

***Coastal Oil & Gas Corp. v. Garza Energy Trust:*
Some New Paradigms for the Rule of Capture
and Implied Covenant Jurisprudence¹**

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¹ *Coastal Oil & Gas Corp. v. Garza Energy Trust*, 268 S.W.3d 1 (Tex. 2008), *rev’g*, *Mission Resources, Inc. v. Garza Energy Trust*, 166 S.W.3d 301 (Tex. App.-Corpus Christi 2005)[hereinafter *Coastal Oil*].

§ 11.01. Introduction.

Oil and gas law and the rule of capture go hand in hand.² The rule of capture had its origin in the Appalachian Basin. The doctrine has been modified by judicial rulings and by state oil and gas conservation statutes.³ As the issues surrounding the rule have moved from the reasonably simple issues involving ownership of produced hydrocarbons to the more complex issues relating to subterranean storage of natural gas and the injection of fluids and/or gasses into producing formations, the rule has been invoked to respond to those technological innovations. The vast increase in the use of hydraulic fracturing techniques to recover hydrocarbons from shale and tight sands formations has triggered judicial inconsistency in the application of the rule.⁴ In *Coastal Oil & Gas Corp. v. Garza Energy Trust*,⁵ the Texas Supreme Court attempted to resolve some of those inconsistencies and apply the rule of capture so as to insulate, in most cases, an oil and gas operator from liability in the circumstance where that operator engaged in a fracing operation whereby the injected fluids crossed property lines.

Oil and gas law and the doctrine of implied covenants also go hand in hand. The origin of the implied doctrine dates back to the 1880s and the landmark decision formally pronouncing the “arrival” of the doctrine was issued in 1905 by a federal court of appeals.⁶ Notwithstanding the century-old existence of the doctrine, however, there are still plenty of unanswered questions regarding its application to specific circumstances. One such unanswered question is what remedy is available to the lessor when the

² See Bruce M. Kramer & Owen L. Anderson, “The Rule of Capture – An Oil and Gas Perspective,” 35 *Envtl. L.* 899 (2005)[hereinafter The Rule of Capture]. I want to thank my good friend Owen Anderson for not only co-authoring the Rule of Capture article with me but also in writing an article on the *Coastal Oil* case that was presented at the Annual Institute of Oil and Gas Law and Taxation in February 2009. Owen L. Anderson, “Subsurface Trespass After Coastal v. Garza,” 60 *Inst. on Oil & Gas L. & Tax’n* __ (2009) [hereinafter Anderson, Subsurface Trespass].

³ See Bruce M. Kramer and Patrick H. Martin, *The Law of Pooling and Unitization* ch. 2-3 (3d ed. 2008)[hereinafter Kramer & Martin].

⁴ “The Rule of Capture,” 35 *Envtl. L.* at 933-35.

⁵ *Coastal Oil*, 268 S.W.3d 1 (Tex. 2008).

⁶ *Stoddard v. Emery*, 18 A. 339 (Pa. 1889); *Brewster v. Lanyon Zinc Co.*, 140 F. 801 (8th Cir. 1905). See generally, Patrick H. Martin and Bruce M. Kramer, *Williams & Meyers Oil and Gas Law* § 802 (2008)[hereinafter Williams & Meyers].

lessee breaches the implied covenant of reasonable development. While the traditional panoply of implied covenantal remedies usually apply, including cancellation, conditional cancellation and damages, there has been some dispute on two sub-issues, namely should damages be the sole remedy and if so, how do you measure them?⁷ The *Coastal* opinion addressed the second of these sub-issues and did so in a way that did not clearly set out how one should calculate those damages.

§ 11.02. Some Basic Definitions.

[1] — Hydraulic Fracturing or Fracing.

Hydraulic fracturing or fracing describes a mechanical method of increasing the permeability of the reservoir rock which should lead to increased production of the trapped hydrocarbons.⁸ Unlike secondary and enhanced recovery operations which through various mechanical techniques seek to increase production after the primary recovery period is over, fracing facilitates and in many cases is required to have primary production.⁹ Hydraulic fracturing has been used since the 1940s but it was only with its use in coalbed methane, tight sands and shale formations in the 1990s that its use has become more widespread.¹⁰ Fluids, typically water, are injected into the formation under high pressure.¹¹ After the initial injection has hopefully fractured the reservoir rock, additional fluids containing proppants

⁷ 5 Williams & Meyers, at § 834.

⁸ 8 Williams & Meyers, *supra* note 6, 479; Anderson, “Subsurface Trespass” at § 11.03.

⁹ Stephen A. Holditch *et al.*, Topic Paper # 29, *Unconventional Gas, Working Document of the NPC Global Oil and Gas Study* (July 18, 2007) http://www.npc.org/Study_Topic_Papers/29-TTG-Unconventional-Gas.pdf.

¹⁰ Anderson, “Subsurface Trespass” at n. 48. For a discussion of the use of fracing in coalbed methane production *see* Markus G. Puder, “Did the Eleventh Circuit Crack ‘Frac’? – Hydraulic Fracturing After the Court’s Landmark *LEAF* Decision,” 18 *Va. Envtl. L.J.* 507 (1999).

¹¹ In the early days of fracing, gasoline gelled with napalm was used, followed by gelled oil and then by gelled water. For a while diesel fuels were used but because of the problems relating to the pollution of underground water supplies the principal fluid used today is water. Anderson, “Surface Trespass” at n. 48. There were also a few attempts by the Atomic Energy Commission in the 1950s to detonate underground nuclear devices with the hope of freeing the trapped hydrocarbons. Those efforts were unsuccessful.