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after the meal has concluded. Inquiring when your dining partner's next appointment is or what the rest of their day has on tap is a courteous way to subtly indicate that it's time for all of you to head back to the office.

These tips for a business meal only scratch the surface for how to comport oneself while dining, and ultimately common sense will serve anyone well in making sure that – rather than falling prey to an avoidable pitfall – they always make a positive impression.

The article below is being published in a two-part series. Part 1 is below.

Ready! Fire! Aim! Two Drafting Traps to Avoid in Papering a "Rush" Deal

By Brandon Durret, Dykema Cox Smith

Agreements for the acquisition of oil and gas properties—indeed, acquisition agreements in any context—often require highly complex legal drafting within a short time frame. Parties are typically eager to get under contract and close as quickly as possible to avoid the other party losing interest or backing out. Sellers, in particular, want to limit the amount of time their assets are off the market and the amount of time their buyers may inspect the assets for defects. These time constraints make acquisition agreements particularly prone to errors and drafting oversights.

This article will discuss the proper use and risky misuses of two clauses common to oil and gas acquisition agreements that are often perceived as drafting shortcuts in "rush" deals. The first topic is the effect of a "subject to the Purchase and Sale Agreement" clause in an assignment of leases, and the degree to which it controls over the actual assignment terms and prevents merger of the Purchase and Sale Agreement into the assignment. The second topic is when, how, and to what extent the phrase "notwithstanding anything herein to the contrary" will cause the language it precedes to override other contract terms.

I. "SUBJECT TO THE PSA" CLAUSE VS. MERGER BY DEED

The urgency involved in a sale of oil and gas leases does not end when the parties sign a formal Purchase and Sale Agreement ("PSA"). In the author's experience, the parties' eagerness to close is usually even more intense. Typically, the weeks between contracting and closing is a whirlwind of time-intensive due diligence, including data room analysis, review of financial records and corporate filings, examination of title documents and material contracts, regulatory and environmental inspections, purchase price adjustments and knockdowns, and minor renegotiations.

With all that activity, both before and after getting under contract, the parties look for time-saving efficiencies wherever they can find them. As a result, the formal assignment of leases often gets less drafting attention than it deserves. Rather than carefully drafting the assignment to closely track the relevant PSA terms, it is tempting to simply pull an unrelated assignment form from your files, fill in the blanks and exhibits, and add a clause making the conveyance "subject to" the terms of the PSA. The thinking behind this approach is that the PSA terms will control in the event they conflict with the assignment terms, so an error or omission in the assignment is not critical.

This thinking is wrong and hazardous due to the legal doctrine of "merger by deed," or the merger doctrine. It holds that when the seller executes, and the buyer accepts, a conveyance pursuant to a contract for sale of real property, the contract "merges" into the conveyance. As a result, the contract terms regarding the property conveyed do not survive closing, even if they contradict the conveyance terms. Alvarado v. Bolton, 749 S.W.2d 47, 48 (Tex. 1988). Put another way:

> [I]n the absence of fraud, accident, or mistake in the execution, the deed, an absolute conveyance on its face, must be considered the *final expression* and the *sole repository* of the terms upon which [the parties] have agreed with respect to the *property conveyed*, the consideration, and the method of payment.

Carter v. Barclay, 476 S.W.2d 909, 914-15 (Tex. Civ. App.—Amarillo 1972, no writ) (emphasis added). But can the merger doctrine be expressly overridden? Not easily, it seems. The merger doctrine is so durable, in fact, that it cannot be defeated by making the conveyance "subject to the terms" of the contract for sale, as the following cases demonstrate in the oil and gas context.

A good illustration of how merger by deed and a "subject to" clause interact is *Devon Energy Prod. Co., L.P. v. KCS Res., LLC*, decided in 2014 by the Houston 14th District Court of Appeals. 450 S.W.3d 203 (Tex. App.—Houston [14th Dist.] 2014, pet. denied). Devon had entered a PSA to sell KCS a large package of mineral tracts, which was duly closed by delivery of deeds. Years later, a third party operator proposed new wells on some of the mineral tracts and a question arose as to whether Devon had conveyed all of its right, title, and interest in the entire tracts, per the deed language, or merely in certain existing wells thereon listed in the PSA. Devon filed a declaratory judgment action to determine the parties' respective rights.

KCS argued that because the rights of the parties rest solely in the deeds, per the merger doctrine, a construction of the PSA by the court would not resolve any justiciable

claim and therefore the court lacked jurisdiction to do so. Devon countered that because the deeds were "expressly made subject to" the PSA, no merger occurred and the PSA terms still control what interests were conveyed. The court disagreed:

> The Supreme Court of Texas has long recognized that the conveyance provisions in a contract for the sale of real property merge into the deed executed in accordance with the contract. The merger doctrine requires courts to look to the deed alone in evaluating the parties' respective rights even if the terms of the deed vary from the contract.

Id. at 211. The court further stated, "we reject Devon's argument that the [deed's] language that it is 'subject to' the PSA indicates the parties' intent that the PSA would not be merged into, superseded by, or mooted by the [deed]." *Id.* at 214. As supporting evidence, the court cited revisions made to legal descriptions in the deed exhibits due to title errors found during KCS's due diligence investigations, though the PSA exhibits were not correspondingly revised. "[I]f the conveyance terms of the [deed] were 'subject to' the PSA," the court stated, "then the revisions the parties made to deeds during the due diligence period would be irrelevant" and would "undermine the purpose of the merger doctrine." *Id.*

The court also rejected Devon's argument that because the PSA contains surviving collateral terms, meaning contract obligations not fully performed by execution and delivery of the deeds, such as indemnification provisions and covenants to cooperate in effectuating the intent of the PSA. The court agreed that such terms are not released or impaired by the merger doctrine, observing that the PSA merges into the deed only as to "'property conveyed, the consideration, and the method of payment.'" Id. citing Carter, 476 S.W.2d at 914-15. But Devon's claim failed because the parties disputed the scope of the conveyance itself, not surviving collateral terms of the PSA.

In March of 2017, the Corpus Christi Court of Appeals directly addressed a similar merger question involving an overriding royalty conveyance in *Burlington Res. Oil & Gas Co. LP v. Tex. Crude Energy, LLC*. 516 S.W.3d 638 (Tex. App.—Corpus Christi 2017, pet. filed). Burlington and Texas Crude had entered a Prospect Development Agreement ("PDA") with an "Area of Mutual Interest" clause providing, among other things, that Texas Crude will reserve an overriding royalty in any oil and gas lease it assigns to Burlington, and likewise Burlington will assign an overriding royalty to Texas Crude in any oil and gas lease it acquires.

All of the assignments creating Texas Crude's overriding royalties stated that the override will be paid based on the "amount realized" from the sale of production. As operator and owner of the working interests that the overrides were carved out of, Burlington had been proportionately deducting post-production costs from Texas Crude's overriding royalty payments. However, prompted by the landmark holding in 2016 by the Supreme Court of Texas in *Chesapeake Exploration, L.L.C. v. Hyder*, 483 S.W.3d 870 (Tex. 2016), Texas Crude sued Burlington to recover those post-production costs, arguing that the "amount realized" language in the assignments prohibited such deductions.

Burlington countered that the PDA does not authorize or contemplate overrides that are free of post-production costs, and that, because the override reservations and conveyances were expressly made "subject to the terms and conditions of the PDA," the court should construe them as "typical" overrides that bear such costs. Citing Devon, the court disagreed based on application of the doctrine of merger by deed:

> [E]ven assuming that the PDA … contemplated only the reservation of "typical" [overrides], which would bear post-production costs, the assignments themselves are the only instruments we must look to in determining whether such "typical" [overrides] were, in fact, conveyed. We conclude that they were not.

Like *Devon*, the *Texas Crude* case demonstrates that "subject to" language in the closing assignment pursuant to a PSA has little or no effect in preventing application of the merger doctrine. Disappointingly, the court does not explain how or why. But this case prompts the author to wonder, "What is the actual function or purpose of a 'subject to the PSA' clause in a closing conveyance?" It is present in most, if not virtually all, assignments closing large PSAs. But if it does not prevent merger, and the surviving collateral PSA terms are enforceable regardless, does it have any legal effect at all? The only effect the author can think of is to supply record notice to future purchasers that they may be subject to unperformed surviving collateral obligations under the PSA.

As *Texas Crude* demonstrates, the merger doctrine can override "subject to" language not just in PSAs, but in any kind of oil and gas agreement that contemplates formal transfer of a real property interest. This may include farmouts, lease offers, participation agreements, joint ventures, operating agreements, and letter agreements.

Keep in mind that the merger doctrine only applies to assignment terms "with respect to the property conveyed, the consideration, and the method of payment [of consideration]." But *Texas Crude* illustrates the long reach of the merger doctrine in abrogating the terms of the underlying agreement.

Specifically, merger extends even to real covenants benefiting the interest conveyed—calculation of royalty, in this case—not just to terms which directly control the size and shape of the property conveyed, such as legal description or reservations.

Texas law does not give us a comprehensive list of the types of assignment terms that may be subject to merger, but they appear to include the following:

- Legal descriptions (*Carter*, 476 S.W.2d at 914-15)
- Reservations from the grant (depths, royalty, security interest, etc.) (*Barker v. Coastal Builders, Inc.*, 271 S.W.2d 798 (Tex. 1954); *Tex. Indep. Exploration, Ltd. v. Peoples Energy Production-Texas L.P.*, 2009 Tex. App. LEXIS 6941 (Tex. App.—San Antonio 2009, no pet.))
- Exceptions to the grant (tracts, prior reservations, easements, etc.) (*Turberville v. Upper Valley Farms, Inc.*, 616 S.W.2d 676 (Tex. App.—Corpus Christi 1981, no writ))
- Warranties and disclaimers thereof (general vs. special vs. none, against encumbrances, etc.) (*Alvarado v. Bolton*, 749 S.W.2d 47 (Tex. 1988))
- Conveyance language (quitclaim vs. grant of land, grantor's capacity, etc.) (*Commercial Bank, Uninc, v. Satterwhite*, 413 S.W.2d 905 (Tex. 1967))
- Royalty calculation (sales price vs. market value, etc.) (*Tex. Crude, LLC*, 516 S.W.3d at 642)
- Performance covenants and conditions (payment or drilling obligations, etc.) (*Sunderman v. Roberts*, 213 S.W.2d 705 (Tex. App.—San Antonio 1948, no writ))
- Restrictions on use (*Smith v. Harrison County*, 824 S.W.2d 788 (Tex. App.—Texarcana 1992, no writ))
- Reservations of vendor's liens (*Scull v. Davis*, 434 S.W.2d 391 (Tex. Civ. App.—El Paso 1968, writ ref'd n.r.e.))

Although the author has not identified Texas cases directly on point, merger would also arguably eliminate, if left out of the assignment, terms like special limitations on the duration of the grant (as in term assignments, oil and gas leases, etc.), proportionate reductions of the grant (for an overriding royalty, for example), and consents to assign. However, Texas cases also illustrate the type of collateral contract terms which would survive closing and not be merged into the assignment, like indemnity obligations (*Devon Energy*, 450 S.W.3d at 209), arbitration provisions (*Stanford Dev. Corp. v. Stanford Condominium Owners Ass'n*, 285 S.W.3d 45 (Tex. App.—Houston [1st Dist.] 2009, no pet.)), obligations to furnish materials (title policy, files, data, etc.) (*Pleasant Grove Builders, Inc. v. Phillips*, 355 S.W.2d 818 (Tex. Civ. App.—Dallas 1962, writ ref'd n.r.e.)), and releases and assumptions of liability (*Bates v. Lefforge*, 63 S.W.2d 360 (Tex. Com. App. 1933, holding approved); *Baker v. Baker*, 207 S.W.2d 244 (Tex. Civ. App.—San Antonio 1947, no writ)).

Editor's Note: Part II. Perils of the "Notwithstanding" Clause will appear in the next issue of *The Energy Dispatch*.

Recent Cases from Federal Courts of Appeal Indicate Expansion of Both Jurisdiction and Liability Under the Federal Clean Water Act

By Claire Juneau, Kean Miller LLP

Recent cases from the Federal Fourth Circuit Court of Appeal and the Federal Ninth Circuit Court of Appeal could mean a significant expansion of both jurisdiction and liability under the Federal Clean Water Act ("CWA"). These cases follow a recent trend from a number of district court cases examining similar issues.

Decided this past February, the Ninth Circuit in *Hawai'i Wildlife Fund v. County of Maui*, 886 F.2d 737 (9th Cir. 2018) held that Maui County's unpermitted point source discharges and injections of treated wastewater into disposal wells violated the CWA despite the fact that the injected wastewater reached a navigable water body (the Pacific Ocean) only via groundwater.

In *Hawai'i Wildlife Fund*, a number of environmental groups sued Maui County under the citizens' suit provision of the CWA. The claim arose from the County's operation of four injection wells at the Lahaina Wastewater Reclamation Facility. It was undisputed that the County was injecting approximately 3 to 5 million gallons of treated wastewater per day into the groundwater via its wells. And it was undisputed that some of this wastewater reached the Pacific Ocean.

On summary judgement, the district court found that the county violated the CWA because it was discharging pollutants from its wells into the ocean without a proper NPDES permit. In affirming the district court, the Ninth Circuit found CWA liability because: "(1) the county discharged pollutants from a point source, (2) the pollutants [were] fairly traceable from the point source to a navigable water such that the discharge [was] the functional equivalent of a discharge into the navigable water, and (3) the pollutant levels reaching navigable water [were] more than *de minimis*." The Court, notably, rejected the Environmental Protection Agency's proposed standard for when liability attaches for indirect discharges – a direct hydrological connection between the point source and the navigable water – and, instead, required only a "fairly traceable connection" for a CWA violation to be found.

In reaching this holding, the court rejected Maui County's