Double Fractions in Oil and Gas Conveyances and Leases – Resulting Interpretive Issues

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Overview

A common interpretive problem in oil and gas conveyances and leases arises when the owner of a fractional mineral interest either conveys or reserves a fraction using unclear language. One way that can happen is when a "double fraction" clause is used. That's a clause that creates uncertainty as to whether the grant or reservation is a fraction of what the grantor owns or a fraction of the whole interest. For instance, if Bubba owns an undivided ½ interest in minerals and conveys "an undivided ½ interest in the minerals," does that mean that Bubba conveyed a ½ interest in all of the minerals or simply ½ of Bubba's ½? This interpretive issue can also arise when mineral interests are devised from a decedent's estate. It also occurs when a conveyancing instrument refers to both "minerals" and a "royalty" or blends the two concepts in the same instrument.

The interpretive issues associated with a double fraction clause recently came up again in a Texas case. That case involved the construction of a 1924 deed containing a mineral reservation clause, and it could have wide-ranging impact on oil and gas titles in Texas and, perhaps, elsewhere.

The meaning of a "double-fraction" clause and the impact on future oil and gas conveyances – it's the topic of today's post.

Royalty Deed Interpretation

A royalty interest is an interest in a share of production, or the value or proceeds of production, free of the cots of production, when and if there is production. It is usually expressed as a fraction. But, the way those fractional interests are express can create confusion, whether the fraction is expressed as a "fraction of royalty" or as a "fractional royalty."

Fractional royalty interests. With a fractional royalty interest, the owner is entitled to a share of gross production, free of cost in an amount determined by the fractional size of the owner's interest. The share of production the owner is entitled to does not "float" with royalties of differing amounts reserved in an oil and gas lease. An expression of a fractional royalty clause is, for example, "an undivided 1/16th royalty interest of any oil, gas, or minerals that may hereafter be produced."

Fraction of royalty interest. With a fraction or royalty interest, the amount of production that is associated with the interest will "float" depending on the royalty reserved in an oil and gas lease. The owner gets a share in production equal to a fraction multiplied by the royalty reserved in an oil and gas lease. Examples of such a clause would be, "1/16th of all oil and gas royalty" or "an undivided ½ interest

in and to all of the royalty" or "1/2 of 1/8th of the oil, gas and other mineral royalty that may be produced."

Double fractions. Complexity increases when a double fraction is used to describe the royalty interest. For instance, "1/4th of 1/8th of all royalty…" is an example of a double fraction clause. Many courts utilize the multiplication approach and would conclude that such a clause would convey a 1/32nd interest. Indeed, for conveyance or reservation clauses drafted before the 1970s, the general assumption was that the royalty provided for in an oil and gas lease would always be 1/8th. Thus, a right to "1/4th of royalty" would be the same thing as the right to 1/4th of the 1/8th royalty reserved in an oil and gas lease – a 1/32nd royalty. But, since the 1970s, mineral owners have often been able to negotiate a wider range of royalties in mineral leases with many of them larger than 1/8th (often ranging from 10 percent to over 30 percent). This resulted in the double fraction clause creating confusion as to the drafter's intent. This confusion can arise not only in oil and gas conveyancing instruments, but also in bequests from a decedent's estate.

Bequests. In *Hysaw v. Dawkins, 483 S.W.3d 1 (Tex. 2015),* the decedent executed a will in 1947 that divided three tracts of real estate among her three children. The will also distributed her mineral estates on the tracts using double fraction language – "each of my children shall have and hold an undivided one-third (1/3) of an undivided one-eighth (1/8) of all oil, gas or other minerals in or under that may be produced from any of said lands… and should there be any royalty sold during my lifetime then [the three children], shall each receive one-third of the remainder of the unsold royalty." The question was whether the double fraction language fixed the heirs devised royalty at 1/24th with any negotiated royalty above 1/8th passing to the current fee owner, or if the decedent intended her heirs to receive 1/3 of all future royalties, regardless of what the royalty fraction was. The heirs of two of the decedent's children sought 1/3rd of the 1/5th royalty in a new oil and gas lease, and the successors of the other child claimed that the successors of the siblings were only entitled to 1/3rd of 1/8th and that any additional royalty belonged to the fee simple owner.

Note: The *Hysaw* case involved the "estate-misconception theory." That theory reflects the historic prevalent belief that, in entering into an oil-and-gas lease, a lessor retained only a 1/8 interest in the minerals rather than the entire mineral estate in fee simple determinable." In turn, for decades afterwards, many lessors referred to their entire interest in the mineral estate with the simple use of "1/8." One court has described the "estate misconception" theory as follows: "In earlier times, many landowners labored under the misconception that when they leased their mineral estate to an operator, they only retained 1/8th of the minerals in place, rather than a fee simple determinable with the possibility of reverter in the entirety of the mineral estate… Therefore, when the landowner conveyed a mineral interest to a third party in land that was already subject to a lease, he would often use a fraction of 1/8 to express what interest he intended to convey in his possibility of reverter. Since a landowner in reality retains a full 8/8 interest in the reverter, the application of the estate misconception doctrine has tremendous consequences." *Greer v. Shook, 503 S.W.3d 571 (Tex. Ct. App. 2016).*

The Texas Supreme Court determined that the outcome should turn on the decedent's intent. Based on the evidence, the Court found that intent to be to equally divide the royalties among the decedent's

children. Accordingly, the Court held that the decedent had devised a 1/3rd fraction of a royalty interest (regardless of the amount of that royalty) to each of her children. In other words, the decedent has used the phrase "one-eighth royalty" as a shorthand phrase for the entire royalty interest that a lessor could retain under a mineral lease. She had left a floating 1/3rd royalty to each child.

Recent Texas Case

Van Dyke v. The Navigator Group, No. 21-0146,

2023 Tex. LEXIS 144 (Tex. Sup. Ct. Feb. 17, 2023)

Facts. This case culminated a decade-long battle over a mineral interest reservation involving a double fraction and accumulated royalties of approximately $44 million. In 1924, the Mulkeys deeded their ranch to White and Tom reserving "one-half of one-eighth" of all minerals and mineral rights. After the conveyance, both parties conducted themselves as if they believed that they each owned one-half of the mineral interest, as did all successors-in-interest.

In 2012, an energy company drilled a well and paid both the successors-in-interest to the Mulkeys (the "Mulkey parties") and the successors-in-interest to White and Tom (the "White parties") equal one-half shares. The White parties filed a trespass-to-try-title action, claiming that the 1924 deed reserved only a 1/16th (1/2 of 1/8th) of the minerals to the Mulkey parties, and that the White parties owned fifteen-sixteenths of the minerals. The Mulkey parties claimed that the interest reserved was one-half of the *total mineral estate*, and that the reference to one-eighth of the minerals was a term of art under the "estate misconception" theory. Under that theory (which had been forgotten over time), one-eighth was commonly believed to mean the entire mineral estate.

Alternatively, the Mulkey parties claimed entitlement to one-half of the minerals because of the long history of the original parties and the successors-in-interest acting as if each party owned one-half of the mineral interest.

Trial and appellate courts. The trial court held that the 1924 deed unambiguously reserved a one-sixteenth interest in the Mulkey parties. The appellate court affirmed, also concluding that the "estate misconception theory" did not apply because "the deed did not contain any conflicting provisions requiring harmonization and the subject property was not burdened by an oil and gas lease at the time of conveyance."

Texas Supreme Court. On further review, the Texas Supreme Court reversed and remanded. The Court noted that in the early 20th century that landowners commonly retained a one-eighth royalty interest under an oil and gas lease and that, over time, "1/8th" became synonymous with the mineral interest itself or as a proxy for the customary royalty of 1/8th. In essence, it became a term of art. The Court looked to *Hysaw* where, as noted, the Court held that each child received a "floating one-third interest in the royalty" based on what the evidence showed was the decedent's intent. While, as the Court noted, using "1/8" to mean the entire mineral estate is rebuttable, such a rebuttal can only be accomplished with evidence from the document itself suggesting basic multiplication be applied. The Court found that while "1/8" was a term of art in use at the time the deed was drafted to mean the

entire mineral estate, there was nothing else in the deed to rebut this meaning. As a result, the Court held that the Mulkey grantors did in fact reserve a full 1/2 interest in the mineral estate.

Note: The Court also noted that the court of appeals misapprehended how the estate-misconception theory is applied to instruments, such as the 1924 deed. Instead of looking to whether the lack of inconsistencies in an instrument require harmonization, courts should first assume that the specific use of a double fraction was intentional (a rebuttable presumption) and if the document lacks anything that could rebut that presumption (inconsistencies) then the intended (historical) use of the double fraction stands. For instance, the instrument in this case included the use of a double fraction ("1/2 of 1/8") and there was no evidence to rebut the presumption that the parties intended "1/2 of 1/8" to mean "1/2 of the mineral estate." As for the land not being encumbered by a lease at the time of the deed, the Court stated that the theory's "relevance has never depended on the considerations that the court of appeals identified."

The Court went on to examine the presumed-grant doctrine – a common law form of adverse possession. The Court noted three elements which must be satisfied for the presumed grant doctrine to prevail: "(1) a long-asserted and open claim, adverse to that of the apparent owner; (2) nonclaim by the apparent owner; and (3) acquiescence by the apparent owner in the adverse claim." The Court noted that a ninety-year history existed between the parties in which "conveyances, leases, ratifications, division orders, contract, probate inventories, and a myriad of other instruments" were recorded, thus providing notice of the interests owned by both parties. Likewise, for nearly a century, both parties had stipulated multiple times to the one-half ownership of the mineral estate. Indeed, in a 1950 conveyance, White had recited that he only held an undivided one-half interest in the oil, gas, and other minerals on the ranch. Based on all of this evidence and the conduct of the parties over time, the Court held that the Mulkey parties conclusively established their ownership under the presumed grant doctrine.

What Would Happen In Kansas?

In Kansas, a royalty deed is normally interpreted in accordance with the evidence concerning usage over time by the parties involved along with other relevant evidence. But, in *Bellport v. Harrison, 255 P. 52 (Kan. 1927*), the Court held that "royalty" must be construed in accordance with its "well-known meaning" and that it was not appropriate to look to custom to define the term "royalty." The Court also concluded that the term "royalty" cannot have a meaning different from its "well-known" meaning as a result of usage. The case involved a sale by Harrison of "one-half of [a] royalty." The receipt stated, "Received of A.J. Bellport, $2,400.00 payment for 1/16 royalty…". The mineral interest was leased at the time and provided for payment of a 1/8th royalty. Harrison asserted that Bellport acquired one-half of Harrison's 1/8th royalty, but Bellport claimed he purchased one-half of the mineral interest and that the reference to "1/16th royalty" conveyed to him a one-half mineral interest entitling him to one-half of the 1/8th royalty.

The trial court, based on custom, agreed with *Bellport* but the Kansas Supreme Court reversed. Arguably, the Court believed that the usage was unreasonable and not probative. The Court made a clear distinction between a royalty interest and a mineral interest. A "royalty" refers to a right

to share in the production of oil and gas at severance. A royalty is personal property and does not include a perpetual interest in and to oil and gas in and other minerals in and under the land. Conversely, a "mineral interest" means an interest in and to oil and gas in and under the land and constitutes the present ownership of an interest in real property. *See, e.g., Shepard v. John Hancock Mutual Life Insurance Co., 368 P.2d 19 (Kan. 1962).*

As a result, a Kansas court facing a double-fraction set of facts in a conveyancing instrument would likely focus on facts that enlighten the true nature of the instrument based on the language utilized rather than what the parties call it. This appears to be somewhat like the approach of the Texas Supreme Court taken in *Van Dyke*. The "estate misconception" theory is merely instructive, perhaps, but is not dispositive. It might also be safe to say that is the approach in Texas. *See, e.g., Concord Oil Co. v. Pennzoil Exploration & Production Co., 966 S.W.2d 451 (Tex. 1998).*

Conclusion

The *Van Dyke* ruling, at least in Texas, will probably have longstanding effect on oil and gas titles. The term "one-eighth" in a double fraction clause refers to the entire estate absent evidence to the contrary that proves otherwise and satisfies the presumed-grant doctrine. In any event, practitioners would do well to refrain from using double-fraction clauses.