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CLERK OF THE HASKELL COUNTY DISTRICT COURT
CASE NUMBER: 2016-CV-000017

IN THE DISTRICT COURT OF HASKELL COUNTY, KANSAS

COOPER CLARK FOUNDATION, on behalf of itself and all others similarly situated,	)	
Plaintiff,	)	
v.	)	Case No. 2016-CV-000017
OXY USA Inc.,	)	
Defendant.	)	

(Pursuant to Chapter 60)

FIRST AMENDED CLASS ACTION PETITION

Plaintiff brings this class action to recover royalties due on Residue Gas only,[1] 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 state-wide claims for the improper deductions from royalties. *See* Stip. of Settlement, *Littell, et al. v. OXY USA, Inc.*, No. 98-CV-51 (Kan. Dist. Ct., Stevens Cnty.) ("*Littell* Settlement"), attached hereto as **Exhibit 1**.

2. As part of the *Littell* Settlement, the *Littell* Class and OXY agreed that OXY would limit its deduction of "Gathering Charges" to $0.15/MMBtu from royalty paid for gas production after July 2007. (*Littell* Settlement ¶2.5; *see also id.* at ¶2.6). The *Littell* Settlement defines "Gathering Charges" as "all charges, expenses, or assessments, including fuel associated with any and all activities occurring between the wellhead of any well producing gas…and the inlet to any

[1] Plaintiff drops its claims for underpayment of royalty on NGLs and Helium and focuses its claims on the underpayment of royalty on Residue Gas only.

mainline transmission facility.…Gathering Charges include, but are not limited to, compression and dehydration, regardless of (1) whether such activities occurred on or off the leased premises, (2) what entity provided such services or how it is paid for, and (3) where or how title to the gas is transferred." (*Littell* Settlement ¶1.10). Plaintiff asserts no claim for Gathering Charges because OXY appears to deduct only $0.15/MMBtu from royalty as agreed under the *Littell* Settlement.

3. In other respects, however, OXY appears to violate provisions of the *Littell* Settlement, specifically:

a. OXY agreed not to deduct any "Fuel Charges" from royalty on gas produced on or after July 1, 2008. (*Littell* Settlement ¶2.4). "Fuel Charges" is defined as "gas used to operate compressors located on a Gathering Facility." (*Littell* Settlement ¶1.9). "Gathering Facility" is defined as "all activities occurring between the wellhead of any well producing gas… and the inlet to any mainline transmission facility…" (*Littell* Settlement ¶1.11). But despite these provisions, OXY continues to deduct "Fuel Lost & Unaccounted for" ("FL&U") from royalty; thereby, paying royalty on less than the full volume of gas produced from the Class Wells;

b. The *Littell* Settlement allows OXY to deduct from royalty "all fees and costs payable to third-party mainline transmission companies so long as those fees and costs are incurred pursuant to an approved FERC Tariff or at negotiated rates that are below an approved FERC Tariff for the same or similar services." (*Littell* Settlement ¶2.8). But mainline transmission costs are for transportation of Residue gas on the high pressure transmission line, in this case, at the tailgate of the processing plant after recompression so that the Residue can enter the

high pressure line. But OXY has not limited its transportation deductions to the mainline transmission lines. Instead its deductions include other undisclosed components that OXY is calling mainline transportation. This practice violates the *Littell* Settlement.

4. Apart from the *Littell* Settlement, OXY gives away gas from the Class Wells for the Midstream Service Provider to use as fuel to run its plant operations, i.e. "Plant Fuel". Processing and the Plant Fuel consumed during processing separates raw-make NGLs from Residue and is usually charged against Residue. Under the gas contract applicable in this case, title to the Residue Gas remains with OXY and never transfers to Regency Midcon Gas, LLC. [2] Under *Fawcett v. Oil Producers, Inc., of Kansas,* there is no sale, or even purported sale, before the gas is processed, making the Plant Fuel non-deductible as a processing fee.

5. Also apart from the *Littell* Settlement, OXY paid royalty on a starting price significantly less than either the Index Price or Weighted Average Sales Price ("WASP") under the OXY/OEMI contracts.

6. Additionally, given the affiliate relationship between OXY and OEMI, OXY should have paid royalty on the highest of the two starting prices (Index or WASP) at which OEMI sold the Residue Gas to third parties in arm's length transactions.

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[2] 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 based on one gathering and processing agreement, as well as the Master Service Agreement and Master Gas Sales and Purchase Agreement between OXY and its affiliate OEMI, is the result.

7. As in the original petition, Plaintiff includes the claim for interest on the amounts that OXY refunded in unlawfully withheld Conservation Fees.

8. Plaintiff and the Class bring claims based upon OXY's underpayment of royalties based on deductions taken in violation of the *Littell* Stipulation of Settlement, and taken during processing to obtain Residue, all as more fully described above and below.

VENUE AND JURISDICTION

9. 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.

10. 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

11. Plaintiff is a royalty owner in at least the Fletcher A-1; A-2; A-3; and G-3 wells in Haskell County, which Defendant operated and marketed gas from under a Gathering and Processing Agreement with Regency Midcon Gas, LLC (dated December 1, 2004), paid royalties on gas produced, and deducted Processing costs from those royalty payments.

12. 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. Service of process was obtained through OXY's resident agent, The Corporation Company, Inc. OXY has already appeared in this action.

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. During the Class Period, July 1, 2007 to April 30, 2014, OXY was one of the largest gas producers in this County. And, from 2010 to 2014, OXY was the third largest operator of natural gas wells in Kansas, producing 8.6% of the total gas volume in Kansas.

c. OXY marketed all of its Kansas residue gas to its affiliate, Occidental Energy Marketing, Inc. ("OEMI") at Index price, which OEMI then resold to third parties at WASP which was often higher than Index.

d. In 2014, OXY sold all of its Kansas leases, wells, and assets to Merit Energy Company. OXY paid royalties to Class members through April, 2014, the end date of the proposed Class Period in this case.

ROYALTY UNDERPAYMENT FOR GAS

13. Raw gas taken from Plaintiff's wells, and from the wells of all Class members, contains various valuable elements and substances along with worthless and deleterious substances.

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

15. In the leases covering the wells in which Plaintiff and the Class Members own royalty interests, Defendant had an implied covenant to market the valuable elements and substances.

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

17. Raw gas, including its valuable constituent parts, produced from Class Wells during

the Class Period was never sold "at the well" or "at the mouth of the well," but off the lease.

18. Instead, the gas from Class Wells was first sold after processing to OEMI as Residue Gas. OEMI then sold the Residue Gas in arm's length transactions to one or more third-parties to obtain generally a higher WASP price.

19. All of the Class Residue Gas produced from Class Wells is marketed, but not sold, under the December 1, 2004 gas contract between OXY and Regency Midcon Gas, LLC.

20. **OXY Paid Royalty Using Lower Affiliate Sale Price**. OXY admitted in the *Littell* Settlement Agreement, Ex. 1, that it sold Residue Gas to OEMI at Index price and that OEMI sometimes received higher than Index price when it sold the Residue Gas to third parties. OXY claimed that it was entitled to keep this differential and owed nothing to the royalty owners when OEMI received a higher than Index price. *See Littell* Settlement Exhibit 1, ¶1 ("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.").[3] However, OXY cannot use a sale to its affiliate to obtain for itself a starting price higher than the starting price on which it bases its royalty payments. The starting price on which OXY paid royalty should be the higher of the Index or WASP price that OEMI obtains in its sale of the Residue Gas in the arm's length transactions with third parties, and nothing less.

21. **Illegal Conservation Fee.** Defendant wrongfully deducted from royalties the statutory Conservation Fee that it owes to help fund the KCC. But, under *Hockett*, royalty owners

[3] OEMI charged OXY a marketing fee under the Master Services Agreement. OXY claims it did not deduct this fee from royalty owners so Plaintiff does not seek recovery of that fee. But Plaintiff does seek to recover royalty on the higher price that OEMI received even though OXY claims that OEMI did not always get a higher WASP price. But OEMI usually got a higher WASP price for the Residue Gas from Class Wells. Royalty owners should have gotten that higher price too.

do not owe the statutory Conservation Fee. *Hockett v. Trees Oil Co.*, 292 Kan. 213, 251 P.3d 65 (2011). In 2012, OXY refunded the Conservation Fees illegally deducted, due to the *Roderick* lawsuit previously filed, *see supra* n.3, but OXY did not pay interest on refunded amounts at the full 10% per annum interest. Accordingly, Plaintiff seeks to recover interests on the principal amounts refunded.

22. 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.

23. **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.*, 302 Kan. 350, 359, 352 P.3d 1032 (2015) (quoting the Court of Appeals opinion, *Fawcett*, 49 Kan. App. 2d 194, 199, 306 P.3d 318, 321 (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 Residue Gas is ready for the first commercial market identified in those gas contracts—the Index pool for Residue Gas.

b. ***Fawcett* Concession #2**: The "at the well" language in the lease sets the valuation point. *See Fawcett*, 302 Kan. at 359 (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 interpretation in *Sternberger v. Marathon Oil Co.*, 257 Kan. 315, 341, 894 P.2d 788, 805 (1995). Factually, the only gas sold "at the well" is for irrigation purposes, which is not part of this case because irrigation gas is not marketed under the gas contracts 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 [duty of good faith] might entail." *Fawcett*, 350 Kan. at 366 ([a]-[c] added). First, Plaintiff and the Class here do contest all three. [a] OXY's good faith as to royalty owners because OXY entered into gas contracts focused on its own interest in a "net" revenue stream rather than the royalty owners' right to a "gross" revenue stream and manipulated the terms of the gas contract through a premature or unnecessary title transfer clause to impose a "net" payment on royalty owners; [b] OXY's prudence in entering into the 2004 Gas Contract and OEMI Agreements because they are contrary to a prudent operator's conduct to act to mutually benefit royalty owners as well as itself and to obtain the best available price. The OEMI Agreements financially benefit only OXY by its own admission: "Prior to the formation of [OEMI], OXY determined the sales proceeds for use in the

payment of royalties…by computing a Weighted Average Sales Price received for gas produced and sold. After the formation of OEMI, in most cases the sale proceeds were determined pursuant to the contract between OXY and OEMI which used 100% of one or more published index prices…It is OXY's position that proceeds received by OEMI (when it resells the gas downstream) in excess of 100% of the index price, if any, are for services provided by OEMI and are not subject to royalty." Exhibit 1 to the *Littell* Settlement at (2). Before OEMI's formation, OXY performed the same function as OEMI; hence, there was no reason for the OEMI agreement at all, except to financially benefit OEMI/OXY when OEMI sold the Residue gas at higher than the Index price at which OXY sold the Residue to OEMI; [c] the material terms of: (i) the 2004 Regency Gas Contract because it is based on a fiction that title can be transferred to some molecules mixed within a single commingled gas stream and not others; and (ii) the material terms of the OEMI Agreements because they were completely unnecessary and used to obtain for OEMI a higher starting price for Residue than the Index price OXY provided to 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 only a few ED Leases in this case and they are excluded from the Class by definition. This issue was not raised or 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 to bar OXY and other lessees from treating leases that say nothing about the lessee's authority to deduct costs from royalty as ED leases by their drafting of gas contracts, especially because title transfer clauses are unnecessary to receive Midstream Services—as this case illustrates for Residue. This will be a common question of law for the entire Class.

e. ***Fawcett* was based on a false factual premise without factual support.** Had the undisputed fact been presented that most Kansas gas receives Midstream Services without a paper title transfer, the outcome of *Fawcett* may have been different.

24. ***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 OXY using an unfair and improper starting price by the subterfuge of an affiliate sale contract and by taking (directly or indirectly) volumetric and fee deductions occurring before any purported sale of Residue and not expressly authorized by the *Littell* Class Settlement.

25. ***Class's Conservation Fee Interest Claims***. From July 1, 2007 to January 1, 2012, OXY wrongfully deducted Conservation Fees from royalties paid to the Plaintiff and the Class. OXY thereafter refunded the wrongfully deducted amounts but paid no interest on those amounts. This action seeks recovery of interest at 10% per annum under K.S.A. 16-201.

CLASS ACTION ALLEGATIONS

26. 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 in Kansas wells from which OXY USA Inc. marketed gas production from July 1, 2007 to April 30, 2014, under Gathering and Processing

Agreement between OXY USA, Inc. and Regency Midcon Gas, LLC dated December 1, 2004, as amended.

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; (3) OXY USA Inc. its affiliates, its predecessors-in-interest, and their respective employees, officers, and directors; (4) royalty owners in the Coke A-1, Coke CDP, Jones 13-2, Jones-Ladner 13, Jones R-1, Marshall 1, McCoy 1, and McCoy 1-2 wells; and (5) royalty owners being paid under leases that provide the market value is "less a proportionate part of…the cost incurred by Lessee in delivering, processing or otherwise marketing such gas or other substances." [4]

27. The members of the Class are so numerous and geographically dispersed that joinder of all members is impracticable. OXY marketed gas from approximately 250 wells or more under the Gathering and Processing Agreement between OXY USA, Inc. and Regency Midcon Gas, LLC dated December 1, 2004, as amended ("2004 Gas Contract"). With more than one royalty owner for each well, there are more than 800 Class members. Some of these Class Members reside in Kansas, although others reside in a number of other states, making joinder impracticable.

28. 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 in their oil and gas leases;

b. Whether OXY's continued deduction of FL&U after July 1, 2008 breached the *Littell* Settlement and resulted in OXY's payment of royalty on less than the full volume of Residue Gas produced;

c. Whether OXY's deduction of transportation costs from Residue Gas

[4] The Bates numbers of these leases are: OXY-COOPER-RL-00000362; OXY-COOPER-RL-00000365; OXY-COOPER-RL-00000368; OXY-COOPER-RL-00000371; OXY-COOPER-RL-00000374; OXY-COOPER-RL-00000377; OXY-COOPER-RL-00000380; OXY-COOPER-RL-00000383.

included costs not attributable to mainline transportation;

d. Whether OXY's deduction of processing fees and plant fuel from Residue Gas occurred before the Residue Gas was sold so as to breach the implied duty to market and of good faith under *Fawcett*;

e. Whether Defendant (including any of its affiliates) paid royalty to Plaintiff and the Class members based on the lowest, rather than the highest, starting price for Residue Gas.

f. Whether Defendant owes interest on the amounts of Conservation Fee that it improperly deducted and later refunded to royalty owners.

29. Plaintiff is typical of other class members because OXY paid royalty to Plaintiff and other class members using a common method based on the net revenue OXY received under the 2004 Gas Contract and its Agreements with its affiliate OEMI. Royalty owners do not know or approve any contract terms. The 2004 Gas Contract was necessary to transform the raw gas into Residue Gas for it to be sold to OEMI. Plaintiff and the Class members are also typical because their leases contain no express provision authorizing deductions of all of the costs, both monetary and volumetric, for sale of the Residue Gas to OEMI. Plaintiff and the Class members are also typical because OXY paid them no interest on the refunded Conservation Fees.

30. Plaintiff will fairly and adequately protect the interests of the members of the Class. Plaintiff is a royalty owner paid by Defendant, and understand its duties as Class representative. Plaintiff has retained counsel competent and experienced in class action and royalty owner litigation.

31. 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* ¶28, above. Individual Class members do not need to testify in order to establish Defendant's liability or even damages to the Class.

32. 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.

33. 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

34. Plaintiff and the Class incorporate by this reference the allegations in paragraphs 1-36.

35. Plaintiff and members of the Class entered into written, fully executed, oil and gas leases with Defendant.

36. 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.

37. Defendant entered into a gas contract to obtain the best reasonable price for Residue gas (namely Index or WASP thereafter), but failed to pay on the full volume of Residue Gas coming from each Class Well at the best price available and deducted amounts not authorized under the leases or under the *Littell* Settlement.

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

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

40. 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.

COUNT II—BREACH OF *LITTELL* SETTLEMENT

41. Plaintiff and the Class incorporate by this reference the allegations in paragraphs 1-43, above.

42. In the fall of 2007, OXY and the Settlement Class of mineral interest owners in Kansas wells settled claims for royalty underpayment and agreed to certain provisions to govern the payment of royalty in the future. See Stipulation of Settlement, *Littell, et al. v. OXY USA, Inc.*, No. 98-CV-51 (Kan. Dist. Ct., Stevens Cnty.), attached as **Exhibit 1.**

43. As set forth above, OXY agreed to not deduct FL&U from gas produced after July 1, 2008 but OXY continued to do so.

44. As set forth above, OXY agreed to deduct only the actual costs for mainline transportation costs from gas produced after July 1, 2007. But OXY deducted costs that were not mainline transportation.

45. In so doing, Defendant breached the *Littell* Settlement.

46. 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. Certifying this action as a class action, with the appointment of Plaintiff as Class Representative and Plaintiff's Counsel as Class Counsel;

b. Awarding Plaintiff and the Class damages from Defendant's breach of lease and breach of the *Littell* Settlement with 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; and,

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

Respectfully submitted,

/s/ Rex A. Sharp

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CERTIFICATE OF SERVICE

I hereby certify that on the 1st day of December, 2017, a true and correct copy of the above and foregoing document was emailed to the following:

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