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Oil and Gas Royalty Synonymous with Mineral Interest

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Criticism of the sales tax has long clustered about a charge that it is regressive in that it places an inordinate burden upon the poor. The extent to which a so called "separate" tax will be passed on to consumers is not to be easily determined.¹³ It is conceivable, however, that an assumption by vendors of a portion of the sales tax burden could assist in rebutting the argument that the tax works a hardship upon vendees who are possessed of limited assets.

There seems to be no doubt that the sales tax will, because of its revenue gathering attributes, insure its own survival.¹⁴ A realistic acceptance of the presence and permanence of the tax leaves small ground for condemnation of the innovation which Wyoming has placed upon it. The collection mechanisms in force throughout the nation are too broadly divergent in type and method to justifiably censor any one technique as a departure from some hypothetical norm. Judgment as to the attributes and evils of particular systems and features thereof must be founded upon sound principles of public welfare, fiscal need, and constitutional conformity.¹⁵

ELMER K. NELSON, JR.

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13. Dayton D. McKean, Soaking the Poor, *New Republic*, 84:121, Sept. 11, 1935: "A tax of 1 per cent is often absorbed by the seller".
 14. Robert C. Brown, *Some Legal Aspects of State Sales and Use Taxes*, (1943) 18 *Ind. L. J.*, P. 78: "The enormous productivity of the sales tax, even in periods of comparative financial stress, is likely to insure, not merely its maintenance, but its continual extension."
 15. In *Walgreen Company v. State Board of Equalization*, Civil Number 3045, an action pending before the District Court of the United States for the District of Wyoming, an injunction is presently being sought, on grounds of constitutionality, against the payment of the tax attacked in the instant case.

OIL AND GAS ROYALTY SYNONYMOUS WITH MINERAL INTEREST

In an action for an accounting the parties were in sharp conflict as to the meaning of the term "royalty" as used in an oral contract and in letters pertaining to the contract. Hudson owned a one-half interest in and under three separate tracts of land, which he conveyed to the Mabee Oil and Gas Co. reserving to himself a one-fourth interest in the profits in excess of \$6,000.00. In letters relating to the oral contract, Hudson always referred to his interest as the "mineral interest", while Mabee referred to Hudson's interest as the "royalty" interest. The dispute arose when Hudson contended that he was to receive his share from all the profits derived from the "mineral interest" even after the expiration of the existing leases, whereas Mabee contended that Hudson was to receive his share from the existing leases only. The first drilling had resulted in dry holes and after the expiration of the leases the Mabee Co. developed the property and realized substantial production. In determining the case the trial court held that the term "royalty" as used in the contract was synonymous with the term "mineral interest" and that Hudson's "royalty" was a real property interest. This decision was upheld by the Tenth Circuit Court of Appeals as being the meaning attached to the term "royalty" in the Oklahoma oil fraternity. *Hudson v. Mabee Oil & Gas Co.*, (1946) 156 F. (2d) 450.

Historically the term "royalty" in English law applied to certain rights reserved to the Crown, such as the right to a percentage paid to the Crown of all gold and silver taken from mines, or a tax exacted in lieu of such share, hence a share of the product or profit reserved to the owner of land for permitting another to use the property.¹ The term "royalty" in the oil and gas business has come to have several connotations which cause considerable confusion in interpretation and usage; such as what is meant by "lessor's royalty", "leasee's royalty", "overriding royalty", "unaccrued royalty" and "participating royalty". The question raised is whether it is an interest in real property or an interest in personal property. In the strict sense the term "royalty" as used in the foremost oil and gas producing states, means a share of the product or profit reserved to the owner of land for permitting another to produce oil and gas thereon.²

The courts seem to be about evenly divided as to whether a "royalty" interest is a real property interest or a personal property interest.³ It has even been suggested that "royalty" is a distinct species of property.⁴ Cases holding that a "royalty" interest is a real property interest include, among others, the following: A case on taxation,⁵ a case of quiet title,⁶ cases on the applicable section of the statute of frauds,⁷ a case involving inheritance and reversion,⁸ and

1. See, *Blake: The Oil and Gas Lease*, (1940) 13 So. Cal. L. Rev. 393, 410.
2. *Carroll v. Bowen*, (1937) 180 Okla. 215, 68 P (2d) 773; *Homestake Exploration Corp. v. Schoregge*, (1928) 81 Mont. 604, 264 Pac. 388; *Robinson v. Jones*, (1925) 119 Kan. 609, 240 Pac. 957; *Hill v. Roberts*, (1926) (Tex. Civ. App.) 284 S. W. 246; *Indiana Natural Gas & Oil Co. v. Stewart*, (1910) 45 Ind. App. 554, 90 N. E. 384; *McIntire's Adm'r v. Bond*, (1929) 227 Ky. 607, 13 S. W. (2d) 772; see *Sartor v. United Gas Pub. Serv. Co.*, (1937) 186 La. 555, 173 S. 103.
3. The following are some of the cases holding that royalty, when used in the conveyance or lease of oil and gas rights, means an interest in real property: *United States v. Looney*, (1929) (C.C.A. 5th), 29 F. (2d) 884; *Pugh v. Commissioner of Int. Rev.*, (1931) (C.C.A. 5th), 49 F. (2d) 76, Cert. Denied (1931) 284 U. S. 642, 52 Sup. Ct. 22; *Arrington v. United Royalty Co.*, (1933) 188 Ark. 270, 65 S. W. (2d) 36; *Hager v. Stakes*, (1927) 116 Tex. 453, 294 S. W. 835; *Musgrave v. Musgrave*, (1920) 86 W. Va. 119, 103 S.E. 302; *Marias River Syndicate v. Big West Oil Co.*, (1934) 98 Mont. 207, 38 P (2d) 599; *Updegraff v. Blue Creek Coal & Land Co.*, (1914) 74 W. Va. 316, 81 S.E. 1050. Likewise in the following cases it has been held to be personal property: *Nonamaker v. Amos*, (1905) 73 Ohio St. 163, 76 N.E. 949; *Wetengel v. Gormley*, (1898) 184 Pa. St. 354, 39 Atl. 57; *Curley v. Anderson and Patterson*, (1921) (Tex. Civ. App.) 235 S.W. 622; *O'Brien v. Jones*, (1922) (Tex. Civ. App.) 239 S.W. 1013; *Campbell v. Lynch*, (1917) 81 W. Va. 374, 94 S.E. 739, but see *Musgrave v. Musgrave*, (1920) 86 W. Va. 119, 103 S.E. 302, which in effect overrules the *Campbell* case; *Pure Oil Co. v. Kindall*, (1927) 116 Ohio St. 188, 156 N. E. 119; (contra *Marias River Synd. v. Big West Oil Co.*, (1934) 98 Mont. 207, 38 P (2d) 599).
4. See *Levy: A Distinct Species of Property*, (1938) 11 So. Cal. L. Rev. 319, wherein the author proposes for consideration and discussion a classification of royalty which will more properly fit into the law. He suggests, either, (1) recognition of the term royalty as including any share of production . . . ; or (2) limitation of such term to cases in which a percentage of production is given for the privilege of drilling for and producing of oil and gas . . . This whether the interests involved be classified as realty or personalty—one factor in common to each: They are all intended to, and purport to convey a present right to share in future production of oil and gas from particular premises.
5. *Hager v. Stakes*, (1927) 116 Tex. 453, 294 S.W. 835.
6. *Taylor v. Higgins, Oil and Fuel Co.*, (1928) (Tex. Civ. App.) 2 S.W. (2d) 288.
7. *Robichaux v. Bordages*, (1932) (Tex. Civ. App.) 48 S.W. (2d) 698; *Allen v. Thompson*, (1925) 169 Ark. 169, 273 S.W. 396; *Arrington v. United Royalty Co.*, (1933) 188 Ark. 270, 65 S. W. (2d) 36.
8. *McIntire's Adm'r. v. Bond*, (1929) 227 Ky. 607, 13 S. W. (2d) 772.

cases involving "royalty" as the subject matter of a conveyance.⁹ On the other hand "royalty" has been held to be an interest in personal property in a case involving a lease for a definite term of years,¹⁰ in a case construing a lease reserving a "royalty" to the grantor,¹¹ in a case holding "royalty" to be personalty under the statute of frauds,¹² in a case regarding a share of oil actually produced,¹³ and in a case where a deed referred only to "royalty" as reserved and not to oil and gas as reserved.¹⁴

No substantial definition of the term has ever been stated. Consequently it has been applied to various types of property interests; but in general "royalty" when connected with oil and gas *in situ* is held to be an interest in real property, whereas it is generally held to be an interest in personal property when connected with oil and gas already extracted.¹⁵

Since the earth may be divided horizontally as well as vertically, it would seem that the oil and gas rights in land should be severable from the general estate. The result is that an oil right becomes an incorporeal hereditament; therefore a severance of the title to the "mineral interest" from the title to the surface land supports the real property view of the term "royalty". Although a few states, New York,¹⁶ Louisiana,¹⁷ and Indiana¹⁸ do not give recognition to such a severance, the majority of the oil producing states, Arkansas,¹⁹ Kansas,²⁰

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9. In *Godfrey v. Central State Bank*, (1928) (Tex. Civ. App.) 5 S.W. (2d) 529, reversed on other grounds (1930) 29 S.W. (2d) 1015, it was held that the intent of the parties in using the terms royalty and mineral rights in correspondence arranging a sale the reference of both terms was to the same subject matter; namely real estate in the oil and gas in the ground; cf. *United States v. Looney*, (1929) C.C.A. 5th 29 F. (2d) 884, which held that royalty was an interest in land, but did identify royalty with title to oil in the ground.
 10. *Wettengel v. Gormley*, (1898) 184 Pa. 354, 39 Atl. 57.
 11. *Nonamaker v. Amos*, (1905) 73 Ohio 163, 76 N.E. 949.
 12. *O'Brien v. Jones*, (1922) (Tex. Civ. App.) 239 S.W. 1013; contra *Hager v. Stakes*, (1927) 116 Tex. 453, 294 S.W. 835.
 13. *Corrigan v. Shell Petroleum Corp.*, (1933) (Tex. Civ. App.) 62 S.W. (2d) 663; cf. *South Penn. Oil Co. v. Haught*, (1913) 71 W. Va. 720, 78 S.E. 759.
 14. *Pureoil Co. v. Kendall*, (1927) 116 Ohio St. 188, 156 N.E. 119.
 15. See, *Blake: The Oil and Gas Lease*, (1940) 13 So. Cal. L. Rev. 393, 408.
 16. *Shepard v. McCalmont Oil Co.*, (1885) 38 Hun. (N. Y.) 37; cf. *Lovelace v. Southwestern Petroleum Co.*, (1920) (C.C.A. 6th) 267 F. 513.
 17. The early cases inclined to the majority rule: *Strother v. Manghum*, (1915) 138 La. 437, 70 So. 426; *DeMoss v. Sample*, (1918) 143 La. 243, 78 So. 482; *Calhoun v. Ardis*, (1918) 144 La. 311, 80 So. 548, rehearing denied (1919). However in later cases considering the question again, the court held that separate ownership of oil and gas apart from the land, not only would not be recognized, but that such was forbidden by law. The reason being that there is no absolute ownership of minerals *in situ* and a conveyance of the minerals in fee is repugnant to the grant. *Frost Johnson Lumber Co. v. Sallings' Heirs*, (1920) 150 La. 756, 91 So. 207; *Pugh v. Commissioner of Int. Rev.*, (1931) (C.C.A. 5th) 49 F. (2d) 76, cert. Denied (1931) 52 Sup. Ct. 22; *Leiber v. Ouachita Natural Gas & Oil Co.*, (1922) 153 La. 160, 95 So. 538; *Wetherby v. Railroad Lands Co.*, (1923) 153 La. 1059, 97 So. 40.
 18. *Peoples Gas Co. v. Tyner*, (1892) 131 Ind. 277, 31 N.E. 59; *Heller v. Dailey*, (1902) 28 Ind. App. 555, 63 N.E. 490.
 19. *Bodcaw Lumber Co. v. Goode*, (1923) 48 Ark. 160, 254 S.W. 345.
 20. *Kurt v. Lanyon*, (1905) 72 Kan. 60, 82 P. 459; *Moore v. Griffen*, (1905) 72 Kan. 164, 83 P. 395; *Luman v. Davis*, (1921) 108 Kan. 801, 196 P. 1078.

Kentucky,²¹ Michigan,²² Montana,²³ Ohio,²⁴ Pennsylvania,²⁵ Tennessee,²⁶ Texas,²⁷ and West Virginia,²⁸ do recognize such a severance. Recent Oklahoma cases clearly indicate that the courts of that state do not recognize the severance of title doctrine as noted above, but only recognize the severance of the right to search for oil and gas and the courts hold that such a right is an interest in real property.²⁹

The problem in Wyoming has been the same as in the rest of the petroleum jurisdictions. The taking of oil and gas from the ground is a depletion of the freehold and a grant to do so has been held to be a grant of a "royalty" by the Supreme Court of Wyoming.³⁰ The Court thus treats it as real property. There can be no doubt but that when oil and gas have been brought to the surface Wyoming Courts recognize them as personal property.³¹ This holding is in line with the view taken by the Supreme Court of the United States, "that rents and royalties were profits issuing out of the land. When they accrued they became personal property; but rents and royalties to accrue were a part of the estate remaining in the lessor".³²

Wyoming courts favor the view that a "royalty" is an interest in real property, although recognizing the dual nature attached to the term. A percentage of oil and gas produced under a Government permit for only a term of years is personal property,³³ but a deed to oil and gas in and under a certain tract of land was held to be a conveyance of a real property interest.³⁴ Likewise a "royalty" interest in oil not limited to a term of years is considered to be a real property interest. Thus a deed granting a one-sixteenth of all oil and minerals is a grant of a real property interest and is considered to be a grant of a "royalty" by

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25. *Hyde v. Rainey*, (1912) 233 Pa. 540, 82 Atl. 781; *Mandle v. Gharing*, (1917) 256 Pa. 121, 100 Atl. 535; *Hamilton v. Foster*, (1922) 272 Pa. 95, 116 Atl. 50.
 26. *Murray v. Allard*, (1897) 100 Tenn. 100, 43 S.W. 355.
 27. *Texas Co. v. Daugherty*, (1915) 107 Tex. 226, 176 S.W. 717; *Stephens County v. Mid-Kansas Oil & Gas Co.*, (1923) 113 Tex. 160, 254 S.W. 290; *Luse v. Boatman*, (1919) (Tex. Civ. App.) 217 S.W. 1096; *States Oil Corp v. Ward*, (1920) (Tex. Civ. App.) 223 S.W. 250, reversed on other grounds in (1922) (Comm. of App. of Tex., Sect. A) 236 S.W. 446.
 28. *Williamson v. Jones*, (1894) 39 W. Va. 231, 19 S.E. 436; later appeal (1897) 43 W. Va. 562, 27 S.E. 411; *Harris v. Cobb*, (1901) 49 W. Va. 350, 38 S.E. 559; *Kiser v. McLean*, (1910) 67 W. Va. 294, 67 S.E. 725; *Snodgrass v. Koen*, (1918) 82 W. Va. 337, 96 S.E. 606; *Hale v. Grow*, (1921) 88 W. Va. 173, 106 S.E. 409.
 21. *Scott v. Laws*, (1919) 185 Ky. 440, 215 S.W. 81; *Hoskins v. Northern Lee Oil & Gas Co.*, (1922) 194 Ky. 628, 240 S.W. 377.
 22. *Weaver v. Richards*, (1909) 156 Mich. 320, 120 N.W. 818.
 23. *Krutzfeld v. Stevenson*, (1930) 86 Mont. 463, 284 P. 553; *Broderick v. Stevenson Consolidated Oil Co.*, (1930) 88 Mont. 34, 290 P. 244; *Hodgkiss v. Northland Petroleum Consolidated*, (1937) 104 Mont. 328, 67 P. (2d) 811; cf. *Rist v. Toole County* (1945) 159 P. (2d) 340, 162 A.L.R. 406.
 24. *Curtis v. Chartiers Oil Co.*, (1911) 34 Ohio C.C. 106; 14 Ohio C.C.N.S. 593, affirmed in (1913) 88 Ohio St. 594, 106 N.E. 1053, without opinion.
 29. *Melton v. Snead*, (1940) 188 Okla. 388, 109 P. (2d) 509; *Hudson v. Smith*, (1935) 171 Okla. 79, 41 P. (2d) 861.
 30. *State v. Snyder*, (1923) 29 Wyo. 163, 212 P. 758, see *State v. Hoskins*, (1923) 29 Wyo. 198, 212 P. 766.
 31. *Denver Joint Stock Land Bank of Denver v. Dixon*, (1942) 57 Wyo. 523, 122 P. (2d) 842.
 32. *United States v. Noble*, (1915) 237 U.S. 74, 35 Sup. Ct. 532.
 33. *Rue v. Merrill*, (1931) 42 Wyo. 497, 297 P. 375.
 34. *Tendolle v. Eureka Oil Syndicate*, (1928) 38 Wyo. 442, 268 P. 185.

the Wyoming Supreme Court.³⁵ The holding in this case clearly shows that a "royalty" is a real property interest and as such may be synonymous with mineral interest.

There is obviously great need for caution in its use. And while the decision in the principal case seems sound, no hope of reducing litigation appears justified so long as a term as ambiguous as "royalty" is used in oil and gas transactions.

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35. *Denver Joint Stock Land Bank of Denver v. Dixon*, (1942) 57 Wyo. 523, 122 P. (2d) 842.