Business contracts are often compared to marriages, and for good reason. Both imply a deep level of mutual commitment to the relationship. But at what point in the relationship do businesses say “I do,” and at what point may one of the businesses walk away from the relationship with no obligation to the other company?

Two cases currently before the Texas Supreme Court will go a long way toward answering these questions. These cases examine the very nature of business partnerships and contractual agreements, particularly at what point in negotiations potential liabilities are created. The decisions the Justices reach in *Energy Transfer Partners LP et al. v. Enterprise Products Partners LP et al.* and *Chalker Energy Partners III LLC et al. v. Le Norman Operating LLC* offer the court a chance to clarify at what point a deal is a deal and likely will shape future co-working relationships and transactions in the Texas oil and gas industry for years to come.
Oil Industry Heavyweights Clash in Contractual Dispute over Pipeline Project

The long-running legal drama of *ETP v. Enterprise* has captivated oil and gas industry observers throughout the Lone Star State and beyond. Enterprise Products Partners LP and Energy Transfer Partners were working together on the development of a potential pipeline to transport crude oil from Oklahoma to refineries near the Gulf of Mexico. The parties signed a nonbinding letter of intent, as is typical in the oil and gas industry, which stated definitive agreements and board approval was required as a prerequisite to creating a binding pipeline agreement. Enterprise later dropped the project with ETP and moved forward with a similar pipeline with another party. ETP sued, alleging Enterprise violated a binding deal.

In 2014, a Dallas jury handed down one of the largest verdicts in Texas history, awarding ETP $535 million in damages. The jury found that ETP and Enterprise had been partners in the pipeline deal and that Enterprise breached the duty of loyalty owed between partners by building a similar pipeline with another company instead of ETP. The jurors concluded the companies’ dealings satisfied the statutory partnership-formation test even though the companies did not execute definitive agreements or obtain board approval for the deal, which were both conditions precedent to a binding deal per the letter of intent.

However, the Fifth Court of Appeals overturned that half-billion-dollar verdict in 2017. The Appeals Court ruled that the two companies did not have a valid contractual agreement and, therefore, Enterprise could not be responsible for breaching a duty of loyalty.

The key to the appeal was a signed agreement between the two companies stating that a binding pipeline agreement would not formally exist unless certain terms and conditions were met. Enterprise successfully argued on appeal that those terms and conditions were not met and the company was free to do business with ETP rival Enbridge Inc. The Court of Appeals found that the prior written agreement barred finding a partnership existed without a jury finding that the prerequisites to a binding deal were waived, and therefore there was no duty of loyalty to breach.

The Texas Supreme Court agreed to take the case and heard oral argument on October 8, 2019.

The case has generated tremendous interest in Texas’ oil and gas industry, not just because of the size of the initial judgment or the market share of the two companies, but because the very definition of what constitutes a binding agreement or business partnership is under the microscope.

The parties’ preliminary agreement – the Letter of Intent — and its prerequisites to formation of a binding deal is at issue in the appeal. The letter agreement required the boards of both companies to approve the deal before it was finalized. In addition, the letter agreement said that the companies must trade executed agreements that documented the final terms of the deal.

Enterprise has maintained since the start of the dispute that because those “conditions precedent” were not met, a binding deal never existed. Enterprise
attorneys argued that the working relationship between the two companies simply was a trial period and their client made the decision to move on before a formal deal was entered or partnership was formed.

On the other hand, ETP attorneys say Enterprise’s actions during the period the companies were working together satisfy the terms of partnership formation under the Texas Business Organizations Code (TBOC).

During oral argument, Texas Supreme Court Justice Eva Guzman asked ETP counsel, “Could you ever have conditions precedent to the formation of a contract that weren’t subsumed by the five-factor TBOC test?”

One key component of the TBOC Partnership Formation test is that a working arrangement must be “for profit” in order for it to be a partnership. Enterprise said the working arrangement simply was exploratory because the “for profit” aspects of the pipeline wouldn’t occur until the construction and operation phases.

But ETP’s attorneys told the Justices that “These parties weren’t doing this for fun” and there is no question that the end goal of both companies was to make money on the pipeline.

Sales Agreement—or Lack Thereof—at Center of $350 Million Chalker Energy Case

A similar dispute, regarding the sale of oil and gas interests, is taking place in Chalker Energy Partners III LLC et al. v. Le Norman Operating LLC. (For the sake of transparency, we should note that we are representing Chalker Energy in this case.) The Texas Supreme Court is scheduled to hear oral argument in the case on Dec. 4.

A multi-party group led by Chalker Energy initially discussed selling their oil and gas producing properties in the Texas Panhandle via a competitive bid process. One of the potential bidders was LNO. To facilitate the negotiations Chalker and LNO entered a Confidentiality Agreement containing a “No Obligation” clause which allowed the parties to negotiate without fear of either being bound to a sale “unless and until a definitive agreement was executed and delivered”. But when the sellers reached an agreement to sell the oil & gas interests to Jones Energy, a competing bidder, LNO sued Chalker Energy, et al, claiming the sellers breached an agreement to sell to them.

Similar to the arguments in ETP v. Enterprise, Chalker and the other sellers argued that no definitive agreement (a purchase and sale agreement) ever existed, was signed or delivered, which the parties had agreed were prerequisites to a binding deal. In contrast, LNO argues that some emails exchanged between the parties and their representatives constitute a definitive agreement or the parties were outside the bid process such that the conditions precedent to formation of a binding contract no longer applied.

In 2015, a Harris County District Court agreed with the sellers. The court ruled that no definitive agreement to sell to LNO existed and, thus, the sellers were within their rights to sell to Jones Energy.
But in 2017, the First Court of Appeals reversed this ruling. The appeals court noted that the LNO offer came in after the initial bid process had concluded, and, so, it was not subject to the bid process rules. The appeals court then remanded the case back to the trial court for further consideration.

Noting that the First Court of Appeals admitted it could not “determine the nature of the agreement between LNO and the sellers, if any,” the sellers’ counsel wrote in their brief to the Texas Supreme Court, “If the courts cannot determine the nature, or even the existence of an agreement, between LNO and the sellers, there is no ‘definitive agreement.’”

The Court’s decision in Chalker Energy will provide critical guidance to any party doing business in Texas, particularly those communicating via email and those attempting to negotiate complicated multi-party transactions through a pre-agreed organized process – as is common in oil and gas transactions.

**Broad Implications on Business**

Given the similarities between the two cases, as well as the close proximity of the oral arguments, it is likely that the Texas Supreme Court will use these cases to answer critical questions for Texas business’ as to when a deal is a deal, and whether Texas courts will enforce written agreements regarding parties’ willingness to negotiate and intent to be bound. The consequences of these two cases extend far beyond the parties to these two disputes.

At the heart of both cases is whether the parties ever said, “I do.” The Texas Supreme Court’s rulings will have broad implications on how companies do business, particularly in the oil and gas industry. Stay tuned for further updates.

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