Westlaw.

For a fully searchable and synchronized transcript and oral argument video, go to the TX-ORALARG database on Westlaw.com.

This is an unofficial transcript derived from video/audio recordings

Supreme Court of Texas.
O. Lee Tawes, III
v.
Doris Barnes, Individually and as Independent Executrix of the Estate of Leon McNair Barnes, Deceased.
No. 10-0581.

November 9, 2010.

Appearances:

Barnet B. Skelton, Jr., for petitioner and Russell S. Post of Beck, Redden & Secrest, LLP, for petitioner.Richard D. Watt of Watt, Beckworth, Thompson & Henneman, LLP, for respondent.

Before:

Chief Justice Wallace B. Jefferson; Nathan L. Hecht, Dale Wainwright, David M. Medina, Paul W. Green, Phil Johnson, Don R. Willett, Eva M. Guzman, and Debra H. Lehrmann, Justices.

CONTENTS

ORAL ARGUMENT OF BARNET B. SKELTON, JR. ON BEHALF OF THE PETITIONER

ORAL ARGUMENT OF RICHARD D. WATT ON BEHALF OF THE RESPONDENT

REBUTTAL ARGUMENT OF RUSSELL S. POST ON BEHALF OF PETITIONER

CHIEF JUSTICE WALLACE B. JEFFERSON: The Court is ready to hear argument in 10- 0581 O. Lee Tawes, III v. Doris Barnes.

MARSHAL: May it please the Court, Mr. Skelton will present arguments for the appellant. Appellant has reserved five minutes for rebuttal.

ORAL ARGUMENT OF BARNET B. SKELTON, JR. ON BEHALF OF THE PETITIONER

ATTORNEY BARNET B. SKELTON: Your Honor, Russell Post and I are proud to be here today on behalf of O. Lee Tawes. Mr. Tawes was the losing party in a judgment of the bankruptcy court back in 2006. It was appealed to the Federal District Court in Victoria, lost again. We appealed then to the 5th Circuit Court of Appeals and sometimes I felt like a voice crying in the wilderness, but we have a certification opinion from the 5th Circuit, which sent three questions to this Court. Those three questions have varying [inaudible] impact. However they are all, the first two are case dispositive, but I'd like to start with the second because it is potentially it's a game-over question as far as we're concerned, Barnes will lose, and yet it can be decided on a narrow basis. The second question has to do with whether the provisions of the working interest unit agreement executed by my

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

client, other investors, Moose Oil & Gas and Dominion has a provision, provision five, which simply eliminates any potential cause of action against any party other than Dominion. Our position is that, rather other than Moose Oil & Gas, our position is that if Dominion had any claim, it would have only been against Moose Oil & Gas, that Moose Oil and Gas was the liable and responsible party. If that is the case, then even if Barnes prevails on her theory that she could be a third-party beneficiary of the joint operating agreement then she still comes up against a shut door because she can rise no higher than the rights that Dominion would have had against Moose Oil & Gas.

JUSTICE NATHAN L. HECHT: The problem with that is it just doesn't seem to make any sense because Moose was non-consenting.

ATTORNEY BARNET B. SKELTON: Moose was a non-consenting party.

JUSTICE NATHAN L. HECHT: Why should you look to the non-consenting party to be paid something that the non-consenting party doesn't care whether he get paid or not?

ATTORNEY BARNET B. SKELTON: Well Moose was a consenting party, Your Honor.

JUSTINCE NATHAN L. HECHT: Moose was--

ATTORNEY BARNET B. SKELTON: Dominion was the only non-consenting party.

JUSTICE NATHAN L. HECHT: But you have to look through, you have to look through Dominion to get to Moose, do you not or not?

ATTORNEY BARNET B. SKELTON: No, Your Honor, the non-consenting parties, and I think it might be helpful to look at the bench exhibit that we've submitted. First you have in the upper right-hand corner Doris Barnes; she's the lessor of the property in question.

JUSTICE NATHAN L. HECHT: And Dominion was non-consent.

ATTORNEY BARNET B. SKELTON: Dominion was the lessee and it went non-consent.

JUSTICE NATHAN L. HECHT: But that's the only person she has an agreement with.

ATTORNEY BARNET B. SKELTON: She has no agreement with anyone other than Dominion, that's correct. However, whether Dominion goes non-consent or not, Dominion is liable to Ms. Barnes because it has privity of contract and privity of estate with her. So in other words, Dominion's liability to Barnes, it's there no matter what. The joint operating agreement doesn't change it; the working interest unit agreement doesn't change it. Barnes cannot get around the fact that Dominion was her lessee. She could have always gone against Dominion. She did go against Dominion, but she settled, got enough money and then tried to shake down Mr. Tawes, who has no privity of contract, no privity of estate and no dealings with her.

JUSTICE NATHAN L. HECHT: And on that, on that subject, I'm a little unclear. Is, don't we have to take from the bankruptcy court's ruling that she has not been paid through the settlement?

ATTORNEY BARNET B. SKELTON: I don't think so, Your Honor. I think what the bankruptcy court says is that the settlement didn't characterize how the money should be applied.

JUSTICE NATHAN L. HECHT: Right.

ATTORNEY BARNET B. SKELTON: But what we're saying is, Your Honor, dollar for dollar, she got paid

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

every bit of the $291,846 that's at issue here.

JUSTICE NATHAN L. HECHT: But she was claiming a million.

ATTORNEY BARNET B. SKELTON: She was claiming a million; people can claim a lot of things, but there was no basis for that.

JUSTICE NATHAN L. HECHT: I know, but she had other claims and the bankruptcy court said well you can't tell that this is for royalty so don't we have to take that is was not paid for royalty?

ATTORNEY BARNET B. SKELTON: I don't believe so, Your Honor. I think he sent, I think frankly he just established that I didn't make a record as to what the funds were applied to. But in terms of whether we should feel sorry for poor Ms. Barnes she didn't get any money, she got a settlement, which dollar for dollar wise paid those unpaid royalties. She's had a lot of other clients.

JUSTICE NATHAN L. HECHT: But if she hadn't gotten that settlement, your position would still be the same?

ATTORNEY BARNET B. SKELTON: We don't owe her any money. Absolutely.

JUSTINCE NATHAN L. HECHT: And does that mean that you will get the, your share of production free of the burden of royalty that it would ordinarily be impressed with?

ATTORNEY BARNET B. SKELTON: I'm glad you brought that up, Your Honor, because here's the reality of how this operation works; here's how it happens in the oil and gas business. My client's a non-operator. The operator has full control over all operations. The operator, in fact in this case, had a contract with a purchaser of gas. The operator, which was an affiliate of Moose Oil & Gas, Moose Operating, sold the gas, collected the money. My client never saw a penny of the royalty stream money that otherwise would have gone to Ms. Barnes. That never happens. The royalty, the non- operating working interest owners are in a completely different situation. They just get a net check. The operator collects the money from the sale of gas. If there are sums owed for working interest amounts that are owed for equipment, etc., they net it out, you get your net check. Mr. Tawes never had any control and I want the Court to particularly understand that because there has been suggestion in other courts that there should be a sympathy factor, Tawes ran off with the money. Never happened. He just got his share.

JUSTICE PHIL JOHNSON: Well, is his share net of the royalties that would have been paid to Ms. Barnes?

ATTORNEY BARNET B. SKELTON: Absolutely.

JUSTICE PHIL JOHNSON: Okay, so what happened to the royalties that would have ordinarily been paid to Ms. Barnes? Who got it?

ATTORNEY BARNET B. SKELTON: Moose Oil & Gas, the company that ended up, frankly, for want of a better word, absconding with the money, not spending it on other things.

JUSTICE PHIL JOHNSON: Well let me ask you this, how do you know that Moose kept the money instead of sending part of it to Tawes?

ATTORNEY BARNET B. SKELTON: Well we know that, Your Honor, because.

JUSTICE PHIL JOHNSON: Ms. Barnes' money that is.

ATTORNEY BARNET B. SKELTON: The reason we know that is that Tawes never received the money and--

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

JUSTICE PHIL JOHNSON: But how, he received some money.

ATTORNEY BARNET B. SKELTON: He received his working interest share, his net revenue interest share, in other words not including her money.

JUSTICE PHIL JOHNSON: Okay, so how do you, how does the record show that none of her money flowed to him?

ATTORNEY BARNET B. SKELTON: Alright actually.

JUSTICE PHIL JOHNSON: [inaudible] at Moose.

ATTORNEY BARNET B. SKELTON: Actually there is a, there is an order that was entered by Judge Stine, I can get the record reference during the other side, but bottom line is he found, it wasn't in the main order that disposed of the issue at hand today. He found that Moose Oil and Gas had the contract. It collected the money and it didn't pay the royalty. It is in the record.

JUSTICE PHIL JOHNSON: Okay, but did he take any, what I'm wondering is this, does the record show that he, that Moose did not distribute any of that royalty stream to its, to Tawes and the other interest owners here.

ATTORNEY BARNET B. SKELTON: What the record reflects is that Moose collected the money. Moose did not pay Barnes and that the only two checks that were written to pay Barnes royalty from these wells, they're also part of the record and I can get you the references to those two checks.

JUSTICE PHIL JOHNSON: Okay, but you keep, we're missing each other somehow. Does the record show, is there a determination that when Moose got the money over here, when Moose got, because they got the money because Dominion is non-consenting, Moose collected the money. It could have sent some back up to Ms. Barnes, which she had coming from someone. What did it do with her money that she, it didn't send back up there? Did it send it out to its distributees?

ATTORNEY BARNET B. SKELTON: There is not an exhibit in the record that shows that Tawes didn't get the money. It's just frankly never been an issue in dispute. I mean Moose took the money. The only money Tawes ever got was attributable to his share. And that's simple.

JUSTICE PHIL JOHNSON: But there's nothing to show that his share as he received excluded any of the money that should have gone to Ms. Barnes.

ATTORNEY BARNET B. SKELTON: The way this operating agreement works, that's not the way it happens. The operator pays the royalty. That's simply the way it works.

JUSTICE PHIL JOHNSON: Okay, but my question is, as I understand what you're telling me, there's nothing in here that says that you can say he did not get any of the money that should have gone to Ms. Barnes.

ATTORNEY BARNET B. SKELTON: No I can't think of a specific exhibit that shows that he did not receive that royalty. But he did not receive that royalty, I mean that's just, that's been the record that we've dealt with all the way up. What we're going to show Your Honors is that it's not just provision five of the working interest unit agreement that compels the result that Barnes has no claim against Tawes, but only would have had a claim again Moose Oil & Gas. These agreements are not in conflict with each other and there was a line in the 5th Circuit certification opinion that gives me pause to think that there might have been some confusion about that. We don't contend that the working interest unit agreement trumps the joint operating agreement. We contend

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

that they're in harmony with each other and I'll demonstrate why. First of all, Moose Oil and Gas was designated as the responsible and liable party in the working interest unit agreement, which is signed by all of the parties who are denominated as the Moose investors, including Tawes.

JUSTICE DALE WAINWRIGHT: Let me make sure I follow your point about provision five. It says Moose shall be the liable party to the operator for the entire 46% working interest.

ATTORNEY BARNET B. SKELTON: Mm-hm.

JUSTICE DALE WAINWRIGHT: And Barnes' property was pooled not withstanding and expressed no pool ing clause. Her property constituted over 50% of the 640 acres. This says Moose is responsible for the entire 46% working interest. How does that, how does that relate to the 54% that Barnes' property constituted?

ATTORNEY BARNET B. SKELTON: No, I think the 54% you're referring to is actually Dominion's share. In other words, the Moose parties had 46% of the working interest, Dominion had 54%. It has nothing to do with Baker or Barnes. It is not, it has nothing to do with how much Miss Barnes' property comprised of the unit. The 54% is, actually there was another party with Dominion called Seisgen that Dominion later acquired its share. So you have 47% of Dominion, 6.75% for Seisgen, that's where you get to the 54%. So that's where the 54% is. The way it meshes into the joint operating agreement, notice the signature page on the joint operating agreement. The signature page bares only the signatures of Moose Oil and Gas, Seisgen and Dominion not any of the parties denominated as the Moose parties, including Tawes. And that's not just a coincidence. It's all part of the scheme. The scheme is that Moose Oil & Gas is undertaking the responsibility for the parties that signed the working interest unit agreement. Another example of this is found in Exhibit A attached to--

JUSTICE DAVID M. MEDINA: So are you saying a third-party beneficiary always has to sign a contract?

ATTORNEY BARNET B. SKELTON: No, no what I'm saying is, and I'm talking here about Tawes, who was one of these Moose investors for whom Moose Oil & Gas said it will undertake and protect them from and be the responsible and liable party. Tawes and the other parties, and if you look at your bench exhibit, who are listed along the bottom of the exhibit, none of them signed the joint operating agreement. Then when you go to Exhibit A, to the joint operating agreement, that is the exhibit which is a lawyered exhibit, it's not part of the form and it is the sharing percentages of the parties to the joint operating agreement. And what you'll find when you look at the Exhibit A to the joint operating agreement you'll see Seisgen, you'll see Dominion and you'll see Moose Oil & Gas 46%. Now in the working interest unit agreement, they made a distinction between Moose Oil & Gas and the parties, the other parties denominated at Moose. If they had intended to show that Tawes and the other parties should be included on Exhibit A and have liability under the joint operating agreement, they would have done so. They did not. This was a bargain for agreement involving three kinds of parties that are very typical in the oil and gas business. Dominion didn't want to fool with all these non- operators. It wanted to just deal with Moose so it suited them to have Moose take on that responsibility. Moose wanted to get the investors like Tawes, so naturally it wanted to offer them protection. I'll be the responsible and liable party; it all makes sense. So we believe that issue two is a trump card, Tawes wins on exhibit, on issue two. We frankly think issue three is a no-brainer jurisprudentially. There is no way on God's green Earth Tawes as a 13% working interest owner could possibly be jointly and severally liable for all of the debt. So we'd like to, we'd rely on our brief and Mr. Post will follow up. Our main distinction on third-party beneficiary, and of course time is eluding me and I want to get right to the point, is this. This case is not at all like Stine vs. Stewart. Stine vs. Stewart was a case in which, in that agreement incident to divorce provided that the parties to the divorce would pay Miss Stine, who loaned them money to buy their house, a specific sum of money from a specific source. That is a far cry from what we have here where we have various categories of expenses. And Stine vs. Stewart makes the distinction that will, I think, influence the Court to rule that there couldn't possibility be a third-party beneficiary situation. This case is more like Brown vs. Fullenweider, which was a divorce case in which the parties agreed to allocate categories of expenses between them. That's what happened here. There were just categories of expenses rather than a direct promise to pay a sum certain to a particular person and Miss Barnes' name will not be found any-

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

where in any of these agreements. Am I out of time?

CHIEF JUSTICE WALLACE B. JEFFERSON: Yes, Counsel, do you, are there any further questions? Thank you.

ATTORNEY BARNET B. SKELTON: Thank you.

CHIEF JUSTICE WALLACE B. JEFFERSON: The Court is ready to hear argument from the Appellee.

MARSHAL: May it please the Court, Mr. Watt will present argument for the Appellee.

ORAL ARGUMENT OF RICHARD D. WATT ON BEHALF OF THE RESPONDENT

ATTORNEY RICHARD D. WATT: May it please the Court, I have distributed a packet to you. There are six pages each with a number in the right-hand corner, red, a very sophisticated system. If I say turn to page two, please turn to page two. It's, I do if for two reasons, one so that I can read it, two, when I've been an arbitrator before, I like to make notes on things. Anyway you have the paper in front of you, that's what I'm referring to when I say that. Let's go I guess to the third-party beneficiary, creditor beneficiary part first. The, I think Ms. Barnes' position is obviously exactly as Miss Stine's was in Stine vs. Stewart. First off, let's look at the, what Judge Rainey's opinion called the non-consent royalty provision. It says during the time, consenting parties are entitled to receive non-consenting parties' share of production, consenting parties shall be responsible for the payment of all royalty applicable to the non-consenting parties' share of production. That means that in this instance, the Barnes lease, Justice Wainwright, did allow pooling but it had a clause that said that a bunch of things had to be done before it could happen. And so they got an amendment to the Barnes' lease and so it was pooled and its acreage comprised 54% of the unit and the Moose leases comprised 46% of the unit. Therefore, Ms. Barnes' royalty was reduced from 17.126% down to 9.675%. Therefore, had Dominion participated, Dominion would have gotten 54% of the money. Let's say in a month it was $100 to make the math easy. Dominion would have got $54, but out of that would come $9.67 that goes as royalty to Ms. Barnes.

JUSTICE DAVID M. MEDINA: Help me out here, how's this like the Stine's case? I mean that seems very, very simplistic. You got the Stine case.

ATTORNEY RICHARD D. WATT: Yes, sir?

JUSTICE DAVID M. MEDINA: You represented earlier in your argument.

ATTORNEY RICHARD D. WATT: Yes, sir. Yes, sir--

JUSTICE DAVID M. MEDINA: It seems too simplistic for this. I mean there you just had a, what a husband a wife got a divorce, they agreed to pay the mother what she gave them for their house and wouldn't pay it. I mean this is a little more complex than that.

ATTORNEY RICHARD D. WATT: Well it's a little more complex, I agree. But let's, let's, let's look at number three for Stine okay? The promise when a party goes non-consent under the operating agreement, the promise is that the consenting parties promise the non-consenting parties that they will pay the royalty attributable to the non-consenting parties' share. Dominion only had one lease contributed to this unit, the Barnes' lease. As I stated earlier, Dominion got 54% and had to pay a 9.675% royalty. When Dominion went non-consent that meant that the 54% that would have gone to Dominion goes to Moose and Tawes, okay? Of course, the 9% royalty is still due to Ms. Barnes. Now to get to your point, in the, in the Stine case there's the definition that 80 S.W.2d 589 that a creditor, an agreement benefits a creditor beneficiary if under the agreement that performance will come to him in satisfaction of a legal duty owed to him by the promisee. Right below that, I have it

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

sketched out here. Here the consenting parties, Moose, Tawes, Moose, et al, is the promisor and promises the non-consenting party, Dominion, to pay the royalty owed under the Barnes lease, which is a legal duty of promisee or Dominion; thus Barnes is the credit to beneficiary.

JUSTICE NATHAN L. HECHT: But one thing that is very clear in our case law is that the parties to the agreement have to intend that there be a third-party beneficiary. And the only argument that I see in your briefs about where that intent is evidenced was at pages 12 to 13 in your brief where you say that the parties to the agreements, the two agreements, intended this to happen so that Dominion not, being a non-consent, the non-consenting party would not get sued. But Dominion's going to get sued anyway, right?

ATTORNEY RICHARD D. WATT: Not if they pay all the royalty. If the non, if the consenting parties pay all the royalty to Ms. Barnes, Dominion never gets sued.

JUSTICE NATHAN L. HECHT: Well, you say thus this language demonstrates the party's intent to pay Ms. Barnes her royalty is the only guaranteed way to protect the non-consenting party, Dominion, from being sued, but it seems to me that since Ms. Barnes' only agreement is with Dominion, they're going to get sued whether the royalty, I mean if there's any non payment of royalty, they're going to get sued because that's who she has to look to, to get sued.

ATTORNEY RICHARD D. WATT: Well remember--

JUSTICE NATHAN L. HECHT: To get paid.

ATTORNEY RICHARD D. WATT: First off and they say this, they argue that even Dominion couldn't sue under this. Dominion couldn't sue Moose, okay?

JUSTICE NATHAN L. HECHT: Which I'm not sure I understand, but it's, it still seems to me that your only argument for intent is to keep Dominion from getting sued and I don't see any way to keep Dominion from getting sued.

ATTORNEY RICHARD D. WATT: Well, the way to keep Dominion from getting sued is for the non- consenting parties to live up to their agreement to pay Ms. Barnes the royalty. That's what keeps Dominion from getting sued.

JUSTICE NATHAN L. HECHT: But that is the only argument about intent, I take it.

ATTORNEY RICHARD D. WATT: Well, yes. Now let's continue looking at number three. This Court said in Stine, the third-party beneficiary does not have to show that the signatories executed the contract solely to benefit her as a contracting, non-contracting party. Obviously, Ms. Barnes is not the sole beneficiary here. Rather, and this is a key, the focus is on whether the contracting parties intended, at least in part, to discharge an obligation owed to a third party. If you put the proper focus here, the focus is on the promising parties, promising Dominion that they will fulfill her, its legal obligation, which is the royalty to Miss Barnes. That's what they promised. Dominion is obligated to pay the royalty. The consenting parties promised Dominion they will pay it. They didn't and she's a third- party beneficiary.

JUSTICE DALE WAINWRIGHT: [Inaudible] says and maybe you can sketch out a different view of this, I assume you do have a different view, that the whole structure was organized such that the working interest owners, they didn't want to run the show, they wanted, and Moose said because they got them on board as investors we'll take care of that so look to Moose, we'll provide those protections as Moose to the working interest owners. And under provision five, that's where the buck stops because, and he says it makes sense, the structure as he laid it out. Do you agree with that structure? I know you agree with the conclusion. But was it structured differently from your perspective?

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

ATTORNEY RICHARD D. WATT: Here's what provision five means to me. It says Moose shall be the liable party to the operator for the entire 46% working interest. And then the sentence that follows that says it will be the responsible party for each said party to the operator for obtaining and delivering elections, I'm on number one now, elections, notices, invoices, payments and bills. Alright, in the next sentence, it says should one or more of the Moose parties decide not to participate in a proposed operation, well that automatically, the only place that that is covered is in the attached operating agreement, which under four says we'll govern this, okay? Once you get to the, to the non-consent part of the operating agreement, the non-consent, which is Article VI.B.2, you no longer have operator, non- operator. You have consenting parties and non-consenting parties. Now to your question, what they're saying is that Dominion signed this working interest unit agreement and agreed that despite a whole bunch of people who are identified as Moose in the preamble to it that Dominion agreed that it would not look to any of those people for payment. What this provision is obviously for is let's say that Dominion was going to drill a well for a $1 million, it needs $460,000 from Moose. Dominion didn't want to go investor by investor by investor by investor to pick it up. It said Moose you do it. There is nothing in here anywhere that says, and if there's a non-consent situation then, and Dominion goes non-consent, then we won't look to anybody but Moose to pay the royalty to our share. In fact, Justice Wainwright, when, you have the paragraph under provision five, I'm still on page one down at the bottom, that allows the Moose parties to participate or not participate and that puts them in the same status as everybody else. They can propose operations, they can do anything that any other non-operator can. They are non-operators under the operating agreement. Here they become consenting parties. To say that Dominion by this meant, by this language and provision five, meant to change the non-consent provisions of Article VI.B.2 without saying so stretches my, stretches me a lot. You wrote the opinion, Justice Wainwright--

JUSTICE NATHAN L. HECHT: So you think Dominion could have sued Tawes?

ATTORNEY RICHARD D. WATT: Absolutely.

JUSTICE NATHAN L. HECHT: Yep and so--

ATTORNEY RICHARD D. WATT: But because Tawes was a consenting party and Dominion was a non-consenting party.

JUSTICE NATHAN L. HECHT: Right, and so couldn't this have been, couldn't this current situation have been avoided if you simply took an assignment from Dominion of its right to Tawes?

ATTORNEY RICHARD D. WATT: You mean if Dominion had assigned a cause of action to Ms. Barnes?

JUSTICE NATHAN L. HECHT: Yes.

ATTORNEY RICHARD D. WATT: I suppose so, yes.

JUSTICE NATHAN L. HECHT: And that would be preferable to trying to figure out if every royalty owner is a third-party beneficiary of these kinds of agreements?

ATTORNEY RICHARD D. WATT: We're not saying that every royalty owner is a beneficiary of these kinds of agreements. We're trying to say the one provision in this agreement that addresses non-consent provisions, that the royalty owner is a third-party creditor beneficiary of that under the, under the Stine language that I just read and I just have on number three here. Justice Wainwright, you wrote this Court's opinion in Valence v. Dorsett and it involved a non-consent clause, but it was a different issue. You'll recall it was a proposing party made a proposal for a well, the party receiving it didn't respond during the 30-day period, they're deemed to be non-consenting because of that. Then the proposing party went ahead and within that period drilled a well. The other party sued for breach of contract saying you drilled a well within the 30 days. You said in your opinion re-

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

jecting that claim that there is no language in the agreement that forbids the commencing of a well within 30 days. In other words that language in there, there is no language in this agreement that says that if in a non-consent situation that only Moose will be liable. There's just not language in this agreement and to read the language on provision five to modify Article VI.B.2 of the attached joint operating agreement, I just don't see the connection.
JUSTICE NATHAN L. HECHT: Let me ask you this, suppose in this case, I know this is an issue, but suppose it was undisputed in answer to Justice Johnson's question earlier that Tawes was paid only net of the royalty obligations, that's all Tawes received. In your view of the case, Ms. Barnes could still sue Tawes to recover her royalty payment?

ATTORNEY RICHARD D. WATT: Correct.

JUSTICE NATHAN L. HECHT: So that Tawes, as an investor, would end up paying the royalty twice basically?

ATTORNEY RICHARD D. WATT: No, not necessarily. He would, you're saying, well first, if she had already been paid all of her royalty he wouldn't have to pay it twice that's the whole thing.

JUSTICE NATHAN L. HECHT: No, if Moose ran off with the money.

ATTORNEY RICHARD D. WATT: Right.

JUSTICE NATHAN L. HECHT: So Ms. Barnes doesn't get paid.

ATTORNEY RICHARD D. WATT: Right.

JUSTICE NATHAN L. HECHT: But Tawes only gets what he would have gotten net of the royalty.

ATTORNEY RICHARD D. WATT: Right.

JUSTICE NATHAN L. HECHT: That's all he get's from Moose.

ATTORNEY RICHARD D. WATT: Right.

JUSTICE NATHAN L. HECHT: If you can sue Miss, if you can sue Tawes for the royalty, he has to pay the royalty twice.

ATTORNEY RICHARD D. WATT: Well that, exactly; that's part of being jointly and severally liable for the, for the non-consenting parties' royalty obligation. I mean that's what that means.

JUSTICE NATHAN L. HECHT: Right.

ATTORNEY RICHARD D. WATT: And the reason that, that Dominion would have bargained for that joint and several liability is, again, they wouldn't want to have happen what did happen and that's that one of the parties wouldn't pay, that was Moose, they went bankrupt and the rest would because in that event, they're going to get sued by the royalty owner. In the words of Justice Rainey, Judge Rainey in page 14 of his opinion, it's not surprising that the non-consenting parties bargained for maximum protection for that reason. This is what you and I were talking about earlier on not getting sued and getting sued. To me, this is a contractual limitation between sophisticated parties. One of them says if I don't participate in an operation and you're going to get all my interest until there's a certain financial threshold is met, I want to make sure that the royalty gets paid so that I'm not obligated to pay it and I don't get sued for not paying it and that's the reason for this and I don't see why sophisticated businessmen cannot make an agreement like this. In fact, if there were anything, I've heard the sky is

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

falling in this case that if you rule in favor of Ms. Barnes, there's going to be chaos across the oil and gas industry. I think that probably the most chaotic thing you could do would be to say that that Dominion can enforce a non-consent royalty provision like this when they go non-consent. And of course if Domin--

JUSTICE NATHAN L. HECHT: But to say that Dominion can and Tawes can and Barnes can are two different things.

ATTORNEY RICHARD D. WATT: Sir--

JUSTICE NATHAN L. HECHT: To say Dominion can and that Barnes can are two different things. I don't think anybody disagrees that Dominion could enforce it. They're all parties to the agreement, but the question is whether Ms. Barnes can enforce it.

ATTORNEY RICHARD D. WATT: Well, if, then that is the question whether she's a third-party beneficiary and that's what, I think she's exactly under Stine v. Stewart because Dominion owed her a legal obligation and the non-consenting, I mean the consenting parties, including Tawes, agreed to fulfill that legal obligation of Dominion. That is the definition and that is to quote Stine v. Stewart again, that is the proper focus here. And this agreement or two agreements viewed as a whole, which everybody agrees they should be construed together, I think that's a fair reading and certainly Judge Rainey and Judge Stine did. Now there's one thing I want to address. When Mr. Skelton was up here, we tried this case in the bankruptcy court and this entire proceeding emanates from that, only stipulated facts. I heard a bunch of stuff that isn't in those stipulated facts about who got what money, that sort of thing. The stipulated fact was that under the Baker 1 and 2 Wells, Ms. Barnes was short, under those two wells, $291,000 in royalty; that is stipulated, okay? Now if, you got to look at this this way, it's the simplest way of looking at it. Tawes' only claim, his only right to take the minerals from underneath Ms. Barnes' land is the Dominion lease. How can Tawes continue to take money off that lease when she's short and she never signed any of these agreements? She signed an oil and gas lease with Dominion. How can Tawes continue to take money when she is short? Could Dominion do that? Of course not. Dominion would have to pay her the $291,000. Tawes should be no different. Joint and several liability is the presumed position. If you go to number four, it's under the, I mean it's black letter law that if you have multiple promisors, which we have here, the consenting parties, to a single promise, that is to pay the royalty, then there is a presumption that is joint and several unless it's specifically negated. It is not, the entire non-consenting royalty clause never negates the several joint, never says anything about several liability.

JUSTICE PHIL JOHNSON: Well, Counsel, there are several places in the agreement though, it seems as though where it says, for example, all other loses, all loses incurred shall be borne by the parties in proportion to their interests and it seems like that is carried through, but yet your position is that Mr. Tawes has to pay the entire royalty.

ATTORNEY RICHARD D. WATT: Under the non-consenting situation only. You're right, Justice Johnson, normally the parties don't; it is a several liability. I agree with you completely. But under that one situation where one party is giving up its entire interest, that agreement made between the consenting parties and the non-consenting parties is that the consenting parties have to pay all of the non-consenting party's royalty obligation.

JUSTICE DALE WAINWRIGHT: And that explanation applies as well to Article VII.A of the JOA where it says the liability of the parties shall be several not joint or collective?

ATTORNEY RICHARD D. WATT: Absolutely, it does.

JUSTICE DALE WAINWRIGHT: It explains it as well?

ATTORNEY RICHARD D. WATT: Absolutely, it does because otherwise you're always going to have a non-consenting party and so that interest is out and so you're never going to have 100% of the consenting parties. So

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

it's got to be that way. And it's just the mechanism that the parties designed to accommodate this situation. My time is up unless there are questions.

CHIEF JUSTICE WALLACE B. JEFFERSON: Any further questions? Thank you, Mr. Watt.

ATTORNEY RICHARD D. WATT: Thank you.

MARSHAL: May it please the Court, Mr. Post will present the rebuttal for the appellant.

REBUTTAL ARGUMENT OF RUSSELL S. POST ON BEHALF OF PETITIONER

ATTORNEY RUSSELL S. POST: May it please the Court, I think that Justice Hecht has the central issue of the case on the third-party beneficiary test exactly right and that's what we believe is dispositive here. The Court requires an unambiguous statement of an intent to confer direct benefit on a third party to recognize third-party beneficiary standing and there's a presumption against third-party beneficiary standing and there is no explicit statement anywhere in the joint operating agreement of an intention to confer a benefit directly on a third party. In fact, Counsel has acknowledged on his brief and acknowledged again today to the Court, the purpose of this provision in Article VI.B.2 upon which they rest their claim is to protect the interests of the operators with respect to non-operators and to respect the interests of the consenting parties with respect to non-consenting parties. It is not directly to benefit the royalty owner. It would be a classic case of an incidental benefit at best that does not meet the Court's plain statement rule to confer third-party beneficiary standing. What this provision is working on in Article VI.B.2 is an allocation of expenses internally among the parties to the joint operating agreement. It has nothing to do with the obligations owed to third parties. And, in fact, in that sense, the case is much more like Brown v. Fullenweider, this Court's third-party beneficiary decision in which parties had agreed to allocate expenses between themselves and had no intention to confer direct benefit on a third party and the Court rejected third-party beneficiary standing. I also think for that reason, it falls classically into this Court's line of cases from the construction contracts and the retainage cases, which Counsel never answered in his brief, didn't answer here again today. And in Corpus Christie Bank, in Citizen's National Bank and in that long line of cases, this Court has consistently held third-party trade predators cannot be intended creditor beneficiaries of a retainage provision and construction contract because those provisions are designed to protect the principal parties, to protect the property owner from any liens on the property, not to confer a benefit on the third parties. That's exactly what's at work here in Article VI.B.2. This provision is an internal accounting provision that is not intended to affect the rights of a third party. And for that reason, it doesn't provide third-party beneficiary standing. In addition, I think important with respect to the way that works is Justice Wainwright's question about Article VII.A and the way in which liabilities are allocated to the parties in Article VII because Article VII governs allocations of liabilities and Article VII.C makes explicit that the operator pays expenses and they're charged to the joint account. And in the accounting procedures that are attached to the JOA, it's Exhibit C to the JOA in Section 22, the accounting procedures make clear the operator pays expenses and charges those expenses to the joint account and that has two consequences. Number one, it confirms that this provision in Article VI.B.2 simply is determining internal accounting among the parties to the JOA with respect to obligations, such as expenses that are paid by the operator. And Article VII.C confirms the royalties are part of those expenses. This is not a third-party beneficiary situation. But the second consequence it has is it underscores the point with respect to issue two that even if there could be a third-party beneficiary claim here, that claim could lie only against Moose because Moose was the operator. Now much of the discussion today has focused on the second prong of that argument.

JUSTICE DAVID M. MEDINA: Let me ask you this.

ATTORNEY RUSSELL S. POST: Yes, Your Honor.

JUSTICE DAVID M. MEDINA: If she is a third-party beneficiary--

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE

ATTORNEY RUSSELL S. POST: Yes.

JUSTICE DAVID M. MEDINA: What's your position on joint and several?

ATTORNEY RUSSELL S. POST: Well my position on joint and several is that it's unthinkable given the language of this agreement that there could be joint and several liability and the reason is that every provision that speaks to this issue makes clear liability of several. Article VI.B.2 itself, the provision upon which they rely, says that the entire cost and risk of these operations will be borne by the consenting parties in the proportions they elect to bear and then Article VII.A, as Justice Wainwright recognizes, makes clear that the liability is always several. So I think there's no question here that the manifested intention of the parties is only for several liability. Turning back then to Article VII.C and the consequence of this provision that makes the operator responsible for the payment of these expenses, I want to make sure that the Court doesn't misunderstand our answer to question two. It doesn't depend only on Article V of the working interest unit agreement. It also fits hand in gloves with the provisions in Article VII that say the operator pays expenses. Because what that means is that if there is a third-party beneficiary claim here, it could lie only against the party that had the obligation under the contract. It is bedrock third-party beneficiary law that a third party never has greater rights than the contract provides. This contract provided only for the operator to fulfill the royalty obligations. The claim lies only against the operator and Tawes is not the operator. Thank you very much.

CHIEF JUSTICE WALLACE B. JEFFERSON: Thank you, Counsel. The cause is submitted. This concludes arguments for this morning and the Marshal will adjourn the Court.

MARSHAL: All rise.

2010 WL 4663236 (Tex.)

END OF DOCUMENT

© 2010 Thomson Reuters/West. No Claim to Orig. US Gov. Works.
NOT FOR COMMERCIAL RE-USE