UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF FLORIDA
TAMPA DIVISION

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v. Case No. 8:09-cv-0087-T-26TBM

ARTHUR NADEL,
SCOOP CAPITAL, LLC,
SCOOP MANAGEMENT, INC.

Defendants,

SCOOP REAL ESTATE, L.P.
VALHALLA INVESTMENT PARTNERS, L.P.,
VALHALLA MANAGEMENT, INC.
VICTORY IRA FUND, LTD,
VICTORY FUND, LTD,
VIKING IRA FUND, LLC,
VIKING FUND, LLC, AND
VIKING MANAGEMENT,

Relief Defendants.
_____/

THE RECEIVER'S MEMORANDUM ON THE HATCHETT LEASE

Burton W. Wiand, as Receiver (the "**Receiver**") for Quest Energy Management Group, Inc. ("**Quest**"), filed a motion (Doc. 1261) on March 3, 2017 (the "**Motion**"), seeking, in relevant part, to enjoin an administrative proceeding before the Texas Railroad Commission relating to Quest's oil and gas operations under a lease (the "**Lease**") on a plot of land in Callahan County, Texas, consisting of twenty-seven tracts covering approximately 4,346.63 mineral acres (the "**Hatchett Ranch**"). While the Lease has numerous lessors, only two – John Carney and Byron Hatchett – opposed the Motion and subsequently appeared at a hearing

before the Court on March 22, 2017 (the "**March Hearing**").[1] A significant portion of the March Hearing focused on whether the Lease expired on April 15, 2016 (the "**Lease Deadline**"). At the end of the hearing, the Court directed the parties to file supplemental briefs regarding their respective positions as to whether the Lease expired.

As set forth below, Quest's drilling and reworking activities leading up to and following the Lease Deadline extended the Lease. Because the Lease continued to be in effect and Quest continued to work under the Lease, the Hatchetts' wrongful eviction of Quest from the Hatchett Ranch in October 2016 violated the Lease. The Hatchetts both failed to provide timely written notice of any purported default and failed to provide the Receiver 60 days to cure any such default, as required by the Lease. By suddenly taking these positions without notice to the Receiver after months of silence and inaction, the Hatchetts also wrongfully prevented Quest from exercising its contractual right to remove, within 120 days of termination, machinery and equipment valued at $250,000 from the Hatchett Ranch. As such, even if the Lease Deadline or Termination Letter ended the Lease, Quest's wrongful eviction from the Hatchett Ranch without written notice operated as a conversion of Quest's machinery and equipment, which violated this Court's orders (*see* Docs. 8, 2024).

[1] The original lessors under the Lease were Jim Hatchett, Sarah Hatchett, and Bill Hatchett. Along with others, John Carney and Byron Hatchett have rights under the Lease as heirs and/or assigns of the original lessors. The original lessors along with any pertinent heirs or assigns are referred to collectively herein as the "**Hatchetts**." At least one lessor, Peter Gryska, indicated to the Receiver that he did not agree with the positions taken by Messrs. Carney and Hatchett in opposition to the Motion.

BACKGROUND

As the Court is aware, this enforcement action followed the collapse of a massive Ponzi scheme (the "**scheme**") perpetrated by Arthur Nadel ("**Nadel**") through various hedge funds from 1999 until January 2009. During the course of the ten-year scheme, Nadel and his purported business partners, Neil and Christopher Moody, used scheme proceeds – *i.e.*, money stolen from investors – to found or otherwise fund numerous businesses. Quest is one such business because it was funded in large part with scheme proceeds. On March 21, 2013, the Receiver moved to expand the Receivership to include Quest (Doc. 993), and the Court granted the Receiver's motion on May 24, 2013 (Doc. 1024). Following his appointment over Quest, the Receiver notified all parties with a potential interest in Quest – including the Hatchetts – of his appointment and provided them with copies of the pertinent orders. *See* Docs. 8, 1024 (the "**Appointing Orders**").

Consistent with his duties under the Appointing Orders, the Receiver undertook significant efforts to secure Quest's assets and to preserve them for the benefit of its defrauded investors.[2] Specifically, the Receiver traveled to Texas to secure Quest's office, interviewed personnel, and examined Quest's records and assets. The Receiver also hired a forensic accountant to analyze Quest's records, which revealed that Quest was insolvent and seriously mismanaged prior to its addition to the Receivership. Quest also faced serious regulatory issues as a result of the Downeys' failure to conduct basic well maintenance. If uncorrected,

[2] The Securities and Exchange Commission eventually brought an enforcement action against Quest's former principals – Jeff and Paul Downey (collectively, the "**Downeys**") – alleging that they defrauded Quest's investors. On July 25, 2016, the U.S. District Court for the Northern District of Texas entered summary judgment against the Downeys. *See S.E.C. v. Paul R. Downey et al.*, Case No. 14-cv-00185-C (N.D. Tex. July 25, 2016).

those issues would have prevented Quest from legally operating its wells and thus prevented any potential sale to a third party. The Receiver spent considerable time and money to resolve these regulatory issues and to implement a maintenance and repair plan. The Receiver's strategy is and has always been to preserve the value of Quest's assets while also attempting to sell those assets to a third-party purchaser.[3]

On June 15, 2016, the Receiver filed a motion to initiate a claims process for Quest seeking, among other things, approval of claim forms and procedures. Doc. 1240. The Court granted that motion, established a claim bar date of October 12, 2016, and provided that any person or entity's failure to timely submit a proof of claim to the Receiver by that date barred and precluded that person or entity from asserting any claim against Quest. The Hatchetts received notice of the claims process and the appropriate forms, but none of them filed a proof of claim. *See* Declaration of Jeffrey Rizzo ("**Rizzo Decl.**"), which is being filed contemporaneously with this supplemental brief, at ¶ 10. As such, they are barred from asserting any claims against Quest.

A. The Hatchett Lease

At the time it was placed in Receivership, Quest maintained leases on three fields containing a total of 90 oil and gas wells. Eleven of those wells are subject to the Lease at issue here, which Quest executed on April 15, 2011 – more than two years before it was placed in receivership and while under the Downeys' ownership and control. The Lease carried a

[3] While Quest is one of several entities in this Receivership, the Receiver has segregated the management of its assets because it did not play a direct role in Nadel's scheme or target investors in that scheme. This segregation includes using only funds generated by Quest's assets to preserve and administer those assets.

five-year initial term with certain provisions allowing the lease to remain in force based upon various production activities. Paragraph 5 of the Lease provides, in relevant part:

> If at the expiration of the primary term, oil or gas is not being produced on said land, but Lessee is then engaged in drilling or reworking operations thereon, or shall have completed a dry hole thereon within 60 days prior to the end of the primary term, the lease shall remain in force so long as operations on said well or for drilling or reworking of any additional wells are prosecuted with no cessation of more than 60 consecutive days, and if they result in the production of oil or gas, so long thereafter as oil or gas is produced from said land. If, after the expiration of the primary term of this lease and after oil or gas is produced from said land, the production thereof should cease from any cause, this lease shall not terminate if Lessee commences operations for drilling or reworking within 60 days after the cessation of such production, but shall remain in force and effect so long as such operations are prosecuted with no cessation of more than 60 consecutive days, and if they result in the production of oil or gas, so long thereafter as oil or gas is produced from said land...

Rizzo Decl. Ex. 9 ¶ 5. In other words, the Lease would extend at the culmination of the five-year initial term if Quest was engaged in drilling or reworking operations within 60 days of the Lease Deadline. Going forward, the Lease would remain in effect should Quest continue to engage in those drilling or reworking operations absent any cessation of more than 60 days.

In addition, the Lease further provides that if Quest defaults, it is entitled to written notice of the default and 60 days to cure any noticed default. *Id*. ¶ 7. If Quest does not cure the default after receiving such written notice, the Lease affords Quest 120 days to remove its equipment from the Hatchett Ranch. *Id.* ¶ 18.

B. The Lease Did Not Terminate On The Lease Deadline Because Quest Was Engaged In "Reworking Operations" Within 60 Days Prior To That Deadline

Despite the Receiver's limited resources and the obstacles faced in dealing with Quest after the Downeys' mismanagement, Quest was engaged in significant drilling and reworking operations under the Lease during 2015 and 2016. Indeed, the Receiver, his agents, and

Quest's employees engaged in numerous discussions relating to the drilling of new wells on the Hatchett Ranch. *See* Transcript of March 22, 2017 Hearing ("**Hearing Tr.**"), attached hereto as **Exhibit A**, at 26:19-27:6. These efforts included conducting workovers on multiple wells, significant testing and repair of the wells, and extraction of dozens of barrels of oil. These activities continued in the time leading up to the Lease Deadline. The Receiver also entered into an agreement to sell Quest's gas production from the Lease in August 2015, which included the company's replacement of meters and gas lines on the property. These efforts not only preserved Quest's value to a potential purchaser but also resulted in the production of saleable oil and gas. There are currently 90 barrels of oil on hand and ready for sale (subject to certain reserve requirements or limitations). Rizzo Decl. ¶ 12.

Specifically, Quest brought multiple wells to production status beginning in October 2015. Hearing Tr. at 20:20-25-22:1-19. These efforts were initially successful, producing approximately 40 barrels of oil over the course of four months that continued until January 2016. *Id.* In mid-February 2016, Quest obtained a workover rig to work on the wells. *Id.* at 22:10-23. The workover rig was initially successful and succeeded in re-establishing the flow of oil but ultimately experienced issues with well pressure. Nevertheless, according to Chad Gray, Quest's Field Supervisor, the presence and use of a workover rig at the Hatchett Ranch was sufficient to constitute a "workover" of a well. *Id.* at 22:24-25-23:1-3. Quest was thus engaged in "reworking operations" under paragraph 5 of the Lease within 60 days of the Lease Deadline, and as a result, the Lease did not expire on April 15, 2016. At no point did the Receiver indicate any intention to idle or discontinue any of Quest's activities on the Hatchett Ranch. *Id.* at 27:12-13.

After hiring a workover rig in February 2016, Quest continued to actively engage in reworking operations. In March or April 2016, Quest began communicating with a geologist about drilling a new well. Hearing Tr. at 78:24-79:5. Several days later, on April 8, 2016, Quest commissioned testing on multiple wells, which included a sonic survey and annual fluid level testing. Rizzo Decl. ¶ 9. Quest continued these efforts, subsequently commissioning a survey of a new well location, securing a drilling rig, communicating with the Texas Groundwater Advisory Unit, having discussions with vendors and suppliers, and staking a location for a new well. Hearing Tr. at 23:8-16. Following completion of these steps, Quest applied for and received a permit to drill a new well. *Id.* at 23:16-19.

In commencing drilling operations, Quest followed the provisions of the Lease. Specifically, Section 13 of the Lease required Quest to tender $1,500 to the pertinent surface owner before drilling a new well. To fulfill this obligation, Quest sent a check on or about October 6, 2016, for $1,500 to John Carney along with related correspondence. Rizzo Decl. ¶ 6, Ex. 7. Mr. Carney is an attorney, who represented the Hatchetts in prior dealings with the Receiver. *Id.* ¶ 5, Exs. 3-6. Mr. Carney claims he never received the $1,500 check, but the Receiver sent the check to the same address Mr. Carney previously used to send and receive correspondence related to Quest. *Id.* ¶ 3, 5. Given the Receiver's correspondence with Mr. Carney and the other activities described above, he and the Hatchetts undoubtedly knew the Receiver was attempting to obtain a drilling permit and drill a new well. Mr. Carney also surely knew Quest was still engaged in such activities under the assumption that the Lease had been extended, yet he took no action to notify Quest that he (or other Hatchett lessors) considered the Lease terminated. As an attorney, Mr. Carney undoubtedly knew the prejudicial

legal impact of his inaction on Quest, which as explained below, supports the Receiver's invocation of the equitable estoppel doctrine.[4] Mr. Carney let the Receiver proceed with these efforts until the drilling was set to commence and then forced the Receiver off the Hatchett Ranch and claimed all of the Receiver's equipment and machinery for the Hatchetts.

C. The Hatchetts Unilaterally Terminated The Lease And Wrongfully Evicted Quest From The Hatchett Ranch In October 2016

On October 14, 2016, Mr. Carney sent correspondence to the Receiver on the letterhead of Hatchett Land & Development Co. LLC (the "**Termination Letter**"), copying several individuals, including Byron Hatchett and Jim R. Hatchett. Rizzo Decl. at ¶ 8, Ex. 8.[5] The Termination Letter (1) claimed that the Lease terminated on the Lease Deadline, (2) requested contact information for the Receiver's insurance carrier and bonding company as a result of "significant liabilities arising under the lease with the Hatchett family interests," (3) claimed

[4] During the March Hearing, the Court asked Mr. Carney on multiple occasions whether he was a lawyer and why he did not consult a lawyer in dealing with the Lease. *See, e.g.*, Hearing Tr. 3:16-25, 66:7-16. Mr. Carney never disclosed that he is, in fact, a lawyer with many years' experience, and he allowed the Court to believe otherwise, because he is serving a four-year suspension from practicing law for misconduct. *See* Rizzo Decl. ¶ 4, Ex. 2. Specifically, on May 21, 2015, Mr. Carney received a four-year partially probated suspension stemming from his mismanagement of client funds. *See* *http://txboda.org/cases/john-hatchett-carney-v-commn-lawyer-discipline*. In addition, the United States Department of Justice sued Mr. Carney in 2012 on allegations that he owed millions in income and employment taxes dating to 1984. This recently led to negotiations in which Mr. Carney agreed to surrender his residence in exchange for the Justice Department's agreement not to impose federal tax liens on the Hatchett Ranch. *See* *https://www.dallasnews.com/news/news/2015/03/09/dallas-attorney-who-helped-defend-john-wiley-price-to-lose-1m-house-over-taxes*.

[5] Notably, the address listed for Mr. Carney in the Termination Letter is the same address to which the Receiver sent the $1,500 check. *Id.* at ¶ 7. While the Receiver believed that Mr. Carney sent the Termination Letter on behalf of all pertinent lessors, Mr. Carney indicated for the first time at the March Hearing that he sent it only on his own behalf. Hearing Tr. at 60:9-21.

the Receiver had "no right to enter or be on the property for any reason," and (4) threatened Quest and its employees with trespassing charges:

> YOU ARE ADVISED THAT ANY ENTRY BY YOU OR ANY ONE PURPORTING TO BE ACTING ON YOUR BEHALF ONTO THE HATCHETT RANCH IS TRESPASSING. YOU HAVE FORFEITED ANY AND ALL RIGHTS TO SALVAGE ANY EQUIPMENT OR PIPELINE.

Id. The Hatchetts subsequently prohibited Quest from entering the Hatchett Ranch and informed Quest's employees they would be subject to criminal prosecution if the employees entered the land. Hearing Tr. at 25:1-11.

Prior to the Termination Letter, neither the Hatchetts nor anyone else ever notified the Receiver that they objected to Quest's continuing activities on the Hatchett Ranch or that the Lease had terminated or was otherwise no longer in effect. In fact, when Mr. Carney sent the Termination Letter, the Receiver was less than two weeks away from bringing a rig to the property to begin drilling a new well. Hearing Tr. 25:9-10. Quest also had approximately 90 barrels of oil in its holding tanks. Rizzo Decl. ¶ 12. Had the Receiver been properly notified at the Lease Deadline that the Hatchetts considered the Lease in default or otherwise terminated, he would have immediately engaged in discussions with the Hatchetts and ensured that he complied with all provisions of the Lease governing post-termination obligations (*e.g.*, curing any such default and/or removing Receivership property and equipment). As explained below, however, the Hatchetts never provided the written notice of default and opportunity to cure required by the Lease.

D. Any Purported Termination Of The Lease Was Ineffective Because The Hatchetts Never Provided The Receiver Written Notice Of A Breach Or Default Nor An Opportunity To Cure Or Retrieve Equipment

Any Purported Termination of the Lease was ineffective because the Hatchetts failed to comply with paragraph 7 of the Lease, which governs breach and default:

> **In the event of a breach or default by Lessee of any provision of this Lease, and such breach or default is not cured within 60 days of written notice to Lessee, this Lease shall terminate as to all lands covered hereby.**

Rizzo Decl. Ex. 9 ¶ 7 (emphasis added). The Hatchetts never provided Quest with written notice regarding any purported default or breach of the Lease at the Lease Deadline or at any other time before Mr. Carney sent the Termination Letter. The Termination Letter, however, did not constitute sufficient written notice under paragraph 7 because it simultaneously denied the Receiver any opportunity to cure the purported default. To the contrary, it claimed that Quest forfeited its equipment and other materials on the Hatchett Ranch and threatened its employees with criminal charges.

Similarly, pursuant to paragraph 18 of the Lease, Quest had 120 days to remove its valuable equipment and materials:

> Lessee shall, within 120 days from the date of termination of this lease, remove all surface equipment and facilities or, after said 120 day period at the option of the surface owner, such equipment and facilities shall be considered abandoned and become owned by surface owner. **It is specifically understood that wellhead and subsurface casing pipe and equipment shall remain the property of the Lessee.**

Id. ¶ 18 (emphasis added). The Hatchetts not only failed to give Quest written notice of default and an opportunity to cure, they also failed to give Quest an opportunity to retrieve its equipment and materials, which are valued between $200,000 and $250,000. To the contrary,

the Hatchetts claimed Quest forfeited all of its equipment, which is contrary to the plain language of paragraph 18. Put simply, the Hatchetts failed to comply with both paragraphs 7 and 18 of the Lease and thus wrongfully evicted Quest from the Hatchett Ranch, which prohibited Quest from performing under the Lease. But for this wrongful eviction, Quest would have continued its reworking and drilling operations. Actual drilling would have commenced within two weeks, and this entire dispute could have been avoided.

ARGUMENT

I. THE HATCHETTS WRONGFULLY REPUDIATED THE LEASE

Courts have held, in the oil and gas context, that a lessor wrongfully repudiates a contract when the "lessor tells the lessee, that he, the lessor, is the owner of the property to the exclusion of all rights formerly held or claimed by the lessee." *Red River Res. Inc. v. Wickford, Inc.*, 443 B.R. 74, 84 (E.D. Tex. 2010). This has included situations where a lessor effectively took steps wrongfully terminating the lease and preventing the lessee from entering the subject property. *See, e.g.*, *Cheyenne Res., Inc. v. Criswell*, 714 S.W. 2d 103 (Tex.App.-Eastland 1986, no writ) (lessor posted a sign on gate to leased premises notifying lessee that lease had expired); *Shell Oil Co. v. Goodroe,* 197 S.W. 2d 395 (Tex.Civ.App.-Texarkana 1946, writ ref'd n.r.e.) (lessors sent lessees letter stating that "the oil and gas lease formerly held by you ... has terminated … [t]herefore, this is to demand that you execute and forward to me a proper release of said oil and gas lease."). The doctrine of repudiation is a variation of the doctrine of estoppel. *Cheyenne Res., Inc.*, 714 S.W. 2d at 105.

The Lease remained in effect after the Lease Deadline, and the Receiver continued to work under the Lease with the Hatchetts' knowledge. They stood silent and thus failed to

provide any notice to the Receiver or Quest. Accordingly, the Termination Letter that evicted Quest from the property, informed Quest that the lease had been terminated, and forbid Quest and its agents from entering the property constituted the Hatchetts' wrongful repudiation of the Lease. As set forth in Background Section B above, Quest was engaged in numerous activities before and after the Lease Deadline that operated to extend the Lease. The Hatchetts were clearly aware that Quest was performing these activities and continuing to work the Lease based on a belief that the Lease had been extended, as the Hatchetts failed to take any action until nearly six months after the Lease Deadline to inform Quest of the purported termination. Indeed, despite Mr. Carney's claim that he never received the $1,500 check from Quest for drilling a new well, Mr. Carney sent the Termination Letter to Quest approximately one week after the Receiver sent the $1,500 check to Mr. Carney. The Receiver also filed public records regarding the Lease and Quest's development activities with the Texas Railroad Commission, which approved Quest's application to drill a new well on September 26, 2016.[6] It seems plain that Mr. Carney's letter was a reaction to the letter he received from the Receiver (or the issuance of the drilling permit and other publically filed documents related to drilling plans). By frustrating these Receiver's drilling activities and sending the Termination Letter, the Hatchetts wrongfully repudiated the Lease.

II. THE HATCHETTS FAILED TO COMPLY WITH THE LEASE PROVISIONS GOVERNING DEFAULT, CURE, AND THE RECOVERY OF EQUIPMENT

The Hatchetts' wrongful termination of the Lease violated the provisions of the Lease in paragraphs 7 and 18, governing default and the Receiver's ability to cure or to remove

[6] These records are available from the Texas Railroad Commission's online system.

equipment. As explained above in the background section, if the Receiver's activities did not satisfy the requirements of the Lease, pursuant to paragraph 7, the Receiver was entitled to written notice and a 60-day opportunity to cure any purported breach or default. It is undisputed that the Termination Letter was the only written notice Quest received about any alleged breach or default, but the Termination Letter also wrongfully evicted Quest from the Hatchett Ranch and warned Quest that any future entry onto the Hatchett Ranch would be considered trespassing. It thus denied Quest any opportunity to cure the purported breach or default in violation of paragraph 7 of the Lease. Had the Receiver been given the required opportunity to cure, rather than being prohibited from entering the property, it is undisputed that actual drilling activities would have commenced within two weeks. Hearing Tr. 25:9-10.

As also explained above in the background section, pursuant to paragraph 18 of the Lease, the Hatchetts should have afforded Quest 120 days from, at minimum, the Termination Letter to remove its valuable material and equipment, but the Hatchetts prohibited the Receiver's ability to exercise that contractual right and even threatened Quest's employees with criminal trespassing charges. In sum, the Hatchetts failure to comply with the Lease has damaged Quest through the wrongful conversion of Quest's valuable machinery and equipment for the Hatchetts' own benefit.

III. ALLOWING THE HATCHETTS TO TERMINATE THE LEASE UNDERMINES THE AUTHORITY OF THIS COURT AND THE RECEIVER

Inherent in the Court's supervision of this Receivership are broad equitable powers to determine the appropriate action to be taken in the administration of the Receivership. *See, e.g., SEC v. Elliott,* 953 F.2d 1560, 1566 (11th Cir. 1992); *SEC v. First City Fin. Corp*., 890 F.2d 1215, 1230 (D.C. Cir. 1989); *SEC v. Hardy*, 803 F.2d 1034, 1037 (9th Cir. 1986). The

Court's wide discretion derives from the inherent powers of an equity court to fashion relief. *See SEC v. Vescor Capital Corp.*, 599 F.3d 1189, 1194 (10th Cir. 2010) (concluding stay of all actions related to property held within receivership estate was well within the district court's broad equitable powers to fashion relief). An overriding purpose of an equity receivership is "to protect the estate property and ultimately return that property to the proper parties in interest," and a receiver is vested with the duty and authority to marshal and preserve assets to effectuate an orderly, efficient, and equitable administration. *Credit Bancorp, Ltd.*, 93 F. Supp. 2d at 476-77; *Vescor Capital Corp.*, 599 F.3d at 1197 (observing "in a case involving a Ponzi scheme, the interests of the [r]eceiver are very broad and include not only protection of the receivership *res*, but also protection of defrauded investors and considerations of judicial economy."); *see also* 28 U.S.C. § 754 (noting a receiver "appointed in any civil action or proceeding involving property . . . shall be vested with complete jurisdiction and control of all such property with the right to take possession thereof").

Allowing the Hatchetts to unilaterally terminate the Lease would be inequitable for at least three reasons. First, stripping the Lease from Quest's assets would cause a significant decrease in the amount Quest might be worth to a third-party purchaser, which would ultimately result in a lesser amount that might be distributed to claimants holding approved claims relating to their investment in Quest. Because the hedge funds Nadel used to defraud investors were Quest's largest creditor, those claimants holding approved claims from the hedge funds also stand to receive a proportionally smaller distribution from Quest to the hedge funds in the event the Lease is no longer included in Quest's assets.

Second, despite declining to participate in the Quest claims process (of which they were on notice), allowing the Hatchetts to divest Quest's interest in the Lease will circumvent the claims process and allow the Hatchetts – who are creditors – to obtain preferential treatment over Quest's defrauded investors.[7] This is contrary to the generally accepted principle that investors should be afforded the highest priority – and higher than general creditors – in recovering assets from a Ponzi scheme. *See, e.g.*¸ *Quilling v. Trade Partners, Inc.*, 2006 WL 3694629, *1 (W.D. Mich. 2006) (distinguishing between fraud victims and general creditors). The Court has previously applied this principle in several contexts, including by approving procedures for the claims processes that give priority to defrauded investors. *See, e.g.*, Doc. 776 (approving claims motion and subordinating general or trade creditors)

Third, as explained in the following section, equity requires that the Hatchetts should not be rewarded for their silence and inaction (*e.g.*, waiting to act until the Receiver was literally days away from new drilling) while the Receiver expended time and money to develop and maintain the Lease.

IV. THE DOCTRINE OF EQUITABLE ESTOPPEL PREVENTS THE HATCHETTS FROM CLAIMING THE LEASE TERMINATED

Equitable estoppel "is based on principles of fair play and essential justice and arises when one party lulls another party into a disadvantageous legal position." *Fla. Dep't of Health & Rehab. Servs. v. S.A.P.*, 835 So. 2d 1091, 1096 (Fla. 2002). The doctrine presupposes a legal shortcoming in a party's case that is directly attributable to the opposing party's

[7] While the exact amount of the Hatchetts' claim is unknown due to their decision not to participate in the claims process, it follows that their complete divestiture of Quest's rights to the Lease is a far greater recovery than they would have received through the claims process.

misconduct ... [and] bars the wrongdoer from asserting that shortcoming and profiting from his or her own misconduct." *Major League Baseball v. Morsani*, 790 So. 2d 1071, 1077 (Fla. 2001); *see also City of Fredericksburg v. Bopp*, 126 S.W.3d 218, 221 (Tex. App. 2003) ("equitable estoppel is based on the principle that 'one who by his conduct has induced another to act in a particular manner should not be permitted to adopt an inconsistent position and thereby cause loss or injury to the other'"). Equitable estoppel "functions as a shield, not a sword ...." *Mid-Continent Cas. Co. v. Basdeo*, 742 F. Supp. 2d 1293, 1330-31 (S.D. Fla. 2010), *aff'd* 477 Fed. Appx. 702 (11th Cir. 2012).

Equitable estoppel requires three elements: (1) a representation by the party estopped to the party claiming the estoppel as to some material fact, which representation is contrary to the condition of affairs later asserted by the estopped party; (2) a reliance upon this representation by the party claiming the estoppel; and (3) a change in the position of the party claiming the estoppel to his detriment, caused by the representation and his reliance thereon. *Travelers Indem. Co. v. Swanson*, 662 F.2d 1098, 1102 (5th Cir. 1981). An express representation is not necessary to satisfy the first element; rather, "it is enough that a representation is implied, either from acts, **silence**, or other conduct." *MDS (Canada), Inc. v. Rad Source Techs., Inc.*, 822 F. Supp. 2d 1263, 1312 (S.D. Fla. 2011) (emphasis added); *Davis v. Evans*, 132 So.2d 476, 481 (Fla. 1st DCA 1961); *see also Republic Ins. Co. v. Dickson*, 69 S.W.2d 599, 602 (Tex. Civ. App. 1934) ("A waiver or estoppel may be predicated upon the silence or inaction of the company where it is apt to mislead and does mislead[.]").

Quest conducted significant reworking and drilling activities on the Hatchett Ranch up to and after the Lease Deadline in April 2016. This included extracting oil from an injection

well, preparing a reworking rig, conducting testing, securing a drilling rig to drill a new well, and obtaining a drilling permit from the Texas Railroad Commission. Hearing Tr. at 20:20-22:23; 23:8-19; 78:24-89:5. The Hatchetts, who were undoubtedly aware of these activities given their proximity to the Hatchett Ranch, did not once contact Quest or the Receiver to voice their objections to Quest's activities or otherwise indicate they believed the Lease was terminated. Rather, they acquiesced while Quest incurred significant expenses in conducting these activities. Only upon Quest's tendering of $1,500 to John Carney in October 2016 – more than six months after the original Lease Deadline – did Quest receive any indication that the Hatchetts viewed the Lease as terminated. The Hatchetts' inaction and silence for more than six months after the April 2016 Lease Deadline suggested they did not consider the Lease expired or in default. Such inaction constitutes a representation concerning a material fact that directly contradicts the position they took six months later in the Termination Letter. It is evident that Quest relied on the Hatchetts' silence and inaction as a representation that the Lease had not terminated, as Quest continued to move forward with drilling and reworking activities. This reliance has significantly and detrimentally damaged Quest, as Quest not only spent great time and money in conducting the reworking activities but also made no effort to remove its equipment and machinery, which the Hatchetts have now wrongfully converted. In short, the Hatchetts are equitably estopped from asserting that the Lease was terminated in the face of their months of silence, inaction, and acquiescence to Quest's activities from April 2016 forward.

V. EVEN IF THE LEASE WAS TERMINATED, EQUITABLE PRINCIPLES ALSO PROHIBIT THE HATCHETTS' WRONGFUL CONVERSION OF QUEST'S EQUIPMENT FROM THE HATCHETT RANCH

As set forth in Background Section C above, Quest's eviction as a result of the Termination Letter was not only contrary to multiple provisions of the Lease but also operated to wrongfully convert Quest's valuable equipment. In the normal course of operating under the Lease, Quest needed to maintain a significant amount of machinery and drilling equipment on the property. This would have been evident not only to the Hatchetts but even to the most casual observer. Quest had no reason to proactively remove its equipment from the Hatchett Ranch prior to receipt of the Termination Letter because the Hatchetts did not provide Quest with any prior notice that they considered the Lease terminated. The Receiver understood the Hatchetts' silence and inaction following the April 2016 Lease Deadline to be an acknowledgment that Quest's efforts had extended the Lease. The Hatchetts were required to provide written notice to Quest in the event of a default or breach, and the Lease also expressly provided that Quest would have 120 days to remove all surface equipment and facilities after any termination before that equipment would be deemed abandoned. This provision specifically carved out any potential abandonment of certain valuable materials and equipment, providing that "wellhead and subsurface casing, pipe and equipment shall remain the property of Lessee." Lease at ¶ 18. By prohibiting the Receiver from removing these Receivership assets, the Hatchetts have violated the Court's Appointing Orders.

Given that the Termination Letter was Quest's first notice that Mr. Carney (and what the Receiver understood to be all Hatchett Ranch lessors) considered the Lease to be terminated, it follows that Quest had 120 days to remove its equipment and facilities as

provided in Paragraph 18. Yet, the Termination Letter made it clear that neither Quest nor its employees were permitted to re-enter the property for any reason and could potentially be subject to criminal prosecution. Even if this Court determined that the Lease terminated, equity requires that Quest not be forced to forfeit its valuable equipment and machinery as a result of the Hatchetts' deceptive conduct and failure to abide by the Lease. Holding otherwise would constitute an improper forfeiture of equipment that is estimated to have a value between $200,000 and $250,000, as of the date of the Termination Letter. If the Court should find the lease terminated, Quest requests that the Court find that Quest has not abandoned the machinery and equipment and rule that Quest be afforded a reasonable period of time to retrieve the equipment from the Hatchett Ranch. Quest should also have the ability to seek damages from the Hatchett leaseholders for any decline in value of the equipment resulting from the Hatchetts' failure to maintain or otherwise preserve the equipment from the date of the Termination Letter.

VI. THE REQUIREMENTS OF PARAGRAPHS 7 AND 18 ARE NOT AMBIGUOUS

As explained above, paragraphs 7 and 18 of the Lease required the Hatchetts to provide Quest written notice of default, 60 days to cure the default, and if unable to do so, 120 days to remove valuable equipment and materials. Those provisions are not ambiguous, but even assuming otherwise for the sake of argument, courts are clear that, in the oil and gas context, an ambiguous provision in a lease cannot be the basis for a forfeiture. *See, e.g., Dewhurst*, 55 S.W.3d 91. For example, paragraph 18 of the Lease does not specify any mechanism for providing notice to a lessee of the lease's termination that would then trigger the 120-day period for the removal of lessee's equipment. Rather, the provision indicates that the 120-day

period shall start following "the date of termination of this lease." As such, whether the 120-period runs from the Lease Deadline or the date of the Termination Letter is arguably ambiguous, but such ambiguity cannot be the basis for the forfeiture of Quest's valuable assets, including the Lease itself. The same is true for the 60-day cure period under paragraph 7.

CONCLUSION

For the foregoing reasons, the Receiver respectfully requests entry of an Order: (1) finding that Quest's reworking and drilling operations operated to extend the term of the Lease past the April 15, 2016, deadline; (2) finding that the Hatchetts' prolonged silence and inaction estopped them from later contending the Lease terminated; (3) finding that the Hatchetts wrongfully repudiated the Lease by sending the Termination Letter; (4) finding that Quest is entitled to recover all equipment, machinery, and parts belonging to it on the Hatchett Ranch; and (5) any further relief deemed just and proper.

Respectfully submitted,

/s/ Jordan D. Maglich
Michael Lamont, FBN 527122
mlamont@wiandlaw.com
Jordan D. Maglich, FBN 0086106
jmaglich@wiandlaw.com
WIAND GUERRA KING P.A.
5505 West Gray Street
Tampa, Florida 33609
T: (813) 347-5100
F: (813) 347-5199

Attorneys for the Receiver, Burton W. Wiand

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on May 5, 2017, I electronically filed the foregoing with the Clerk of the Court by using the CM/ECF system.

I FURTHER CERTIFY that on May 5, 2017, a true and correct copy of the foregoing was provided via U.S. First Class Mail to the following:

John H. Carney, Esq.
John H. Carney & Associates
5005 Greenville Ave., Suite 200
Dallas, Texas 75206

Byron W. Hatchett
Hatchett Law Firm
P.O. Box 3374
Abilene, Texas 79510

/s/ Jordan D. Maglich
Attorney