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**A Texas Time Capsule:
Leasing Issues for Lands Affected by the
Relinquishment Act**

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Mazurek & Holliday PC

Mazurek & Holliday PC is an energy law firm focused on title examination and operational/regulatory advising across the continental United States. We actively represent our clients throughout all stages of a drilling program, from acquisition to divestiture.

Through our San Antonio office, MH provides a full range of title services ranging from acquisition/due diligence to preparation of division order title opinions for operations in Texas, Oklahoma, Ohio, New Mexico, Colorado, North Dakota, and Illinois.

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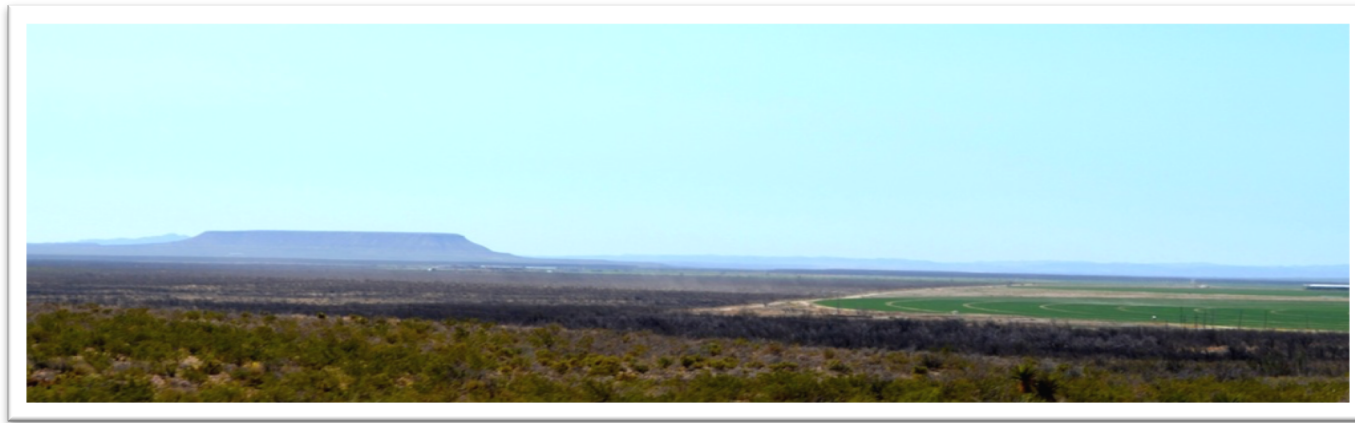
Overview

- Background of the Relinquishment Act
- Understanding the Act
- Ownership and Leasing Issues
 - Rules
 - GLO Guidelines
 - Resources
- This is a story about Texas' search for revenue
- *Special thank you to our colleague Matthew Royall for his efforts on this presentation.*



Historical Context

- The Relinquishment Act cannot be fully understood outside of its historical context.
- The subsequent judicial interpretations of the Act's text draw on the situation in West Texas at the turn of the 20th Century.



Land Management Pre-1895

- Texas Independence, Statehood 1.0, Confederate Statehood, Statehood 2.0 – Texas retained sovereign title to all minerals in all lands sold.
- Texas Constitution of 1876
 - Set aside half of Texas's public lands to benefit public schools.
 - Responsibility of the Legislature to sell the lands.
- Subsequent Land Sales and Relinquishment Acts
- Texas is seeking to monetize land resources to fund public schools

1895 Land Acts

- Various 1895 Statutes release all minerals in lands previously sold
- Legislation is effective 9/1/1895 – This is why the 9/1/1895 date is the beginning our Mineral Classification inquiry
 - For lands patented before 9/1/1895, we are not concerned with State ownership of minerals
- In 1895, the Texas Legislature also passed a series of land acts which established a specific procedure for prospectively granting unsold public lands.



1895 Land Acts

- Mining Act of 1895 – Beginning of Mineral Classification
 - GLO ordered to map all unsold lands, and utilize geologists to identify mineral lands
 - Lands were identified as Mineral Lands if found to contain or likely to contain mineral deposits
- Nature of State Mineral Lands from 1895 to 1907 – Lands found to contain valuable minerals **COULD NOT** be sold
 - Illustrated a hesitance to sever the estates.

Land Sales Act of 1907

- Classification System is Officially Born
 - GLO may specifically classify lands as “Mineral Lands” and sell them
 - These are the tracts identified by virtue of Mining Act of 1907
- BUT
 - “. . . all sales of such land shall be upon the express condition that the minerals shall be and are reserved to the fund to which the land belongs and such reservation shall be stated in all applications to purchase.” 1907 Land Sales Act § 6f
- The Surface Estate and the Mineral Estate have been severed.

Quick Recap – Evolution of Effort to Monetize Public Lands

- 1836-1866 (Post Independence from Mexico): Texas retains title to all minerals in lands sold, whether or not specifically stated on the Patent
- 1876: Texas Constitution sets aside 1/2 of all unsold public land to benefit public schools
- 1866-1895: A series of legislative acts release Texas mineral claims in lands previously sold
- 1895 Mining Act: Identifies minerally valuable lands, but prohibits their sale; hesitancy to sever estates
- Land Sales Act of 1907: GLO can ‘minerally classify’ lands and sell surface only; minerals are severed and reserved to the originating fund.



Subsequent Permitting and Leasing Acts

- PROBLEM: No mechanism for authorizing development of State-owned minerals.
- SOLUTION: Permitting and Leasing Acts of 1913 and 1917
- Private individual or company who wished to explore state owned minerals for oil and gas was now able to apply for an exploration permit.
- If exploration resulted in the discovery of oil or gas, the permittee could request a lease to cover the lands.
- Hence, the development of State owned minerals had begun.

Snapshot of Ownership Post - 1913

- Private Citizens own the surface.
- State owns the minerals.
- Companies wish to explore and develop the State's minerals.
 - They will need to access and commence operations on the privately owned surface.
- Early days of oil, especially in West Texas...
 - How do we think the surface owners will react?
 - If your answer was “not well,” you’re right!



Conflict of the Estates

- PROBLEM: Surface Owners are hostile to development.
 - Who were these surface owners?
 - Ranchers and Farmers
 - Permit & Leasing Acts provided for total compensation to surface owner of 10-cents/acre/year
 - The land owners blocked entry and threatened those oilmen who rushed west to develop these state owned minerals.
 - This probably isn't surprising to most of you.
- SOLUTION: The Relinquishment Act of 1919.

Oil in Texas: The Gusher Age, 1895-1945:

“Here was the incentive for farmers and ranchers to keep their dogs penned and their shotguns on racks in the parlor when oil company landmen came to call.”



Emphasis on the Purpose of the Act

- Texas Supreme Court in *Greene v. Robison*:

“There was a dual or double ownership of the land, the surface estate and the mineral estate, each antagonistic to and conflicting with the other. There was no provision of law for the protection of the owner of the soil in his peaceable enjoyment and possession of his property. The development of an oil field on it would be disastrous to him and utterly destructive to his property. Therefore the attitude of owners of the school and asylum lands was practically one of armed resistance. The conditions were inimical to any effort at development, and the state was not realizing on its mineral estate in these lands. The purpose of the act was to meet this practical situation.”

Greene v. Robison at 531



The Text of the Relinquishment Act of 1919

- PROCEED WITH CAUTION!



The Text of the Relinquishment Act of 1919

- Codified in the Texas Natural Resources Code 52.171 through 52.190.
- 52.171: The state hereby constitutes the owner of the soil its agent for the purposes herein named, and in consideration therefor, relinquishes and vests in the owner of the soil an undivided fifteen-sixteenths of all oil and gas which has been undeveloped and the value of the same that may be upon and within the surveyed and unsurveyed public free school land and asylum lands and portions of such surveys sold with a mineral classification or mineral reservation, subject to the terms of this law. The remaining undivided portion of said oil and gas and its value is hereby reserved for the use of and benefit of the public school fund and the several asylum funds.

The Text of the Relinquishment Act of 1919

- 52.172: The owner of said lands is hereby authorized to sell or lease to any person, firm or corporation the oil and gas that may be thereon or therein upon such terms and conditions as such owner may deem best, subject only to the provisions hereof, and he may have a second lien thereon to secure the payment of any sum due to him. All leases and sales so made shall be assignable. No oil or gas rights shall be sold or leased hereunder for less than ten cents per acre per year plus royalty, and in case of production, the lessee or purchaser shall pay the state the undivided one-sixteenths of the value of the oil and gas reserved herein, and like amounts to the owner of the soil.
- 52.182: The payment of the ten cents per acre and the obligation to pay the owner of the soil one sixteenth of the production and the payment of same when produced and acceptance of same by owner shall be in lieu of all damages to the soil.

Date Range for the Relinquishment Act lands

Lands patented by the state between:

September 1, 1895 through June 29, 1931



Greene v. Robison (1928)

- Definitive Case Interpreting the Language of the Act
 - Actually six cases consolidated into one.
- Constitutional Challenge: Facts not important. Key issue “Is Relinquishment Act of 1919 Constitutional under Texas Constitution?”

Constitutional Challenges:

- 1) R.A. is a an unconstitutional/unauthorized gift
- 2) R.A. diverts public school funds in unconstitutional/unauthorized manner
- 3) R.A. delegates to an agent the duties imposed by the Constitution on the Legislature.

***Greene v. Robison* (1928)**

Court's Conclusion #1: There is no vesting of title or interest in the oil and gas in the owner of the soil.

NO UNCONSTITUTIONAL GIFT.

“The expressions in article 5367 that the state “relinquishes and vests” in the surface owner fifteen-sixteenths of the oil and gas, and that the remaining portion is “reserved” for the benefit of the school and asylum funds, are *confusing and uncertain of meaning*, and perhaps not of importance.”

Court focuses on the overall purpose of the act, reading the entire act as one, so as to determine what the Legislature *intended*, rather than what they actually said.



Greene v. Robison (1928)

Court's Conclusion #2: The payments made to the owner of the soil are just payments in lieu of damage to the soil.

**NO UNCONSTITUTIONAL DIVERSION OF PUBLIC FUNDS,
BECAUSE THESE ARE DAMAGES PAYMENTS AND NOT SALE
PROCEEDS.**

Reasoning: Payments provided for by the Relinquishment Act were payments in lieu of damage to the soil. Intention of the legislature was that the payments were not part of the consideration for the sale (leasing) of oil and gas.

“The Legislature has brought about this desired result in a lawful manner by requiring the purchaser of the oil and gas to compensate the owner of the soil for the use he makes of the surface, independent of the price he pays for the minerals.”



***Greene v. Robison* (1928)**

Court's Conclusion #3: Compensation under the lease is to be paid equally to the state and the owner of the soil.

**NO UNCONSTITUTIONAL DELEGATION BECAUSE
CONSTITUTION DOESN'T REQUIRE EXACT TERMS**

The Court, almost in passing, interpreted the act to require payment in “like amounts” to the state and the owner of the soil. *Id.*

Note: The Court states that the “Constitution has never been construed to require that the Legislature should prescribe in detail and with exactness” the price of the sale. *Id.* at 533.



***Greene v. Robison* (1928)**

KEY TAKEAWAYS

- 1. Surface owner owns no oil and gas. No vesting occurred under R.A.**
- 2. State owns 100% of mineral estate in R.A. lands.**
- 3. All payment to surface owners are liquidated damages payments, not payment of sale proceeds of State-owned oil & gas.**
- 4. 50/50 Rule: All lease benefits/compensation split equally between State of Texas and surface owner**

The general rule derived from *Greene* is that the owner of the surface of lands subject to the Relinquishment Act is a leasing agent for the state, entitled to one-half of the benefits of said lease, and those benefits and agency run with the land.



Mineral Conveyances/Reservations are VOID

- Mineral Deeds and Mineral Reservations from surface owners for R.A. lands are VOID.
 - *McDonald v. Dees*, 15 S.W.2d 1075 (Tex Civ. App – El Paso 1929).
- Because the Court in *Greene* established that the owner of the soil had no right to the oil and gas in place, the owner cannot sell the minerals as he could if he were a true mineral owner. *See Greene; State v, Magnolia Petroleum Co.*, 173 S.W.2d (Tex Civ. App - San Antonio 1943).

Transferability of Lease Benefits

- *Lemar, et al. v. Garner*, 121 Tex. 503 (1932) **Exception:** Surface owner may convey/reserve lease benefits under an **existing** lease
 - This case emphasizes the longstanding Texas policy against restraints on alienation.
- The primary issue set out in *Lemar* was whether the benefits of a lease on Relinquishment Act lands could be severed from actual ownership of the surface estate. *Id.* at 509.
- Can a surface owner lease as agent for the state, and later sell the surface but retain the benefits under the original lease? **(YES)** Or must the benefits necessarily run with the land? **(NO)**

Transferability of Lease Benefits

- Per *Lemar*, benefits under an existing lease are a property right which can be conveyed:

“That when a valid and binding lease or conveyance of the minerals is made by the owner of the land, as the agent of the state, then in that event he receives the foregoing amounts as compensation for his services. His share of the rentals, royalties, and bonuses derived from the leases executed by him become property rights during the period of time for which the lease runs.”
- Conceptually like an ORRI - when lease terminates, the reserved/conveyed rights of the original owner of the soil/agent for the state also terminate and re-vest in current surface owner.
- **Common Title Pitfall. Pay special attention.**

The Agency Relationship: Duty

- The Relinquishment Act, as clarified by *Greene*, creates an agency relationship between the owner of the soil and the State of Texas. *See* Tex. Nat. Res. Code Ann § 52.172.
- 1919 – 1985: Many Questions About Nature Agency/Duties
 - *State v. Durham*
 - Limited Scope of the agency
 - Fiduciary duty that would be violated by self-dealing
- 1985 Amendment Codified in Tex. Nat. Res. Code Ann. § 52.189 (b):
 - “An owner of the soil owes the state a fiduciary duty and a duty of utmost good faith... Any conflict of interest must be resolved by putting the interests of the state before the interests of the owner of the soil.”

The Agency Relationship: Duty

Current State of Surface Owner's Agency Duties:

1. Surface Owner owes the State of Texas a Fiduciary Duty of Utmost Good Faith (highest duty)
2. Surface Owner required to put best interest of State of Texas before his own
3. *In practice – you have a duty to lease on good terms to a good operator.*

Recall:

1. Payments to surface owner are liquidated surface damages
2. Surface owner and State of Texas split all payments 50/50



The Agency Relationship: Duty

COMMON CONFLICT OF INTEREST: Surface owner attempts to negotiate separate surface damages provisions or agreement.

1. Per R.A., lease payments to surface owners are in lieu of surface damages
2. Per GLO: “Participation by the owner of the soil in the bonus, rentals and royalties is in lieu of surface damages and such collateral agreement could render the lease invalid and subject to the surface owner’s agency rights to forfeiture.”
3. WHY:
 - Surface Damages have already been accounted for.
 - Introduces motive for surface owner to seek additional surface use damages in exchange for lower bonus/royalty. This would lead to unequal split of lease benefits, violating agency.

Practical Rule: No Collateral Agreements. All terms must be in lease.



Capacity and Agents of the Owner

- A minor or person of unsound mind cannot act as the state's agent.
 - However, a person authorized by law to act on such persons behalf may do so.
- Attorney-in-Fact for Surface Owner
 - Generally Accepted Approach: An agent of the surface owner, including an attorney-in-fact cannot execute the lease.
 - There a split of professional opinion, though no hard rule
 - If relying on a POA, it must expressly authorizes the AIF to execute Relinquishment Act Leases.
 - POA shall be submitted to the GLO concurrently with the lease.
 - Both owe the state a fiduciary duty.
- Corporations may execute a lease through any duly authorized officer or agent.



Unavailable Owner

Relinquishment Act addresses this scenario specifically in Section 52.186.

- If deemed unavailable by the terms of the statute, agency rights are forfeited and the oil and gas can be leased under the procedure for leasing unsold surveyed public school lands.
 - Subsection (b) explains the requirements in which an owner may be legally deemed unavailable.
- 1. Operator proves up unavailability under the statute..
- 2. Commissioner provides written notice to the owner of the soil explaining the consequences of finding him “unavailable.”
- 3. Notice is sent to the owner’s last known address and provided by publication.
- 4. The owner of the soil has 30 days at this point to contact the GLO.
- 5. If no reply, agency rights terminated and process goes to sealed bid by School Land Board.
- 6. 2 Year Redemption Period for surface owner if can prove improper notice.



Forfeited Rights of the Owner

- Leasing procedure when the surface owner's agency rights are forfeited:
 - The land shall be leased under a sealed bid process.
 - The surface owner shall not be entitled to share in the proceeds of such lease.
 - Upon expiration or termination of such lease, the owner's agency rights will be reinstated.
- If no lease is executed within one year or forfeiture, the agency rights may be reinstated at the commissioner's discretion.



Lease “Negotiation”

- PER STATUTE: Surface owner is authorized to act as the state’s leasing agent on ‘such terms and conditions as surface owner deems’
- REALITY: Bonus is up for negotiation. The lease must be on the GLO lease form and contain highest royalty in area.
- WHY: No lease is effective until accepted for recording by GLO.
 - GLO will refuse to accept any lease deemed inconsistent with the State’s best interest.
 - Proposed lease submitted to the GLO prior to recording in county records.
- No top-leases, because the GLO says so.

State Approval of the Lease

- Lease may not provide for a term of more than 5 years.
- May not encompass more than four full sections or 2,560 acres.
 - A mother hubbard clause is not acceptable.
- Private land and Relinquishment Act land may not be included in the same lease.



State Lease Form & Additional Resources

- State Lease Form
- GLO Guidelines for Leasing Relinquishment Act Lands
 - Texas Administrative Code
- Application and Checklist



Key Takeaways

1. Surface owner owns no oil and gas. No vesting occurred under R.A.
2. State owns 100% of mineral estate in R.A. lands.
3. All payment to surface owners are liquidated damages payments, not payment of sale proceeds of State-owned oil & gas.
4. 50/50 Rule: All lease benefits/compensation split equally between State of Texas and surface owner.
5. No collateral agreements; all provisions must be in the lease. This means no separate surface damages agreements.
6. Surface owner has a fiduciary duty of good faith to act in State of Texas' best interest. If he doesn't, he could lose his agency rights.
7. Mineral deeds/reservations are VOID. Existing lease benefits can be sold/reserved, but last only for life of the lease. Think ORRI.
8. Use the State of Texas Lease Form.



QUESTIONS?

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AT MAZUREK & HOLLIDAY, WE STAND FOR **MORE.**