



**APPENDIX OF EXHIBITS TO
COMMENTS OF MOBIL OIL CORPORATION
May 28, 1997
on "Proposed Rules
Establishing Oil Value for Royalty Due on Federal Leases,
and on Sale of Federal Royalty Oil"
Department of the Interior
MINERALS MANAGEMENT SERVICE
62 Fed. Reg. 3742, January 24, 1997**

Section 1

1 FIFTH JUDICIAL DISTRICT COURT
2 COUNTY OF CHAVES
3 STATE OF NEW MEXICO
4 Case Number CV-95-322

5 CARL ENGWALL, as Co-Trustee of the
6 Carl and Ruth Engwall Living Trust
7 et al.,

8 Plaintiffs,

9 vs.

10 AMERADA HESS CORPORATION, et al.,

11 Defendants.

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TRANSCRIPT OF PROCEEDINGS

Volume 5

26 On the 17th day of January, 1997, at 8:30 AM,
27 this matter came on for hearing before the HONORABLE
28 ALVIN F. JONES, Judge of the Fifth Judicial District,
29 State of New Mexico, Division II, in Roswell, New
30 Mexico.

1 whether this case can be tried as a class.

2 I don't know what else we can say, Judge.

3 THE COURT: I am going to accept your
4 characterization of the issue as one under 703 rather
5 than the 1,006, and I will allow this to proceed over
6 objection.

7 Q. (BY MR. ZOTT) At long last, I'd like to
8 direct you to your primary findings and conclusions
9 and in particular, the question that we are here to
10 decide, at least as I understand it, is whether the
11 issue of crude oil royalty value at the lease can be
12 resolved through a common classwide method, and I
13 would like to ask you, what have you found in
14 connection with that inquiry?

15 A. Let me begin generally --

16 MR. EAVES: Could I just have a continuing
17 objection so I don't have to interpret?

18 THE COURT: Certainly.

19 THE WITNESS: I have set forth in Tab 1-1
20 of my notebook and on the board that is on the
right-hand
21 easel a bullet point summary of the main points and
22 main findings that I have reached that I will talk
23 about in my testimony.

24 proper First, as indicated on the board, the
25 method of valuing crude oil at the lease is

1 arm's-length comparable transactions. I will talk a
2 lot about that, but the heart of the matter is that
by 3 looking at outright transactions at arm's-length for
4 the comparable level of commerce under comparable
5 supply and demand conditions, one can then see what
6 the market says, what market force places of supply
7 and demand say -- marketplace forces of supply and
8 demand say about the value of crude oil at the lease.

9 Given that as a methodologic framework,
then 10 I tried to ask, if one uses a proper method of
valuing 11 crude oil in the context of a classwide analysis,
what 12 does one find? As I indicated in the second bullet,
13 arm's-length comparable transactions at the lease
14 demonstrate the influence of highly localized supply
15 and demand factors, that is the value of crude oil
16 both within and across leases, such significant
17 variation in attributes of those specific leases in
18 transactions that the marketplace picks up and is
19 valuing of crude oil as revealed by the arm's-length
20 transactions.

21 Then third, I have analyzed the
22 methodologies set forth by the plaintiffs and their
23 experts, and I believe it to be reliable.
Plaintiffs'
24 experts' proposed valuation methods cannot avoid
25 highly localized inquiry. That is that given the

1 A. Sure. If I could draw a little bit.

2 Q. Sure.

3 A. I want to try to go to the heart of what I
4 see as one of the key disputes between the parties
5 here and try to provide an economic analysis of that
6 for the Court. Let me do it in the context of a
7 representation of the plaintiffs' methodology as
8 compared to the defendants'. The plaintiffs'
9 methodologies, at least for valuing internal company
10 transfers and buy-sell transactions, begins with
trade
11 center values, typically used trade center values,
and
12 the notion is that if you engage in a buy-sell, and
13 you give up your crude at the lease but get back
14 another crude at the trade center, then that was part
15 of the compensation for your crude, and it had a
value
16 that might be reflected at the trade center.

17 So a trade center value -- the crude on the
18 receipt end of a buy-sell might have a trade center
19 value of \$22. Back at the lease, let's say that
crude
20 was transacted in the buy-sell, sold to the other
21 party, so maybe Amoco sells some of its equity crude
22 to a trading partner, anybody else on the other side,
23 at \$19. Let's just say that is the posted price for
24 the moment.

25 Then the plaintiffs' analysis looks and

1 says, well, the buy-sell has a delta or a differential

2 in it, and let's say that was a \$2 buy-sell
3 differential, leaving this to be \$20, then there is
\$1
4 left over.

5 The plaintiffs' methodology says what Amoco
6 in this hypothetical received was not \$19 for this
7 crude under the plaintiffs' methodology, but,
instead,

8 say the plaintiffs, what Amoco received was a receipt
9 crude worth \$22, then Amoco had to hand over a \$2
10 differential, so Amoco received a net of \$20 for that
11 transaction. Amoco -- the defendants say, "No, we
12 received \$19 at the lease for that transaction."

13 The heart of this dispute, Your Honor, is
14 what this \$1 represents. The plaintiffs' methodology
15 represents this \$1 difference, the measured net
16 receipts in the buy-sell, as underpayment for crude
17 oil value at the lease.

18 I believe that, in fact, what this \$1
19 represents is the downstream marketing value added in
20 this hypothetical through the vertically integrated
21 transaction between transactions at the lease and
22 transactions at a trade center. Let me say what I
23 mean by that. In the evidence that an economist
looks
24 at in trying to decide where to divide the line
within

25 Amoco, where does the production function end, and

1 where does its downstream marketing functions start?

2 We know in the industry there is a very
3 large number, as we all recognize and Mr. Johnson
4 testified about it, the hundreds of these independent
5 resellers out there who are not vertically integrated
6 back into production. Those independent resellers
7 engage in buy-sells themselves. They purchase
8 outright at the lease. They turn around and do a
9 buy-sell transaction with some other party who needs
10 the oil repositioned for their refinery.

11 So these vertically integrated companies
12 come in and buy at the lease at \$19. They then turn
13 around and do a buy-sell transaction. This is
someone
14 who has no interest in production. Hundreds of them
15 survive. What do they profit by doing so?

16 Well, in this transaction, what's gone on
is
17 let's imagine that an EOTT or a Scurlock comes in,
18 buys at \$19 and arranges the buy-sell transactions I
19 portray here. Scurlock gets back \$22 crude at the
20 trade center minus a \$2 difference, Scurlock, not an
21 integrated, an independent, gets back \$20. What is
22 that \$1 compensation? That is the \$1 that the Kochs,
23 the Scurlocks, the EOTTs, the hundreds of independent
24 sellers live off of. They receive that compensation
25 because they are -- because they are not vertically

1 integrated engaging in a marketing function which is
2 engaging in what Mr. Svenvold characterized as
3 repositioning of crude oil. That is different from
4 production.

5 The important economic content of this is
6 that if you think about the economics that we
7 encounter in tax policy, merger policy, if you have a
8 vertically integrated chain of production, the basic
9 way that economics says you go about deciding where

to

10 divide the line, in this case production and
11 marketing, is you ask what do the nonvertically
12 integrated companies earn? Those nonintegrated
13 companies earn this differential here, the \$1, not
14 buy-sell differential, and that is what is their
15 compensation for the value added downstream of the
16 lease after the production process.

the

17 Now, when you are an integrated company,

the

18 plaintiffs look at it and say, "Look at Amoco, they
19 are a production company, they received this," but
20 that is not Amoco in its role as a production company
21 because it is also very clear doing what the Kochs

and

22 Scurlocks did, that is setting up the repositioning
23 crude oil and all the marketing that goes into that.

of

24 It turns out that that is a very sophisticated

process

25 that goes on here.

1 The companies that do it maintain
everything
2 from Risk Management services, letters of credit, all
3 sorts of inputs to makes themselves viable in this
4 market.

5 The punch line or the summary of the
dispute
6 between the parties, as I see it, is that the very
7 existence of the not vertically integrated layer of
8 this industry and their ability to survive by
9 providing a useful service tells you those companies
10 aren't vertically integrated into production, they
are
11 telling you where the market divides production
12 function and downstream marketing function.

13 I think that the heart of this dispute
14 between the parties is this is compensation for
15 downstream marketing, and while in a vertically
16 integrated company who happened to produce the crude,
17 they did receive that dollar, and it is not
18 compensation for production. It is not compensation
19 for the value of crude oil at the lease. It is the
20 compensation for repositioning of crude through
21 buy-sell transactions.

22 Q. At the end, we might return to this issue.
23 This is, in essence, the same level of commerce point
24 that you are referring to here?

25 A. The parties are disputing that, and I

1 believe that the proper level of commerce is, if you
2 will, to go to the \$19 and look what transactions are
3 occurring at the lease level in outright purchases.

4 Q. Before there is any kind of downstream
5 marketing?

6 A. That is correct.

7 Q. Let's turn to the lease market at that
level
8 of commerce. First of all, Professor, I believe that
of
9 we have got some tabs here that will -- get an idea
10 what kind of a market we are talking about. I'd like
of
11 to move through these quickly. I know we are short
12 time.

13 Could you tell the Court a little bit about
14 the kind of companies that engage in this lease-level
15 market? I believe your Tab 1-3 is a list of sample
16 first purchasers, is that right? Can you tell the
17 Court a little about that?

18 A. Yes. I think, as the Court learned from
Mr.
19 Johnson, the State of New Mexico does not provide
in
20 comprehensive or systematic data on first purchases
21 New Mexico oil fields, but from the transactions
22 database, as well as from information on gatherers in
23 New Mexico, it's been possible to sample at least the
24 first purchasers that are operating in New Mexico.
25 That is shown on Tab 1-3, and they range from some of

1 systematic lists of the permitted operators in New
2 Mexico, and that is what is shown in Tab 1-5.

3 Q. What kind of -- would every one of these
4 companies be selling outright at the lease all the
5 time?

6 A. I don't think I could conclude that, no.

7 Q. With respect to this list of operators,
what
8 kind of companies do we see on that side, on the
9 selling side?

10 A. Well, you again see the production arms of
11 most of the major oil companies, integrated
companies,
12 and you also see the independent oil producer, and
13 those range from specialized companies, midsize
14 independents, the Penrocs, et cetera, some very large
15 independents, Apache, Arch, companies like that, all
16 the way down to some quite small independent
17 producers.

18 Q. Based on the nature and diversity of the
19 sellers and the buyers -- why don't we finish up the
20 tabs. Go to Tab 1-6. Can you explain to the Court
21 basically what is in Tab 1-6 and how that fits into
22 your analysis?

23 A. I wanted to illustrate for the Court the
24 nature of the business that these independent
25 resellers engage in. You will recall the company I

1 just spoke about, Ada Crude, is a division of Adams
2 Resources and Energy, Incorporated, and in their
3 annual report, Adams Resources describes the nature
of
4 their business.

5 They say that, "Crude oil is generally
6 purchased at field posted prices that fluctuate with
7 market conditions. The crude oil is transported and
8 either sold outright at the field level or the
company

9 will enter into buy-sell arrangements, trades, in
10 order to minimize transportation or to maximize the
11 sales price" -- that the reseller gets back, Adams
12 gets back.

13 "Except in certain limited situations where
14 back-to-back fixed price trades are in place, the
15 contracted sales price is also pegged to a posted
16 price that fluctuates with market conditions, thus
17 reducing the company's loss exposure from sudden
18 changes in crude oil prices. Sales of crude oil are
19 facilitated in the industry by established trade
20 points that include Cushing Oklahoma, St. James,
21 Louisiana, and Midland, Texas. A key element of the
22 company's profitability is the differential between
23 market prices at the field level and at the various
24 trade points. Such price differentials will vary
with
25 local supply and demand conditions and unforeseen

1 fluctuations in price differentials can impact the
2 company's financial results in either a favorable or
3 unfavorable manner."

4 Q. What conclusions did you draw from this? I
5 assume this isn't a unique example of an annual
report
6 of one of these independent marketers?

7 A. I don't believe it is. I think what you
are
8 seeing here is a company describing that it is not
9 vertically integrated production. It is buying other
10 people's crude and engaging in buy-sells and living
11 off of the only money left over for them to live off
12 of, that \$1 I have shown on the board.

13 Q. Incidentally, I note this publicly
available
14 annual report refers to buy-sell agreements. Are you
15 aware of any concealment of those transactions based
16 on the data you reviewed?

17 A. No. I have been aware of buy-sells since
18 the 1970's from public information.

19 Q. Now, we have got two annual reports. Can
20 you tell the Court -- the next one is Falco, how that
21 plays into your analysis or what significance this
22 annual report has for you?

23 A. Well, what I have shown in Tab 1-6, which
24 comes from another one of these marketers in this
25 case, in this case Falco, is how these firms operate.

1 These firms play, from an economic point of view, an
2 important role in keeping the market running, keeping
3 buyers and sellers engaged and able to transact with
4 each other, perhaps notwithstanding different levels
5 of sophistication, and the way they do it is they go
6 out and chase business. That is their job. They are
7 the middlemen that do that.

believe

8 They say in their annual report, "We

9 the key factor for our success is Falco's ability to
10 buy lease production. The philosophy behind our
11 success in this area is simple but effective:
12 Establish and maintain relationships with the
13 operators, pay competitive prices, and above all else
14 provide the best service in the industry. Any
15 operator who receives a new permit will also receive

a

16 letter from Falco in which we wish the operator
17 success in his venture and inform him of Falco's
18 capability and desire to provide their service.
19 Following this letter, the lease buyer makes a
20 personal visit and/or phone call to the operator in
21 order to reaffirm our interest in providing service.
22 The lease buyers spend a large percentage of their
23 time visiting prospective customers."

24 Falco, in other words, is a company whose
25 corporate strategy is one of direct personal contact

1 with operators.

2 Q. Without moving through the EOTT brochure
3 that you have there, I think we can not read through
4 it, but in the interest of time --

5 A. I included this in the notebook, Your
Honor,
6 to give you an illustration of a slightly different
7 corporate strategy by the marketers. I am sure EOTT
8 would say they also try to provide personal service,
9 but EOTT, which is a division of Enron Corporation --
10 the whole corporation is known for, in economist
11 jargon, marketing contractual designs, and you will
12 see, this is called their smart pricing brochure,
13 where they are out trying to strike contracts with
14 producers and convince the producer that they offer
an
15 interesting portfolio or selection of types of
16 contracts by which to conduct the producer's business
17 and sell the producer's crude.

18 Q. Then we have the last part of Tab 1-6,
which
19 looks like it is something you got off the Internet?

20 A. Yes.

21 Q. What is this?

22 A. Well, in the course of the depositions in
23 this case, there was discussion of -- the plaintiffs
24 have computers on their tables or whatever, more
25 generally, access to information, so I asked one of
my

1 staff to go on the Internet and see what they found,
2 and this is the kind of thing they came back with.
3 This is Mr. Lasser who, as best we can understand, is
4 a broker, does not take title like a reseller does,
5 apparently performs more of the kinds of functions I
6 think Mr. Johnson's firm does of providing
information
7 for a fee as opposed to taking title and all the
risks
8 thereof in arranging all the transactions.

9 These are the kinds of people -- mechanisms
10 by which these people chase the business of producers
11 and operators who have crude oil to sell.

12 Q. You were here, I am sure, when Mr. Johnson
13 claimed that the resellers frequently will buy from
14 the uninformed small producer and therefore will get
a
15 lower price because they are really buying from
16 uninformed, unsophisticated parties.

17 What is the nature of the market that you
18 have just shown the Court with respect to sellers and
19 buyers? How does that square with Mr. Johnson's
20 assertion?

21 A. It is certainly plausible, and I would have
22 no doubt that on the seller side of the lease level
23 market, we see varying degrees of sophistication and
24 capacity. From an economic perspective, the very
25 reason for the existence and the role, economically,

1 that these independent resellers, as well as the
2 brokers, play, as well as the integrated marketing
3 arms of the major oil companies, is that through the
4 process of chasing the business through these various
5 mechanisms, they are the mechanisms by which buyers
6 and sellers are linked up together through a
7 competitive process that is interjecting the
8 information that protects the seller in this case, as
9 this is sort of a seller beware kind of setting.

drawn 10 I believe the correct conclusion to be

11 is that that is a market that works well in terms of
12 allowing willing buyers and willing sellers to meet
13 with opposing economic interests and satisfy that
14 arm's-length transaction criteria that I set forth in
15 1-2.

you 16 Q. Okay. Now, you testified yesterday that

17 are an expert and have substantial expertise in the
18 area of antitrust economics.

would 19 I don't want to dwell on the point. I

20 just like to ask you -- Mr. Johnson testified that
21 these defendants have, quote, tremendous market
22 unquote; and Mr. Eaves referred in his opening to the
23 collective economic power of these defendants to
24 manipulate prices.

25 What does the data, in the nature of the

1 A. Yes. Your Honor, as I indicated, I began
2 with a hypothesis that it was possible that supply
3 demand factors varied from lease-to-lease and from
4 transaction-to-transaction; and that, given the
5 economics of supply and demand, with those factors
6 varying, then it was then possible that those supply
7 and demand factors would be reflected as a range,
8 rather than a common price, for all arm's-length
9 comparable transactions at the lease.

10 Plaintiffs' experts' proposed valuation
11 methods cannot avoid highly localized inquiry, and
12 what this second bullet on Tab 1-1 goes into, if you
13 look at the data on actual arm's-length comparable
14 transactions, you do indeed find that those
15 transactions at the lease demonstrate the influence
16 highly localized supply and demand factors, and in a
17 quite substantial way -- that is, in magnitudes that
18 matter.

19 THE COURT: We're going to take about ten
20 minutes at this time.

21 MR. ZOTT: Thank you, Your Honor.

22 (Recess held.)

23 THE COURT: Be seated.

24 MR. ZOTT: Proceed?

25 THE COURT: Please.

1 method that would yield an accurate value across the
2 field. Let's start with that.

3 Let's begin with your primary conclusion as
4 reflected on Tab 3-1.

5 A. Sure.

6 What I've tried to show here, and what I
7 want to talk about, obviously, is I believe that when
8 one examines the methodologies put forth by the
9 plaintiffs, particularly those for valuing
10 arm's-length -- I'm sorry, valuing internal company
11 transfers and buy-sell or exchange agreements --

12 Q. Let me stop you.

13 What methodologies of the plaintiffs -- as
14 you understand it, what is it they are contending in
15 terms of methodologies? We've heard of a lot of
16 different methodologies.

17 A. I think -- with respect to outright
18 transactions at the lease, outright sales and
19 purchases, I think that the methodology would -- as I
20 understand it, would look at arm's-length
comparables,
21 would look and see if they were really outright.

22 There were some opinions voiced by the
23 plaintiffs' experts that they would then also check
24 those against a net-back by looking at trade center
25 values, minus transportation, sulfur and gravity

1 adjustments.

2 With respect to arm's-length transactions

--

3 I'm sorry, internal company transfer transactions, as

would

4 I understand the plaintiffs' methodologies, they

5 look at representative trade center values and from

6 that gather a data set on buy-sell differentials and

7 use something like the average of those buy-sell

to

8 differentials to arrive -- that board behind 3-1 --

9 arrive at that \$22 minus \$2 as their method of

10 valuation.

11 Then with respect to buy-sell transactions,

12 as I understand it, they would go to those buy-sell

13 transactions, and, if possible, trace the crude to a

value,

14 trade center, if possible to use a trade center

15 and deduct the buy-sell differential from that

16 buy-sell transaction, the sort of \$22 minus \$2

17 calculation that I showed on the board with my

18 handwriting on it.

19 Q. You understand the term net-back or
net-back

20 methodology?

21 A. I understand how the parties are using it,

22 yes.

23 Q. And as you understand the term, are any of

24 those methods an impact method from a downstream

25 value?

1 Q. Are we at Tab 3-2? Is that where we're
2 going?

3 A. Yes.

4 Q. Okay.

5 A. If I could say one thing.

6 Q. Shall I move this over?

7 A. Yes. I believe that the plaintiffs'
8 methodologies are unable to capture field level
supply
9 and demand factors.

10 This methodology -- for example, think of
11 using trade center values for internal company
12 transfers, subtracting off buy-sell differentials, an
13 average buy-sell differential, but down there at the
14 lease level, there is a lot of variation, as we've
15 already seen, in the actual value of crude oil
16 reflecting specific supply and demand factors in
17 specific transactions and leases.

18 So that valuing transactions in that way
19 from a trade center price, subtracting an average
20 buy-sell differential, just would not pick up that
21 variation; and, hence, if you wanted to accurately
22 value the crude, one would want to compare its
23 attributes and the property of the attributes to,
24 instead, arm's-length comparables, where you can pick
25 up those kinds of things, such as the Southwest

1 Q. This has been a source of discussion
2 throughout the case.

3 Can you just tell the Court, very briefly,
4 what we're seeing here?

5 A. What I've tried to do is provide an
6 illustration of the kinds of sources of value added
7 that goes on in the marketing function, whether it's
8 vertically integrated into one of the majors or not.

9 What I've shown here, and I won't read
10 through the whole thing, is the kinds of functions --
11 I think it was the independent marketers buying
12 outright, turning around and taking the crude away
13 from the lease, perhaps in a buy-sell or perhaps
14 transporting itself, and it ranges from -- ranging
for
15 gathering and transporting, ranging for storing,
16 either at receipt or delivery points, it involves the
17 development of marketing and market information and
18 expertise regarding types of crude oil as to what
19 customers like what kinds of crude oil, how to handle
20 transactions costs.

21 An important component is the assuming and
22 managing of risk. To give you an illustration, that
23 Falco Company that we looked at earlier, one of the
24 independent marketers, highly sophisticated business,
25 but bearing lots of risks, goes to Banque Paribas, a

1 transfers, that is the proposed mechanism for valuing
2 what they call the proceeds from the production of
the
3 crude oil.

4 Q. Why don't we turn, then, to what some of
the
5 plaintiffs' experts have actually -- how they've
6 tried
7 to account for this dollar that we've been talking
8 about colloquially.

9 First, you've got a quote from Dr.
McDonald,
10 he's the plaintiffs' economic expert whose deposition
11 was taken, and I have a sense we're not going to be
12 hearing from him, but why don't you tell me what he
13 had to say about that?

14 A. Well, Mr. McDonald is quizzed, Tab 3-4, "Is
performing
15 it possible that the Kochs or Scurlocks are
16 a service as a marketer and as a merchant that the
17 market values?"

18 "A. That would be one explanation."

19 "Q. Do you have any others?"

20 "A. No."

21 Q. How about Mr. Johnson, what did he have to
22 say about the marketing function that accounts for
23 that dollar?

24 I think we've probably gone over this
Tab
25 before, so we can just direct the Court -- this is
3-4?

1 them over the full year?

you

2 A. Well, if you look at the differences that
3 are sustained over a year and get yearly averages,
4 find sustained values of fairly large amounts and
5 sustained runs over multiple years for these -- where
6 these two prices -- the NYMEX and the P plus are not
7 running together.

them

8 I did the calculations and didn't write
9 down.

10 Q. I did.

11 A. Okay.

12 Q. I wrote them down.

13 A. It's faster if you did.

14 Q. I wrote them down.

15 A. And I verified them.

16 Q. Here we go. Can you see it?

17 A. Yes.

18 So what you see here is that in 1990, the
19 NYMEX is above the -- I'm sorry, is below the P plus
20 by about 72 cents a barrel, and then the NYMEX stays
21 above for three consecutive years the P plus, 68
22 cents, 10 cents, 81 cents, over '91, '92 and '93, and
23 then they switch again and the P plus is higher than
24 the NYMEX by 31 cents.

25 Q. Okay. Now, before we get to the

1 significance of that to this case, let me ask you,
2 we're now comparing basically, as I understand it,
two
3 prices for delivery at Cushing, Oklahoma.

4 A. Yes, that's correct.

5 Q. Are there also -- what do you observe if
you
6 compare market trading centers?

7 We've heard a lot about Midland and we've
8 heard a lot about Cushing. What happens if you look
9 between trade centers rather than at the same trade
10 center?

11 A. Sure. If you look at Tab 3-6 -- I don't
12 think I prepared a big board on this -- but you'll
see
13 a comparison of the Midland and Cushing WTI spot
14 prices.

15 Q. Okay. What is that, then? What are those
16 prices? Just describe what we're talking about.

17 A. Sure. What you're seeing here is the
18 Midland minus Cushing difference on the Platt's
19 reported WTI spot. It's a difference.

20 So the vertical axis is showing you the
21 delta between them over the period January of 1988 to
22 January of 1996.

23 Again, in this case, you see across trade
24 centers that the selection of prices shows the same
25 kind of volatility and sustained differences over

1 sustained periods of time.

2 Also note that in this figure that were
3 these two trade centers reflecting the same supply
and
4 demand conditions -- in other words, if you didn't
5 have to look any farther than trade centers to pick
up
6 the localized supply and demand forces, one would
have
7 anticipated that these prices should only differ by
8 the transportation cost difference between Midland
and
9 Cushing.

10 Q. Do they?

11 A. That's not a plausible consequence here.
12 There is a positive transportation cost from
13 Cushing -- from Midland to Cushing, and even though
14 you might have seen some variations in the
15 transportation cost, you've never seen them switching
16 positive to negative, there would always be a
positive
17 difference between them.

18 Q. So then, I think you've made it clear, but
19 what accounts for these differences?

20 A. The reasonable conclusion to be drawn is
21 that even at trade centers one sees different
22 localized supply and demand factors that are specific
23 to that trade center and make it different from the
24 trade center, and based on my evidence, also
different
25 from the supply and demand factors that one sees

Section 2

FIFTH JUDICIAL DISTRICT COURT
COUNTY OF CHAVES
STATE OF NEW MEXICO

FIFTH JUDICIAL DISTRICT
CHAVES COUNTY
FILED

97 MAR 26 PM 1:19

BEE J. CLEM
CLERK DISTRICT COURT

CARL ENGWALL, as Co-Trustee of
the Carl and Ruth Engwall Living
Trust, et al.,

Plaintiffs,

vs.

No. CV-95-322

AMERADA HESS, et al.,

Defendants.

DECISION

FINDINGS OF FACT

1. Plaintiffs are residents of Chaves County, New Mexico. The Defendants are corporations doing business in New Mexico.
2. Plaintiffs claim that the defendants' breached expressed and implied contractual statutory and common law duties to pay crude oil and condensate royalties and over-riding royalties based on the "highest price reasonably obtainable" and upon the actual value of the proceeds received by the defendants of plaintiffs' crude oil and condensate.
3. Plaintiffs seek certification of a class estimated to exceed 12,000 persons national wide, said class defined as those individuals "owning royalty interests or over-riding royalty interests on crude oil and condensate produced in the state of New Mexico to whom the defendants have underpaid royalty or over-riding royalty payments on crude oil".

4. Plaintiffs' allegations encompass oil and condensate production over the last decade under thousands of leases and other contractual instruments relating to thousands of wells and 989 separate fields in New Mexico located predominately in the northwest New Mexico oil producing region known as the San Juan Basin and the southeast New Mexico oil producing region referred to as the Permian Basin.

5. Production output of individual wells in the fields of New Mexico varies from small stripper wells to large producing units producing hundreds of barrels daily.

6. Different oil fields produce different types of oil generally characterized as West Texas Intermediate, New Mexico Intermediate, and West Texas Sour. These grades are subject to gravity adjustments on a well to well basis.

7. The defendants have a wide variety of lease forms in use in New Mexico which in turn contain a variety of royalty provisions.

8. The defendants have thousands of division orders in force in New Mexico with variations in the language providing for the payment for crude oil and condensate.

9. A similar diversity attends to the existence of the provisions for payment of over-riding royalty both as to their number and variety of individual provisions.

10. The various claims asserted by plaintiffs against the defendants are novel in the sense that plaintiffs have not cited to the Court previous precedent from any jurisdiction which has accepted plaintiffs' legal theories with regard to the royalty and over-riding royalty obligation of the defendants to pay royalty based upon highest price attainable or the highest price reasonably obtainable or the actual value of proceeds received by the defendants for the crude oil.

11. A variety of transportation producing arrangements attend to each of the fields in New Mexico which would have to be specifically inquired into in each instance.

12. Plaintiffs' various claims relief would require specific inquiry into the circumstances of each plaintiff. Similarly defendants affirmative defenses will require fact specific determinations as to each plaintiff.

Based upon the foregoing Findings of Fact the Court reaches the following Conclusions of Law.

CONCLUSIONS OF LAW

1. The Court must consider under a request for certification of a class under Rule 23 A et. seq. the issues of numerosity, commonality, typicality, and adequacy.

2. The Court's primary concern relates in this matter to the issue of commonality.

3. Under commonality the Court must find that a predominating question of fact or law is common to the class and which question when answered as to one class member would answer such a question as to all class members.

4. Given the variety of issues pertaining to the diversity of contracts in use in this case as they relate to leases, division orders, and over-riding royalty agreements as well as the individual fact inquiries necessarily required by the diversity in fields and wells and oil quality as well as the diversity in transportation arrangements, the Court determines that there are no predominating questions of fact or law common to the class which would meet the requirements of commonality.

TOTAL P.05

- 5. Plaintiffs' theories of recovery should be tested in individual proceedings before application of such theories is undertaken on a class wide basis.
- 6. The lack of commonality is fatal to the request of plaintiffs for certification of a class in this matter, and the Court need not consider the other arguments made regarding other aspects of class certification.


 ALVIN F. JONES
 DISTRICT JUDGE

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