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OIL, GAS AND MINERAL LAW

*Richard F. Brown**

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I. INTRODUCTION

This article focuses on the interpretations of and changes relating to oil, gas, and mineral law in Texas from November 1, 2014, through October 31, 2015. The cases examined include decisions of state and federal courts in the State of Texas and the U.S. Court of Appeals for the Fifth Circuit.¹

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1. This article is devoted exclusively to Texas law. Cases involving questions of oil, gas, and mineral law decided by courts sitting in Texas but applying laws of other states are not included. Page limitations of this publication required the omission of some cases of interest. The facts in the cases are sometimes simplified to focus on the legal principles.

II. TITLE AND CONVEYANCING ISSUES²A. *COSGROVE V. CADE*

Cosgrove v. Cade held that under the common law and under the recording statute a plain omission in an unambiguous deed charges the parties with irrebuttable notice of the deed's contents when the deed is executed, and the discovery rule does not toll the statute of limitations.³ In October 2006, Michael and Billie Cade (Grantors) sold two acres of land to Barbara Cosgrove (Grantee). The real estate contract reserved all of the mineral rights; however, the deed conveyed the land in fee simple. There was also a closing document entitled "Acceptance of Title and Closing Agreements" that required both parties to "fully cooperate, adjust, and correct any errors or omissions and to execute any and all documents needed or necessary to comply with all provisions of the above mentioned real estate contract."⁴ In December 2010, the Grantors became aware of the issue with their reservation and promptly filed suit for a declaratory judgment to reform the deed, for breach of contract under the Acceptance of Title and Closing Agreements document, and for various torts. Grantors' claims were subject to either a two or four-year statute of limitations.⁵

The first issue before the Texas Supreme Court was whether the discovery rule tolls the statute of limitations when there is "a mistaken-but-unmistakable omission in an unambiguous warranty deed."⁶ The discovery rule "defers accrual of a claim until the injured party learned of, or in the exercise of reasonable diligence should have learned of, the wrongful act causing the injury."⁷ "A plainly evident omission on an unambiguous deed's face is not a type of injury for which the discovery rule is available."⁸ "There is generally a rebuttable presumption that a grantor has

2. Other cases dealing with title and conveyancing issues include the following: *Lykken v. Kindsvater*, No. 02-13-00214-CV, 2014 WL 5771832 (Tex. App.—Fort Worth Nov. 6, 2014, no pet.) (per curiam) (mem. op.) (outstanding oil and gas leases as breach of covenant of seizen); *Griswold v. EOG Res., Inc.*, 459 S.W.3d 713 (Tex. App.—Fort Worth 2015, no pet.) (deed exception); *Cole v. McWillie*, 464 S.W.3d 896 (Tex. App.—Eastland 2015, pet. denied) (deed executed by attorney-in-fact); *Medina Interests, Ltd. v. Trial*, 469 S.W.3d 619 (Tex. App.—San Antonio 2015, pet. denied) (fixed or floating royalty); *Leal v. Cuanto Antes Mejor LLC*, No. 04-14-00694-CV, 2015 WL 3999034 (Tex. App.—San Antonio 2015, no pet.) (mem. op.) (fixed or floating royalty); *Saenz v. Thorp Petroleum Corp.*, No. 04-14-00527-CV, 2015 WL 4273270 (Tex. App.—San Antonio 2015, pet. denied) (partition agreement); *Orca Assets, G.P., L.L.C. v. Dorfman*, 470 S.W.3d 153 (Tex. App.—Fort Worth 2015, pet. denied) (bona fide purchaser); *Fort Apache Energy, Inc. v. Hous. Energy, L.P.*, No. 09-14-00007-CV, 2015 WL 5042133 (Tex. App.—Beaumont Aug. 27, 2015, no pet.) (mem. op.) (proportionate reduction of overriding royalty); *Red Boot Prod. Co. v. Samson Expl., LLC*, No. 09-14-00191-CV, 2015 WL 5730789 (Tex. App.—Beaumont Oct. 1, 2015, no pet.) (mem. op.) (conveyance to centerline of canal); *Hosek v. Scott*, No. 04-14-00655-CV, 2015 WL 6163385 (Tex. App.—San Antonio Oct. 21, 2015, no pet.) (mem. op.) (partition agreement).

3. *Cosgrove v. Cade*, 468 S.W.3d 32, 34–35 (Tex. 2015).

4. *Id.* at 35.

5. *Id.*

6. *Id.* at 34, 36.

7. *Id.* at 36 (citing *Sullivan v. Barnett*, 471 S.W.2d 39, 45 (Tex. 1971)).

8. *Id.*

immediate knowledge of defects in a deed that result from mutual mistake.”⁹ “Once the presumption is rebutted, the reformation claim does not accrue until the grantor actually knew, or in the exercise of reasonable diligence should have known of the mistake.”¹⁰ However, “[p]arties are charged as a matter of law with knowledge of an unambiguous deed’s material omissions from the date of its execution, and the statute of limitations runs from that date.”¹¹ The Grantors were charged with knowledge that their deed did not include a mineral reservation from the date of execution in October 2006. Thus, the applicable statute of limitations for their claims had already run in December 2010.¹²

The second issue in the case was whether Property Code § 13.002 (recording statute)—“[a]n instrument that is properly recorded in the proper country is . . . notice to all persons of the existence of the instrument”—also provides all persons, including the grantor, with notice of the deed’s contents.¹³ The supreme court previously held that knowledge imputed as constructive notice under the statute applied to grantees, and therefore, the discovery rule was unavailable to grantees to toll the statute as to obvious omissions in unambiguous deeds.¹⁴ In this case, the supreme court extended the holding to include grantors.¹⁵

The supreme court then addressed the Grantors’ breach of contract claim.¹⁶ Grantors contended that limitations on this claim did not begin to run until Grantee refused to correct the deed.¹⁷ The supreme court did not rely upon the merger doctrine.¹⁸ Instead, the supreme court reasoned that the documents were part of a single transaction, the issue was obvious when the deed was executed, and the four-year statute for breach of contract ran from the same date.¹⁹

The significance of this case is the holding that a plain omission in an unambiguous deed charges the parties with irrebuttable notice of the deed’s contents and the discovery rule does not apply to toll the statute of limitations for reformation.²⁰ The holding is limited to omissions from unambiguous deeds.²¹ The clock will run on what the deed says, but perhaps not as to what it means.

9. *Id.* (citing *Sullivan*, 471 S.W.2d at 45).

10. *Id.* at 36–37 (citing *Sullivan*, 471 S.W.2d at 45).

11. *Id.* at 37 (citing *McClung v. Lawrence*, 430 S.W.2d 179, 181 (Tex. 1968)).

12. *Id.*

13. *Id.* at 34 (quoting TEX. PROP. CODE ANN. § 13.002 (West 2014)) (alteration in original).

14. *Id.* at 38–39.

15. *Id.* at 38.

16. *Id.* at 39–40.

17. *Id.*

18. *Id.* at 40.

19. *Id.*

20. *See id.* at 34.

21. *See id.* at 37.

III. LEASE AND LEASING ISSUES²²A. *ENDEAVOR ENERGY RESOURCES, L.P. v. DISCOVERY OPERATING, INC.*

Endeavor Energy Resources, L.P. v. Discovery Operating, Inc. held that a lease terminated as to all acreage not included in a proration unit plat filed with the Texas Railroad Commission (TRC).²³ Endeavor et al., (Base Lessee) leased approximately 960 acres in an area subject to Special Field Rules issued by the TRC for the Spraberry (Trend Area) Field. The Special Field Rules provided for proration units of 80 acres or optional 160 acres. Base Lessee drilled and completed enough wells to include all of the leased acreage in a proration unit. Two quarter sections, however, were not included in any proration unit. Discovery et al., (Top Lessee) leased the two quarter sections not included in a proration unit.²⁴ The Base Leases had already terminated at the end of the continuous development period, but the termination clauses included a limitation:

[T]his lease shall automatically terminate as to all lands and depths covered herein, save and except those lands and depths located within a government proration unit assigned to a well producing oil . . . and . . . with each such governmental proration unit to contain the number of acres required to comply with the applicable rules . . . of the [TRC] for obtaining the maximum producing allowable for the particular well.²⁵

22. Other notable cases dealing with lease and leasing issues include the following: *Comm'r of Gen. Land Office v. SandRidge Energy, Inc.*, 454 S.W.3d 603 (Tex. App.—El Paso 2014, pet. filed) (royalty on CO₂); *Trinity Materials, Inc. v. Sansom*, No. 03-11-00483-CV, 2014 WL 7464023 (Tex. App.—Austin Dec. 31, 2014, pet. filed) (mem. op.) (breach of sand and gravel mining lease); *Petrohawk Properties, L.P. v. Jones*, 455 S.W.3d 753 (Tex. App.—Texarkana 2015, pet. dismissed) (failure to pay bonus); *Albert v. Dunlap Expl., Inc.*, 457 S.W.3d 554 (Tex. App.—Eastland 2015, pet. denied) (ratification of pooling modifying Pugh clause); *BP Am. Prod. Co. v. Laddex, Ltd.*, 458 S.W.3d 683 (Tex. App.—Amarillo 2015, pet. filed) (production in paying quantities over a “reasonable” period of time); *BP Am. Prod. Co. v. Red Deer Res., LLC*, 466 S.W.3d 335 (Tex. App.—Amarillo 2015, pet. filed) (production in paying quantities and shut-in royalties); *Chesapeake Expl., L.L.C. v. Hyder*, 483 S.W.3d 870 (Tex. 2015) (post-production cost burden on overriding royalty); *Clayton Williams Energy, Inc. v. BMT O & G TX, L.P.*, 473 S.W.3d 341 (Tex. App.—El Paso 2015, pet. filed) (breach of lease’s assignment and operations clause); *ROCA Res. Co. v. Devon Energy Prod. Co.*, No. 4:14-CV-085-DAE, 2015 WL 4479118 (W.D. Tex. July 22, 2015) (ORRI assignment and duty to develop); *Orca Assets, G.P., L.L.C. v. JPMorgan Chase Bank, N.A.*, No. 05-13-01700-CV, 2015 WL 4736786 (Tex. App.—Dallas Aug. 11, 2015, pet. filed) (mem. op.) (double leasing and disclaimer of warranty); *Samson Expl., LLC v. T.S. Reed Properties, Inc.*, No. 09-13-00366-CV, 2015 WL 6295726 (Tex. App.—Beaumont Oct. 22, 2015, pet. filed) (mem. op.) (amendment of pooled unit); *Titan Operating, LLC v. Marsden*, No. 02-14-00303-CV, 2015 WL 5727573 (Tex. App.—Fort Worth Aug. 27, 2015, pet. denied) (mem. op.) (nuisance claims by lessor against lessee and quasi-estoppel); *XOG Operating, LLC v. Chesapeake Expl. Ltd. P’ship*, No. 07-13-00439-CV, 2015 WL 5244718 (Tex. App.—Amarillo Sept. 2, 2015, pet. filed) (retained acreage clause).

23. *Endeavor Energy Res., L.P. v. Discovery Operating, Inc.*, 448 S.W.3d 169, 178 (Tex. App.—Eastland 2014, pet. filed).

24. *Id.* at 171–74.

25. *Id.* at 172.

Rule 3 of the Special Field Rules required operators to file certified plats with the TRC that show “all of those things pertinent to the determination of the acreage credit claimed for each well.”²⁶ The TRC would not act on Base Lessee’s request to expand its proration units to include the two missing quarter sections because of the pending title litigation between Base Lessee and Top Lessee.²⁷

The single issue in the case was the interpretation and construction of the automatic termination clause in the Base Leases.²⁸ The parties and the Eastland Court of Appeals agreed that the Base Leases were unambiguous.²⁹ Top Lessee asserted that the Base Leases “automatically terminated as to the lands in the disputed quarter sections because, on the date that the continuous development period ended, the lands in the disputed quarter sections were not located in a governmental proration unit assigned by [Base Lessee] to a well.”³⁰ Because the Special Field Rules allow “a proration unit to contain 160 acres to obtain the maximum producing allowable in a well in the Spraberry (Trend Area) Field,” Base Lessee asserted that “each of its producing wells held 160 acres under lease.”³¹ Base Lessee reasoned that the last “clause automatically establishe[d] the size of the proration units to be 160 acres” and that interpreting the automatic termination provision to require it to assign acreage in a certified proration plat ignored and would render meaningless the last clause. Therefore, Base Lessee “was not required to file a proration plat or to take any other action to maintain its leased acreage.”³²

Considering the provision in its entirety, the court of appeals ruled that the parties intended in the last clause to define the amount of acres that Base Lessee “was to include in the governmental proration units that it assigned in its certified proration plats filed with the [TRC].”³³ Concluding that the last clause did not relieve Endeavor of its obligation “to assign acreage to a well in a certified proration plat to maintain the acreage under lease,” the court of appeals noted:

[I]t is not the failure to designate the larger proration unit that automatically terminates the lease as to the disputed quarter sections; the automatic termination is the result of the lease terms. The failure to designate the additional acreage merely quantifies the amount of acreage as to which the lease provides for automatic termination.³⁴

The significance of the case is the literal reading of the lease and the holding that the failure to include acreage in the plat filed with the TRC was a failure to assign acreage to a proration unit, resulting in lease termi-

26. *Id.* at 177 (quoting Rule 3 of the Spraberry (Trend Area) Field Rules).

27. *Id.* at 174.

28. *Id.* at 175.

29. *Id.*

30. *Id.* at 176 (emphasis added).

31. *Id.*

32. *Id.* at 177.

33. *Id.* at 177–78.

34. *Id.* at 178.

nation as to all acreage not included in a proration unit.³⁵

B. *KCM FINANCIAL LLC v. BRADSHAW*

KCM Financial LLC v. Bradshaw examines the nature of the duty owed by the executive and the executive's lessee to the non-executive in an oil and gas leasing transaction.³⁶ Two deeds executed in 1960 reserved a non-participating royalty interest. The deeds reserved "an undivided one-half of any future royalty," but not less than a one-sixteenth (1/16) share of gross production.³⁷ The parties to the litigation aligned as successors to the Executive, Non-Executive, Lessee, and Executive's Assignees. The Executive leased for a one-eighth (1/8) royalty and a bonus of more than \$13 million, and the Executive conveyed part of the Executive's royalty interest to the Executive's Assignees.³⁸ The Non-Executive contended that the terms of the leasing transaction were for a sub-market (1/8 rather than 1/4) royalty rate (shared by the Executive and the Non-Executive), an above-market bonus (payable only to the Executive), that the Lessee acted in concert with the Executive, and that a constructive trust should be imposed on the royalty payments payable to the Executive's Assignees. The Executive and the other defendants won on summary judgment in the trial court.³⁹ The core issue on appeal was the nature of the duty owed by an executive to the non-executive.⁴⁰

The Texas Supreme Court reviewed all of its prior holdings, which referred to the duty as one of "utmost fair dealing," "confidential relationship," "utmost good faith," or "a fiduciary relationship," and which occasionally held that "the executive's duty is to 'acquire for the non-executive every benefit that he exacts for himself.'"⁴¹ The supreme court concluded:

If the semantics surrounding the nature of this duty have shifted subtly over the years, this much is clear: An executive owes a non-executive a duty that prohibits self-dealing but does not require the executive to subjugate its interests to those of the non-executive. Thus, in ascertaining whether the executive breached its duty to the non-executive, the controlling inquiry is whether the executive engaged in acts of self-dealing that unfairly diminished the value of the non-executive interest. Although the contours of the duty remain somewhat indistinct, these tenets guide our analysis of the claims before us.⁴²

35. *Id.* at 178–79.

36. *KCM Fin. LLC v. Bradshaw*, 457 S.W.3d 70, 74 (Tex. 2015).

37. *Id.* at 75.

38. *Id.* at 76–78.

39. *Id.* at 74.

40. *Id.*

41. *Id.* at 80–81 (quoting *Lesley v. Veterans Land Bd.*, 352 S.W.3d 479, 490 (Tex. 2011)).

42. *Id.* at 82.

The supreme court recognized that “[a]s articulated, the executive’s duty is deceptively simple in its explication, but not necessarily straightforward in its application.”⁴³

This is because “obtaining the same *royalty*” is not necessarily equivalent to obtaining “the same *benefit*.”⁴⁴ This case is focused on the interplay between royalty and bonus, but the interests and benefits of the executive and the non-executive can also diverge on other issues, such as surface damages, water rights, well locations, easements, drilling commitments, development of other tracts, and timing of development, etc. Obviously, the executive will almost never acquire every benefit he acquires for himself for the non-executive.⁴⁵ For example, a non-participating royalty owner does not share in bonus or delay rentals.⁴⁶ “This situation thus presents a conundrum that requires balancing the bundle of rights that comprise a mineral estate.”⁴⁷

The supreme court then examined the facts of the case and concluded that on the record there was some evidence precluding summary judgment on whether the Executive breached the Executive’s duty to the Non-Executive.⁴⁸ “Although in many cases this will be a fact question, we do not foreclose the possibility that breach of duty may be determined as a matter of law, depending on the evidence in a particular case.”⁴⁹ Nevertheless, it is clear that a breach will generally be a fact question, yet the supreme court does not expressly explain how the issue is to be submitted. The opinion does say that “the subject transaction must be viewed as a whole in determining whether the terms of a mineral lease, including the negotiated royalty, reflect the executive’s utmost good faith and fair dealing vis-à-vis the non-executive.”⁵⁰

Our decision today reaffirms a principle that has existed in our jurisprudence for eighty years: An executive owes a duty of utmost good faith and fair dealing to a non-executive and is prohibited from engaging in self-dealing in connection with the formation of a mineral-lease agreement. However, the failure to obtain a market-rate royalty does not, in and of itself, constitute a breach of that duty.⁵¹

The supreme court then considered whether any of the derivative claims against the Lessee could be sustained. Regardless of whether the jury ultimately determines the Executive breached the Executive’s duty to the Non-Executive, there was, as a matter of law, no evidence that Lessee breached any duty owed to the Non-Executive.⁵² Regardless of the Lessee’s knowledge of the existence of the non-participating royalty

43. *Id.* at 83.

44. *Id.*

45. *Id.*

46. *Id.*

47. *Id.*

48. *Id.* at 84.

49. *Id.*

50. *Id.*

51. *Id.* at 89.

52. *Id.* at 85.

interest and regardless of the Lessee's knowledge of the tension between the Executive and the Non-Executive, "the uncontroverted evidence reflects that [Lessee] merely secured a mineral-lease agreement on mutually acceptable terms."⁵³

The Texas Oil & Gas Association argues in an amicus brief that a lessee should not be tasked—directly or derivatively—with policing the executive's duty to non-executive interest holders. Nor should a lessee be expected to give weight to a non-participating royalty interest holder's economic interests; as we have held, that is the executive's responsibility. We agree with the Association that "in negotiating with the executive, a lessee should not fear liability for doing nothing more than getting a good deal closed."⁵⁴

If there is no existing fiduciary or confidential relationship between the lessee and the non-executive, and if the lessor and lessee are unaffiliated parties except as adverse parties in an arm's-length leasing transaction, after this decision, it is very unlikely that the lessee will be subjected to some derivative liability or duty to the non-executive.⁵⁵

The supreme court also rejected the constructive trust claim against the royalty owned by the Executive's Assignees, because the interest transferred to them was out of the one-half (1/2) interest owned by the Executive, which was not owned by the Non-Executive.⁵⁶

The significance of the case is the effort to clarify the nature of the duty: In the leasing transaction, it is not a traditional fiduciary duty; it is a duty of utmost good faith and fair dealing. Breach of the duty will generally be a fact question, and the pivotal issue will usually be whether the executive obtained some benefit for himself, but not for the non-executive, through some "legal contrivance" that unfairly diminishes the value of the non-executive interest. The lessee generally has no duty to protect the non-executive in the leasing transaction and need not fear liability for doing nothing more than getting a good deal closed.

C. *AYCOCK v. VANTAGE FORT WORTH ENERGY, LLC*

Aycock v. Vantage Fort Worth Energy, LLC held that a recovery by unleased cotenants for payment of bonus after ratification of the lease must come from the lessor, not the lessee.⁵⁷ Vantage leased some of the cotenants in a 1,409-acre tract and paid its lessors \$750 per net mineral acre for their undivided 526-acre interest. Vantage never drilled and the lease expired. The unleased cotenants claimed that they had ratified the lease and sued Vantage for their share of the bonus.⁵⁸

53. *Id.* at 85–86.

54. *Id.* at 86.

55. *Id.*

56. *Id.* at 88.

57. *Aycock v. Vantage Fort Worth Energy, LLC*, No. 11-13-00338-CV, 2015 WL 1322003, at *3 (Tex. App.—Eastland Mar. 20, 2015, pet. denied) (mem. op.).

58. *Id.* at *1.

The Eastland Court of Appeals introduced its analysis with the following principle:

Owners of undivided mineral interests are tenants in common. A cotenant may lease its undivided interest without joinder of another cotenant. The lease does not bind a nonconsenting cotenant. The lessor cotenant, however, must account to its nonconsenting cotenant for any minerals produced where the lessor cotenant has leased both its and the nonconsenting cotenant's interest or has received production payments on the nonconsenting cotenant's interest.⁵⁹

The unpaid cotenants argued that Vantage leased the entire 1,409 acres and that they ratified the lease by a subsequent letter to Vantage.⁶⁰ Vantage claimed that the proportionate reduction clause in the lease, along with other documents, shows that Vantage only intended to lease the 526-acre undivided interest.⁶¹ The court of appeals noted that “[a] proportionate reduction clause acts to protect the lessee from paying the lessor more than the lessor is due, but it does not act to reduce what the lessor conveys to the lessee.”⁶²

The court of appeals, however, assumed, without deciding, that Vantage leased the entire interest and that the unleased cotenants ratified the lease.⁶³ Vantage was “not the lessor cotenant and received no money accruing under the lease. Therefore, the unpaid mineral cotenants cannot recover bonus money from Vantage.”⁶⁴ The court of appeals concluded that Vantage established that the unpaid cotenants could “only recover [from] bonus money paid to” the lessors, if any, for the unleased cotenants' interest.⁶⁵ The unleased cotenants also could not recover against Vantage on an unjust enrichment claim, because Vantage did not profit at their expense.⁶⁶

The significance of the case is the holding that a recovery by unleased cotenants for payment of bonus after ratification of the lease must come from the lessor, not the lessee.⁶⁷

IV. INDUSTRY CONTRACTS⁶⁸

A. *IN RE DEEPWATER HORIZON*

In re Deepwater Horizon held that an operator was not an additional insured entitled to coverage for damages from subsurface pollution under

59. *Id.* (internal citations omitted).

60. *Id.* at *2.

61. *Id.*

62. *Id.* (citing *McMahon v. Christmann*, 303 S.W.2d 341, 346 (Tex. 1957)).

63. *Id.*

64. *Id.* at *3 (internal citations omitted).

65. *Id.*

66. *Id.*

67. *See id.* at *1–2.

68. Other cases dealing with industry contracts include the following: *Cresson SWD Servs., L.P. v. Basic Energy Servs., L.P.*, No. 02-13-00141-CV, 2014 WL 6686501 (Tex. App.—Fort Worth Nov. 26, 2014, pet. denied) (mem. op.) (failure to complete reworking of saltwater well); *Gray v. Chesapeake Expl., L.L.C.*, No. SA-14-CA-1020, 2015 WL

the drilling contractor's insurance policies because the drilling contract limited the drilling contractor's obligation to insure.⁶⁹ "This is an insurance-coverage dispute arising from the April 2010 explosion and sinking of the *Deepwater Horizon* drilling rig."⁷⁰ Various Transocean entities (Transocean) owned the *Deepwater Horizon*, and operated in the Gulf of Mexico pursuant to a drilling contract (Drilling Contract) with the BP entities (BP) as the Operator. The rig exploded causing 11 deaths, numerous injuries, and multiple claims for environmental and economic damages. In the Drilling Contract, Transocean agreed "to indemnify BP for above-surface pollution regardless of fault, and BP agreed to indemnify Transocean for all pollution risk Transocean did not assume, *i.e.*, subsurface pollution."⁷¹ "[T]he Drilling Contract further required Transocean to carry multiple types of insurance at its own expense" and to name BP as an additional insured.⁷² Transocean and BP sought coverage under Transocean's primary and excess insurance policies.⁷³ After BP made its demand for coverage, Transocean aligned with the insurers and sought a declaration that BP was not entitled to additional-insured coverage because the Drilling Contract limited the additional-insured obligation to "liabilities assumed by [Transocean] under the terms of [the Drilling] Contract,"⁷⁴ and the only liabilities assumed by Transocean were for above-surface pollution. The issues were: "(1) whether the language in the insurance policies refers to, and thus incorporates, coverage limitations in the Drilling Contract from which BP's additional-insured status derives; [and] (2) whether the Drilling Contract actually imposes any limitation on the extent of additional-insured coverage under the primary-

339744 (W.D. Tex. Jan. 26, 2015) (breach of surface use agreement by use of off-site water); *Sanders Oil & Gas GP, LLC v. Ridgeway Elec.*, No. 08-13-00299-CV, 2015 WL 590874 (Tex. App.—El Paso Feb. 11, 2015, no pet.) (mechanic's and materialman's lien); *Kilgore Expl., Inc. v. Apache Corp.*, No. 01-13-00347-CV, 2015 WL 505275 (Tex. App.—Houston [1st Dist.] Feb. 5, 2015, no pet.) (mem. op.) (payment of expenses in excess of AFE); *ConocoPhillips Co. v. Noble Energy, Inc.*, 462 S.W.3d 255 (Tex. App.—Houston [14th Dist.] 2015, pet. filed) (executory contracts in bankruptcy); *Prime Nat. Res., Inc. v. Certain Underwriters at Lloyd's, London*, No. 01-11-00995-CV, 2015 WL 1457534 (Tex. App.—Houston [1st Dist.] Mar. 26, 2015, no pet.) (mem. op.) (well insurance); *Kachina Pipeline Co., Inc. v. Lillis*, 471 S.W.3d 445 (Tex. 2015) (gas gathering agreement); *Anderson Energy Corp. v. Dominion Okla. Tex. Expl. & Prod., Inc.*, 469 S.W.3d 280 (Tex. App.—San Antonio 2015, no pet.) (meaning of Contract Area under JOA); *Dernick Res., Inc. v. Wilstein*, 471 S.W.3d 468 (Tex. App.—Houston [1st Dist.] 2015, pet. filed) (duties of joint venturers); *BP Oil Pipeline Co. v. Plains Pipeline, L.P.*, 472 S.W.3d 296 (Tex. App.—Houston [14th Dist.] 2015, pet. filed) (PSA indemnity); *Wolf Hollow I, L.P. v. El Paso Mktg., L.P.*, 472 S.W.3d 325 (Tex. App.—Houston [14th Dist.] 2015, pet. denied) (quality provision in gas contract); *Conglomerate Gas II, L.P. v. Gibb*, No. 02-14-00119-CV, 2015 WL 6081919 (Tex. App.—Fort Worth Oct. 15, 2015, pet. denied) (mem. op.) (assignment of back-in); *St. Paul Fire & Marine Ins. Co. v. Petroplex Energy, Inc.*, 474 S.W.3d 454 (Tex. App.—Eastland 2015, pet. dismissed) (blowout insurance).

69. *In re Deepwater Horizon*, 470 S.W.3d 452, 464–65 (Tex. 2015).

70. *Id.* at 455.

71. *Id.* at 456.

72. *Id.* at 457.

73. *Id.*

74. *Id.* at 458.

and excess-insurance policies.”⁷⁵

Under Transocean’s contract-construction theory, “the Drilling Contract requires Transocean to name BP as an additional insured only for the above-surface pollution risk that Transocean assumed and, as a result, BP [is not entitled to] additional-insured status for subsurface pollution risks.”⁷⁶ The Texas Supreme Court reasoned that determining BP’s additional-insured coverage begins within the four corners of the insurance policies, but “it does not necessarily end there.”⁷⁷ The supreme court explained:

We do not require “magic” words to incorporate a restriction from another contract into an insurance policy; rather, it is enough that the policy clearly manifests an intent to include the contract as part of the policy. . . . [W]e determine the scope of coverage from the language employed in the insurance policy, and if the policy directs us elsewhere, we will refer to an incorporated document to the extent required by the policy. Unless obligated to do so by the terms of the policy, however, we do not consider coverage limitations in underlying transactional documents.⁷⁸

Addressing the second issue, the supreme court noted: “BP is not named in any of the insurance policies nor is there any claim or evidence that it is expressly included as an additional insured in an endorsement or certificate of insurance.”⁷⁹

Instead, the policies confer coverage by reference to the Drilling Contract in which (1) Transocean assumed some liability for pollution that might otherwise be imposed on BP (making that contract an ‘Insured Contract’) and (2) Transocean is ‘obliged’ to procure insurance coverage for BP as an additional insured (making BP an ‘Insured’).⁸⁰

The supreme court explained that “it becomes apparent that the only reasonable interpretation of [the Drilling Contract’s additional-insured clause] is that the parties did not intend for BP to be named as an additional insured for the subsurface pollution liabilities BP expressly assumed in the Drilling Contract.”⁸¹

Despite generally being an additional insured under Transocean’s policy, BP did not have coverage here. The supreme court did not restrict its analysis to the four corners of Transocean’s insurance policy; rather, because Transocean’s insurance policy connected the additional insured coverage to the indemnities assumed by Transocean under the Drilling Contract, the supreme court held that the Drilling Contract limited the

75. *Id.*

76. *Id.*

77. *Id.* at 459–60.

78. *Id.* (internal citations omitted).

79. *Id.* at 464.

80. *Id.*

81. *Id.* at 465.

scope of BP's additional insured status under the insurance policy.⁸² BP sought coverage for a subsurface release, but this was not included in the liabilities assumed in Transocean's indemnity obligations in the Drilling Contract and, thus, not an event Transocean was obliged to provide coverage for in its insurance obligations in the Drilling Contract.⁸³ Because Transocean's insurance policy only provided additional insured status to those for whom Transocean was obliged to provide insurance, BP was not an additional insured for this event.⁸⁴

The significance of this case is "the interplay between an insurance policy and provisions in a drilling contract" governing the allocation of risk and the obligation to extend coverage to an additional insured.⁸⁵

B. *PLAINS EXPLORATION & PRODUCTION CO. v. TORCH ENERGY ADVISORS INC.*

Plains Exploration & Production Co. v. Torch Energy Advisors Inc. construes the Excluded Assets clause in a typical Purchase and Sale Agreement. Prior to 1990, there was a regulatory scheme in place governing offshore leasing.⁸⁶ In 1990, that scheme was amended. In 1994, Torch Energy Advisors Incorporated (Torch) obtained interests in various undeveloped leases on the Pacific outer continental shelf (OCS leases). In 1996, pursuant to a Purchase and Sale Agreement (PSA), Torch conveyed its interests in the OCS leases into the chain of title of Plains Exploration & Production Company (Plains) subject to the Excluded Assets clause in the 1996 PSA.⁸⁷ In 2001, California successfully sued the federal government for matters affecting the OCS leases resulting in a different construction of the 1990 statutory amendment than the one anticipated by the leasing parties.⁸⁸ This and other litigation effectively made development of the OCS leases impossible.⁸⁹ In 2005, Plains obtained a judgment that governmental repudiation occurred in 2001, and as a result of the lawsuit, Plains was awarded restitution damages measured by the original lease bonus payments of approximately \$83 million.⁹⁰ Torch sued Plains for breach of contract under the Excluded Assets clause in the 1996 PSA and various other theories for its part of the restitution damages.⁹¹

The specific PSA language at issue read as follows:

1.2. *Excluded Assets.* As used herein, "*Excluded Assets*" means . . .
(b) all claims and causes of action of [Torch] (i) arising from acts,

82. *Id.* at 467.

83. *Id.*

84. *Id.*

85. *See id.* at 455, 468.

86. *Plains Expl. & Prod. Co. v. Torch Energy Advisors Inc.*, 473 S.W.3d 296, 299 (Tex. 2015).

87. *Id.* at 300.

88. *Id.* at 301.

89. *Id.*

90. *Id.* at 301-02.

91. *Id.* at 302.

omissions or events, or damage to or destruction of property, occurring prior to the Effective Date, (ii) arising under or with respect to any of the Contracts that are attributable to periods of time prior to the Effective Date (including claims for adjustments or refunds); . . . (g) all proceeds, income or revenues (and any security or other deposits made) attributable to (i) the Properties for any period prior to the Effective Date, or (ii) any Excluded Assets⁹²

The PSA specifically reserved some inconsequential items, but made no reference to bonus, and Torch represented in the PSA that there were no pending claims.⁹³ The Texas Supreme Court described the 2005 judgment as the asset at issue and was heavily influenced by the provisions relating to the Effective Date.⁹⁴

The supreme court applied a plain meaning analysis to the operative words, “arising from,” “arising under or with respect to,” and “attributable to.”⁹⁵ The supreme court concluded these terms “unambiguously require a pre-effective date causal nexus that does not exist in this case.”⁹⁶ Torch argued for a “but for” connection.⁹⁷ “But for” the payment of bonus (before the Effective Date) there would be no leases and thus no judgment.⁹⁸ Adopting that argument “would render the temporal division employed in the relevant exclusions utterly meaningless.”⁹⁹ The U.S. Court of Appeals for the Federal Circuit had held that enactment of the amendment in 1990 did not breach or repudiate the OCS leases; it was events and actions taken in 2001 and later.¹⁰⁰ Moreover, lease bonus was only used as a measure of damages in the 2005 judgment.¹⁰¹ “Because the proceeds of the . . . judgment are neither attributable to or arising from or with respect to pre-conveyance events, they are not excluded assets”¹⁰²

The form of the PSA and the Excluded Assets provision appear to be fairly typical, and thus the significance of the case seems to be that in the absence of specifically identified claims or assets, the Effective Date will have a great impact on determining what is or is not conveyed or excluded.¹⁰³

92. *Id.* at 304.

93. *Id.* at 306.

94. *Id.* at 304.

95. *Id.* at 307.

96. *Id.*

97. *Id.* at 308.

98. *Id.*

99. *Id.* at 309.

100. *Id.*

101. *Id.*

102. *Id.* at 310.

103. *See id.* at 307.

V. LITIGATION ISSUES¹⁰⁴A. *ENVIRONMENTAL PROCESSING SYSTEMS, L.C. v. FPL FARMING, LTD.*

Environmental Processing Systems, L.C. v. FPL Farming, Ltd. held that “lack of consent” is an element of the cause of action for trespass and not an affirmative defense.¹⁰⁵ FPL Farming, LTD (FPL) farms rice in Liberty County, Texas. Environmental Processing System (EPS) leases and operates a five-acre wastewater disposal facility adjacent to FPL’s property. FPL brought a trespass claim against EPS for deep subsurface wastewater migration onto FPL’s property.¹⁰⁶ The trial court judge presented the jury with the following question on the issue of trespass:

Question 1: Did EPS trespass on FPL [Farming’s] property?

“Trespass” means an entry on the property of another *without having consent of the owner*. To constitute a trespass, entry upon another’s property need not be in person, but may be made by causing or permitting a thing to cross the boundary of the property below the surface of the earth. Every *unauthorized* entry upon the property of another is a trespass, and the intent or motive prompting the trespass is immaterial.

Answer yes or no.¹⁰⁷

The issues were: (1) Whether consent is an element of the cause of action of trespass, or an affirmative defense?; and (2) Who has the burden of proving consent in a trespass cause of action?¹⁰⁸

The Texas Supreme Court reviewed a century and a half of trespass-related decisions to conclude that the supreme court has “never departed from the inclusion of lack of consent or authorization in the definition of

104. Other cases dealing with litigation issues include the following: *In re T.S.C. Seiber Services, L.C.*, 771 F.3d 246 (5th Cir. 2014) (mineral subcontractor’s liens in bankruptcy); *Crosstex N. Texas Pipeline, L.P. v. Gardiner*, 451 S.W.3d 150 (Tex. App.—Fort Worth 2014, pet. granted) (nuisance in operation of compressor site); *Matador Prod. Co. v. Weatherford Artificial Lift Sys., Inc.*, 450 S.W.3d 580 (Tex. App.—Texarkana 2014, pet. denied) (bad frac and contractor liability); *Riemer v. State*, 452 S.W.3d 491 (Tex. App.—Amarillo 2014, pet. denied) (Canadian River class action on river boundary); *Crawford v. XTO Energy, Inc.*, 455 S.W.3d 245 (Tex. App.—Amarillo 2015, pet. granted) (joinder of owners in a pooled unit as affected by lease dispute); *In re Lipsky*, 460 S.W.3d 579 (Tex. 2015) (water well pollution); *Biltex Enters., Inc. v. Myers*, No. 02-13-00465-CV, 2015 WL 1967285 (Tex. App.—Fort Worth Apr. 30, 2015, no pet.) (mem. op.) (attorney’s fees in trespass to try title); *Clark v. ConocoPhillips Co.*, 465 S.W.3d 720 (Tex. App.—Houston [1st Dist.] 2015, no pet.) (statute of limitations on payment of royalties in class action cases); *Sciscoe v. Enbridge Gathering (N. Texas), L.P.*, No. 07-13-00391-CV, 2015 WL 3463490 (Tex. App.—Amarillo 2015, pet. filed) (light noise, and airborne particulate pollution); *Brenham Oil & Gas, Inc. v. TGS-NOPEC Geophysical Co.*, 472 S.W.3d 744 (Tex. App.—Houston [1st Dist.] 2015, no pet.) (tortious interference with production agreement); *Lightning Oil Co. v. Anadarko E&P Onshore LLC*, 480 S.W.3d 628 (Tex. App.—San Antonio Oct. 14, 2015, pet. filed) (subsurface trespass by drilling); *In re ATP Oil & Gas Corp.*, 540 B.R. 294 (Bankr. S.D. Tex. 2015) (assignments of ORRI in bankruptcy).

105. *Envtl. Processing Sys., L.C. v. FPL Farming, Ltd.*, 457 S.W.3d 414, 425 (Tex. 2015).

106. *Id.* at 417.

107. *Id.* (emphasis in original).

108. *Id.*

a trespass.”¹⁰⁹ A “[t]respass to real property is an *unauthorized* entry upon the land of another, and may occur when one enters—or causes something to enter—another’s property.”¹¹⁰

Many Texas appellate courts have concluded that “consent is an affirmative defense to be pleaded and proven by the defendant.”¹¹¹ Texas courts, however, allocate the burden of proof of a particular claim by taking into consideration: “(1) [t]he comparative likelihood that a certain situation may occur in a reasonable percentage of cases’; and (2) the difficulty in proving a negative.”¹¹² Typically, only a small fraction of trespass cases present a consent question due to the fact that landowners have no reason to suspect a trespass may occur and is rarely presented with an opportunity to consent to trespass.¹¹³ When consent is at issue, the supreme court determined that the landowner is in the best position to prove lack of consent or authorization “because only ‘someone acting with the authority of the landowner or one with rightful possession’ can authorize, or consent to, the entry.”¹¹⁴ To hold otherwise, the supreme court explained, would require plaintiffs only prove an entry upon their land, which would ignore the supreme court’s clear precedent requiring plaintiffs demonstrate that the entry was unauthorized.¹¹⁵

Importantly, the supreme court’s resolution of the consent issue—coupled with the jury’s determination that EPS did not trespass upon FPL’s property—allowed the supreme court to decline FPL’s invitation to address the question of whether deep “subsurface wastewater migration can constitute a cause of action for trespass” under Texas law.¹¹⁶

The significance of this case is the supreme court’s holding that unauthorized entry, or lack of consent, is an element of the cause of action for trespass with the burden on the plaintiff.¹¹⁷ It is also significant that the supreme court neither approved nor disapproved of the lower court’s analysis and holding on subsurface trespass.¹¹⁸

B. *IN RE LONGVIEW ENERGY CO.*

In re Longview Energy Co. analyzed the appropriate amount of a supersedeas bond when the judgment imposes a constructive trust on an oil and gas prospect.¹¹⁹ Longview Energy Co. (Longview) was pursuing the acquisition of 46,000 acres in the Eagle Ford Shale which Huff Energy

109. *Id.* at 418–22.

110. *Id.* at 422 (emphasis in original) (quoting *Barnes v. Mathis*, 353 S.W.3d 760, 764 (Tex. 2011)).

111. *Id.*

112. *Id.* at 424 (quoting *20801, Inc. v. Parker*, 249 S.W.3d 392, 397 (Tex. 2008)).

113. *Id.*

114. *Id.* (quoting *Gen. Mills Rests., Inc. v. Texas Wings, Inc.*, 12 S.W.3d 827, 835 (Tex. App.—Dallas 2000), *abrogated by Env'tl. Processing Sys., L.C.*, 457 S.W.3d 414).

115. *Id.*

116. *Id.* at 426.

117. *See id.*

118. *See id.*

119. *In re Longview Energy Co.*, 464 S.W.3d 353, 360 (Tex. 2015).

Fund, L.P. et al., (Huff) obtained. Huff was a minority shareholder in Longview and there were overlapping directors and principals. “Longview sought disgorgement of [Huff’s] unjust enrichment but did not seek damages.”¹²⁰ Longview also did not request jury findings on damages, because it thought the assets were undervalued.¹²¹ The jury found a breach of fiduciary duty.¹²² The trial court judgment awarded Longview a constructive trust over the prospect and “future production revenues net of royalties and production taxes.”¹²³ Separately, the judgment awarded “the same future net production revenues covered by the constructive trust ‘and an additional \$95,500,000.00’” with no explanation for the monetary award.¹²⁴ An earlier (withdrawn) judgment “described the \$95.5 million as being ‘based on the jury’s finding regarding the value of past-production revenues derived from the [Eagle Ford Shale assets, \$120 million]’ but without credit for either the \$127 million development costs found by the jury or the other production expenses.”¹²⁵ The multiple Huff defendants jointly posted a \$25 million bond as security to supersede enforcement of the judgment, Longview persuaded the trial court to increase the bond to \$25 million for each defendant, and all parties petitioned the Texas Supreme Court for relief by mandamus as to the amount of the supersedeas bond.¹²⁶

The amount of a supersedeas bond is governed by Chapter 52.006 of the Civil Practice and Remedies Code, which is tracked by Rule 24.2 of the Rules of Appellate Procedure.¹²⁷ The bond “must equal the sum of compensatory damages awarded in the judgment, interest for the estimated duration of the appeal, and costs awarded in the judgment.”¹²⁸ The issue in the case was whether the \$95.5 million was compensatory damages.¹²⁹

To begin its analysis, the supreme court noted: “If the trial court did not calculate the \$95.5 million the way the [trial] court first explained [in the withdrawn judgment], then the number seems to have been pulled from thin air. Longview offers no explanation for what the figure represents.”¹³⁰ Longview argued that the judgment was not punitive and therefore it must be compensatory.¹³¹ The supreme court reasoned that the judgment *could* be punitive because it awarded *gross* past production revenues less asset acquisition costs, which presumably made the defendants liable for an amount in excess of net gains.¹³² Regardless, disgorgement is

120. *Id.* at 356.

121. *Id.* at 351.

122. *Id.* at 356.

123. *Id.*

124. *Id.*

125. *Id.* (quoting the withdrawn trial court judgment).

126. *Id.* at 356–57.

127. *Id.* at 358–59.

128. *Id.* at 359 (quoting TEX. R. APP. P. 24.2).

129. *Id.* at 360.

130. *Id.*

131. *Id.*

132. *Id.* at 360–61.

not damages.¹³³ The supreme court had previously construed Rule 24.2 in the context of attorney fees and held that attorney fees are not compensatory damages for purposes of calculating a supersedeas bond.¹³⁴ The supreme court there analyzed the recovery of attorney fees as “compensatory in that they help make a claimant whole, but they are not, and have never been, damages.”¹³⁵ The supreme court had previously held that equitable forfeiture “is not mainly compensatory . . . nor is it mainly punitive” and “cannot . . . be measured by . . . actual damages.”¹³⁶ “Disgorgement is compensatory in the same sense attorney fees, interest, and costs are, but it is not damages.”¹³⁷ Therefore, in this case, “[t]he only . . . amount for which security must be given is costs, which [were] \$66,645.”¹³⁸

Another issue in the case was the trial court’s post-judgment order that Huff produce monthly to Longview, during the appeal, all of the documents affecting the prospect, which was affirmed.¹³⁹

The significance of the case is the stark contrast in the amount required for a supersedeas bond in a damages case compared to a disgorgement or constructive trust case, particularly when the dispute involves an oil and gas prospect.¹⁴⁰

C. *PHILLIPS v. CARLTON ENERGY GROUP, LLC*

Phillips v. Carlton Energy Group, LLC held that when the market value of a prospect is measured by lost profits, lost profits must be proved with reasonable certainty.¹⁴¹ This case arose out of a dispute among parties competing for a concession to explore for coalbed methane in an unproven field in Bulgaria. The alignment of the parties and the facts were complicated, but Carlton secured a jury verdict of tortious interference with contract resulting in the loss of the prospect.¹⁴² Carlton alleged it was entitled to recover the market value of its lost interest in the Bulgaria prospect, and the issue in the case was the determination of market value by proof of lost profits attributable to the loss of the prospect. Carlton’s experts provided three damages models ranging from \$12.54 million to \$31.16 million to \$11.305 billion.¹⁴³ The models were intended to establish the fair market value of Carlton’s lost investment measured by the amount of its lost profits.¹⁴⁴ The jury awarded Carlton \$66.5 million in

133. *Id.* at 361.

134. *Id.* at 360 (citing *In re Nalle Plastics Family Ltd. P’ship*, 406 S.W.3d 168, 174 (Tex. 2013)).

135. *Id.* (quoting *In re Nalle Plastics Family Ltd. P’ship*, 406 S.W.3d at 173).

136. *Id.* at 361 (quoting *Burrow v. Arce*, 997 S.W.2d 229, 240 (Tex. 1999)).

137. *Id.*

138. *Id.*

139. *Id.* at 362.

140. *See id.* at 359–61.

141. *Phillips v. Carlton Energy Group, LLC*, 475 S.W.3d 265, 269 (Tex. 2015).

142. *Id.* at 269–73.

143. *Id.* at 274.

144. *Id.* at 273–75.

actual damages,¹⁴⁵ which did not clearly relate to any of Carlton's three models.

Phillips argued that the fair market value of the prospect was too speculative to support an award of damages.¹⁴⁶ "A property's fair market value is what a willing buyer would pay a willing seller, neither acting under any compulsion."¹⁴⁷ "Fair market value is generally determined either by using comparable market sales, calculating replacement cost less depreciation, or capitalizing net income—that is, profits."¹⁴⁸ The Texas Supreme Court recognized that where lost profits are sought to be recovered as consequential damages, the "lost profits can be recovered only when the amount is proved with reasonable certainty."¹⁴⁹ "The reasonable certainty requirement 'is intended to be flexible enough to accommodate the myriad circumstances in which claims for lost profits arise.'"¹⁵⁰

The question in this case was whether the reasonable certainty requirement should be extended to cases where "lost profits are not sought as damages themselves but are used to determine the market value of property for which recovery is sought."¹⁵¹ The supreme court held that the reasonable certainty requirement should be extended to such cases, because "[t]he purpose of the requirement is to prevent recovery based on speculation," and there was no reason why the requirement should not apply equally to lost profits and lost market value.¹⁵²

The supreme court determined that two of Carlton's damage models were merely conjectural and based on sweeping assumptions.¹⁵³ Specifically, Carlton's experts made unsupported projections about the value of gas in the ground, the amount of gas actually recoverable, cost of recovery, and cost of marketing, etc.¹⁵⁴ However, there was evidence that the parties fixed various prices as they bought and sold fractional parts of the prospect.¹⁵⁵ The supreme court held that when there is evidence of prices fixed by real investors in a market in which such interests are bought and sold, all of the speculation is subsumed into the data they rely upon to reach their valuation.¹⁵⁶ Therefore, at least one of the damage models had some evidence to support the verdict. Specifically, the supreme court looked to Phillips' agreement to pay Carlton \$8.5 million in exchange for a 10% interest in the project (and adjusted for other factors), to support a

145. *Id.* at 275.

146. *Id.* at 277.

147. *Id.* (citing *Hous. Unlimited, Inc. Metal Processing v. Mel Acres Ranch*, 443 S.W.3d 820, 831 (Tex. 2014)).

148. *Id.* (citing *City of Harlingen v. Estate of Sharboneau*, 48 S.W.3d 177, 182 (Tex. 2001); *Miga v. Jensen*, 96 S.W.3d 207, 213 (Tex. 2002)).

149. *Id.* (citing *Tex. Instruments, Inc. v. Teletron Energy Mgmt., Inc.*, 877 S.W.2d 276, 279 (Tex. 1994)).

150. *Id.* (quoting *Tex. Instruments, Inc.*, 877 S.W.2d at 279).

151. *Id.* at 280.

152. *Id.*

153. *Id.* at 281.

154. *Id.*

155. *Id.* at 281–82.

156. *Id.* at 282.

valuation of \$31.16 million.¹⁵⁷ The issue was ultimately remanded to the court of appeals to address factual insufficiency as to valuation.¹⁵⁸

The significance of this case is the holding that the valuation of a lost prospect, when measured by lost profits to find market value, is subject to the requirement that the lost profits must be proved with reasonable certainty.¹⁵⁹ The case also provides examples of expert testimony on gas in place market value that a court will not accept as proof to a reasonable certainty.

D. *RANCHERO ESPERANZA, LTD. V. MARATHON OIL CO.*

Ranchero Esperanza, Ltd. v. Marathon Oil Co. analyzed the related issues of standing, accrual of the cause of action, limitations, and the discovery rule in a case involving salt water surface damages caused by negligence in plugging a well.¹⁶⁰ In 1989, Marathon “plugged and abandoned Well 812.”¹⁶¹ In 1999, Marathon ceased operating and sold the property. In 2004, Ranchero Esperanza bought the surface estate and an undivided one-half interest in the Trinity Aquifer beneath the land.¹⁶² On July 20, 2008, a subsequent operator discovered salt water flowing from Well 812, apparently because the plug in Well 812 had failed and the salt water was migrating from a nearby injection well. On July 28, 2008, Ranchero Esperanza had actual knowledge of the leak. On July 27, 2010, Ranchero Esperanza filed suit asserting claims “for negligence, trespass, and nuisance.”¹⁶³

On appeal of summary judgment, there were two issues: (1) whether Ranchero Esperanza had standing to sue Marathon; and (2) if so, whether Ranchero Esperanza’s claims were barred by the statute of limitations.¹⁶⁴ In response to the limitations defense, Ranchero Esperanza invoked the discovery rule.¹⁶⁵ The El Paso Court of Appeals began the analysis by addressing Ranchero Esperanza’s standing, which is jurisdictional. There is a well established principle that “injury to land is a personal right belonging to the [landowner] at the time of injury,” and such claims do not pass to subsequent purchasers absent an express assignment of the claim.¹⁶⁶ If the cause of action accrued prior to Ranchero Esperanza’s purchase in 2004, Ranchero Esperanza would lack standing

157. *Id.* at 281–82.

158. *Id.* at 283.

159. *See id.* at 269.

160. *Ranchero Esperanza, Ltd. v. Marathon Oil Co.*, 488 S.W.3d 354 (Tex. App.—El Paso 2015, no pet.).

161. *Id.* at 356.

162. *Id.*

163. *Id.* at 357.

164. *Id.* at 356–47.

165. *Id.* at 363.

166. *Id.* at 359 (quoting *La Tierra de Simmons Familia, Ltd. v. Main Event Entm’t, LP*, No. 03-10-00503-CV, 2012 WL 753184, at *5 (Tex. App.—El Paso 2013, no pet.) (mem. op.)) (citing *Exxon Corp. v. Emerald Oil & Gas Co.*, 331 S.W.3d 419, 424 (Tex. 2010)).

because it received no assignment of claims.¹⁶⁷ Ordinarily, the time when a cause of action accrues is a question of law, and it accrues when the injury first occurs.¹⁶⁸ Marathon argued that the injury accrued in 1989 when the well was negligently plugged, and Ranchero Esperanza argued that the injury accrued in 2008 when the well first leaked salt water.¹⁶⁹ Many cases analyze when the cause of action accrues in relation to the time the defendant acted,¹⁷⁰ which are difficult to parse, but this court of appeals concluded that the one consistency is that there must be some injury, however slight.¹⁷¹ The court of appeals decided that the claims accrued in July 2008 when the surface damages first occurred.¹⁷²

The parties stipulated that all of the claims were subject to a two-year statute of limitations. Suit was filed approximately two years and a week after the cause of action accrued (when the subsequent operator first discovered the salt water leak). Ranchero Esperanza, however, did not have any actual knowledge of the leak until about a week after the leak began. Ranchero Esperanza invoked the discovery rule to toll the running of the statute of limitations for that week.¹⁷³ To negate the discovery rule, Marathon had to prove, as a matter of law, that there is “no genuine issue of material fact about when the plaintiff discovered, or in the exercise of reasonable diligence, should have discovered the nature of its injury.”¹⁷⁴ Generally, the discovery rule applies only to situations where the injury is “‘inherently undiscoverable’ and the evidence of the injury is objectively verifiable.”¹⁷⁵ The court of appeals held that the nature of the injury, that is, surface damage due to leaking salt water, is “not inherently undiscoverable.”¹⁷⁶ “Inherently undiscoverable is a legal question ‘decided on a categorical basis rather than case-specific basis,’ so surface damages arising from salt water emerging from an oil well is not inherently undiscoverable.¹⁷⁷ The discovery rule does not apply to this category of claims.¹⁷⁸ Marathon met its burden as a matter of law that the statute of limitations had expired prior to Ranchero Esperanza bringing its claims.¹⁷⁹

The significance of the case is the holding that a cause of action for a defective plug does not accrue until the plug fails, which could be many years after the well is abandoned.¹⁸⁰ A cause of action for salt water sur-

167. *Id.*

168. *Id.*

169. *Id.*

170. *Id.* at 359–63.

171. *Id.* (citing *Hous. Water-Works Co. v. Kennedy*, 8 S.W. 36, 37 (Tex. 1888)).

172. *Id.* at 361.

173. *Id.* at 364 n.9.

174. *Id.* (citing *KPMG Peat Marwick v. Harrison Cty. Hous. Fin. Corp.* 988 S.W.2d 746, 748 (Tex. 1999)).

175. *Id.* at 365 (citing *Murphy v. Campbell*, 964 S.W.2d 265, 270 (Tex. 1997); *S.V. v. R.V.*, 933 S.W.2d 1, 6–7 (Tex. 1996)).

176. *Id.*

177. *Id.* (quoting *Via Net, U.S. v. TIG Ins. Co.*, 211 S.W.3d 310, 314 (Tex. 2006)).

178. *Id.*

179. *Id.*

180. *See id.* at 363.

face damages accrues when the plug fails,¹⁸¹ and that is inherently discoverable when salt water emerges from the well.¹⁸²

VI. REGULATION ISSUES¹⁸³

A. *HOOKS v. SAMSON LONE STAR, LTD. PARTNERSHIP*

Hooks v. Samson Lone Star, Ltd. Partnership held that although reasonable diligence should lead to discovery of information in the records of the TRC, fraudulent filings in the TRC by lessee created a fact question as to whether earlier, correct filings should have been discovered by lessor in the exercise of reasonable diligence.¹⁸⁴ Hooks leased to Samson. The Hooks lease prohibited pooling and included offset obligations that triggered if a gas well was “completed within 1,320 feet of Hooks’ lease line.”¹⁸⁵ The offset obligations were to drill, release, or pay compensatory royalty. In 2000, Samson drilled a well that bottomed about 1,186 feet from Hooks’ lease line and triggered the offset obligation. Hooks and Samson agreed to amend the Hooks lease to pool the lease into a unit associated with the new well. In 2007, Hooks sued Samson for fraud and breach of contract. During the 2001 negotiations to amend the lease, Samson’s landman presented Hooks with a plat showing the well to be located outside the protected zone. Earlier, in 2000, Samson filed a similar plat with the TRC that incorrectly located the bottom hole outside the protected zone. Months before that, Samson filed another plat at the TRC that correctly located the well as within the protected zone.¹⁸⁶ There was some conflicting evidence on the meaning of each plat, but the central issue was whether reasonable diligence required Hooks to go behind the incorrect plats to find the earlier correct plat at the TRC.¹⁸⁷ The jury found that Hooks could not have discovered Samson’s fraud until 2007¹⁸⁸ and the lower court awarded Hooks a judgment for more than \$21 million in damages, attorney’s fees and post-judgment interest at a rate of 18%.¹⁸⁹

Through a series of decisions, the Texas Supreme Court has been gradually defining the effect of TRC filings upon the running of the statute of limitations and fraudulent concealment. “We have held that not all [TRC] records create constructive notice, meaning that in some circumstances,

181. *See id.* at 362.

182. *See id.* at 365.

183. Other cases dealing with regulation issues include the following: *Oneok, Inc. v. Learjet, Inc.*, 135 S. Ct. 1591 (2015) (natural gas index pricing and state antitrust claims); *Exxon Mobil Corp. v. United States*, 108 F. Supp. 3d 486 (S.D. Tex. 2015) (mem. op.) (CERCLA liability for clean up costs); *Entergy Corp. v. Jenkins*, 469 S.W.3d 330 (Tex. App.—Houston [1st Dist.] 2015, no pet.) (FERC jurisdiction).

184. *Hooks v. Samson Lone Star, Ltd. P’ship*, 457 S.W.3d 52, 55 (Tex. 2015).

185. *Id.* at 57.

186. *Id.* at 56.

187. *Id.* at 57.

188. *Id.*

189. *Id.* at 56.

[TRC] filings may exist that one is not charged with discovering.”¹⁹⁰ If TRC records do not impart constructive notice, then the issue focuses on what would be discovered in the TRC records by the exercise of reasonable diligence. The decided cases indicate that the supreme court is very reluctant to delay the accrual of a cause of action or to toll the running of limitations. “These cases reveal that when there is actual or constructive notice, or when information is ‘readily accessible and publicly available,’ then, as a matter of law, the accrual of a fraud claim is not delayed.”¹⁹¹ “Although ‘the date a cause of action accrues is normally a question of law,’ reasonable diligence is an issue of fact. Nevertheless, in some circumstances, we can still determine as a matter of law that reasonable diligence would have uncovered the wrong.”¹⁹² The supreme court then reviewed and affirmed “*BP America Production Co. v. Marshall*, 342 S.W.3d 59 (Tex. 2011) and *Shell Oil Co. v. Ross*, 356 S.W.3d 924 (Tex. 2011), where reasonable diligence required sophisticated lessors to acquaint themselves with [TRC] records.”¹⁹³ That is, the lessor is generally charged with knowledge of whatever an examination of the TRC records would reveal.

In this case, the supreme court held that the exercise of reasonable diligence was a fact question which could not be determined as a matter of law.¹⁹⁴ “The factfinder, no doubt, may consider the failure to examine older records when determining whether reasonable diligence was exercised, but their availability is not enough to establish that reasonable diligence was not exercised as a matter of law.”¹⁹⁵ “[H]ere the records themselves were tainted by fraud and thus provide no conclusive proof on the subject.”¹⁹⁶ The opinion does not hold that a lessor is relieved of the duty to review all TRC records in its exercise of reasonable diligence: “We hold that when the defendant’s fraudulent misrepresentations extend to the [TRC] record itself, earlier inconsistent filings cannot be used to establish, as a matter of law, reasonable diligence was not exercised. Under these circumstances, reasonable diligence remains a fact question.”¹⁹⁷

Hooks also claimed that Samson breached the contract under the most-favored-nations clause in the Hooks lease.¹⁹⁸ Samson originally “leased a qualifying oil and gas interest from the State [of Texas] at the same 25% royalty [it] paid Hooks.”¹⁹⁹ “[T]o induce the State to consent to a Pooling Agreement, Samson increased the State’s” share of production from the pooled unit so that the State was effectively receiving a 28.28896% roy-

190. *Id.* at 60 (citing *HECI Exploration Co. v. Neel*, 982 S.W.2d 881, 886 (Tex. 1998)).

191. *Id.* at 59 (quoting *Shell Oil Co. v. Ross*, 356 S.W.3d 924, 929 (Tex. 2011)).

192. *Id.* at 57–58 (internal citations omitted).

193. *Id.* at 57–59.

194. *Id.* at 61.

195. *Id.*

196. *Id.* at 55.

197. *Id.* at 61.

198. *Id.* at 63.

199. *Id.* at 62.

alty on the State's tract.²⁰⁰ Samson argued that this did not increase the royalty under the State's lease.²⁰¹ Reasoning that "royalty owed on production from the whole unit is necessarily tied to royalty owed on production from the lessor's individual tracts," the supreme court ruled that the later pooling agreement, which allocated a unit royalty interest to the State, resulted in a higher royalty payment on the State's tract.²⁰² Therefore, Samson was obligated to match this amount when paying royalties to Hooks, and its failure to do so was a breach.²⁰³

Hooks also had two more leases with Samson which contained similar offset obligations (drill, release, or compensatory royalty). Hooks argued that the duty to pay compensatory royalty was a recurring obligation and that Hooks could recover beginning with the payment due four years before suit was filed.²⁰⁴ Samson argued that even if the failure to pay compensatory royalties was recurring, which would bring the claim within the limitations period, the leases authorized Samson to elect non-recurring options, such as to release or drill, and a breach of these provisions would be barred.²⁰⁵ The supreme court noted that payment of compensatory royalties was to take place after the first two options, and therefore, "Samson impliedly elected to perform the later one" because "it would not be just to allow the obligor's silent, continuous breach to constitute an election of the non-recurring alternative."²⁰⁶

The case affirms that TRC records are not constructive notice, but that a lessor (or at least a sophisticated lessor) is generally subject to whatever would be discovered from a review of the TRC records.²⁰⁷ A court will hold, as a matter of law, that the lessor knew whatever those records contain.²⁰⁸ The significance of this case is that fraudulent filings make it a question of fact whether earlier, correct filings should have been discovered.²⁰⁹

B. *ROLAND OIL CO. v. R.R. COMMISSION OF TEXAS*

Roland Oil Co. v. R.R. Commission of Texas held that an operator did not establish a good faith claim to a continuing right to operate a lease under the rules of the TRC.²¹⁰ Beginning in 1994, Roland Oil Company (Roland) operated the North Charlotte Field Unit Lease in Atascosa County, Texas. The lease consisted of thirty-one wells drilled as far back as the 1950s. In 2005, Roland asked the TRC "for an extension of time to

200. *Id.*

201. *Id.*

202. *Id.* at 63.

203. *Id.*

204. *Id.* at 66–67.

205. *Id.* at 67–68.

206. *Id.* at 68.

207. *See id.* at 60.

208. *See id.*

209. *See id.*

210. *Roland Oil Co. v. R.R. Comm'n of Tex.*, No. 03-12-00247-CV, 2015 WL 870232, at *1 (Tex. App.—Austin Feb. 27, 2015, no pet.) (mem. op.).

complete the required testing on certain inactive wells” that was required to be completed before the wells could be plugged under Texas Administrative Code § 3.14(b)(2)–(3).²¹¹ “[T]he [TRC] determined that Roland had been delinquent on the required testing since 1994,” denied Roland’s request, and “issued a February 2005 ‘severance’ order [that] effectively bar[red] Roland from producing [any] well on the Lease.”²¹² Roland ceased producing from May 2005 to August 2006 (fifteen months), when it finally completed the repairs necessary for the testing, and the TRC then lifted the severance and granted the extension of time to plug.²¹³ However, “in June 2006, a mineral owner under the Lease had alerted the [TRC] to [the mineral owner’s] contention that the Lease had lapsed during the period of non-production.”²¹⁴

Under the TRC’s rules, the TRC could grant an extension to plug only if the operator has a good faith claim to a continuing right to operate the well. “A ‘good faith claim’ in this context is defined as a ‘factually supported claim based on a recognized legal theory to a continuing possessory right in a mineral estate, such as evidence of a currently valid oil and gas lease or a recorded deed conveying a fee interest in the mineral estate.’”²¹⁵ “[The TRC] notified Roland of the mineral owner’s assertion, . . . asked Roland to provide evidence of its good faith claim to operate the [lease],” and indicated that its “failure to do so would result in cancellation of” the extension to plug.²¹⁶ Roland asserted that the repair and testing activities were unit operations under the Unit Agreement, and therefore Roland’s lease had not lapsed.²¹⁷ Alternatively, Roland argued that the TRC’s “severance order had triggered the . . . force majeure clause and suspended its obligation to conduct ‘Unit Operations.’”²¹⁸ The TRC cancelled the plugging extensions.²¹⁹

The term of the Unit Agreement continued for so long as there were Unit Operations without a cessation of more than ninety days.²²⁰ The Unit Agreement defined Unit Operations as “all operations conducted . . . pursuant to this agreement . . . for or on account of the development and operation of the Unitized Formation for the production of Unitized Substances.”²²¹ Roland contended that work done on inactive wells was Unit Operations. The Austin Court of Appeals disagreed and held that the required operations must be for production and that work done in preparation for plugging was not for production.²²² Therefore, “the

211. *Id.* at *1–2.

212. *Id.* at *2.

213. *Id.*

214. *Id.* at *1–2.

215. *Id.* at *2. (quoting former 16 TEX. ADMIN. CODE § 3.14(a)(1)(E) (2014)).

216. *Id.*

217. *Id.*

218. *Id.* at *7.

219. *Id.* at *3.

220. *Id.* at *7.

221. *Id.*

222. *Id.*

[TRC's] legal conclusion regarding the meaning of 'operations' was not in error."²²³ "[T]he work in question was performed on inactive wells to comply with the former Commission Rule 3.14," to prepare for the plugging of those inactive wells, and "those inactive wells remained inactive after the required testing."²²⁴ Therefore, Roland's work "did not constitute good faith [effort] to produce oil and gas."²²⁵

There must be some reasonable basis in the record to support the TRC's finding that the only work done between May 2005 and August 2006 was done to *inactive* wells.²²⁶ Though there was testimony by Roland's principal as to various other work and maintenance that went on at the lease during the gap in production ("i.e., 'constant' maintenance work, including flow-line and electrical repairs, monitoring for leaks, inspecting roads, fixing pumps, and mowing the grass"), the evidence did "not specify when this work was done, how often it was performed or whether it was performed on any . . . active wells."²²⁷ Under the substantial evidence rule, there was a reasonable basis in the record to support the agency's finding.²²⁸

If the repair and testing activities were found to trigger the force majeure clause, then Roland's obligations under the Unit Agreement would be suspended.²²⁹ The Unit Agreement's force majeure provision stated that "[a]ll obligations imposed by this agreement . . . shall be suspended while compliance is prevented, in whole or in part by . . . order of a governmental agency . . . or by any other cause or causes beyond reasonable control of the party."²³⁰ The provision used the phrase "force majeure" twice and it incorporated the common force majeure concept of listing events beyond the parties' control and then including a catchall "other" category.²³¹ A reasonable construction of this force majeure clause is that the catchall "by any other cause or causes beyond reasonable control of the party" must be read in context of the other listed events.²³² The inclusion of "other" was an expression of intent by the drafters of the Unit Agreement that the force majeure clause be triggered by events or orders beyond the reasonable control of the party.²³³ "[T]he [TRC's] order of severance . . . was within the reasonable control of Roland."²³⁴

This is an administrative appeal which bears only upon the TRC's determination and the implications it may have on future matters requiring

223. *Id.*

224. *Id.* at *8.

225. *Id.*

226. *Id.*

227. *Id.*

228. *Id.*

229. *Id.* at *4-5.

230. *Id.* at *5 (emphasis in original).

231. *Id.*

232. *Id.* at *5-6 (emphasis removed).

233. *Id.* at *6.

234. *Id.*

a showing of a good faith claim to a continuing right to operate a well.²³⁵ It is not a decision that determines or creates “title or a right to possession.”²³⁶ The significance of the case is limited to those regulatory matters.²³⁷

C. ETC MARKETING, LTD. v. HARRIS COUNTY APPRAISAL DISTRICT

ETC Marketing, Ltd. v. Harris County Appraisal District held that natural gas stored in Texas for future transportation and sale in interstate commerce was subject to ad valorem taxation in Texas.²³⁸ ETC Marketing, Ltd. (ETC), a natural gas marketer, conducted business in Texas and had multiple employees and offices there. Its purpose was to buy and sell natural gas in the interstate market. ETC bought principally from the “Katy Hub,” a central delivery and distribution point for natural gas in and out of Texas, and sold to out of state customers. ETC immediately entrusted gas it purchased to its affiliate Houston Pipeline Company (Houston), an intrastate pipeline company located wholly in Texas. Houston stored ETC’s gas for up to several months in the Bammel reservoir, which Houston owned in Harris County, Texas. This allowed ETC to market and sell the gas at a more financially advantageous time. All gas from ETC and others, both in the pipeline and in storage, is commingled and segregated only by paper allocations. Houston paid ad valorem taxes on the equipment and property it owned in Harris County, including that related to the Bammel reservoir. In 2010, the Harris County Appraisal District (HCAD) appraised natural gas ETC had purchased at the Katy Hub and stored with Houston in the Bammel reservoir and assessed ETC ad valorem taxes.²³⁹ ETC challenged the assessment arguing that the stored gas was in interstate commerce and exempt from state ad valorem taxation.²⁴⁰

The U.S. Supreme Court interpreted the Commerce Clause,²⁴¹ which governs the power to regulate interstate commerce, “to include a ‘dormant’ Commerce Clause” that implicitly prohibits “a state’s imposition of discriminatory burdens on interstate commerce.”²⁴² It “does not relieve those engaged in interstate commerce” from sharing the state tax burden for services the state provides.²⁴³ To prove a tax invalid under the Dormant Commerce Clause, a taxpayer must demonstrate that the taxed ac-

235. *See id.* at *1.

236. *See id.* at *2 n.6.

237. *See id.*

238. *ETC Mktg., Ltd. v. Harris Cty. Appraisal Dist.*, 476 S.W.3d 501 (Tex. App.—Houston [1st Dist.] 2015, pet. filed).

239. *Id.* at 504–06.

240. *Id.* at 506, 513; *see also id.* at 508 (For purposes of its opinion, the court of appeals “assume[d] without deciding that the natural gas at issue [was] in the stream of interstate commerce”—ETC’s primary argument throughout the course of the case.).

241. U.S. CONST. art. I, § 8, cl. 3.

242. *ETC Marketing, Ltd.*, 476 S.W.3d at 507 (citing *Am. Trucking Ass’ns, Inc. v. Mich. Pub. Servs. Comm’n*, 545 U.S. 429, 433 (2005)).

243. *Id.* at 508 (citing *W. Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938)).

tivity “lack[s] a substantial nexus to the taxing state; . . . is not fairly apportioned; . . . discriminates against interstate commerce; or . . . is not fairly related to the services provided by the State.”²⁴⁴

Despite ETC’s argument that there was no substantial nexus between the activity to which the tax applied and the taxing state, the First Houston Court of Appeals identified many factors in support of its holding that there was a substantial nexus between ETC’s natural gas in the Bammel reservoir and the state of Texas.²⁴⁵ ETC had multiple offices and employees in Texas. It purchased the gas in Texas, transported it through an intrastate pipeline company located wholly within the state, made the decision to store it in Texas, admitted to owning the gas at the time and place of appraisal,²⁴⁶ deliberately stored it in Harris County for months at a time for its own business purposes, had the right to sell it wherever it wished, and had not already designated it for transport to another state.²⁴⁷

The court of appeals held that the tax was fairly apportioned.²⁴⁸ The Texas Tax Code taxed only the tangible personal property stored in the jurisdiction of the taxing entity beyond a temporary period. The tax was “internally consistent” in that it would not result in multiple taxation to an entity taxed in another state under an identical statute (because it only taxed gas in storage in Texas on a particular date).²⁴⁹ It was “externally consistent” in that it taxed only that portion of revenue from interstate activity reflecting the in-state component of the activity taxed.²⁵⁰

The court of appeals held the tax did not discriminate against interstate commerce.²⁵¹ The tax was imposed only on the quantity of gas stored in Harris County, which ETC acknowledged it owned on the date of taxation. The tax placed no burden on interstate commerce that was not placed on comparable competing intrastate commerce.²⁵² There was no

244. *Id.* (quoting *Barclays Bank PLC v. Franchise Tax Bd. of Cal.*, 512 U.S. 298, 310–11 (1994)).

245. *See id.* at 508–09.

246. *Id.* at 505 n.3 (ETC had alleged in its original petition that it owned property within HCAD’s jurisdiction and specifically defined property to include “Bammel Working Gas.”); *see also e.g., id.* at 506–11 (making frequent reference to this admission as a fact in holding ETC liable for the taxes as assessed).

247. *See id.* at 509–10 (distinguishing *Peoples Gas, Light, & Coke Co. v. Harrison Cent. Appraisal Dist.*, 270 S.W.3d 208 (Tex. App.—Texarkana 2008, pet. denied), because “Peoples Gas had no physical facilities, employees, representatives, or customers in Texas”); *id.* at 510 (distinguishing *Midland Central Appraisal District v. BP America Production Co.*, 282 S.W.3d 215 (Tex. App.—Eastland 2009, pet. denied), because in *Midland*, oil passing through interstate pipeline was held temporarily in a Texas tank, but not for any business purpose of owner); *see also id.* (dismissing ETC’s contention that physical presence does not satisfy the substantial nexus test in ad valorem cases).

248. *Id.* at 512.

249. *Id.* at 511.

250. *Id.* at 511–12 (The court of appeals, relying on ETC’s admission of ownership, dismissed the “argument that the tax was externally inconsistent” because the properties of gas and gas transportation make it impossible to identify the particular gas molecules at issue as being the same gas bought and stored in Texas.).

251. *Id.*

252. *Id.*

evidence that the “taxes were selectively imposed on interstate commerce or that the rates” or procedures were more onerous than for property not in interstate commerce.²⁵³

ETC argued that the tax did not fairly relate to any services provided by the state, because Houston paid ad valorem taxes on the Bammel reservoir and had control over the activity taxed. The court of appeals held that ETC “retained control over the disposition of the gas for its own business purposes.”²⁵⁴ It also found that services such as “police and fire protection . . . [and] State’s maintenance of a civilized society are justifications enough for the imposition of a tax,” and both the owner of the gas and the pipeline company benefited from state provided services.²⁵⁵ Therefore, the tax was “fairly related to services provided” within the state.²⁵⁶

“Under the Tax Code, unless exempt by law, tangible personal property is taxable if it is located in the taxing unit ‘for longer than a temporary period.’”²⁵⁷ The significance of the case is the holding that gas destined for the interstate market, but held in storage for several months in Texas before a sale into the interstate market, is subject to Texas ad valorem tax.²⁵⁸

D. *UNITED STATES V. CITGO PETROLEUM CORP.*

United States v. CITGO Petroleum Corp. held that uncovered wastewater treatment tanks resulting in dead birds was not a criminal violation of either the Clean Air Act or the Migratory Bird Treaty Act.²⁵⁹ Oil refinery wastewater treatment systems may “emit dangerous levels of volatile organic compounds (‘VOCs’).”²⁶⁰ Wastewater is collected through a series of lateral sewers and treated at multiple stages designed to separate the oil from the wastewater and to treat the water before release. The first stage is called an oil-water separator. The oil-water separator causes oils and solids to separate from the water, allowing between 50% to 99% of the oils and solids to be skimmed away. After passing through the oil-water separator, the wastewater is allowed to pool in equalization tanks that act as a holding system for wastewater to control the flow to the other downstream treatment processes. While in the equalization tanks, gases are pumped into the wastewater to generate bubbles, which attach to oils in the wastewater, allowing more oil to be skimmed off and recycled. The wastewater then flows through biological treatment and a clarifier before being released. CITGO’s oil-water separators had roofs,

253. *Id.*

254. *Id.* at 513.

255. *Id.* (quoting *Okla. Tax. Comm’n v. Jefferson Lines, Inc.*, 514 U.S. 175, 200 (1995)).

256. *Id.*

257. *Id.* at 507 (quoting *TEX. TAX CODE Ann.* § 11.12 (West 2015)); *see also id.* at 507 n.6.

258. *See id.* at 513.

259. *United States v. CITGO Petroleum Corp.*, 801 F.3d 477, 483–84 (5th Cir. 2015).

260. *Id.* at 479.

but the equalization tanks did not. An inspection revealed 130,000 barrels of oil floating on the top of the equalization tanks and the remains of five pelicans and several dozen ducks.²⁶¹

The Clean Air Act requires oil-water separators to have roofs.²⁶² Subpart QQQ of the regulations (Subpart QQQ) defines an oil-water separator as wastewater treatment equipment:

[U]sed to separate oil from water consisting of a separation tank, which also includes the forebay and other separator basins, skimmers, weirs, grit chambers, and sludge hoppers. Slop oil facilities, including tanks, are included in this term along with storage vessels and auxiliary equipment located between individual drain systems and the oil-water separator. This term does not include storage vessels or auxiliary equipment which do not come in contact with or store oily wastewater.²⁶³

Inspectors determined that CITGO was utilizing the equalization tanks as oil-water separators and cited CITGO for failing to have roofs on the equalization tanks.²⁶⁴ The issue was whether an equalization tank can be an oil-water separator.²⁶⁵

The EPA argued that equipment “used to separate oil from water” included the equalization tanks (an argument that the Fifth Circuit said would include the whole wastewater treatment process). The U.S. Court of Appeals for the Fifth Circuit focused on a plain reading of the definition of oil-water separator and concluded that the regulation was not directed solely at the process but at the process and specific equipment.²⁶⁶ Specifically, the Fifth Circuit stated that “[t]he relative pronoun ‘which’ refers to the noun immediately preceding it—‘separation tank.’”²⁶⁷ In other words, the definition of an oil-water separator includes all of the spaces in which separation occurs, and thus all components of the oil-water separator (forebay, separation tank, outlet basin) must be covered, but not the equalization tanks.²⁶⁸

The Fifth Circuit bolsters its conclusion by pointing out that Subpart Kb of the Clean Air Act (Subpart Kb)²⁶⁹ governs the operation of storage vessels used in the wastewater treatment process, requiring them to have roofs, if they emit VOCs above a certain threshold.²⁷⁰ Interpreting Subpart QQQ to include equalization tanks would be to eliminate the force of Subpart Kb’s vapor pressure trigger.²⁷¹

261. *Id.* at 480 n.4.

262. *Id.* at 480.

263. *Id.* at 482 (quoting 40 C.F.R. § 60.691 (2015)).

264. *Id.* at 480.

265. *Id.* at 481.

266. *Id.* at 481, 485–86.

267. *Id.* 484.

268. *Id.*

269. *Id.* at 485 (citing 40 C.F.R. § 60.692–3(d) (2015)).

270. *Id.* (citing 40 C.F.R. §§ 60.110b(a), 60.112b(a)).

271. *Id.* at 485–86.

The Migratory Bird Treaty Act of 1918 “makes it ‘unlawful at any time, by any means or in any manner, to pursue, hunt, take, capture, kill, attempt to take, capture or kill . . . any migratory bird,’ in violation of regulations and permits.”²⁷² “The act imposes strict liability on violators, punishable by a maximum \$15,000 fine and six months imprisonment.”²⁷³ “CITGO was indicted for ‘taking’ . . . [the] birds, not for ‘killing’ them.”²⁷⁴ The Fifth Circuit compared numerous cases and analyzed the split in opinion among the circuit courts. Generally, the Second and Tenth Circuits hold oilfield equipment operators guilty when birds die as a result of operations. The Eighth and Ninth Circuits do not. In this case, the Fifth Circuit joined the latter and held “that a ‘taking’ is limited to deliberate acts done directly and intentionally to migratory birds.”²⁷⁵

The Fifth Circuit reasoned that to take or to kill migratory birds required some affirmative action.²⁷⁶ The Fifth Circuit cited various sources to note that despite the Migratory Bird Act protecting approximately 836 species of birds, each year, as many as 976 million birds are killed flying into windows, 60 million birds are killed by cars, and, just in Wisconsin, 39 million birds are killed by domesticated cats.²⁷⁷ According to the Fifth Circuit, it would be absurd to conclude that Congress intended for someone to pay \$15,000 and serve six months for each of those deaths.²⁷⁸

The significance of the case is the holding in the Fifth Circuit that “illegally ‘taking’ migratory birds involves only ‘conduct intentionally directed at birds, such as hunting and trapping, not [] commercial activity that unintentionally and indirectly causes’ migratory bird deaths.”²⁷⁹ The rejection of the EPA’s expansion of the obligation to enclose tanks is mostly significant as a strict reading of an existing regulation, which the EPA has the power to amend and expand.²⁸⁰

VII. CONCLUSION

Given that the production of oil in the United States has approximately doubled since 2005, it is not surprising that the number of reported oil and gas cases in a given year has also approximately doubled. Because we have been on the up side of the commodity cycle and have been experiencing a broad expansion of exploration and development, reported cases have been concentrated on issues commonly arising with those activities. We have seen a number of cases on the nature and scope of a proceeding in trespass to try title, categorical limitations of the scope of the discovery rule, and clarification of the notice provided by public

272. *Id.* at 488 (citing 16 U.S.C. §§ 703(a), § 704(a) (2012)).

273. *Id.* (citing 16 U.S.C. § 707(a)).

274. *Id.* at 489.

275. *Id.* at 488–93.

276. *Id.* at 492.

277. *Id.* at 493–94.

278. *Id.*

279. *See id.* 488, 494.

280. *See id.* at 483–84.

records not included in the deed records. These are generally conveyancing, lease and leasing cases.

More recently, there has been an increase in cases dealing with operational issues, such as condemnation, easements, surface damages, trespass, subsurface and particulate trespass, and issues and disputes arising under industry contracts, such as exploration agreements, operating agreements, drilling contracts, and insurance contracts. Litigation over the scope and meaning of purchase and sale agreements was focused on what was conveyed, but it is now shifting toward representations, warranties, indemnities, and exclusions.

Most recently, there is an uptick in cases involving liens, security interests, and bankruptcy, which can be expected to accelerate. There has been a steady stream of lease termination cases driven by the dramatic increase in bonus payments. The downturn in commodity prices will reduce those bonus payments, but lessees will struggle to produce their wells in paying quantities, so lease termination cases are likely to continue. The midstream sector has also been aggressively expanding, and those projects tend to be long term and many will continue to fill in the gaps in the infrastructure. We will probably see more cases on condemnation, easements, surface damages, and nuisance.

With over 100 years of oil and gas case law in Texas, the direction of oil and gas jurisprudence is generally evolutionary, not revolutionary. Lawyers and judges are usually knowledgeable, and most cases add something useful in the quest to perfect that jurisprudence.

