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Oil and Gas: The Implied Covenant for Further Exploration–Does it Exist in Oklahoma

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if the well is a dry hole, then the loss must fall on the parties to the venture as a calculated business risk. In light of economic realities and the ultimate goal of development, Oklahoma courts should not unduly penalize the prudent operator.

If an informed attorney is involved at the initial stages of a proposed drilling operation, many of the problems outlined above may be avoided. Draftsmanship evident in many oil and gas leases now in use displays not only a less than adequate working knowledge of basic oil and gas law but a certain degree of irresponsibility toward the business risks associated with oil and gas ventures. An attorney who utilizes the barest minimum of "saving" clauses is asking for almost certain litigation and financial misfortune for his client. The use of an expansive saving clause that allows operations past the primary term in anticipation of uncertainties that arise in the oil and gas industry will better accomplish the ultimate goal of development, the production of oil and gas.

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Oil and Gas: The Implied Covenant for Further Exploration—Does It Exist in Oklahoma?

In 1956 a new theory was proposed involving implied covenants in the field of oil and gas law. This new theory was identified as the implied covenant of further exploration.[1] This proposed covenant has caused substantial controversy among many writers and courts as to whether it should be recognized as a separate covenant, distinct from the implied covenant of further development. Opinions have been written about this new covenant approving it,[2] rejecting it,[3] and finding no need for it because the existing covenant of further development is said to encompass all situations adequately.[4] This proposed covenant has caused the area involving implied covenants to be scrutinized more closely than ever before.[5]

1. Meyers, *The Implied Covenant of Further Exploration*, 34 TEX. L. REV. 553 (1956) [hereinafter cited as Meyers].

2. *See* Meyers, *supra* note 1; E. KUNTZ, OIL AND GAS § 62.1; R. HEMINGWAY, OIL AND GAS § 8.3 (1971).

3. *See* Brown, *The Proposed New Covenant of Further Exploration: Reply to Comment*, 37 TEX. L. REV. 303 (1959); Brown, *The Implied Covenant for Additional Development*, 13 SW. L.J. 149 (1959); Merrill, *The Implied Covenant of Further Exploration*, 4 ROCKY MTN. MIN. L. INST. 205 (1958).

4. *See* Galvin, *Meyers v. Brown—Jurisprudence in Action*, 7 U.C.L.A. L. REV. 589 (1960); Merrill, *The Implied Covenant of Further Exploration*, 4 ROCKY MTN. MIN. L. INST. 205 (1958); Merrill, *The Implied Covenant of Further Exploration in Oklahoma*, 13 OKLA. L. REV. 249 (1960).

5. Merrill, *The Implied Covenant for Further Exploration*, 4 ROCKY MTN. MIN. L. INST.

A recent Oklahoma case, *Mitchell v. Amerada Hess Corp.*,[6] has determined that the implied covenant to further explore does not exist separately from the covenant to further develop. This conclusion seems to be in direct conflict with prior Oklahoma case law that indicates it does exist, although the courts may not have used the specific term of "further exploration" to identify it.[7]

The intent of this note is to analyze the Oklahoma cases to determine if, in fact, Oklahoma courts recognize a covenant of further exploration separately from the covenant of further development, and to determine the appropriate standard for its application.

Analysis of the Covenants for Further Exploration and Further Development

To understand the implied covenant for further exploration as discussed in this note, it is necessary to distinguish between the duty to explore and the duty to develop. The duty to develop is concerned with additional drilling in known producing formations, while the duty for further exploration is concerned with additional drilling in potentially productive strata that are as yet unproved.[8]

The implied covenant of further development is intended to prevent delays in recovering oil and gas in place. Because the development of the leasehold is the main consideration for the granting of a lease, maximum development is required to further the original purpose of the parties. Failure to develop the leasehold deprives the lessor of royalties and prevents him from procuring further development himself. Delay in development may result in drainage of adjoining lands as the remainder of the field is fully developed and depleted.[9]

The covenant for further exploration differs from the covenant for further development, both in the reasons given for it and in the harm it seeks to avoid. The covenant for further exploration was suggested by Professor Meyers in 1956.[10] He suggests it should apply to situations where lessors demand additional drilling in unproved strata. An example of when the covenant would

205, 244 (1958), wherein Professor Merrill states: "Professor Meyers has made a challenging and stimulating suggestion for dealing with a most puzzling set of decisions. We all owe him a debt of gratitude for making us think the whole subject through once more."

6. 638 P.2d 441 (Okla. 1981).

7. *See* Sauder v. Mid-Continent Pet. Corp., 292 U.S. 272 (1934); Magnolia Pet. Co. v. Wilson, 215 F.2d 317 (10th Cir. 1954); Trust Co. of Chicago v. Samedan Oil Corp., 192 F.2d 282 (10th Cir. 1951); Crocker v. Humble Oil & Ref. Co., 419 P.2d 265 (Okla. 1965); Producer's Pipe & Supply Co. v. James, 332 P.2d 958 (Okla. 1958); Neff v. Jones, 288 P.2d 712 (Okla. 1955); Sand Springs Home v. Clemens, 276 P.2d 262 (Okla. 1954); Colpitt v. Tull, 204 Okla. 289, 228 P.2d 1000 (1950); McKenna v. Nichlos, 193 Okla. 526, 145 P.2d 957 (1944); Doss Oil Royalty Co. v. Texas Co., 192 Okla. 359, 137 P.2d 934 (1943).

8. H. WILLIAMS & C. MEYERS, OIL AND GAS LAW § 831 (1982). *See also* Chenowith v. Pan American Pet. Corp., 314 F.2d 63 (10th Cir. 1964); E. KUNTZ, OIL AND GAS § 58.1 (1978); R. HEMINGWAY, OIL AND GAS § 8.3 (1971).

9. E. KUNTZ, OIL AND GAS § 58.1, at 61.

10. Meyers, *supra* note 1.

be applicable is as follows: Suppose an oil and gas lease is executed on 1,280 acres of land for a primary term of five years. The lessee drills and obtains a commercial gas well at 4,500 feet in the third year of the primary term. Ten years later, other operators conduct drilling at greater depths in the general vicinity and discover a productive formation. Thereafter, the lessor demands deeper test wells on his land but the lessee refuses, stating that further drilling is unwarranted at that time. Twelve years later, the lessor sues to cancel the lease, except for the 160 acres surrounding the producing gas well. Experts testify that there is a fair chance of discovering oil at greater depths but that any well drilled would be a wildcat. One operator testifies that he would be willing to drill a test well on the lessor's land if he could obtain a lease.[11] The question is whether the lessor should be able to cancel the lease under these circumstances.

The covenant for further exploration may also apply to further exploration in the horizontal plane. Suppose in the above example that a well is drilled in the northeast corner of the 1,280 acres and the lessor seeks drilling in the southwest portion of the land to the same producing horizon. The lessee refuses because he thinks the risk is too great.[12] Again, the question is whether the lessor should be allowed cancellation of the lease.

A definition of the breach of the covenant of further exploration has been summarized as follows:

> [T]o establish breach of the covenant of further exploration, the lessor must show that under the circumstances the failure to drill exploratory wells in search of a new producing formation is unreasonable. Among the circumstances relevant to the inquiry are: (1) the period of time that has elapsed since the well was drilled; (2) the size of the tract and the number and location of existing wells in relation thereto; (3) the existence on the land of untested geological formations favorable to the accumulation of hydrocarbon substances; (4) the attitude of the lessee toward further testing of the land, and his operations on the land and elsewhere in the vicinity in this regard; (5) the feasibility of further exploratory drilling, including the cost of drilling, the market for the product, and the size of the block needed to justify a test well; (6) whether part of the leasehold is excluded from a production unit, so that the

11. H. WILLIAMS & C. MEYERS, OIL AND GAS LAW § 842, at 264-65 (1982).

12. *Id.* at 265 n.3. *See also* example given in Meyers, *supra* note 1, at 555:
A rancher executed a lease on 640 acres of land in 1930. In 1932, oil production was obtained in the northeast quarter-section. Four wells were drilled, the first three were producers and the fourth, in the southwest quarter of the quarter-section, a dry hole. No other wells were drilled. In 1956 production totals sixty barrels daily from all three wells. But in 1955 another and deeper producing formation was discovered by a well located two miles to the southwest of the southern boundary of the lease. The rancher demands further exploratory drilling on his land. Should he get it?

> lease is being preserved thereon without the payment of royalty for such acreage or the conducting of operations thereon.[13]

The reasons given for this covenant are derived from the two main objectives the lessor seeks by granting the oil and gas lease: the testing and the developing of all portions of the leased premises.[14] If the lessee fails either to develop fully all portions of the leased premises, or to explore all portions of it, the essential purpose for which the lease was granted ceases to exist, and the lease should be subject to cancellation as to the unexplored portions of it.

The harm in exploration cases is also different from that in the development cases. In the exploration cases, the harm to the lessor is the lack of further exploration on the lessor's land that could result in monetary losses, especially if there is another operator willing to explore by drilling if he could acquire the lease. The harm to the lessor in a development case is the deprivation of royalties and a denial of the opportunity to have the land further developed.

Analysis of the Standards To Be Applied

If the implied covenant for further exploration is adopted, it will be necessary to formulate an appropriate standard for evaluating the operator's performance.

The ultimate question involved in this controversy is whether the standard of the reasonably prudent operator that applies to the covenant of further development is to be applied in further exploration cases. The rule has been well defined as follows: "[T]he lessor, in order to prove a breach of the covenant to drill additional wells, must show that the additional well would probably produce sufficient amounts to repay the expense of drilling, equipping and operating such well and also produce a reasonable profit on the entire outlay."[15]

Since the implied covenant for further development contemplates drilling in proved formations, the reasonably prudent operator rule is the appropriate standard. This rule incorporates the requirements for demand and notice prior to cancellation and gives the lessee an opportunity to commence further drilling. If he can show that further development would be unprofitable, the leasehold will not be canceled. The lessor presumably is not harmed because no prudent operator would drill even if the lessor could give him a lease. In these lease cancellation cases, drainage is always an appropriate consideration in discussing offset wells, and substantial drainage indicates that another well would be profitable.

The prudent operator rule is inappropriate for the implied covenant for further exploration mainly because the covenant contemplates drilling in unproved formations. If the prudent operator rule is strictly applied to explora-

13. H. WILLIAMS & C. MEYERS, OIL AND GAS LAW § 841, at 259-60 (1982).
14. Producer's Pipe & Supply Co. v. James, 332 P.2d 958 (Okla. 1958).
15. Ramsey Pet. Corp. v. Davis, 184 Okla. 155, 158, 85 P.2d 427, 430 (1938).

tion situations, the lessor would be required to prove the probable profitability of the requested additional well. Since the covenant for further exploration contemplates drilling in unproved formations, it would be next to impossible for the lessor to prove this probable profit. Consequently the lessor would not be entitled to the exploratory well in any circumstance. It has been argued that if the lessor does not have the burden of showing that additional drilling would be profitable to the lessee, this would defeat the purposes and intent of the contracting parties in an oil and gas lease.[16] This is not true. If the lessee holding a large tract of land under an oil and gas lease has developed only a small portion of it and an unreasonable length of time has passed since the last drilling, the lessee presumably is not harmed because he was not going to drill additional wells anyway. He may be losing the right to hold the larger tract for purely speculative purposes, but such speculation is expressly forbidden by case law.[17]

The intent behind an oil and gas lease was stated as follows in *Fox Petroleum Co. v. Booker*[18]:

> The principle, as we understand it, is that development of every part of the lease is an implied condition. Therefore, whether the undeveloped portion be a single tract remote from the rest, or a considerable portion of a very large tract, or a deeper stratum, the existence of which may be doubtful, or the east one hundred acres of a tract of 160, it is an implied condition that the lessee will test every part. When he abandons all further testing and disclaims any obligation to test, he may be required likewise to surrender all claim to the property.[19]

This definition implicitly incorporates the duty for further exploration without the prudent operator test. It seems reasonable that the prudent operator rule not be strictly applied, if it is to be applied at all. If the rule is rigidly applied, the result will invariably favor the lessee, and the lessor will be harmed because he cannot procure any further testing of the remainder of the leasehold. If another standard is used and the lease is canceled as to the unproved formations, the lessee is not harmed because he was not planning to test those formations anyway.

One court has stated that the prudent operator rule is to be used as a "measuring stick" and that it should be flexible, adjusting to the circumstances of each case.[20] In applying this new, flexible standard, the courts should require that a demand be made of the lessee, giving him a chance to drill another well to avoid cancellation of the lease. The only factor this new standard should not require is that the lessor prove that the additional well would be pro-

16. Producer's Pipe & Supply Co. v. James, 332 P.2d 958 (Okla. 1958).
17. Doss Oil Royalty Co. v. Texas Co., 192 Okla. 359, 137 P.2d 934 (1943).
18. Fox Pet. Co. v. Booker, 123 Okla. 276, 253 P. 33 (1976).
19. *Id.* at 282, 253 P.2d at 38.
20. Doss Oil Royalty Co. v. Texas Co., 192 Okla. 359, 137 P.2d 934, 938 (1943).

fitable to the lessee. Other factors involved are the length of time that has passed since the completion of the last well, the size of the tract involved, and the number and locations of wells that have already been completed. The lessee could still prevail, however, if he shows definite proof that the drilling would be unprofitable. This, in effect, shifts the burden of proof of profitability from the lessor to the lessee when the lessor initially shows an unreasonable length of time since the last drilling.

With this in mind, it appears it would be beneficial to have the courts adopt a new standard of application along with the covenant of further exploration as a separate and distinct covenant from that of further development. An attempt to keep all factual situations under the prudent operator rule would be to take a well-settled rule of law and stretch it beyond recognition, or to allow the exceptions to swallow the rule entirely. As a result, there will be a greater number of litigated cases than in the past because no one can be sure how a particular court will construe the prudent operator rule under a given set of facts.

Oklahoma Authority for the Covenant of Further Exploration

In the recent case of *Mitchell v. Amerada Hess Corp.*,[21] the Oklahoma Supreme Court expressly held: "[T]here is no implied covenant to further explore after paying production is obtained, as distinguished from the implied covenant to further develop."[22]

This note questions the conclusion reached by the supreme court in light of the past Oklahoma decisions in this area of law. An analysis of the cases that seem to indicate there is, or should be, a separate covenant will be compared with the analysis of *Mitchell.*

Although the cases to be discussed do not use the express terms of "covenant of further exploration," there is no doubt that the court has recognized that there is a difference between the two covenants. This is shown by the fact that the court does not require the lessor to prove probable profitability in all the cases, which is usually the essential element under the prudent operator rule.

The first case to discuss this covenant is *Fox Petroleum Co. v. Booker.*[23] In *Fox* the court came very close to expressly recognizing the covenant of further exploration.[24] The lessee held a lease consisting of 60 acres. When

21. 638 P.2d 441 (Okla. 1981).
22. *Id.* at 449.
23. 123 Okla. 276, 253 P. 33 (1926).
24. *Id.* at 281, 253 P.2d at 37:

> And if the obligation of the lessees be viewed as one for exploration rather than development (and so, perhaps, not affected by the possibility of financial return), the evidence still fails to establish want of reasonable diligence in exploration. When this suit was filed some six months had elapsed since the completion of the last well. Under the facts and circumstances presented by this record, considering the fact that the wells already drilled on the 60 acres were to a certain extent an exploration of the entire tract, it does not appear that the delay was unreasonable.

the suit was filed, six months had elapsed since the completion of the last well. The court was concerned with the strong policy against allowing the lessee to hold a productive lease for speculation purposes, but held that the lease would stay in effect because there was not an unreasonable delay in drilling, and the lessor did not make any demands upon the lessee for an additional well.[25]

Although *Fox* relied on an abandonment theory, this theory was stricken in *Doss Oil Royalty Co. v. Texas Co.*[26] In *Doss* the court rejected the abandonment theory and turned to the theory of breach of covenant, without the requirement that the lessor show probable profitability. The suit for cancellation was brought for the undeveloped portions of two leases. No wells had been drilled for fourteen years, and the lessor's demand to the lessee to drill was refused. The lessor then sued under the theory of abandonment. The court rejected this theory, stating that it was a legal fiction used to arrive at an equitable result and that the true basis of the decision was cancellation for breach of covenant.[27] The ultimate question the court raised was whether the courts should grant relief without requiring the lessor to prove that the additional wells could be drilled with a reasonable expectation of profit and, if so, upon what theory.[28]

In answering this question, the court pointed out:

> The important fact, regardless of theory, is that the defendant had, at the commencement of this action, held substantial undeveloped portions of these leases for over fourteen years without drilling a single well thereon. Defendant contends that it is entitled to hold the whole of both leases because it has production on other parts of the leases and that further development is not required under the implied covenants because circumstances have not indicated that development would be profitable. If defendant's theory is correct, it may hold the land without further development as long as production from the present wells continues in paying quantities, regardless of how long that may be. The courts and text writers condemn such attempts of lessees to so indefinitely freeze the undeveloped portions of oil and gas leases, hold them for speculative purposes and thus prevent the owners from getting full development of their land.[29]

The court, holding that the lessor may have cancellation of the unused portions of the lease without proof that the additional drilling would be profitable to the lessee, explained how the prudent operator rule operates in these circumstances.

25. Six months had elapsed since the last drilling.
26. 192 Okla. 359, 137 P.2d 934 (1943).
27. *Id.* at 363, 137 P.2d at 938.
28. *Id.* at 361, 137 P.2d at 936.
29. *Id.*

> The prudent operator rule may be considered as a measuring stick to guide the court in determining the diligence required of the lessee in order to ascertain whether a breach of the implied covenant has occurred. Like other rules of equity, the prudent operator rule is not inflexible. The statement that the implied covenant for further operations is limited to cases where there is a likelihood of profit to the lessee must be taken in a restricted sense and is not of universal application. It will depend upon the facts and circumstances of the particular case. The broad rule as to burden of proof . . . is not to be applied after the lapse of an unreasonable length of time.[30]

Although the court spoke in terms of the implied covenant to further develop, it apparently recognized that the covenant it applied is substantially different from the covenant of further development, the difference being the standard that is applied with regard to the profitability requirement.

In a decision following *Doss*, the court faced the question of whether a lease should be canceled as to deeper formations the lessees had failed to explore. The lease in *McKenna v. Nichlos*[31] was executed in 1917 with a primary term of five years. The lease covered two tracts of land and two wells were drilled on the south 40 acres to the Fortuna sand (2,400'). No other wells were drilled. Twenty-three years after the execution of the lease, the lessor brought suit to cancel the lease. The lessee testified that the Fortuna sand under the lease was exhausted and offered to assign the lease to the plaintiff insofar as the Fortuna sand was concerned. The evidence showed the field was not a proved field, and a well drilled to deeper sands would be purely exploratory. The lessee testified that he intended to drill to deeper sands "whenever conditions justified it," but that conditions would not justify such a well until there was a better market for gas and oil and more certainty of production from deeper sands.[32]

There was no evidence indicating that a prudent operator would undertake the drilling of such a well with a reasonable expectation of profit. The trial court canceled the lease to the Fortuna sand and all sands above it but left the lease in effect as to deeper sands. On appeal, the Oklahoma Supreme Court remanded the case with instructions to grant the defendant sixty days within which to commence a well to the deeper formations and, if the drilling was not commenced within that time, the lease would be canceled as to all formations. The court stated:

> [T]he duty to drill further wells, after the lapse of an unreasonable length of time, is not tested by the standard of the prudent operator alone. . . . [W]e would also give weight to other considerations, particularly the length of time which the lessee had held the lease without further development. In other words after the passage of

30. *Id.* at 363, 137 P.2d at 938.
31. 193 Okla. 526, 145 P.2d 957 (1944).
32. *Id.* at 527, 145 P.2d at 957.

> a reasonable length of time the duty to drill additional wells becomes progressively greater, and the standard of the prudent operator becomes progressively of less importance in determining whether such a duty exists.[33]

McKenna makes it clear that the court was again recognizing a covenant substantively different from the covenant of further development. If it were not, why did the court explicitly state that there was no reasonable expectation of profit with regard to the deeper formations and then proceed conditionally to cancel the lease? This flexible prudent operator rule was imposed not only to encourage the development of natural resources and to comply with the intentions of the contracting parties, i.e., all of the lease premises would be fully developed, but also to prevent speculation by the lessee.

Ten years after this decision, a decision was rendered showing another example of the Oklahoma rule. *Sand Springs Home v. Clemens*[34] involved a lease executed in 1938 on a 120-acre tract of land. A well was drilled on the southwest 40 acres in 1938, and in 1939 a dry hole was drilled in the southeast 40 acres. Twelve years after the execution of the lease, the lessor sued for cancellation of the lease for failure to develop and operate the lease diligently. The lessee testified that because of the number of dry holes drilled in the area no further development would be justified. Judgment was rendered for the lessor, relying on *Doss*:

> To permit the lessee to hold the lease for an unreasonable length of time for merely speculative purposes is to allow him to protect his own interest and to disregard the interest of the lessor. If conditions do not indicate to him that further development will be profitable, it is but fair that, after a reasonable time has expired, he surrender the undeveloped portions of the lease and allow the lessor to procure development by others or assume the burden of showing why in equity and good conscience the undeveloped portion should not be cancelled so that the owner may, if possible, get it developed by others.[35]

The court, in its summation stated:

> That reasoning is particularly applicable to the situation in the case

33. *Id.* at 528-29, 145 P.2d at 960.

34. 276 P.2d 262 (Okla. 1954). *See also* Neff v. Jones, 288 P.2d 712 (Okla. 1955), where, in the syllabus, the court states:

> 2. In a lessor's action to cancel the undeveloped portions of an oil and gas lease on account of a breach of one or more of its covenants, the burden generally rests upon him to plead and prove sufficient facts to induce a reasonable conclusion that such breach has occurred, but where, from the alleged facts, it may be thus concluded that the lessee's alleged breach of the implied covenant for further development has continued for an unreasonable or unconscionable period, it is not necessary for the lessor to plead and prove that a reasonably prudent operator would, under the circumstances, undertake such development.

35. Doss Oil Royalty Co. v. Texas Co., 192 Okla. 359, 137 P.2d 934 (1943).

> at bar. One small producing well was drilled on the entire 120 acre tract over a period of some twelve years. The testimony in the record can lead to but one conclusion, namely, that the defendant because of one dry hole drilled by it and another drilled some twenty years previously indicate that further development would prove unprofitable. If such be the case, no injury could result to defendant by a cancellation of the lease as to the undeveloped portion of the lands embraced therein. Equity and justice to the plaintiff require that it be done.[36]

There was no mention of a requirement that the lessor show the probable profitability of any additional wells.

Mitchell v. Amerada Hess Corp.

At this point, it is appropriate to consider the recent Oklahoma decision of *Mitchell v. Amerada Hess Corp.*[37] *Mitchell* expressly held that a covenant to further explore does not exist separately from the covenant to further develop.[38]

Mitchell involved a suit for cancellation and release of the 23-year-old oil and gas leases held by the defendant lessees. The lessors alleged that exploration in the general area had established the presence of numerous potentially productive formations that the defendants had failed to explore and that the defendants were holding the lease through marginal production from one formation for speculation purposes only. The trial court granted conditional cancellations of the lease on the theory of breach of the implied covenant for further exploration. The supreme court reversed the judgment, stating that no such covenant exists in Oklahoma. The court rationalized this by stating:

> The machinery to adjudicate an "exploration" controversy exists presently in the form of the covenant to diligently develop. . . . It is simply not realistic to ignore profit as a consideration of the standard of a prudent operator simply because the lessor demands a wildcat be drilled on a productive lease rather than an additional well to a productive formation.[39]

In view of the previous Oklahoma case law,[40] which holds that relief is not dependent upon proof by the lessor that an additional well would be profitable, the supreme court's statement is obviously inconsistent.

In reaching this decision, the court attempted to distinguish the prior Oklahoma cases granting cancellation without a showing of probable profitability and relied on the 1959 Texas case of *Clifton v. Koontz.*[41] *Clifton* disap-

36. Sand Springs Home v. Clemens, 276 P.2d 262, 263 (Okla. 1954).
37. 638 P.2d 441 (Okla. 1981).
38. *Id.* at 449.
39. *Id.* at 447.
40. *See generally* cases cited at note 7 *supra.*
41. 325 S.W.2d 684 (Tex. 1959).

proved of the existence of a covenant to further explore as being untenable and "diametrically opposed to our established prudent operator rule where expectation of profit is an essential element."[42] While *Mitchell* relies on *Clifton* for its authority, the court fails to recognize the prior Oklahoma cases that recognize the covenant for further exploration. It should be noted that *Clifton* did not involve the same facts as in other exploration-type cases. *Clifton* involved a lease executed in 1940 covering two tracts of land encompassing 350 acres. During the primary term, a well was drilled that produced both gas and oil, but very little oil. It was classified as an associated (with oil) gas well. The next operation on the land was seven years later when the lessee successfully reworked the same well, this date of reworking being subsequent to the filing of the case. The Texas Supreme Court recognized these different facts and stated:

> However it should be noted that we do not have a factual situation where the lease covers several thousand acres and an effort is being made to hold such vast acreage by showing production from a comparatively small area. Neither are we confronted with a situation where an unreasonably long length of time has elapsed since the last development of the leased premises. Therefore, we do not pass upon these questions.[43]

From this modifying language, it is uncertain what the Texas view will be in a factual situation involving a true exploration case where the lessor has requested further exploration of the same formation, is unable to show profitability, and the lessee has not engaged in development for an unreasonable length of time or expressly refuses to explore further.

Mitchell also relies on *Sauder v. Mid-Continent Petroleum Corp.*,[44] the same case Professor Meyers cites as the leading case recognizing his proposed covenant of further exploration. *Sauder* involved a lease on two tracts of lands, one consisting of 320 acres and another of 40 acres. An oil and gas lease was executed in 1916, and two wells were drilled on the 40-acre tract from 1920 to 1921. The lessor requested further exploration on the 320-acre tract, and when it was refused, brought suit in 1930 for cancellation of the lease. The lessee's defense was that the sands pinched out, making production highly unlikely. The lessor did not show that the lessee could drill at a profit, but the court ruled that the lease to the 320-acre tract would be canceled unless development was begun within a reasonable time.

Although other cases have followed the *Sauder* rule,[45] *Mitchell* distinguished

42. *Id.* at 697.
43. *Id.* at 696.
44. 292 U.S. 272 (1934).
45. Magnolia Pet. Co. v. Wilson, 215 F.2d 317 (10th Cir. 1954); Trust Co. of Chicago v. Samedan Oil Corp., 192 F.2d 282 (10th Cir. 1951); Sand Springs Home v. Clemens, 276 P.2d 262 (Okla. 1954); McKenna v. Nichlos, 193 Okla. 526, 145 P.2d 957 (1944); Doss Oil Royalty Co. v. Texas Co., 192 Okla. 359, 137 P.2d 934 (1943).

the holding in *Sauder* by attaching unwarranted meaning to the words in the lease, emphasizing form over substance. One passage on which the court relied states: "[T]he respondent . . . had not . . . explored and developed the lands as required by the *express* and implied covenants of the lease."[46] The court went on to state that: "The question for discussion is whether the respondent failed to comply with an implied covenant to develop the tract with reasonable diligence."[47] As noted in the above-cited cases, the fact that the court uses the term "implied covenant of development" does not conclusively determine that the court does not recognize something substantively different. The ultimate issue involves what standard is to be applied to determine if the lessee is in breach.

Obviously *Mitchell* is not in accord with previous Oklahoma decisions. The court disregards prior contrary cases with minimal analysis of the holdings.[48] The cases that *Mitchell* does not discuss[49] are of extreme importance and bear directly on the statement by the court requiring proof of probable profitability of the additional wells.

> Failure to recognize the profit motive as an instrumental force in oil and gas leases on behalf of both lessor and lessee is to ignore the very essence of the contract. It is unquestionable that both the lessee and lessor intended to benefit monetarily from the produce of the land through sale of its hydrocarbons.[50]

These "ignored" cases state that a showing of profitability is *not* required in order for the lessor to receive relief. The court tries to avoid these cases without explaining the rationale behind the avoidance. For example, in discussing *Doss*,[51] the court held the fact that the wells in the area were drilled every two and one-half acres (the standard practice at that time) bears directly on profitability and, therefore, "it cannot truly be said *Doss* stands as an exploration case or an action cancelling a lease without consideration of evidence relating to the profitability of further drilling."[52] As noted in the discussion of *Doss* above, *Doss* specifically held that proof of profitability is *not* a prerequisite to cancellation of an oil and gas lease where there has been an unreasonable delay in drilling additional wells. It can hardly be said that *Doss* considered profitability proof by the lessor just because the lessor showed that the practice at the time was to drill a well every two and one-half acres.

46. Mitchell v. Amerada Hess Corp., 638 P.2d 441, 448 (Okla. 1981) (emphasis by the court).

47. *Id.* at 448.

48. *Id.*, where the court states: "While these cases can be viewed as the proffered authority, we decline to state that the issue of probable profitability is not a relevant consideration in an action to cancel a lease for failure to further develop thus creating an action to cancel for failure to further explore."

49. *See* Neff v. Jones, 288 P.2d 712 (Okla. 1955); Sand Springs Home v. Clemens, 276 P.2d 262 (Okla. 1954).

50. Mitchell v. Amerada Hess Corp., 638 P.2d 441, 447 (Okla. 1981).

51. Doss Oil Royalty Co. v. Texas Co., 192 Okla. 359, 137 P.2d 934 (1943).

52. Mitchell v. Amerada Hess Corp., 638 P.2d 441, 449 (Okla. 1981).