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Mineral Rights - Cancellation of Lease - Obligation to Develop

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MINERAL RIGHTS—CANCELLATION OF LEASE—OBLIGATION TO DEVELOP

Plaintiff lessor and defendant Shell Oil Company on July 30, 1935, executed an oil and gas lease covering an eighty-four acre tract for a primary term of ten years. Subsequently, the other defendant Vanson Production Corporation acquired the entire lease from Shell Oil Company. On July 23, 1945, forty-four acres of the leased tract were included in a drilling unit formed by the Department of Conservation. No well was ever drilled on the leased premises, but a producing gas well was brought in on the portion of the unit outside the leased premises after the expiration of the primary term of the lease. Alleging that defendants had failed to develop the portion of the leased tract lying outside the unit and that plaintiff had received from another party a bona fide offer to develop it, plaintiff sought cancellation of that portion of the lease. Defendant Shell Oil Company obtained a judgment of nonsuit. From a judgment on the merits in favor of defendant Vanson Production Company, plaintiff appealed. *Held*, reversed. In refusing to drill a well on plaintiff's land outside the unit where the plaintiff had received another party's bona fide offer to do so, defendant failed to fulfill its obligation to develop. Plaintiff was entitled to cancellation of the lease on the portion of the leased premises lying outside the unit. *Nunley v. Shell Oil Co.*, 76 So.2d 111 (La. App. 1954).

In *Hunter Co. v. Shell Oil Co.*[1] and *LeBlanc v. Danciger Oil & Refining Co.*,[2] the court denied the lessor a cancellation of the lease on the portion of the leased premises lying outside the unit. However, in those cases a well had been drilled on the unit during the primary term of the lease. Moreover, in each case the plaintiff was relying on the failure of defendant during the primary term of the lease to drill a well on the portion of the leased premises lying outside the unit, and not, as in the instant case, on defendant's failure to develop that portion. In the *Hunter* and *LeBlanc* cases the court held that the lessee's obligation to drill a well had been fulfilled by the drilling of a well on the unit, although not on the leased prem-

1. 211 La. 893, 31 So.2d 10 (1947); *The Work of the Louisiana Supreme Court for the 1946-1947 Term—Mineral Rights*, 8 LOUISIANA LAW REVIEW 212, 216 (1948); Comment, 12 LOUISIANA LAW REVIEW 445, 452 (1952).

2. 218 La. 463, 49 So.2d 855 (1950); *The Work of the Louisiana Supreme Court for the 1950-1951 Term—Mineral Rights*, 12 LOUISIANA LAW REVIEW 131, 132 (1952); Comment, 12 LOUISIANA LAW REVIEW 445, 452 (1952).

ises, during the primary term of the lease. Therefore, in both cases, since a well had been drilled and since the lessor failed to show nondevelopment of his leased premises, the court refused to cancel the lease on any portion of the premises. However, the court's language in the *Hunter* case is significant: "[I]f the producing well in the unit is not sufficient to meet the obligation of adequate development of the property covered by the lease, the law gives plaintiff a remedy."[3] Thus the court recognized that the lessee was under an obligation to develop the leased premises sufficiently. The court in *Carter v. Arkansas-Louisiana Gas Co.* also recognized the lessee's obligation to develop by saying that "the main consideration of a mineral lease is the development of the leased premises for minerals."[4] In *Eota Realty Co. v. Carter Oil Co.*[5] the same point was also emphasized.

In the instant case no well had been drilled on the unit during the primary term of the lease. Moreover, the lessor was able to prove that defendant lessee had failed to reasonably develop the leased premises. The lessor showed that a prudent operator had made a bona fide offer to lease the forty-acre portion of the premises lying outside the unit and had offered both immediate payment and his promise to drill a well. The lessee, on the other hand, introduced the opinion of a geologist that all of that portion of plaintiff's premises, with the possible exception of one acre, would be completely unproductive. The court, however, pointed out that the opinions of geologists are frequently erroneous and refused to accept his opinion. The defendant further maintained that he should be allowed to retain the lease because of certain privileges such as laying pipelines and because the property might become valuable subsequently as a result of possible production from another formation. In rejecting this contention, the court stated that all rights of a lessee are determined on the basis of his compliance with his obligation to develop prudently and reasonably the leased premises.

It is submitted that the decision in the instant case is sound. As indicated above, it can be distinguished from the *Hunter*

3. 211 La. 893, 905, 31 So.2d 10, 14 (1947).

4. 213 La. 1028, 1034, 36 So.2d 26, 28 (1948); *The Work of the Louisiana Supreme Court for the 1947-1948 Term—Mineral Rights*, 9 LOUISIANA LAW REVIEW 189, 191 (1949).

5. 225 La. 790, 74 So.2d 30 (1954); *The Work of the Louisiana Supreme Court for the 1953-1954 Term—Mineral Rights*, 15 LOUISIANA LAW REVIEW 300, 309 (1955); 3 OIL & GAS REP. 1876 (1954).

and *LeBlanc* cases. The decision is also consistent with a decision rendered in Mississippi. In *Texas Gulf Producing Co. v. Griffith*, the Mississippi Supreme Court, confronted with a similar fact situation, allowed cancellation of the lease on the portion of the tract lying outside the unit and said that to hold otherwise would "be a violation of the constitutional guaranty that no person shall be deprived of his property without due process of law."[6] A most significant point in the instant case is that plaintiff lessor was able to overcome a geologist's testimony by showing that he had received from a prudent operator a bona fide offer to drill if the land was freed from the lease. The Court of Appeals for the Fifth Circuit in *Romero v. Humble Oil and Refining Co.*[7] had taken a step in that direction, but had required the plaintiff's offeror to give assurance that he would drill before the lease to defendant would be cancelled for nondevelopment. Because of the importance the court in the instant case seemed to place on the fact that a well had been drilled during the primary term in both the *Hunter* and the *LeBlanc* cases, it is not entirely clear whether the result reached in the instant case would have been the same had the lessee drilled during the primary term. However, the remedy afforded the lessor in the instant case was probably within the contemplation of the court in the *Hunter* case.[8] It is submitted that regardless of when the well is drilled on the unit, if the lessor can prove that the lessee has not adequately developed the portion of the leased premises outside the unit, then the lease on that portion should be cancelled.

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MINERAL RIGHTS—INTERPRETATION OF LEASE—EFFECT OF SIGNING A DIVISION ORDER

Plaintiff lessors sued to cancel a mineral lease for failure of lessee to drill or pay delay rentals as required by the terms of the contract.[1] The lessee had completed and placed in production

6. 65 So.2d 447, 452 (Miss. 1953), 2 OIL & GAS REP. 1103, 1111 (1953).
7. 194 F.2d 383 (5th Cir. 1952), 1 OIL & GAS REP. 358 (1952).
8. See language quoted page 854 *supra*.
1. Section 4 of the lease provides in part: "If operations for the drilling of a well be not commenced on said land, or any unitized area hereunder, on or before the 3rd day of September, 1949, this lease shall terminate, unless Lessee on or before that date pays to lessor a rental. . . ." Wilcox v. Shell Oil Co., 76 So.2d 416, 419 (La. 1954).