IN THE UNITED STATES COURT OF APPEALS

FOR THE FIFTH CIRCUIT

NO. 92-2779

JOHN C. LUCK, JR., ET AL.,

Plaintiffs,

LUCK PETROLEUM CORPORATION,

Plaintiff-Appellant,
Cross Appellee,

versus

HOWARD A. SMITH, ET AL.,

Defendants-Appellees,

O & G CARRIERS, INC.,

Defendants, Counter Claim
Plaintiff-Appellee,
Cross-Appellant-Appellant,

versus

HOWARD A. SMITH, ET AL.,

Counter Defendants-Appellees.

Appeals from the United States District Court
for the Southern District of Texas
(CA-H-89-1403)

(July 15, 1994)

Before KING, BARKSDALE and PARKER,[1] Circuit Judges.

Per curiam[2]:

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[1] Judge Parker was Chief Judge of the Eastern District of Texas, sitting by designation at the time of oral argument.

[2] Local rule 47.5 provides: "The publication of opinions that have no precedential value and merely decide particular cases on the basis of well-settled principles of law imposes

In April of 1986, Luck Petroleum Corporation[3] purchased oil, gas and mineral leasehold interests, producing oil wells and oil field equipment located in Galveston County, Texas. Luck then transferred the interests that it had purchased to O&G Carriers, Inc. ("O&G") and Smith Energy 1986-A Partnership,[4] reserving to itself a contingent reversionary interest and option, which Luck could elect to exercise if O&G and Smith received revenues from oil and gas production in excess of the combined costs of acquisition and operation. Smith received approximately 68% of the working interest and O&G received the remaining share. The parties entered into two additional agreements, dated April 8, 1986 and May 12, 1986, which contemplated that Luck would be the operator of the property, while Smith and O&G were working interest owners. In April, 1989 Luck brought the suit underlying this appeal against Smith and O&G for breach of all three agreements, contending, among other things, that the Defendants had failed to pay operating expenses. Federal jurisdiction was based on diversity of citizenship between Luck, a citizen of Texas, O&G, a citizen of New

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needless expense on the public and burdens on the legal profession." Pursuant to that Rule, the court has determined that this opinion should not be published.

[3] John C. Luck, Jr. and Luck Petroleum Corporation were plaintiffs in the trial court. Only Luck Petroleum Corporation perfected an appeal from the holding below. References to "Luck" in this opinion refer to the corporate Appellant.

[4] Smith 1986-A Partnership is the party to the contracts in question. Howard Smith and Smith Energy Company, Inc., the general partners, were brought into the suit to trigger individual liability if the partnership was found liable. These three defendants will be referred to collectively as "Smith."

York and Delaware, and Smith, a citizen of New York. O&G counterclaimed against Luck in October, 1989 contending that Luck was negligent, and that the expenses of operation were falsified and padded. At approximately the same time, Luck settled and dismissed all claims against Smith. Smith then succeeded Luck as operator of the property. Seventeen months later, Smith was brought back into the suit when O&G amended its counterclaim against Luck to include claims that Smith participated in, sanctioned or directed Luck's wrongful conduct.

Prior to settlement between Luck and Smith, O&G commenced a lawsuit in New York against Smith and Luck. After the Luck-Smith settlement, Smith filed a third suit against O&G in a Galveston state court, seeking to recover from O&G the operating expenses previously sought by Luck as well as other relief. Luck was not a party to the Galveston suit, which was tried to a jury in 1992. The jury found that O&G failed to comply with the Operating Agreement by not paying its share of the operating expenses, but that failure was excused by Smith's failure to comply with material obligations under the same agreement. Finally, the jury found that Smith did not engage in any fraudulent or unconscionable action that was a producing cause of damage to O&G. The court below held that the jury findings in the Galveston case resolved all claims between Smith and O&G in the instant suit.

Luck moved for summary judgment dismissing O&G's counterclaim, which the trial court granted. Luck also moved for summary judgment against O&G establishing liability for damages Luck

allegedly sustained due to O&G's breach of express and implied covenants, which was denied. The court held that Luck's claims against O&G for operating expenses were resolved by the jury findings in the Galveston case and by Luck's settlement with Smith. Finally the Court dismissed Luck's claim that O&G breached an implied covenant to develop for failure to state a cause of action. Luck's claim under the express covenant was dismissed by the final judgment without explanation.

Luck now appeals, asking this Court to reverse the dismissal of those claims against O&G which were based on express and implied covenants and render judgment finding O&G liable to Luck under those covenants. O&G has also appealed the take nothing judgment on its claims against Smith and Luck, asking that its counterclaims be remanded to the district court for trial on the merits.

STANDARD OF REVIEW

The district court invited the parties to file motions for summary judgment, putting all the parties on notice to come forward with their best evidence. There is some confusion both in the lower court opinion and in the parties' contentions on appeal concerning whether the disposition of Luck's claims against O&G could most accurately be characterized as a dismissal under Federal Rule of Civil Procedure 12(b)(6) or a grant of summary judgment, and whether the case was in a procedural posture that gave the Court authority to dispose of the claim. "'[D]istrict courts are widely acknowledged to possess the power to enter summary judgments sua sponte, so long as the losing party was on notice that she had

to come forward with all of her evidence.'" *Arkwright-Boston Mfrs. Mut. Ins. Co. v. Aries Marine Corp.*, 932 F.2d 442, 445 (5th Cir. 1991) (quoting *Celotex Corp. v. Catrett*, 477 U.S. 317, 326, 106 S.Ct. 2548, 2554, 91 L.Ed.2d 265 (1986)). We find that, because the record indicates that matters outside the pleadings were presented to and considered by the lower court, the ruling was a grant of summary judgment, appropriately made after notice to all parties.

To review the decision of the trial court, this Court must perform its own *de novo* review of the record following the same summary judgment standards as the trial court to determine whether there are genuine issues of material fact. *Christopher v. Mobil Oil Corp.*, 950 F.2d 1209, 1213-14 (5th Cir. 1992), Fed.R.Civ.P. 56(c). In reviewing the evidence, we must make all justifiable inferences in favor of the non-moving party. *Id.*, at 1213-14. However, if a movant has advanced summary judgment evidence regarding an issue on which the non-movant has the burden of proof at trial, the burden shifts to the non-movant to come forth with evidence establishing each of the challenged elements of its case. *Duckett v. Cedar Park*, 950 F.2d 272, 276 (5th Cir. 1992). The non-movant is not allowed to rely on its pleadings at this juncture. Mere allegations that facts exist which create a genuine issue of material fact are insufficient to defeat a properly supported motion for summary judgment. *Hanks v. Transcontinental Gas Pipe Line Corp.*, 953 F.2d 996, 997 (5th Cir. 1992).

LUCK'S CLAIM AGAINST O&G BASED ON EXPRESS COVENANT

Luck claims that O&G breached an express covenant to develop the lease, which arose from language in the operating agreement that obligated Smith and O&G to test a minimum of three wells per year. In its Memorandum Opinion, the Court below held that Luck failed to state a cause of action on its implied covenant claim, and then denied Luck's motion for partial summary judgment establishing liability on the express and implied covenant claims, leaving the express covenant claim pending. The same day the court entered a final take nothing judgment in the case, although the express covenant claim had not been previously disposed of.

Perhaps it could be argued that the district court's language earlier in the Memorandum Opinion finding that "[d]ismissal [of Luck's suit against Smith] resulted in a dismissal of all of Luck's claims against Smith and O&G Carriers," was intended to dispose of the express covenant claim. However, the referenced settlement disposed of Luck's claims for operating expenses only, and did not include its express and implied covenant claims. The district court acknowledged this by discussing both claims and disposing of the implied covenant claim separately in the same order.

Because the Final Judgment had the effect of dismissing the express covenant claim, this Court must determine whether the trial court's dismissal should be affirmed on a ground not expressly relied on. The judgment must be affirmed if it is sustainable on any legal ground apparent in the record, *Jaffke v. Dunham*, 352 U.S. 280, 77 S.Ct. 307, 1 L.Ed.2d 314 (1957), even if the district court's reasoning is rejected. *Levene v. Pintail Enterprises, Inc.*,

943 F.2d 528, 534 (5th Cir. 1991).

O&G takes the position that Luck's express covenant claim was properly dismissed because various work done on the lease fulfilled the contractual obligation to test three wells per year, and Luck failed to submit competent summary judgment evidence demonstrating that the testing required by the covenant had not been done. In fact, the deposition of Howard Smith attached to Plaintiffs' Motion for Partial Summary Judgment as to Liability (Mr. Smith testified that O&G did not pay their bills which prevented the required testing) creates a genuine issue of material fact concerning whether or not the required testing was done.

Next O&G argues that Luck had not and could not demonstrate that any damages arose from the failure to test the wells, because there was no express obligation in any of the agreements among the parties to place tested wells back in operation. The language of the partial assignment binds O&G and the other assignees "to test a minimum of three (3) of the presently existing shut-in wells upon the above-described leases per year from the date of this instrument." If the wells proved not to be productive they were to be assigned to a third party, and if they turned out to be productive they were to be retained by the working interest owners. The language of the contract does not expressly require that any affirmative action be taken as to productive wells. Had the wells been properly tested, the lease, and therefore Luck, might have benefitted from the assignment of nonproductive wells, or the working interest owners may have chosen to put productive wells

into operation. However, the testing may have cost more than any benefit gained. It would have been a simple matter to produce expert testimony that addressed the likelihood of economic benefit from the testing procedure. However, a close perusal of the record reveals nothing more than speculation, which does not create a fact issue concerning whether Luck was more likely than not damaged by the failure to test three wells per year. Because the record reveals no evidence of damages beyond mere speculation, the trial court's effective grant of summary judgment must be affirmed.

We therefore find that the district court did not err in dismissing Luck's claim based on the express covenant.

LUCK'S CLAIM UNDER AN IMPLIED COVENANT

Luck claimed that O&G breached an implied covenant to reasonably develop the leases. The court below found that there was no implied covenant because the express terms of the agreement describe the parties' obligations to each other. We agree. Luck cannot assert a breach of an implied covenant to develop where the written agreement sets forth the parties' obligation. See *Exxon Corp. v. Atlantic Richfield Co.*, 678 S.W.2d 944, 947 (Tex. 1984).

Luck argues that the duty implied under Texas law to develop the leasehold estate is a greater obligation and is in addition to the obligation to test a minimum of three presently existing shut-in wells per year. A lessee's obligation to develop and protect the lease which is implied under Texas law is indeed broader than O&G's express contractual duty in this case. However, that duty is not in addition to an express covenant and is implied only when an oil

and gas lease fails to express the lessee's obligation to develop and protect the lease. *Amoco Production Co. v. Alexander*, 622 S.W.2d 563 (Tex.1981). Texas law does not prevent parties from expressly limiting, expanding, or specifying the details of the duty to develop a particular lease by contract, as the parties did in this case. We therefore hold that the district court did not err in finding that there was no implied covenant in this case.

Because there is no implied covenant, it is unnecessary to reach the question, raised by Luck, of whether under Texas law an implied covenant, which traditionally runs between the lessee and the lessor or royalty interest owner, can be implied for the benefit of a reversionary interest owner.

SUMMARY JUDGMENT ON O&G'S COUNTERCLAIMS

The district court granted John C. Luck summary judgment against O&G on O&G's counterclaim for failure to state a cause of action, noting that O&G had sued Luck individually, although he was not a party to the contractual agreements that formed the basis of the lawsuit. O&G's brief on appeal argues only that the "Luck counter defendants" should not have prevailed on the basis of the compulsory counterclaim rule or collateral estoppel. John C. Luck filed no brief on appeal. We find no basis for disturbing the district court's award of summary judgment for John C. Luck against O&G.

O&G filed a counterclaim seeking damages from Smith for breach of contract, fraud, negligence, conversion, misrepresentation and violations of the Texas Deceptive Trade Practices Act. The court

below held that all of these assertions could have been litigated or had been litigated in the Galveston and New York cases involving the same facts and the same parties. Therefore, citing the rule of compulsory counterclaims and the doctrine of collateral estoppel, the court granted Smith's motion for dismissal of the counterclaim.

O&G argues on appeal that the counterclaims against Smith were not controlled by the compulsory counterclaim rule and were not barred by collateral estoppel. Smith responds that the district court's dismissal was essentially based on deference to the state-court litigation. A federal district court may decline to exercise its jurisdiction because of parallel state-court litigation only in exceptional circumstances. Only the clearest of justifications will warrant dismissal. *Colorado River Water Conservation District v. United States*, 424 U.S. 800, 818-819, 96 S.Ct. 1236, 1246-1247, 47 L.Ed.2d 483 (1976). Although there are no hard-and-fast rules for dismissals due to the presence of a concurrent state proceeding, the Supreme Court has listed the following factors as relevant to the decision: 1) inconvenience of the federal forum, 2) the desirability of avoiding piecemeal litigation, and 3) the order in which jurisdiction was obtained by the concurrent forums. *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 15, 103 S.Ct. 927, 937, 74 L.Ed.2d 765 (1983). The weight to be given any one factor may vary greatly from case to case, depending on the circumstances of the case. *Id.*

When, as here, the counterclaim rests entirely on Texas law and has all but been resolved in a Texas court, the district court has

no independent jurisdiction over the counterclaim and has dismissed the claim that established jurisdiction, and the counterclaimant unduly delayed filing the counterclaim in federal court, deference to the parallel state court action is called for primarily based on factor two, the avoidance of piecemeal litigation. Although the district court did not specifically rely on *Cone/Colorado River* abstention, the facts of the case and the language in the lower court's order support the conclusion that this was an appropriate case for dismissal in deference to the Galveston litigation. We therefore affirm the district court's dismissal of O&G's counterclaim against Smith on the basis of abstention. See *Jaffke v. Dunham*, 352 U.S. 280, 77 S.Ct. 307 1 L.Ed.2d 314 (1957).

Because the district court was correct in dismissing O&G's counterclaim against Smith, we decline to address the remaining arguments advanced by Smith for affirming the dismissal.

CONCLUSION

The district court's order is AFFIRMED.