Operator Beware: Your New Mexico Contract May Not Mean What it Says

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Many operators are expanding activity in New Mexico as they continue to explore and produce oil and gas from the Permian Basin. For some, this activity will bring increased contact with New Mexico courts, where they may encounter a different set of laws than they are accustomed to. One significant difference between New Mexico and other oil and gas producing states is its approach to contract interpretation and enforcement.

Operators in Texas have grown used to the state's strict enforcement of written contractual terms. The Texas Supreme Court has repeatedly emphasized that "[o]bjective manifestations of intent control, not what one side or the other alleges they intended to say but did not," [1] and that "courts will not rewrite agreements to insert provisions parties could have included or to imply restraints for which they have not bargained."[2]

New Mexico does not always adhere to this philosophy, however, as shown by two examples. First, New Mexico has a doctrine of "mutual mistake" that allows courts to reform agreements—even unambiguous ones—that do not reflect what the parties actually intended. This contrasts with the Texas doctrine of mutual mistake, which arises only when "parties to an agreement have contracted under a misconception or ignorance of a material fact[.]"[3] For the Texas doctrine to apply, there must be a shared misunderstanding of an objective fact—for example, a shared misunderstanding about the location of property.[4]

The New Mexico doctrine of mutual mistake does not depend on mistaken factual assumptions. Instead, it applies if the contract, "in its written form, does not express what was really intended by the parties thereto."[5] If the parties did not say what they meant, the court can "reform" the written agreement to reflect their true intentions. The New Mexico Supreme Court has applied this doctrine to avoid enforcing a contract that it acknowledged was "unambiguous" in its terms, due to what it admitted was "conflicting" evidence that the parties had intended to agree to something else.[6] The court's willingness to avoid the unambiguous terms of the parties' written agreement in

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[1] *URI, Inc. v. Kleberg Cty.*, 543 S.W.3d 755, 763 (Tex. 2018); *see also, e.g., Burlington Resources Oil & Gas Co. v. Texas Crude Energy LLC*, 62 Tex. Sup. Ct. J. 529, 531-32 (March 1, 2019); *Tittizer v. Union Gas Corp.*, 171 S.W.3d 857, 860 (Tex. 2005); *Sun Oil Co. v. Madeley*, 626 S.W.2d 726, 728 (Tex. 1981).

[2] *Tenneco Inc. v. Enter. Prods. Co.*, 925 S.W.2d 640, 646 (Tex. 1996)

[3] *Williams v. Glash*, 789 S.W.2d 261, 264 (Tex. 1990).

[4] *Myraid Properties v. LaSalle Bank Nat'l Ass'n*, 300 S.W.3d 746, 750 (Tex. 2009), *abrogated by statute as stated in Flores v. Zimprich*, 559 S.W.3d 223, 229 (Tex. App. El. Paso, 2018, no pet.)

[5] *C.R. Anthony Co. v. Loretto Mall Partners*, 817 P.2d 238, 245 (N.M. 1991) (citation and quotation marks omitted); *Christy v. Travelers Indem. Co. of Am.*, 810 F.3d 1220, 1225 n.4 (New Mexico law allows for reformation of a contract "where there has been a meeting of the minds, an agreement actually entered into, but the contract, deed, settlement, or other instrument, in its written form, does not express what was really intended by the parties thereto.") (10th Cir. 2016) (quoting *C.R. Anthony*, 817 P.2d at 245).

[6] *Id.* at 246 (remanding to trial court for "full evidentiary hearing" regarding the "parties' intent").

favor of disputed, unexpressed intentions reflects a very different approach to contract enforcement than some other states.

Second, New Mexico implies a covenant of good faith and fair dealing in every contract.[7] While the implied covenant of good faith and fair dealing is recognized by some oil producing states,[8] and not others,[9] it is particularly robust in New Mexico. In one New Mexico Supreme Court decision, a contractor recovered over $680,000 against a company for its breach of the parties' "reasonable expectations." Despite the fact that there was no breach of any "specific clause or term of the contract," the company was found liable for having violated the "spirit of the bargain"—as evidenced by the parties' pre-contract negotiations.[10]

Thus, parties in New Mexico should not take for granted that the written terms of their agreements will determine litigation outcomes. To the extent possible, they should ensure that their communications during negotiations, and their subsequent courses of dealing, reinforce their intentions for the agreement. Litigants, too, must account for these potential arguments when analyzing their prospects and presenting their case.

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[7] *Spencer v. J.P. White Bldg.*, 585 P.2d 1092, 1095 (N.M. 1978) (quoting *Flying Tiger Lines, Inc. v. United States Aircoach*, 51 Cal.2d 199, 331 P.2d 37, 51 (1958))

[8] *See Universal Drilling Co., LLC v. R & R Rig Serv., LLC*, 20120 WY 31, ¶¶ 38-41 ("Under Wyoming law, the implied covenant requires that neither party to a commercial contract act in a manner that would injure the rights of the other party to receive the benefit of the agreement."); *R.J.B. Gas Pipelines Co. v. Colo. Interstate Gas Co.*, 813 P.2d 14, 25 (Okla. 1990) (discussing Oklahoma's implied duty of good faith and fair dealing for certain contracts).

[9] The Texas Supreme Court has "specifically rejected the implication of a general duty of good faith and fair dealing in all contracts." *Crim Truck & Tractor Co. v. Navistar Int'l Transp. Corp.*, 823 S.W.2d 591, 595 n.5 (Tex. 1992) (citing *English v. Fischer*, 660 S.W.2d 521, 522 (Tex. 1983)).

[10] *Sanders v. FedEx Ground Package Sys.*, 188 P.3d 1200, 1203-04 (N.M. 2008) (awarding contractor $680,161 for the company's alleged "breach of the implied covenant of good faith and fair dealing"; the company refused to sell the contractor additional routes, and the contractor recovered damages even while the Court acknowledged the company had not violated any express contract terms).