



THE ATTORNEY GENERAL OF TEXAS

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JOHN L. BILL
ATTORNEY GENERAL

April 12, 1977

The Honorable Joe C. Hanna
Texas House of Representatives
Chairman, Energy Resources
P. O. Box 2910
Austin, Texas 78769

Letter Advisory No. 136

Re: Constitutionality of
House Bill 85 which would
authorize Railroad Commission
review of proposed price re-
determination for natural gas.

Dear Representative Hanna:

You have requested our opinion concerning the constitutionality of House Bill 85. The Bill would authorize the Railroad Commission to review price increases pursuant to redetermination clauses in gas sales contracts. Such clauses generally allow increases in price when the producer, the purchaser, or in some cases a third party enters into another contract providing for a higher price. You have asked whether the Bill would violate the federal or state constitutions as an impairment of the obligation of contracts.

It is well established that the federal constitutional provision involving the obligation of contracts does not prohibit proper exercises of the state's police power. El Paso v. Simmons, 379 U.S. 497 (1965); Texas Railroad Commission v. Rowan & Nichols Oil Co., 310 U.S. 573 (1940); Viex v. Sixth Ward Bldg. & Loan Assn., 310 U.S. 32 (1939); Henderson Co. v. Thompson, 300 U.S. 258 (1937). Since the apparent intent of House Bill 85 is to protect consumers, in our view such regulation would be held to be within the police power of the state and House Bill 85 would not violate article 1, section 10 of the Federal Constitution.

The Texas Constitution provides a more difficult issue. Article 1, section 16 of the Texas Constitution provides in part:

No . . . law impairing the obligation of contracts, shall be made.

The Texas courts have applied at least two standards to challenges of statutes under article 1, section 16. In State v. Missouri K. & T. Ry. Co. of Texas, 91 S.W. 214 (Tex. 1906), the court reviewed a statute which prohibited trusts and stated:

. . . the state may, in the exercise of its police power, prohibit the continuance in the future of those things already in existence which are so injurious to the rights and interests of its citizens generally as to justify such an exercise of the power whether the continuance of the things is provided for by contract or not.

Id. at 220. This language essentially requires a balancing of the public interest against the private contractual rights. This construction of article 1, section 16 was followed for several years by the Texas courts. Lingo Lumber Co. v. Hayes, 64 S.W.2d 835 (Tex. Civ. App. -- Dallas 1933, no writ); Edgar v. McDonald, 106 S.W. 1135 (Tex. Civ. App. 1908, no writ). See Municipal Gas Co. v. Lone Star Gas Co., 259 S.W. 684 (Tex. Civ. App. -- Dallas 1924), aff'd, 3 S.W.2d 790 (Tex. 1928).

However, in Travelers' Insurance Co. v. Marshall, 76 S.W.2d 1007 (Tex. 1934), the court held unconstitutional a statute which granted stays and continuances in foreclosure actions otherwise maintainable under pre-existing contracts. The court stated that the act was in violation of article 1, section 16 for it "necessarily impairs the original obligation" Id. at 1025. The court rejected the argument that emergency measures should be exempted from the constitutional provision, and specifically ruled that statutes enacted under the state's police power are not excepted from the requirements of article 1, section 16. This ruling was followed in Hutchings v. Slemons, 174 S.W.2d 487 (Tex. 1943) and Langever v. Miller, 76 S.W.2d 1025 (Tex. 1934). These cases have been construed as prohibiting statutes "directed against the terms of contracts." Henderson Co. v. Thompson, supra; Dovalina v. Albert, 409 S.W.2d 616 (Tex. Civ. App. -- Amarillo 1966, writ ref'd n.r.e.).

These cases do not mention the Missouri K. & T. Ry. case, and it has not been overruled. In our view, the language of the Travelers' case is questionable if it is construed in its

broadest sense, and the case has not been strictly applied by courts in recent years. Few would doubt that contracts for the sale of an unregulated narcotic would prevent a valid prohibition thereof by the state, but such a result would be required under Travelers'. Since Travelers', the courts have dealt with article 1, section 16 in different ways. Some cases have turned upon whether the right affected was "vested." Texas State Board of Barber Examiners v. Beaumont Barber College, Inc., 454 S.W.2d 729 (Tex. 1970); McCain v. Yost, 284 S.W.2d 898 (Tex. 1955). In our view this standard differs from the original balancing test only in semantics. Some courts have ignored the Travelers' case and applied the balancing test. State Board of Registration for Professional Engineers v. Wichita Engineering Co., 504 S.W.2d 606 (Tex. Civ. App. -- Ft. Worth 1973, writ ref'd n.r.e.); Palmer v. Unauthorized Practice Committee of State Bar of Texas, 438 S.W.2d 374 (Tex. Civ. App. -- Houston 1969, no writ); Biddle v. Board of Adjustment, Village of Spring Valley, 316 S.W.2d 437 (Tex. Civ. App. -- Houston 1958, writ ref'd n.r.e.). In Palmer the court stated that the state's interest in the welfare of its citizens should be balanced against the private rights involved.

In our opinion the balancing test is the proper standard to apply to conflicts between the state's police power and private contractual rights. It makes little sense under any other standard to hold a statute invalid as impairing obligations of a contract where the statute affects a term in the contract while holding a statute valid which abrogates the entire contract at issue. Compare, Travelers' Insurance Co. v. Marshall, supra, with Henderson Co. v. Thompson, supra, and Dovalina v. Albert, supra. However, the Texas Supreme Court has not spoken to the question in recent years; we are unable to advise you concerning the controlling standard.

If the Texas courts apply the balancing test to House Bill 85 it would be more likely that the constitutionality of the bill would be sustained. Of course, a legislative declaration of the necessity for such legislation would be of value in any constitutional analysis.

Under the Travelers' case, House Bill 85 is much more questionable. It is clearly "directed against the terms of contract." If enacted it would authorize the Railroad Commission to reduce prices arrived at pursuant to contractual provisions.

In Humble Oil & Refining Co. v. Railroad Commission of Texas, 128 S.W.2d 9 (Tex. 1939), the court held invalid an attempt by the Railroad Commission to fix the price for sales of natural gas by a mere producer. The court states:

. . . the rate making jurisdiction of the Commission has not been extended to cover mere producers of gas who sell their product at the point of origin.

Id. at 15. The Commission's rate-making jurisdiction was held to be limited to gas utilities and pipelines. See Railroad Commission of Texas v. City of Austin, 524 S.W.2d 262 (Tex. 1975). Thus the price of gas sold by a producer which is not a gas utility is not subject to regulation by the Commission under the present statutes. However, producers of gas have long been on notice of the state's police power over its natural resources. In Gulf Land Co. v. Atlantic Refining Co., 131 S.W.2d 73 (Tex. 1939), the court stated:

. . . the business of producing . . . oil and gas is a business affected with a public interest and subject to regulation by the State.

Id. at 82. In Railroad Commission of Texas v. Rowan Oil Co., 259 S.W.2d 173 (Tex. 1953), the court noted that all property was held subject to the state's police power; diminished profits would not invalidate the proper exercise thereof. The purpose of Railroad Commission jurisdiction

is to in the end fix and effectuate just and reasonable ultimate consumer or burner tip rates for which natural gas may be sold to the public.

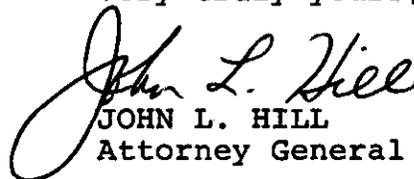
State v. Public Service Corporation of Texas, 88 S.W.2d 627, 629 (Tex. Civ. App. -- Austin 1935, writ ref'd). Thus producers of gas are at one end of a thoroughly regulated industry. They have been subject to Railroad Commission jurisdiction concerning waste. Their rates have been regulated by the Federal Power Commission. Accordingly, a court could hold that intra-state gas sales contracts are executed with a reasonable expectation that the price terms thereof might be subjected to regulation if and when such regulation is in the public interest.

In this manner House Bill 85 could be upheld even under the Travelers' doctrine. See Houston Lighting & Power Co. v. Railroad Commission of Texas, 529 S.W.2d 763 (Tex. 1975); Crystal City v. Lo-Vaca Gathering Co., 535 S.W.2d 722 (Tex. Civ. App. -- El Paso 1976, no writ); Railroad Commission of Texas v. Permian Basin Pipeline Co., 302 S.W.2d 238 (Tex. Civ. App. -- Austin 1957, writ ref'd n.r.e.), app. dismissed, 358 U.S. 37 (1958); City of Wink v. Wink Gas Co., 115 S.W.2d 973 (Tex. Civ. App. -- El Paso 1938, writ ref'd); State v. Lone Star Gas Co., 86 S.W.2d 484 (Tex. Civ. App. -- Austin 1935, writ ref'd), rev'd on other grounds, 304 U.S. 224 (1938).

We can offer no assurance that a court proceeding under the Travelers' doctrine would so view the application of the regulated industry exception to House Bill 85. The provisions of the Bill are clearly aimed at a term of a valid contract.

In short, given the use of different standards by the Texas Supreme Court, it is impossible to say with certainty whether the Bill would be upheld. We believe House Bill 85 would probably be held constitutional by a court applying the balancing standard to article 1, section 16 challenges. If the court followed the Travelers' doctrine the Bill could be upheld under the regulated industry exception, but that exception has not as yet been so broadly applied. While this presents one of the most difficult decisions regarding constitutionality with which we have been presented, we believe it is likely House Bill 85 would withstand constitutional challenge if the Legislature carefully spells out a legislative declaration of necessity and demonstrates such necessity in the legislative record.

Very truly yours,


JOHN L. HILL
Attorney General of Texas

APPROVED:


DAVID M. KENDALL, First Assistant

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A handwritten signature in cursive script, appearing to read "C. Robert Heath". The signature is written in dark ink and is positioned above a horizontal line.

C. ROBERT HEATH, Chairman
Opinion Committee

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