Section 5

MMS-RVS-EVB:86-0794
Mail Stop 653

DEC 9 1986

Mr. Richard Hopkins
Chief, Subvention Audit Branch
Division of Audits
Controller of the State of California
545 Downtown Plaza, Suite 220
Sacramento, California 95814

Dear Mr. Hopkins:

This letter is written in response to your inquiry of August 14, 1986, addressed to our Royalty Valuation and Standards Division. That inquiry asked for our comments regarding the refinery netback approach to valuing crude oil as developed by Putnam, Hayes, and Bartlett, Inc. Through a subsequent telephone conversation with Mr. Robert Fees of your staff, we are informed that you are actually most interested in hearing our response to statements made by State of California representatives that onshore posted prices in California are not representative of crude oil market values. The Minerals Management Service has investigated onshore posted prices in California. The enclosed report summarizes our findings.

If you have any questions regarding the enclosed report, please contact us at (303) 231-3154.

Sincerely,

Original signed by
Jerry D. Hill

Jerry D. Hill
Associate Director for
Royalty Management

Enclosure

DOI FOIA 001479

MINERALS MANAGEMENT SERVICE
ROYALTY MANAGEMENT PROGRAM

State of California's Statements Regarding Valuation of Crude Oil Onshore California

General Background

In a July 2, 1986, meeting in Washington, D.C., between representatives of the Minerals Management Service (MMS); the law firm of Lobel, Novins, Lamont, and Flug; and the consulting firm of Putnam, Hayes, and Bartlett, Inc. (PHB); statements were made that crude oil produced from onshore Federal leases in California is being undervalued for royalty purposes. According to representatives of the State of California (the State), posted prices in California are not reflective of crude oil market values. A personal computer program developed by PHB allegedly gives crude oil values for California that are more reflective of the true market value than are the prices offered in field postings.

By letter of August 14, 1986, to the Royalty Valuation and Standards Division, the California State Controller's Office (CSCO) formally requested that MMS comment on the personal computer refinery netback valuation model. The MMS was later advised by Mr. Robert Fees of CSCO that the State was actually most interested in MMS's comments as to whether posted prices used to value oil from onshore Federal leases in California are reflective of crude oil market values.

On behalf of CSCO, PHB developed a system to estimate refined product values (RPV's) for California crude oil over the 1977 to 1983 time period. Reportedly they found that computed RPV's for Gulf Coast oils approximated the posted prices for the Gulf Coast. However, when a similar computation was made for onshore California crude oils, it resulted in values that were well above the posted prices for California; i.e., Gulf Coast oil is properly valued--reportedly California crude oil is worth more than purchasers are offering.

The RPV's are calculated by multiplying the price of certain refined products; i.e., gasoline, No. 2 fuel oil, and residual fuel oil, by the quantity of each product derivable from a barrel of crude oil, less the estimated cost of refining that barrel of crude oil. The State has identified additional royalties of over $22 million that it maintains should be due as the result of the application of RPV's which allegedly represent the true value of crude oil from onshore Federal leases in California during the period 1981 to 1983.

Findings

Regulations governing the valuation of crude oil produced from all Federal onshore leases are contained at Title 30 of the Code of Federal Regulations (CFR) Part 206.103. This Part states:

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"The value of production, for the purpose of computing royalty, shall be the estimated reasonable value of the product as determined by the Associate Director due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Under no circumstances shall the value of production of any of said substances for the purpose of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price per barrel, thousand cubic feet, or gallon paid or offered at the time of production in a fair and open market for the major portion of like-quality oil, gas, or other products produced and sold from the field or area where the leased lands are situated will be considered to be reasonable value." (Emphasis Added)

The Department of the Interior (DOI) is responsible for obtaining reasonable value for production from Federal and Indian leases. For crude oil, posted prices paid under arm's-length conditions have historically been considered to be representative of reasonable value. Generally, these posted prices track both the market and other postings in the same field or area and, thus, represent the value of the majority portion of production. Also, they generally represent the gross proceeds received by the lessee, and often are the highest prices being paid for oil of like quality.

Posted prices represent the price a buyer is willing to offer for the crude oil in a given field or area. Postings are affected by numerous factors including: (1) the need for and the availability of crude oil supply, (2) the cost of transportation from the field to a refinery, (3) the chemical composition and refining characteristics of the crude oil, (4) the cost to refine the crude oil, (5) the value of refined products derived from the crude oil, (6) the postings of other buyers for the same or comparable crude oils, and (7) other economic criteria. There are several advantages to basing royalty value on posted prices in that these prices:

-- Represent an offer to buy a specific quality of crude oil in a specific field or area,

-- Can be easily ascertained from publicly available documents and reviewed as frequently as required,

-- Provide the only broad-based, market-tested information specific to the quality of the product and the producing area,

-- Generally represent the price received by the lessee,

-- Generally represent gross proceeds to the lessee, and

-- usually represent the prices actually paid for the major share of supply for refiners and, thus, generally reflect prices paid for a majority of production in a given field or area--especially when posted by purchasers of large and widely traded crude oil streams.

On July 10 and 11, 1986, representatives from MMS traveled to California for the purpose of obtaining information on the prices received by the State and the City of Long Beach (the City) for their crude oil interests within the City. Representatives of the City (operator of the Long Beach Unit located in the Wilmington Field) provided MMS with documentation indicating that the City values its "sell-off" crude oil from the Long Beach Unit at the average of the posted prices in the Wilmington Field. Because the crude oil is sold in a competitive bidding process, the City sometimes accepts a positive bonus amount (on a dollar-per-barrel basis) and receives monies over and above the average of the posted prices. Conversely, the City sometimes accepts a negative bonus amount and receives less money than the average of the Wilmington Field posted prices. At the time of MMS's visit, the City was receiving approximately the same price for its crude oil sales as was being received by MMS for oil from its onshore Federal leases. From this, MMS concluded that the market forces represented by posted prices reinforced by the market forces represented in a competitive bidding process verified that value received for royalty purposes for Federal leases located in California satisfied the requirement of the regulations and fulfilled the obligations of DOI.

While in California, MMS representatives met with representatives of the law firm of Hnecker and McMahon. This law firm represents the City and the State in an antitrust lawsuit against seven major oil companies in California. The suit, which has been carried on over a period of more than 11 years, claims that the oil companies have conspired to keep posted prices artificially low, thus causing the City's and State's interests in the Wilmington Field to be undervalued. The Federal District Court has ruled that there has been no conspiracy to artificially constrain prices. This is presently being appealed by the City and the State to the Ninth Circuit Court of California.

The MMS has concluded from all of this that arm's-length crude oil posted prices have been and should continue to be used as reasonable value, for royalty purposes, for crude oil from onshore Federal leases.

The MMS submits that the netback methodology developed by PHB would not be preferable to the use of posted prices for the following reasons:

1) Calculation of RPV's requires numerous assumptions by Government officials about the cost of refining and transporting a barrel of crude oil. Such assumptions cannot accurately portray conditions within the crude oil market;

2) The RPV's generally lag the market value of crude oil. Thus, when crude oil prices decline or increase rapidly (witness recent crude oil market conditions), product prices do not generally fall (or rise) as quickly as crude oil prices. Under such circumstances it would be difficult to apply the appropriate market price to the applicable production stream without an elaborate, expensive, labor-intensive bookkeeping system;

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3) Calculation of meaningful RPV's for all Federal and Indian leases would be administratively impractical in the present, or any foreseeable, Federal budget climate.

Based on the information available at this time, MMS sees no reason to alter its historical operating policy of accepting the arm's-length posted price received by the lessee as value for royalty purposes for oil from onshore Federal leases in California.

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Section 6

January 30, 1997

QUESTIONS & ANSWERS
CALIFORNIA CRUDE OIL UNDERPAYMENTS AND PROPOSED OIL VALUATION REGULATIONS

Q) **How did this California pricing project get started?**

A) It started with the City of Long Beach litigation that was initiated in 1975 and settled in 1991. After a review of this settlement, Assistant Secretary for Land and Minerals Management Bob Armstrong commissioned an interagency task force to study the situation. Members of the task force included the Department of Interior, Department of Commerce, Department of Energy and the Department of Justice, with assistance from the State of California..

Q) **Why did you start your collection efforts with January 1980?**

A) Crude oil was under price controls until the deregulation of heavy crude oil (i.e., oil with an API gravity of 16 degrees or less) in December 1979. A significant portion of crude oil produced in California is heavy crude. With the lifting of Federal price controls, companies once again had flexibility in pricing their crude oil and could obtain prices other than the maximums specified by the Government. Also, by far the largest potential collections, including interest, are in the 1980-85 period. This approach was also suggested by members of the interagency task force.

Q) **How many companies are being audited and how were they selected?**

A) We looked at federal sales and royalty history over a 13-year period for crude oil and determined that 20 companies produced over 97% of the crude oil from federal properties on- and offshore California. Thus, these 20 companies were selected for audit.

Q) **If you are auditing 20 companies, why were bills sent to only 10?**

A) Bills have been sent to 10 integrated companies for the period 10/1/83-2/29/88, and to 9 of these same companies for the period 1/1/80-9/30/83. Additional royalties due from those companies after 2/29/88 and from the non-integrated companies will be determined by the review of documents at the companies. These reviews are currently underway.

Q) Why have two sets of bills been sent out?

A) Computerized sales and royalty data was readily available for the period October 1983 through February 1988 after the Minerals Management Service was created. Therefore, the first set of bills sent covered this period. The records for the earlier period of January 1980 through September 1983 were not computerized and took much longer to obtain.

Q) Were bills sent to all integrated companies?

A) No. Two companies, Chevron and Exxon, have settlement agreements that preclude billing prior to October 1, 1989 without a finding of fraud, collusion, or improper conduct. One of the 20 companies, Pennzoil, did not have any federal properties in California during the period of January 1, 1980 through February 29, 1988.

Q) How were underpayments determined for the integrated companies for the periods covered by the bills (January 1, 1980 - February 29, 1988)?

A) Alaska North Slope (ANS) prices were compared to applicable posted prices used by the integrated companies as their basis for royalty payments. Where ANS prices exceeded posted prices a premium was calculated based on the differences. The royalty underpayments were calculated by multiplying those premiums times the royalty volumes reported by the companies.

Q) Why were ANS prices used?

A) The task force determined that the ANS price has been used by companies in California to determine the profitability of transactions; ANS crude oil is the primary substitute for California oil; and, 30% to 45% of the crude oil refined in California was ANS. The regulations for that period of time gave the Secretary broad authority to determine the method of pricing crude oil. This situation prevailed through February 29, 1988, when the federal crude oil valuation regulations changed.

Q) What about the remaining 7 non-integrated companies before 1988?

A) Bills will be sent to the remaining 7 companies after the reviews of documents at those companies have been completed.

Q) How much have you billed so far?

A) Bills sent out to date total $385.4 million.

Q: **If you were to collect the full $440 million, how much would the state of California receive?**

A: About $80 million. This estimate is based on the ratios for offshore and onshore production used by the inter-agency team in developing their high estimate of $856 million. It includes approximately $9 million for leases in the so called "8(g)" zone.

Q) **How much have you collected?**

A) To date nothing. The companies have yet to exhaust the administrative remedies available to them. When these remedies are exhausted, the courts may be involved in resolving these issues.

Q) **How long will it take to complete the California project?**

A) The MMS implementation plan requires all bills to be sent out no later than 12 months after the documents that are necessary to determine the underpayments have been received from the companies. Several companies have been less than co-operative in providing documentation, and eight subpoenas have been issued.

Q) **What about crude prices in the rest of the country?**

A) The MMS has an initiative under way to review the records of 125 additional companies doing business in all parts of the country, to determine if significant royalty underpayment exists.

Q) **Why 125 companies?**

A) These 125 companies account for over 85 percent of the 1991-1995 oil revenue from federal and Indian leases. For several months, MMS has held open past audit periods at the major companies from 1989 forward. Plans call for auditing current periods first, and if indications of earlier violations are identified, we may go back to earlier periods (pre-1990).

Q) **Why do the existing rules need to be changed?**

A) The current Federal and Indian oil valuation rules may not always result in market value being used as royalty value. For example, the existing rules rely fairly heavily on posted prices--the prices published by oil refiners. MMS believes that posted prices may now represent the beginning point for price negotiation or something similar, but no longer generally represent market value.

Q) What process did you use to develop the proposed rule?

A) MMS first published an advance notice of proposed rulemaking to get feedback on whether the rule should be changed, especially its reliance on posted prices. The comments it received led MMS to put together a regulatory writing team composed of MMS staff and representatives of States, Indians, and the Western States Land Commissioners. Industry was not represented on the team because their comments on the advance notice indicated they didn't want to participate until their related litigation elsewhere is resolved. During its deliberations the team relied not only on its combined internal expertise but also presentations by: crude oil brokers and refiners, commercial oil price reporting services, companies that market oil directly, and private consultants knowledgeable in crude oil marketing. MMS' deliberations were aided greatly by a wide range of expert advice.

Q) How would the new Federal oil valuation rule be different from the current one?

A) Royalty valuation under the existing rules relies on the proceeds received by the lessee in its arm's-length transactions. If the lessee disposes of its oil under a non-arm's-length contract or doesn't sell it at all--such as when it refines the oil itself--a series of benchmarks apply. These benchmarks rely on posted prices and arm's-length contract prices in the area.

The proposed rule would still rely on arm's-length proceeds, but on a limited basis. Because of the frequency of oil exchange agreements, reciprocal deals between crude oil buyers and sellers, and other factors where the real consideration for the transaction could be hidden, arm's-length contract prices would be used as royalty value only by producers who do not also purchase crude oil. Where a company's affiliate takes the production and sells it at arm's length, value would be the affiliate's proceeds or, optionally, NYMEX or spot prices adjusted for location and quality differences. For all other non-arm's-length transactions or where no sales occur, the value would be determined by index prices--either NYMEX or spot prices--adjusted for location and quality differences.

Q) What is the difference between arm's-length and non-arm's-length contracts?

A) For a transaction to be at arm's length, it must be between independent, nonaffiliated parties with opposing economic interests in the contract. If these conditions don't exist, then the contract is non-arm's-length. In the proposed rule, arm's-length contract prices would be used as royalty value only by producers who do not also purchase crude oil. In addition, certain transactions such as exchange agreements would always be valued as if not at arm's length because of their reciprocal nature. (That is, as long as the two parties receive the proper relative value, they may have little incentive to assure that the absolute contract price reflects market value.)

Q) How are you determining the difference between integrated and non-integrated companies?

A) We have defined an integrated company as one that has U.S. refining capability. An integrated company will not normally sell its crude oil production. It will therefore not have gross proceeds on which to base royalty payments. A non-integrated company is one that does not have U.S. refining capability; thus, will sell its crude oil to outsiders.

Q) What is the NYMEX price?

A) NYMEX stands for the New York Mercantile Exchange. The proposed index price for leases other than in California or Alaska is the NYMEX futures price at Cushing, Oklahoma, for oil deliveries in the following month. MMS searched for indicators to best reflect current market prices and settled on NYMEX for several reasons. It represents the price for a widely traded domestic crude oil (West Texas Intermediate at Cushing Oklahoma). It is the most widely accepted benchmark of crude oil worldwide. Because of the sheer volume of oil futures contracts traded on NYMEX and the low possibility that any one party could unduly influence prices, the NYMEX futures prices generally are considered the best single indicator of oil market value. Also, NYMEX prices were regarded by many of the experts MMS consulted to be the best available measure of oil value. The most difficult problem, as will be discussed in more detail below, would be to make appropriate location and quality adjustments when comparing the NYMEX crude with the crude produced.

Q) What are spot prices?

A) Spot prices are published by trade publications; they represent surveys of market prices for particular types of crude oil produced in specific areas. For California and Alaska, published spot prices for Alaska North Slope crude oil, rather than NYMEX prices, would be the index value. This is due to the difficulties in adjusting prices in those locales for locational differences compared to Cushing, Oklahoma.

Q) What other major provisions are included in the proposed rule?

A) The proposed rule contains two other significant provisions: (1) valuation of oil taken in kind by the Government would be tied to NYMEX and spot prices as discussed earlier, and (2) lessees would no longer be permitted to use their FERC tariffs as a transportation allowance in moving their own oil--they would have to do actual cost calculations.

Q) Is Indian oil valuation tied to the Federal rules?

A) No. At the request of several tribes, MMS will develop a separate Indian rule after consultation with them. A three-day meeting is scheduled in mid-February to get feedback from Indians on drafting the separate rule. The proposed Indian rule would differ from its Federal counterpart to better accommodate the different terms of Indian leases--principally the provisions requiring value on the "highest price paid for a part or majority of like-quality crude" in the field or area.

Q) When do you expect to publish a final Federal rule?

A) MMS doesn't have a definite projected date for publishing the Federal rule in final form. The comment period is scheduled for 60 days, and follow-up activity depends on the extent of comments received and modifications needed. However, we should be able to publish a final rule by the end of the year.

Q) Will the new rules mean more royalty collections, and if so, how much?

A) We believe the proposed Federal rule would result in increased royalty collections--perhaps on the order of $50-100 million per year.

Q) What has been industry's reaction?

A) They have been noncommittal to date. Industry chose not to participate in any negotiated rulemaking on this issue because of their involvement in private litigation involving crude oil valuation. We expect to receive numerous comments from them on the proposed rule.

Section 7

JUDGE JACK TENNER (RETIRED)
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Judge Pro Tem

SUPERIOR COURT OF THE STATE OF CALIFORNIA

FOR THE COUNTY OF LOS ANGELES

THE PEOPLE OF THE STATE OF CALIFORNIA, THE CITY OF LONG BEACH as Trustee for the State of California, and THE STATE OF CALIFORNIA, as Beneficiary, Plaintiffs, -vs- CHEVRON CORPORATION; UNOCAL CORPORATION; MOBIL OIL CORPORATION; SHELL OIL COMPANY; SHELL CALIFORNIA PRODUCTION, INC.; TEXACO, INC.; EXXON CORPORATION; EXXON COMPANY, U.S.A., and DOES 1 through 10, Inclusive, Defendants.	CASE NO: C 587 912 AMENDED AND REVISED STATEMENT OF DECISION AND JUDGMENT RE MOBIL

1. Plaintiffs the City of Long Beach and the State of California brought this action pursuant to Business and

February 19, 1986. On its face Plaintiffs' complaint addressed only Mobil's conduct occurring between January 1, 1980, and December 31, 1985. In recognition of Plaintiffs' claims for prospective equitable and declatory relief, however, the Court received evidence and makes its findings and conclusion on Mobil's conduct occurring form January 1, 1980, through the time of trial.

4. Trial commenced on January 25, 1993, and concluded on February 11, 1993. Subsequent to trial, the parties were ordered to file written final arguments. A final oral argument was scheduled and held on May 5, 1993.

5. The Court heard the testimony of live witnesses and received many exhibits and depositions and after weighing the relevance of the exhibits and the credibility of witnesses, and the receipt of written and oral arguments, the Court issued a tentative decision on May 20, 1993. As to Mobil, that decision was in favor of the Defendant.

6. Numerous facts were vigorously contested as were the principles of law applicable to these facts. The Court hereby adopts the following findings of fact and conclusions of law as the principal findings and conclusions of law in support of the Court's decision concerning the MSJV line.

FINDINGS OF FACT

(1) Mobil is an integrated petroleum company that

explores for and produces crude oil, refines it into marketable products such as gasoline and diesel fuel and distributes and sells refined products to consumers. Mobil conducts all these types of activities within the state of California, as well as elsewhere in the United States and the world.

(2) Mobil is the sole owner and operator of the MSJV line, which runs from the San Joaquin Valley south to the Mobil Refinery in Torrance. The Torrance refinery is the "MSJV's" only destination in the Los Angeles basin.

(3) The Torrance refinery is designed to refine most efficiently an array ("a slate") of predominately heavy California crude oil that includes substantial quantities of heavy crude produced in the San Joaquin Valley.

(4) The Torrance refinery operates most efficiently and provides Mobil with the greatest economic return on its substantial investments when it runs a high percentage of heavy crude oils including San Joaquin Valley crude oil.

(5) Mobil delivers heavy San Joaquin Valley crude oil to its Torrance refinery principally through the MSJV line. Mobil holds title to and in fact owns all crude oil in the MSJV line or in any Mobil facility such as a Mobil storage tank in the vicinity of the Mobil line.

(6) Coordinated with its refinery investments, Mobil has made considerable investment in its MSJV line. Mobil expanded the capacity of the MSJV pipeline to deliver crude oil to Torrance to 49,000 barrels per day in 1967, and to 63,500

barrels per day in 1983. In recent years, Mobil has replaced much of the M-70 portion on the MSJV line. With completion of the M-70 replacement project, the MSJV pipeline will have the capacity to deliver 95,000 barrels per day to the Torrance refinery. Mobil invested approximately $107 million in the most recent pipeline project.

(7) Throughout the relevant period, the MSJV line has supplied an increasing percentage of the crude oil refined at Torrance. In 1980, the MSJV pipeline provided approximately 50.2% of the crude oil run daily at Torrance. By 1989, that figure had increased to 76.1% of the crude run daily at Torrance. TX4027. With the completion of the M-70 replacement project, the Mobil line can continue to supply approximately 75% of the Torrance refinery's crude needs for the foreseeable future.

(8) The MSJV pipeline is an extension of the Torrance refinery, sized to meet the Torrance refinery's demands for heavy San Joaquin Valley crude oil. As Torrance's ability to refine heavy San Joaquin Valley crude has increased, Mobil has concomitantly increased the MSJV's capacity.

(9) Virtually all of the oil injected into the MSJV pipeline during the relevant period was transported to the Torrance refinery and refined by Mobil.

(10) Mobil produces a substantial amount of California crude oil in the San Joaquin Valley, in the Los Angeles Basin, and in California's coastal region, including San Ardo. Mobil

also has some offshore California production. Historically, however, Mobil's own production of California crude oil has been less than the amount of crude oil needed to keep the refining units at Torrance fully loaded for efficient operation.

(11) Throughout the relevant period, the capacity of the MSJV pipeline was greater than Mobil's production of crude oil in the San Joaquin Valley. Recently, Mobil's own production has increased to the point that it comes closer to the operating capacity of the MSJV to deliver crude oil to the Torrance refinery.

(12) All of Mobil's crude oil exchanges and buy/sell transactions are negotiated at arms-length with the other contracting party. The agreement between the parties is memorialized in a written contract. Mobil does not enter any exchange or buy/sell arrangement without a written agreement.

(13) Mobil typically uses crude oil exchanges and buy/sell transactions, as well as outright purchases and sales, to balance its supply of heavy San Joaquin Valley crude with its ability to transport those crude through the MSJV pipeline to the Torrance refinery. When Mobil's production and purchases of San Joaquin Valley crude exceed the capacity of the MSJV pipeline, the net of Mobil's purchases, sales and exchanges is to sell any modest excess of San Joaquin Valley crude, acquiring crude produced elsewhere, such as the Los Angeles basin or the coastal region. When Mobil's San Joaquin Valley crude production and purchases are less than the desired operating

capacity of the MSJV pipeline, the net relocation from this trading process is reversed. The primary purpose of this buying and selling activity is to keep the MSJV pipeline at the volume that will meet the Torrance refinery's demand for heavy San Joaquin Valley crude oil.

(14) Few, if any, of Mobil's exchange and buy/sell transactions are agreements for the transportation of crude oil for third parties through the MSJV pipeline for compensation.

(15) Mobil takes title to all crude oil it acquires on exchange and buy/sell transactions as it enters Mobil's facilities. Mobil also assumes the risk of loss of crude oil received at that point.

(16) On none of the exchanges which involved, according to Plaintiffs, transportation of crude oil on the MSJV line did Mobil receive a loss allowance from its contracting partner, nor did Mobil require or receive additional crude oil to send as line fill.

(17) Accepting Plaintiffs' evidence arguendo, during the period 1981-1987, 9% of MSJV's pipeline volume related to alleged transportation arrangements, moreover, at least 96% of this 9% (8.6% compared to MSJV pipeline volume) over the same period related to "reciprocal" exchanges admitted by Plaintiffs to involve no physical transportation for others through the MSJV, leaving only .4% of remaining alleged transportation activity.

(18) The proportion of exchange volume (for exchanges

alleged to involve the MSJV pipeline) to MSJV volume has tended to decrease over time from 1982, through 1992.

(19) Many, if not all, of Mobil's exchange contracts proffered as involving the MSJV pipeline do not obligate Mobil to place crude delivered to it into the MSJV pipeline. Plaintiffs failed to establish, in fact, that crude received by Mobil on all of these proffered exchanges was placed into the MSJV pipeline. Except on the "reciprocal" Pacoima exchange, Mobil received no crude on the MSJV.

(20) The MSJV pipeline is not part of an "integrated system" of pipelines for transportation of crude oil in California.

(21) Mobil's MSJV pipeline, whether considered individually or jointly with the Chevron and Texaco heated pipelines at issue in this case, is not an "essential facility" for the transportation of heavy San Joaquin Valley crude oil.

(22) Plaintiffs did not establish that Mobil's Torrance refinery is dependent on any pipelines of other companies for efficient operation.

(23) Throughout the relevant period, two short segments respectively of the M-55 and M-70 portions of the MSJV pipeline crossed federal lands under right-of-way permits granted by the federal government under section 28(r) of the Mineral Leasing Act ("MLA").

(24) In 1987, Mobil received requests from PAR Petroleum, Inc.("PAR") through its principal, Alfred R. Pacheco,

ostensibly to ship PAR's crude in Mobil's MSJV pipeline pursuant to non-existent published tariffs but which requests were not viable for other reasons. After some months of negotiation, PAR revised its request to one apparently for transportation of PAR-owned crude from the San Joaquin Valley to the Newhall Refinery.

(25) Plaintiffs did not establish that PAR actually owned or had rights to own the crude that it sought to transport on Mobil's line. The evidence established that PAR owned no crude, and that its requests to Mobil were not genuine business requests.

(26) As part of negotiation over PAR's request, Mobil offered to enter an exchange contract with PAR. Under the proposed exchange, Mobil would purchase crude oil from PAR, at the price at which it purchased such crude from others, and sell crude to PAR out of the MSJV pipeline at the Newhall Refinery. PAR declined Mobil's exchange offer.

(27) PAR never had any arrangement to sell crude oil to the Newhall Refinery that would have permitted it to take delivery from the MSJV at the Newhall Refinery.

(28) In 1990, Berry Petroleum Company ("Berry"), an independent crude oil producer, inquired about a possible pipeline connection to Mobil's MSJV line at some unspecified future time.

(29) On several occasions, Mobil offered to buy outright or by exchange crude oil that Berry produced at Mobil's posted price, which is the price at which Mobil bought crude oil

from others. Berry declined those offers, stating it could get a higher price for its oil by selling it to someone else.

(30) Plaintiffs offered into evidence at trial an audit report prepared by the Inspector General of the Department of the Interior, concerning the Bureau of Land Management's enforcement of the MLA common carrier provisions. 30 U.S.C. §185 (r). The Court has excluded that report because it is irrelevant to the dedication issues to be resolved in this action. Even if the audit report were formally admitted into evidence, the Court would give it no weight. The subject matter of this report is an evaluation of the Bureau of Land Management's enforcement policy and action regarding the MLA; the report is not reliable.

(31) As part of the M-70 replacement project, Mobil obtained a new right-of-way under the Mineral Leasing Act for the portion of the M-70 pipeline that crosses federal land. During the permitting process, the United States Forest Service, the agency in charge of issuing the permit, determined that Mobil's operation of the M-70 portion of its pipeline was in compliance with the common carrier obligations of section 28(r) of the Mineral Leasing Act.

(32) Mobil has not held out the MSJV line for the transporting of crude oil for a fee to the public or a portion thereof.

(33) Any conclusion of law which should be adopted as a finding of fact is hereby adopted as such.

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CONCLUSIONS OF LAW

1. Any Finding of Fact which should be deemed a conclusion of law is hereby adopted as such.

2. The applicable standard of proof is proof by a preponderance of evidence. Weiner vs Fleischman (1991) 54 Cal. 3d 476, 286 Cal. Rptr. 40; Liodas vs Sahadi (1977) 19 Cal. 3d 278, 137 Cal. Rptr. 635; Cal. Evidence Code Section 115.

3. The question of whether Mobil's MSJV pipeline has been dedicated to public use is one of fact. See California Water & Telephone Co. v Public Utilities Commission, 51 Cal. 2d 478, 494, 334 P. 2d 887,896 (1959); Van Hoosear v Railroad Commission, 184 Cal. 553, 554, 194 P. 1003, 1004 (1920).

4. Plaintiffs' bear the burden of proving that Mobil has dedicated its line to public use by a preponderance of the evidence. Weiner v Fleischman, 54 Cal. 3d 476, 816 P. 2d 892, 286 Cal. Rptr. 40 (1991).

5. Mobil's MSJV pipeline is a public utility only if it falls within one of enumerated classes of business declared by the Legislature to be a "public utility". California Public Utilities Code §216(a); Television Transmission, Inc. v Public Utilities Commission, 47 Cal. 2d at 82, 85, 301 P. 2d 862, 863 (1956).

6. The only statutory categories potentially applicable to Mobil's MSJV pipeline are "pipeline corporation" and "common carrier". California Public Utilities Code §216(a).

7. In the context of crude oil pipelines, claims of dedication by implication from alleged transportation conduct have three factual elements. First, Plaintiffs must show that Mobil physically transported crude oil for third parties through the MSJV pipeline. California Public Utilities Code §§211, 216, 227-28; see Television Transmission, Inc. v Public Utilities Commission, 47 Cal. 2d 82, 301 P.2d 862 (1956).

8. Mobil's MSJV pipeline is a "public utility" only if it provides a "public utility" service to the public or any portion thereof. California Public Utilities Code §216(a). A "public utility" service is a service of the type generally performed by one of the business entities enumerated in Public Utilities Code Section 216(a) and which potentially necessitates regulation by the Public Utilities Commission in the public interest. See California Community Television Association v General Telephone Company, 73 Cal. P.U.C. 507 (1972).

9. Plaintiffs have not shown by a preponderance of the evidence that Mobil performed a transportation service for the public or a portion thereof.

10. In addition to proving that Mobil used the MSJV line to provide a transportation service, Plaintiffs must prove a second element, namely that the transportation service was performed for some compensation or payment. California Public Utilities Code §216.

11. Plaintiffs have failed to prove by a preponderance of the evidence that Mobil received any

substantial compensation for the provision of any transportation services involving the MSJV pipeline.

12. The third indispensable element is proof of "dedication" of the subject pipeline to public use. Richfield Oil Corporation v Public Utilities Commission, 54 Cal. 2d 419, 354 P.2d 4, 6 Cal. Rptr. 548, cert. denied sub nom., Southern Counties Gas Company v Public Utilities Commission, 364 U.S. 900 (1060).

13. "To hold that property has been dedicated to a public use 'is not a trivial thing'", Allen v Railroad Commission, 179 Cal. 68, 85 175 P. 466, 473 (1918) (citing City of San Francisco v Grote, 120 Cal. 59, 52 P. 127 (1898)), cert denied, 249 U.S. 601 (1919), because it deprives the property owner of exclusive use of its property.

14. Because of its serious effect on property ownership, dedication is never presumed and must be shown by evidence of unequivocal intention. California Water & Telephone Company, 51 Cal. 2d at 494, 334 P. 2d at 897; Richardson v Railroad Commission, 191 Cal. 716, 721, 218 P. 418, 420 (1923); Van Hoosear, 184 Cal. at 554, 194 P. at 1004; Allen, 179 Cal. at 85, 175 P. at 473.

15. Dedication cannot be inferred solely from the number of customers served. The question is one of intent and is to be resolved by reference to the property owner's dealings and relations to the property sought to be impressed with public utility duties. California Water & Telephone Company, 51 Cal.

Cal. 2d at 494, 334 P. 2d at 897; Samuel Edwards Associates v Railroad Commission, 196 Cal. 62, 70-71, 235 P. 647, 650 (1925).

16. Mobil has not expressly dedicated its MSJV pipeline to public use.

17. Plaintiffs have failed to prove by a preponderance of the evidence that Mobil's conduct with respect to the MSJV pipeline manifests an unequivocal intention to dedicate the line to public use.

18. Since Mobil has not manifest an unequivocal intent to dedicate its MSJV line to public use, the MSJV pipeline is not a public utility.

19. The point at which the amount of activity actually or allegedly constituting transportation for compensation is de minimis and insufficient to justify a finding of dedication to public use is not precise and depends on the particular facts and circumstances of the pipeline owner and its operations.

20. Under both federal and state law, "all words and provisions of statutes are intended to have meaning and are to be given effect, and words of a statute are not to be construed as surplusage". Wilderness Society v Morton, 479 F. 2d 842, 856 (D.C. Cir.), cert. denied, 411 U.S. 917 (1973); see also In re Estate of MacDonald, 51 Cal. 3d 262, 269-70, 794 P. 2d 911, 916, 272 Cal. Rptr. 153, 158 (1990) (statutory construction rendering some words surplusage to be avoided); City and County of San Francisco v Farrell, 32 Cal. 3d 47, 54, 648 P. 2d 935,

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938, 184 Cal. Rptr. 713, 716 (1982) ("In construing the words of a statute or constitutional provision to discern its purpose, the provisions should be read together; an interpretation which would render terms surplusage should be avoided, and every word should be given significance, leaving no part useless or devoid of meaning".)

21. The Mineral Leasing Act does not regulate pipeline operations such as, for example, rate regulations and tariff filings. Chapman v El Paso Natural Gas, Co., 204 F 2d 46, 51 (D.C. Cir. 1951). Regulatory authority of the Secretary of the Interior under the Mineral Leasing Act is largely limited to matters pertaining to the physical aspects of the right-of-way over federal lands. Action under the act is limited to the Secretary of the Interior.

22. While pipelines crossing federal lands under section 28 of the Mineral Leasing Act must be "constructed, operated, and maintained as common carriers", 30 U.S.C. §185(r)(1), mere proof that Mobil accepted a MLA permit does not establish dedication, nor is it substantial evidence of dedication.

23. A Mineral Leasing Act "common carrier" is not the equivalent of a "common carrier" under California state law. Richfield, 54 Cal. 2d 440-41, 354 P. 2d at 17-18, 6 Cal. Rptr. at 561.

24. A MLA "common carrier" may meet its MLA common carriage obligations by "accept[ing], convey[ing],

transport[ing], or purchase[ing] without discrimination" crude oil tendered to the pipeline. 30 U.S.C. §185 (r)(2) (emphasis added). Thus, the MLA does not require Mobil to dedicate its MSJV pipeline to public use under California law. Richfield, supra; see also Chapman v El Paso Natural Gas Co., 204 F. 2d 46 (D.C. Cir. 1953).

25. Mobil satisfies its MLA common carrier obligation by purchasing crude oil without discriminating and is in compliance with the Mineral Leasing Act.

26. If any MLA common carrier obligation to PAR Petroleum and/or to Berry Petroleum existed, it was satisfied by Mobil's offering to purchase or exchange crude oil.

27. Because Mobil may satisfy its MLA common carrier obligation solely by purchasing crude oil without discrimination and need not physically transport crude oil for others through the MSJV pipeline, not holding out to serve the public is implicit in its acceptance of MLA permits for segments of the MSJV pipeline. Richfield, 54 Cal. 2d 440-41, 354 P. 2d at 17, 6 Cal. Rptr. at 561.

28. The differences between common carrier status under California law and the MLA allow pipelines in California to maintain dual status---private and proprietary under state law and common carrier for purposes of the Mineral Leasing Act. The MSJV pipeline maintains such dual status.

29. Plaintiffs may not enforce the common carrier provisions of the Mineral Leasing Act directly against Mobil.

No explicit private right of action exists under the Mineral Leasing Act, and one may not fairly be implied. See Cort v Ash, 411 U.S. 66 (1975). Likewise, Plaintiffs may not use California Business and Professions Code §17200 to bootstrap themselves into a private right of action under the MLA. People ex rel. Department of Transportation v Naegele Outdoor Advertising Co., 38 Cal. 3d 509, 698 P.2d 150, 213 Cal. Rptr. 246 (1985), cert. denied, 475 U.S. 1045 (1986).

30. Plaintiffs have failed to prove by a preponderance of the evidence that Mobil's MSJV pipeline is part of an "integrated system" of pipelines used to transport crude oil in California.

31. Plaintiffs have failed to prove by preponderance of the evidence that the Mobil's MSJV pipeline is an " essential facility" for the transportation of crude oil from the San Joaquin Valley to the Los Angeles Basin.

32. The "essential facilities" doctrine and Plaintiffs' other claims of anti-competitive harm resulting from the operation of proprietary pipelines in California are irrelevant as a matter of law to the question whether a particular pipeline is a public utility subject to the jurisdiction of the Public Utilities Commission. Associated Pipeline Co. v Public Utilities Commission, 176 Cal. 518, 169 P 62 (1917) (pipeline is not public utility absent dedication; threat of monopoly is no substitute for dedication).

33. Plaintiffs have failed to show by a preponderance

of the evidence that Mobil illegally discriminated against independent producers or any other crude oil owner in the transportation of crude oil on the Mobil line.

34. The existence of alleged discrimination is irrelevant to the issues in this case as a matter of law. Absent dedication to public use, Mobil has no obligation to carry crude oil for others on its line.

35. Plaintiffs have failed to establish that Mobil's operation on its MSJV pipeline is in violation of either section 17200 of the California Business and Professions Code or section 2106 of the Public Utilities Code.

36. The Court hereby rules that as to the MSJV line, Plaintiffs have failed to meet their burden of proof and that the MSJV line is neither a public utility nor a common carrier under California law.

Dated: August 6, 1993

Jack Tenner
Judge Pro Tem

PROOF OF SERVICE BY MAIL

I, Patricia UpdeGraff, not a party to the within action, hereby declare that on August 9, 1993 I served the attached Amended and Revised Statement of Decision and Judgment re: Mobil on the parties in the within action by depositing true copies thereof enclosed in sealed envelopes with postage thereon fully prepaid, in the United States Mail, at SANTA MONICA, CALIFORNIA, addressed as follows:

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I declare under penalty of perjury the foregoing to be true and correct. Executed at SANTA MONICA, CALIFORNIA on August 9, 1993.

Patricia Goldhoff.
Signature

Section 8

United States Department of the Interior

MINERALS MANAGEMENT SERVICE
Washington, DC 20240

MAR 18 1997

American Petroleum Institute
1220 L Street, NW
Washington, D.C. 20005

Dear Sir or Madam:

Thank you for your letter dated February 28, 1997, concerning an extension of the public comment period for our proposed rule on establishing oil value for royalty due on Federal leases and on the sale of Federal royalty oil.

This rule was published in the Federal Register on January 24, 1997, as a proposed rule with a comment period of 60 days. I am pleased to inform you that at industry's request, on February 18, 1997, we extended the comment period by 30 days to April 28, 1997. Subsequently, and again at industry's request, we also rescheduled the public meetings for this rule from March 4, 1997, to April 15, 1997, in Denver, Colorado, and from February 25, 1997, to April 17, 1997, in Houston, Texas.

As I am sure you know, the issue of whether posted prices fairly represent value for royalty purposes has been around for many years. In fact, the Minerals Management Service (MMS) began the process of revising its current oil valuation rules on December 20, 1995, when we published an Advance Notice of Proposed Rulemaking (Notice) requesting comments on alternative valuation methods. Unfortunately, many of the major companies and industry associations who responded to the Notice declined to provide substantive comments, citing pending litigation as the primary reason. For the most part, industry also commented that it could not participate in any negotiated rulemaking effort citing the same litigation related constraints. Additionally, we verbally requested input from oil companies after the comment period on the Notice closed. Only three companies responded to that request.

In September 1995, the Royalty Policy Committee established a subcommittee on valuation for several products including oil. The oil valuation subcommittee members included representatives from a number of industry associations. After an initial meeting in June 1996, no consensus could be reached on an agenda or discussion items, and the subcommittee was disbanded. We had hoped this subcommittee would serve as a forum for industry input on revised oil valuation rules.

Since the proposed rulemaking was published on January 24, 1997, I have met with representatives of independent producers to discuss their procedural concerns regarding the amount of time needed to comment. Neither the arguments presented by the independent producers in that meeting nor those set forth in your letter to request this additional extension were persuasive, given our long history of discussing this issue and our concern over possible loss of revenues to the Federal and State treasuries. We must move promptly to fulfill our public responsibility to obtain fair market value for oil produced on Federal lands. Therefore, I have decided not to further extend the comment period at this time.

However, I would note that we are making a concerted effort to respond as quickly as possible to your requests under the Freedom of Information Act for documents related to the proposed rulemaking. A basic core package of information was mailed to you on March 14, 1997. Additional materials will be provided in the near future.

It is important to us that we hear from you and other interested parties concerning this proposed rulemaking. The MMS is using this rulemaking to obtain information from all affected parties so that it may appropriately refine the rule to obtain fair market value for oil. We encourage you to submit your comments before April 28, 1997, and we welcome your participation at the public hearings in Denver and Houston.

If you have any further questions, please call me at (202) 208-3500, or you may contact Ms. Lucy R. Querques, Associate Director for Royalty Management at (202) 208-3415.

Sincerely,

Cynthia Quarterman
Director

Similar letters sent to:

Domestic Petroleum Council
Independent Petroleum Association of America
Independent Petroleum Association of Mountain States
Mid-Continent Oil and Gas Association
Rocky Mountain Oil and Gas Association

Section 9

Mobil Exploration & Producing U.S. Inc.

P.O. BOX 850232
DALLAS, TEXAS 75265-0232

March 14, 1996

David S. Guzy
Minerals Management Service
Royalty Management Program
Rules and Procedures Staff
Denver Federal Center, Building 85
P. O. Box 25165, Mail Stop 3101
Denver, Colorado 80225-0165

Re: Advance Notice of Proposed Rulemaking
Valuation of Oil from Federal and Indian Leases
30 CFR Part 206
60 FR 65610 - December 20, 1995

MAR 1 5 1996

Gentlemen:

As a significant producer of federal and Indian oil, the issue of oil valuation is important to Mobil and we appreciate the opportunity to comment on this advance notice of proposed rulemaking (ANPR).

Mobil believes the posted oil price has historically been representative of fair market value at the lease. If the MMS has a concern that this will not continue to be true in the future, it could pursue taking its royalty oil in-kind and bidding it out to available purchasers in the area. This would alleviate any concerns regarding oil valuation that the MMS might have, since it would be assured of receiving fair market value for its oil through arm's-length contracts between itself and willing purchasers at or near the lease.

There may be other valuation options available as well. Oil valuation is an extremely complex issue, however, and the existing regulations, which were crafted after many years of careful consideration by the agency, should not be lightly abandoned.

Mobil is currently involved in litigation regarding oil valuation. Because this litigation is still in its initial stages, Mobil believes that it would be inappropriate for it to comment further on the ANPR at the present time. However, we hope you understand that Mobil strongly supports the notice and comment provisions of the Administrative Procedures Act.

Respectively submitted,

Ron G. Kissick

Ron G. Kissick