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Energy Industry Update

You Made Your Bed, Now Lie in It: *Samson Exploration, LLC v. T.S. Reed Properties, Inc.*

Action Item: In Texas, watch out for overlapping units when exercising your contractual authority to unilaterally pool leases. You could be paying double.

In *Samson Exploration, LLC v. T.S. Reed Properties, Inc.*, the Texas Supreme Court affirmed the decision by the Ninth Court of Appeals siding with royalty owners in concluding that the operator of a well within two overlapping units had to pay twice.

Samson's leases contractually authorized unilateral pooling. Samson created Unit 1, which had boundaries of 6,000 to 13,800 feet subsurface, and obtained production from two wells within Unit 1's boundaries, Well No. 1 and Well No. 2. Well No. 1 produced from 12,304 feet to 12,332 feet subsurface. Well No. 2 produced from 13,150 to 13,176 feet. Samson then unilaterally amended Unit 1 to reduce the surface acreage and change the depth to 12,400 feet subsurface and below (the "Amended Unit"). No production from Well No. 1 was attributed to the Amended Unit.

After creating the Amended Unit, Samson drilled Well No. 3 that produced from 12,197 to 12,342 feet. Samson retroactively designated a new unit to cover this well's depth. The new unit covered production "occurring below a depth of 12,000 feet" (the "New Unit"). The New Unit overlapped depths encompassed in the Amended Unit. The overlap included the depth at which Well No. 2 was producing. Consequently, Well No. 2 was included in both the Amended Unit and the New Unit. Samson, however, only paid royalties to interest holders in the Amended Unit, and not the interest holders in the New Unit.

Samson claimed that the creation of overlapping units was a mistake and stood on the principle that title to the same property cannot be conveyed twice. Absent a cross-conveyance of title, Samson argued that the new unit never came into existence. Accordingly, Samson had no obligation to pay royalty owners with an interest in the new unit. The Court did not mince words when it called Samson's argument a "theoretical construct that holds no water."

The Court reasoned that pooling implicates both contract and property law. Contracts create authority to pool interests, and pooling creates interests in realty. Regardless of whether the new unit pooling designation effected a conveyance of title, Samson's obligation arose from its own unit designations done in conformity with the pooling authority granted by the leases.

Harkening back to the Fifth Circuit's decision in 1968 from *Howell v. Union Producing Co.,* 392 F.2d 95, 115 (5th Cir. 1968), the Court hammered home that when you mistakenly agree to pay double royalties, it is not the responsibility of the judiciary to rewrite your clear albeit unusual contract, but rather to enforce it:

> [The lessee,] unfortunately, has agreed to pay royalties two ways. Our conscience, though aroused, is relieved by the recognition that [the lessee] was the scrivener, and lucidity was in its hands and with its pen. While it may be unusual to have double royalty agreements, contract conformity to the usual is not a judicial responsibility. To argue that we must enforce only reasonable contracts or contracts which reasonable men enter into, mistakes our function. We can and do enforce unreasonable contracts if they be clear. Unreasonable men make reasonable contracts and reasonable men make unreasonable contracts.

The Court concluded that even though Samson "bemoans the economic consequences of its actions, this is a circumstance of Samson's own making."

The case is *Samson Exploration, LLC v. T.S. Reed Properties, Inc., et al,* No. 15-0886 (Tex. June 23, 2017).

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