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The Duty to Act Diligently

SLT Holdings, LLC v. Mitch-Well Energy, Inc., No. 542 WDA 2018 (Pa. Super. Ct. 2019)

In *SLT Holdings*, Defendants, Mitch-Well Energy, Inc. (“Mitch-Well”) and William E. Mitchell, Jr., appealed a 2018 trial court decision holding that they had abandoned two 1985 leases covering minerals situated in Warren County, Pennsylvania, owned by Plaintiffs, SLT Holdings, LLC and Jack and Zureya McLaughlin, due to a prolonged period of inaction.

The leases required Mitch-Well to drill a total of 50 wells and make specified minimum payments each year if the royalties from production failed to exceed stated minimum payments. However, the Defendants drilled only two wells, and the Plaintiffs testified that they had not received payments of any kind pursuant to the leases. Additionally, a report filed by the Pennsylvania Department of Environmental Protection evidenced that the wells had been abandoned as early as March 27, 1990.

Following nearly two decades of inaction, in 2013, Mitch-Well entered onto the Plaintiffs’ properties to pump oil, which it subsequently sold. The trial court found that this action constituted a conversion. On appeal, the Defendants presented the following arguments: (1) only Mitch-Well could properly determine the end of the lease term because the leases provided that they would continue in effect for so long as Mitch-Well determined that the leased materials could be produced in paying quantities, and (2) the leases could not terminate due to default because each required the Plaintiffs to give Mitch-Well written notice describing any default, to wit it would have 30 days to cure.

The Superior Court affirmed the lower court ruling, finding that the Defendants abandoned the wells and no longer had any right to remove Plaintiffs’ minerals. The court elaborated that even if the wells were capable of producing oil and gas, the leases could only be maintained by active production or the payment of shut-in gas royalties; the mere presence of a well arguably capable of production is insufficient to continue the lease into its secondary term and does not relieve a Lessee of its duty to comply with other lease terms. The court also agreed with the lower court’s conclusion that the Plaintiffs were not required to notify the Defendants of their default due to their abandonment of the wells.

While the court did not develop a bright-line rule concerning the time necessary to definitively establish abandonment, *SLT Holdings* serves as an important reminder that Lessees have an implied covenant to act in a diligent manner to produce and market oil and gas. Lease provisions, which appear to extend the term of a lease in perpetuity, should be reviewed cautiously, particularly if they do not appear to impose any duty on the Lessee. Finally, terms that appear to make an act contingent solely on the judgment of the Lessee should be read in the context of an implied clause of good faith, meaning that the decision-making process should not be arbitrary but rather based on sound judgment guided by the facts of the situation.

For a copy of the *SLT Holdings* decision or any questions or concerns regarding duties under oil and gas leases, please contact the Energy Group at Dickie, McCamey and Chilcote P.C.



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