

## Chapter 4

# Equitable and Statute of Limitations Defenses to Lease Expiration Claims

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**§ 4.01. Introduction and Overview.**

This chapter addresses the application of equitable and statute of limitations defenses to claims that a lease expired automatically under its habendum clause. The ‘Introduction’ immediately below discusses briefly the factual context for these increasingly common claims and the practical difficulties operators face in defending them. The brief ‘Overview’ introduces the reader to the organization of this chapter and to the legal concepts that inform the application of equitable and statute of limitations defenses in the unique context of oil and gas leases.

**[1] — Introduction.**

There are perhaps tens of thousands of oil and gas leases in the Appalachian Basin that are beyond their primary terms and therefore depend on continuous production to maintain their viability. Many such leases were signed decades ago or more. And many such leases support unconventional shale investments and drilling projects through continued production at shallow depths; in common parlance, the deeper shale rights are said to be held by production (or HBP) of the shallow depths. It goes without saying that much is riding on maintaining the continued existence of these older leases. To compound matters, lessors in the shale era are frequently incentivized to find grounds to terminate older leases and enter into new agreements — often for significantly higher royalties and lucrative lease bonuses. Because the typical oil and gas lease expires automatically under its habendum clause if oil or gas ceases to be produced from the leased premises during its secondary term, a lessor attempting to get out from under a lease may scour through years of production reports in order to locate a period of non-commercial production or an outright cessation of production. When a lessor alleges that a lease expired due to a deficiency in production that occurred years or decades earlier, the lessee may encounter practical difficulties in responding to the lessor’s claim. The lessee may rightly claim that the lease continued to produce in paying quantities notwithstanding a period of non-commercial production, or that a lapse in production is excused under the temporary cessation of production doctrine. But these doctrines may require

fact-specific analyses. When dealing with an ancient deficiency in production, the witnesses, records and other evidence necessary for the lessee to mount a successful defense simply may be unavailable.

Often, following a period when production was not commercial or outright ceased, the parties will resume their relationship — with the lessee restoring production (and perhaps engaging in further development) and the lessor willingly accepting royalties or other lease benefits — until improved market conditions finally prompt the lessor to reevaluate the status of the lease. Under such circumstances, could equitable defenses — like estoppel, waiver, or laches — or an applicable statute of limitations bar the lessor's termination claim? This chapter explores the application of these defenses to claims that a lease expired automatically under its habendum clause.

### **[2] — Overview.**

To place the availability of such defenses in proper legal context, this chapter begins in Section 4.02, *The Termination of an Oil and Gas Lease Under Its Habendum Clause*, by considering the nature of the oil and gas lease habendum clause itself, its mechanics, the requirement for production in paying quantities and the circumstances under which production under the lease is said to cease and thus terminate the lease. The discussion then turns, in Section 4.03, to *Applicability of Equitable Defenses to Lease Expiration Claims* and in Section 4.04, *Statutes of Limitations*, to the availability of equitable doctrines — like estoppel, waiver and laches — and to statutes of limitation as defenses to a claim that a lease expired under its habendum clause.

## **§ 4.02. The Termination of an Oil and Gas Lease Under Its Habendum Clause.**

Since the turn of the nineteenth century, the American petroleum industry has largely settled on the basic elements of the oil and gas lease. Chief among these is a granting clause that conveys the title to, or an interest in, oil and gas and a two-tiered habendum clause that provides for a relatively short fixed or primary term and a secondary term that continues so long as there is