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Supreme Court of Texas.
Wagner and Brown, Ltd., et al., Appellants,
v.
Jane Turner Sheppard, Individually and as Independent Executrix of the
Estate
of Sybil Turner, Deceased, Appellee.
No. 06-0845.

December 5, 2007.

Appearances:
Macey Reasoner Stokes, Baker Botts, L.L.P., Houston, Texas, for
petitioner.
Ben L. Mesches, Haynes and Boone, LLP, Dallas, Texas, for
respondent.

Before:

Chief Justice, Wallace B. Jefferson, Nathan L. Hecht, Harriet
O'Neill, Dale Wainwright, Scott A. Brister, David Medina, Paul W.
Green, and Phil Johnson, Circuit Justices.

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CHIEF JUSTICE JEFFERSON: The court is now ready to hear argument
in 06- 0845, Wagner and Brown Limited versus Jane Turner Sheppard.

COURT ATTENDANT: May it please the Court. Ms. Stokes focus an
argument for the petitioners. The petitioners reserved seven minutes
for rebuttal.

ORAL ARGUMENT OF MACEY REASONER STOKES ON BEHALF OF THE PETITIONER

MS. STOKES: May it please the Court. We're here today because the
Court of Appeals got the long run. The Court held that the termination
of an oil and gas lease automatically terminates the lessors
participation in a separate unit agreement. As a matter of law without
regard for the terms of either the lease or the agreement. Where the
Court went wrong was its fairly recognized that the unit agreement in
this case is a contractual commitment of Sheppard's land to the unit.
Separate and distinct from the lease of her mineral interest to CW
resources. In that lease the pooling clause which is excerpt at the tab
B of your handout. That CW resources was broadly authorized to pooled
cloth all nor any part of the lease premises or interest there, and,
and it define lease premises as the land. And which Sheppard held the

mineral interest. And that's the Sheppard Tract reflected on tab A of your handout. The clause also provided that any pooling could be terminated by the lessee upon absence or cessation of production in paying quantities. Under well established Texas law, this cause have the effect of making CW resources. The agent of Sheppard in entering into the separate unit agreement. And that unit agreement which is exerted at tab C of your handout. Sheppard broadly pooled her leases and lands. Therefore, the unit agreement was a contractual commitment of Sheppard's land to the unit for so long as production continued from the unit. And the subsequent termination of the lease of her mineral interest to CW resources could not and did not have any effect on her separate contractual commitment to the unit holders.

CHIEF JUSTICE JEFFERSON: What is their current-- what is their current relationship between Wagner and Sheppard are they-- they're no longer lease one, lessor. Correct?

MS. STOKES: That's right, your Honor they're co-tenants under the law. Because, because we held lessees on the remaining 7/8 interest in the Sheppard Tract. We became co-tenants with her-- and her full 1/8 interest in the ...

CHIEF JUSTICE JEFFERSON: If somehow, if they're not lessor and lessor - lessee, how does the unit agreement would seem to sort of presuppose that relationship continue to remain important and [inaudible].

MS. STOKES: Well, your Honor, I believe that while the unit agreement was entered under the authority granted about the lease. It was a separate in distinct contract and it was a contractual commitment entered into by CW resources as her agent.

JUSTICE GREEN: But the consideration failed.

MS. STOKES: No, your Honor. I'm not sure I understand the question really.

JUSTICE GREEN: [inaudible] to the reason at lease terminated because the failure complied with the terms in the lease agreement through all this.

MS. STOKES: Right. And that lease has terminated. And we have paid her four times or shared of production under the lease since that lease was terminated. But we-- what we maintain-- she is not entitled as to nearly eight times are shared of production of a none pooled interest.

JUDGE: But it didn't terminate before the unitization of the lease.

MS. STOKES: That's right your Honor, the, the unit had already been signed and he begun producing before well, before her at lease terminated.

JUDGE: She's the co-tenant with the lessee because the lessee has other interest in the track.

MS. STOKES: That's right your Honor.

JUSTICE HECHT: But with respect to the well I guess she's entitled the all of her 1/8 production after the expenses all the times.

MS. STOKES: Well, well, we, we say that she's entitled to her full 1/8 which would be her proportion on-- the proportion that her lease average bears to the unit times or 1/8.

JUSTICE HECHT: Could, can the parties really agreed to anything going in. Could they, could they say, "Well, it will terminate if any lease terminates here."

MS. STOKES: Yes, your Honor. They're-- then there of the three's has do say that, that there have been lease provisions that going a last only as long as the lease-- and she could have negotiated such a provision in this case. The evidence show that she was a lawyer, she

was represented by a lawyer at the time a lease was negotiated. And that she negotiated the four page addendum to our form lease that extracted several concessions from the lessee. So she could have done that in this case. Instead we have a provision that a-- that pooling was effective as long as, as production from the unit.

JUSTICE WAINWRIGHT: And you think the term to the agreement provide the exclusive means for terminating the unit.

MS. STOKES: Yes, your Honor. I do believed that we need to enforce the terms of the agreement as written.

CHIEF JUSTICE JEFFERSON: It seems like the, the commentators have wrote the uniform against the-- why you [inaudible] interpret this transaction that ...

MS. STOKES: Your Honor, I respectfully disagree with that and few commentators spoken about this. But, but the primary one you has is Cramer and Martin who was distinguished on pooling. And I believed that they reject the type of automatic termination rule announced by the Court of Appeals in this case. They said that all the circumstances at the time of termination has to be considered. And that the lessor should be continued to be bound by the pooling agreement if she is already benefited from pooling in form of production that she would not of otherwise obtained. Here it's undisputed that the-- the wheels would not have drilled on her tract but for the unit agreement. So she has obtained production as a result of the unit then the pooling that she would not otherwise have got them.

JUSTICE HECT: She explained to pay more out of the operating change of it?

MS. STOKES: Yes, your Honor. What we the producer is having to pay more than the proportion and share of the unit production that they had, that they had bargain for.

JUSTICE HECHT: So the other, in the none producing tract they're in-- they're rolling entries have not been reduce as a result of this.

MS. STOKES: Well, not only this, this particular-- well, they, they were not parties to this case. And so that refer Director Rolly doesn't reflect. There's-- how their shares have been affected in this case.

JUSTICE HECHT: Ms. Stokes what-- you might want to stay [inaudible] or you might get out of it.

MS. STOKES: That's exactly right your Honor. This-- the Court of Appeals rules is so broad and with this derogation of the terms of agreement. I could have applied their situation where Sheppard owned an interest in a none producing tract. And there she would be-- her lands would-- her interest would be automatically withdrawn from the unit. And I would submit in that situation. She would argue that was unfair to her and that the rule shouldn't be as such-- but, but the, the fact that she happens to own the interesting, the producing tract here, she shouldn't dictate the policy.

CHIEF JUSTICE JEFFERSON: So if, if she was on the other foot if-- because a family does lease your client could terminate it anytime by just stop paying.

MS. STOKES: That's right your Honor. Well, let's just try it.

CHIEF JUSTICE JEFFERSON: Do you say stop paying for 120 days lease was over. So it was really terminable at well on their side.

MS. STOKES: Right and ...

CHIEF JUSTICE JEFFERSON: And if they have terminated the lease she could just tell demand payment from the pooled?

MS. STOKES: Yes, sure. Your, your-- our position is that, she would solely bound by the pooled. And that we would take here by

pooling.

CHIEF JUSTICE JEFFERSON: Bill not just bound the benefit.

MS. STOKES: Bill-- yeah. And not just-- I'm sorry, your, your talking about with the wells were not on here tract. Exactly your Honor, that she would benefit in that situation and that we would-- our position is that the pooling would continue in that situation as well. Now, now, there's a little law on the issue with the effect of a constitutently his termination on the separate unit agreement. I think what law there is out there supports continued pooling in this case.

The Fourth Court of Appeals and it's Ladd Petroleum versus Eagle Oil and Gas case that we cited at page 10 of our brief. Held that determination of lessees on the only producing tract and then unit did not innate of itself terminate the unit. The Ninth Circuit and it's 1961 opinion in Stumpf versus Fidelity Gas held that determination of the plaintiffs lease did not automatically withdraw the plaintiffs lands from the producing unit, which the plaintiff had authorized the lessee to signed as agent during the term of the lease. And, and again the trade that I just discuss-- I think the comment ...

JUSTICE HECHT: Williams and Meyers [inaudible] ...

MS. STOKES: Well, Williams and Meyers has really-- just a single sentence that I, that I would submit is ambiguous. And they don't cite any law or other authority for that opposition. And as we know that in our briefs Williams and Meyers as now edited by Cramer and Martin.

CHIEF JUSTICE JEFFERSON: Is the length screen of your argument observed some sort of [inaudible]

MS. STOKES: Well, I, I guess, they-- I think the-- where Cramer and Martin actually studies the issue and reflects upon it. They, they would support pooling in this interest . And there's a true assignees that I think is ambiguous in Williams, Williams and Meyers.

CHIEF JUSTICE JEFFERSON: Cramer and Martin you say supports your viewed based on agency who run?

MS. STOKES: No, your Honor. I think that they, they don't-- I think they recognized that the agency theory is one way of looking on it. They don't endorse it but they do say in the situation that the unit is already producing. And the formal lessor already benefited from the pooling that they ought to remain bound. But it's still doesn't apply in agency theory. And the Texas cases that don't involved or exact lease-- cases all recognized the agency relationship inherent in the unit agreement. I think the comment they mean, what few cases there are, is the recognition of the sanctity of the unit once it's been validly formed and once production has begun. Now the cases cited in the opinion in the brief of Sheppard to the extent that even involved pooling or unit are all distinguishable on one of three grounds.

One, they involved in community lease in which the law implies pooling into the lease itself. And therefore, when the lease terminates so does the implication.

Or two, they involved cases where the Court found that the lessee never had the authority to polled the lessors interest in this manner in the first place.

Or three, they involved units that were never producing.

I think the Court of Appeals refused that full pooling once a lease terminates of course not only with the law. But also with clear Texas Public Policy. It's been a policy of the States since at least the 1930's. To promote and encourage pooling and unitization as an efficient means of producing minerals while I believe in a ways associated with multiple wells.

This Court recognized in 1976 and it's opinion in Mengan versus

Peninsula Production Company which is cited at page 23 of our brief. The pooling and unitization are essential to the oil and gas industry not that they benefit both the lessor and the lessee.

Today pooling is become only more common as Williams and Meyers recognized this. And it's become even more vitally necessary given the increasing importance of oil and gas to both our economy international security as well as the increasing difficulty of finding new reserved of oil and gas in this.

JUSTICE O'NEILL: But he returned out client to busted the pooled image. And that's the distinction between this case in Ladd. I mean, you're not trying the-- to-- nothing the Court of Appeals said would under mind the public policy that favors any decision.

MS. STOKES: Well, you know your Honor, I, I take exception that, that I think that the Court's rule is so broad that it would apply that the situation that could, that could busted to you. And that means, say for example Sheppard had own a hundred percent of the interest in the Sheppard Tract which is the only wells in the unit. The Court's rule would have the effect of taking the tracts out of the unit all together. And there would be no production to sustained the unit.

JUSTICE BRISTER: And we have to drill out the wells. And it have to be -

MS. STOKES: Yes. And assuming that that would be ...

JUSTICE BRISTER: - there was [inaudible] would have to drill also at wells to get the same oil and gas all.

MS. STOKES: Well, in your-- yes your Honor. And that assumes that it would even be economically feasible to do so. Given the circumstances that may not-- it may not be that the cause of drilling additional wells on the none producing tracts it maybe that they would outset the likely production revenues that we can extract from underneath her wells and her tract. I, I also think that, that pooling is even more vitally needed as today given the increasing fragmentation in minerals interest but in Texas and the United States as whole since the 1930's.

JUSTICE HECHT: Does the record show the only shift of the mineral interest in the unit?

MS. STOKES: I'm sorry, the, the-- all the other interest, we got the unit designation and the amended unit designation do leased and all [inaudible] the tracks and the lease ownership. They don't reflect subsequent-- any subsequent assignments for transferrers.

JUSTICE HECHT: Are they related either in unit or in the Sheppard Tract as to relationship therein this moment ended up with an eight of the mineral interest as one of the other of 7/8's [inaudible].

MS. STOKES: Who were own by relatives ...

JUSTICE HECHT: Of any member?

MS. STOKES: You know, your Honor I don't recall of the top of my head that the record does, does not actively reflect that. And I have not examined the names to determine that. Thank you.

CHIEF JUSTICE JEFFERSON: Thank you. The court is ready to hear argument from the respondent.

COURT ATTENDANT: May it please the Court Mr. Mesches will present argument for the correspondent.

ORAL ARGUMENT OF BEN L. MESCHES ON BEHALF OF THE RESPONDENT

MR. MESCHES: May it please the Court. The central question presented in this case is whether or less his poor ongoing pooling rights survive expiration of the lessee determinable fee interest of the minerals. That we believed that reversal the Court of Appeals decision hearing would upset almost the century of black letter that oil and gas that upholding with upon termination the entire minerals state reversed is the lessor and their possibly where board off.

JUDGE: When you say it century exactly how many Texas cases is that?

MR. MESCHES: Well, we're talking about the beginning in 1923 in Stevenson case and up to pooling-- there are-- I'm not-- to the pooling case and he doesn't know.

CHIEF JUSTICE JEFFERSON: No, one or two cases in the lease and then [inaudible]

MR. MESCHES: Well, well, in term-- we had talk about it in terms of the reversion of the fees and [inaudible] interest. Because we believed that's the controlling questions case. Because the pooling rights that are granted under the terms of the lease are part of the property grant. And they're, they're, they are the lessees rights. And when on fees simple determinable terminates or extinguished because failure to pay the royalties. Does rights terminate and the fees simply absolutely reserved

JUSTICE BRISTER: But that's, if I've got land and a mobile home on it, and I sell it to somebody and I finance it myself. And they sell the mobile home when they got it and then they stop paying me and I revert time or reverts to me. I don't get the whole-- go get the mobile home back, they owned it, they sold it while they had titled to it. And I do get fee back to the land but if they sold something in the mean time that's gone.

MR. MESCHES: Right. And I, I think the difference between your example and the situation we have here is really the nature that oil and gas lease transaction. And that is the, there're any rights that grants to the lessee under the transaction are subject to in the rise out of the real property grants. And that's what it is you take this simple to terminable and all the lessees rights are subject to that grant. And our position is that when those rights are-- or when we say, the underlying proper grants is extinguished the rights to lessee ...

CHIEF JUSTICE JEFFERSON: How is that different from a mobile home itself. If mobile homes are on the property and I sell it. It's, it-- your, your-- it, it takes everything with it and you have whatever authority you have. And sells stuff in the meantime -

MR. MESCHES: Uh-huh.

CHIEF JUSTICE JEFFERSON: - yes, it cancels, it means it comes back to me. But it cancels only what's [inaudible] ...

MR. MESCHES: Well, I think the nature of the mineral state is what make, what make it different case, different example.

CHIEF JUSTICE JEFFERSON: But that just different from all other ...

MR. MESCHES: I, I think, I think it's a different situation.

JUSTICE MEDINA: That seems, that seems to make a lot of sense except-- I get lose to-- when they have a pooling agreement it seems to say something else we have, we have two different agreements. And, and that for me that arises different issue that's difficult.

MR. MESCHES: Well, I think ...

JUSTICE MEDINA: Or otherwise it's simply the way you said it.

MR. MESCHES: Right. Well, I think, I think the issue that you separate agreements is a little bit mischaracterized by the

petitioner's. Because there, there are two different sets of documents here, we have the lease document and we have the unitization agreement or the designation of the pooling unit. But the lease itself is more than just a mere contract and that's why the decision, the Stumpf decision from the Ninth Circuit really gets it wrong. Because what that-- what the lease agreement is, is the grand right of the property rights. A few sample determinable and all the-- any contractual rights or other rights that flow from that, flow from that arrangement are completely tight in with the few sample determinable state. So it's not like a ...

JUSTICE HECHT: You, you don't think the lessor could agree going in in the lease to a difference, to survival of the [inaudible] ...

MR. MESCHES: I, I think that the lease in this case just to say actually answer that question. In paragraph 6 of the leased, the most in the hand out they cited for the pooling rights probations. But in paragraph 6 of the lease it states that the illusion, that is the right to dilute based on the unit agreement is, is som - right for lessee has only respect to the called " lessor's royalty." That is the parties have agreed on this case. That, that right to dilute, that right to divide the property. And this is the only source of that right is limited to the lessor royalty. When the parties relationship transformed upon termination of the real property grant that meant that the-- there's no Sheppard status-- it's lessors co-tenants. And there's no royalty interest anymore. It is a co-tenancy right of recovery.

JUSTICE HECHT: But what I'm asking just at the [inaudible] -

MR. MESCHES: Uh-huh.

JUSTICE HECHT: - is the lessor could agree otherwise.

MR. MESCHES: It is possible to agree otherwise. I, I would-- I, I ...

JUSTICE HECHT: They could cover this whole thing by agreement.

MR. MESCHES: It could be covered by agreement. I think that, that for language of the lease here though answers that question as well. And I think that the-- with respect to other probations of the, of the pooling rights probations that Ms. Stokes mentioned it particularly the termination probation, that's a lessee termination right probation. That it doesn't preclude termination on some, some other basis is not been exclusive termination probation.

JUSTICE HECHT: Look, the list allows pooling of the lease premises?

MR. MESCHES: That's correct.

JUSTICE HECHT: Describe this-- the whole as the well as that.

MR. MESCHES: Right.

JUSTICE HECHT: As minerals.

MR. MESCHES: Correct.

JUSTICE HECHT: So why isn't that lessors interested as well.

MR. MESCHES: The reason why isn't the lessor-- that's a lessors interest up until the time of determination. But, but whether you call it lands or leasehold or lease, it's all that under the, under the terms of the grant and the way that Texas law has always understood the nature of that grant. It is a real property grant and, and that those lands lease that real property is extinguish. There's no more rights that lessee holds that property as rights grant to it. They are subject to the real property grant likewise terminates.

JUSTICE WAINWRIGHT: And that approach that you're talking about is essential to the Court of Appeals. The fact that there's a royalty interest that's been conveyed and then terminate it. One particular concern with that is, there's any called-- some lack of stability and

may create the possibility of destabilizing a unit when individual leaseholders or owners can control or, or steps to great impact on the unit.

MR. MESCHES: Right. I think, I think there's a couple of facts I have about that question.

First of all, in this case we are not dealing with the unit while shut down, what we have in this case Sheppard on a 1/8 mineral interest that the defendants in this case on this remaining ...

JUSTICE BRISTER: [inaudible] some of them could easily be.

MR. MESCHES: In, in another case ...

JUSTICE BRISTER: Her argument-- your argument would be exactly the same that she owned this lands.

MR. MESCHES: That, that's correct. It, it could be in the ...

JUSTICE BRISTER: [inaudible].

MR. MESCHES: And, and if ...

JUSTICE BRISTER: And that they have to drill other well.

MR. MESCHES: In that case, that is a different case. And I think, our case is different and I thought people ...

JUSTICE BRISTER: You're an expert but I know.

MR. MESCHES: Right.

JUSTICE BRISTER: If we run a rule favored by ...

MR. MESCHES: Right. I understand that.

JUSTICE BRISTER: We don't want to write a rule where everybody's-- going back like the warning Texas by the Delaware ride on the edge of your property ...

MR. MESCHES: Uh-huh.

JUSTICE BRISTER: - because otherwise those guys next are stealing.

MR. MESCHES: Well, and I, and , and I understand that concern, Justice Brister but I think it, I think the, the core to this issue in this case is, where are you going to place the responsibility for what is happened here. It's not the lessors responsibility that the, that the lease terminate it. It is the lessees responsibility-- This is a limitation that was as Ms. Stokes pointed out was heavily negotiated. And this is a limitation in which-- and most cases, and most cases the reason why a lease will terminate-- a reason why the unit might terminate would probably be because of cessation of production. And the implication you're talking about will not be drawn out of there. This, this is unique in the sense that is a royalty based limitation on the leased. I think the other, the other point I make about, about the concern with Justice Wainwright raised and you, you've just raised is that pooling is not separating under Texas law. There are number of cases from, from this Court that limits.

JUSTICE BRISTER: It's the public policy favors it over individual.

MR. MESCHES: That, that is absolutely correct. But there are-- if there's-- some very important cases from this Court going back to [inaudible] decision that really outline how the lease can control the nature of pooling. Right. And, and that, and that is the, it's the lease that defines with [inaudible] rights probation that defines the scope of the rights, and that's exactly why our argument is here. That the, the nature of the real property grant controls the scoop of the-- whatever agency or contractual authority that makes it.

JUSTICE BRISTER: And that's two different things. One thing to say parties consent whatever they want if there's a growing up [inaudible] lawyers. They accept this up however they want to. But of course there's always cases like this one that they didn't think about that for us.

MR. MESCHES: Right

JUSTICE BRISTER: That's different thing from saying-- what you're saying is "We're going to imply from the theory. I mean, the cont - the part context don't say anywhere pooling evaporates when the lease does not explicit."

MR. MESCHES: That is tribute with the contract did you say is that, that the lessee does not have any contractual or any other real property right after the probation. Because the probation on appoint-- she before in the pooling rights probation specifically says, "The right to dilute." Which is really the issue here. That is, it's how you going to accounts as a results of the change that relation the accounting probation applies to the court lessor royalty. So I think that the lease probation, the probation of lease actually answer that aspect of question.

JUSTICE JOHNSON: Counsel, the Court of Appeals said and I read it from here "The pooling agreement itself expressly transferred only lessee's interest not that, that the determinable fee that ceased when the lease terminated. And it doesn't spoke the language on that." Do you have any thoughts on what the Court of Appeals met when it said.

MR. MESCHES: The act ...

JUSTICE JOHNSON: It-- put that in a tenants. Only transferred, only lessee's uses it first.

MR. MESCHES: Yeah. I think that's a little-- I do have an answer what's that about, maybe it's time for-- from a prior statement [inaudible] Court of Appeals opinion discussing the cross conveyances hard that's in returns the lease. With that, that provision that was the fact that the royalty interest owners are not transfer. That there's not joint ownership of the pooled unit as result of pooling. Well, I think the Court of Appeals was referring to-- is what happens when you pooled. That is the lessee is exercising rights, dominion control will probably control over the minerals when, when the lease is [inaudible]. And I think that's, that's sort of, that's put in the language. And in terms of what the declaration of the entities that bring together leases and lands in those concept and so bring it together the mineral interest. I don't think that there is a transfer from the lessee to other parties to the unit agreement under the terms of the unit. I don't think that's what, what occurs here.

JUSTICE JOHNSON: Okay. How about the pooling agreement, contract [inaudible] -

MR. MESCHES: Right.

JUSTICE JOHNSON: - with lessee's interest.

MR. MESCHES: That, that-- in that probation there actually is not a bar and to my knowledge it's not a bar on the cross-conveyance, but I don't think it is expresses in intent to cross-convey property interest. I think within-- it is a unit together, production purposes and then the royalty interest and other-- a royalty interest [inaudible] have the rights based on the terms of there leases production from the unit. So I don't think there's necessarily a property transfer to other parties of the unit.

JUSTICE JOHNSON: Okay. So you still on the lease limiting what would be transferred and not the pooling agreement. And what it did for lessor.

MR. MESCHES: That's right. Yeah. It's, it's up to us-- it's, it's the lease.

CHIEF JUSTICE JEFFERSON: I have two, two questions.

One, on what the commentators say cause it-- there's not a whole lot of case law on this.

MR. MESCHES: Right.

CHIEF JUSTICE JEFFERSON: And they still says that, that it's the Court more opposition than yours.

And then, the second and maybe after this report but I'm-- maybe I can elaborate on what, what's wrong with the Stumpf court's formulation transfer because they proposed on this way. If A authorizes B divide him to a contract with C, and B her Sheppard does so. The contract between A and C is not terminated by forfeiture of the original contract which mean A and B of that agreement was in, in fact -

MR. MESCHES: Right.

CHIEF JUSTICE JEFFERSON: - the time, the contract was with C sign. If you're following [inaudible] -

MR. MESCHES: Right. Yeah, I know is that what you think. I'm just ...

CHIEF JUSTICE JEFFERSON: - [inaudible] comment, the commentators and then [inaudible]

MR. MESCHES: Yes. I start with the commentators. I, I conclude with this [inaudible] petitioner's view, Cramer Martin says that they evaluates a kind of argument this, this principle agency argument is raises-- raised in the Stumpf decision. And they say "The better view is that the , that the rights granted and in the lease to pooled expire, determinate and they lapse when the lease itself expires." And that's based on the nature of the leasehold interest. They said that basic property law consideration should apply. And the main point they're making is that the right to pooled, and to maintain pooling is not an additional right that's granted, that would extent beyond the terms of the lease. And so I think that the commentators answer back to Stumpf decision. And said this agency do his reply.

Now as far as the Stumpf decision itself, that decision I think is, is wrong in, in a couple of important ways. But I'll begin with-- it has been a pre-heavily criticize decision because it's determination about the nature of the lease termination. That is they concluded that the lease did not per-- terminate during the primary terminal lease. Because there was no proper notice given by the lessor to the lessee. That's a few distinct and fully discredited by the Ladd Oil and Gas, States and Authorities.

Now, with the-- they, they used that conclusion to say that the unit agreement at the time of formation, that's already the decision the time of it's designation was properly designate.

Remember, that is not the issue in our case whether or not the unit at the time of it's designation was proper.

The question is the ongoing pooling rights.

Now, the other aspect I think of the Stumpf decision that gets, that gets it very wrong is I think the agency analysis is flood. Because as I mentioned before the relationship between A and B in your hypothe - in the hypothetical proposed is not merely contractual; is not merely contractual. It's real property in any rights that flow from that A, B relations. Or rights have granted to be onto that relationship only subject to the real property grants. And when that real property grant is extinguished those rights, I think likewise are extinguished as well.

JUSTICE HECT: If the leased determinate it had been for a larger interest. It might not be possible to high royalties to the none producing tract interest gather, gathering that unit -

MR. MESCHES: Uh-huh.

JUSTICE HECT: - out of the operator interest. Right?

MR. MESCHES: I think it could-- I, I think the, the answer to the question, it does not change with the royalty interest owners. Right to

royalty is-- but I think it could in fact with the working interest owners could pay. I think it's possible could effect with there ability to pay out.

JUSTICE HECT: Which is another troubling thing because the-- whatever the equities are in this situation, it looks like the lessors in the none producing part of the unit are completely unseat. I mean, they had nothing to do with anyone.

MR. MESCHES: Right.

JUSTICE HECT: So there share would seem another result that there-- if there financial -

MR. MESCHES: Uh-huh.

JUSTICE HECT: - pay out should diminished because of what's happened between the operator and one[inaudible].

MR. MESCHES: Right. But I think, I think actually that is in terms of the other lessors if it, it became to a situation where there some kind of need to shutdown the unit or to lessee exercise the right to terminate the unit, because it couldn't produce in the way that it can made economic sense. I think the key things that you could mind are those lessors, they would retained a piece and simple absence in there mineral interest. They can ignore the lease so they can drawout there self help aspect of it to the lessor. And so they, they could maintain a potential and some economic benefits as well. So I don't think it's a clear cut answer what would happened in that situation.

JUSTICE BRISTER: And if to see was on the other foot, if the wells where on the other properties and not on the Sheppard's property -

MR. MESCHES: Rights.

JUSTICE BRISTER: - and the lease is terminable at well. So they could shut her out.

MR. MESCHES: That is, that is correct. They could shut her out and that's ...

JUSTICE BRISTER: The rule, the rule arguing for will allow operators to shut people out -

MR. MESCHES: I think base ...

JUSTICE BRISTER: - as long, as long they have a lease like this one. Where they can do something to cancel the lease. And then, you can-- they can kick out the people on the pooled they don't like, they kick people-- they do.

MR. MESCHES: They can-- under there's very specific provision they can definitely do that. I think under ...

JUSTICE BRISTER: That did not trouble everyone. It don't happen to you.

MR. MESCHES: Well, I think that, I think the way to look at it, a good analogy in, in the fuel for this discussion that would happened in Ladd decision. Where you had parties to, to steal about leases. It seems to determinate based on production on another-- based on the release of the lease on the producing [inaudible] drill side tract. And with the Court of Appeals said "There you can't terminate the entire unit based on the release by another lease." So I think when I would come back to that, that example that you proposed, it may, it may occur in the context of this royalty limitation on the property right. But I think it's a general matter you're dealing with the production issue. And it's not a likely the current issue, I don't believed.

And as far as whether-- when the shoes under repair again there is a constancy right, they would, they would flow to-- Well, I guess in this instances when a mineral, mineral interest they would flow back to, to Sheppard as result of termination. So then, there are the rights in their parts that they are very valuable [inaudible].

JUSTICE BRISTER: [inaudible] the unit polled falls apart and always drill more wells.

MR. MESCHES: Right.

JUSTICE BRISTER: That's very upholding. So you -

MR. MESCHES: Well, that is right. But again ...

JUSTICE BRISTER: So you don't have to drill with it.

MR. MESCHES: Right. But I think, I, I think would point the to Court to you know, the nature of this particular case. And I understand the concern about, about future cases. But I think that there's not-- it's not clear to me. That on future case that would necessarily held complete shutdown of well operations. I think there other advantages that would flow back to the lessor in terms of, in terms of self help by drilling their own well or entering to leases or renegotiating the terms of the leases that are part of the unit. There are number of options that I think prevent necessarily that result from occurring.

JUSTICE HECT: There's statement in the brief about whether the wells would have been drill without the unit.

MR. MESCHES: Uh- huh.

JUSTICE HECT: What's the state of the evidence on that?

MR. MESCHES: Well, the state of the evident to me on that, I think-- I think a couple of things is not clear to me from the record that you have to drill to that, that you have--there was a spacing issue. Wells spacing issue. And as a result that is what the dependants states the reason why they want to have and unitize the-- all these tracts together.

However, there's also testimony in the record, I believed it's from, from the cross-examination of Wagner and Browns who have witness Oman Brown. And the questions they asked him about seeking exception under rule 37. We're all commission and I think in this case particularly if look at the interest, there was a-- there was-- that, that was an available option to the, to the lessee, to the worker interested. They could have gone to the available commission because the only party who standing to object is part like I tell in the record. I would be the working interest on that and that's all the defense in this case. So I don't think it's necessary and I don't think it's clear that she, that the second well from the record. I'm not sure if the second well was needed to create the second amount but I'm not sure about to say the evidences as far as that's concern.

JUSTICE HECT: But if, if wells would have not been drilled without the unitization that seems to ordered in favor of maintaining the unit even after that one of the lessee's expires.

MR. MESCHES: Well, I think that, I think that the issue about benefits of pooling cause it goes to what there-- what there view about this stuff or idea in effect to a unit. In this case, I think it's, it's very important to understand. They are drilled side tracts. And so in the second well-- those second well has been responsible for less than 20 percent of the over all production. The landowner number one has been the line shown. And that, that is numbered our detail in the judgment. So the benefits to pooling in this case are not as clear as example in the Ladd case. Where the lessors is not to terminate the entire unit where benefiting entirely from production on another tract. And so I think that there's a, there's a clear difference between those, those kind of situations. Any further questions from the Court?

CHIEF JUSTICE JEFFERSON: No further questions. Thank you.

MR. MESCHES: Thank you.

REBUTTAL ARGUMENT OF MACEY REASONER STOKES ON BEHALF OF PETITIONER

MS. STOKES: Your Honor. A couple of points justice had done when you asked about the evidence on the wells being gross based on the unit, Oman Brown, Wagner Brown Division Line Manager testified clearly that we-- that she's well to a drill because of the unit that was under the spacing regulations of the available commission we needed the unit. He admit, he said on cross in response to the question of Mr. Wholeman could Sheppard have sought and accept that she wanted to drill these two wells. And he said, "Yes, she could have but production would have been kept, we would not have the same revenues if from production that we do have on this case." There's no assurance and exception would have been granted. And ultimately they would have-- could-- should have of what could have been done doesn't change the fact that this wells were drilled and relies on the unit. And, and Mr. Mesches talks about the, the second well being drilled but it's, it's undisputed that at the time the lease terminated nobody was, nobody realized that it was not in burden that she was on paid royalties within a 120 days. So they didn't realized that it terminate in. Justice Hecht, do you also asked about the effect on the other unit holders if she had own the entire interest in the producing tract. I think one of the pernicious problems with the Court of Appeals rule is that we don't know what the exact effects would be on everyone else until that case gets filed, tried and decided. But the possibilities are all negative about the possibility that, that the other unit holders who committed their tracts to this unit and you pay their share of production of the two wells on her property. Now received nothing, no, no share of production.

Another possibility is that the producer occur withhold the producer to the terms in the unit agreement and force it to pay share to all other unit holders when it's not receiving a single done from the tract.

Another situation is obviously the, the unit will become completely uneconomical to the producer. And, and either way we were destroying the, the benefits in the bar-- the bargain benefits in the union-- excuse me, the unit to other the unit holders or, or the producer lessee. Justice Hecht, I did confirmed that the other interest owners in the Sheppard Tract are not related to Ms. Sheppard. Mr. Mesches also talk about this cases such as Steven sentence about the burden on the leease, burden on the lessee's interest automatically disappear when the lessee's interest reversed to the lessor determination of the lease.

Now, those cases, none of them involved units but they also involved assignment occur about of the lessee's interest. Which the lessee is entitled to do even without a probation in the lease. Is it, is it's fees involved determinable-- excuse me, fee determinable interest to do with us as wish. They do not involved a separate contract that the lessor - lessee was authorize to enter into as the lessor agents. Which is a completely different circumstance. And also I think it's interesting that, that now they-- they are focusing on, on the commitment of the royalty to the unit agreement when, when all along they had been ignoring that. And, and Justice Johnson-- the Court of Appeal, I think was confused when they said that it's the lessee's interest that's transferred. And the entire cross-conveyance probation doesn't explain that holding. Because that probation provides that neither parties interest would be transferred or conveyed in a pooling.

So I think, I think the Court was simply refuses and then cite a line for that proposition but Ladd said that the purpose of the unit agreement is to commit the lessors royalty interest.

JUSTICE JOHNSON: So your position is, that is the pooling agreement. The opposing counsel says the lease agreement is what governments-- and keeps that in your position is that the pooling agreement which you look at?

MR. MESCHES: No, your Honor. I think we should look at both of them. And looked at the terms of both of them and force them as written. I think that the lease agreement makes clear that she's committing her lands broadly, her lands and any interest there in. Which would include her royalty, her possibility of the burden what have you under Texas law that makes see every resources her agents to sign the unit agreement and she's bound by the terms of the unit agreement. So I think we can enforce both contracts.

JUSTICE JOHNSON: If-- if the lease agreement and the pooling agreement for 20 millions specifically code this matter. Is that limits us in used of some equitable theory such as staple fact theory or something to keep the unit together under the commentator they say, well, if the lessee, I mean if the lessor received the benefit. We don't want to break the party. We have to look at the situation to see if a benefit it been were save but that sound like an equitable time process and that's-- is that in conflict with this when we has specific language in the conflict on those.

MS. STOKES: Your Honor, I don't think that there in conflict. I think that we can enforce the agreement as written that could there actually commit her land to the unit for as long as production continues undisputed conduct-- production has been continues since inception. And that the common theories statement about looking at the circumstances that it's still producing or received-- receiving the benefits just to-- but address that conclusion but I don't think it requires you to ignore that. You enforce the term and no just the fact that your also promoting unitization on pooling as you should under the president is just a excerpt support for that proposition.

JUSTICE HECT: And then in your view, if I where the case that the lessor here would continue to be paid as it to list would not expired?

MS. STOKES: No your Honor. We will conti-- we will, we pay her co-tenants interest which is a fall-- excuse me, which is full 1/8 that supposed to a full 1/4 of the 1/8. We're not paying-- she was only getting a 1/3 second share as a royalty. So she will get the 1/8 but it would be the fourth ...

MR. HECHT: They loaded by it.

MS. STOKES: Exactly your Honor. Yes. And finally, unless the Court has any further questions, so get back to an anyone time. Thank you very much.

CHIEF JUSTICE JEFFERSON: Thank you Counsel. The case is submitted. And the Court will take a brief recess.

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