



2013

# Oil, Gas, and Mineral law

Richard F. Brown

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## Recommended Citation

Richard F. Brown, *Oil, Gas, and Mineral law*, 66 SMU L. Rev. 1003 (2013)  
<https://scholar.smu.edu/smulr/vol66/iss5/8>

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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 November 1, 2010, through October 31, 2012, with emphasis on cases decided in the past year. The cases examined include decisions of state and federal courts in the State of Texas and the Fifth Circuit Court of Appeals.<sup>1</sup>

## II. TITLE AND CONVEYANCING ISSUES

*State v. Cemex Construction Materials South, L.L.C.*<sup>2</sup> held that all de-

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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.

2. *State v. Cemex Constr. Materials S., L.L.C.*, 350 S.W.3d 396, 410 (Tex. App.—El Paso 2011, pet. granted, judgment vacated w.r.m.). For other notable cases dealing with title and conveyancing issues, see *ConocoPhillips Co. v. Dahlberg*, No. C-10-285, 2011 WL 710604 (S.D. Tex. Feb. 22, 2011) (legal description); *Moore v. Noble Energy, Inc.*, 374 S.W.3d 644 (Tex. App.—Amarillo 2012, no pet.) (fractional deed construction); *Farm & Ranch Investors, Ltd. v. Titan Operating, LLC*, 369 S.W.3d 679 (Tex. App.—Fort Worth 2012, pet. denied) (deed restrictions as a mineral reservation); *Philipello v. Taylor*, No. 10-11-00014-CV, 2012 WL 1435171 (Tex. App.—Waco Apr. 25, 2012, pet. denied) (mem. op.) (Duhig Rule and surrounding circumstances); *Hunsaker v. Brown Distribut. Co.*, 373 S.W.3d 153 (Tex. App.—San Antonio 2012, pet. denied) (fractional conveyance of land described); *Coghill v. Griffith*, 358 S.W.3d 834 (Tex. App.—Tyler 2012, pet. denied) (fraction of royalty deed); *Harrington v. Magellan Pipeline Co., L.P.*, No. 10-09-00131-CV, 2011 WL 6225276 (Tex. App.—Waco Dec. 14, 2011, no pet.) (mem. op.) (multiple pipelines on single easement); *Sundance Minerals, L.P. v. Moore*, 354 S.W.3d 507 (Tex. App.—Fort Worth 2011, pet. denied) (fraction of royalty deed reservation); *Philipello v. Nelson Family Farming Trust*, 349 S.W.3d 692 (Tex. App.—Houston [14th Dist.] 2011, pet. denied) (proportionate reduction of reserved royalty); *Fisher v. Wynn*, No. 12-11-00008-CV, 2011 WL 3338771 (Tex. App.—Tyler Aug. 3, 2011, no pet.) (mem. op.) (subject to clause not a second grant); *Elder v. Anadarko E & P Co.*, No. 12-10-00250-CV, 2011 WL 2713817 (Tex.

posits of granite, limestone, gravel, sand, and any other mineral substances of whatever kind or character having commercial value on public school lands are reserved to the State of Texas if they were originally conveyed pursuant to the Mining Act of 1895. Four parcels (Section 22 and Surveys 271, 221, and 222) in El Paso County were set apart for the benefit of public schools. The State originally conveyed the four parcels in 1900, 1906, and 1912 to the predecessors of Cemex Construction Materials South, L.L.C. (Cemex). All four parcels were classified as dry grazing mineral land. Section 22 was conveyed with no mineral reservation. Surveys 271, 221, and 222 were conveyed with a reservation of 1/16 of the minerals. The State alleged that the State owned title to all minerals under the 1895 Land Sales Act and Title LXXI of the Mining Act of 1895. Cemex alleged that dirt, caliche, sand, gravel, limestone, and the other materials at issue were not “minerals” reserved to the State.

The parcels were designated as public school lands, and the law in existence at the time of the original conveyances applied to their sales.<sup>3</sup> At the time of the original conveyances, the Land Sales Act of 1895 and the Mining Act of 1895 were in effect. The Mining Act of 1895 stated that public school lands designated as containing valuable mineral deposits had to be purchased “‘under regulations prescribed by law. . . .’”<sup>4</sup> All sales of public school lands were subject to a reservation of the mineral estate.<sup>5</sup>

In analyzing and applying the law outlined above, the El Paso Court of Appeals looked to *Schwarz v. State*<sup>6</sup> for guidance.<sup>7</sup> *Schwarz* also involved land designated as containing minerals that was sold pursuant to the Land Sales Act of 1895.<sup>8</sup> There, the original conveyance by the State was subject to a reservation of the mineral estate. Over forty years after the original conveyance, the State again provided notice of the mineral estate reservation to the landowners by way of letters patent. After another thirty-one years passed, the landowners executed a lease for the extraction of coal and lignite. The leaseholder, Schwarz, later sought a declaration that he owned the minerals he had extracted pursuant to the lease. Looking at the law in effect at the time of the original conveyance, the

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App.—Tyler July 13, 2011, no pet.) (mem. op.) (rules of construction for deeds); *Hernandez v. El Paso Prod. Co.*, No. 13-09-184-CV, 2011 WL 1442991 (Tex. App.—Corpus Christi Apr. 14, 2011, pet. denied) (mem. op.) (inconsistent fractions in deed); *Gail v. Berry*, 343 S.W.3d 520 (Tex. App.—Eastland 2011, pet. denied) (reformation of deed for mutual mistake); *Carpenter v. Phelps*, 391 S.W.3d 143 (Tex. App.—Houston [1st Dist.] 2011, no pet.) (legal description); *Walker v. Campuzano Enters., Ltd.*, No. 02-10-00061-CV, 2011 WL 945167 (Tex. App.—Fort Worth Mar. 17, 2011, no pet.) (mem. op.) (Duhig Rule); *Hausser v. Cuellar*, 345 S.W.3d 462 (Tex. App.—San Antonio 2011, pet. denied) (inconsistent fractions in deed).

3. *Cemex Constr. Materials S., L.L.C.*, 350 S.W.3d at 401.

4. *Id.* at 402 (quoting Act of April 30th, 1895, 24th Leg., R.S., ch. 127, § 1, 1895 Tex. Gen. Laws 197 (repealed 1913)).

5. *Id.* at 403 (citing *Tynes v. Mauro*, 860 S.W.2d 168, 170 (Tex. App.—El Paso 1993, pet. denied)).

6. *Schwarz v. State*, 703 S.W.2d 187 (Tex. 1986).

7. *Cemex Constr. Materials S., L.L.C.*, 350 S.W.3d at 403–05.

8. *Id.* at 404 (citing *Schwarz*, 703 S.W.2d at 188).

Supreme Court of Texas determined that the State retained the mineral estate.<sup>9</sup> Further, clarifying the extent of the mineral estate reserved by the State, the *Schwarz* court held that “whatever is not unequivocally granted in clear and explicit terms is withheld and any ambiguity or obscurity in the terms of the statute, such as the term ‘the minerals,’ must be interpreted in favor of the State.”<sup>10</sup>

The court in *Cemex* also determined that the State had reserved the minerals embraced by the Mineral Act of 1895.<sup>11</sup> In addition to the statutory mandate that only the surface estate of the four public school land parcels be sold, the court pointed out acknowledgement of the mineral estate reservations in the required affidavits and applications filed by the original grantees as part of either the original conveyance or the second conveyance. The court held that, pursuant to *Schwarz*, because the State did not unequivocally grant to the purchaser anything other than the surface estate, no minerals were conveyed.<sup>12</sup> The court then addressed *Cemex*’s argument that dirt, caliche, sand, gravel, limestone, and other materials were not “minerals” that the State had reserved. Relying again on *Schwarz*, the court held that, because none of the materials to which *Cemex* claimed ownership were clearly granted by the State in the original conveyance, those items were withheld from the State’s conveyances, and any ambiguity in the terms of the statute had to be resolved in the State’s favor.<sup>13</sup> The possible ambiguities included such terms as “the minerals,” “stones valuable for ornamental or building purposes,” and “other valuable building material.”<sup>14</sup> The specific holding was that the State reserved “all deposits of granite, limestone, gravel, sand, and any other mineral substances of whatever kind or character having commercial value . . . .”<sup>15</sup>

The significance of the case is that the holdings disregarded the effect of express reservations of 1/16 of the minerals or no reservations of the minerals thereby reserving all minerals to the State, and that the court construed all ambiguities within the meaning of “minerals” under the statute against the grantee.

The Texas Supreme Court’s order of March 16, 2012, states:

**PETITION FOR REVIEW IS GRANTED.**

First and second amended agreed motions to dismiss petition for review granted as follows:

Pursuant to Texas Rule of Appellate Procedure 56.3, without hearing oral argument or considering the merits, the Court grants the petition for review, vacates the court of appeals’ judgment, and remands the case to the trial court for rendition of

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9. *Id.* at 404–05 (summarizing *Schwarz*, 703 S.W.2d at 189).

10. *Id.* at 404 (quoting *Schwarz*, 703 S.W.2d at 189).

11. *Id.* at 406–08.

12. *Id.* at 408.

13. *Id.* at 408–09.

14. *Id.* at 409.

15. *Id.* at 410.

judgment pursuant to the parties' settlement agreement.<sup>16</sup>

Texas Rule of Appellate Procedure 56.3 states:

If a case is settled by agreement of the parties and the parties so move, the Supreme Court may grant the petition if it has not already been granted and, without hearing argument or considering the merits, render a judgment to effectuate the agreement. The Supreme Court's action may include setting aside the *judgment* of the court of appeals or the trial court without regard to the merits and remanding the case to the trial court for rendition of a judgment in accordance with the agreement. The Supreme Court may abate the case until the lower court's proceedings to effectuate the agreement are complete. A severable portion of the proceeding may be disposed of if it will not prejudice the remaining parties. In any event, the Supreme Court's order does not vacate the court of appeals' opinion unless the order specifically provides otherwise. An agreement or motion cannot be conditioned on vacating the court of appeals' *opinion*.<sup>17</sup>

The Supreme Court of Texas adopted the above procedure in order to preserve the public nature of an appellate court's opinion while allowing parties to settle their disputes during the pendency of an appeal.<sup>18</sup> Upon joint motion, the Texas Supreme Court grants the petition

without reference to the merits, sets aside the judgments of the court of appeals and trial court without reference to the merits and remands the cause to the trial court for entry of judgment in accordance with the settlement agreement of the parties—the court of appeals' opinion is not vacated. Although the application for [petition] is granted, the precedential authority of a court of appeals opinion which is not vacated under these circumstances is equivalent to a “[pet.] dismissed” case.<sup>19</sup>

Here, the Texas Supreme Court vacated the appellate court's judgment without considering the merits and did not expressly vacate the opinion.<sup>20</sup> Therefore, the El Paso Court of Appeal's opinion in *State v. Cemex*<sup>21</sup> has the same precedential authority of a case where the petition was dismissed.

*MPH Production Co. v. Smith*<sup>22</sup> held that a right of first refusal to purchase minerals was a covenant running with the land, and it was attached to and conveyed with the surface estate. The parties aligned as successors-in-interest to Grantor and Grantee under a deed executed in

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16. *Cemex Constr. Materials S., L.L.C. v. State*, No. 11-0790, 2012 Tex. LEXIS 231, at \*1 (Tex. Mar. 16, 2012).

17. Tex. R. App. P. 56.3 (emphasis added).

18. *Houston Cable TV, Inc. v. Inwood W. Civic Ass'n*, 860 S.W.2d 72, 73 & n.3 (Tex. 1993).

19. *Id.*

20. *Id.*

21. *State v. Cemex Constr. Materials S., L.L.C.*, 350 S.W.3d 396 (Tex. App.—El Paso 2011, pet. granted, judgment vacated w.r.m.).

22. *MPH Prod. Co. v. Smith*, No. 06-11-00085-CV, 2012 WL 1813467, at \*1 (Tex. App.—Texarkana May 18, 2012, no pet.) (mem. op.).

1979, which covered 18.620 acres in Harrison County. Grantor conveyed the surface estate and a right of first refusal to buy the minerals in the land (ROFR) to Grantee. The issue was whether the successors to Grantee acquired the ROFR either (1) as a covenant running with the land, or (2) as part of the rights transferred by the assignments of the surface estate to them.<sup>23</sup>

In Texas, a real property covenant runs with the land when it touches and concerns the land, it relates to a thing in existence or specifically binds the parties and their assigns, it is intended by the parties to run with the land, and the successor to the burden has notice.<sup>24</sup>

Privity of estate between the parties is also required.<sup>25</sup> In this case, only privity of estate and the intent of the parties were in dispute.

“Privity of estate exists when there is a mutual or successive relationship to the same rights of property.”<sup>26</sup> Two separate estates were created when Grantor reserved the mineral estate subject to the ROFR. Grantor argued there was no privity of estate because the 1979 deed only conveyed the surface interest, and therefore, there was no simultaneous or successive interest in the mineral estate between Grantor and Grantee. The court held there was privity of estate even though the 1979 deed created two separate estates because the mineral estate owned by Grantor became burdened with the obligation represented by the ROFR.<sup>27</sup>

The parties disputed whether the deed expressed sufficient intent for the ROFR to run with the land. “In order for a covenant to run with the land, the parties who created the covenant must intend for it to do so.”<sup>28</sup> The deed states:

And for the same consideration, we have granted, and do grant, to the Grantees the right, privilege and option of purchasing the oil, gas and other minerals, or any portion thereof, in and under the above described land, for such sum as we may be willing to accept upon our receipt of a bona fide offer from any third party (being any party other than one of the Grantors); and upon the receipt by either of the Grantors of an offer to purchase a Grantor’s interest in oil, gas and other minerals, or any portion thereof, which said Grantor desires to accept, the Grantor receiving such offer shall notify the Grantees of such offer and the terms thereof, and such Grantor’s willingness to accept such offer, and the Grantees shall have the right and privilege of purchasing the interest of said Grantor in the oil, gas and other minerals of the price and upon the terms and conditions therein stated, at any time within twenty days after the Grantees re-

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23. *Id.*

24. *Id.* at \*2 (citing *Inwood N. Homeowners’ Ass’n v. Harris*, 736 S.W.2d 632, 635 (Tex. 1987)).

25. *Id.*

26. *Id.*

27. *Id.*

28. *Id.* at \*3 (citing *Rolling Lands Invs., L.C. v. Nw. Airport Mgmt., L.P.*, 111 S.W.3d 187, 200 (Tex. App.—Texarkana 2003, pet. denied)).

ceive such notice from said Grantor.<sup>29</sup>

Immediately after the right of first refusal was the following language:

“The right, privilege and option herein granted shall be binding upon the Grantors, and their respective heirs and assigns. No sale of an interest in oil, gas and other minerals may be made by a Grantor without complying with the provisions set out herein.”<sup>30</sup>

The habendum clause contained general warranty language that Grantee relied on to support Grantee’s argument that the parties intended the right to pass to Grantee’s successors in title. The court analyzed the language of the 1979 deed and concluded that the ROFR was a covenant running with the land.<sup>31</sup>

Finally, the court also held (but with more conviction) that, because the subsequent deeds out of the Grantee in 1981 conveyed the fee subject to any mineral reservations, these deeds conveyed the surface and the ROFR, which was a right connected to the ownership of the surface.<sup>32</sup> In other words, regardless of whether the ROFR was a covenant running with the land, the ROFR was a part of the surface estate expressly assigned to Grantee’s successors. “[I]t is a stretch to read into the subtleties of the deed’s text an intent to make the right of first refusal a personal right only.”<sup>33</sup>

The significance of the case is the conclusion that it is unlikely that a ROFR is a personal right only, and therefore: (1) it will be included in the property rights of the estate to which the ROFR is first attached, and (2) it will be included in any subsequent conveyance unless excepted. The analysis of the deed in this case suggests that a ROFR will generally be construed as a covenant running with the land.

### III. LEASE AND LEASING ISSUES

*Shell Oil Co. v. Ross*<sup>34</sup> held that neither the doctrine of fraudulent con-

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29. *Id.*

30. *Id.* at \*4.

31. *Id.* at \*5–6.

32. *Id.* at \*6.

33. *Id.*

34. *Shell Oil Co. v. Ross*, 356 S.W.3d 924, 925 (Tex. 2011). For other notable cases dealing with lease and leasing issues, see *PEC Minerals LP v. Chevron USA Inc.*, 439 F. App’x 413 (5th Cir. 2011) (production anywhere on lease holds multiple tracts/units); *Coll v. Abaco Operating LLC*, No. 2:08-CV-345-TJW, 2011 WL 1831748 (E.D. Tex. May 12, 2011) (severance tax); *Thomson Oil Royalty, LLC v. Graham*, 351 S.W.3d 162 (Tex. App.—Tyler 2011), *aff’d*, 2011 Tex. App. LEXIS 7842 (Tex. 2011) (ratification of voidable lease by paying bonus); *Glencrest Res., LLC v. Ellis*, No. 02–12–00060–CV, 2012 WL 3500324 (Tex. App.—Fort Worth Aug. 16, 2012, no pet.) (mem. op.) (urban lease class action); *Samson Lone Star, Ltd. P’ship v. Hooks*, 389 S.W.3d 409 (Tex. App.—Houston [1st Dist.] 2012, pet. filed) (lease offset clause; TRC records; unpooling); *SM Energy Co. v. Sutton*, 376 S.W.3d 787 (Tex. App.—San Antonio 2012, pet. denied) (termination of ORRI on partial release of lease); *Kantner v. Chesapeake Energy Corp.*, No. 02–11–00378–CV, et al., 2012 WL 1859873 (Tex. App.—Fort Worth May 10, 2012, pet. denied) (mem. op.) (urban lease and homeowners association); *E. Express, L.P. v. XTO Energy, Inc.*, Nos. 02–10–00395–CV, 02–10–00396–CV, 02–10–00397–CV, 2012 WL 1059080 (Tex. App.—

cealment nor the discovery rule will toll the statute of limitations when readily accessible, publicly available information would reveal a cause of action for underpayment of lease royalties. In 1961, Lessor leased to Lessee for a royalty on gas equal to “one-eighth of the amount realized” by Lessee.<sup>35</sup> Part of the leased land was pooled into two pooled units. One producing well was drilled on each of the pooled units, and two producing wells were drilled on the leased land. The unit wells were on state lands, and the royalty was proportionately reduced. From 1988 to 1994, Lessee computed the royalty on the unit wells on the basis of a weighted-average of third-party sales prices for sales from the pooled units by Lessee and other operators. Lessee, however, could provide no explanation for the basis of royalty computations on the lease wells from 1994 to 1997. The parties aligned as Lessor and Lessee, and Lessor sued Lessee in 2002 for breach of contract, unjust enrichment, and fraud. Lessee conceded that Lessor was entitled to damages but asserted a statute of limitations defense. Lessor countered that Lessee had “‘set up an elaborate scheme to allow it to [underpay] royalties, and then made multiple misrepresentations to cover up this scheme, [including] making false representations in the monthly [royalty] statements.’”<sup>36</sup> Lessor secured a jury finding on fraudulent concealment.<sup>37</sup>

The issues before the Texas Supreme Court were (1) whether the statute of limitations was tolled by the doctrine of fraudulent concealment, and (2) whether the discovery rule delayed the accrual of the cause of action. The supreme court stated that fraudulent concealment requires that the party asserting it demonstrate that the party committing the fraud “‘actually knew a wrong occurred, had a fixed purpose to conceal the wrong, and did conceal the wrong.’”<sup>38</sup> However, the doctrine only applies until “‘the fraud is discovered or could have been discovered with reasonable diligence.’”<sup>39</sup>

The supreme court’s opinion focused almost exclusively on the second element of the test, namely whether the fraud could have been discovered with reasonable diligence. Lessor argued that reasonable reliance on Lessee’s misrepresentations negated its duty to engage in due diligence.

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Fort Worth Mar. 29, 2012, pet. denied) (mem. op.) (urban lease and homeowners association); *Maddox v. Vantage Energy, LLC*, 361 S.W.3d 752 (Tex. App.—Fort Worth 2012, pet. denied) (urban lease and homeowners association); *Aston Meadows, Ltd. v. Devon Energy Prod. Co.*, 359 S.W.3d 856 (Tex. App.—Fort Worth 2012, pet. denied) (lease covering land in two counties as notice); *Royalco Oil & Gas Corp. v. Stockhome Trading Corp.*, 361 S.W.3d 725 (Tex. App.—Fort Worth 2012, no pet.) (salt water disposal lease is not a mineral lease); *EOG Resources, Inc. v. Hurt*, 357 S.W.3d 144 (Tex. App.—Fort Worth 2011, pet. denied) (damages to Lessor’s tenant as third party beneficiary of oil and gas lease); *Pharaoh Oil & Gas, Inc. v. Rancho Esperanza, Ltd.*, 343 S.W.3d 875 (Tex. App.—El Paso 2011, no pet.) (surface use and temporary injunction); *Merriman v. XTO Energy, Inc.*, No. 10-09-00276-CV, 2011 WL 1901987 (Tex. App.—Waco May 11, 2011, pet. granted) (mem. op.) (accommodation doctrine).

35. *Ross*, 356 S.W.3d at 926.

36. *Id.* (alterations in original).

37. *Id.* at 927.

38. *Id.* (quoting *Shah v. Moss*, 67 S.W.3d 836, 841 (Tex. 2001)).

39. *Id.* (quoting *BP Am. Prod. Co. v. Marshall*, 342 S.W.3d 59, 67 (Tex. 2011)).



The supreme court rejected this argument, stating that the duty of diligence was triggered once Lessor was “put on notice of the alleged harm of injury-causing actions.”<sup>40</sup> In this case, there was a large disparity in the price received from production on the lease wells and from production on the unit wells. The supreme court reasoned that, because the wells were in a common reservoir, the disparity in prices should have alerted Lessor about a potential wrongdoing by Lessee, thus triggering the duty of diligence. Lessor argued that the disparity in prices could have been attributed to differences in heating values, but the court rejected this argument, stating that a hypothetical, albeit reasonable, explanation for a suspicious royalty payment does not relieve a royalty owner of the duty to investigate.<sup>41</sup>

According to the supreme court, the duty of reasonable diligence requires that property owners “make themselves aware of relevant information available in the public record.”<sup>42</sup> Accordingly, “[Lessor] did not exercise reasonable diligence and [Lessor’s] claims are barred by limitations if readily accessible and publicly available information could have revealed [Lessee’s] wrongdoing before the limitations period expired.”<sup>43</sup> In this case, the fraud could have been discovered by reference to the El Paso Permian Basin Index or the Texas General Land Office Records. Both of these resources were publicly available, and reference to either of them would have revealed that Lessee was underpaying the royalty.<sup>44</sup> Accordingly, the supreme court held that, as a matter of law, Lessor had not exercised reasonable diligence, and the doctrine of fraudulent concealment did not apply.<sup>45</sup>

The supreme court then turned to the issue of whether the discovery rule could be applied to delay the accrual of the cause of action. The supreme court characterized the discovery rule as a “very limited exception to the statutes of limitations.”<sup>46</sup> Moreover, the rule applies “only when the nature of the plaintiff’s injury is both inherently undiscoverable and objectively verifiable.”<sup>47</sup> An injury is inherently undiscoverable when it is “unlikely to be discovered within the prescribed limitations period despite due diligence.”<sup>48</sup> The supreme court stated again that Lessor had not exercised due diligence.<sup>49</sup> Accordingly, the discovery rule did not apply.

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40. *Id.* at 928 (quoting *Exxon Corp. v. Emerald Oil & Gas Co.*, 348 S.W.3d 194, 207 (Tex. 2011)).

41. *Id.* at 929 (citing *Wagner & Brown, Ltd. v. Horwood*, 58 S.W.3d 732, 737 (Tex. 2001)).

42. *Id.* at 928.

43. *Id.*

44. *Id.* at 929.

45. *Id.*

46. *Id.* at 929 (quoting *Computer Assocs. Int’l, Inc. v. Altai, Inc.*, 918 S.W.2d 453, 455 (Tex. 1994)).

47. *Id.* at 930 (quoting *Wagner & Brown, Ltd. v. Horwood*, 58 S.W.3d 732, 734 (Tex. 2001)).

48. *Id.* (quoting *S.V. v. R.V.*, 933 S.W.2d 1, 7 (Tex. 1996)).

49. *Id.*

The case is a continuation of a pronounced trend at the supreme court to enforce statutes of limitation, to require that injured parties take reasonable steps to be informed and to take prompt action to assert their claims, and to narrow the application of fraudulent concealment and the discovery rule in extending a statute of limitations.

*Jones v. Clem*<sup>50</sup> held that the only lessee entitled to notice under the change in ownership clause of a lease is the lessee at the time the change in ownership occurs. The facts as summarized in the opinion are not entirely clear. Evans owned a mineral interest that was leased for oil and gas. In 1991, Clem acquired Evans's interest through a bankruptcy proceeding, and Clem recorded the deed in the Coleman County Clerk's office. Although Clem gave no notice of assignment to anyone, Clem immediately began receiving royalty payments from the purchaser, Western Gas. In 1999, for some reason, payments to Clem stopped. In 2002, someone assigned the lease on Clem's interest to Jones. Jones received some document (possibly a paydeck) from a predecessor lessee that showed Evans as the owner. When Jones tried to pay Evans, Jones discovered that Evans had died, and Jones then began paying Evans's daughter. In 2008, Clem discovered that the lease was still producing and sued Jones and Evans's daughter for unpaid royalties. Judgment was entered for Clem against Jones for \$27,169.38 and against Evans's daughter for \$11,376.15. Judgment was entered for Jones against Evans's daughter for \$27,169.38. There is no explanation as to the reason for the splits in liability, and Evans's daughter did not appeal.<sup>51</sup> Jones relied upon the change of ownership clause in the lease as an affirmative defense.<sup>52</sup>

The change of ownership clause relied upon by Jones was a typical lease clause. It expressly permitted assignments but expressly limited lessee's obligations in part as follows:

No such change or division in the ownership of the land, rentals or royalties shall be binding upon lessee for any purpose until such person acquiring any interest has furnished lessee with the instrument or instruments, or certified copies thereof, constituting his chain of title from the original lessor.<sup>53</sup>

These clauses "relieve a lessee from liability for the misplayment of royalty or delay rentals, when the misplayment is caused by a change in ownership and no notice is given to the lessee of such change."<sup>54</sup> "Where such a provision is included in the lease, the lessee is not charged with constructive notice from the record of a subsequent transfer by the lessor."<sup>55</sup>

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50. *Jones v. Clem*, No. 11-10-00123-CV, 2012 WL 1069168, at \*4 (Tex. App.—Eastland Mar. 29, 2012, no pet.) (mem. op.).

51. *Id.* at \*1-2.

52. *Id.* at \*2.

53. *Id.* at \*3.

54. *Id.*

55. *Id.* (citing *Jackson v. United Producers' Pipe Line Co.*, 33 S.W.2d 540 (Tex. Civ. App.—Fort Worth 1930, writ ref'd); *Brandt v. Roxana Petroleum Corp.*, 29 F.2d 980 (5th Cir. 1929)).

The opinion identifies Western Gas as the “purchaser”<sup>56</sup> and as the “lessee”<sup>57</sup> at the time Clem first acquired the interest, so the capacity in which Western Gas acted is not clear. Nevertheless, Clem apparently conceded that Western Gas was the lessee at the time and could have invoked the clause against Clem. The opinion is silent as to whether Jones made the same concession. The court then assumed a waiver of the change in ownership notice by Western Gas based on the payments made by Western Gas. Obviously, if Western Gas was only the purchaser, and not the lessee, payments by Western Gas would not necessarily be a waiver of the change in ownership clause in the lease.

The Eastland Court of Appeals held that Jones was not entitled to notice under the change of ownership clause because it applies only when there has been a change or division of ownership during the lease term, and there was no such change during Jones’s “tenure” as lessee.<sup>58</sup> However, the lease did not say anything about a change during any particular lessee’s “tenure,” only that the lessor must give notice to the lessee. Perhaps the court is relying upon the presumed waiver by Western Gas; perhaps the court actually means that only changes during the “tenure” of a particular lessee trigger the protection of the change of ownership clause. The court commented that Jones could have examined the record or obtained a title opinion, but of course, avoiding that obligation is exactly why a change of ownership clause is included in a lease. The lessee can obtain a title opinion, put division orders in place, rely on the change of ownership provision, maintain a lease file with any transfer of ownership notice received, and never examine title again.

Here, the court relied on the doctrine of constructive notice. Jones was charged with constructive notice because the deed to Clem was on file when Jones took the leasehold interest.<sup>59</sup> The filing of the deed was notice to all persons, and “[t]he doctrine of constructive notice creates an irrebuttable presumption of actual notice” in certain situations.<sup>60</sup>

Jones also tried to rely on a “division order” document that was unsigned by Clem, which also had a disclaimer of any warranty that it reflected the correct title.<sup>61</sup> The opinion was unclear about the exact nature of this document, but it was clearly not a division order, and we can only assume that it was some kind of paydeck.

Because there is so little precedent on the change in ownership clause, the case could be significant, but the facts are so unclear that it is difficult to analyze. A holding that the change of ownership clause is only triggered by a change that occurs during the “tenure” of a particular lessee seems unsupportable. Given that properties are frequently sold today without a title opinion and often with very poor (or no) lease files, the

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56. *Id.* at \*1.

57. *Id.* at \*3.

58. *Id.*

59. *Id.* at \*4.

60. *Id.* (citing *HECI Exploration Co. v. Neel*, 982 S.W.2d 881, 887 (Tex. 1998)).

61. *Id.*

allocation of risks in the purchase and sale agreement becomes very important. Allocating risk based on the effective date of a sale may not be effective to limit a purchaser's risk because a purchaser could pay the wrong party going forward, just as Jones did in this case.

#### IV. INDUSTRY CONTRACTS

*Tawes v. Barnes*<sup>62</sup> held that a lessor of lands included within a Joint Operating Agreement (JOA) had no right to sue under the JOA, either as a third-party beneficiary of the JOA or by virtue of having privity of estate. Two adjacent tracts of land were leased by landowners Barnes and Baker. Thereafter, the Barnes Lease and the Baker Lease were pooled into a single unit. The working interest owners in the unit entered into a Working Interest Unit Agreement (WIUA) and an attached JOA.<sup>63</sup> Moose, a non-operator and one of the lessees under the Baker Lease, proposed drilling two additional wells in the pooled unit under the terms of the JOA. The operator, who was the lessee under the Barnes Lease, elected to go non-consent. Moose, Tawes, and various other non-operators who owned the lessee's interest under the Baker Lease drilled the wells. Moose acted as operator for the consenting parties in drilling the wells. Tawes and another company later acquired Moose's working interest in the Baker Lease and the wells in a foreclosure sale. At issue in this case was Tawes's liability, as a consenting party, for the payment of royalty to Barnes under the provisions of the WIUA and JOA.<sup>64</sup>

The JOA in Article VI.B2 provided that "[t]he entire cost and risk of conducting such operations shall be borne by the Consenting Parties in the proportions they have elected to bear."<sup>65</sup> In a subsequent portion of Article VI, the JOA provided that

[d]uring the period of time Consenting Parties are entitled to receive Non-Consenting Party's share of production, or the proceeds therefrom, Consenting Parties shall be responsible for the payment of all production, severance, excise, gathering and other taxes, and all royalty, overriding royalty and other burdens applicable to Non-Consenting Party's share of production.<sup>66</sup>

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62. *Tawes v. Barnes*, 340 S.W.3d 419, 428–29, 451 (Tex. 2011). For other notable cases dealing with industry contracts, see *Chesapeake Operating, Inc. v. Sanchez Oil & Gas Corp.*, CIV.A. H-11-1890, 2012 WL 2133554 (S.D. Tex. June 12, 2012) (exculpatory clause under 1977 and 1982 M.F.O.A); *Paradigm Oil, Inc. v. Retamco Operating, Inc.*, 372 S.W.3d 177 (Tex. 2012) (fraud based on concealment of payout); *Sonerra Res. Corp. v. Helmerich & Payne Int'l Drilling Co.*, No. 01-11-00459-CV, 2012 WL 3776428 (Tex. App.—Houston. [1st Dist.] Aug. 30, 2012, pet. denied) (mem. op.) (indemnity under drilling contract); *Long v. Rim Operating, Inc.*, 345 S.W.3d 79 (Tex. App.—Eastland 2011, pet. denied) (enforceability of JOA blackout provision); *Aurora Petroleum, Inc. v. Cholla Petroleum Inc.*, No. 07-10-0035-CV, 2011 WL 652843 (Tex. App.—Amarillo Feb. 23, 2011, no pet.) (mem. op.) (FOA unenforceable without test well site).

63. *Tawes*, 340 S.W.3d at 421.

64. *Id.* at 424–25.

65. *Id.* at 422.

66. *Id.* at 423.

The Texas Supreme Court called this the "Royalty Provision" for identification.<sup>67</sup>

The JOA in this case was similar to most JOAs because it allocated all costs and expenses, along with the sharing of revenue, in accordance with an allocation based on the interests owned by the working interest owners. However, the Royalty Provision recited that "Consenting Parties shall be responsible for the payment of . . . all royalty," language that was arguably consistent with either joint or several liability for royalty payments between and among the Consenting Parties.<sup>68</sup>

Barnes asserted that Tawes, as a Consenting Party, was liable for all royalty owed to her, and she asserted that she had standing to sue under the Royalty Provision as a third-party beneficiary of the JOA. Alternatively, Barnes argued that she could recover against Tawes for the payment of royalty because they were in privity of estate. The federal courts found Tawes to be liable and responsible for all royalty, and the matter arrived at the Texas Supreme Court by way of certified questions from the United States Court of Appeals for the Fifth Circuit.<sup>69</sup>

The supreme court considered the following certified question as one of three questions submitted:

1. Does Barnes have any right [to] enforce the [Dominion—Moose Agreements]—the WIUA and JOA—between Dominion, Moose . . . and the Moose Assignees, including Tawes, to recover unpaid royalties, between the date of first production and February 2002, of Baker-Barnes Nos. 1 & 2 wells under what we have called the "Royalty Provision" of the JOA, either as a third-party beneficiary of the WIUA and JOA or by virtue of having privity of estate with Tawes?<sup>70</sup>

Answering the foregoing question, the supreme court first held that Barnes was not a third-party beneficiary.<sup>71</sup> "A third party may enforce a contract it did not sign when the parties to the contract entered the agreement with the clear and express intention of directly benefitting the third party. When the contract confers only an indirect, incidental benefit, a third party cannot enforce the contract."<sup>72</sup> The language of the contract must be clear, and the intent of the contracting parties controls. "Traditionally, Texas courts have maintained a presumption against third-party beneficiary agreements."<sup>73</sup> "Therefore, in the absence of a clear and unequivocal expression of the contracting parties' intent to directly benefit a third party, courts will not confer third-party beneficiary status by

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67. *Id.*

68. *Id.*

69. *Id.* at 424.

70. *Id.* (alteration and ellipses in original).

71. *Id.* at 426.

72. *Id.* at 425 (citing *MCI Telecomm. Corp. v. Tex. Util. Elec. Co.*, 995 S.W.2d 647, 651 (Tex. 1999)).

73. *Id.* (citing *Corpus Christi Bank & Trust v. Smith*, 525 S.W.2d 501, 503-04 (Tex. 1975)).

implication.”<sup>74</sup>

Here, Dominion and Moose did not express a clear intent to directly benefit Barnes, and any benefit received by her was merely incidental.<sup>75</sup>

JOAs are “contract[s] typical to the oil and gas industry whose function is to designate an operator, describe the scope of the operator’s authority, provide for the allocation of costs and production among the parties to the agreement, and provide for recourse among the parties if one or more default in their obligations.”<sup>76</sup>

The supreme court deduced “from the oil and gas industry’s customary purpose for using JOAs, and from the plain language of the JOA at issue here, that neither Dominion nor Moose included the JOA Royalty Provision with the intention of directly benefitting any lessor of a Baker Unit lease.”<sup>77</sup>

We do not find it determinative that the 1982 version of the AAPL’s Model Form JOA used here does not expressly waive third-party liability like the contract at issue in *MCI* . . . . Instead, the controlling factor is the absence of any sufficiently clear and unequivocal language demonstrating an intent to directly benefit Barnes or any other would-be beneficiary of the contract.<sup>78</sup>

Accordingly, Barnes was not a third-party beneficiary to the JOA.

Barnes argued that, even if she was not a third-party beneficiary, she could recover against Tawes for the payment of royalty because they were in privity of estate. “‘Liability to . . . [a] lessor for the payment of rent or the performance of other lease covenants may arise from either privity of contract or privity of estate.’”<sup>79</sup> Barnes asserted that Tawes came into privity of estate with her when Tawes undertook the obligation to pay royalty under the Barnes Lease. This argument is apparently based on the reasoning that the original lessee had to pay royalty to Barnes, Moose agreed to pay the royalty owed by the original lessee pursuant to the JOA, Tawes acquired Moose’s interest, and therefore Tawes must pay Barnes.

“[W]hen privity of estate exists between an assignee of an oil and gas lessee’s entire leasehold interest and the original oil and gas lessor, the assignee must pay the lessor’s royalties as required by the oil and gas lease.”<sup>80</sup> However, Tawes’s interest in the Barnes Lease was derived from the JOA and WIUA, and Tawes’s interest in the Baker-Barnes Wells No. 1 and No. 2 became possessory when the operator of the Barnes Lease went non-consent. Article III.B of the JOA expressly provided that

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74. *Id.* (citing *MCI Telecomm. Corp.*, 995 S.W.2d at 651).

75. *Id.* at 428–29.

76. *Id.* at 426 (quoting *Seagull Energy E&P, Inc. v. Eland Energy, Inc.*, 207 S.W.3d 342, 345 (Tex. 2006)) (internal citations omitted).

77. *Id.*

78. *Id.* at 428.

79. *Id.* at 429 (alterations in original) (quoting *Amco Trust Inc. v. Naylor*, 317 S.W.2d 47, 50 (Tex. 1958)).

80. *Id.*

“[n]othing contained in this [contract] shall be deemed an assignment or cross-assignment of interests covered hereby.”<sup>81</sup> Moreover, the JOA provided the methodology used to calculate the period of time the consenting parties are granted temporary ownership of the non-consenting parties’ share of production. This time period is of a limited duration, and the non-consenting parties’ share of production will revert back to the non-consenting parties at the end of the time period.<sup>82</sup> “Therefore, the terms of the Dominion-Moose Agreements make clear that by opting to go non-consent as to the Baker-Barnes Wells No. 1 and No. 2, Dominion did not assign its interest as Barnes’s lessee to Tawes or any other consenting party.”<sup>83</sup> Instead, Dominion retained a reversionary interest in the non-consent wells. Tawes, as a consenting party, received no permanent interest in the Barnes Lease. Accordingly, privity of estate did not exist between Barnes and Tawes.

In response to the Fifth Circuit’s first certified question, the Texas Supreme Court held “that Barnes ha[d] no right to enforce the Dominion–Moose Agreements as a third-party beneficiary or by way of privity of estate.”<sup>84</sup> The other two certified questions were only applicable in the event that Barnes could enforce the Dominion–Moose Agreements. Accordingly, because Barnes could not enforce the Agreements, the supreme court did not address the following two certified questions:

2. If Barnes may enforce the [Dominion–Moose Agreements], does the WIUA prevent Barnes from recovering from Tawes? . . .
3. If Tawes, as a Consenting Party, is responsible for royalties under the JOA, does the JOA Royalty Provision change the agreement within the JOA such that Tawes is responsible for all of Barnes’[s] unpaid royalty jointly and severally, or does the JOA limit Tawes’[s] liability for unpaid royalty to the extent of his interest in the two wells at issue between the date of first production and February 2002?<sup>85</sup>

This case is significant because it does not open the door for lessors to assert that they are third-party beneficiaries under this common form JOA. There are many terms and provisions in a typical JOA that arguably could tie back to implied or express lease covenants. While there is no doubt that no one in the industry has actually intended that result, except in the most unusual of documents, if the Texas Supreme Court had read that intent into this form JOA, then the unintended consequence of the use of the forms would have been to significantly increase the risk of liability for working interest owners.

*Reeder v. Wood County Energy, L.L.C.*<sup>86</sup> held that the gross negligence or willful misconduct exculpatory clause in the 1989 Model Form Operat-

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81. *Id.* (alterations in original).

82. *Id.* at 429–30.

83. *Id.* at 430.

84. *Id.* at 431.

85. *Id.* at 431, 424–25 (alterations in original).

86. *Reeder v. Wood Cnty. Energy, L.L.C.*, 395 S.W.3d 789 (Tex. 2012).

ing Agreement applied to breach of contract claims, but in this case, there was insufficient evidence to support a finding against the operator. Reeder became the “Operator”<sup>87</sup> of a property subject to a JOA modeled after the 1989 Model Form JOA.<sup>88</sup> It contained an exculpatory clause that limited the Operator’s liability for “its activities under this agreement” to actions involving gross negligence and willful misconduct.<sup>89</sup> There was an unusual provision incorporated into this JOA providing that the Operator “agrees to produce and/or conduct operations on the [Contract Area] sufficient to maintain the leases and the unit.”<sup>90</sup> The Operator had a poor relationship with his non-operating working interest owners (non-operators).<sup>91</sup> Consequently, when it became apparent that several of the wells would have to undergo expensive testing and repairs, the Operator was unable to obtain the consent of some of the non-operators. The JOA forbade the Operator from undertaking any project expected to cost more than \$5,000 without consent, except in emergencies.<sup>92</sup> The Operator put in some of his own money, until he ran out of money. Because the testing and repairs were not performed, the Texas Railroad Commission suspended production and ordered the well to be plugged,<sup>93</sup> and the underlying leasehold interest was lost.<sup>94</sup> The JOA required the Operator to offer the well to the non-operators if the Operator elected to abandon or plug the well, but the Operator made no such offer.<sup>95</sup>

Multiple claims were asserted, but this appeal was focused on the damages awarded to the non-operators by the jury because the Operator failed to maintain production and failed to offer the well to the non-operators before it was plugged. The trial court applied the gross negligence and willful misconduct standard and properly instructed the jury on that standard.<sup>96</sup>

The Texas Supreme Court first considered the applicability of the JOA’s exculpatory clause to adjudicate the breach of contract claims against the Operator. The exculpatory clause in the 1977 and 1982 Model Form Operating Agreements limited liability for “all such operations,” but the 1989 Model Form Operating Agreement limited liability for “activities under this agreement.”<sup>97</sup> Case law under the earlier forms generally held that the exculpatory clause applied only to operations on the Contract Area and not to contract claims.<sup>98</sup>

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87. *Id.* at 791.

88. *Id.* at 793 (citing A.A.P.L. Form 610, Model Form Operating Agreement—1989, American Association of Petroleum Landmen).

89. *Id.*

90. *Reeder v. Wood Cnty. Energy, L.L.C.*, 320 S.W.3d 433, 446 (Tex. App.—Tyler 2010, pet. granted).

91. *Reeder*, 395 S.W.3d at 791.

92. *Id.* at 797.

93. *Id.* at 791.

94. *Id.*

95. *Id.* at 792.

96. *Id.* at 797.

97. *Id.* at 794.

98. *Id.* at 793–94



The supreme court first noted that some commentary concludes that the change in language effectively broadened the scope of the exculpatory clause.<sup>99</sup> The supreme court also applied its own semantic analysis:

Here, the parties modeled their JOA after the 1989 model form—recognizing the distinction between “such operations” and “its activities.” The modifier “such” references operations under the JOA, while the deletion of that word and use of the term “its activities” includes actions under the JOA that are not limited to operations.<sup>100</sup>

According to the supreme court, this expanded application of the exculpatory clause meant that the Operator in this case was not liable for breach of contract unless the Operator’s conduct rose to the level of gross negligence or willful misconduct.<sup>101</sup>

Applying this standard, the supreme court evaluated the sufficiency of the evidence for the claims in the case.<sup>102</sup> The supreme court noted that gross negligence requires that “the defendant knew about the peril, but his acts or omissions demonstrate that he did not care.”<sup>103</sup> The substance of the breach of contract claims appeared to be the Operator’s failure to complete testing and repairs that the wells required, and the Operator’s failure to comply with the JOA provision that required him to offer the well to the non-operators prior to plugging it.<sup>104</sup> In regards to the former, the Operator testified that he sought permission and funding from the non-operators, but they declined his requests.<sup>105</sup> Regarding his failure to offer the well to the other non-operators, the supreme court noted that because the Operator was ordered to plug the well, he did not have an opportunity to offer it to the non-operators.<sup>106</sup> Considering this evidence in the context of the entire record, the supreme court held that there was no evidence to support a finding of gross negligence or willful misconduct.<sup>107</sup>

This case is important because it determined the scope of the exculpatory clause under the 1977, 1982, and 1989 Model Form Operating Agreements and clearly held that the operator’s liability under the 1989 form was significantly less than the operator’s liability under the 1977 and 1982 forms.

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99. *Id.* at 794 (citing Robert C. Bledsoe, *The Operating Agreement: Matters Not Covered or Inadequately Covered*, 47 ROCKY MTN. MIN. L. INST. § 15.03[1] (2001); Wilson Woods, Comment, *The Effect of Exculpatory Clauses in Joint Operating Agreements: What Protections Do Operators Really Have in the Oil Patch?*, 38 TEX. TECH. L. REV. 211, 214–15 (2005)).

100. *Id.* at 795.

101. *Id.*

102. *Id.* at 795–97.

103. *Id.* at 796 (quoting *Diamond Shamrock Ref. Co. v. Hall*, 168 S.W.3d 164, 173 (Tex. 2005)).

104. *Id.*

105. *Id.* at 797.

106. *Id.*

107. *Id.*

## V. LITIGATION

*BP America Production Co. v. Marshall*<sup>108</sup> held that, among cotenants, the payment of a royalty, rather than a cotenant share, is sufficiently hostile to put the cotenant on notice for adverse possession. The case also held that the accrual of a cause of action for fraud is not deferred by the discovery rule and that the statute of limitations for fraud is not tolled by fraudulent concealment when the alleged fraud could have been discovered with reasonable diligence in Texas Railroad Commission (TRC) records.<sup>109</sup> In the 1970's, BP obtained oil and gas leases on the Slator Ranch, including a lease from the Marshall family (Marshall) covering 1/16 of the minerals and a lease from the Vaquillas family (Vaquillas) covering 1/4 of the minerals. The leases contained common savings clauses that allowed them to continue beyond the primary term, provided that BP was engaged in "good-faith drilling or reworking operations designed to produce paying quantities of oil or gas with no cessation of operations for more than sixty days."<sup>110</sup> Two weeks before the expiration of the primary term in July 1980, BP drilled a well. BP continued work on the well throughout the remainder of the year, but it never achieved production. The lessors inquired about the status of the well and the leases. BP informed them that it was engaged in continuous operations sufficient to satisfy the savings clause and keep the leases in effect. The lessors did not engage in any further inquiries or investigate public records. On March 25, 1981, BP transferred its interest to Sanchez-O'Brien. Sanchez-O'Brien drilled a productive well in April 1981, and later the leases were assigned to Wagner.<sup>111</sup> It was undisputed that all lessees had conducted continuous, good-faith operations since April 1981.

The lawsuit was first filed in 1997. Marshall conceded that Wagner had acquired the leasehold title by adverse possession and went to trial against BP on a fraud claim. Marshall obtained a favorable jury finding on fraud, and the issue on appeal was BP's statute of limitations defense.<sup>112</sup> Vaquillas settled with BP and then went to trial against Wagner, claiming that the title reverted to Vaquillas prior to the assignment of the lease from BP.<sup>113</sup> The issue on appeal was Wagner's adverse possession of the leasehold title. Thus, notwithstanding the complications of the differ-

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108. *BP Am. Prod. Co. v. Marshall*, 342 S.W.3d 59, 63 (Tex. 2011). For other notable cases dealing with litigation, see *Enbridge Pipelines (East Texas) L.P. v. Avinger Timber, LLC*, 386 S.W.3d 256 (Tex. 2012) (condemnation of gas plant site); *Bomar Oil & Gas, Inc. v. Loyd*, 381 S.W.3d 689 (Tex. App.—Amarillo 2012, pet. denied) (collateral estoppel based on division order); *May v. Buck*, 375 S.W.3d 568 (Tex. App.—Dallas 2012, no. pet.) (statute of frauds); *Conley v. Comstock Oil & Gas, LP*, 356 S.W.3d 755 (Tex. App.—Beaumont 2011, no. pet.) (common law adverse possession and ten-year statute); *Teon Mgmt., LLC v. Turquoise Bay Corp.*, 357 S.W.3d 719 (Tex. App.—Eastland 2011, pet. denied) (trespass to try title for lease termination); *XTO Energy Inc. v. Nikolai*, 357 S.W.3d 47 (Tex. App.—Fort Worth 2011, pet. denied) (estoppel by deed in trespass by try title).

109. *Marshall*, 342 S.W.3d at 68–69.

110. *Id.* at 63.

111. *Id.* at 64.

112. *Id.* at 65.

113. *Id.* at 64.

ing positions among the parties, the issues on appeal were (1) whether the accrual of the cause of action for fraud was deferred by the discovery rule, and/or whether the statute of limitations was tolled by fraudulent concealment; and (2) whether Wagner's conduct satisfied the requirements for adverse possession.<sup>114</sup>

Under the discovery rule, the accrual of a cause of action is deferred "until the injury could reasonably have been discovered."<sup>115</sup> The rule is reserved for injuries that are "inherently undiscoverable," and the evidence of injury is "objectively verifiable."<sup>116</sup> An injury is not inherently undiscoverable if it can "be discovered through the exercise of reasonable diligence."<sup>117</sup> Applying these rules, the Texas Supreme Court concluded that the accrual of the cause of action was not deferred on Marshall's fraud claim because evidence of BP's failure to maintain the lease was in the TRC records.<sup>118</sup> BP had filed a well log and a plugging report with the TRC, and these documents were publicly available. If Marshall had chosen to exercise reasonable diligence, Marshall could have discovered that BP was not making good-faith efforts to produce. Therefore, the discovery rule did not apply.

In reaching its holding, the supreme court repeated that the discovery rule is applied categorically and that it is a very limited exception to statutes of limitations.<sup>119</sup> It specifically referred to *HECI Exploration Co. v. Neel*, a case where it had previously held that the discovery rule would not apply when the necessary facts were available in public records at the TRC.<sup>120</sup> Thus, it now appears clear that the discovery rule will not apply to the "category" of cases where the information necessary to discover the injury is publicly available at the TRC.

Fraudulent concealment is an equitable doctrine that may operate to extend the limitations period, and unlike the discovery rule, deciding whether the doctrine applies is a fact-specific inquiry.<sup>121</sup> "A defendant's fraudulent concealment of wrongdoing may toll the statute of limitations after the cause of action accrues."<sup>122</sup> There was evidence, which the jury accepted, that BP concealed its problems on the lease.<sup>123</sup> Nevertheless, the necessary information was also available at the TRC, and because a lessor is required to exercise due diligence the supreme court held that, as a matter of law, Marshall would have been able to discover BP's fraud.<sup>124</sup>

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114. *Id.* at 64–65.

115. *Id.* at 65 (citing *Computer Assocs. Int'l, Inc. v. Altai, Inc.*, 918 S.W.2d 453, 455–56 (Tex. 1996)).

116. *Id.* at 65–66 (citing *Altai*, 918 S.W.2d at 456).

117. *Id.* at 66 (citing *Wagner & Brown, Ltd. v. Horwood*, 58 S.W.3d 732, 734–35 (Tex. 2001)).

118. *Id.* at 67.

119. *Id.* at 66–67.

120. *Id.* at 66 (citing *HECI Exploration Co. v. Neel*, 982 S.W.2d 881, 886 (Tex. 1998)).

121. *Id.* at 67.

122. *Id.* (citing *Kerlin v. Saucedo*, 263 S.W.3d 920, 925 (Tex. 2008)).

123. *Id.* at 68.

124. *Id.* at 69.

TRC records will now defeat claims of fraudulent concealment if the necessary facts to discover the injury are publicly available.

In *Vaquillas's* suit against *Wagner* to regain the leasehold, *Wagner* argued that even if the lease had reverted to *Vaquillas*, *Wagner* had since regained the leasehold interest through adverse possession. The dispute boiled down to whether *Wagner's* conduct was sufficiently hostile to put *Vaquillas*, as cotenant, on notice of *Wagner's* intent to oust him (ouster as between cotenants).<sup>125</sup>

The supreme court noted that when a lease expires the former lessor becomes an unleased cotenant.<sup>126</sup> An unleased cotenant is "entitled to 'the value of the minerals taken less the necessary and reasonable cost of producing and marketing the same . . . .'"<sup>127</sup> In *Vaquillas's* case, a cotenant's share would have entitled *Vaquillas* to approximately 25% of production. *Wagner* had only paid *Vaquillas* a royalty interest of 4.23%. The great disparity between these two amounts, the characterization of the interest owned, and the payment as a "royalty interest" in various documents and records (including division orders) was sufficient to put *Vaquillas* on notice.<sup>128</sup> Accordingly, the supreme court held that *Wagner* had adversely acquired the leasehold estate:

By accepting a clearly labeled and computed royalty, *Vaquillas* was on notice that *Wagner* claimed title to the leasehold—an unequivocal claim to ownership unmistakably inconsistent with and hostile to *Vaquillas's* claim of a cotenant relationship. Accordingly, *Wagner* acquired the same interest it adversely possessed—a leasehold estate as defined by the original lease.<sup>129</sup>

The case is significant because it makes clear that TRC records will generally be sufficient to defeat the application of both the discovery rule and fraudulent concealment to circumvent the statutes of limitations. Because the information filed with the TRC is extensive, this will be significant in oil and gas cases. The case is also significant because of its holding that royalty checks are enough to establish cotenant ouster in a lease termination case. The continuation of payments under a terminated lease will almost certainly be described as royalty payments. The case emphasizes the supreme court's continuing trend of avoiding exceptions to the statutes of limitation and resisting any finding of an enforceable lease termination based on claims made long after the date of termination, notwithstanding that if a lease is a determinable fee.

*Exxon Corp. v. Emerald Oil & Gas Co.*<sup>130</sup> held that the Texas Natural Resources Code creates private causes of action for breach of the statu-

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125. *Id.*

126. *Id.* at 70 (citing *Wagner & Brown, Ltd. v. Sheppard*, 282 S.W.3d 419, 421–22 (Tex. 2008)).

127. *Id.* at 71 (quoting *Cox v. Davison*, 397 S.W.2d 200, 201 (Tex. 1965)).

128. *Id.* at 71–72.

129. *Id.* at 72 (citing *Natural Gas Pipeline Co. Am. v. Pool*, 124 S.W.3d 188, 199 (Tex. 2003)).

130. *Exxon Corp. v. Emerald Oil & Gas Co.*, 331 S.W.3d 419, 420 (Tex. 2010).

tory duties to properly plug wells and to not commit waste, and that subsequent owners do not have standing to sue prior owners for injury to realty if it occurred before the subsequent owner acquired his interest. Exxon Corporation (Exxon) held mineral leases subject to a 50% royalty covering several thousand acres in Refugio County, Texas. During the 1980s, after negotiations to reduce the royalty failed, Exxon systematically plugged and abandoned its wells because the leases were no longer profitable. After the leases terminated, Emerald Oil & Gas Company (Emerald) acquired a portion of the leases and attempted to re-enter the wells, but it encountered unexpected difficulties. Emerald alleged that Exxon caused those difficulties by intentionally sabotaging the wells during Exxon's plugging and abandonment of the leases. Among other claims, Emerald sued Exxon for (1) breach of the statutory duty to properly plug a well, and (2) breach of the statutory duty to not commit waste.<sup>131</sup>

Section 85.321 of the Texas Natural Resources Code provides:

A party who owns an interest in property or production that may be damaged by another party violating the provisions of this chapter . . . or another law of this state prohibiting waste or a valid rule or order of the commission may sue for and recover damages and have any other relief to which he may be entitled at law or in equity.<sup>132</sup>

The Texas Supreme Court held that the plain language of the statute creates private causes of action.<sup>133</sup>

The supreme court next analyzed whether Emerald, as a subsequent lessee, had standing to maintain suit.<sup>134</sup> The supreme court explained that the statute's use of the participle phrase "a party who owns an interest in property . . . may be damaged by another party *violating* the provisions of this chapter" could support different interpretations.<sup>135</sup> This phrase could support an interpretation that an owner may bring suit only for an injury concurrent with ownership. This phrase also could support the interpretation that an owner may bring suit for any past violation or violation concurrent with ownership.

To determine the meaning of the phrase, the supreme court looked to the statute's predecessor, which preserved common law standards. Common law provides that:

[A] cause of action for injury to real property accrues when the injury is committed. The right to sue is a personal right that belongs to the person who owns the property at the time of the injury, and the right to sue does not pass to a subsequent purchaser of the property unless there is an express assignment of the cause of action.<sup>136</sup>

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131. *Id.* at 421.

132. *Id.* at 422 (quoting TEX. NAT. RES. CODE ANN. § 85.321 (West 2001)).

133. *Id.*

134. *Id.* at 424.

135. *Id.* (emphasis added).

136. *Id.* (citation omitted).

The supreme court clarified some confusion that originated in its prior, withdrawn opinion by explaining that its holding was not intended to mean that only Exxon could sue Exxon. The royalty owners could have standing to sue and actually did sue, but they were too late in this case.<sup>137</sup>

The supreme court also deleted from its withdrawn opinion the holding that Exxon's actions did not constitute waste. Given that the court concluded Emerald had no standing on the plugging claim, it must have concluded that no standing on the waste claim was sufficient for its holding, without reaching the question of whether Exxon's actions did or did not constitute waste.<sup>138</sup>

The significance of the case is the unequivocal holding that the Texas Natural Resources Code creates a private cause of action for damages resulting from statutory violations. In dictum, the supreme court also recognized that there is a statutory defense to such civil claims based on the reasonably prudent operator standard.<sup>139</sup> The holding that a subsequent owner lacks standing to sue for pre-existing damages to realty, absent an express assignment of the cause of action,<sup>140</sup> is consistent with long-standing precedent.

*Exxon Corp. v. Emerald Oil & Gas Co.*<sup>141</sup> held that false filings with the Texas Railroad Commission (TRC) will generally not support private causes of action for fraud. This case was the culmination of almost fifteen years of litigation between royalty owners and their lessee, based on disputes arising under leases granted in the 1950s. The leases covered several thousand acres and included a 50% royalty clause and a stringent well data disclosure clause.<sup>142</sup> The leases also required the lessee and successor lessees (collectively, Exxon) to fully develop the field by drilling and completing at least one well in each horizon capable of producing in paying quantities and to operate the tract in a way that realized the full value of the leased premises.<sup>143</sup> During the term of the leases, Exxon drilled 121 wells and produced at least fifteen million barrels of oil and more than sixty-five billion cubic feet of gas, resulting in the payment of more than \$43 million in royalties. As the field began to decline, Exxon sought to amend the leases and reduce the royalty.<sup>144</sup> The royalty owners refused, and negotiations continued for years, increasing in intensity as Exxon's threat to plug and abandon became more imminent. The royalty owners identified other oil companies interested in taking over the leases and urged Exxon to sell or transfer its interest to some other company.

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137. *Id.* at 425 n.4; see *Exxon Corp. v. Miesch*, No. 13-00-00104-cv, 2012 WL 4854726 (Tex. App.—Corpus Christi-Edinburg Oct. 11, 2012) (mem. op.).

138. See *Exxon Corp. v. Emerald Oil & Gas Co.*, No. 05-0729, 2009 WL 795760 (Tex. Mar. 27, 2009), *opinion withdrawn and superseded by*, 331 S.W.3d 419 (Tex. 2010).

139. *Exxon Corp.*, 331 S.W.3d at 422.

140. *Id.* at 425.

141. *Exxon Corp. v. Emerald Oil & Gas Co.*, 348 S.W.3d 194, 198 (Tex. 2011).

142. *Id.* at 199.

143. *Id.* at 210.

144. *Id.* at 199.

Because Exxon determined that the leases were no longer profitable, it finally began plugging wells in 1989. The royalty owners threatened to sue Exxon in August of 1990 if Exxon plugged any wells that were capable of producing in paying quantities. The royalty owners threatened to sue under the lease contracts and under the common law doctrine of waste. As Exxon plugged the wells, it disclosed the plugging methods for each well in a plugging report on Form W-3 filed with the TRC.<sup>145</sup> The filing requires that the operator disclose the specific methods used to plug the wells and sign an oath verifying that the statements in the report are true.<sup>146</sup> Exxon pursued the plugging project until its completion in 1991, despite objections from the royalty owners and offers from potential buyers.<sup>147</sup>

In 1993, after the leases had terminated, the royalty owners leased part of the lands originally included in Exxon's leases to Pace West Production, Ltd. (Pace), later known as Emerald Oil & Gas Company, L.C. (Emerald). In deciding whether to lease, Emerald reviewed Exxon's publicly filed plugging reports. The filings seemed to indicate that Exxon had properly plugged the wells, but when Emerald attempted to reopen the plugged wells in 1994, Emerald's attempts proved futile because it encountered junk in the holes. In a 1994 written report to the royalty owners, Emerald indicated that Exxon had cut casings while plugging the wells and that Emerald found junk in the wells.<sup>148</sup> In January 1995, Emerald obtained Exxon's internal well records on the plugged wells from another party on an adjoining tract and discovered that Exxon's internal records differed substantially from the records filed with the TRC. Concluding that Exxon intentionally sabotaged the field, Emerald sued Exxon in July of 1996, and the royalty owners intervened in August and September of 1996.

The trial court severed the plaintiffs' negligence per se claim and claims based on the statutory duties to properly plug the wells and to avoid committing waste.<sup>149</sup> The statutory claims and the issues on private causes of action and standing were resolved in the companion case also styled *Exxon Corp. v. Emerald Oil & Gas Co.*<sup>150</sup>

All of the tort claims asserted and appealed in this case that were subject to a two-year statute of limitations were held to be barred by limitations.<sup>151</sup> The remainder of the opinion focused on two things: (1) the alleged fraud in the Form W-3s that were filed with the TRC, and (2) the

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145. *Id.* at 200.

146. *Id.* at 200 n.3 (citing 16 TEX. ADMIN. CODE § 3.14 (West 2013)).

147. *Id.* at 200.

148. *Id.* at 201.

149. *Id.*

150. *See Exxon Corp. v. Emerald Oil & Gas Co.*, 331 S.W.3d 419 (Tex. 2010).

151. *Exxon Corp.*, 348 S.W.3d at 202-03. The royalty owners had knowledge of the alleged injuries caused by early abandonment no later than the 1990 letter threatening to sue Exxon, and the royalty owners and Emerald had actual knowledge of the alleged injuries to the wellbores no later than June 1994 or more than two years before suit was filed as to both sets of claims. *Id.* at 206.

royalty owners' claim that Exxon breached the development clauses in the leases.<sup>152</sup>

Regarding plaintiffs' claim of fraud based on the Form W-3s filed with the TRC, Exxon did not dispute that it plugged at least some of the wells using non-standard plugging procedures.<sup>153</sup> It admitted to cutting the well casing and leaving it in the wellbore. Emerald and the royalty owners claimed that Exxon injured them by making material misrepresentations on its plugging reports, upon which the plaintiffs justifiably relied.<sup>154</sup> However, to prevail on their claim of fraud, the plaintiffs also had to demonstrate that Exxon "made the representation with the intent that the other party would act on that representation or intended to induce the party's reliance on the representation."<sup>155</sup>

The TRC rules provide that "[n]on-drillable material that would hamper or prevent re-entry of a well shall not be placed in any wellbore during plugging operations. . . . Pipe and unretrievable junk shall not be cemented in the hole during plugging operations without prior approval by the district director . . . ."<sup>156</sup> Exxon obviously did not comply with this rule. Exxon nevertheless claimed that it could not have anticipated that the plugging reports it filed would impact future operators because the reporting requirements were intended to protect against pollution and are not intended to provide notice to future operators.<sup>157</sup> The Texas Supreme Court rejected Exxon's argument based on the TRC's stated objectives for the reporting requirements, which included: (1) protecting the environment and (2) allowing "re-entry into the wells for commercial purposes."<sup>158</sup>

Although the supreme court accepted Emerald's argument that false information in the plugging records could reasonably induce detrimental reliance, the supreme court stated that this alone did not establish that Exxon *intended* to induce the plaintiffs' reliance.<sup>159</sup> Rather, the plaintiffs were required to show that "[t]he maker of the misrepresentation [has] information that would lead a reasonable man to conclude that there is an especial likelihood that it will reach those persons and will influence their conduct."<sup>160</sup> This is a specific, focused inquiry. Reliance on public information gathered as part of a general industry practice, even if it turns out to be false, is insufficient as a matter of law.<sup>161</sup> The inquiry "is not satisfied by evidence that a misrepresentation may be read in the fu-

152. *Id.* at 216–17.

153. *Id.* at 200 n.5.

154. *Id.* at 206.

155. *Id.* at 217 (citing *DeSantis v. Wackenhut Corp.*, 793 S.W.2d 670, 688 (Tex. 1990)).

156. *Id.* at 218 (quoting 16 TEX. ADMIN. CODE § 3.14(d)(10) (West 2013)).

157. *Id.*

158. *Id.*

159. *Id.*

160. *Id.* at 219 (alterations in original) (quoting RESTATEMENT (SECOND) OF TORTS § 531 cmt. d (1977)).

161. *Id.* (citing *Ernst & Young, L.L.P. v. Pac. Mut. Life Ins. Co.*, 51 S.W.3d 573, 580–82 (Tex. 2001)).



ture by some unknown member of the public or of a specific industry."<sup>162</sup> The supreme court found that Pace's earlier attempts to acquire the wells and Emerald and the royalty owners' attempts to stop Exxon's plugging could be evidence of fraud.<sup>163</sup> Additionally, there were fact issues regarding intent, such as whether Pace and Emerald were effectively the same entity and whether the W-3s were actually inaccurate. Because of these issues, the supreme court reversed the trial court's directed verdict for Exxon and remanded that issue to the trial court.<sup>164</sup>

The leases with Exxon contained a development clause that required Exxon to fully develop the leased tracts.<sup>165</sup> The tracts were deemed "fully developed" when "at least one (1) well has been drilled and completed in each horizon or stratum capable of producing oil or sulphur in paying quantities for each twenty (20) acres of said tract."<sup>166</sup> As required by the lease, Exxon generally drilled the required number of wells.<sup>167</sup> However, the royalty owners claimed that Exxon did not "complete" two productive zones because it failed to exploit the full potential of the tracts. Also, the royalty owners claimed that, because Article 4 of the leases required Exxon to realize the "full value" of the tract, Exxon was required to drill more than the single well specified for each horizon when the land could be further developed before it could abandon the leases.

Because Article 3 specified the number of wells required to fully develop the land, the supreme court held that Article 3 established and limited Exxon's duty.<sup>168</sup> "Where the Lease expressly defines the duty, we will not impose a more stringent obligation unless it is clear that the parties intended to warrant production beyond that defined obligation."<sup>169</sup> The supreme court held that under this particular lease (with its express development clause) and in the absence of an express clause defining "drilled and completed," for a well to be drilled and completed "a hole must be bored in the ground, and if oil or gas in paying quantities is encountered, the casing must be perforated or otherwise prepared for production."<sup>170</sup> The supreme court also noted that "completed" meant capable of producing oil or gas, without a requirement that it be actually producing or ever produce, and that by contract parties may agree that a well is completed even though it is a dry hole.<sup>171</sup> Because Exxon drilled the required number of wells and produced in paying quantities from the two contested zones, the supreme court held that Exxon did not breach the leases, even though it did not fully exploit the zones' potential.<sup>172</sup>

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162. *Id.*

163. *Id.* at 219-20.

164. *Id.* at 221.

165. *Id.* at 210.

166. *Id.*

167. *Id.* at 213.

168. *Id.* at 214.

169. *Id.* at 215.

170. *Id.* at 212.

171. *Id.*

172. *Id.* at 216.

Exxon was not liable for breaching the development clause of the leases.<sup>173</sup>

The significance of the case is the supreme court's holding that false filings with the TRC did not support private causes of action based on fraud, except in very narrow circumstances.<sup>174</sup> A plaintiff must show that the party making the false filing has information that would lead a reasonable person to conclude that there is an especial likelihood that it will reach those persons and influence their conduct. The fact that the information may influence some unknown person, or the fact that the industry generally relies upon such filings, is not enough. The case also provides a definition of "drill and complete," which at least under this lease is construed to mean to drill and perforate the hole or otherwise prepare for production. The contention that "complete" means to fully develop, when used in the context of this case, was rejected. Finally, the plaintiffs' loss on all the two-year tort claims based on limitations suggests that landowners should be more aggressive about filing suit or seeking tolling agreements, regardless of the status of on-going lease negotiations.

## VI. REGULATION

*Texas Rice Land Partners, Ltd. v. Denbury Green Pipeline-Texas LLC*<sup>175</sup> held that the grant of a T-4 permit to a pipeline company by the Texas Railroad Commission (TRC) did not conclusively establish the company's status as a common carrier and confer on the company the power of eminent domain. The company seeking to exercise the power of eminent domain has the burden of establishing that it is a common carrier. Texas Rice refused Denbury Green access to Texas Rice's property to survey the proposed location of a carbon dioxide pipeline. Denbury Green filed suit claiming it was a common carrier and requested a permanent injunction preventing Texas Rice from denying it access to the property.<sup>176</sup> Denbury Green prevailed on summary judgment, primarily based on the T-4 permit granted by the TRC.<sup>177</sup> The principal issue was whether a landowner can challenge in court the eminent domain power of a pipeline company holding a common carrier permit to operate a pipeline issued by the TRC.

The Texas Supreme Court began its review by analyzing Section 111.002(6) of the Texas Natural Resources Code, which states that a person is a common carrier if he:

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173. *Id.*

174. *Id.*

175. *Tex. Rice Land Partners, Ltd. v. Denbury Green Pipeline-Tex., LLC*, 363 S.W.3d 192, 204 (Tex. 2012). For other notable cases dealing with regulation, see *R.R. Comm'n of Tex. v. Tex. Citizens for a Safe Future & Clean Water*, 336 S.W.3d 619 (Tex. 2011) (TRC injection well permitting process); *W. Ref. Inc. v. FERC*, 636 F.3d 719 (5th Cir. 2011) (FERC jurisdiction over oil pipelines); *Allegiance Hillview, L.P. v. Range Tex. Prod., LLC*, 347 S.W.3d 855 (Tex. App.—Fort Worth 2011, no pet.) (city permitting of well site).

176. *Tex. Rice Land Partners*, 363 S.W.3d at 196.

177. *Id.* at 196, 203–04.

“owns, operates, or manages, wholly or partially, pipelines for the transportation of carbon dioxide . . . to or for the public for hire, but only if such person files with the commission a written acceptance of the provisions of this chapter expressly agreeing that, in consideration of the rights acquired, it becomes a common carrier subject to the duties and obligations conferred or imposed by this chapter.”<sup>178</sup>

A common carrier, as defined by the Texas Natural Resources Code, has the “right and power of eminent domain.”<sup>179</sup> The supreme court noted that “[w]hile these provisions plainly give private pipeline companies the power of eminent domain, that authority is subject to special scrutiny by the courts” because Article 1, Section 17 of the Texas Constitution “prohibits the taking of property for *private* use.”<sup>180</sup>

The supreme court reviewed the TRC’s administrative process in granting an applicant common carrier status and found that it did not include any inquiry or adjudication as to whether the pipeline would be used for public or private purposes.<sup>181</sup>

Apparently, in order to receive a common-carrier permit, the applicant need only place an “x” in a box indicating that the pipeline will be operated as a common carrier, and to agree under Section 111.002(6) to subject itself to “duties and obligations conferred or imposed” by Chapter 111. Under these minimal requirements, Denbury Green reported itself as a common carrier and obtained a permit a few days later.<sup>182</sup>

“Private property cannot be imperiled with such nonchalance, via an irrefutable presumption created by checking a certain box on a one-page government form.”<sup>183</sup> The supreme court held “that the T-4 permit alone did not conclusively establish Denbury Green’s status as a common carrier and confer the power of eminent domain.”<sup>184</sup> “[A] permit granting common-carrier status is *prima facie* valid. But once a landowner challenges that status, the burden falls upon the pipeline company to establish its common-carrier *bona fides* if it wishes to exercise the power of eminent domain.”<sup>185</sup>

The supreme court rejected Denbury Green’s argument that making the pipeline available for public use was sufficient to establish common carrier status.

[T]o qualify as a common carrier under Section 111.002(6), a reasonable probability must exist that the pipeline will at some point after construction serve the public by transporting gas for one or more customers who will either retain ownership of their gas or sell it to

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178. *Id.* at 197 (ellipses in original) (quoting TEX. NAT. RES. CODE ANN. § 111.002(6) (West 2006)).

179. *Id.* (quoting TEX. NAT. RES. CODE ANN. § 111.019(b)).

180. *Id.* (quoting *Maher v. Lasater*, 354 S.W.2d 923, 924 (Tex. 1962)).

181. *Id.* at 199–201.

182. *Id.* at 199.

183. *Id.*

184. *Id.* at 198.

185. *Id.* at 202.

parties other than the carrier.<sup>186</sup>

There was some evidence that Denbury Green intended to fully utilize the pipeline for its own purposes, and therefore, Denbury Green did not establish common carrier status as a matter of law.<sup>187</sup>

The significance of this case is the supreme court's holding that the T-4 permit issued by the TRC is prima facie valid, but when a landowner challenges the company's right to exercise the power of eminent domain, the pipeline company has the burden to establish that it is a common carrier. The pipeline must be for a public use and not just for a private use.<sup>188</sup>

*FPL Farming Ltd. v. Environmental Processing Systems, L.C.*<sup>189</sup> held that subsurface wastewater migration can constitute a trespass at common law. FPL Farming Ltd. (FPL) owned land adjacent to land on which Environmental Processing Systems, L.C. (EPS) was operating a deep wastewater injection well under permits issued by the Texas Commission on Environmental Quality (TCEQ). FPL filed this suit against EPS claiming trespass because the wastewater being injected was naturally migrating into FPL's land. After the jury found that no trespass occurred, and the trial judge entered a take-nothing judgment against FPL, FPL appealed. The Beaumont Court of Appeals affirmed on the basis that the TCEQ permits shielded EPS from tort liability, but the Texas Supreme Court reversed, holding that a TCEQ permit did not shield a tortfeasor from civil liability and remanded this case back to the court of appeals for consideration of all issues raised by the parties related to the alleged trespass.<sup>190</sup> The supreme court did not decide whether subsurface wastewater migration can constitute a trespass or whether it did in this case.<sup>191</sup>

The most important issue on appeal was whether a cause of action exists for trespass for subsurface wastewater migration. First, the supreme court held that FPL, as the owner of the surface, had a possessory interest and ownership interest in the briny water below its tracts sufficient to establish standing to sue for trespass.<sup>192</sup> The supreme court then noted that Texas case law and the Texas Legislature have recognized that a surface owner has a property interest in the water (both fresh and salt water) in place below the surface.<sup>193</sup> The supreme court also noted, as this lawsuit demonstrates, that the subsurface levels have economic value for

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186. *Id.* (footnotes omitted).

187. *Id.* at 204.

188. *Id.*

189. *FPL Farming Ltd. v. Env'tl. Processing Sys., L.C.*, 383 S.W.3d 274, 277-78 (Tex. App.—Beaumont 2012, pet. pending).

190. *Id.* at 278-79; *FPL Farming Ltd. v. Env'tl. Processing Sys., L.C.*, 351 S.W.3d 306, 308 (Tex. 2011).

191. *FPL Farming Ltd.*, 351 S.W.3d at 314-15.

192. *FPL Farming Ltd.*, 383 S.W.3d at 279-80.

193. *Id.* at 280 (citing TEX. WATER CODE ANN. §§ 36.001, 36.002 (West Supp. 2011)); *Edwards Aquifer Auth. v. Day*, 369 S.W.3d 814, 832 (Tex. 2012); *Robinson v. Robbins Petroleum Corp.*, 501 S.W.2d 865, 867 (Tex. 1973)).

storing waste.<sup>194</sup> Further, the Texas Legislature had not given FPL, as an adjacent property owner, the right to pool its affected property with other adjoining landowners in order to capitalize on the commercial storage value of the subsurface levels. Without a trespass remedy, FPL would be unable to protect its commercial interest in its property. The supreme court concluded that FPL had a cause of action for trespass at common law.<sup>195</sup>

The supreme court recognized that it was not constrained to follow the law applicable to surface trespass cases in resolving a subsurface trespass.<sup>196</sup> Nevertheless, the supreme court followed the prior opinions of seven Texas appellate courts in surface trespass cases and held that the burden of consent in a trespass action rests on the alleged trespasser.<sup>197</sup> The supreme court reasoned that the burden should be placed upon the alleged trespasser based on: "(1) the comparative likelihood that a certain situation may occur in a reasonable percentage of cases; and (2) the difficulty in proving a negative."<sup>198</sup> After finding that the jury instruction erroneously placed the burden of proof on the question of consent on FPL, the supreme court held the error was harmful and remanded for a new trial.<sup>199</sup>

This case is important because it establishes a precedent for a cause of action for trespass based on subsurface wastewater migration, even when the injection is permitted by the TCEQ on adjacent lands.

## VII. CONCLUSION

The oil and gas industry routinely operates within two separate universes: (1) title and property rights, which are determined by conveyances and contracts interpreted by the courts; and (2) rights to produce, which are determined by statutes and regulations enforced by regulatory agencies. Nevertheless, the boundaries between those separate universes are not always distinct, and litigants may find that what has transpired in one universe may have an effect on the parallel universe. During this reporting period, perhaps the most important trend has been that courts have resolved some of those overlaps in a way that will limit future litigation.

The Texas Railroad Commission maintains voluminous public records. No authority holds that these documents provide notice or constructive notice affecting the chain of title found in the county records. It is now clear, however, that the duty of reasonable diligence requires that property owners must make themselves aware of relevant information available in the public records at the Texas Railroad Commission because the information in those records may be used to defeat the application of

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194. *Id.* at 281.

195. *Id.* at 282.

196. *Id.* (citing *Coastal Oil & Gas Corp. v. Garza Energy Trust*, 268 S.W.3d 1, 11 (Tex. 2008)).

197. *Id.* at 283–84.

198. *Id.* at 283.

199. *Id.* at 289.

both the discovery rule and fraudulent concealment as doctrines by which the statute of limitations may be circumvented. Because so much information is available in the Commission records, this will be significant in many oil and gas cases. The recent cases are the culmination of a very pronounced trend to limit the number of stale claims that can be litigated. The regulatory universe will make it very hard to avoid a defense of limitations in the universe of conveyance and contract disputes.

Further, plaintiffs seeking to use Texas Railroad Commission filings to create causes of action have had limited success. For example, the reporting requirements create a private cause of action for fraud based on statutory violations, such as the statutory duties to properly plug wells and to not commit waste. Nevertheless, false filings will generally not support private causes of action for fraud because the plaintiff must show that the party making the false filing had information that would lead a reasonable person to conclude that there was an especial likelihood that the false filing will reach the plaintiff and will influence the plaintiff's conduct. It is not enough that the information may influence some unknown person or that the industry generally relies upon such filings. Plaintiffs will have a very difficult time meeting this burden. There is also a statutory defense to such civil claims based on the reasonably prudent operator standard. Finally, the cause of action for fraud resulting in injury to realty is seriously limited because subsequent owners do not have standing to sue prior owners for injury to realty that occurred before the subsequent owner acquired his interest.

In the universe of title and property rights, operating agreements were closely reviewed. The holding that lessors are not third-party beneficiaries of an operating agreement closed the door on a potential firestorm of additional litigation. The decision on the scope of the exculpatory clause in the model form operating agreements limits the operator's liability under the 1989 form but apparently accepts the earlier lower court decisions finding that the exculpatory clause did not limit the operator's liability as to contract claims.

The holding that continuing to pay royalty under a terminated lease will serve as notice of adverse possession to the cotenant/former lessor as to the reversionary estate will limit the number of lease termination cases. It is very common for royalty payments to continue after lease termination because one or both parties are unaware of the termination.

There is now authority for the proposition that a regulatory permit for an oil and gas operation will not shield the operator from civil liability for the permitted conduct, and permitted conduct can nevertheless be the basis for subsurface trespass. The regulatory process for granting an applicant common carrier status will not conclusively establish that status and thus confer the power of eminent domain. These holdings generally preserve the concept of two separate universes.

In summary, if there is any unifying trend, it is that many of the reported decisions have been resolved in a way that is likely to limit future litigation.