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Oil and Gas: **Whether the retained acreage is the operator-designated area or the maximum amount the Railroad Commission allows to be designated depends on the wording of the retained acreage clause.**

***Oil and Gas*: "Special Limitation" clauses must be clear, direct, and unequivocal to be enforceable.**

Endeavor Energy Resources, L.P. v. Discovery Operating, Inc. and *XOG Operating, LLC v. Chesapeake Exploration Limited Partnership* involved the interpretation of retained acreage clauses in oil and gas leases and the consequences of the manner in which these clauses were worded. A retained acreage clause is a lease provision releasing acreage not assigned to a producing well at the end of the primary lease. Both opinions were unanimous and reached opposite outcomes by application of common principles of contract interpretation.

In *Endeavor Energy*, the retained acreage clause provided that, at the later of the end of the lease's primary term or "cessation of the continuous development," the lease terminated except for the areas situated in a "governmental proration unit assigned to a well producing oil or gas in paying quantities." The clause further specified that each proration unit should contain the number of acres necessary under Railroad Commission rules of Texas *for obtaining maximum production allowed* for that well. Commission rules allowed up to 160 acres to be assigned to the proration unit, but the operator only assigned roughly half that amount. The issue was whether the retained-acreage clause retained the 160 acres that could have been assigned to the proration unit under Commission rules, or only the 81 acres that the operator *actually* assigned. According to the opinion, "governmental proration unit" could only refer to the acreage *actually* assigned because only the operator could do the assigning. As a result, Endeavor had only retained the 81 acres it actually assigned, not the 160 acres that could have been assigned but were not.

In *XOG Operating*, the wording of the retained acreage clause caused the court to reach the opposite conclusion: the acreage retained was the quantity that could have been assigned to the well, not the amount the operator actually assigned in the plat filed with the Commission. The retained acreage clause specified the area

included within the proration … unit of each well …. "[P]roration unit" … mean[s] the area … then *established or prescribed* by field rules or special order of the appropriate regulatory authority…. In the absence of such field rules or special order, each proration unit shall be deemed to be 320 acres … surrounding[the] well….

At first blush, one might think that "established" might refer, like the clause in *Endeavor*, to the acreage the operator actually assigned to the well. After all, only the operator can assign – i.e., "establish" – the area included in the proration unit. The opinion reasoned, however, that "established or prescribed by field rules or special order of the appropriate regulatory authority" could only refer to the area that the Commission's rules and regulations allowed to be assigned to the well, not the area that the operator actually designated. As a result, the operator was held to have retained 320 acres per well, which far exceeded the area the operator had actually assigned to each well in the proration plats filed with the Commission. Apparently sensitive to an outcome differing from that in *Endeavor*, the court pointed

[1] The opinions expressed are solely those of the author. They do not necessarily represent the views of Munsch, Hardt Kopf & Harr, P.C. or its clients.

out that retained acreage clauses vary widely "because parties are free to contract in any way they choose not prohibited by law." "[A]s with any contract, the parties to a retained-acreage provision are presumed to know the law and to have stated their agreement in light of it."

The interpretations in *Endeavor* and *XOG* were also driven by the court's attitude about "special limitations" provisions that automatically terminate a lease when a special event happens. Confirming that such limitations are not to be favored, it indicated that courts "will not find a special limitation 'unless the language is so clear, precise, and unequivocal that [courts] can reasonably give it no other meaning.'" In other words, such clauses must be clear, precise, and unequivocal before being treated as a valid special limitations.

***Attorney's Fees*: If a contingency fee arrangement is unenforceable because it's unwritten or not signed by both attorney and client, the attorney may recover in *quantum meruit* the value of the benefit conferred. But the fees that would have been recoverable under the unenforceable contingency agreement is not evidence of the amount of the benefit conferred.**

Under Government Code § 82.065(a), a contingency fee contract cannot be enforced unless written and signed by both attorney and client. If the agreement is unenforceable because it fails to meet these requirements, can the attorney nevertheless recover the value of the benefit the attorney's services conferred on the client?[2] If so, can the terms of the unenforceable contingency fee agreement be considered to measure the value of that benefit? These are the questions that Justice Green addressed in a unanimous opinion for the Justices participating in *Hill v. Shamoun & Norman*.

1. *An attorney may recover the value of the benefit the legal services conferred on the client even if the contingency fee agreement is unenforceable.*

Because his oral contingency agreement was unenforceable, the attorney sought to recover in *quantum meruit*. The court rejected the argument that the attorney could not recover under any theory for violating the Government Code's "statute of frauds." Generally, a party cannot recover as damages the benefit of an agreement that is unenforceable for failure to comply with the statute of frauds. However, recovery under *quantum meruit* does not run afoul of this prohibition because it seeks only the value of the services rendered to the client, not the benefits specified in the unenforceable agreement. Even at common law, the courts allowed equitable recovery under *quantum meruit* because without it, a shield is turned into a sword: clients could be unjustly enriched by the very statute intended to protect them.

2. *Attorneys may recover separately for services when the engagement letter for particular matters restricts the attorney's representation to providing services other than those that are the subject of the* quantum meruit *action.*

The court rejected the client's argument that the attorney should not be entitled to any recovery for representing the client in "global settlement" negotiations for all of several disparate cases. The client's argument was based on the existence of separate engagements for each of these matters. The court pointed out, however, that these engagements were for very specific representation in relation to specific legal services. They were not "general" engagements that would have included settlement negotiations. The services provided were not part of a pre-existing obligation and, therefore, recovery of some amount for them was not foreclosed as a matter of law.

3. *But the attorney cannot indirectly recover the amount that would have been owed under the unenforceable contingency fee agreement by using it as a means of measuring recovery based on the reasonable value of the benefit conferred.*

One can recover in *quantum meruit* the reasonable value of services provided to and accepted by the defendant who had reason to know the provider expected to be paid. In this case, the attorney's fees expert in *Hill* cleverly – too

[2] Paragraph (c) of §82.065 authorizing recovery in *quantum meruit* when the contingency agreement was not enforceable due to paragraph (a) did not apply because the agreement in question was entered before this paragraph became effective.

cleverly as it turns out – tried to establish "reasonable value" only with the percentages allegedly included in the oral contingency fee agreement instead of proving the value of those services independently of the percentage contingency. The percentage assessed in the unenforceable contingency fee agreement is not evidence of reasonable value of only the services provided. Thus, the court overturned the jury's verdict about the amount of recovery for legally insufficient evidence.

Ordinarily, when a finding for the plaintiff is overturned for legally insufficient evidence, the court renders a take-nothing judgment. However, when the topic is the *recoverable amount* of attorney's fees, when the evidence shows that the attorney provided some services to the client, it remands for a determination of the amount of those fees instead of denying recovery altogether. It is *good* to hold a Bar Card. In this case, it was undisputed that the attorney provided services and that the parties had agreed that services other than those that were the subject of the oral contingency fee arrangement would be compensated at a stated hourly rate. Moreover, the charge submitted as a measure of damages the product of the hourly rate and hours worked. Because there was *some* evidence of the reasonable value of the attorney's services beyond those included in the engagement letters for each matter, the Court remanded the case for a new trial on the attorney's *quantum meruit* recovery of attorney's fees for his services in represent the client in the global settlement negotiations. Otherwise, the client would be unjustly enriched.

In arriving at its decision, the court addressed the proper standard of review. In proceedings to determine recovery in equity, the parties are entitled to a jury determination of objective facts, such as the existence and value of the services. But application of equitable principles is a question of law that only the judge can determine, which is reviewed for abuse of discretion. Thus, the trial court's decision to disregard the jury's determination of the recoverable amount, which was based only on impermissible evidence about the amount of the unenforceable contingent fee, was neither arbitrary nor capricious. However, the trial court's decision to deny recovery of any amount was an abuse because there was some evidence of a lesser value of the legal services provided. On remand, it is the attorney's burden to show the reasonableness of the valuation of the services provided sans an enforceable contract.

Extra-Contractual Damages: **Even if there is no breach, policy benefits are recoverable as damages for an insurer's violation of an extra-contractual duty if the violation caused the loss of the contractual right or inflicts an independent injury.**

***Conflicting Jury Verdicts*: Appellate courts can remand for new trial under Rule 295 on the basis of an irreconcilable conflict in the jury's verdict even if the parties and the trial judge agree that there was no conflict and, therefore, there is no objection preserving the error in rendering judgment on a conflicting verdict.**
The court also revisited its opinion in *USAA Texas Lloyds Insurance Co. v. Menchaca* (*Menchaca I*), previously issued April 7, 2017. *Menchaca* involved a claim under the insured's property insurance. The jury did not find that the insurer breached the policy, but nonetheless found insurer violated the Insurance Code by failing to reasonably investigate. Thus, the question *Menchaca I* initially addressed was when policy benefits could be recovered as damages if an insurer engages in conduct that violates the statutory or common law standards for good faith and fair dealing but does not breach the policy itself.

1. *When policy benefits can be recovered as extra-contractual damages without a finding that the insurer breached the policy*

Briefly stated, the rule announced in *Menchaca I* was that policy benefits, if lost or denied as the result of the insurers' common-law "bad faith" or statutory violations, could be recovered as damages for those violations. However, if the insured would have been entitled to no policy benefits regardless of the statutory violations or "bad faith," such conduct alone would not make contractual benefits recoverable as extra-contractual damages.
Menchaca I announced five "rules" to determine whether policy benefits could be recovered as extra-contractual damages. Rule 1 is that an insured generally "cannot recover policy benefits as damages for an insurer's statutory [or common-law bad faith] violation if the policy does not provide the insured a right to receive those benefits." Rules 2 and 3 are that an "insured who establishes a right to [insurance policy benefits] … can recover those benefits as actual [extra-contractual] damages if the insurer's … violation causes the loss of the benefits" or the contractual right to receive them. Rule 4 is the insured may recover damages for *that injury* even if the policy does not grant the insured a right to benefits. The last rule follows from the four previous rules: an insured cannot recover any damages based on an insurer's violation of an extra-contractual duty if the insured had no right to receive benefits under the policy

and sustained no injury independent of a right to benefits. For a more complete summary of *Menchaca I*, see the *Update* for opinions issued April 7, 2017.

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Seven Justices joined the portion of *Menchaca II* that included a virtually verbatim repetition of the holding in the *Menchaca I*. Justice Johnson did not participate in the decision and Justice Blacklock concurred in the judgment without joining any particular opinion.

2. *Appellate courts may remand for new trial if it finds the jury verdict contains conflicting answers even if there is no objection in the trial court asserting the existence of an irreconcilable conflict.*

The real difference between *Menchaca II* and *Menchaca I* concerned whether a remand for further proceeding was necessary to resolve the tension between the jury's failure to find a contractual breach while awarding policy benefits as damages for violating the statutory duty to reasonably investigate the claim.

Six Justices agreed the jury's verdicts concerning breach of contract and the Insurance Code violations irreconcilably conflicted. But they disagreed about the proper consequences of the conflict. Justices Boyd, Lehrmann and Devine did not believe the court could overturn the trial court's judgment because neither party objected that the jury's verdict was conflicting before the jury was dismissed. The Boyd opinion took the view that Rule 295 only allowed the conflict to be resolved by directing the jury to engage in further deliberations – something that could not happen once the jury was released.

A conflicting jury verdict, however, like the lack of subject-matter jurisdiction, is one of the few instances that is deemed fundamental error that cannot be waived by a failure to object. Without referring to this rule, Justice Green, joined by Justices Guzman and Brown, would have rendered judgment that the insured take nothing due to the conflicting verdicts by relying on that part of Texas Rule of Civil Procedure 295 that allows the trial court to "reform" the verdict to render judgment for the defendant if no one asserts the verdict is conflicting and no one challenges the jury's answers. Justice Green's opinion pointed out one of the few bases on which appellate courts can review the granting of a new trial is when the new trial is granted due to a perceived fatal conflict in the verdict.

Chief Justice Hecht in a concurring opinion broke the 3:3 tie over the proper disposition of the case. He pointed out that the insured had raised the issue of a possible conflict before the jury was released. The trial court refused to entertain this objection, however, because the insured insisted on including the breach of contract question despite knowing a conflicting verdict was likely. The Chief Justice believed it "defie[d] logic" to hold that an appellate court could not overturn a verdict for failure to object when the trial court and both parties did not believe further deliberations were necessary and when neither party could know which of them would be challenging the judgment. Chief Justice Hecht pointed out that neither party could object without being inconsistent with their common position that the there was no conflict in the verdict. By a 5:3 decision, the case was remanded to the trial court for a new trial.