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Is There an Implied Obligation to Develop for Oil and Gas When There is an Agreement to Pay Delay Rental?

If A leases his farm to B for five years and B agrees to give A one-half of the produce raised upon such farm, there would undoubtedly be an implied obligation on the part of B to farm the land with reasonable diligence even though the lease did not expressly so provide, for otherwise there might be no produce of the farm and A might get nothing. If B should not observe this duty A could hold him liable for a breach of this implied agreement. If A's remedy at law were inadequate a court of equity might even hold that there was an implied condition that B should farm the land with reasonable diligence and that if he did not do so, A might forfeit the lease for breach of this implied condition and have it canceled as a cloud on his title.

Likewise if A should lease his land to B for the purpose of exploring for and producing oil and gas, and B covenanted to give to A one-eighth of all the oil or gas produced and saved, there would be an implied obligation that B should explore for and produce oil and gas with reasonable diligence in order that the purpose of the lease might be carried out, for certainly the parties must have intended that B should proceed to search for oil and gas and produce them if found in paying quantities. If B does not
EDITORIAL NOTES

perform with reasonable diligence his duty to search for oil and gas and to produce them if found, then, since A's remedy at law in such case may well be inadequate, a court of equity will hold that there is a condition that B search for oil and gas and if he finds them that he operate with reasonable diligence and on breach of this condition A may forfeit the lease and a court of equity may go so far as to enter a decree in aid of such forfeiture.¹

But suppose in the agricultural lease above suggested the parties expressly provided that B was to give to A one-half of the produce of the farm or in lieu thereof B was to have the right to pay to A five dollars per acre annually, and suppose B then did not farm the land but did pay to A five dollars per acre annually, would there be an implied duty on B's part to farm the land and an implied condition that he must farm it, assuming that the farm would suffer no damage from lying idle? Certainly there could be no such implications in face of the express option which B has under the lease to pay A five dollars per acre instead of half the produce.

Now suppose we add to the oil and gas lease a provision that B is to complete a well within one year or in lieu thereof to pay to A the sum of one dollar per acre annually until such well is completed. If we say B is still under a duty to explore for oil and gas and produce them if found in paying quantities and that, in addition, if he fails in performance of such duty, A may forfeit the lease, we will certainly destroy the express option given to B under the lease to pay one dollar per year in lieu of drilling a well. Of course there must be a good consideration to support the lease including all its covenants. Granting there is such good consideration, why should not a provision like the above be valid and binding on both parties and why should it be destroyed by implication? It is believed no satisfactory reason can be given, yet some courts, while they seem to hold the lease valid, still have asserted that there is an implied condition and that after due notice, if B does not drill with reasonable diligence, A may forfeit the lease and may have it removed as a cloud on his title. In other words, a contract is made for the parties, apparently according to the ideas of these courts as to what the parties ought to have put into the contract. Under this doctrine A cannot act during any time

¹See Gadbury v. Indiana Consolidated Gas Co., 162 Ind. 9, 67 N. E. 259 (1903); Brewster v. Lanyon Zinc Co., 140 Fed. 801 (1905); Lovett v. Eastern Oil Co., 68 W. Va. 667, 70 S. E. 707 (1911).
for which he has accepted delay rental but he may refuse delay rental and give B notice to drill a well, and if B does not do so within a reasonable time, A may declare the lease forfeited and have it canceled by a court of equity. Hence while B is bound to pay delay rental if he does not drill a well, A is not bound to accept delay rental even though he expressly covenants he will accept it. This implication is made at least partly on the authority of cases involving leases by the terms of which the lessee had no option to pay delay rental and such cases are clearly distinguishable.

The above doctrine was announced in West Virginia in Wilson v. Reserve Gas Company. In this case there had been an oil and gas lease on the land in question for a term of five years and before it expired the parties made a new agreement, which they termed "an agreement in lieu of drilling" under which delay rentals were paid and accepted for about eleven years. By this agreement the lessee covenanted to pay and the lessor covenanted to accept seventy-five dollars for each subsequent quarterly period in lieu of the completion of a well until such time as the gas company "shall surrender or abandon said lease." The agreement concluded with the following clause: "that this agreement shall not be construed to require said gas company to drill any well or wells on said land, but that it permits said gas company during the term for which said payments are made to drill or not to drill as it may elect." Notwithstanding this plain and unequivocal language the court said:

"The lessee can not hold the leased land indefinitely without exploring the land and producing oil or gas. There is nothing in the contract to deny the lessors the right to terminate the lease upon reasonable notice. They have not shorn themselves of that power."

The court expressly held the lease valid and free from fraud, and further held that the fact that the lessee had a right to surrender it at any time did not make the tenancy a tenancy at will. There was no provision in the agreement expressly giving the lessor a right to terminate the lease and there clearly was the express language quoted above giving the lessee a right to pay delay rentals and thus continue the lease in force so long as desired.

78 W. Va. 329, 88 S. E. 1075 (1916).
EDITORIAL NOTES

Just how the lessors could have "shorn themselves" of power to terminate the lease if not by the language used is difficult to see.

The court cites as authority Monarch Oil, Gas & Coal Co. v. Richardson, 3 a Kentucky case, Venedocia Oil & Gas Co. v. Robinson, 4 an Ohio case, and Consumers Gas Trust Co. v. Litler, 5 an Indiana case. The Indiana case is not in point for the lease involved in that case provided that the lessee was to pay forty dollars a month rent and there was a subsequent provision that if the lessee completed a well there should be no further obligation to pay this rent. Hence there was no option in the lessee to pay rental for delay in drilling, and a duty to explore for oil and gas might be implied as easily as if there had been no rental provision whatever. At least such implication would not run counter to any express provision of the instrument. There is perhaps a weak dictum in the Ohio case but certainly no more, and that dictum is apparently partially based on the authority of the Indiana case above, which, as pointed out, is not in point. The Kentucky case is in point but it cites no authorities which support the language of the court. The lease involved in that case simply provided that the lessee was to begin a well within one year or pay thereafter an annual rental of sixteen dollars. It had no provision that the agreement should not be construed to require the lessee to drill. A more recent Kentucky case 6 has announced the same doctrine as the law in that state in a case involving a lease very similar to that under consideration in the prior case. In West Virginia in a subsequent case the same doctrine has been announced—Johnson v. Armstrong—that the lease provided that: "In case no well is completed within three months, then this grant shall be null and void, unless the second party pay to the first party thirty-four dollars in advance for each three months thereafter such completion is delayed." In none of the cases mentioned above has a forfeiture actually been sustained, so none of them contains more than strong dicta.

Upon what reasons is such a doctrine based? It is believed the reasons usually given are stated in the following quotation from Monarch Oil, Gas & Coal Co. v. Richardson:

3124 Ky. 602, 99 S. E. 668 (1907).
471 O. St. 302, 73 N. E. 222 (1905).
5162 Ind. 320, 70 N. E. 383 (1904).
6Ocala Oil Co. v. Hughes, 218 S. W. 799 (1920).
781 W. Va. 399, 94 S. E. 722 (1917).
“Oil and gas leases yield nothing to the owner when not worked, and are an incumbrance on his land, preventing him from selling or leasing it to others, although it costs the lessee nothing except the mere pittance paid as rent. The development of mineral, oil, and gas lands is too expensive for the landowner himself to undertake, and requires skill and capital ordinarily beyond the reach of the owner of the soil. So that, in order that these resources may be developed and profit realized therefrom, it is necessary that the privileges be granted to persons who are engaged in the business of exploring and developing oil, gas, and mineral fields. The fluctuating and uncertain value of this class of property renders it necessary for the protection of the lessor that the properties leased should be developed as speedily as possible, and that the lessee will not be permitted to hold the land for speculative or other purposes an unreasonable length of time for a mere nominal rent, when a royalty on the product is the chief object for the execution of the lease.”

It is submitted that in the above excerpt the court has made assumptions which are not necessarily true and has construed the lease in a way not contemplated by the parties when it was made, though perhaps according to the contention of the lessor after the value of the lease had become apparent. Is it true that the parties to an oil and gas lease always contemplate development by the lessee as soon as possible? It is submitted that it is not true where the language of the lease gives the lessee the privilege of paying delay rental instead of drilling a well. Very many lessors are today collecting delay rentals and hoping their respective lessees will not surrender because the lessors do not believe oil or gas in paying quantities can be found in the land. Furthermore, if the parties do contemplate early development, as the courts say they do, then why do they continue to put in their leases provisions such as that in Wilson v. Reserve Gas Company which expressly provide that the lessee shall have the privilege of paying delay rental and that he shall not be compelled to drill a well? The whole purpose of any delay rental clause is clearly to permit the lessee to delay drilling. Why should not the lessee contract to accept a sum as payment for delay in development? He still has the oil and gas in his land if there is any. It does not escape from the land so long as there is no drainage and so why not treat this provision like a similar one would be treated if found in a coal
or other mineral lease? The lease if fraudulent could be set aside but there is no fraud in the above cases.

Is it true that the delay rental provided in most oil and gas leases is merely a nominal consideration, not to be permitted to interfere with the court's idea as to the main purpose of the lease? It is submitted that the delay rental is frequently very substantial. Frequently a delay rental is paid on land which is valueless and perhaps most oil and gas leases result in loss to the lessee. In some cases the delay rental may be inadequate but inadequacy of consideration is ordinarily a matter for the parties and not for the courts in the absence of fraud. The doctrine does not attempt to distinguish the adequate from the inadequate but condemns all alike. In the lease involved in Wilson v. Reserve Gas Company the delay rental was certainly substantial and adequate. The lessee had paid $300 per year for some eleven years on a tract of one hundred and forty-two acres. The royalty provided in the lease for a gas well was seventy-five dollars per year. Hence, for eleven years the lessee had been paying to the lessor the equivalent of the royalties on four paying gas wells and all of the gas was still in the land. Since the lease was in gas territory it is doubtful whether the lessor would ever get more from gas wells than from daily rental.

A week after Wilson v. Reserve Gas Company was decided the West Virginia Supreme Court of Appeals handed down a decision in a case in which the lessor sought to recover damages at law from the lessee for breach of the alleged duty of the lessee to develop the premises for oil and gas, which decision is inconsistent with the doctrine suggested. In this case the Court said:

"In so far as right of recovery is asserted in the declaration and evidence, on the ground of duty to drill, merely because the premises are shown to be gas producing territory, the case is obviously bad. By their written lease, the plaintiffs expressly assented to delay in drilling and agreed to accept, in satisfaction thereof, specified pecuniary compensation which has been paid. In other words, they took a conditional covenant from the lessee to complete a well within a specified period or pay, periodically, in lieu thereof, stipulated sums of money, and provided a like option for the lessee as to subsequent periods of like length. The lessee having elected to pay the

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money instead of drilling, as it was expressly authorized to do, the lessors have accepted it. To permit them now to recover damages for an omission to which they have assented and for which they have been compensated according to a standard or measure fixed by their own solemn contract would violate a fundamental principle of the law of contracts. . .

"No implied covenant on the part of an oil or gas lease for diligent operation, or operation at all, under such conditions, has ever been suggested or declared by this or any other court. There are some decisions properly holding that, in the absence of a provision for delay compensable in money, and any other consideration, there is an implied covenant to search for the mineral, because there is no substantial consideration for such lease, unless it impliedly contains a covenant for exploration."

It is submitted that the rule laid down in Carper v. United Fuel Gas Company to the effect that where the parties have expressly provided that the lessee shall have the right to pay delay rental instead of drilling there can be no implied duty on his part to develop for oil and gas so long as he pays delay rental is sound but that this rule as to the effect of a delay rental provision in an oil and gas lease is irreconcilable with that expressed in Wilson v. Reserve Gas Company and Johnson v. Armstrong. In the Carper Case the court held that while there could be no implication either of a covenant or a condition on the part of the lessee to develop for oil and gas so long as there was no drainage of oil and gas from the leased premises, yet since the parties certainly did not contemplate that the lessee should have the right to hold the lease while the minerals were drained from beneath the land that it was proper to imply a condition that the lessee was to drill such wells as were necessary to prevent loss of the mineral by drainage.

It is said that the lessee will not be permitted to hold a lease for speculative purposes. Why not, if the lessor contracts to take money in return for such privilege? If the Carper Case is correct the lessee must protect the land from drainage and if that is done then the lessor will not lose the oil and gas in his land. All other forms of property are held for speculative purposes, so why

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6The settled rule of construction to the effect that where the parties have an express provision in their contract on a certain subject there can be no implication inconsistent therewith has often been applied to oil and gas leases. Among the cases on this point are Kachelmancher v. Laird, 92 O. St. 324, 110 N. E. 933 (1915); Greek v. Wyle, 109 Atl. 529 (Pa. 1920).
except oil and gas leases? It is submitted there is no sound reason why a delay rental provision should not be fully enforced against the lessee so long as there is no drainage.

In conclusion, it is submitted that the doctrine that the lessor may compel the lessee to develop notwithstanding the fact he has by contract given the lessee an option to pay money in lieu of development is unsound, and that such a provision should be held valid and binding on the lessor and that there should be no implications contrary to the delay rental clause at least so long as there is no drainage of the oil and gas from the land. It is further submitted that if these delay rental clauses are considered detrimental to the public, courts ought to declare them void. As the matter now stands in West Virginia it is difficult to tell whether a delay rental provision is valid or void. The cases of Wilson v. Reserve Gas Company and Johnson v. Armstrong merely asserted the doctrine under discussion and did not enforce it by a decree in aid of a forfeiture after due notice to the lessee to develop, and therefore contain little more than dicta. On the other hand the Carper Case is, in so far as it goes, an actual decision that so long as there is no drainage there can be no implied duty on the lessee inconsistent with the delay rental provision of the lease. This seems not only sound on principle but also states a definite rule which parties can understand and use as a guide in future dealings.

—J. W. S.

Unwholesome Competition.—It has been said that so long as there are shyster clients there will be shyster lawyers. Such an utterance, of course, carries with it the implication that people get what they want, and, therefore, what they deserve—a process of let dog eat dog not so deplorable if the public in general could be protected by some method of segregation. However this may be, it frequently has occurred to the writer that a lack of legitimate clients offers a very fertile field in which to evolve both shyster lawyers and shyster clients. Every farmer knows that if the crop is too thin the weeds will smother it; and this result is entirely consistent with the fact that a few giant oaks may spread their circumferences so high above the smaller vegetation that they may ignore their environment. The central thought has