Michigan Law Review

Volume 58 | Issue 2

1959

Future Interests - Oil and Gas - Applicability on the Rule Against Perpetuities to Remote Future Interest Following Reserved Oil and Gas Interest

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FUTURE INTERESTS — OIL AND GAS — APPLICABILITY OF THE RULE AGAINST PERPETUITIES TO REMOTE FUTURE INTEREST FOLLOWING RESERVED OIL AND GAS INTEREST — A grantor conveyed real property to defendant reserving "all oil and gas and all minerals" in and under the land "for the period of twenty-five years . . . and as long thereafter as oil or gas or petroleum products" should be produced. Following this reservation, but in another clause of the deed, the grantor provided, "Subject to the reservations and conditions aforesaid, [grantor] hereby grants . . . all of said real property . . . to the [defendant], together with . . . the reversion and reversions . . . thereof." Some years later, the same grantor quitclaimed to the plaintiff "all oil and gas in and under" the same property. The plaintiff sued to quiet title in the oil and gas, arguing that because the defendant's interest, which was to begin on the termination of the grantor's reserved interest, was void for remoteness under the Rule against Perpetuities,[1] the entire interest in oil and gas remained in the grantor and was effectively transferred to the plaintiff by the quitclaim deed. Judgment was entered quieting title in the defendant.[2] On appeal, *held,* affirmed. Even if the common grantor's attempt to grant a future interest in oil and gas to the defendant was void under the Rule against Perpetuities, the common grantor thereupon "held" that interest as a reversion and this reversion was

1 The provision applicable to the conveyance is Art. XX, §9 of the California Constitution: "No perpetuities shall be allowed except for eleemosynary purposes." 2 MASON, CONSTITUTION OF CALIFORNIA (1953). The provision requires estates to vest "within lives in being and twenty-one years." See Estate of Sahlender, 89 Cal. App. (2d) 329, 201 P. (2d) 69 (1948).

2 The defendant had brought cross actions seeking such relief. During suit the twenty-five year period elapsed, no oil or gas ever having been produced.

effectively conveyed to the defendant by the last clause in the same deed. *Brown v. Terra Bella Irrigation District,* 51 Cal. (2d) 33, 330 P. (2d) 775 (1958).[3]

It is generally accepted that the Rule against Perpetuities is applicable to executory interests but not to possibilities of reverter even though there is little difference in the quantum of these two future interests.[4] And if a grantor transfers his possibility of reverter at a later time in a deed other than the one in which he conveyed the precedent indeterminate estate, his grantee is likewise deemed to hold a possibility of reverter immunized from the Rule.[5] But the holding of the principal case, in allowing an executory interest, invalid as too remote, to pass sheltered from the rule under the guise of a reversion in a subsequent clause of the same deed seems highly questionable.[6] Indeed, the suggestion of the court that the grantor retained or "held" a reversionary interest for a length of time sufficient to warrant the conclusion that the defendant received a reversionary interest cannot be reconciled with the fact that a deed becomes instantaneously operative in its entirety at the moment of execution and delivery.[7] In grounding the result of the principal case on such extremely tenuous grounds the court managed to avoid an important question which was squarely presented by the facts and the arguments of the parties,

[3] This decision affirmed Brown v. Terra Bella Irrigation District, (Cal. App. 1958) 321 P. (2d) 835. Compare Victory Oil Co. v. Hancock Oil Co., 125 Cal. App. (2d) 222, 270 P. (2d) 604 (1954), discussed in note 8 infra.

[4] See 3 SIMES AND SMITH, FUTURE INTERESTS, 2d ed., §1235 et seq. (1956). The distinction has been criticized, and it has been suggested that possibilities of reverter and other reversionary interests should be subject to the rule. See, e.g., Leach, "Perpetuities in Perspective: Ending the Rule's Reign of Terror," 65 HARV. L. REV. 721 at 741 (1952). The granting of a future interest, with reservation of a determinable fee, seems indistinguishable from an attempt to create an executory interest and the validity of the future interest should be tested by the Rule against Perpetuities. No one, except the California court, has yet suggested that executory interests should be called reversionary interests to avoid the rule. (A reversion in oil and gas could arise only in a grantor upon a conveyance of a present "possessory interest" which was less than the total interest of the grantor.) 1 SIMES AND SMITH, FUTURE INTERESTS, 2d ed., §8.1 (1956).

[5] See 3 SIMES AND SMITH, FUTURE INTERESTS, 2d ed., §1235 (1956); Leach, "Perpetuities in Perspective: Ending the Rule's Reign of Terror," 65 HARV. L. REV. 721 at 743 (1952).

[6] The common grantor obviously did not intend the final clause in the first deed to pass the defendant's interest in oil and gas; absent such intent, the effect of passing the interest should not be assigned to the clause. See 3 AMERICAN LAW OF PROPERTY §12.44 (1952).

[7] See 3 SIMES AND SMITH, FUTURE INTERESTS, 2d ed., §1241 (1956). But see Brown v. Independent Baptist Church of Woburn, 325 Mass. 645, 91 N.E. (2d) 922 (1950), where, in connection with a will, an executory interest void under the rule against perpetuities was held to pass as a reversion under the residuary clause to the same persons who were intended to take the void executory interest. There, however, the determinable fee had been granted to a third party. Apparently no one has undertaken to criticize the decision seriously. Discussions point out that the exemption of possibilities of reverter from operation of the Rule against Perpetuities made either alternative that faced the court undesirable. See note, 64 HARV. L. REV. 864 (1951); Leach, "Perpetuities in Perspective: Ending the Rule's Reign of Terror," 65 HARV. L. REV. 721 at 741 (1952). Professor Leach does, however, express a preference for a construction which would deny the double operation of an executed document.

namely, whether the Rule against Perpetuities should be applicable to a future interest which follows a grantor's reservation of an interest in oil and gas for an indeterminate time.[8] Conflicting theories as to the nature of a landowner's interest in oil and gas under his land suggest different answers to this problem.[9] Some states have decided that oil and gas can be owned as a separate estate in the land.[10] In contrast, other states have held that an oil and gas interest can be no more than an exclusive right to drill and remove these minerals.[11] In these latter jurisdictions the interest in oil and gas is considered incorporeal, and when separated by conveyance from the surface estate has the incidents of a profit à prendre.[12] In states espousing this non-ownership theory, future interests in oil and gas intended for the present owner of the surface estate may be saved from the Rule against Perpetuities by means of an argument suggested by Professor Gray.[13] The argument states that even if an incorporeal interest in land might terminate at a remote time, the rule does not apply to the succeeding interest if the prior interest terminates by disappearing into the servient estate rather than vesting in a third party.[14] In other words, such interests are simply ex-

8 In Victory Oil Co. v. Hancock Oil Co., note 3 supra, a grantor of real property reserved an interest in oil and gas for twenty years and as long thereafter as oil and gas were produced; the interest was to terminate if no oil or gas were found within five years, and the grantor was to pay royalty to the grantee. The grantee's interest in oil and gas (other than the royalty) was held void because of the Rule against Perpetuities. See comment, 53 MICH. L. REV. 462 (1955). The decision in the principal case merely causes confusion for persons who desire to know the status of such arrangements.

9 For general discussions of the prevailing property theories concerning oil and gas, see 1 SUMMERS, OIL AND GAS, c. 4 (1938); Cohen, "Property Theories Affecting the Landowner in a New Oil and Gas Producing State," 10 ALA. L. REV. 323 (1958).

10 See, e.g., Texas Co. v. Daugherty, 107 Tex. 226, 176 S.W. 717 (1915).

11 See, e.g., Callahan v. Martin, 3 Cal. (2d) 110 at 117, 43 P. (2d) 788 (1935). Oil and gas in their natural state are locked tightly in place, and in general migrate if, and only if, the pool in which they lie is tapped by drilling. It was originally believed that they migrated under ground as water does. See the discussion of these matters in Cohen, "Property Theories Affecting the Landowner in a New Oil and Gas Producing State," 10 ALA. L. REV. 323 at 325-327 (1958). Every jurisdiction which has had occasion to pass upon the issue holds that, exclusive of statute, a landowner has no cause of action for oil and gas drained from beneath his lands by drilling on adjacent tracts. See, e.g., Western Gulf Oil Co. v. Superior Oil Co., 92 Cal. App. (2d) 299, 206 P. (2d) 944 (1949) (non-ownership jurisdiction); Prairie Oil and Gas Co. v. State, (Tex. Com. App. 1921) 231 S.W. 1088 (ownership in place jurisdiction). It is also uniformly held, however, that the oil and gas estate can be severed from the surface estate and carved up into lesser interests. See, e.g., Brown v. Copp, 105 Cal. App. (2d) 1, 232 P. (2d) 868 (1951); 1 SUMMERS, OIL AND GAS, §133, p. 322 (1938); 2 AMERICAN LAW OF PROPERTY §10.6 (1952). Also, an interest in oil and gas is not subject to loss by abandonment. See 1 SUMMERS, OIL AND GAS §139 (1938). In light of these holdings, it is understandable that there might be some difference of opinion in categorizing this interest.

12 "It is generally recognized that the ownership or title to oil and gas in place is a limited interest of estate in land in the nature of a *profit à prendre*. . . ." Lever v. Smith, 30 Cal. App. (2d) 667 at 670, 87 P. (2d) 66 (1939). A profit à prendre is defined as an incorporeal right to take something of substance from the land of another. 3 TIFFANY, REAL PROPERTY, 3d ed., §839 (1939).

13 GRAY, RULE AGAINST PERPETUITIES, 4th ed., §279 (1942).

14 Compare 3 SIMES AND SMITH, FUTURE INTERESTS, 2d ed., §1248 (1956).

tinguished, and upon their "merger" with the servient estate, no new estate begins which could be subject to invalidation by remoteness.[15] But in jurisdictions holding that the landowner owns oil and gas as corporeal property, this argument is not applicable in cases where the owner excepts ownership in those substances from a conveyance of the surface estate.[16] However, the validity of the present landowner's future interest in the minerals under his surface estate should not depend upon categorization of the interest as corporeal or incorporeal.[17] Property categories which were not designed to take account of the peculiar features of interests in oil and gas cannot serve as satisfactory criteria for resolving all controversies arising out of such interests.[18] Rather than attempting doubtful categorization in order to resolve the perpetuities question, it would seem desirable to resort directly to the policy considerations involved in special circumstances like those in the principal case. One such consideration is that separation of oil and gas interests, for purposes other than immediate development, tends to hinder the rapid and orderly development of these vital resources, since many holders of these interests disappear and others use their interest to prevent the development of the oil and gas while exploiting more valuable holdings elsewhere.[19] Furthermore, a protracted separation may unduly hinder the useful over-all development of the entire tract.[20] In view of these arguments, it would seem that the Rule against Perpetuities should not be applied to void a future interest in oil and gas where the result would be to enlarge the reserved mineral interest from one limited to the duration of active production to one in fee, thereby extending indefinitely the separation of mineral and surface interests.

Robert B. Nelson, S.Ed.

[15] Cf. 2 AMERICAN LAW OF PROPERTY §8.98 (1952). Since California follows the non-ownership theory, the court could have used Gray's argument to resolve the controversy in the principal case.

[16] It would have application where a grantor merely reserved a right to take the substances.

[17] In view of the facts mentioned in note 11 supra, an assertion that interests in oil and gas are either corporeal or incorporeal can mean only that they appear, to those making the assertion, to be "more like" interests of the one type than of the other.

[18] See, generally, Ballem, "Pitfalls in the Categorization of Petroleum and Natural Gas Leases," 2 UNIV. B.C. LAW NOTES 329 (1956).

[19] See Cohen, "Property Theories Affecting the Landowner in a New Oil and Gas Producing State," 10 ALA. L. REV. 323 at 337 (1958).

[20] In several states severed estates in oil and gas can be terminated for non-user. Tenn. Code Ann. (1955) §64-704 (ten-year limitation); La. Civ. Code (Dart, 1945) §789 (ten-year limitation). In Crawford v. Texas Co., (W.D. La. 1953) 114 F. Supp. 218, the Louisiana statute was applied to facts similar to those in the principal case. In Virginia a severed title to oil and gas may be extinguished under certain conditions after 35 years non-user. Va. Code (1950) §55-154.