989-9614

duty to supplement? —

geophysicist — evaluate/testify

difficult scheduling

★ Subpoena April 2001 "no seismic" June 18
★ Ted Galowski, witness resigned
Dean Hornig — took over
started over — old hearing, returned to seismic
discussed w/ EOG
EOG sent seismic log - public log
8-30
9-3 — got

★ shut-in in July — on order of Division

★ Terry Durham on staff, geophysicist

Scott: client would want to know about well restored to production

Scott — 30 minutes
Bill — 5 witnesses
Tom — 3 witnesses

10-21 Newberg

Bill Carr, Newberg Exploration
Great Western
CO+F Resources
Layne

Scott Hall, Raptor Natural Pipeline

Tom Kellahin, Redrock Operating LLP Co.

Carr: simple case
2 questions: ① $ 34/Morrow - one reservoir or 2 pools?
② existing spacing unit is E/2?

facts: State lease N/2 terminated 1999
rebid - w/out stipulation Great Western Jan 2000
APD - N/2 (C102) 2 (N/2??)
completed
July 2000, OCD calls - pool boundary in center of $
Newberg filed admin app., 2 160-acre units
NE/4, SE/4

what about SW/4?

Newberg called Division - August nomenclature hearing

Is Morrow one pool or two?
if one - N/2 can be approved
if two - (fault) - then should be E/2

Mistakes were made by Newberg - OCD, Land office, Raptor

Geology - pressure communication across section
no fault possible

(2) historic E/2 unit
communitization agreement terminated 3-31-91
all unit terminated as of the date the SCO cancelled

N/2 royalty interest owners developed prospect brought it to Newberg - their interests would be cut in half -

Kellahin -

key issues: OR owner 10% in S/2
5% interest in Newberg well

§34 - collective - Morrow -
E/2 -
W/2 gas storage unit

Newberg's proposed to separate out GRE sand (lower Morrow)

historically assign 320 acres to Morrow
Llano - 4 bct (lower B Morrow)

* (104(e) - permits still in Morrow?)

N/2 standup in Morrow
Newberg's interpretation is for E-W standup to make claim that GRE stringer doesn't extend into SE/4
material balance doesn't work unless production included on other side of fault
mud log - B-9

Newberg didn't do much research

adjoining spacing unit orientation ???

produced 1 bcf before shut-in

ORE drawing SE/4

Land Office - no objection to NSL if everyone else agrees
12-11-01 - letter: all issues resolved before the Division

Hall: wants latitude
go through exhibits - extended

production / gas storage facility - a hybrid
certificated by FERC

1973 - unit operator bought reserves - left reserves in ground to provide cushion gas

2500 lbs psi

federal & state unit side by side

surface ownership reflects cost of use
if hydrocarbons produced - its attributed to mineral owners

Raptor contacted BLM - original lessee - reinstated

Land office apparently didn't reinstate

LOTE worked out problem w/ Yates

Canyon changed LOTE, changed name to Raptor

j: Storage unit takes in entire §34?

Look at 3C - history

Ex. 13 - communication can't be ruled out with absolute certainty

relevance: (Raptor) unit operator must report injection must also report C-115 - gas volumes

Newberry Ex. 9
- approved w/2 unit (from 1979)
presents an "administrative obstacle"

a "contract right" to put a well in E Gramma Ridge, in E/2, §34

"boundary" ~~d~~: Dr. Lee

Carr: well in SW/4 → dedication changed to S/2 unit

Bob Shelton

land manager

dismiss app. in SE/4

~~1st~~ 1st Morrow SW/4, §34
Llano well pt A'ed, 11-01 ceased production in '91
started in '84

W/2 - ROW agreement / storage agreement (Gramma Ridge Morrow)

R-11768 - denied app. - with Nomenclature case

visited w/ Kaitz - explained Nomenclature process - adjust pool boundaries -

Redrock ORR
assigned to ~~Reba Redrock Resources~~ 5-27-97 ~~3-1-98~~ (Redrock EX/O)

Reba Resources 3-1-98

Llano - had E/2 acreage dedication terminated 3-1-91
well did not produce
spacing unit ceased 3-1-91 (OCD rules?)

Tim Cochran @ Redrock was previously @ Lo+E & the one responsible for gas storage unit

produced if not.. royalties disbursed on basis on N/2

Exs. 1-2 - admitted

=

Kellahin cross:

Donna Pitzer call -
w/2 Gramma Ridge - Storage pool
E/2 Gramma Ridge E - Newberry pool

when filed APD, unaware of 2 pools -

→ believes w/2 dedicated to gas storage limited to purposes of gas storage

R-11611 - special pool rules re: gas storage unit

well drilled in 3-00, 6-00 producing Morrow well
APD, acreage dedicated

Newbury
Great West
CMM
} drilled

Hobbs called after completion report filed
crossed pool boundaries

talked to Raptor, SLO (Ex. 8)
~~[illegible]~~
Natural gas -

trying to operate Morrow as one
will not perforate zones that implicate storage unit
no royalties from Raptor - not included in unit

admin. apps. filed 12-01
objection from Raptor (ORRI)
waiver from EOG
" " SLO

well shut-in

Newbury contacted EOG - negotiated and obtained
EOG - working interest is in common in E/2
and N/2

SLO - Llano well report - Newbury plugged
well subsequently

if push boundaries - will dedicate N/2
have moved

"asked Kantz to take action?" relevance?

Phil Brewer gave them a title opinion on N/2
did not alert to storage unit

letter to attorneys re: exhibit book for Steve Brewer

re: Llano No. 1
evaluated wellbore
told SLO had no further plans for well
no additional tests performed
no test made in GRE
no mechanical entry
[redacted]
worked at SE/4 - no potential

why acquire EOG interest?
did it to protect interest, not to exploit
resources in SE4

re: fault
regional maps show different interpretation

re: Nearburg well
1 bcf gas?
well has paid out -
paying ORR in NE/4

Dear Hornung

geologist
supervisor at N.M.

Chevron / Terreco
20 yrs. in Morrow / SE-NM

supervisory of exploration

~~Pogo~~
prospect brought Jan. 2000

received history of pool
exhibits from 1974 hearing
subsurface data
public sources-
OCD

geologic interpretation
no seismic-based on well control

March 19 Ex. 3 - straight subsurface fault 500' - 1000'
curved fault not typical

well drilled, came in high, not low

Ex. 4
[GRM 4
[Getty 35

got top of Morrow clastics correct

concludes - fault not there

ORE - no productive sands in SE/4

concludes - no communication w/ storage unit

3-6, 8-11

Golowski - no longer a geologist @ Nearburg

Nearburg
cross section (Ex 5) prepared before examined the mud log at Redrock -

★★ below Morrow main sand - evidence of GRE sands below -

mud log - shows "lithologic body" below main sand; now believes it is a remnant of GRE

isopach should include GRE on ~~isopach~~ as 6' of gross sand instead of as represented on Ex. 9 (Nearburg)

★★ re: orientation - of GRE sand
lack of data points is NW/4 to anchor data points there - arbitrary -

"hypothesis worked because of depositional patterns, NE-SW"

disagrees this is a channel system -

mud log - sandy sands with shale

"strike oriented" -

Nearburg at one time had a map that showed a fault in §34

★ the only evidence used to get rid of fault was the supposition that the L1 gas well would have been completed but for current

that would communicate w/ gas storage unit (1290?)

Redrock E-4 shows local fault in §34, geologist named galowski

this may have been used to show L6+E that no communication —

re: Neerburg 9
gross/net feet of pay —

used engineering data to conclude that the pod is much smaller

re: RFT data

Redrock exhibit 6 - 6RE sands oriented N/S (not E-W)

facies may change orientation when looked at closely

Morrow B - marine
Morrow B above - non marine ? fluvial?

overall N/S - but areas w/ marine influence -

lower portion of 6RE sand has marine influence of fracture E-W

general trend is fluvial, eg N-S

members coarsening up - "marine"

George Friedeen

Oil Property Engineering
Consulting engineer
Midland
BS Pet. Eng.
Tenneco, Enron, Coastal 26 years exp.
16- Permian Basin

pressure history of § 34
development " " "

pressure data - NO ~~fault~~ fault
GRE- 1.2 bcf, not in communication w/ storage unit

Ex. 18
RFT
Repeat Formation Testing log
obtains pressure data

Llano 34 well
September, 1979 (shortly after drilling)
had to prove not in comm. w/ gas storage unit

morrow perfs. not in communication w/ gas storage
main sand " " " " "
bottom " " " " "

pressure @ gas storage substantially below
gas storage sand.

only well producing in 1979 - drawn down
60s

pressure data shows that storage sands not associated with major sands in Llano well

re: Ex. 19
1966 pressures
1973 pressure minimum
1973 – pressures vary after that – as used for gas storage

re: Ex. 20
11-16-79 memo.
Mgr. of Engineering / Mineral Inc.

Morrow B – No perfs. – gas storage unit

re: Ex. 13, 12
Redrock letter, title opinion

reserve estimates → 1.1 bcf to 1.9 bcf
used P/Z curve, decline curve analysis
very hurried study

since hearing – more study, shut-in pressure results

re: Ex. 21
Cum v. P/Z

EUR = 1.2 bcf
gas in place = 1.4 bcf

5300 → 1000 = shows small reservoir (page 2)

Volumetrics

no communication w/ gas storage

Ex. 22
§25

Ex. 23 – E/2 §34 Assignment

§34 one common pool
no faults,
no interruption
no reservoir
everyone has known since 1979 –
but communication w/ gas storage
was being avoided – everyone ~~knew~~
knew that communication w/ gas storage
w/ no interruption – would protect

=

Kellahin

M: RFT Log
22 tests –

depletion in Llano well – in gas storage
interval –

* * has not looked for other wells that could
explain depletion –

* * other gas storage wells in 4 of 31[10] on same side
of fault may explain depletion

witness
(did not look @ this issue)

3600# ± Llano

#4	2~~4~~20
#1	2875
#3	3,250
#2	3,720

Redrock 7

- witness stumbles
- seems consistent w/ pressure data

terrible witness
hasn't looked outside §34

well filer for storage unit wells

Richie Cox
Midland
Great Western Drilling Co.
BS, MS – Geology
Marathon, BTA, Great Western
Permian Basin

geological study –
reviewed prospect initially

no seismic, well control only

marine beach or offshore bar deposit
perpendicular to depositional dip –
therefore consistent w/ deposition pattern
N/S

zone has not been tested in Newberg well –

not complicated by faulting –

Newberg concludes

10-22 Redrock case

Hall: C-105s show
GRMU #1 8-19-65
#2 3-18-66
#3 12-1-66
#4 6-1-65
§10 Llano 3-16-66
(withdrawn from the unit)

Kellahin: seismic data
withdrawn

James Brazina
consulting geologist (20 yrs.)

fairly recently retained

GRE sand - orientation
Newberg excluded Llano well
used all data pts.

N-S fluvial deltaic, incorporating E/2 of §34

Ex. B-4

gross thickness of ORE sand

looking @ gamma ray logs

Llano has 6' of clean sand on gamma ray

S4/4 - no ORE sand

Ex. B-5

used 8% porosity cut-off (Neuburg used same)

must [compensated neutron density log - 8% cut off
sonic log

orientation must be same as the gross sand orientation

faults: faulting post-depositional
geometry of sand body pre-existing

N: Neuburg's 22

Neuburg doesn't honor Llano gamma ray or mud log -

fault would wipe out Neuburg reserves
can't contour reserves estimated

Redrock B-2

Splinter fault
300 feet per mile - NE

* faulting caused anti-regional dip

rate of regional dip interrupted near §34—
caused by splinter fault in §34
(from main fault)

Ex. B-1

no GRE sands in W/2

fault has no significance
simply no pre-fault GRE sands in the E/2

No evidence that GRE sands present in NW/4

Ex. E-8

another possible source of Llano well depletion

Llano well communicates w/ Superior
Government # #1 in §.10

low pressure in Llano could be explained by
~~lost pressure~~ depletion from Superior well
see E-9

~~Ex~~ Ex. B-3

GRE Sand not located in W/2 of §34

Carr Cross

re: B-4

8% a reas. cut-off for porosity to have a producable reservoir

sand bodies oriented in N/S
gross sands

separate small pod in §35
interprets a channel in between bodies

re: Newberg 22

net pay
No channel in Newberg's channel

=

if fault present - reservoir not big enough in N/2

=

N/S trend - Bill suggest

=

B-7
shows N/S channel

doesn't agree w/ change

=

B-5

only 4 wells w/ net sand depicted
(NW/SE trending contradicts interpretation shown)

no perforations in Llano well — (so what?)

B-2

placed fault across §34 because of pick on top of Middle Morrow, together with the regional dip, shows uplift

fault placed where Mr. Galowski (Veralms) placed fault

- throw of 50' - 100' expected for fault in §34

((Carr: B-2 map shows no throw?))

John Wells

Pet. engineer

similar methodology to Friesen

B_g, Z (D-5, D-6)

planimetered volumes from Blaszka's sand volumes (& obtain pore space) (D-1)

gas in place -	1.9 bcf
N of fault	.1 bcf
S of fault	1.8 bcf

P/Z (D-2)

initial pressure 6837
divided by Z = ~6,000 psi

other plots based on pressures / production
3057 psi 555 mmcf
1562 psi 1 bcf

P/z
6.1 P – 1.6 bcf on D-1
(volumetric calculation = 1.8 bcf)

initial pressure – uncertain –
using static pressure gradient
Newburg 20 shows 7,000+
divide by 13,145 – pressure gradient greater than normal
(7900 gives a .6 gradient – unlikely)
elected .5 gradient as a res. gradient
to arrive at initial pressure
low permeability will flatten here

D-1 =
D-9 ∅ testified concerning special project rules!!

on L6+E

=

retained by Raptor w/ L6+E simultaneously

=

has an opinion on whether 2 pools –
won't give!!!

=

Hall objection

=

project area – all §34
testified: one common source of supply –
project area 5-21-01
hearing,
Case No 12,588
12,441

lateral extent of Morrow not precisely known

RFT loss.

re: D-1
based on geology

P/Z or geology?
depends on number of data points –

in this – neither is more reliable

=

[redacted]

=

discussion of boundary survey – gas
storage
unit

=

Carr/Nearburg

Cox (recalled):

Nearburg Ex. 25

Storage unit sand absent NW §3

Could not have contributed to depletion seen in Llano

nor could well in §10 have drained Llano well

★ evidence of fault in Division record

fault not present ???

Great Western Exhibit – E/W orientation
(when selling prospect)
Newburg No. 17

Red rocks explain could not how ~~Ancestor~~ deposits occurred

COX –

GRE in marine –

N/2
move pool boundaries 1/2 section E
address storage issues – particular w/2 unit
★ don't know where boundary is – need to know to
ensure that not ~~taking~~ producing native gas for which
not paying royalties
★ ask Division to investigate
get boundary information –

Q: Why don't we make storage
units prove up boundary ??

Nearbys

703
235
3750

Storage issue

Mineral Leasing Act 30 USC § 226(m)
storage facilities

43 CFR § 3105.5-4

Texas Eastern Transmission Corp. (lease for pure storage terminates when annual rental payment not made)
14 IBLA 361

Law of Federal O.7 al Gas Leases
§ 23.12, § 18.10
see- 30 USC § 226(m)

"not clear whether a separate underground storage lease when an existing O+G lessee exists & covering the same lands."

BLM regs. ⇒ storage
43 CFR 3105.5-1 to 5-5

(1983. [illegible]) American Natural Gas Production Co.
49 IBLA 230
existing oil al gas lease modified to extent to permit storage unit

M. Robert Paglee
59 IBLA 192
withdrawal lease in formation already committed to gas storage unit
- special casing al cementing for protection of storage unit

5 Summers § 757 (??)

~~10.3t~~
~~deliberations~~
~~order~~

State Lease K-3592-1 covered N/2 § 34
canceled on 1-13-99 for non-payment
of rentals

New lease issued 2-1-2000 (VO-5683)
made subject to Lessee's right to inject, withdraw
and store gas pursuant to the "unit agreement"
apparently Commissioner agrees that right to
inject, withdraw and store "extraneous" gas
(defined as gas injected - not produced)

Amendment appears to make production of
indigenous gas subject to pre-existing rights
to inject, withdraw and store extraneous
gas —

RSTP 2:30pm

0+6 R

54:491, 501 ✓

~~93:9?~~

~~[redacted]~~

~~58:455~~ (1x)

~~76:242?~~

6:819

7:37

~~94:240~~

~~71:371~~

~~[redacted]~~

46:101

~~48:456~~

~~56:398~~

~~68:49~~

~~[redacted]~~

~~64:205~~

~~64:542~~

~~99:117~~

~~61:368~~

~~64:503~~

~~78:83~~

~~[redacted]~~

who owns the injected gas?

☆ 48:516

~~☆ 56:398~~

☆ 14:253

Humble v. West 508 SW2d 812

94 ACR2d 543

Bezzi v. Hocker 370 F.2d 533
(10th Cir)

- ✱ Question: if Raptor bought out the other interest owners, is there any longer a question of what constitutes "indigenous gas"?
- ✱ Should Raptor be Reporting production of indigenous gas regardless of common ownership?
- ✱ What is a "gas storage unit" and what is its relationship to "a unit" or a "proration unit"

ELLIS et ux. v. ARKANSAS LOUISIANA GAS COMPANY

United States District Court
Eastern District of Oklahoma
March 31, 1978—Civ. No. 76-211
450 F. Supp. 412

Storage of Gas: Underground Storage: Relative Rights of Mineral Owners and Surface Owners—Prescription—Acquisition of Storage Rights from Surface Owner by Prescription.

Arkla, successor owner of once-producing oil and gas leases covering a now-depleted gas producing formation, obtained a gas storage lease from the owners of the severed minerals thereunder, and also an easement from the surface owner granting the right to lay pipelines and install a gas injection well. The surface owner brought this action to enjoin Arkla from its storage operations and to recover damages for unauthorized use of plaintiff's lands. Held: Judgment for defendant. The surface owner, not the mineral owners, had the right to grant subsurface storage rights, and the written easement obtained from the surface owner here did not convey such rights. Nor did the mineral owners have anything to lease in a depleted stratum. Where the storage reservoir was well defined and no commingling occurred with unproduced gas, Arkla did not lose title to its stored gas upon injection. However, Arkla had continuously and openly conducted its storage operations for more than the statutory period (15 years) with the actual and constructive knowledge of the surface owner and his predecessors in title, under color of the otherwise ineffective oil and gas leases, gas storage lease, and easement, and therefore acquired a prescriptive easement for the storage of gas beneath plaintiff's lands.

MEMORANDUM OPINION

MORRIS, Chief Judge.

The principal question in this case has not been decided in Oklahoma and remains undecided in the overwhelming majority of jurisdictions in the United States. The question

is: when the oil, gas and other minerals have been severed by conveyance from the fee simple estate in a tract of land, and subsequent to severance natural gas is injected in and under that tract of land as a part of an underground gas storage reservoir, from whom must the injector secure permission to store natural gas?

Plaintiffs, James C. Ellis, and Wanda Lou Ellis, his wife, are the surface owners of approximately 78 acres of land in Pontotoc County, Oklahoma. They seek to recover damages and injunctive relief for the unauthorized use by defendant of an underground strata of plaintiffs' land for the storage of natural gas. Plaintiffs also seek damages for the unauthorized use of an injection well located on plaintiffs' land and claim that an easement given by plaintiffs to defendant which grants defendant the right to operate a gas injection well on plaintiffs' land should be rescinded for lack of consideration. Mr. Ellis will sometimes be referred to herein as plaintiff.

The defendant denies any liability to plaintiffs, claims it has the right to inject gas by virtue of certain oil and gas leases, gas storage leases and the gas injection easement granted to defendant by plaintiffs. Defendant further claims that plaintiffs' action is barred by the doctrine of prescription.

The case was tried to the court without a jury. At trial neither side introduced into evidence the instruments which effected the severance of the oil, gas and other minerals from the surface and because the court viewed the record as incomplete without such instruments, the court invited counsel to submit them for the court's consideration and to make them part of the record. By stipulation filed on November 22, 1977, counsel so stipulated.

Plaintiffs acquired the surface of approximately 76 acres of the land in question in 1963, referred to in this action as Tract I; they acquired the surface of approximately 2½ acres of the land in question in 1972, referred to in this action

as Tract II (Tr. 5 and 19). The surface to Tract I had been severed from the oil, gas and other minerals in 1939 in a deed from O. W. Skirvin to Eunice Davidson which reserved to Skirvin all of the oil, gas and other minerals (Stipulation filed November 22, 1977). Eunice Davidson conveyed the surface of Tract I to her son, Glen D. Davidson, in December of 1962 or January 1963 (Tr. 117) and shortly thereafter in 1963 Davidson conveyed the surface of Tract I to plaintiffs (Tr. 5 and 120).

The surface of Tract II was severed from the oil, gas and other minerals in a series of deeds commencing in 1921 with a complete severance of all oil, gas and other minerals from the surface being effected on July 16, 1945. Plaintiffs have always been surface owners only; they have never been the owners of the oil, gas and other minerals in and under Tracts I and II (Stipulation filed November 22, 1977).

In 1928 the predecessor in title of defendant secured gas leases from the then owners of Tracts I and II. These leases did grant, lease, let and demise unto the lessee for "the *sole* and *only purpose of mining and operating for gas* and laying pipe lines, building tanks, towers, stations and structures thereon, to *produce, save* and take care of said products" on land embraced in Tracts I and II (Emphasis added). Each of the two leases was for a flat term of 50 years, during which 50 year term the lessee was to have "the sole and exclusive right to *prospect* for and *produce,* use and market gas, including the natural gasoline . . . ." (Emphasis added). The leases further provided that the consideration paid at the time of lease execution by the lessee to the lessor relieved the lessee of any "obligation to *develop* said lands for gas or pay any rental or royalty on the production thereof, and that no *implied obligation for development* shall apply to this lease as to offset wells or otherwise, and the amount and extent of *exploration* and *development* of said lands shall be optional with lessee only." (Emphasis added). The leases further provided that "failure to develop said lands or any part thereof shall not be construed as an abandonment

of the whole or part of the land." (Defendant's Exhibits 1 and 2).

In 1939 the first mineral severance occurred. The deed effecting the severance of the minerals from the surface in Tract I provided in part as follows:

> It is especially understood and agreed by the parties hereto that ALL interest in and to all of the oil, petroleum, gas, coal, asphalt and all other minerals of every kind or character in and under, and that may be *produced* from the above described land, is hereby reserved by party of the first part, together with the *right of ingress and egress at all times for the purpose of mining, drilling and exploring* said lands for said minerals and removing the same therefrom, and with the rights of way, easement and servitudes for pipe lines, telephone and telegraph lines, for tanks, power houses, stations, gasoline plants and fixtures for *producing,* treating and caring for such products, and housing and boarding employees, and all other rights and privileges necessary, incident to, or convenient for the economical operation of the said land for the *production of said minerals,* . . . (Emphasis added).

Exhibit A Stipulation filed November 22, 1977.

Three deeds effected the severance of the minerals from the surface of Tract II, the last one being executed in 1945. These three deeds provided in part as follows:

> 1. WITNESSETH: That said parties of the first part in consideration of the sum of One Dollars, ($1.00) and other valuable consideration, the receipt of which is hereby acknowledged, do by these presents grant, bargain, sell and convey unto the said party of the second part, his heirs and assigns, an undivided one-half interest in and to all oil, gas and all other mineral substances in and under the hereinafter described land and the right to *extract and market the same,* together with *all right of ingress and egress,* at all times, *for the purpose of prospecting* for said

oil, gas or minerals, including, the right to occupy and use so much of the surface of said land as may reasonably be necessary to carry on the work of *extracting, mining, piping,* . . . (Emphasis added).

Exhibit B to Stipulation filed November 22, 1977.

2. EXCEPT Grantor does hereby except from this grant and reserves unto himself, his heirs, executors, administrators, and assigns, an undivided one-fourth (1/4th) interest in and to all of the oil, gas and other minerals, in and under the surface of all the above described lands . . . together with the free right of ingress and egress thereto, and the right to use and occupy such portion of the land as may be reasonably necessary for the purpose of *operating, drilling and marketing the production therefrom.* (Emphasis added).

Exhibit C to Stipulation filed November 22, 1977.

3. It is especially understood and agreed by the parties hereto that Grantor's undivided interest in and to all of the oil, petroleum, gas, coal, asphalt and all other minerals of every kind or character *in and under, and that may be produced from* the above described lands, is hereby reserved by party of the first part, *together with the right of ingress and egress at all times for the purpose of mining, drilling, and exploring said lands* for said minerals and *removing the same therefrom,* and with the rights of way, easements and servitudes for pipe lines, telephone and telegraph lines, for tanks, power houses, stations, gasoline plants and fixtures for producing, treating and caring for such products, and housing and boarding employees, and all other rights and privileges necessary, incident to, or convenient for the economical operation of the said land *for the production of said minerals.* (Emphasis added).

Exhibit D to Stipulation filed November 22, 1977.

In 1946 and 1947, *subsequent to the severance* of the surface from the oil, gas and other minerals, the *mineral interest*

owners executed instruments denominated as gas storage leases in favor of Southwest Natural Gas Company. These gas storage leases were thereafter acquired by the defendant.

The gas storage lease on Tract I provided in part as follows:

> WHEREAS, Second Party is desirous of obtaining a lease on the above described premises for the purpose of *introducing and storing gas in,* and extracting said gas from, any sand or formation down to a depth of 1,500 feet deemed suitable by second party for such purposes but particularly in and from what is commonly known as the Cromwell Sand found at approximate depth of 1,300 feet;
>
> NOW, THEREFORE, for and in consideration of the sum of Ten Dollars ($10.00), cash in hand paid by second party, receipt whereof is hereby acknowledged, first party hereby grants and leases unto second party the exclusive right and privilege of *introducing and storing gas in any form and extracting and taking such gas from said sand or sands,* either through a well or wells now or to be situated on said premises, or through wells located on adjacent and surrounding premises, and for the purposes of laying pipe lines, building power stations and structures, warehouses, dwellings, telephone and telegraph lines used in conjunction with the storing and extracting of said gas, together with the right of ingress and egress, and the further right to drill any additional well or wells on said premises in such locations as deemed advisable by second party *for the purpose of introducing or extracting gas already introduced and stored.* (Emphasis added). (Defendant's Exhibit 3).

The gas storage lease on Tract II contained virtually identical language with minor differences in language being used to identify the parties (Defendant's Exhibit 4). The *surface owners did not join* in the execution of the gas storage leases.

Tract No. I is essentially the East Half of the Northeast Quarter of Section 17, Township 6 East, Range 4 North,

Pontotoc County, Oklahoma, with a small piece out in the northwest corner (Plaintiff's Exhibit 2). When plaintiffs acquired Tract I there were four pipelines running across the land. Three of those pipelines run essentially north and south and almost the full length of Tract I (Tr. 7, 118, 119). Portions of at least two of those pipelines were on the surface and were visible a long time before plaintiff bought Tract I (Tr. 119). The 8" and 4" lines going straight to his house could be seen on top of the ground (Tr. 132).

Plaintiff is a building contractor (Tr. 6). He has lived in this area all of his life (Tr. 18). Shortly after he acquired Tract I he built a home on his land. It is a three minute drive away from Ada (Tr. 12). He later made an addition to his home, converted his garage to an office and started a 36 foot long car port (Tr. 7). It was discovered during the construction that one of the defendant's pipelines ran beneath the corner of plaintiff's house and would also be beneath a swimming pool he proposed to build. (Tr. 7, 81, Defendant's Exhibit 5). Plaintiff immediately contacted a representative of the defendant (Tr. 7). Thereafter defendant's representative Mr. Courtney came out to plaintiff's house and discussed the matter with him at length. There was some discussion concerning who should pay the cost of rerouting and relocating the lines, whether or not the defendant had any easements for the initial laying of the lines, and whether the defendant had permission to use the gas injection well, which, together with the blow pit, is located 450 or 500 feet south of plaintiffs' house (Tr. 11-12 and 81-85). As a result of these conversations, an instrument dated June 3, 1967 and signed by plaintiffs was executed and delivered by them to the defendant (Plaintiffs' Exhibit 7) and the pipeline which ran beneath the corner of their house was taken out of use insofar as the transmission of gas was concerned and the gas line was rerouted (Tr. 84-85; Defendant's Exhibit 5). The easement signed by plaintiffs grants to the defendant the right-of-way to maintain, alter, repair, operate and remove pipelines for the

transportation of oil, gas or products of oil and gas on, over and through certain lands described as follows:

> The existing four (4) pipelines on the surface across part of the E/2 NE/4 Section 17-T4N-R6E, including a Gas injection well for gas storage and a pit.
>
> Relocation of approximately 450′ of 8″ Transmission Line #634 across part of the North End of the E/2 NE/4 Section 17-T4N-R6E, lying East and South of dwelling.

The instrument recites that the consideration paid to plaintiffs was $5.00. The $5.00 was not in fact paid (Tr. 96-97). The defendant's cost of installing, rerouting and relocating the pipeline was $2,736.34 (Defendant's Exhibit 7; Tr. 158).

Tracts I and II are located within the confines of what is sometimes referred to as the Ada Storage Facility. (Plaintiff's Exhibits 3 and 4). The sand strata which is being used for the underground storage of gas by the defendant is the Upper Cromwell Sand. It is bounded on all four sides by an impermeable barrier of some type and thus makes a good underground gas storage reservoir (Tr. 46-47). The total acres inside the reservoir limits are 1230; of those 1230 acres plaintiffs own approximately 78 (Tr. 49, 44 & 64). The average pay thickness of the reservoir as a whole is 100 feet with the average pay thickness in and under plaintiffs' land being 96 feet (Tr. 49; Plaintiff's Exhibit 5).

The reservoir comprising the Ada Storage Facility (the Upper Cromwell Sand) was originally a gas only producing reservoir; there was never any oil in this reservoir (Tr. 48). The reservoir was discovered as a producing gas reservoir in 1922, it produced more than 23 billion cubic feet of gas before it was depleted in 1928 (Tr. 50). "The volumes of recoverable native gas originally in place therein were depleted prior to the commencement of gas storage operations . . ." (Findings of the Oklahoma Corporation Com-

mission on October 3, 1973, p. 3 of Order attached as Exhibit A to Exhibit A of Plaintiff's Request for Admissions. See Tr. 75). It has been used continuously since 1949 by the defendant for underground storage of natural gas and some use was made of it as a storage facility prior to that time (Order and Journal Entry of Judgment of District Court within and for Pontotoc County, Oklahoma, filed December 16, 1975, a part of plaintiffs' request for admissions; Tr. 75). Plaintiff's expert witness, Victor W. Pryor, testified that it had been used as an underground storage facility for approximately 50 years (Tr. 48). There are nine gas producing-injection wells in the reservoir (Plaintiffs' Exhibit 3, Tr. 49). Two of the nine injection wells are located on plaintiffs' Tract I (Plaintiffs' Ex. 3; Tr. 7) although one has been plugged (Tr. 126). A third injection well, the Balthrop #6, is located just across the road immediately north a short distance from plaintiffs' house (Plaintiffs' Ex. 3; Tr. 11). On plaintiffs' land and south of their house 450 to 500 feet is an injection well. It is identified as WP #3 (Plaintiffs' Ex. 2; Tr. 127). This well has been serviced by an employee of defendant once or twice a week, and oftener when the weather was cold from 1945 to the date of trial (Tr. 127, 128, 141). Plaintiff knew what the well was being used for (Tr. 130). The WP #3 "sticks up out of the ground there and it has a big blow pit to the west of it that takes up nearly a half acre where, when it gets water in the tank it has a huge silver tank, when they take gas out of the ground moisture comes up and catches and blows it out in the pit and the pit takes up some of it, the well takes up some of it, and then at times the cattle in the pasture, it has a big handle on it, pull it down and it blowed gas, after the fluid is all gone it blows natural gas and sometimes the cattle gets against that, it has an automatic turn-on and turn-off, and sometimes it gets hung and blows gas, and that gas smell gets real strong at times. And it would make noise, wake us up in the middle of the night and make noise. I called Mr. Scroggins if it gets hung and he would come down and fix it. The blow pit killed a few trees

around there and all. I guess you expect stuff like that." (Tr. 11-12).

Although plaintiff testified that he did not know at the time he purchased Tract I that it was part of an underground gas storage reservoir (Tr. 18, 22) and that he did not learn that it was until 1967, the court finds that he in fact had both actual and constructive knowledge that Tract I was part of a gas storage reservoir at the time he bought it in 1963. Mr. Davidson, plaintiffs' grantor, told Mr. Ellis prior to his purchase of the land that he was getting the "surface only"—none of the minerals—but "because of the storage of gas . . . on the place, he would get free gas for this one house." (Tr. 120). Furthermore, the Gas Storage Lease which covered Tract I was recorded in the office of the County Clerk of Pontotoc County on February 14, 1947 (Defendant's Ex. 3) thereby giving him constructive knowledge of its terms. 16 O.S. § 16. And he had the title examined prior to purchase (Tr. 121). Moreover he described in considerable detail the gas injection well just south of his house—how it looked, how it sounded and how it smelled. Thus, although the testimony is in conflict the court finds that plaintiff knew that the land in question was being used as a gas storage reservoir.

There is no issue in this case relating to who is entitled to produce the injected gas although both sides have directed this court's attention to various cases which do involve that issue. See Hammonds v. Central Kentucky Natural Gas Co., 255 Ky. 685, 75 S.W.2d 204 (1934); Lone Star Gas Co. v. J. W. Murchison, 353 S.W.2d 870, [16 O&GR 816] 94 A.L.R. 2d 529 (Tex.Civ.App. 1962), error refused n.r.e.; White v. New York State Natural Gas Corp., 190 F.Supp. 342 [14 O&GR 253] (W.D.Pa. 1960). Plaintiffs, as surface owners, are not asserting that they have title to or the right to drill into and produce any of the injected gas. But plaintiffs do assert that after the pore spaces in the reservoir rock have been depleted of native natural gas—and it is uncontroverted in this case that all economically recoverable gas reserves

were depleted by 1928 (Tr. 50)—that they, as surface owners, own the reservoir and the void pore space in the rocks which is now being utilized by the defendant in storing natural gas produced elsewhere and injected into the reservoir. They claim in essence that their land is being used by the defendant without authority and that they are entitled to damages for its unauthorized use.

Defendants, on the other hand, deny liability and assert that because of the peculiar nature of the common law concerning ownership of natural gas in place, the ownership of the subsurface strata does not determine the right to store and recapture natural gas and that one injecting natural gas into such a stratum cannot be held to have committed a trespass. It further argues that gas storage rights were properly secured from the mineral owners by the oil and gas leases and the gas storage leases in 1928, 1946 and 1947 and that it is the mineral interest owner and not the surface owner who is empowered by law to grant storage rights to the defendant. The defendant argues that under the authority of *Hammonds,* supra, Central Kentucky Natural Gas Co. v. Smallwood, 252 S.W.2d 866 [2 O&GR 19] (1952) and West Edmond Salt Water Disposal Association v. Rosecrans, 226 P.2d 965 (Okl. 1950) one who reinjects gas or water into a reservoir loses ownership of the reinjected fluid, that such fluid becomes subject to the law of capture and that because ownership is lost by virtue of reinjection, the defendant cannot be held liable for trespass or damages. The defendant especially urges *West Edmond* because it was decided by the Oklahoma Supreme Court.

There is no question, this being a diversity case, but that this court is obligated to follow state law. But in this court's view, *West Edmond* is not dispositive. *West Edmond* was concerned with the potential liability of a party who injected salt water into an underground formation, which formation was already saturated with salt water. Proof was adduced that salt water, which was injected by defendant into a well

located on a 40-acre tract which adjoined plaintiffs' land to the west, was forced to the east through the porous stratum into which it was injected where it commingled with the salt water which already saturated that stratum in and under plaintiffs' land. Unlike the facts in this case, no one knew what the perimeter boundaries were of the Hoover-Tonkawa formation into which the salt water was injected. That "formation was saturated with salt water and was of great extent, the actual boundaries thereof not being capable of accurate ascertainment." 226 P.2d 965, 968. The court did find, however, that following injection of salt water into the Hoover-Tonkawa Sand, the defendants lost ownership of the injected salt water, did seem to say that minerals were faere naturae and did cite Hammonds, supra, with approval. 226 P.2d at 970-71.

The factual setting of *West Edmond* is important. There, the salt water which was injected was commingled with the salt water which already saturated the stratum in and under plaintiffs' land. The salt water was a valueless substance. No one knew what the confines or boundaries were of the formation into which the salt water was injected. In the case before this court none of those circumstances exist. There is no commingling of economically recoverable native gas and storage gas. The reservoir was depleted prior to injection. All of the gas injected is owned by the defendant. The limits of the reservoir are well defined. All of this is undisputed.

In a fact circumstance quite similar to the one which is before this court, and in declining to follow the animal faere naturae analogy, the court in *White,* supra, stated:

> It becomes readily apparent, however, that a strict application of this analogy to the present facts is of no benefit to plaintiff's cause. To begin with, the storage gas in question has not escaped from its owners. On the contrary, it is yet very much in the possession of the storage companies, being within a well-defined storage field, the

> Hebron-Ellisburg Field, and being subject to the control of the storage companies through the same wells by which the gas originally had been injected into the storage pool.

190 F.Supp. 342, 348.

Looking at this same analogy, Professor Kuntz has noted:

> The analogies used are imperfect and objectionable, and the result reached is reasonable only if compelled by a lack of scientific knowledge. The result is not reasonable if the character and area of the reservoir can be determined or if the specific substance can be identified and traced.
>
> If the underground area is capable of being defined with certainty, ownership of the substances injected should not be lost, unless it appears that they have been abandoned. Further, the injector should be held to be a trespasser if the substance was intended to invade the land of another.

1 Kuntz, The Law of Oil and Gas § 2.6, p. 71.

This court's decision in this case is limited to a circumstance where the reservoir is defined and there is no commingling between economically recoverable native gas and injected gas. In this factual setting, it is my view that the law of Oklahoma is that the injector does not lose ownership of the gas by injecting it into the underground reservoir. And for these reasons I do not regard Bezzi v. Hocker, 370 F.2d 533 [26 O&GR 328] (10th Cir. 1966) as determinative in this case. See, *Lone Star Gas Co.*, supra.

But the question still remains: Did the severed mineral interest owners have the legal right to grant gas storage rights to the defendant? If they did the plaintiffs cannot prevail because such rights were granted to the defendant. Professors Williams and Meyers say that in this country there "are two reported cases dealing with this matter." 1 Williams and Meyers, Oil and Gas Law, § 222, p. 328.3. A Kentucky case, Central Kentucky Natural Gas Co. v. Smallwood, 252 S.W.2d 866 (1952), noted in 7 Okla. L. Rev. 225 (1954)

has held that the mineral interest owner has authority, to grant a gas storage lease. A West Virginia case, Tate v. United Fuel Gas Co., 71 S.E.2d 65 [1 O&GR 1459] (1952) holds that the surface owner has authority to grant a gas storage lease. These two cases, looking in opposite directions, were both decided in 1952. The Court of Claims has also addressed the question more recently and has concluded that the right and power to use a depleted reservoir for gas storage purposes is vested in the surface owner. Emeny v. United States, 412 F.2d 1319 [34 O&GR 53] (Ct.Cl. 1969).

Writers and academicians who have looked at the question are about equally divided. Professors Williams and Meyers urge "adoption of the view that the mineral severance should be construed as granting exclusive rights to subterranean strata for all purposes relating to minerals, whether 'native' or 'injected,' absent contrary language in the instrument severing such minerals." Williams and Meyers, supra, at p. 333. In accord with this view, see Stamm, Legal Problems in the Underground Storage of Natural Gas, 36 Tex. L. Rev. 161 (1957). A contrary view is expressed by McGinnis, Some Legal Problems in Underground Gas Storage, Southwestern Legal Foundation, 17th Annual Institute on Oil and Gas and Taxation 23 (1966); Scott, Underground Storage of Natural Gas: A Study of Legal Problems, 19 Okl. L. Rev. 47 (1966); Creekmore and Harvey, Subsurface Storage of Gas, 39 Miss. L. J. 81 (1967).

There are several factors which should be considered in arriving at a decision concerning whether the mineral owner or the surface owner has the right and power to grant the storage right and to receive the compensation therefor. One is intention. What was the intention of the parties at the time the minerals were severed from the surface? Was it the intention that the mineral interest owner have the power to explore, develop, produce and *store* gas in and under the land in question? The first place to look in ascertaining that intention are the deeds which effect the severance. In

this case it seems quite clear that the mineral severance instruments gave to the mineral interest owner all of the oil, gas and other minerals *"that may be produced";* that he had the "right of ingress and egress at all times for the purpose of *mining, drilling* and *exploring* said lands." Indeed all of the words used denote *exploration, production* and *development.* Nothing is said about *injection, storage* or *occupation.* And there is nothing before me which suggests that these rights should be reasonably inferred from other language used in the deeds.

Speaking to this same point, Mr. McGinnis has stated:

> It is submitted, however, that neither the right to store nor the right to use the surface in connection with storage should be implied or presumed in the absence of clear evidence of intent to grant such rights.

McGinnis, Some Legal Problems in Underground Gas Storage, supra, at 51.

Although Professors Williams and Meyers are of the view that the power to grant storage rights should be in the mineral interest owners, they urge this position *"absent contrary language* in the instrument severing such minerals." (Emphasis added). While the severing instruments in this case do not negate in express terms the right to inject or store gas (that is to say, they do not read "the mineral interest owner shall *not* have the power or right to inject or store gas") the only reasonable construction of the language used is that no such power is bestowed upon him. This court accordingly concludes that the parties did not intend that the mineral interest owner should have injection, storage or occupation rights.

Apart from intention, if A owns a tract of land in fee simple and conveys to B all of the oil, gas and other minerals in and under and that may be produced from that tract of land, A retains everything which he did not convey. It is clear in Oklahoma that a grant of minerals simply gives to

the grantee the right to explore for, produce and reduce to possession, if found, the oil, gas and other minerals. It is an incorporeal interest analogous to a profit to hunt and fish on the land of another. Rich v. Doneghey, 71 Okl. 204, 177 P. 86 (1918). Such a deed does not convey the minerals in place and does not convey the stratum of rock containing the pore spaces within which the oil and gas may be found. In the hard mineral area of the law and in the absence of language in the severing deed dictating a different construction, the English and Canadian rule is that the cavern which remains in the land after the hard minerals are mined is owned by the mineral interest owner; the American view is that the cavern is owned by the surface owners. See Mines and Minerals, 54 Am.Jur.2d § 204 (1971); Mines and Minerals, 58 C.J.S. § 162, at 338 (1948); Stamm, Legal Problems in the Underground Storage of Natural Gas, supra, at 168; Creekmore and Harvey, Subsurface Storage of Gas, supra, at 96; Lyndon, The Legal Aspects of Underground Storage of Natural Gas, 1 Alberta L. Rev. 543, 545 (1961). There is no reason in principle why the American rule should not apply to a depleted gas storage reservoir. Mr. Scott, in addressing himself to this question, has stated:

> Based upon the foregoing principles, the surface owner alone should be compensated for the use per se of a stratum. He is the owner of this formation, and like an owner of a warehouse, he is entitled to the rental or other compensation paid for the use of his property.

Scott, Underground Storage of Natural Gas: A Study of Legal Problems, supra, at 61.

While the Supreme Court of Oklahoma has not passed upon this point, it has considered a closely analagous question in dealing with the rights of the mineral and surface owners which leads this court to conclude that it would hold, in the circumstances which face this court, that the surface owner has the power to convey gas storage rights. In Sunray Oil Co. v. Cortez Oil Co., 112 P.2d 792 (Okl. 1941) Cortez

Oil Company was the owner of an undivided 1/4 mineral interest in a tract of land. A well had been drilled by an oil and gas lessee on said land which was unproductive of oil or gas. The Cromwell Sand had been encountered and was approximately 105 feet thick; it was not productive of oil or gas and was saturated with salt water. Sunray Oil Company secured from the lessee an assignment of the oil and gas lease on the ten acres on which the well was situate. Genevieve Greer was the owner of the surface and of 53/80ths of the minerals. Sunray secured from her a license to use the well as a salt water disposal well. Cortez Oil Company sought to enjoin Sunray from so using the well. On the basis of the evidence adduced the court concluded that there was no possibility of finding oil or gas in the Cromwell Sand and hence any threat of injury to the Cortez mineral interest in that formation was purely speculative. The court then addressed the question of who had the right to Grant to Sunray the right to inject and store salt water which was produced by Sunray from oil and gas wells on another lease some distance from the well in question. The court stated:

> So in this case Genevieve Greer, . . . has the right to so use *the surface and substrata* of her land as she sees fit, or permit others so to do, so long as such use does not injure or damage other persons. (Emphasis added).

112 P.2d 792, 795. This court must conclude that a reasonable construction of that language is that Genevieve Greer, *as the surface owner,* was entitled to grant the salt water storage rights to Sunray. I consequently must conclude that a similar construction would be reached by that court on the evidence adduced in the trial of this case.

It is undisputed that the underground storage of natural gas as a conservation measure is one that clearly promotes the general welfare; it is a highly desirable and worthwhile undertaking in our severely energy-short economy. As a matter of policy, it is an undertaking which should be encouraged. The conclusion which the court reaches this day

does not on the whole fetter or burden or make gas storage projects more difficult. If this court had concluded that it was the mineral interest owner and not the surface owner who had the power to grant storage rights, it would typically mean that hundreds of severed mineral interest owners would have to be contacted if those rights were to be obtained privately. Especially is this so if the underground gas storage reservoir was once a producing gas field. Small fractional mineral interests are typically extremely numerous on any tract of land which at some time in its history has been involved in a substantial oil and gas play. Admittedly there may be instances where, for example, the gas storage facility underlays a metropolitan area, it will be necessary to secure the consent of a large number of surface tract owners. But on the whole, that would not ordinarily be the case and there is no evidence before this court to suggest that it is the case here.

Furthermore, even if the mineral interest owner is the one who has the power to grant gas storage rights, all writers apparently agree that if there is to be "some user of the surface for injection or production wells or other surface installations" the surface owner's consent and authority must be secured in all events. Williams and Meyers, supra, at 331.

For all of the foregoing reasons the court concludes that the defendant did not have authorization or permission to inject and store the gas in the subsurface stratum of plaintiffs' land.

Defendant also argues that it acquired gas storage rights on plaintiffs' land by virtue of the easement granted on June 3, 1967 (Plaintiff's Exhibit 7). That easement granted unto the defendant the "right of way to maintain, alter, repair, operate . . . on, over and through" Tract I "the existing four pipelines on the surface . . . including a gas injection well for gas storage and a pit." There is nothing in this instrument which purports to grant gas *storage* rights as such and

the court concludes that such rights are not so granted by it. Even if the mineral interest owner had the right to grant gas storage rights, it would still be necessary for defendant in this circumstance to secure permission from the surface owner to install upon the topographic surface of his land the injection well and other equipment which might be necessary to inject or withdraw natural gas. This easement granted those rights to the defendant; it granted nothing more. Williams and Meyers, supra, pp. 331 and 332.

Plaintiffs argue and allege in the amendment to their complaint that this easement "fails for lack of consideration in that the consideration cited therein has never been paid." They contend that in view of the lack of consideration the court should grant rescission of the instrument.

It is undisputed that $5.00 was not paid to plaintiff. The easement shows on its face, however, that defendant agreed to relocate some 450 feet of pipeline (see also Defendant's Exhibit 5). It is undisputed that this relocation was performed without cost to plaintiffs at a cost to defendant of $2,736.34. Plaintiffs admit in their brief of May 9, 1977 that the relocation, as set out in the instrument in question, was bargained for between the parties. They expressly state that "the only thing that was bargained for as to . . . [the June 3, 1967 instrument] is the relocation of the 450 feet of lines." However, they argue that since the only thing bargained for between the parties was the moving of the pipeline, the balance of the terms and conditions set out in the instrument are severable and should be rescinded.

The argument is without merit. The relocation was performed at substantial expense to defendant. Plaintiffs admit that this relocation was bargained for. Defendant's obligation under the "bargain" was to relocate the pipe and bear all expenses associated therewith. It is obvious that, in exchange for defendant's promise, plaintiffs promised, as set out in the instrument, to grant defendant the right of way to maintain, alter, repair, operate and remove pipelines on

plaintiffs' land, including a gas injection well for gas storage and a pit.

It is clear, therefore, that plaintiffs' promise to grant defendant the easement was supported by defendant's promise to relocate the pipeline. This constituted a bargained-for exchange, since mutual promises are consideration for the formation of a bilateral contract. 15 O.S. § 106; Nadel v. Zeligson, 207 Okla. 658, 662, 252 P.2d 140 [2 O&GR 248] (1953).

The defendant finally contends that it obtained by prescription the right to inject and store gas in the subsurface strata of paintiffs' land. Plaintiff argues that this contention should not be countenanced by the court because it was not contained in the pleadings or in the pretrial order. Prior to the trial this court directed the parties to submit trial briefs and proposed findings of fact and conclusions of law. On April 5, 1977, more than three weeks in advance of trial, the defendant filed and submitted to opposing counsel his proposed findings of fact and conclusions of law. Paragraph 12 of his proposed conclusion of law was:

> Except for the fact that defendant and its predecessors were using the well for gas injection and the Upper Cromwell Sand for gas storage under *express grants* from plaintiffs and their predecessors, defendant long since *would have acquired the prescriptive right to do so, all other elements of adverse possession having been shown by the evidence.* (Emphasis added).

This court has concluded that the "grants" referred to by defendant, namely (1) the oil and gas leases, (2) the gas storage leases, and (3) the line relocation easement provide no authority in law for the defendant's underground storage of natural gas. Substantial amounts of evidence were adduced at trial directly bearing on the maturation of a prescriptive easement. Plaintiff did not suggest before the trial or object during the trial to any evidence being introduced

on the grounds that it was beyond the issues framed by the pleadings or the pretrial order. At the conclusion of the trial the court invited counsel to submit briefs on the question of whether defendant had matured a prescriptive right to store injected gas. Then, for the first time, in his brief filed on May 16, 1977, did plaintiffs object on the grounds that this issue was outside the pleadings and the pretrial order. The Court of Appeals for the Tenth Circuit has quite recently stated:

> It is the general rule that where an issue is developed in the evidence admitted without objection, the issue is before the court for determination and the pleadings should be regarded as amended to conform to the proof. See Rule 15(b) F.R.Civ.P.; Hopkins v. Metcalf, 435 F.2d 123, 124-25 (10th Cir.); and see Rule 16, F.R.Civ.P., governing amendment of pretrial orders.

Sanders v. International Harvester Co., Case No. 76-1407 (10th Cir. 1978).

The contention of plaintiffs is accordingly lacking in merit and the court will consider whether or not the defendant matured an easement by prescription for the storage of gas.

60 O.S. § 333 provides as follows:

> Occupancy for the period prescribed by civil procedure, or any law of this State as sufficient to bar an action for the recovery of the property, confers a title thereto, denominated a title by prescription, which is sufficient against all.

An easement may be acquired by prescription. Frater Oklahoma Realty Corp. v. Allen Laughon Hardware Co., 206 Okl. 666, 245 P.2d 1144, 1147 (1952). The burden of proof is upon the party asserting a prescriptive right and the requisite showing has been stated by the Oklahoma Supreme Court as follows:

> To obtain title to property by prescription, all elements of adverse possession must be established by clear and posi-

> tive proof and cannot be established by inference. Adverse possession is to be taken strictly, and every presumption is in favor of possession in subordination to the rightful owner. The burden of proof rests on the party asserting adverse possession to show the necessary elements of actual, adverse, open, notorious, peaceable, exclusive and hostile possession for a period of fifteen years. Where the evidence is conflicting it is an issue of fact to be determined by the trier of the facts.

Tindle v. Linville, 512 P.2d 176, 178 (Okl. 1973). See also Sears v. State Department of Wildlife Conservation, 549 P.2d 1211 (Okl. 1976).

In this case plaintiffs and their predecessors in title knew that the Upper Cromwell Sand underlying the topographic surface of the land in question was a part of the Ada Gas Storage Facility. The reservoir has been continuously used as a gas storage reservoir since 1949. There are nine injection wells on the surface of the land embraced in the storage facility. Plaintiff is a building contractor and has lived in the area all of his life. One of the principal injection wells is on his land and is located 450 to 500 feet south of his house. It has been there since before 1945. The log from this well formed the basis for the determination by the Oklahoma Corporation Commission concerning the thickness of the Upper Cromwell Sand (Plaintiffs' Ex. 5; Tr. 47). That well, according to plaintiff's testimony, with its "big blow pit" that "takes up nearly a half acre" and its "huge silver tank" is highly visible, is noisy and is smelly (Tr. 11-12). It has been serviced once or twice a week by employees of defendant from 1945 to the date of trial. Plaintiff knew what it was being used for. Some of the pipelines running from the gas reservoir were visible on the surface. The 8″ and 4″ lines going straight to plaintiff's house could be seen on top of the ground.

Plaintiffs' immediate predecessor in title was Mr. Glen D. Davidson and he had acquired title from his mother. Mr.

Davidson was employed by the defendant from 1956 until 1977. He worked at the defendant's Ada warehouse just 3 miles north of Ada (Tr. 115). He and his father had a hog farm on the land where plaintiffs' house is located before plaintiff bought the land from him (Tr. 118). He was quite familiar with the land and had prepared for defendant the diagram (Defendant's Ex. 5) rerouting the pipeline around plaintiffs' house (Tr. 116). Although Mr. Davidson and his father and mother did not live on the land, they were intimately familiar with it and members of their family lived on it for several years (Tr. 118). They all knew of the pipelines and their connection with the gas storage reservoir (Tr. 118-119). Mr. Davidson, plaintiffs' grantor, told plaintiff prior to his purchase of the land that he was getting the "surface only" but "*because of the storage of gas on the place,* he would get free gas for this one house." (Tr. 120). Plaintiff also had constructive knowledge of the gas storage leases (Defendant's Exhibit 3) and had examined the title prior to purchase (Tr. 121).

Plaintiffs argue that the use by the defendant has been permissive. The record is devoid of any evidence which suggests that the plaintiffs or their predecessors in title have granted permissive use to the defendant to store gas. The plaintiff has testified, although the court has found to the contrary, that he did not know his land was being used as an underground gas storage reservoir until 1967. He objected at that time to defendant's use of the land as a gas storage reservoir. He testified as follows:

> Q. And what was it that you said to him complaining about or objecting to the use of the injection well?
>
> A. Well, I remember it very well, I said looks to me like if a man had a big warehouse and it's full of canned oil and I sold you the oil and I said, sir, this is your oil, sir, you can get it out anytime you want to, he gets all of the canned oil out and I look around and he is putting oil back in there that is relatively unfair. When the gas company got

> out their gas out of the land it looks like this property is mine and I should be paid something for using it again. He said it's absolutely under the mineral part of it and you don't have no say-so under it. So, that's how come that is still in that easement with my name on it. (Tr. 32).

Plaintiff then went to an attorney to get an opinion on the right of the defendant to use his land as an underground gas storage reservoir but did not follow it up (Tr. 33) and although he did not formally object again to the gas company, he "moaned and groaned and complained to everbody but an attorney," including his "friends and business acquaintences" (Tr. 33). The record is simply devoid of any evidence whatsoever that any surface owner ever gave permission to the defendant to store gas in and under this land; the only permission defendant obtained was from mineral interest owners.

Plaintiffs next argue that it is essential that the defendant be claiming under color of title and that it was not so claiming. This contention is totally lacking in merit. It is abundantly clear that, mistaken though the defendant was concerning who had authority to grant gas storage rights, it is and always has been claiming under the oil and gas leases, the gas storage leases and the easement it took from plaintiffs; all of these are claims under color of title.

The evidence of knowledge on the part of plaintiffs and their predecessors in title of actual, adverse, open, notorious, peaceable, exclusive and hostile possession by defendant of the Ada Gas Storage Facility for a period of time far in excess of 15 years is overwhelming. The court accordingly must conclude that defendant has matured a prescriptive easement for the underground storage of natural gas.

Plaintiffs also argue that the condemnation action by the defendant in the District Court of Pontotoc County against plaintiffs to condemn the Upper Cromwell Sand pursuant to

state law "is in fact an admission that plaintiffs, as surface owners, own storage rights in the aforedescribed tracts. Such an admission standing alone should warrant only examination of the case on the issue of damages . . . ." (Plaintiff's Trial Brief p. 2). In effect plaintiffs argue that this action somehow bars or prevents the legal assertions which defendant makes here. This contention is not well founded. It may well be that defendant's April 1, 1976 condemnation action exhibits uncertainty concerning the state of the law on whether it is the mineral owner or the surface owner who has the power to grant gas storage leases. That question, after all, had not been resolved in Oklahoma when that action was brought. Indeed, it stands unresolved today in most of the jurisdictions of this country. And it is essential for the effective operation of an underground gas storage reservoir for the injector to acquire the requisite authority from *all of the property interest owners in that reservoir.* But simply because the defendant took a cautious step to protect against the possibility of the very decision which this court today makes does not mean that the defendant is precluded from contending that it had gas storage rights under its gas storage leases and the other instruments of title on which it relies or that it is precluded from asserting that it has matured a prescriptive easement. The contention by plaintiffs that the institution of a condemnation action by the defendant somehow infects the validity of its arguments here is without merit.

Judgment will be entered in accordance with this Memorandum Opinion.

DISCUSSION NOTES

Storage of Gas: Underground Storage: Relative Rights of Mineral Owners and Surface Owners—Prescription—Acquisition of Storage Rights from Surface Owner by Prescription.

The instant case is on appeal to the United States Court of Appeals for the Tenth Circuit.

For the treatment of the Supreme Court of Texas of problems arising where gas is injected into a reservoir still containing native gas, see Humble Oil & Refining Co. v. West, 508 S.W. 2d 812, 48 O&GR 516 (1974), and discussion notes at 48 O&GR 529; and at a later stage, Exxon Corp. v. West, 543 S.W. 2d 667, 56 O&GR 398 (Tex. Civ. App. 1976).

J. S. W.

GARD et al. v. KAISER et al.

Oklahoma Supreme Court
July 19, 1978—No. 50186
582 P. 2d 1311
(As Corrected August 8, 1978)
(Mandate issued September 7, 1978)

Oil and Gas Leases: Habendum Clause: Cessation of Production after Primary Term—Temporary Cessation of Production—Necessity for Marketing.

Shut-In Wells: Shut-In Gas Clauses—Need To Pay Shut-In Gas Royalty To Avoid Termination.

Within the primary terms of the leases in question, a gas well was drilled on the leased premises, and gas was marketed. After the expiration of the primary terms, marketing ceased when the gas pressure became too low for gas to enter the pipeline. The well was shut in for more than two years while lessees were negotiating a new contract and securing permission of the FPC to abandon the existing contract. The leases contained shut-in gas royalty clauses, but shut-in gas royalty was not paid. Marketing of gas was resumed. Plaintiff lessors brought this action to cancel the leases for failure of lessees to pay shut-in gas royalty. The trial court held for defendants. The Court of Appeals reversed the trial court. The Supreme Court granted certiorari, vacated the opinion of the Court of Appeals, and affirmed the trial court. In Oklahoma, marketing is not required as a part of production, a shut-in gas well constitutes production required by the habendum clause, and the failure to pay shut-in gas royalty will not result in termination where the shut-in gas royalty clause does not so provide.

Certiorari to Court of Appeals, Division 2.

Action to cancel leases for failure to pay shut-in royalty payments after expiration of primary terms of oil and gas leases. Judgment for lessees, lessors appeal.

STORCK et al. v. CITIES SERVICE GAS COMPANY

Oklahoma Supreme Court
November 22, 1977—No. 48789
575 P. 2d 1364
As Amended on Denial of Rehearing March 13, 1978
(Mandate issued March 30, 1978)

Storage of Gas: Gas Storage Lease—Title to Native Gas—Construction of Lease To Permit Extraction of Native Oil or Gas—Protection of Statutes Providing for Condemnation of Storage Area—Fraud in Representing That a Prior Well Was Dry—Threat of Condemnation Not Duress.

In 1960 a dry hole was drilled on the land in question. Threatened by a condemnation action, the landowners granted a fifty-year gas storage lease to defendant in 1964. The lease granted the right to store gas in all formations above the base of the Mississippi Lime and contained a covenant by lessors that they would not directly or indirectly conduct operations on the land to produce oil or gas from any such formations. It also provided for notice to the lessee of any operations for oil or gas on the land and provided that any operations on the land would be conducted so as to prevent the escape of any stored gas. The landowners granted an oil and gas lease in 1973. The oil and gas lessee requested permission of the gas storage lessee to drill into the storage strata for oil or gas, and permission was not given. The landowners and the oil and gas lessee brought action against the gas storage lessee for damages in an amount representing the value of the native oil and gas in place under the land in question, to declare the gas storage lease void, and to cancel the lease on the grounds of mutual mistake and fraud. Defendants countered, seeking to enjoin the oil and gas lessee from drilling or producing above the base of the Mississippi Lime. The trial court denied all relief. Plaintiffs appealed. Held: Affirmed and remanded for further proceedings not inconsistent with the court's opinion. The court found no inequity which would require that the gas storage lease be cancelled. A gas storage lease is a lease of real property, but it is not a mineral lease and does not transfer title to native oil or gas. The protections of statutes providing for condemnation of underground formations for gas storage are available to landowners who enter into gas storage leases to avoid threatened condemnation. The execution of such a gas storage lease does not prevent later ex-

ploitation of the native gas from formations not used for storage. Land so leased should be undamaged upon reverting at the end of the term, and allowing drainage away from the land would result in damage to the reversion. Accordingly, a covenant by gas storage lessors that they will not conduct operations to produce oil or gas from any formations above the base of the Mississippi Lime should be construed as an obligation not to interfere with or damage the gas storage operation. The finding of the trial court that there was no mutual mistake of fact is not clearly against the weight of the evidence, and a finding that there was no fraud on the part of defendant in representing that the early well was not capable of producing oil or gas is supported by evidence that the statements were made upon the same kind of knowledge possessed by landowners who did not rely upon the representations. A threat of condemnation is not duress or coercion.

Appeal from District Court of Grant County, Oklahoma; J. Russell Swanson, Trial Judge.

From an order of the District Court denying cancellation of lease for gas storage purposes and denying counterclaim for injunctive relief, plaintiffs appeal.

Affirmed and remanded.

BERRY, Justice.

This case arises from a dispute concerning lease for underground storage of gas. Appellants, members of Storck family [Storcks] and Min-Tex Oil Corporation [Min-Tex], were plaintiffs below; appellee, Cities Service Gas Company [Cities Service], was defendant. Parties will be referred to by name or by title in this Court. The term appellants will be used to include all named appellants.

During the early 1960's Cities Service was establishing an underground gas storage area in Grant County.

In 1960 a well was drilled by Davidor and Davidor on the Storck tract [Davidor well]. The well was never produced for oil or gas but was abandoned as a "dry hole."

In February 1964, Storck family leased part of subsurface

formations under their farm, NW/4 Section 35, T28N, R3W, to Cities Service for a period of 50 years.

The lease gave Cities Service the right to store natural gas in all underground formations above the base of the Mississippi Lime. The lease required drilling operations on the Storck property to have prior approval of Cities Service, and allowed Cities Service to have a representative present during those operations.

In 1973 Storcks executed mineral leases giving Min-Tex the right to conduct oil and gas producing operations in all formations underlying the farm. Min-Tex requested permission of Cities Service to drill into the storage strata for oil and gas; permission was not forthcoming.

Appellants commenced this action to declare gas storage lease void and cancel lease on several grounds, and for actual and exemplary damages [the damage issues have yet to be tried]. Appellee countered with suit to enjoin Min-Tex from drilling and producing above base of Mississippi Lime formation. Trial court denied each party relief requested. Appellants commenced this appeal. Cities Service did not appeal.

We first consider appellants' final proposition and then the remaining propositions in order.

Appellants' fifth proposition is this Court should adjust the equities between the parties. Appellants present the Court with two alternatives: [1] cancellation of the gas storage lease insofar as it purports to prohibit drilling and production upon the realty in question; [2] entry of judgment for appellants for the amount of $5,270,346.00 which they claim represents the value of the oil and native gas in place under the land in question.

The issues of damages, in appellants' fifth and sixth causes of action, have not yet been determined by trial court. We refrain from comment upon damages to any greater extent than necessary to determine this appeal.

We will not cancel gas storage lease. Construing lease provisions and applicable statutory law of this State we find no such inequity as would authorize cancellation of gas storage lease.

We have held the State may impose statutory limits on the right to contract where limitation is a reasonable exercise of the police power. In such situation the statute is an implied part of the contract, and performance is subject to prohibitions in the statute. East Central Oklahoma Electric Cooperative, Inc. v. Public Service Co., Okl., 469 P.2d 662.

The record shows the gas storage lease was concluded between Storcks and Cities Service in contemplation of condemnation proceedings under 52 O.S. 1971 § 36.3. This section provides for condemnation of subsurface strata for storage of natural gas. The action may be maintained in district court.

The gas storage lease was negotiated, in part, on the premise parties could thereby avoid a lawsuit to condemn the underground strata. Cities Service's landman, from the beginning of the lease negotiations, informed Storcks that condemnation proceedings would be had if the lease was not concluded. We will not say Storcks, by entering into this lease in lieu of condemnation, divested themselves of protections available to them under condemnation statutes in the facts of this case.

The terms of 52 O.S. 1971 § 36.3, provide limitations upon the type of strata which may be condemned:

". . .

"(a) No sand, formation, or stratum which is producing or which is capable of producing oil in paying quantities, through any known recovery method, shall be subject to appropriation . . .

"(b) No gas bearing sand, formation, or stratum shall be subject to appropriation hereunder, unless the volumes of

native gas originally in place therein shall be shown to be substantially depleted, and that such sand, formation or stratum has a greater value or utility as a gas storage reservoir for the purpose of insuring an adequate supply of natural gas for any particular class or group of consumers of natural gas, or for the conservation of natural gas, than for the production of the relatively small volumes of native gas which remain therein, provided that no gas sand, formation or stratum shall be condemned (in certain other, immaterial, circumstances) . . .

"(c) Only such area of such underground sand, formation or stratum as may reasonably be expected to be penetrated by gas displaced or injected into such underground gas storage reservoir may be appropriated hereunder.

". . .

"The right of condemnation hereby granted shall be without prejudice to the rights of the owner of said lands or of other rights or interests therein to drill or bore through the underground stratum or formation so appropriated in such manner as shall comply with the orders, rules and regulations of the (Corporation C)ommission issued for the purpose of protecting underground storage strata or formations against pollution and against the escape of natural gas therefrom and shall be without prejudice to the rights of the owner of said lands or other rights or interests therein as to all other uses thereof. The additional cost of complying with such regulations or orders in order to protect the storage shall be paid by the public utility."

The pertinent clauses of the lease are:

"4. Lessors hereby covenant and agree that, during the term of this lease, they will carry on no operations on said land to produce oil or gas from any formations lying above the base of the Mississippi Lime, either directly or by lease or agreement with others, and will, themselves, or by lease or agreement with others, conduct no operations which

will interfere with or damage Lessee's operations on, in and under said land in accordance with the purpose granted in this lease.

"10. It is agreed that any operation on said land, which without limitation includes drilling and mining, while gas is stored on said land pursuant to this lease shall be so conducted as to prevent the escape of gas from, and the intrusion of water and other fluids into, any formation in which gas is so stored. Before any party begins any operation connected with or resulting from drilling and mining on said land, such party shall notify Lessee in writing by United States mail addressed to Lessee at Oklahoma City, Oklahoma, not less than thirty days prior to the intended beginning of any such operation. Thereupon and before actually beginning any such operation, such party and Lessee shall agree upon the methods and practices which such party shall use in any such operation, which without limitation includes plugging and abandoning thereof. Lessee shall have the right to have a representative present at all times while any such operation is conducted and shall have the right of access to records of such operation."

It is public policy that ". . . The production of oil in the State of Oklahoma in such manner as to constitute waste as . . . defined is hereby prohibited . . ." 52 O.S. 1971 § 86.2. The term "waste" as applied to the production of oil is defined in part as economic waste and underground waste. Ibid. As applied to the production of gas the term "waste" is defined in part as the production of gas in such quantities or in such manner as unreasonably to reduce reservoir pressure or unreasonably to diminish the quantity of oil or gas that might be recovered from a common source of supply. 52 O.S. 1971 § 86.3. Waste can consist of unreasonable production or unreasonable non-production. See Sinclair Oil and Gas Company v. Bishop, Okl., 441 P.2d 436 [30 O&GR 614].

Cities Service seems to argue lease of a stratum for gas storage forecloses the possibility of later exploitation for oil

and native gas. The position is untenable. The statutes do not authorize a change in the legal treatment of oil or native gas. The Storcks have a right to produce oil and native gas from those horizons not actually used for gas storage. The identity of horizons actually used for gas storage is a fact question for the proper forum. By mineral lease, Min-Tex succeeds to the Storcks' right.

The gas storage lease is clearly not a mineral lease. The lease does not transfer title to minerals in place [native oil or gas] to Cities Service. We deem the provisions giving Cities Service title to all gas ". . . introduced, stored or removed" from the tract as simply preserving in Cities Service the ownership of the gas it injects under the Storck farm.

Rather, the gas storage lease is a lease of real property. Appellants, as reversioners, have the right to expect return of the property at the expiration of the lease in the same condition as when it was delivered to Cities Service, fair wear and tear excepted. Allowing oil or native gas to migrate away would damage the reversion.

Cities Service argues paragraph 4 of gas storage lease forbids any operations to produce hydrocarbons from horizons above the Mississippi Lime. If we were to accept that construction the lease would protect unreasonable underground waste or allow drainage by offset production. However, paragraph 4 could be construed to mean production of hydrocarbons from leased horizons is limited by obligation to not interfere with or damage gas storage operation. We think that interpretation is reasonable, and would allow a protection of Cities Service's interest and the reversionary interest.

Accordingly, Cities Service may permit, and be present during, appellants' production from underground strata subject to lease. Appellants may take only that oil and native gas which may be in place. If Cities Service refuses to allow appellants to explore or produce from the leased strata Cities Service must protect oil and native gas in place, allow none to migrate away, and deliver premises to appellants with oil and native gas undiminished at the termination of

the lease. Otherwise, Cities Service could be required to pay appellants the fair market value of any oil or native gas which Cities Service has failed to protect and which has migrated off the premises during lease term. Nothing herein indicates appellants may do anything to interfere with Cities Service's proper use of the premises for storage, nor prevent Cities Service from being present during appellants' production efforts.

Adjustments of equities, by way of cancellation or reformation of the gas storage lease, is not required in this situation. Each party's rights to enjoyment of the leased horizons, and to the oil and gas in place in those strata, can be protected legally.

The procedures for, and concepts of, unitization of mineral operations among draining tracts and drained tracts are not part of the jurisdiction of the district court, and nothing we say herein should be taken to impinge on any right parties hereto may have before the Corporation Commission.

Appellants' first proposition is the gas storage lease was entered into under a mutual mistake of fact and is therefore void and should be cancelled.

Appellants maintain parties to gas storage lease were mistaken as to presence of hydrocarbons in paying quantities in strata underlying Storck's tract.

Trial court found no mutual mistake of fact. We are not inclined to disturb trial court's conclusion.

We do not disturb trial court's findings of fact in cases of this nature unless findings appear clearly against weight of the evidence. Matter of Woodward, Okl., 549 P.2d 1207. We do not find this standard satisfied here. Appellants introduced testimony of one geologist concerning the Davidor well drilled on the Storck tract in 1960 and abandoned as "dry hole." He testified the well might have been a producer had it not been abandoned when drilled. To counter that, testimony of Davidor's geologist at the trial shows he is still of the opinion the well is a dry hole. The Corporation

Commission [without notice to Storcks] found the tract, and same strata in the neighboring area, to be depleted to the extent necessary to justify use of area for gas storage. It further found production to the west of appellants' tract has been started since the gas storage project was initiated. In view of this state of the record we cannot say trial court erred in finding no mutual mistake of fact.

Appellants' second proposition is gas storage lease, insofar as it purports to prohibit drilling and production, violates public policy of this State and express statutory provisions against economic waste, and is therefore void and unenforceable. Appellants cite no authority for the theory the gas storage lease violates statute, and in this case we are not persuaded.

We do not conclude the underground storage of natural gas is contrary to public policy. The legislature has declared underground storage of natural gas to be in accordance with public policy. 52 O.S. 1971 § 36.2.

Nor do we conclude statutes of this State favoring conservation of oil and gas and statutes providing for underground storage of natural gas are in conflict, for reasons set out above. We deem appellants' second proposition not well taken.

Appellants' third proposition is gas storage lease was procured through fraud, duress, undue influence and coercion and is therefore void and unenforceable and ought to be cancelled.

We do not agree with appellants' position. Appellants argue Cities Service's landman placed Storcks in some form of duress or coerced them into signing the gas storage lease. The record contains insufficient evidence to sustain appellants' point. Appellants seem to see the action of Cities Service's agent in threatening to condemn the property for gas storage as duress or coercion. However, condemnation was a possible legal alternative open to appellee at the time

the lease was negotiated. Negotiations were, in part, based on the desire to avoid such a suit. The record does not support appellants' contention that appellee's agent overstepped the bounds of propriety.

Trial court ruled there had been no fraud committed by Cities Service in obtaining the lease. Appellants insist Cities Service's landman defrauded Storcks by representing Davidor well as a dry hole when it was capable of producing hydrocarbons. There has been no evidence to show appellee or its employee knew in 1964 the Davidor hole might be capable of producing oil. The landman's statements were made upon the same kind of knowledge about Davidor well as Storcks possessed. The record does not establish Storcks relied on the landman's statements. We cannot say trial court erred in its conclusion that fraud was not proved.

Appellants take the position the local banker stood in a confidential relation to appellants and violated that relation by urging them to execute the lease. Appellants claim the banker was actually appellee's agent and failed to disclose that fact to them. As proof of this issue they show the banker received a check from appellee for an amount equal to one dollar per acre of the Storck tract leased to appellee, and was marked "Expense . . . to the Storck lease." Cities Service's landman and the banker both testified this check was for expenses attendant upon landman's use of the banker's office and telephone. They denied the banker had any connection with the gas storage project other than as a public spirited citizen who thought this kind of development would be beneficial for the community.

In any event trial court did not see banker's influence upon Storcks was as great as claimed. Our review of the record discloses appellant Carl Storck, who negotiated the lease for Storcks, was engaged in negotiations for a considerable period of time, that he consulted his brother, a co-lessor and appellant, and the banker, and finally that he insisted on

extensive revision of the proposed lease prior to executing the instrument. We cannot say appellants have shown Storcks surrendered to banker the duties ordinarily exercised by a prudent lessor. It does not appear the decision to execute lease was substantially banker's because of substitution of his will for will of the Storcks. Absent a showing will of Storcks was subordinated to and replaced by the will of banker we will not say undue influence has been proved. Derdyn v. Low, 94 Okl. 41, 220 P. 945. See Blanchard v. Gordon, Okl., 418 P.2d 678.

In part A of the fourth proposition appellants argue it was error for district court to exclude certain testimony offered by appellants. The transcript of trial contains the following exchange:

"By (appellants' counsel):

"Q. . . . Now, Mr. Storck, at the time you executed the lease, what was your understanding of what you were giving up in consideration for the payment to you by Cities Service?

"A. Well, that they got—

"Mr. (appellee's counsel):

"Objection, your Honor.

"The Court:

"Mr. (appellants' counsel):

"If the Court please, your Honor, one of our causes of action is on the basis that this lease is vague, indefinite and ambiguous, and I submit that, one, it appears so on its face, and two, that we wish to have the plaintiff testify as to how he interpreted the lease; what he thought it meant.

"The Court:

"The objection is sustained."

Appellants argue where fraud is alleged testimony about circumstances leading up to signing the instrument and extrinsic facts showing interpretation parties put upon the writing are all admissible. We agree on this academic proposition. Oklahoma Company v. O'Neill, Okl., 440 P.2d 978 [30 O&GR 589]; Bobo v. Bigbee, Okl., 548 P.2d 224.

Assuming testimony of Carl Storck may properly have been admitted, appellants have shown us no way in which that evidence would have changed the result in the case.

Where it appears admission of evidence improperly excluded would not affect the outcome, the error in excluding the evidence is harmless. See McMillan v. Lane Wood & Company, Okl., 361 P.2d 487; Gray v. Gray, Okl., 459 P.2d 181.

Appellants urge, part B of proposition four, that trial court erred in refusing to admit an exhibit in rebuttal. Appellants had introduced many exhibits in an effort to prove a fault sealed their tract from the rest of the gas storage area and their tract was underlain with paying quantities of hydrocarbons.

At the conclusion of Cities Service's case appellants sought to introduce a report authored by a geologist employee of Cities Service. Appellants attempted to elicit testimony about the report from its author. The report concerned the property in question and was undertaken and completed after the gas storage lease had been executed. The court refused to admit the geologist's report.

We have examined the proffered exhibit and it would constitute cumulative evidence before trial court. The court did not err in refusing to admit cumulative evidence.

In light of the foregoing, trial court is affirmed. This matter is remanded for further proceedings not inconsistent with this opinion.

Concur: LAVENDER, V.C.J., and DAVISON, WILLIAMS, IRWIN, SIMMS and DOOLIN, JJ.

Dissent: HODGES, C.J., and BARNES, J.

DISCUSSION NOTES

Storage of Gas: Gas Storage Lease—Title to Native Gas—Construction of Lease To Permit Extraction of Native Oil or Gas—Protection of Statutes Providing for Condemnation of Storage Area—Fraud in Representing That a Prior Well Was Dry—Threat of Condemnation Not Duress.

From the principal case it is clear that a provision prohibiting operations to produce oil or gas from the described gas storage strata cannot be counted on to prohibit such operations and may not yield the protection desired by the gas storage lessee. It is now obvious that if the gas storage lessee desires to prohibit all operations to produce from the gas storage strata, he should acquire title to the oil and gas rights in such strata in addition to or as part of the storage lease. A landowner who has no desire to sell his mineral rights in the storage strata might be prevailed upon to agree that any native oil or gas in the storage strata will remain undisturbed during the life of the storage lease to serve as cushion oil or gas for gas stored now or in the future, with a further agreement that the gas storage lessee will not be impeachable for waste or otherwise liable for drainage of oil or gas away from the gas storage strata. For related problems in underground storage, see Kuntz, Oil & Gas § 2.6.

E. O. K.

COHEN v. McCUTCHIN et. al.

Texas Supreme Court
April 26, 1978—No. B-7093
565 S.W. 2d 230
(Rehearing denied May 31, 1978)

Statute of Frauds: Oil and Gas Leases—Assignments—Farmout Agreements—Parties to Farmout Agreement Must Be Named in Writing To Comply with Statute.

Suit for balance due on farmout agreements. P, administrator of the estate of the deceased assignor, alleged that the assignor and the defendants entered into two written agreements in which the assignor agreed to drill an exploratory well and to assign a fractional interest in a leasehold estate to defendants, who then were to pay designated amounts. The terms of the written agreements were set forth in the Court of Civil Appeals decision, 58 O&GR 378. After drilling the well, assignor sought the balance due from defendants, who refused to pay. Suit for balance due was filed. Defendants defend upon the Statute of Frauds, Tex. Bus. & C.C. § 26, which provides that a contract for the sale of real estate must be in writing and signed by the party to be charged. The defendants had signed the farmout letter agreements, but the name of the assignor did not appear in either of the farmout letter agreements. The defendant contended that the written letter agreements were not complete in that they did not name the party to assign the acreage and that the name of the assignor was an essential part of a contract and could not be supplied by parol evidence. Both parties filed for summary judgment. Plaintiff's motion was denied and defendants' motion was granted, and a take nothing judgment was rendered against plaintiff. On appeal to the Court of Civil Appeals, the trial court was affirmed on the basis that the written contract upon which the suit was based did not contain the name of the assignor and that such an essential term could not be supplied by the check stubs and other memoranda introduced to show the identity of the assignor, such not being in existence at the time of the contract. 58 O&GR 378. On appeal, held: Affirmed. The issue on appeal was whether the defendants had sustained their summary judgment burden of negating the existence of other memoranda which might meet the requirements of the Statute of Frauds and show the identity of the assignor. Since plaintiff had pleaded the two written letter agreements as the basis of his suit, and had not al-

CABOT CORPORATION v. BROWN et al.

Texas Court of Appeals, Corpus Christi
August 29, 1986—No. 13-85-070-CV
716 S.W. 2d 656
(Rehearing denied September 30, 1986)
(Writ granted April 22, 1987)

Royalties and Royalty Interests: Division Order—Binding Effect of Division Order Until Revoked—Division Order Until Revoked Alleviates Implied Covenant To Reasonably Market—Division Order Can Result in Payment of Gas Royalty Less Than Market Value Provided in the Lease.

Breach of implied covenant to reasonably market and the effect of division order. Brown, and others, executed a lease to Cabot in 1967, and upon which it drilled a producing gas well in 1968. The lease provided for gas royalty on market value of gas sold or used off the premises. In 1968, Brown signed a division order obligating Cabot to pay royalties based on prices determined by the Federal Power Commission ". . . if such sale be subject to the Federal Power Commission." In 1967, Cabot and TW Pipeline Co. had entered into an "Exchange of Gas" agreement. Under this contract Cabot delivered gas from Brown's well to TW at its interstate pipeline in another county in Texas, and TW delivered from its interstate pipeline from another point in Texas an equivalent volume of gas to Cabot, which then transported the gas to its processing plant in Texas. Cabot paid 2 cents per MCF to TW for transportation. Cabot sought and received a "Henshaw exemption" from applicable FPC regulations on September 26, 1975, for the exchange gas processed and sold in Texas. After processing by Cabot at its processing plant, the majority of this gas was sold in the intrastate market at $1.35 per MCF. Because this price exceeded that price on which royalties paid was based, Brown filed suit in March, 1981, claiming that Cabot had failed to reasonably market the gas for four years prior to filing the suit. Cabot had paid royalties of $0.35 per MCF from March, 1977, to October, 1980, and $0.80 per MCF from October 1980 to date of trial. Brown claimed that the FPC regulations had not attached to the sale of the gas and that royalties had been on an amount less than market value, and in the alternative, if FPC jurisdiction had attached to the gas exchange, Cabot had an obligation to seek an abandonment from the FPC of its jurisdiction. Jury found that Cabot had failed to reasonably market the gas, and had failed to pay royalties based on market value from March 19, 1977 to present. Judgment

Texas follows the rule that reinjected gas is owned by the injector and not the owner of the mineral estate (Lone Star Gas Co. v. Murchison, 353 S.W. 2d 870, 16 O&GR 816 (Tex. Civ. App. 1962), writ ref'd n.r.e.), but the City nonetheless made an interesting point in the factual determination of how much recoverable gas was located in the storage formation. In theory the injector should be able to present evidence that its injection program artificially increases reservoir pressure which would increase the amount of gas that would otherwise be economically recoverable by the owner of the mineral interest. In this case such evidence was apparently presented but the jury chose to ignore it. I believe that the holding is sound in that the amount of recoverable gas is a fact question and should not be determined as a matter of law. The city in this case failed to persuade the factfinder that what was economically recoverable should have been discounted by the artificial pressure caused by its injection and storage program. The case again shows the need to control all of a storage horizon in order to avoid serious problems with mineral owners and adverse jury findings.

It is also interesting to note that Texas allows punitive or exemplary damages to be recovered against municipalities where the acts were committed with "malice or evil intent" or such gross negligence as to be equivalent to such intent. City of Gladewater v. Pike, 727 S.W. 2d 514 (Tex. 1987). Punitive damages are not available, however, against a municipality, if a plaintiff files a 42 U.S.C. § 1983 action. City of Newport v. Fact Concerts, Inc., 453 U.S. 247 (1981).

B.M.K.

from the cross-defendant's lands. The judgment did not expressly dispose of the cross-defendants.

The Texas Supreme Court in North East Independent School District v. Aldridge, 400 S.W. 2d 893, 897-8 (Tex. 1966), recognized that it is not always essential that the judgment expressly dispose of all parties and issues:

> When a judgment, not intrinsically interlocutory in character, is rendered and entered in a case regularly set for a conventional trial on the merits, no order for a separate trial of issues having been entered pursuant to Rule 174, Texas Rules of Civil Procedure, it will be presumed for appeal purposes that the Court intended to, and did, dispose of all parties legally before it and of all issues made by the pleadings between such parties.

So far as can be determined from the record, Hickey was never served with citation and did not answer. Therefore, the case stands as if there had been a discontinuance as to Hickey, and the judgment is to be regarded as final for the purposes of appeal. Youngstown Sheet & Tube Co. v. Penn, 363 S.W. 2d 230 [17 O&GR 836] (Tex. 1962). While the judgment did not expressly decree that the City take nothing as to the cross-defendants, the trial court by implication found no liability as to cross-defendants when the judgment is considered in its entirety. See Twin City Fire Insurance Company v. Brown, 602 S.W. 2d 118 (Tex. Civ. App.—Waco 1980, no writ).

All of the points of error are overruled. The judgment of the trial court is affirmed.

DISCUSSION NOTES

Underground Storage of Gas: Ownership—Slander of Title—Tortious Interference with Contractural Relationship.

The court was quite correct in stating that

owns the wells. And all we need to know is how much he is entitled to produce.

ATTORNEY FOR PLAINTIFFS: Well, that is fine. I just wanted that on the record.

THE COURT: Then it will be agreed and stipulated that the judgment will recite—

ATTORNEY FOR CITY: *He's entitled to produce X amount of gas out of those wells.*

ATTORNEY FOR PLAINTIFFS: And it will be the first gas that he produces. He doesn't have to share it or anything. Whatever the jury says is his net recoverable, economic recoverable gas, less what he's already produced, he can produce that much gas.

ATTORNEY FOR CITY: *That's right. They are his wells, he can open them up.*

THE COURT: It's so agreed then and stipulated. (Emphasis added)

The City cannot now complain that the trial court committed reversible error when the act of which it complains actually benefitted the City. Moreover, the City stipulated that the Bennies, Diamond, and Morris were "entitled to produce X amount of gas out of those wells." The amount of native gas that the Bennies, Diamond, and Morris were allowed to recover under the trial court's judgment is *less* than the amount the City agreed that plaintiffs could recover.

Finally, the City contends that the trial court erred in entering a judgment which did not dispose of all the parties. The City brought a cross-action against Rosanell Caraway Hickey and Union Central Life Insurance Company as cross-defendant's for an accounting of the gas previously withdrawn and for a declaration of the amount of native and extraneous gases remaining for production

native gas is the property of the Defendant, City of Brady, or their assigns.

During the objections to the charge, the following discussion occurred between the trial court and counsel for the parties:

ATTORNEY FOR PLAINTIFFS: Your Honor, there are a couple of matters that I think need to be made on the record, in regard to the case. The first is that I have been troubled by the fact that we do not have a percentage of gas question, as you know. My inquiry at this point in time is that when the jury answers how much mcf is in place under the proposed charge it's theoretically possible that there could be gas under the lease still that was injected gas as well. And [the attorney for the city] said that he felt that the court would in its judgment take care of that problem by reciting that Mr. Bennie would be entitled to take the amount that the jury put in there, in that issue as his gas as the first gas withdrawn.

Now, if that is correct and we can have that stipulation, then that will solve the problem of the percent.

* * *

Now, if [the attorney for the City] and I can agree, the court will enter it in the judgment if there is one appropriate. I must add that whatever they put as native gas, you know, it would be less what Mr. Bennie's already produced since the date would have to be subtracted from that, but the balance would be his to recover as the first gas he recovers. That would solve the problem.

ATTORNEY FOR CITY: *I don't have any objection to that. That is what I proposed earlier. My notion in the matter is Bennie's got wells out there, they are on his property and he*

time of the purchase of the land by them absent injection of extraneous gas was 200,000 MCF. The Court finds further that the Bennies produced and sold gas in the amount of 14,166 MCF from the time they purchased the property until the wells were shut in on the 5th day of March, 1984. The Court further finds that the Plaintiffs have been damaged according to the answer in Special issue #6 in the amount of TWO HUNDRED AND SEVENTY FIVE THOUSAND DOLLARS ($275,000.00). The Court finds that the fair market value of gas was $3.00 per MCF and said sum therefore totals 91,666 MCF. The Court finds therefore, that the damages awarded are the fair market value of 91,666 MCF. The Court further finds that the Plaintiffs have produced 14,166 MCF of gas from the 31st day of July, 1981 until March 5, 1984 which includes funds suspended and held by Lone Star Gas Company, plus 91,666 MCF they have received credit for as damages leaving 94,168 MCF of native recoverable gas under their property absent injection of extraneous gas. The Court further finds that the first gas to be produced from the "Caddo" formation by the Bennie #1 and Bennie #3 wells after the entry of this Judgment in the amount of 94,168 MCF will be native gas absent extraneous injection gas and will be the property of the Plaintiffs. Any remaining gas following the production of that amount will be injected gas and the property of the Defendant or their assigns.

IT IS THEREFORE, ORDERED, ADJUDGED AND DECREED by the Court that Terry Bennie, Julie Bennie, Diamond Mineral Investments, Inc., and Dr. J.L. Morris do own 94,168 MCF in the "Caddo" Formation under the Terry Bennie properties which is native recoverable gas absent injection of extraneous gas which is their property and which may be produced by them. Any remaining gas following the removal of the

attorneys were discussing the proposed charge of the court, the City stipulated that the only thing that would keep the O'Brien leases "alive" would be the farmout agreement litigation. This litigation between O'Brien (the lessee) and Brady Gas (the assignee) did not constitute a "repudiation" of the lease by the lessor.

At best, the evidence raises a fact question as to the validity of the O'Brien leases. The trial court properly overruled the City's motion for judgment notwithstanding the verdict.

The City next argues that the trial court erred in admitting evidence of the City's dealings with Archer and the Archer tract because such evidence was highly prejudicial to the City as it was used to create an argument that the City had discriminated against the Bennies, Diamond, and Morris. The City objected at trial on the grounds that the witness could not "speculate on why the City treated somebody differently if, in fact, they treated them differently. Mr. Archer's a problem we've got to deal with and we're not dealing with him in this lawsuit."

The objection at trial is not the same as the objection urged in the point of error and presents nothing for review. Texas Imports v. Allday, 649 S.W. 2d 730 (Tex. App.—Tyler 1983, writ ref'd n.r.e.); Wilkerson v. Pic Realty Corp., 590 S.W. 2d 780 (Tex. Civ. App.—Houston [14th Dist.] 1979, no writ). The testimony concerning the City's dealings with Archer was admissible because it was relevant to the issue of whether the City acted with malice.

The City argues that the trial court entered its judgment based upon findings not made by the jury and not requested to be submitted to the jury. The Trial court's judgment states in part:

> The Court finds that in Answer to Special Issue #1 that the jury found that the economic recoverable gas in the "Caddo" formation under the Bennie property at the

International, Inc., 369 S.W. 2d 797 (Tex. Civ. App.—Beaumont 1963, writ ref'd n.r.e.); Kingsbery v. Phillips Petroleum Company, 315 S.W. 2d 561 (Tex. Civ. App.—Austin 1958, writ ref'd n.r.e.); Richardson v. Terry, 212 S.W. 523 (Tex. Civ. App.—El Paso 1919, writ dism'd); and Roberts v. Clark, 103 S.W. 417 (Tex. Civ. App.—1907, no writ).

These cases deal with contracts terminable at will or with option contracts where the non-performing party had the absolute or legal right to arbitrarily refuse to carry out the contract. The gas purchase agreement was not similar to the terminable at will contracts and option contracts found in the above cases; therefore, these cases are not controlling.

The record does not support the City's contention that the only reason Lone Star shut in the Bennie No. 1 was because the carbon dioxide content of the gas exceeded three percent. As previously discussed, the record supports the theory that Lone Star shut in the Bennie No. 1 because of the letter.

Next, the City contends that the trial court erred in not granting its motion for judgment notwithstanding the verdict because the undisputed evidence demonstrates that the City owned valid leases covering the mineral estate beneath the Bennie property. The alleged error of the trial court in refusing to render judgment non obstante veredicto raises only no evidence questions for appellate review. Rego Company v. Brannon, 682 S.W. 2d 677 (Tex. App.—Houston [1st Dist.] 1984, writ ref'd n.r.e.); Wise v. Pena, 552 S.W. 2d 196 (Tex. Civ. App.—Corpus Christi 1977, writ dism'd). In acting upon a motion for judgment notwithstanding the verdict, all testimony must be considered in a light most favorable to the party against whom the motion is sought, and every reasonable intendment deducible from the evidence is to be indulged in such party's favor. Miranda v. Joe Myers Ford, Inc., 638 S.W. 2d 36

held liable for exemplary damages. The Supreme Court recently set out the acts which give rise to a claim for exemplary damages against a municipality in City of Gladewater v. Pike, 727 S.W. 2d 514, 523 (Tex. 1987):

> In the context of exemplary damages against a municipality, however, we agree with the reasoning used by the Fifth Circuit in Peace v. City of Center, 372 F. 2d 649 (5th Cir. 1967). There, the court held that liability will result only if it is "pleaded and proved that the acts giving rise to the claim were committed with such malice or evil intent, or such gross negligence as to be equivalent to such intent." Peace at 650. Thus, in order to recover, the plaintiff must show at least that amount of conscious indifference which would tend to show *malice or evil intent* on the part of the actor. (Emphasis added)

A finding of actual malice will support an award of exemplary damages. Courts have defined actual malice as "ill-will, spite, evil motive, or purposing the injuring of another." Top Value Enterprises, Inc. v. Carlson Marketing Group, Inc. 703 S.W. 2d 806, 813 (Tex. App.—El Paso 1986, writ ref'd n.r.e.). See Fortner v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 687 S.W. 2d 8 (Tex. App.—Dallas 1984, writ ref'd n.r.e.); State National Bank of El Paso v. Farah Manufacturing Company, Inc., 678 S.W. 2d 661 (Tex. App.—El Paso 1984, writ dism. by agr.).

The City contends that there was no breach of contract because the gas purchase agreement contained a provision which allowed Lone Star the right not to purchase the gas if the carbon dioxide content of the gas exceeded three percent and because the record reflects that the carbon dioxide content was consistently above this level. Arguing that a cause of action for interference with contractual relations cannot exist where a party has an option under the contract to either perform or not perform, the City cites the following cases: C. E. Services v. Control Data Corporation, 759 F. 2d 1241 (5th Cir. 1985); Davis v. Alwac

from the time the Bennie No. 1 was shut-in until the time of trial.

There is evidence of probative force to support the jury's finding in Special Issue No. 4 that the writing of the letter was a proximate cause of the damages to the Bennies, Morris, and Diamond. After carefully reviewing all the evidence, we hold that the jury's finding on Special Issue No. 4 is not so contrary to the overwhelming weight of the evidence as to be clearly wrong and unjust.

Next, the City challenges the jury's findings to Special Issues Nos. 5 and 7.

Special Issue No. 5 contains an improper definition of "actual malice," but the City did not object. Tex. R. Civ. P. 274 states that "[a]ny complaint as to an instruction, issue, definition or explanatory instruction, on account of any defect, omission, or fault in pleading, shall be deemed waived unless specifically included in the objections." See Yellow Cab and Baggage Company v. Green, 277 S.W. 2d 92 (Tex. 1955); Charter Builders v. Durham, 683 S.W. 2d 487 (Tex. App.—Dallas 1984, writ ref'd n.r.e.); Jones v. City of Odessa, 574 S.W. 2d 850 (Tex. Civ. App.—El Paso 1978, writ ref'd n.r.e.). Because the City did not object, the City is bound by the definition submitted and has waived its right to complain about this definition on appeal.

As stated above, the evidence is sufficient to support a finding by the jury that the City sent the letter with reckless disregard of whether it was false or not. We hold that there is evidence of probative force to support the jury's findings in Special Issues Nos. 5 and 7 on actual malice and exemplary damages and that the jury's finding on Special Issue No. 5 is not so contrary to the overwhelming weight of the evidence as to be clearly wrong and unjust.

The City also challenges the findings to Special Issues Nos. 5 and 7 on the grounds that a municipality cannot be

the storage reservoir, and that the City had decided to "do nothing" about the situation. The jury could have inferred that the February 7, 1984, letter to Lone Star was an intentional continuation of the City's policy to "just wait them [the Bennies] out."

The Bennies, Diamond, and Morris argue that the record establishes that the "City Council determined that they would attempt to starve out Terry Bennie." However, this "starve out" testimony was presented outside the presence of the jury. We cannot consider the statements made outside the presence of the jury in determining a no evidence or a factually insufficient evidence point of error.

There is evidence of probative force to support the jury's finding in Special Issue No. 3 that writing the letter was an act of unjustified interference by the City. After carefully reviewing all the evidence, we hold that the jury's finding on Special Issue No. 3 is not so contrary to the overwhelming weight of the evidence as to be clearly wrong and unjust.

There is evidence that the writing of the letter proximately caused the damages to the Bennies, Morris and Diamond. Plaintiff's Exhibit No. 64, a Lone Star interoffice memo, stated:

> The February 7 letter from Mr. J. E. Gangstad, an attorney representing the City of Brady, appears to create a bona fide controversy concerning ownership of gas produced from the Terry Bennie No. 1 Well; therefore, under the provisions of Article XIII of the subject gas purchase contract it would be proper to suspense payments for production from the subject well until the controversy between the City of Brady and Diamond Mineral Investments has abated.

The record also reflects that while the Bennie No. 1 was shut-in, the gas pressure for the well decreased. The jury awarded damages in Special Issue No. 6 for the loss of gas

Refining Co., 83 S.W. 2d 935 (Tex. 1935). Therefore, the Bennies, Diamond, and Morris were entitled to recover the native gas beneath their land.

After carefully reviewing all the evidence, we hold that there is evidence of probative force to support the jury's findings to Special Issues Nos. 1 and 6 and that those findings are not so contrary to the overwhelming weight of the evidence as to be clearly wrong and unjust.

The City also challenges the findings to Special Issues Nos. 3 and 4.

Gary D. Askins, a former general manager of the City's gas contracts and lease records and an assistant city manager in charge of general management of the Brady Gas Company, testified as to problems with various titles to tracts of land in the Janellen Field. Askins examined the farmout agreements, the City's records, and other related documents dealing with various tracts in the Janellen field. He informed the City Council several times "that we had a serious problem with the Bennie properties"; that "several of these leases had expired and there were holes in the field"; and that in his opinion "the George O'Brien oil and gas lease had expired, due to nonpayment of rentals or nonpayments of delay royalties." Askins recommended that the council authorize him to contact Mr. Bennie and "offer to essentially reacquire a storage lease on his land for some cash consideration" or that the council proceed with condemnation proceedings. Askins was authorized to make an initial contact with Bennie in early 1982 but nothing further was done. Askins testified that the council wanted to wait to see what developed. Askins also testified that the same problem existed with another tract of land known as the Archer tract but that the City handled that situation differently.

Askins' testimony reflects that the City was aware that the O'Brien leases had expired, that there were "holes" in

able native gas absent the pressurization caused by the injected gas.

The City argues that "absent" means absent the increased pressurization caused by the injected gas. Again, we disagree. The phrase "absent the injection of extraneous gas" as used in the context of Humble Oil and Refining Company v. West, supra, means that the Bennies, Diamond, and Morris are entitled to recover only the native gas, not native gas and extraneous gas. The phrase "absent the injection of extraneous gas" means to subtract or take away the extraneous gas from the total gas beneath the Bennie land. Even if the native gas was commingled with the injected or extraneous gas, there is sufficient evidence to support the jury's finding that, "absent" the injected gas, the volume of economically recoverable native gas was 200,000 mcf. The City's pressurization theory is not applicable.

The record supports the theory that the gas beneath the Bennie property is native gas, not injected or commingled gas. Dan Tindol, a chemist, testified that he compared samples of the gas from the Bennie No. 1 with samples of the injected gas and concluded that the samples were "two different gases" from "two different sources." Stacey Smyre, an engineer, testified that the gas under the Bennie tract was different from the injected gas.

The Texas Supreme Court stated in Elliff v. Texon Drilling Co., 210 S.W. 2d 558, 561 (Tex. 1948):

> In our state the landowner is regarded as having absolute title in severalty to the oil and gas in place beneath his land. The only qualification of that rule of ownership is that it must be considered in connection with the law of capture and is subject to police regulations. (Citations omitted)

See Halbouty v. Railroad Commission, 357 S.W. 2d 364, 374[16 O&GR 788] (Tex. 1962); Brown v. Humble Oil &

S.W. 2d 812 [48 O&GR 516] (Tex. 1974); Exxon Corporation v. West, 543 S.W. 2d 667 [56 O&GR 398] (Tex. Civ. App.—Houston [1st Dist.] 1976, writ ref'd n.r.e.), cert. denied, 434 U.S. 875, 98 S. Ct. 224, 54 L.Ed. 2d 154 (1977); and Lone Star Gas Company v. Murchison, 353 S.W. 2d 870 [16 O&GR 816] (Tex. Civ. App.—Dallas 1962, writ ref'd n.r.e.). These cases do not support the City's "pressure" theory.

The court in Lone Star Gas Company v. Murchison, supra at 878, [16 O&GR at 826-827], embraced the language of White v. New York State Natural Gas Corp., 190 F. Supp. 342 [14 O&GR 253] (W.D. Pa. 1960), where it was stated that "[o]nce severed from the realty, however, gas and oil, like other minerals, become personal property . . . .[T]itle to natural gas once having been reduced to possession is not lost by the injection of such gas into a natural reservoir for storage purposes." See also Humble Oil and Refining Company v. West, supra at 817 [48 O&GR at 525]. The Court in Humble Oil and Refining Company v. West, supra at 819 [48 O&GR at 528], reached the following holding:

> [I]t is our view that the act of commingling native and extraneous gas did not impose upon Humble [the injector of the gas] the obligation of paying royalties on all [both injected and native] gas thereafter produced from the reservoir, if the evidence establishes with reasonable certainty the volume of gas reserves upon which the Wests would have been entitled to royalties, absent injection of extraneous gas.

The Exxon Corporation v. West case involved the re-trial and subsequent appeal of the Humble Oil and Refining Company v. West case. The above cases do not require the fact finder to take the "pressure" of the injected gas into consideration when determining the amount of recoverable native gas. The jury in Special Issue No. 1 was not asked to determine the amount of economically recover-

damages. You may consider compensation for inconvenience, attorney's fees, expense of litigation, and other expenses not recoverable as actual damages.

The City argues that there is no evidence to support the jury's answers to all of these special issues and that, alternatively, there is insufficient evidence to support the jury's answers to Special Issues Nos. 1, 3, 4, 5, and 6. We disagree.

In reviewing a no evidence point, only the evidence and the inferences therefrom which tend to support the jury verdict shall be considered, with all evidence to the contrary being disregarded; and if there is any evidence of probative value to support the jury verdict, the verdict must be affirmed. International Armament Corporation v. King, 686 S.W. 2d 595 (Tex. 1985); Martinez v. Delta Brands, Inc., 515 S.W. 2d 263 (Tex. 1974); Garza v. Alviar, 395 S.W. 2d 821 (Tex. 1965). In reviewing the City's factually insufficient evidence points of error, this Court must consider and weigh all the evidence and reverse the trial court only if the jury's findings are so contrary to the overwhelming weight of the evidence as to be clearly wrong and unjust. Pool v. Ford Motor Company, 715 S.W. 2d 629 (Tex. 1986); Dyson v. Olin Corporation, 692 S.W. 2d 456 (Tex. 1985); In re King's Estate, 244 S.W. 2d 660 (Tex. 1951).

Concerning Special Issues Nos. 1 and 6, the City contends that: (1) there is no evidence that, absent the injected gas, the economically recoverable native gas is 200,000 mcf; and (2) the reason the economically recoverable gas under the Bennie tract, absent the injection of extraneous gas, is zero is "because when the *pressure* in the reservoir furnished by the volume of injected gas is removed from consideration, there is insufficient *pressure* to allow economic recovery." (Emphasis added) In support of this position, the City cites the following cases as controlling: Humble Oil and Refining Company v. West, 508

that the City of Brady acted with actual malice in sending the letter to Lone Star Gas Company on February 7, 1984?

Answer "We do" or "We do not."

ANSWER: We do

You are instructed that "ACTUAL MALICE" means that something is communicated with knowledge that it was false or with reckless disregard of whether it was false or not.

If you have answered Special Issue No. 5 "We do," and only in that event, answer Special Issue No. 7.

SPECIAL ISSUE NO. 6

What sum of money, if paid now in cash, do you find from a preponderance of the evidence would compensate the Plaintiffs for their damages, if any, from the loss of their gas from the Bennie property from March 5, 1984 until the present time?

Answer in dollars and cents, if any.

ANSWER: $275,000.00

SPECIAL ISSUE NO. 7

What sum of money, if paid now in cash, do you find from a preponderance of the evidence, should be assessed against the City of Brady as exemplary damages?

Answer in dollars and cents, if any.

ANSWER: $25,000.00

"EXEMPLARY DAMAGES" means an amount that you may in your discretion award as an example to others and as a penalty or by way of punishment, in addition to any amount you may have found as actual

SPECIAL ISSUE NO. 3

Do you find from a preponderance of the evidence that the writing of the letter of February 7, 1984 was an act of unjustified interference by the City of Brady between the Plaintiffs and Lone Star Gas Company?

Answer "We do" or "We do not."

ANSWER: We do

You are further instructed that a party is justified in interfering with contractual relationships of others where such interference is in exercise of the party's own rights or where the party possesses an equal or superior interest in the subject matter.

If you have answered Special issue No. 3 "We do," and only in that event, answer Special Issue No 4.

SPECIAL ISSUE NO. 4

Do you find from a preponderance of the evidence that such act was a proximate cause of the damages to the Plaintiffs, if any?

Answer "We do" or "We do not."

ANSWER: We do

The term "PROXIMATE CAUSE" means that cause which, in a natural and continuous sequence, produces an event, and without which cause such event would not have occurred; and in order to be a proximate cause, the act or omission complained of must be such that a person using ordinary care would have foreseen that the event, or some similar event, might reasonably result therefrom.

SPECIAL ISSUE NO. 5

Do you find from a preponderance of the evidence

the same case." 48 Tex. Jur. 3d Judgments sec. 353 (1986). 48 Tex. Jur. 3d Judgments sec. 353 (1986) also states:

> The doctrine of stare decisis is a rule under which the determination of a question of law by a court of ultimate resort becomes a part of the law of the state and a precedent governing the decision of subsequent matters involving the same point.

The question of law decided in the appeal of the libel suit, that an absolute privilege should be granted to the attorney's letter relating to pending or proposed litigation, differs from the qualified privilege question in this case. Here, the City is not entitled to an "absolute" privilege defense in a suit for tortious interference. See Sakowitz, Inc. v. Steck, supra. Even though the letter was a privileged communication by the City's attorney in an action in damages for libel, the cause of action for tortious interference against the City is not barred. See James v. Brown, supra; Steck v. Sakowitz, Inc., 659 S.W. 2d 91 (Tex. App. — Houston [14th Dist.] 1983), rev'd on other grounds, 669 S.W. 2d 105 (Tex. 1984).

The trial court submitted the following special issues involving the tortious interference theory:

SPECIAL ISSUE NO. 1

> From a preponderance of the evidence, what do you find to have been the volume of economically recoverable native gas, if any, which the Bennies would have had under their land on July 31, 1981 absent injection of extraneous gas?
>
> Answer in mcf:
>
> ANSWER: 200,000 MCF

* * *

Justice Wallace in his dissenting opinion, supra at 109, also stated:

> It must be noted that the claimed privilege is not absolute, *but qualified*, and can only be sustained if the interferor can show either: (1) that he has an equal or superior right to that of the plaintiff or, (2) he has a good faith belief that such a superior right exists. C.f., Black Lake Pipe Line Co. v. Union Construction Co., 538 S.W. 2d 80, 91 (Tex. 1976). (Emphasis in original)

Citing Griffin v. Rowden, 702 S.W. 2d 692 (Tex. App. — Dallas 1985, writ ref'd n.r.e.), the City argues that lis pendens is absolutely privileged in an action for tortious interference with a contract. The letter was not the filing of a lis pendens, and this case does not involve lis pendens.

The City also claims that the libel suit is conclusive of this case, is res judicata, is the law of the case, and is stare decisis. We disagree.

Res Judicata is defined as:

> [T]he doctrine that a question of law or fact, distinctly put in issue and directly determined by a court of competent jurisdiction as a ground for recovery or defense in a suit or action between parties sui generis, is conclusively settled by the final judgment or decree therein, so that it cannot be futher litigated in a subsequent suit between the same parties or their privies.

48 Tex. Jur. 3d Judgments sec. 351 (1986). This appeal involves different causes of actions, issues, and parties than the libel suit. Therefore, the doctrine of res judicata does not apply; and the libel suit is not conclusive of this case.

The City also argues that the doctrines of the law of the case and of stare decisis apply. The doctrine of the law of the case "applies only to decisions of questions of law and is confined in its operation to subsequent proceedings in

ages is precluded because of this Court's opinion in the libel suit;[3] (3) there is no evidence, and alternatively insufficient evidence, to support the jury's findings on the tortious interference with a contract theory; (4) exemplary damages cannot be awarded against a municipality; (5) no breach of the Lone Star gas purchase contract occurred; (6) the City had valid mineral leases on the Bennie property; (7) testimony was improperly admitted; and (8) the judgment was based upon findings not submitted to the jury and did not dispose of all the parties. In view of our affirmance on the tortious interference theory, the points challenging the findings on the slander of title theory will not be discussed.

The City argues that the trial court erred in refusing to grant the City's motion for judgment notwithstanding the verdict because the letter sent to Lone Star was absolutely privileged as determined in the libel suit. We disagree.

Communications made in the course of a judicial proceeding are absolutely privileged and cannot constitute the basis of an action for libel or slander. Reagan v. Guardian Life Ins. Co., 166 S.W. 2d 909 (Tex. 1942). This privilege extends to communications made in contemplation of a judicial proceeding. James v. Brown, 637 S.W. 2d 914 (Tex. 1982). However, as stated by the majority and dissenting opinions in Sakowitz, Inc. v. Steck, 669 S.W. 2d 105 (Tex. 1984), a "qualified," but not an "absolute," privilege may be urged in a suit for tortious interference. The majority opinion in Sakowitz, Inc. v. Steck, supra at 107, stated:

> To establish the necessary elements for her claim of tortious interference, Steck [plaintiff] had to show (1) that the defendant maliciously interfered with the contractual relationship, (2) without legal justification or excuse.

[3] Terry Bennie et ux. et al. v. Brown, Maroney, Rose, Barber, and Dye and John E. Gangstad, supra.

> Our client [City of Brady] has previously injected natural gas into the Janellen (Caddo) Field and believes that the Subject Well [Bennie Well No. 1] is producing such injected gas. As you know (see Lone Star Gas Co. v. Murchison, 353 S.W. 2d 870 [16 O&GR 816] (Tex. Civ. App.—Dallas, 1963 writ ref'd n.r.e.) it is the rule in Texas that the owner of natural gas does not lose title thereto when that gas is stored in an underground reservoir. By draining our client's stored natural gas, Diamond is guilty of converting that gas and has no authority to sell such gas to Lone Star.
>
> The City of Brady has instructed us to pursue all available legal remedies to protect its stored gas. We hereby request that payments be suspended until title to the gas in question can be determined.

The letter was dated February 7, 1984; Lone Star shut in the Bennie No. 1 on March 5, 1984.

The Bennies and Diamond sued the City alleging tortious interference with the Lone Star gas purchase contract and slander of title and sued the attorney for libel. Summary judgment was granted in favor of the attorney, and the libel suit was severed from the present case.[2] Morris was then added as a plaintiff to the tortious interference with a contract and slander of title actions.

The City contends that: (1) there is no evidence, and alternatively insufficient evidence, to support the jury's finding on the slander of title theory; (2) recovery for dam-

[2] The summary judgment in the libel suit was affirmed by this Court on appeal. Terry Bennie et ux. et al. v. Brown, Maroney, Rose, Barber, and Dye and John E. Gangstad, No. 11-85-069-CV (Tex. App.—Eastland, August 1, 1985, no writ) (unpublished opinion). This Court held that the attorney's letter was written preliminary to a proposed judicial proceeding ans was, therefore, absolutely privileged. Russell v. Clark, 620 S.W. 2d 865 (Tex. Civ. App.—Dallas 1981, writ ref'd n.r.e.).

agreement; and Tanbark drilled wells under the terms of the farmout agreement. Brady Gas refused to deliver assignments of the acreage allegedly earned by the Tanbark wells contending that Tanbark had improperly drilled into the storage reservoir. This refusal to assign resulted in Tanbark suing Brady Gas.[1] Eventually Brady Gas' assets, as well as its contracts and liabilities, were transferred to the City of Brady.

On July 31, 1981, Terry and Julie Bennie purchased the three tracts of land from Morris. Morris retained a mineral interest in the tracts. These tracts are known as Bennie Tracts Nos. 1, 2, and 3. In September of 1982, Diamond Mineral Investments, Inc., a closely held family corporation formed by the Bennies, acquired a lease from the Bennies and Morris on Tract No. 3. Diamond purchased the well known as the Bennie No. 1 on Tract No. 3 from Tanbark in May 1983 and subsequently entered into a gas purchase agreement with Lone Star Gas Company to sell gas from the Bennie No. 1.

The present suit arose out of a letter concerning the purchase of gas from the Bennie No. 1. The letter, written by an attorney employed by the City and addressed to Lone Star, stated in part:

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[1] Prior to trial in the state court, Brady Gas filed a petition in bankruptcy; and the state court action was stayed. The Bankruptcy Court approved a reorganization plan which provided in part that all of Brady Gas' assets would be transferred to the City of Brady and that the City would assume all contracts and obligations. Summary judgment was then granted in the state court action in favor of the City on the grounds that Tanbark's damage claim was barred by res judicata because it could have been pursued in the bankruptcy court but was not. The summary judgment was affirmed on appeal. Tanbark Oil Company 1978-1, Ltd., George H. O'Brien and George O. Sanders v. City of Brady, Texas, No. 11-85-080-CV, (Tex. App.—Eastland, August 22, 1985, writ ref's n.r.e.) (unpublished opinion).

said reservoir which inflated the amount of recoverable gas. The court concluded that the jury need not have been instructed that they must not consider the artificial pressure of the reservoir in coming to their conclusion as to how much economically recoverable natural gas was in place. The court also concluded that there was evidence in the record to support a finding of actual malice on behalf of the City in order to meet the requirements for the tortious interference claim. That same finding of actual malice could also be used to support an award of punitive damages against the municipality.

McCLOUD, Chief Justice.

Terry and Julie Bennie, Dr. J.L. Morris, and Diamond Mineral Investments, Inc. sued the City of Brady for tortious interference with a gas purchase contract and for slander of title. Based upon the jury's answers to special issues, judgment was entered for the plaintiffs. We affirm.

Dr. J.L. Morris owned three tracts of land in Brown County which covered a part of a gas storage reservoir located in the Caddo Formation in the Janellen Field. In 1962, Morris entered into a 10-year gas storage lease covering these three tracts. The gas storage lease contained two 10-year renewal options; however, the storage lease expired in 1972 when Brady Municipal Gas Corporation, the holder of the lease, failed to properly exercise the first 10-year option.

In 1976, Morris leased by separate leases the three tracts to George O'Brien, who subsequently assigned the leases to Brady Gas. Brady Gas then entered into a farmout agreement with O'Brien which allowed O'Brien to produce minerals above and below a defined area of the Caddo Formation. Under the terms of the agreement, Brady Gas was to assign to O'Brien or his assignees acreage within the leases upon the drilling and completion of wells to a depth either above or below the designated area. Through subsequent, partial assignments, George O. Sanders and Tanbark Oil Company acquired interests in the farmout

CITY OF BRADY v. BENNIE et al.

Texas Court of Appeals, Eastland
July 18, 1987—No. 11-86-087-CV
735 S.W. 2d 275
(Rehearing denied September 17, 1987)

Underground Storage of Gas: Ownership—Slander of Title—Tortious Interference with Contractual Relationship.

The plaintiffs were the owners of the mineral interests in the Caddo Formation. At one time the defendant City or its predecessor in interest owned the gas storage rights in the formation pursuant to a lease. The lease purportedly expired as to the plaintiff's interest. The plaintiffs developed their mineral estate and entered into a gas purchase contract with Lone Star Gas. The City authorized its attorney to send a letter to Lone Star informing them that the gas was owned by the City and not by the plaintiffs. Lone Star immediately began to place the purchase money into a suspense account. Plaintiffs instituted this action claiming tortious interference with the contract, slander of title and libel against the attorney who wrote the letter. The libel action was severed and tried separately. A summary judgment was entered for the attorney in that case, the court concluding that the letter was absolutely privileged as it was written preliminary to a proposed judicial proceeding. The remaining two causes of action were tried to a jury which found that the defendants had tortiously interfered with the plaintiff's gas purchase contract and awarded both compensatory and punitive damages against the City. Held: Affirmed. The City made numerous challenges to the jury's verdict all of which were rejected by the court. Initially they argued that the judgment in the libel suit was either the law of the *case or res judicata*. The court disagreed noting that in libel cases there is an absolute privilege for communications made in anticipation of a lawsuit while in this case only a qualified privilege was involved in the cause of action alleging tortious interference with contract. In discussing the challenge to the jury's verdict that the plaintiffs owned the gas they were selling, the court concluded that while it was clear that the City did have title to the reinjected gas it was equally clear that title to the native gas belonged to the plaintiffs. The court rejected the City's claim that the jury's finding that there was 200,000 MCF of recoverable native gas was without any basis in the record. The City proffered the theory that whatever native gas there was below the plaintiffs' acreage, the fact that the City injected gas into the reservoir artificially increased the pressure of

RAYL v. EAST OHIO GAS COMPANY et al.*

Ohio Court of Appeals
Summit County
August 8, 1973—Docket No. 7141
348 N.E. 2d 385

Storage of Gas: Distinction Between Oil and Gas Lease and Gas Storage Agreement.

In 1928, predecessors in title to the appellant executed and delivered to the appellee an oil and gas lease which gave appellee the right to drill for oil and gas for a minimum rental plus an additional royalty for any oil or gas produced. Appellant drilled several wells and produced gas; a $200 gas royalty was paid quarterly. In 1948, the original lease was supplemented by appellant's predecessors in title by a document entitled "Supplemental Gas Storage Agreement." This agreement purported to extend the original lease by granting the additional right of "introducing, injecting, storing and removing gas of any kind." The agreement was to be for a primary term of ten years and so much longer either as gas was being produced, stored, withdrawn, or held in storage by the lessee in the subsurface sands or as oil or gas was found on the land. This agreement also provided for payments of $200 per year per well, quarterly, and in lieu thereof, oil and gas royalties if either was produced and marketed. Several wells were converted to storage use. All quarterly payments were made until November 1972 when appellants refused payment. Appellants had filed suit in July 1971, seeking a declaratory judgment that the 1928 lease was terminated and that the storage agreement was void and if it was not void, that it terminated in 1958. Appellee answered, claiming both agreements were valid, and appellants were estopped by reason of their acceptance of the rents. The lower court gave judgment for appellee. On appeal, the principal question was whether the supplemental gas storage agreement was to be treated as an ordinary contractual lease or as an oil and gas lease. Held: Judgment accordingly. An oil and gas lease is an exploitation of the minerals under the surface of an owner's land. The storage agreement is simply a rental agreement for

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* A motion to certify the record was overruled by the Supreme Court of Ohio, December 7, 1973.

the use of the lessor's land. The supplemental gas storage agreement is not definite and certain beyond its primary term. The term is determined by the will of the lessee and is a tenancy at will. The supplemental gas storage agreement was a valid and subsisting contract which, beyond the primary term, was terminable at the will of the lessors or lessees.

SYLLABUS BY THE COURT

The distinction between an oil and gas lease, and a gas storage agreement is that the former involves the exploitation of minerals under the surface of the owner's land, while the latter is simply a rental agreement for the use of the lessor's land. The former involves expenditures of great sums of money on a gamble that oil or gas will be found, and the law protects the investing discoverer. Gas storage agreements do not have those attendant risks, and do not warrant the extension of the "locator or discoverer's rights" principle. The lessor as well as the lessee may terminate a tenancy at will.

MAHONEY, Judge.

On August 10, 1928, the predecessors in title to land owned by plaintiffs, the appellants herein, situated in section 31 of Green Township, Summit County, executed and delivered to the defendant, East Ohio Gas Co. (an appellee), an oil and gas lease for the primary term of five years, and "so much longer as oil or gas . . . is or are found on said premises in paying quantities in the judgment of the lessee . . ."

The lease gave the East Ohio Gas the right to drill, extract, and operate oil wells, etc., and lay pipe, etc., for a minimum annual rent of $165 ($1 per acre). If a well was drilled and oil found, a "one-eighth" royalty was to be paid, with a greater royalty for greater quantities marketed and used off the premises.

In 1933, prior to the expiration of the primary term of the lease, East Ohio Gas well No. 1312 was drilled, and gas produced. Thereafter, a $200 royalty was paid quarterly. In 1936, East Ohio Gas well No. 1376 was completed, gas was produced, and thereafter a royalty was paid quarterly.

In 1948, the predecessors in title to the plaintiffs executed and delivered to East Ohio Gas a written document labeled "Supplemental Gas Storage Agreement." The agreement was not signed by East Ohio Gas. It recites a beginning date of September 1, 1948, but the notarial acknowledgments are dated September 28, 1948, and December 18, 1948.

This agreement, for a consideration of $1, purports to modify and extend the 1928 lease by granting the additional right of ". . . introducing, injecting, storing and removing gas of any kind, including gas now or at any time hereafter lying under said premises, either through wells now located or hereafter drilled upon said premises or through wells located upon any other premises within the so-called Clinton Sands area . . . [and] to drill as it may elect . . . and to install and maintain . . . such additional equipment and pipe lines . . . as may be necessary . . . ."

The agreement was alleged to be for a primary term of ten years "and so much longer either (1) as gas is being produced, stored, withdrawn, or held in storage by the lessee, in the sub-surface sands . . . or (2) as oil is found on said premises, or gas is found in sub-surface formations . . . in paying quantities in the judgment of lessee . . . ." This agreement also provided for payments of $200 per year per well, payable quarterly, and, in lieu thereof, oil and gas royalties, if oil or gas was produced and marketed.

Wells numbers 1312 and 1376 were "shut in" on August 2, 1948, but not "plugged." They were converted to storage use on August 1, 1949. Thereafter, wells numbers 2164 and 2165 were drilled, in 1960, for storage purposes. In 1965, a settlement was reached and releases were executed

by plaintiffs and East Ohio Gas for damages caused on the premises by East Ohio Gas up to March 25, 1965. In 1971, storage well No. 2547 was drilled.

From and after 1948, every quarterly payment was made on every well until November 2, 1972, when the plaintiffs refused tendered payments. East Ohio Gas has continuously, since 1949, used the wells for the injection, storage and withdrawal of gas produced elsewhere, and transported to plaintiffs' property, or other property in the Clinton Sands area, by pipe and injection into the subterranean sands and caverns.

Plaintiffs commenced this action on July 30, 1971, seeking relief, as follows:

(1) A declaratory judgment that the lease of 1928 was terminated.

(2) A declaratory judgment that the storage agreement was void and, if it was not void, that it terminated on September 1, 1958.

(3) A finding that East Ohio Gas Company's use of the land since that date is a trespass and nuisance, and that the plaintiffs ought to recover damages therefor.

(4) To enjoin the East Ohio Gas Company from further activity on plaintiffs' premises, and order the removal of equipment, etc.

East Ohio Gas answered, asserting the validity of both agreements, and claiming that the plaintiffs are estopped by reason of their acceptance of the rents, and that the company relied, to its detriment, on such acceptance and prior agreements. Its other defenses are: (1) a lack of necessary parties plaintiff; (2) the statute of limitations; (3) and the release executed on March 25, 1965 as to the claimed damages.

The matter was submitted to this court upon the pleadings, interrogatories and answers thereto, exhibits, and a

transcript of proceedings. This transcript, supposedly, was to be an agreed statement of facts, but it contains a maze of opening statements, opinions, some testimony, closing arguments, and the trial judge's opinion that: "I have to honor this supplemental gas storage agreement based on what has been told to this court . . . ."

The plaintiffs orally requested separate findings of fact and conclusions of law. The court, thereafter, found, in addition to the facts stated above, that the first two oil wells were never abandoned, and that, in reliance on the storage agreement, East Ohio Gas drilled three more wells. The court's conclusions of law were that the two agreements are "valid and subsisting agreements conveying an interest in the land . . ." And that the plaintiffs are estopped to deny their validity by reason of their acceptance of payments. A judgment was entered in favor of the defendant. The plaintiffs claim that the judgment is contrary to law and against the manifest weight of the evidence.

The chief questions before us relate to the interpretation that should be placed on the supplemental gas storage agreement proviso, which reads:

> "To have and to hold the said oil and gas lease . . . for a term of ten years, and so much longer . . . as gas is being produced, stored, withdrawn, or held in storage . . . in the sub-surface sands. . . ."
>
> First, is the agreement to be treated as an ordinary contractual lease, or as an oil and gas lease? Second, should the court extend protection to the "locator or discoverer" as it has on occasion in the past?

In the early days of mining and drilling explorations, a body of law developed peculiar to those operations. One of these was a principle called the "locator or discoverer's right." Under this principle, the law protected the locator and discoverer, so that when he expended large sums of money for exploration and drilling, he was afforded protec-

tion against the property owner, the government or third parties for his discoveries by giving him the right to mine or drill, and to produce and market those minerals that he found during his exploration.

This principle found its way into the oil and gas leases and eventually raised reciprocal implied covenants by the lessee. These were the duties to explore, drill, produce and market the product just as any "reasonably prudent operator" would do under the circumstances. The courts did grant forfeitures for failure to operate or develop prudently where there was an express covenant in the lease. This body of law provided that uncertainties in leases were ordinarily resolved in favor of lessors. Thus, the law required the lessee-operator to perform prudently or his "discoverer's rights" would be cut off. Each side benefited as each had a duty, and the royalty of one-eighth was fair to both sides.

East Ohio Gas urges the same circumstances still exist, and that the same principle should be applied to gas storage agreements. It urges the necessity of protecting the large investments of the gas companies, and points to the general public's benefit of having an ample supply of gas for fuel during the winter months.

Let us, therefore, compare the two types of agreements. The oil and gas lease provided for minimum rentals, plus royalties in the event that oil or gas was produced in greater quantities. Oil royalties could rise or fall with production and the value of the dollar. Gas royalties were governed strictly by quantities. However, in the storage agreement, the rental payment of $200 per year per well remained constant, regardless of the quantity of gas stored.

The oil and gas lease, which provides "for a term of five years *and so much longer as oil or gas . . . [is found] in paying quantities . . .*" is essentially a bilateral contract in which the lessors are required to permit the continued production, but the lessee is required to operate in a prudent manner.

On the other hand, the storage lease is actually unilateral, after the primary term, as the lessors are required to accept the lessee's actions on lessors' premises. The lessee has no obligation to inject and store gas. (Emphasis supplied.)

The bilateral oil and gas lease was enforceable against either party. The lessors could obtain a forfeiture of the lessee's rights, if it failed to operate prudently. In contrast, there is the storage agreement which only the lessee could enforce after the primary term.

The usual oil and gas lease was ordinarily terminable beyond the primary term, when the oil and gas were no longer produced in paying quantities, or by forfeiture by operation of law. It was terminable by contingency or operation of the law and not at the will of either party. However, the storage agreement, in the instant case, could be terminated at any time by the lessee by simply withdrawing all the gas and stopping payments.

The main difference is that an oil and gas lease is an exploitation of the minerals under the surface of an owner's land. The storage agreement is simply a rental agreement for the use of the lessor's land. The former involves expenditures of great sums of money on a gamble that oil or gas would be found, and the law, therefore protects the investing discoverer. In the latter situation, there is no element of risk, as the lessee is well aware of the amount he can store and control his expenditures.

We, therefore, must conclude that the same circumstances and conditions do not exist as to warrant the extension of the oil and gas "locator or discoverer's rights" principle to gas storage agreements. Does the public necessity for an ample supply of gas justify the extension of the principle? We do not think so. The legislature has recognized the public necessity by granting the right of eminent domain to gas companies for storage purposes under certain conditions. This prevents the deprivation of property without due

process of law. If we were to force this lease upon the lessors for that reason alone, it would be an appropriation of property without due process of law.

The question then becomes: What kind of a lease is the supplemental gas storage agreement in this case? We use the term "lease" loosely, because oil and gas agreements have been characterized as leases, licenses, corporeal hereditaments, rights, easements, and/or interests in real estate.

We note that this lease, beyond its primary term, is not definite and certain. The contingency controlling the term is regulated exclusively by the lessee, East Ohio Gas Company. The term, therefore, is determined by the will of the lessee, who is under no obligation to inject and store gas.

Under the common law, a tenancy at the will of one party is also a tenancy at the will of the other. This rule has been recognized by the Supreme Court in Brown v. Fowler, 65 Ohio St. 507, at 523, 63 N.E. 76. This common law doctrine has been approved by the majority of courts in this country. See: annotation, 137 A.L.R. 366, Subdivision III, "Option of One Party to Terminate Lease"; 51C C.J.S. Landlord and Tenant, § 167, p. 473, and 32 American Jurisprudence 81, Landlord and Tenant, Sections 66 and 67. The rule has also been followed by this court in the case of Freedline v. Cielensky, 115 Ohio App. 138, 184 N.E.2d 433.

We are aware that the court, in Brown v. Fowler, supra, did not find a tenancy at will. There, the court treated a surrender clause as a condition subsequent during the primary term, and simply terminated the tenancy for failure to drill and develop within the primary term of two years.

Moreover, we are cognizant of the view held by the text writers (such as 1 Tiffany, Real Property, Section 159 [3d ed. 1939], and 2 Summers, Oil and Gas, Section 235 [1959]), that American courts have been misled by a dictum in Lord Coke's commentary on Littleton (Co.Litt. 55A). However,

the fact remains that the principle was adopted by Kent and Blackstone, and is now followed by the majority of American courts. This "error" in Coke's commentary was set forth in the case of Gas Co. v. Eckert, 70 Ohio St. 127, 71 N.E. 281.

The case of Gas Co. v. Eckert is readily distinguishable from the case at issue, as well as other oil and gas leases. It involved what was generally referred to, around the turn of the century, as a "no-term" lease. Courts generally read into such a lease an implied condition that the developer could not indefinitely postpone the development or drilling by the payment of annual delay rents. (2 Summers, supra at Section 10.) We think it fair to assume that the court in Gas Co. v. Eckert found that the developer had not unreasonably delayed exploration and it, therefore, denied the lessor's request to cancel the lease.

Additionally, as we have already indicated, there is no reason to treat the storage agreement as an oil and gas lease. It does not involve any grant of oil, gas, or minerals. It is simply a rental of land. As such, there is no reason to treat it other than as an ordinary contractual lease. It is at the will of the lessee and, therefore, it is likewise at the will of the lessors.

East Ohio Gas argues that even if it is considered a tenancy at will, the plaintiffs should be estopped to terminate the tenancy, since the court found that East Ohio Gas, in reliance on the agreement, constructed three wells and laid and installed equipment. However, an examination of the proceedings fails to disclose sufficient facts, as a matter of law, from which the court could find that an estoppel should be imposed, and, thus, the trial court erred. (We note that East Ohio Gas concurs with the finding of this court regarding estoppel.)

We find, from the record, that the trial court also erred in finding against the plaintiffs on the questions relating to damage and trespass. While the release would properly ex-

clude claims prior to its execution, the plaintiffs (lessors) certainly had the right to offer evidence of damage since that time, as to wells numbers 2164, 2165, and 2547, and, of course, subject to the statute of limitations.

We, therefore, conclude that the supplemental gas storage agreement, executed in 1948, was a valid and subsisting contract which, beyond the primary term, was terminable at the will of the lessors or lessee, and that it was terminated by the lessors' refusal to accept rents as of November 1, 1972, unless the lessors should be estopped from asserting that right. This question should be determined by a trial on the merits of lessee's defense of estoppel.

Judgment accordingly.

Concur: BRENNEMAN, P. J., and VICTOR, J.

DISCUSSION NOTES

Storage of Gas: Distinction Between Oil and Gas Lease and Gas Storage Agreement.

The Court is treating the supplemental gas storage agreement as a mere rental agreement which apparently does not attain the stature of an oil and gas lease. See McGinnis, "Some Legal Problems in Underground Gas Storage," 17th Oil & Gas Inst. 23 (Sw. Legal Fdn. 1966). See also, Ozier v. Central Illinois Public Service Co., 297 N.E. 2d 21, 46 O&GR 1 (Ill. App. 1973); and related case at 54 O&GR 501.

A. B. C.

HUMBLE OIL AND REFINING COMPANY, Petitioner,

v.

Wesley WEST et al., Respondents.

No. B-4132.

Supreme Court of Texas.

April 24, 1974.

Rehearing Denied June 5, 1974.

The owners of a royalty interest in gas brought suit to enjoin the oil company to which they had conveyed the gas field from using it as a storage reservoir until all native gas had been produced. Injunctive relief was denied by the 164th District Court, Harris County, Warren P. Cunningham, J., but the Waco Court of Appeals, 10th Supreme Judicial District, 496 S.W.2d 212, reversed and remanded. Writ of error was granted to the oil company. The Supreme Court, Steakley, J., held that where the reservation of the conveyance imposed on the oil company the obligation to pay royalties on all gas "produced and saved," there was a reservation of royalties on native gas in the reservoir, and the oil company's ownership of extraneous gas which it injected into the field for storage was unaffected by such language of reservation. However, where the oil company was responsible for its injection of its extraneous gas into the field and where the oil company was possessed with peculiar knowledge of the gas injection, it was under the burden of establishing aliquot shares of its own and of the owners of the royalty interest with reasonable certainty, and if the oil company failed to sustain such burden, the royalty owners were entitled to royalty on all gas produced, native or injected.

Judgment of Court of Civil Appeals reversed and cause remanded to trial court.

1. Mines and Minerals ⇦47

Owner with fee simple interest owns not only surface and mineral estates but also matrix of underlying earth, i. e., reservoir storage space, subject only to reserved right of royalty owners to payment of royalties on minerals that are produced and saved.

2. Mines and Minerals ⇦47

In conciliating conflicts between owners of surface and of mineral rights, reasonable accommodation is required between them.

3. Mines and Minerals ⇦55(6)

Where oil company had fee interest in gas field subject only to royalty interests, and where but for injection of extraneous gas the storage capacity of field would be destroyed by encroachment of water and where field was particularly suitable for storage of extraneous gas, reasonable balancing of interests and public interest in conservation of natural resource required that oil company be allowed to use field for such storage.

4. Mines and Minerals ⇦55(5)

Where oil company owned natural gas as personal property, gas remained property of oil company following injection of gas into field to which oil company had fee interest, though such fee interest was subject to royalty interests.

5. Mines and Minerals ⇦55(5)

Where reservation of conveyance to oil company imposed on oil company obligation to pay royalties on all gas "produced and saved," there was reservation of royalties on native gas in gas field reservoir, and oil company's ownership of extraneous gas which is injected into reservoir for storage was unaffected by such language of reservation.

See publication Words and Phrases for other judicial constructions and definitions.

6. Confusion of Goods ⇦3

Generally, confusion of goods theory attaches only when commingled goods of different parties are so confused that prop-

erty of each cannot be distinguished; where mixture is homogeneous, goods being similar in nature and value, and if portion of each may be properly shown, each party may claim his aliquot share of the mass.

7. Confusion of Goods ⇐12, 13

Burden is upon one commingling goods to properly identify aliquot share of each owner in homogeneous mixture, and if goods are so confused as to render mixture incapable of proper division according to pre-existing rights of parties, loss must fall on one who occasioned the mixture.

8. Confusion of Goods ⇐12, 13

Where oil company was responsible for its injection of its extraneous gas into gas field which it owned in fee subject to royalties on native gas in the reservoir, and where oil company was possessed with peculiar knowledge of the gas injection, it was under burden of establishing its own aliquot shares and those of owners of royalty interest with reasonable certainty, and if oil company failed to sustain such burden, royalty owners were entitled, under confusion of goods theory, to royalty on all gas produced, native or injected.

McGinnis, Lochridge & Kilgore, Robert C. McGinnis, Austin, Walter B. Morgan, Dillard W. Baker, Talbert J. Fox and J. Lamar Hart, Houston, for petitioner.

Stayton, Maloney, Black, Hearne & Babb, John W. Stayton, Austin, for respondents.

STEAKLEY, Justice.

This is a suit by West, et al., Respondents, who are royalty owners, for injunction and, in the alternative, for declaratory judgment. The action is brought against Humble Oil and Refining Company, Petitioner, the fee owner of the gas field and mineral rights, subject to the royalty interests. The problem arises from Humble's action of injecting extraneous gas into the underground reservoir, for purposes of storage, prior to production of all the recoverable native gas. The history of the matter will be recited in some detail.

The Wests, by fee simple conveyance dated December 28, 1938, deeded all lands owned by them in the West Clear Lake (Frio) gas field in Harris County, Texas, to Humble. Each conveyance recited that the Wests "except from this conveyance and retain unto themselves, their heirs, successors and assigns, those certain royalties on oil, gas and other minerals which may be produced and saved from the lands hereby conveyed." Insofar as gas is concerned, the retained royalty was described as "a royalty equal to the market value at the well of one-sixth (1/6) of the dry gas so sold or used; provided that on such dry gas sold at the wells the royalties shall be one-sixth (1/6) of the amount realized from such sale."

The West Clear Lake Field, a water drive field, has been producing gas since 1938. In 1969, Humble concluded that the reservoir was approaching depletion and that the injection of extraneous gas was necessary to preserve the reservoir from destruction by water encroachment. In response to Humble's application, and after a hearing on September 23, 1969, at which the Wests appeared in opposition, the Railroad Commission of Texas, under date of January 20, 1970, authorized use of the reservoir for the storage of gas. There was no appeal from this order.

On March 26, 1970, the Wests instituted this suit against Humble for permanent injunction, i. e., "that upon final trial hereof defendant be enjoined from using the Clear Lake, W. (Frio) Field, Harris County, Texas, as a gas storage reservoir until all the native gas therein has been produced." In the alternative, the Wests sought a "declaratory judgment decreeing that if defendant uses said reservoir as a gas storage reservoir, defendant must account to plaintiffs for their royalty inter-

ests in all gas produced from said reservoir irrespective of whether said produced gas be native gas or stored gas."

Humble commenced the injection of extraneous gas on September 1, 1970. In response to the Wests' suit, Humble's first amended answer, filed June 2, 1972, alleged that before commencement of the gas storage project, it had produced 89% of the recoverable gas reserves in the reservoir and that production of the remaining recoverable gas would have resulted in destruction of the reservoir's gas storage capability. Further, in answer, Humble committed itself to continue to pay royalties on production from the reservoir "until, but only until, the total volume of all gas so produced from the particular tract is equal to the volume of gas in place in the reservoir in such tract above the gas-water contact as of January 1, 1969, terminating all royalty payments as to such tract in such reservoir when such production has occurred."

Under date of September 18, 1972, and after a trial before the Court, judgment was entered denying the prayer of the Wests for permanent injunction but decreeing "[t]hat defendant must account to plaintiffs for their royalty interests in all gas produced from the tracts in which they own royalty interests in the Clear Lake W. (Frio) Field, Harris County, Texas, irrespective of whether said produced gas be native gas or stored gas."

Upon appeal by all parties, the Court of Civil Appeals reversed the judgment of the trial court and remanded the cause, with instructions "to enter a permanent injunction restraining defendant from further injecting the field and using same as a gas storage reservoir until all native gas has been produced therefrom." 496 S.W.2d 212. Writ of error was granted at the instance of Humble. We reverse and remand.

The initial and underlying problem to be solved is whether, under the contract between the parties and the existing circumstances, the Wests are entitled to enjoin Humble from injecting gas in the reservoir until all recoverable native gas has been produced. If not, we must then determine the rights of the parties under the Wests' alternative prayer that Humble account to them in royalty payments on all gas produced from the reservoir, whether native or stored.

As to the first issue, the Wests argue that prior writings of this Court establish principles which entitle them to injunctive relief. They cite Sheffield v. Hogg, 124 Tex. 290, 77 S.W.2d 1021 (1934), where this Court determined that in the context of property taxation, a royalty interest, whether payable in money or in kind, should be denominated an interest in land. *See* also Brown v. Smith, 141 Tex. 425, 174 S.W.2d 43 (1943); Watkins v. Slaughter, 144 Tex. 179, 189 S.W.2d 699 (1945). They emphasize that one in the position of Humble is required not only to produce and market gas from the tract found in paying quantities, W. T. Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 19 S.W.2d 27 (1929); Knight v. Chicago Corp., 144 Tex. 98, 188 S.W.2d 564 (1945), but also to accurately measure such production and sales in order to accurately account to the royalty owner. French v. George, 139 S.W.2d 566 (Tex.Civ.App.—Amarillo 1942, writ ref'd); Brown v. Smith, *supra*. Thus, the Wests contend that the proprietary and contractual rights arising from their royalty interest translate into certain absolute rights in the native gas now in the reservoir, under which they are entitled to total production of all native gas prior to utilization of the reservoir for storage of extraneous gas. Otherwise stated, it is their position that the nature of their royalty interest, coupled with their right to royalties on all native gas produced at market demand and sold at prevailing market prices, precludes any right in Humble to commingle gas in the reservoir, and that Humble's actions so impaired the rights of the Wests as to entitle them to enjoin further commingling. Additionally, they argue by analogy the applicability of the

principle of awarding injunctive relief when one intentionally appropriates another's property interest by encroachment, Bickler v. Bickler, 403 S.W.2d 354 (Tex. 1966), or when one is acting in violation of building restrictions. Welton v. 40 East Oak Street Building Corp., 70 F.2d 377 (7th Cir. 1934) cert. denied 293 U.S. 590, 55 S.Ct. 105, 79 L.Ed. 685 (1934).

[1] The nature of the respective property interests of the parties should first be noted. As stated, the Wests conveyed fee title to the lands but reserved "royalties on oil, gas and other minerals which may be produced and saved from the lands hereby conveyed," payable in money. Humble, on the other hand, owns the lands in fee simple, and this includes not only the surface and mineral estates, but also the matrix of the underlying earth, i. e., the reservoir storage space, subject only to the reserved right of the Wests to the payment of royalties on minerals that are produced and saved. *See* Emeny v. United States, 412 F.2d 1319, 188 Ct.Cl. 1024 (1969), where it was said that the surface of the leased lands remaining as the property of the respective landowners included the geological structures beneath the surface, together with any such structure that might be suitable for the underground storage of extraneous gas produced elsewhere. Indeed, the Wests do not challenge Humble's ownership of the reservoir and its right to utilize it for storage; instead, they direct their argument to the time at which, they say, the storage right accrues. They argue, in essence, that the exercise of such right by Humble is postponed by the royalty reservation until total depletion of all recoverable native gas from the reservoir.

[2] It is manifest that the interests of the parties have come into conflict and are not fully compatible. Thus, we have again the recurring problem of adjusting correlative rights. The factual context is unique and there is no directly controlling precedent; however, this Court has led the way in conciliating conflicts between owners of the surface and of the mineral rights, and in requiring reasonable accommodations between them. *See* Robinson v. Robbins Petroleum Corp., 501 S.W.2d 865 (Tex.1973); Sun Oil Co. v. Whitaker, 483 S.W.2d 808 (Tex.1972); Acker v. Guinn, 464 S.W.2d 348 (Tex.1971); Getty Oil Co. v. Jones, 470 S.W.2d 618 (Tex.1971); Humble Oil & Refining Co. v. Williams, 420 S.W.2d 133 (Tex.1967); Railroad Commission v. Manziel, 361 S.W.2d 560 (Tex.1962); Brown v. Lundell, 162 Tex. 84, 344 S.W.2d 863 (1961); Warren Petroleum Corp. v. Monzingo, 157 Tex. 479, 304 S.W.2d 362 (1957); Warren Petroleum Corp. v. Martin, 153 Tex. 465, 271 S.W.2d 410 (1954). These writings and the principles which they establish are instructive here.

In Acker v. Guinn, *supra*, we affirmed that it is not ordinarily contemplated in mineral leases or deeds that the utility of the surface will be destroyed or substantially impaired by the uses made of the surface for the production of minerals.

In Getty Oil Co. v. Jones, *supra*, a dispute arose between the surface owner and the oil and gas lessee over rights to exclusive use of air space above the surface area occupied by oil pumping units required for production of the minerals. This Court was faced with seemingly irreconcilable positions; the surface owner was unable to operate his automatic irrigation sprinkler system, and hence unable to fully utilize his surface rights because of obstacles in the form of the lessee's existing pumping units. In addressing the conflict between the parties, we recognized the well settled principle that the oil and gas estate is dominant over the surface estate; further, that the lessee has a right to use as much of the premises as necessary to produce and remove the minerals. However, we also reiterated that while the rights accruing from the dominant estate are well established, they are not absolute. The lessee is required to exercise his rights with due regard for the rights of the surface owner; and we held that the lessee

was subject to the rules of reasonable usage with respect to an existing use of the surface. Thus, the factual context, coupled with the public policy of developing resources and promoting productive agricultural use, required an accommodation between the rights of the dominant and servient estates.

A further example of the balancing of competing interests in the oil and gas context is found in Railroad Commission v. Manziel, *supra*. Here, this Court was faced with a question of whether an enjoinable "trespass" occurred when an adjoining mineral estate was invaded by salt water injected pursuant to secondary recovery projects authorized by the Railroad Commission. While the issue arose in the context of the validity of the Railroad Commission order, we emphasized that application of orthodox rules and principles may not be appropriate under such circumstances; we spoke of balancing the interests of society and the interests of the oil and gas industry as a whole against the interest of the individual operator.

In Woodson Oil Co. v. Pruett, 298 S.W. 2d 856 (Tex.Civ.App.—San Antonio 1957, writ ref'd n. r. e.), a lease was lost as the result of non-production. The lease specifically provided that Woodson had the right to remove all property and fixtures, including the casing, and Woodson sought an injunction to enforce this contractual right against a producing well. While fully recognizing Woodson's explicit rights under the lease, the court determined that the destruction of the well and the waste of natural resources which would result from such removal were sufficient reason to deny the equitable relief.

[3] In the case at hand, the interests of the parties are evident; the Wests possess a royalty interest in native gas produced from the West Clear Lake Field, while Humble owns fee title to the lands, including the subsurface reservoir. In conciliating the interests asserted by each party, we must necessarily consider the unusual nature of the subsurface reservoir and the West Clear Lake gas fields. The unique geologic and geographic characteristics of the reservoir are shown by the record; further, the evidence establishes that since this reservoir lies in a water drive field, salt water encroachment reduces the storage capability as native gas is produced. Absent injection of extraneous gas, production of native gas to depletion will result in a "watering out" or total destruction of the storage capability of the reservoir. As a consequence, injunction against the injection of extraneous gas would render illusory Humble's ownership of the storage rights in the reservoir.

Moreover, our ruling will determine the continued existence of an important natural resource. The record reveals two significant features of the reservoir which vitally affect the public interest. First, the reservoir is well-suited as a "peaking" facility which can handle the seasonal fluctuations and rapidly increasing energy demands for the greater Houston area; secondly, it is a strategically located "emergency" facility, capable of providing a readily deliverable supply of gas at times when accidents, natural disasters or mechanical failures make continued delivery through normal channels impossible.

Under these circumstances, the accepted principles of accommodation that have ruled the resolution of like conflicts are determinative, and we hold that the Court of Civil Appeals erred in ordering the injunctive relief sought by the Wests.

The denial of injunctive relief requires a determination of whether the contractual obligation of Humble is to account in royalties on the production of all gas from the reservoir, "irrespective of whether said produced gas be native or stored gas," as decreed by the trial court.

The Wests argue that this "pay forever" judgment is compelled by the language of the original conveyance. The conveyance stated that the Wests "except from this conveyance and retain unto themselves

their heirs, successors and assigns, those certain royalties on oil, gas and other minerals which may be produced and saved from the lands hereby conveyed." Thus, the Wests claim that while Humble may be permitted to inject extraneous gas for storage purposes, *all* gas produced and saved from the lands is subject to the Wests' royalty interest. The original conveyance made no distinction between native gas and extraneous or stored gas, and the Wests contend that to hold that Humble is not under obligation to pay royalties on the stored gas "produced and saved" would require a rewriting of the existing instruments of conveyance.

To date, the only Texas case dealing with the issue of ownership of gas stored in a natural reservoir is Lone Star Gas Co. v. Murchison, 353 S.W.2d 870 (Tex.Civ. App.—Dallas 1962, writ ref'd n. r. e.). Lone Star Gas, by various conveyances, acquired wells and leases in the Bacon Lime Field; Lone Star Gas also executed a unit operating agreement by which it acquired the right to inject and store extraneous gas in the Bacon storage reservoir. The Murchison group possessed rights as oil and gas lessees on the Jackson tract, and the southwestern part of the Bacon storage reservoir extended under the Jackson tract. The Murchisons drilled a well into the Bacon storage reservoir and took large quantities of gas therefrom. The question was whether the title and ownership of extraneous gas which Lone Star injected into the reservoir for storage was lost upon production of the commingled gas. The Murchisons urged the court to adopt the reasoning of Hammonds v. Central Kentucky Natural Gas Company, 255 Ky. 685, 75 S.W.2d 204 (1934); when faced with a similar fact situation, the Kentucky court determined that the doctrine of animals ferae naturae was applicable. Thus, once extraneous gas which was "turned loose" in the earth wandered to another's land, the party injecting the stored gas ceased to be the exclusive owner of gas; the gas became a mineral ferae naturae.

[4] The Court of Civil Appeals in *Murchison* rejected the doctrine established in *Hammonds* and embraced the language of White v. New York State Natural Gas Corp. et al, 190 F.Supp. 342 (W.D.Pa. 1960), where it was stated that "once severed from the realty, gas and oil, like other minerals, become personal property . . . title to natural gas once having been reduced to possession is not lost by the injection of such gas into a natural reservoir for storage purposes." Therefore, under *Murchison*, the extraneous gas injected for storage by Humble having assumed the character of personal property, remained its property. *See* also Chaffin v. Hall, 210 S.W.2d 191 (Tex.Civ.App.—Eastland 1948, writ ref'd n. r. e.); Stephens v. Stephens, 292 S.W. 290 (Tex.Civ.App.—Amarillo 1927, writ dism'd).

[5] The Wests assert, however, that since they possess a perpetual royalty on the gas produced from the field, their royalty interest "expires with the end of time." Thus, they argue that the contractual relationship of the parties, i. e., the obligation to pay royalty on all gas produced and saved, becomes the controlling distinction between the instant case and *Murchison*. In our view, this is not a tenable distinction but one which if adopted would implicitly recognize the doctrine of minerals ferae naturae which was rejected in *Murchison*. In accord with *Murchison*, Humble's ownership of the gas as personal property is not altered either upon injection of the gas into the reservoir or upon later production of the gas. The language of the conveyance does no more than reserve the royalty interest in the native gas in the reservoir, and Humble's ownership of the extraneous gas is unaffected thereby.

An alternative basis to be considered is whether the trial court judgment may be sustained on a confusion of goods theory. Under *Murchison*, as noted, the extraneous gas is the personal property of Humble. However, by injecting this extraneous gas

into the reservoir prior to production of all native gas, Humble has commingled extraneous gas, in which Humble has an exclusive property interest, and native gas, in which the Wests have a royalty interest. The question thus becomes one of determining whether Humble's intentional "confusion" of the two bodies of gas should result in the forfeiture of its exclusive rights to the extraneous gas. If such a forfeiture is proper, the Wests would be entitled to a royalty on all gas produced, consistent with the trial court judgment.

[6-8] As a general rule, the confusion of goods theory attaches only when the commingled goods of different parties are so confused that the property of each cannot be distinguished. Where the mixture is homogeneous, the goods being similar in nature and value, and if the portion of each may be properly shown, each party may claim his aliquot share of the mass. Belcher v. Cassidy Bros. Live Stock Commission Co., 26 Tex.Civ.App. 60, 62 S.W. 924 (Tex.Civ.App.—1901, writ ref'd); Farrow v. Farrow, 238 S.W.2d 255 (Tex. Civ.App.—Austin 1951, no writ); 1 Am. Jur.2d Accession and Confusion, § 21 (1962); 15A C.J.S. Confusion of Goods § 7 (1967). Additionally, the burden is on the one commingling the goods to properly identify the aliquot share of each owner; thus, if goods are so confused as to render the mixture incapable of proper division according to the pre-existing rights of the parties, the loss must fall on the one who occasioned the mixture. 15A C.J.S. Confusion of Goods §§ 7, 12 (1967); 1 Am.Jur. 2d Accession and Confusion, §§ 18, 24 (1962). Stated differently, since Humble is responsible for, and is possessed with peculiar knowledge of the gas injection, it is under the burden of establishing the aliquot shares with reasonable certainty. *See* Eaton v. Husted, 141 Tex. 349, 172 S.W.2d 493 (1943); *Cf.* Mooers v. Richardson Petroleum Co., 146 Tex. 174, 204 S.W.2d 606 (1947); Ortiz Oil Co. v. Luttes, 141 S.W. 2d 1050 (Tex.Civ.App.—1940, writ dism'd); 1 W. Summers, The Law of Oil and Gas § 27 (1954).

Humble sought to discharge this burden by offering expert opinion evidence in estimation of the volume of native gas as of January 1, 1969; its commitment in the trial court was to continue the payment of royalties to the Wests on the basis of this proof until production of the commingled gas equaled the volume of the gas in place at such time. As to this, the Wests contend that the obligation of Humble to account for their royalty interests may not rest upon expert opinion evidence and that, at the least, upon its election to utilize the reservoir for storage and hence to commingle native and extraneous gas, Humble came under the obligation of paying royalties on all gas thereafter produced from the reservoir.

The counter position of Humble is that the opinion testimony of the geology and engineering witnesses is reasonably certain; that their testimony was based upon more than acceptable well control for mapping the reservoir, and that there existed sufficient data upon which to compute reservoir pressure, reservoir temperature, gas formation volume factor, reservoir porosity and permeability and connate water saturation. Thus, Humble asserts that the Wests' aliquot share of the gas in the reservoir prior to injection of the extraneous gas is subject to a reasonable estimate and that the expert testimony sufficiently established the volume of the reserves.

In the context of their asserted right to equitable relief, the Wests emphasize, on the other hand, that Warnack, Humble's geologist witness, admitted that a certain "judgment or opinion decision" had to be made in calculating the reservoir size. They stress that the witness acknowledged that wide discrepancies may exist in determining the size of a reservoir and insist that his calculations were based upon limited and unacceptable information. Also, they note that Whitson, the petroleum engineer called to testify by Humble, made critical calculations of porosity and permeability by means of mathematical averages; further, that experts agree that the limits of a reservoir are difficult of exact determination.

As we have indicated, it is our view that the act of commingling native and extraneous gas did not impose upon Humble the obligation of paying royalties on all gas thereafter produced from the reservoir, if the evidence establishes with reasonable certainty the volume of gas reserves upon which the Wests would have been entitled to royalties, absent injection of extraneous gas. The burden of this showing devolves upon Humble after proof by the Wests of their royalty interests, together with proof of Humble's commingling of extraneous and native gas. The threshold question for determination is whether the requisite computation of reserves is capable of establishment with reasonable certainty; and, if so, the further question to be resolved is whether the burden defined above is discharged by Humble under the evidence. We have concluded that the cause should be generally remanded to the trial court for determination of these issues at the trial level, as well as for consideration of any other issues the parties may raise in the light of our rulings.

The judgment of the Court of Civil Appeals is reversed and the cause remanded to the trial court for further proceedings in accordance with this opinion.

Jacinto Ramirez ZAMORA, Appellant,

v.

The STATE of Texas, Appellee.

No. 48066.

Court of Criminal Appeals of Texas.

April 24, 1974.

Rehearing Denied May 22, 1974.

Defendant was convicted in the Criminal District Court, Dallas County, Jerome Chamberlain, J., for possession of marihuana, and he appealed. The Court of Criminal Appeals, Davis, C., held that evidence sustained conviction, and that refusal to grant requested charge of entrapment was not error.

Affirmed.

1. Drugs and Narcotics ⇨117

Evidence sustained conviction of defendant, who had secured and driven vehicle in trunk of which a large quantity of marihuana was found, for possession of marihuana.

2. Drugs and Narcotics ⇨117

In proving possession in narcotics cases, facts and circumstances surrounding a search or an arrest may be shown to prove that accused and other persons acted together in jointly possessing a narcotic.

3. Criminal Law ⇨1038.1(6), 1038.4

Defendant's contentions that trial court erred in failing to charge jury on circumstantial evidence and that in order to convict jury must find that defendant had knowledge that contraband was in automobile and that it was marihuana were not before the Court of Criminal Appeals for consideration, where neither written objection to trial court's charge nor a written request for the charge desired was filed with the trial court. Vernon's Ann. C.C.P. arts. 36.14, 36.15.

4. Criminal Law ⇨1038.1(6), 1038.4

Objections and requested charges dictated to court reporter are not sufficient to preserve error.

5. Criminal Law ⇨37(1)

Defense of entrapment is not available to a defendant who denies that he committed the offense charged.

6. Criminal Law ⇨772(6)

Where defendant's defense was based on lack of knowledge that there was contraband in vehicle in which he was a passenger, refusal to charge on defense of entrapment was not error.

Act. The Secretary *may* (as opposed to *shall* or *must*) ratify and approve amendments to the tribal constitution and bylaws. Such discretionary action is not subject to review. See Hamel v. Nelson, 226 F.Supp. 96 (N.D.Cal.1963) and cases cited therein.

[10] Lastly, plaintiffs assert that defendants' actions have deprived plaintiffs of rights guaranteed by the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States. This argument ignores one of the most basic tenets of American constitutional law. The guarantees of the Due Process Clause relate solely to action by a state government, Rice v. Sioux City Memorial Park Cemetery, 349 U.S. 70, 75 S.Ct. 614, 99 L.Ed. 897 (1955); Watkins v. Oaklawn Jockey Club, 183 F.2d 440 (8th Cir. 1950), and have no application to actions of Indian tribes, acting as such. See Barta v. Oglala Sioux Tribe of Pine Ridge Res., 259 F.2d 553 (8th Cir. 1958), cert. denied, 358 U.S. 932, 79 S.Ct. 320, 3 L.Ed.2d 304 (1959). Here, neither the State of Minnesota nor any other state acted in any wise to affect plaintiffs. All plaintiffs' complaints are directed toward the Minnesota Chippewa Tribe, a federal corporation, and the agents of the United States Department of the Interior.

[11] Similar reasoning precludes granting plaintiffs relief under the Fifth Amendment to the Constitution of the United States. The Fifth Amendment imposes restraints only on the federal government. Koch v. Zuieback, 316 F.2d 1 (9th Cir. 1963).

[12] It has long been established that Indian tribes, while engaged in the processes of local government, are not subject to the Fifth Amendment. Talton v. Mayes, 163 U.S. 376, 16 S.Ct. 986, 41 L. Ed. 196 (1896); Martinez v. Southern Ute Tribe, supra. The principal action complained of in the instant case was the tribal council's compilation of a tribal voting list in preparation for an upcoming referendum to amend the tribal constitution and bylaws. We can think of no better example of a tribe's local governmental procedure than that of regulating a tribal election amending the tribe's constitution and bylaws, the very framework of the local government. Cf Martinez v. Southern Ute Tribe, 151 F.Supp. 476 (D.C.Col.1957), aff'd., 249 F.2d 915 (10th Cir. 1957), cert. denied, 356 U.S. 960, 78 S.Ct. 998, 2 L.Ed.2d 1067 (1958). But cf. Colliflower v. Garland, 342 F.2d 369 (9th Cir. 1965).

Affirmed.

Elizabeth Jane BEZZI, E. M. Woody, Marie Woody, M. Cliff West, Robert L. Gerry, Jr., individually and as Trustee of the Nancy L. Gerry Trust, and Gerry Brothers & Co., a limited partnership, Appellants,

v.

F. M. HOCKER, individually, W. E. Hocker, Jr., individually, Shell Oil Company, a corporation, Noel Jones, F. M. Hocker and Walter E. Hocker, Trustees, Appellees.

No. 8388.

United States Court of Appeals
Tenth Circuit.
Dec. 27, 1966.

Action to recover proportionate share of proceeds from sale of gas produced by unit operator. The United States District Court for the Western District of Oklahoma, Luther Bohanon, J., entered judgment adverse to plaintiffs who appealed. The Court of Appeals, Pickett, Circuit Judge, held that, under Oklahoma law, whatever title owners of mineral interest in tract had to residue gas prior to date their mineral interest terminated, it was lost when gas was reinjected into common source of supply and commingled with virgin gas exist-

ing there and it became subject to law of capture.

Affirmed.

1. Mines and Minerals ⇐47

Owner of land has qualified title to oil and gas in and under his land with exclusive right to produce it, but has no absolute title thereto.

2. Mines and Minerals ⇐47

Oil and gas are mobile and fugacious, and if they escape to other lands or come under another's control, whatever title original owner had is lost.

3. Mines and Minerals ⇐47

Oil and gas belong to person who legally obtains control and possession.

4. Mines and Minerals ⇐47

Under Oklahoma law, whatever title owner of mineral interest in tract had to residue gas prior to date their mineral interest terminated, it was lost when gas was reinjected into common source of supply and commingled with virgin gas existing there and it became subject to law of capture.

5. Courts ⇐406.2

In absence of controlling decisions, Court of Appeals will accept determination by federal district court of applicable state law unless convinced to the contrary.

Barth P. Walker, of Walker & Watson, Oklahoma City, Okl., for appellants.

V. P. Crowe, of Crowe, Boxley, Dunlevy, Thweatt, Swinford & Johnson, Oklahoma City, Okl. (Andrew M. Coats, Oklahoma City, Okl., with him on the brief), for appellees.

Before PICKETT, LEWIS and HICKEY, Circuit Judges.

PICKETT, Circuit Judge.

Elizabeth Jane Bezzi, one of the appellants, brought this action to recover her proportionate share of the proceeds from the sale of gas produced by the unit operator from the Elk City Hoxbar Sand Conglomerate Unit subsequent to January 11, 1961.[1] Appellants owned a mineral interest in a 40 acre tract of land within the unit, which terminated on January 11, 1961. Their claim arises out of the sale of gas which was produced during the reservation period but reinjected into unit wells for conservation purposes and alleged to have been recovered and sold subsequent to the expiration of that period.[2] Bezzi alleges that the title to the residue gas remained in those having an interest in the unit, although such gas was reinjected into the wells for cycling, repressuring, pressure maintenance, and other unit operations, as authorized by the approved plan of unitization. In denying relief to appellants, the trial court held that when the residue gas was reinjected into its natural environment and the common source of supply, and the gas, being mobile and fugacious, it then became subject to the Oklahoma law of capture.

The material facts are not in dispute. On January 11, 1941 Bezzi joined in a warranty deed conveying certain tracts of land to appellees, F. M. Hocker and W. E. Hocker, Jr. This deed reserved to the grantors for a period of 20 years, an undivided one-half interest in the oil and gas underlying the land. On March 24, 1945, oil and gas leases covering this property were executed. These leases were thereafter assigned to appellee Shell Oil Company, and are now in full force and effect. The lessors were to receive a 1/8 royalty from all oil and gas produced and sold during the period, with options not here important. Oil and gas was discovered in Hoxbar Sands underlying the leased lands.

1. The other appellants were permitted to intervene and adopt the allegations of the amended complaint filed by Bezzi.

2. Before the gas was reinjected, it was processed for the removal of liquifiable hydrocarbons, principally propane and butanes. After the processing, the gas is referred to as "residue gas."

On October 26, 1950, the Oklahoma Corporation Commission approved the creation of the Elk City Hoxbar Sand Conglomerate Unit and made all oil and gas production from the unit area subject to the plan of unitization. Appellee Shell Oil Company was designated operator of the unit, subject to the direction of an operating committee.[3]

When Shell began operation of the unit, plant facilities were constructed to process the natural gas produced therefrom for the removal of liquifiable hydrocarbons, which were then sold and the proceeds distributed pursuant to the plan. As authorized by the unit plan, the residue gas was returned to the original structure reservoir, where it commingled with and became part of the virgin gas remaining in the common source of supply. When gas of any kind is used for conservation purposes, the plan provides that no royalties or production payments are required or payable.[4]

After the term of Bezzi's reservation expired on January 11, 1961, the unit operator produced, processed and sold gas, a portion of which was believed to be reinjected gas commingled with the virgin gas in the reservoir. It is this gas that Bezzi contends she had title to when it was originally produced; that such title was not lost by the reinjection procedure; and that she was entitled to be paid therefor although the gas was sold after the expiration of her reserved mineral interests. The trial court held:

"The gas injected into the common source of supply was free to move and migrate to any point in the common source of supply, and the Unit Operator had no control over the gas so injected into the reservoir. When the gas was reinjected it became mobile and fugacious and was returned to its wild state in the reservoir. The Unit Operator in a sense had control, or substantial control and possession, over the reinjected gas prior to its reinjection. The Unit Operator, however, had no control or possession over the reinjected gas after it re-entered the reservoir than it had over the virgin gas originally in the reservoir. When the residue gas was reinjected into the reservoir, plaintiff and intervenors had no right, title, or ownership therein, and such gas thereafter became subject to the law of capture."

[1–3] The Oklahoma courts have not considered the precise question presented here. It has been held, however, that the owner of land has a qualified title to the oil and gas in and under his land with the exclusive right to produce it, but has no absolute title thereto. Rich v. Doneghey, 71 Okl. 204, 177 P. 86, 3 A.L.R. 352. It is recognized that oil and gas are mobile and fugacious, and if it escapes to other lands or comes under another's control, whatever title the original owner had, is lost. It belongs to the person who legally obtains control and possession of it. Carter Oil Co. v. State, 205 Okl. 541, 240 P.2d 787; Magnolia Petroleum Co. v. Ball, 203 Okl. 514, 223 P.2d 136; Wright v. Carter Oil Co., 97 Okl. 46, 223 P. 835. See, also, United States v. Stanolind Crude Oil Purchasing Co., 10 Cir., 113 F.2d 194.

3. When the unit operation became effective, it included eighty-one 40 acre tracts, including the one which is the subject of this action. By subsequent additions, it was enlarged to include 295 such units at the time of trial.

4. Authority for the unit operator to so utilize the residue gas for the development and operation of the unit, and fixing the rights of interested partes to payment therefor, is found in Section VII of the plan, where it is provided:

"The unit operator shall have the right to take and utilize or use so much of the unit production as may be necessary or desirable in the development and operation of the unit area, including but without being limited to the use of gas, including residue gas, for cycling, repressuring, pressure maintenance or other operations under this plan of unitization. No royalties, overriding royalties, production payments or other payments shall be required or payable upon or with respect to the portion of the unit production so taken and utilized or used, or that which is unavoidably lost."

[4] In determining that title to the reinjected gas was lost because of its fugacious nature and that the gas then became subject to the law of capture, the trial court relied upon West Edmond Salt Water Disposal Ass'n v. Rosecrans, 204 Okl. 9, 226 P.2d 965, appeal dismissed 340 U.S. 924, 71 S.Ct. 500, 95 L.Ed. 667. That case involved the liability of one who injected into underground strata of land, salt water, which migrated, or percolated, beyond the boundaries of the land where injected. While the Supreme Court of Oklahoma was not presented with the precise question here, it did liken salt water to oil, gas, and other fugacious minerals which are subject to the law of capture. The court considered the contention that title to the salt water remained in those who injected it into a well where it commingled with salt water already present and then migrated to plaintiff's land, and, at page 970, said:

"Under all the authorities we have been able to find upon the subject, the assumption that the salt water remained the property of defendants after it permeated or penetrated into the Hoover-Tonkawa formation underlying the land of plaintiffs is incorrect. In Willis' Revision of Thornton on the Law of Oil and Gas, Vol. 1, p. 78, section 40, the author, quoting from Westmoreland & Cambria Natural Gas Co. v. DeWitt, 130 Pa. 235, 18 A. 724, 5 L.R.A. 731, says: '"Water and oil", said the court, "and still more strongly gas, may be classed by themselves, if the analogy be not too fanciful, as minerals ferae naturae. In common with animals, and unlike other minerals, they have the power and tendency to escape without the volition of the owner. Their 'fugitive and wandering existence within the limits of a particular tract is uncertain.' They belong to the owner of the land and are part of it, and are subject to his control; but when they escape, and go into other land, or come under another's control, the title of the former owner is gone."'"

We think the Supreme Court of Oklahoma has clearly indicated that whatever title Bezzi may have had to the residue gas prior to January 11, 1961, it was lost when that gas was reinjected into the common source of supply and commingled with the virgin gas existing there, becoming subject to the law of capture.

[5] Furthermore, in the absence of controlling decisions, this court will accept the determination by the District Court of applicable state law unless convinced to the contrary. Jamaica Time Petroleum Inc. v. Federal Ins. Co., 10 Cir., 366 F.2d 156; Pittsburgh-Des Moines Steel Co. v. American Surety Co. of N. Y., 10 Cir., 365 F.2d 412; Bushman Constr. Co. v. Conner, 10 Cir., 351 F.2d 681, cert. denied 384 U.S. 906; Bledsoe v. United States, 10 Cir., 349 F.2d 605.

Affirmed.

J. G. ALEXANDER, Appellant,

v.

Gerald B. LEAVEY, Deputy Commissioner, Southern Stevedoring & Contracting Co. and Texas Employers' Insurance Association, Appellees.

No. 23248.

United States Court of Appeals
Fifth Circuit.

Dec. 28, 1966.

Rehearing Denied Jan. 27, 1967.

Suit under Longshoremen's and Harbor Workers' Act. The United States District Court for the Southern District of Texas, Ben C. Connally, J., entered judgment adverse to plaintiff who appealed. The Court of Appeals held that finding of deputy commissioner that plaintiff was partially disabled to specific date was tantamount to finding

PACIFIC GAS & ELECTRIC COMPANY v. ZUCKERMAN et al.

California Court of Appeals, Third District
February 13, 1987 — No. Civ. 25009
234 Cal. Rptr. 630

Storage of Gas: Underground Storage — Condemnation — Valuation — Escape of Gas Injected for Storage — Title to Gas.

Oil and Gas Leases: Allowance of Extrinsic Evidence in Interpretation.

PG&E brought an action in eminent domain "to acquire the right to inject, store and withdraw gas" from a parcel adjacent to an exhausted gas reservoir in which PG&E had acquired storage rights; the action also sought to quiet title to "gas which had migrated under defendants' land after its injection into the underground storage facility" and a refund of "excess royalty payments" made under an agreement with defendant landowners to operate wells on the acreage in question. There were cross complaints for "declaratory relief, inverse condemnation, trespass, nuisance, breach of lease, and estoppel." The trial resulted in a judgment for condemnation with damages of $13,793,155 and prejudgment interest; the court also found that PG&E was required "to produce and pay royalties upon gas" from the parcel in question "without regard to whether it was native or injected gas"; in addition the court ordered "litigation expenses to defendants in the sum of $169,011.69, but denying . . . attorneys' fees." Held: Reversed and remanded. The condemnation award as to storage rights was not supported by appropriate evidence. The transactions presented as comparable differed in material respects and other erroneous standards and analysis were present in the expert testimony relied on by the trial court. The award for the taking of mineral rights was based on the proposition that plaintiff company had obligated itself to pay royalties on gas extracted from the tract in question "whether it was injected or native gas." Two matters are involved in considering this question: (1) Whether property in gas is lost under the "rule of capture" by "injecting it into an underground storage reservoir"; (2) the interpretation of the agreement by PG&E to pay royalty on gas from the tract in question to defendant. As to (1), the statutory policy of California relating to underground storage of gas leads to the conclusion "that once gas is reduced to personal possession the owner of the gas is not . . . divested of ownership simply because it injects the gas into an underground storage reservoir"; as to (2) the trial court erred in refusing to admit extrinsic evidence as to the meaning of the lease providing

for the royalties in question since the test is not whether the language to be interpreted is ambiguous or not "but whether the extrinsic evidence is offered to support a meaning to which the language of the instrument is reasonably susceptible." The remand is for the purpose of allowing such evidence to be produced. As to royalties already paid on gas drained from PG&E's storage area, payments were made "with an awareness of the facts" and accepted in good faith and they need not be refunded. The question of attorney's fees and litigation expenses must await further determinations in the case.

SPARKS, Associate Justice.

In this appeal we are called upon to determine a variation on the theme of the "rule of capture" as it applies to recovered gas. Plaintiff Pacific Gas & Electric Company (PGandE) acquired storage rights to an exhausted gas reservoir on an island in the San Joaquin delta. It also entered into an oil and gas agreement with the owners of the island to operate a nearby well on a parcel adjacent to the reservoir and to pay royalties for gas extracted from the well. PGandE then purchased gas from suppliers in Texas and Canada and injected it into the reservoir for use in periods of high demand. Meantime, it operated the nearby well. As fate would have it, the injected gas migrated to the adjacent parcel and PGandE found itself paying royalties on its own gas. This inevitable lawsuit eventually followed. The trial court entered a judgment requiring PGandE to pay over $6.5 million in royalties on its own gas. One of the questions on appeal is whether the owner loses its ownership of recovered gas when it injects that gas into a natural reservoir and the gas migrates. We hold that once gas has been reduced to personal possession, the owner is not thereafter divested of ownership simply because it stores the gas underground and that gas migrates. Consequently, the stored gas was not subject to capture by others and PGandE was not required to pay royalties on its own gas. In addition to this question, we also consider the valuation of storage and mineral rights and the appli-

cation of the parol evidence rule to an oil and gas agreement.

This litigation commenced when PGandE filed an action in eminent domain to acquire the right to inject, store and withdraw gas from beneath 472 acres on the adjacent parcel belonging to the defendants. Additionally PGandE sought to quiet title to gas which had migrated under defendants' land after its injection into the underground storage facility. PGandE also sought a refund of excess royalty payments it had made to defendants. Defendants cross-complained for what they termed declaratory relief, inverse condemnation, trespass, nuisance, breach of lease, and estoppel. After a court trial, judgment was entered granting PGandE's request for condemnation of the property interest it sought, and awarding defendants damages in the amount of $13,793,155, together with prejudgment interest. The court entered a subsequent order granting litigation expenses to defendants in the sum of $169,011.69, but denying their request for attorney's fees. PGandE appeals from the judgment awarding defendants nearly $14 million and defendants appeal from the denial of attorneys' fees. Additionally, defendants have filed a motion for sanctions against PGandE for prosecuting a frivolous appeal. For reasons we shall explain, we have concluded that the judgment must be reversed. Needless to say, the request for sanctions must be denied as well.

FACTS AND PROCEDURAL HISTORY

Recently in Lynch v. State Bd. of Equalization (1985) 164 Cal. App. 3d 94, 210 Cal. Rptr. 335, we were confronted with questions concerning the valuation of oil and gas producing properties for property tax purposes. In this case we are again confronted with questions concerning valuation, but here the date of valuation arises at a time after the life of the oil and gas producing property has expired. As we noted in *Lynch*, oil and gas exists in the interstices of rock occupying certain strata. (Id., at p. 99,

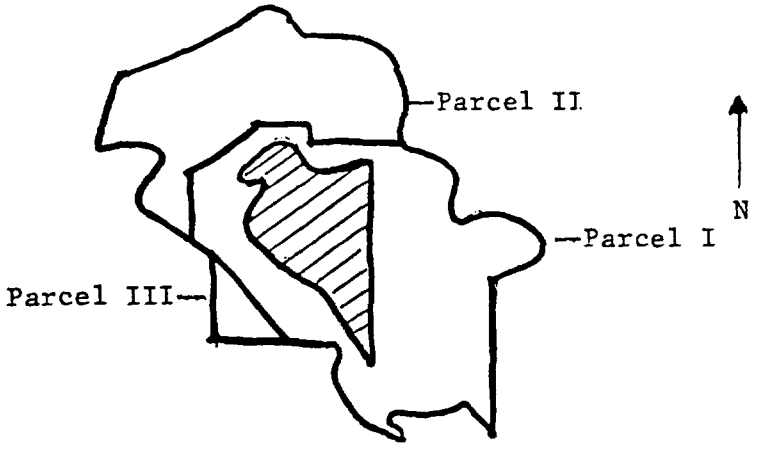
210 Cal. Rptr. 335.) When these deposits are located, the oil and gas can be extracted, initially by the use of the reserve's natural pressure (called reservoir energy) and later through secondary methods of extraction. (Id., at pp. 99, 101, 210 Cal. Rptr. 335.) Although not all the oil and gas can be extracted from a deposit, eventually a field will be depleted to the extent that it is no longer useful as a producing property. (Ibid.) When this occurs some gas fields, due to their geological and geographical characteristics and their large capacity, can be economically used for storage purposes. In this process the user of the field (typically, but not invariably a public utility) purchases gas from other sources during periods of low demand, and injects it into the now depleted reservoir. During periods of high demand this foreign gas can be withdrawn from the reservoir and sold to customers. This case concerns such a property, known as the McDonald Island gas field.

The McDonald Island gas field was originally discovered in June 1936 by the Standard Oil Company of California. The reservoir, called the McDonald sands, lies approximately 5200 to 5300 feet below sea level.[1] Standard operated the property as a gas producing property until 1958. Beginning in 1947, as the McDonald Island field was nearing the end of its productive life, Standard acquired the right to store gas in the lands in which it had previously only held oil and gas leases. In 1958 PGandE and Standard agreed to an exchange of properties. It appears that PGandE then held an oil and gas interest in a producing gas field in Rio Vista which it used to trade for the McDonald Island interests of Standard. The parties placed a value on the trade of $7,391,597, which was approved by the Public Utilities Commission. PGandE sought and obtained approval of the Public Utilities Commission to use the McDonald Island Property as a storage project.

[1] In describing oil and gas reservoirs geologists utilize subsea levels without regard to depth below the actual surface.

Defendants are the landowners of McDonald Island. They have acted through John Zuckerman, who was appointed as agent for all the landowners. By 1962 Zuckerman had come to the conclusion that the existing agreements were inequitable and so he sought to renegotiate them. Among other things, he objected that the agreements did not require exploratory drilling on land not occupied by the storage reservoir.[2] He stated that if the agreements were not changed then "we were going to court and ask that they be changed on the basis of inequity." The parties renegotiated and in 1963 a new agreement was executed. It is that agreement which is in dispute here.

In the 1963 agreement McDonald Island was divided into three parcels, which may be illustrated with the following diagram:



[2] As noted the McDonald sands lie at a depth of approximately 5200 feet below sea level. The agreements by which Standard acquired storage rights gave Standard rights to a depth of 6835 feet subsea. Defendants retained mineral interests in zones deeper than that, and in the property outside of the storage reservoir. The Standard Oil agreements, however, did not require that exploration be conducted for other oil and gas deposits.

In the diagram, the cross-hatched area in the center of parcel I represents the area the parties then believed to be occupied by the storage reservoir. Parcel I included the storage reservoir and in that parcel PGandE owned storage rights and all the mineral rights. In parcel II PGandE retained the storage rights and the gas rights and defendants retained the oil rights. For this purpose, "oil" was defined as hydrocarbons recovered in paying quantities as a liquid and which remained as a liquid under atmospheric pressure and temperature, and "gas" included all other hydrocarbons but did not include asphaltum. Under the agreement PGandE leased the oil rights from defendants in parcel II, but was not required to explore for oil while it operated the storage reservoir. Parcel III included the property to the west of parcel I, and additionally included the mineral rights below parcels I and II at a depth greater than 6835 subsea.[3] Defendants retained the mineral rights in parcel III and PGandE leased those rights pursuant to a traditional oil and gas lease. PGandE was required by this agreement to explore for oil and gas in parcel III and, upon discovery of oil or gas, to produce that oil or gas so long as it could be produced in paying quantities. In the event PGandE failed in its obligations under the lease with respect to parcel III, then the leased rights would terminate and revert back to defendants.

Acting under the terms of the agreement PGandE explored parcel III for hydrocarbons by drilling a well known as Zuckerman-Henning No. 1. Initial exploratory efforts were negative, but on redrilling gas bearing sands were discovered.[4] These gas bearing sands were located at a

[3] In fact, parcel III is somewhat larger geographically than the triangular parcel depicted in the diagram. Nevertheless, the triangular parcel labeled Parcel III on the diagram is the parcel which is at issue in this proceeding. For purposes of this appeal then it is sufficient to refer to this parcel as parcel III.

[4] In exploring for oil and gas the same initial bore can be used for multiple explorations. Typically the first drill will be straight down,

depth that was approximately equal to the depth of the storage reservoir. This indicated that perhaps PGandE had struck the storage reservoir. Although initially the gas extracted through the Zuckerman-Henning No. 1 well was native gas (that is, gas that had been there originally), it ultimately became clear that the deposit in parcel III was connected to the storage reservoir. Two primary factors established this fact. First, the pressure initially encountered in the well was less than should have been expected in a separate reservoir, and rather than decrease with production it varied with the pressure variance in the storage reservoir.[5] The second factor which indicated that the storage reservoir was connected to the Zuckerman-Henning deposit was the gradual rise in the BTU (British Thermal Unit) quality of the gas recovered. The heating value of gas is measured in BTUs per cubic foot. The gas originally in the McDonald Island deposit, and the gas originally extracted from Zuckerman-Henning No. 1, had a BTU content of 962 per cubic foot. The gas which PGandE was purchasing from sources outside California and injecting into the storage reservoir had a much higher BTU content.

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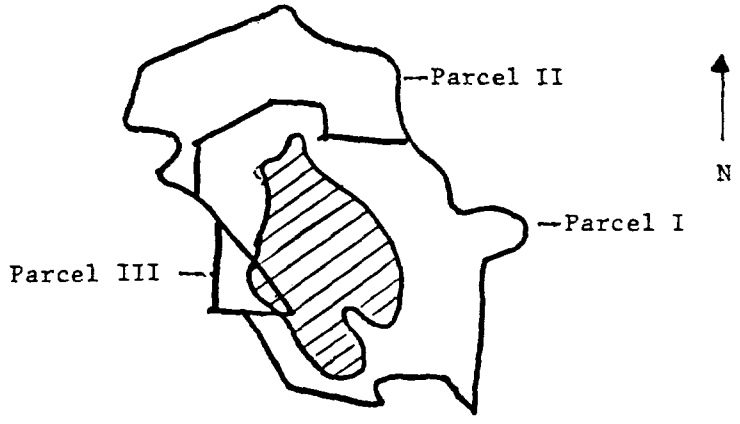
and where that is negative the driller can come partially back up the hole, close it with cement, and drill on an angle to another direction. With the Zuckerman-Henning No. 1 well it took a third redrill before gas was discovered in paying quantities.

[5] In the early stages of oil and gas production the reservoir's natural pressure is used and as depletion reduces natural pressure secondary methods of extraction, including gas and water injection to increase pressure, may be used. (Lynch v. State Bd. of Equalization, supra, 164 Cal. App. 3d at p. 101, 210 Cal. Rptr. 335.) These methods are generally used only with respect to the production of oil; few, if any, secondary production methods are used for the recovery of gas. (Id., at p. 101, fn. 1.) Of course, it makes no economic sense to inject gas into a reservoir simply to enhance the recovery of other gas. Nevertheless, in the peculiar circumstances of this case it appears that PGandE's gas injection into the storage reservoir had the effect of enhancing pressure in the Zuckerman-Henning portion of the reservoir and thus PGand E was unintentionally engaged in secondary methods of gas recovery from the commencement of production.

As the Zuckerman-Henning well was operated over time the BTU content of the recovered gas gradually rose, which indicated that the native gas was mixing with injected gas.

The situation after the discovery of gas in the Zuckerman-Henning well can be illustrated by the following diagram:



Comparison of this diagram with the 1963 diagram, reveals two changes. First, the cross-hatched area which represents the storage reservoir has changed and it now appears that the storage reservoir in fact intrudes into the ground underlying parcel III. Second, the storage rights controlled by PGandE have been increased by the addition of a portion of land in the southwest of parcel I. This addition occurred after the property owners in that portion of land drilled a well that hit the storage reservoir and PGandE was forced to purchase the storage rights to that tract, referred to as the Lower Jones tract.

When the Zuckerman-Henning well struck a portion of the storage reservoir PGandE was placed between the proverbial rock and a hard place. It had "dug up a snake," to use the terminology of one of PGandE's employees. PGandE had invested a large sum (estimated in excess of $25 million) in the storage project. Although the gas ini-

tially extracted from the Zuckerman-Henning well was native gas, it was apparent that due to the fugacious nature of gas the injected gas would migrate to the Zuckerman-Henning well as the native gas was produced. (See Lynch v. State Bd. of Equalization, supra, 164 Cal. App. 3d at p. 100, 210 Cal. Rptr. 335.) Under its lease obligations with respect to parcel III PGandE had a duty to operate the well and to pay royalties to defendants so long as the well could produce paying quantities, and if PGandE ceased operating the well the right to operate it would revert to defendants.

PGandE was unsure of its legal position but in order to avoid a question of default it determined to operate the well and pay a royalty to defendants. Defendants were notified of the facts and diplomatically advised that "In due course, when the results of further drilling have been evaluated, we anticipate discussing with you the ultimate resolution of the problems resulting from this exploration." PGandE operated the well and paid royalties to defendants from 1967 until 1980. At some point it became clear that a greater volume of gas had been produced from the well than had originally been in place. Eventually it also became clear that all of the original gas had been produced with the result that the well was then yielding only injected gas. In 1980 PGandE notified defendants that it would cease paying royalties on injected gas and would seek to condemn additional storage rights by eminent domain. The decision led to the filing of this suit.

The matter was tried to the court. The parties agreed that this is an appropriate case for eminent domain and the only questions at trial were the elements and amount of damages to be paid. The trial court awarded three types of damages. It found the value of the storage rights to be $6,930,000 and awarded defendants this amount with the legal rate of interest from August 1, 1980. The court found that PGandE was also required to compensate defendants for their mineral interest in the subject property and the

court found that this interest included the right to insist that PGandE operate the Zuckerman-Henning well without regard to whether gas extracted through that well was native or injected and to receive a royalty on gas extracted through the well for so long as the well could produce gas in paying quantities. This essentially meant for as long as PGandE operated its storage reservoir. The value of this interest was found to be $6,505,155 and this amount was awarded with interest from February 22, 1982. The court further found severance damages to be $358,000 and it awarded this amount with interest from the date of judgment. The judgment included additional findings that by ceasing to operate the Zuckerman-Henning well PGandE breached the 1963 lease agreement, and awarded damages for breach of contract in the amount of $6,505,155 as an alternative to damages for condemnation of the defendants' mineral interests. The court further found that PGandE abandoned the gas underlying parcel III as of August 1, 1980, and awarded defendants the sum of $2,938,000, but held that sum to be subsumed within the damages awarded for condemnation of the mineral rights. By subsequent order the court awarded defendants litigation costs of $169,011.69, but denied their request for attorneys' fees.

DISCUSSION

When private property is taken through eminent domain, the condemning agency must pay "just compensation" to the owner. (U.S. Const., 5th Amend.; Cal. Const., art. I, § 19.) The measure of just compensation is the fair market value of the property taken. (Code Civ. Proc., § 1263.310.) In normal circumstances the "fair market value of the property taken is the highest price on the date of valuation that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obliged to sell, and a buyer, being ready, willing, and able to buy but under no particular necessity for so doing, each dealing with the other with full knowl-

edge of all the uses and purposes for which the property is reasonably adaptable and available." (Code Civ. Proc., § 1263.320, subd. (a).) But where there is no relevant market for the property then the fair market value is to be determined by any method of valuation that is just and equitable. (Code Civ. Proc., § 1263.320, subd. (b); Evid. Code, § 823.)

In condemnation cases it is a firmly established principle that the compensation payable is to be based upon the loss to the owner rather than upon the benefit received by the taker. (City of Los Angeles v. Decker (1977) 18 Cal. 3d 860, 866, 135 Cal. Rptr. 647, 558 P.2d 545.) The California Supreme Court early stated that "it seems monstrous to say that the benefit arising from the proposed improvement is to be taken into consideration as an element of the value of the land." (San Diego Land etc. Co. v. Neale (1888) 78 Cal. 63, 75, 20 P. 372.) This has been construed to mean that "[t]he beneficial purpose to be derived by the condemnor's use of the property is not to be taken into consideration in determining market values, for it is wholly irrelevant." (People v. La Macchia (1953) 41 Cal. 2d 738, 754, 264 P.2d 15, overruled on another ground in County of Los Angeles v. Faus (1957) 48 Cal. 2d 672, 680, 312 P.2d 680, and quoted with approval in Merced Irrigation Dist. v. Woolstenhulme (1971) 4 Cal. 3d 478, 491, 93 Cal Rptr. 833, 483 p.2d 1.) This rule, however, does not mean that evidence of the highest and best use of the property must be excluded simply because that is the use that the condemnor intends to make of the property. In *Neale*, the court held that it was not proper to take into consideration the ongoing construction of a dam in valuing the property and that it was improper to consider the enhanced value the condemnor would obtain in other property after completion of the dam. (78 Cal. at pp. 74-75, 20 P. 372.) But the court went on to hold that it was proper to consider the value of the land 'as a reservoir site." (Id., at p. 71, 20 P. 372.) Similarly in City of Los Angeles v. Decker, supra, 18 Cal. 3d at page 869, 135 Cal. Rptr. 647,

558, P.2d 545, the court reiterated that it is improper to award compensation based upon the value to the condemnor, but held that it was proper in that case to consider the value of the property for parking purposes (the highest and best use) despite the fact that the city intended to use it for such purposes. Finally, the rule does not mean that a condemnor can appropriate property for nothing simply because in one sense it might be said that the property has no market value in the hands of the owner. (San Diego Land etc. Co. v. Neale, supra, 78 Cal. at page 68, 20 P. 372. See also Code Civ. Proc., § 1263.320, subd. (b).) With these principles in mind we turn to a consideration of the elements of damage awarded defendants.

I

STORAGE RIGHTS

The trial court awarded defendants the sum of $6,930,000 for the condemnation of the storage rights in parcel III. In doing so the court accepted without qualification the valuation of defendants' expert witness, Robert Paschall. PGandE contends that reasoning employed by Paschall was so irrational and unsupportable that his opinion on value does not constitute substantial evidence. Defendants retort that Paschall's testimony provides formidable support for the trial court's findings of value. Because we find Paschall's evaluation to be riddled with error and to be a clearly overinflated estimate of the value of the storage rights, we agree with PGandE that the award cannot stand.

Pascall's evaluation can be best described as a modified comparable sales approach. In the ordinary case, a sale of other property, to be considered comparable, "must have been made sufficiently near in time to the date of valuation, and the property sold must be located sufficiently near the property being valued, and must be sufficiently alike in respect to character, size, situation, usability, and improvements, to make it clear that the property sold and

the property being valued are comparable in value and that the price realized for the property sold may fairly be considered as shedding light on the value of the property being valued." (Evid. Code, § 816; see also City of Pleasant Hill v. First Baptist Church (1969) 1 Cal. App. 3d 384, 415, 82 Cal. Rptr. 1.) But this was not an ordinary case. It may fairly be said that there are no true "comparables" in dealing with underground storage reservoirs. There are relatively few such properties in the state, and those noted by the experts involved different geographical locations, temporal transactions, and physical characteristics. In normal circumstances this would preclude the use of a comparable sales approach. But it is clear that underground storage properties are sui generis and that normal approaches to valuation are problematical. For this reason latitude must be accorded an expert in valuing such properties, and any approach that is "just and equitable" may be considered. (Evid. Code, § 823; Code Civ. Proc., § 1263.320, subd. (b).)

For all that, there are limitations and those limits were exceeded here. Where an expert attempts to value property by considering sales of other property which are not truly comparable, then it is necessary, in evaluating the validity of the expert's opinion, to consider the effect the differences between the properties may have on value. When those differences are examined in this case, the variations are so material that, when coupled with other faulty assumptions, they undermine the validity of the expert's opinion to such an extent that his opinion cannot be deemed to constitute substantial evidence of value.

Paschall began by rejecting the transactions involving other storage facilities and elected instead to base his estimate of value upon the 1958 transaction in which PGandE acquired the McDonald Island rights from Standard Oil.[6]

[6] Paschall's refusal to consider other transactions in determining his estimate of value for the parcel III rights is explicable only in terms

As reported to the Public Utilities Commission (P.U.C.), the total value of the transaction to PGandE was $7,391,597. This value was arrived at through negotiations of the parties by using a capitalization of income approach to value the Rio Vista producing properties given in exchange for the McDonald Island properties, with a retention of a royalty interest in the Rio Vista properties by PGandE's wholly owned subsidiary, Natural Gas Company. In its

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of his unflagging desire to unduly puff the damages to be awarded defendants. As a matter of law the closer a property is in terms of physical characteristics and time of sale the more comparable it is to the subject transaction. Even though underground storage areas tend to be sui generis, the most nearly comparable sale to the entire McDonald Island tract was the 1979 transaction involving property known as Ten Section. The Ten Section transaction involved 2471 acres compared to McDonald Island's 2,080 acres. It has a working capacity of 50 billion cubic feet compared to McDonald Island's 54 billion cubic feet. And the transaction occurred in 1979, less than three years before the date of valuation here, and more than 21 years closer in time than the original McDonald Island transaction. The 1979 acquisition cost of all of the Ten Section rights was $34,145,000. The parties designated the value of the storage rights as $6,092,000. Even utilizing Paschall's method of including other nonstorage property rights in the storage rights for valuation purposes, an approach we reject, Paschall was still only able to claim a 1979 storage right value of $15,357,000 for the Ten Section parcel, which was indexed to 1982 at $19,964,000. This may be contrasted with the 1982 value of the McDonald Island storage rights claimed by Paschall to be $64,355,000. Even using Paschall's approach, which we find to be erroneous in many ways, a comparison of McDonald Island with Ten Section would produce a value of the parcel III rights far less than one-third of the value he claims those rights have. Another obvious comparable transaction ignored by Paschall was the 1968 acquisition by PGandE of the Lower Jones tract. As noted in the diagram, the storage reservoir at McDonald Island not only intruded into parcel III, it also intruded into land to the south of parcel III owned by other parties. When this was discovered PGandE was forced to negotiate the purchase of rights in the Lower Jones tract. This involved 462 acres, compared to the total of 472 acres involved here. It also involved the purchase of rights which represent a small portion of a much larger storage reservoir. In 1968 PGandE paid $211,000 for all of the rights in the Lower Jones tract, and the parties designated $42,000 as the price of the storage rights. That transaction

P.U.C. application for approval of the transaction and to operate the storage facility PGandE reported a value of $1,639,681 for the storage rights acquired at McDonald Island.

Paschall eschewed the P.U.C. approved figure and derived his own estimate of the value of the McDonald Island storage rights, purportedly from the P.U.C. report. His approach was to deduct from the total P.U.C. value of the transaction the sums he considered to be attributed to nonsubsurface rights. He used a value of $2,811,000 for the nonsubsurface rights.[7] A review of the P.U.C. report and Paschall's testimony reveals that his approach was to deduct from the total value of the transaction the assigned value of all interests except leaseholds, storage rights, gas in the underground reservoir, and the value of interests retained by Natural Gas Company.

would indicate a value of the parcel III storage rights which would be but a fraction of those claimed by Paschall. A third comparable transaction is the state's lease rights in McDonald Island. As explained below, the state owns approximately 8.827 percent of the land over the storage reservoir on McDonald Island and PGandE leases the state's portion of the reservoir. Paschall used a capitalization of income (rent) approach to value the state's interest and determined its value to be $1,165,428. Even using an acreage approach, which we find erroneous, Paschall determined this would indicate a value of $1,421,822 for the parcel III rights. Paschall refused to consider the other storage rights transactions because there were few of them and they indicated a wide range of values. He dismissed the comparison with the State's McDonald Island interest by saying "I considered the State had a bad bargain of it." Paschall's refusal to consider these clearly more comparable transactions in favor considering a transaction 24 years prior to the valuation date casts severe doubt upon the validity of his approach. Despite these defects, we reject his evaluation for even more serious errors.

[7] In his report Paschall stated that the value of $2,811,000 represented the value of the nonsubsurface rights and properties at Rio Vista. Obviously the value of nonsubsurface rights at Rio Vista has nothing whatsoever to do with the value of the nonstorage rights at McDonald Island, but it appears that the statement in the report was simply an error in explanation.

Paschall's approach was clearly erroneous. Property cannot be considered comparable where it includes various fixtures, rights, improvements, and personal property which the property being condemned does not include. For example, in City of Santa Cruz v. Wood (1967) 252 Cal. App. 2d 52, at page 56, 60 Cal. Rptr. 26, the city sought to acquire property for sewerage purposes. The defendant owner sought to introduce into evidence an estimate of the acquisition cost by the city's Director of Public Works. The estimate, however, included many miles of rights of way in other property besides a part of the land at issue. The court held that the exclusion of the evidence was proper since it had no logical tendency to prove the value of the land in question and could only have served to confuse the court and jury. Similarly, in Los Angeles etc. School Dist. v. Swensen (1964) 226 Cal. App. 2d 574, at page 583, 38 Cal. Rptr. 214, the trial court excluded evidence of the unit sale of three parcels of property in the same tract as the subject property. The Court of Appeal upheld the exclusion, noting that the three lots had a much greater frontage area, far more living space, fronted on a principal business street, and the price included an indeterminate amount for furniture and art objects which were included in the sale. (See also City of Rosemead v. Anderson (1969) 270 Cal. App. 2d 260, 266-267, 75 Cal. Rptr. 575.)

In valuing the storage rights in parcel III the only property interest at issue was the naked right to store gas deep within the earth under defendants' land. PGandE acquired no surface rights in parcel III, and interference with surface uses was compensable as severance damages. Any mineral interests defendants may have, including the right to gas in the portion of the storage reservior under parcel III, were treated by the court and the parties as a separate item of damages. In the 1958 transaction PGandE acquired from Standard Oil a number of surface and nonsurface rights and leaseholds, including oil and gas leases

on all of McDonald Island. To fail to exclude these leasehold interests in considering the value of the storage rights was improper. It was likewise improper to include consideration of the value of the interests retained by Natural Gas Company since those interests inured to the benefit of PGandE and reduced rather than increased the costs of the McDonald Island rights. The major error, however, was to include the value of the gas in the storage reservoir acquired by PGandE in the 1958 transaction.[8] As we have noted, any right defendants had to the gas in the storage reservoir was to be compensated, if at all, as a separate item of damages. In determining the value of the storage rights it was therefore erroneous to attempt to compare the property to a storage reservoir with existing gas supplies. The value of the gas in storage in 1958 was $2,739,014, an amount well in excess of one-half of the total value Paschall arrived at for the 1958 storage rights. Through this approach Paschall was able to ignore the P.U.C. approved value of $1,639,681 for the storage rights, and to assign a value of $4,581,000 to those rights in 1958.

Since PGandE did not acquire all of the rights to the storage reservoir in 1958 it was necessary to adjust the value of the rights it obtained to reflect the value of the whole field. Paschall made two adjustments to the $4,581,000 figure. One was reasonable and is easily ex-

[8] It was established that in the operation of an underground storage reservoir the entire volume of the reservoir cannot be utilized for working purposes. A "cushion" volume of gas is required which will remain in the reservoir at all times and which will be recovered only upon termination of the use of the reservoir for storage purposes. When a storage facility is acquired the buyer will be required to inject gas into the reservoir to reach the cushion level before it can be used for storage, and if there is a volume of gas in the reservoir in excess of the cushion then the buyer acquires usable gas in the transaction. In either event, the buyer is required to pay for the gas which is then in the storage reservoir; it cannot simply purchase the rights without the gas.

plained. It appears that Whiskey Slough meanders across parcels I and II and crosses directly over the storage reservoir. The State of California owns the land underlying Whiskey Slough and the portion of the storage reservoir in state lands was not acquired by PGandE from Standard Oil. PGandE is required to lease that portion of the reservoir from the state. Paschall concluded that the State's portion of the reservoir is 8.827 percent, and thus PGandE acquired only 91.173 percent of the reservoir from Standard. In order to determine the value of the whole reservoir it was necessary to divide the price paid by PGandE by the 91.173 percent interest it acquired. Paschall used a similar method to adjust defendants' royalty rights in McDonald Island. But the royalty rights in McDonald Island related to any potential minerals outside of the storage reservoir; there were no outstanding royalty rights in the storage reservoir. This latter adjustment to the 1958 purchase price of the storage rights was unsupported.

It is necessary, as all the experts agreed, to translate the prices paid in earlier comparable sales into 1982 dollars, that being the date of valuation in this case. The gross national product rate of inflation between 1958 and 1982 was 309 percent, which produces a multiplier of 3.09, and which was utilized by most of the experts in considering the earlier McDonald Island transaction. Paschall testified that the State Board of Equalization maintains inflation factors for petroleum exploration and production properties, and that the Board's factor for 1958 to 1982 was 3.29. Paschall rejected both the gross national product and the State Board of Equalization factors and created his own by comparing the wellhead price of gas from 1958 to 1982. In 1958 the wellhead price of gas was 29 cents per cubic foot, while in 1982 it was $3.25 per cubic foot. This was an inflation rate of 1.121 percent, which produced a multiplier of 11.21. This was the multiplier Paschall chose to use. His approach was flawed for numerous reasons. Paschall testified that since the parties used a capitalization of income method in valuing the Rio Vista properties in

1958 they ought to be willing to do so again. However, a capitalization of income approach considers the net income stream to be derived from a producing property. The wellhead price of gas is a gross price and changes in the wellhead price do not necessarily reflect changes in the net income to be derived from the property. Moreover, in determining the value of the Rio Vista properties in 1958 the parties estimated future increases in the price of gas and thus to an extent already took into consideration the inflation factors used by Paschall. Further, the capitalization of income approach was used to value the Rio Vista properties and not the McDonald Island properties. Rio Vista was a producing gas field. While increases in the price of gas might cause an increase [in] the value of a producing field, it is wholly speculative whether increases in the gross price of gas would result in a proportionate increase in the value of storage rights. In any event, nothing in the record would support such a conclusion.

In our view the decision in East Bay Mun. Utility Dist. v. Kieffer (1929) 99 Cal. App. 240, at page 250, 278 P. 476, aptly sets forth the controlling principle. There the utility district sought to acquire property for water reservoir purposes and the defendant unsuccessfully sought to introduce evidence of the selling price of water and electricity as evidence of value. Affirming the rejection of that evidence, the court said: "But the relation between the value of land in a proposed reservoir and the current price of water and electric energy is too remote and conjectural to be of any reliable assistance to the jury in determining the market value of the land taken." Likewise in People v. Dunn (1956) 46 Cal. 2d 639, at page 641, 297 P.2d 964, it is said: "It is settled that evidence of profits derived from a business conducted on the land is too speculative, uncertain and remote to be considered as a basis for ascertaining market value."

Finally, Paschall's assumption that an increase in value in a storage property may be determined by direct com-

parison with a producing property also fails. In In re Marriage of Hewitson (1983) 142 Cal. App. 3d 874, at pages 885-887, 191 Cal. Rptr. 392, the trial court valued a closely held corporation by relying solely on the testimony of an expert who evaluated the business by comparing it with the selling price/book value ratio of publicly traded corporations. Due to the dissimilarities between the two types of businesses the comparison failed and the expert's testimony was held not to constitute substantial evidence to support the judgment. Similarly, a storage facility is obviously too dissimilar to a producing property to permit direct comparison in the manner utilized by Paschall.

After going through these flawed steps Paschall derived a 1982 value for the entire storage reservoir of $64,348,000. It was then necessary to determine the portion of this value which was attributable to the portion of the reservoir under parcel III. In order to do this Paschall used surface acreage. It was estimated that the parcel III portion of the reservoir was 10.77 percent of the entire reservoir, and thus that the value of the parcel III portion was $6,929,636, rounded to $6,930,000. Once again Paschall erred. It was established, and Paschall conceded, that the reservoir is thickest in the middle and the fringes of the reservoir contain far less storage capacity than the middle areas. It was variously estimated that the portion of the reservoir in parcel III contains from 2.55 percent to 4 percent of the total reservoir capacity. PGandE acquired no surface rights and in valuing the storage rights the surface area is irrelevant. To belabor the obvious, the storage rights have value only for storage purposes, and the sole factor that gives them value is storage capacity. Clearly, the portion of the reservoir's value which is attributable to the parcel III property must be based upon volume rather than surface area.

The final value which Paschall assigned to the storage rights was totally disproportionate to any other estimate of value given, including Paschall's own estimates using dif-

ferent methods of valuation. The disproportionate nature of that valuation can be shown by reference to McDonald Island transaction. Everyone agreed that in 1958 PGandE paid $7,391,597 for the McDonald Island rights. Included in the transaction were numerous surface rights, rights of way, leasehold interests, equipment and facilities, and oil and gas leases on all of McDonald Island with the provision that exploration was not required for so long as the storage reservoir was utilized. No such additional rights are at issue in valuing the storage rights in this case. However, even if we make no adjustment for those interests, the portion of the 1958 transaction which could be attributed to a 2.55 percent portion of the properties would be $188,485.72, and the portion attributable to 4 percent portion would be $295,663.88. The gross national product rate of inflation from 1958 to 1982 was 309 percent, which produced a multiplier of 3.09. The judgment here results in a rate of inflation of 3,677 percent (multiplier of 36.77) for a 2.55 percent portion of the transaction, and 2,344 percent (multiplier of 23.44) for a 4 percent portion of the transaction.

In an action in eminent domain the value of the property condemned is a factual question and the trier of fact's valuation findings will be upheld when they are supported by substantial evidence. (Los Angeles etc. School Dist. v. Swensen, supra. 226 Cal. App. 2d at p. 581, 38 Cal. Rptr. 214.) But this does not mean that any determination of value, no matter how excessive and absurd, will constitute substantial evidence simply because some expert is willing to state it as his opinion. To be considered substantial, evidence must be "'of ponderable legal significance . . . reasonable in nature, credible, and of solid value.'" (People v. Johnson (1980) 26 Cal. 3d 557, 576, 162 Cal. Rptr. 431, 606 P.2d 738, quoting Estate of Teed (1952) 112 Cal. App. 2d 638, 644, 247 P.2d 54.) Courts, both trial and appellate, have the responsibility of insuring that an expert's determination of value takes into account only reasonable and credible factors. As this court said in Sacramento, etc.

Drainage Dist. ex rel. State Reclamation Bd. v. Reed (1963) 215 Cal. App. 2d 60, at page 69, 29 Cal. Rptr. 847:

> "A condemnation trial is a sober inquiry into values, designed to strike a balance between the economic interests of the public and those of the landowner. [Citation.] There is a limit to imaginative claims even when described in terms of a prospective buyer's mental reactions. To say that only the witness' valuation opinion has probative value, that his 'reasons' have none, ignores reality. His reasons may influence the verdict more than his figures. To say that all objections to his reasons go to weight, not admissibility, is to minimize judicial responsibility for limiting the permissible arena in condemnation trials. The responsibility for defining the extent of compensable rights is that of the courts. [Citations.]"

The opinion of an expert must be on matter "that is of a type that reasonably may be relied upon by an expert in forming an opinion upon the subject to which his testimony relates." (Evid. Code, § 801, subd. (b).) As Witkin notes, "[w]hat are reliable matters depends on the particular subject, and no statutory listing is possible. The Evidence Code prescribes minimum requisites for all cases, leaving particular rules to be formulated, as in the past, by judicial decisions." (Witkin, Cal. Evidence (2d 1966) The Opinion Rule, § 409, pp. 367-368.) This requirement of reliability has been carried over into the statutes containing "special rules of evidence applicable to any action in which the value of property is to be ascertained." (Evid. Code, § 810, subd. (a).) Thus Evidence Code section 814 provides that "[t]he opinion of a witness as to the value of property is limited to such an opinion as is based on the matter perceived by or personally known to the witness or made known to the witness at or before the hearing, whether or not admissible, that is of a type that reasonably may be relied upon by an expert in forming an opinion as to the value of property, including but not limited to the matters listed in Sections 815 to 821, inclusive, unless a

witness is precluded by law from using such matter as a basis for an opinion." A special statute deals with the unusual occurrence when there is no relevant market. Evidence Code section 823 provides: "Notwithstanding any other provison of this article, the value of property for which there is no relevant market may be determined by any method of valuation that is just and equitable." This section parallels Code of Civil Procedure section 1263.320, subdivision (b), which provides that "[t]he fair market value of property taken for which there is no relevant market is its value on the date of valuation as determined by any method of valuation that is just and equitable." As the comment to this section notes, "subdivision (b) has been added to the definition because there may be no relevant market for some types of special purpose properties such as schools, churches, cemeteries, parks, utilities, and similar properties. All properties, special as well as general, are valued subject to the limits of Article 2 (commencing with Section 810) of the Chapter 1 of Division 7 of the Evidence Code. The Evidence Code provides that, regardless of whether there is a relevant market for property, its fair market value may be determined by reference to matters of a type that reasonably may be relied upon by an expert in forming an opinion as to the value of property including where appropriate, but not limited to, (1) the market data (or comparable sales) approach, (2) the income (or capitalization) method, and (3) the cost analysis (or reproduction less depreciation) formula." (Legis. com. com., West's Ann. Code Civ. Proc. (1982 ed.) § 1263.320, p. 39.)

The value of opinion evidence rests not in the conclusion reached but in the factors considered and the reasoning employed. (People v. Coogler (1969) 71 Cal. 2d 153, 166, 77 Cal. Rptr. 790, 454 P.2d 686; People v. Bassett (1968) 69 Cal. 2d 122, 141, 70 Cal. Rptr. 193, 443 P.2d 777.) Where an expert bases his conclusion upon assumptions which are not supported by the record, upon matters which are not reasonably relied upon [by] other experts, or upon

factors which are speculative, remote or conjectural, then his conclusion has no evidentiary value. (Hyatt v. Sierra Boat Co. (1978) 79 Cal. App. 3d 325, 338-339, 145 Cal. Rptr. 47; Richard v. Scott (1978) 79 Cal. App. 3d 57, 63, 144 Cal. Rptr. 672.) In those circumstances the expert's opinion cannot rise to the dignity of substantial evidence. (Hyatt v. Sierra Boat Co., supra.) When a trial court has accepted an expert's ultimate conclusion without critical consideration of his reasoning and it appears the conclusion was based upon improper or unwarranted matters, then the judgment must be reversed for lack of substantial evidence. (In re Marriage of Hewitson, supra, 142 Cal. App. 3d at pp. 885-887, 191 Cal. Rptr. 392; In re Marriage of Rives (1982) 130 Cal. App. 3d 138, 149-151, 181 Cal. Rptr. 572. See also Evid. Code, § 801.) For example, in In re Marriage of Hewitson, supra, the expert attempted to determine the value of a closely held corporation by using the selling price/book value ratio of publicly traded corporations. Due to the differences in the two types of companies the analogy was improper and the judgment based upon the expert's testimony was not supported by substantial evidence. (142 Cal. App. 3d at p. 887, 191 Cal. Rptr. 392; see also In re Marriage of Lotz (1981) 120 Cal. App. 3d 379, 384, 174 Cal. Rptr. 618.) Likewise, in In re Marriage of Rives, supra, 130 Cal. App. 3d at pages 149-151, 181 Cal. Rptr. 572, this court reversed a determination of the value of a queen bee business because the court accepted the testimony of an expert who had relied upon false assumptions and improper factors, and who had failed to consider all of the relevant factors which established value.

We find this to be a case in which an appellate court cannot defer to the trial court's traditional role in drawing inferences and resolving conflicts in the evidence. In his evaluation Paschall gave no consideration to more comparable transactions and relied instead on an adjustment of a temporally remote transaction. In adjusting the remote transaction to reflect modern values he rejected the P.U.C. approved valuation of the storage rights and in-

cluded in his consideration several items of property rights which are not included in the parcel III condemnation. He made an adjustment for nonexistent royalty rights in the storage reservoir. In adjusting 1958 values to 1982 values he disregarded the gross national product and State Board of Equalization inflationary factors and created his own factor based upon changes in the gross price of gas, an approach which is wholly speculative, remote, and conjectural. And in determining the portion of the reservoir's value attributable to parcel III Paschall rejected the sole factor which gives the storage rights value (volume) in favor of using the wholly irrelevant factor of acreage. The end result was a valuation of the parcel III storage rights which is excessive on its face and disproportionate to any other evaluation of the rights. The trial court accepted Paschall's conclusion without any critical assessment of the reasoning employed and the assumptions relied upon. Because we find insufficient evidence to support the judgment, it must be reversed and remanded for a new trial on the damages PGandE must pay for the storage rights underlying parcel III. For the benefit of the parties on remand it is necessary to note that defendants are not to be deprived of their property without just compensation simply because it has little or no value to them or to anyone other than PGandE. On the other hand, PGandE cannot lawfully be forced to pay a disproportionate and inflated price for the storage rights simply because it finds itself between a rock and a hard place and has become a forced purchaser of those rights. Any reasoned approach which reaches a just and equitable result may be considered. (Code Civ. Proc., § 1263.320, subd. (b).) But whatever the approach, the emphasis must be on "just and equitable."

II

MINERAL INTERESTS

The trial court awarded defendants the sum of $6,505,155 for their mineral interests in the portion of par-

cel III which was condemned. As an alternative the court awarded the same amount for breach of the 1963 agreement. This award was premised on the court's conclusion that defendants had the right to insist that PGandE extract and pay royalties upon gas from the Zuckerman-Henning well for so long as gas could be extracted without regard to whether it was injected or native gas. The court reached this conclusion under the 1963 agreement, and did not consider whether California's oil and gas law supported such a result. We conclude that neither the agreement nor the law supports the award for mineral interests.

The basic aspect of our oil and gas law which must be considered here is the so-called "rule of capture." The rule has been stated this way: "'The owner of a tract of land acquires title to the oil and gas which he produces from wells drilled thereon, though it may be proved that part of such oil or gas migrated from adjoining lands.'" (1 Williams & Meyers, Oil and Gas Law (1983) § 204.4, p. 55, quoting from Hardwick, The Rule of Capture and Its Implications as Applied to Oil and Gas (1935) 13 Tex. L. Rev. 391, 403.) The principle may be easily explained. Essentially, the law provides that oil and gas becomes the personal property of whoever brings it to the surface and reduces it to possession. (See Lynch v. State Bd. of Equalization, supra, 164 Cal. App. 3d at p. 102, 210 Cal. Rptr. 335.) The right to drill for oil and gas is dependent upon ownership of the surface of the land. (Ibid.) The surface owner, or those claiming under him, who brings the oil or gas to the surface obtains a personal property interest in the oil or gas despite the fact that his activities may have caused the oil or gas to migrate to his land from the land of another. (Ibid.) Although this is the basic American law of oil and gas, different jurisdictions reach this result in different ways. In some jurisdictions, and under early California law, it has been held that the surface owner of the land has absolute title to the oil and gas underlying his land, but that title is defeasible if the oil or gas should

migrate to the land of another. (164 Cal. App. 3d at p. 102, 210 Cal. Rptr. 335.) In other jurisdictions, and at one time in California, it has been held that ownership of oil and gas is inchoate and subject to "potential possession." (Ibid.) Now it is firmly established in California that no one owns oil and gas in its natural setting. (Ibid.) The surface owner of real property has the exclusive right on his premises to drill for oil and gas, and he may transfer that right as a profit à prendre to another. (Ibid.)

With the use of depleted gas reservoirs for storage purposes the question naturally arises whether the owner of recovered oil and gas loses his ownership interest in the property by injecting it into a natural reservoir. The issue has not been determined in California, but the courts of a few other jurisdictions have considered the issue with conflicting results. (See Annot., Gas-Storage in Natural Reservoir (1964) 94 A.L.R. 2d 543, and cases cited there. See also Bezzi v. Hocker (10th Cir. 1966) 370 F. 2d 533 [26 O&GR 328], applying Oklahoma law.) If we were simply to choose between the conflicting decisions from other jurisdictions we would follow those which hold that ownership is not lost by injection into a storage reservoir, since they are the better reasoned and reach a more equitable result. (See White v. New York State Natural Gas Corporation (1960) W.D. Penn. 1960) 190 F. Supp. 342 [14 O&GR 253], applying Pennsylvania law; Lone Star Gas Co. v. Murchison (Tex. Civ. App. 1962) 353 S.W. 2d 870, 94 A.L.R. 2d 529 [16 O&GR 816].)[9] Fortuitously, in this

[9] The cases which have held that the owner of natural gas loses his ownership interest in the gas by injecting into an underground storage facility have done so by analogy to the common law rule of animals ferae naturae. The common law held that wild animals could be owned only so long as they remained captive and that upon escape and return to their natural habitat any ownership interest was lost. (See Hammonds v. Central Kentucky Natural Gas Co. (1934) 255 Ky. 685, 75 S.W. 2d 204.) So it is with natural gas where the analogy is accepted. (Ibid.) However, the courts which have concluded that injection into a

state we have a clear indication of legislative intent that an owner is not to be considered to have lost his ownership interest in gas by injecting it into an underground storage reservoir.

In 1975 the Legislature acted to end any uncertainty which might arise over a public utility's use of an underground gas storage reservoir. At that time section 613 was added to the Public Utilities Code to provide that a gas corporation may condemn any property necessary for the construction and maintenance of its gas plant. (Stats. 1975, ch. 1240, § 65, p. 3178, operative July 1, 1976.) Section 221 of that code was amended to provide specifically that "gas plant" includes underground storage. (Stats. 1975, ch. 1240, § 64, p. 3178.) The Law Revision Commission stated that the amendment was intended to make express the inherent right of a gas corporation to condemn property for the underground storage of natural gas. In this legislation we find clear legislative recognition of underground storage of natural gas and the intent that gas in underground storage is to be considered to be within the gas corpora-

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storage reservoir does not divest the owner of his personal property interest in the gas have done so by recognizing that natural gas is not perfectly analogous to wild animals. (See White v. New York State Natural Gas Corp., supra; Lone Star Gas Co. v. Murchison, supra.) In Lynch v. State Bd. of Equalization, supra, 164 Cal. App. 3d at page 99, 210 Cal. Rptr. 335, we recognized that oil and gas interests are sui generis and that analogies drawn from other fields are often inapt for comparison. This would lead us to reject the analogy attempted in *Hammonds* and other cases reaching similar results. However, even if we accepted the comparison it would lead to a contrary result in California. In Civil Code section 996, our Legislature has provided that fur bearing animals brought into captivity are personal property and remain so regardless whether they remain in or escape from captivity. This is a legislative abrogation of the common law with respect to commercially valuable living wild animals, and if we attempted to analogize commercially valuable oil and gas to the law of wild animals we would conclude that the policy of this state is that the ownership interest gained from capturing valuable natural commodities is not defeated by "escape" of the commodity.

tion's "gas plant." It would be entirely inconsistent with this policy to hold that a gas corporation is somehow divested of its ownership of gas simply because it stores it underground. Accordingly, we conclude that once gas is reduced to personal possession the owner of the gas is not to be considered to have been divested of ownership simply because it stores the gas in an underground storage reservoir. To be sure an owner who allows gas to escape to the property of another may liable in trespass, nuisance, inverse condemnation, or on other applicable theories, but it still remains the owner of such gas.

Since we conclude that the law of capture does not apply to divest PGandE of the ownership of its injected gas, it is necessary to determine whether defendants acquired an interest in that gas by the 1963 agreement. The trial court concluded that they did acquire such rights as a matter of law. We find the decision of the trial court to be in error and to compel the reversal of that aspect of the judgment.

In paragraph 15 of the 1963 agreement PGandE agreed, subject to various other terms and conditions, to pay defendants as royalty and rent one-sixth of the gross proceeds derived from the sale of "gas produced hereunder from Parcel III . . . ." It was further provided in the last clause that "[t]he provisions of this Paragraph 15 shall not apply to any gas which has been injected and stored in and thereafter withdrawn from Parcels I or II." The trial court's ruling was made on motion of the defendants before the first witness was called. Defendants argued that the lease agreement was not ambiguous and that since it is not ambiguous it is unnecessary to consider extrinsic evidence to interpret it. Defense counsel's argument was that since the agreement "says all gas produced, . . . it doesn't make any difference whether it's extraneous gas. I use the term extraneous to mean injected and stored gas; okay? And in fact, it doesn't tell you what kind of gas they are going to pay a royalty on. It simply says all gas produced. Therefore, it means that it is unambiguous." Counsel for

PGandE retorted that the "term, 'gas produced,' is an ambiguous term, in that it does not say in the lease, on the face of the lease, and that's what we are looking at, as to whether or not it refers to injected gas or native gas or both." Commenting on the last clause, PGandE's counsel observed that defense counsel had pointed to "the very final paragraph where it says that paragraph 15 shall not apply to injected gas in Parcels I and II. They, therefore, infer—they make an inference that, since it doesn't say III, that paragraph 15 does not apply to Parcel III. . . . In this particular situation, there will be an offer of proof that the parties, Mr. Zuckerman and the known parties on behalf of PG&E, each believed that the injected gas was solely on Parcel No. 1. Neither party ever contemplated that the injected gas was in Parcel III." Defense counsel responded that he "wasn't inferring anything at all from the last clause of paragraph 15. . . . I don't think it makes any difference whether the clause is in there or not in there for the purposes that we are talking about today." (Ibid.) PGandE then offered to prove that at the time of the 1963 agreement neither party believed the injected gas would intrude into parcel III. PGandE's counsel said: "Going back to the point raised by defense counsel, that evidence of undisclosed intent of parties is not permissible to determine what was meant when the contract was entered into, as part of our offer of proof, and I should have also included, there are numerous documents which our PG&E filed, and copies have been made available to defendant. [¶] Those documents show that there was correspondence between Mr. Zuckerman and Mr. Johns of PG&E, that the descriptions of the parcels, Parcels I, II and III, were agreed upon by the parties before ever entering into the agreement, that all of the parties understood that as Parcels I, II and III. There were certain items which we found in each of those parcels, and Mr. Johns and Mr. Zuckerman clearly set out that Parcel I was the storage area. [¶] This is also extrinsic evidence showing what was the intent of PG&E at the time. It's not an undisclosed intent of the parties. This was

an intent of both parties, discussed between both parties, agreed to by both parties as to what this contract was supposed to be about. [¶] And there has also been testimony from Mr. Zuckerman on that issue to support our understanding of what these documents in fact purport, what were the negotiations between the parties at the time that they drew up the contract, and as an offer of proof, we have numerous documents, Your Honor, going to that, and also documents wherein PG&E indicated that the reason they were entering into this lease was to permit Mr. Zuckerman to drill in the deep zones in Parcel III, because that's where they felt there may have been a possibility of some further gas and not in any storage zone area. [¶] The reason they permitted drilling in Parcel III is perhaps there was—there was going to be productive gas at the 10,000-foot level or so, or 12,000-foot level, wherever they would find the winter sands, and this is all part of the offer of proof going to what was intended by the parties when they drew up this lease." Despite this offer of proof the court ruled that the contract was unambiguous, and that it required PGandE to produce and pay royalties upon gas from parcel III without regard to whether it was native or injected gas.

The court's ruling constituted reversible error. Under the California parol evidence rule a party is entitled to introduce any extrinsic evidence which may aid in an interpretation of a written contract. (Code Civ. Proc., § 1856, subd. (g); see generally, 2 Witkin, Cal. Evidence (3d ed. 1986) Documentary Evidence, § 960, p. 908.) The test is not whether the agreement appears to the court to be clear and unambiguous on its face, but whether the extrinsic evidence is offered to support a meaning to which the language of the instrument is reasonably susceptible. (Pacific Gas & E. Co. v. G.W. Thomas Drayage etc. Co. (1968) 69 Cal. 2d 33, 37, 69 Cal. Rptr. 561, 442 P.2d 641.) As Jefferson notes, this holding makes "extrinsic evidence admissible to interpret or explain the meaning of a written

instrument even though, on its face, the written instrument appears not to lend itself to the meaning contended for by the party-proponent of the extrinsic evidence because of the instrument's seemingly plain and unambiguous language." (2 Jefferson, Cal. Evidence Benchbook (2d ed. 1982) Parol Evidence Rule § 32.2, p. 1139.) "Accordingly, rational interpretation requires at least a preliminary consideration of all credible evidence offered to prove the intention of the parties." (Pacific Gas & E. Co. v. G.W. Thomas Drayage etc. Co., supra, 69 Cal. 2d at pp. 39-40, fn. and citations omitted, 69 Cal. Rptr. 561, 442 P.2d 641.) If, after considering the evidence, the court concludes that it does not support a meaning to which the agreement is reasonably susceptible then the evidence may be rejected. (Ibid.) But it is reversible error to refuse to consider the evidence based upon a conclusion that the agreement is clear on its face. (Ibid.) Here the trial court erroneously refused to even provisionally consider the extrinsic evidence because of its conclusion that the agreement was clear on its face and from that error reversal must follow.

Defendants insist, however, that the court could properly exclude PGandE's extrinsic evidence under the rule that precludes evidence of an undisclosed intention from controverting the objective meaning of a contract. That rule simply prohibits a party from saying one thing but meaning another. (See Brant v. California Dairies, Inc. (1935) 4 Cal. 2d 128, 133, 48 P.2d 13.) It does not preclude a party from introducing extrinsic evidence to establish what the mutually understood meaning of the contract was. As noted in Pacific Gas & E. Co. v. G.W. Thomas Drayage etc. Co., supra, words do not have absolute and constant referents; the meaning of particular words or groups of words varies with the verbal context and surrounding circumstances and purposes, and the education and experience of the parties. (69 Cal. 2d at p. 38, 69 Cal. Rptr. 561, 442 P.2d 641.) While a party may not testify to his undisclosed subjective intent in entering into an agreement, the rule does not preclude admission of evidence of

the surrounding circumstances, usage and custom in the industry, negotiations and discussion, or any other extrinsic evidence which may shed light on the mutual intention of the parties. (Ibid.; Mission Valley East, Inc. v. County of Kern (1981) 120 Cal. App. 3d 89, 98, 174 Cal. Rptr. 300.) PGandE's offer of proof clearly establishes that it was this latter type of evidence and not a mere undisclosed subjective intent that it sought to introduce. It was error to exclude such evidence without at least provisionally considering it.

Nor can we accept the claim that PGandE failed to make an adequate offer of proof. Normally the exclusion of evidence will not be considered on appeal unless the substance, purpose and relevance of the excluded evidence was made known to the trial court. (Evid. Code, § 354, subd. (a).) But "[w]here an entire class of evidence has been declared inadmissible or the trial court has clearly intimated it will receive no evidence of a particular class or upon a particular issue, an offer of proof is not a prerequisite to raising the question on appeal, and an offer, if made, may be broad and general." (Beneficial etc. Ins. Co. v. Kurt Hitke & Co. (1956) 46 Cal. 2d 517, 522, 267 P.2d 428; Montez v. Superior Court (1970) 10 Cal. App. 3d 343, 351, 88 Cal. Rptr. 736. See Evid. Code, § 354, subd. (b).) This is precisely the type of case in which a complete offer of proof is unnecessary. The specific reason for defendants' motion was to "short-circuit" the need to have witnesses appear on the issue. In response to defendants' aggressive but misguided advocacy the court misapplied the parol evidence rule and ruled that extrinsic evidence would not be received in aid of interpretation of the contract. PGandE's offer of proof was adequate under these circumstances. (Montez v. Superior Court, supra, 10 Cal. App. 3d at p. 351, 88 Cal. Rptr. 736; see Pacific Gas & E. Co. v. G.W. Thomas Drayage etc. Co., supra, 69 Cal. 2d at p. 36, fn. 1, 69 Cal. Rptr. 561, 442 p.2d 641.)

In any event, the trial court erred in concluding that the

agreement was clear and unambiguous on its face. The agreement was negotiated because the older agreement did not require PGandE to explore for additional natural oil and gas reserves on McDonald Island for so long as it operated the storage reservoir and did not permit defendants to do so. Defendants, however, believed that there may have been additional undiscovered oil and gas native to the property. The clear intent of the agreement was to permit such exploration while maintaining the integrity of the storage facility. Throughout the agreement numerous provisions are found to protect the integrity of the storage facility and PGandE's right to gas injected and stored there. In every instance throughout the agreement where the parties referred to the extraction of injected gas from the storage reservoir they used the word "withdrawn" or "withdrawal" while the word "produced" was restricted to reference to extraction of newly discovered native gas. If the word "produced" in paragraph 15 refers to the extraction of injected gas from the storage reservoir, then it is the only instance in a 40 page agreement where it was so used.

As we have noted, the final provision in paragraph 15 provides: "The provisions of this Paragraph 15 shall not apply to any gas which has been injected and stored in and thereafter withdrawn from parcels I or II." All of the injected gas was injected into and stored in parcel I. The operation of the Zuckerman-Henning well on parcel III caused the gas to migrate into parcel III, and thus to be "withdrawn" from parcel I. This would make it appear that the royalty provisions of paragraph 15 were not intended to apply to injected gas. The trial court held just the opposite. It concluded with respect to the final provision of paragraph 15 that it "is quite clear that Parcel III was not intended to be included in that exclusion. . . ." That provision cannot be so easily disregarded. In other parts of the agreement PGandE was given the sole and exclusive right to inject, store, and withdraw gas from parcels I and II, free of any royalty interest. Paragraph 15 deals with the

royalties to be paid to defendants for gas produced from wells on parcel III. Unless the last provision of that paragraph was intended to insure that injected gas would be free from those royalty interests it would have no meaning whatsoever. It is not to be lightly assumed that the parties to a contract included provisions which have no meaning. It is a general rule of construction that an interpretation of a contract should, where possible, give effect to every provision. (Civ. Code. § 1641; Moore v. Wood (1945) 26 Cal. 2d 621, 630, 160 P.2d 772; General Ins. Co. v. Truck Ins. Exch. (1966) 242 Cal. App. 2d 419, 426, 51 Cal. Rptr. 462.) Moreover, since that final provision of paragraph 15 is a limiting provision and was placed within paragraph 15 it must be construed as a limitation upon the rights granted in paragraph 15. As such it can only have been intended to exclude injected gas from the royalty provisions of paragraph 15.

The interpretation of a written agreement is a question of law. Where there is no extrinsic evidence, or the extrinsic evidence is not conflicting (and therefore poses no question of credibility), then a reviewing court must make an independent determination of the meaning of the agreement. (Parsons v. Bristol Development Co. (1965) 62 Cal. 2d 861, 866, 44 Cal. Rptr. 767, 402 P.2d 839; Blumenfeld v. R. H. Macy & Co. (1979) 92 Cal. App. 3d 38, 44, 154 Cal. Rptr. 652.) If we were to construe the agreement on its face without reference to extrinsic evidence we would reject the trial court's interpretation and find in favor of PGandE since it seems clear on the face of the agreement that the parties did not intend that defendants would acquire any rights in the stored gas. But in doing so we would be engaging in the same error made by the trial court. The trial court's ruling precluded introduction of extrinsic evidence by PGandE and made it unnecessary for defendants to introduce such evidence. Since extrinsic evidence must be considered before it can be determined whether it supports a meaning to which the agreement is reasonably susceptible, the matter must be remanded so that both

PGandE and defendants will have the opportunity to produce any evidence they believe supports their interpretation of the agreement.

Two further points must be addressed. Defendants contended, and the trial court found, that PGandE is estopped from denying that it must pay defendants a perpetual royalty on injected gas which can be extracted through the Zuckerman-Henning well. The record does not support the application of estoppel in that manner. Evidence Code section 623 provides that "Whenever a party has, by his own statement or conduct, intentionally and deliberately led another to believe a particular thing true and to act upon such belief, he is not, in any litigation arising out of such statement or conduct, permitted to contradict it." Estoppel then is an equitable doctrine which prevents a party from profiting from the detriment he induced another to suffer. "The doctrine acts defensively only. It operates to prevent one from taking an unfair advantage of another but not to give an unfair advantage to one seeking to invoke the doctrine." (Peskin v. Phinney (1960) 182 Cal. App. 2d 632, 636, 6 Cal. Rptr. 389.) The essence of an estoppel is that a party who is actually and permissibly ignorant of the facts has been induced to act to his detriment by representations or concealment by a party with superior knowledge who intended to induce action. (See 7 Witkin, Summary of Cal. Law (8th ed. 1974) Equity, § 132, pp. 5351-5352.) Defendants argue that from 1967 to 1980 PGandE extracted gas from the Zuckerman-Henning well and paid royalties upon it although it was aware that the deposit was connected to the storage reservoir and that at least some of the gas extracted was injected rather than native gas. Defendants conclude from this that PGandE should be estopped from refusing to continue to pay royalties on injected gas in perpetuity. This is not a defensive use of the estoppel doctrine. We find no detrimental reliance suggested by the record and no basis whatsoever for the application of an estoppel in this manner.

We do agree with the trial court, however, that PGandE cannot be permitted to recover excess royalties that it did pay to defendants. The record established that during the period PGandE was extracting gas and paying royalties on the Zuckerman-Henning well it paid royalties on more gas than was originally in place in the deposit, and thus in fact paid royalties on some injected gas. PGandE made those payments with an awareness of the facts, and defendants accepted the payments in good faith and cannot be made to refund them at this time.[10]

Finally, the trial court found that PGandE abandoned the gas in place under parcel III as of August 1, 1980, and awarded the sum of $2,938,000 to defendants as an alternative to the mineral interest/breach of contract damages. There is not a scintilla of evidence in the record to support an abandonment. Abandonment of property requires both nonuser and the intent to abandon. (Gerhard v. Stephens (1968) 68 Cal. 2d 864, 889, 69 Cal. Rptr. 612, 442 P.2d 692.) Before an abandonment may be found it is necessary to establish nonuser accompanied by unequivocal and decisive acts showing an intent to abandon. (Id., at p. 890.) In this case PGandE was placed in a difficult position when it became obvious that the storage reservoir was not limited to the confines of parcel I as had been believed. But

[10] Defendants also suggest that the PGandE's action supports the interpretation of the contract found by the trial court. The subsequent conduct of the parties to a contract may be considered in interpreting the contract. (1 Witkin, Summary of Cal. Law (8th ed. 1973) Contracts, § 527, p. 449.) Of course, PGandE offered a well supported and reasonable explanation for why it paid the royalties from 1967 to 1980, which would diminish the value of that conduct as evidence for defendants' position. Nevertheless, this is not a question we must resolve. The subsequent conduct of the parties to a contract is one of a variety of permissible types of extrinsic evidence which may be considered in interpreting a contract. Since the trial court precluded PGandE from offering its extrinsic evidence it would be improper and unfair to consider extrinsic evidence on appeal without the opportunity for a retrial.

everything PGandE did both before and after was done to protect its interests in the storage reservoir and the injected gas. The finding of abandonment is without support in the evidence and must be reversed.

In summary, it appears that the 1963 agreement was negotiated in order to permit the exploration and production of native gas in McDonald Island outside of the storage reservoir while protecting PGandE's storage rights. Pursuant to that agreement PGandE explored for and discovered a deposit of native gas in parcel III which, it turned out, was connected to the storage reservoir. PGandE produced and paid for all of the native gas which was within the deposit. We conclude that the law of capture does not give defendants mineral interests in the injected and stored gas in the reservoir. We also conclude that the trial court erred in concluding that the 1963 agreement gave defendants such rights on its face and as a matter of law. We reverse the judgment and remand so that the parties can produce any extrinsic evidence they believe supports the interpretation they urge. In view of this resolution it is unnecessary to consider whether the trial court's assessment of the value of defendants' mineral interests, based entirely upon the valuation of Mr. Paschall, is supported by the evidence and we express no opinion on that question.

III

SEVERANCE DAMAGES

The trial court awarded severance damages in the amount of $358,000. This amount represented the acceptance without question of the testimony of Mr. Paschall. Paschall testified that in the event wildcat wells were to be drilled for the purpose of exploring the earth beneath the condemned storage reservoir they would have to be slant drilled from outside the property. He estimated that slant

drilling would cost approximately $179,000 more than straight drilling to reach a depth of 10,000 to 12,000 feet, and he concluded that the additional cost of two wells to that depth would represent severance damages. The trial court awarded damages for two such wells as severance damages.

We agree with PGandE that the award for severance damages cannot stand. A condemnation award cannot be based upon a speculative projected use for the property claimed by the owner. (City of Los Angeles v. Retlaw Enterprises, Inc. (1976) 16 Cal. 3d 473, 488, 128 Cal. Rptr. 436; County of Los Angeles v. Bean (1959) 176 Cal. App. 2d 521, 528, 1 Cal. Rptr. 464.) In Sacramento, etc. Drainage Dist. ex rel. State Reclamation Bd. v. Reed, supra, 215 Cal. App. 2d at page 70, 29 Cal. Rptr. 847, this court reversed an award of severance damages because it was based upon "a conjectural buyer's conjectural fears of conjectural flooding created by conjectural levees." The award for severance damages here is equally conjectural. There is nothing in the record to suggest that the property is suited to further oil and gas exploration,[11] that any potential oil or gas deposit at a depth beneath the condemned storage reservoir could not be produced from wells outside the condemned area, that it would be economically or geologically advisable to conduct such exploration, or that if exploration were conducted it would be defendants rather than an oil and gas lessee that would bear the burden of any added costs of drilling. The award for severance damages is totally speculative and cannot stand.

[11] In fact, the condemned parcel has already been explored for oil and gas to a depth below 10,000 feet subsea in the initial exploratory drilling conducted with the Zuckerman-Henning No. 1 well. The negative results experienced in that exploration would indicate that further exploration is unwarranted, and nothing in the record would suggest otherwise.

IV

PREJUDGMENT INTEREST, LITIGATION EXPENSES, ATTORNEYS' FEES AND SANCTIONS

PGandE contends that the trial court erred in awarding defendants prejudgment interest on their awards. Defendants have not responded to this contention. The judgment provides for the payment of interest at the legal rate on the award for the storage rights from August 1, 1980, and from February 22, 1982, on the mineral rights. At the time judgment was entered in this case Code of Civil Procedure section 1263.310 provided: "The compensation awarded in the proceedings shall draw legal interest from the earliest of the following dates: [¶] (a) The date of entry of judgment. [¶] (b) The date the plaintiff takes possession of the property. [¶] (c) The date after which the plaintiff is authorized to take possession of the property as stated in an order for possession." (Stats. 1975, ch. 1275, § 2, p. 3461.) Although PGandE applied for an order of possession in 1982, its application was denied. Since PGandE neither took nor had the right to take, possession of defendants' property before the entry of judgment, the statute requires that interest run from the date of the entry of judgment. The award of prejudgment interest was therefore erroneous and must be reversed.

The trial court awarded defendants their litigation expenses, but denied an award of attorneys' fees. Defendants filed a cross-appeal from the order denying attorneys' fees, and have moved for sanctions against PGandE for a frivolous appeal. Since we find that the judgment must be reversed on all elements of damages awarded by the trial court the award of litigation expenses must be reversed and it is unnecessary to consider at this time whether attorney's fees should be awarded. Since we find the appeal meritorious we obviously deny the request for sanctions.

The judgment is reversed and the cause is remanded to the trial court for further proceedings in accordance with

the views expressed in this opinion. PGandE shall recover costs.

Concur: BLEASE, Acting P.J., and SIMS, J.

MODIFICATION OF OPINION AND DENIAL OF REHEARING

BY THE COURT.

On petition for a rehearing the defendants contend that our decision erroneously awarded costs to PGandE. The general rule on appeal is that the prevailing party is entitled to costs. (Cal. Rules of Court, rule 26(a).) However, with respect to condemnation actions Code of Civil Procedure section 1268.720 provides: "Unless the court otherwise orders, whether or not he is the prevailing party, the defendant in the proceeding shall be allowed his costs on appeal. This section does not apply to an appeal involving issues between defendants." This statutory rule favoring an award of costs to the defendant in an eminent domain action has a constitutional origin. The constitutional requirement of just compensation dictates that the defendant's award should not be diminished by the costs which attach to the process of ascertaining the award. (See City of Los Angeles v. Ricards (1973) 10 Cal. 3d 385, 390-391; In re Redevelopment Plan for Bunker Hill (1964) 61 Cal. 2d 21, 68-71; Sacramento Drainage Dist. ex rel. State Rec. Bd. v. Reed (1963) 217 Cal. App. 2d 611, 612-613.) There are, to be sure, circumstances where an award of costs to the condemner is permissible. (See Yolo Water etc. Co. v. Edmands (1922) 188 Cal. 344, 346-347 [appeal wholly the fault of the defendant for causelessly insisting the plaintiff continue an action it desired to dismiss]; Oakland v. Pacific Coast Lumber Co. (1916) 172 Cal. 332, 335-337 [costs may be awarded to plaintiff where the defendant unsuccessfully appeals]; Los Angeles etc. Ry. Co. v. Rumpp (1894) 104 Cal. 20, 23-24 [defendant required to pay costs, pursuant to statute, for a second trial granted on her ap-

plication where the award was less than in the first trial].) And a court may deny particular items of costs where they are not incurred reasonably and in good faith. (City of Los Angeles v. Ricards, supra, 10 Cal. 3d at p. 390; San Francisco v. Collins (1893) 98 Cal. 259, 263.) But in the absence of such circumstances the constitutional requirement of just compensation is a limitation upon the phrase "Unless the court otherwise orders" in Code of Civil Procedure, section 1268.720. Although, as PGandE points out, this action involved a cross-complaint for such things as nuisance, breach of lease, trespass and estoppel, the primary issues, both at trial and on appeal, involved the amount PGandE must pay to condemn defendants' property. Accordingly defendants are entitled to their costs even though PGandE is the prevailing party. The opinion is modified to award costs to defendants.

Defendants also contend that our decision was erroneous with respect to prejudgment interest. Code of Civil Procedure section 1268.310 provides that interest on a condemnation award accrues from the earliest of the date of judgment, the taking of possession, or an order authorizing the taking of possession. In its judgment the trial court held that PGandE was required to pay royalties to defendants for so long as it operates the storage reservoir. In view of this finding it could not be said that PGandE took possession of the property since the payment of royalties entitled PGandE, as lessee, to the possession and use of the property, and the receipt of the emoluments of ownership by defendants precludes a finding they were deprived of possession. Accordingly, an award of prejudgment interest was improper on the findings of the trial court. However, we have reversed the judgment holding that PGandE is required to pay a continuous royalty to defendants. If PGandE prevails on this issue upon retrial, then it may be held to have taken possession when it ceased paying royalties to defendants, since it was storing gas in the condemned parcel at that time. Our opinion on appeal

is without prejudice to the trial court to determine the date PGandE actually took possession of the condemned property in light of its other findings upon retrial.

None of defendants' other contentions on petition for rehearing warrants discussion. The opinion is modified to provide defendants, and not PGandE, shall recover their costs on appeal. The petition for a rehearing is denied. (CERTIFIED FOR PUBLICATION.)

FOR THE COURT: BLEASE, Acting P.J., SPARKS and SIMS, JJ.

DISCUSSION NOTES

Storage of Gas: Underground Storage—Condemnation—Valuation—Escape of Gas Injected for Storage—Title to Gas.

Oil and Gas Leases: Allowance of Extrinsic Evidence in Interpretation.

Not discussed.

R.C.M.

SHEWMAKE et al. v. BADGER OIL CORPORATION

United States District Court
District of Colorado
February 27, 1987—Civ. A. No. 86-K-1355
654 F. Supp. 1184

Oil and Gas Leasing: Overriding Royalty Interest—Assignment—Third-Party Beneficiary.

Plaintiffs were employees of Fuelex. They allege that, before leaving Fuelex's employ, they were granted an overriding royalty interest in an oil and gas lease. Fuelex assigned its interests to Badger Oil Corp., and plaintiffs allege that they were third party beneficiaries to this assignment. Held: Defendant's motion for summary judgment was granted under two theories: 1) if plaintiffs were third party beneficiaries to the assignment, then res judicata barred their action due to completed litigation on the same matter between Fuelex and Badger; 2) if plaintiffs were not third party beneficiaries, they cannot prevail, because Badger owed them no duty in implied contract simply because they were employees of Fuelex and had financial interest in certain provisions of the agreement.

MEMORANDUM OPINION AND ORDER

KANE, District Judge.

This diversity action is before me on defendant's motion for summary judgment. Plaintiffs claim in tort and as third party beneficiaries of an assigned oil lease allegedly breached by defendant.

Plaintiffs Shewmake and Warmath were geologists and employees of Fuel Exploration, Inc., also known as "Fuelex." In May of 1981, during the period of plaintiffs' employment, Fuelex entered into an oil and gas lease with landowners Joseph and Maxine Fazzio. The lease provided if no well was commenced on a specific acreage of Fazzio property in Utah within three years, the lease would

KEASLER v. NATURAL GAS PIPELINE CO. OF AMERICA

United States District Court
Eastern District of Texas
June 30, 1983—Civ. A No. M-79-13-CA
569 F. Supp. 1180

Storage of Gas: Fraud in Acquisition of Rights in Depleted Reservoir—No Conversion of Realty-Type as Opposed to Personalty-Type Interests—Rights Acquired by Storage Easement.

In a class action the court indicated bordered on frivolous Plaintiffs, landowners, and/or royalty owners in the North Lansing gas field which was at or nearly at depletion, contended that Defendant gas pipeline company's acquisition of storage rights through easement agreements, royalty agreements, and easement and royalty agreements was induced by fraudulent non-disclosures accomplished through (1) not predicting possible future field prospects (2) lump sum payments without intemization, (3) making "non-negotiable" offers, then compromising is some instances, and (4) overstating the extent of the conveyances obtained. All of these claims are examined and found without merit. In addition, parties who signed storage easements only contend they did not convey their interests in remaining (but unrecoverable) native gas and hydrocarbons in place, claiming conversion of these. The court found (1) the remaining minerals in place were realty, not personalty, and thus not susceptible of conversion; (2) there was no showing the pipeline company had withdrawn more than it injected; and (3) anyway, the easement agreements as drawn sold the right to remove gas and other hydrocarbons, including gas condensate, to the pipeline company.

MEMORANDUM OPINION AND FINAL JUDGMENT

JOE J. FISHER, District Judge.

In 1974, the Defendant, Natural Gas Pipeline Company of America (Natural) concluded a search for a natural gas storage reservoir with its decision to acquire the Rodessa-Young formation of the North Lansing field in Harrison

County in east Texas. Natural purchased rights in the field and to the surface, sufficient, it claims, to give it use of the virtually depleted field as a storage reservoir.

The Plaintiffs in this class action, all having been paid by Natural for some interest, challenged the rights of Natural in the field. Inter alia, the Plaintiffs allege that Natural did and continues to commit conversion, taking hydrocarbons for which it did not pay. Moreover, Plaintiffs claim that such hydrocarbons and storage rights as Natural bought were obtained by fraud and deceitful misrepresentation. Plaintiffs allege violations of: section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1976); S.E.C. rule 10(b)(5), 17 C.F.R. 240, 10(b)–5; the Texas fraud statute, Tex. Bus. & Com. Code, section 27.01 (Vernon 1968 & Supp. 1982); and common law fraud, as well as conversion.

The court has jurisdiction of the case by virtue of 28 U.S.C. 1331 and 1332 (1976). The court certified the class in November, 1979, and the parties tried the case to the court in November, 1982.

I. UNDERLYING FACTS

Circa 1970, Natural sought an underground storage facility near its Gulf coast trunkline. Discussions with Atlantic Richfield Co. directed Natural to the North Lansing field near an existing Natural pipeline. The field had been producing since 1941. Two formations in the field, the Rodessa-Young and the lower Petit zone, were nearly depleted. Some wells there had since ceased to produce in paying quantities, while those that remained had marginal output. No wells were expected to produce beyond 1975. Natural determined to buy the right to use the depleted formations to store pipeline gas so as to meet peak demands.

After buying the working interests from the field's

operators, Natural obtained the requisite bureaucratic approval from the Texas Railroad Commission and the Federal Power Commission. As necessary, Natural secured surface rights for construction of new above-ground equipment. From every mineral owner of the proposed storage area, Natural bought "easement rights" in the formations. Moreover, Natural paid the owners of royalty interests (pursuant to still producing leases) in satisfaction of royalty expectations unfulfilled when Natural stopped production in the field. Natural apparently intended to compensate the lessors for all hydrocarbons remaining in the formations, and it appears that they accepted the payments as such. In doing so, however, Natural purchased the lessors' royalty interests, as well. Thereafter, Natural shut down production and began storing gas. At that time, the leases terminated and the reversionary rights of the mineral estate owners rematerialized.

The payments to the mineral estate owners were in proportion to the area of their respective estates. Natural paid the Dallas consulting firm of DeGolyer & McNaughton to make an independent reservoir study and estimate of volumes remaining therein. Working interest owners received payment for the volume of gas estimated to remain in their tracts, as did the lessors, as royalty interest owners.

Natural predicated payments to the lessors on: (1) the maximum lawful rate for interstate gas; (2) applied to the higher of (a) the DeGolyer & McNaughton estimated volume, and (b) the in-house estimate of Natural. According to Natural, it paid not only for recoverable gas remaining, but non-recoverable gas, as well. Moreover, most of the royalty interest owners received a higher rate than the existing production contracts called for.

Natural contends that, in light of the imminent depletion of the field and the end to royalty income that would bring, the Plaintiffs were substantially overpaid for their

interests. It appears to the court that Natural chose to make "generous" offers in order to promptly and without litigation obtain the right to store gas in the formations. Natural did not, however, reckon on the tenacity and ingenuity of the Keaslers.

II. COMPLAINTS OF THE PLAINTIFFS

The Keaslers owned substantial acreage within the North Lansing field, and retained the mineral rights thereto. Natural negotiated with and paid them and other owners for their royalty interests, acquiring all their rights in the mineral leases then existing. Natural also bought an easement which gave it extensive rights in and to the formations. Some five years later, Plaintiffs brought this action. Plaintiffs previously alleged that they were paid too low a rate for the gas, paid for too low a volume of gas, not paid at all for "liquid hydrocarbons," and, in some cases, not paid for gas made recoverable by the storage operations. Most of these theories were later abandoned in favor of the fraud claims made in the final complaint.

The final amended complaint has two discernable components: fraud, perpetrated on all the grantors of royalty and easement agreements; and conversion, as to grantors of easements in non-producing (i.e., depleted) zones. The Plaintiffs fall into three conceivable sets:

(1) parties to easement agreements only;

(2) parties to royalty agreements only; and

(3) parties to both easement *and* royalty agreements.

As a practical matter, it appears that all members of set (2) are subsumed within set (3). The conversion claim is made only by those in the first set. The fraud claims apply to all sets above.

As noted above, two types of agreements are involved:

(1) the royalty payment agreements, wherein Natural purchased from Plaintiffs "all of their right, title, and interest in all existing oil and gas leases in the north Lansing field, Harrison County, Texas effective January 1, 1974," and

(2) the gas storage easement agreements, wherein Natural bought the potentially perpetual right "to introduce natural gas into the Rodessa formation . . . to store . . . and retain the possession of gas . . . and to remove such gas, together with any . . . hydrocarbons, or other substances from the storage reservoir and the exclusive right . . . to use, hold and occupy the storage reservoir for all such purposes." Moreover, Plaintiffs agreed that "any gas [recovered by any reasonable method '(including water, water vapor and hydrocarbons or other substances)'] shall be considered as being the personal property of Natural."

By the terms of the complaint, it is clear that the Plaintiffs do not deny that by accepting "royalty" payments they sold Natural all their interest in outstanding leases. Neither do Plaintiffs directly challenge the extent of the conveyance made in the easement agreements by the lessors of still producing acreage. That is, Plaintiffs concede that he who signed *both* agreements conveyed all his relevant interests in the mineral estate. But parties to only the storage easement agreement, who were not paid for an interest in existing oil and gas leases because none then existed, argue that the easement agreement, standing alone, is insufficient to convey their interest in remaining (but unrecoverable) gas and hydrocarbons in place. Finally, all the Plaintiffs challenge the *legality* of both agreements, charging fraud in their inducement.

A. CONVERSION

The Plaintiffs claim: that Natural "appropriated to its own use natural gas and gas condensate in place belonging to [certain Plaintiffs, and] exercised complete control and

dominion over the Field and all natural gas and gas condensate therein . . ." Moreover, Plaintiffs assert there is "no basis in law by which [Natural] could justify its possession and use . . ."

To the extent that the gas in place serves as "cushion gas" in the reservoir, it has arguably been put to "use" by Natural. Natural might also be said to "exercise complete control and dominion over the Field" and the hydrocarbons therein by virtue of its ongoing storage operations. Although the familiar phrases of dominion and control appear to apply to Natural's activities, a claim of conversion is not automatically established by their invocation.

Oil and gas *in place* are, by long established rules of Texas property law, a part of the realty or corpus of the land. Texas Co. v. Daugherty, 107 Tex. 226, 176 S.W. 717 (Tex. 1915). The minerals do not become personalty until removed from the soil. Bracewell v. Fair, 638 S.W. 2d 612 (Tex. Civ. App. 1982—no writ.); Humble Oil & Refining Co. v. West, 508 S.W. 2d 812 [48 O&GR 516] (Tex. 1974), cert. denied 434 U.S. 875, 98 S. Ct. 224, 54 L.Ed. 2d 154 (1977); W.B. Johnson Drilling Co. v. Lacy, 336 S.W. 2d 230 [13 O&GR 311] (Tex. Civ. App. 1960—no writ.); Stephens v. Stephens, 292 S.W. 290 (Tex. Civ. App. 1927—writ dism'd).

Whereas trover lies for an unauthorized severance from land of the minerals, Bender v. Brooks, 103 Tex. 329, 127 S.W. 168 (Tex. 1910), one cannot commit conversion of realty. Branham v. Prewitt, 636 S.W.2d 507 (Tex. Civ. App. 1982—no writ); Rodriguez v. Dipp, 546 S.W. 2d 655 (Tex. Civ. App. 1977—writ ref'd n.r.e.). Necessarily, there can therefore be no conversion of oil and gas in place. Choice v. Texas Co., 2 F. Supp. 160 (N.D. Tex. 1933).

To prevail, Plaintiffs must prove that Natural *removed* hydrocarbons that belong to them. The court notes that this set of Plaintiffs owned non-producing, i.e., already

depleted, tracts in which unrecoverable hydrocarbons remain. Into their depleted tracts Natural injects gas, stores and then removes it. The court concludes that, absent a showing that Natural has to date withdrawn more gas than it has injected, there has been no severance of gas from the realty. Plaintiffs offered no such evidence.

Plaintiffs claim, as well, that Natural removed substantial quantities of liquid hydrocarbons that belong to them. It is undisputed that liquids, including hydrocarbons, are extracted from the withdrawn storage gas following its removal from the reservoir. Natural dries the gas after, rather than before, storage in order to remove any additional water vapor and impurities that mix with the stored gas. The evidence showed that Natural pays to have the extracted condensation, including hydrocarbons, disposed of. Indeed, the extracted condensation appears to be more a liability than an asset. Nonetheless, Plaintiffs claim that Natural's "conversion" of the extracted "gas condensate" damaged them in an amount exceeding 14 million dollars.

Laboratory reports introduced in evidence showed that Natural derived no net gain in B.T.U. content between the gas injected and that withdrawn, further indication that Natural took nothing of value from the reservoir itself. Of course, benefit to the alleged wrongdoer is not a condition of conversion. Fenberg v. Fenberg, 307 S.W. 2d 139 (Tex. Civ. App. 1957—no writ). Rather, it is the owner's loss which is the controlling element. Bradley v. McKinzie, 226 S.W. 2d 458 (Tex. Civ. App. 1950—no writ). Assuming, arguendo, that Plaintiffs could show that Natural removed hydrocarbons in addition to the storage gas, to prove a loss they must first show their ownership of the minerals in place.

In determining the ownership of the minerals, the court looks to the written agreement between the parties, an

agreement drawn and executed in accord with the rules governing conveyances of realty in Texas. See, e.g., Norsworthy v. Hewgley, 234 S.W.2d 126 (Tex. Civ. App. 1950—writ ref'd); Texas Co. v. Daugherty, 107 Tex. 226, 176 S.W. 717 (Tex. 1915).

The "Gas Storage Easement" (the Agreement), duly signed, acknowledged, and delivered, is the dispositive instrument. Interpreting the Agreement in the light least favorable to its author, Natural, the court finds that by plain language the Agreement manifests the intent of the parties to convey control of the mineral estate within the Rodessa formation. Plaintiffs unequivocally sold to Natural the right, inter alia, to remove not only gas, but "any water, water vapor, hydrocarbons, or other substances . . ." as well. Moreover, in another clause, Plaintiffs agree that any gas which migrates beyond the reservoir—"including water, water vapor and hydrocarbons or other substances"—and is recovered by Natural, "shall be considered as being the personal property of Natural." Therefore, even assuming that which Plaintiffs did not prove: that previously unrecoverable hydrocarbons are being severed by the Natural storage process, the court finds that Plaintiffs did convey by valid contract the right to remove such substances.

The conversion complaint of Plaintiffs is without merit, amounting to little more than an attack on the adequacy of consideration paid. It is irrelevant that this set of grantors received no "royalty" payments from Natural. In exchange for such payments, the lessors conveyed only their royalty interest under existing leases. When Natural stopped production, its royalty interest terminated along with the leases. That event left all the easement grantors in the same position: possessing reversionary rights in mineral estates without mineral leases, but burdened by the gas storage easement. The court concludes that the Agreement was sufficient to convey title, of all the grantors, to any minerals removed incidental to Natural's storage operation.

B. FRAUD

As explained above, Plaintiffs seek to recover for fraud and misrepresentation under three theories: the federal securities law, the Texas fraud statute, and the common law. While the particular elements of each theory vary somewhat prove, the complaint alleges common acts of misrepresentation. The court's analysis of the culpability of Natural's acts will therefore precede discussion of Plaintiffs' legal theories.

The deceitful misrepresentations upon which Plaintiffs claim to have relied fall into four sets:

(1) Not telling Plaintiffs about "likely" *future* events, to wit,

(a) "future prospects" for enhanced gas production in depleted fields;

(b) Federal Power Commission consideration of "significant increases" in interstate gas prices;

(c) the likely production of "gas condensate" from the injection and withdrawal of storage gas; and

(d) the possibility the field might produce longer than expected;

(2) Offering lump sum payments to Plaintiffs for their interests without having itemized all the crucial facts, such as,

(a) the price paid per Mcf;

(b) the volume of gas in place purchased;

(c) the methods used to estimate the minerals remaining in place; and

(d) the "real value" of the hydrocarbons being purchased;

(3) Negotiating with fraudulent or deceptive tactics, for example,

(a) styling the offer "non-negotiable" and uniform, then compromising with some, but not all, of the offerees;

(b failing to tell all the offerees it had compromised with some;

(c) tendering a check as payment for the "gross value" of all natural gas and gas condensate in place, producible and nonproducible; and

(4) Overstating the extent of the grantors' conveyances to Natural, i.e.,

(a) claiming to have bought all instead of some of the gas remaining in place;

(b) claiming to have bought condensate when it did not; and

(c) claiming to have bought the "non-recoverable gas in place" from owners of non-producing tracts.

Plaintiffs claim that had Natural shared with them all of its "knowledge" about: the field, the negotiations, the contracts, and the future, Plaintiffs would not have sold their interests.

Having reviewed the complaint, the record, the exhibits, and briefs filed by the parties, the court is unable to perceive any culpable acts of misrepresentation or fraud. As a general rule, fraud consists of either a false representation of a *past* or *present* material fact, or a false promise to do some *future* act. See, e.g., Tex. Bus. & Com. Code Ann. Sec. 27.01(a), (Vernon's 1968 & Supp. 1982); Restatement (Second) of Contracts, sections 159 et seq. (1981); Restatement (Second) of Torts, sections 525 et seq. (1977).

The concept of fraud includes acts of nondisclosure. Id. at section 550. To the extent the law requires disclosure, however, it is fact, not speculation as to the future, that must be disclosed. The first set of allegations, that Natural committed fraud by failing to make predictions—about

the productive life of the reservoir, regulatory acts of Congress and federal agencies, and the advancement of petroleum engineering—is bizarre in the extreme. Moreover, even had Natural been prescient, it was under no duty to share its prognostications with Plaintiffs.

> The rule . . . reflects the traditional ethics of bargaining between adversaries, in the absence of any special reason for application of a different rule. When the facts are patent or when the plaintiff has equal opportunity for obtaining information that he may be expected to utilize if he cares to do so, or when the defendant has no reason to think that the plaintiff is acting under a misapprehension, there is no obligation to give aid to a bargaining antagonist by disclosing what the defendant has himself discerned. To a considerable extent, sanctioned by the customs and mores of the community, superior information and better business acumen are legitimate advantages, which lead to no liability. The defendant may reasonably expect the plaintiff to make his own investigation, draw his own conclusions and protect himself; and if the plaintiff is indolent, inexperienced or ignorant, or his judgment is bad, or he does not have access to adequate information, the defendant is under no obligation to make good his deficiencies. This is true, in general, when it is the buyer of land or chattels who has the better information and fails to disclose it. Somewhat less frequently, it may be true of the seller.

Id. at section 551, Comment: k. The Defendant is not obliged to be a fortune teller for the Plaintiffs' benefit.

The second set of allegations also entail acts of nondisclosure. Plaintiffs complain that Natural's offer of a lump sum payment for the "gross value" of their royalty interests was deceitful because the factors of volume and unit price were not disclosed. The Keaslers suggest that had those factors been revealed, they would have been aware of the "real value" of the hydrocarbons in place. In other

words, Natural's offer to pay certain sums for the "gross value" of minerals remaining was fraudulent because the sum offered was, Plaintiffs claim, less than the minerals' "real value." The court finds no precedent for penalizing one who offers his adversary less then the "real value" in opening negotiations. Moreover, the hidden premise of Plaintiffs argument—that the consideration was inadequate—was originally pled but later abandoned, unproven. There is no credible evidence to show that the "real value" of the rights conveyed to Natural are other than the price paid.

The Keaslers further assert that Natural had a duty to disclose the methodology used to estimate the volume of hydrocarbons in place. There is no evidence that Natural withheld information about its reserve estimates from anyone who inquired. Neither is there evidence that Natural based its offers on estimates known to be inaccurate. Indeed, when the estimates of the independent consultant differed from its own, Natural based its offer on the higher of the two. Natural did the same with unit prices, paying the highest rate allowed by federal law.

This portion of the complaint appears to be nothing more than one of inadequacy of consideration—that Natural drove too hard a bargain in its negotiations with Plaintiffs—disguised as a fraud claim. It is without merit with respect to both types of transaction.

The third set of complaints assails the negotiating tactics of Natural as deceitful. In particular, Plaintiffs attack Natural for its pretense that the offer was "non-negotiable" when, in fact, it was open to compromise. Moreover, Plaintiffs urge that Natural had a duty, once it had negotiated or compromised with one offeree, to advise the other offerees it would do the same with them. While the representation of Natural that its offer was "non-negotiable" may have been falsely made to induce the offerees to assent, it was nonetheless a mere negotiating ploy. The

representation was neither material nor basic to the transaction; in no sense were the offerees entitled to rely thereon. To determine whether Natural's offer was actually non-negotiable, the offerees had only to make a counter-offer. That some failed to do so and simply acquiesced to the offer of Natural is no ground for recovery.

Plaintiffs complain that Natural further defrauded the owners of depleted fields by failing to offer to buy their interest in non-existing mineral leases. This is nonsensical. In effect, this is merely another indirect attack on the adequacy of consideration. This theory simply adds a further, confusing dimension to the claim for conversion. It is similarly without merit. The court perceives no liability in fraud for not offering to buy a putative interest.

The fourth and final set of complaints do not even arguably fit within the bounds of fraud or misrepresentation. Plaintiffs charge that Natural "overstated" the extent of its purchase—of both royalty interests and easement rights—and thereby deceived the Plaintiffs. That is, Natural paid them for more than it actually got. This argument seems to cut against Plaintiffs. First, it assumes a breach of contract, that Natural took more than its due, which Plaintiffs have not plead or proven. Second, it appears to concede that Plaintiffs were overpaid inasmuch as they no longer directly challenge the adequacy of consideration in either type of transaction. The theory of Plaintiffs would make a grantee liable in fraud whenever he disagreed with his grantor as to the extent of the conveyance. The court finds this an absurd rule. Moreover, even if it be true that Natural claimed to have bought more rights than it did, how are Plaintiffs harmed by the discovery that they retain more rights than they thought?

As with other portions of their complaint, Plaintiffs here, perhaps intentionally, confuse breach of contract with fraud. The Plaintiffs' bizarre pleadings and presentation of their case forced the court to interpret the contracts

in order to make findings as to the alleged acts of fraud and misrepresentation. Having done so, the court finds that Natural did lawfully purchase from the Plaintiffs: the right to occupy and use the reservoir; the right to inject gas and store it there as personal property; the right to withdraw gas and any other materials associated therewith, whether they entered with the gas or were somehow absorbed by it while in the reservoir; and the right of ownership in all such withdrawn materials, be they gaseous or liquid hydrocarbons, valuable or worthless. The court further finds that the Plaintiffs received adequate consideration for the rights conveyed to Natural. Moreover, the evidence indicates that the Plaintiffs fully intended to make such conveyances.

Plaintiffs altogehter failed to prove that Natural made any misrepresentation or omission of material fact on which they were reasonably entitled to rely, much less that Natural "employed any device, scheme or artifice to defraud" them. It is the opinion of the court that any misstatements by Natural made before or during the negotiations were not material or basic to the contracts. The court concludes that the Plaintiffs were not entitled to rely, if indeed they did, on any such misstatements of Natural incident to the negotiations. Accordingly, the federal securities fraud claim is without merit. See, Simpson v. Southeastern Investment Trust, 697 F. 2d 1257 (5th Cir. 1983); Chemetron Corp. v. Business Funds, Inc., 682 F. 2d 1149 (5th Cir. 1982). Similarly groundless are the Plaintiffs' State and common law fraud claims. See, Sawyer v. Pierce, 580 S.W. 2d 117 (Tex. Civ. App. 1979—writ ref'd n.r.e.).

It is the conclusion of the court, therefore, that the Plaintiffs are not entitled to recover from the Defendant, Natural. While the court hesitates to term this lawsuit frivolous, the cause borders upon it. At the best, Plaintiffs have been disingenuous, if not ingenious. For that reason,

the court orders that the costs of court be borne by the Plaintiffs, and it is, therefore

ORDERED ADJUDGED, and DECREED that FINAL JUDGMENT be and is hereby entered for the Defendant, NATURAL GAS PIPELINE CO. OF AMERICA and that the Plaintiffs go and take nothing in this cause, paying costs of court.

DISCUSSION NOTES

Storage of Gas: Fraud in Acquisition of Rights in Depleted Reservoir—No Conversion of Realty-Type as Opposed to Personalty-Type Interests—Rights Acquired by Storage Easement.

Not discussed.

W. J. F.

LITTLE et al. v. LINDER

Texas Court of Appeals
April 28, 1983—No. 1541
651 S.W. 2d 895
(Rehearing denied May 26, 1983)
(Writ of error refused. No reversible error.)

Deeds: Mineral Reservation—Reservation Clause Is Ineffective To Create Rights in the Spouse of the Grantor.

Action for declaratory judgment to establish that plaintiff owned an undivided half interest in the mineral estate. Defendants, who asserted title to an undivided three-fourths interest in the minerals, claimed that they had received an undivided half interest by deed from the husband of the original owner and half of the remaining half interest by intestate inheritance from the owner. The defendants appealed from the trial court's decision in favor of the plaintiff. Held: Affirmed. The property was originally held as the separate property of the plaintiff's grandmother. A subsequent deed of the surface to their daughter, one of the defendants herein, was not effective to create any interest in the owner's husband, who had joined in the deed, even though it contained a reservation of the oil, gas and minerals in favor of the "grantors . . . their heirs, and assigns." Thus, a later deed from the surviving husband to his daughter of all his undivided interest in the minerals was not effective to pass any fee simple interest in the minerals to her.

SUMMERS, Chief Justice.

Plaintiff/appellee Robert Ewing Linder brought this suit seeking a declaratory judgment establishing that appellee is the owner of an undivided one-half (½) interest in and to the mineral estate in and under 736.36 acres of land in Henderson County, Texas, and that defendants/appellants Anna Ruth Little and John H. Little are the owners of the other one-half (½) interest. Appellants Little claim that appellee owns only an undivided one-fourth (¼) interest in such minerals, and that appellants own the other three-fourths (¾) in equal portions. After a nonjury

United States Department of the Interior

OFFICE OF HEARINGS AND APPEALS
INTERIOR BOARD OF LAND APPEALS
4015 WILSON BOULEVARD
ARLINGTON, VIRGINIA 22203

AMERICAN NATURAL GAS PRODUCTION CO.

IBLA 80-208 Decided August 12, 1980

Appeal from the decision of the Utah State Office, Bureau of Land Management, rejecting noncompetitive oil and gas lease offer U-44386.

Affirmed.

1. Oil and Gas Leases: Lands Subject To--Oil and Gas Leases: Subsurface Storage

Under sec. 17(j) of the Mineral Leasing Act, the Secretary of the Interior may authorize the subsurface storage of oil and gas in lands leased or subject to leasing under the Act. Any lease on which storage is authorized shall be extended at least for the period of storage and so long thereafter as oil or gas not previously produced is produced in paying quantities. A storage agreement which recognizes an existing lease and only reserves to the United States all of the United States interest in minerals in the lands does not terminate the rights of the existing lessee to drill for and produce oil and gas. An oil and gas lease offer submitted subsequently by a third party for the lands subject to the lease is properly rejected since the United States does not hold the mineral interest sought.

APPEARANCES: Alan A. Enke, Esq., Ray, Quinney & Nebeker, Salt Lake City, Utah, for appellant; Ruland J. Gill, Jr., Esq., Salt Lake City, Utah, for Mountain Fuel Supply Company.

OPINION BY ADMINISTRATIVE JUDGE BURSKI

American Natural Gas Production Company has appealed the decision of the Utah State Office, Bureau of Land Management (BLM), rejecting its noncompetitive oil and gas lease offer, U-44386, because the lands already are included in oil and gas leases SL 070555 and SL 070555-A. Appellant's lease offer covers the following lands: Lots 1-7, SE 1/4 NW 1/4, S 1/2 NE 1/4, E 1/2 SW 1/4, SE 1/4, sec. 6, T. 2 N., R. 6 E., Salt Lake meridian.

On January 1, 1951, BLM issued oil and gas lease SL 070555 covering the above described lands to Edythe F. Parkinson for a 5-year term. The lease was extended for an additional 5 years to December 31, 1960. After various assignments, the ownership of the lease became vested in Mountain Fuel Supply Company (Mountain Fuel) in 1957. Oil and gas lease SL 070555-A covering Lot 7, sec. 6. T. 2 N., R. 6 E., Salt Lake meridian, was created by partial assignment of SL 070555 on December 13, 1960. The terms of both leases were extended to November 30, 1962, pursuant to 43 CFR 192.144(b) (1954) (now 43 CFR 3107.6-2) because of this assignment. SL 070555-A was reassigned to Mountain Fuel on February 1, 1961.

On January 1, 1961, the Department of the Interior entered into an agreement with Mountain Fuel pursuant to 30 U.S.C. § 226(j) (1976) entitled "Agreement for the Subsurface Storage of Gas" (Agreement). Under the terms of the Agreement, Mountain Fuel was permitted to store gas under certain lands including those covered by leases SL 070555 and SL 070555-A.

In its statement of reasons, appellant argues that the Agreement modified the rights granted under oil and gas leases SL 070555 and SL 070555-A. In effect, appellant contends that Mountain Fuel no longer has the right to drill for, extract, and dispose of oil and gas deposits on the leasehold. Appellant contends that instead, under the Agreement, Mountain Fuel is allowed to store natural gas exclusively in the specified area and to perform related activities. Appellant then focuses on section 9 of the Agreement which reserves to the United States the right to lease or otherwise dispose of the surface lands, the right to all of the United States interest in the minerals in the lands, and the right to use or lease the lands for any purpose, all subject to the rights of Mountain Fuel. Appellant argues that no new development has occurred under the subject tract, Mountain Fuel continues to store fuel, and unless the United States leases those rights which were reserved to it, any gas in formations on the leasehold other than that in the storage area "will remain locked in the ground and unproductive. Such a result would be contrary to the intent of Congress [with respect to multiple mineral development] and

would also negate the contractual rights which the United States reserved to itself."

[1] Section 17(j) of the Mineral Leasing Act, 30 U.S.C. § 226(j) (1976), provides, in relevant part, that:

> The Secretary of the Interior, to avoid waste or to promote conservation of natural resources, may authorize the subsurface storage of oil or gas, whether or not produced from federally owned lands, in lands leased or subject to lease under this chapter. Such authorization may provide for the payment of a storage fee or rental on such stored oil or gas or, in lieu of such fee or rental, for a royalty other than that prescribed in the lease when such stored oil or gas is produced in conjunction with oil or gas not previously produced. Any lease on which storage is so authorized shall be extended at least for the period of storage and so long thereafter as oil or gas not previously produced is produced in paying quantities. [Emphasis added.]

Thus, oil and gas leases on which storage is authorized are extended by operation of law for the storage period. See also 43 CFR 3105.5-4. The BLM status plat in the case record indicates and appellant acknowledges that the storage agreement between Mountain Fuel and the Department of the Interior is still in effect. Oil and gas leases SL 070555 and SL 070555-A therefore remain in effect, provided annual rental is paid. See Texas Eastern Transmission Corp., 14 IBLA 361 (1974).

We do not agree with appellant that the terms of the leases have been modified by the Agreement in the manner argued by appellant. The leases and the Agreement represent separate legal transactions. The Agreement expressly recognizes Mountain Fuel's existing interest in the lands as well as other existing leases and only reserves to the United States "the right to all of the United States' interest in the minerals on, in, or under" the lands (Agreement, preamble, sections 9, 10, 12). Mountain Fuel's right to drill and produce oil and gas is only modified to the extent that such activities would be inconsistant with Mountain Fuel's own storage operation. Appellant argues, in effect, that the Agreement terminates that right altogether. That it does not do. The oil and gas leases have been extended and Mountain Fuel may drill and produce to the same extent that any other lessee who obtains a lease to any part of the Federal interest may do.

The United States does not hold the mineral interests sought by appellant. Therefore, BLM properly rejected oil and gas lease offer U-44386.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

James L. Burski
Administrative Judge

We concur:

Douglas E. Henriques
Administrative Judge

Edward W. Stuebing
Administrative Judge

United States Department of the Interior

OFFICE OF HEARINGS AND APPEALS
INTERIOR BOARD OF LAND APPEALS
4015 WILSON BOULEVARD
ARLINGTON, VIRGINIA 22203

M. ROBERT PAGLEE

IBLA 81-658 Decided October 27, 1981

Appeal from decision of the Wyoming State Office, Bureau of Land Management, requiring execution of a special stipulation as a condition precedent to issuing oil and gas lease W 74532.

Affirmed.

1. Oil and Gas Leases: Lands Subject to—Oil and Gas Leases: Subsurface Storage

   Under sec. 17(j) of the Mineral Leasing Act the Secretary of the Interior may authorize the subsurface storage of oil and gas in lands leased or subject to leasing under the Act. Where an oil and gas lease applicant applies for lands underlain by such a storage area he may properly be required to execute a stipulation for the protection of the storage area.

2. Oil and Gas Leases: Stipulations—Oil and Gas Leases: Subsurface Storage—Secretary of the Interior

   The Secretary of the Interior may require an oil and gas lease applicant to accept a stipulation reasonably designed to protect a duly established subsurface oil and gas storage area as a condition precedent to the issuance of a lease.

APPEARANCES: M. Robert Paglee, pro se.

OPINION BY ADMINISTRATIVE JUDGE LEWIS

M. Robert Paglee has appealed from a letter decision dated April 28, 1981, of the Wyoming State Office, Bureau of Land Management (BLM), requiring the execution of a stipulation as a condition of issuing lease W 74532.

The lease, on form 3120-7 (competitive public domain lands), described the following lands:

> T. 26 N, R 87 W, 6th PM, WY Sec 28: S 1/2 NW 1/4 excluding and withholding from leasing the oil and gas rights of the Muddy Sandstone, Skull Creek, Dakota, and Sundance formations encountered between the depths of 1,988 feet and 2,192 feet and between depths of 2,570 feet and 2,650 feet with respect to the Sundance formation, as logged in Sinclair Oil Company Well No. 1 Federal, SE 1/4 SW 1/4 Sec. 29, T 26 N, R 87 W, containing 80 acres, more or less * * *.

Attached to the lease was a stipulation providing in relevant part as follows:

> If drilling for deeper producing formations is contemplated, the storage formations can not be produced and MUST be thoroughly protected. An intermediate casing string MUST be cemented from 100 feet below the Chugwater formation to surface and tested per API Specifications.
>
> The gas is stored at 1000 psi therefore the drilling mud must be of sufficient weight to contain this 1000 psi pressure from the Dakota at 2240' through the Chugwater at about 2766'. No air drilling will be permitted.

Appellant wanted to revise this stipulation to permit the production of oil only from the gas storage formations.

In its letter-decision BLM declined to accept appellant's proposal for revision as follows:

> With your return of the executed lease forms and balance of bonus bid, you advised that you wished to have the stipulations which was attached to the lease revised. This cannot be done as the gas storage area is excluded from your lease.
>
> This lease was parcel 20 of the March 11, 1981 competitive oil and gas sale. The sale notice listed the parcels available and this parcel specifically gave the exclusion, to wit,
>
> > T 26 N, R 87 W, 6th PM, WY Sec 28: S 1/2 NW 1/4 excluding and witholding from leasing the oil and gas rights of the Muddy Sandstone, Skull Creek, Dakota, and * * *.
>
> [Emphasis supplied.]

> The stipulation which was made part of the lease was supplied by the U.S. Geological Survey to protect the stor age area should drilling for deeper formations occur.

In his statement of reasons, appellant alleges that the section in which the subject lease is located has not been determined to be a gas storage area with producing zone characteristics which would drain gas from adjoining sections. Appellant emphatically suggests that any problem could be remedied by reinjecting gas after separating the oil, and that the matter should be reviewed to determine if (1) this is a bona fide storage area, and this is not an unreasonable degree of "protection" for producers in certain adjoining sections; and (2) an acceptable method can be agreed upon for separating any oil from the gas, and for reinjecting all the gas into the "storage" area.

The file shows that parcel 20, among others, lies within the East Mahoney Dome Gas Storage Area. Effective October 1, 1971, Northern Utilities, Incorporated, was issued permit number 14-008-0001-12375, to use this area to store gas in the Dakota, Sundance, and Chugwater formations.

[1, 2] Section 17(j) of the Mineral Leasing Act, 30 U.S.C. § 226(j) (1976), provides, in relevant part, that: "The Secretary of the Interior, to avoid waste or to promote conservation of natural resources, may authorize the subsurface storage of oil or gas, whether or not produced from federally owned lands, in lands leased or subject to lease under this chapter." This grant of discretionary authority is repeated, 43 CFR 3105.5-2. In the case before us, since a storage permit was granted, this authority was exercised. Neither the statute nor the regulation circumscribes the Secretary's authority by requiring the storage area to have the particular characteristics mentioned in the statement of reasons to provide for separation and reinjection of the gas. The stipulation to which appellant objects is designed to protect this storage area and appellant has not shown that it is either an arbitrary or unreasonable condition precedent to issuance of his lease. The Secretary of the Interior has the discretionary authority to issue oil and gas leases under such rules and regulations as he deems necessary, 30 U.S.C. § 189 (1976). The Secretary also has the discretion to refuse to issue any lease at all on any given tract. Udall v. Tallman, 380 U.S. 1, 4 (1965), rehearing denied, 380 U.S. 989 (1965). If the Secretary decides to issue a lease, he may require the execution of special stipulations to protect land use values. Vern K. Jones, 26 IBLA 165 (1976); 43 CFR 3109.2-1. However, proposed special stipulations must be supported by valid reasons which will be weighed by this Department with due regard for the public interest. A. A. McGregor, 18 IBLA 74 (1974); George A. Breene, 13 IBLA 53 (1974). The protection of the highly pressurized gas storage area is a valid reason for the stipulation herein.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

Anne Poindexter Lewis
Administrative Judge

We concur:

Gail M. Frazier
Administrative Judge

Douglas E. Henriques
Administrative Judge