IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF TEXAS
MIDLAND/ODESSA DIVISION

WILLIAMS O & G RESOURCES, LLC,	§	
	§	
Plaintiff,	§	
	§	
v.	§	**MO:24-CV-00185-DC-RCG**
	§	
DIAMONDBACK ENERGY, INC. and DIAMONDBACK E&P, LLC,	§	
	§	
Defendants.	§	

REPORT AND RECOMMENDATION OF THE U.S. MAGISTRATE JUDGE

BEFORE THE COURT is Defendants Diamondback Energy, Inc. and Diamondback E&P, LLC's (together, "Defendants" or "Defendants Diamondback") Motion to Dismiss. (Doc. 23).[1] This case is before the undersigned through a Standing Order pursuant to 28 U.S.C. § 636 and Appendix C of the Local Court Rules for the Assignment of Duties to United States Magistrate Judges. After due consideration of the Parties' briefs and the case law, the Court **RECOMMENDS** that Defendants' Motion to Dismiss be **GRANTED IN PART** and **DENIED IN PART**. (Doc. 23).

I. BACKGROUND

On February 6, 2024, Plaintiff Williams O&G Resources, LLC ("Plaintiff" or "Plaintiff Williams") filed its Original Complaint against Defendants Diamondback in the Austin Division of the United States District Court for the Western District of Texas. (Doc. 1). Plaintiff Williams filed its First Amended Complaint on May 31, 2024. (Doc. 22). On June 13, 2024, Defendants Diamondback filed a renewed Motion to Transfer Venue to the Midland/Odessa Division of the

1. All page number citations are to CM/ECF generated pagination unless otherwise noted.

Western District of Texas (Doc. 24). Defendants' Motion was granted, and the case is now properly in the Midland/Odessa Division. (Doc. 37).

Plaintiff's factual allegations are as follows. This case involves a tract of land situated in Reeves County, Texas, described as: the eastern 280 acres of Section 16, Block C-4, Public School Lands, Reeves County, Texas ("Mineral Reserved Land"). (Doc. 22 at 6). On August 4, 1948, the State of Texas awarded the Mineral Reserved Land to Martin Kearney—Plaintiff's predecessor-in-interest. *Id*.; (Doc. 22-1 at 1). The land was awarded "with a reservation of one-eighth of the sulphur and one-sixteenth of all other minerals as a free royalty to the State." (Doc. 22-1 at 1). On June 28, 1957, Kearney, as Lessor, executed and delivered an Oil, Gas, and Mineral Lease ("Williams' Lease" or "Lease") that encumbers the Mineral Reserved Land to El Paso Natural Gas Company, as Lessee. (Doc. 22 at 7); (Doc. 13-3 at 2–3). On March 12, 1968, the Lease was amended. (Doc. 13-3 at 4–6). On October 31, 1978, Kearney died, and the Mineral Reserved Land was inherited by Kearney's great-uncle, Emmett Williams. (Doc. 22 at 8). Emmett then assigned and transferred the ownership of the Mineral Reserved Land into a Texas limited liability company—Plaintiff Williams. *Id*. The sole Member of the company is Emmett's daughter, Dorthy Brothers. *Id*.

The original lessee of the Williams' Lease was El Paso Natural Gas Company. *Id*. Through assignment, the oil and gas leasehold estate of the Williams' Lease was "horizontally severed to cover four separate sections of geological strata within the Mineral Reserved Land, with separate ownership of each geological strata . . . ." *Id*. at 8–9. Relevant here, "[a] second middle-level rights oil and gas lease that covers depths between 7,798' (recited as being 300' above the Bone Spring formation) and 12,830' (recited as being the base of the Wolfcamp formation) in the Mineral Reserved Land" is vested in Defendants Diamondback. *Id*. at 9.

Therefore, this lawsuit only concerns the surface estate of the Mineral Reserved Land and the geological strata of 7,798' and 12,830', of which the oil and gas leasehold estate of the Williams' Lease was owned by Defendants for the period through October 31, 2023. *Id*. at 9–10. On November 1, 2023, Defendants sold their interest in the Williams' Lease, and Plaintiff does not assert any claims arising after that date. *Id*. at 10.

Separate from the Lease, in 2017, Plaintiff and Defendants entered into a Surface Use Agreement ("SUA"). *Id*. at 11. The Complaint states that the SUA granted Defendants permission to construct drill-site locations, pads, pits, and other surface facilities; drill, complete, operate, and plug wells drilled; drill into the subsurface of the Mineral Reserved Land; have ingress and egress with respect to the Mineral Reserved Land; construct and operate a tank battery; construct and operate roads, electrical lines, and pipelines; and purchase Plaintiff's caliche for road and pad construction. *Id*. at 11–12. Further, the SUA also contained a provision related to Defendants purchasing water from Plaintiff. *Id*. at 12. Under the authority of the Williams' Lease and the SUA, Defendants applied for and received drilling permits issued by the Texas Railroad Commission to drill and complete six oil wells on the Mineral Reserved Land. *Id*. at 13–14. "Through October 31 of 2023, the above six (6) wells . . . have cumulatively produced 1,810,970 barrels of oil and 5,871,683 mcf of natural gas." *Id*. at 18.

In its First Amended Complaint, Plaintiff Williams brings substantive claims under the Texas Relinquishment Act, TEX. NAT. RES. CODE § 52.171, *et seq*.; the Texas Free Royalty Act, TEX. NAT. RES. CODE § 51.054, *et seq*.; the implied covenant to manage and administer the lease as would a reasonably prudent oil and gas operator/lessee with respect to paying compensatory royalties and failing to pool; and breach of contract. (Doc. 22 at 20–27). Plaintiff also asserts

derivative claims, including attorney's fees, discovery rule, and conditions precent fulfilled. *Id*. at 26–27.

On June 13, 2024, Defendants Diamondback filed a renewed Motion to Dismiss Plaintiff's First Amended Complaint. (Doc. 23). Defendants argue Plaintiff Williams' (1) Counts One and Two should be dismissed because the Lease is not subject to the Texas Relinquishment Act; (2) Count Three should be dismissed because the express language of the lease supersedes the implied duty to pool Williams' Lease with an adjacent lease; (3) Count Four should be dismissed because Plaintiff has failed to state a claim for relief under a breach of contract theory; and (4) Counts Five, Six, and Seven are derivative claims of Counts One through Four and necessarily fail as Plaintiff did not state a claim for relief. *Id*. The instant matter is fully briefed and ripe for disposition.

II. LEGAL STANDARD

Federal Rule of Civil Procedure 12(b)(6) allows a party to move for the dismissal of a complaint for "failure to state a claim upon which relief can be granted." To survive a motion to dismiss, "a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007)). "A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Iqbal*, 556 U.S. at 678. A claim for relief must contain: (1) "a short and plain statement of the grounds for the court's jurisdiction"; (2) "a short and plain statement of the claim showing that the pleader is entitled to the relief"; and (3) "a demand for the relief sought." FED. R. CIV. P. 8(a). A plaintiff "must provide enough factual allegations to draw the reasonable inference that the elements exist." *Innova Hosp. San Antonio, L.P. v. Blue*

Cross & Blue Shield of Ga., Inc., 995 F. Supp. 2d 587, 602 (N.D. Tex. 2014) (citing *Patrick v. Wal–Mart, Inc.-Store No. 155*, 681 F.3d 614, 617 (5th Cir. 2012)); *see also Torch Liquidating Tr. ex rel. Bridge Assocs. L.L.C. v. Stockstill*, 561 F.3d 377, 384 (5th Cir. 2009) ("[T]he complaint must contain either direct allegations or permit properly drawn inferences to support every material point necessary to sustain recovery") (internal quotation marks and citations omitted).

In a court's review of a motion to dismiss under Rule 12(b)(6), all factual allegations from the complaint should be taken as true, and the facts are to be construed in the light most favorable to the nonmoving party. *Fernandez-Montes v. Allied Pilots Assoc.*, 987 F.2d 278, 284 (5th Cir. 1993). Still, a complaint must contain "more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." *Twombly*, 550 U.S. at 555. "'[N]aked assertions' devoid of 'further factual enhancement,'" and "threadbare recitals of the elements of a cause of action, supported by mere conclusory statements," are not entitled to the presumption of truth. *Iqbal*, 556 U.S. at 678 (quoting *Twombly*, 550 U.S. at 557); *see also R2 Invs. LDC v. Phillips*, 401 F.3d 638, 642 (5th Cir. 2005) (stating that the Court should neither "strain to find inferences favorable to plaintiffs" nor accept "conclusory allegations, unwarranted deductions, or legal conclusions.").

"When reviewing a motion to dismiss, a district court must consider the complaint in its entirety, as well as other sources courts ordinarily examine when ruling on Rule 12(b)(6) motions to dismiss, in particular, documents incorporated into the complaint by reference, and matters of which a court may take judicial notice." *Funk v. Stryker Corp.*, 631 F.3d 777, 783 (5th Cir. 2011). This includes "documents attached to the complaint, and any documents attached to the motion to dismiss that are central to the claim and referenced by the complaint." *Lone Star Fund V*

(U.S.), L.P. v. Barclays Bank PLC, 594 F.3d 383, 387 (5th Cir. 2010) (citing *Collins v. Morgan Stanley Dean Witter*, 224 F.3d 496, 498–99 (5th Cir. 2000)).

III. DISCUSSION

A. Counts One and Two

1. Texas Relinquishment Act and Land Sales Act

In Count One of its First Amended Complaint, Plaintiff Williams alleges that Defendants Diamondback breached their express statutory obligations under the Texas Relinquishment Act of 1919 ("Relinquishment Act") to either drill offset wells, or alternatively, to pay Plaintiff compensatory royalties. (Doc. 22 at 21–22). Similarly, in Count Two, Plaintiffs allege that Defendants breached their implied duty to manage and administer the Lease as would a reasonable prudent oil and gas operator by failing to pay compensatory royalties to Plaintiff in lieu of drilling offset wells required by the Relinquishment Act. *Id*. at 23. In their Motion to Dismiss, Defendants argue that Counts One and Two are based on a fundamentally incorrect premise—that Williams' Lease is subject to the Relinquishment Act. (Doc. 23 at 1). Instead, Defendants assert that Williams' land, minerals, and the Williams' Lease are subject to the Land Sales Act of the State of Texas[2] ("Land Sales Act"), which contains no duty to drill offset wells or pay compensatory royalties. *Id*. at 13. Therefore, the threshold issue before the Court is the interplay between the Relinquishment Act and the Land Sale Act.

Defendants' argument can be boiled down to this: The Relinquishment Act only applies to public land sold by the State of Texas between September 1, 1895, and August 31, 1931.[3]

2. Plaintiff consistently refer to the "Land Sales Act" as the "Texas Free Royalty Act," but Defendants acknowledge there are many names for this statute. (Doc. 23 at 2 n.1). The Court will refer to the statute as the "Land Sales Act."

3. Defendants assert Texas authorities are split on whether the Relinquishment Act extends to lands sold by the State until May 29, 1931, or until August 21, 1931. (Doc. 23 at 10 n.4). The Court is not asked to decide this issue as it will not affect the outcome of this case. *Id*.

(Doc. 23 at 10). The land and minerals underlying Williams' Lease were sold by the State to Plaintiff's predecessor-in-interest on August 4, 1948, so the Relinquishment Act does not apply. *Id*. at 2. To the contrary, Plaintiff asserts that the Mineral Reserved Land, and the minerals within it, are subject to both the Relinquishment Act and the Land Sales Act. (Doc. 22 at 7). Specifically, the Relinquishment Act governs the oil and gas, and the Land Sales Act deals with the land and other minerals. Therefore, all the provisions of both Acts are incorporated by law in the Williams' Lease. *Id*. at 8.

To adjudicate this question, the Court must review a portion of the extensive legislative history surrounding public school lands and mineral rights in Texas. *See Magnolia Petrol. Co. v. Walker*, 83 S.W.2d 929, 932 (Tex. 1935) ("To one who will study the extent and intricacies of our school land laws, and the purposes for which they were enacted, it is quite obvious that they were not always clear in their meaning."). In the Texas Constitution of 1876, the State set aside more than 42,500,000 acres of land in support of public schools. TEX. CONST. OF 1876, art. VII, § 2; A. W. Walker, Jr., *The Texas Relinquishment Act*, 1 INST. ON OIL & GAS L. & TAX'N. 245, 248 (1949), *cited with approval in Scott v. Exxon Corp.*, 763 S.W.2d 764 (Tex. 1988). As early as 1883, the Texas Legislature began enacting laws to classify and sell these public lands, as well as the minerals thereunder. *Magnolia Petroleum Co.*, 83 S.W.2d at 932. The first law pertinent to the case at hand is the Relinquishment Act passed in 1919. The relevant sections of the Relinquishment Act to be applied here provide:

> § 52.171. School and Asylum Lands
>
> The state hereby constitutes the owner of the soil its agent for the purposes herein named, and in consideration therefor, relinquishes and vests in the owner of the soil an undivided fifteen-sixteenths of all oil and gas which has been undeveloped and the value of the same that may be upon and within the surveyed and unsurveyed public free school land and asylum lands and portions of such

> surveys sold with a mineral classification or mineral reservation, subject to the terms of this law. The remaining undivided portion of said oil and gas and its value is hereby reserved for the use of and benefit of the public school fund and the several asylum funds.
>
> § 52.172. Sale and Lease by Agent
>
> The owner of said land is hereby authorized to sell or lease to any person, firm, or corporation the oil and gas that may be thereon or therein upon such terms and conditions as such owner may deem best, subject only to the provisions hereof, and he may have a second lien thereon to secure the payment of any sum due him. All leases and sales so made shall be assignable. No oil or gas rights shall be sold or leased hereunder for less than 10 cents per acre per year plus royalty, and the lessee or purchaser shall in every case pay the state 10 cents per acre per year of sales and rentals; and in case of production shall pay the state the undivided one-sixteenth of the value of the oil and gas reserved herein, and like amounts to the owner of the soil.
>
> § 52.182. Damages to Soil
>
> The payment of delay rentals and the obligation to pay the owner of the soil one-sixteenth of the production and the payment of same when produced and the acceptance of same by the owner, shall be in lieu of all damages to the soil.

TEX. NAT. RES. CODE §§ 52.171–52.172, 52.182.

Following the enactment of the Relinquishment Act, in 1928, the Texas Supreme Court interpreted the law in *Greene v. Robison*, 8 S.W.2d 655 (Tex. 1928). There, the Court held that public lands sold by the State to individuals—referred to as "owners of the soil"—under the Relinquishment Act did not grant to the owners interest in the mineral rights. *Id.*; *Scott*, 763 S.W.2d at 766. Rather, the State maintained title to the oil and gas beneath the surface but relinquished to the surface owners the authority to lease 15/16th of the State's undeveloped oil and gas. *Scott*, 763 S.W.2d at 766. In effect, landowners, as agents of the State, held the leasing rights, but the oil and gas remained vested in the State. *See id.*; *State of Tex. v. Figueroa*, 389 F.2d 251, 252 (5th Cir. 1968). As a part of the Act, "the State is to receive as a minimum for the sale

of the gas and oil one-sixteenth of all gas and oil as royalty, and 10 cents per acre annum as rental, and certain sums are to be received by the owner of the land for his services in making the lease as the agent of the State, during the term of the lease." *Wintermann v. McDonald*, 102 S.W.2d 167, 170 (Tex. 1937). Further, the Relinquishment Act imposed certain duties on the agent in control of the land regarding the production of oil and gas. *See* TEX. NAT. RES. CODE § 52.173.

Then, in 1931, the Legislature enacted Senate Bill 310, which, contrary to the Relinquishment Act, granted surface owners title to 15/16th of all minerals in all lands described in the Act and reserved only 1/16th of the minerals as a free royalty to the State. *Wintermann*, 102 S.W.2d at 170. This, however, was declared unconstitutional in *Empire Gas & Fuel Co. v. State*, 47 S.W.2d 265 (Tex. 1932). While Senate Bill 310 was still on the books, the Legislature also passed House Bill 358—this would come to be called the Land Sales Act. *Wintermann*, 102 S.W.2d at 171. The Land Sales Act, as amended, in pertinent part provides:

> (a) Except as otherwise provided in this section, land dedicated to the permanent school fund shall be sold subject to a reservation set by the board of not less than one-eighth of all sulphur and other mineral substances from which sulphur may be derived or produced and not less than one-sixteenth of all other minerals to the state; provided, that if leasing rights are retained hereunder, the reserved minerals shall be subject to lease as provided by [the Relinquishment Act] . . . .
>
> (b) Land that is set apart for the various asylum funds shall be sold with the oil, gas, coal, and all other minerals reserved to the fund to which the land belongs.
>
> (c) The provisions of this section do not apply to oil and gas sold from public school land covered by [the Relinquishment Act].
>
> (e) An oil, gas, or other mineral lease on land in which the state reserves a mineral or royalty interest is not effective until a certified copy of the recorded lease is filed in the General Land Office.

TEX. NAT. RES. CODE § 51.054.

With both the Relinquishment Act and the Land Sales Act in place, questions arose as to how to square the two laws together. In 1937, a landowner brought this question to the Texas Supreme Court. *See Wintermann*, 102 S.W.2d at 168. In this case, the State awarded the landowner nine acres of unsurveyed school land in 1934. *Id*. The landowner argued, under the Land Sale Act,[4] that the "land should be sold to him without condition of settlement and with a reservation of one-sixteenth of all minerals, except sulphur, as a free royalty to the State, and one-eighth of all sulphur and other mineral substances from which sulphur may be derived or produced, as a free royalty to the State." *Id*. Conversely, the Commissioner of the General Land Office stated that he had "issued many awards and patents to public school lands under the [Land Sales Act], and in all such awards and patents there has been placed therein a reservation of all minerals to the State." *Id*. Therefore, the issue before the *Wintermann* court was which Act should apply: the Land Sales Act—with a reservation to the State of only 1/16th of all minerals and 1/8th of sulphur as a free royalty—or the Relinquishment Act—with a reservation to the State of all minerals in, under, and on the land. *Id*. at 169. In its analysis, the court explained, "[The Land Sales Act] and the Relinquishment Act should be construed together. It is plain that the [Land Sales] Act is not intended to repeal the Relinquishment Act; nor does the Relinquishment Act occupy the field covered by this law. This law covers a wider field than the Relinquishment Act. The land sold under the provisions of this act will be governed by the terms thereof, and not by the terms of the Relinquishment Act." *Id*. at 172. Ultimately, the court held that the Land Commission must award the land pursuant to the Land Sales Act, without a full reservation of minerals to the State. *Id*. at 173.

4. In *Wintermann*, the court refers to the Land Sale Act as the "Act of 1931" or "1931 Act." *Wintermann*, 102 S.W.2d 167.

Here, the parties dispute how to interpret the *Wintermann* case. Plaintiff asserts "*Wintermann* held that the Relinquishment Act dealt only with oil and gas, and the [Land Sale Act] dealt only with land and other minerals." (Doc. 31 at 10). On the other hand, Defendants believe the court "harmonized the Relinquishment Act and the Sales Act in *Wintermann*, holding the Relinquishment Act applies to conveyances prior to the adoption of the Sales Act and does not apply to the lands sold subject to the Sales Act." (Doc. 23 at 11). The Court agrees with Defendants. While, admittedly, the *Wintermann* case is not entirely clear, the Court finds that public lands, and the minerals within, bought after the passage of the Land Sales Act are not subject to the Relinquishment Act.

The Court does not find Plaintiff's argument persuasive that the Acts apply to separate minerals. Within the opinion, the Texas Supreme Court explicitly says that the Relinquishment Act "deals only with oil and gas." *Wintermann*, 102 S.W.2d at 172. However, when discussing the Land Sale Act, the court consistently refers to "minerals," without a limitation. *See generally id*. Further, in the court's holding, it explained that land bought in 1934 would be subject to the reservation constraints of the Land Sales Act but made no mention that any potential oil and gas below the land would be bound by the Relinquishment Act. *See id*. Additionally, the belief that the Land Sale Act encompasses oil and gas can be seen in other sources as well, including other Texas Supreme Court cases. *See Caples v. Cole*, 102 S.W.2d 173, 174–75 (Tex. 1937) (explaining one Party was seeking to purchase, or, in the alternative, lease the public land for oil and gas purposes under the Land Sale Act). In the text of the Land Sales Act, it provides, "The provisions of this section do not apply to oil and gas sold from public school land covered by [the Relinquishment Act]." TEX. NAT. RES. CODE § 51.054(c). The Act specifically excludes oil and gas sold from certain lands but does not exclude oil and gas entirely. *See id*. Further, within

the Texas Administrative Code, there is a statute that discusses the ways in which oil and gas underlying state lands can be leased, depending on the type of land. 31 TEX. ADMIN. CODE § 9.21 (1999). In the statute, it separates the oil and gas lease requirements for Relinquishment Act lands from Free Royalty lands,[5] which shows oil and gas is not solely subject to the Relinquishment Act. *Id*. § 9.21(3). Further, when discussing the procedures to lease Free Royalty lands, the statute explicitly states, "The holder of the executive or leasing rights on free royalty land shall act as the state's agent in executing *oil and gas leases* covering the state's free royalty interest." § 9.22(4)(B) (emphasis added). Looking at these Texas statutes, the Court concludes that oil and gas leased from public lands bought from the State following the passage of the Land Sales Act are covered by said Act.

Based on its reading of *Wintermann*, Plaintiff also argues that if the Mineral Reserved Land was not subject to the Relinquishment Act, it would not have had the authority to execute oil and gas leases for the last 67 years. (Doc. 31 at 11). However, the authority to lease minerals, including oil and gas, on land sold under the Land Sales Act is derived from the Act itself, not the Relinquishment Act. *See Wintermann*, 102 S.W.2d at 172 ("The land sold under the provisions of this act will be governed by the terms thereof, and not by the terms of the Relinquishment Act . . . . [W]e think that [the Land Sale Act], when construed in the light of the policy of this State relating to public lands and minerals as expressed in certain laws, if not directly, impliedly authorizes the landowner to act as the agent of the State in executing mineral leases thereon, and reserving to the State the free royalties described in [the Land Sale Act].").

While this Court may be the first federal court to address this issue, the Court is not alone in its interpretation of *Wintermann*. The Texas Administrative Code, the Texas General Land

5. Free Royalty lands is synonymous with Land Sales Act lands. 31 TEX. ADMIN. CODE § 9.1(6) (1999) ("Free royalty lands—Lands sold by the state in which the state reserved a free royalty interest but did not retain any leasing or executive rights." (citing the Land Sales Act)).

Office ("GLO"), the Texas Attorney General ("Texas AG"), and many legal commentators all support the notion that lands, and the minerals within it, are only subject to the Relinquishment Act if the land was bought before the Land Sales Act passed in 1931.

To start, the Texas Administrative Code explicitly defines Relinquishment Act lands as "[a]ny public free school or asylum lands, whether surveyed or unsurveyed, sold with a mineral classification or reservation between September 1, 1895, and May 29, 1931 . . . ." 31 TEX. ADMIN. CODE § 9.1(17) (1999). Similarly, the GLO has a brochure entitled, "Guidelines for Leasing Relinquishment Act Lands."[6] In it, the GLO provides a history of the Relinquishment Act and states, "Enacted in 1919, the Relinquishment Act, as interpreted by the Courts, reserves all minerals to the State in those lands sold with a mineral classification between September 1, 1895 and June 29, 1931."[7] Additionally, in an Opinion in 1943, the Texas AG weighed in on the relationship between the Relinquishment Act and the Land Sales Act.[8] The Texas AG was asked, "Do leases issued by the land owner on Public School Lands, sold under the Sales Act of 1931, come within the provision of what is known as the Relinquishment Act?"[9] The AG "answered in the negative."[10] The opinion further stated that all public lands in Texas, at that time, were subject to *either* the Relinquishment Act or the Land Sales Act:

> While all lands once subject to the provisions of the Relinquishment Act remain so, this Act was replaced by the Sales

6. GUIDELINES FOR LEASING RELINQUISHMENT ACT LANDS, TEX. GEN. LAND OFF. (2018), https://www.glo.texas.gov/sites/default/files/resources/glo/energy-business/oil-gas/mineral-leasing/leasing/forms/Guidelines-for-Leasing-Relinquishment-Act-Lands.pdf.

7. *Id*. at 1.

8. Power of Commissioner of General Land Office to Accept for Filing or to Approve Mineral Lease with Pooling Clause, Tex. Att'ys Gen. Op. No. 0-5700, at 2 (1943), https://www.texasattorneygeneral.gov/sites/default/files/opinion-files/opinion/1943/O-5700.pdf.

9. *Id*.

10. *Id*. at 9.

> Act of 1931, House Bill 358 as passed by the 42nd Legislature in 1931. This original Act and the amendment to it are now known as Article 5421c, Vernon's Annotated Civil Statutes. Thus, we find that all public lands in Texas in which the State has a mineral reservation, sold or to be sold, are subject to the terms of one or the other of these Acts.[11]

Finally, legal commentators in this field overwhelmingly suggest that the Relinquishment Act only applies to lands bought before the passage of the Land Sales Act. *See, e.g.*, Walker, *supra*, at 249; James D. Shields, *Leasing Lands Subject to the Texas Relinquishment Act*, 13 ST. MARY'S L.J. 869, 871 (1982); Kirk J. Billy, *Royalty on Take-or-Pay Payments and Related Consideration Accruing to Producers*, 27 HOUS. L. REV. 105, 123 (1990); Patrick H. Martin, *Royalty Issues on Lands Owned by State or Local Governments*, 33B ROCKY MTN. MIN. L. INST. 5 (1993); Emeka Duruigbo, *Oil, Turmoil, and a Texas Export for Energy Security*, 37 T. MARSHALL L. REV. 231, 245 (2012).

Lastly, turning to the case at hand, neither the land grant nor the oil and gas leases for the Mineral Reserved Land suggest that the Relinquishment Act should apply here. The public school land award by the State to Martin Kearney states, "I do hereby award to said applicant the survey of land described above with a reservation of one-eight of the sulphur and one-sixteenth of all other minerals as a free royalty to the State." (Doc. 22-1 at 1). This mirrors the language of the Land Sale Act exactly. If the land was subject to the Relinquishment Act, the owner of the soil would have no title or interest in the minerals. Instead, the minerals would be vested in the State, and Kearney would be left with the authority to lease 15/16th of the minerals, acting as the State's agent. *Scott*, 763 S.W.2d at 766 ("No title or interest in the oil and gas in and under the mineral reserved lands vests in the owner of the surface estate."); *State v. Durham*, 804 S.W.2d 312, 316 (Tex. App.—Austin 1991, *rev'd on other grounds*) ("Passed in 1919, the

11. *Id.* at 6.

Relinquishment Act applies to permanent school fund lands. The oil and gas underlying these lands belong to the State.").

Similarly, the oil and gas Lease is void of any of the requirements under the Relinquishment Act. The Texas Administrative Code sets out procedures for public school lands that "will be leased for the exploration and development of oil and gas." 31 TEX. ADMIN. CODE § 9.22 (1999). Again, the statute separates the requirements for Relinquishment Act lands and Land Sales Act lands. *See id*. For Relinquishment Act lands, while the surface owner—Martin Kearney in this case—is authorized to act as the State's leasing agent, "[t]he lease shall be on the GLO lease form in use on the date of execution." *Id*. § 9.22(2)(E)(ii). And "[a]ll of the negotiated terms must be included in the lease instrument. No lease term or provision may be included in a collateral contract or agreement." *Id*. § 9.22(2)(E)(iii). In contrast, for Land Sales Act leases, the State does not require a certain form or review of the lease terms. *Id*. § 9.22(4). While the copy of the Lease that the Parties provided is admittedly hard to read, there is no indication that GLO produced this form, and, as far as the Court can tell, it makes no reference to the State. (Doc. 22-1 at 2–3). Further, Defendants provide that the Lease only reserves a royalty to the Lessor, not the State. (Doc. 35 at 6); 31 TEX. ADMIN. CODE § 9.22(2)(F)(ix) (1999) ("A Relinquishment Act lease must provide the state with a royalty of at least 1/16th and a delay rental during the primary term of at least $.10 per acre per year to the state, or, on paid up leases, a paid up payment of at least $.10 per acre per year in the primary term."). While Plaintiff arguably—though, not clearly—alleges in its Complaint that the Lease reserved a 1/16th mineral interest to the State as a free royalty, no citation is provided, and the Court does not see that within the Lease. (Doc. 22 at 18). Finally, the Code states, "Any additions, modifications, deletions, or changes to the GLO lease form must be approved by the commissioner." 31 TEX. ADMIN. CODE § 9.22(3)(F)(i)

(1999). There was an amendment made to the lease on March 12, 1968, with no evidence that the changes had been approved. (Doc. 22-1 at 4). This all leads the Court to believe that the Williams' Lease of the Mineral Reserved Land was made pursuant to the Land Sales Act.

Ultimately, the Court agrees with Defendants that the Mineral Reserved Land is not subject to the requirements and duties under the Relinquishment Act. The *Wintermann* court made clear that the Land Sales Act did not repeal the Relinquishment Act. *Wintermann*, 102 S.W.2d at 172. Thus, the Relinquishment Act is still in effect today. So, taking Plaintiff's argument to its logical conclusion, the oil and gas under all public school land sold by the State at any point to this day would be subject to the Relinquishment Act of 1919. However, the Court is unable to find a case—and Plaintiff points to none—that describes a situation where an individual purchases land after the passage of the Land Sale Act but remains subject to the Relinquishment Act. *But see, e.g.*, *Caples*, 102 S.W.2d at 174–75 (finding public school land purchased on June 17, 1931—twenty days after the Land Sale Act passed—was subject to the Land Sale Act). For the reasons stated above, the Court finds the Relinquishment Act does not apply.

In Count One of the Complaint, Plaintiff asserts that Defendants breached an express obligation under the Relinquishment Act to offset their wells or to pay compensatory royalties. (Doc. 22 at 20–22). Because the Mineral Reserved Land is not subject to the Relinquishment Act, the Court **RECOMMENDS** Defendants' Motion to Dismiss as to Count One be **GRANTED** and Count One be **DISMISSED**. (Doc. 23).

2. Implied Covenant to Manage and Administer the Lease (Failing to Pay Compensatory Royalties)

In Count Two of its Complaint, Plaintiff alleges that Defendants breached "the implied covenant to manage and administer the lease as would a reasonably prudent oil and gas

Operator/Lessee with respect to paying compensatory royalty." (Doc. 22 at 23). Plaintiff further specifies that Defendants "breached their duties to act as a reasonably prudent operator in managing and administering the [Williams' Lease] by failing to pay compensatory royalty to Plaintiff in lieu of drilling required offset wells." *Id*. This language exactly mirrors the Plaintiff's description in Count One of the duties the Relinquishment Act imposes: "The Defendants' duty to manage and administer the Oil and Gas Lease as would a reasonably prudent oil and gas operator also obligated [Defendants] to seek authority from the Texas GLO Commissioner to pay compensatory royalty to Plaintiff in lieu of drilling the required offset wells." *Id*. at 22. While in its Response Plaintiff asserts that this claim may stand even if the Lease is not controlled by the Relinquishment Act, Plaintiff fails to explain how. (*See* Doc. 31 at 14–15). As Defendants argue, there is nothing within the Lease that would lead the Court to believe that the Parties contemplated imposing a duty on Defendants to drill offset wells or, alternatively, pay compensatory royalties to the Plaintiff. *See HECI Expl. Co. v. Neel*, 982 S.W.2d 881, 888 (Tex. 1998) ("A covenant will not be implied unless it appears from the express terms of the contract that 'it was so clearly within the contemplation of the parties that they deemed it unnecessary to express it,' and therefore they omitted to do so, or 'it must appear that it is necessary to infer such a covenant in order to effectuate the full purpose of the contract as a whole as gathered from the written instrument.'"). Therefore, as the Court explained above, the Relinquishment Act does not apply to impose such duties, and the Court declines to read these duties into the Lease. Thus, the Court **RECOMMENDS** Defendants' Motion to Dismiss as to Count Two be **GRANTED** and Count Two be **DISMISSED**. (Doc. 23).

B. Count Three—Implied Duty to Manage and Administer the Lease (Failing to Pool with Adjacent Lands)

In its Complaint, Plaintiff alleges that Defendants "breached their duties to act as a reasonably prudent operator in managing and administering the [Williams' Lease] by failing to pool it with adjacent lands in order to prevent it from becoming 'surrounded and stranded' by development on adjacent lands." (Doc. 22 at 24). To counter, Defendants argue that the express terms of the Lease address pooing, thus no implied duty to pool exists, and either way, Plaintiff did not sufficiently plead the allegations because there would need to be facts that the lack of pooling led to drainage. (Doc. 23 at 17). The Court agrees with Defendants.

The Texas Supreme Court has held that "[c]ertain covenants are implied in most oil and gas leases. The standard of care in measuring a lessee's performance of these implied covenants is that of a reasonably prudent operator carrying out the purposes of the lease under the same or similar circumstances." *Se. Pipe Line Co. v. Tichacek*, 997 S.W.2d 166, 170 (Tex. 1999). Broadly, three implied covenants have been recognized: "(1) develop, which means to drill an initial well and to reasonably develop the lease, (2) protect the leasehold, which includes protection from local and field-wide drainage, and (3) manage and administer the lease." *HECI Expl. Co.*, 982 S.W.2d at 889. Plaintiff attempts to argue that an implied duty to pool could be extracted from each of these three implied covenants: "(1) the implied covenant to protect against drainage can be used to imply a pooling clause into a lease; (2) the implied covenant to manage and administer the lease also gives rise to an operator's obligation to take actions, such as pooling, to prevent the 'stranding' of a leased property; and (3) the implied covenant of diligent exploration and development may give rise to an operator's obligation to pool and prevent the 'stranding' of leased land." (Doc. 31 at 14).[12] While the Court agrees that a common measure to protect from

12. The Court notes that generally, "the duty to pool derives from the duty to protect the leasehold from drainage rather than from the duty to manage and administer the lease." *Green v. Gemini Expl. Co.*, No. 03-02-00334-CV, 2003 WL 1986859, at *7 (Tex. App.—Austin 2003, *pet. denied*) (citing *Se. Pipe Line Co.*, 997 S.W.2d at 170). In its Complaint, Plaintiff alleges that Defendants breached the duty to manage and administer by failing to pool, but then

drainage is "for the lessee to exercise its *contractual* pooling authority," the Texas Supreme Court has stated, "A lessee has no power to pool without the lessor's express authorization, which is usually contained in the lease's pooling clause. For pooling to be valid, it must be done in accordance with the method and purposes specified in the lease." *Se. Pipe Line Co.*, 997 S.W.2d at 170 (emphasis added); *Key Operating & Equip., Inc. v. Hegar*, 435 S.W.3d 794, 798 (Tex. 2014) ("Mineral lessees of multiple tracts may pool some or all of the tracts by combining them into a single unit, *provided pooling is authorized by the leases*." (emphasis added)); *Browning Oil Co. v. Luecke*, 38 S.W.3d 625, 634 (Tex. App.—Austin 2000, *pet. denied*) ("A lessee's authority to pool is derived solely from the terms of the lease; a lessee has no power to pool absent express authority.").

As Plaintiff explicitly states, "[T]here is absolutely no provision in the [Williams' Lease] covering oil well pooling." (Doc. 31 at 13). Instead, the pooling clause specifically states:

> 12. Lessee, at its option is hereby given the right and power to pool or combine the acreage covered by this lease or any portion thereof, *as to gas and associated liquid hydrocarbons only*, with other land, lease or leases in the immediate vicinity thereof . . . .

Id. Plaintiff argues that because pooling oil wells is not mentioned in the Lease, it is necessary for the Court to imply one. *Id*. However, "when parties reduce their agreements to writing, the written instrument is presumed to embody their entire contract, and the court should not read into the instrument additional provisions unless this be necessary in order to effectuate the intention of the parties as disclosed by the contract as a whole." *Danciger Oil & Refin. Co. v. Powell*, 154 S.W.2d 632, 635 (1941). Because the Lease explicitly leaves out the ability to pool oil wells, the Court will not find there is an implied covenant to pool.

---

raised in its Response for the first time that failing to pool could be a breach of all three implied covenants. (Docs. 22 at 24; 31 at 14). Because this does not affect the outcome, the Court declines to weigh in on this issue.

Even if the Court did imply a duty to pool, Plaintiff did not sufficiently plead this claim. "In order to recover for breach of the duty to protect from drainage, a lessor must present proof (1) of substantial drainage of the lessor's land, and (2) that a reasonably prudent operator would have acted to prevent the drainage." *Se. Pipe Line Co.*, 997 S.W.2d at 170. Further, a lessee is not required to take steps to prevent drainage, such as by pooling, "unless there is a reasonable expectation of profit." *HECI Expl. Co.*, 982 S.W.2d at 889. Based on Plaintiff's Response, it appears as though the Mineral Reserved Land had not suffered any drainage: "Under these circumstances, it is necessary for the court to imply an oil pooling clause into the Lease so that the Mineral Reserved Land *does not suffer drainage or become stranded* and impossible to develop." (Doc. 31 at 13) (emphasis added). Further, Plaintiff does not provide any facts surrounding the expenses of pooling the oil wells, nor the profit that would be foreseen from such pooling. Therefore, Plaintiff does not properly allege a breach of the duty to protect from drainage.

Thus, the Court **RECOMMENDS** Defendants' Motion to Dismiss as to Count Three be **GRANTED** and Count Three be **DISMISSED**. (Doc. 23).

C. Count Four—Breach of the Surface Use Agreement

In Count Four of its Complaint, Plaintiff alleges that Defendants breached Section 8 of the Parties' SUA by failing to purchase all its water requirements to operate the six wells they drilled on the Mineral Reserved Land, as well as to fulfill its water purchase requirements with respect to its drilling of other wells in the area. (Doc. 22 at 25).[13] Defendants counter, however,

13. In its Complaint, Plaintiff also alleges that Defendants breached the SUA by failing to dig, build, and operate a frac pit on the Mineral Reserved Land. (Doc. 22 at 25–26). However, in its Response, Plaintiff "elected to abandon its claims for relief under the Surface Use Agreement relative to the frac/water pit and metering." (Doc. 31 at 16 n.56).

that under the SUA, Defendants have no obligation to purchase water to support operations off the Lease. (Doc. 23 at 18–19). Section 8 of the SUA provides:

> 8. Purchase of Water. *Lessee agrees to purchase from Lessor all of the water needed for Lessee's drilling and completion of any oil or gas well drilled by Lessee to produce from any part of said the Leased Premises and/or other lands* if and to the extent that Lessor has water of sufficient quality and in sufficient quantity for such purpose from the well drilled by Lessee in the Leased Premises as contemplated herein or from any other well or wells of Lessor in said the Leased Premises. Lessee agrees to pay Lessor the attached hereto Exhibit D for oil and gas facilities and operations on lands for a barrel of water so used. Lessee shall be responsible for the measurement of such water using suitable and accurate meters. If and only if Lessor does not have suitable water available in sufficient quantities to supply Lessee's requirements in drilling and completing wells in the Leased Premises and/or other lands, Lessee will be relieved of its obligation to purchase water from Lessor to the extent of such deficiency. *It is understood that Lessee is not required to purchase water from such well for the drilling and completion of wells drilled from the Drillsite Location to other lands.*

(Doc. 22-1 at 13) (emphasis added).

In dispute is the first and last sentence of Section 8. On one hand, Plaintiff asserts that the correct interpretation of this provision is using the first sentence that says Defendants are required to purchase its water needs for drilling on both Plaintiff's land and "other lands." (Doc. 31 at 16). Plaintiff explains the intent of the Parties can be shown by the fact that Defendants bought water from Plaintiff for a well that was "commenced on Plaintiff's Mineral Reserved Land but then was turned horizontally and drilled for over a mile onto [neighboring land]; thus the water provided by Plaintiff was used by Defendants for drilling BOTH on Plaintiff's land AND on 'other lands.'" *Id*. To read this provision in that light, Plaintiff provides two alternative theories. First, Section 8 is not ambiguous. *Id*. at 17–18. Plaintiff argues the Court should consider the last sentence a Scrivener's error because it is "wholly contradictory" to the rest of

the provision. *Id*. Alternatively, Plaintiff asks the Court to find that there is an irreconcilable conflict in the provision so that the contract is ambiguous and the factual issue of intent must be decided at trial. *Id*. at 18–20.

On the other hand, Defendants argue that the Court cannot disregard the last sentence of the provision because the rules of contract construction provide that courts must examine and consider the entire writing in an effort to harmonize and give effect to all the provisions, so none are rendered meaningless. (Doc. 35 at 9). Further, Defendants assert that the contract cannot be ambiguous because there are not two reasonable interpretations of Section 8: "Taken to its logical conclusion, Williams' argument would require Diamondback to purchase water for use in drilling wells not just on neighboring tracts, but on *any* 'other lands' regardless of their location." *Id*. at 10.

At the motion to dismiss stage, a district court can determine whether contractual ambiguity exists. *Div. One Foods, Inc. v. Pizza Inn, Inc.*, No. 20-CV-02065, 2021 WL 3172176, at *1 (N.D. Tex. July 27, 2021). In diversity cases involving contract claims, federal courts will look to the substantive law of the forum state. *Kent Distrib., Inc. v. Travelers Cas. & Surety Co. of Am.*, No. 22-CV-00221, 2023 WL 6536245, at *2 (W.D. Tex. Aug. 3, 2023) (citing *Tex. Indus., Inc. v. Factory Mut. Ins.*, 486 F.3d 844, 846 (5th Cir. 2007)). "Whether a contract is ambiguous is itself a question of law." *Am. Mfrs. Mut. Ins. v. Schaefer*, 124 S.W.3d 154, 157 (Tex. 2003). Under Texas law, "[w]hen interpreting a written contract, the prime directive is to ascertain the parties' intent as expressed in the instrument." *URI, Inc. v. Kleberg County*, 543 S.W.3d 755, 757 (Tex. 2018). Courts "presume parties intend what the words of their contract say and interpret contract language according to its plain, ordinary, and generally accepted meaning." *Id*. at 764 (internal quotations omitted). "If a written contract is so worded that it can be given a certain or

definite legal meaning or interpretation, it is not ambiguous." *Sun Oil Co. (Del.) v. Madeley*, 626 S.W.2d 726, 732 (Tex. 1981). "If the contract is subject to two or more reasonable interpretations after applying the pertinent rules of construction, however, the contract is ambiguous, creating a fact issue on the parties' intent." *ConocoPhillips Co. v. Koopmann*, 547 S.W.3d 858, 874 (Tex. 2018). If a contract is determined to be ambiguous, the Court can then consider the parties' interpretations of the contract and "admit extraneous evidence to determine the true meaning of the instrument." *Nat'l Union Fire Ins. Co. of Pittsburgh v. CBI Indus., Inc.*, 907 S.W.2d 517, 520 (Tex. 1995).

Here, the Court finds Section 8 of the SUA ambiguous. The Court is unable to conclude what the certain or definite meaning or interpretation of this provision is. The ambiguity stems from several points within the provision. First, the Court finds that the term "other lands" could reasonably mean neighboring tracts that were drilled to horizontally from the Mineral Reserved Land or it could refer to any other piece of real property. Second, the use of the phrase "and/or" changes the meaning of the sentence, but both interpretations are not necessarily reasonable, depending on the meaning of "other lands." *See Stellar Restoration Servs., LLC v. James Christopher Courtney*, 533 F. Supp. 3d 394, 405 (E.D. Tex. 2021) ("Indeed, courts have long noted that the term 'and/or' can be ambiguous." (collecting cases)). Third, there is an apparent contradiction between the first sentence and the last sentence of the provision. The Court finds that extraneous evidence of the Parties' intent is needed to understand the ambiguities present here and determining intent is a question of fact that must be addressed at a later stage of litigation. Further, Plaintiff alleges in its Complaint that Defendants "only purchased approximately 3,700,000 barrels of water from Plaintiff, when they should have purchased at least an additional 20,000,000 barrels of water from Plaintiff." Thus, if Plaintiff's interpretation

of the contract is correct that Defendants were required to purchase all their water from Plaintiff, the Complaint has sufficiently alleged facts to state a breach of contract claim to survive the motion to dismiss stage.

Therefore, the Court **RECOMMENDS** Defendants' Motion to Dismiss as to Count Four be **DENIED**. (Doc. 23).

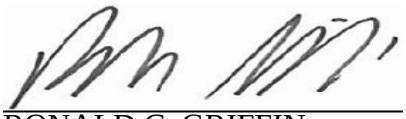
D. Counts Five, Six, and Seven—Attorney's Fees, Discovery Rule, and Conditions Precedent Fulfilled

In its Complaint, Plaintiff alleges three counts that are derivative of Plaintiff's substantive Counts One through Four. (Doc. 22 at 26–27). Because the Court finds that Plaintiff's Count Four sufficiently states a claim for relief under Rule 12(b)(6), it follows that derivative Counts Five, Six, and Seven survive as well. Therefore, the Court **RECOMMENDS** Defendants' Motion to Dismiss as to Counts Five, Six, and Seven be **DENIED**. (Doc. 23).

IV. CONCLUSION

For the foregoing reasons, the Court **RECOMMENDS** Defendants' Motion to Dismiss be **GRANTED IN PART** and **DENIED IN PART** and that Plaintiff's Counts One, Two, and Three be **DISMISSED WITH PREJUDICE**. (Doc. 23).

SIGNED this 27th day of January, 2025.



RONALD C. GRIFFIN
UNITED STATES MAGISTRATE JUDGE

INSTRUCTIONS FOR SERVICE AND NOTICE OF RIGHT TO APPEAL/OBJECT

In the event that a party ***has not been served*** by the Clerk with this Report and Recommendation electronically, pursuant to the CM/ECF procedures of this District, the Clerk is **ORDERED** to mail such party a copy of this Report and Recommendation by certified mail. Pursuant to 28 U.S.C. § 636(b)(1), any party who desires to object to this report must serve and file written objections within fourteen (14) days after being served with a copy. A party filing objections must specifically identify those findings, conclusions, or recommendations to which objections are being made; the District Judge need not consider frivolous, conclusive, or general objections. Such party shall file the objections with the Clerk of the Court and serve the objections on all other parties. A party's failure to file such objections to the proposed findings, conclusions, and recommendations contained in this report shall bar the party from a *de novo* determination by the District Judge. Additionally, a party's failure to file written objections to the proposed findings, conclusions, and recommendations contained in this report within fourteen (14) days after being served with a copy shall bar that party, except upon grounds of plain error, from attacking on appeal the unobjected-to proposed factual findings and legal conclusions accepted by the District Judge. *Douglass v. United Servs. Auto. Ass'n*, 79 F.3d 1415, 1428–29 (5th Cir. 1996).