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C. C. Williams Jr.

*West Virginia University College of Law*

R. B. Goodwin

*West Virginia University College of Law*

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# WEST VIRGINIA LAW QUARTERLY

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## FORFEITURE OF LEASE FOR FAILURE TO MARKET GAS

C. C. WILLIAMS, JR.\*

R. B. GOODWIN\*\*

By the custom of Cornwall, suspension of mining operations for a year and a day was ground for forfeiture of the operator's interest in the mineral lands.<sup>1</sup> That ancient ruling of the Stannary Court was "not founded on the doctrine of demand and supply, but on the expediency simply of bringing the mineral to the surface for the use of men."<sup>2</sup> During the last few decades a similar theory has been received over into American law, forbidding a lessee of the minerals from seeking to tie up property indefinitely to the exclusion of the owner.<sup>3</sup> No such lease, it is usually said, "can be construed to enable" the operator "merely to hold for purposes of speculation" without any obligation to mine or compensate: "otherwise, the agreement might prove entirely fruitless"

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\* Professor of Law, West Virginia University.

\*\* Member of the Student Board of Editors, West Virginia Law Quarterly.

<sup>1</sup> *Loveland v. Longhenry*, 145 Wis. 60, 68-69, 129 N. W. 650 (1911), decreeing forfeiture after fourteen months' failure to mine iron ore. *Cf.* *Cole Petroleum Co. v. United States Gas & Oil Co.*, 121 Tex. 59, 41 S. W. (2d) 414, 86 A. L. R. 719 (1931) where there was cancellation because of the operator's omission to market gas diligently over a period of two years and eight months.

<sup>2</sup> *Rogers v. Brenton*, 10 Q. B. 26, 59, 116 Eng. Rep. E. 10 (1847). The court explained (at p. 58): "The only things which make this reasonable are the render of the toll tin to the owner, and the benefit to the public secured thereby in the extraction of the mineral from the bowels of the earth. Both these are not only lost, but the latter, it may be, positively prevented, if the bounder may decline to work, and yet retain the right to exclude the owner."

<sup>3</sup> *Starn v. Hoffman*, 62 W. Va. 422, 59 S. E. 179 (1907) in which Judge Brannon affirmed the forfeiture of a coal lease for failure to mine, after a default of two years and three months. *Cf.* *Elliott v. Crystal Springs Oil Co.*, 106 Kan. 248, 187 Pac. 692 (1920), holding an oil and gas lease terminated by its specific terms, when for seven months operations had ceased because of lack of market for the gas produced.

as to rents and royalties.<sup>4</sup> The very uniformity in this judicial reasoning seems to indicate a corresponding uniformity in the cause that has prompted it.

As to its origin, this rule has no doubt sprung from an eternal conflict of policy between owner and operator, — the one demanding immediate exploitation of his minerals, with the other looking only to possible gains out of mining operations. And perhaps over the centuries the lessee's frequent abuse of his exclusive privilege has led judges to formulate this drastic sanction, "to encourage the others" to speedy development. In any event, it has been assumed blindly that the interests of society required early production, and that only: the important thing was to get the minerals out of the ground and to their market. Practical difficulties in extraction, — considerations of over-production, — or even modern notions about conservation of natural resources meant relatively little to the courts. Sometimes their decisions stressed an economic ideal of national self-sufficiency; more often, the owner's claim to rents and royalties dictated the result. But on one principle or another, there has had to be some sort of continuous mining activity if the operator wanted to avoid dangerous litigation.

Naturally the operator's job of developing will vary in extent, having regard to the minerals under exploitation; and in the oil and gas field, his obligations must be more exacting because of their fugacious character. Thus it is that there exists in the oil and gas lease an implied covenant for the use of reasonable diligence in the marketing of the product,<sup>5</sup> quite in addition to the customary task of drilling and protecting the leasehold. That implied covenant connotes the duty of the ordinary prudent lessee under all the

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<sup>4</sup> *Crawford v. Richey*, 43 W. Va. 252, 258, 27 S. E. 220 (1897), approving a suit to quiet title since the lessee had done absolutely nothing, though nearly eight years had elapsed. "Generally, all leases of land for the exploration and development of minerals are executed with the expectation and upon the condition, either express or implied, that the land will be developed for such a purpose and where the parties have not fully covered the subject of delay by rental provisions, the lessee's rights terminate upon his non-performance of the conditions", *Benedum-Trees Oil Co. v. Davis*, 107 F. (2d) 981, 984 (C. C. A. 6th, 1939).

<sup>5</sup> More precisely, the duty of the lessee is either to market the product or deliver it for marketing. In the event of default, there are two theories as to lessor's remedy:

1. The lessor may only recover damages for breach of the implied covenant in this regard.
2. The lessor may cancel the lease in equity, on the basis of an implied condition of forfeiture for failure to market.

The authorities are fairly evenly divided as to which of these remedies may be available in an extreme situation.

circumstances, taking into account the interests of both parties.<sup>6</sup> Unfortunately, our courts have in the past failed to spell out more precisely either the nature of this duty or the penalty to be imposed for failure to market diligently: their opinions are scarcely entitled to the praise of clearness in expression or fidelity to the declared judicial doctrine. Recent cases<sup>7</sup> have now brought the problem once more to the attention of the oil and gas industry, so that the implied covenant to market tends to have increasing significance particularly as respects gas production. It is accordingly important to ascertain whether there may properly be forfeiture of an oil and gas lease merely for failure to market diligently the gas from producing wells.

In order to clarify the issue, certain necessary assumptions ought to be made at the start. If the oil and gas lease is regarded as conveying to the lessee a *profit a prendre* (in theory at least), no question will then arise of forfeiting any corporeal mineral interest.<sup>8</sup> On the other hand, discovery plus protection must be held in West Virginia to establish a "vested estate" for the life of the

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<sup>6</sup> *Harris v. Ohio Oil Co.*, 57 Ohio St. 118, 127, 48 N. E. 502 (1897): "The development and protection of lines which is thus implied when the lease is silent is such as is usually found in the same business of an ordinarily prudent man, — neither the highest nor the lowest, but the medium or average." This standard was adopted by Judge Van Devanter in the leading case of *Brewster v. Lanyon Zinc Co.*, 140 Fed. 801, 72 C. C. A. 213 (C. C. A. 8th, 1905), and became the West Virginia rule in *Jennings v. So. Carbon Co.*, 73 W. Va. 215, 80 S. E. 368 (1913).

In *Trimble v. Hope Natural Gas Co.*, 117 W. Va. 650, 664-665, 187 S. E. 331 (1936), Judge Maxwell said: "Matters pertaining to the drilling of oil and gas wells, and to the producing of oil and gas are primarily within the sound discretion of the operator. It is he who carries the hazard and the burden of the cost. As long as his procedure is in accord with standard methods he will not be interfered with by the courts. It is only when it seems evident the procedure adopted by him is clearly prejudicial to the rights of the lessor, that he (operator) will be required by a court of equity to do otherwise."

<sup>7</sup> Representative decisions raising the issue are *Hutchinson v. McCue*, 101 F. (2d) 111 (C. C. A. 4th, 1939), discussed in Note (1940) 46 W. VA. L. Q. 154, and *Benedum-Trees Oil Co. v. Davis*, 107 F. (2d) 981 (C. C. A. 6th, 1939).

<sup>8</sup> See *Simonton, The Nature of the Interest of the Grantee under an Oil and Gas Lease* (1917) 25 W. VA. L. Q. 295. The extent of the operator's investment makes this an exclusive *profit a prendre*.

Where the jurisdiction recognizes a legal corporeal estate in the mineral lessee, as in *Wilmore Coal Co. v. Brown*, 147 Fed. 931 (C. C. Pa. 1906), 153 Fed. 143 (C. C. A. 3d, 1907), or *Stephens County v. Mid-Kansas O. & G. Co.*, 113 Tex. 160, 254 S. W. 290, 29 A. L. R. 566 (1923), there is far greater difficulty. Theoretically, there cannot be *abandonment* of such a property interest: thus the favorite method for cancelling leases would be removed out of the court's reach, and termination rendered much less feasible.

field,<sup>9</sup> subject of course to loss through serious misconduct.<sup>10</sup> Obviously the production should satisfy the "paying quantities" test<sup>11</sup> in volume and pressure only; whether or not the lessee can market seems wholly immaterial on *this* score. That is simply to say a gas well may be thought of as producing in paying quantities, even though it has been capped for a time awaiting further marketing facilities.<sup>12</sup> For present purposes, also, it is of little moment which of the various standards be chosen for measuring the operator's conduct,<sup>13</sup>—the essential fact being always that he has acquitted himself of his task in a fair and honorable fashion. Over and above these considerations, it must be assumed procedurally that the lessor has duly served adequate notice to market,<sup>14</sup> unless lapse

<sup>9</sup> Eastern Oil Co. v. Coulehan, 65 W. Va. 531, 64 S. E. 836 (1909), syl. par. 4: "The discovery of oil or gas under a lease giving right of exploration and production, unless there is something in the lease manifesting a contrary intention, is sufficient to create a vested estate in the lessee in the exclusive right to produce oil or gas provided for therein."

<sup>10</sup> Carper v. United Fuel Gas Co., 78 W. Va. 433, 88 S. E. 1075 (1916); Adkins v. Huntington Dev. & Gas Co., 113 W. Va. 490, 168 S. E. 366 (1933); Trimble v. Hope Natural Gas Co., 113 W. Va. 839, 169 S. E. 529 (1933); and Dillard v. United Fuel Gas Co., 114 W. Va. 684, 183 S. E. 573 (1934).

<sup>11</sup> Barbour, Stedman & Co. v. Tompkins, 81 W. Va. 116, 93 S. E. 1038, L. R. A. 1918B 365 (1917). In Union Gas & Oil Co. v. Adkins, 278 Fed. 854 (C. C. A. 6th, 1922), the distinction is suggested as to who determines the "paying quantities", between the percentage *gas royalty* case and the *gas well rental* situation. See, also, on the issue of the operator's ability to market as defining "paying quantities", United States v. Brown, 15 F. (2d) 565 (D. C. 1926), and Nystel v. Thomas, 42 S. W. (2d) 168 (Tex. Civ. App. 1931).

<sup>12</sup> Summerville v. Apollo Gas Co., 207 Pa. 334, 338, 56 Atl. 876 (1904): "It may be that for some time the lessee was not able to find a purchaser for the gas, but that was not the affair of the lessors. They were not interested in the proceeds of the sale of the gas. Their rights under the agreement extended only to the receipts of a stipulated annual rental for each well and the free use of gas for domestic purposes. Beyond this the question of whether or not the quantity of gas was profitable was for the decision of the lessee. It may be that the final disposition of the product was such as to amply remunerate it (lessee) for the delay in finding a market." J. B. Gathright Land Co. v. Kentucky-W. Va. Gas Co., 65 F. (2d) 907 (C. C. A. 6th, 1933), *acc. Cf.*, however, Benedum-Trees Oil Co. v. Davis, 107 F. (2d) 981, 985 (C. C. A. 6th, 1939): "The term 'paying quantities' involves not only the amount of production, but also the ability to market at a profit." Hanks v. Magnolia Petroleum Co., 24 S. W. (2d) 5 (Tex. Com. App. 1930) seems to hold with the latter statement.

<sup>13</sup> Apart from the prudent operator test, mentioned in footnote 6, *supra*, there is the "good faith" standard. Colgan v. Forest Oil Co., 194 Pa. 234, 242, 45 Atl. 119 (1899), decided that as long as a "lessee is acting in good faith on business judgment, he is not bound to take the other party's, but may stand on his own." That Pennsylvania doctrine has been widely adopted in other jurisdictions; a federal court of another circuit even characterized it as "apparently well-established in the West Virginia courts." See Updegraff v. United Fuel Gas Co., 67 F. (2d) 431 (C. C. A. 6th, 1933).

<sup>14</sup> Howerton v. Kansas Natural Gas Co., 82 Kan. 367, 108 Pac. 813 (1910); American Wholesale Corp. v. F. & S. Oil & Gas Co., 242 Ky. 356, 46 S. W. (2d)

of time and long indifference have dispensed with such a condition precedent.<sup>15</sup> Analogously, ordinary defenses founded on waiver or estoppel are disregarded here,<sup>16</sup> so far as they are likely to mislead or confuse the solution.

Moreover, it should not be inferred that relief automatically follows whenever the producing well is shut in and marketing of gas suspended. Certainly a temporary cessation of production where deeper drilling is in progress,<sup>17</sup> — or where short periods of business depression intervene,<sup>18</sup> — or, perhaps, where an extensive reserve is being built up to care for unusual seasonal demands,<sup>19</sup> —

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498 (1932); and *Berthelote v. Loy Oil Co.*, 95 Mont. 434, 28 P. (2d) 187 (1934). In *Alford v. Dennis*, 102 Kan. 403, 407, 170 Pac. 1005 (1918), the court held: "We think this lawsuit will answer the purpose of a demand for drilling."

<sup>15</sup> *Benedum-Trees Oil Co. v. Davis*, 107 F. (2d) 981, 986 (C. C. A. 6th, 1939): "The rule laid down in *Leeper v. Lemon G. Neely Co.*, 6 Cir., 293 F. 967, 971, that before a lease can be terminated by the lessor for failure to develop, notice must be given lessee, is inapplicable here. Such notice or demand is unnecessary where termination of the lease may be inferred from the fact the lessee has been in default for an unreasonable time or has intentionally breached the express or implied obligations of the contract." *Gadbury v. Ohio & I. Gas Co.*, 162 Ind. 9, 67 N. E. 259 (1903); *Soaper v. King*, 167 Ky. 121, 180 S. W. 46 (1915); and *Hitt v. Henderson*, 112 Okla. 194, 240 Pac. 745 (1925), *acc.*

<sup>16</sup> In *Steven v. Potlatch Oil & Ref. Co.*, 80 Mont. 239, 260 Pac. 119 (1927), the express language of the lease provided that during the time any such gas was "shut in by reason of there being no profitable market for its output, there shall be no royalty." The court accordingly held there was no *expiration* at the end of the definite term.

On the analogy of the rule that acceptance of delay rentals operates to waive breaches of the implied covenant to test (if fraudulent drainage be absent), *Reserve Gas Co. v. Wilson*, 78 W. Va. 329, 88 S. E. 1075 (1916), and *Johnson v. Armstrong*, 81 W. Va. 399, 94 S. E. 753 (1918), it has been held in California similarly as to royalties that their voluntary receipt constitutes waiver. *Kern Sunset Oil Co. v. Good Roads Oil Co.*, 214 Cal. 435, 6 P. (2d) 71, 80 A. L. R. 453 (1931). The alleged fraudulent drainage decisions, *Trimble v. Hope Natural Gas Co.*, 113 W. Va. 839, 169 S. E. 529 (1933), as to payment of delay rentals, and *Dillard v. United Fuel Gas Co.*, 114 W. Va. 684, 173 S. E. 573 (1934), as to payment of oil and gas royalties, must rest on their own peculiar facts.

<sup>17</sup> As in *Eastern Oil Co. v. Coulehan*, 65 W. Va. 531, 64 S. E. 836 (1909). See Note (1931) 72 A. L. R. 372. *Cf.* *Rogers v. Brenton*, 10 Q. B. 26, 64, 116 Eng. Rep. R. 10 (1847): "Nothing we have said compels the bounder to strictly continuous working: such reasonable time for consideration, preparation and due selection of places and planes, must always be allowed as the nature of the undertaking reasonably requires; and, when he has once bona fide worked, his ceasing to work for a time will be therefore open to explanation, so as to prevent a forfeiture. It is only when the conduct of the bounder is such as to warrant the conclusion that he has ceased to be, in good faith, pursuing that object which alone justified his entry on the land, and which is the reasonable foundation of his title."

<sup>18</sup> See *Pennagrade Oil & Gas Co. v. Martin*, 211 Ky. 137, 277 S. W. 302 (1925).

<sup>19</sup> *Clear Creek Oil & Gas Co. v. Bushmaier*, 165 Ark. 303, 264 S. W. 830 (1924).

should lie within the reasonable discretion of the operator. Again, statutory regulation of large gas fields may attempt some plan of "pro-rating" production;<sup>20</sup> if a constitutional method is ultimately achieved, legal impossibility should then adequately explain any consequent failure to dispose of the gas.<sup>21</sup> Instances of this sort, however, have persuaded the larger operating companies in many states<sup>22</sup> to include within their standard leases a provision which substitutes a gas well rental for the customary gas royalty, where sale off the premises is unavoidably prevented.<sup>23</sup> The lessor will in fact contract out of any cause of action founded on the failure to market.

<sup>20</sup> See LEGAL HISTORY OF CONSERVATION OF OIL AND GAS (1938), a Symposium published by the Section of Mineral Law of the American Bar Association.

In Texas, for example, during the fall of 1934, under stripping permits, over a billion cubic feet of gas was being blown into the air daily, making an annual loss in energy equal to 62,634,000 barrels of oil or 487,000 freight cars of coal. These operations so rapidly depleted the supply of gas in the West Panhandle Field that legislative hearings were begun to prevent further waste. A new gas conservation statute was prepared and enacted (Tex. Acts 1935, c. 120) authorizing administrative pro-rating of the production of gas from each common reservoir, and administrative adjustment of the correlative rights and privileges of each owner to produce and market. A few months later, an administrative order was entered by the Texas commission regulating production in the Panhandle Field: this was held unconstitutional, within the due process clause, in *Thompson v. Consolidated Gas Utils. Corp.*, 300 U. S. 55, 57 S. Ct. 364, 81 L. Ed. 510 (1937). A contemporary effort of the industry in the East Texas and mid-continent fields, with the approval and blessing of certain governmental authorities, to eliminate existing distress gasoline by a general raising of prices, has recently been held to have been a violation of the Sherman Anti-Trust Act: *United States v. Socony-Vacuum Oil Co., Inc.*, 60 S. Ct. 811, 84 L. Ed. 760 (U. S. 1940). (The shocking conditions that have prevailed in this highly competitive business of exploiting gas and oil resources and the apparent legislative inability to correct them might serve to remind one once more that "of all the arts, that of government has been brought least to perfection.") But see *Railroad Comm. of Texas v. Rowan & Nichols Oil Co.*, 84 L. Ed. 983 (U. S. 1940).

<sup>21</sup> *Buie v. Porter*, 228 S. W. 999 (Tex. Civ. App. 1921); *Jamieson v. Indiana Natural Gas & Oil Co.*, 128 Ind. 555, 28 N. E. 76 (1891).

<sup>22</sup> Among these are Arkansas, California, Louisiana and Texas. Older jurisdictions in oil and gas law, — such as Pennsylvania and West Virginia, — do not seem to have such a lease provision.

<sup>23</sup> An example of the newer lease provision follows:

*Louisiana Oil and Gas Lease, Form 10 Corrected, Revised.*

"During any period when, after a discovery of gas on said land, gas is not sold on account of lack of a market, and is not being used off the land or in the manufacture of gasoline or other product, and there is no current production or operation on said land sufficient to keep this lease in force, lessee may pay as royalty Fifty Dollars (\$50) per year for each shut-in gas well, and it will be considered that gas is being produced, within the meaning of paragraph 2 hereof, during any period for which such payment is made, and no rental shall inure during any period covered by such a payment."

The problem, one must note carefully, is one of *forfeiture* of the lease for unreasonable failure to market gas production,— which entails the implication of an equitable condition subsequent through which the lessee's valuable interest may be divested because of grave misconduct. Other doctrines favoring the lessor on slightly different facts have no part in this discussion. More specifically, there is the one theory of *expiration* of the lease: following the primary or fixed term for exploration, it is said to be a condition prerequisite to the operation of the extension clause, ("and so long thereafter as oil or gas is produced in paying quantities"), that actual profitable production exist. In other words, unless the lessee is producing and marketing gas from the leasehold on the last day of the fixed term, the extension provision of the habendum never takes effect; the lease just expires, so it is claimed, by its very language. For example, assuming originally a ten-year initial period, the operator's interest is at an end in the absence of marketing ten years later.<sup>24</sup> To be sure, that expiration theory runs squarely counter to prevailing ideas about the lessee's "vested estate for the life of the field", and it is difficult to understand how these can simultaneously thrive in any jurisdiction. But it is well within judicial powers to practice such legerdemain occasionally,— with the result that the possibility of expiration must always be kept in mind.

The other theory which is excluded from the present investigation is that of *abandonment*, — a concept sadly overworked in oil and gas litigation. Analytically, it is a shorthand way of

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<sup>24</sup> This seems to have been the latent *ratio decidendi* in *Hutchinson v. McCue*, 101 F. (2d) 111 (C. C. A. 4th, 1939) and *Benedum-Trees Oil Co. v. Davis*, 107 F. (2d) 981 (C. C. A. 6th, 1939). To the same general effect are *Collins v. Mt. Pleasant Oil & Gas Co.*, 85 Kan. 483, 118 Pac. 54 (1911); *Smith v. Sun Oil Co.*, 172 La. 655, 135 So. 15 (1931); and *Berthelote v. Loy Oil Co.*, 95 Mont. 434, 28 P. (2d) 187 (1934). Cf. dictum in *Smith v. Dudley*, 114 W. Va. 696, 698, 174 S. E. 523 (1934): "If, after expiration of the eighteen year period, production should cease, the grantor's rights should immediately terminate. The right beyond eighteen years was dependent upon a paying production at the expiration of that time." See, also, *Harness v. Eastern Oil Co.*, 49 W. Va. 232, 38 S. E. 662 (1901).

On the other hand, in *McCutcheon v. Enon Oil & Gas Co.*, 102 W. Va. 345, 353-354, 135 S. E. 238 (1926), the court remarked: "We can see very little strength in the claim that the lease has expired by its own terms at the end of the ten-year period. If there had been no development, and a vested interest had not accrued, then the payment of delayed land rental would not extend the right to drill after the ten years given for that purpose. . . . The law favors the vesting of estates, and is adverse to their destruction after they have been vested. . . . Under the facts shown it cannot be held that the lease had expired at the end of the ten year term." The *McCutcheon* case is perhaps a leading authority to the effect that *expiration* cannot be based on mere failure to market gas from producing wells.



describing what amounts to the surrender by operation of law of an easement or profit; certainly there is nothing in the common law of real property that permits one to divest himself of title simply by relinquishing it, in the manner of "abandoning" a chattel. And clearly the lessee under an undeveloped "or" lease (without a surrender clause) cannot escape payment of delay rentals by a unilateral renouncement of his rights. Nor may the parties by informal agreement achieve a surrender in fact, in defiance of the Statute of Frauds. The best analogy in legal doctrine has to do with the resumption of possession by a landlord, after his tenant has moved out, and the former's utilizing the premises for his own purposes thereafter. So, in the field of mineral law, where the senior lessee deliberately neglects or quits his leasehold, the owner may by re-letting to a junior lessee accept the other's "offer" for a surrender by operation of law of the prior oil and gas lease;<sup>25</sup> it is only a confusion of terms when courts follow the lay practice of calling this abandonment. Nevertheless, the theory (however it be named) does have considerable value within limits. Applying it in instances where the operator's conduct has been outrageous, there is usually a most salutary result. Where the lessee under the "or" lease goes along for years without drilling or paying,<sup>26</sup> — or the lessee pulls the casing from a producer and moves away with his machinery and equipment,<sup>27</sup> — or he shuts in a paying well and

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<sup>25</sup> *Clark v. Wright*, 311 Pa. 69, 77-78, 166 Atl. 775 (1933): "An unexplained cessation of operations under a lease the term of which depends upon production, without remuneration to the lessor for an unreasonable length of time, gives rise to a fair presumption of surrender, and, standing alone and admitted, would justify the court in declaring an abandonment or a surrender as a matter of law." *Simonton, Abandonment of Interests in Land* (1930) 25 ILL. L. REV. 261, 275: "The cases holding mining leases terminable by abandonment because of long continued breach of the duty to develop use the term inaccurately. The termination in such cases is by implied release or implied surrender, depending on whether the court treats the mining lease as a true lease or as a profit." *Carper v. United Fuel Gas Co.*, 78 W. Va. 433, 438, 89 S. E. 12 (1916): "As a matter of actual decision, the doctrine of implied covenants in mineral leases has thus far been limited to those cases in which it has been invoked to . . . make effective the principle of surrender by operation of law, when the premises have been abandoned after discovery of mineral and delay rentals have ceased."

*Sult v. A. Hochstetter Oil Co.*, 63 W. Va. 317, 61 S. E. 307 (1908) is an excellent example of the statement in the text. As to solid minerals, see the famous opinion in *Chandler v. French*, 73 W. Va. 658, 81 S. E. 825 (1914).

<sup>26</sup> *Smith v. Root*, 66 W. Va. 633, 66 S. E. 1005 (1910); *Martin v. Consol. Coal & Oil Corp.*, 101 W. Va. 721, 133 S. E. 626 (1926).

<sup>27</sup> *Parish Fork Oil Co. v. Bridgewater Gas Co.*, 51 W. Va. 583, 42 S. E. 655 (1902); *Lowther Oil Co. v. Miller-Sibley Oil Co.*, 53 W. Va. 501, 44 S. E. 433 (1903).

without reasonable explanation ignores the available market,<sup>28</sup> — in all these cases completely indifferent to the lessor's hope of royalties, the lessee should properly be held to a surrender. Here his acts speak louder than words; taking such behavior at its face value, the owner has a simple remedy of self-help by executing a junior lease.

Thus in the typical abandonment situation one meets a set of facts where there can be little sympathy for the operator. The trouble is that courts tend to overemphasize the theory. If proceedings in equity come before the trial chancellor, entitling the complainant to relief by forfeiture for violation of some implied condition, the decree of cancellation is more often intuitively based on legal abandonment. Even though the evidence conclusively negatives any conduct remotely resembling surrender, the opinion will just the same refer to it as "a technical abandonment."<sup>29</sup> Perhaps the explanation lies in the old maxim to the effect that "equity abhors a forfeiture"; judicial reasoning is squeamish as to forfeitures, when any other theory (no matter how far-fetched) can be employed to justify the result. Too frequently courts ignore the enlightened dictum of Judge Van Devanter:<sup>30</sup>

"There is no insuperable objection to the enforcement of a forfeiture when that is more consonant with the principles of right, justice, and morality than to withhold equitable relief."

But in the circumstances, since the incompatible advantages of reality and deception cannot be united, matters of doctrine become somewhat muddled, — and strict abandonment theory gradually extends by equitable fiction into wholly new fields.

Whenever a lessee fails to market gas from a producing well and litigation ensues, the claim that there has been an abandonment

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<sup>28</sup> *Beatty-Nickel Oil Co. v. Smethers*, 49 Ind. App. 602, 96 N. E. 19 (1911); *Monarch Oil & Gas Co. v. Hunt*, 193 Ky. 315, 235 S. W. 772 (1921). *Cf.*, also, *Harris v. Michael*, 70 W. Va. 356, 73 S. E. 934 (1912).

<sup>29</sup> *Hutchinson v. McCue*, 101 F. (2d) 111, 120 (C. C. A. 4th, 1939): "One hardly expects to find a parallel for the extraordinary conduct of the Hamilton Gas Company in deliberately refusing profitable business. The fact that gas had been found and made ready for delivery to customers did not excuse the company's refusal to produce and market, but served rather to condemn it. The actions of the company, if not a technical abandonment by the lessee, were of a strikingly similar character."

<sup>30</sup> In the great case of *Brewster v. Lanyon Zinc Co.*, 140 Fed. 801, 819, 72 C. C. A. 213 (C. C. A. 8th, 1905). *Abell v. Bishop*, 86 Mont. 478, 497, 284 Pac. 525 (1930): "The general rule that forfeitures are not favored in the law does not apply to leases for the purpose of having lands explored for oil or gas; rather in this class of cases forfeitures are favored."

is fairly certain to be made somewhere along the line. Quite possibly the lessee did in effect abandon his leasehold, for one reason or another, and the proof will establish this: there are plenty of cases in the books where that has occurred. It is essential to realize, however, that in nearly all these instances he has also been guilty of other far more serious acts than mere failure to market. In substance, he has ignored most of his express and implied obligations as to testing, protecting and further developing the leasehold: the lack of marketing is merely a cumulative incident in his abandonment by conduct. The problem as to forfeiture solely because the operator does not duly dispose of the gas is quite different. Here there has been no disposition on his part to neglect any additional phase of development or protection. By way of instance,<sup>31</sup> he has kept the equipment painted and in good order, and has mowed the right of way; he has made periodical tests of open flows and rock pressures; and, in general, he has taken the reasonably prudent operator's care of these wells. Additionally, within the rule of the *Black Band* case,<sup>32</sup> he has had the lease properly assessed and paid necessary taxes thereon. Under such conditions and apart from deliberate fraud, there can hardly be room for any contention involving the claim of abandonment.

Granted the problem of forfeiture can be wholly isolated from theories of expiration and abandonment, it would be well to investigate the various types of situations in which the issue arises. Perhaps the most common one involves the development of a gas field in "wildcat" territory: sometimes lessors believe the mere discovery of oil or gas in paying quantities will, in and of itself, create an adequate market.<sup>33</sup> The question then is whether the parties could reasonably have contemplated gas would not be sold

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<sup>31</sup> *Hutchinson v. McCue*, 101 F. (2d) 111 (C. C. A. 4th, 1939), Record, p. 36, Finding of Fact No. 7. *McCutcheon v. Enon Oil & Gas Co.*, 102 W. Va. 345, 350, 135 S. E. 238 (1926): "Its (the lessee's) failure to pay the rental does not work abandonment."

<sup>32</sup> *State v. Black Band Consol. Coal Co.*, 113 W. Va. 872, 169 S. E. 614 (1933), to the effect that proper assessment of an operator's producing oil and gas leasehold, together with timely payment of all taxes thereon, prevents forfeiture of the lease by virtue of a tax sale covering the lessor's property. Thus, the operator may now adequately safeguard his leasehold, as regards the State's claim for taxes, simply by having it duly assessed in the county where it is located and by taking care of the taxes as these are levied, — quite regardless of what the lessor may or may not do in this regard.

<sup>33</sup> In *McCutcheon v. Enon Oil & Gas Co.*, 102 W. Va. 345, 348, 135 S. E. 238 (1926), the lease was in wildcat territory: it was hardly within the contemplation of either party that gas would be marketed until a pipe-line had been built into that territory. The court commented: "The gas from the first well was never marketed, for there was no market for it, except by piping it

until at some future time a pipe line had been built into that region. The real difficulty here is as to the fate of the small independent operators who initially develop the field, only to find other companies later taking leases on all sides and the danger of drainage a very real one. When the pipe line is finally constructed, the independent with limited capital is under pressure to market at almost any price; in default thereof, his lessors are hardly likely to remain quiescent over very many years, without definite prospect of royalty payments. Often the marketing agreement signed will provide merely that the purchaser promises to buy the other's gas, but for the immediate future only if and when the purchaser needs it. It may indeed be hard to convince the lessors that patience is essential to the welfare of each. Another situation involves the drilling of new wells in a proven field, where the operator confidently expects to market as soon as an additional already-projected pipe line is completed. In this second instance, one can scarcely argue (as before) that lessor and lessee made it an implied term of their bargain, to dispense altogether with rents and royalties pending arrival of the pipe line. And yet it is safe to assume the operator has ordinarily no other marketing facilities at hand. Hence, an unforeseen delay in the arrival of the new line may prevent sale of the gas for a considerably long period, and present the lessor with an opportunity of seeking forfeiture on these facts.<sup>34</sup> However, the situation most representative of unanticipated hardship is that created in a regularly producing area by a severe business depression nearby: the operator must lose his best customers when their industries close down, so that there can be no alternative

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a great distance, the cost of which would have been prohibitive." *Cf. White v. Green River Gas Co.*, 8 F. (2d) 261, 263 (C. C. A. 6th, 1925): "While it appears from the record that the time this lease was executed this territory was known by lessors and lessee to be 'wildcat' territory, yet the presumption naturally obtains that the term of five years named in the lease was in the opinion of both parties sufficient time in which this 'wildcat' territory could be reasonably developed." *Masterson v. Amarillo Oil Co.*, 253 S. W. 908, 914 (Tex. Civ. App. 1923) lays down a sensible doctrine as to these issues: "What is a reasonable time in which the gas shall be marketed, and what amounts to the exercise of reasonable diligence in wildcat territory under all the circumstances, are questions of fact."

<sup>34</sup> Delay in the construction of the necessary pipe-line was involved both in *Hutchinson v. McCue*, 101 F. (2d) 111 (C. C. A. 4th, 1939), and in *Benedum-Trees Oil Co. v. Davis*, 107 F. (2d) 981 (C. C. A. 6th, 1939). But see *Union Gas & Oil Co. v. Adkins*, 278 Fed. 854, 857-858 (C. C. A. 6th, 1922): "Nevertheless a court of equity would hesitate to decree the cancellation of a lease, where . . . the failure to procure the laying of a pipe-line within the term named in the lease, is in no wise chargeable to the delay or default of the lessee in the development of the territory to such an extent as would justify a pipe-line company in making this expenditure."

other than to shut in the wells. No doubt the lessor never thought of that contingency: on the other hand, the operator may not be able to continue to pay rentals without some sort of market for the gas. After such a prolonged suspension of operations, it is likely the issue will ultimately reach the stage of a cancellation suit.

Frequently, the lessee will try to avoid litigation by making stipulated payments under his lease despite conditions that suspend marketing. Where the instrument provides for a fixed gas well rental,<sup>35</sup> there seems little doubt<sup>36</sup> that that procedure effectively safeguards his rights. One might even generalize: just as equity will never forfeit a lease in this jurisdiction for mere failure to pay money,<sup>37</sup> so the payment or tender of contractual well rentals will normally avert forfeiture for any sort of failure to market. Beyond that generalization, one can only guess as to a court's holding. A common practice in many gas fields is to arrange a formal compromise with the lessor, (whichever be the character of the gas revenue originally promised), by the terms of which the lessee resumes payment of ordinary delay rentals over the period of suspension. Surely by accepting these "delay rentals", the lessor definitely waives the alleged cause of action growing out of the implied duty to sell off the premises; for after all he need not take the reduced payments unless there were the compromise agreement. The newer lease provision elsewhere, already referred to,<sup>38</sup> permits the operator to pay specified well rental in the event of a shut-in: it is practically certain such a clause will be upheld. So long as the lessor receives some reasonable compensation, forfeiture for nonmarketing is hardly probable,—provided always drainage possibilities are absent.

What if the operator cannot or will not pay rentals or royalties during the cessation of operations? At law, the lessor seems remediless: the standard form of lease covenants for those payments only "on gas produced from said land and sold or used off the land."<sup>39</sup> One court has held any sums actually paid were

<sup>35</sup> McGraw Oil & Gas Co. v. Kennedy, 65 W. Va. 595, 64 S. E. 1027 (1909); Smith v. McGill, 12 F. (2d) 32 (C. C. A. 8th, 1926).

<sup>36</sup> White v. Green River Gas Co., 8 F. (2d) 261 (C. C. A. 6th, 1925), raises some troubling questions in this regard.

<sup>37</sup> Reserve Gas Co. v. Carbon Black Mfg. Co., 72 W. Va. 757, 79 S. E. 1002 (1913); Pheasant v. Hanna, 63 W. Va. 613, 60 S. E. 618 (1908).

<sup>38</sup> See footnote 23, *supra*.

<sup>39</sup> The ordinary gas well rental provision in West Virginia reads as follows: ". . . To pay . . . (\$ . . . ) Dollars each three months in advance for the gas from each and every gas well drilled on said premises, the product from which is marketed and used off the premises as a gas well, said payment

“mere gratuities”: “the lessors had no right to demand and no right of action to recover these rentals.”<sup>40</sup> Any redress must then be sought in equity. And even there, if the lease provides for fixed gas well rentals (rather than gas royalties), the operator ought to be able to placate the trial chancellor by tender of a sum covering the period of nonactivity down to the date of the equity bill. The narrow issue as to possible forfeiture for failure properly to market can be raised only in two instances: first, where there is an absolute refusal to pay the fixed rentals under any circumstances while marketing remains impossible; and second, where the lessor’s compensation is in the form of a gas royalty provision, calculation of which is not feasible after the well has been capped. In the one case the operator will not pay, but in the other, there is no way for him to estimate fairly the proper payment. In both, the lessor is being deprived of the promised advantage of the mining operation.

In the light of the foregoing discussion, the present problem has to do with an operator who has been unable to market gas for a considerable time because of factual conditions wholly beyond his control. While there has been no expiration of the vested estate nor abandonment of the leasehold, the operator simply will not or cannot make the contractual payments to the lessor, until an opportunity of marketing creates the obligation and determines its extent. On the other hand, the lessor’s minerals have been tied up more or less indefinitely, so that his lease is proving “entirely fruitless” as to rents and royalties. Attempts to reconcile the conflicting

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to be made on each well from date utilized, and to be paid each three months thereafter while the gas from said well is so marketed and used.”

In construing a rental provision to this effect, it has been held there is no liability for rentals unless the operator is in fact able to market: *Leslie v. Chase National Bank*, 83 F. (2d) 1013 (C. C. A. 6th, 1936), Printed Record therein, p. 53, lower court opinion *per* Cochran, Dist. J. (1933). See, also, Note (1933) 40 W. VA. L. Q. 68; *Rockcastle Gas Co. v. Horn*, 241 Ky. 393, 44 S. W. (2d) 273 (1931); *Iams v. Carnegie Natural Gas Co.*, 194 Pa. 72, 45 Atl. 54 (1899); *Brooks v. Ark.-La. Pipe Line Co.*, 77 F. (2d) 965 (C. C. A. 8th, 1935).

<sup>40</sup> *White v. Green River Gas Co.*, 8 F. (2d) 261, 263 (C. C. A. 6th, 1925). *A fortiori*, in the gas royalty situation under the following type of lease provision: “If any well on said premises shall produce natural gas in paying quantities, and such natural gas is used off the premises or marketed by Lessee, then Lessor shall be paid, as royalty, one-eighth (1/8) of the value, at the mouth of the well, of so much of such gas as is used off the premises and one-eighth (1/8) of the net proceeds from the sale of so much of such gas as is so marketed by Lessee.”

Gas royalty provisions have occasionally been examined in West Virginia decisions, — *e. g.*, *Moore v. Ohio Valley Gas Co.*, 63 W. Va. 455, 60 S. E. 401 (1908), and *Trimble v. Hope Natural Gas Co.*, 117 W. Va. 650, 187 S. E. 331 (1936).

legal doctrines herein are not apt to prove completely successful. For the lessor, it will be contended that the construction of the lease must be in his favor,<sup>41</sup> — all things being equal, — particularly where as in the instant case his revenue must depend on an apparently potestative condition involving the other party's ability to market. Furthermore, where the original lessor's reversion has been conveyed to a life tenant with remainder over, the latter may suffer real hardship if income from the minerals be completely withheld.<sup>42</sup> In contrast, the operator may assert the reasonings are just, but the premises false. Neither at law nor in equity is the duty of marketing more than one of exercising reasonable diligence;<sup>43</sup> if it be absolutely impossible to dispose of the gas, the complainant's prayer for cancellation should be rejected without hesitation. Appealing to the "equities" of the situation, the operator will seek comparison of his own very substantial investment in drilling and equipment, with the relatively inferior sums that might have been included in the rents or royalties from marketing. With the labor of balancing these diametrically-opposing views, the court might be inclined to look to the social policy involved and to hold that the implication of such an equitable right of re-entry for condition broken would be contrary to the welfare of the public, — to the extent that the sanction of forfeiture for any failure to market might lead to overproduction and consequent waste of gas. Even despite the arid, unimaginative temper of the law in this field, the court's "authoritative ideal, however tenuous or inarticulate",<sup>44</sup> could thus prove to be a recognized social interest in the conservation of natural resources.<sup>45</sup>

<sup>41</sup> *Bettman v. Harness*, 42 W. Va. 433, 26 S. E. 271 (1896). Cf. *Masterson v. Amarillo Oil Co.*, 253 S. W. 908 (Tex. Civ. App. 1923), indicating that leases should not be construed so strongly against lessees in wildcat territory.

<sup>42</sup> The life tenant is of course entitled to the whole of the royalties from "already-opened" mines. *Koen v. Bartlett*, 41 W. Va. 559, 23 S. E. 604 (1895); *Bramer v. Bramer*, 84 W. Va. 168, 99 S. E. 329 (1919). Other instances where the withholding of revenue from a producing well may create real hardship can readily be imagined.

<sup>43</sup> *Carroll Gas & Oil Co. v. Skaggs*, 231 Ky. 284, 21 S. W. (2d) 445 (1929); *Roads Drilling Co. v. Allred*, 123 Tex. 229, 70 S. W. (2d) 576 (1934). However, in *Mid-Continent Petroleum Corp. v. Sander*, 67 F. (2d) 9 (C. C. A. 10th, 1933), after a federal court had used the "prudent operator" standard, the Supreme Court reversed, 292 U. S. 272, 54 S. Ct. 671, 78 L. Ed. 788 (1934), holding the lessee's failure to develop to be a breach of the implied covenants, even despite unfavorable geologic data and past experience.

<sup>44</sup> *Hardman, Public Utilities, I. The Quest for a Concept — Another Word* (1934) 40 W. VA. L. Q. 230, 240.

<sup>45</sup> The court's interpretation of the lessee's implied obligation to develop would thus take into account the paramount necessity of avoiding injury to the common source of supply. See *Union Gas & Oil Co. v. Fyffe*, 219 Ky. 640,

Quite apart from the purely legal considerations, there is a similar clash in the physical and economic facts that encompass the problem. First and foremost, the marketing of gas has to reckon with a practical impossibility of storage once the product has been mined. No industrial purchaser can ever lay in an extra supply, for consumption must perforce be on a hand-to-mouth basis. Though oil production may permit of tanks and other storage facilities and though moderate stocks of coal might occasionally be accumulated,<sup>46</sup> the gas operator must either leave his surplus mineral in place or pump it back into the ground through other wells.<sup>47</sup> Perhaps the storage factor would seem unanswerable, were it not for the ever-present danger of drainage, — and this more than anything else influences the decree in gas production suits. Estimation and conjecture as to drainage will have to take into account the high or low porosity of the gas-producing sand, its thickness of “pay” and the amount of rock pressure; but when these geological mysteries have been unveiled, one finds a curiously sympathetic disposition in favor of the lessor where the entire advantage of the situation appears to be with the expert operator. No doubt in the past the perils of drainage were somewhat exaggerated:<sup>48</sup> the real question now is whether modern deep-well drilling to sands of great volume or pressure ought to necessitate additional legal safeguards.<sup>49</sup> It is no good to leave the product unmarketed

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294 S. W. 176 (1927). In *Manufacturers Gas & Oil Co. v. Indiana Natural Gas & Oil Co.*, 155 Ind. 461, 474, 57 N. E. 912 (1900), it was said: “Independently, however, of any statute for the reason already stated, the common owners of the gas in the common reservoir, separately or together, have the right to enjoin any and all acts of another owner which will materially injure, or which will involve the destruction of, the property in the common fund, or supply of gas.”

<sup>46</sup> But see Reeder, *Some Problems of the Bituminous Coal Industry* (1939) 45 W. VA. L. Q. 109.

<sup>47</sup> An example of this is found in *Hammonds v. Central Kentucky Natural Gas Co.*, 225 Ky. 685, 75 S. W. (2d) 204 (1934), discussed in Comment (1935) 41 W. VA. L. Q. 431.

<sup>48</sup> Veasey, *The Law of Oil and Gas* (1920) 18 MICH. L. REV. 445, 652, 749. CRAIG, OIL FINDING (1912) 46: “From all of these considerations it will be seen that the migration of petroleum is a very circumscribed action, and cannot be called upon to explain any very widespread phenomena in oil fields. To put it briefly, petroleum goes where it can; but, from the very nature of the conditions under which it has been formed and under which it is preserved, its migrating movements are checked and hindered in almost all directions. Thus, when earth oils are discovered in any locality, we are almost justified in applying to them the famous conclusions of the gentleman who devoted his life to research upon the subject of the ‘fiery, flying serpents in the wilderness’, with special attention to their origin and subsequent history: (1) ‘They was there all the time;’ and (2d) ‘they stayed where they was.’ ”

<sup>49</sup> TUCKER, DEEP WELL RECORDS (1936) WEST VIRGINIA GEOLOGICAL SURVEY; MARTENS, PETROGRAPHY AND CORRELATION OF DEEP WELL SECTIONS IN WEST



if a not far-distant development on other property can sooner or later drain away the lessor's gas, so that eventually the whole field is gradually "played out". Moreover, at the other end of the scale, the producing wells may prove of small volume or be low pressured; and pumping will thus be requisite in order to step up the pressure to the regular pipe-line flow. The expense of preparing the product for market has to be met ultimately from the price the purchaser is willing to give, varying with periods of prosperity or depression. Which brings up the paramount economic factor in the discussion, — the operator's profit out of marketing transactions. With a very considerable investment in the well itself and with some inevitable overhead, it probably amounts to unreasonable confiscation to compel sale off the premises at substantial loss. Yet should this reasoning be completely followed out, the operator could easily gain the unconscionable position of holding the leasehold "for purposes of speculation", without heeding the lessor's protests. Certainly no principle of public utility law would guarantee or limit the marketing profit within reasonable bounds. In short, all these factors set the issue in so clear a light that it is impossible to be blind to the difficulties inherent to the solution.

The analysis up to this point is fairly open to criticism of having dealt largely with abstract considerations, without going into the more concrete matters of proof that confront counsel in the ordinary cancellation proceeding. These often escape attention in any theoretical discussion, but in the present instance attention is definitely called for. By and large, it is feasible to group such evidentiary facts under four principal headings:

1. *Length of time.* Between the two extremes of a relatively brief suspension of marketing and the indefinitely long cessation of operations upon the leasehold one meets a middle ground where the time factor will be most determinative. While there cannot be any hard-and-fast rule as to this,<sup>50</sup> — no presumption of forfeiture after seven years' unexplained non-

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VIRGINIA AND ADJACENT STATES (1939) WEST VIRGINIA GEOLOGICAL SURVEY. Note Judge Maxwell's careful discussion of the drainage problem in Trimble v. Hope Natural Gas Co., 117 W. Va. 650, 660-661, 187 S. E. 331 (1936).

<sup>50</sup> In *Starn v. Hoffman*, 62 W. Va. 422, 423, 59 S. E. 179 (1907), Judge Brannon remarked: "The very requirement to begin mining the next day, and the very nature of the purpose of the contract show that time is of the essence of the contract." Note (1933) 40 W. VA. L. Q. 68, 69-70: "However, it is believed that one year should be the maximum period, from either (a) the expiration of the fixed term, assuming that there has never been any utilization, or (b) the date upon which the gas was last utilized.

marketing, — still the very absence of sales over a considerable period appears persuasive as to the improbability of the lessee's future success. In strict legal theory of course, the lease denotes the conveyance of a property interest; and it is perhaps unsound to contend that time should here be of the essence, unless the instrument were construed as a simple bilateral contract<sup>51</sup> (which would be contrary to its express terms). Anyway, it ought to be unnecessary as regards the time element to go beyond the implication of a condition subsequent for forfeiture, reasonably founded on a complete and permanent failure in the true purpose of the *profit a prendre*.<sup>52</sup>

2. *Extent of diligence.* After the lessor has made out his *prima facie* case by proving the lapse of time without marketing, the operator should then comply with the procedural burden of going forward by showing precisely what efforts were actually undertaken. Courts are apt to be lenient in this type of litigation if in fact the operator is diligently seeking an available market. His proof ought to go into the quality and pressure of the gas, the accessibility of pipe lines, prevalent prices in that field and the extent of negotiation with prospective purchasers.<sup>53</sup> If there has been slackness or indifferent management, the eventual result is not difficult to predict. On the other hand, a sensible and candid lessee, firm in his en-

<sup>51</sup> The leading decision treating a lease as a bilateral contract is *University Club of Chicago v. Deakin*, 265 Ill. 257, 106 N. E. 790 (1914). The weight of authority holds to the contrary, — that a lease represents on the one side the conveyance of an estate to the lessee, and on the other, the independent covenants of the lessee to perform certain obligations.

<sup>52</sup> The doctrine of essential error, when impossibility is urged as a defence to contractual liability, might serve by way of analogy here. See, too, *Muhlenberg v. Henning*, 116 Pa. St. 138, 9 Atl. 144 (1887), excusing performance because of the mutual mistake of the parties as to the existence of adequate iron ore. In the present instance, one might argue there was an erroneous assumption as to the availability of a market for the gas.

<sup>53</sup> *Strange v. Hicks*, 78 Okla. 1, 2, 188 Pac. 347 (1920): "The lessees for a period of three years after the execution of the lease continued to develop this territory, drilling some 30 wells, with the hope that sufficient gas would be discovered that would justify a pipe-line being laid to this field. The record shows that (the lessee) negotiated with at least 10 different pipe-line companies or parties interested in same in order to sell the gas from these leases, going with them upon the leases, but, owing to conditions then prevailing and the small quantity of gas then discovered he was unable to secure a line. . . . Finally, (he) did negotiate for a pipe-line to be laid, which was explained to the lessors. A pipe-line was finally laid to this field." Cancellation was accordingly refused in this case. It is interesting to compare the judicial technique employed in *Benedum-Trees Oil Co. v. Davis*, 107 F. (2d) 981, 986 (C. C. A. 6th, 1939): "The record is replete with evidence that for more than nine years the lessees have made fruitless efforts to get a pipe-line built to the wells here in question and to those adjacent. . . . We are of the opinion that because of the long delay in finding a market for the gas, the leases terminated." See *Stranahan v. Independent Natural Gas Co.*, 98 Mont. 597, 41 P. (2d) 39 (1935).

deavor to operate for the benefit of both parties, can safely anticipate favorable consideration.

3. *Probability of speculation.* As a sort of replication to the alleged diligent efforts of the operator, the property owner may introduce evidence tending to establish the other's real purpose as one of speculating in mineral development.<sup>54</sup> No doubt a fair amount of shrewd business judgment in awaiting satisfactory market conditions must be held reasonable in as risky a trade as the oil and gas industry. The operator might shut in his wells for a year or thereabouts in order to get a better price, without encountering serious trouble. Yet let the chancellor once gain the impression from the entire record that the failure to market over an extended period came about as the result of a bad speculative guess, and the case is irretrievably lost.<sup>55</sup> The law simply will not permit the property to be tied up for so long a time, without rents or royalties, by a lease that represents primarily an intent to

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<sup>54</sup> *Benedum-Trees Oil Co. v. Davis*, 107 F. (2d) 981, 986 (C. C. A. 6th, 1939): "Gas leases are sometimes retained for speculative purposes, after the cessation of exploration and the failure within a reasonable time to find a market for the mineral. *Sauder v. Mid-Continent Petroleum Corp.*, 292 U. S. 272, 282, 54 S. Ct. 671, 78 L. Ed. 1255, 93 A. L. R. 454 (1934)." "Shall the lease stand to tie up the land and prevent its owner from the use of the coal and let the lessee hold it up for speculation?" *per Brannon, J.*, in *Starn v. Hoffman*, 62 W. Va. 422, 423, 59 S. E. 179 (1907). See *Hutchinson v. McCue*, 101 F. (2d) 111 (C. C. A. 4th, 1939), Brief for Appellants, pp. 36-37: "The lessee was under the duty to sell the gas, and pay the rental therefor, yet the trial court holds that it was equitable for the lessee to refuse a market at hand in favor of a mere speculation, and make the lessor pay the cost of the speculation."

<sup>55</sup> *Hutchinson v. McCue*, 101 F. (2d) 111, 120 (C. C. A. 4th, 1939): "It may be said here . . . that there is no case which goes so far as to say that the lessee after discovery 'may cease operation, refuse to develop the property, tie up the oil by his lease, and simply hold it for speculative purposes or to await his own pleasure as to the time of development.'" Such was also the approach in *Collins v. Mt. Pleasant Oil & Gas Co.*, 85 Kan. 483, 118 Pac. 54 (1911).

In the former case, the court apparently concluded that the operator voluntarily, — or at least without adequate explanation, — relinquished an existing marketing arrangement for the sale of its gas at twelve cents per m. c. f., because of its hope that "a more desirable customer could be found." As it turned out, the operator later got a contract (when a projected pipe-line was finally constructed), subject to a priority in favor of other producers totalling 50,000,000 cu. ft. daily production: but, for one reason or another, no gas was actually sold under this contract until after the ten-year fixed term of the lease had elapsed, — thus entailing a period of four years during which the wells were shut in. Eventually, the operator agreed to modify the new contract by selling the gas at eleven cents per m. c. f., for a limited period of time, and marketing was then resumed, (Brief for Appellants, pp. 12-17). On these facts, the court commented (p. 120): "One hardly expects to find a parallel for the extraordinary conduct of the (lessee) in deliberately refusing profitable business." However, reviewing the same record, the federal district judge and the dissenting senior circuit judge found otherwise.

gamble. And apparently giving up one customer to secure a better contract with another now falls within this category.

4. *Amount of investment.* In the long run, "the equities" of the suit will likely control its outcome. And aside from the length of time, extent of diligence and probability of speculation, the salient "equity" is the cost of the wells to the operator. Where that reaches any large figure, courts are generally reluctant to forfeit. There is every reason to protect such an investment: its very size comprehends a serious loss of interest on capital, so that the operator has definite incentive to utilize any sort of chance to market. Granted this economic pressure, one has a reasonably sound guarantee of good faith in the management of the wells. Even without that, it would be grossly unfair and inequitable to take away valuable gas properties when the lessor's financial claims total only a small fraction of the expenditure already incurred.<sup>56</sup> Details as to development costs are thus readily admissible into evidence, their relevancy going to the issue of the relief to be decreed.

Such, in all its various aspects, is the problem of forfeiture for failure to market gas from a producing leasehold. Reduced to its respective common denominators, the outlines of certainty become more definite, and the shades of probability more distinct. The operator who makes some rental payment by lease stipulation or later compromise is pretty sure to be safe from troublesome disputes almost indefinitely. It is only when the lessor receives no return, — though his land seems to be burdened with a perpetual servitude, — that the ancient tradition of the common law requires redress. Unquestionably, on principle there must be some limit beyond which this anomalous situation cannot continue: in the end the operator must either market or pay, if cancellation is to be averted. But the end may prove to be considerably far off. Disregarding the mere temporary suspensions over brief periods, courts are fairly tolerant (and rightly so) in the situations where no reasonable diligence can achieve successful marketing for the

<sup>56</sup> Compare, for example, *Strange v. Hicks*, 78 Okla. 1, 2, 188 Pac. 347 (1920), where lessee's total outlay was "from \$60,000 to \$75,000", and *Pryor Mountain Oil & Gas Co. v. Cross*, 31 Wyo. 9, 16, 222 Pac. 570 (1924) where "the lessees expended about \$24,000 in drilling", — with *Hutchinson v. McCue*, 101 F. (2d) 111, 114 (C. C. A. 4th, 1939) where the total "drilling cost" was \$37,232.04, and *Benedum-Trees Oil Co. v. Davis*, 107 F. (2d) 981, 984 (C. C. A. 6th, 1939) where the drilling and shutting-in cost was \$13,400. In the first two cases, the courts protected the investment by refusing cancellation: in the other two, the "equities" were held to be with the lessor even despite the operator's expenditures.

immediate future. Any other holding would have the untoward result of speeding up the reckless waste of gas resources.

The border-line instance causes the difficulty. Without deciding whether the hard cases have made good or bad law, it is proper to say that forfeiture for nonmarketing has been more freely available in recent decisions than the historical precedents of chancery would justify. That remedy should never be decreed unless in an extreme case the operator's conduct has been such as clearly to indicate that he cannot or will not market within any reasonable future period.<sup>57</sup> And seeking equity, probably the lessor ought to do equity by compensating the operator for casing and necessary equipment;<sup>58</sup> their confiscation without payment might violate the lease, but their removal would quite likely destroy the producing well. If one may not turn the clock back as regards present law, then it might be wise to substitute conditional decrees, — so that the forfeiture would become effective only in the event the lessee were unwilling to pay damages based on his failure to market. These damages could quickly be calculated if the lease called for gas well rentals;<sup>59</sup> otherwise, the estimated gas royalties

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<sup>57</sup> One may be asked to define more exactly the phrase, "within any reasonable future period." Perhaps here the future should be judged by the past. If for several years there has been complete failure to market, despite every sort of diligent effort on the operator's part, — and if further there is no immediate prospect of successful marketing ahead, — then surely the lease should terminate. Practically, the investment is lost almost as completely as if the operator had drilled a dry hole. And any other result would have the effect of giving the operator an absolute fee simple in the gas, instead of the exclusive *profit a prendre* that was bargained for.

Obviously the term "several years" is ambiguous; yet its more precise limitation is for the legislature and not for the courts, if an iron-clad statute of limitations is to be formulated for this problem.

<sup>58</sup> Ordinarily, the lessee has a definite right to pull the casing, *Gartland v. Hickman*, 56 W. Va. 75, 49 S. E. 14 (1904); *Collins v. Mt. Pleasant Oil & Gas Co.*, 85 Kan. 483, 118 Pac. 54 (1911). Yet in *Warner v. Shell Petroleum Corp.*, 132 Kan. 837, 842, 297 Pac. 682 (1931), it was held the "lessee is not permitted to dismantle the operating equipment and pull the casing without offering the lessor the right to test the production and fairly determine whether the well could be profitably operated." Thus equity may enjoin an inequitable removal: *Powers v. Bridgeport Oil Co.*, 238 Ill. 397, 87 N. E. 381 (1909); *S. W. Oil & Gas Co. v. Kimball Oil & Dev. Co.*, 224 S. W. 1111 (Tex. Civ. App. 1920). See *Proposed Louisiana Mineral Code* (second revised draft) art. 117: "All casing in wells removed by the lessee must be so removed in such manner as not to injure the property or its underlying mineral content." Still any confiscation of the equipment without compensating the operator would seem unfair and possibly outrageous in an extreme case.

<sup>59</sup> The amount owing can be estimated as in *McGraw Oil & Gas Co. v. Kennedy*, 65 W. Va. 595, 64 S. E. 1027 (1909). For the conditional decree, see *Adkins v. Huntington Dev. & Gas Co.*, 113 W. Va. 490, 497-498, 168 S. E. 366 (1933): "Therefore, the decree must be modified so as to require the drilling of an offset well, or the payment of \$300.00 per year in lieu thereof, until

lost might follow the measure of damages sanctioned in those few jurisdictions which limit the lessor to an action at law on the implied covenant to market.<sup>60</sup> In effect, the respondent could thus pay up or surrender.

The increasing use of gas royalty provisions may before long raise the question in West Virginia courts as to the fate of the nonmarketing lessee. The profession has no clear indication at present of what the judicial attitude will be on such facts.<sup>61</sup> Meantime, the contractual substitution of fixed rentals for unearned royalties in the newer leases ought to work as well here as it has done in other states, and perhaps prove the best possible solution to the problem. Nevertheless, whatever happens, our common law can never allow the oil and gas lease to become through the lessee's inactivity "a snare for the entrapment and injury of the unwary landlord."<sup>62</sup>

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such time as such a well is drilled, or the lease abandoned, or in case neither is done, that the lease be cancelled as to all the property, with the exception of the designated acreage around the present well." *Dillard v. United Fuel Gas Co.*, 114 W. Va. 684, 173 S. E. 573 (1934); *Union Gas & Oil Co. v. Fyffe*, 219 Ky. 640, 294 S. W. 176 (1927). Cf. *McCutcheon v. Enon Oil & Gas Co.*, 102 W. Va. 345, 135 S. E. 238 (1926).

<sup>60</sup> See *Daughetee v. Ohio Oil Co.*, 263 Ill. 518, 105 N. E. 308 (1914); *Carroll Gas & Oil Co. v. Skaggs*, 231 Ky. 284, 21 S. W. (2d) 445 (1929); *Harris v. Ohio Oil Co.*, 57 Ohio St. 118, 48 N. E. 502 (1897). The ascertainment of such damages for failure to market should be no more difficult than the estimation of damages in libel actions or where damages for nervous shock are recoverable.

<sup>61</sup> The narrow problem of failure to market gas as possible ground for forfeiture of the lease has never been squarely considered by the supreme court of appeals, in an instance where abandonment or expiration on the one side, or waiver or estoppel on the other was not available as a basis for the ultimate decision. There is no reason to believe *Grass v. Big Creek Development Co.*, 75 W. Va. 719, 84 S. E. 750 (1915), — holding that the lessor's remedy for breach of implied covenants is in the absence of fraud limited to the recovery of damages, — is necessarily controlling in this sort of situation. In *Allen v. Colonial Oil Co.*, 92 W. Va. 689, 699, 115 S. E. 842 (1923), it was said: "To justify cancellation of a lease upon grounds not stipulated, but upon implied covenants only, a case of extraordinary hardship, occasioned by lack of diligence in the development of the land leased for oil and gas, must be alleged and proved." No doubt that "case of extraordinary hardship" will some day be found.

<sup>62</sup> *Iron Co. v. Trout*, 83 Va. 397, 409, 2 S. E. 713 (1887): "Yet, looking to its nature and object, it cannot be contended that the lessees had the option to work or not to work the ore mines for an indefinite time, and thus convert what was designed to yield a handsome daily income to the lessors into a mere barren encumbrance on his land, a cloud on his title, an incubus and a manacle which would oppress him and destroy the marketable value of his land."