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2017 Feb 16 PM 2:21
CLERK OF THE GRANT COUNTY DISTRICT COURT
CASE NUMBER: 2017-CV-000003

IN THE DISTRICT COURT OF GRANT COUNTY, KANSAS

COOPER CLARK FOUNDATION, on behalf of itself and all others similarly situated, Plaintiff, v. OXY USA Inc., Defendant.	)	Case No. _____

(Pursuant to Chapter 60)

CLASS ACTION PETITION

Plaintiff brings this class action to recover royalties due on gas, and would show the Court as follows:

NATURE OF THE ACTION

1. The prior class action *Littell, et al. v. OXY USA, Inc.,* No. 98-CV-51 (Kan. Dist. Ct. Stevens Cnty) settled claims for the improper deduction of Midstream Gathering, Compression, Dehydration, and Treatment (GCDT) costs incurred before the processing plant.[1] Plaintiff and the Class bring claims based upon OXY's underpayment of royalties based on deductions taken after the processing plant inlet, all as more fully described below.

VENUE AND JURISDICTION

[1] In *Wallace B. Roderick Revocable Living Trust v. OXY USA, Inc.*, No. 2008 CV9 (Kan. Dist. Ct. Kearny Cnty.), Judge Frederick certified a state-wide class of royalty owners seeking to recover the processing deductions. OXY never appealed the order granting class certification. Instead, after Class Notice was given, OXY removed the case to federal court where Judge Melgren decertified the class in June of 2016. *Wallace B. Roderick Revocable Living Trust v. OXY USA, Inc.,* No. 12-cv-01215-EFM-GEB (ECF No. 233). The case was then dismissed without prejudice as an individual suit. *Id.* (ECF No. 239). Judge Melgren suggested that the case might have to be certified on a gas contract-by-gas contract basis. Though Plaintiff's Counsel agrees with Judge Frederick and disagrees with Judge Melgren, this case is the result.

2. This Court has both specific and general jurisdiction over Defendant because its wrongful acts occurred and caused damages to Plaintiff and Class members in this County, and Defendant is authorized to do and does or did substantial business in Kansas, both generally and specifically as to this case.

3. Venue is proper in this Court because many, if not all, of the wells, including Plaintiff's well, and royalties therefrom, are located in this County.

PARTIES

4. Plaintiff is a royalty owner in at least the Cooper C (a/k/a C-1); Cooper C-2; and Cooper C-3 (a/k/a Cooper C-3 Infill) wells from which Defendant operated and marketed gas from under a Gas Gathering Agreement, a Gas Processing Contract, and a Helium Purchase Agreement, paid royalties on gas produced, and deducted Processing costs from those royalty payments. The gas from these wells flowed over Ulysses (UGGS)/Hickok/BP (now Linn) lines to the Jayhawk Plant for processing in this County.

5. Defendant OXY USA Inc. ("OXY") is believed to be a Delaware corporation with its principal place of business in Texas, authorized to do business in the State of Kansas, and doing business in the State of Kansas. OXY can be served by serving The Corporation Company, Inc., 112 SW 7th Street, Suite 3C, Topeka, KS 66603.

a. OXY is (or was during the Class Period) in the business of producing and marketing gas and constituent products from the wells in which Class members hold royalty interests.

b. OXY was the third largest operator of natural gas wells in Kansas from 2010-2014, producing 8.6% of the total gas volume in Kansas, and sold all of its Kansas leases, wells, and assets to Merit Energy in 2014, and paid

royalties to Class members through April, 2014.

c. OXY marketed almost all of its Kansas residue gas and almost half of its NGLs through its affiliate, Occidental Energy Marketing, Inc. ("OEMI"), which OEMI then resold to third parties.

d. During the Class Period, July 1, 2007 to April 30, 2014, OXY was one of the largest gas producers in this County.

ROYALTY UNDERPAYMENT FOR GAS

6. Gas taken from Plaintiff's wells and that of all Class members contain various valuable elements and substances along with worthless and deleterious substances.

7. During the Class Period, Defendant had a working interest in each of Plaintiff's wells and that of every Class member.

8. Defendant had an implied covenant to market the valuable elements and substances contained in each lease with Plaintiff and all Class members.

9. None of the leases upon which Class Wells exist *expressly* authorized the deductions from royalty owners complained of in this case.

10. Gas, including its valuable constituent parts, from Class Wells during the Class Period was never been sold "at the well" or "at the mouth of the well."

11. Instead, all of the gas from Class Wells was first sold:

(a) as Residue after processing, to OEMI and thereafter in an arm's length transaction; or,

(b) as NGLs after processing (including TF&S), either to OEMI or to a third party.

12. To be in marketable condition, the valuable gas components must be segregated

from: (a) the raw gas stream, (b) the worthless and deleterious components, and (c) each other, to achieve the fungible quality necessary for trading in a market. The fungible product is then priced and completely sold in a real commercial market.

13. For the gas from each Class Well, this segregation into marketable products requires one or more of the following processes: (a) separation of liquids from gas; (b) Gathering; (c) Compression; (d) Dehydration; (e) Treatment; and (f) Processing (including helium processing to Grade A and TF&S for NGLs).

14. This segregation process is sometimes known as gas conditioning, field services, post-production, or Midstream Services.

15. While it is possible to "sell" gas and its valuable constituent parts before it is commercial grade or marketable condition, such as to a local irrigator, less than 2% of the gas is sold that way, and even then the products are priced at commercial grade. None of the gas from Class Wells was produced and marketed during the Class Period to be sold only to local irrigators, and none of the Class gas is sold that way, rather it is marketed under gas contracts.

16. All other gas and its valuable constituents, which includes all Class gas, was sold at commercial grade, or not sold at all but given away to the Midstream Service Provider as an in-kind fee for services.

17. Some of the gas marketing contracts fictitiously refer to paper title transfers at the gathering line inlet, but in truth, the gas (and its valuable constituents) was not and could not be sold there because, among other reasons:

a. During the Class Period, none of the gas or its constituent parts is in commercial grade at the gathering line inlet;

b. There is no fungible commercial grade market price index at the gathering

line inlet; such commercial grade market index prices only occur at the Residue Gas interstate pipeline index pool for "pipeline quality" gas that meets the FERC tariff quality, at fractionated NGL commercial quality posted pricing (known as OPIS), and at Grade A commercial grade pricing;

c. Custody transfer occurs at the gathering line inlet so that third parties, rather than OXY, can perform gathering and processing services. And the gas contracts are primarily service contracts, not the sale of goods. Without the services being rendered, there would be no sale.

d. Even if paper title transfers at the gathering line inlet was some sort of sale, at best it would be a conditional sale since no sale is completed at the custody transfer meter. Under all types of gas contracts, the sale is completed when the services and contract are completed, which always occurs at the Residue index pool and the NGL fractionation market.

e. Under some types of gas contracts (but not others), so-called paper title transfer purports to occur there, but the risk of loss and downstream gas conditioning costs remain on OXY. Likewise, the Midstream Service Provider continues to owe contractual duties to OXY after the title transfer, including the obligation to use its best efforts to sell the gas and constituent parts in the actual commercial market and remit all or most of the proceeds therefrom to OXY.

18. Even if a paper title transfer at the gathering line inlet could be considered a sale, it would be bad faith to include a title transfer clause at the gathering line inlet since the same

Midstream Services could be obtained for the same price without it.

19. Plaintiff and the Class complain in this case about not being paid the full gross value for all valuable constituents coming from Class Wells. Instead, OXY paid royalties on the net value after deducting Processing costs.

20. **Uniform Processing Deductions Taken**. In the *Littell* Settlement, OXY represented: "OXY now pays (and previously has paid) royalties on NGLs and Helium by applying the applicable royalty percentage to one hundred percent (100%) of the proceeds of sale which it receives from liquid hydrocarbons and helium ***after deducting the cost of processing*** where applicable." *See Littell* Settlement Exhibit 1, ¶ 2, P's Ex. 32C (emphasis added). Incredibly, sometimes OXY did not even pay at all for the valuable helium that came from Class Wells.

21. In addition, the gas marketing contracts refer to a sale to Occidental Energy Marketing Inc. ("OEMI"), an affiliate of OXY, which later resells NGLs and/or Residue Gas to a third party in an arm's length sale.

22. **OXY Pays Royalty Owners a Lower Affiliate Sale Price Rather than the Commercial Price**. Defendant has admitted in the *Littell* Settlement Agreement, Ex. 1, that it sells residue gas to OEMI at index price but sometimes OEMI receives higher than index price. Furthermore, "It is OXY's position that proceeds received by OEMI (when it resells the gas downstream) in excess of 100% of index price, if any, are for services provided by OEMI and are not subject to royalty."

23. Plaintiff and the Class complain in this case about being paid based on the affiliate sale price, instead of the higher arm's length third party starting price.

24. **Illegal Conservation Fee.** Defendant wrongfully deducted from royalties the

statutory Conservation Fee that it owes to help fund the KCC, but royalty owners do not owe the statutory Conservation Fee. In 2012, OXY refunded the Conservation Fees illegally deducted, due to the *Roderick* lawsuit previously filed, *see supra* n.1, but OXY did not pay interest on refunded amounts at the full 10% per annum interest.

25. Defendant settled similar claims in Kansas under *Littell* before July 1, 2007, so this case only seeks recovery for these wrongful deductions on or after July 1, 2007.

26. ***Marketable Product Rule and Good Faith.***

a. OXY may contend that the Class gas and its constituent parts are marketable products before or at the gathering line inlet so that all Midstream Service Costs are deductible, including the Processing cost disputed.

b. Plaintiff and the Class contend that the gas and its constituent parts are not marketable products until after the Midstream Services have been completed so the gas constituents are in fungible commercial grade, ready for a complete and absolute sale, in a commercial market to a third party in an arm's length transaction. Second, under the facts of this Class case, any sale before Processing would not be in good faith and would not be for the mutual benefit of lessor and lessee.

27. The *Fawcett* Case Was Decided On Concessions Not Made Here.

a. ***Fawcett* Concession #1**: "The gas in this case was sold at the wellhead." *Fawcett v. Oil Producers of Kansas, Inc.*, 352 P.3d 1032, 1039 (Kan. 2015) (quoting the Court of Appeals opinion, *Fawcett*, 306 P.3d 318, 321 (Kan.App. 2013) ("[T]he geography of the sale of gas was at the well and

the geography for the calculation of the royalty was also at the well" and stating, "The parties have taken no exception to the panel's conclusions in this regard.")). But, in this case, the location of the sale was after Processing, not at the well. All of the Class gas in this case, including Plaintiff's gas, is sold under a gas contract and an affiliate sale agreement where the sale is not completed until after the processing services have been performed and the gas products are ready for the first commercial market identified in those gas contracts—the Index pool for residue gas and the OPIS market for fractionated NGLs.

b. ***Fawcett* Concession #2**: The "at the well" language in the lease sets the valuation point. *See Fawcett*, 352 P.3d at 1036, 1039 (quoted above). That is a legal conclusion that is not conceded here, and is contrary to Kansas law. Rather, the "at the well" phrase describes the gas constituents produced "at the well" upon which the proceeds or market value royalty must be paid. Texas law interprets "at the well" to be a valuation point so that subsequent Midstream Service costs can be deducted, but Kansas law rejected that in *Sternberger*. Factually, the only gas sold "at the well" is for irrigation purposes, which constitutes less than 2% of the gas coming from Class Wells. However, irrigation gas is not within the Class because irrigation gas is not marketed under the gas contract(s) in question.

c. ***Fawcett* Concession #3**: "Fawcett does not challenge [a] OPIK's good faith, [b] its prudence in entering into the purchase agreements at issue, or [c] their material terms. Accordingly, we need not dwell further on what

this might entail." *Fawcett,* 352 P.3d at 1042 (a-c added). First, Plaintiff and the Class here do contest [a] OXY's good faith even if it tries to claim or manufacture an excuse, such as via a title transfer clause, for not paying royalty based on its actual arm's length sales after all of the Midstream Services have been performed. Second, Plaintiff and the Class do contest [b] OXY's prudence in entering into the arm's length gas contracts because the gas contracts show (i) the completion of gas sales for fungible residue and NGLs products in the commercial marketplace, but (ii) not for helium which is not sold as Grade A Helium in a commercial marketplace and is not prudent. Third, Plaintiff and the Class do not contest [c] the material terms of OXY arm's length gas contracts with third parties. But Plaintiff and the Class do contest the material terms of the affiliate sales and the failure to insist on Grade A helium payment. OXY can conduct its business as it sees fit, by doing all or part of the necessary Midstream Services itself, through an affiliate, or hiring a third party to perform the services, but OXY cannot use the affiliate and third party contract to unilaterally shift Midstream Service Costs onto royalty owners.

d. **Not Raised in *Fawcett*.** Under Kansas law, mutual consent is the only way a lessee can impose GCDTP costs on royalty owners, i.e. by Express Deduction (ED) leases. There are no ED Leases in this Class case. This issue was not raised and ruled upon by the Kansas Supreme Court in *Fawcett*, and if given the chance, without the appellate concessions listed above, the Kansas Supreme Court would likely uphold the mutual consent

rule and bar OXY and other lessees from unilaterally amending the silent leases into ED leases by the way it drafts its gas contracts, especially since title transfer clauses are not necessary to receive Midstream Services. This will be a common question of law for the entire Class.

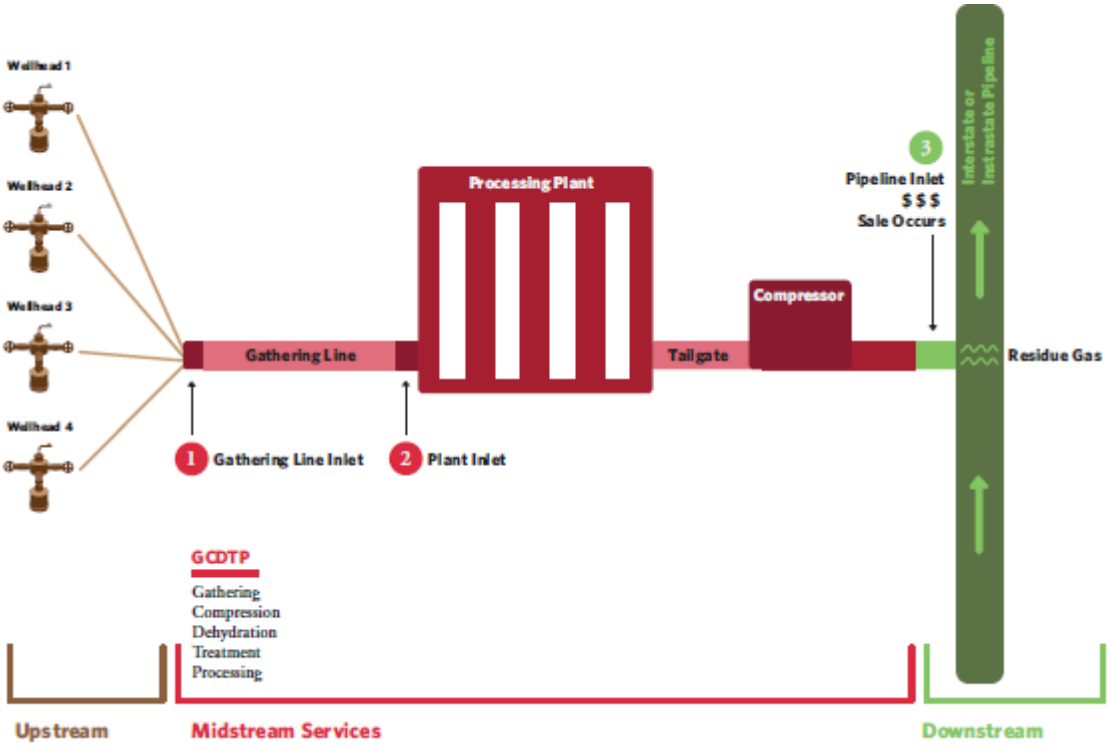
e. ***Fawcett* Requirements.** Gas quality can be a completely objective determination based on pressure, water vapor content, and gas analysis, but measured against what? *Fawcett* suggests that the quality can be measured against what a (i) true "purchaser" (a/k/a good faith sale for mutual benefit), (ii) in the "market," (iii) would "accept."

i. Under (i), A Midstream company is a service provider and is only a true purchaser if it buys the gas at the Index, OPIS, and Grade A markets. Before that, the gas sale would be a sham sale or at best a conditional sale based only on a paper title transfer, but not a completed sale. In this case, the true purchase and sale occurs at the interstate pipeline Index pool for Residue, OPIS for NGLs, and Grade A for helium. Any purported sale before that would not be in good faith or for mutual benefit.

ii. Under (ii), since a sale can be done anywhere under any circumstances, it must be done in a market, otherwise the "duty to prepare the gas for market" could be avoided. *Gilmore*, 388 P.2d at 603-04, Syl. ¶5 ("[A] lessee who fails to use reasonable diligence in finding a market for gas produced and further fails to see that such gas is prepared for market, runs the risk of causing the lease

to lapse or to be declared to be abandoned."). There is no "market" before Index, OPIS, or Grade A.

iii. Under (iii), the Midstream company does not accept any gas for the purpose of sale at the gathering line inlet, only for the purpose of gathering in a secret deal for gas conditioning to be sold later at the first real commercial market. The interstate pipeline pool is where the true purchaser accepts the gas at FERC tariff quality. The diagram below illustrates the point. The common issue is whether the sale of residue gas occurs at points 1 or 3 on the diagram. Point 1 is the gathering line inlet. No sale occurs here. Point 3 is the inlet to the interstate or intrastate pipeline. The completed sale occurs here.



Similar diagrams can be drawn for each gas product, such as helium and NGLs.

iv. **Good Faith After *Fawcett*.** The implied duty of good faith arises from the lease and prevents the lessee-defendant from exercising its discretion to improperly influence any of these (i)-(iii) factors so as to shift the burden of paying for Midstream GCDTP Costs onto royalty owners. That is exactly what defendants often try to do by including a title transfer clause in some of its gas contracts in an effort to manufacture a "sale," a "purchaser," and "market" when there are none. But OXY has made no such attempt in this Class, and the very existence of gas contracts such as those in this Class case, show that including a title transfer clause is not necessary to obtain the necessary Midstream Services and it only included as detriment to royalty owners and a benefit to lessee (violating the mutual benefit ports on the good faith duty).

28. ***Class's Residue Gas Claims*.** From July 1, 2007 to April 30, 2014, Plaintiff and the Class were underpaid royalties for Residue Gas due to deductions taken (directly or indirectly, and in cash, in kind, or both) from royalties for: (a) Residue Gas processing deductions (including but not limited to fees, retainage, plant fuel, recompression, treatment, etc.); and (b) for paying on a starting price based on the OXY/OEMI price instead of the higher OEMI/Third Party arm's length pricing.[2]

29. ***Class's NGL Claims***. From July 1, 2007 to April 30, 2014, OXY underpaid to Plaintiff and the Class royalties for NGLs due to deductions taken (directly or indirectly, and in

[2] The Residue Gas and NGL affiliate sale issue involves a marketing fee charged by OEMI which OXY claims was not deducted from royalty owners. Second, although OXY claims that OEMI did not always get a higher WASP than Index, OEMI usually did get a higher WASP price, but royalty owners never did.

cash, in kind, or both) from royalties (a) by the amount of the NGLs processing deductions (such as retainage percentage and TF&S); (b) by not receiving payment based on the full NGL recovery factors for each NGL; and (c) for paying on a starting price based on the OXY/OEMI price instead of the higher OEMI/Third Party arm's length pricing.

30. ***Class's Helium Claims***. From July 1, 2007 to April 30, 2014, OXY underpaid to Plaintiff and the Class royalties for Helium due to deductions taken (directly or indirectly, and in cash, in kind, or both) from royalties by way of: (a) Helium processing deductions; and, (b) not obtaining the Grade A Helium price.

31. ***Class's Conservation Fee Interest Claims***. From July 1, 2007 to January 1, 2012, OXY wrongfully deducted Conservation Fees from Plaintiff and the Class royalties, and thereafter did refund the wrongful deductions but without paying the 10% per annum interest.

CLASS ACTION ALLEGATIONS

32. Plaintiff brings this action individually and, pursuant to K.S.A. 60-223(a) and (b)(3), as representative of a Class defined as follows:

> All royalty owners Kansas wells: (a) where OXY USA Inc. was the operator (or, as a non-operator, separately marketed gas); (b) who were paid royalties for production of gas, NGLs, or Helium from July 1, 2007 to April 30, 2014; and (c) whose gas was moved over the ONEOK/West Texas Gas/NNG lines to the Jayhawk Plant for processing.
>
> Excluded from the Class are: (1) the Office of Natural Resources Revenue, formerly known as the Mineral Management Service (Indian tribes and the United States); (2) all presiding judge(s) together with their immediate family members; and, (3) OXY USA Inc. its affiliates, its predecessors-in-interest, and their respective employees, officers, and directors.

33. The members of the Class are so numerous and geographically dispersed that joinder of all members is impracticable. For instance, OXY has marketed Class Gas from over 20 wells, with more than one royalty owner for each well. Thus, there are more than 40 Class

members, some of whom remain in Kansas, though many others reside in numerous other states such that joinder is impracticable.

34. The questions of fact or law common to Plaintiff and the Class include, without limitation, one or more of the following:

a. Whether Plaintiff and the Class members are the beneficiaries of an implied duty to market;

b. If so, whether under *Fawcett* (without the appellate concessions), the quality of the gas, the location of the completed sale, and the actual first market are relevant factual considerations for determining whether the gas has been prepared for market;

i. Is the quality of gas a common issue provable through generalized evidence or will inquiry of individual class members be needed?

ii. Is the location of the completed sale of gas a common issue provable through generalized evidence or will inquiry of individual class members be needed?

iii. Is the market for gas a common issue provable through generalized evidence or will inquiry of individual class members be needed?

iv. Is a paper title transfer clause in a gas contract that does not transfer the subsequent risk of loss or subsequent cost, a good faith completed market sale?

c. Whether Defendant deducted (in cash or in kind) amounts for

preparing the gas for market before paying royalty to Plaintiff and the Class members.

d. Whether Defendant (including any of its affiliates) paid royalty to Plaintiff and the Class members based on a starting price below what Defendant or its affiliates received in arm's-length sales transactions;

e. Whether Defendant paid royalty to Plaintiff and the Class members for all gas constituents, such as NGLs and helium, produced from their wells.

f. Whether Kansas law imposes the Conservation Fee on Plaintiff and the Class members, and if not, whether Defendant improperly deducted Conservation Fees from royalty owners or failed to fully reimburse the royalty owners for wrongfully withheld Conservation Fee with interest.

35. Plaintiff is typical of other class members because OXY pays royalty to Plaintiff and other class members using a common method based on the net revenue OXY receives under its marketing contract(s). The marketing contract terms are unknown to and unapproved by royalty owners. The contracts are necessary to place the gas and its constituent parts into marketable condition. Plaintiff and the Class members are also typical because their leases do not contain an express provision authorizing deductions of all of the gas conditioning costs to make the gas into marketable condition, and of Conservation Fees.

36. Plaintiff will fairly and adequately protect the interests of the members of the Class. Plaintiff is a royalty owner paid by Defendant, and understand his duties as Class

representative. Plaintiff has retained counsel competent and experienced in class action and royalty owner litigation.

37. This action is properly maintainable as a class action under (b)(3). Common questions of law *or* fact exist as to all members of the Class and those common questions predominate over any questions solely affecting individual members of such Class. *See* ¶ 34 above. There is no need for individual Class members to testify in order to establish Defendant's liability or even damages to the Class.

38. Class action treatment is appropriate in this matter and is superior to the alternative of numerous individual lawsuits by members of the Class. Class action treatment will allow a large number of similarly situated individuals to prosecute their common claims in a single forum, simultaneously, efficiently, and without duplication of time, expense and effort on the part of those individuals, witnesses, the courts and/or Defendant. Likewise, class action treatment will avoid the possibility of inconsistent and/or varying results in this matter arising out of the same facts. No difficulties are likely to be encountered in the management of this class action that would preclude its maintenance as a class action and no superior alternative forum exists for the fair and efficient adjudication of the claims of all Class members.

39. Class action treatment in this matter is further superior to the alternative of numerous individual lawsuits by the members of the Class because joinder of all members of those Class would be either highly impracticable or impossible and because the amounts at stake for individual Class members, while significant in the aggregate, are not great enough to enable them to enlist the assistance of competent legal counsel to pursue their claims individually. In the absence of a class action in this matter, Defendant will likely retain the benefit of its wrongdoing.

COUNT I—BREACH OF LEASE

40. Plaintiff and the Class incorporate by this reference the allegations in paragraphs 1-39.

41. Plaintiff and the Class entered into written, fully executed, oil and gas leases with Defendant, and those leases include implied covenants including: (a) duty to market; (b) duty of good faith and fair dealing; (c) mutual benefit rule; and, (d) duty to get the best reasonable price for the gas products. Defendant entered into a gas contract to obtain the best reasonable price for gas products, but failed to pay on the full volume of gas products coming from each Class Well at that full commercial price.

42. At all material times, Plaintiff and the Class have performed their terms and obligations under the leases.

43. Defendant breached the implied covenants of the leases by its actions and/or inactions.

44. As a result of Defendant's breaches, Plaintiff and the Class have been damaged through underpayment of the actual amounts due in an amount less than $5 million, exclusive of interest and attorneys' fees.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff prays for an Order and Judgment against Defendant as follows:

a. The case be certified as a class action, with Plaintiff appointed as the class representative and Plaintiff's Counsel as Class Counsel;

b. Awarding Plaintiff and the Class damages from Defendant's breach of lease and interest at the highest allowable rate at law or equity;

c. Granting Plaintiff and the Class the costs of prosecuting this action together with

reasonable attorney's fees out of the recovery in the unlikely event that Defendant claims a statute applies which would authorize the same; and,

d. Granting such other relief as this Court may deem just, equitable and proper.

WHEREFORE, this case should be certified as a class action, Defendant should be ordered to pay Plaintiff and the Class for improper deductions, underpricing, and Conservation Fee subtractions, including pre-judgment and post-judgment interest at the highest statutory, equitable, or common law rate of 10% per annum. *See Lightcap v. Mobil Oil Corp.*, 221 Kan. 448, 468-69, 562 P.2d 1, *cert. denied*, 434 U.S. 876 (1977), and for such other relief as the Court deems proper.

Respectfully submitted,

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