COMMENTARY

Crude awakening: Oil patch lawsuits shift into high gear

By Reagan M. Marble

Elizabeth Conley / Staff photographer

When oil prices plummet, contract disputes and lawsuits between oil and gas producers and landowners inevitably rise, says the author. Court cases could put the COVID-19 pandemic and Saudi-Russia "price war" in the spotlight.

Oil patch lawsuits between landowners and producers ramp up with clockwork predictability when the price of West Texas Intermediate dramatically sinks.

But when the price of crude crashed into the negative range on April 20, oil and gas litigation took an especially sharp turn. Now, oil and gas companies are trying to save themselves as landowners try to protect their royalty income. Here are a few of the latest trends:

Force majeure disputes

Most oil and gas leases include a "force majeure" clause. This clause allows parties to excuse their obligations under a contract due to events beyond their control, or force majeure events often described as "acts of God," "acts of war," "labor disputes" and "governmental orders."

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While industry friendly form contracts may include "lack of market" as a force majeure event, landowner friendly forms may specifically exclude market conditions from force majeure.

Boilerplate forms that were not the result of individual negotiations, however, are likely to contain boilerplate force majeure language that does not specifically mention the lack of market due to a global pandemic.

As a result, at least one state government (located immediately north of the Red River) asked President Donald Trump to declare the COVID-19 pandemic an "act of God" in an attempt to aid oil and gas companies in invoking force majeure clauses that use this more general term.

Just last week, a Texas oil company invoked its force majeure clause, citing the Russian-Saudi "price war" as the triggering event.

Media appeal notwithstanding, it remains to be seen whether the law will recognize a unilateral declaration from a government official or company that an occurrence is a force majeure event under a particular contract, a determination that is ordinarily left to the courts.

Shut-in wells

If an oil and gas company cannot delay its performance under an oil and gas lease through a force majeure clause, it may be able to do so by turning to its "shut-in" clause. This clause typically allows an oil and gas company to shut in a gas well by tendering a pre-agreed amount of money.

Some older form leases, however, may not specifically limit shut-in clauses to gas wells and would allow a company to shut in an oil well, too. There will, nevertheless, be situations where companies shut in wells that primarily produce oil but are "capable of producing gas," a move that would lead everyone involved back to the courthouse.

Lease terminations

If an oil and gas company cannot invoke force majeure or shut-in provisions, it may be forced to try to perpetuate the oil and gas lease by marginal production. Generally, companies must produce oil or gas "in paying quantities," which roughly means that revenues exceed expenses from operating and marketing oil and gas over a reasonable period of time.

When a barrel of oil costs less than a burger, expenses can quickly exceed revenues. Because many oil and gas companies were operating with little or no profit before the current price collapse, disputes between landowners and producers over whether an oil and gas lease is still "producing in paying quantities" are likely to proliferate in the near future.

In times like these, when asset value is diminishing, oil and gas companies and landowners alike should seek experienced legal counsel to navigate these developments and maintain maximum value of their assets.

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