

No. 13-02-00136-CV

IN THE COURT OF APPEALS
FOR THE THIRTEENTH DISTRICT OF TEXAS
AT CORPUS CHRISTI

COASTAL OIL & GAS CORPORATION,
COASTAL OIL & GAS USA, L.P.,

Appellants,

v.

GARZA ENERGY TRUST, ET AL.,

Appellees.

BRIEF OF *AMICUS CURIAE*
TEXAS OIL & GAS ASSOCIATION

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BRIEF OF *AMICUS CURIAE*
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To The Court of Appeals:

The undersigned attorneys submit this *Amicus Curiae* Brief pursuant to Rule 11 of the Texas Rules of Appellate Procedure and respectfully request that it be received and considered by the Court.

TxOGA'S INTEREST

This Brief is submitted on behalf of the Texas Oil & Gas Association ("TxOGA"), a general, multipurpose, trade association representing the Texas oil and gas industry. TxOGA's members, which produce and market more than ninety percent of all Texas' crude oil and natural gas, are directly and

significantly affected by all aspects of Texas oil and gas law. As an organization, TxOGA participates actively in selected cases as *amicus curiae* to encourage the observance and maintenance of that substantial body of oil and gas law Texas courts have carefully developed over many decades, and to urge caution in departing from the general principles underlying that jurisprudence. TxOGA is particularly mindful of the need for restrained and deliberate judicial scrutiny of attempts to modify or enlarge obligations implied by courts.

TxOGA has agreed to pay the undersigned a fee for the preparation and submission of this Brief.^{1/}

TxOGA'S CONCERNS

By awarding oil and gas lessors actual and substantial punitive damages for “subsurface trespass”^{2/} based on a hydraulic fracture on an adjoining lease, the court below departed from basic oil and gas principles governing the nature of a lessor’s interest and the relationship between a lessor and its lessee. If not reversed, it would establish for the first time in Texas that such an operation constitutes an actionable trespass, answerable in punitive damages.

^{1/} Although Appellants are members of TxOGA, neither of them participated in the preparation of this Brief, and neither will contribute to funding the payment of fees to the undersigned.

^{2/} While the judgment below would afford relief to Appellees based on other claims, this Brief concerns only that portion of the judgment pertaining to subsurface trespass.

Appellees are lessors, and Appellants are lessees, under an oil and gas lease (“Share 13”), and Appellants own an adjoining property (“Share 12”). Appellants operate both properties. Appellees complained about a hydraulic fracturing operation that Appellants conducted on Share 12, the effect of which (according to Appellees) was to drain hydrocarbons from Share 13. “Fracing,” as the technique is commonly known, is an industry-wide procedure to increase oil and gas production. There are several troubling aspects of the lower court’s action.

First, trespass (a tort) is injury to a possessory interest in real property. In order to affirm the judgment below, this court would need to ignore (or undermine) one of the most fundamental principles of oil and gas law, that a lessor owns no possessory interest in the minerals subject to its gas lease. That would constitute a radical departure from basic oil and gas law, and would introduce an unacceptable degree of uncertainty to an area of the law that has been settled for decades.

Second, Texas does not recognize a cause of action for damages for subsurface trespass based on a hydraulic fracture, *even for a proper plaintiff*. In the last forty years, the Texas Supreme Court has rendered only three decisions providing any guidance on the issue. In one, the Court suggested a hydraulic fracture might constitute a trespass. In the second, while holding that

a secondary recovery by waterflood would *not* constitute trespass, the Court made it clear that it had not decided whether such a cause of action could be based on a hydraulic fracture. In the third, the Court concluded that a hydraulic fracture *could* constitute trespass, but that decision was promptly withdrawn, leaving intact the court of appeals holding that such an operation is not a trespass. In view of the serious public policy considerations implicated in determining whether to allow suits for trespass based on hydraulic fracture, and considering that Appellees would have no standing to assert such a cause of action—even if the Supreme Court were to determine one exists—this is the wrong case for this court of appeals to make new law.

Third, if allowed to stand, the judgment below would allow a lessor to bypass its contract remedies (against its lessee for breach of the implied covenant to protect the leasehold) in favor of a tort (with the prospect of punitive damages), all based on novel theories of subsurface trespass and without regard to the fundamental aspect of a non-possessory royalty interest.

This is simply another dispute between an oil and gas lessor and its lessee. Texas law is clear that such disputes are contractual in nature, with the oil and gas lease, supplemented by implied covenants where appropriate, governing the legal rights and obligations attaching to the lessor-lessee relationship. The court

of appeals should reverse that portion of the judgment concerning subsurface trespass.

DISCUSSION

I. Appellees Lacked Standing

A. A Lessor Has No Possessory Interest In Minerals

A Texas oil and gas lease conveys to the lessee title to the minerals in place, subject only to the contractual obligation to pay royalty on the minerals, if, as and when produced.^{3/} It was established nearly eighty years ago that a lessor owns no possessory interest in the minerals subject to its lease.^{4/} The lessee owns

[A]n estate [which] has all the incidents of a fee simple, and while this estate continues, and until the qualification upon which it is limited is at an end, the grantee or proprietor has the same rights and privileges over his estate as if it was a fee simple. He has an absolute right to the *exclusive* possession, use, and enjoyment of the

^{3/} *Concord Oil Co. v. Pennzoil Prod. Co.*, 966 S.W.2d 451, 460 (Tex. 1998); *see also Hurd Enters. v. Bruni*, 828 S.W.2d 101, 109 (Tex.App.—San Antonio 1992, writ denied); *Stanolind Oil & Gas Co. v. Barnhill*, 107 S.W.2d 746 (Tex. Civ. App.—Amarillo 1937, writ ref'd).

^{4/} An oil and gas lease operates as a present conveyance, vesting the lessee with a fee simple determinable in the oil and gas in place, and leaving the lessor with a mere possibility of reverter in the fee estate. *Stephens County v. Mid-Kansas Oil & Gas Co.*, 113 Tex. 160, 254 S.W. 290 (1923). *See also Luckel v. White*, 819 S.W.2d 459, 464 (Tex. 1991); *Jupiter Oil Co. v. Snow*, 819 S.W.2d 466, 469 (Tex. 1991); *Halbouty v. Railroad Comm'n of Texas*, 163 Tex. 417, 357 S.W.2d 364 (Tex. 1962), *cert. denied*, 371 U.S. 888 (1962); *Sheffield v. Hogg*, 77 S.W.2d 1021 (Tex. 1934); *Bruni*, 828 S.W.2d at 109-10 (“An oil and gas lease conveys to the lessee title to the gas in place, subject only to the contractual obligation to pay royalty on gas, if, as, and when produced.”).

land and as [sic] complete dominion over it for all purposes as though he held it in fee simple.

Hanks v. Magnolia Petroleum Co.^{5/} In fact, the execution of an oil and gas lease has been held to be a “sale” of an interest in land,^{6/} the legal effect of which has been described as follows:

The execution of an oil and gas lease simultaneously divests the grantor (lessor) of the right to possess, use, or dispose of the oil and gas in, upon or under the land in question and invests these rights in the grantee (lessee) of the lease.

Texas Oil & Gas Corp. v. Ostrum.^{7/}

By virtue of their oil and gas lease, Appellees divested themselves of all rights of possession of the minerals underlying the lease, and simultaneously vested their lessee with the exclusive ownership and possession of those minerals. Appellees retained only a possibility of reverter and a royalty interest, both of which are non-possessory interests.^{8/}

^{5/} 14 S.W.2d 348, 351 (Tex. Civ. App.—Eastland 1928), *aff'd*, 24 S.W.2d 5 (Tex. Comm'n App. 1930, judgm't adopted) (emphasis added). See *Davis v. Skipper*, 83 S.W.2d 318 (Tex. Comm'n App. 1935, judgm't adopted).

^{6/} *Cherokee Water Co. v. Forderhause*, 641 S.W.2d 522, 525 (Tex. 1982) (citing *W.T. Waggoner Estate v. Sigler Oil Co.*, 118 Tex. 509, 19 S.W.2d 27 (1929)).

^{7/} 638 SW.2d. 231, 234 (Tex.App.—Tyler 1982, writ ref'd n.r.e.) (citing *Stephens County v. Mid-Kansas Oil & Gas Co.*, 254 S.W. 290 (Tex. 1923)) (emphasis added). The lessee's exclusive possession and ownership of the oil and gas in place or produced from the leasehold premise continues until such time as the lease expires. *Ostrum*, 638 S.W.2d at 234. See also *Hanks*, 14 S.W.2d at 351.

^{8/} The lessor's retained interest under an oil and gas lease is a non-possessory
(continued...)

As the Supreme Court recently said,

Under a typical lease providing for 1/8 royalty, the lessor *may think* that the interest retained is 1/8 of the minerals including 1/8 of the royalties. . . . In actuality, the lease conveys a fee simple determinable with the possibility of reverter. When the lessor owns all the mineral estate (8/8) and executes an oil and gas lease, *the lessor has conveyed all the mineral estate (8/8)* but has retained a possibility of reverter in the entire mineral estate (8/8).

Concord Oil Co.^{9/} Because the mineral estate is the separate property, and within the exclusive control, of the lessee, *only the lessee* has the legal right to take action to protect the leasehold.

B. Trespass Injures Only A Possessory Interest

The basis for an action for trespass to real property is an injury to the right of possession, and in order to maintain an action for trespass a party must, at the time of the trespass, have been in actual or constructive possession of the land.^{10/} When a landowner is not in (or entitled to) possession, unlawful

^{9/} (...continued)

reversionary interest, *Jupiter*, 819 S.W.2d at 468; *Ostrum*, 638 S.W.2d at 234-35, and the royalty interest is also non-possessory. *Luckel*, 819 S.W.2d at 463; *T-Vestco Litt-Vada v. Lu-Cal One Oil Co.*, 651 S.W.2d 284, 289-90 (Tex. App.—Austin 1983, writ ref'd n.r.e.); *Douglas v. Butcher*, 272 S.W.2d 553, 555 (Tex. Civ. App.—San Antonio, 1954, writ ref'd n.r.e.) (lessee has exclusive right of possession and development under a lease, and royalty interest is a non-possessory interest, and only lessor to receive proceeds if, as and when minerals are produced).

^{9/} 966 S.W.2d at 460 (emphasis added).

^{10/} See *Pentagon Enters. v. Southwestern Bell Tel. Co.*, 540 S.W.2d 477 (Tex. Civ. App.—Houston [14th Dist.] 1976, writ ref'd n.r.e.); 70 TEX. JUR. 3d *Trespass to Realty* § 1 (1999); RESTATEMENT (SECOND) OF TORTS § 329 (1965). See also *Cain v. Fontana*, 423 S.W.2d (continued...)

interference with the mineral estate does not constitute trespass to any real property interest of the landowner.^{11/}

TxOGA has found no Texas case permitting a trespass action by a lessor for damage or loss to the minerals under the lease.^{12/} On the other hand, Texas courts have consistently held that an oil and gas lessor lacks the standing to maintain other causes of action requiring a possessory interest in land. Thus, for example, a mineral lessor lacks any interest sufficient to support an action for trespass to try title,^{13/} and it may neither demand nor defeat a partition.^{14/} A

^{10/} (...continued)

134, 137 (Tex. Civ. App.—San Antonio 1967, writ ref'd) (an “action for trespass is designed to protect the interest in exclusive possession of the land involved in its intact physical condition, and any person in actual and exclusive possession of the property may maintain such action.”).

^{11/} See 1 W. L. SUMMERS, THE LAW OF OIL & GAS § 21 (1954); Laura H. Burney & Norman J. Hyne, *Hydraulic Fracturing: Stimulating Your Well or Trespassing?*, 44 ROCKY MTN. MIN. L. INST. 19-1, 19-48 (1998).

^{12/} Of all the Texas cases TxOGA has found which have entertained a claim against an adjoining operator for damage or loss to the subsurface oil and gas estate, only *Elliff v. Texon Drilling Co.*, 146 Tex. 575, 210 S.W.2d 558 (1948), involved a plaintiff who owned a non-possessory oil and gas royalty interest. All of the other cases involved claims either by lessees or by unleased mineral interest owners.

Elliff involved a claim by a lessor against an adjoining lessee for the negligent waste and destruction of gas through an uncontrolled blowout. *Id.* at 579-80. The claim in *Elliff* was in negligence, not trespass, unlike a negligent-waste claim, trespass is based on injury to a possessory interest in land.

^{13/} *Shell Petroleum Corp. v. State*, 86 S.W.2d 245 (Tex. Civ. App.—Austin 1935, no writ).

^{14/} *Ostrum*, 638 S.W.2d at 234.

lessor cannot maintain an action for seismic trespass of the mineral estate,^{15/} and a party owning only a possibility of a reverter does not have such a present interest as to authorize him to enjoin production from the leased premises.^{16/}

In this case, Appellees would have the Court fashion a special rule of standing, arguing that *their* non-possessory interests “can be trespassed upon on *in this factual context.*”^{17/} Specifically, they contend that “[t]he equities must afford [them] standing to assert a [trespass] claim” because their lessee cannot “lodge a claim against itself”.^{18/} TxOGA respectfully asks this court to reject those contentions.

There is no need in this case to modify or enlarge the standing requirements for trespass, and there is absolutely no basis (equitable or otherwise) to carve out a special rule to protect these lessors from the claimed drainage. Texas law affords all lessors (including Appellees) an adequate remedy for drainage of minerals from beneath the leasehold, and that remedy would be

^{15/} *Wilson v. Texas Co.*, 237 S.W.2d 649, 650 (Tex. Civ. App.–Fort Worth 1951, writ ref’d n.r.e.) (typical lease conveys exclusive right to explore, and thus conduct seismic surveys, to the lessee).

^{16/} *Davis*, 83 S.W.2d at 319-20.

^{17/} Appellees’ Br. at 23 (emphasis added).

^{18/} Appellees’ Br. at 10, 23.

a contractual action against the lessee for breach of the implied covenant to protect the leasehold.

II. Appellants Breached No Tort Duties

That no higher duty is owed by an oil and gas lessee to its lessor is also clearly established in Texas, because the contractual relationship created by a Texas oil and gas lease is not one of the relationships that impose a fiduciary duty as a matter of law.^{19/} Nor does it give rise to an “informal” fiduciary relationship, such as may exist “in those cases ‘in which influence has been acquired and abused, in which confidence has been reposed and betrayed.’”^{20/}

Unlike the relationship of insured and insurer, where Texas courts are most likely to find “special” relationships, the lessor-lessee relationship is one in which each party is motivated by a desire to make a profit, and there is no element of trust or unequal bargaining position. As the Supreme Court has said, “a party to a contract is free to pursue its own interests, even if it results in a breach of that contract, without incurring tort liability.”^{21/} In fact, the inherent

^{19/} See *Crim Truck & Tractor Co. v. Navistar Int'l Transp. Corp.*, 823 S.W.2d 591, 593-94 (Tex. 1992) (citing *Kinzbach Tool Co. v. Corbett-Wallace Corp.*, 138 Tex. 565, 160 S.W.2d 509, 513 (1942) (principal/agent) and *Johnson v. Peckham*, 132 Tex. 148, 120 S.W.2d 786, 787 (1938) (partners)).

^{20/} *Crim Truck & Tractor*, 823 S.W.2d at 594 (quoting *Texas Bank & Trust Co. v. Moore*, 595 S.W.2d 502, 507 (Tex. 1980)).

^{21/} 823 S.W.2d at 594.

conflict of interest between lessor and lessee precludes a fiducial or “special” relationship.^{22/}

Texas courts have consistently held that under a typical oil and gas lease no fiducial duties are owed by a lessee to a lessor, because the lessee is neither a formal fiduciary (he is not agent, lawyer, partner, etc.), nor an informal fiduciary (no confidential relationship exists), and the relationship is not “special” (as that term is understood in Texas jurisprudence). As early as 1967, the Texas Supreme Court held that there is no fiduciary or confidential relationship between a mineral lessee and its lessor, nor does a constructive trust arise between those parties.^{23/}

^{22/} The lessee-lessor relationship bears no resemblance to a “special” relationship, the characteristics of which have been variously described as follows: (a) where the public interest dictates; out of contracts of adhesion; or in fiduciary relationships; see Note, *San Antonio Court of Appeals Hampered by Unclear Texas Precedent*, 21 TEX. TECH. L. REV. 801, 812 (1990); (b) where the parties enjoy unequal bargaining positions; in certain kinds of contracts (such as insurance); and where there is a potential for abuse by the insurer; *Arnold v. Nat'l County Mut. Fire Ins. Co.*, 725 S.W.2d 165, 167 (Tex. 1987); and (c) where there is an imbalance of bargaining power or where there is an element of trust that is necessary to accomplish the goals of the undertaking, *English v. Fischer*, 660 S.W.2d 521, 524 (Tex. 1983) (Spears, J., concurring). TxOGA finds it significant that in *Crim Truck & Tractor* (noting a party's right to pursue its own interests without incurring tort liability), the Court cited *Amoco Prod. Co. v. Alexander*, 622 S.W.2d 563, 571 (Tex. 1981), in which the Court specifically adopted the prudent operator standard to test a lessee's compliance with implied covenants. See also *El Paso Natural Gas Co. v. Am. Petrofina Co.*, 733 S.W.2d 541, 550 (Tex. App.—Houston [1st Dist.] 1986, writ ref'd, n.r.e.), cert. denied, 485 U.S. 987 (1988) (“The existence of a contract . . . does not give rise to any implied covenant that neither party will do anything that injures the right of the other party to receive the benefits of the agreement.”) (citing *English*, 660 S.W.2d at 522).

^{23/} *Sunac Petroleum Corp. v. Parkes*, 416 S.W.2d 798, 805 (Tex. 1967). While it has been held that an *executive* (the holder of the right to lease the minerals) may owe a duty
(continued...)

The Court's most straightforward rejection of any such relationship appeared in *Texas Oil and Gas Corp. v. Hagen*,^{24/} in which the Court said flatly that "no fiduciary or special relationship exists between [oil and gas] lessee and lessors,"^{25/} and noted that

This court has never adopted a fiduciary or "highest good faith" or "utmost fair dealing" standard in any oil and gas implied covenant case. To the contrary, we have specifically held that unless the lease document itself creates in law a trust, or unless a relationship of trust and confidence necessarily results from the lessor-lessee relationship, the standard of conduct of the lessee cannot be appropriately characterized as fiduciary.

31 Tex. Sup. Ct. J. at 141-42. No other basis for tort liability flows from either the oil and gas lease or the lessor-lessee relationship.^{26/}

^{23/} (...continued)

of utmost good faith to nonexecutives, any such duty would arise from the relationship of the parties and not from the terms, expressed or implied, of a contract or deed. *Manges v. Guerra*, 673 S.W.2d 180 (Tex. 1984).

^{24/} 31 Tex. Sup. Ct. J. 140 (1987), *opinion withdrawn case settled*, 760 S.W.2d 960 (Tex. 1988). It should be noted that, while technically this opinion has been withdrawn, it nevertheless has since been cited by other courts: The San Antonio Court of Appeals cited *Hagen* for the proposition that this Court has "never advocated a fiduciary or 'highest good faith' or 'utmost good faith' standard in any oil and gas implied covenant case," *Bruni*, 828 S.W.2d at 108. The Fifth Circuit cited *Hagen* for the proposition that a contractual relationship did not give rise to "the highest duty of fair dealing and good faith." *B & A Pipeline Co. v. Dorney*, 904 F.2d 996, 999 n.9 (5th Cir. 1990).

^{25/} 31 Tex. Sup. Ct. J. at 143.

^{26/} The lessee has not been entrusted with the executive management of royalties belonging to his lessor, *Pickens v. Hope*, 764 S.W.2d 256, 267 (Tex. App.—San Antonio 1988, writ denied). In *Pickens* the San Antonio Court of Appeals held that a mineral owner did not have a fiduciary duty to a nonparticipating royalty owner. See also *Cambridge Oil Co. v. Huggins*, 765 S.W.2d 540, 544 (Tex. App.—Corpus Christi 1989, writ denied). And, "the
(continued...)

Moreover, to the extent that drainage causes a potential diminution in royalties, the lessor's loss is an economic injury under the lease. Where the injury is only the economic loss to the subject of a contract, the action sounds in contract alone.^{27/} Because the jury in this case found that Appellees' loss was the "value of the royalty on the gas" drained by the alleged trespass,^{28/} the lessors' injury, if any, was solely an economic loss under the lease, and that loss would not support an award of punitive damages.^{29/}

III. Technical Rules of Trespass Should Not Apply

There are at least two reasons for the Court to resolve this case on the

^{26/} (...continued)

lessee has not undertaken to manage the property for the sole benefit of the lessor." *El Paso Natural Gas Co.*, 733 S.W.2d at 551. Under these circumstances, a lessee is not a fiduciary as a matter of law, because he has not undertaken to manage and develop the property for the sole benefit of the lessor. See *Pickens*, 764 S.W.2d at 267-68 (citing with approval the discussion in *Hagen* that this Court has never adopted a fiduciary or highest good faith or utmost fair dealing standard in any oil and gas implied covenant case); see also *Bruni*, 828 S.W.2d at 112 ("[A] party to a contract is free to pursue its own interest, even if it results in a breach of that contract, without incurring tort liability.").

^{27/} *Southwestern Bell Tel. Co. v. DeLanney*, 809 S.W.2d 493, 494-95 (Tex. 1991).

^{28/} Appellants' Br. at 34, 35.

^{29/} See *Grace Petroleum Corp. v. Williamson*, 906 S.W.2d 66, 69-70 (Tex. App.—Tyler 1995, no writ) (court reversed award of punitive damages in suit by a lessor against its lessee for drainage, finding the nature of the loss to be economic and sounding only in contract). Although TxOGA agrees that the measure of damages claimed by Appellees for drainage is incorrect, Appellees nevertheless claimed an economic loss under their lease. In any event, the proper measure of damages for breach of the drainage covenant is the royalty interest on the production that would have been obtained if the lessee had acted as a reasonably prudent operator to prevent the drainage. *Mandell v. Hamman Oil & Refining Co.*, 822 S.W.2d 153, 164 (Tex. App.—Houston [1st Dist.] 1991, writ denied).

basis of standing, as discussed above, and not attempt to reach the issue of fracture stimulation as a trespass. First, sound principles of judicial economy support that resolution. Second, no Texas precedent holds that well fracturing across lease lines constitutes a subsurface trespass. One case holds that no trespass occurs when an authorized secondary recovery project results in the movement of water across lease lines. Two other cases leave the question of fracture stimulation unresolved. Taken together, the three cases illustrate the wisdom of not attempting to apply the technical rules of trespass in this case.

A. The *Gregg* Decision (fracture stimulation)

In *Gregg v. Delhi-Taylor Oil Corp.*,^{30/} Delhi sought to prevent an adjoining lessee from fracturing a well, contending that the fracture would extend onto Delhi's lease and constitute a subsurface trespass.^{31/} Gregg argued the case should be dismissed because the Railroad Commission of Texas (the "Commission") had primary jurisdiction over the dispute.^{32/} The trial court found primary jurisdiction in the Commission and dismissed the case.

The Court of Appeals reversed (remanding to the trial court), and the Supreme Court affirmed, holding that the power to determine whether the

^{30/} 344 S.W.2d 411 (Tex. 1961).

^{31/} *Id.* at 412.

^{32/} *Id.* at 412-13.

proposed operation would result in a subsurface trespass was not exclusively within the Commission's jurisdiction.^{33/} The basis for the holding was that, with respect to a question that is "inherently judicial in nature (as we think the question of trespass is), the courts are not ousted from jurisdiction unless the Legislature, by a valid statute, has explicitly granted exclusive jurisdiction to the administrative body,"^{34/} which it had not done.

The opinion did note that Delhi's allegations were "sufficient to raise an issue whether there [was] a trespass,"^{35/} but the Court made it clear the following year in *Railroad Comm'n of Texas v. Manziel*,^{36/} that this did not mean it had decided that a fracture stimulation constituted a subsurface trespass.^{37/}

^{33/} The Court framed the issue as

whether the courts have the power to determine whether a subsurface trespass is occurring or is about to occur, or whether the Railroad Commission has this power to the exclusion of the courts, with the courts having the power only to review, under the substantial evidence rule, or otherwise, the action of the Commission.

Id. at 412. It later restated the issue as "do the courts have the authority to issue an injunction to ascertain whether there is a trespass, and to enjoin it if there is?" *Id.* at 415.

^{34/} *Id.* at 415.

^{35/} *Id.* at 416.

^{36/} 361 S.W.2d 560 (Tex. 1962).

^{37/} Concerning its decision in *Gregg*, the Court said that "the question of trespass by authorized sandfracturing on adjoining property was posed [in *Gregg*] but not decided." 361 S.W.2d at 567, n. 3.

B. The *Manziel* Decision (waterflood)

Manziel was an appeal from a Commission order authorizing a secondary recovery waterflood project, which *Manziel* claimed would result in a trespass of its subsurface estate. Specifically, he argued that the Commission could not authorize “a trespass by injected water that will result in the premature destruction of [*Manziel*’s] well.”^{38/} The Texas Supreme Court disagreed.

It first stated the legal basis for its conclusion:

“What may be called a ‘negative rule of capture’ appears to be developing. Just as under the rule of capture a landowner may capture such oil or gas as will migrate from adjoining premises to a well bottomed on his own land, so also may he inject into a formation substances which may migrate through the structure to the land of others, even if this results in the displacement under such land of more valuable with less valuable substances (*e.g.*, the displacement of wet gas by dry gas).”

Id. at 568.^{39/} Then it discussed the public policy considerations:

Secondary recovery operations are carried on to increase the ultimate recovery of oil and gas, and it is established that pressure maintenance projects will result in more recovery than was obtained by primary methods. It cannot be disputed that such operations should be encouraged, for as the pressure behind the primary production dissipates, the greater is the public necessity for applying secondary recovery forces. It is obvious that secondary recovery programs could not and would not be conducted if any adjoining operator could stop the project on the ground of subsurface trespass. As is pointed out by *amicus curiae*, if the

^{38/} *Id.* at 565.

^{39/} Quoting 1 HOWARD R. WILLIAMS & CHARLES J. MEYERS, OIL AND GAS LAW § 204.5.

Manziels' theory of subsurface trespass be accepted, the injection of salt water in the East Texas field has caused subsurface trespasses of the greatest magnitude.

Id. at 568.

Based on the law and the announced public policy the Court concluded that the technical rules of trespass simply do not apply to the secondary recovery operations at issue:

The orthodox rules and principles applied by the courts as regards surface invasions of land may not be appropriately applied to subsurface invasions as arise out of the secondary recovery of natural resources. If the intrusions of salt water are to be regarded as trespassory in character, then under common notions of surface invasions, the justifying public policy considerations behind secondary recovery operations could not be reached in considering the validity and reasonableness of such operations. Certainly, it is relevant to consider and weigh the interests of society and the oil and gas industry as a whole against the interests of the individual operator who is damaged; and if the authorized activities in an adjoining secondary recovery unit are found to be based on some substantial, justifying occasion, then this court should sustain their validity.

Id. at 568-69 (citations omitted).

C. The *Geo-Viking* Decision (fracture stimulation)

Despite thousands of fracturing operations and hundreds, if not thousands of secondary recovery projects occurring since the *Gregg* and *Manziel* decisions, Texas courts did not again address such trespass claims until 1991. In *Geo-*

Viking, Inc. v. Tex-Lee Operating Co.,^{40/} an operator claimed that Geo-Viking improperly performed a fracture operation that damaged its well, and sought damages for oil and gas that would have been produced had the fracture been properly performed.^{41/}

On appeal, Geo-Viking claimed the damages were overstated because a properly-performed fracture would have crossed lease lines, trespassing on an adjoining lease, and no damages should be recovered for oil and gas that would have been drained from another lease by a subsurface trespass.^{42/} Relying on the rule of capture, “which permits the owner of a tract to drill as many wells as the Railroad Commission will allow and provides that he is not liable to adjacent landowners whose lands are drained as a result of his operations,” the court of appeals rejected the trespass arguments.^{43/}

The Supreme Court initially reversed, holding that fracturing beyond lease lines “constitute[d] a subsurface trespass.”^{44/} However, the Court subsequently

^{40/} 817 S.W.2d 357 (Tex. App.—Texarkana 1991), *writ denied per curiam*, 839 S.W.2d 797 (Tex. 1992).

^{41/} *Id.* at 363.

^{42/} *Id.* at 363-64.

^{43/} *Id.* at 364.

^{44/} *Geo-Viking, Inc. v. Tex-Lee Operating Co.*, 35 Tex. Sup. Ct. J. 661, 662 (April 22, 1992) (*per curiam*).

withdrew its opinion and judgment, leaving the court of appeals opinion intact as “writ denied.”^{45/} Commentators suggest that the Court reconsidered its holding on the same public policy grounds the Court addressed in *Manziel*.^{46/}

IV. Public Policy Considerations

There are significant public policy considerations in favor of promoting the use of hydraulic fracturing, a practice that has been described as the “universal well completion technique in tight gas sands”^{47/} which are encountered in many of the productive gas reservoirs in Texas.^{48/} It is a recognized method for increasing ultimate production “by both extending the drainage radius of the wells and the life of the well.”^{49/} It is used widely in Texas.^{50/} And, many wells would be uneconomic without its use.^{51/} A judicial holding that fracturing constitutes trespass would not only be contrary to these policy considerations,

^{45/} *Geo-Viking, Inc. v. Tex-Lee Operating Co.*, 839 S.W.2d 797 (Tex. 1992).

^{46/} See Laura H. Burney, *A Pragmatic Approach to Decision Making in the Next Era of Oil and Gas Jurisprudence*, 16 J. ENERGY NAT. RESOURCES & ENVTL. L. 1, 39 (1996); Jacqueline L. Weaver, *The Politics of Oil and Gas Jurisprudence: The Eighty-Six Percent Factor*, 33 WASHBURN L. J. 492, 524 (1994).

^{47/} 44 ROCKY MTN MIN. L. INST. at 19-17.

^{48/} Fifty percent of gas wells and thirty percent of oil wells drilled in the United States are fracture stimulated to enhance production, and in many instances, make them economically productive wells. *Id.* at 19-16, 19-17.

^{49/} 44 ROCKY MTN MIN. L. INST. at 19-17.

^{50/} *Id.*

^{51/} *Id.*

it would discourage its use because of concerns that adjoining owners might sue for substantial (including punitive) damages or even seek to enjoin its use altogether.^{52/}

The same policy considerations that supported the Supreme Court's holding that secondary recovery operations do not constitute a trespass, apply to hydraulic fracturing. Paraphrasing the Court's decision in *Manziel*, if fracturing operations were held to constitute trespass, "then under common notions of surface invasions, the justifying public policy considerations behind [fracturing] could not be reached in considering the validity and reasonableness of such operations [and it] is obvious that [fracturing operations] *could and would not be conducted* if any adjoining operator could stop the project on the ground of subsurface trespass."^{53/}

Appellees suggest that this concern is unfounded because those desiring to conduct fracture operations need simply obtain consent from adjoining owners. However, since the precise direction and length of fractures cannot be pre-determined, a party would not, in many instances, know if the fractures might propagate outside its lease boundaries, and even if such propagation is

^{52/} The uncertainty of threatened litigation is exacerbated by the fact that it is not practical to determine with certainty that "an induced fracture has crossed a lease line." *Id.* at 19-16. It may be impossible to make such a determination ahead of time. *Id.*

^{53/} *Manziel*, 361 S.W.2d at 568 (emphasis added).

anticipated, which adjoining lands may be affected. Furthermore, under Appellees' scenario, it is likely the fracture operations would be frustrated, due to the inability of the operator to reach a suitable agreement from adjoining owners as a result to demands by adjoining owners for terms or consideration that would make the fracturing operation not economically or otherwise feasible.

The suggestion that "consent" could be obtained from adjoining lessors before beginning a fracture operations begs the question: only the adjoining *lessees* (or unleased mineral owners) would have the power to give such consent. Moreover, the practical problems associated with that suggestion are overwhelming. In many cases (due primarily to inheritances of royalty interests by multiple parties), it would not be particularly uncommon to have dozens, or even hundreds of royalty owners in each tract, many of whom will have no knowledge of oil and gas operations and will be reluctant to execute a document they did not understand.

Finally, if the court accepts Appellants' theory of subsurface trespass, hydraulic fracturing techniques will have resulted as a matter of law in "subsurface trespasses of the greatest magnitude."^{54/}

TXOGA urges this Court to weigh the foregoing considerations against the interests of individual lessors, whose legitimate interests enjoy the protections

^{54/} 361 S.W.2d at 568.

of their own oil and gas leases. There is simply no need to apply traditional, orthodox trespass rules and principals to well fracturing operations.

V. The Oil and Gas Lease Affords an Adequate Legal Remedy

The lessor-lessee relationship is strictly contractual,^{55/} and must be determined from the provisions of the lease.^{56/} On that basis, Texas courts have consistently rejected attempts by lessors to fashion tort claims for loss or underpayment of royalties, even where the losses or underpayments resulted from affirmative acts of their lessee on adjoining lands or from “self-dealing.”^{57/} Instead, Texas courts protect the lessor’s interest by enforcing express lease terms and by implying various other lease covenants where necessary and appropriate. Implied covenants, including the covenant to protect against drainage, protect a lessor against self-interests of a lessee or conflicts of the lessee’s interests with those of his lessor.^{58/}

^{55/} *Bruni*, 828 S.W.2d at 107 (citing *Cambridge*, 765 S.W.2d at 544).

^{56/} *Texas Oil & Gas Corp. v. Vela*, 429 S.W.2d 866, 870 (Tex. 1968); *Exxon Corp. v. Middleton*, 613 S.W.2d 240, 245 (Tex. 1981).

^{57/} See, e.g., *Alexander*, 622 S.W.2d 563; *Grace*, 906 S.W.2d 66; and *Bruni*, 828 S.W.2d 101.

^{58/} *Bruni*, 828 S.W.2d at 107-08.

[T]he relationship between a lessor and lessee has been held to be purely contractual. . . . A unity of interest arises as a result of the lessor/lessee relationship because the parties derive mutual economic benefits from the gas production It is also recognized that the parties’ interests will

(continued...)

The Supreme Court applied this very principle in *Amoco Prod. Co. v. Alexander*,^{59/} in which the lessor had asserted a claim against Amoco for “tortious drainage of oil and gas.” The lessor asserted that Amoco (its lessee) was operating adjoining leases (in which Amoco was subject to lower royalty burdens) so as to maximize production from those leases and drain production from Alexander’s lease.^{60/} Citing Amoco’s self-interest in producing the adjoining lease at the expense of its lease, Alexander argued that the drainage should be considered tortious *due to the unique fact that Amoco was both its lessee and was causing the drainage*.^{61/} The trial court agreed, awarding nearly \$4 million in punitive damages, and the award was affirmed by the court of appeals.^{62/} But the Supreme Court reversed, holding that the remedy for Amoco’s conduct was a

^{58/} (...continued)

conflict in matters pertaining to production, marketing the product, treating, testing and reworking wells, and in appearing before administrative bodies. The protection for the lessor arises out of the lease agreement and is provided through the use of express covenants, like the duty to pay royalty, and through implied covenants which arise by virtue of the lessor/lessee relationship.

Id. at 107.

^{59/} 622 S.W.2d 563 (Tex. 1981).

^{60/} *Amoco Prod. Co. v. Alexander*, 594 S.W.2d 467, 479-80 (Tex. Civ. App.—Houston [1st Dist.] 1979), *modified and aff’d*, 622 S.W.2d 563 (Tex. 1981).

^{61/} *Id.* at 479.

^{62/} *Id.*

breach of the covenant to protect against drainage, which was contractual in nature, and would not support a claim for punitive damages.^{63/}

The Court made it clear that “[e]very claim of improper operation by a lessor against a lessee should be tested against the general duty of the lessee to conduct operations as a reasonably prudent operator in order to carry out the purposes of the oil and gas lease.”^{64/} The Court also made it clear that a lessee’s liability for drainage is neither increased nor judged by a higher standard, just because the drainage is caused by the lessee’s actions on adjoining lands.^{65/}

CONCLUSION

TxOGA urges the court of appeals to dispose of this case without attempting to decide whether fracture stimulation constitutes trespass, by reversing the judgment below based upon the clear lack of standing of Appellees to prosecute a claim for trespass to the mineral estate. These lessors, like all those under typical oil and gas leases in Texas, enjoy the protections of their

^{63/} *Alexander*, 622 S.W.2d at 571.

^{64/} *Id.* at 568. See also *HECI Exploration Co. v. Neel*, 982 S.W.2d 881, 887 (Tex. 1998) (lessee who stands by while lease is drained by well on adjoining lands, when a reasonably prudent operator would have taken action, violates the implied covenant to protect against drainage); and *Shell Oil Co. v. Stansbury*, 410 S.W.2d 187, 188 (Tex. 1967) (lessee under duty to act as a reasonably prudent operator to protect lessor against drainage by affirmative act of the lessee upon adjoining land).

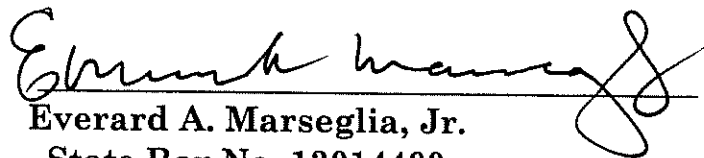
^{65/} Likewise, in *Hagen*, the Supreme Court refused to adopt a fiduciary standard or duty with respect to the implied marketing covenant.

lease, both express and implied, and they do not need a special rule of law for their particular circumstances.

This is the wrong case in which to decide the trespass issue. But, if the court should reach that question, TxOGA urges the court to hold that there is no cause of action for damages for subsurface trespass based on a hydraulic fracture.

Respectfully submitted,

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March 28, 2003

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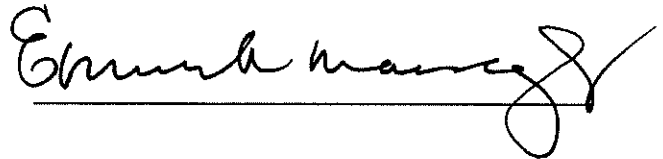
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