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Recent Developments

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RECENT DEVELOPMENTS

Oil and Gas — Confusion Arising in Texas From the "Producing Gas Only" Shut-in Clause

Suit was brought by lessors¹ to declare an oil and gas lease terminated and to remove the lease as a cloud on their title. The lease was an ordinary oil and gas lease for a primary term of ten years with the typical "thereafter" or habendum clause provision. The habendum clause was subject to a "producing gas only" shut-in royalty clause.² Drilling operations were commenced before the end of the primary term and resulted in the completion of a well capable of "producing gas only."³ The completed well was tested and calculated to be capable of producing in paying quantities and then was shut-in because there was no accessible market for the gas. The shut-in gas royalty payments were paid timely for a period of almost three years; then the well was connected to a pipeline, and gas was produced and marketed. This was the only well drilled on the two sections (1287 acres) held under the lease in question. The lessors alleged that the well reasonably could have been completed as one capable of producing liquids in paying quantities; that it was thus removed from the classification of one "producing gas only"; and that the shut-in clause, therefore, was inapplicable, and the lease should be terminated for lack of production. The trial court instructed the jury that it was to "deal" with the well in question as it was actually completed and not as it could have been or might have been completed.⁴ (Emphasis added) Held, reversed and remanded:⁵ A well completed to produce only gas is not one "producing gas only" within the terms of the shut-in clause if there is a finding that the well could have been completed as a liquid or liquid-gas well and that a diligent, prudent operator acting in good faith would have undertaken to complete it as such. Duke v. Sun Oil Co., 320 F.2d 853 (5th Cir. 1963).

¹ Suit originally was brought in the state courts of Texas in the form of a statutory trespass to try title action. The lessee removed the action on the basis of diversity of citizenship to the United States district court. Duke v. Sun Oil Co., 320 F.2d 853, 857 (5th Cir. 1963).
² The shut-in clause provided: "[W]here gas from a well producing gas only is not sold or used, Lessee may pay as royalty Fifty Dollars ($50.00) per well per year, and upon such payment it will be considered that gas is being produced within the meaning of [the habendum clause]." Id. at 858 n.3. (Emphasis added.)
³ See note 42 infra.
⁴ Duke v. Sun Oil Co., 320 F.2d 853, 863 (5th Cir. 1963).
⁵ "The Judge [in the trial court] erred in giving the instruction which limited the jury's consideration to the well as actually completed. This necessitates a new trial." However, the summary judgment as to the timely payment of the shut-in royalty was proper, and it will not be a question on remand. 320 F.2d at 865.
The habendum clause is one of the major provisions of an oil and gas lease. Its function is to limit the duration of the interest granted. In legal theory the interest will endure forever if the requirements set forth in the habendum clause are fulfilled. The Texas courts have construed the requirements of the habendum clause to be a special limitation; therefore the requirements do not impose duties on the lessee. However, nonperformance or complete cessation of performance will cause the lease to terminate ipso facto. The first definite statement of the limitation imposed by the habendum clause and the satisfaction thereof was made in Waggoner Estate v. Sigler Oil Co.:

The estate acquired is lost on cessation of the use of the land for purposes of oil and gas exploration, development, and production. Regardless of the lessee's intention, his estate terminates, under its limitation, when there is a complete cessation of actual use of the land for the purpose of the lease. But it is not a partial use, nor a negligent use, nor an imperfect use, but cessation of use, which terminates the lessee's estate.

The continuation of production in paying quantities satisfies the...

*Ordinarily, the habendum clause consists of two parts—one creating the primary term which is for a definite period and one creating the secondary term, also called the thereafter clause, which is of indefinite duration. "It is agreed that this lease shall remain in force for a term being hereinafter called 'Primary Term,' and as long thereafter as oil and gas or either of them is produced from said land by the lessee." Sullivan, Oil & Gas Law 91 (1955). Such provisions fix the ultimate duration of the lessee's interest. See Comment, 11 Sw. L.J. 340 (1917).

7 Gulf Oil Corp. v. Reid, 161 Tex. 51, 337 S.W.2d 267, 269 (1960); Freeman v. Magnolia Petroleum Co., 141 Tex. 274, 171 S.W.2d 339, 342 (1943); Watson v. Rochmill, 137 Tex. 565, 155 S.W.2d 781, 784 (1941); Mon-Tex Corp. v. Poteet, 118 Tex. 546, 19 S.W.2d 32 (1929); Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 19 S.W.2d 27 (1929); Texas Co. v. Davis, 113 Tex. 321, 214 S.W. 304, 306 (1923); Grubb v. McAfee, 109 Tex. 527, 212 S.W. 464, 465 (1919).

8 Waggoner Estate v. Sigler Oil Co., supra note 7, at 28; Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 214 S.W. 290, 291 (1923); see Texas Co. v. Davis, supra note 7; see also Brown, Oil & Gas Leases § 3.02 (1958); Sullivan, op. cit. supra note 6, at 95; Walker, The Nature of the Property Interests Created by an Oil and Gas Lease in Texas, 8 Texas L. Rev. 483, 493 (1930).

9 "A limitation cannot in its very nature impose a duty because the happening of the event named in the limitation clause automatically terminates the estate, and the law will not countenance the absurdity of holding that a man may be discharged of a duty by his very act of breaching it." Walker, supra note 8, at 488; see Masterton, The Shut-in Royalty Clause In An Oil And Gas Lease, 12 Sw. L.J. 459, 473 (1958).

10 See Vernon v. Union Oil Co., 270 F.2d 441 (5th Cir. 1959); Haby v. Stanolind Oil & Gas Co., 228 F.2d 298 (5th Cir. 1951); Gulf Oil Corp. v. Reid, 161 Tex. 51, 337 S.W.2d 267 (1960); Waggoner Estate v. Sigler Oil Co., 118 Tex. 109, 19 S.W.2d 27 (1929); Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 214 S.W. 290 (1923); Caruthers v. Leonard, 254 S.W. 779 (Tex. Comm. App. 1923). In an unusual Oklahoma case the habendum clause served another purpose. The habendum clause (so long thereafter as in paying quantities to the lessor) gave the lessee the privilege of operating the lease after it ceased to produce in paying quantities. The court held that such a provision creates a duty on the part of the lessee to operate the lease as long as there is a return to the lessor even though the lessee will incur a loss by doing so. Briggs v. Waggoner, 375 P.2d 896 (Okl. 1962).

11 118 Tex. 509, 19 S.W.2d 27, 28 (1929).
special limitation requiring devotion of the premises to the purposes of exploration, development, and production and preserves the lease even though no other operations are conducted. The production of oil, gas, or other minerals in paying quantities from anywhere on the lease, horizontally or vertically, will satisfy this special limitation. Because of this limitation upon the duration of a lessee's estate, his estate has been designated a determinable fee simple.

Most oil and gas leases do not express the character of the development or the proper operating practices required of the lessee after he has satisfied the habendum clause by obtaining production in paying quantities or its equivalent; however, the lessee is under an implied duty to operate properly and to develop the premises with reasonable diligence. Of course, this duty will exist only so long as the lease is preserved by the lessee's satisfying the habendum clause.

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14 See Sinclair Oil & Gas Co. v. Masterson, 271 F.2d 310 (5th Cir. 1959); Clifton v. Koontz, 160 Tex. 82, 321 S.W.2d 684 (1959); Garcia v. King, 139 Tex. 578, 164 S.W.2d 509 (1942); Flato v. Weil, 4 S.W.2d 992, 993 (Tex. Civ. App. 1927); see also Note, 14 Sw. L.J. 283 (1960).

15 A lease is considered indivisible; consequently, production on any part of the lease acreage is deemed to hold the entire lease. Gypsy Oil Co. v. Cover, 78 Okla. 158, 189 Pac. 540 (1920); see Clifton v. Koontz, supra note 14; Garcia v. King, supra note 14; Flato v. Weil, supra note 14; see also 3 Summers, Oil & Gas § 511 (1959).

16 The first definite statement of this effect was made in Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 154 S.W. 290 (1923): It seems obvious: First, that the grants might endure forever, since the lands might never cease the profitable production of oil or gas; and, second, that it was intended by all parties that the lands should be used for no other purpose than the specified mineral exploration and production, and that the grants were to be enjoyed only while such use continued and were to immediately terminate on cessation of the use. At common law, a grant of land for a term and for such use and purpose . . . created the estate called a determinable fee.

Id. at 291, (Emphasis added.)

17 Such a duty arises "from the presumed intention of the parties as gathered from the instrument as a whole." Danciger Oil & Ref. Co. v. Powell, 137 Tex. 484, 174 S.W.2d 652, 655 (1941). "The covenant does not arise as to any oil and gas lease unless and until (1) there has been drilling and development (a completion) on the lease, (2) oil or gas is being produced thereon in paying quantities, and (3) there are no express provisions in the lease defining the extent of drilling required of the lessee." Brown, Covenants Implied in Oil and Gas Leases, in A.B.A. Proceedings, Section of Mineral & Natural Resource Law 162, 170 (1960). One author thinks the duty is one of law because "there is no basis upon which we can infer that lessors and lessees have in mind the implied covenant obligations when they contract." Merrill, Covenants Implied In Oil And Gas Leases 460 (2d ed. 1940); see Sinclair Oil & Gas Co. v. Masterson, 271 F.2d 310 (5th Cir. 1959); Clifton v. Koontz, 160 Tex. 82, 321 S.W.2d 684 (1959); Mon-Tex Corp. v. Poteet, 118 Tex. 146, 19 S.W.2d 32 (1929); Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 19 S.W.2d 27 (1929); Freeport Sulphur Co. v. American Sulphur Royalty Co., 117 Tex. 439, 6 S.W.2d 1039 (1928).
provision. The Texas Supreme Court, in *Waggoner Estate v. Sigler Oil Co.*, held this duty to be an implied covenant and not a special limitation upon the lessee's estate. There is a definite distinction between satisfying the special limitation of the habendum clause and satisfying the duty to operate properly and to develop the lease. In determining whether a lessee has complied with the habendum clause requirements, the only issue would be the question of whether or not, as a matter of fact, the lessee had ceased pursuing the purpose for which the minerals were conveyed to him, *i.e.*, production of oil, gas, or other minerals. To determine whether the lessee has performed the implied covenant, the issue is whether the lessee's acts of operation and development satisfied the standard of the prudent operator rule.

The Texas courts construe the habendum clause literally; the lessee must be producing oil or gas at the end of the primary term or his estate will terminate ipso facto. This is not a forfeiture, but the

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18 Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas*, 11 Texas L. Rev. 399, 411 (1933); see Merrill, *op. cit. supra* note 17, at 128; 2 Summers, *op. cit. supra* note 13, at § 398.


20 *Waggoner Estate v. Sigler Oil Co.*, 118 Tex. 509, 19 S.W.2d 27, 30 (1929). The court went on to state: "The express provision of the [habendum] clause is that the lease shall remain in force, *i.e.*, shall not terminate, as long as either oil or gas is produced from the land by the lessee. . . . [T]he duration of the granted estate *does not* depend on the *degree of diligence* used in the continued exploration, development, and production of oil and gas on the land, after their discovery. . . ." *Ibid.* The court rejected the "judicial interpretation, that the lease shall terminate before the cessation of production of oil or gas from the land by the lessee, if, by reasonable diligence, more oil and gas could have been found, produced, or marketed." *Ibid.* See *Walker, supra* note 8 at 494.

21 The lessee owes no obligation to carry the operations to such a point that they will not be profitable to him. See Rhodes Drilling Co. v. Allred, 123 Tex. 229, 70 S.W.2d 576 (1934); Texas Co. v. Ramsomer, 10 S.W.2d 537 (Tex. Comm. App. 1928); Hutchins v. Humble Oil & Ref. Co., 161 S.W.2d 571 (Tex. Civ. App. 1942) *error ref.* In Oklahoma if there has been a failure to develop over a long length of time, the burden is on the lessee to justify the delay in drilling. Colpitt v. Tull, 204 Okla. 289, 228 P.2d 1000 (1950); Ferguson v. Gulf Oil Corp., 192 Okla. 355, 137 P.2d 940 (1943).

22 Whatever, in the circumstances, would be reasonably expected of operators of ordinary prudence, having regard to the interests of both lessor and lessee, is what is required." Brewster v. Lanyon Zinc Co., 140 Fed. 801, 814 (8th Cir. 1901). In Texas the *Brewster* rule is followed. Texas Pac. Coal & Oil Co. v. Barker, 117 Tex. 418, 6 S.W.2d 1031, 1036 (1928).

23 See note 6 *supra*.

24 *Waggoner Estate v. Sigler Oil Co.*, 118 Tex. 509, 19 S.W.2d 27, 30 (1929). Upon completion of a well, no reasonable time for marketing is implied. There must be production resulting in the marketing of gas by the end of the primary term. Because of the different property interest a lessee gains through an oil and gas lease, some jurisdictions do not recognize the literal application of the habendum clause and allow a reasonable time to obtain production thereof. See State *ex rel. Comm'r's of the Land Office* v. Carter Oil Co., 316 P.2d 1086 (Okla. 1950); Eastern Oil Co. v. Coulehan, 65 W. Va. 531, 64 S.E. 816 (1909). Moreover, the Texas courts hold that production must be in paying quantities even though the term "paying quantities" is not used in the habendum clause. Clifton v.
termination of a determinable fee by its own terms of duration.\textsuperscript{8} The strict requirement that there be a completion with production\textsuperscript{7} in paying quantities within the primary term is a condition precedent to the extension and maintenance of a lease.\textsuperscript{8} Such a construction places a hardship upon the lessee if he has discovered gas in paying quantities, but is unable to market it for lack of a pipeline. This is the principal reason that a shut-in royalty clause is included in the modern lease form. The supposed intent of the parties to the instrument is to provide the lessee a means for extending the lease past the primary term. Thus, if the lessee has discovered gas in paying quantities, but because of a lack of an accessible market production is prohibited, he may extend his lease by complying with the requirements of the shut-in clause. The shut-in clause only qualifies the requirement of production engrossed in the habendum clause; consequently, the lessee is still under a duty to comply with the implied covenants by diligently developing the lease and by seeking to market the gas while extending the lease term by payment of shut-in royalty.\textsuperscript{9}

The shut-in clause was first introduced as a provision to be bargained for by a lessee. Until 1959 its standard form authorized extension of the lease by shut-in payments only if the well in question was capable of “producing gas only.” In \textit{Vernon v. Union Oil Co.}\textsuperscript{5} a federal court held that a gas well capable of producing liquid condensate in paying quantities is not one “producing gas only” within the terms of the shut-in clause. Although this decision brought an abrupt change in the standard form shut-in clause to include condensate, the Texas courts have not ruled on the interpretation of this provision. However, a recent case may show a tendency by the Texas courts to disagree with the \textit{Vernon} case.\textsuperscript{21}

\textsuperscript{8} Skelly Oil Co. v. Harris, 163 Tex. 92, 332 S.W.2d 950, 953 (1960), noted in 17 Sw. L.J. 272 (1963); Gulf Oil Corp. v. Reid, 161 Tex. 51, 337 S.W.2d 267, 269 (1960); Garcia v. King, \textit{supra} note 25, at 512. “Neither unavoidable delays or accidents, acts of God, unfavorable economic conditions, nor financial difficulties of the lessee will afford an excuse for the failure to comply literally with the provisions of this clause in the absence of an express stipulation otherwise contained in the lease.” Walker, \textit{supra} note 8, at 516.

\textsuperscript{9} See note 13 \textit{supra} and accompanying text.

\textsuperscript{20} Freeman v. Magnolia Petroleum Co., 141 Tex. 274, 171 S.W.2d 339, 342 (1943). In Texas the shut-in clause has been construed as a conditional limitation rather than a covenant. The shut-in payments must be made on time, or the lease will terminate. Gulf Oil Corp. v. Reid, 161 Tex. 51, 337 S.W.2d 267, 271 (1960).

\textsuperscript{21} Masterson v. Amarillo Oil Co., 233 S.W. 908 (Tex. Civ. App. 1921) error dism. w.o.j.; Mill & Willingham, Oil & Gas § 130 (1926).

\textsuperscript{22} Vernon v. Union Oil Co., 270 F.2d 441 (5th Cir. 1959); Freeman v. Magnolia Petroleum Co., 161 Tex. 274, 171 S.W.2d 339 (1943); Reid v. Gulf Oil Corp., 323 S.W.2d 107 (Tex. Civ. App. 1959), aff'd, 161 Tex. 51, 337 S.W.2d 267 (1960).

\textsuperscript{23} Vernon v. Union Oil Co., \textit{supra} note 32, at 444; Skelly Oil Co. v. Harris, 161 Tex. 92, 332 S.W.2d 950 (1962); Gulf Oil Corp. v. Reid, 161 Tex. 51, 337 S.W.2d 267 (1960); Freeman v. Magnolia Petroleum Co., \textit{supra} note 30.
A shut-in clause qualifies the habendum clause by providing a substitute for actual production; therefore, it is "an integral part of the habendum clause of the lease ... Neither unavoidable delays or accidents, acts of God, unfavorable economic conditions, nor financial difficulties of the lessee will afford an excuse for the failure to comply literally with the provisions of this clause. ..." The late payment of a shut-in royalty ipso facto terminates the lease since there is no substitute for the actual production required by the habendum clause. The shut-in clause expressly states the conditions for its operation and, as the habendum clause, places no duty on the lessee to perform the conditions; however, nonperformance of the conditions will prevent its operation.

In the principal case the court ruled that the right to pay shut-in royalties was governed by the diligence of the lessee's completion practices. The operation of a "producing gas only" shut-in royalty clause was found to depend on whether a diligent lessee would have completed the well as one capable of producing gas and liquid fluids in paying quantities instead of as a well capable of producing only gas in paying quantities. In so holding, the court has applied a standard of diligence to the lessee's act of completion instead of literally construing the shut-in clause. This presents a questionable departure from the Texas case law and decisions of federal courts applying Texas law.

Since a shut-in clause with a "producing gas only" provision took form at a time when a well was considered either an oil well or a well capable of producing gas only, such provision creates a lease

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32 There is some case development in Louisiana holding that the implied covenant to market cannot be deferred indefinitely by payment of shut-in royalties. See Lelong v. Richardson, 126 So. 2d 819 (La. Ct. App. 1961). But see Masterson, supra note 9, at 470.

33 See note 30 supra.

270 F.2d 441 (5th Cir. 1959).


38 "If the facts warrant a finding that there is a substantial probability that oil can be produced in paying quantities, the lessee will not be allowed to maintain the lease through constructive production by pinching off commercially productive sands to bring in a gas well only." 320 F.2d at 866. Contra, "We are asked to say, by judicial interpretation, that the lease shall terminate before the cessation of production of oil or gas from the land by the lessee, if, by reasonable diligence, more oil or gas could have been found, produced, or marketed. A court should never override by implication the intention of parties expressed in a binding writing." Waggoner Estate v. Sigler Oil Co., 118 Tex. 599, 19 S.W.2d 27, 30 (1929). (Emphasis added.)

39 320 F.2d at 865.

40 "The question is whether under all the pertinent circumstances ... a diligent, prudent operator acting in good faith would have undertaken to complete it as such, rather than as a gas-only well. ..." Ibid.

41 See quotations in note 36 supra.

42 See note 13 supra and accompanying text.

43 "[T]he shut-in royalty clause initially referred to wells capable of producing only gas because this clause grew out of the old gas-royalty clause, which in turn was worded
construction problem if the lessee completes a well capable of producing liquid substances in addition to "gas only." In *Vernon v. Union Oil Co.* the Fifth Circuit, applying Texas law, was presented such a lease construction problem. This court held that the ability of a completed well to produce condensate removed it from the classification of one "producing gas only" if "it would be reasonable to operate the well to produce liquid condensate alone. . . ." This, of course, was not the fact situation before the court in *Duke.* In *Duke* there was finding that the lessee had completed a well capable of "producing gas only" in paying quantities. Such a finding adequately satisfied the requirements of the habendum and shut-in clauses. The court's inquiry as to the reasonableness of the lessee's completion practices resulted from an extended application of the *Vernon* decision. Such extension of the *Vernon* rule is questionable since the *Duke* well was a "gas only" well and, as completed, was not capable of producing liquids or condensate in paying quantities. The court ignored the uncontested fact that the *Duke* well was producing only gas in paying quantities. The court, in its extended application of the *Vernon* rule, overlooked the basic principle that a completed well producing oil or gas from any strata or portion of a strata in paying quantities will satisfy the requirements of the habendum clause although the lessor may have a cause of action based on

at a time when a well was considered either an oil well or a well capable of producing only gas, there being no middle ground. . . ." Masterson, *supra* note 9, at 467. (Emphasis added.)

43 Definition of a "producing gas only" well: Wells capable of producing no substance other than natural gas, which are shut-in for lack of a readily accessible market for gas, and the further absence of any reasonable and legally permissible use for the gas; or wells capable of producing liquids in addition to natural gas, but for lack of a market for gas, and the further absence of any reasonable and legally permissible use for the gas, the operation of extracting the liquids is prohibited because of cost or governmental regulation. *Vernon v. Union Oil Co.*, 270 F.2d 441 (5th Cir. 1959); see Tex. Rev. Civ. Stat. Ann. art. 6008, § 2(f) (1948). For tax purposes condensate is distinguished from gas. Tex. Rev. Civ. Stat. Ann. art. 7047b, § 2 (5) (1948).

44 270 F.2d 441 (5th Cir. 1959).

45 "[W]e have no doubts that the well as actually completed was a well 'producing gas only.' The jury so found in answer to special interrogatories. . . ." 320 F.2d at 862.

46 See note 15 supra and accompanying text.

47 In *Vernon* this same court specifically held that reservoir conditions were important only as they affect the state of the final product. The reservoir conditions were viewed in light of the possible production from the well as completed, not as it should have been completed. 270 F.2d at 446; see also note 34 supra and accompanying text.

48 The *Duke* court limited the application of the extension: "[W]e are not dealing with the right of the lessee ordinarily to choose between several possible strata in which to complete a well." 320 F.2d at 866.

49 See quotation in note 26 supra; see also note 31 supra and accompanying text. The *Duke* decision is also against the strict, literal interpretation the Texas courts give the habendum and shut-in clauses. In Texas the lessee's completion practices must yield production by the end of the primary term; therefore, upon completion of a well, no reasonable time for marketing is implied. The discovery of oil or gas does not give the lessee
the breach of an implied covenant.\textsuperscript{60}

Nonetheless, the federal courts in Texas are bound\textsuperscript{5} by the instant decision until the Texas courts declare to the contrary. Since the relief that can be awarded under the \textit{Duke} holding is lease termination,\textsuperscript{55} similar litigation undoubtedly will be encouraged. “The prize which will encourage such litigation is the prospect of getting back, freed of the lease, highly valuable developed acreage for, absent special facts raising an estoppel (and mere acceptance of shut-in royalty payments plainly is not enough under this opinion), termination of the leasehold as of the moment of completion would be automatic, by its own limitations.”\textsuperscript{56}

Such an apparent confusion of habendum clause principles with reasonable time to make a completion and start production, \textit{i.e.}, when the lessee discovers oil or gas in paying quantities in a shallow sand, but cases off that sand and drills with hopes of finding a deeper formation, the lease will terminate at the end of the primary term unless there is production in paying quantities. The Texas courts refuse to take notice of a mere discovery even if a reasonable, prudent operator would have drilled past the primary term in hopes of finding oil or gas in more profitable quantities in a deeper formation. Gulf Oil Corp. v. Reid, 161 Tex. 51, 337 S.W.2d 267 (1960), \textit{affirming} 323 S.W.2d 107 (Tex. Civ. App. 1959); Clark v. Holchak, 152 Tex. 26, 254 S.W.2d 101 (1953); Archer County v. Webb, 326 S.W. 250 (Tex. Civ. App. 1959), \textit{aff'd}, 161 Tex. 210, 338 S.W.2d 435 (1960); Sellers v. Breidenbach, 300 S.W.2d 178 (Tex. Civ. App. 1957) \textit{error ref.}; Morrison v. Swaim, 220 S.W.2d 493 (Tex. Civ. App. 1949) \textit{error ref. n.r.e.}; see also Vernon v. Union Oil Co., 270 F.2d 441, 445 (5th Cir. 1959); Scott v. Union Producing Co., 173 F. Supp. 161 (S.D. Tex. 1959), \textit{aff'd}, 267 F.2d 469 (5th Cir. 1959).

However, the underlying reasoning of the above cases is inconsistent with the approach taken by the Texas Supreme Court in Clifton v. Koontz, 160 Tex. 82, 325 S.W.2d 684 (1959). Although the above cases refuse to imply a reasonable time after a discovery or after completion of the well, the Texas Supreme Court in \textit{Clifton v. Koontz}, "through application of a reasonable, prudent operator test, avoided the necessity of requiring uninterrupted production in paying quantities as a requisite for continued duration of the lease under the habendum clause." Note, 17 \textit{Sw. L.J.} 272, 277 (1963).

If an oil and gas lease provides for oil or gas royalties and does not “define the lessee's duty as regards development after discovery of paying oil or gas, the law implied the obligation from the lessee to continue the development and production of oil or gas with reasonable diligence.” Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 19 S.W.2d 27, 29 (1929); see Sinclair Oil & Gas Co. v. Masterson, 271 F.2d 310 (5th Cir. 1959); Clifton v. Koontz, \textit{supra} note 49; Mon-Tex Corp. v. Poteet, 118 Tex. 154, 19 S.W.2d 32 (1929); Freeport Sulphur Co. v. American Sulphur Royalty Co., 117 Tex. 459, 10 S.W.2d 1039, 1042 (1928); \textit{Texas Pac. Coal} & Oil Co. v. Stuard, 7 S.W.2d 878 (Tex. Civ. App. 1928).

See Brown, \textit{The Implied Covenant For Additional Development}, 13 Sw. L.J. 149, 150 (1919).

\textsuperscript{51} “\textit{U}ntil Texas declares to the contrary we are bound by Vernon v. Union Oil Co. . . .” 320 F.2d at 862. Now the federal courts are bound by the \textit{Duke} decision.

\textsuperscript{52} Breach of the lessee's implied obligation for reasonable mineral operations will not authorize the forfeiture of the lease as for breach of condition subsequent; such obligation being a covenant. The usual remedy for breach of the lessee's implied covenants for reasonable development of oil and gas is an action for damages, though, under extraordinary circumstances—where there can be no other adequate relief—a court of equity will entertain an action to cancel the lease in whole or in part.


\textsuperscript{53} Discussion Note, 19 Oil & Gas Rep. 236, 237 (1964).
implied covenant principles stems from a complete disregard of the better reasoning of the Texas courts for more than forty years. The right of a state to select its own law of property is fundamental. A federal court sitting in diversity has at most a duty to apply the law of the state as best it can divine if the state has not announced the applicable principles. In setting sail, the present court ignored fundamental rules of Texas oil and gas law. Moreover, a venture into a juridical area in which the principles are well announced requires at most the lifting of anchor. The principal case should receive careful consideration in the future Texas cases.

Michael T. Garrett

Evidence — Spontaneous Exclamations — Admissibility When Opinion

Plaintiffs' car was struck from the rear by a truck driven by an employee of the defendant. Immediately afterward the employee said to the plaintiffs, "Well, I know it was my fault, and if I had had three feet further back I could have missed you." The plaintiffs testified to this statement in the trial court action in which the employee was not a party defendant. Held: Statements by an employee that he was at fault for an accident, even though made immediately after the accident, are not admissible against the defendant employer because the statements are pure conclusions and opinions. Isaacs v. Plains Transp. Co., — Tex. —, 367 S.W.2d 152 (1963).

The Hearsay Rule generally prohibits attempts to prove that an event happened through testimony by A that "B told me it did," that is, a narration by a witness of statements previously made by himself or another, if offered for the purpose of proving the truth of such previous statements, is inadmissible as hearsay. The rule has been crystallized since the 1700s, long enough for innumerable exceptions to develop and fester into controversy. One exception is for spontaneous exclamations made very near in time and place to the event that is the subject of the suit. An example would be the man who staggers from his wrecked car exclaiming, "My brakes wouldn't hold." The theory is that he blurts out the truth before

1 361 S.W.2d 919, 924 (1962).
2 6 Wigmore, Evidence § 1361 (1d ed. 1940).
4 6 Wigmore, op. cit. supra note 2, at § 1364.
5 Id., at § 1747.
he has time to realize the possible consequences. Courts frequently refer to these spontaneous exclamations as the "res gestae exception" to the Hearsay Rule. If admitted under this exception, the ground usually is said to be that the statement was related so closely to the litigated act as to be a part of it.

Another exception to the Hearsay Rule is for admissions. An admission is any prior act or statement by a party that is inconsistent with his position in court. For example, a party may contend in court that he kept a proper lookout. His party-opponent can introduce testimony to show that in describing the collision afterward he told someone, "I've had so many things on my mind I guess I forgot to look." To qualify as an admission, the statement need not have been made at the time and place of the accident. Admissions made by an agent are considered admissions of his principal if the agent was within the scope of his authority when he made them. Typically, the principal denies his agent had such authority, and the struggle is over that point.

Another broad ground for exclusion of testimony is the Opinion Rule. Its purpose is to restrict the witness to what he knows about the event, as opposed to what he thinks about it. The rule has been criticized often and severely, and, as the Hearsay Rule, it is riddled with exceptions. One, of course, is for the expert witness who can assist the jury in interpreting the facts. Another exception is for the nonexpert witness who is speaking of a situation difficult to describe objectively, i.e., that the defendant appeared to be "mad."

If an employed driver admits fault at the scene of an accident and his employer is sued, both the hearsay rule and the opinion rule must be considered by the court in determining whether another witness can testify to what the driver said. His statement could be a spontaneous exclamation, an admission, and an opinion.

Spontaneous statements of facts made immediately after an accident or other exciting event have long been admitted by Texas

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8 McLean v. Hargrove, 159 Tex. 236, 162 S.W.2d 934 (1942).
13 7 Wigmore, op. cit. supra note 2, at § 1917.
14 Ibid.
15 See, e.g., Central R.R. v. Monahan, 11 F.2d 212 (2d Cir. 1926).
16 7 Wigmore, op. cit. supra note 2, at § 1923.
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courts as exceptions to the Hearsay Rule.\(^{18}\) Statements not made immediately after the event are admitted if it is shown that the declarant was still in the grip of the excitement caused by the event.\(^{19}\) As the time and place of the statement move farther from the exciting event, it becomes progressively more difficult to show that the declarant was still excited and spoke spontaneously.\(^{20}\)

If the spontaneous utterance is also an opinion, there is a split of authority whether it should be admitted. If allowed, it must come in as an exception, not only to the Hearsay Rule, but also to the Opinion Rule. By the weight of authority, in Texas\(^{21}\) and elsewhere,\(^{22}\) this is one rule too many. The courts have taken the position

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that, since the declarant would not be allowed to give his opinion if he were testifying in court, his opinion given out of court is similarly unacceptable. However, some have admitted highly opinionated statements because they were part of the res gestae. Others have said the statement by a participant was not really an opinion or conclusion because he was there and knew what happened. Opinion statements have also been admitted for impeachment purposes if the declarant took the stand and said he did not make any statement at the scene of the accident. In criminal cases opinion statements are often admitted under the label "shorthand rendition of the facts." Finally, if the spontaneous statement is made by an agent admitting fault for which his employer will be liable, the decisions also are split. The test is whether the agent was within the scope of his authority. Some courts have found implied authority if the statement was made while the agent was performing an authorized act or immediately afterward. It often is said that the statements were part of the res gestae if they closely accompanied an authorized act. However, the preponderance of recent decisions exclude opinion statements by agents even if made immediately after an authorized act. In most

cases in which the agent's statement is admitted, (1) the statement is one which could be interpreted either as a fact or an opinion or (2) the agent is a party defendant to the suit. Despite the confusion, real and apparent, the Texas Supreme Court in the instant case follows a fairly consistent line of decisions for similar fact situations. Though often deprecated by legal writers, it is conceded to be the prevailing rule. In *San Antonio Pub. Serv. Co. v. Alexander* the court said:

The doctrine by which the hearsay rule of evidence is relaxed so as to admit spontaneous contemporaneous statements as part of the res gestae does not extend to statements, such as those under consideration here, which are but the expressions of opinion by the declarant. The rule is that the reproduction of statements will not be permitted under the res gestae exception, where the declarant, if present as a witness himself, would not be permitted to testify to the facts embodied in the statement.

In *A.B.C. Storage & Moving Co. v. Herron* the trial court had excluded testimony that the driver had admitted fault at the scene of the accident. The appeals court said, "Whatever may be the rule

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McCormick & Ray, op. cit. supra note 3, at § 1406: "In line with the weight of authority elsewhere, our courts hold that the opinion rule is applicable to hearsay statements admissible under some exception to the hearsay rule." The authors join other distinguished commentators in taking exception to the cases excluding statements solely on the basis of their being "opinion."
in other states and whatever ought to be the rule in principle, the trial court applied the rule as it exists in Texas.\(^{28}\) Even before these cases were decided, it was held that a prior statement of an opinion, even though inconsistent with the person's position in court, was not admissible against the person making it.\(^{30}\) A statement that another person was "completely honorable" was held not inconsistent with a later assertion in court that that person had acted dishonestly in a specific transaction.\(^{30}\)

Apparently the court in the principal case did not regard Houston Oxygen Co. v. Davis\(^{41}\) as contrary authority. This 1942 Texas Supreme Court case went the other way on facts not too different from the San Antonio Pub. Serv.\(^{42}\) case. The witness, a passenger, repeated in court the observation made by the driver to him about the persons in the passing car that "they must have been drunk, that... we would find them somewhere on the road wrecked if they kept that rate of speed up."\(^{43}\)

Inasmuch as opinion testimony has produced so much difficulty and controversy, one wishes the court in the instant case had given a full discussion. What it does say, however, it says plainly. Opinions of an agent, even though made in excitement immediately after an accident, are not admissible against the principal. Whether the statement would be admissible against the agent if he also were a party defendant was not decided since the agent was not a party here and the question was not before the court. It can be inferred from the opinion that the statement could be used for impeachment if the agent-declarant testified that he did not make any statement at all at the accident scene or that he said something different. The court said: "These statements of the driver were pure conclusions and opinions, were not offered for impeachment, and were not admissible against the employer even though made immediately after the collision."\(^{44}\) (Emphasis added.)

Desirability of the rule can be argued with reason either way. It is sure to be viewed with dismay by those who have advocated with considerable success the present-day trend toward liberality in admis-

\(^{28}\) Id. at 216.
\(^{30}\) Id. at 230.
\(^{41}\) 139 Tex. 1, 161 S.W.2d 474 (1942).
\(^{31}\) See note 14 supra.
\(^{42}\) Houston Oxygen Co. v. Davis, 139 Tex. 1, 161 S.W.2d 474, 476 (1942).
\(^{43}\) 367 S.W.2d at 153.
sion of testimony in opinion form.\(^{46}\) Certainly, few would want to return to an Opinion Rule which often served as a gag and prevented the witness from telling his story in everyday terms.\(^{46}\) Of the impossibilities posed by the rule in full flower, Judge L. Hand observed, "The line between opinion and fact is at best one of degree."\(^{47}\) Wigmore predicted the eventual disappearance of the Opinion Rule,\(^{48}\) and many have urged that the day be hastened by abolishing it altogether.\(^{49}\) Proposals by the American Law Institute\(^{50}\) and the National Conference of Commissioners on Uniform State Law\(^{51}\) would, generally speaking, permit witnesses to testify in opinion form to what they have perceived personally.

The main problem posed by the principal case is the brief, categorical way in which the court seems to brush aside the disputed statements as "pure conclusions and opinions."\(^{52}\) This approach, taken indiscriminately, could provide a means of choking off testimony that meets all tests of fairness and relevance. In-court statements that are quite ordinary and natural in their phrasing and out-of-court statements that meet all requirements for an admission or an

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\(^{48}\) Central R.R. v. Monahan, 11 F.2d 212, 214 (2d Cir. 1926). Judge Hand said: "Every judge of experience in the trial of causes has again and again seen the whole story garbled, because of insistence upon a form with which the witness cannot comply, since, like most men, he is unaware of the extent to which inference enters into his perceptions. He is telling the 'facts' in the only way that he knows how, and the result of nagging and checking him is often to choke him altogether, which is, indeed, usually its purpose." Id. at 214.

\(^{49}\) 7 Wigmore, op. cit. supra note 2, at § 1929.

\(^{50}\) Fisch, supra note 45.

\(^{51}\) Model Code of Evidence rule 401, at 199; Rule 401, Testimony in Terms of Opinion

(1) In testifying to what he has perceived a witness, whether or not an expert, may give his testimony in terms which include inferences and may state all relevant inferences, whether or not embracing ultimate issues to be decided by the trier of fact, unless the judge finds

(a) that to draw such inferences requires a special knowledge, skill, experience, or training which the witness does not possess, or

(b) that the witness can readily and with equal accuracy and adequacy communicate what he has perceived to the trier of facts without testifying in terms of inference or stating inferences, and his use of inferences in testifying will be likely to mislead the trier of fact to prejudice of the objecting party.

(2) The judge may require that a witness, before testifying in terms of inference, be first examined concerning the data upon which the inference is founded.

\(^{52}\) Uniform Rules of Evidence Rule 56, at 193 (1953): "If the witness is not testifying as an expert his testimony in the form of opinions or inferences is limited to such opinions or inferences as the judge finds (a) may be rationally based on the perception of the witness and (b) are helpful to a clear understanding of his testimony or to the determination of the fact in issue."

\(^{53}\) 367 S.W.2d at 153.
exception to the Hearsay Rule could be excluded because in the form of an "opinion or conclusion." Most authorities would regard this as a retrogression in the law of evidence.\(^3\)

It should be noted, however, that this case is not one of the type which has earned the Opinion Rule such low esteem. Here we do not have the typical case of the earnest, but inarticulate, witness who is being harried into speechless confusion by opposite counsel's insistence on an impossibly factual standard. Contention is over whether a witness can repeat the opinion expressed by another person out of court. Perhaps it might be well to lay aside legal principles for the moment and consider basic pros and cons of an unconsidered opinion given as a reaction to a shocking event. On the pro side Wigmore says the excitement "stills the reflective faculties and removes their control so that the utterance which then occurs is a spontaneous and sincere response to the actual sensations . . . during the brief period when considerations of self-interest could not have been fully brought to bear by reasoned reflection."\(^4\) In other words the excited person forgets to protect himself with well-chosen words. The principle would seem similar to that of the old adage, "In vino veritas."

But the studies of social scientists counsel caution against a too-ready acceptance of these free-wheeling statements of the upset. Careful studies have shown that the emotional reaction to an exciting event may cause people to make irrational statements which, when made, they believe to be true.\(^5\) Even considered opinions are believed to be affected strongly by personality and experiences.\(^7\) Behavioral scientists who have considered the problems of evaluating testimony tend to view lack of intent to lie as a flimsy guarantee of truthfulness, particularly if excitement is introduced.\(^8\) Everyone has had the experience of hearing as many versions of a shocking event as there were observers. Burtt observed from his experiments, "[T]he introduction of considerable excitement seems to militate against accurate

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\(^3\) McCormick & Ray, op. cit. supra note 3, at § 1394; Morgan, Basic Problems of Evidence, 215; 6 Wigmore, op. cit. supra note 2, at § 1919; Comment, 24 Conn. B.J. 436 (1950); Note, 39 Geo. L.J. 101 (1951); Note, 20 U. Cinc. L. Rev. 484 (1951).

\(^4\) 6 Wigmore, op. cit. supra note 2, at § 1747.

\(^5\) In wine, the truth.

\(^6\) Moore, Tornadoes over Texas 311-13 (1958) (a study of individual and community reaction to disaster).

\(^7\) Smith, Bruner & White, Opinions & Personality 253, 275 (1956).

\(^8\) Munsterberg, On the Witness Stand 47 (1923). The author warns against belief "that the conditions for complete truth are given if the witness is not ready to lie . . . . What is meant is only that all the motives are lacking, which, in our social turmoil, may lead others to the intentional hiding of truth . . . . The subjective truth may thus be secured, and yet the idle talk of the drunkard and the child and the fool may be objectively untrue from beginning to end."
Excitement in the extreme form of mass hysteria has been responsible for some of the more bizarre chapters of history, i.e., the Salem witch trials in which sober, God-fearing citizens testified under oath to fantastic happenings.

Whether the court considered these possible dangers in its decision to exclude the testimony, we cannot know. Certainly all testimony by witnesses cannot be excluded because of the inherent inferiority of man to the tape recorder and camera as an accurate and detached observer and reporter. However, considering how damaging a statement admitting fault could be, the court was not without good reason for excluding it since the person making it had no responsibility for its effect. The rule set down by the court is justly limited. It will not protect those who blurt out facts and later try to tell a different story as to these facts. What it does exclude is an acknowledgment of fault by an agent who is not a defendant, whether this admission is made magnanimously by one who knows he will not have to pay or hysterically by one who does not at the time know or care what he is saying.

Reba Graham Rasor

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80 Burtt, Legal Psychology 72 (1931). Brown & Menninger, The Psychodynamics of Abnormal Behavior 105 (1940). "If one knows the emotional frustrations under which the thinker is suffering one can usually show in some detail just how the wish is father to the thought."

60 Gemmill, The Salem Witch Trials 233-34 (1924). Twenty persons were accused and executed in three months. Of a typical woman-turned-witch, various citizens testified that they had seen her enter a room through the cracks in the door, ride through the air on a broom and cast spells on their children. More amazing were the stories of some of the "witches" who not only admitted all but gave graphic accounts of meetings with the devil. "The whole community was under a spell . . . . Reason was not dead. It was only paralyzed."