The remedies are now premised on a breach of the fiduciary duty, as opposed to a breach of the implied contract of the "utmost fair dealing" standard. Exemplary damages, cancellation of either the lease or the executive right, or both, imposition of a resulting or constructive trust, all familiar to the law of fiduciaries, are now applicable.

However, the Texas Civil Appellate Courts have not read Manges as dictating a wholesale riddance of the "utmost fair dealing" standard with its prudent landowner test. Emphasizing that Manges did involve cotenants to a mineral interest where the executive owner determined by leasing the share of royalty, bonus and delay rentals received by the non-participating mineral owners, the appellate courts have limited the fiduciary duty of Manges to instances in which the executive "controls" the amount of lease benefits received by a non-executive owner. Thus, the fiduciary duty of Manges is imposed on the mineral owner with the executive right to a fraction of non-participating royalty and mandates, at least, that the owner of the latter interest receive their proportionate share in whatever royalty is obtained by the executive in the lease negotiation. However, the
fractional share royalty interest, which is entitled to its fixed fractional share regardless of the size of the lease royalty, is protected by the "utmost fair dealing" standard of the prudent landowner test.97

Mims v. Beall98 is an illustrative case. In that case, the plaintiffs owned a 1/4th of non-participating royalties with John Mims and his wife, Chattie, owning the executive right. The Mimses executed an oil and gas lease to their son, Angus Mims, that provided for no bonus and a 1/8th royalty. Subsequently, five months later, Angus Mims assigned the lease to a third-party in return for a 1/16th overriding royalty. Plaintiffs, contending that the 1/8th royalty in the Angus Mims lease was unreasonably low, sued John and Chattie Mims and Angus Mims for damages occasioned by the breach of the duty owed by the executive to the non-executive in the Mims to Mims lease. Finding that the "duty of good faith and fair dealing" was breached, the trial court awarded actual damages against the Mimses. Also, for "participating in the breach," the court assessed actual damages against Angus Mims. A constructive trust was imposed on the non-participating royalty owner's share of the overriding interest in the third-party lease. Further, finding that both parties acted in an "unconscionable, willful and wanton manner and in total disregard of the plaintiffs' rights" exemplary damages of $2500 were assessed against the Mimses and $5000 against Angus Mims.

On appeal, both defendants argued that no fiduciary relationship between the Mimses and Beall existed. The Court rejected that argument and held that the fiduciary standard of Manges applied because the exercise of the executive right "controlled" the amount of royalty that the fraction of non-participating royalty interest receives under the lease. The executive violated the fiduciary obligation in executing the Mims to Mims lease in several respects: engaging in "self dealing" which includes parents dealing with a son; failing to negotiate at arms length for current market terms; and, as consequence of the self-dealing, the son's overriding royalty interest reserved in the third-party lease was treated as if it were owned by the parents, resulting in the executives having exacted a royalty share for themselves which was not shared with the non-participating royalty owner. The award of actual and exemplary damages against the executives, the Mimses, as well as the imposition of the constructive trust on the overriding interest, was affirmed.

**The Lessee's Liability for Inducing or Participating in the Breach of the Standard of Care**

Mims v. Beall is instructive on the potential for a lessee
to incur liability in the leasing transaction in which the mineral owner with the executive right violates the requisite standard of care owed to the non-executive interest. Angus Mims, the son, the lessee to the lease in which the executives, his parents, violated the fiduciary duty to the non-participating royalty owners, did not owe a fiduciary duty to the non-participating royalty owners. However, the lessee was liable to the non-executive interest for "knowingly participating" in the breach of the executive duty. Thus, the award of actual and exemplary damages against the lessee was affirmed. Further, the executive who breaches the standard of care owed to the non-executive and the lessee who induces or participates in that breach are jointly and severally liable.

The general rule of liability for the lessee who takes a lease from an executive subject to a non-executive interest was stated in Mims v. Beall:

"So long as the lessee maintains an arm's length position in the transaction, he does not owe a fiduciary duty or a duty of utmost good faith to the owner of the non-executive interest. If, however, the lessee agrees with the executive to an arrangement made for the purpose of excluding or minimizing the benefits of an outstanding or non-participating interest owner, the lessee can be held liable to the injured third party."99

Thus, if the lessee either "induces" the executive to breach the standard of care or "knowingly participates" in the breach, i.e., agrees with the executive to an arrangement for the express purpose of lessening the non-executive's lease benefits, the lessee is liable to the non-executive interest.

More importantly, the Court indicated that the lessee may also be liable if he should reasonably have been aware that the executive was acting in breach of his duty. As to this basis of liability, the Court further noted that the fact that the non-participating royalty deed is recorded puts the lessee on constructive notice of the existence of the non-participating royalty owner.

One lesson of Mims v. Beall is that the lessee can avoid liability while negotiating a lease from a mineral owner burdened by a non-participating royalty owner. The fundamental premise of the decision is the lessee does not owe a fiduciary duty or a duty of utmost fair dealing to the non-participating royalty owner. So long as the lessee maintains the negotiations with the executive owner at arms length, and secures a lease from the executive that are competitive with current market conditions, including the royalty prevailing in the area, the lessee should avoid liability.
What the lessee cannot do is to "induce" the executive to violate the duty of care owed to the non-participating royalty owner. "Induce" clearly encompasses "planting the seed in the mind" of the executive that the two should cut a deal that breaches the duty. However, the mere offer of a lower than prevailing royalty and a higher than customary bonus as a special incentive for the executive to grant the lease may well constitute "inducement" and incur liability. Also, the lessee cannot "knowingly participate" in the executive's perpetration of the breach of the duty on the non-executive. The lessee cannot agree with the executive to a royalty share that has the express purpose of excluding or lessening the non-participating royalty owner's royalty share.

What is unsettling about Mims v. Beall is the dicta that indicates that the lessee may be liable if he should have reasonably been aware that the executive was acting in breach of his duty. The lessee's knowledge of the existence of the non-participating royalty interest may be based on constructive notice that is based on the non-participating royalty deed being recorded. Thus, if a lease is taken on the basis of a superficial title search which does not determine the existence and extent of non-participating royalty interests, but only focuses on the ownership of the executive right, the lessee, if the dicta ultimately prevails as law, may be found liable to the non-participating royalty owner for agreeing to such lease terms as an unusually low royalty or an overriding royalty interest that expressly denominated in the lease as bonus.

Conclusion

Non-participating royalty interests should incite caution to the lawyer and the landman. The difference between a fraction of and a fractional share royalty interest involves a distinction with a difference. Older royalty conveyances have created a wealth of interpretation problems and array of inconsistent and often puzzling case law. Care must be exacted in construing royalty deeds to determine if a fraction of or a fractional share royalty has been conveyed. Finally, the duty that the mineral owner owes to the fraction of non-participating royalty owner in negotiating the oil and gas lease is becoming more stringent in its substantive content and more drastic remedies are available for its breach. Even though the lessee owes no duty to the non-participating royalty owner in the lease negotiations, care must be exercised to avoid "inducing" or "knowingly participating" or "should have known that you were participating" in the executive's breach to avoid the imposition of liability, including the possibility of punitive damages and lease cancellation.
1. A non-participating royalty interest may be created by grant or by reservation. To facilitate the discussion, the terms will be used interchangeably.

2. A non-participating royalty interest may be for a fee, term or defeasible term. For a discussion of term and defeasible term royalty interests, see, Norvell, "Defeasible Term Mineral and Royalty Interests", 24th Annual Arkansas Natural Resources Law Institute (1985). Also, for an examination of the non-participating royalty deed form that has been traditionally utilized in Arkansas, see, Clegg, "The Arkansas Royalty Deed: Questions and Answers," 21st Annual Arkansas Natural Resources Law Institute (1982).


5. Id.

6. Id.


8. Williams v. Meyers, supra n. 2 at § 327.2.

9. Id.


11. Miller v. Speed, 248 S.W.2d 250 (Tex. Civ. App. 1952). See also, Hanson v. Ware, 224 Ark. 430, 431, 274 S.W.2d 359, 361, wherein the granting clause to a 1919 royalty deed conveyed a "one-sixteenth part of all oil and gas produced and saved."

12. Karaker v. Unknown Heirs, 434 P.2d 282 (Okla. 1966). In Karaker, the Court was construing a reservation in a 1924 deed. The sole issue was whether the reservation reserved a 1/16th of gross production or only a 1/16 of a 1/8th royalty. The Court found the reservation ambiguous. Moreover, the court admitted into evidence a 1926 oil and gas lease that provided that the lease royalty was to be divided (1/2) equally between the grantor and grantee of the deed. The court held that the reservation was
to a 1/16th of gross production as a non-participating royalty. In reaching this result, the Court emphasized that the reservation stated 1/16 royalty of any oil and gas produced, as opposed to 1/16 of any royalty interest, noting that a distinction exists between the term "royalty" and "royalty interest."


14. See, Helms v. Guthrie, 573 S.W.2d 855 (Tex. Civ. App. 1978) wherein dicta noted that a grant of "one-fourth (1/4th) of the royalty" conveyed a "fraction of royalty" and the ultimate share of production accruing to the interest was "determinable upon the execution of some future lease." Id. at 857. The grantee received 1/4th of the 1/8th lease royalty as well as 1/4th of 1/16th of the 7/8 overriding royalty reserved in a subsequent oil and gas lease.

15. "It is accepted convention that "of" is the same as times in a multiplication formula". W.D. Masterson, Jr., 6 Oil & Gas Reporter 1372 (1956), discussing Minchen v. Hirsch, 295 S.W.2d 529 (Tex. Civ. App. 1956), writ of error refused.


19. Helms v. Guthrie, 575 S.W.2d 855 (Tex. Civ. App. 1978), reh'g denied. In Helms, the grantee in the deed sued to recover a 1/16th share of a 1/16th of 7/8ths overriding royalty interest that had been reserved in the lease in addition to the 1/8th royalty share. In Texas, as noted in the case, overriding royalty is royalty. The Court held that Helms was only entitled to a 1/16th of gross production. The Court observed that "Helms owns a 'fractional royalty' of 1/16th of total production, not a 'fraction of royalty,' determinable upon the execution of some future lease."

20. Ernest E. Smith, supra n. 16 at G-1.

21. Id. at G-2.


23. To facilitate the discussion, the parties will be, as in the appellate court opinion, referred to as the principals, Lindsey, Roberts, and Mabee, as opposed to their successors-in-interest.
24. To facilitate the understanding of the case, the calculation of the lease royalty shares pursuant to the theories of the different claimants appears below.

Lindsey, the plaintiff, claimed a 1/4 of the 3/16 royalty, or 3/64 of gross production. He recognized the defendant, Mabee, as owning 3/4 of 3/16 or 9/64ths of gross production while Roberts, the intervenors, pursuant to his theory, was entitled to no royalty.

Mabee, the defendant, claims it is entitled to all royalty reserved under any lease in excess of 1/4th of 1/8th (1/32nd), with the ownership of the 3/16th lease royalty lease being as follows: Lindsey, 1/4th of 1/8th = 1/32nd share of gross production and Mabee, a full 3/16th minus Lindsey's 1/32nd share, entitling him to 10/64ths. Roberts, again, was entitled to no royalty.

Roberts, the intervenor, claimed 1/4th of any royalty in excess of 1/8th reserved on any lease (1/4th of 1/16th, or 1/64th). She recognized Lindsey was entitled to 1/32nd of gross production and Mabee was entitled to 3/4ths of 3/16th or 9/64ths of gross production.

25. 575 S.W.2d at 331.


27. The Court notes that Roberts conveyed a 3/4th mineral interest to Mabee. As to the remaining 1/4th mineral interest she conveyed to Mabee the executive right, the right to bonus and delays. Thus, she owned the 1/4th mineral interest short of the executive, delay rentals, bonus and a 1/8th of royalty. Note that despite the fact that most of the incidents of ownership of her 1/4th non-participating mineral estate, deprived of bonus, delay rentals, and 1/8th royalty, she only shares in any benefits of mineral ownership in the event the lease royalty is in excess of 1/8th.

28. In Remuda Oil Co. v. Wilson, 264 S.W.2d 192 (Tex. Civ, App. 1954), reh'g denied, the Court construed a royalty deed that granted a 1/4th of non-participating royalty as conveying only a 1/4th of 1/8th royalty. The 1/4th of royalty deed contained, following the legal description, a clause referring to a prior deed "for all purposes." The prior deed was the source of the grantor's title that reserved to the grantor only an "undivided 1/2 of 1/8th royalty." Subsequently, an oil and gas lease was executed providing for a variable royalty, a 1/4th royalty that under certain circumstances would increase to a 7/16ths royalty. The holding that the 1/4th of royalty deed conveyed only a 1/4th of 1/8th royalty was based on: (1) the usual lease royalty is a 1/8th royalty share; and (2) it would be unjust to construe the deed to convey a 1/4th of royalty when the grantor only owned a
1/2 of 1/8th royalty, which is less than a 1/4th of royalty share to the potential 7/16th lease royalty. Therefore, the reference to the prior deed "for all purposes" referred to the 1/2 of 1/8th royalty share owned by the grantor and disclosed the intention to convey to the grantee 1/4th of that 1/8th royalty.

Although Remuda Oil Co. is the converse case, a 1/4th of royalty is being construed as a 1/4th of 1/8th royalty, the decision is representative of an instance in which specific language in a deed, though not uncommon, or unusual circumstances, may result in an interpretation of fractional share or fraction of royalty that differs from the traditional construction of such deeds or reservations.

29. 593 S.W.2d 939 (Tex. 1980), reh'g denied.

30. The royalty to be paid on the pre-existing gas well was also an issue. Havard alleged that Brown was also only entitled to 1/16th of the proceeds from the gas well. Brown contended that he was entitled to 1/2 of the gross production from the gas well and 1/2 of the 3/8ths royalty from the M-Tex well. The jury, based on extrinsic evidence, held that Brown was entitled to 1/16th of the production from any well. The trial judge, finding the deed unambiguous, entered a Judgment notwithstanding the verdict or (JNOV) that held that Brown was entitled to 1/2 of the production from the gas well and 1/2 of the 3/8ths royalty from the M-Tex lease. The Court on appeal held the the deed was ambiguous, in part, because Brown was awarded 1/2 of gross production from the gas well but only 1/2 of the 3/8ths royalty from the M-Tex wells. The dissent rejected the view that the difference in the trial judge's award as to the share of production from the gas well and the oil wells as a basis finding an ambiguity. The dissent noted that Havard was the operator and owner of the gas well and, more importantly, the judge's verdict as to the 1/2 share of gross production from the gas well was derived from a pre-trial stipulation made by the parties that agreed to that division of the production from that well. Because of the stipulation as to the division of the gas well production, my analysis of the case will only consider the issue as to the division of the 3/8ths M-Tex lease royalty in order to facilitate and simplify the discussion.

31. The specific language of the majority opinion on the possible construction of the parenthetical phrase, "Being equal to, not less than an undivided 1/16th," is as follows:

"The parenthetical language itself is subject to more than one interpretation. One interpretation is that the parties intended to reserve 1/2 of the conventional 1/8th royalty, "being equal to" a 1/16th. The additional phrase "not less than" insured that the reservation was 1/2 of the conventional 1/8th royalty,

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and if the royalty were reduced, the Browns would still receive their 1/16th. On the other hand, the parenthetical language can be construed, as urged by the Browns, to reserve 1/2 of the royalties contained in future leases, providing further that such share must not be less than 1/16th. Such a construction must ignore the presence of the "comma" between the phrase "Being equal to" and the phrase "not less than an undivided 1/16th." 539 S.W.2d at 942.

32. Id. at 946.

33. See, Ernest E. Smith, supra n. 10 at G-4.

34. 263 Ark. 731, 567 S.W.2d 295 (1978).

35. Id. at 263 Ark. 731, 733. 567 S.W.2d 295,296.


37. Harris v. Ritter, 154 Tex. 474, 279 S.W.2d 845 (1955); Richardson v. Hart, 143 Tex. 392, 185 S.W.2d 563 (1945) reh'g denied.


39. 705 S.W.2d 690 (Tex. 1986), reh'g denied.

40. Arnold v. Ashbel Smith Land Co., 307 S.W.2d 818 (Tex. Civ. App. 1957), reh'g denied, provides another example of a large fractional share royalty. The case involved the construction of reservation of a 49 year term royalty in which the first clause provided:

"Grantor expressly reserves unto itself, its successors and assigns, a one-fourth royalty in all oil, gas and other minerals in and under or hereafter produced ... ."

The last clause of the reservation indicated that the grantor's reservation was non-participating as to the executive right, bonus and delay rentals. At the end of this clause was the following language:

"... but if oil, gas or other minerals be produced in commercial quantities, then Grantor, ... shall during the term and existence of such reserved royalty, have and receive one-fourth part of such oil, gas and other minerals so produced as a royalty." (Emphasis added).
The successors-in-interest of the grantees, the plaintiffs, argued that the reservation created a 1/4th fraction of royalty, as opposed to a 1/4th fractional share royalty. Plaintiffs argued that if a "comma" after the language "so produced" and before the language "as a royalty", the words "so produced" would modify "produced in commercial quantities," and the words "as a royalty" would modify "one-fourth part of such oil, gas and other minerals. Thus, the construction would be "1/4th royalty part of production," or a 1/4th of royalty. The Court observed that the "comma" could be inserted if necessary to arrive at the intent of the parties. However, reading the language at issue along with the entire reservation, the language was clear and unambiguous. As to the grammatical construction, the Court noted that the words "so produced" and "as a royalty" followed the same sequence as their respective antecedents. Further, if the grantors were only to receive "1/4th of royalty, there would be no reason for the inclusion of the article "a" that immediately preceded the word "royalty." A 1/4th fractional share royalty was reserved.


42. The division order has historically authorized the purchaser of production, or the operator who disburses the proceeds of production, to receive the production and to distribute the proceeds from the sale pursuant to the specified division of interest. Traditionally, if the proceeds are distributed pursuant to the division of ownership interest specified in the executed division order, an interest owner is estopped to assert a claim against the purchaser or operator for an inadequate payment. Dale v. Case, 217 Miss. 298, 64 So.2d 344 (1957); Exxon Corp. v. Middleton, 613 S.W.2d 240 (Tex. 1981). See, also, 4 Williams and Meyers, supra n.2 at § 704.5 for a citation to other authorities.

In Gavenda the Supreme Court of Texas is holding that the estoppel arising from reliance on the division of ownership interest specified in the division order only precludes liability when the overpayment is made to a third-party and is not retained by the party disbursing the proceeds of production.

43. The "subject to" and "future lease" clauses and the problems of interpretation resulting from conflicting fractions appearing in the various clauses, typically arising from a misunderstanding of the difference between a mineral and a royalty estate, including an analysis of the Texas cases and the infamous "two grant" or "multiple grant" constructions, have been the subject of a number of law review articles. See, Laura H. Burney, The Regrettable Rebirth of the Two-Grant Doctrine in Texas Deed Construction, 34 S.Tex.L.Rev. 73 (1993); Tevis Herd, Deed Construction and the "Repugnant to the Grant" Doctrine, 21 Tex. Tech.L.Rev.635 (1990); Bruce Kramer, The Sisyphean Task of Interpreting Mineral Deeds and Leases, 24 Tex. Tech. L. Rev. 64.


45. *Harris v. Currie*, 142 Tex. 93, 176 S.W.2d 302 (1943), reh'g denied.

46. *Heven v. Harnett*, 235 Kan. 117, 679 P.2d 1152 (1984), a 1984 Kansas Supreme Court case, best illustrates the problem. The Court was construing a 1925 mineral deed in which the granting clause conveyed a 1/16th mineral estate and the subject to clause provided:

"if the land is covered by a valid mineral lease, the grantee ... shall have an undivided 1/2 interest in the Royalties, Rentals, ... ."

Plaintiff, the successor-in-interest of the grantee, argued that the deed was unambiguous, conveyed a 1/16th mineral interest, as specified in the granting clause, that only entitled the defendants, the successors-in-interest of the grantees, an undivided 1/16 of the royalties to a subsequent lease. The plaintiff further argued that the "subject to" clause only provided for 1/2 of royalties if the land was then subject to an existing oil and gas lease, and, because their was no such lease, that contingency failed, rendering that clause inapplicable to convey any interest in royalties under subsequent leases. The defendant argued that the deed was ambiguous and conveyed a 1/2 mineral estate entitling them to 1/2 of the royalties to be paid under the subsequent lease. Finding the deed ambiguous, admitting extrinsic evidence that indicated that the parties had subsequently treated the conveyance as conveying a 1/2 mineral estate, the Court held that the deed conveyed a 1/2 mineral estate. In so doing the Court made the following observation:

"It is not uncommon for parties to mineral deeds or reservations, where a royalty or mineral interest is conveyed or reserved subject to an existing oil and gas lease, to confuse the fractional interest conveyed or reserved.

"As the most common leasing arrangement provides for a one-eighth royalty reserved to the lessor, the confusion of fractional interests stems primarily from the mistaken premise that all the lessor-landowner owns is a one-eighth royalty. In conveying minerals subject to an existing lease and also assigning a corresponding fractional interest in the royalties received, mistake is often made in the fraction of the minerals conveyed by multiplying the intended fraction by one-eighth. Thus, if a conveyance of an undivided one-half of the
minerals is intended, the parties will multiply one-half by one-eighth and the instrument will erroneously specify a conveyance of one-sixteenth of the minerals upon the assumption that one-sixteenth is one-half of what the grantor owns. An ambiguity is created because the instrument will also show that the conveyance of one-sixteenth of the minerals is meant to entitle the grantor to one-half of the royalty. Of course, an undivided one-half of the minerals is needed to carry one-half of any royalties reserved." 235 Kan. 117, 124, 679 P.2d 1152, 1158.

47. The "two grant doctrine" originated in the early Texas case of Hoffman v. Magnolia Petroleum Co., 273 S.W.2d 828 (Tex. Comm. App. 1925) in which 90 acres in fee were severed by deed from a 366 acre tract that was subject to an outstanding oil and gas lease. The "subject to" clause in the deed provided, inter alia, that the grantee was to receive "1/2 of all oil royalty and gas rental or royalty due to be paid under the terms of said lease." (Emphasis added.) The Court construed the deed as executing two conveyances. One was the conveyance of the 90 acre tract in fee. The second conveyance, effectuated by the "subject to" clause, conveyed 1/2 of the royalties under the existing lease as to the entire 366 acre tract. The Court reasoned that the "subject to" clause covered 1/2 of the royalty from the "said lease" and was not restricted to royalties accruing from production on the 90 acre tract. The construction in Hoffman has been universally condemned. The likely intent of the parties in inserting the "subject to" clause was to avoid Caruthers to ensure that the grantee received 1/2 of the rentals and royalties as to the 90 acre tract that was conveyed. It seems unlikely that the parties would have utilized the "subject to" clause to convey 1/2 of the royalties under the entire 366 acre tract.

For a discussion of the origin and applicability of the "subject to" clause, including Hoffman and the "two grant" theory prior to Luckel v. White, discussed infra, see, Ernest E. Smith, supra n. 43. For a discussion that covers Hoffman and the Texas cases through Luckel v. White and Jupiter Oil Co. v. Snow, also discussed infra, see, Laura H. Burney, supra n. 43 at 89-105, and Bruce M. Kramer, supra n. 43 at 19-43.

48. Richardson v. Hart, 143 Tex. 392, 185 S.W.2d 563 (1945) reh'g denied, illustrates the applicability of the two grant doctrine. The Texas Supreme Court held, inter alia, that a deed with a the granting clause purporting to convey a 1/16th of 1/8th mineral interest and a subject to clause reciting that it "covers and includes 1/16 of 1/8 of all the oil royalty" conveyed two distinct grants. (Emphasis added.) The granting clause conveyed a 1/16th of 1/8th or a 1/128 minerals interest and the "subject to" clause also conveyed a 1/16 of 1/8th of royalty or a 1/1024th of gross production. The fact that the first grant, the 1/128th mineral interest, due to the existence of a lease with a 1/8th
landowner's royalty, would entitle the grantee to a 1/1024 share of production, which is the same as the royalty share granted in the subject to clause, was irrelevant as to the reality of the "two grants." Referring to the grant in the subject to clause, the Court observed:

The fact that it fixes the share in the present royalties the same as would have obtained by operation of law does not lessen its force and effect as a conveyance. As is often the case such payment of royalty might have been larger or smaller than a pro rata share. 43 Tex. at 393, 185 S.W.2d 564.

In addition to Richardson, the other "two grant" theory cases that appeared after Hoffman v. Magnolia, supra n. 47, are Benge v. Scharbauer, 152 Tex, 447, 259 S.W.2d 166 (1953) and Woods v. Sims, 154 Tex. 59, 273 S.W.2d 617 (1954) which, like Hoffman, are factually unrelated to disparate fractions in the granting, "subject to" or "future lease" clause. For a discussion of these cases, see the citations at supra n. 47.

49. Garrett v. Dills Co., 299 S.W.2d 904 (Tex. 1957) is viewed by some commentators as a milestone case that departed from the "two grant" theory in favor of the "four corners" rule of construction. The case involved the misconception of the difference between fractional shares of mineral and royalty interests. The granting clause purported to convey an "undivided 1/64th interest in the minerals" while the subject to clause included "1/8th of any royalties and 1/8th of said money rentals payable by the lessee." The future lease clause provided that the grantee would own

"1/8th of the lease interests and all future rentals ..., he owning one-eighth of one-eighth of all oil, gas and other minerals...together with one-eighth interest in future rents."

The lease in existence expired and a subsequent lease was executed that provided for a 1/8th royalty. The issue presented was whether the grantee was entitled to 1/64th of royalty or a 1/64th royalty share under the subsequent lease.

The Supreme Court in a divided opinion held, inter alia, that the deed conveyed a 1/8th of the minerals entitling the grantee to 1/8th of the royalty, or a 1/64th royalty share. The majority construed the deed from its "four corners," viewing all of the clauses collectively, to ascertain the intent of the parties. First, the majority noted that the granting clause purported to convey a 1/64 mineral interest. However, the "subject to" clause indicated that the parties understood a 1/64th of the minerals to embrace a 1/64th royalty or 1/8th of the 1/8th royalty. The language of the "future lease" clause that the grantee would own 1/8th of 1/8th of the minerals
reflected the intent to convey a 1/8th of the royalty under future leases. Further, the language in the latter clause that the grantee acquired "1/8th of the lease interest and future rentals" indicated that the grantee had the right to lease an undivided 1/8th interest and to receive 1/8th of the bonus and rentals. In essence, the parties intended that the grantee was to share in the same royalty under future leases as the existing lease and was conveyed a 1/8th mineral interest.

For a more detailed analysis of Garrett as applying the "four corners" rule of construction and, more importantly, rejecting the "two grant" theory, parties, see, Laura H. Burney, supra n.43 at 95-106.


51. 671 S.W.2d 870 (1984), reh'g denied 1984.

52. Although the dissent did not elaborate on the "good reason," I would speculate that a 1/16th mineral estate subject to a lease that yields (or may yield) a 1/16 of 1/8th royalties may be of equal or greater value to an undivided 1/2 mineral estate after the lease expires when prospective royalties, or bonuses, are speculative.

53. The opinion also cited and endorsed Garret v. Dills, supra n. 49, 671 S.W.2d at 876.

54. See Burney, supra n. 43 at 93.

55. During its short reign, the rule was applied in two appellate cases. In Hawkins v. Texas Oil and Gas Corp., 724 S.W.2d 878 (Tex. Civ. App. 1987), the granting clause conveyed a 1/32nd fractional share royalty while the "future lease" clause specified a 1/4th mineral estate. The granting clause conveyed a 1/4th of 1/8th royalty and the future lease provision specified a 1/4th mineral estate upon termination of the existing lease. Alford was followed and the granting clause prevailed resulting in the deed only conveying a 1/32nd royalty share. Hawkins provides a detailed and lucid account of the evolution of the "two grant" and "repugnancy to the grant" theories. In Stag Sales Co. v. Flores, 697 S.W.2d 493, the granting clause specified a 1/2 of royalty while the "subject to" and "future lease" clause specified a 1/16th royalty. The subsequent oil and gas lease provided for a 1/6th landowner's royalty. Following Alford, the granting clause prevailed, thus, the deed conveyed a 1/2 of royalty entitling the grantees to a 1/12th production share.


57. The deed also contained a clause that recited that it was "understood... that Mayes is the owner of 1/2 of the royalties to be paid under the terms of the present existing lease, the other
1/2 having been previously transferred by her to her children, and by the execution of this instrument, ... Mayes conveyed 1/2 of her 1/16th royalty now reserved by her." \textit{Id.} at 461.

58. That conclusion that \textit{Luckel v. White} represents a return to the "two grant" mode of construction by the Texas Supreme Court is reinforced by \textit{Jupiter Oil Co. v. Snow}, 819 S.W.2d 466 (Tex. 1991), \textit{reh'g denied} (1992), a case decided the same day as \textit{Luckel}. There, the issue involved the construction of a 1918 mineral deed that had been executed when the land was then subject to an oil and gas lease providing for a 1/8th royalty. The deed contained a granting clause conveying a 1/16th mineral interest and a "future lease" clause that provided, \textit{inter alia.} that if the existing lease terminated without production, the "subject to" clause provided that the "grantee herein or his assigns "are to have ... under this conveyance an undivided 1/2 of all the oil. [sic] gas or other mineral ... and it is the intention of the grantors herein that in the event said lease is forfeited, then in that event the grantee is to have and hold an equal undivided one half of all such minerals." Apparently, the lessee drilled a producing well on the assumption the deed only conveyed a 1/16th mineral interest and the accounting as to a cotenancy would only be on a 1/16th net profit basis. Plaintiffs, the successors-in-interest to the grantee, arguing the deed conveyed a 1/2 mineral interest sought an accounting on a 1/2 net profits basis. The Court of Appeals, affirming the judgment of the trial court, applied \textit{Alford}, and held that the deed, pursuant to the granting clause that controlled the inconsistent "subject to" clause, only conveyed a 1/16th mineral interest. The Supreme Court reversed holding that the granting clause conveyed a 1/16th mineral interest while the "subject to" clause simultaneously conveyed a 7/16 interest in the possibility of reverter in the mineral estate. Thus, when the existing lease expired, the grantee owned a fee 1/2 mineral estate. Thus, the lessee had to account on a 1/2 net profits basis. Although noting that the case had been overruled in \textit{Luckel}, the Court in \textit{Jupiter Oil} distinguished \textit{Alford} on the basis the deed in \textit{Jupiter Oil} unambiguously granted a 1/16th fee mineral interest and a 7/16ths interest in the possibility of reverter to the mineral estate.

To fully comprehend the "two grant" analysis, \textit{Jupiter Oil} should be compared with the \textit{Heyen v. Harnett}, 235 Kan. 117, 679 P.2d 1152 (1984), wherein Kansas Supreme Court reached the same result on a different theory. \textit{Heyen} is discussed at supra \textit{n}. 46.

59. The Court opined that the only difference between the instrument in \textit{Alford} and the deed in \textit{Luckel} is that the former was mineral deed and the latter was a royalty deed and that was not a material distinction. Thus, deeds involving disparate mineral and royalty fractions are to be construed by the \textit{Luckel} standard. \textit{Id.} at 463.
60. *Id.* at 466. The dissent is quoting from 4 Williams & Meyers, *supra* n. 2 at § 340.2.


62. The Court referred to the clause as a "royalty" clause. 264 Ark. at 136; 572 S.W.2d 136.

63. This reading of *Kuhn* is premised on the Court's articulating the issue as to whether the "1/8th of royalty" language in royalty clause permits the royalty owners to shale in "All royalty revenue" or the "usual 1/8th royalty. *Id.* at 352.

64. 312 Ark. 330, 850 S.W. 302 (1993)

65. The opinion alternatively describes the royalty share at issue as an overriding royalty and as lease royalty share. I have assumed that for purposes of the discussion that the 3/16th share of royalty was a landowner's royalty share.

66. The Court also held that plaintiff's action was not time-barred. Thus, plaintiff was entitled to recover for the deficiency that accrued from the date of the execution of the division order in 1983. The statute of limitations applicable to division orders, Ark. Code Ann. § 16-56-111 (1987), that prescribes a five year limitations period for actions relating to written contracts, was tolled by the "partial payments," i.e. the underpayment.

67. See the discussion at *supra* n. 42.

68. For a discussion of the myriad instances in which the applicability of requisite standard of care that the executive rights owner owes to the non-executive interest holder, see, Williams & Meyers, *supra* n. 2 at § 339.

69. The same problem exists to grants or reservations of "all of the royalty," which encompasses all of the landowner's lease royalty. To facilitate the discussion as to the standard of care, the reference to the fraction of royalty includes the "all of the royalty" conveyancing phenomena.

70. A "naked" executive right, entitling the hold4er thereof to the development and leasing rights, may be severed in fee from the mineral estate without the executive rights holder owning any other interest in the mineral estate. The ownership of the non-executive interest is to a "non-participating mineral estate." See, respectively, Richard W. Hemingway, *The Law of Oil and Gas,* § 2.2 and § 2.7(H) (West 2nd. ed. 1992).
71. Further complicating the applicability of the requisite standard of care the motivation of the executive holder to negotiate for a reduced royalty share may be to acquire a shorter primary term that may yield an additional leasing opportunity with another bonus or surface damages or non-development clauses. For a general discussion, see, Ernest E. Smith, Implications of a Fiduciary Standard of Conduct for the Holder of the Executive Right, 64 Tex. L. Rev. 371, 386-88 (1985).

72. An additional complication is that bonus, the consideration paid to the mineral owner for executing the oil and gas lease, need not be paid, as it typically is, as a cash payment. Any consideration may be paid as bonus, including a share of production, such as an overriding royalty interest or a production payment. When the lease benefits include a share of production, in addition to the landowner's royalty share, the issue is presented as to whether its bonus to be paid to the mineral owner or royalty to be paid to the royalty owner.

Two differing views exist in the case law. The Texas cases determine whether a share of production is bonus or royalty solely by whether the interest reserved has the characteristics of the generally accepted definitions of bonus or royalty. If the share of production is paid over the life of the lease, its royalty. If it is a sum certain to be paid out of production, it is a bonus. The parties' express designation as to whether the interest is bonus or royalty is not controlling. Thus, in Griffith v. Taylor, 156 Tex. 1, 291 S.W.2d 673 (1956), the reservation in an oil and gas lease of a 1/16th share of gross production to be paid over the life of the lease that expressly stated that it was "in addition [to] the royalties ..., as additional consideration and bonus royalty" reserved a royalty interest. See also, Lane v. Elkins, 441 S.W.2d 871 (Tex. Civ. App. 1969, reh'g denied. Texas has consistently held that the typical overriding royalty reservation in an oil and gas lease is royalty that is to be paid to the royalty owner.

In Oklahoma the parties designation in the lease as whether the interest is bonus or royalty is determinative. Therefore, the intent, not the characteristics of the interest reserved, is conclusive as to whether a production share, in addition to royalty, is bonus or royalty. The basis of the Oklahoma rule is Sykes v. Dillingham, 318 P.2d 416 (Okla. 1957), wherein the Oklahoma Supreme Court held that a share of production in excess of a 1/8th royalty intended by the parties to the lease to be a part of the consideration for the execution of the lease is bonus.

73. For a citation to the extensive literature on the duty that the executive owes the non-executive interest in negotiating the oil and gas lease, see, Joshua M. Morse & Jaimie A. Ross, New Remedies for Executive Duty Breaches: The Courts Should Throw J.R. Ewing Out of the Oil Patch, 40 Ala. L. Rev. 187, 188 n. 3 (1988).
74. For a discussion of the various labels used to describe the duty that the executive owner owes to the non-executive owner, see, William & Meyers, supra n. 2 at § 339.2. Many of the descriptive terms have been used interchangeably, such as the "utmost good faith," to describe the traditionally prevalent "prudent landowner" standard of the "utmost fair dealing" duty. Id. Differing opinions have been expressed over the years as to the appropriate duty to impose on the executive to adequately protect the non-executive interest. Suggestions have included the no duty rule, ordinary care and good faith, utmost fair dealing, and the fiduciary duty. Lloyd Lochridge, Abuse of Executive Rights, 36th Oil & Gas Inst. § 2.02 (Matthew Bender 1985). For a criticism of the "utmost fair dealing" duty, and its "prudent landowner" standard, see, Joshua M. Morse and Jaimie A. Ross, supra n. 73 at 213-28.

75. 673 S.W.2d 180 (1984), reh'g denied.

76. The "same degree of diligence and discretion on the part of the mineral fee holder as would be expected of the average landowner ..." is from a leading and oft quoted "utmost fair dealing" case, Federal Land Bank v. United States, 168 F. Supp. 788, 791 (Ct. Cl. 1958). The Court held therein, inter alia, that the unreasonable delay in leasing by the mineral owner which delayed production until after a term royalty interest had expired violated the "utmost fair dealing" standard. The standard originates from an eminent law review article in the Texas Law Review, Jones, "Non-Participating Royalty," 26 Tex. L. Rev. 569, 574. For a short historical discussion of the evolution of the "utmost fair dealing" standard, see Joshua M. Morse & Jaimie A. Ross, supra n. 73 at 213-18.

77. Joshua M. Morse & Jaimie A. Ross, supra n. at 9. Also, see, Loyd Lochridge, Abuse of Executive Rights, 36th Oil & Gas Inst. § 2.02 (Matthew Bender 1985) and 2 Williams & Meyers, supra n. 2 at § 339.2 at 210.7.


79. For the most common explication of the "prudent landowner" criteria of the "utmost good faith" standard, Williams v. Meyers, supra n. 2 at § 339.2.

80. Dean Ernest Smith notes that "As usually interpreted, utmost fair dealing requires the executive right holder to execute the same type of oil and gas lease on the same terms as he would have done in the absence of an outstanding non-participating interest in a third party." Ernest E. Smith, supra n. 71 at 371, 372.
Dean Smith argues that the mineral owner should be free without liability under the prudent landowner standard to trade off a high bonus for a lower royalty, if the royalty is consistent with leasing practices in the area. Ernest E. Smith, The Standard of Conduct Owed by Executive Rights Holders and Operators to the Owners of Nonparticipating and Nonoperating Interests, 32 Inst. on Oil & Gas L. Tax’n, 241, 244 (1981 Matthew Bender).

Joshua M. Morse & Jaimie A. Ross, supra n. 73 at 229, 230.

673 S.W.2d 180 (Tex. 1984), reh'g denied.

It is disputed as to whether Manges applied a "fiduciary duty" or the traditional "utmost fair dealing" standard. The argument for the former is based in part on an initial opinion issued in the case but subsequently withdrawn by the Texas Supreme Court, Manges v. Guerra, 26 Tex. Sup. Ct. 430 (June 8, 1983) (opinion withdrawn) that contained no language of a fiduciary opinion, that is contained in the substituted opinion, Manges v. Guerra, 674 S.W.2d 180 (Tex. 1984). For an analysis of the case that favors the fiduciary duty construction, see, Ernest E. Smith, supra n. 71 at 377-78.

Manges also acquired other benefits for himself which were not shared with his non-executive mineral cotenants. First, Manges mortgaged (by deed of trust) the executive right to secure a promissory note for approximately $7 million. Next, in connection with another loan of $2.8 million (later increased to $5 million), Manges granted an option to purchase the production from the mineral estate to a third-party. In addition to securing the loans, which benefited Manges but not his non-executive mineral cotenants, both transactions removed the mineral estate from the leasing market. The trial court declared the mortgage to be ineffective and non-existent as to the executive interest. The mortgagee declared at trial that the mortgage was not effective as to the mineral interests. The trial court also cancelled the option to purchase production.

Manges was also found liable for failing to lease other lands not subject to the Manges to Manges lease, which he could have leased, but did not, to a third party.

When Manges executed the lease to himself, the land was being drained by offset production and the non-participating mineral owners had filed suit, with lis pendens, which Manges argued, precluded him from leasing to others. In addition to the farm out, discussed in the text, Manges also granted a "top lease" to the third-party that was to be effective if the Manges to Manges lease was judicially cancelled.
87. The non-participating mineral owners recovered the following from Manges for his breach of the fiduciary obligation: their proportionate share of the net profits from the wells drilled on the cancelled Manges-Manges lease, as cotenants; actual damages of $382,608.79; and, exemplary damages of $500,000.

88. The non-participating mineral owner's basis for cancelling the executive right in Manges was "fraudulent inducement" to convey the executive right to Manges in the deed of severance. The trial court found that the non-participating mineral owners had been fraudulently induced to convey their executive interests.

89. Joshua M. Morse & Jaimie A. Ross, supra n. 73 at 232.

90. Smith, supra n. 71 at 387-88.

91. Id. Smith also suggests that the executive under this standard should be able to trade a large royalty (1/6th) and a small bonus for a large bonus and small royalty (1/8th) so long as the small royalty was consistent with current leasing practices in the area.


93. See, Joshua M. Morse & Jaimie A. Ross, supra n. 73 at 231 for a complete description of the potential remedies.

94. The distinction that "control" over the lease benefits is determinative as to whether the fiduciary standard of Manges is applicable appears well-entrenched in the Texas Civil Appellate Courts. In Dearing, Inc. v. Spiller, 824 S.W.2d 728, 731 (Tex. Civ. App. 1992), the fiduciary standard was applied to a non-participating mineral interest. Mims v. Beall, 810 S.W.2d 876 (Tex. App. 1991) reh'd denied, involved the applicability of the fiduciary standard to a fraction of non-participating royalty interest. Pickens v. Hope, 764 S.W.2d 263-64 (Tex. Civ. App. 1988), rejected the applicability of the fiduciary duty to a fractional share royalty interest and applied the "utmost good faith" prudent landowner standard. Finally, Comanche Land and Cattle Co., Inc. Adams, 688 S.W.2d 914 (Tex. Civ. App. 1985) reh'g denied, applied the fiduciary duty standard to a defeasible term fraction of non-participating royalty interest.

96. The question remains unanswered as to whether the fiduciary standard of Manges requires the executive to exact for the non-executive the highest royalty obtainable.


99. Id. at 880,881.