UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF VIRGINIA
ABINGDON DIVISION

SHARON B. HEALY, etc.,	)	
Plaintiffs,	)	
	)	**REPORT AND**
	)	**RECOMMENDATION**
	)	
v.	)	**Case No. 1:10cv00023**
	)	
CHESAPEAKE APPALACHIA, LLC,	)	
NISOURCE INC. and COLUMBIA	)	
ENERGY GROUP,	)	
Defendants	)	

This case comes before the court on defendants' Motion To Dismiss, (Docket Item No. 52) ("Motion"). The Motion is before the undersigned magistrate judge by referral pursuant to 28 U.S.C. § 636(b)(1)(B). As directed by the order of referral, the undersigned now submits the following report and recommended disposition.

I. Facts and Procedural History

The plaintiff, Sharon B. Healy, sues Chesapeake Appalachia, LLC, ("Chesapeake"), NiSource Inc. and Columbia Energy Group, ("Columbia"), on behalf of herself and others similarly situated. The Amended Complaint alleges that Healy owns gas interests in certain tracts of land in Buchanan County, Virginia, and is entitled to payments from Chesapeake as lessor under certain gas leases on these properties. The court's jurisdiction is based on diversity of citizenship. *See* 28 U.S.C.A. § 1332(d)(2)(A) (West 2006). Healy alleges that, under the gas leases,

Chesapeake is responsible for the proper determination, calculation, distribution and payment of royalties due and owing to her on gas produced from the properties. Healy alleges that Chesapeake has underpaid royalties under the leases by selling gas at below-market prices to affiliated companies and by improperly deducting certain post-production costs from royalties. Healy further alleges that Chesapeake has purposefully concealed these improper deductions by intentionally omitting these deductions from the accounting statements that accompany royalty payments. Healy seeks compensatory and punitive damages from Chesapeake, NiSource and Columbia for breach of contract, breach of implied duties to market, failure to act as a reasonably prudent operator and breach of good faith and fair dealing, breach of fiduciary duties, fraud and fraudulent concealment, unjust enrichment, civil conspiracy, conversion and negligence. The plaintiff also seeks an accounting from Chesapeake. Neither the leases at issue nor any of the accounting statements that accompanied royalty payments were attached as exhibits to the Amended Complaint.

The defendants move for the court to dismiss Healy's claims for failing to state a claim under Federal Rule of Civil Procedure 12(b)(6). The defendants have filed the 1948 lease at issue, (Docket Item No. 72, Att. No. 1) ("Lease"), along with two extensions of this lease, (Docket Item No. 72, Att. Nos. 2, 3). The parties have agreed that the language of the Lease may be considered in ruling on the Motion without converting the matter to a motion for summary judgment.

The Lease states that it shall remain in effect for 10 years from June 1, 1948, or for as long as oil and gas are being drilled for or produced on the property. The Lease also contains the following language:

> Should a well be found producing natural or casinghead gas suitable for marketing, the lessee shall pay a royalty of one-eighth (⅛) of the wholesale price at the well for all natural or casinghead gas produced from said land which is marketed or used ..., and if for any reason such sale price cannot be determined, or, if same is being sold to an affiliated, parent or subsidiary company which would render such sale price inequitable to the lessor, then, at the wholesale price prevailing in Buchanan County, Virginia, but in no event shall such price be less than sixteen cents (16¢) per thousand cubic feet for every purpose of gas royalty determination herunder.
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> ...
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> Payments of all royalties shall be made quarterly on the twentieth days of January, April, July and October, for the quarter ending on the last day of the preceding month. The lessee shall furnish to the lessor, on or before the twentieth day of each month, a statement in such detail as may be reasonably required in order to show the amounts of royalties accrued during the preceding month.
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> ...
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> The lessor shall have the right at all times to appoint an agent (a) to inspect and examine the books, papers and records of the lessee and all affiliated corporations, partnerships, concerns or individuals owned or controlled by the lessee for the purpose of and only to the extent necessary for determining any and all royalties, sums of money and rents payable to the lessor under this lease....

The extensions provided to the court show that the Lease was extended for 10 additional years beginning June 1, 1968, or for "so long after the expiration of said additional term of years as the said land is operated by the Lessee in the search for or production of oil or gas." One of these extensions is signed by Anne Reagan Barkley and her husband, Harold J. Barkley, Jr.

Healy alleges that she holds an interest in the lands covered by the Lease and, thus, an interest under the Lease itself, which passed from Anne Reagan, her mother.

Healy attached four documents to her Amended Complaint. One of these documents is a Quitclaim Mineral Deed dated February 28, 2008, from Anne S. Reagan to Harold J. Barkley, III, who Healy alleges is her brother. The deed purports to convey Reagan's mineral interest in the 21 tracts of land covered by the Lease. The deed is signed by Barkley, acting as power of attorney for Reagan. Attached to this deed is a March 1, 2007, Durable Power Of Attorney purportedly executed by Reagan giving Barkley her power of attorney. These documents also include a Quitclaim Mineral Deed dated October 14, 2009, from Barkley to Healy for an one-half interest in the mineral rights of the same 21 tracts of land and a February 3, 2010, Assignment from Barkley giving Healy his interest in any claims arising out of his ownership of these 21 tracts or the mineral rights on these tracts.

The quitclaim deeds contain identical language, which states that the grantor granted "all right, title, and interest in and to any and all oil, gas, and other minerals ... in, upon, and under" the identified tracts of land. The Assignment states:

> ...[Barkley] does hereby assign and transfer to [Healy], all of the assignor's right, claim or chose [sic] in action against any person, firm, corporation or other legal entity by reason of damage suffered by the assignor to any and all of his interests in the oil, gas, and other minerals ... in, upon, and under those certain tracts or parcels of land and property, ... conveyed by the assignor to the assignee in that certain Quitclaim Mineral Deed....

The defendants also have provided the court with bills of complaint or amended bills of complaint filed in two separate Buchanan County Circuit Court cases, in which Reagan was named as a defendant. (Docket Item No. 72, Att. Nos. 6, 7). In addition, the defendants have provided two letters from an attorney purporting to

provide copies of these amended bills of complaint to Reagan in 2002. (Docket Item No. 72, Att. Nos. 8, 9). The amended bills of complaint in each of these cases list Anne Sharon Reagan as a defendant in the cases. The defendants have provided the court with no evidence that Reagan ever actually received notice of the suits.

The first of these suits seeks a declaratory judgment ruling that the Lease created a joint or community lease, and, as such, entitled the plaintiffs, trustees for certain trusts, to a portion of the royalties paid pursuant to the Lease. The suit also sought an accounting from the gas well producer, Columbia Natural Resources, ("CNR"), of the royalties "wrongfully paid by it to Marjorie Coleman and to her successors ... along with a judgment against the Defendant CNR for the amount of monies (royalties) demonstrated to be due and owing" the plaintiff. The second of these suits alleges that the wells on the lands at issue had produced a substantially higher volume of gas than reported by the defendants, CNR and Columbia Gas Transmission Corporation, and, thus, the defendants had not paid royalties as required under the Lease. The suit, however, seeks only an accounting of the royalties paid from the wells and that the plaintiffs share of those royalties be paid to them. While the suit does ask for "such other, further and general relief as may be appropriate," the suit does not specifically seek an accounting of the volume of gas produced by the wells. The defendants allege that these two suits are still pending.

II. Analysis

The Motion seeks dismissal of the Amended Complaint for failure to state a claim for relief under Federal Rule of Civil Procedure 12(b)(6). Specifically, the

defendants argue that Healy's contract claims are barred by Virginia's five-year statute of limitations on actions based on a written contract. The defendants argue that Healy's other claims also are barred by the applicable statutes of limitations. The defendants also argue that Healy's claims, other than the breach of contract claim, are not recognized by Virginia law.

The Supreme Court recently revisited the proper standard of review for a motion to dismiss and stated that the long-used "no set of facts" language from *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957), has "earned its retirement" and "is best forgotten" because it is an "incomplete, negative gloss on an accepted pleading standard." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 562-63 (2007). In *Twombly*, the Supreme Court stated that "a plaintiff's obligation to provide the 'grounds' of ... 'entitle[ment] to relief' requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." 550 U.S. at 555 (quoting *Papasan v. Allain*, 478 U.S. 265, 286 (1986)). The "[f]actual allegations must be enough to raise a right to relief above the speculative level." *Twombly*, 550 U.S. at 555 (citations omitted). Additionally, the Court established a "plausibility standard" in which the pleadings must allege enough to make it clear that relief is not merely conceivable but plausible. *See Twombly*, 550 U.S. at 555-63.

The Court further explained the *Twombly* standard in *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949-50:

> Two working principles underlie our decision in *Twombly*. First, the tenet that a court must accept as true all of the allegations contained in a complaint is inapplicable to legal conclusions. Threadbare recitals

> of the elements of a cause of action, supported by mere conclusory statements, do not suffice. ... Second, only a complaint that states a plausible claim for relief survives a motion to dismiss. ...
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> In keeping with these principles a court considering a motion to dismiss can choose to begin by identifying pleadings that, because they are no more than conclusions, are not entitled to the assumption of truth. While legal conclusions can provide the framework of a complaint, they must be supported by factual allegations. When there are well-pleaded factual allegations, a court should assume their veracity and then determine whether they plausibly give rise to an entitlement to relief.

(Internal citations omitted.)

Generally, a court may not consider matters outside of the pleadings on a motion to dismiss without converting it to a motion for summary judgment. *See* FED. R. CIV. P. 12(d); *Gay v. Wall*, 761 F.2d 175, 178 (4th Cir. 1985). The court may, however, consider documents that are attached to or referenced in the complaint. *See Moore v. Flagstar Bank*, 6 F. Supp. 2d 496 (E.D.Va. 1997) (citing 5A CHARLES A. WRIGHT &ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 1357 (1990)). Since the Lease is referenced in the Amended Complaint, this court will consider the Lease as if its terms were contained in the Amended Complaint.

Since this court's jurisdiction is based upon diversity, the court must apply the substantive law of the forum state, including the forum state's choice of law rules. *See Klaxon Co. v. Stentor Elec. Mfg. Co., Inc.*, 313 U.S. 487, 496-97 (1941); *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938). This court sits in Virginia. Virginia adheres to the use of traditional rules applicable to conflict of laws. "Under such rules, questions of substantive law are governed by the law of the place of the transaction or the place where the right is acquired (lex loci)." *Frye v. Commonwealth*, 345 S.E.2d 267, 272

(Va. 1986). Under Virginia law, issues regarding real estate are governed by the law of the state where the property is located. *See Mort v. Jones*, 51 S.E. 220, 221 (Va. 1905). Furthermore, under Virginia law, claims for personal injury, whether they be for property damage or conversion, are governed by the law of the state where the injury occurred. *See Ryder Truck Rental, Inc. v. UTF Carriers, Inc.*, 790 F. Supp. 637 (W.D. Va. 1992). "Generally, where a cause of action arises in tort, Virginia applies the law of the state where the tortious conduct or injury occurred." *Hitachia Credit Am. Corp. v. Signet Bank*, 166 F.3d 614, 628 (4th Cir. 1999) (citing *Jones v. R.S. Jones & Assocs*. 431 S.E.2d 33, 34 (Va. 1993)).

The Amended Complaint alleges that the Lease was to be performed in Virginia. The Amended Complaint also alleges that the Lease granted the defendants' predecessors in interest the right to extract gas from real property located in Virginia. Furthermore, insofar as it is alleged that the defendants violated their obligations or exceeded their rights under the Lease, these actions appear to have occurred with regard to the production of and accounting for gas gathered in Virginia. Therefore, under Virginia's conflict of law rules, Virginia substantive law, including Virginia's statutes or periods of limitation, would control. *See Guaranty Trust Co. of N.Y. v. York*, 326 U.S. 99, 109 (1945) ("the outcome of the litigation in the federal court should be substantially the same, so far as legal rules determine the outcome of litigation, as it would be if tried in a State court"); *Atkins v. Schmutz Mfg. Co.*, 401 F.2d 731, 734 (4th Cir. 1968).

Under Virginia law, an action based upon a written contract must be filed within five years of accrual. *See* VA. CODE ANN. § 8.01-246(2) (2007 Repl. Vol.).

Furthermore, Virginia law states that a right of action accrues on "the date the injury is sustained in the case of injury to the person or damage to property, when the breach of contract occurs in actions ex contractu and not when the resulting damage is discovered...." VA. CODE ANN. § 8.01-230 (2007 Repl. Vol.).

Healy's claims in this case revolve around the allegation that the defendants have not paid the amounts owed to her under the Lease. Specifically, Healy alleges that, beginning in 1993, the defendants began improperly deducting various post-production and marketing costs, such as costs for gathering, processing and other expenses, from royalties paid under the Lease. Healy alleges that, beginning in 1993, the defendants also underreported the volume of gas produced from the wells and the price paid for the gas produced. Healy further alleges that in 1999 and 2000, the defendants entered into "forward-sales" contracts to supply gas at below-market prices from August 2001 to July 2005.

The defendants argue that any claim for breach of the terms of the Lease is barred by Virginia's five-year statute of limitations on claims based on written contracts. In particular, the defendants argue that, if they have improperly deducted post-production expenses from the royalties paid on these leaseholds, they have done so for approximately 17 years. If deducting post-production expenses from these royalties breached the Lease, the defendants argue, the breach occurred when these deductions were first taken – approximately 17 years ago. The defendants further argue that, if, as alleged by plaintiffs, their self-dealing resulted in the underpayment of royalties from 2001 to 2005, any resulting breach of the Lease as a result of these alleged underpayments occurred beginning in 2001, more than nine years prior to the

filing of this case.

In support of their argument, the defendants cite the Virginia Supreme Court's 1989 decision in *Westminster Investing Corp. v. Lamps Unlimited, Inc.*, 379 S.E.2d 316 (Va. 1989). In *Westminster,* the Virginia Supreme Court rejected a "continuous breach" exception to Virginia's five-year period of limitations on suing for a breach of a written contract. *See* 379 S.E.2d at 319. The plaintiff-lessee, Lamps Unlimited, sued the defendant-lessor, Westminster, to recover damages resulting from Westminster's alleged breach of a written lease agreement. Lamps Unlimited had entered into the lease on July 27, 1976, leasing retail space at a Northern Virginia shopping center from Westminster for a period of 10 years. The term of the lease began on October 1, 1976. During negotiations, a representative of Westminster represented that it intended to begin enforcing uniform business hours for all of the shopping center's tenants. This representation induced Lamps Unlimited to enter into the lease. Shortly after entering into the lease, Lamps Unlimited learned that Westminster was not enforcing uniform business hours on the shopping center's tenants. Over the years, Lamps Unlimited lodged numerous complaints over Westminster's failure to enforce uniform business hours. In June 1983, three years before the expiration of its lease, Lamps Unlimited vacated its store. On October 28, 1985, Lamps Unlimited sued Westminster based on breach of contract. *See Westminster*, 379 S.E.2d at 316-17.

Westminster argued that Lamp Unlimited's claim accrued in 1976 when it first learned that Westminster was not enforcing uniform business hours, and, therefore, Lamps Unlimited's claim was barred by Virginia's five-year period of limitations on

claims based on written contracts. *See* VA. CODE ANN. § 8.01-246(2). Lamps Unlimited argued that Westminster's continuous failure to enforce uniform business hours constituted a breach that continued until the day that it vacated the premises in 1983. While Lamps Unlimited agreed that the five-year limitations period applied to its claim, it argued that the limitations period's only effect was to restrict its claim for damages to the five-year period prior to the date it filed suit. *See Westminster*, 379 S.E.2d at 317.

With little explanation, the Virginia Supreme Court rejected the "continuous breach" theory. *See Westminster*, 379 S.E.2d at 319. The court stated:

> Statutes of limitation "serve an important and salutary purpose." ... Indeed, without limitations on actions,
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> > defendants could find themselves at the mercy of unscrupulous plaintiffs who hoard evidence that supports their position while waiting for their prospective opponents to discard evidence that would help make a defense. In light of the policy that surrounds statutes of limitation, the bar of such statutes should not be lifted unless the legislature makes unmistakably clear that such is to occur in a given case. Where there exists any doubt, it should be resolved in favor of the operation of the statute of limitations.
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> ...
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> Thus, courts are obligated to enforce statutes of limitations strictly and to construe any exception thereto narrowly.

Westminster, 379 S.E.2d at 318.

The court recognized that, where an injury, even though slight, occurred as a

result of the wrongful or negligent act of another, and the law provided a remedy, the right of action had accrued and that the statute of limitations began to run. *See Westminster*, 379 S.E.2d at 317-18. The court stated that it was "immaterial" that all damages resulting from a breach had not been sustained. *See Westminster*, 379 S.E.2d at 319. Thus, the court held that Lamps Unlimited's claim accrued in 1976, and its suit filed in 1985 was barred by the statute of limitations. *See* 379 S.E.2d at 319.

The defendants also cite a recent opinion from the Eastern District of Virginia in support of their argument that Healy's breach of contract claim is barred by the statute of limitations. In *Hunter v. Custom Business Graphics*, 635 F. Supp. 2d 420 (E.D.Va. 2009), the Eastern District of Virginia held that an employer's failure to pay an employee's monthly car allowance provided for by contract or to pay the employee's commission at the contract rate did not constitute a new breach with every pay period. Instead, the court held that the employer's actions were a continuation of the original breach that occurred when the employer first refused to pay the employee his car allowance or to honor the contract rate for his commission. *See Hunter*, 635 F. Supp. 2d at 433. The court found since the employer instituted these pay changes more than five years earlier, the employee's breach of contract claims based on the employer's actions were completely barred by the five-year Virginia statute of limitations. *See Hunter,* 635 F.Supp.2d at 433.

Plea of the statute of limitations is an affirmative defense. Thus, the defendants bear the burden of proving that the plaintiffs' claims are barred by the statute of limitations. *See Heirs of Roberts v. Coal Processing Corp,* 369 S.E.2d188, 190 (Va. 1988). Healy argues that the defendants cannot meet this burden for three reasons.

First, Healy asserts that the statute of limitations has been tolled by the defendants' fraudulent concealment of their actions. Second, Healy asserts that, under the "continuing undertaking" rule, the statute of limitations has not begun to run on her claims. Third, Healy claims that each underpayment of royalties was the result of a discrete and interval-based breach, which constituted a new cause of action and which restarted the statute of limitations. Thus, Healy argues that, at the very least, she should be allowed to pursue those claims which have arisen in the previous five years.

I first will address Healy's argument that the statute of limitations has not begun to run under the "continuing undertaking" rule. In *Riverview Land Co. v. Dance*, 35 S.E. 720 (Va. 1900), the Virginia Supreme Court recognized that the limitations period does not begin to run until a right of action accrues and, further, that there can be no right of action until a person who is performing continuing services has a right to demand payment. The court reasoned:

> As a general proposition, where there is an undertaking or agency which requires a continuation of services, the statute of limitations does not begin to run against advances lawfully made by the agent in the prosecution of the undertaking or agency, or against compensation for the services of the agent, until the termination of the undertaking or agency. The law looks upon the employment as an entire contract, and regards the claim for disbursements and compensation as an entire demand, to which the right does not accrue until the completion of the service or the termination of the employment or agency.

Riverview, 35 S.E. at 722. The case before the court in *Riverview* involved a claim by a real estate agency against landowners for sums advanced to develop property for sale.

In 1905, the Virginia Supreme Court, citing its opinion in *Riverview*, held that "when there is an undertaking or agency which requires a continuation of services, the statute of limitations does not begin to run until the termination of the undertaking or agency." *Wilson v. Miller* 51 S.E. 837, 838 (Va. 1905). The claims in *Wilson* arose out of a power of attorney executed to allow an agent to conduct certain business and collect certain debts for the out-of-state principals. *See Wilson*, 51 S.E. at 838. The court applied the rule to the attorney-client relationship in *Beale v. Moore*, 32 S.E.2d 696, 698-99 (Va. 1945). *See also Wood v. Carwile*, 343 S.E.2d 346, 349-50 (Va. 1986)*; McCormick v. Romans*, 198 S.E.2d 651, 654-655 (Va. 1973). The court has recognized a variant of the rule, the so-called "continuing treatment" rule, with regard to claims between patients and healthcare providers. *See Farley v. Goode*, 252 S.E.2d 594, 599 (Va. 1979) (cause of action for malpractice accrues, and the statute of limitations commences to run, when an improper course of examination and treatment for a particular malady terminates). The court also has applied the rule to claims against or by accountants. *See Boone v. C. Arthur Weaver Co., Inc.*, 365 S.E.2d 764, 766 (Va. 1988).

As the Virginia court, itself, recognized, the "continuing services" rule has been invoked in "varying circumstances in which a principal has entrusted an agent with a continuing series of transactions, or a single but long-protracted transaction." *Keller v. Denny*, 352 S.E.2d, 327, 329 (Va. 1987) (rule applied in legal malpractice claim). "[The] Court has recognized the continuing undertaking doctrine only with regard to a continuous or recurring course of professional services related to a particular undertaking." *Harris v. K & K Ins. Agency, Inc.*, 453 S.E.2d 284, 286 (Va. 1995). The court also has made clear that the rule is not a "continuing agency" rule, under which

the right of action would accrue only upon the termination of the professional relationship between the parties. *See Boone*, 365 S.E.2d at 767 (citing *Keller*, 352 S.E.2d 327).

Along these lines, the Virginia court has refused to apply the rule in two cases involving professional services rendered by architects based on findings that the contracts at issue were divisible into separate and distinct phases, and, therefore, the architects' services were severable rather than continuous. *See Nelson v. Commonwealth*, 368 S.E.2d 239, 248 (Va. 1988); *Comptroller of Va. ex rel. Va. Military Inst. v. King*, 232 S.E.2d 895, 900 (Va. 1977). The court also has refused to apply the rule to actions involving insureds' allegations of breach of contract against insurance agencies and their brokers. *See Harris*, 453 S.E.2d at 286-87. In *Harris*, the court reasoned that acts of insurance agents and brokers in selling, renewing or changing policies or processing insurance claims were "not analogous to the professional services at issue" in their previous cases. 453 S.E.2d at 286-87. Furthermore, the court stated that the agents' and brokers' actions could not be characterized as performing continuing services on a particular undertaking. *See Harris*, 453 S.E.2d at 287.

The same could be said of Healy's allegations in this case. There are no allegations that Healy or the proposed class members contracted for the defendants to render any type of continuing professional services to them. Instead, Healy's claims all arise from the allegation that the defendants have underpaid the royalties due her under the Lease. Therefore, I recommend that the court hold that Virginia's continuing undertaking rule should not be applied to the facts of this case.

I next will consider whether the plaintiffs have sufficiently alleged fraudulent conduct on the part of the defendants to toll the running of the statute of limitations. Virginia courts have long-held that a defendant's action may estop a defendant from pleading and relying on the statute of limitations to defeat a claim. *See City of Bedford v. James Leffel & Co.*, 558 F.2d 216, 217-19 (4th Cir. 1977); *Richmond Redevelopment & Housing Auth. v. Laburnum Constr. Corp.*, 80 S.E.2d 574, 582 (Va. 1954) (if defendant intends to conceal the discovery of a cause of action by trick or artifice and succeeds, the running of the statute of limitations is tolled); *Sadler v. Marsden*, 168 S.E. 357, 360 (Va. 1933) (fraudulent promise to execute new deed of trust prevents defendant from asserting statute of limitations defense to enforcement of original deed of trust); *see also Wilson v. Butt*, 190 S.E. 260 (Va. 1937). The Virginia Supreme Court has held that a party seeking to invoke the doctrine of estoppel must prove by clear, precise and unequivocal evidence that (1) a material fact was falsely represented or concealed; (2) the representation or concealment was made with knowledge of the fact; (3) the party to whom the representation was made was ignorant of the truth of the matter; (4) the representation was made with the intention that the other party should act upon it; (5) the other party was induced to act upon it; and (6) the party claiming estoppel was misled to his injury. *See Boykins Narrow Fabrics Corp. v. Weldon Roofing & Sheet Metal, Inc.*, 266 S.E. 2d 887, 890 (Va. 1980) (citing *Coleman v. Nationwide Life Ins. Co.*, 179 S.E.2d 466, 469 (Va. 1971)).

The Fourth Circuit has issued conflicting opinions as to whether Virginia law requires a showing of fraud to justify application of the doctrine of equitable estoppel to toll the running of the statute of limitations. In 1986 a panel wrote that, under Virginia law, "one may be estopped to plead the bar of a statute of limitations by

conduct short of fraud." *Barry v. Donnelly*, 781 F.2d 1040, 1042 (4th Cir. 1986) (citing *Bedford,* 558 F.2d at 217-18). "While equitable estoppel in both its general applications as well as in its special application to statutes of limitations pleas frequently involves fraud or deceit and is 'most clearly applicable' when it does, 'deceit is not an essential element of estoppel' in either its general or special applications under Virginia law." *Barry*, 781 F.2d at 1042 (citing *Bedford*, 558 F.2d at 218). In 1993, however, a panel of the circuit held: "Although equitable estoppel in Virginia generally does not require an intentional misrepresentation, ... the Virginia Supreme Court has required intentional conduct to allow the doctrine to toll the running of a statute of limitations." *FDIC v. Cocke*, 7 F.3d 396, 402 (4th Cir. 1993) (*citing Richmond Redevelopment & Housing Auth.*, 80 S.E.2d at 582).

As the Fourth Circuit held in *FDIC*, it appears that the Virginia high court no longer requires an intentional misrepresentation to apply the doctrine of equitable estoppel in general. *See FDIC*, 7 F.3d at 402 (citing *T v. T*, 224 S.E.2d, 148, 152 (Va. 1976)). Nevertheless, the Virginia court has not overruled its holding in *Boykins Narrow Fabrics Corp.*, 266 S.E. 2d at 890, requiring a knowingly false representation or concealment to apply the doctrine of equitable estoppel to toll the running of a statute of limitations. *See Adams v. Alliant Techsystems, Inc.*, 201 F. Supp. 2d 700, 713 (W.D. Va. 2002) (citing *Boykins Narrow Fabrics Corp*., 266 S.E.2d at 890) (under Virginia law, a defendant is estopped from raising a statute of limitations defense when the defendant has obstructed the plaintiff from asserting his claim by fraudulently concealing the potential cause of action). It appears that this distinction may have developed based on the courts' obligation to strictly enforce statutes of limitations and to narrowly construe any exceptions. *See Westminster Investing Corp*.,

379 S.E.2d at 318 ("It is well settled, and needs the citation of no authority to that effect, that the statute [of limitations] begins to run when the right of action accrues. It is equally well settled that in its terms the statute is absolute, admitting of no exception which itself does not recognize, unless under certain extraordinary circumstances, wherein the positive and plain requirements of an equitable estoppel preclude its application"). That being the case, I hold, as the Fourth Circuit did in *FDIC*, that a showing of an intentional misrepresentation or concealment is necessary to apply the doctrine of equitable estoppel to toll a statute of limitations under Virginia law. *See FDIC*, 7 F.3d at 402. Thus, under Virginia law, "a statute of limitations is tolled until a person intentionally misled by a putative defendant could reasonably discover the wrongdoing and bring action to redress it." *FDIC*, 7 F.3d at 402.

Healy asserts that the fraudulent concealment doctrine prevents the defendants from raising a statute of limitations defense. The case cited in support of Healy's argument, however, recognizes that the fraudulent concealment doctrine applies with regard to federal statutes of limitations. *See Supermarket of Marlinton, Inc. v. Meadow Gold Dairies, Inc.*, 71 F.3d 119, 122 (4th Cir. 1995). As stated above, this case involves claims governed by Virginia state law. The plaintiffs argue that the fraudulent concealment doctrine has been codified in Virginia. *See* VA. CODE ANN. § 8.01-229(D) (2007 Repl. Vol.). This statute, on its face, however, applies only when "the filing of an action is obstructed by a defendant's ... using any ... direct or indirect means *to obstruct the filing of an action*." VA. CODE ANN. § 8.01-229(D) (emphasis added). In such circumstances, "the time that such obstruction has continued shall not be counted as any part of the period within which the action must be brought." VA. CODE ANN. § 8.01-229(D). The Virginia Supreme Court has held that any plaintiff

who seeks to rely upon the tolling provision in this code section "must establish that the defendant undertook an affirmative act designed or intended, directly or indirectly, to obstruct the plaintiff's right to file her action." *Grimes v. Suzukawa*, 551 S.E.2d 644, 646 (Va. 2001).

The Amended Complaint does not allege that the defendants took any action to obstruct the filing of this suit. Instead, the Amended Complaint claims that the defendants fraudulently concealed the facts necessary for Healy and others similarly situated to know that they had a cause of action. The Virginia Supreme Court, in dicta, has accepted that this section applies to the fraudulent concealment of the existence of a cause of action. *See Newman v. Walker*, 618 S.E.2d 336, 338 (Va. 2005). The court also has recognized that a predecessor to this code section allowed tolling of the statute of limitations upon a finding that the plaintiff's ignorance of the existence of a cause of action was caused by the defendant's fraud. *See Culpeper Nat'l Bank v. Tidewater Improvement Co., Inc*. 89 S.E. 118, 121 (Va. 1916).

Healy also argues that she should, at the very least, be allowed to pursue her breach of contract claim based on any underpayments made within five years of the date of the filing of this action. Specifically, Healy asserts that each underpayment of royalties was a discrete breach, which constituted a new cause of action. The defendants argue otherwise based on the *Hunter* decision, 635 F. Supp. 2d 420. Based on the facts alleged in the Amended Complaint, it appears that, at this stage, Healy should be allowed to pursue her claims for any underpayments made within the five years prior to filing. Healy alleges that the underpayment of royalties occurred due to several reasons. Among these reasons are that the defendants underreported the

volume of gas produced each month, underreported the amount paid for the gas and sold the gas at below-market prices. Unlike a specific deduction from royalties, which begins at a point in time and continues, underpayment due to the above reasons would be separate independent breaches, subject to separate accrual dates. Therefore, I recommend that the court find that Healy has pled facts sufficient to pursue her breach of contract claim for any underpayments of royalties within the five years prior to filing of this claim.

The court next must determine whether the facts as alleged in the Amended Complaint are sufficient, if proven, to toll the statute of limitations under either the equitable estoppel or fraudulent concealment doctrines. In the Amended Complaint, Healy alleges that the defendants have, since at least 1993, purposefully provided false information to royalty owners in an effort to prevent the royalty owners from discovering that the defendants were not paying all royalties due under their leases. According to the Amended Complaint:

> Through ... unlawful operational, marketing and accounting practices, acts and omissions – and the improper inter-corporate transactions, self-dealing and fraud perpetrated to benefit the [defendants] ..., Chesapeake has failed to pay the true Royalties owed to Plaintiff, or her predecessors-in-interest, and the Class Members, and has actively misrepresented and fraudulently concealed data and information exclusively within the [defendants'] possession, custody, or control from which Plaintiff and the Class Members could have learned of or advanced their claims to the ultimate detriment and damage of Plaintiff and the ... Class. Plaintiff, or her predecessors-in-interest, and the Class Members relied upon the [defendants'] misrepresentations and have been and continue to be damaged....

(Docket Item No. 46, ("Amended Complaint"), at 13-14).

Specifically, the Amended Complaint alleges that the defendants have been improperly deducting certain post-production expenses from royalties and then purposefully falsely reporting to the royalty owners on their monthly statements that they have taken no deductions from royalties. Healy also alleges that the defendants or their predecessors-in-interest entered into two "forward sales" contracts for the sale of CBM at below-market rates. Healy alleges that the defendants then purposefully misrepresented the volumes of gas drawn from the wells and the amounts paid for that gas on the royalty owners' monthly statements in an effort to conceal their actions. Healy further alleges that the defendants also have concealed that they have sold gas at below-market prices to inter-affiliated companies, who, in turn, sold the gas for a profit, resulting in underpayment of royalties.

The Amended Complaint states:

> Chesapeake accounted to Royalty owners by sending each Royalty owner a check and statement which had columns of data ostensibly "disclosing" to Plaintiff and the Class Members monthly: (a) the "rate" in dollars for which gas was sold (per Mcf); (b) the volume which was taken from each well; (c) the deductions that were taken when calculating Royalties; (d) the amount due Plaintiff and each Class Member under their Lease; and (e) other well information such as its name, county, period of reporting, percentage interest of the royalty owner in each well, and type of interest held by each Royalty owner. ... Chesapeake did not report to Plaintiff or the Class Members: (a) gathering fee deductions per Mcf; (b) processing fee deductions; (c) the total amount actually due; (d) the total charges of dollar deductions; (e) the actual withheld volume that was measured or calculated by Chesapeake; or (f) the true "gross Mcf" as opposed to a calculated

number which was not actual and was reported and used to calculate the Royalty.

... Chesapeake materially misrepresented most, if not all, of the various categories of the monthly accounting statements sent to Plaintiffs and the Class Members in a variety of ways, such as:

A. The volume that was represented on the accounting statement to have been produced was never as much as the true volume actually produced.

B. Chesapeake reported deductions of "$0.00" when the truth is that, beginning in or around 1993, significant sums of money were deducted from the Royalty interests for gathering, processing and/or related expenses.

C. The check stub or accounting statement column reporting the "rate" at which Gas was sold was a misrepresentation, because the Gas was never sold at that rate and/or because the rate was very substantially less than the market rate or the highest price reasonably obtainable for which Chesapeake was obliged to sell the Gas.

(Amended Complaint at 23-24).

Healy alleges that the improper deductions taken from royalties were intentionally hidden by the defendants. Healy also alleges that the defendants purposefully falsely represented the rate or price paid when gas was sold in an effort to conceal the forward-sales contracts and the inter-affiliated company sales at below-market rates.

Interestingly, the defendants do not attempt to argue that Healy's allegations are insufficient to state a claim estopping them from asserting a statute of limitations defense. Instead, the defendants argue that Healy cannot assert a claim of fraudulent concealment because her predecessor-in-interest, her mother, had notice of her claims

against the defendants as a result of the Buchanan County Circuit Court cases in which she was named as a defendant. The documents tendered by the defendants, without more, do not provide evidence that Reagan had notice of the defendants' alleged wrongdoings. The defendants have not provided any evidence that Reagan actually received notice of these claims. Even if this evidence had been provided, it would be just that – evidence that would be relevant on the factual issue of whether the court should apply the fraudulent concealment or equitable estoppel doctrines to toll the statute of limitations. Based on the above, I find that Healy has pled sufficient facts to earn an opportunity to prove that the defendants' actions should toll the running of the applicable statute of limitations.

The defendants also assert that Healy possesses no claims against them. In particular, the defendants argue that, under Virginia law, tort claims are personal claims, which cannot be assigned and would not pass through the chain of title. They also claim that, insofar as the assignment of her brother's claims was valid, Healy would possess only those claims that her brother acquired after he received his interest in February 2008.

As stated above, Healy claims that she takes her interest in the Lease through her mother, Reagan, and her brother, Barkley. The Lease at issue conveys only oil and gas rights, and it does not address the lessors' ability to transfer their interests under the Lease. The documents attached to the Amended Complaint show that Reagan's interests in the mineral rights on the properties covered by the Lease passed to Barkley in February 2008 by Quitclaim Mineral Deed and, one-half interest, from Barkley to Healy in October 2009 by Quitclaim Mineral Deed. Barkley also executed an

Assignment on February 3, 2010, purporting to assign any right he had for any claim for damages arising under his mineral rights interests.

Under the Virginia Code, only causes of action for damages to real or personal property or those based on contract are assignable. *See* VA. CODE ANN. § 8.01-26 (2007 Repl. Vol). Thus, under Virginia law, causes of action for personal injuries cannot be assigned. *See In re Musser*, 24 B.R. 913, 920 (W.D. Va. 1982). Also, personal torts, such as an action for fraud or misrepresentation, cannot be assigned. *See Winchester Homes, Inc. v. Hoover Univ., Inc*., 27 Va. Cir. 62 (1992). "In the absence of an express prohibition, all leases are assignable." *Taylor v. King Cole Theatres*, 31 S.E.2d 260, 261 (Va. 1944) (citing *Wainwright v. Bankers' Loan, etc., Co.*, 72 S.E. 129 (Va. 1911)). Furthermore, when an owner of property conveys it to another, that person assumes all the rights which belonged to the original owner of the property, including any right to recover for damages to the property. *See City of Lynchburg v. Mitchell*, 76 S.E. 286, 287 (Va. 1912).

Insofar as Healy's Amended Complaint raises personal claims, such as those based on fraud, those claims must be based on the defendants' actions toward Healy, herself, and not any of her predecessors-in-interest. On the other hand, any contract claims or any claims arising out of damage to the mineral estate at issue, insofar as they survive, would pass to Healy.

The defendants further argue that none of Healy's claims are sufficiently pled to withstand their Motion. I will spend little time addressing defendants' argument that Healy has not sufficiently pled a claim based on breach of contract because she

did not attach the specific contract at issue to her complaint. "In Virginia, the elements of a cause of action for breach of contract are as follows: (1) a legal obligation of a defendant to the plaintiff; (2) a violation or a breach of that right or duty; and (3) a consequential injury or damage to the plaintiff." *Aviation Resources, Inc. v. XL Specialty Ins. Co.*, 276 F. Supp. 2d 567, 568 (W.D. Va. 2003) (citing *Brown v. Harms*, 467 S.E. 2d 805, 807 (Va. 1996)). In her Amended Complaint, Healy alleges that she and the class members are royalty owners under certain gas and oil leases held and operated by the defendants. She further alleges that, under these leases, the defendants were responsible for the proper determination, calculation, distribution, reporting and payment of the royalties due. Healy alleges that the defendants have failed to pay the royalties owed under the lease. In fact, the Amended Complaint alleges in great detail the acts Healy alleges that the defendants have taken in furtherance of their breach of the leases at issue by the underpayment of royalties owed. Further, the Amended Complaint alleges that Healy and the class members have been injured by receiving less than the amount due in royalties under the leases. Under Virginia law, these facts are sufficient to plead a cause of action for breach of contract. Furthermore, while the Lease was not attached to the Amended Complaint, it has been tendered to the court by the defendants, and all the parties are in agreement that the court may consider the terms of the Lease on the Motion without converting it to a motion for summary judgment. *See Bryant v. Wash. Mut. Bank*, 524 F. Supp. 2d 753, 757 n.4 (W.D. Va. 2007). Therefore, I will recommend that the court deny the Motion on this ground.

I find more persuasive the defendants' argument that at least one of Healy's claims should be dismissed because Virginia law does not recognize a separate cause of action for breach of implied duties arising out of a written contract. It does not

appear that the Virginia Supreme Court has specifically addressed what, if any, implied duties arise on the part of the parties to a written contract under the common law. *See Tymshare, Inc. v. Covell*, 727 F.2d 1145, 1151-52 (D.C. Cir. 1984) (unable to discover any Virginia authority on the existence of a generally applicable "duty to perform in good faith"); *see also L & E Corp. v. Days Inns of Am., Inc.*, 992 F.2d 55, 59 n.2 (4th Cir. 1993) (Virginia Supreme Court has yet to recognize implied covenant of good faith and fair dealing); *but see Enomoto v. Space Adventures, Ltd.*, 624 F. Supp. 2d 443, 450 (E.D. Va. 2009) (citing only federal cases for proposition that, under Virginia law, every contract contains an implied covenant of good faith and fair dealing and allowing independent claim for breach of implied covenant); VA. CODE ANN. § 8.1A-304 ("Every contract or duty within the Uniform Commercial Code imposes an obligation of good faith in its performance and enforcement"). Whether or not any implied duties arise out of a written contract, Virginia courts have held that a party's breach of an implied duty does not give rise to an independent tort, but gives rise to a cause of action for breach of contract only. *See Charles E. Brauer Co., Inc. v. Nationsbank of Va.*, 466 S.E.2d 382, 385 (Va. 1996); *see also A&E Supply Co., Inc. v. Nationwide Mut. Fire Ins. Co.*, 798 F.2d 669, 676 (4th Cir. 1986) ("in a first-party Virginia insurance relationship, liability for bad faith conduct is a matter of contract rather than tort law"). The Virginia courts also have held that an implied duty cannot be used to override or modify any explicit contractual term or right. *See Ward's Equip., Inc. v. New Holland N. Am., Inc.*, 493 S.E.2d 516, 520 (Va. 1997); *see also Riggs Nat'l Bank of Washington, D.C. v. Linch*, 36 F.3d 370, 373 (4th Cir. 1994).

Healy argues that it is well-established that oil and gas leases impose certain implied duties on an operator. Those include, she argues, a duty to market the gas

produced and to operate diligently and prudently. While the Virginia Supreme Court has not specifically addressed this issue, it does appear that other courts have recognized these implied duties in the context of oil and gas leases. "Implied obligations are as much a part of an oil, gas, and mineral lease and are just as binding as though they were expressed." 38 AM. JUR. 2d *Gas And Oil* § 91 (2010) (citing *McCarter v. Ransom*, 473 S.W.2d 235, 238 (Tex. Civ. App. 1971)). However, no implied covenant is recognized if the oil and gas lease contains an express covenant on the same subject matter. *See Bowden v. Phillips Petroleum Co.*, 247 S.W.3d 690, 701 (Tex. 2008).

Colorado courts have recognized four implied covenants in oil and gas leases. These include implied covenants "to conduct exploratory drilling; to develop after discovering resources that can be profitably developed; to operate diligently and prudently; and to protect the leased premises against drainage." *Whitham Farms, LLC v. City of Longmont*, 97 P.3d 135, 137 (Colo. App. 2003). The Colorado courts have held that the implied duty to operate diligently and prudently includes an implied covenant to market. *See Garman v. Conoco, Inc.*, 886 P.2d 652, 659 (Colo. 1994). "[T]he covenant obligates the lessee to engage in marketing efforts which 'would be reasonably expected of all operators of ordinary prudence, having regard to the interests of both lessor and lessee.'" *Garman*, 886 P.2d at 659. Kansas, Oklahoma, Ohio and West Virginia also have recognized this implied duty to market. *See Gilmore v. Superior Oil Co.*, 388 P.2d 602, 606 (Kan. 1964); *Wood v. TXO Prod. Corp.*, 854 P.2d 880, 882 (Okla. 1992); *Am. Energy Servs., Inc. v. Lekan*, 598 N.E.2d 1315, 1321-22 (Ohio Ct. App. 1992); *Wellman v. Energy Res., Inc.*, 557 S.E.2d 254, 265 (W.Va. 2001); *see also* 58 CJS *Mines And Minerals* § 308 (2010) (under an oil

and gas lease, lessee generally has an implied duty to market the product). Furthermore, "[t]he reasonably prudent operator concept is an essential part of every implied covenant. Every claim of improper operation by a lessor against a lessee should be tested against the general duty of the lessee to conduct operations as a reasonably prudent operator in order to carry out the purposes of the oil and gas lease." *Amoco Prod. Co. v. Alexander,* 622 S.W.2d 563, 568 (Tex. 1981); *see Smith v. Amoco Prod. Co.*, 31 P.3d 255, 272 (Kan. 2001) (oil and gas lessee has "duty to act at all times as a reasonably prudent operator"); *SW. Gas Producing Co. v. Seale*, 191 So. 2d 115, 119 (Miss. 1966) ("great majority of jurisdictions, including Mississippi, apply the 'prudent operator' standard").

The Lease at issue in this case makes no mention of a duty on behalf of lessees to act diligently and prudently or to market any oil or gas discovered. The courts which have recognized these implied duties reason that the purpose of oil and gas leases is to "provide for the exploration, development, production and operation of the property for the mutual benefit of the lessor and lessee." *Garman,* 886 P.2d at 656 (quoting *Davis v. Cramer*, 808 P.2d 358, 360 (Colo. 1991)). The major consideration given to the lessors in oil and gas leases is a royalty interest, which pays only upon production. Furthermore, royalty interests are usually nonrisk and noncost bearing interests. Therefore, royalty owners have no control over where and when to explore for and complete wells and establish production. *See Garman*, 886 P.2d at 657. Without recognizing an implied duty on the part of the operator to act diligently and prudently, royalty owners would have no assurance of ever receiving any benefit of their bargain.

Based on the above reasoning, I hold that Virginia courts would recognize an implied duty on the part of oil and gas lessees to operate diligently and prudently, including a duty to market the gas produced. This does not mean, however, that the Virginia courts would recognize a separate cause of action for a breach of these implied duties. As explained above, the Virginia courts have held that breach of an implied duty gives rise to a breach of contract action only. *See Charles E. Brauer Co., Inc.*, 466 S.E.2d at 385. Therefore, I recommend that the court grant the Motion and dismiss Count VII of the Amended Complaint insofar as Count VII attempts to state a separate claim for breach of implied duties. Any breach of these duties may be considered as evidence of Healy's breach of contract claim found in Count VIII of the Amended Complaint.

I also am persuaded that the court should dismiss Count I of the Amended Complaint for failure to state a claim upon which relief may be granted. Count I of the Amended Complaint purports to state a claim for declaratory judgment holding that the defendants may not relitigate the plaintiff's claims under the doctrine of offensive collateral estoppel. "The Declaratory Judgment Act, 28 U.S.C.A. §§ 2201 and 2202, does not create any new substantive right but rather creates a procedure for adjudicating existing rights." *W. Cas. & Sur. Co. v. Herman*, 405 F.2d 121, 124 (8th Cir. 1968) (citing *Walker Process Equip., Inc. v. FMC Corp.*, 356 F.2d 449, 451 (7th Cir 1966)). "'(T)he operation of the Declaratory Judgment Act is procedural only.'" *Skelly Oil Co. v. Phillips Petroleum Co.*, 339 U.S. 667, 671 (1950) (quoting *Aetna Life Ins. Co. of Hartford, Conn. v. Haworth*, 300 U.S. 227, 240 (1937)); *see also City Nat'l Bank v. Edmisten*, 681 F.2d 942, 945 n.6 (4th Cir. 1982) (Declaratory Judgment Act is "remedial only"). Thus, a declaratory judgment is a remedy and not a right of

action.

Furthermore, collateral estoppel is a judicially created doctrine used to promote judicial efficiency and fairness and is not a separate claim or cause of action. *See Montana v. United States*, 440 U.S. 147, 153-54 (1979); *Ritter v. Mount St. Mary's College*, 814 F.2d 986, 994 (4th Cir. 1987). "The application of collateral estoppel precludes the relitigation of any issues 'actually litigated and necessary to the outcome of the first action.'" *Buchanan County, Va. v. Blankenship*, 496 F. Supp. 2d 715, 719 (W.D. Va. 2007) (quoting *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326 n.5 (1979)). The plaintiff bears the burden of establishing the facts she seeks to have precluded. *See Blankenship*, 496 F. Supp. 2d at 719 (citing *Dowling v. United States*, 493 U.S. 342, 350 (1990)). In this case, the plaintiff argues that the doctrine of "offensive nonmutual collateral estoppel" prevents the defendants from relitigating certain issues decided against them in a West Virginia Circuit Court in *Tawney*.[1] "Collateral estoppel is 'offensive' when a plaintiff seeks to 'foreclose the defendant from litigating an issue the defendant has previously litigated unsuccessfully,' and it is nonmutual when the party seeking to rely on the earlier ruling was not a party to the earlier proceeding and is not in privity with a party." *Collins v. Pond Creek Mining Co.*, 468 F.3d 213, 217 n.4 (4th Cir. 2006).

The court's jurisdiction in this case is based on diversity of citizenship, and the court has determined that Virginia state law controls the substantive claims raised. The defendants argue that Virginia law also should control whether the *Tawney* decision

[1]Estate of Garrison G. Tawney, et al. v. Columbia Natural Resources, LLC, et al., Case No. 03-C-10E, Circuit Court of Roane County, West Virginia (filed February 3, 2003, and tried in January 2007 to a jury verdict in favor of the plaintiffs).

precludes them from litigating certain issues in this court. *See Penn Re, Inc. v. Stonewall Ins. Co.*, 894 F.2d 402, at *2 (4th Cir. Jan. 16, 1990) (table decision) (citing *Erie R.R. Co.*, 304 U.S. 64); *see also Sims v. Hartford Accident & Indem. Co.*, 120 F.3d 265, at *3 (5th Cir. June 30, 1997) (table decision) (substantive law of the forum state regarding collateral estoppel applies in diversity case). Virginia law, they argue, does not allow nonmutual offensive collateral estoppel. *See Norfolk & W. Ry. Co. v. Bailey Lumber Co.*, 272 S.E.2d 217 (Va. 1980).

The Supreme Court, however, has held that the Full Faith and Credit Clause of the U.S. Constitution, U.S. CONST., art. IV, § 1, implemented by the Federal Full Faith and Credit Statute, 28 U.S.C.A. § 1738 (West 2006), requires a federal court to give a state-court judgment "the same preclusive effect as would be given that judgment under the law of the State in which the judgment was rendered." *Migra v. Warren City School Dist. Bd. of Educ.*, 465 U.S. 75, 81 (1984). "'It has long been established that §1738 does not allow federal courts to employ their own rules of res judicata in determining the effect of state judgments. Rather, it goes beyond the common law and commands a federal court to accept the rules chosen by the State from which the judgment is taken.'" *Ross v. Commc'n Satellite Corp*, 759 F.2d 355, 361 (4th Cir 1985) (quoting *Kremer v. Chem. Constr. Corp*. 456 U.S. 461, 481-82 (1982)). Therefore, the court must decide what, if any, preclusive effect a West Virginia court would give the *Tawney* decision.

To apply the doctrine of collateral estoppel under West Virginia law, the plaintiff must show:

> (1) The issue previously decided is identical to the one presented in the action in question; (2) there is a final adjudication on the merits of the prior action; (3) the party against whom the doctrine is invoked was a party or in privity with a party to a prior action; and (4) the party against whom the doctrine is raised had a full and fair opportunity to litigate the issue in the prior action.

State v. Miller, 459 S.E.2d 114, 120 (W. Va. 1995). Since the *Tawney* court applied West Virginia law, and the substantive claims raised in this case are controlled by Virginia law, it would appear that issue preclusion would not be available because none of the issues would be identical. *See* 18 CHARLES A. WRIGHT, ARTHUR R. MILLER & EDWARD H. COOPER, FEDERAL PRACTICE AND PROCEDURE § 4417 at 165 (1981) (not only the facts but also the legal standards and procedures used to assess them must be similar to apply issue preclusion).

Nonetheless, it appears that the plaintiff seeks to preclude relitigation of certain factual issues she claims were decided by the *Tawney* decision. The defendants argue that, even under West Virginia law, the application of the doctrine of collateral estoppel is inappropriate here because there was no final adjudication in the *Tawney* case, and they did not have a full and fair opportunity to litigate the issues in the prior action. Under West Virginia law, the fact that a case ultimately settled would not prevent it from being used to preclude relitigation of the facts determined in the case prior to settlement. *See In re McIntosh's Estate*, 109 S.E.2d 153, 158 (W.Va. 1959) (citing *Murden v. Wilbert*, 53 S.E.2d 42, 43 (Va. 1949)). In response to the Motion, the plaintiff filed with the court a copy of the parties' proposed settlement agreement in *Tawney*. (Docket Item No. 65, Att. 2.) That agreement, if approved by the court, may answer the question as to whether West Virginia courts would give the *Tawney*

decision any preclusive effect. The settlement agreement specifically stated that the court's previous rulings should have no preclusive effect because settlement was reached prior to the court's Judgment Order becoming final. If that portion of the settlement agreement was adopted by the West Virginia court, it would appear by the court's own order, the prior rulings in the case would have no preclusive effect. Whether the court adopted this language in its order approving the settlement cannot be answered based on the record before the court at this stage.

Thus, it appears that attempting to raise collateral estoppel through a separate declaratory judgment action claim is inappropriate. Therefore, I recommend that the court grant the Motion as to Count I of the Amended Complaint and dismiss that count. That does not mean, however, that the doctrine of collateral estoppel will not be applied in this case. As stated above, it is the plaintiff who bears the burden of proving which, if any, facts or issues the defendants should be precluded from relitigating.

The defendants also argue that Healy's claims for fraud (Count IV), unjust enrichment (Count V), negligence (Count VIII), breach of fiduciary duty (Count XI) and conversion (Count XII) should be dismissed because they cannot be maintained based on a breach of duties imposed by contract. To avoid allowing every breach of contract to be turned into a tort, the Virginia Supreme Court has held that "in order to recover in tort, 'the duty tortiously or negligently breached must be a common law duty, not one existing between the parties solely by virtue of the contract.'" *Augusta Mut. Ins. Co. v. Mason*, 645 S.E.2d 290, 293 (Va. 2007) (quoting *Foreign Mission Bd. of So. Baptist Convention v. Wade*, 409 S.E.2d 144, 148 (Va. 1991)). "In determining

whether a cause of action sounds in contract or tort, the source of the duty violated must be ascertained." *Richmond Metro. Auth. v. McDevitt Street Bovis, Inc.*, 507 S.E.2d 344, 347 (Va. 1998). In *Oleyar v. Kerr, Trustee*, 225 S.E.2d 398, 399-400 (Va. 1976), the Virginia court distinguished between actions for tort and contract:

> If the cause of complaint be for an act of omission or non-feasance which, without proof of a contract to do what was left undone, would not give rise to any cause of action (because no duty apart from contract to do what is complained of exists) then the action is founded upon contract, and not upon tort. If, on the other hand, the relation of the plaintiff and the defendants be such that a duty arises from that relationship, irrespective of the contract, to take due care, and the defendants are negligent, then the action is one of tort.

As this court recently recognized, this Virginia precedent does not prevent the raising of all tort claims among parties whose relationship is based on contract. *See Pre-Fab Steel Erectors, Inc. v. Stephens*, 2009 WL 891828 (W.D.Va. Apr. 1, 2009). In fact, the Virginia Supreme Court in *Richmond Metro* recognized that "a party can, in certain circumstances, show both a breach of contract and a tortious breach of duty." 507 S.E.2d at 347. It appears these cases turn on the distinction between nonfeasance or malfeasance, not simply performing as required under a contract, and misfeasance, performing a wrongful act. *See Atlas Partners II, L.P. v. Brumberg, Mackey & Wall, PLC*, 2006 WL 42332, at *8 (W.D.Va. Jan. 6, 2006) (citing *Insteel Indus., Inc. v. Costanza Contracting Co., Inc.*, 276 F. Supp. 2d 479, 485 (E.D.Va. 2003)).

This issue is often relevant in cases such as this one where the plaintiff has pled both breach of contract and fraud claims. *See City of Richmond v. Madison Mgmt.*

Group, Inc., 918 F.2d 438, 446-47 (4th Cir. 1990). In such cases, the courts also look to the distinction between "a statement that is false when made (which is fraud) and a promise that becomes false only when the promisor later fails to keep his word (which is a breach of contract)." *Hitachi Credit Am. Corp*, 166 F.3d at 631 n.9. "[A]n action based upon fraud must aver the misrepresentation of present pre-existing facts, and cannot ordinarily be predicated on unfulfilled promises or statements as to future events. Were the general rule otherwise, every breach of contract could be made the basis of an action in tort for fraud." *Lloyd v. Smith*, 142 S.E. 363, 365 (Va. 1928). The elements of actionable fraud under Virginia law are:

> ... (1) a false representation, (2) of a material fact, (3) made intentionally and knowingly, (4) with intent to mislead, (5) reliance by the party misled, and (6) resulting damage to the party misled.

Winn v. Aleda Constr. Co., Inc., 315 S.E.2d 193, 195 (Va. 1984) (citations omitted). The Virginia Supreme Court also has held "concealment, whether accomplished by word or conduct, may be the equivalent of a false representation, because concealment always involves deliberate nondisclosure designed to prevent another from learning the truth." *Spence v. Griffin*, 372 S.E.2d 595, 599 (Va. 1988).

In this case, Healy has pled that the defendants have not paid royalties as required under the Lease. Healy also has pled, however, that the defendants have made purposeful false representations as to the deductions taken, the amounts of gas produced and the prices paid for the gas. These misrepresentations, according to the Amended Complaint, were made for the purpose of concealing a scheme of self-dealing and preventing Healy and others similarly situated from discovering the

underpayments. Healy's fraud claim does not rest on the fact that the defendants did not fulfill their obligations under the contract. Healy's fraud claim rests on the allegations that the monthly accounting statements provided purposefully false information. "Under Virginia law, ... such falsities give rise to an action for fraud." *Insteel Indus., Inc.*, 276 F. Supp. 2d at 485-86; *see also Pre-Fab Steel Erectors, Inc.*, 2009 WL 891828 at *8. Therefore, I find that the Amended Complaint adequately pleads a cause of action for fraud in addition to one for breach of contract. Since that action, however, is a personal claim, as set forth above, Healy's fraud claim is limited to any fraud perpetrated against her personally.

I further find that Healy's claims for unjust enrichment (Count V), indemnification and assumption of liability (Count IX), breach of fiduciary duty (Count XI) and negligence (Count XIII) should be dismissed for failing to state a claim upon which relief may be granted.

Regarding Healy's claim for unjust enrichment, Virginia law allows a plaintiff to plead quasi-contract or implied contract theories of quantum meruit or unjust enrichment as alternative theories of liability only when the validity of an express contract is challenged. *See Cochran v. Bise*, 90 S.E.2d 178, 181-82 (Va. 1956) (quoting *Roller v. Murray*, 72 S.E. 665, 666 (Va. 1911)); *Royer v. Bd. of County Supervisors of Albemarle County*, 10 S.E.2d 876, 881 (Va. 1940) (citing *Hendrickson v. Meredith*, 170 S.E. 602, 604 (Va. 1933)). Where there is an express and enforceable contract in existence, which governs the rights of the parties, the law will not imply a contract. *See Ellis & Myers Lumber Co. v. Hubbard*, 96 S.E. 754, 760 (Va. 1918). The Amended Complaint in this case specifically alleges that the parties' relationship,

rights and obligations are set out in a valid express contract, the Lease. That being the case, I find that Healy cannot recover for unjust enrichment, and I recommend that the court dismiss Count V of the Amended Complaint.

The defendants also argue that Healy's claim for indemnification and assumption of liability in Count IX should be dismissed. In Count IX of the Amended Complaint Healy alleges that NiSource and Columbia "have agreed to indemnify Chesapeake for liability or loss arising from claims of the type asserted herein." The terms of this agreement are not contained in the Amended Complaint, and the specific agreement is not attached to or referenced in the Amended Complaint. Nevertheless, Healy claims that she and the proposed class members are third-party beneficiaries of this indemnification agreement. Under Virginia law, only intended third-party beneficiaries have standing to sue to enforce such an agreement. *See Radosevic v. Va. Intermont College*, 651 F. Supp. 1037, 1038 (W.D. Va. 1987). In order to qualify as a intended third-party beneficiary, a plaintiff must demonstrate that the contracting parties clearly and definitely intended to directly benefit her. *Norfolk-Portsmouth Newspapers, Inc. v. Stott*, 156 S.E.2d 610, 612 (Va. 1967). Courts should look to the contract itself to determine whether the contracting parties clearly and definitely intended to directly benefit a third party. *See Radosevic*, 651 F. Supp. at 1039. Healy's conclusory statement that she and the proposed class members are third-party beneficiaries, without more, simply does not allege sufficient facts to give Healy standing to sue seeking damages from NiSource and Columbia under this agreement. Therefore, I recommend that the court grant the Motion and dismiss Count IX of the Amended Complaint.

With regard to Healy's claim for breach of fiduciary duty contained in Count IX, the Amended Complaint does not allege sufficient facts to establish that the defendants owed Healy any fiduciary duty. The facts alleged in the Amended Complaint, if true, establish that Healy has a business relationship with the defendants, whereby the defendants have the right to produce coalbed methane gas from property in which Healy owns the mineral rights in exchange for paying Healy a royalty on that gas. Healy's business relationship was established by contract, and the Lease does not impose any fiduciary duties upon the defendants. Healy argues that the defendants' ongoing undertakings to handle properties and monies for Healy and others similarly situated and to provide continuing "operational, accounting and reporting services" to Healy and others puts the defendants in the position of a fiduciary.

A fiduciary relationship exists where "special confidence has been reposed in one who in equity and good conscience is bound to act in good faith and with due regard for the interests of the one reposing the confidence." *H-B Ltd. P'ship v. Wimmer*, 257 S.E.2d 770, 773 (Va. 1979). Fiduciary duties can arise either from a contractual provision or through a common law duty. *See Foreign Mission Bd. of So. Baptist Convention*, 409 S.E.2d at 148. Virginia courts have recognized fiduciary relationships between an attorney and client, an agent and principal, a trustee and beneficiary, a parent and child, and a caretaker and invalid. *See Rossmann v. Lazarus*, 2008 WL 4642213, at *7 (E.D. Va. Oct. 15, 2008). When the parties' relationship is entirely defined by contract, and the contract imposes no fiduciary duty, none exists. *See Rossmann*, 2008 WL 4642213, at *7.

"A fiduciary owes total fidelity to the interests of his principal." *State Farm*

Mut. Auto. Ins. Co. v. Floyd, 366 S.E.2d 93, 97 (Va. 1988). Simply put, a fiduciary must put the interests of his principal ahead of his own interests. While the relationship exists, the fiduciary may engage in no self-dealing which may have any adverse effect on the interests of his principal. *See State Farm Mut. Auto. Ins. Co.*, 366 S.E.2d at 97. If the alleged fiduciary has the right to protect its own interests pursuant to a contract, then no fiduciary relationship exists. *See State Farm Mut. Auto. Ins. Co.*, 366 S.E.2d at 97.

A fiduciary relationship does exist in an agency relationship. "'It is well settled that an agent is a fiduciary with respect to the matters within the scope of his agency. The very relation implies that the principal has reposed some trust or confidence in the agent. Therefore, the agent or employee is bound to the exercise of the utmost good faith and loyalty toward his principal or employer. He is duty bound not to act adversely to the interest of his employer by serving or acquiring any private interest of his own in antagonism or opposition thereto....'" *Byars v. Stone*, 42 S.E.2d 847, 853 (Va. 1947) (quoting 3 AM. JUR. 2d *Agency* § 252, p. 203.) There is no presumption of agency, however. *See Raney v. Barnes Lumber Corp.*, 81 S.E.2d 578, 584 (Va. 1954). If a party is not an agent, that party cannot be a fiduciary. *See Banks v. Mario Indus. of Va., Inc.*, 650 S.E.2d 687, 695 (Va. 2007). The power of control, or its absence, is an important consideration in determining whether an agency relationship exists. *See Reistroffer v. Person*, 439 S.E.2d 376, 378 (Va. 1994).

There are no allegations in this case that the defendants undertook to perform any functions as an agent of Healy. While the Amended Complaint alleges that the defendants, as operators, *voluntarily* undertook to provide operational, accounting and

reporting services for Healy, the Lease shows otherwise. From the language of the Lease, it is clear that the defendants performed these duties to fulfill their obligations to produce gas, account for it and pay Healy and others royalties for it. *See United States v. Bitter Root Dev. Co.*, 200 U.S. 451, 477-78 (1906) (it is doubtful that duty to report amount of timber cut creates a fiduciary relationship between licensee and property owner). The court should resist the request to turn a "garden variety, arm's length ... transaction" into a fiduciary relationship. *Diaz Vicente v. Obenauer*, 736 F. Supp. 679, 695 (E.D. Va. 1990). Furthermore, the Amended Complaint makes no allegation the Healy had the power to control the defendants' actions. Therefore, I find that Healy has not alleged sufficient facts to show that the defendants held a fiduciary duty toward her.

I further recommend that the court find that the Amended Complaint fails to state a claim for negligence and grant the Motion and dismiss Count XIII. The Virginia Supreme Court has held "losses suffered as a result of the breach of a duty assumed only by agreement, rather than a duty imposed by law, remain the sole province of the law of contracts." *Filak v. George*, 594 S.E.2d 610, 613 (Va. 2004). The court explained:

> The rationale for this rule lies in the distinctly different policy considerations distinguishing the law of torts from the law of contracts.
>
> The primary consideration underlying tort law is the protection of persons and property from injury, while the major consideration underlying contract law is the protection of bargained for expectations. Thus, when a plaintiff alleges and proves nothing more than disappointed economic expectations assumed only by agreement, the law of contracts, not the law of torts, provides the remedy for such economic losses.

Filak, 594 S.E.2d at 613 (citations omitted). This "economic loss rule" prohibits the recovery of purely economic losses in a tort action "by simply recasting a contract claim as a tort claim." *Waytec Elecs. Corp. v. Rohm and Haas Elec. Materials, LLC*, 459 F. Supp. 2d 480, 491 (W.D.Va. 2006) (citing *Sensenbrenner v. Rust, Orling & Neale, Architects, Inc.*, 374 S.E.2d 55, 57 (Va. 1988)). In this case, the defendants' obligations arise out of the Lease. Failing to perform the obligations required of the defendants under the Lease is not negligence, but a breach of contract. Therefore, I recommend that the court dismiss Count XIII of the Amended Complaint.

On the other hand, this court has recognized that, under Virginia law, a claim for conversion may be pled in conjunction with a breach of contract claim. *See Combined Ins. Co. of Am. v. Wiest*, 578 F. Supp. 2d 822, 833 (W.D.Va. 2008). "'[T]he duty not to convert the property of another for one's one purposes' exists in the absence of any contract, and thus provides the basis for an 'independent tort from the contract claims' arising out of the parties' relationship." *Combined Ins. Co. of Am.*, 578 F. Supp. 2d at 833 (quoting *Hewlette v. Hovis*, 318 F. Supp. 2d 332, 337 (E.D. Va. 2004)). Virginia law defines conversion as any distinct act of dominion or control wrongfully exerted over the property of another, either inconsistent with, or in denial of, the owner's rights. *See Simmons v. Miller,* 544 S.E.2d 666, 679 (Va. 2001); *Hairston Motor Co. v. Newsome*, 480 S.E.2d 741, 744 (Va. 1997). In this case, Healy has alleged that the defendants have wrongfully converted certain amounts of the CBM gas produced from the wells at issue for their own use without properly accounting for it or paying royalties on it. Healy also alleges that the defendants have wrongfully withheld for their own use monies owed to Healy and others similarly

situated without properly accounting for it. I find that these facts are sufficient to allege an independent cause of action for conversion, and I recommend that the court deny the Motion as to Count XII. *See PGI, Inc. v. Rathe Prods., Inc.*, 576 S.E.2d 438, 443 (Va. 2003) (any wrongful exercise over another's goods, including sums of money, in denial of the lawful owner's rights, states a claim for conversion).

The defendants also assert that Count X of the Amended Complaint should be dismissed. Count X purports to assert a claim for civil conspiracy, joint venture and/or alter-ego against the defendants. Under Virginia law, a corporation cannot conspire with its agents. "Under those circumstances, a conspiracy [is] a legal impossibility because a principal and an agent are not separate persons...." *Charles E. Brauer Co., Inc.*, 466 S.E.2d at 387. In this count, Healy alleges both that the defendants conspired to injure her, as well as that the defendants acted as mere agents for each other. In particular, the Amended Complaint alleges: "At all times alleged after February 28, 2000, CEG and Chesapeake were controlled by NiSource and were the agents, alter ego, and mere business conduits of NiSource for the acts and omissions complained of herein." (Amended Complaint at 39, ¶ 100). That being the case, no claim can prevail for any conspiracy among the defendants after February 28, 2000. "[A] single entity cannot conspire with itself." *Fox v. Deese*, 362 S.E.2d 699, 708 (Va. 1987).

Healy, however, has pled that prior to the February 28, 2000, merger, the defendants, each acting separately, conspired to enter into agreements in an effort to deprive her and others similarly situated of their rightful royalties. The defendants argue that this is insufficient to state a claim for civil conspiracy because Healy has failed to allege any underlying wrongdoing as a result of the conspiracy. Since I have

recommended that the Amended Complaint adequately states claims for breach of contract, fraud and conversion, I find that the Amended Complaint has sufficiently alleged underlying wrongdoings as a result of the conspiracy. Therefore, I will recommend that the court deny the Motion as to Count X.

The defendants also argue that Healy's claims for an accounting and prejudgment interest should be dismissed because they are remedies rather than causes of action. Whether these items should have more properly been included only in a prayer for relief than set out in separate counts of the Amended Complaint is of no concern to the court.[2] The Virginia Supreme Court has recognized that an accounting can be sought to determine what, if any, amounts are owed pursuant to a mineral lease. *See Pepper v. Dixie Splint Coal Co.*, 181 S.E. 406, 412 (Va. 1935). Furthermore, Virginia law allows prejudgment interest to be awarded. *See* VA. CODE ANN. § 8.01-382 (2007 Repl. Vol. & Supp. 2010); *Shepard v. Capitol Foundry of Va., Inc.*, 554 S.E.2d 72, 76 (Va. 2001); *Dairyland Ins. Co. v. Douthat*, 449 S.E.2d 799, 801-02 (Va. 1994). Thus, at this stage, Healy's claims for both forms of relief should remain.

Finally, the defendants argue that the Amended Complaint is defective because it seeks to certify a class which will include royalty owners whose leases include mandatory arbitration. The defendants do not assert that Healy is bound by mandatory arbitration. This case is currently before the court on the defendants' Motion To Dismiss. Whether this matter will be certified as a class action and the definition of

[2]The court notes that Healy's request for prejudgment interest also is included in her prayer for relief.

that class are matters to be determined by the court at a later date, and these matters do not require dismissal of Healy's claims.

PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

As supplemented by the above summary and analysis, the undersigned now submits the following formal findings, conclusions and recommendations:

1. The court's jurisdiction is based on diversity of citizenship;

2. The court must apply the substantive law of the forum state, including the forum state's choice of law rules;

3. Under Virginia's choice of law rules, Virginia's substantive law, including Virginia's statutes on periods of limitation, controls;

4. Under Virginia law, an action based upon a written contract must be filed within five years of accrual;

5. Under Virginia law, a cause of action for breach of contract accrues when the breach occurs;

6. Under Virginia law, a cause of action for injury to the person or damage to property accrues the date the injury is sustained;

7. Virginia's continuing undertaking rule should not be applied to the facts of this case to delay the accrual of the cause of action;

8. The Amended Complaint asserts sufficient facts to show that Healy's breach of contract claim for underpayment of royalties paid during the five years prior to the filing of this action are not barred by the statute of limitations;

9. Under Virginia law, the fraudulent concealment doctrine tolls the statute of limitations until a person who has been intentionally misled could reasonably discover the wrongdoing;

10. The Amended Complaint pleads sufficient facts to assert that the defendants' fraudulent concealment should toll the running of the applicable statute of limitations;

11. The Amended Complaint pleads sufficient facts to show that any contract claim or any claim arising out of damage to the mineral estate at issue passed to Healy;

12. Insofar as Healy raises any personal claims, such as those based on fraud, those claims must be based on the defendants' actions toward Healy, herself, and not her predecessors-in-interest;

13. The Amended Complaint pleads sufficient facts to assert a cause of action for breach of contract;

14. Virginia courts would recognize an implied duty on the part of oil and gas lessees to operate diligently and prudently, including a duty to market the gas produced;

15. Virginia courts would not recognize a separate cause of action, other than breach of contract, for breach of an implied duty;

16. Count VII should be dismissed because the Amended Complaint fails to state a claim for breach of an implied duty;

17. Count I should be dismissed because the Amended Complaint fails to state a claim for collateral estoppel;

18. Healy bears the burden at trial of proving which, if any, facts or issues the defendants should be precluded from relitigating;

19. Count IV of the Amended Complaint adequately pleads a cause of action for fraud;

20. Healy's fraud claim, as a personal action, is limited to any fraud perpetrated against her personally;

21. Count V should be dismissed because the Amended Complaint fails to state a claim for unjust enrichment;

22. Count IX should be dismissed because the Amended Complaint fails to state a claim for indemnification and assumption of liability;

23. Count XI should be dismissed because the Amended Complaint fails to state a claim for breach of fiduciary duty;

24. Count XII of the Amended Complaint adequately pleads a cause of action for conversion;

25. Count XIII should be dismissed because the Amended Complaint fails to state a claim for negligence;

26. Count X of the Amended Complaint adequately pleads a claim for civil conspiracy prior to February 28, 2000;

27. Insofar as Count X alleges a civil conspiracy based on the defendants' actions after February 28, 2000, those claims should be dismissed; and

28. Healy's claims for an accounting and for prejudgment interest are recognized by Virginia law and, therefore, should not be dismissed simply because as remedies they are not set forth in the prayer for relief.

RECOMMENDED DISPOSITION

Based on the above-stated reasons, I recommend that the court grant the Motion in part and deny the Motion in part as set forth above.

Notice to Parties

Notice is hereby given to the parties of the provisions of 28 U.S.C. § 636(b)(1)(C):

> Within fourteen days after being served with a copy [of this Report and Recommendation], any party may serve and file written objections to such proposed findings and recommendations as provided by rules of court. A judge of the court shall make a de novo determination of those portions of the report or specified proposed finding or recommendation to which objection is made. A judge of the court may accept, reject, or modify, in whole or in part, the findings or recommendations made by the magistrate judge. The judge may also receive further evidence to recommit the matter to the magistrate judge with instructions.

Failure to file written objection to these proposed findings and recommendations within 14 days could waive appellate review. At the conclusion of the 14-day period, the Clerk is directed to transmit the record in this matter to the Honorable James P. Jones, United States District Judge.

The Clerk is directed to send copies of this Report and Recommendation to all counsel of record.

DATED: This 5th day of January 2011.

/s/ *Pamela Meade Sargent*
UNITED STATES MAGISTRATE JUDGE