What Rights do Urban Micro-Tract Owners in the Barnett Shale Have? Rule 37 Spacing Exception Permits, the Mineral Interest Pooling Act, the Common Law, and More

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A. Introduction

Applying current Texas Oil and Gas Law to micro-tract owners in urban areas ripe for horizontal drilling is often like attempting to put a square peg into a round hole. The Law was written with vertical drills and large and small, but not micro-sized, rural tracts in mind. Inside large metropolitan areas where tracts often consist of a mere tenth of an acre, application of current law may result in a taking of private property even if only in small amounts.

With modern horizontal drilling and hydraulic fracturing techniques for natural gas extraction, a single pad site located in an urban area can be used to drill ten or more lateral wells miles beneath the surface each extending for thousands of feet in different directions. In the Barnett Shale, in an area like Fort Worth, Texas, hundreds of houses often lie on top of the surface of the drilling area.

The Texas Supreme Court held in *Coastal Oil and Gas Corp. v. Garza*[1] that subsurface fracking of unleased property does not constitute trespass and further than no compensation for taken minerals must be given when four conditions exist. Each of these conditions serves to ensure that the property rights of the unleased landowner are adequately protected.

[1] Coastal Oil & Gas Corp. v. Garza Energy Trust, 268 S.W.3d 1 (2008).

In urban areas, often only one of the four conditions exists, and even then, the last remaining condition likely only offers partial protection. This partial protection may result in a taking of property.

The four conditions are as follows: (1) if the unleased landowner can drill his own well, then his only remedy for drainage is to do so (this is the basic Rule of Capture), (2) if the landowner leased and his lessee negligently fails to drill an offset well, then the landowner can sue the lessee for damages, (3) the Railroad Commission can regulate production to prevent drainage, and (4) if none of the other remedies are available, then the aggrieved landowner can use the Mineral Interest Pooling Act ("MIPA") to force pool her interest. For the urban landowner on less than an acre with a house taking up much of the surface area, drilling an offset well is both legally and practically impossible, which cancels out the first two conditions. The third condition offers no relief because regardless of how production is regulated, the unleased landowner will be subjected to uncompensated drainage. The fourth condition does potentially offer relief, but even if the micro-tract urban landowner can clear all of MIPA's hurdles, relief is almost certainly not available as of the date that drainage began.

The Supreme Court of the United States has held that even slight physical occupation of property is a taking "to the extent of the occupation."[2] Consequently, MIPA cases involving unleased urban micro-tract owners subject to Rule 37 spacing exceptions could result in a confiscation claim for (a) drainage occurring between the time that drainage began and entry of the Railroad Commission's interim escrow order, or (b) for drainage that goes uncompensated due to inadequate protection under Texas's anachronistic forced-pooling act.

[2] *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 434–35 (1982).

In the current environment where the rights of unleased, urban, micro-tract owners are unclear, offers are generally made to lease and sometimes to participate as a working interest owner. Often, however, no significant competitive market exists once an operator has filed a courthouse unit, and been designated as operator of the urban unit. Offers are sometimes made with take-or-leave-it, adhesion-basis terms possibly because the urban, micro-tract landowners are thought to lack the sophistication and leverage to bargain for their rights, unlike their rural, small-tract counterparts who have grown savvy over many decades of rural development.

B. The Rule of Capture Relies Ineluctably on the Availability of the Self-Help Remedy of Offset Well Drilling and Without the Self-Help Remedy; the Rule of Capture Becomes Inapplicable.

The remedy of an injured landowner for uncompensated drainage is "said to be self-help." *See Coastal Oil & Gas Corp. v. Garza Energy Trust*, 268 S.W.3d 1, 14 (2008) ("The rule of capture is justified because a landowner can protect himself from drainage by drilling his own well"); *Geo Viking, Inc. v. Tex-Lee Operating Co.*, 817 S.W.2d 357, 364 (Tex. App.—Texarkana 1991) (citing *Brown v. Humble Oil & Refining Co.*, 126 Tex. 296, 83 S.W.2d 935, 940 (1935)) *writ denied*, 839 S.W.2d 797 (Tex. 1992); Levi Rodgers, *Subsurface Trespass by Hydraulic Fracturing: Escaping Coastal v. Garza's Disparate Jurisprudence Through Equitable Compromise*, 45 Tex. Tech L. Rev. Online Ed. 99, 118 (2013). More specifically, the self-help is the ability to drill an offset well. *Brown v. Humble Oil & Ref. Co.*, 126 Tex. 296, 305 (1935) (Under the rule of capture, the "only way the landowner can protect himself is to drill offset wells."). Regardless of whether the "ownership in place" theory or the "exclusive right to take" theory of mineral interest ownership is used, the rule of capture has always been subject to reasonable limitations to protect private property. John S. Lowe, Owen L. Anderson, Ernest E. Smith, David E. Pierce, *Cases and Materials on Oil and Gas Law* 26 (5th ed., West 2008).

Without a self-help remedy, that is, without any practical or legal ability to drill one's own offset well on one's own property, that the rule of capture fails for lack of essential purpose and justification.

1. A Full Mineral Rights Owner Has a Claim Unlike the Royalty Interest Owner-Plaintiff in *Garza*.

The Texas Supreme Court, in *Coastal v. Garza*, held that the owner of a royalty interest may only sue for trespass on the case and not trespass *quare clausum fregit* because the royalty owner owned a reversionary interest that was non-possessory. *Garza*, 267 S.W.3d at 9–10. Consequently, the royalty owner had to prove actual injury, which he could not do because, under the rule of capture, he did not own the minerals taken. *Id.* at 11, 15. The court suggested that the royalty owner's proper remedy would be to sue the lessee for negligently failing to exercise self-help rights. *Id.* at 13.

More specifically, the Court said, "As a mineral lessor, [the plaintiff] has only 'a royalty interest and the possibility of reverter' should the leases terminate, but 'no right to possess, explore for, or produce the minerals.'" *Id.* at 9. The Court reasoned that, because the lessee had control over the right to develop the minerals, that only the lessee could enforce that right. If the lessee failed to prudently exercise that right, then the only remedy for the royalty owner would be to sue under the implied covenant to prevent drainage. Bruce M. Kramer, *Coastal Oil & Gas Corp. v. Garza Energy Trust: Some New Paradigms for the Rule of Capture and Implied Covenant Jurisprudence*, 30 *Energy & Min. L. Inst.* 11, 362 (2009). The question of whether the lessee could have sued for trespass went unanswered. *Garza*, 267 S.W.3d at 12 ("We need not decide the broader issue here. In this case, actionable trespass requires injury."). In *Garza*, the defendant happened to be both the plaintiff's lessee and the party allegedly doing the draining.

Bruce M. Kramer, Coastal Oil & Gas Corp. v. Garza Energy Trust*: Some New Paradigms for the Rule of Capture and Implied Covenant Jurisprudence*, 30 Energy & Min. L. Inst. 11, 341 (2009).

Many urban small-tract owners own what the *Garza* plaintiff did not, namely, the full mineral interest. The mineral interest in a tract of land consists of the following incidents of ownership: "(1) the right to use the surface; (2) the right to incur costs and to retain profits (the right to develop); (3) the right to alienate; and (4) the right to retain lease benefits." John S. Lowe, Owen L. Anderson, Ernest E. Smith, David E. Pierce, *Cases and Materials on Oil and Gas Law* 51 (Fifth Edition, West 2008). The rule of capture can be justified when a landowner keeps his right to develop the minerals by retaining the right to drill an offset well. The rule of capture's constitutionality and judicial justifiability has always been predicated on the ability to drill an offset well.

C. Without the Rule of Capture's Predicate, the Rule of Capture Would Not Only Become Unjustifiable, but Could Also Sanction Confiscation

Generally, when a regulation deprives a property owner of "all economically beneficial or productive use of land" a regulatory taking has occurred. *Palazzolo v. Rhode Island*, 533 U.S. 606, 617–18 (2001) (quoting *Armstrong v. United States*, 364 U.S. 40, 49 (1960)). This rule looks at "complete deprivation of use, not value." Steven J. Eagle, *Regulatory Takings* § 7-3(b)(5) (4th ed. 2009). "Most regulations do not constitute a total taking, in which case compensation is due only if the owner's investment and reasonable intended use is outweighed by the government's interest in protecting public health, safety, and welfare." *Penn Central Transportation Co. v. City of New York*, 438 U.S. 104 (1978); Lowe, Anderson, Smith & Pierce, *Cases and Materials on Oil and Gas Law* 130 (5th ed. 2008). A regulation must leave more than a "token interest." *Palazzolo*, 533 U.S. at 631–32. Otherwise, the regulation may be considered a mere "adjust[ment of] the benefits and burdens of economic life to promote the common good."

Lucas, 505 U.S. at 1018. This would be particularly true where the regulation can be fairly considered to offer significant "average reciprocity of advantage" to the aggrieved party. Eagle, *supra* § 7-7(a)(1); *Also see Pa. Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922).

The "right to develop" is an incident of ownership of a mineral interest. Lowe, Anderson, Smith & Pierce, *supra* at 51. The right to develop still has significant remaining value even after application of the rule of capture when adequate self-help remedies are available. Without self-help remedies, however, the right to develop has no value—not even "token" value.

Because Railroad Commission regulations can take away "the right of self-help to protect property rights," the "regulations must afford the protection, in addition to prevention of waste." Robert E. Hardwicke, M.K. Woodward, *Fair Share and the Small Tract in Texas*, 41 Tex. L. Rev. 75, 80 (1962). The Texas Supreme Court has a long history of intervening when practices before the Railroad Commission threaten to wholly deprive mineral interest owners of a property right. *Id.* at 76 (discussing *Halbouty v. R.R. Comm'n*, 357 S.W.2d 364 (Tex. 1962) and *Atlantic Ref. Co. v. R.R. Comm'n*, 346 S.W.2d 801 (Tex. 1961)).

The Texas Supreme Court has said that "The exercise of the police power under [Rule 37] does not change the rule of property. It merely regulates and controls the way in which his property shall be used and enjoyed. Each person still owns the oil and gas in place under his land, and each still has the right to possession, use, enjoyment, and ownership of the oil and gas produced through wells located on his land, regardless of its origin." *Humble Oil*, 126 Tex. at 312.

If Rule 37 does not change property rules, then it cannot be used as a method of circumventing property rules. Rule 37 was never meant to deprive mineral rights owners of all economic value of the mineral estate. Instead, Rule 37 and its exceptions were enacted to protect

property rights. *See id.* ("When . . . [Rule 37] is construed in connection with the cardinal rules of property above stated, we think the language used is for the dominant purpose of protecting . . . property rights.").

While the Texas Supreme Court suggested in *Garza* that the rule of capture could also be justified by the availability of self-help relief under the Mineral Interest Pooling Act ("MIPA"), current Texas MIPA law does not provide for compensation from the date that drainage began, but rather from the date of the Railroad Commission's interim escrow order. 1-13 Bruce M. Kramer and Patrick H. Martin, The Law of Pooling and Unitization, § 13.03 (3d ed., LexisNexis Matthew Bender 2013). The urban, micro-tract owner affected by a Rule 37 spacing exception who has no ability to drill an offset well should not be forced to initiate action before the Railroad Commission immediately or lose her right to compensation for drainage. Often the urban, small-tract owner lacks the resources to prosecute such a claim in a process that was originally designed for far larger rural tracts affected by vertical wells.

When a "permanent physical occupation of property" occurs, then a taking occurs "to the extent of the occupation" without regard to public benefits or amount of economic impact. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 434–35 (1982). If an urban homeowner is deprived of all self-help rights for any duration of time and during that time such owner's minerals are drained, then such owner's development right has been wholly occupied, and such occupation's extent continues up until such owner has at least some available remedy. If the only available remedy is relief under the Texas MIPA, then the landowner should not be forced to waive his rights up until he prosecutes a MIPA action.

As explained below, operators employing horizontal drilling techniques in urban areas have two methods of obtaining administrative consent to the operation. One is a Rule 37 spacing exception. The other is forced pooling.

1. The Urban Unit Operator's Proper Avenue for Taking Neighboring Unleased Urban Small-Tract Homeowner's Rights Should Be the Texas Forced Pooling Statute, Which Operators Have Utilized Successfully, Because the Statute Provides for Compensation to Aggrieved Property Owners. Spacing Exceptions (Which Historically Protected Small-Tract Owners in Rural Areas) Should Not be Used in Urban Areas as a Cheap, Quick, Easy, Confiscatory Alternative to Forced Pooling.

Forced pooling is an administrative procedure that the Texas legislature carefully designed to compensate landowners who are deprived of their development rights. Spacing exceptions, under Rule 37, on the other hand, require no compensation to aggrieved landowners. In rural areas, the rule of capture may apply, subject to the usual limitations, to a particular tract of land to allow something less than a total deprivation of a neighbor's use of the right to develop her minerals. In urban areas, however, the tracts are very small, often less than an acre, and ownership is extremely dispersed. In many cases, no single landowner in a unit will have the legal or practical ability to drill a well. Forced pooling has proved, in recent years, to be a very successful method of dealing with issues unique to horizontal drilling in urban areas and to clear the way for drilling while ensuring compensation to all landowners within the unit.

Unleased, small-tract mineral owners who are subject to horizontal drilling in urban areas "are left out in the cold under the current framework." Brady Paul Behrens, *Rule 37 Exceptions and Small Mineral Tracts in Urban Areas: An Argument for Incorporating Compulsory Pooling into Special Field Rules in Texas*, 44 Tex. Tech L. Rev. 1053, 1077 (2012). Further,

> "If [the operator] obtains its Rule 37 exception-either administratively or after a hearing-the common law rule of capture will apply, and [the landowner] will receive no compensation for the minerals drained from beneath his tract. Because producers

> have little incentive to pursue voluntary-and especially not compulsory-pooling options, the most efficient option for producers is to seek Rule 37 exceptions from the [Railroad Commission]." *Id.*

Rule 37 spacing exceptions should not be used in urban areas as a cheap, quick, easy, confiscatory alternative to forced pooling of micro-tracts.

Urban, small-tract landowners should not be forced to prosecute a MIPA action after losing a Rule 37 protest. Such a practice puts the burden on micro-tract owners of prosecuting a MIPA case that the Railroad Commission's own guide to MIPA warns is not a "cure-all" because MIPA is so limited in scope and effect and could take six months or well over a year involving "a procedural maze of time limits, venue, and standing problems." 3 Ernest E. Smith and Jacqueline Lang Weaver, *Texas Law of Oil and Gas*, § 12.1[B], at 12-7 (2d ed., LexisNexis). Rule 37 has traditionally benefitted small tract owners, not hurt them. *Id.* The typical urban micro-tract owner, however, is in a different circumstance from the rural small-tract owners that Rule 37 exceptions have traditionally protected. Due to the nature of the technology, these landowners, even given unlimited money and resources, could not drill their own well. These landowners should be able to obtain compensation for their minerals from the date that confiscation begins and they should have a process available to them for enforcing their rights that involves time and effort that is in reasonable proportion to the very small size of their tracts.

The Texas Mineral Interest Pooling Act ("MIPA") has not been updated since 1977 and was originally designed for rural, vertical drilling. Smith & Weaver, *Id.* at § 9.9[A] p. 9-144; Tex. Nat. Res. Code § 102.001–102.112. In fact, use of MIPA to force pool unleased, micro-tract, mineral owners in residential subdivisions, which is sometimes colloquially called "reverse MIPA," was first sanctioned in 2008 in *Application of Finley Resources, Inc. for the Formation of a Unit Pursuant to the Mineral Interest Pooling Act*, R.R. Comm'n Oil & Gas Docket No. 09-

0252373 (Final Order, Aug. 25, 2008) (hereinafter "*Finley*"). *See* John Camp, *Forced Pooling in Texas: The Mineral Interest Pooling Act: When Can I Use it and How Does it Work?*, Oil & Gas Regulation in Texas Seminar (Tab H Apr. 14, 2011):

> At the time of the MIPA's enactment in 1965, many practitioners believed this statute would facilitate the drilling of additional wells by force pooling holdouts into proposed proration units for yet to be drilled wells. Despite this expectation, the MIPA had been used almost exclusively by parties left out of production seeking to force pool their interests in to production from an existing well, until the advent of mineral development in established subdivisions in the Newark, East (Barnett Shale) Field. *Id.*

Furthermore in *Finley* (the seminal Barnett Shale reverse MIPA case),

> "The original examiners' recommendation concluded that the MIPA could not be used to force an unwilling party into participation in a force pooled unit because [the] statute was limited to protect small tract lessees/owners and was not a broad authorization to protect correlative rights generally or allow large tract lessees more flexibility in development." *Id.* at H24.

Eventually, "[a] final order granting Finley's application was ultimately signed by two of the three [Texas Railroad Commission] Commissioners over one year after the hearing was held on the application. *Id.* "Thanks to the *Finley* case, MIPA is an operator's newest tool in urban gas development." Eric C. Camp, *Dealing with Missing Persons and Holdouts: Using Rule 37 and MIPA for Urban Gas Development*, Dallas Bar Ass'n – Energy Law Section, January 2011 CLE Luncheon, at 14.

Arguments have been made that the Railroad Commission's *Finley* decision was too favorable to landowners. Ronnie Blackwell, *Forced Pooling Within the Barnett Shale: How Should the Texas Mineral Interest Pooling Act Apply to Units with Horizontal Wells?*, 17 Tex. Wesleyan L. Rev. 1, 17–20 (2010). Still, the Commission's MIPA decisions since *Finley* have stayed "essentially the same since then." Eric Camp, *supra* at 21.

Good arguments may exist for why the time has come for the Texas legislature to update MIPA. Those arguments, however, belong in that forum and not in the courts because while the Texas courts wait on a better legislative solution, they should not sanction uncompensated confiscation of a well-established private property right, namely the right to develop a mineral interest, as a stop-gap measure.

Spacing exceptions may allow drilling, but they do not sanction conduct that is otherwise unlawful or operations that extend over lease lines. The Texas Supreme Court has said that "As a general rule, a permit granted by an agency does not act to immunize the permit holder from civil tort liability from private parties for actions arising out of the use of the permit." *FPL Farming Ltd. V. Envt'l Processing Sys.*, L.C., 351 S.W.3d 306, 310–11 (2011). In other words, operations violating the rights of third-parties are not cleansed of liability just because the Railroad Commission grants a Rule 37 exception permit. Operators should have the option to either obtain a spacing exception, drill, and pay damages to urban micro-tract owners, or create a force-pooled unit. The damages for the former should encourage the latter because the latter provides for compensation to aggrieved landowners who likely cannot afford to prosecute their own forced pooling claim.

D. The Claim Discussed in this Article for Urban, Micro-Tract Owners Who are Being Drained Following a Rule 37 Spacing Exception May be Characterized as Trespass, Conversion, Nuisance, Strict Liability, Confiscation, or Possibly Negligence.

Caselaw, law review articles, and other legal scholarship suggests that under the novel circumstances caused by the recent outburst of lateral drilling in urban areas "a cause of action may lie in trespass, nuisance, strict liability, or confiscation." John S. Lowe, Owen L. Anderson, Ernest E. Smith, David E. Pierce, *Cases and Materials on Oil and Gas Law* 301 (5th Ed., West 2008) (aggregating caselaw). Other theories of liability include negligence and conversion. *Id.*

1. Trespass

Trespass is defined as "an intentional and unprivileged use or other invasion of another person's real property." *See* Terry D. Ragsdale, *Hydraulic Fracturing: The Stealthy Subsurface Trespass*, 28 Tulsa L.J. 311 (1993) ("In modern times, the common law tort of trespass constitutes an 'intentional and unprivileged use or other invasion of another person's real property.'").

The owner of the full, present, possessory mineral interest and not a mere royalty interest has more rights. The mineral interest in a tract of land consists of the following incidents of ownership: "(1) the right to use the surface; (2) the right to incur costs and to retain profits (the right to develop); (3) the right to alienate; and (4) the right to retain lease benefits." John S. Lowe, Owen L. Anderson, Ernest E. Smith, David E. Pierce, *Cases and Materials on Oil and Gas Law* 51 (5th Ed., West 2008). Rule 37 spacing exceptions carry the potential to violate urban micro-tract owners' "right to develop." While the Texas Supreme Court has said that "[t]he minerals owner is entitled, not to the molecules actually residing below the surface," the Court has explained that the "right to develop" includes the right to "a fair chance to recover the oil and gas in or under his land, or their equivalents in kind." *Garza*, 268 S.W.3d at 15 (citing *Gulf Land Co. v. Atl. Ref. Co.*, 131 S.W.2d 73, 80 (Tex. 1939)). It is this "right to develop" that urban operators may trespass against. Without the shield provided by the rule of capture, trespass remains a viable theory.

Additionally, "the injection of fluids and proppants across [a] boundary line that permanently changes the underground structure is not functionally different from a slant hole." Bruce M. Kramer, *Coastal Oil & Gas Corp. v. Garza Energy Trust: Some New Paradigms for the Rule of Capture and Implied Covenant Jurisprudence*, 30 *Energy & Min. L. Inst.* 11, 362

(2009). This is particularly true when "both the hydraulic and propped length [are] designed to extend beyond the property line." *Id.* Because the proppants change the character of the underground structure, the presence of such proppants could also constitute a continuing trespass.

The Texas Supreme Court has suggested that "the law of trespass need no more be the same two miles below the surface than two miles above" and that the *ad coelum* doctrine (the idea that a landowner owns everything from the sky to the core of the earth) "has no place in the modern world."[3] From the foregoing authorities, two principles of law should emerge: (1) a mineral rights owner has the right to develop his minerals and that right includes a fair chance to recover the oil and gas beneath his land, and (2) intentional and unprivileged deprivation of the mineral estate owner's right to develop his minerals by depriving him of a fair opportunity to produce those minerals is an unlawful invasion of a private property right and thus a trespassory invasion of another's real property rights.

2. Conversion

Because minerals become personal property once extracted and because the appropriate damages formula depends on the value of the minerals at the surface,[4] conversion may be a more appropriate label than trespass. Regardless, however, of whether the trespass was to personal or to real property, a cause of action could exist.

> "In the directional well subsurface entry context, courts have permitted the aggrieved landowner to recover conversion damages for oil and gas produced from the trespassing well. The good faith, bad faith dichotomy used to determine subsurface trespass

[3] Coastal, 268 S.W.3d at 11.

[4] The measure of damages for oil converted by unlawful means is the value of minerals at the surface. 56 Tex. Jur. 3d *Oil and Gas* § 719 n.2 (2013) (citing *Harrington v. Texaco, Inc.*, 339 F.2d 814 (5th Cir. 1964)). 56 Tex. Jur. 3d *Oil and Gas* § 719 (2013) ("a good-faith trespasser is liable in damages only for the value of the minerals removed less drilling and operating costs"). "[A] bad faith trespasser is a lessee who continues to enter under an oil and gas lease after its termination without a good faith belief in the existence of the lease." *Prize Energy Res., L.P. v. Cliff Hoskins, Inc.*, 345 S.W.3d 537, 557 (Tex. App.—San Antonio 2011, no pet.).

> damages applies in the conversion context as well. The list of potential defendants in a conversion action may exceed that for subsurface trespass, extending beyond those directly involved in the subsurface entrance."

Terry D. Ragsdale, *Hydraulic Fracturing: The Stealthy Subsurface Trespass*, 28 Tulsa L.J. 311, 344 (1993) (aggregating cases).

3. Private Nuisance

A private nuisance is "a substantial and unreasonable interference with the plaintiff's use and enjoyment of his real property." *Id.* The fundamental difference between trespass and nuisance is that a trespass invades "possessory interests in real property" while nuisance is an invasion of the "use and enjoyment of land." *Id.* at n. 169. Regardless of whether the mineral interest owner's right to develop the minerals is considered a "possessory" right or a "use" right, it is a right that urban operators may invade.

4. Strict Liability

"A trespass *quare clausum friget* cause of action is basically a strict liability tort based on the physical invasion of a possessory estate." Bruce M. Kramer, Coastal Oil & Gas Corp. v. Garza Energy Trust*: Some New Paradigms for the Rule of Capture and Implied Covenant Jurisprudence*, 30 Energy & Min. L. Inst. 11, 371 (2009). Urban homeowners, unlike the royalty-owner plaintiff in *Garza*, may hold a *quare clausum friget* cause of action for physical invasion of a possessory interest rather than a mere trespass-on-the-case cause of action for injury to a non-possessory interest. *See Garza*, 268 S.W.3d at 9–10 (describing trespass *quare clausum fregit* and trespass-on-the-case).

5. Confiscation

Confiscation, according to Black's Law Dictionary, is the "[s]eizure of property by actual or supposed authority." CONFISCATION, Black's Law Dictionary (9th ed. 2009). Taking private

property from micro-tract, urban homeowners and giving it to a large corporate conglomerate for the purpose of promoting economic development and such development's reciprocal benefits to society smacks of the wildly unpopular *Kelo v. City of New London* decision, a case that former Supreme Court Justice John Paul Stevens described as "the most unpopular opinion that I wrote during my thirty-four year tenure on the Supreme Court. Indeed, I think it the most unpopular opinion that any member of the Court wrote during that period." Justice John Paul Stevens (Ret.), *Kelo, Popularity, and Substantive Due Process*, 63 Ala. L. Rev. 941, 941 (2012). To be fair, operators generally represent not only their own interests, but also the interests of their lessors.

Many states, including Texas, passed laws in direct response to *Kelo*, "restricting [the state's] power to use eminent domain for economic development." *Id.* The Texas legislation "shifts the burden of proof in public use cases to the condemning authority." Ilya Somin, *The Limits of Backlash: Assessing the Political Response to Kelo*, 93 Minn. L. Rev. 2100, 2137 (2009). Furthermore, the Texas legislation "forbids private-to-private condemnations under statutes other than those allowing the use of eminent domain for blight alleviation and 'community development.'" *Id.* When a small-tract, urban homeowner has his minerals drained without compensation after a Rule 37 hearing, his development rights are essentially transferred without compensation to other private parties, namely the operator and its lessors, so that those parties can engage in economic development that primarily benefits themselves. Such practice should be changed to afford compensation to the aggrieved landowners.

Furthermore, Rule 37 hearings may not adequately consider private property rights. "State conservation agencies have always treated the prevention of underground waste as their primary responsibility." Bruce M. Kramer, Coastal Oil & Gas Corp. v. Garza Energy Trust*:*

Some New Paradigms for the Rule of Capture and Implied Covenant Jurisprudence, 30 Energy & Min. L. Inst. 11, 371 (2009). Because the concept of protection correlative rights takes a back seat to waste prevention in administrative proceedings, the common law is the best protector of individual rights. *Id.* Such is the case at least in part because "[c]ourts are not insulated from political considerations, but are certainly more insulated than either the legislative or administrative branches of government." *Id.* In Rule 37 hearings, protection of individual rights is at best a secondary concern, likely because MIPA is seen as the appropriate forum for protecting individual rights. MIPA, however, is outdated and rarely used.[5]

i. Public Policy

Regulating all significant value out of urban homeowner's development rights in order to decrease production costs to operators and increase the state's tax revenues can hardly be considered "community development" or "blight alleviation." *See Garza*, 268 S.W.3d at 33–34 (discussing the State's interest in encouraging production and increasing tax revenues on production). Community development and blight alleviation are the only permissible purposes under the Texas *Kelo*-response act for sanctioning the transfer of private property from one party to another. Tex. Gov't Code § 2206.001.

6. Negligence

"A trespass on the case cause of action . . . is not all that different from a negligence cause of action." Kramer, *supra* at 359. This cause of action requires proof of actual injury and is available to the owner of a possibility of reverter. *Id.*

When a mortgage predates a mineral lease, foreclosure of the mortgage extinguishes the lease. Eugene Kuntz, *A Treatise on the Law of Oil and Gas*, § 52.3 p. 323 (Matthew Bender Rev. Ed.); Todd v. Hunt, 127 S.W.2d 340, 344 (Tex. Civ. App. 1939). Generally, the mortgage

[5] In both 2009 and 2010, only five MIPA cases were filed. John Camp, *supra* at 37.

contract on a piece of residential real estate requires lender consent to a mineral lease. Despite this requirement, leases are often entered into without lender consent. In Rule 37 hearings, the lender typically does not get notice and an opportunity to be heard at the proceeding, despite arguably being an "owner of record,"[6] even if only an "in rem" owner. As a result, foreclosure sale purchasers are finding themselves the owner of unleased mineral rights affected by a Rule 37 spacing exception that happened without notice and an opportunity to be heard either by the original lender or the foreclosure sale purchaser.

In addition to the aforementioned causes of action, these foreclosure sale purchasers may hold a negligence cause of action. A prudent operator would have obtained lender permission and a subordination agreement. The operator breached that duty to act prudently by tortuously interfering with the mortgage contract to the lender's detriment because the lender had the right to apply the mineral estate toward the satisfaction of its promissory note. Such breach caused damages to the foreclosure sale buyer because the buyer took the property subject to a Rule 37 spacing exception that allowed his minerals to be drained from the date of purchase onward. The purchaser was damaged by the amount of minerals drained starting on the date of purchase. The purchaser cannot drill an offset well, arguably cannot be heard before the Railroad Commission on the Rule 37 exception permit unless he can convince the Commission to reopen the case, and can get MIPA relief, if at all, only from the date of the interim escrow order.

i. Damages Would Be Calculated Based on the Market Value of the Minerals At the Surface Produced After Lease Termination Due to Foreclosure

"[T]he common law of trespass and other wrongful conduct operates as a limitation of the rule of capture, and by the very nature of rules of ownership and capture, the landowner's right to produce his or her fair share of oil and gas from a common pool is limited to legitimate

[6] 16 Tex. Admin Code § 3.37(a)(2)(A)(iii).

operations." 56 Tex. Jur. 3d Oil and Gas § 706 (2013) (quoting *SWEPI*, 139 S.W.3d at 341). When the rule of capture is limited, Texas courts have laid out different damages calculations depending on whether the wrongful conduct was in good faith.

The measure of damages for oil converted by unlawful means is the value of minerals at the surface. 56 Tex. Jur. 3d *Oil and Gas* § 719 n.2 (2013) (citing *Harrington v. Texaco, Inc.*, 339 F.2d 814 (5th Cir. 1964)). "[A] good-faith trespasser is liable in damages only for the value of the minerals removed less drilling and operating costs." 56 Tex. Jur. 3d *Oil and Gas* § 719 (2013). "[A] bad faith trespasser is a lessee who continues to enter under an oil and gas lease after its termination without a good faith belief in the existence of the lease." *Prize Energy Res., L.P. v. Cliff Hoskins, Inc.*, 345 S.W.3d 537, 557 (Tex. App.—San Antonio 2011, no pet.).

When an operator does not act in good faith, the "plaintiff recovers the highest value which oil of a like grade and quality reached between the date of production and the date on which the suit is filed." 56 Tex. Jur. 3d Oil and Gas § 719 (2013). Where the act is in good faith, however, the value is determined as of the date of production and the highest-intermediate-value rule is not applied. *Id.* (citing *Corrigan v. Shell Petroleum Corp.*, 62 S.W.2d 663 (Tex. Civ. App.—Austin 1933, no writ)). Also, interest is owed. *Kishi v. Humble Oil & Ref. Co.*, 10 F.2d 356, 357 (1925).

E. Public Policy

In *Garza*, the Texas Supreme Court received amicus briefs from "every corner of the industry" and "all oppose[d] liability for hydraulic fracturing, almost always warning of adverse consequences in the direst language." *Garza*, 268 S.W.3d at 16–17. Now that reverse MIPA is viable, the chicken-little arguments should fade. Also, are drainage damages so different from

the *Findley* deal?[7] Could drilling possibly stop because a small percentage of landowners want to be compensated for their net share of minerals produced rather than receiving only up-front payments and a royalty? Under a joint operating agreement, the operator still charges market rates on operations, which assumedly includes a healthy profit margin. Affording reasonable relief to unleased, urban, micro-tract owners affected by spacing exceptions would not contravene the longstanding State of Texas public policy of encouraging mineral development.

[7] Whether the *Findley* deal terms are fair is a topic beyond the scope of this article. Those interested, however, should follow the MIPA application of Vantage Fort Worth Energy, LLC, Docket Nos. 09-0284751, 09-0284752, 09-0284753, and 09-284754, that was first heard before the Railroad Commission on October 31, 2013.