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EFFECT OF DRILLING REGULATIONS UPON THE LAW OF CAPTURE

THE rapid development of the petroleum industry in the United States has required a corresponding development in legal concepts of property to be applied to operations in this field.[1] During the early days of the industry the courts, most of which conceded that landowners had some sort of property rights in minerals beneath the surface of their land, were faced generally with the following three possible theories of ownership which could be applied:[2] (1) Owners of the surface above a reservoir could be treated as tenants in common of the reservoir. (2) The common law concept of ownership of real property[3] could be applied so that each surface owner would be held to have title to the oil and gas in place beneath his tract and retain ownership of it regardless of its migration elsewhere. (3) Each owner of surface above a reservoir could be accorded a property interest in the reservoir in the nature of a privilege to produce all the oil and gas which he was able to reduce to possession by operations on his tract;[4] this has been called the "law of capture" or "rule of capture." All other theories of ownership of oil and gas in the reservoir are combinations or variations of these three.

The application of a theory of co-ownership of the reservoir presented insurmountable difficulties to the courts fifty years ago due to the lack of knowledge of the nature and properties of the reservoirs in which oil and gas were discovered and the technical

[1] Apparently the first case in the United States which involved property rights in oil was Hail v. Reed, 54 Ky. 383 (1854).

[2] Masterson, *The Legal Position of the Drilling Contractor*, First Annual Institute on Oil and Gas Law, Southwestern Legal Foundation (1949) 183, 207.

[3] Early legal writers confidently stated that ownership of land carried with it complete dominion upwards to the heavens and downwards to the center of the earth. Development of aircraft as well as the development of the petroleum industry has required some revision of thought on this point. *See* Hinman v. United Airlines Transport Corp., 84 F. 2d 755 (1936), *cert. denied*, 300 U. S. 654 (1937).

[4] Of course, this rule never extended to oil or gas recovered by operations not entirely on the land of the producer. Liability for drainage which results from bottoming a well on the land of another is well established. *See* Aphonzo E. Bell Corporation v. Bell View Oil Syndicate, 24 Cal. App. 2d 587, 76 P. 2d 167 (1938); Gliptis v. Fifteen Oil Co., 204 La. 896, 16 So. 2d 471 (1943).

problems inherent in a determination of the extent of the reservoirs and their exact location. It was impossible to treat surface owners as tenants in common of the pool if it could not be decided under whose lands it lay. The theory of ownership in place also presented great difficulties because of the fugacious nature of the subject matter. Once migration has begun, the original location of oil or gas cannot be determined. Oil produced from the wells on one tract may have come from another tract a considerable distance away—there are no characteristics by which oil or gas originating under a particular surface area can be identified.[5] However, Texas and some other states adopted the theory of ownership in place and have continued to follow it in name.[6] In practice the theory has been limited by the necessity of the contemporaneous application of the law of capture.[7]

The law of capture has been applied by the courts in two different forms. The first is that discussed above, a theory of ownership of an interest in an oil and gas reservoir—a privilege to produce oil and gas accorded to owners of the surface, limited only by the requirement that production be within their own boundaries. The second form which the law of capture has taken is that of a rule of property which merely settles the question of title to oil and gas which has been reduced to possession without regard to the rights or liabilities which may arise as a result of the production. In other words, although the law of capture is followed by name in all states,[8] some of the courts interpret it as meaning to a producer of oil and gas, "You can take all that you can get by operations on your own land," while the other courts reach the result, "You

[5] Hardwicke, *The Rule of Capture and Its Implications as Applied to Oil and Gas*, 13 Tex. L. Rev. 391 (1935).

[6] Apparently the primary justification for the ownership in place or absolute ownership theory is its practicality in application to transfers of interests in the minerals before severance. Treatment of the oil and gas in a reservoir as a part of the land above it has simplified this field of law and prevented courts from falling into some of the inconsistencies of reasoning found in the opinions of courts in the qualified ownership and non-ownership states.

[7] Walker, *Property Rights in Oil and Gas and Their Effect Upon Police Regulation of Production*, 16 Tex. L. Rev. 370 (1938).

[8] Hardwicke, *supra* note 5, at 391 *et seq.*

own all the oil and gas you produce, but if your methods of production are illegal or unreasonable, you may be liable to adjacent landowners who are injured." In fact, the increasing recognition by the courts of correlative rights and duties of operators in a common reservoir has so pruned the law of capture as a theory of ownership of a privilege to produce that it is often difficult to distinguish the result in many situations from that which would have been reached had a theory of co-ownership been applied and each of the producers required to account to the others for any production which exceeded his fair share.

This modification of the law of capture has occurred through the recognition by many of our courts that the results reached by a strict application of the rule are, at times, contrary to established rules of justice and equity and detrimental to the public well-being.[9] Development of scientific skills in the petroleum industry has made it possible to determine with reasonable accuracy the exact location of discovered reservoirs and the amount of oil and gas contained therein. The courts have begun to recognize that it is now possible to ascertain whether or not production from one tract is resulting in drainage from under another and that the determination of the amount of drainage so caused is not an insoluble problem.[10] As the ability to solve the problems relating to physical properties of the reservoirs has developed, the application of traditional concepts of property ownership developed by the courts in the early cases are no longer necessary.[11] It is not improbable that continued encroachments, by court decisions, upon the law of capture will soon limit its application to the determination of title to oil and gas reduced to possession.

The development of limitations on the law of capture is exempli-

[9] Kelley v. Ohio Oil Co., 57 Ohio St. 317, 49 N. E. 399, 39 L. R. A. 765 (1897); Hague v. Wheeler, 157 Pa. 324, 27 Atl. 714, 22 L. R. A. 141 (1893).

[10] Patterson v. Stanolind Oil & Gas Co., 182 Okla. 155, 77 P. 2d 83 (1938); Brown v. Humble Oil & Refining Co., 126 Tex. 296, 83 S. W. 2d 935, 87 S. W. 2d 1069, 99 A. L. R. 1107, 101 A. L. R. 1393 (1935); Elliff v. Texon Drilling Co., 146 Tex. 575, 210 S. W. 2d 558, 4 A. L. R. 2d 191 (1948).

[11] 1 SUMMERS, THE LAW OF OIL AND GAS (1938 ed.) § 63.

fied by the recent Texas case of *Loeffler v. King*[12] A simplified statement of the problem arising in this case, insofar as it pertains to the law of capture, is as follows: Plaintiff owned a mineral interest in an 80-acre tract which was part of a larger tract of approximately 143 acres. Plaintiff executed an oil and gas lease to *A* covering the 80-acre tract. The lease expired for lack of production. *A* also obtained a lease on the remainder of the larger tract. Acting in ignorance of the expiration of the lease on plaintiff's tract, he entered into an agreement with *B* assigning the north one-half of the large tract to *B*. *A* and *B* drilled wells on the tract and complied with the well-spacing regulations[13] with reference to the division line between the north and south halves of the tract. Since plaintiff's 80-acre tract extended into the south half of the larger tract, wells drilled by *A*, which were 330 feet from the division line of the half assigned to *B*, although not on plaintiff's tract, were within less than the required 330 feet of the south boundary thereof. These wells produced oil in paying quantities, and plaintiff brought suit for a declaration that *A's* lease on his tract had expired and for damages resulting from unlawful drainage of the 80-acre tract due to the violation of Rule 37. The court of civil appeals held that plaintiff had a cause of action for wrongful drainage of his tract. No decision as to the measure of damages was rendered.[14] The court based its decision upon the premise that the law of capture is limited in its application to legitimate operation of a producer. Since Rule 37 has for its objective the protection of land from unreasonable drainage by adjacent wells, it is a restraint upon the unlimited right of capture, for breach of which there is a right of action by adjacent mineral owners whose interest in the common reservoir is jeopardized thereby.[15]

[12] 228 S. W. 2d 201 (Tex. Civ. App. 1950).

[13] Rule 37 of the Railroad Commission of Texas.

[14] This case is, at present, on appeal to the Supreme Court of Texas. Due to the complicated nature of the case and the many problems, other than the one under discussion, which are involved, the supreme court may dispose of the case without passing on the question of liability for wrongful drainage based on a violation of Rule 37.

[15] 228 S. W. 2d at 210-215.

Loeffler v. King is the first case in Texas in which a cause of action for wrongful drainage based upon violation of well-spacing regulations has been recognized.[16] The courts have been slow in recognizing any right of action for wrongful drainage. Many of the early cases refused to allow any recovery even where injury by drainage was apparent. In *Hague v. Wheeler*[17] the court refused to enjoin waste of natural gas from a common reservoir and, in referring to the rights of a surface owner in the gas, said,

> "He cannot prevent its movement, away from him, towards an outlet on some other person's land, which may be more or less rapid, depending on the dip of the rock or the coarseness of the sand composing it; but so long as he can reach it, and bring it to the surface it is his absolutely, to sell, to use, to give away, or to squander, as in the case of his other property."

The absolute right to take oil and gas under the law of capture was recognized to the extent that cases refused recovery for excessive drainage due to artificial means of production,[18] location of wells close to plaintiff's boundary lines,[19] or negligently allowing a well to blow out with resulting depletion of the reservoir.[20] However, this application of an unlimited right of capture seems to have been repugnant to some courts from the beginning, and the cases upholding the existence of correlative rights and duties among owners of interests in a common reservoir have become more frequent, until today, according to Mr. Summers, "clear recognition is given to the rights of landowners against drainage of

[16] Only one other case was found in which recovery was permitted for wrongful drainage due to drilling too close to a boundary line. In Ross v. Damm, 278 Mich. 388, 270 N. W. 722 (1936), recovery was predicated upon proof that the location of defendant's wells was such that they drained substantially all of the oil from plaintiff's land while, at the same time, rendering it impossible for plaintiff to obtain a drilling permit to offset the wells and prevent such drainage.

[17] 157 Pa. 324, 27 Atl. 714, 720, 22 L. R. A. 141 (1893).

[18] Higgins Oil and Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206, 5 A. L. R. 411 (1919); Jones v. Forest Oil Co., 194 Pa. St. 379, 44 Atl. 1074, 48 L. R. A. 748 (1900).

[19] Kelley v. Ohio Oil Co., 57 Ohio St. 217, 49 N. E. 399, 39 L. R. A. 765 (1897); Barnard v. Monongahela Natural Gas Co., 216 Pa. 362, 65 Atl. 801 (1907).

[20] McCoy v. Arkansas Natural Gas Co., 175 La. 487, 143 So. 383, 85 A. L. R. 1147 (1932), *cert denied*, 287 U. S. 661 (1932); Louisiana Gas & Fuel Co. v. White Bros., 157 La. 728, 103 So. 23 (1925).

oil and gas, and privileges or opportunities to produce their equitable shares."[21]

In the case of *Manufacturer's Gas and Oil Co. v. Indiana Natural Gas and Oil Co.*[22] plaintiff sought an injunction against another operator who was taking gas from a common reservoir by means of artificial pumping devices. The court, in deciding that plaintiff had a right to such an injunction, said,

> "Natural gas in the ground is so far the subject of property rights in the owners of the superincumbent lands, that while each of them has the right to bore or mine for it on his own land, and to use such portion of it as, when left to the natural laws of flowage, may rise in the wells of such owner and into his pipes, no one of the owners of such lands has the right, without the consent of all the other owners, to induce an unnatural flow into or through his own wells, or to do any act with reference to the common reservoir, and the body of gas therein, injurious to, or calculated to destroy it. . . . So, in the case of natural gas, the manner of taking must be reasonable. . . ."[23]

Landowners over a common reservoir have a right that the oil and gas therein shall not be wasted or destroyed.[24] There is a right of action against the owner of a well which is abandoned without having been properly plugged.[25] An operator is liable for damage to the common reservoir which results from negligent use of nitroglycerine in shooting a well[26] or from negligent drilling which causes his well to blow out.[27] A landowner may secure an injunction against the sinking of wells on adjoining tracts without proper permits,[28] or he may secure damages where wells drilled contrary

[21] Summers, *Legal Rights Against Drainage of Oil and Gas*, 18 Tex. L. Rev. 27, 38 (1939).

[22] 155 Ind. 461, 57 N. E. 912, 50 L. R. A. 768 (1900); *see also* Peterson v. Grayce Oil Co., 37 S. W. 2d 367 (Tex. Civ. App. 1931), *aff'd*, 128 Tex. 550, 98 S. W. 2d 781 (1936).

[23] 57 N. E. at 915.

[24] Louisville Gas Co. v. Kentucky Heating Co., 117 Ky. 71, 77 S. W. 368, 70 L. R. A. 558 (1903).

[25] Atkinson v. Virginia Oil and Gas Co., 72 W. Va. 707, 79 S. E. 647, 48 L. R. A. (N. S.) 167 (1913).

[26] Comanche Duke Oil Co. v. Texas & Pacific Coal & Oil Co., 298 S. W. 554 (Tex. Comm. App. 1927).

[27] Elliff v. Texon Drilling Co., 146 Tex. 575, 210 S. W. 2d 558, 4 A. L. R. 2d 191 (1948); *see* comments in 62 Harv. L. Rev. 146 (1948); 20 Miss. L. J. 96 (1948); 27 Tex. L. Rev. 349 (1949).

to spacing regulations have drained his tract.[29] In general each owner of a right to produce minerals from a reservoir has a right that production by other owners shall not jeopardize his opportunity to obtain his fair share of the oil or gas which was in place in the reservoir in its natural state.[30]

The extent to which this right to a fair share of the minerals is protected by the courts is still not completely settled. Although the results in *Elliff v. Texon Drilling Co.*[31] indicate that, in Texas, negligent injury to the reservoir is sufficient basis for recovery of damages for drainage resulting therefrom, there is little authority supporting this proposition in other states.[32] Where recovery is sought upon the basis of breach of a duty imposed upon an operator by statute or by a rule or regulation imposed under statutory authority, it seems clear that there should be no question of the right of recovery for wrongful drainage. That there is statutory authority in Texas for such recovery seems clear from the following language:

> "Nothing herein contained or authorized, and no suit by or against the [Railroad] Commission, and no penalties imposed upon or claimed against any party violating any Statute of this State, or any rule, regulation, or order of the Commission, shall impair or abridge or delay any cause of action for damages, or other relief, any owner of any land or any producer of crude petroleum oil or natural gas, or any other party at interest may have or assert against any party violating any rule or regulation or order of the Commission, or any judgment herein

[28] Magnolia Petroleum Co. v. Railroad Commission, 90 S. W. 2d 659 (Tex. Civ. App. 1936), *modified*, 128 Tex. 189, 96 S. W. 2d 273 (1936); Stanolind Oil and Gas Co. v. Railroad Commission, 92 S. W. 2d 1057 (Tex. Civ. App. 1936); Empire Gas and Fuel Co. v. Railroad Commission, 94 S. W. 2d 1240 (Tex. Civ. App. 1936).

[29] Loeffler v. King, 228 S. W. 2d 201 (Tex. Civ. App. 1950).

[30] "This reasonable opportunity to produce his fair share of the oil and gas is the landowner's common-law right under our theory of absolute ownership of the minerals in place. But from the very nature of this theory, the right of each land holder is qualified and is limited to legitimate operations." Elliff v. Texon Drilling Co., 146 Tex. 575, 210 S. W. 2d 558, 562 (1948).

[31] *Id.*

[32] But see the statement of the Louisiana court in McCoy v. Arkansas Natural Gas Co., 175 La. 487, 143 So. 383, 384 (1932), indicating that recovery might have been allowed in that case on proof of negligence of defendant as opposed to proof of mere "bad judgment."

mentioned. Any party owning any interest in any property or production which may be damaged by any other party violating this act or any other Statute of this State prohibiting waste or violating any valid rule, regulation or order of the Commission, may sue for and recover such damages, and have such other relief as he may be entitled to in law or in equity."[33]

This statute is cited as authority for the recovery authorized in *Loeffler v. King*. It seems that even in the absence of any express authority to sue for damages caused by breach of a statutory duty, such a right to sue would exist where the statute violated has as its purpose not only the protection of the public as a whole by conservation of natural resources but also the protection of individual owners of interests in oil and gas reservoirs from actions by others which deprive them of an opportunity to produce their fair share of the minerals.[34]

Statutes in most oil and gas producing states have imposed specific duties on producers which are clearly contrary to the theory of the law of capture as an unrestricted privilege to produce. In general, these statutes have been upheld as a valid exercise of the states' police power.[35] The duties imposed may be divided into the following classes: (1) prevention of underground and surface waste by requirements that abandoned wells be plugged, proper casing be used in wells, certain wasteful means of production not be used, certain gas-oil ratios be maintained, prohibition of wasteful burning of gas, requirement of repressuring of formations, and restrictions upon the open flow of gas wells; (2) location and spacing regulations; and (3) proration of production.[36]

There seems to be no valid reason for failure to recognize that a cause of action would exist where any of these duties imposed

[33] TEX. REV. CIV. STAT. (Vernon, 1948) art. 6049 c, sec. 13.

[34] Elliff v. Texon Drilling Co., 146 Tex. 575, 210 S. W. 2d 558 (1948).

[35] Ohio Oil Co. v. State of Indiana, 177 U. S. 190 (1900); Patterson v. Stanolind Oil & Gas Co., 182 Okla. 155, 77 P. 2d 83 (1938), *app. dism'd*, 305 U. S. 376 (1939); Oxford Oil Co. v. Atlantic Oil & Producing Co., 22 F. 2d 597 (C. C. A. 5th, 1927), *cert. denied*, 277 U. S. 585 (1928).

[36] 1 SUMMERS, THE LAW OF OIL AND GAS (1938 ed.) c. 5; *see* TEX. REV. CIV. STAT. (Vernon, 1948) tit. 102 for examples of such statutes.

by statute is violated. Wrongful drainage of a neighbor's tract through violation of proration regulations seems no more tortious than drainage due to violation of a spacing rule.[37] If the courts follow *Loeffler v. King* and extend the rights of landowners to recovery for any violation of rules, regulations or statutes, it is submitted that the rule of capture will exist only as a rule of property in determining title to oil and gas reduced to possession and that privileges to produce will be essentially the same under the extant law as if the courts were applying a theory of co-ownership of the reservoir by owners of the surface.

Since modern scientific techniques have made possible the determination of the location and potential production of a reservoir with reasonable accuracy, it does not seem that treatment of owners of the superincumbent lands as tenants in common of the reservoir would be the source of problems substantially more difficult than those which arise from tenancies in common of the surface. The alienability of interests in the minerals would not be adversely affected. The interest would be an interest in land and subject to recordation statutes and the Statute of Frauds. Oil and gas fields might be developed more economically by obviating the necessity of drilling a well on each small tract to protect the interests of its owner. In short, the recognition of the theory of co-ownership by the courts would have essentially the same effect as do the statutes which have been adopted in a number of jurisdictions requiring the forced pooling of mineral lands. The co-ownership theory is, therefore, subject to both the praises and the criticisms which apply to forced pooling laws.

Insofar as the law of capture is considered merely a rule of property in oil and gas which has been produced, it is not inconsistent with the theory of the cases allowing recovery for wrongful drainage. The courts can hold that title to oil or gas vests in the person producing it as soon as it is reduced to possession while, at

[37] But see Ivey v. Phillips Petroleum Co., 36 F. Supp. 811 (S. D. Tex. 1941), denying recovery for drainage due to a violation of a proration order on the grounds that there had been no previous cases allowing such recovery.

the same time, recognizing that the producer may be liable in damages to other owners of interests in the common reservoir due to wrongful drainage of their tracts. This liability is not for wrongful production but for wrongful drainage. Therefore, the law of capture, like the common law doctrines of accession and adjunction, may pass title of property from an innocent person to a wrongdoer under certain conditions but does not affect liability for the injury actually done by the wrongdoer. There can be a loss of the right to the return of property taken, without the loss of a right of action for damages sustained by reason of the taking.

In formulating the rules to be applied in this comparatively new field of law, tort liability for wrongful drainage, the courts are faced with the problem of determining a measure of damages. The law of capture, as qualified by the requirement of reasonable and legal production, is more consistent with a measure of damages which would necessitate the reimbursement of the injured party only for damages actually suffered and not for the value of the oil wrongfully produced. Part of the oil or gas may have come from the land of the wrongdoer and part from the land of the innocent party. A reasonably accurate scientific determination of the amount belonging to each, with all doubts resolved in favor of the innocent party, could be made which would certainly serve as an equitable basis for the adjustment of the rights and liabilities of the parties. The law of capture would pass title to the whole of the production to the wrongdoer, and his liability could be based either upon the decrease in the value of the innocent party's land or upon the market value of the oil or gas produced less credit for a proportionate part of the drilling and operating expenses.[38] If the courts should adopt the view that the wrongdoer is a converter of the oil and gas drained and is, therefore, liable for its full value at the mouth of the well or if the strict common-law doctrine of confusion should be applied to divest the wrongdoer of any title

[38] If a good-faith trespasser is entitled to reimbursement from production for drilling and operating expenses, Swiss Oil Corporation v. Hupp, 253 Ky. 552, 69 S. W. 2d 1037 (1934), there is greater reason for allowing such reimbursement to a person guilty only of wrongful drainage if he too acted in good faith.

to the oil and gas produced by wrongful drainage, the result would not only be inconsistent with the law of capture but would also cause a very unjust result in cases such as *Loeffler v. King*, in which the wrongdoer acted in good faith.[89]

A number of additional problems will arise in connection with the increasing recognition of liability for wrongful drainage. Is the owner of a royalty interest in a tract on which a well is producing by reason of wrongful drainage from another tract entitled to royalty payments on this production? Does the owner of a royalty interest in the drained tract have a right of action against the wrongdoer, or does this right belong solely to the owners of mineral interests? What damage due to wrongful drainage will be considered too remote to be the basis for a cause of action? The answer to these and other questions should appear in the decisions of courts during the next few years. Whether the effect upon the oil and gas industry of the extension of tort liability to cases of wrongful drainage will be detrimental or beneficial will depend upon the ability of the courts and the legal profession as a whole to formulate just and workable rules of law to meet the needs which will arise in this new field.

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[89] But notice the theory applied by the Texas Supreme Court in Elliff v. Texon Drilling Co., 146 Tex. 575, 210 S. W. 2d 558 (1948).