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## Oil, Gas and Mineral Law

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# OIL, GAS AND MINERAL LAW

Richard F. Brown\*

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## I. INTRODUCTION

**T**HIS Article focuses on the interpretations of, and changes relating to, oil, gas and mineral law in Texas from October 1, 1997 through September 30, 1998. The cases examined include decisions of courts of the State of Texas and the Fifth Circuit Court of Appeals.<sup>1</sup>

## II. CONVEYANCING ISSUES

*Concord Oil Company v. Pennzoil Exploration and Petroleum Company*<sup>2</sup> is a recent troublesome “two-grant” deed case which again divides the court as it struggles to deal with this difficult line of cases.<sup>3</sup> In a 1937 deed, the grantor, who owned a 1/12th mineral interest in land subject to a producing oil and gas lease, conveyed to grantee:

[a]n undivided one-ninety sixth (1/96) interest in and to all of the oil, gas and other minerals in and under, and that may be produced from . . . [the land]. . . together with all rights . . . necessary . . . to the full use and enjoyment of such estate herein conveyed . . . . While the estate hereby conveyed does not depend upon the validity thereof, neither shall it be affected by the termination thereof, this conveyance is made subject to the terms of any valid subsisting oil, gas and/or mineral lease or mineral lease or leases on above described land or any part thereof, but covers and includes one-twelfth (1/12) of all rentals and royalty of every kind and character that may be payable by the terms of such lease or leases insofar as the same

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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 in this Survey.

2. 966 S.W.2d 451 (Tex. 1998).

3. See, e.g., *Jupiter Oil Co. v. Snow*, 819 S.W.2d 466 (Tex. 1991); *Luckel v. White*, 819 S.W.2d 459 (Tex. 1991); *Garrett v. Dils Co.*, 157 Tex. 92, 299 S.W.2d 904 (1957); *Tipps v. Bodine*, 101 S.W.2d 1076 (Tex. Civ. App.—Texarkana 1937, writ ref’d).

pertain to the above described land, or any part thereof.<sup>4</sup>  
The 1937 deed did not contain an express future lease clause.

In a 1961 warranty deed, the same grantor purported to convey a 7/96 mineral interest that was eventually acquired by Pennzoil. Concord, as successor to the grantee in the 1937 deed, filed suit against Pennzoil asserting that the 1937 deed conveyed all of the grantor's 1/12 mineral interest in the land.<sup>5</sup> A holding that the 1937 deed conveyed all of the 1/12 mineral interest, rather than the 1/96 mineral interest specified in the granting clause, would wipe out all of Pennzoil's interest derived from the 1961 deed.

The majority opinion (Justices Owen, Phillips, Hecht and Abbott) reversed the judgment for Pennzoil and rendered judgment for Concord.<sup>6</sup> The court heavily emphasized the "four corners" rule and the harmonizing canon of construction in construing the parties' intention from the conveyance "in its entirety."<sup>7</sup> The court read its recent decision in *Luckel v. White*<sup>8</sup> as identifying "a unifying principle: the entire document must be examined to glean the parties' intent."<sup>9</sup> Moreover, the "conveyance must be considered as a whole to determine the intent of the parties and that seemingly conflicting provisions are to be harmonized if possible."<sup>10</sup>

Nevertheless, the majority opinion seems to be focused on the reference to a single "estate" in the granting clause of the 1937 deed in concluding that the grant conveyed a single, simultaneous 1/12 unified mineral interest subject to the existing lease, which included 1/12 of royalties and delay rentals under both existing and future leases, and a 1/12 interest in the possibility of reverter in the minerals.<sup>11</sup> The court concluded that the grantor's intent was to convey a single estate, and that it need only determine the size and character of that single estate.<sup>12</sup> Because the intent was to convey a single estate, the court concluded that the quantum of interest conveyed was the greater interest—1/12 instead of 1/96.<sup>13</sup> Finally, the court concluded that the nature of the interest conveyed was a mineral interest rather than a royalty interest because the granting clause contained all of the classic language used in granting an interest in minerals.<sup>14</sup>

Once again the court refused to adopt a "bright-line" rule of construction for construing mineral and royalty conveyances that contain differing fractions. The principles adopted by the court are intended to give effect

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4. *Concord Oil Co.*, 966 S.W.2d at 453.

5. *See id.*

6. *See id.* at 463.

7. *See id.* at 454.

8. 819 S.W.2d 459 (Tex. 1991).

9. *Concord Oil Co.*, 966 S.W.2d at 454 (citing *Luckel*, 819 S.W.2d at 462).

10. *Id.* at 457.

11. *See id.* at 457-58.

12. *See id.* at 458.

13. *See id.* at 459.

14. *See id.* (Mineral interest rights include rights to possess, drill, lay pipeline, build tanks, etc.)

to the intent of the parties as actually expressed within the four corners of the conveyance and to "harmonize" provisions that appear to conflict.<sup>15</sup> This is little comfort to the title examiner who must somehow translate the cacophony of poorly drafted deeds and discordant judicial opinions into "harmony," while poring over some dusty deed records in the corner of the County Clerk's office. The dissent stated: "The Court's opinion promotes ad-hoc analysis of every mineral deed and wreaks havoc on title stability."<sup>16</sup>

Justice Enoch provided the swing vote. He agreed with the plurality that the deed could not reasonably be interpreted as conveying two estates.<sup>17</sup> In his opinion, however, the majority relied on an improper pre-supposition that grantors typically intend to convey only one estate and that the subsequent clause in this deed includes future leases.<sup>18</sup> The dissent would be correct in construing the deed as a two-grant deed, except that in his view, had the granting clause and the subsequent clause each conveyed separate "estates," an overconveyance and an unavoidable conflict would result. If there were two grants, then 9/96 would be conveyed under the then-current lease.<sup>19</sup> Construing the deed as a non-simultaneous grant would be unreasonable and contrary to the language of both clauses.<sup>20</sup>

The dissenting opinion (Justices Gonzales, Spector, Baker and Hankinson) would hold that the deed unambiguously conveys two estates of different sizes and durations: 1/96th interest in the mineral fee and a 1/12 interest in rentals and royalties that terminated when the existing lease terminated.<sup>21</sup> There is no overconveyance because the 1/12 interest is in royalty from an existing lease and the 1/96 interest is in the possibility of reverter. The right to royalty from subsisting leases and the possibility of reverter are separate interests which should not be added together.<sup>22</sup> There is no irreconcilable conflict just because two fractions appear in the deed. The dissent contends that its construction avoids the assumption made by the majority that the grantor meant to convey 1/12 when grantor wrote 1/96.<sup>23</sup>

In a case of first impression, *Ely v. Briley*<sup>24</sup> holds that a constructively severed riparian mineral interest is subject to the doctrine of accretion.<sup>25</sup> Accretion is the result of a river gradually changing its course over time so that a tract described as bounded by the river increases in size. Texas recognizes the doctrine of accretion under which the owner of riparian

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15. *Id.* at 461.

16. *Id.* at 467.

17. *See id.* at 463.

18. *See id.*

19. *See id.* at 464.

20. *See id.* at 465.

21. *See id.*

22. *See id.* at 467.

23. *See id.*

24. 959 S.W.2d 723 (Tex. App.—Austin 1998, no pet.).

25. *See id.* at 726.

land gains title to land that accretes to his property.<sup>26</sup> In this case the tract of land had been described since 1879 as having one boundary going to the Brazos river and up the river with its meanders. In a 1947 deed, grantor reserved "an undivided one-half (1/2) interest in and to all of the oil, gas and other mineral [sic] in and under the herein described property."<sup>27</sup> After 1947, the conveyed tract increased in size by approximately 266 acres by accretion.<sup>28</sup>

Successors to the grantee claimed that under the deed of severance the grantee was entitled to all royalties from the 266 acres added by accretion because (1) a severed riparian mineral interest was not subject to accretion, or alternatively, and (2) the deed of severance limited grantor's reserved mineral interest to the boundaries as they existed in 1947 by the language used in the deed ("in and under the herein described property").<sup>29</sup> The court noted that under Texas law, a mineral interest is a property interest regardless of whether or not the mineral estate is severed from the surface estate. Holding that severed minerals are subject to the law of accretion the same as the surface estate is supported by the practical consideration that the location of original mineral boundaries is often undeterminable.<sup>30</sup> The holding follows other jurisdictions that have considered the issue.<sup>31</sup>

This holding applies regardless of the language in the reservation in the 1947 deed, which used the words "in and under the herein described property." Those words were used as words of description and not of limitation.<sup>32</sup> An unqualified reservation of the mineral estate reserves the entire bundle of property rights which comprise the mineral estate, such as the rights to lease and to receive bonus, rentals and royalties.<sup>33</sup> The 1947 deed reserved all rights to the mineral estate; the right to increase by accretion is part of the bundle of riparian property rights, and therefore an unqualified reservation of the riparian mineral estate reserves the right to future accretion.<sup>34</sup>

*Lee M. Bass, Inc. v. Shell Western E & P, Inc.*<sup>35</sup> reviews a lease clause that provided lessee would reimburse lessor for "all production, severance, gathering, sales, excise and similar taxes imposed upon or assessed with respect to or measured by or charged against the production or value of production or proceeds of the sale of production attributable to Lessor's royalty interest."<sup>36</sup> The lessor contended that the lessee should

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26. *See id.*

27. *Id.* at 725.

28. *See id.*

29. *See id.* at 725-26.

30. *See id.* at 726.

31. *See, e.g.,* Nilsen v. Tenneco Oil Co., 614 P.2d 36 (Okla. 1980); Jackson v. Burlington Northern, Inc., 667 P.2d 406 (Mont. 1983).

32. *See Ely*, 959 S.W.2d at 727.

33. *See id.*

34. *See id.*

35. 957 S.W.2d 159 (Tex. App.—San Antonio 1997, no pet.).

36. *Id.* at 160.

reimburse the lessor for ad valorem taxes assessed against the royalty interest.

The court held that reimbursement was not required because ad valorem taxes existed at the time the lease was executed, and if the parties intended to include ad valorem taxes then ad valorem taxes should have been listed.<sup>37</sup> Moreover, the court reasoned that ad valorem taxes are not "similar taxes" within the meaning of the lease. The "value of production" refers to oil and gas that has actually been severed from the ground. Ad valorem taxes are assessed against minerals still in the ground, not on production.<sup>38</sup>

It is unusual for language such as this to be in an oil and gas lease, so that the decision is not likely to affect many leases. However, it is quite common for conveyances of overriding royalty to expressly place the burden of paying certain taxes on either the owner of the overriding royalty or on the owner of the working interest. The significance of this case may be more important in its effect on the construction of the language creating various overriding royalty interests in which there is a list of taxes followed by a dragnet clause, such as "and other similar taxes assessed against the *value of production*."

*Riley v. Riley*<sup>39</sup> reviews homestead rights in oil and gas production and the applicability of the open mine doctrine. At the time Elbert and Bobbie Riley were married, Elbert Riley owned as separate property the Home Place (160 acres) and the River Place (74.7 acres). The Rileys lived on the Home Place throughout their marriage, and the widow Bobbie continued to live there after Elbert's death. The Rileys farmed and ranched all of the property during their marriage for part of their support. There was also oil and gas production from the River Place.<sup>40</sup>

Bobbie Riley was rightfully entitled to claim 200 acres as her homestead because during their marriage Elbert and Bobbie were entitled to claim a rural homestead of 200 acres on Elbert Riley's separate property. The surviving spouse has the same homestead right in the property as both spouses had prior to the death of one spouse.<sup>41</sup>

Bobbie Riley claimed a homestead in 140 acres of the Home Place and 59.7 acres of the River Place, including the production of oil and gas. The first issue considered was whether Bobbie Riley could designate less than all of the Home Place so that she could also designate 59.7 mineral-rich acres in the River Place. The designation was upheld because a homestead designation may exclude part of a tract actually occupied to obtain acreage in another tract when the evidence shows that the properties were used in such a manner as to establish homestead rights in the properties.<sup>42</sup>

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37. See *id.* at 161.

38. See *id.* at 162 & n.4.

39. 972 S.W.2d 149 (Tex. App.—Texarkana 1998, no pet. h.).

40. See *id.* at 151.

41. See *id.* at 154.

42. See *id.*

The parties also contested the right to royalties from the date of Elbert's death until the conveyance of the properties out of the estate. Under the open mine doctrine, a homestead claimant is entitled to receive and expend all royalties from the homestead, when the homestead was producing oil or gas when the right in the property came into existence.<sup>43</sup> Because the 59.7 acres in the River Place were producing and included in the homestead designation, Bobbie Riley was held entitled to those royalties.<sup>44</sup> As to the other 15 acres in the River Place, the case was remanded because the record was not fully developed.<sup>45</sup>

### III. OIL, GAS AND MINERAL LEASES

*Horizon Resources, Inc. v. Putnam*<sup>46</sup> determined whether an overriding royalty payable to the lessor and included in an attached addendum to a printed lease form is subject to the proportionate reduction clause found in the printed lease form. The printed lease form included a typical royalty clause, and it also included a proportionate reduction clause which provided:

[I]t is agreed that if this lease covers a less interest in the oil, gas, sulphur, or other minerals in all or any part of said land than the entire and undivided fee simple estate . . . then the royalties, delay rental and other monies accruing from any part as to which this lease covers less than such full interest, shall be paid only in the proportion which the interest therein, if any, covered by this lease, bears to the whole and undivided fee simple estate therein.<sup>47</sup>

The clause adding an overriding royalty in the addendum provided: "As additional bonus for the making of this lease, LESSOR shall receive an overriding two-thirty fifths (2/35) royalty in all oil, gas, liquid hydrocarbon and sulphur associated with their production, produced from these leased premises."<sup>48</sup>

A portion of the leased premises in which the lessor owned a 50% interest was pooled into a producing unit. Lessor signed division orders in which the overriding royalty was proportionately reduced, and lessor accepted reduced payments for more than two years. Lessor then filed suit to recover the underpaid overriding royalty, and lessor and lessee filed cross motions for summary judgment.<sup>49</sup>

The court held that the overriding royalty was subject to proportionate reduction and relied heavily upon *McMahon v. Christmann*<sup>50</sup> and *Newport Oil Co. v. Lamb*,<sup>51</sup> which were based on similar facts. In *McMahon*,

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43. See *id.* at 155.

44. See *id.*

45. See *id.* at 156.

46. 976 S.W.2d 268 (Tex. App.—Corpus Christi 1998, no pet. h.).

47. *Id.* at 269.

48. *Id.*

49. See *id.* at 270.

50. 157 Tex. 403, 303 S.W.2d 341 (1957).

51. 352 S.W.2d 861 (Tex. Civ. App.—Eastland 1962, no writ).

the overriding royalty was held to be free from reduction, primarily because the language in the addendum creating the overriding royalty recited that it was to be "without reduction."<sup>52</sup> In *Newport*, there was no similar "without reduction" language in the addendum, and the court held that, absent express language to the contrary, the proportionate reduction clause, although found in the printed portion of the lease, was applicable to the overriding royalty provision.<sup>53</sup> The opinion in the *Putnam* case ignores the division orders in reaching its decision.

*Houston Endowment Inc. v. Atlantic Richfield Co.*<sup>54</sup> is a discovery rule case. Texaco, Arco and others were lessees under various leases unitized into a gas unit. Production from the gas unit was run through a gas plant that was owned by the lessees and operated by Texaco. Each lessee paid royalties to the royalty owners separately, pursuant to separate leases and division orders.<sup>55</sup> In 1977, Texaco reduced the percentage of royalties it paid on the processed natural gas liquids from 100% to 85% in order to defray the costs of building a new plant. All of the other lessees followed suit, but the lessees continued to deduct severance taxes from the royalty owners based on 100% of the value of the natural gas liquids. In 1986, Arco sold all of its interests. The lawsuit is focused on plaintiff royalty owners' claims against Arco for underpayment of royalties from 1977 to 1986.<sup>56</sup>

The royalty owners sued Texaco and others in 1990. In 1993, during the course of discovery, the royalty owners claimed they first learned of the working interest owners' agreement to withhold royalties and that Arco was a party to the alleged scheme.<sup>57</sup> Arco relied upon limitations for its defense, and plaintiff royalty owners contended that limitations was tolled by the discovery rule or by fraudulent concealment. Arco prevailed because the facts established that the royalty owners knew or should have known of the underpayment more than four years before they took action on their claim, and their knowledge defeated any claim that they reasonably relied upon fraudulent concealment.<sup>58</sup>

Arco prevailed in this case on unusually favorable facts. However, the significance of the case is that the Court found that underpayments of royalty are generally undiscoverable and are subject to the discovery rule under the usual facts and circumstances. The Court applied the test articulated in *Computer Association International, Inc. v. Altai, Inc.*<sup>59</sup> to determine whether the discovery rule was applicable. Because it was undisputed that the royalty owners alleged injuries were objectively verifiable, the inquiry was focused on whether the injury was "inherently un-

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52. *McMahon*, 303 S.W.2d at 343.

53. *See Putnam*, 976 S.W.2d at 271.

54. 972 S.W.2d 156 (Tex. App.—Houston [14<sup>th</sup> Dist.] 1998, no pet. h.).

55. *See id.* at 158.

56. *See id.*

57. *See id.*

58. *See id.* at 162-63.

59. 918 S.W.2d 453 (Tex. 1996).



discoverable.”<sup>60</sup> The Court found that the royalty owners did not receive a detailed accounting showing the basis for the calculation of royalties, and that the amount of the royalties could not be calculated from the information Arco supplied in its monthly statements.<sup>61</sup> The significant holding of the case is:

Arco's underpayment of royalties was not information about which the royalty owners, using due diligence, would ordinarily learn; they would not learn this information unless it was supplied by a working interest owner. Thus, the injury was inherently undiscoverable. As such, the discovery rule tolls the statute of limitation until the [royalty owners] subjectively knew or should have known of the underpayment.<sup>62</sup>

This holding suggests that there may be many underpayment cases in which the recovery period could cover many, many years.

*Shivers v. Texaco Exploration and Production, Inc.*<sup>63</sup> is another discovery rule case. Under 26 U.S.C.A. § 29(a) and (c), the tax code grants a “Section 29 Tight Sands” tax credit. Shivers was a royalty owner in a property eligible for the tax credit. When Shivers actually became aware of his eligibility, he filed amended returns for prior years for the three prior years permitted by the tax code. He then sued Texaco for damages attributable to all of the prior years for which he could not file amended tax returns.<sup>64</sup>

Texaco prevailed on its motion for summary judgment, which was urged on multiple grounds in the trial court.<sup>65</sup> On appeal, the Court upheld the summary judgment on limitations and did not rule on Texaco's fundamental challenge of no duty.<sup>66</sup> The principal issue was thus whether Shivers' injury was “inherently undiscoverable.”<sup>67</sup> To compute and claim the Section 29 tax credit, a royalty owner must know:

- (1) that the well produced gas from a “tight formation” as determined by the Federal Energy Regulatory Commission (FERC);
- (2) that the well had been certified as a “tight formation” by the Texas Railroad Commission (TRC);
- (3) that the leasehold was dedicated or committed to interstate commerce on or before April 20, 1977; and
- (4) the average annual B.T.U. of the gas for the tax year.<sup>68</sup>

In concluding that the Shivers claim was not inherently undiscoverable and that a diligent lessor would have filed suit within the statute of limitations, the court relied very heavily upon the presumption that taxpayers are charged with knowledge of the tax code and that publications in the

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60. *Houston Endowment*, 972 S.W.2d at 159.

61. *See id.*

62. *Id.* at 160.

63. 965 S.W.2d 727 (Tex. App.—Texarkana 1998, pct. denied).

64. *See id.* at 730.

65. *See id.*

66. *See id.* at 733-34.

67. *See id.* at 734.

68. *Id.* at 735.

Federal Register and in the public records of the TRC amount to constructive notice.<sup>69</sup>

#### IV. OPERATIONAL ISSUES

*Holloway v. Atlantic Richfield Co.*<sup>70</sup> reviews the duties owed by an operator to a nonoperator when the operator undertakes to market the nonoperator's gas. The operator entered into a series of favorable gas purchase contracts that were breached by the gas purchaser when oil and gas prices dropped. The settlement of the ensuing take-or-pay litigation resulted in amendments to the gas purchase contracts for greater takes but lower prices. The operator marketed the nonoperator's gas under the amended contracts for a short period of time, and then the operator completely stopped marketing the nonoperator's gas.<sup>71</sup>

The applicable operating agreements had typical language providing that the nonoperator had the right to take in-kind or separately dispose of his oil and gas, and that the operator had the right, but not the obligation, to purchase the oil and gas of the nonoperator if the nonoperator did not take or sell it himself. The operator was obligated to sell the oil and gas, if it did undertake to sell it "at the best price obtainable in the area of such production."<sup>72</sup>

The nonoperator contended that the operator breached its fiduciary duty and breached its contractual duty by amending the gas purchase contracts and by failing to market the gas at the best price obtainable. The nonoperator sought to avoid summary judgment on the fiduciary duty claim by relying upon *Johnston v. American Cometra, Inc.*,<sup>73</sup> which had held that "the scope of [the operator's] duties to [nonoperators] is an undetermined fact issue that precludes summary judgment. . . ."<sup>74</sup> *Johnston* was distinguished in *Holloway* because in *Holloway* it was undisputed that the nonoperator's gas was *not* dedicated.<sup>75</sup> Therefore, the operator owed the nonoperator only the limited duty to account for the monies received for selling his gas, to avoid conflicts of interests, and not to act as an adverse party in its capacity as the seller of the gas.<sup>76</sup> The court also relied upon the related litigation in *Atlantic Richfield Company v. Long Trusts*.<sup>77</sup>

The breach of contract claim that the operator had not obtained "the best price obtainable in the area" was based on the contention that the original gas purchase contracts were the best price obtainable. As a matter of law, when the nonoperator reserves the right to take the production

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69. *See id.*

70. 970 S.W.2d 641 (Tex. App.—Tyler 1998, no pet.).

71. *See id.* at 642.

72. *Id.*

73. 837 S.W.2d 711 (Tex. App. - Austin 1992, writ denied).

74. *Id.* at 716.

75. *See Holloway*, 970 S.W.2d at 643.

76. *See id.*

77. 860 S.W.2d 439 (Tex. App.—Texarkana 1993, writ denied).

of the well in-kind, the production of the nonoperator is not dedicated. If the gas is not dedicated, the nonoperator cannot contend that the operator is obligated to the nonoperator under the operator's original gas purchase contract.<sup>78</sup>

The operator offered proof of fair market value for undedicated gas, but market price and best price obtainable are not synonymous terms. Because it is possible that by the exercise of reasonable effort the operator might obtain more favorable terms than market price, the summary judgment on this point was not proper.<sup>79</sup>

*Intratex Gas Co. v. Beeson*<sup>80</sup> upholds an order certifying a class action brought to enforce an alleged private cause of action arising under Rule 34 of the Statewide Conservation Rules of the Texas Railroad Commission (known as the Market Demand Rule). The Market Demand Rule states: "A first purchaser shall not discriminate between different wells from which it purchases in the same field, nor shall it discriminate unjustly or unreasonably between separate fields."<sup>81</sup> Plaintiffs alleged that Intratex did not purchase gas ratably from the wells of more than 900 producers by selectively producing increases in demand from wells that had a weighted average cost below the current spot market price and by increasing takes from certain wells immediately after exercising a downward price redetermination on those wells.<sup>82</sup> The class was defined as "[a]ll persons who were producers of natural gas sold to the defendant between January 1, 1978 and December 31, 1988 whose natural gas was taken by the defendant in quantities less than their ratable proportions."<sup>83</sup>

Intratex contended that the definition of the class required an improper conclusion on the merits of plaintiffs' claims. Although trial courts enjoy a wide range of discretion in determining whether to maintain a lawsuit as a class action, the trial court may not consider the substantive merits of the class claims in making such a determination.<sup>84</sup> In upholding the certification, the court held that it is the act of not taking ratably, and not the reasons for the undertaking or whether there is proof of a compensable injury, that defines the class by reference to the objective conduct of Intratex.<sup>85</sup> The dissent would reverse because the definition requires a finding of wrongdoing in order to constitute the class. The concept of ratability, as used by the plaintiffs, subsumes the notion of discrimination, so that the unlawful conduct is predetermined.<sup>86</sup> However, the majority was apparently persuaded that the class was objectively

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78. See *Holloway* 970 S.W.2d at 644.

79. See *id.*

80. 960 S.W.2d 389 (Tex. App.—Houston [1<sup>st</sup> Dist.] 1998, pet. denied).

81. *Id.* at 400.

82. See *id.* at 396.

83. *Id.* at 394.

84. See *id.* at 393.

85. See *id.* at 394-95.

86. See *id.* at 399-400.

defined in relation to Intratex's act of not taking, and it was undisputed that the identity of the producers could be obtained from Intratex's own records and from the Texas Railroad Commission records, so that the class could always later be decertified or the class definition modified.<sup>87</sup>

*Mitchell Energy Corp. v. Bartlett*<sup>88</sup> is another discovery rule case, and it reviews the application of the rule to various causes of action based on hydrogen sulfide pollution. Mitchell allegedly failed to properly maintain its gas wells, causing hydrogen sulfide to migrate from the gas wells into the Trinity Aquifer, the source of the land owners' water supply. Hydrogen sulfide is associated with a "rotten egg" odor. Mitchell had drilled approximately 3,700 gas wells in Wise County and in surrounding counties since the 1950's, and at the time of trial operated approximately 2,000 active wells in the area. The Bartletts and many other land owners sued Mitchell and alleged that various deficiencies in Mitchell's maintenance made Mitchell liable on theories of nuisance, negligence, trespass, violation of various regulatory rules, and fraud.<sup>89</sup> The jury found for the land owners on all of their claims and awarded compensatory damages for mental anguish; physical pain; discomfort, annoyance and inconvenience; out-of-pocket expenses; property damage; and diminished value of real estate. The jury also found that Mitchell's conduct constituted gross negligence and was committed with malice. The jury awarded the land owners punitive damages of \$200,000,000.<sup>90</sup>

The judgment was reversed and rendered because almost all of the land owners' claims were found to be barred by the two-year statute of limitations. Claims for personal injury and property damage are governed by the two-year statute and must be brought within two years from the date of "accrual" of the cause of action.<sup>91</sup> Generally, a cause of action accrues when a wrongful act causes an injury, regardless of when the plaintiff learns of the injury.<sup>92</sup> However, Texas courts have applied the discovery rule of accrual to causes of action for damage to property.<sup>93</sup> When applied, this rule operates to toll the running of the limitations period until the plaintiff discovers, or through the exercise of reasonable care and diligence should have discovered, the fact of injury.<sup>94</sup> Regarding claims for permanent injury to property, the action accrues and the statute begins to run when the injury is first discovered or should have been discovered.<sup>95</sup> Therefore, in this case, the proper inquiry was: "Did [land owners] file their lawsuits within two years of the date they discovered, or in the exercise of reasonable diligence should have discovered, the fact of their

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87. See *id.* at 395.

88. 958 S.W.2d 430 (Tex. App.—Fort Worth 1997, pet. denied).

89. See *id.* at 434-35.

90. See *id.* at 435.

91. See *id.*

92. See *id.* at 436.

93. *Id.*

94. *Id.*

95. See *id.*

injury?"<sup>96</sup>

The evidence conclusively established that the land owners knew that their water tasted bad and smelled bad for many years before they sued, and therefore, their claims were barred. Because there were a few land owners who did timely file their suit, the court went on to consider whether there was any evidence of causation. The court then effectively threw out the land owners' expert testimony because of defects in the underlying facts and methodology.

## V. REGULATORY ISSUES

*In re H.L.S. Energy Co., Inc.*<sup>97</sup> holds that post-petition expenses for the remediation of post-petition environmental liabilities constitute an administrative expense entitled to priority in bankruptcy over the claims of other secured creditors.<sup>98</sup> The debtor was the sole owner of the operating interests in wells that ceased producing, and the estate's obligation to plug the wells under state law arose post-petition.<sup>99</sup> The Chapter 11 Trustee negotiated an agreement with the State of Texas in which the state waived substantial penalties, plugged the wells and charged the cost of plugging to the estate.<sup>100</sup>

The trustee contested the state's priority status, contending that the plugging did not benefit the estate.<sup>101</sup> Under federal law, bankruptcy trustees must comply with state law and may not abandon property in contravention of a state law reasonably designed to protect public health or safety.<sup>102</sup> The court expressly did not reach the question of whether post-petition expenses for the remediation of pre-petition environmental liabilities would likewise constitute an administrative expense.<sup>103</sup> The decision is significant to the state's continuing efforts to enforce plugging obligations because the failure to plug is frequently attributable to business failure.

*Sea Robin Pipeline Co. v. F.E.R.C.*<sup>104</sup> vacates and remands an order of the Federal Energy Regulatory Commission which had denied Sea Robin's petition for a declaration that Sea Robin's facilities perform a "gathering" function, rather than a "transportation" function.<sup>105</sup> Section 1(b) of the Natural Gas Act<sup>106</sup> governs "the transportation of natural gas in interstate commerce."<sup>107</sup> This section expressly exempts from the Commission's jurisdiction the production or gathering of gas. Thus, the

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96. *Id.* at 437.

97. 151 F.3d 434 (5th Cir. 1998).

98. *See id.* at 436.

99. *See id.* at 439.

100. *See id.* at 436.

101. *See id.* at 438.

102. *See id.*

103. *See id.* at 439.

104. 127 F.3d 365 (5th Cir. 1997).

105. *See id.* at 367.

106. 15 U.S.C. § 717, *et seq.* (1998).

107. *Id.* at § 717(b).

characterization of a pipeline system as a “gathering” or “transportation” system determines whether it will be subject to Commission jurisdiction.<sup>108</sup>

The pipeline system in issue was a very large offshore system with major facilities onshore for separating, dehydrating, processing and compressing the gas.<sup>109</sup> The Commission emphasized non-physical criteria in reaching its decision. Specifically, the Commission gave great weight to the system’s prior certification as a jurisdictional pipeline, ownership by an interstate pipeline and that granting gathering status to Sea Robin would amount to the deregulation of the entire natural gas pipeline system on the outer continental shelf. The Court concluded that the “Commission’s accent on business purpose, ownership, and prior certification status misses the basic thrust of the primary function test—making a technical distinction between gathering and transportation based on the physical and operational characteristics of a pipeline facility.”<sup>110</sup> By enacting the regulatory scheme encompassed in the Natural Gas Act, Congress defined the jurisdictional reach of the Commission by the distinctions between gathering and transporting.<sup>111</sup>

*State v. Triax Oil and Gas, Inc.*<sup>112</sup> holds corporate officers individually liable for their company’s failure to properly plug and abandon wells.<sup>113</sup> The Railroad Commission sent notice of a hearing to Triax in December 1992. A hearing was held in January 1993 at which Triax failed to appear. The corporate charter of Triax was forfeited for failure to file a franchise tax report in February 1993. The Commission eventually imposed administrative penalties and incurred costs by expending state funds to plug Triax wells. In September 1995, the state sued to enforce the administrative penalties, to recover plugging costs and for additional civil penalties for failure to abide by the order, court costs and attorney’s fees.<sup>114</sup> The state also sued under the Tax Code to hold the directors individually liable for all liabilities of Triax due to the forfeiture of the corporate charter.<sup>115</sup>

The trial court apparently believed that the proceeding before the Commission imposing the administrative penalties was not final because the directors allegedly never received notice that the motion for rehearing was overruled.<sup>116</sup> The court held that the motion for rehearing was overruled by operation of law, regardless of whether the directors did or did not receive notice. Therefore, the Commission order was final, it was not appealed by judicial review, and to attack that decision in this pro-

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108. *See Sea Robin Pipeline*, 127 F.3d at 368.

109. *See id.* at 367.

110. *Id.* at 370.

111. *See id.* at 371.

112. 966 S.W.2d 123 (Tex. App.—Austin 1998, no pet.).

113. *See id.* at 128.

114. *See id.* at 125.

115. *See id.*

116. *See id.* at 126.

ceeding would be an impermissible collateral attack. Judgment for administrative fees was rendered. The state's claims for a civil penalty and the recovery of reasonable expenses were remanded because the state had been denied the opportunity to present its case by the trial court's take nothing judgment.<sup>117</sup>

The court also held that the Commission was under no duty to accept well equipment allegedly tendered by the directors as an offset against the plugging costs, and because the Commission was under no duty to accept, it could not be liable for negligence in failing to exercise control over the equipment.<sup>118</sup>

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117. *See id.* at 126-27.

118. *See id.* at 127-28.