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Playing the "Wild Card" in the Highstakes Game of Urban Drilling: Unconscionability in the Early Barnett Shale Gas Leases

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NOTES AND COMMENTS

PLAYING THE "WILD CARD" IN THE HIGH-STAKES GAME OF URBAN DRILLING: UNCONSCIONABILITY IN THE EARLY BARNETT SHALE GAS LEASES

J. Zach Burt

I. INTRODUCTION

As the price of oil and gas continues to rise, there is mounting public pressure to reduce the United States's dependence on foreign energy sources.[1] However, conventional petroleum reserves are dwindling in this country, forcing energy companies to set their sights on "unconventional domestic sources."[2] This search for new and unconventional domestic sources recently led oil companies to flock to an unlikely spot—a patch of land in North Texas, known as the "Barnett Shale," that already seemed tapped from fifty years of intense oil

1. Marc Airhart, Press Release, Jackson Sch. of Geosciences, Univ. of Tex. at Austin, Barnett Boom Ignites Hunt for Unconventional Gas Resources (Jan. 2007), http://www.jsg.utexas.edu/news/feats/2007/barnett.html.
2. *Id.*

and gas drilling.[3] The Barnett Shale is a unique natural gas play because much of the untapped gas lies beneath the highly-populated region of Tarrant County, which includes the Fort Worth metropolitan area[4]—not the wide-open spaces of West Texas where one might expect drilling for natural gas to occur. Also unique to the Barnett Shale are the numerous legal questions arising as a result of the oil and gas industry colliding with this heavily-populated urban area. The purpose of this Comment is to explore one of the legal questions exposed by the unprecedented Barnett Shale situation: whether a claim of unconscionability could be brought by early signers of Barnett Shale gas leases.

Fort Worth residents, and those living in surrounding areas, were first introduced to the Barnett Shale when they began to receive offers from oil and gas companies wanting to lease their mineral rights. Some offers just started arriving in residents' mailboxes,[5] while others learned about the Barnett Shale through various oil gas company representatives or landmen who were busy going door-to-door[6] with lease forms in hand, seeking permission to drill for the natural gas under the homes and businesses of Tarrant County residents.[7] One Tarrant County newspaper likened the urban leasing effort to a "well-orchestrated" and "well-funded" political campaign.[8] Because of the Barnett Shale, this age-old practice of mineral-rights leasing has been thrust into a whole new realm that was surely not envisioned by the old Texas wildcatters who used to roam the plains of Texas waiting for the next oil boom. Thus, with the unprecedented Barnett Shale urban leasing effort in full effect and happening at a rapid pace in 2008, new legal questions about the age-old practice of mineral rights-leasing have come to the forefront.

When the Barnett Shale natural-gas-boom began, most Tarrant County residents were unaware what legal rights they had to the natural gas lying below their feet or even what legal rights they were signing away when they signed a lease with an oil and gas company.[9] The majority of residents did not know the difference between surface and mineral rights or even whether they owned the rights to any oil and

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3. *Id.*

4. *Id.*

5. Alyson Ward, *Hidden Treasure: The Barnett Shale*, FORT WORTH STAR-TELEGRAM, Dec. 31, 2006, at G9, *available at* 2006 WLNR 22756088.

6. Dan Piller, *When Drillers Call: How to Deal with Sudden Mineral Wealth*, FORT WORTH STAR-TELEGRAM, Apr. 9, 2006, at F1, *available at* 2006 WLNR 5971973; *see also* Laurie Fox & Marice Richter, *They're Getting to Know the Drill*, DALLAS MORNING NEWS, Mar. 27, 2007, *available at* http://www.dallasnews.com/sharedcontent/dws/news/localnews/stories/032707dnmeturbandrilling.39a2721.html (describing landmen "moving through neighborhoods with military precision").

7. Bruce Nichols, *Fort Worth, Gas Boom Fuels Public Outreach Plan*, July 11, 2007, http://www.reuters.com/article/idUKN1141711220070711.

8. Fox & Richter, *supra* note 6.

9. *See* Nichols, *supra* note 7.

gas that could potentially be found beneath their quarter-acre lot.[10] In the early days of the Barnett Shale boom, most homeowners did not have the experience or the expertise to negotiate a lease with a seasoned oil and gas company (or the landman who represented it) and would sign leases without knowing what they were signing.[11]

Without knowing where to turn for answers, residents began to flood City Hall with questions such as: "I've got a lease offer with a twenty-five percent royalty and a $300 bonus. Is this a good offer? Should I sign it?"[12] However, at the beginning of the Barnett Shale boom most of these questions went unanswered because many Tarrant County officials were just as unprepared for the Barnett Shale boom as their residents.[13] This is not a remark intended to disparage the intelligence of Tarrant County residents, but merely a recitation of the fact that most laypersons, and even most attorneys who are not versed in the oil and gas law, lack the understanding of an oil and gas lease to be able to effectively negotiate a good bargain for a mineral rights owner.[14]

In the early stages of the Barnett Shale boom, most leases offered to Tarrant County residents included signing bonuses between $300 and $400 per residential lot and royalty terms between 12.5% and 18.5%.[15] In addition, most early Barnett Shale leases were unlikely to contain lease provisions favorable to the Tarrant County residents.[16] Lease terms providing for restrictions on surface-right access, road access restrictions, noise-and-pollution restrictions, and lease terms prohibiting drilling operations during certain times of day were uncommon in the early stages of Barnett Shale leasing.[17] Lease terms such as these were likely left out of early Barnett Shale leases because

10. *Id.*

11. Jim Fuquay, *With Piles of Dollars at Stake, Neighborhoods Unite, Groups are Sometimes Able to Get Better Deals on Gas and Oil Leases,* FORT WORTH STAR-TELEGRAM, Nov. 11, 2007, at F1, *available at* 2007 WLNR 22291606.

12. *See* Nichols, *supra* note 7.

13. *See* Laurie Fox, *Barnett Shale Gas Field Paying Off,* DALLAS MORNING NEWS, May 17, 2007, *available at* http://www.dallasnews.com/sharedcontent/dws/news/city/fortworth/stories/051707dnmetbarnettshale.37ed2d2.html; *see also* Nichols, *supra* note 7 (discussing the need to do a better job educating the public about the Barnett Shale).

14. *See* Owen L. Anderson, *David v. Goliath: Negotiating the "Lessor's 88" and Representing Lessors and Surface Owners in Oil and Gas Lease Plays,* 27 ROCKY MTN. MIN. L. INST. 2 (1982), *available at* 27 RMMLF-INST 2 (Westlaw); Ronald D. Nickum, *Negotiating and Drafting a Modern Oil and Gas Lease on Behalf of Lessor,* 13 TEX. TECH. L. REV. 1401, 1402–03 (1982).

15. Leasing: Why it Pays to Stick Together, posting of Jim Fuquay to Barnett Shale: Drilling Deep for Answers About the Natural Gas Boom in North Texas [hereinafter Barnett Shale], http://startelegram.typepad.com/barnett_shale/2007/10/leasing-why-it-.html (Oct. 5, 2007, 11:31 EST); *see also* Mitchell Schnurman, *Fair Lease Provisions Take Leverage,* FORT WORTH STAR-TELEGRAM, Oct. 1, 2006, at F1, *available at* 2006 WLNR 17000709.

16. *See* Ward, *supra* note 5.

17. *See Id.*

early signers did not know they should negotiate or ask for such terms.[18] Residents, enticed by the bonus money and promise of a monthly royalty check, were not concerned about whether they were offered a good deal in comparison to other Barnett Shale leases being signed by their neighbors. Instead, early signers of Barnett Shale leases were seemingly motivated by the fear that if they did not sign quickly, then they would be missing out.[19]

Today, it is a very different story. In early 2008, lease offers to Tarrant Country residents were reaching as high as $18,250 per acre with 27.5% royalties.[20] Furthermore, as a direct result of Tarrant County residents becoming more knowledgeable about the leasing process and neighborhoods organizing and working together, residents are now able to negotiate more favorable lease terms on top of the better bonuses and royalty payments. As fewer and fewer mineral rights are left to be leased in Tarrant County, the sky is the limit for how high lease offers will eventually go. In fact, in late January 2008, a neighborhood in Fort Worth took leasing negotiations to a new level and pitched an offer to the oil and gas companies instead of waiting for the offers to come to them.[21] What was the offer? The best Barnett Shale mineral lease offer to date: $30,000 per acre bonus, and a 30% royalty, along with lease terms that include a primary term of one year and a requirement that the drill site be separated from residences by at least 800 feet.[22] Today, the residents of Tarrant County and the surrounding areas, who are currently negotiating mineral leases or about to start the negotiating process, have benefited financially from this increased awareness, knowledge of the leasing process, and increased competition for their mineral rights.

But what about those who signed leases in the early stages of the Barnett Shale boom? Being uneducated about mineral rights-leasing and unprepared to face negotiations with sophisticated oil and gas companies and landmen, were the early signers of Barnett Shale leases simply the unfortunate pioneers of this unprecedented phenomenon known as "urban leasing?" The early signers of Barnett Shale leases were not privy to the knowledge of how to gain a better bargaining position by organizing their neighborhoods or the benefits of waiting until the competition for their mineral rights heats up before they signed a mineral lease. Are these early signers of Barnett Shale leases simply out of luck? Or is there a legal remedy available to the early signers of Barnett Shale leases that could help even the playing

18. *See Id.*

19. Fox & Richter, *supra* note 6.

20. Scott Nishimura et al., *Chesapeake's Lease Offer is Highest Yet, Group Says*, FORT WORTH STAR-TELEGRAM, Jan. 9, 2008, at C1, *available at* 2008 WLNR 450245.

21. Jim Fuquay, *Group Is Asking for Big Bonus and Royalty*, FORT WORTH STAR-TELEGRAM, Jan. 19, 2008, at C1, *available at* 2008 WLNR 1096798.

22. *Id.*

field or rescind a lease and allow early signers a chance to renegotiate? This Comment will explore potential answers to these questions.

Part II of this Comment provides background information on the Barnett Shale, including a physical description of the Barnett Shale and why it is such an unusual natural gas play. Part III of this Comment introduces the legal document known as the oil and gas lease and explains what legal rights are created when one signs a lease with an oil and gas company. One cannot expect to understand the legal questions that may arise with Barnett Shale gas leases without first understanding the basics of an oil and gas lease. Part IV of this Comment analyzes the area of contract law known as unconscionability, which may be available to the early signers of Barnett Shale leases who want to rescind, renegotiate, or cancel an oil and gas lease. Finally, Part V of this Comment discusses the lessons that hopefully have been learned from the Barnett Shale urban leasing phenomenon and suggests how other cities may better prepare and protect their citizens when the next Barnett Shale is discovered.[23]

II. THE BARNETT SHALE

Before one can understand the setting in which questions of unconscionable Barnett Shale gas leases may arise, background information on the Barnett Shale is needed. The Barnett Shale is a hydrocarbon-producing geological formation which consists of sedimentary rock.[24] The productive portion of the Barnett Shale formation is estimated to stretch 5,000 square miles from the city of Dallas west and south covering at least 18 counties.[25] The Barnett Shale is estimated to contain more than 26 trillion cubic feet of natural-gas resources, making it the largest active onshore gas field in Texas and one of the largest in the United States.[26]

Drilling in the Barnett Shale is often thought to be a recent phenomenon. In fact, the field was discovered, and the first well was drilled, in 1981.[27] However, the possibility for significant production from the Barnett Shale did not become feasible until improvements in recovery methods were developed in the late 1990s.[28] Even with this

23. Airhart, *supra* note 1 (discussing the "Fayetteville Shale" formation in the Arkoma Basin in Arkansas having many of the same characteristics that made the Barnett Shale).

24. R.R. Comm'n of Tex., Barnett Shale Information, http://www.rrc.state.tx.us/barnettshale/index.html (last visited Sept. 21, 2008).

25. The Perryman Group, Bounty from Below: The Impact of Developing Natural Gas Resources Associated with the Barnett Shale on Business Activity in Fort Worth and the Surrounding 14-County Area 24 (2007), http://www.barnettshaleexpo.com/docs/Barnett_Shale_Impact_Study.pdf.

26. Barnett Shale Energy Educ. Council, About Barnett Shale, http://www.bseec.org/index.php/content/facts/about_barnett_shale/ (last visited Aug. 31, 2008).

27. *Id*; *see also* The Perryman Group, *supra* note 25, at 23.

28. The Perryman Group, *supra* note 25, at 23.

newly developed technology, drilling in the Barnett Shale was virtually unheard of as recently as the turn of this century. It was not until natural-gas prices increased, making the new recovery technology more economically feasible, that production in the Barnett Shale accelerated rapidly.[29] By July 2007, more than 6,600 natural-gas wells had been drilled in the Barnett Shale.[30] These wells have resulted in 2.6 trillion cubic feet of natural gas being produced from the Barnett Shale since the year 2000.[31]

What makes this natural-gas play so unusual, besides its size and production, is that much of the Barnett Shale is located in a highly urbanized area.[32] Currently, the majority of Barnett Shale production is happening within the city limits of Fort Worth, Texas. A city of more than 600,000 residents,[33] Fort Worth had almost 800 wells within its city limits by July 2007.[34] Fort Worth city officials project there will be at least 1,160 wells by the end of 2010.[35]

The financial reach of the Barnett Shale affects all facets of life in Tarrant County. The Barnett Shale activity is projected to bring more than 108,000 jobs per year to North Texas through the year 2015.[36] The Barnett Shale activity contributes $3 billion in retail sales in North Texas per year.[37] Barnett Shale drilling on city-owned land is expected to earn the city of Fort Worth $972 million in leases and bonuses over the next 20 to 30 years.[38] Property-tax revenues from the wells drilled on city land could bring that total to more than $1 billion.[39] It is projected that $153 billion of real gross product will be generated by the Barnett Shale in a fourteen-county region in North Texas by 2015.[40] Considering that the Barnett Shale is expected to produce activity for twenty to thirty years,[41] there will be a huge economic impact on many generations to come.

The oil and gas companies, along with the various local governments in the Barnett Shale area, have understood the potential eco-

29. Barnett Shale Energy Educ. Council, *supra* note 26; *see also* The Perryman Group, *supra* note 25, at 23.

30. Nichols, *supra* note 7.

31. R.R. Comm'n of Tex., Texas Gas Well Production in the Newark, East (Barnett Shale) Field, 1993 Through 2006, http://www.rrc.state.tx.us/barnettshale/NewarkEastField_1993-2006.pdf (last visited Sept. 21, 2008).

32. Airhart, *supra* note 1.

33. U.S. Census Bureau, Population Estimates for the 25 Largest U.S. Cities, June 28, 2007, *available at* http://www.census.gov/Press-Release/www/2007/cb07-91table1.pdf.

34. Nichols, *supra* note 7.

35. The Perryman Group, *supra* note25, at 23.

36. *Id.* at 8.

37. Fox, *supra* note 13.

38. Mike Lee, *Plans for Natural Gas Windfall Finalized,* FORT WORTH STAR-TELEGRAM, Jan. 9, 2008, at B1, *available at* 2008 WLNR 450220.

39. Barnett Shale Energy Educ. Council, *supra* note 26.

40. The Perryman Group, *supra* note 25, at 18.

41. *Id.* at 8.

nomic impact from the beginning. The residents, on the other hand, were largely uninformed—but not any more. In 2008, the incentives behind signing a Barnett Shale gas lease have significantly improved because the residents of Tarrant County are no longer uneducated about the process of mineral rights-leasing.[42] Realizing they potentially have thousands of dollars at stake when they sign a Barnett Shale lease, the citizens of Tarrant County have educated themselves on the process of oil and gas leasing and on the legal rights they have to the natural gas in the Barnett Shale.[43] They have also organized their neighborhoods in order to secure a better bargaining positioning against the professional oil and gas companies and landmen seeking their signatures on mineral right leases.[44]

Tarrant County officials and the city of Fort Worth have joined in the education effort. In May 2007, the City of Fort Worth organized and hosted the "Barnett Shale Expo" at the Tarrant County Convention Center.[45] This first area-wide effort to educate the public on the Barnett Shale assembled energy companies, speakers, and exhibitors to educate the public on mineral rights and environmental issues and answer questions.[46] In November 2007, a website was launched in order to provide a source for fact-based information for residents who had questions about important topics such as drilling, leasing, safety, and natural gas.[47] In addition, the Barnett Shale Energy Education Council (BSEEC) was created by eight companies leading the development of the Barnett Shale in order to provide the community with a resource for information about gas drilling and production in the Barnett Shale.[48] Finally, the *Fort Worth Star-Telegram*, the leading newspaper in the Tarrant County area, has created an online blog that discusses topics such as leasing offers in area neighborhoods, to what goes on at City Hall, and information concerning the landmen and drilling companies that are working in the Barnett Shale.[49] This coordinated education effort is paying off for the residents of Tarrant County because they now know how to "play the leasing game" and

42. Fuquay, *supra* note 11.

43. *Id.*

44. *Id.*

45. *See* Fox, *supra* note 13.

46. *Id.*

47. Press Release, Barnett Shale Energy Educ. Council, The New Barnett Shale Energy Education Council Launches Web Site to Help the Public Understand Issue (Nov. 1, 2007), http://www.bseec.org/index.php/content/news_detail/pr_release1/stories.

48. *Id.*

49. Barnett Shale: Drilling Deep for Answers About the Natural Gas Boom in North Texas, http://startelegram.typepad.com/barnett_shale/about_this_blog/index.html (last visited Sept. 18, 2008).

understand that they "hold the ultimate card" if they own mineral rights.[50]

So what is it exactly about the Barnett Shale that gives rise to unprecedented legal questions? Anyone who has taken a first-year law course in Property knows that before oil and gas companies can drill for minerals, they must own or lease the rights to those minerals. The practice of leasing mineral rights is certainly nothing new—especially in the state of Texas—however, oil and gas companies commonly lease thousands of acres at a time.[51] But, in order to get to the richest part of the Barnett Shale, leasing thousands of acres at a time is simply not possible. As noted, the richest part of the Barnett Shale lies under the Fort Worth metropolitan area, and with the average citizen of Fort Worth owning a quarter-acre lot, there has been an unprecedented rush to lease as many mineral rights as possible.[52] In order to comply with Texas law, an oil and gas company needs at least forty acres before a well can be drilled.[53] Thus, before it receives a permit to drill a natural-gas well to tap into the Barnett Shale, an oil and gas company will need an average of 160 leases from Tarrant County residents.

This frenzy to lease as many mineral rights as possible has spawned a new phenomenon, which many are calling "urban leasing."[54] Urban leasing has attracted hundreds of landmen to Tarrant County, the city of Fort Worth, and throughout the various counties the Barnett Shale covers.[55] Landmen, described in layman's terms as "people who collect and manage mineral-right leases," have descended upon the Barnett Shale natural-gas play to research deed records and try to gather as many residents' signatures on Barnett Shale gas leases as possible.[56] Some landmen work directly for one of the many oil and gas companies that are active in the Barnett Shale, while others work independently from any particular oil and gas company.[57] But regardless of whether they are independent of a particular oil company or not, a landman's goal is the same—locate as many mineral owners as possible and negotiate oil and gas leases with them.[58] This record migration of landmen working zealously to lease mineral rights to the Barnett Shale has resulted in more than 100,000 mineral-rights leases

50. *See* Fox & Richter, *supra* note 6 (discussing the fact that residents "hold the ultimate card" in lease negotiations).

51. *See* Nichols, *supra* note 7.

52. *See* Fox, *supra* note 13; *see also* Fox & Richter, *supra* note 6.

53. 16 TEX. ADMIN. CODE § 3.38(b) (Vernon 2008).

54. *See* Fox & Richter, *supra* note 6; *see also* Fox, *supra* note 13.

55. Jim Fuquay, *Drilling Boom Spurs Demand for Landmen,* FORT WORTH STAR-TELEGRAM, Jan. 6, 2008, at E1, *available at* 2008 WLNR 309095.

56. *Id*

57. *Id.*

58. *Id.*

filed in 2007 in Tarrant County alone,[59] turning mineral leasing and royalties into a multibillion-dollar business affecting thousands of residents.[60] In Texas, a single document can transform minerals into millions of dollars—that document is known as the oil and gas lease.

III. THE OIL AND GAS LEASE

Interests in oil and gas are created and transferred like interests in other real property.[61] However, the terminology and underlying economics surrounding the creation and transfer of an oil and gas interests are unique. A fundamental principle of the law of property is that a person owning property has ownership, or a property right, in a whole collection of duties, privileges, benefits, and obligations with respect to the use, enjoyment, and possession of a specific piece of property.[62] This collection of property rights is called a "bundle of sticks"—a metaphor used by lawyers, courts, and law professors quite often.[63] The largest collection of property rights one can have is fee ownership, or the whole "bundle of sticks."[64] If a landowner owns Blackacre in fee, he or she owns the surface, the air space above the surface, and the mineral below the surface.[65]

The landowner may convey any or all of his property rights in Blackacre.[66] If the landowner chooses to convey less than his full property rights in Blackacre, less than the whole bundle of sticks, a severance occurs.[67] When the mineral estates and surface estates have been severed, different legal rights and obligations encompass ownership of each estate.[68] In Texas, when there is a severance of the mineral and the surface estates, the mineral estate is the dominant estate.[69] This "dominant estate rule" simply means that the surface estate is burdened by a servitude.[70] The mineral owner, or his lessee, which is typically an oil and gas company, has a right of ingress and egress as well as a right to use as much of the surface as is "reasonably

59. Tarrant County Sees 100,000 Leases in 2007, posting of Jim Fuquay to Barnett Shale, http://startelegram.typepad.com/barnett_shale/leasing/page/3/ (Dec. 17, 2007, 14:30 CST).

60. Piller, *supra* note 6.

61. JOSEPH SHADE, PRIMER ON THE TEXAS LAW OF OIL AND GAS 53 (3rd ed. 2004).

62. *Id.* at 9.

63. *Id.*

64. *Id.*

65. *Id.* at 9–10.

66. SHADE, *supra* note 61, at 10.

67. *Id.*

68. *Id.*

69. Getty Oil Co. v. Jones, 470 S.W.2d 618, 621 (Tex. 1971).

70. *See* Tarrant County Water Control & Improvement Dist. No. One v. Haupt, Inc., 854 S.W.2d 909, 911 (Tex. 1993); *see also* Moser v. U.S. Steel Corp., 676 S.W.2d 99, 102–03 (Tex. 1984).

necessary" to explore for and produce minerals.[71] Because the mineral estate is dominant, the mineral-estate owner is not obligated to pay for using the surface, nor is he obligated to maintain or restore the surface in the absence of a statute or lease provision requiring such restoration.[72]

How does this general background in Texas oil and gas law affect early signers of Barnett Shale gas leases? It is obvious to many that a landowner who *sells* his mineral rights but retains the surface has effected a severance of the surface and mineral estates. What might not be as clear, especially to those not learned in the law of oil and gas, is that a landowner who *leases* his mineral rights (by signing an oil and gas lease) has also effected a severance of the two estates.[73] Thus, the dominant estate (the mineral estate) is passed to the lessee, which is usually an oil and gas company, for the duration of the lease.[74]

A. *A Unique Legal Document*

The oil and gas lease is the core legal document of oil and gas development. It governs the exploration for and production of oil and gas.[75] What makes the oil and gas lease particularly interesting is that it is structured very differently from an ordinary lease involving real property. In fact, the oil and gas lease is not analogous to a traditional landlord/tenant lease at all.[76] Instead, the oil and gas lease is a document that memorializes a unique business transaction, and the problems that may arise between lessors (usually the landowners or mineral rights owners) and lessees (usually oil and gas companies) are not governed by landlord-tenant law or anything resembling landlord-tenant law.[77]

In the legal world, an oil and gas lease is both a conveyance and a contract.[78] A lease is a conveyance because the landowner is using the lease to convey a property right to an oil company to explore for and produce oil and gas.[79] If the landowner owns both the surface rights and the minerals in place under the surface and then executes a lease for only the minerals, the lease severs the surface estate from the minerals.[80] The oil company is vested with a determinable fee in the min-

71. *See Moser*, 676 S.W.2d at 102–03; *see also* Robinson v. Robbins Petroleum Corp., 501 S.W.2d 865, 867 (Tex. 1973).

72. *Moser*, 676 S.W.2d at 102–03.

73. Joyner v. R. H. Dearing & Sons, 112 S.W.2d 1109, 1111 (Tex. Civ. App.—El Paso 1937, no writ).

74. Lewis v. Oates, 145 Tex. 77, 79, 195 S.W.2d 123, 124 (1946).

75. SHADE, *supra* note 61, at 21.

76. *Id.*

77. *Id.*

78. *Id.* at 22.

79. JOHN S. LOWE ET AL., CASES AND MATERIALS ON OIL AND GAS 125 (4th ed. 2002).

80. Taylor v. Higgins Oil & Fuel Co., 2 S.W.2d 288, 294 (Tex. Civ. App.—El Paso 1928, writ dism'd w.o.j.).

erals (oil, gas, and other minerals) to explore for and produce the minerals, and this right will only terminate upon happenings specified in the lease.[81] A lease is also a contract because the oil company accepts this right to explore and produce by agreeing to be burdened by certain express and implied promises.[82] Also, embodied in an oil and gas lease is a business transaction between a landowner, who typically lacks the capital and technical know-how to explore for or develop the minerals underlying her land, and an oil company, which possesses such capital and technical expertise.[83] The mineral owner and the oil company both seek to make a profit in this business transaction; the oil and gas lease is utilized to establish the contractual terms of that transaction.[84]

B. *Unique Terms*

Under the terms most common in an oil and gas lease, the right to develop the minerals is transferred from the landowner to the oil company.[85] This right of development authorizes the oil company to use the landowner's land to conduct operations on the land at the oil company's sole risk and expense.[86] In exchange, the landowner receives (1) money up front in the form of a bonus and (2) the expectation of more money, if a producing well is completed, in the form of royalty payments.[87]

The most common oil and gas lease used in Texas creates a timeline that divides the terms of the lease into two segments: the Primary Term and the Secondary Term.[88] The primary term of the lease lasts for a fixed number of years.[89] During the primary term, the oil and gas company (lessee) typically is granted the option but not the obligation to drill.[90] The secondary term of the lease, typically called the "thereafter clause," lasts as long as oil or gas is produced from the lease.[91] The secondary term could last only a short time or it could last for generations.[92] In the typical lease, it is the lease's "habendum clause" that sets the mineral estate's duration discussed above.[93] A typical "habendum clause" states that the leases last for a relatively

81. Cherokee Water Co. v. Forderhause, 641 S.W.2d 522, 525 (Tex. 1982).
82. *See id.*
83. SHADE, *supra* note 61, at 22.
84. *Id.*
85. *Id.*
86. *Id.*
87. *Id.*
88. *Id.* at 25.
89. *Id.* at 26; *see also* Exxon Corp. v. Miesch, 180 S.W.3d 299, 334 (Tex. App.—Corpus Christi 2005, pet. granted).
90. SHADE, *supra* note 61, at 26.
91. *Id.*
92. *Id.*
93. *Exxon*, 180 S.W.3d at 334.

short fixed term of years (primary term) and then "as long thereafter as oil, gas or other minerals is produced (secondary term)."[94]

A common misconception about the oil and gas lease, especially by the average landowner, is that the terms of the lease are non-negotiable. In fact, every term in an oil and gas lease—the length of the primary and secondary terms, the royalty and bonus provisions, and even where the drill site is located—is negotiable.[95] One factor that may lead to the misconception that lease terms are non-negotiable is that the landmen, who desire to lease the mineral rights, are generally the ones who prepare the leases for a mineral rights owner to sign.[96] The landmen often arrive with lease and bonus money in hand; all that is needed to complete the deal is the mineral owner's signature.[97] Although many landmen use a similar lease form, especially landmen working to lease mineral rights in the Barnett Shale, there is not a standard industry form that contains the same lease terms for everyone who may sign.[98] There is no such thing as a standard bonus payment or a standard royalty payment. Finally, there are few rules on lease negotiations, and landmen in Texas are not licensed.[99] Therefore, there is no set of standard rules that govern how landmen are to conduct lease negotiations with a mineral rights owner.[100]

IV. UNCONSCIONABILITY

The oil and gas lease is a contract and is interpreted as such by courts in Texas.[101] Accordingly, early signers of Barnett Shale gas leases who hope to find relief from their lease, or at least an opportunity to renegotiate the terms of their lease, should look to the law of contracts for any defenses that may be raised. All of the contract-law defenses (such as fraud, duress, mistake, impossibility, or illegality) are available to be raised in order to try to rescind or cancel an oil and gas lease, and if the facts of a given situation call for any of these defenses, early signers of Barnett Shale leases should explore those options. However, there is only one contract-law defense that seems to give an early signer of a Barnett Shale lease the best chance at an opportunity to re-negotiate a better deal: the doctrine of unconscionability.

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94. *Id.*

95. JUDON FAMBROUGH, REAL ESTATE CENTER, HINTS ON NEGOTIATING AN OIL AND GAS LEASE 1 (1997), http://recenter.tamu.edu/pdf/229.pdf

96. Fox & Richter, *supra* note 6; *see also* Fuquay, *supra* note 55.

97. *See* Ward, *supra* note 5; *see also* Fox & Richter, *supra* note 6.

98. *See* Schnurman, *supra* note 15.

99. *See* Fuquay, *supra* note 55.

100. *Id.* (discussing failure of recent effort by the Texas Legislature to require landmen to be licensed in Texas).

101. Tittizer v. Union Gas Corp., 171 S.W.3d 857, 860 (Tex. 2005); Horizon Res. Inc. v. Putnam, 976 S.W.2d 268, 270 (Tex. App.—Corpus Christi 1998, no pet.) (oil and gas lease should be interpreted like any other contract).

The doctrine of unconscionability has traditionally been the contract-law response to unfair bargains.[102] The inequality of bargaining power between the residents of Tarrant County and the landmen, which was undoubtedly present in the early stages of the Barnett Shale natural-gas boom, leads to the reasonable conclusion that the doctrine of unconscionability is most likely the best contract defense that could potentially be raised by the early signers of Barnett Shale gas leases. However, a significant burden to overcome from the outset is that Texas courts, as do all courts, strongly favor contracting parties having the freedom to contract as they see fit.[103]

"Freedom of contract" is the basic principle that stands for the proposition that parties are free to contract as they see fit and that courts should not interfere with that freedom.[104] Freedom of contract has recently been described by the Texas Supreme Court as the idea that "men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts when entered into freely and voluntarily shall be held sacred and shall be enforced by Courts of justice."[105] In other words, it is not the job of the courts to protect parties from bad deals. Any attack against a contract that was freely entered into by two parties is not taken lightly by a court. This is especially true considering the fact that the freedom to contract is considered a public policy of the highest importance.[106] Furthermore, a person who signs a contract is presumed to have read and understood the document.[107] Thus, an argument that the early signers of Barnett Shale leases simply did not know what they were getting into is not a valid defense to an enforceable contract. "However, the notion that a party should be able to freely choose their bargains," and the terms of their bargains, "conflicts with the notion that grossly unfair bargains should not be enforced."[108] From this conflict came a desire for fairness in the law of contracts from which the doctrine of unconscionability has emerged.[109]

A. *Defining Unconscionability*

A difficult problem with raising the doctrine of unconscionability as a defense to an enforceable contract is that the word "unconscionable" is a "word that defies lawyer-like definition."[110] As a general

102. *See* 49 DAVID R. DOW & CRAIG SMYSER, TEXAS PRACTICE, CONTRACT LAW § 3.9 (2005).
103. BMG Direct Mktg., Inc. v. Peake, 178 S.W.3d 763, 767 (Tex. 2005).
104. J. CALAMARI & J. PERILLO ON CONTRACTS § 1.3 at 5 (5th ed. 2003).
105. Gym-N-I Playgrounds, Inc. v. Snider, 220 S.W.3d 905, 912 (Tex. 2007).
106. *Id.*
107. Tamez v. Sw. Motor Transp., Inc., 155 S.W.3d 564, 570 (Tex. App.—San Antonio 2004, no pet.).
108. DOW & SMYSER, *supra* note 102.
109. *Id.*
110. CALAMARI & PERILLO, *supra* note 104, at 388.

matter, unconscionability is defined as "[e]xtreme unfairness" and as "[t]he principle that a court may refuse to enforce a contract that is unfair or oppressive because of procedural abuses during contract formation or because of overreaching contractual terms, [especially] terms that are unreasonably favorable to one party while precluding meaningful choice for the other party."[111] However, as one Texas court has stated, the word unconscionability "has no precise legal definition because it is not a concept but a determination to be made in light of a variety of factors."[112]

Historically, "a bargain was said to be unconscionable in an action at law if it was such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other."[113] Today, however, unconscionability has been acknowledged to include the absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party.[114] In fact, today, when determining whether a contract is unconscionable or not, a court will look to the entire atmosphere in which the agreement was made.[115] A court's review takes into account a variety of factors, including "the alternatives, if any, which were available to the parties at the time of making the contract; the non-bargaining ability of one party; whether the contract is illegal or against public policy; and, whether the contract is oppressive or unreasonable."[116]

The purpose behind the doctrine of unconscionability is not to relieve a party from the effects of a bad bargain;[117] rather, its purpose is to prevent "oppression and unfair surprise."[118] According to the Uniform Commercial Code (UCC),

> [i]f the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made, the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.[119]

There are several significant observations to be made about the power given to the courts under the UCC when they are faced with an

111. BLACK'S LAW DICTIONARY 742 (3rd Pocket ed. 2006).

112. Pony Express Courier Corp. v. Morris, 921 S.W.2d 817, 821 (Tex. App.—San Antonio 1996, no writ).

113. RESTATEMENT (SECOND) OF CONTRACTS § 208 cmt. b. (1981).

114. Williams v. Walker-Thomas Furniture Co., 350 F.2d 445, 449 (D.C. Cir. 1965); *see also* Carlson v. Gen. Motors Corp., 883 F.2d 287 (4th Cir. 1989).

115. Marsh v. Marsh, 949 S.W.2d 734, 740 (Tex. App.—Houston [14th Dist.] 1997, no writ).

116. *Id.*

117. Wade v. Austin, 524 S.W.2d 79, 85 (Tex. Civ. App.—Texarkana 1975, no writ).

118. CALAMARI & PERILLO, *supra* note 104, at 388; U.C.C. § 2-302 cmt. 1 (2000).

119. U.C.C. § 2-302(1).

unconscionable contract argument or unconscionable terms in a contract. First, the issue of unconscionability is a question of law to be determined by the court rather than a jury.[120] Second, courts have the power to rescind the entire contract.[121] Finally, the court has the power to strike the portion of the contract it decides is unconscionable and enforce the remainder of the contract as it determines proper.[122] The power granted to courts under the UCC is best summed up by the first official comment to the section:

> This section is intended to make it possible for the courts to *police* explicitly against the contracts or clauses which they find to be unconscionable. In the past such policing has been accomplished by adverse construction of language, by manipulation of the rules of offer and acceptance or by determinations that the clause is contrary to public policy or to the dominant purpose of the contract. This section is intended to allow the court to pass directly on the unconscionability of the contract or particular clause therein and to make a conclusion of law as to its unconscionability.[123]

However, despite the purpose and intent behind this UCC section and the broad power that it grants to a reviewing court, "rescission of a contract for unconscionability is an extraordinary remedy usually reserved for the protection of the unsophisticated and uneducated."[124]

Texas Business and Commerce Code section 2.302 adopts the exact language of UCC section 2-302, including all the official comments.[125] However, the Business and Commerce Code, as well as UCC Article 2, is only applicable to contracts that are for the sale of goods.[126] While it is true that in Texas a contract for the *sale* of minerals is a contract for the sale of goods as defined by the Business and Commerce Code,[127] it is not clear from case law whether an oil and gas *lease* is treated as a contract for the sale of goods. It is clear that the unconscionability section of the Texas Business and Commerce Code that applies to consumer leases[128] is inapplicable to oil and gas leases.[129]

The applicability or inapplicability of Texas Business and Commerce Code 2.302 should not be of concern to early signers of Barnett Shale gas leases, because the common law unconscionability doctrine

120. *Id; see also* Martin v. Joseph Harris Co., 767 F.2d 296, 299 (6th Cir. 1985).
121. U.C.C. § 2-302(1).
122. *Id.*
123. U.C.C. § 2-302 cmt. 1 (emphasis added).
124. Wilson v. World Omni Leasing, Inc., 540 So. 2d 713, 717 (Ala. 1989).
125. TEX. BUS. & COM. CODE ANN. § 2.302 (Vernon 2002); U.C.C. § 2-302.
126. TEX. BUS. & COM. CODE ANN. § 2.102; U.C.C. § 2-102.
127. TEX. BUS. & COM. CODE ANN. § 2.107(a); *see also* Howell Crude Oil Co. v. Tana Oil & Gas Co., 860 S.W.2d 634 (Tex. App.—Corpus Christi 1993, no writ).
128. TEX. BUS. & COM. CODE ANN. § 2A.108.
129. *Id.* §§ 2A.102, 103(a)(8).

is substantially the same as the section 2.302.[130] Furthermore, Texas courts look to section 2.302 of the Business and Commerce Code and its comments for guidance when dealing with unconscionability claims that do not involve contracts for the sale of goods—despite the section not applying to the contract the court is reviewing.[131] This is not uncommon behavior for courts in all jurisdictions because the provisions of the UCC doctrine of unconscionability have "entered the general law of contracts and [have] been applied to numerous transactions outside the coverage" of contracts involving the sale of goods.[132] In fact, it seems the drafters of the Restatement of Contracts anticipated this result when drafting restatement section 208 with language that mirrors UCC section 2-302.[133]

Despite its not being applicable to their situation, early signers should utilize section 2.302 of the Business and Commerce Code and its official comments as persuasive authority to plead their case to the court. Although the common-law rule of unconscionability governs the transaction, courts should look to section 2.302 and its official comments for guidance if faced with a question of unconscionability in the context of Barnett Shale gas leases. This is especially true in light of the fact that a challenge to an oil and gas lease on the basis of unconscionability would be a case of first impression in Texas.

B. *Proving Unconscionability in Texas*

What does it take to raise and prove the defense of unconscionability successfully in a Texas courtroom? According to the official comments to section 2.302 of the Business and Commerce Code, the "basic test is whether, in light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract."[134] According to the Supreme Court of Texas, "[a]lthough many factors are relevant and no single formula exists, proof of a claim of unconscionability begins with two broad questions: (1) How did the parties arrive

130. RESTATEMENT (SECOND) CONTRACTS § 208 (1981) ("If a contract or term thereof is unconscionable at the time the contract is made a court may refuse to enforce the contract, or may enforce the remainder of the contract without the unconscionable term, or may so limit the application of any unconscionable term as to avoid any unconscionable result.").

131. Sw. Bell Tel. Co. v. DeLanney, 809 S.W.2d 493, 498 (Tex. 1991) (Gonzalez, J., concurring) (stating a claim of unconscionability in the context of a service contract where section 2.302 of the Business and Commerce Code was not applicable but stating "the provision pertaining to unconscionability 'has been applied to numerous transactions outside the coverage of Article 2 of the code'").

132. CALAMARI & PERILLO, *supra* note 104, at 385 n.1 (discussing the doctrine of unconscionability being accepted as a general doctrine of contract law).

133. RESTATEMENT (SECOND) OF CONTRACTS § 208.

134. TEX. BUS. & COM. CODE ANN. § 2.302 cmt. 1.

at the terms in controversy; and (2) Are there legitimate commercial reasons which justify the inclusion of those terms?"[135]

The first question is often described as the procedural aspect of unconscionability, and it focuses on the assent of the contracting parties. The second question is often described as the substantive aspect of unconscionability, and it focuses on the fairness of the terms in the resulting agreement.[136] Accordingly, it seems clear that the Texas Supreme Court requires something more than bargaining disparity to be shown in order to establish unconscionability.[137] In fact, under Texas law, "the party asserting unconscionability of a contract bears the burden of asserting and proving both procedural and substantive unconscionability."[138] Both inquiries require consideration of all the circumstances that existed at the time when the contract was made, and "not via hindsight."[139]

1. Procedural Unconscionability

The first step in an analysis of a claim of unconscionability begins with a determination of whether procedural unconscionability was present when the contract was formed.[140] When a court considers whether there is procedural unconscionability surrounding a particular contract, the court looks at the facts surrounding the bargaining process—not at the terms of the contract itself.[141] But a determination of whether procedural unconscionability was present in the contract formation process is not limited in its scope to whether the parties held unfair bargaining positions.[142] Generally speaking, procedural unconscionability will be present when "oppression and unfairness . . . taint the negotiation process leading to the [contract's] formation."[143] Procedural unconscionability is illustrated "through such things as 1) the presence of deception, overreaching, and sharp business practices, 2) the absence of a viable alternative, and 3) the relative acumen, knowledge, education, and financial ability of the parties involved."[144] No particular factor is determinative; "rather,

135. *Sw. Bell*, 809 S.W.2d at 498–99 (Gonzalez, J., concurring).

136. *Id.* at 499.

137. *Id.* at 498 (stating that the Business and Commerce Code and the Restatement of Contracts agree that "a disparity in bargaining power, while relevant, is not a litmus test for unconscionability").

138. Ski River Dev., Inc. v. McCalla, 167 S.W.3d 121, 136 (Tex. App.—Waco 2005, no pet.); *see also In re* Turner Bros. Trucking Co., 8 S.W.3d 370, 376–77 (Tex. App.—Texarkana 1999, no pet.).

139. El Paso Natural Gas Co. v. Minco Oil & Gas Co., 964 S.W.2d 54, 61 (Tex. App.—Amarillo 1997), *rev'd on other grounds,* 8 S.W.3d 309 (Tex. 1999); *Ski River*, 167 S.W.3d at 136.

140. *Sw. Bell*, 809 S.W.2d at 499.

141. *Id.*

142. *El Paso,* 964 S.W.2d at 61.

143. *Id.*

144. *Id.*

the totality of the circumstances must be assessed before it can be said that someone fell prey to procedural abuse."[145]

Procedural unconscionability, the first question in a claim of unconscionability, seems promising for early signers of Barnett Shale leases, because procedural unconscionability is the prong of the analysis that takes into account any unequal bargaining positions between the parties.[146] It would be hard to argue against the presence of unequal bargaining power between the early signers of Barnett Shale leases and the landmen or oil and gas companies with whom the early signers were negotiating leases because of two factors in particular: disparity in the parties' knowledge, and a lack of meaningful choice for early signers.

a. Early Signers Lacked Considerable Knowledge

In a procedural unconscionability analysis, the reviewing court is likely to consider whether the stronger party had knowledge that the "weaker party is unable reasonably to protect his or her interests by reason of physical or mental infirmities, *ignorance*, illiteracy, or *inability to understand the language of the agreement.*"[147] This factor is particularly relevant to early signers of Barnett Shale leases, because it is clear that the residents signing these early leases lacked basic knowledge of their rights when negotiating a mineral lease. Early signers of Barnett Shale leases were vulnerable to the superior knowledge and expertise that landmen or representatives from oil and gas companies possess.

The oil and gas lease is full of provisions and terms referencing the payment of royalties, primary and secondary terms, and the drilling and operation of wells—terms that are mostly meaningless to a layman.[148] In contrast, the landman making the sales pitch is knowledgeable about each of the provisions in the lease[149] because it is the landman who most often drafts the lease.[150] Furthermore, the oil and gas lease itself is a document that is written in legalese, with phrases and terminology that even attorneys who do not practice oil and gas law have trouble understanding.[151] Thus, a knowledge gap between

145. *Id.*

146. *Sw. Bell*, 809 S.W.2d at 499.

147. Ski River Dev., Inc., 167 S.W.3d 121, 136 (Tex. App.—Waco 2005, no pet.) (emphasis added).

148. *See* Piller, *supra* note 6 (discussing how "the potential royalty recipient must navigate a swarm of issues, questions and technicalities surrounding a mineral lease that make a typical house sale appear trivial by comparison").

149. *See* Fuquay, *supra* note 11 (discussing how the landmen have the advantage in negotiations).

150. JOHN S. LOWE, OIL AND GAS LAW IN A NUTSHELL 305 (4th ed. 2003).

151. *See* Schnurman, *supra* note 15; *see also* Piller, *supra* note 6 (advising residents not to negotiate oil and gas leases themselves but rather hire an experienced oil and gas attorney).

the average mineral rights owner in Tarrant County and the landmen was clearly evident in the early stages of the Barnett Shale boom and led to blatantly unequal bargaining positions.

Today, the average resident of Tarrant County, whether an owner of mineral rights or not, is well educated in the Barnett Shale and how to negotiate effective leases. Early signers of Barnett Shale leases were simply not privy to the abundance of information that is now available to residents negotiating mineral-right leases.[152] An unfair bargaining positioning and a disparity in knowledge are easily exploitable by a stronger party; it is precisely this exploitation potential that procedural unconscionability aims to police.[153]

b. The Lack of Meaningful Choice for Early Signers

When reviewing a procedural unconscionability claim, a court may also consider if one party to the contract lacked viable alternatives. A court often takes into account whether one of the parties to the contract is a weaker party and, if so, whether that weaker party had no real choice but to enter into the contract.[154] This factor, which is often referred to as "the lack of meaningful choice," aims at policing factual situations that do not rise to the level of duress or undue influence but still call for the resulting agreement to be stricken or modified by a court.

In the early days of the Barnett Shale, the competition for mineral rights leases was minimal in comparison to the competition Tarrant County is seeing in 2008. Early signers of Barnett Shale leases typically had only one company competing for their mineral rights, and they were made offers in a take-it-or-leave-it fashion.[155] In addition, most early signers of Barnett Shale leases were approached by landmen with bonus checks in hand.[156] This very likely only added to the sense of urgency that early signers must have felt, not wanting to miss out on a potential money-making opportunity.

c. Overcoming the Burden of Proof

But are these two factors enough to convince a court that the circumstances surrounding early Barnett Shale lease negotiations were procedurally unconscionable? Nobody can know the answer to that question for sure. But what is known is that before procedural uncon-

152. *See* Ward, *supra* note 5.

153. *See* TEX. BUS. & COM. CODE ANN. § 2.302 cmt. 1 (Vernon 2002).

154. *See* El Paso Natural Gas Co. v. Minco Oil & Gas Co., 964 S.W.2d 54, 61 (Tex. App.—Amarillo 1997), *rev'd on other grounds*, 8 S.W.3d 309 (Tex. 1999); *see also* Ski River Dev., Inc. v. McCalla, 167 S.W.3d 121, 136 (Tex. App.—Waco 2005, no pet.).

155. *See* Fuquay, *supra* note 11; *see also* Jon Nielsen, *Grand Prairie Activist Aims to Educate on Gas Drilling Options*, Dallas Morning News, Nov. 24, 2007, *available at* http://www.dallasnews.com/sharedcontent/dws/news/localnews/stories/112507dnmetgpdrilling.21b6948.html.

156. *See* Schnurman, *supra* note 15.

scionability is found by a court, the circumstances surrounding the negotiations must rise to the level of "shocking."[157] What combination of circumstances that would satisfy a court's definition of "shocking" is unclear and not defined in the case law. Furthermore, there is not a balancing or elemental test that a court can use to weigh a set of facts and determine if the facts rise to the level of "shocking." Claims of procedural unconscionability are reviewed on a case-by-case basis.[158] This fact-specific review makes it difficult to define a set standard for what is or is not considered procedurally unconscionable. However, considering that the main purpose of the procedural unconscionability prong is to address unfairness and gross disparity in bargaining power, the situation in which early signers of Barnett Shale leases find themselves today is likely to meet the burden of "shocking" given the highly unusual context in which it arises. Many common factors that courts consider when reviewing claims of procedural unconscionability are present in this factual context—the absence of a viable alternative, and a disparity in the relative acumen, knowledge, education, and financial ability of the parties involved.[159] Viewing the totality of these circumstances arguably makes a strong case for a reviewing court to enter a finding of procedural unconscionability in the case of early signers of Barnett Shale leases.

2. Substantive Unconscionability

Regardless of how strong a claim of procedural unconscionability early signers of Barnett Shale gas leases may have, proof of substantive unconscionability is still required by Texas courts.[160] When a court is deciding whether substantive unconscionability is present in a contract, the court looks at the fairness or oppressiveness of the contract terms themselves.[161] As the Supreme Court of Texas has explained, "the substantive aspect of unconscionability is concerned with the fairness of the resulting agreement."[162] "The test for substantive unconscionability is whether, given the parties' general commercial background and the commercial needs of the particular trade or case, the clause involved is so one-sided that it is unconscionable under the circumstances existing when the parties made the contract."[163]

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157. *Ski River*, 167 S.W.3d at 136.

158. *In re* Rangel, 45 S.W.3d 783, 786 (Tex. App.—Waco 2001, no pet.).

159. *See Ski River*, 167 S.W.3d at 136; *see also* El Paso Natural Gas Co. v. Minco Oil & Gas Co., 964 S.W.2d 54, 61 (Tex. App.—Amarillo 1997) *rev'd on other grounds*, 8 S.W.3d 309 (Tex. 1999); Sw. Bell Tel. Co. v. DeLanney, 809 S.W.2d 493, 498–99 (Tex. 1991) (Gonzalez, J. concurring).

160. *Ski River*, 167 S.W.3d at 136; *see also In re* Turner Bros. Trucking Co., 8 S.W.3d 370, 376–77 (Tex. App.—Texarkana 1999, no pet.).

161. *See Sw. Bell*, 809 S.W.2d at 499.

162. *Id.*

163. *In re* Palm Harbor Homes, Inc., 195 S.W.3d 672, 678 (Tex. 2006).

This prong of the unconscionability analysis is not easily quantified because the notions of fairness and oppressiveness embodied in this prong "elude ready grasp."[164] One Texas court described substantive unconscionability as terms in a contract that are "sufficiently shocking or gross to compel a court to intercede."[165] Another court illustrated a definition of substantive unconscionability, describing it as a "contract, with its promises, benefits and detriments, [that] must border on being inimical to public policy before it can be said to be sufficiently unfair and oppressive."[166] Regardless of the grounds proffered as illustrative of substantive abuse in a contract, courts in Texas seem to agree that the substantive terms must be amply one-sided before a finding of substantive unconscionability will be made.[167]

a. Are the Terms One-Sided?

Making an argument that lease terms in the typical oil and gas lease are one-sided is not that far of a reach when you consider the nature of the oil and gas lease itself. It seems clear that, because of the nature of the oil and gas business, the terms found in the typical oil and gas lease were meant to be one-sided and to overwhelmingly favor the oil and gas company. The oil and gas business is "capital intensive and risky."[168] Although the advances in technology have greatly increased the chances of drilling a producing well, one cannot tell for sure what lies below the surface until they drill.[169] A substantial amount of scientific know-how and money is required to explore for and produce oil and gas.[170] The oil and gas company possesses the technology and the money but, in order to explore for and produce the minerals, the oil and gas company needs land, or at least the rights to the minerals it is hoping to produce. This is where the oil and gas lease comes into play.

The ultimate expectation of both the mineral right owner (the "Lessor") and the oil and gas company (the "Lessee") when the lease is signed is the same—the expectation of profit from a producing well.[171] But the immediate goals of the two parties are often quite diverse.[172]

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164. *El Paso*, 964 S.W.2d at 61.
165. *Ski River*, 167 S.W.3d at 136; *see also El Paso*, 964 S.W.2d at 62.
166. *El Paso*, 964 S.W.2d at 61.
167. *Id.* at 62; Wade v. Austin, 524 S.W.2d 79, 86 (Tex. Civ. App.—Texarkana 1975, no writ); *see also In re* Luna, 175 S.W.3d 315, 327 (Tex. App.—Houston [1st Dist.] 2004, orig. proceeding), *mand. granted*, *In re* Poly-America, L.P., No. 04-1049, 2008 WL 3990993, at *16 (Tex. Aug. 29, 2008) (holding "it is not the number of provisions weighing toward an overall finding of substantive unconscionability that matters as much as the *cumulative one-sidedness* of the burden that those provisions place on a party.") (emphasis added).
168. SHADE, *supra* note 61, at 1.
169. *Id.*
170. *Id.*
171. *Id.* at 22.
172. *Id.*

The Lessee wants authorization to explore for minerals on the land for as long a period of time as possible, and the Lessee also wants the option to drill a well but does not want to be obligated to drill.[173] These terms are what the Lessee typically gets during the primary term of the lease.[174] If the Lessee drills a producing well, it wants to hold the lease for as long as it is profitable to do so.[175] This is what the Lessee gets during the secondary term of the lease and, as previously noted, the secondary term of the lease will last as long as oil is produced.[176] Finally, the Lessee wants to use the surface for exploration without restriction and seeks to include terms that grant broad surface access rights in the lease.[177] Of course, the Lessee wants to pay as little as possible for all of these rights.[178] The modern oil and gas lease is usually drafted and prepared by landmen that represent, or are working on behalf of, the Lessee, and the lease is designed to protect all of these interests.[179] If the Lessor is unaware of the way the modern oil and gas lease is commonly structured, it is hard for the Lessor to negotiate protection for himself or herself into an oil and gas lease.

How does the nature of the oil and gas business and the oil and gas lease affect a substantive unconscionability analysis? Most early signers of Barnett Shale leases, who were certainly uneducated about their rights under an oil and gas lease and not represented by attorneys in lease negotiations,[180] were signing documents prepared by an experienced oil and gas company or landman with lease terms that overwhelmingly favored the oil and gas company. Because they lacked knowledge about the nature of the oil and gas industry, early signers did not even know what questions to ask or what lease terms to attempt to negotiate.[181]

Because of the nature of the underlying business deal, and considering how the most common oil and gas lease is structured, a strong case for substantive unconscionability can already be made for early signers of Barnett Shale leases on these facts alone. In fact, it is arguable that every oil and gas lease could be considered *per se* substantively unconscionable because the entire contract is extremely one-sided by design. However, terms in an oil and gas lease have not been attacked on substantive unconscionability grounds in Texas. Thus, courts have not had the opportunity to consider these facts. At a minimum, it

173. *Id*
174. SHADE, *supra* note 61, at 22 n.35.
175. *Id.* at 22.
176. *Id.* at 26.
177. *Id.* at 22.
178. *Id.*
179. LOWE, *supra* note 150.
180. *See* Schnurman, *supra* note 15.
181. *Id.;* Ward, *supra* note 5 (discussing early Barnett Shale lease signers' lack of knowledge regarding lease provisions).

seems clear to say that the oil and gas lease is a document meant to protect the interests of the oil and gas company—not the interests of mineral right owner. This one-sidedness in contract terms is what the concept of substantive unconscionability is intended to police.[182]

In addition to facing a contract that is arguably substantively unconscionable from the outset, most early signers of Barnett Shale leases did not know they had a right to negotiate any terms of the lease. It was only after improvements were made in how the public was educated about the Barnett Shale and the best way to negotiate an oil and gas lease that it became easier for citizens to negotiate higher royalty interests and more favorable lease terms. The cumulative effect of the education process helped residents level out the one-sidedness of the modern oil and gas lease. However, early signers of Barnett Shale leases were not afforded this knowledge or opportunity. At first glance, the difference between a royalty interest that is between 12.5% and 18%, which was common in early Barnett Shale leases,[183] and royalty interests between 25% and 27.5%, which is common in 2008,[184] may not seem to rise to the level of substantively unconscionable. However, over the life of a lease, this seemingly small difference can add up exponentially. Because of the secondary term in an oil and gas lease, the lease has the potential to last generations if the well is a strong producer.[185] Thus, the seemingly small difference between the royalty interests in early Barnett Shale leases and the leases signed in 2008 could ultimately mean thousands of dollars in royalty payments over the life of the lease. Certainly, this fact makes a substantive unconscionability argument even stronger.

However, arguably better targets of a substantive unconscionability attack against an early Barnett Shale gas lease are the lease terms that are not monetary in nature. It was not uncommon to hear reports of leases signed in 2007 and 2008 that contained negotiated lease terms that included restrictions on surface right access, restrictions on noise levels, restrictions on hours that the well can be in operation, and even terms increasing the minimum distance between the drill site and a private residence or business.[186] Furthermore, the most recent signers

182. *See* El Paso Natural Gas Co. v. Minco Oil & Gas Co., 964 S.W.2d 54, 61–62 (Tex. App.—Amarillo 1997), *rev'd on other grounds,* 8 S.W. 3d 309 (Tex. 1999); *see also In re* Luna, 175 S.W.3d 315, 327 (Tex. App.—Houston [1st Dist.] 2004, orig. proceeding), *mand. granted*, *In re* Poly-America, L.P., No. 04-1049, 2008 WL 3990993, at *16 (Tex. Aug. 29, 2008).

183. *See* posting of Jim Fuquay to Barnett Shale, *supra* note 15.

184. *See* Jim Fuquay, *Arlington Group Gets Record Residential Bonus*, FORT WORTH STAR-TELEGRAM, Jan. 4, 2008, at C1, *available at* 2008 WLNR 223540; *see also* Jessica Deleon, *Residents United to Get a Better Deal*, FORT WORTH STAR-TELEGRAM, Jan. 22, 2008, at B1, *available at* 2008 WLNR 1212461.

185. SHADE, *supra* note 61.

186. *See* Grapevine Neighborhoods Join Forces, posting of Scott Nishimura to Barnett Shale, http://startelegram.typepad.com/barnett_shale/ (Jan. 9, 2008, 15:25 EST); *see also* Second Arlington Group gets $16,580 Bonus, posting of Scott Nishimura to

of Barnett Shale leases have negotiated shorter the primary terms of their lease, forcing the oil and gas company to act faster when deciding whether or not to drill a well.[187] This makes the lease less speculative, and if the well is not drilled by the end of the primary term, the lease terminates and the mineral rights owner will have the opportunity to negotiate a new lease.[188] Thus, it is seemingly clear that the most recent signers of Barnett Shale leases have leveled the one-sidedness that is prevalent in an oil and gas lease. Early signers of Barnett Shale leases cannot say the same, which makes a strong case that early Barnett Shale leases may be susceptible to attack on substantive unconscionability grounds.

b. The Problem with Hindsight

Two potential problems exist for early signers of Barnett Shale leases that may prevent a successful claim of substantive unconscionability. First, the court must review the lease and its terms at the time the contract was entered into and "not via hindsight."[189] The fact that the court, when reviewing claims of unconscionability, looks at the circumstances surrounding the contract at the time the contract was entered into is potentially problematic for early signers of Barnett Shale leases for two reasons. First, it is likely that a review of the Tarrant County deed records will reveal that most leases filed in the early days of the Barnett Shale were substantially similar to each other, meaning that the terms found in those early leases only possess slight differences. While it is clear that there are glaring differences between the lease terms found in early Barnett Shale leases and the leases signed in 2008, a court, while reviewing a claim of unconscionability, must not view the contract "via hindsight."[190] The court must look at the contract terms and decide if they are substantively unconscionable based on the totality of the circumstances present *when the contract was signed.*[191]

Second, the terms of leases signed in the early days of the Barnett Shale look less and less substantively unconscionable the more leases there are out there with similar terms. Because courts review claims of unconscionability based on the totality of the circumstances existing

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Barnett Shale, http://startelegram.typepad.com/barnett_shale/ (Jan. 7, 2008, 17:35 EST).

187. *See* N. Benbrook Neighborhoods get $15,000 Deal, posting of Scott Nishimura to Barnett Shale, http://startelegram.typepad.com/barnett_shale/ (Jan. 22, 2008, 17:40 EST); *see also* Fuquay, *supra* note 55 (discussing group seeking primary term of one year).

188. *See* Piller, *supra* note 6.

189. El Paso Natural Gas Co. v. Minco Oil & Gas Co., 964 S.W.2d 54, 61 (Tex. App.—Amarillo 1997) *rev'd on other grounds*, 8 S.W.3d 309 (Tex. 1999); Ski River Dev., Inc. v. McCalla, 167 S.W.3d 121, 136 (Tex. App.—Waco 2005, no pet.).

190. *El Paso*, 964 S.W.2d at 61.

191. *Ski River*, 167 S.W.2d at 136.

at the time of the contract, if the majority of residents were signing leases with the same terms, this is a factor that would seem to weigh against a finding of substantive unconscionability.

However, the proposition stated above assumes that a court is just comparing leases of Tarrant County residents who were early signers of Barnett Shale leases against each other. But, if a court looks at the totality of the circumstances at the time these early leases were signed when deciding an issue of substantive unconscionability, it must take into consideration leases that were signed by city governments for publicly owned land at the same time. The court would not be looking at the totality of the circumstances if it did not take these city leases into account and compare the terms of those leases to the leases that were signed by the average citizen. An interesting comparison could be made between leases signed by residents in Tarrant County and the leases signed by city governments for drilling on public land in the early days of the Barnett Shale boom.

How would this affect the outcome of the substantive unconscionability analysis? It is clear that city governments ensured that their best interests were protected by being well-represented during leasing negotiations for public land.[192] "When Fort Worth first considered gas leases on public lands [in 2003], it hired a banking firm, which evaluated proposals, managed competitive bidding, and made sure the city got the best deal."[193] The average resident who signed an early Barnett Shale lease was not well-represented during its lease negotiations, and the average resident certainly did not have someone ensuring he received the best deal in those early days.[194] The city governments ultimately have signed leases that will bring in millions of dollars throughout the life of their leases,[195] while the residents were left to fend for themselves and negotiate leases on their own. During the early days of the Barnett Shale leasing boom (and perhaps even today), the average resident simply could not have negotiated lease terms as favorably as a city government that was represented by a banking firm hired to protect the city's interest. The early signers were clearly disadvantaged, and this resulted in their signing leases that pale in comparison to those signed by city governments. Taking this fact into account certainly seems to lend more credence to a claim of substantive unconscionability by early signers of Barnett Shale leases.

192. *See* Schnurman, *supra* note 15.

193. *Id.*

194. *Id.*

195. *See* The Perryman Group, *supra* note 25, at 60 (reporting that the city of Fort Worth has received $10.4 million in bonuses and royalties in the year 2005 alone).

c. *Overcoming the Burden of Proof*

The second potential problem with raising a claim of substantively unconscionability against an early Barnett Shale lease is the high burden of proof that courts require of the claimant. According to the language used by Texas courts, it takes lease terms that are "sufficiently shocking or gross to compel the court to intercede."[196] Proving that the lease terms in early Barnett Shale leases are "shocking or gross" presents itself as a difficult task. The phrase "sufficiently shocking or gross" is not defined in the case law, but it seems clear from the context that lease terms must be severely disproportionate before a court would make a finding of substantive unconscionability.[197] What types of terms it would take to "shock the conscience" of a court is completely unclear. Considering this fact, and the fact that a search of American oil and gas law jurisprudence shows that nobody has ever attacked an oil and gas lease on unconscionability grounds, leads to the conclusion that early signers of Barnett Shale leases have a steep hill to climb to prove substantive unconscionability. However, seeing that a question of unconscionability is ultimately a question of law to be determined by the court,[198] and that the issue of unconscionability must be reviewed on a case-by-case basis,[199] all hope should not seem lost given the highly unusual and unprecedented nature of the Barnett Shale phenomenon.

A claim of substantive unconscionability in the context of an oil and gas lease would be a case of first impression for a court. Despite this fact, the issue of unconscionability in this context is ripe for a court's review—especially in an oil and gas state like Texas. Using the policing power it is granted by the unconscionability doctrine,[200] a court can be the one to ultimately decide if the terms in a standard oil and gas lease are substantively unconscionable. The court can pay particular attention to terms in the lease that are clearly drafted in favor of the stronger party that operate against the weaker party. Particularly considering that the early signers of Barnett Shale leases were especially uneducated and unprepared to negotiate against these unfavorable terms, a court's review is needed. Regardless of the grounds proffered to illustrate substantive abuse, the resulting terms must be

196. *Ski River*, 167 S.W.3d at 136.

197. *See* Wade v. Austin, 524 S.W.2d 79, 86 (Tex. Civ. App.—Texarkana 1975, no writ); *see also In re* Luna, 175 S.W.3d 315, 327 (Tex. App.—Houston [1st Dist.] 2004, orig. proceeding), *mand. granted, In re* Poly-America, L.P., No. 04-1049, 2008 WL 3990993, at *16 (Tex. Aug. 29, 2008); TEX. BUS. & COM. CODE ANN. § 2.302 cmt. 1 (Vernon 2002).

198. *Ski River*, 167 S.W.3d at 136.

199. Pony Express Courier Corp. v. Morris, 921 S.W.2d 817, 821 (Tex. App.—San Antonio 1996, no writ).

200. *See* TEX. BUS. & COM. CODE ANN. § 2.302 cmt. 1; *see also* RESTATEMENT (SECOND) OF CONTRACTS § 208 (1981).

"sufficiently shocking or gross to compel the courts to intercede."[201] Early signers of Barnett Shale leases have a strong argument for substantive unconscionability: the disadvantage in the bargaining process and the clearly unfavorable lease terms likely trigger a court's authority to intercede under the unconscionability doctrine.[202]

V. LESSONS FOR THE FUTURE?

Are there any lessons that have been learned from this Barnett Shale urban leasing boom in Tarrant County that other cities and counties could apply if they find themselves in a similar situation? Two lessons come to the forefront. First, education of the residents who bear the brunt of urban drilling must be top priority for any urban area city leader. It is not the mayor or the city council members that bear the brunt of an urban gas drilling boom; instead, it is the average city resident that faces off with the experienced oil and gas company. The average citizen cannot expect to be familiar with the intricacies of oil and gas law, and it would not be fair for city and county governments to leave it up to the individual residents to educate themselves or hire lawyers to represent them. It is clearly evident that the Barnett Shale boom has been good to the economy of Tarrant County and has filled the government coffers with an abundance of revenue and financial gain. But how much did this tremendous financial gain cost the average citizen? It must be the job of government officials at the city or county level to educate their citizens in a timely manner in order to bridge the gap between the citizenry and the powerful oil and gas companies. There are many lessons to be learned from the Barnett Shale boom. Hopefully, when the next urban drilling boom takes place the city leaders of that area will learn from Fort Worth's education mistakes, and future citizens living in an urban gas drilling boom will not be left to fend for themselves as the city sits back and gets richer.

Several years into the Barnett Shale boom, Fort Worth city officials realized they were not properly educating the public about Barnett Shale. Even in an oil and gas producing state like Texas, drilling in a large urban area is not a common occurrence. In Texas, it is also uncommon for professional landmen to go door-to-door signing residents to gas leases and passing out money orders as "bonus" money. These landmen cannot be unleashed into the city until the city permits the drilling of a well. A city that permits the drilling within its city limits and, therefore, spawns the leasing of residents' mineral rights, should do as much as it can to educate the residents and make sure that they are not taken advantage of. To the City of Fort Worth's

201. El Paso Natural Gas Co. v. Minco Oil & Gas Co., 964 S.W.2d 54, 62 (Tex. App.—Amarillo 1997) *rev'd on other grounds*, 8 S.W.3d 309 (Tex. 1999).
202. *See id.* at 61–62.

credit, the city itself is a "national guinea pig" for the urban drilling phenomenon. No other heavily populated city in America has seen as much natural gas drilling as Fort Worth,[203] and, although slow in developing, Fort Worth's educational effort has prepared the next wave of residents preparing to sign gas leases with ample information. Now that the Barnett Shale boom is in full effect, other urban areas that face urban drilling should learn from the mistakes of Tarrant County.

A second important lesson to be learned from the Barnett Shale boom is that a city drilling ordinance that adequately protects the citizenry is vital. In January 2008, the Fort Worth City Council voted to re-open the debate about its gas-drilling ordinance in response to citizens concerns about the lack of protection.[204] A city drilling ordinance can help create more uniform leasing terms for all residents who sign leases. An effective city drilling ordinance would help level the negotiating playing field over lease terms, thus removing a lot of questions of inequality of lease terms or even substantive unconscionability of lease terms. The city drilling ordinance should provide broad protection to as many citizens as possible, while allowing an oil and gas company adequate leeway to effectively produce the minerals. A city drilling ordinance allows the city to set limits on the distance between well locations and private residences, businesses, schools, hospitals, etc. A city drilling ordinance can limit the times of day and days of the week that a well can be in operation, as well as limit permitted noise levels that come from the drill itself and the roadways that heavy-machinery trucks can drive on. Additionally, the ordinance can address concerns about the environment and pollution. Fort Worth's drilling ordinance, adopted in 2001, was not drafted with any of these protections in mind. Therefore, many of these protections are being incorporated into Tarrant County residents' leases instead. This does not, however, help the early signers of Barnett Shale leases who did not realize that they needed to incorporate these protections into their leases.

VI. CONCLUSION

Is it good public policy to allow a significant portion of Tarrant County's population to be the "guinea pigs" of the Barnett Shale urban leasing phenomenon? Clearly, the answer is no. It seems hard to dispute that the early signers of Barnett Shale gas leases fell victim to unprecedented events, culminating in their signing unfair gas leases. But, because something looks bad from a public policy standpoint or because a situation is unfair does not mean that there is a legal rem-

203. *Going the Distance*, FORT WORTH STAR-TELEGRAM, May 4, 2006, at B10, *available at* 2006 WLNR 7615177.

204. *See* Fort Worth City Council to Start Rewriting Gas Drilling Rules Next Month, posting of Mike Lee to Barnett Shale, http://startelegram.typepad.com/barnett_shale/2008/01/fort-worth-city.html (Jan. 8, 2008, 16:56 CST).

edy. Furthermore, the contract-law defense of unconscionability was not created for parties to have a legal forum to complain about the bad deals they made or to get relief from them. As one Texas Court of Appeals put it, "Our court system cannot act as the mother hen watching over its chicks, standing ready to ameliorate every unpleasant circumstance which might befall them."[205] This Comment is not intended to suggest that every time an unfair contract is signed, the disadvantaged party should have a legal avenue to run to court so that the judge can protect them. This Comment is also not intended to suggest that the important contract-law principle of freedom of contract should be infringed upon by expanding the reach of the unconscionability doctrine. However, there are certain situations that call for judicial intervention. The situation with the early signers of Barnett Shale leases justifies this judicial intervention. The problems from unprecedented urban gas drilling and leasing need their day in court.

The doctrine of unconscionability serves an important function in contract law jurisprudence. It allows courts to hear cases involving factual situations that do not allow for more traditional contract defenses such as fraud, mistake, misrepresentation, and undue influence, but yet involve contracts that should not be enforced from a public policy standpoint. Early signers of Barnett Shale leases should avail themselves of contract defenses such as fraud, mistake, duress, or misrepresentation if their particular circumstances call for it. But it is unlikely that any tactics used by landmen or oil and gas companies in the early days of Barnett Shale leasing rise to the level of these standard contract defenses. However, what happened to early Barnett Shale signers is still ripe for review by a court because of the unprecedented phenomenon of urban gas leasing. Unconscionability is precisely the legal doctrine that provides a vehicle for that review.

Unconscionability has been described as a "wild card" defense because it is a unique doctrine that lacks definition, defined parameters, or a well-established legal test.[206] Nonetheless, unconscionability is a legitimate contract defense and an important tool in a lawyer's arsenal. Unconscionability is a solid claim for early signers of Barnett Shale leases because under the broad discretion granted by the unconscionability doctrine, a court can "police explicitly against the contracts or clauses which [it] finds to be unconscionable."[207] If a contract, by its terms and the circumstances surrounding it, strikes the court as patently unfair, a court can strike that contract down or, at the very least, strike the unconscionable clause. Simply stated, it is a doctrine that gives a court the opportunity to call it like it sees it. In

205. *El Paso*, 964 S.W.2d at 62.

206. *See* THOMAS D. CRANDALL & DOUGLAS J. WHALEY, CASES, PROBLEMS, AND MATERIALS ON CONTRACTS 679 (3d ed. 1999).

207. TEX. BUS. & COM. CODE ANN. § 2.302 cmt.1 (Vernon 2002).

this respect, applying the doctrine of unconscionability to an unprecedented situation like the Barnett Shale is particularly appealing. Any claim of unconscionability that attacks an otherwise valid, enforceable contract is a difficult course of action to take in any courtroom. But absent any proof of fraud, duress, mistake, or any other contract law defense, unconscionability is the best chance for early signers of Barnett Shale leases to rescind leases they signed under such disadvantageous circumstances.

What happened, and continues to happen, in Tarrant County as a result of the Barnett Shale boom is completely unprecedented. Residents of this highly urbanized area were simply caught by surprise when they began to receive lease offers in the mail and to find landmen at their doors with bonus checks in hand. It happened quickly, and it happened without warning. The doctrine of unconscionability, being as much about public policy as it is anything else, will allow the courts to get involved in this unique situation and set precedent for the future, as well as correct the past. Early signers of Barnett Shale leases were severely disadvantaged from the outset and should be granted relief from their leases, or at least given the chance to renegotiate a better deal. Without unconscionability, it is likely that the misfortunes of early signers of Barnett Shale leases will go unheard in a court of law.