IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF PENNSYLVANIA

A&B CAMPBELL FAMILY LLC, *et al.*,	**ELECTRONICALLY FILED**
Plaintiffs,	**Civil Action No. 3:15-cv-00340-MEM**
v.	**(Judge Malachy E. Mannion)**
CHESAPEAKE ENERGY CORPORATION, *et al.*,	
Defendants.	

MEMORANDUM OF LAW IN SUPPORT OF DEFENDANT MITSUI E&P USA LLC'S MOTION TO DISMISS THE AMENDED COMPLAINT

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INTRODUCTION

In their Amended Complaint ("Complaint"), Plaintiffs seek to transmogrify a conventional breach of contract claim into antitrust and RICO claims through conclusory allegations and group pleading. As to Mitsui E&P USA LLC ("MEPUSA"), at its core, this is a contract case involving a dispute as to the deductibility of post-production costs from the royalties that MEPUSA pays to Plaintiffs under the terms of various oil and gas leases allegedly having a common royalty provision ("Leases"). ¶ 145.[1] As a matter of law, MEPUSA has the right to deduct post-production costs from the sales price of the natural gas, and Plaintiffs have failed to allege any facts plausibly showing that the deductions were excessive or otherwise improper. For these reasons, *all* of the claims in the Complaint fail.

Plaintiffs allege that MEPUSA breached the Leases under one of two mutually exclusive scenarios: MEPUSA either has no right, as a matter of law, to deduct post-production costs under the terms of the Leases, ¶ 303, or, alternatively, MEPUSA has that right but its deductions were excessive, ¶ 306. The former ground fails as a matter of law because the Pennsylvania Supreme Court held in *Kilmer v. Elexco Land Services*, 990 A.2d 1147 (Pa. 2010), that deduction of post-production costs is permissible, while courts have already interpreted the royalty

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[1] All paragraph references are to Plaintiffs' Complaint and are indicated by "¶ X."

provision in the Leases to permit deduction of post-production costs under the net-back method. As to the latter ground, Plaintiffs have not alleged any facts to support the speculative conclusion that MEPUSA's deductions were improper. Because Plaintiffs' breach of contract claim (Count Five) fails, so too do the Complaint's other common law claims in Counts Six (alleging right to an accounting), Seven (alleging conversion of post-production expenses), and Nine (seeking Declaratory Judgment concerning the same flawed contractual allegations).

Plaintiffs' remaining antitrust and RICO claims (Counts One through Four) are fundamentally flawed as to MEPUSA for numerous reasons. First, each of those claims is predicated on the notion that Defendants formed an agreement to overcharge Plaintiffs in the form of reduced royalty payments, but the Complaint is devoid of well-plead allegations as to how or when such an agreement was formed; there is no plausible basis to conclude that MEPUSA entered into such an arrangement; and MEPUSA's alleged decision to recoup a portion of its costs for gathering services from royalty payments was entirely consistent with its own economic interests and not indicative of any collusion. Second, as to the antitrust claims, Plaintiffs have not pled antitrust injury and otherwise lack antitrust standing, among other deficiencies. Third, as to their RICO claims, among other things, Plaintiffs' fraud-based allegations fall far short of the particularity required by Rule 9(b) – especially as to MEPUSA. In short, Plaintiffs' claims are speculative, implausible, and unsalvageable.

PROCEDURAL HISTORY

On February 17, 2015, Plaintiffs filed the Complaint. After receiving an extension of time to respond (ECF Nos. 17, 19), MEPUSA filed a Motion to Dismiss on May 22, 2015 (ECF No. 68). Plaintiffs responded by amending their Complaint. (ECF No. 94). The Court granted MEPUSA's Motion for Leave to Enlarge Length of this Memorandum of Law. (ECF No. 106).

STATEMENT OF FACTS[2]

Plaintiffs are owners/lessors of royalty interests in Bradford, Sullivan, and Wyoming Counties. ¶ 1. MEPUSA, Anadarko E&P Onshore LLC ("Anadarko"), Chesapeake Appalachia, L.L.C. ("Chesapeake"), and Statoil USA Onshore Properties, Inc. ("Statoil") (each a "Lessee" and, collectively, "Lessee Defendants") "hold working interests in the leases in which Plaintiffs hold royalty interests, either as the original lessee party to the lease" or as assignees thereof. ¶ 2. MEPUSA obtained its interest in the Leases through a partial assignment from Anadarko. ¶ 140. Chesapeake is the operator of the wells. ¶ 3.

Each Lessee separately calculates royalties based on its particular fractional interest in the Leases. "*Each* of the Lessee Defendants is responsible for

[2] For purposes of this motion, MEPUSA assumes the truth of the allegations in Plaintiffs' Complaint.

accounting for and distributing *its share* of the royalties due and owing to royalty interest owners." ¶ 4 (emphasis added). The royalty provision states:

> LESSEE . . . shall pay the LESSOR on gas . . . produced from the premises and used off the premises or lands pooled therewith or in the manufacture of gasoline, or other products therefrom, or sold (whether to an affiliated or non-affiliated purchaser) the *market value at the well of one-eighth (1/8th) of the gas so used or sold* . . . . and *market value at the well* shall not exceed *the amount realized* by LESSEE for such production *computed at the well*."

¶ 145 (emphasis added). As Plaintiffs recognize, gas is no longer sold at the well (also referenced as "wellhead"). Instead, producers must transport their gas through pipelines for eventual sale to third parties. ¶ 128. The key phrases for interpreting the royalty provision are "market value at the well … of the gas … sold" and "market value at the well shall not exceed the amount realized by Lessee for such production computed at the well."

Plaintiffs assert that MEPUSA was "not entitled to deduct post-production costs from the proceeds received by them at the point of sale in calculating the royalties payable to Plaintiff," and underpaid royalties by deducting those costs. ¶¶ 303–304. Alternatively, if such deductions are permitted, MEPUSA supposedly breached the Leases by passing along "artificially inflated, grossly excessive, improper and unreasonable charges for purported post-production costs." ¶ 308.

Plaintiffs' antitrust and RICO claims are a re-hash of their core breach of contract claim. Defendants allegedly conspired to deduct – and each separately deducted – from Plaintiffs' royalties excessive post-production costs for gathering and transportation of the gas:

> The *overcharges for gathering and transportation fees*, and resulting underpayment in royalties, to Plaintiffs was an integral and necessary part of the scheme, as they enabled Defendants to profit from their respective interests in Access Midstream and Appalachia Midstream Service (in the case of Chesapeake), and in the shared ownership of the gathering pipelines (in the case of other Defendants), and later enabled Chesapeake to fulfill the payment obligations that it incurred to Access Midstream in connection with the CMO Transaction, and the other Defendants to acquiesce in and profit from such payments (through their continued common ownership interests in the gathering pipelines).

¶ 287 (as to RICO claims) (emphasis added); *see also* ¶¶ 17, 246, 260 (as to antitrust claims). Because MEPUSA deducts 1/8th of those fees from Plaintiffs' royalties, MEPUSA itself pays 7/8th of the "supra-competitive" fees. *See, e.g.*, ¶ 17, ¶ 226 (noting that "a lessor's post-production deductions cannot exceed 12.5% of total post-production costs); ¶ 246 ("deducting a *proportionate share* of the charges from the royalties") (emphasis added); ¶ 260. Other than the fact that Defendants each purportedly passed along a portion of their post-production costs to Plaintiffs, which is permitted by law and not itself evidence of collusion, there are no non-conclusory factual allegations that Defendants formed an agreement to do so.

QUESTIONS INVOLVED

1. Whether each of the Counts in the Complaint fails under Rule 12(b)(6).

ARGUMENT

The Amended Complaint fails to meet the applicable pleading standards and is factually deficient. To survive a motion to dismiss under Rule 12(b)(6), Plaintiffs must state "enough facts to state a claim to relief that is plausible on its face." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007). "[A] plaintiff's obligation to provide the grounds of his entitle[ment] to relief requires more than labels and conclusions, and a formulaic recitation of a cause of action's elements will not do." *Id.* at 555 (internal quotations omitted). "Threadbare recitals of the elements of a cause of action, supported by mere conclusory statements, do not suffice." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009).

I. PLAINTIFFS' ANTITRUST CLAIMS FAIL AS A MATTER OF LAW.

Plaintiffs' antitrust claims should be dismissed because: (1) Plaintiffs have failed to allege facts sufficient to state a plausible antitrust claim; (2) Plaintiffs have not alleged antitrust injury flowing from any competition-reducing conduct; and (3) Plaintiffs lack antitrust standing because they are neither competitors nor customers in the alleged relevant markets.

A. **Plaintiffs Fail To State A Plausible Antitrust Conspiracy.**

To state a Section 1 claim, Plaintiffs must allege facts showing that MEPUSA was party to a "contract, combination . . . or conspiracy," (15 U.S.C. § 1), which had a "unity of purpose or a common design and understanding or a meeting of minds or a conscious commitment to a common scheme." *In re Flat Glass Antitrust Litig.*, 385 F.3d 350, 357 (3d Cir. 2004) (internal quotation marks omitted). A claim for conspiracy to monopolize under Section 2 likewise requires this essential element. *See W. Penn Allegheny Health Sys. v. UPMC*, 627 F.3d 85, 100 (3d Cir. 2010). Plaintiffs have not met that standard.

The core of Plaintiffs' theory is that Defendants conspired to pay Access a "supra-competitive" rate for gas gathering services and then to pass on to Plaintiffs a fraction of the artificially inflated prices they paid through allegedly improper royalty deductions for post-production costs. *See* ¶¶ 17, 246, 260. Plaintiffs' conclusory allegation of a conspiracy among all Defendants, however, is insufficient to state a Section 1 or 2 antitrust conspiracy claim, particularly as to MEPUSA. *Twombly*, 550 U.S. at 555 ("[O]n a motion to dismiss, courts 'are not bound to accept as true a legal conclusion couched as a factual allegation.'"). Plaintiffs make no allegations about the details of *any* agreement between Access (or anyone else) and MEPUSA and fail to allege any facts showing that MEPUSA engaged in collusive behavior regarding the specific terms of a gas gathering contract with Access or that MEPUSA conspired with anyone to pay Access supra-competitive prices.

Plaintiffs likewise cannot allege specific facts to support their claim that MEPUSA conspired to underpay royalties to Plaintiffs in order to fund a purported conspiracy to overpay Access. The decision to deduct a portion of its gas gathering costs, as MEPUSA was permitted to do by law (*infra*), was entirely consistent with its independent economic interests. The fact that other Defendants also made such deductions cannot support an inference that there was an agreement to do so. *Cf. In re: Chocolate Confectionary Antitrust Litig.*, Nos. 14-2790-14-2795, slip op. at 21 (3d Cir. Sept. 15, 2015) ("'[C]onscious parallelism' . . . is lawful under the Sherman Act [because, among other things,] it is not an agreement [and] cannot alone create a reasonable inference of a conspiracy."). Moreover, Plaintiffs fail to make any well-pled factual allegations that would establish the existence of an agreement. Plaintiffs do not even allege: the amount of post-production costs MEPUSA incurs or how much of that cost MEPUSA deducted from any Plaintiff's royalty payment (from which one could deduce an underpayment); whether and how MEPUSA and the other Lessee Defendants aligned the amount of their royalty deductions; knowledge by MEPUSA of how any other Defendant calculated its royalty payments or made deductions (which would not establish anything more than conscious parallelism in any event). In fact, Plaintiffs allege the opposite. ¶ 4 ("*Each* of the Lessee Defendants is responsible for accounting for and distributing *its share* of the royalties due and owing to royalty interest owners."). Plaintiffs' allegations of conspiracy are thus both deficient and impermissibly speculative. *See In re Baby Food Antitrust Litig.*, 166 F. 3d 112, 132 (3d Cir. 1999) (no antitrust conspiracy where "defendants' prices were neither uniform nor within any agreed upon range of each other").

B. Plaintiffs Do Not Allege An Antitrust Injury.

Plaintiffs also must make a threshold showing of antitrust standing. *Assoc. Gen. Contractors of Cal., Inc. v. Carpenters*, 459 U.S. 519, 535 (1983). The first step in the standing analysis is determining whether the plaintiff suffered antitrust injury (*i.e.*, injury flowing from the alleged reduction in competition) and while "[a] showing of antitrust injury is necessary, [it is] not always sufficient, to establish standing." *Cargill, Inc. v. Monfort of Colo., Inc.*, 479 U.S. 104, 110 n.5 (1986). Plaintiffs not only fail to allege antitrust injury, but the injury they do allege is too remote to confer antitrust standing.

"The antitrust injury requirement ensures that a plaintiff can recover only if the loss stems from a competition-reducing aspect or effect of the defendant's behavior." *Atl. Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 344 (1990); *see also Eichorn v. AT&T Corp.*, 248 F.3d 131, 140 (3d Cir. 2001) (noting that the allegedly anticompetitive conduct must have "a wider impact on the [overall] competitive market"). Here, Plaintiffs' alleged injury does not stem from any competition-reducing aspect or effect of the Defendants' alleged behavior, least of all MEPUSA's, because there was no reduction in competition.

Plaintiffs claim that the Defendants conspired to assist Access in obtaining a monopoly in the alleged Gathering Services market through the transfer of Chesapeake's monopoly power to Access. They claim to be harmed by the price Chesapeake agreed to pay Access for those services, a portion of which is passed along to them in the form of reduced royalty payments. *See, e.g.*, ¶¶ 185, 211-212, 246, 260. Plaintiffs' injury, however, is not the result of any reduction in competition in the alleged market for Gathering Services – following Chesapeake's transfer of its midstream business to Access, there remained only one provider of the gathering services, with no effect on the competitive conditions in the alleged Gas Gathering market at all. Chesapeake merely "transferred" an "existing" monopoly from itself to another, a fact which Plaintiffs concede. ¶¶ 199, 211, 247. The transfer of an existing monopoly has no antitrust significance. *See Brunswick Corp. v. Riegel Textile Corp.*, 752 F.2d 261, 266 (7th Cir. 1984) (An act that "creates no monopoly power[, but] merely shifts a lawful monopoly into different hands . . . has no antitrust significance."); *see also Columbia River People's Utility Dist. v. Portland General Elec. Co.*, 217 F.3d 1187, 1190-91 (9th Cir. 2000) (holding that determining which party would be a state-approved monopolist for an electrical plant had no antitrust significance because the monopoly would exist either way). Plaintiffs' claimed harm is, at best, a result of an allegedly fraudulent deal between Chesapeake and Access that purportedly allowed Chesapeake to pass along a portion of the cost to finance the deal to Plaintiffs under the guise of increased fees. ¶¶ 183-89, 198-212. This is not antitrust injury. *See In re LIBOR-Based Financial Instruments Antitrust Litig.*, 2015 U.S. Dist. LEXIS 107225, at *321 (S.D.N.Y. Aug. 4, 2015) (noting that "[a] conspiracy to commit fraud may resemble an antitrust conspiracy [but] is not thereby transmuted into a violation of the Sherman Act," and concluding that "plaintiffs' injuries were not antitrust injuries because they 'resulted from defendants' misrepresentation, not from harm to competition.'").

Moreover, Plaintiffs fail to plead a competition-reducing aspect or effect of <u>*MEPUSA's*</u> behavior. Plaintiffs do not allege any specific details about MEPUSA's gas gathering contract with Access, or how Access' pricing to MEPUSA did, or even could have, harmed competition. Plaintiffs' vague and conclusory reference to the new gathering agreement "augment[ing]" Access' monopoly power (¶ 211) is insufficient as Plaintiffs fail to explain how it did so, what that means, or how it involved MEPUSA.[3] *See Twombly*, 550 U.S. at 555.

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[3] Plaintiffs allege that the "new gathering agreement [was] entered into by

C. **Plaintiffs Lack Antitrust Standing.**

Even if Plaintiffs had adequately alleged antitrust injury, to have antitrust standing they must be the "proper part[ies]" to bring the action. *Ethypharm S.A. Fr. v. Abbott Labs*., 707 F.3d 223, 232 n.17, 233 (3d Cir. 2013) ("[A]ntitrust injury, 'is a necessary but insufficient condition of antitrust standing.'"). Plaintiffs are not the proper parties because they are neither consumers nor competitors in the alleged relevant markets for gas production, gathering, or mineral rights. *W. Penn Allegheny*, 627 F.3d at 102 (Antitrust injury is limited to "consumers and competitors in the restrained market."); *McCullough v. Zimmer, Inc.*, 382 F. App'x 225, 229 (3d Cir. 2010) (no antitrust standing where plaintiffs were "commission based sales representatives who did business with competitors and consumers in the market for surgical orthopedic devices, [but] not as competitors or consumers themselves"). Thus, Plaintiffs lack standing to sue for any injury sustained as a result of alleged harm in those markets. *W. Penn*, 627 F.3d at 102; *see also Elliott Indus. v. BO Am. Prod. Co.*, 407 F.3d 1091, 1125 (10th Cir. 2005) (no antitrust standing for a party entitled to royalties on oil and gas

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Defendants" collectively (¶ 211), which directly contradicts their specific allegation that the new gas gathering agreements were between Access and "certain Chesapeake Energy subsidiaries, including Chesapeake Appalachia." ¶ 196. Legal conclusions contradicted by factual details are not entitled to deference on a motion to dismiss under Rule 12(b)(6). *Barren v. Allegheny County*, No. 14-692, 2014 U.S. Dist. LEXIS 123475, at *6-7 (W.D. Pa. July 21, 2014).

leases because he was neither a consumer nor a competitor in the market for defendant's products).

Plaintiffs attempt to plead around their clear lack of standing by making a vague and conclusory reference to their injury being "inexplicably intertwined" with Defendants' alleged wrongdoing. *See* ¶¶ 252-253. This narrow exception to the general rule, however, confers standing only where the plaintiff's injury is a "*necessary step* in effecting the ends of the alleged illegal conspiracy." *Blue Shield v. McCready*, 457 U.S. 465, 476-79, 484 (1982) (emphasis added). The Third Circuit has limited this exception to instances where "'both plaintiffs and defendants are in the business of selling goods or services *in the same relevant market*,' though they may not directly compete against each other." *Ethypharm,* 707 F.3d at 237. That is not the case here. Moreover, Plaintiffs do not explain how fractional reductions of post-production costs from royalty payments in the Gas Mineral Rights market was the *necessary means* by which MEPUSA restrained competition in the alleged Gathering Services market. Instead, Plaintiffs make a bare and conclusory assertion that the economic injury they purportedly suffered was the "essential means" by which Chesapeake and Access (*but not MEPUSA*) sought to achieve "illegal and anticompetitive ends." *See* ¶ 252. Such labels and legal conclusions are insufficient to allege antitrust standing. *Twombly*, 550 U.S. at 555.

D. Plaintiffs' Claims Are Particularly Deficient As To MEPUSA.

Plaintiffs' assertion of antitrust claims against MEPUSA in the latest complaint appears to have been an afterthought, in which they attempt to mask the lack of a factual basis through undifferentiated and conclusory group pleading. Rather than allege facts as to each Defendant, Plaintiffs blend all Defendants together by using vague references to "defendants," "Lessee Defendants," "other producers," or "other oil and gas companies." *See, e.g.*, ¶¶ 202, 211-212, 240-41, 244, 246, 248; *compare* ¶¶ 155-62 *with* ¶¶ 167 & 225. Such undifferentiated group pleading fails to provide "a reasonable basis from which [the court] can infer [a] defendant's liability," *In re Ernie Haire Ford, Inc.*, 459 B.R. 824, 835 (Bankr. M.D. Fla. 2011), and "fail[s] to put each defendant on notice of the claims against them." *Pietrangelo v. NUI Corp.*, No. Civ. 04-3223 (GEB), 2005 WL 1703200, at *10 (D.N.J. July 20, 2005). "Even under the most liberal notice pleading requirements . . . , a plaintiff must differentiate between defendants." *Shaw v. Hous. Auth. of Camden*, No. 11-4291 (RMB/AMD), 2012 WL 3283402, at *2 (D.N.J. Aug. 10, 2012) (citation omitted).

1. The Challenged Conduct Is Not Specific to MEPUSA.

To plead an antitrust conspiracy case, Plaintiffs must "specify a time or place that [an] actual agreement . . . occurred, [and] indicate [the] particular individuals or [defendants that] made such an agreement." *Burtch v. Milberg*

Factors, Inc., 662 F.3d 212, 225-26 (3d Cir. 2011) (noting that in *Twombly*, the "plaintiff's failure to allege a 'specific time, place, or person involved in the alleged conspiracies' left 'no clue as to which of the [defendants] (much less which of their employees) supposedly agreed, or when and where the illicit agreement took place.'" (quoting *Twombly,* 550 U.S. at 565 n.10) (alteration in original)). As an initial matter, the vast majority of Plaintiffs' allegations that are specific to any Defendant cannot answer these basic questions as to MEPUSA for the simple reason that they have nothing to do with MEPUSA. Instead, the allegations relate to either the purported conduct by or between Chesapeake and Anadarko in the alleged markets for Gas Mineral Rights and/or Operating Rights, or, by or between Chesapeake and Access in the alleged market for Gathering Services. *See, e.g.*, ¶¶ 12-15, 18, 25, 155-162, 176-77, 182, 189-196, 204-211, 213-222, 242, 247-52, 260-62. Indeed, Plaintiffs allege that the improper royalty deductions are the product of a conspiracy among a list of defendants that does not even include MEPUSA. ¶ 25. Of course, MEPUSA received a partial assignment from *Anadarko* and has not contracted with *Chesapeake*. ¶ 140. This is a prime example of Plaintiffs' improper group pleading in an effort to extend their Chesapeake/Access claims to MEPUSA. *In re Ernie Haire Ford*, 459 B.R. at 835; *Pietrangelo,* 2005 WL 1703200, at *10.

Plaintiffs' failure to differentiate among Defendants is evident throughout the Complaint. For example, Plaintiffs refer to a purported scheme between Chesapeake and Access Midstream, coupled with a conclusory allegation that Plaintiffs were harmed by "Defendants' wrongdoing." ¶ 252. Similarly, Plaintiffs make vague allegations regarding the exclusivity of gas gathering agreements entered into with Appalachia Midstream by Chesapeake and "some or all of the other producer-parties." ¶ 185. Plaintiffs likewise refer to a purported conspiracy between Chesapeake and Anadarko E&P allegedly carried out "by and through their respective conduct set forth above," which "later" included "other oil and gas companies." ¶ 240. Plaintiffs cannot satisfy their pleading burden by using "the collective term 'Defendants' or a list of the defendants named individually but with no distinction as to what acts are attributable to whom . . . ." *Robbins v. Oklahoma*, 519 F.3d 1242, 1250 (10th Cir. 2008).

2. The Few Specific Allegations Against MEPUSA Do Not State An Antitrust Violation.

In the rare instances where MEPUSA is referenced specifically, the alleged conduct is innocuous. In Count One, there is a specific allegation against MEPUSA in paragraph 243 and a general reference to "Lessee Defendants" in paragraph 246 that presumably is intended to encompass MEPUSA. Neither allegation is sufficient to state any part of an antitrust claim against MEPUSA. Paragraph 243 alleges that MEPUSA "support[ed]" a purported conspiracy "to enable Chesapeake and Anadarko to fully exploit" a joint exploration agreement by making "financial commitments" in exchange for working interests in certain Leases. On its face, there is nothing illegal or anticompetitive about such conduct, but Plaintiffs nevertheless attempt to assign nefarious intent to this unremarkable business transaction without any factual allegations.[4] "Merely pleading or pointing to an express contract is not enough to show that an actual conspiracy to restrain trade is afoot." *Loren Data Corp. v. GXS, Inc.*, 501 F. App'x. 275, 280 (4th Cir. Md. 2012). Yet that is exactly what Plaintiffs have done here. *See* ¶ 140. If a mere allegation of financial support were sufficient to state a claim, then any party to a contract (whether a purchaser of working interests such as MEPUSA, or lessors of Gas Mineral Rights such as plaintiffs) could be an alleged co-conspirator.

Further, the Court must "take account of the absence of a plausible motive to enter into the alleged . . . conspiracy." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 595 (1986). There is no allegation that MEPUSA received consideration in addition to or different from the working

[4] Given the capital-intensive nature of natural gas exploration and production in unconventional shale plays, producers commonly mitigate risk and manage capital by having other producers participate in operations in a particular unit or geographic area of interest. Joint ventures, by themselves, do not raise antitrust concerns. *See Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 768 (1984) (recognizing that combinations such as joint ventures "hold the promise of increasing a firm's efficiency and enabling it to compete more effectively").

interest for which it paid. At most, Plaintiffs attempt to explain why MEPUSA would conspire to raise the price that MEPUSA itself pays for gathering services by alleging collectively that "Lessee Defendants" have shared ownership interests in the gathering systems. That generalized allegation fails.

In Count Two, there is no specific allegation against MEPUSA at all. This claim is limited to the alleged market for Gathering Services, in which MEPUSA is a customer (purchaser of gas gathering services), not a competitor. ¶ 259. Moreover, and notwithstanding the impermissible group-pleading references to "Defendants'" conduct throughout this Claim, the specific allegations make abundantly clear that Plaintiffs' complaint concerns the purported conduct of others, not MEPUSA. ¶¶ 260-61, 263-266.

Counts One and Two should be dismissed.[5]

[5] Counts One and Two also should be dismissed because Plaintiffs' alleged geographic market is defective. Plaintiffs "must identify the relevant product and geographic markets and allege that the defendant exercises market power within those markets.'" *Queen City Pizza v. Domino's Pizza*, 124 F.3d 430, 435 (3d Cir. 1997). The relevant geographic market is the "area in which a potential buyer may rationally look for the goods or services he or she seeks." *Tunis Bros. Co., Inc. v. Ford Motor Co.*, 952 F.2d 715, 726-27 (3d Cir. 1991). Plaintiffs have alleged three "alternative" geographic markets for Count 1, the first and third of which are alleged "alternative" geographic markets for Count 2. ¶¶ 237, 258. The last of the alternative markets purports to include the undefined geographic areas covered by three contracts that are not attached to the Amended Complaint, as well as "any other dedicated acreage defined in any and all gathering agreements to which Chesapeake Energy or any of its affiliates or subsidiaries …is a party." *See* ¶ 237.

II. PLAINTIFFS FAIL TO ALLEGE A VALID RICO CLAIM.

Plaintiffs' RICO claims (Counts 3 and 4) are insufficient to state a claim because: (1) Plaintiffs have failed to plead their fraud-based claims with particularity; (2) there are no facts to support an association-in-fact enterprise; (3) the purported RICO enterprise is not plausible; (4) Plaintiffs have not adequately alleged that their injury occurred by reason of the alleged predicate acts; and (5) Plaintiffs fail to allege a RICO conspiracy. Counts 3 and 4 should be dismissed.[6]

A. Plaintiffs Fail To Plead Fraud With Particularity.

Because Plaintiffs' RICO claims are predicated on mail and wire fraud, they must be pled with specificity under Rule 9(b). *Lum v. Bank of America*, 361 F.3d 217, 220 (3d Cir. 2004). Plaintiffs' allegations fall far short of that bar. Plaintiffs are required to allege "the date, place or time of the fraud, or through

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On its face, Plaintiffs' purported geographic market definition fails to provide sufficient notice of the relevant geographic market. *See Marchese v. Cablevision Systems, Corp.*, No. 10-2190, 2011 U.S. Dist. LEXIS 80117, at *21-22 (D.N.J. July 21, 2011). Moreover, Plaintiffs have alleged no facts to support any of the alternative geographic markets from a consumer or supplier standpoint. *See Tunis Bros*., 952 F.2d at 727.

[6] The Court's decision in *Suessenbach Family Ltd. P'ship v. Access Midstream Partners, L.P.*, No. 14-cv-2297, 2015 U.S. Dist. LEXIS 40900, at *1 (M.D. Pa. Mar. 31, 2015), does not compel a different result. That complaint alleged a bilateral RICO enterprise between Chesapeake and Access based on a single gas gathering agreement. Here, Plaintiffs have alleged a much longer and larger RICO enterprise involving 11 defendants, "together with their respective officers, directors, employees and agents," ¶¶ 114-27, 270, but, as explained in detail below, have not alleged facts to adequately support their claims against these different entities and individuals, much less with any of the requisite specificity.

alternative means, . . . inject[] precision and some measure of substantiation into their allegations of fraud." *Id.* at 224 (internal quotation marks omitted). "Plaintiffs also must allege who made a misrepresentation to whom and the general content of the misrepresentation." *Id.* Plaintiffs' allegations do not meet any of these requirements.

Plaintiffs allege that "Defendants" entered into a RICO scheme in order to deprive Plaintiffs of a portion of their royalties by mailing fraudulent royalty statements. *See* ¶ 19. Plaintiffs, however, do not provide the date, time, or place of any of the allegedly fraudulent mailings. Instead, they allege in vague and ambiguous language that "the Defendants" issued royalty statements to Plaintiffs on a "periodic" basis, which was "typically, but not always monthly." ¶¶ 19, 233. Indeed, Plaintiffs themselves recognize the lack of specificity in their allegations, admitting that they are "unable to" "allege with particularity the operative details," and "allege such transmissions *generally*." ¶¶ 27, 279 (emphasis added). Rather than "injecting precision" as they are required to do, Plaintiffs attempt to excuse their lack of specificity by claiming that "the specific dates and contents of such transmissions are within the peculiar knowledge of the Defendants." ¶ 279. Yet Plaintiffs explicitly admit that they are, in fact, in possession of the documents that contain the very information they fail to allege – the royalty statements. *See* ¶ 233 ("Defendants sent royalty statements to Plaintiffs."), ¶ 228-29 ("Each of the

Plaintiffs has received, and continues to receive, periodic royalty payments … accompanied by a statement . . . purporting to summarize the basis on which the payment was calculated.”). Plaintiffs’ failure to include such information does nothing to “substantiat[e] their allegations of fraud.” *Lum*, 361 F.3d at 224.

Additionally, Plaintiffs failed to satisfy Rule 9(b) because they do not allege that any particular Defendant made a misrepresentation to any particular Plaintiff; nor do they allege the specific content of any alleged misrepresentation. *Lum*, 361 F.3d at 224 (allegations of mail fraud insufficient because they did not indicate the date, time, or place of any misrepresentation, or which defendant made misrepresentations to which plaintiff); *Rolo v. City Investing Co. Liquidating Trust*, 155 F.3d 644, 659) (3d Cir. 1998) (affirming dismissal of fraud-based RICO claim for failure to plead with specificity, including “when, by whom, and to whom a mailing was sent, and the precise content of each particular mailing.”).

Plaintiffs concede that the Defendants took different approaches to calculating royalty payments, and that there was no uniformity among the different Defendants in their communications to Plaintiffs. *See, e.g.*, ¶¶ 4, 24. Despite these admitted differences, and the *dozens* of individual plaintiffs involved,[7] Plaintiffs fail to allege for even a single Plaintiff or a single Defendant: (i) which plaintiff

[7] Plaintiffs identify *74 separate plaintiff groups*, many of which include multiple plaintiffs, and *11 individual defendants*. ¶¶ 40-127.

received a royalty statement from which Defendant that included a false or misleading communication; (ii) when that communication was made; (iii) what was purportedly false or misleading in a royalty statement; (iv) what the royalty payments actually were and what they should have been; or (v) when the communications between each (or any) Plaintiff and each (or any) Defendant became false or misleading. Plaintiffs' failure to "link their own injuries to the alleged RICO enterprise" by "alleg[ing] what happened to them" requires dismissal. *Rolo*, 155 F.3d at 659. That failure is particularly glaring given that Pennsylvania's Oil and Gas Lease Act identifies specific information that producers must include in royalty statements or other communications with royalty owners, that MEPUSA specifically identified that statute in its Motion to Dismiss the original Complaint, and that Plaintiffs *still* failed to identify information that MEPUSA supposedly failed to disclose or misrepresented. *See* 58 P.S. § 35.2 (2013).

As with the antitrust claims, Plaintiffs have also impermissibly lumped the Defendants together in an apparent attempt to avoid the specificity required under Rule 9(b) for their RICO claims. *See, e.g.*, ¶¶ 269-298. "Where allegations of fraud are brought against multiple defendants, the complaint must plead with particularity . . . the [specific] allegations of fraud applicable to each defendant." *Donachy v. Intrawest U.S. Holdings, Inc.*, No. 10-4038 (RMB/KMW), 2012 WL 869007, at *2 (D.N.J. Mar. 14, 2012) (quoting *MDNet, Inc. v. Pharmacia Corp.*, 147 F. App'x 239, 245 (3d Cir. 2005)). "A complaint that 'lumps' together numerous defendants does not provide sufficient notice of which defendants" allegedly engaged in the fraudulent conduct. *Tredennick v. Bone*, 647 F. Supp. 2d 495, 501 (W.D. Pa. 2007), *aff'd*, 323 F. App'x 103 (3d Cir. 2008).

While the impermissible group pleading attributes purported conduct to the "Lessee Defendants" collectively, there is not a single allegation in the Amended Complaint that specifically avers that MEPUSA took excessive, unauthorized, or unreasonable deductions from any Plaintiff's royalty payment; nor is there a single allegation that specifically avers that MEPUSA sent a fraudulent royalty statement to any particular Plaintiff. *See, e.g.*, ¶ 167 (merely alleging, without any particularity that "*[e]ach of the other Lessee Defendants* likewise commenced wrongfully deducting post-production costs from Plaintiffs' royalties"), ¶ 233 ("*Each of the Lessee Defendants* sent [fraudulent] royalty statement to Plaintiffs."). While Plaintiffs directly allege, in conclusory terms, that other Defendants have made "impermissible retroactive adjustments" to royalties paid to unspecified plaintiffs, MEPUSA is not among those Defendants. ¶¶ 166, 169. Plaintiffs' lack of specificity alone warrants dismissal of their RICO claims.

B. Plaintiffs Fail To Allege An Association-In-Fact Enterprise.

Plaintiffs claim that Defendants constitute an association-in-fact enterprise. ¶ 270. An association-in-fact enterprise is a "group of persons associated together for a common purpose of engaging in a course of conduct" and "must have at least three structural features: a purpose, relationships among those associated with the enterprise, and longevity sufficient to permit these associates to pursue the enterprise's purpose." *Boyle v. United States*, 556 U.S. 938, 946 (2009). This requires a showing that the association is an "ongoing organization" and that the various associates "function as a continuing unit." *Id.* at 944-45. "While an association-in-fact enterprise 'need not have a hierarchical structure or a "chain of command,"' there must be some decision-making: 'decisions may be made on an ad hoc basis and by any number of methods—by majority vote, consensus, a show of strength, etc.'" *Allstate N.J. Ins. Co. v. Summit Pharm., Inc.*, No. 13-5809, 2014 U.S. Dist. LEXIS 61132, at *29-30 (D.N.J. May 1, 2014) (quoting *Boyle*, 556 U.S. at 948).

Here, Plaintiffs claim that the Defendants are "associated for the common purpose of defrauding leaseholders . . . by . . . overcharging them for post-production costs" through improper royalty reductions. ¶¶ 270, 272. But Plaintiffs provide no factual allegations demonstrating that Defendants have ever functioned or are currently functioning as a continuing unit. As explained above, factually based allegations of an overarching agreement among all Defendants to defraud Plaintiffs or mail fraudulent royalty statements to them are simply absent from the Complaint. Plaintiffs' allegations – such as ¶ 4 concerning separate calculation of royalties - reveal nothing other than unilateral decision-making by each individual Defendant, which is insufficient to allege a RICO enterprise. *In re Ins. Brokerage Antitrust Litig.*, 618 F.3d 300, 374 (3d Cir. 2010) ("'[S]everal individuals' who 'engaged in a pattern of crimes listed as RICO predicates' 'independently and without coordination' 'would not establish the existence of an enterprise.'" (quoting *Boyle*, 556 U.S. at 47 n.4)). Plaintiffs make no allegation of any decision-making by the purported enterprise, but instead merely allege that the enterprise was "primarily managed" and "organized" by Chesapeake, and that each of the Defendants "agreed to, and did, participate in the conduct of the Enterprise" using "independent discretion." ¶ 271. Not only are such allegations deficient under *Twombly*, but they are also insufficient to plausibly suggest an enterprise structure under *Boyle*. *See Allstate,* 2014 U.S. Dist. LEXIS 61132, at *29-30. Plaintiffs' claim that Defendants "expressly or implicitly agreed" that the challenged post-production costs would be passed on to royalty interest holders is likewise conclusory and unsupported by factual allegations. ¶ 276(c); *Twombly*, 550 U.S. at 555.

Further, there are no allegations that MEPUSA in particular entered into any agreement, or had any intention to function as part of a continuing unit with any other Defendant, much less all of them. There are no allegations that

MEPUSA or any other Defendant knew the amount of any post-production costs that were deducted from any Plaintiff's royalty payment by any other Defendant. There are no allegations that MEPUSA or any other Defendant knew how any other Defendant calculated any Plaintiff's royalty payment. Instead, Plaintiffs allege independent accounting and distribution by each Defendant of its respective share. ¶ 4. Plaintiffs failed to allege facts showing that Defendants function as a continuing unit dedicated to a common purpose. *Boyle*, 556 U.S. at 944; *Allstate*, 2014 U.S. Dist. LEXIS 61132, at *30-32. As with their antitrust claims, Plaintiffs do not plead an enterprise that is "plausible on its face." *Twombly*, 550 U.S. at 570; *see also In re Ins. Brokerage Antitrust Litig.*, 618 F.3d at 370 ("The enterprise element of RICO claims is a close analogue of § 1's agreement element. Unless a plaintiff is required at the pleading stage to suggest plausibly the existence of an enterprise structure . . . the RICO statute's allowance for association-in-fact enterprises becomes an open gateway to the imposition of potentially massive costs on numerous defendants, regardless of whether there is even a hint of the collaboration necessary to trigger liability.").

C. <u>Plaintiffs Fail To Allege A Rico Injury.</u>

To state a claim under RICO, a plaintiff "is required to show that a RICO predicate offense 'not only was a "but for" cause of his injury, but was the proximate cause as well.'" *Hemi Group, LLC v. City of New York*, 559 U.S. 1, 9

(2010) (citation omitted). To survive a motion to dismiss, Plaintiffs must allege that their injury occurred "by reason of" the alleged predicate acts. *Id.* at 8. Plaintiffs did not meet their burden.

The injury about which Plaintiffs complain is the "loss of royalties" allegedly "due to deductions . . . of unauthorized or artificially inflated costs for gathering, transportation and other post-production costs." ¶¶ 253, 265, 286. These deductions were purportedly part of the implausible scheme to overpay Access for gathering services and then recoup a small fraction of that overpayment from the Plaintiffs. ¶¶ 227, 276(c), 287. Even if true, these allegations do not demonstrate that Plaintiffs' loss of royalties flows directly from, or occurs "by reason of" the alleged predicate acts of mail and wire fraud. If anything, the mailing of purportedly misleading royalty statements is incidental to, not the cause of, the harm about which Plaintiffs complain. Nor does Plaintiffs' injury flow directly from any wire transfer of funds from one Defendant to another, and the Complaint contains no factual allegations otherwise. *See* ¶ 235.

Plaintiffs' vague claim that the presentation of allegedly fraudulent royalty statements lulled them into believing that no fraudulent scheme had occurred (*see* ¶ 286) is belied by the explicit allegations that the royalty statements are the very thing that put them on notice of the allegedly excessive deductions.

¶ 177 (Plaintiffs' beliefs are "based on comparisons of their respective statements from Chesapeake" and "comparisons . . . with statements from other oil and gas companies."). Thus, Plaintiffs' failure to allege that their injury occurred "by reason of" the predicate acts alleged is fatal to their RICO claim. *Hemi*, 559 U.S. at 9; *Anza v. Ideal Steel Supply Corp.*, 547 U.S. 451, 456-57 (2006).

III. <u>PLAINTIFFS FAIL TO ALLEGE A RICO CONSPIRACY.</u>

"To state a RICO conspiracy claim, plaintiff must allege (1) an agreement to commit the predicate act and (2) knowledge that those acts were part of a pattern of racketeering activity conducted in such a way as to violate one of the substantive provisions of the RICO statute." *Domico v. Kontas*, 2013 U.S. Dist. LEXIS 42104, at *32 (M.D. Pa. Mar. 26, 2013) (internal quotation marks omitted). Plaintiffs' allegations fail to establish the basic elements of a RICO conspiracy claim.

The Complaint is devoid of allegations showing an agreement – or even communications that might suggest one – among Defendants to commit mail or wire fraud, much less an agreement that involves MEPUSA. Plaintiffs merely allege in conclusory fashion that Defendants "agreed to, and did, participate in the conduct of the enterprise." ¶ 271. Such conclusory allegations are insufficient to state a claim. *Twombly*, 550 U.S. at 555. The Complaint also lacks factual allegations that MEPUSA or any other Defendant knew that their independent mailing of royalty statements was part of a pattern of racketeering activity. Plaintiffs allege, again in vague and conclusory language, that "Defendants knew and expressly or implicitly agreed, that [inflated gathering fees] would be passed-on to holders of royalty interests." ¶ 276(c). As explained above, there are no allegations that MEPUSA and the other Defendants aligned the amount of their royalty deductions (knowingly or otherwise), or that any Defendant knew how such royalty payments and deductions were even calculated by any other Defendant.

Finally, "[a]ny claim under section 1962(d) based on a conspiracy to violate [1962(c)] necessarily must fail if the substantive claims are themselves deficient." *Lightning Lube v. Witco Corp.*, 4 F.3d 1153, 1191 (3d Cir. 1993). Thus, Plaintiffs' RICO conspiracy claim independently fails for the same reason it fails under Section 1962(c). *See In re Ins. Brokerage Antitrust Litig.*, 618 F.3d at 373 (A "§ 1962(d) claim must be dismissed if the complaint does not adequately allege 'an endeavor which, if completed, would satisfy all of the elements of a substantive [RICO] offense.'" (quoting *Salinas v. United States*, 522 U.S. 52, 65 (1997))).

IV. PLAINTIFFS' BREACH OF CONTRACT CLAIM <u>FAILS AS A MATTER OF LAW</u>.

The Court should dismiss Count Five for two reasons. First, MEPUSA has the right both under Pennsylvania law and the Leases to deduct post-production costs. Second, Plaintiffs have failed to plead a plausible claim that MEPUSA's deduction of post-production costs was excessive.

A. **MEPUSA May Deduct Post-Production Costs.**

The Pennsylvania Supreme Court held in *Kilmer v. Elexco Land Services, Inc.*, that lessee gas producers may deduct their post-production costs from royalty payments. 990 A.2d 1147 (Pa. 2010). The Court adopted the industry definition of "royalty": "the landowner's share of production, free of expenses of production." *Id.* at 1157 (quoting Howard R. Williams & Charles J. Meyers, Manual of Oil and Gas Terms § R (Patrick H. Martin & Bruce M. Kramer eds., 2009). The Court then distinguished costs of *production*, which are not deductible, from *post-production* costs, which are deductible. "Although the royalty is not subject to costs of production, *usually it is subject to costs incurred after production*, e.g., production or gathering taxes, costs of treatment of the product to render it marketable, *costs of transportation to market*." *Id.* (emphasis added). The Court held that the Gas and Minerals Royalty Act ("GMRA"), then in effect, which required lessors to receive a royalty of at least one eighth (1/8) of the sales proceeds, did not prohibit deductions of post-production costs. *Id.* at 1158.

In reaching this result, the Supreme Court specifically analyzed historical industry practices whereby natural gas producers actually sold gas at the wellhead, so leases calculated royalties "at the wellhead" price. *Id*. at 1155. Rather than being sold at the wellhead, gas now enters gathering systems and intrastate pipelines, but many leases – such as the ones here and in *Kilmer* – continue to calculate royalties based on the "value of the gas when it leaves the ground (hereinafter 'at the wellhead')." To determine the value at the wellhead, *Kilmer* sanctioned calculating royalties by "deducting from the sales price the costs of getting the natural gas from the wellhead to the market," otherwise known as the "net-back" method. *Id.* at 1149. The Court characterized these expenses as post-production costs, which are "the costs of getting the product from the wellhead to the point of sale." *Id.* at 1157. Deducting the post-production costs from the downstream sale price is an appropriate means of approximating the price that had once actually been paid at the wellhead. *Id.* at 1158.

In July 2013, subsequent to *Kilmer*, the Pennsylvania legislature enacted the Oil and Gas Lease Act ("OGLA"), replacing the GMRA that applied in *Kilmer*. The OGLA added several new sections regulating relations between oil and gas lessors and lessees, but retained the GMRA's 1/8th royalty provision materially unchanged. *See* 58 P.S. § 33.3 (2013). The legislature's decision to leave the GMRA's royalty provision intact – without prohibiting deduction of post-production costs – demonstrates its agreement with *Kilmer*'s holding. The legislative history also shows that the legislature expressly rejected any statutory prohibition against post-production cost deductions. *See* Attachment 2, 197 Pa. House Leg. J. 1297, 1303–1307 (June 27, 2013).

Following *Kilmer*, federal courts recognized that the Pennsylvania Supreme Court did not intend to limit the deductibility of post-production costs only to those leases with the precise terms as the lease in *Kilmer*, which expressly referenced deduction of post-production expenses. "Such an application of *Kilmer*, or rather, a non-application of *Kilmer*, defies both common sense and the concept of precedent." *Ulmer v. Chesapeake Appalachia, LLC,* No. 4:08-CV-2062, 2011 WL 1344596, at *2 (M.D. Pa. Apr. 8, 2011) (citations omitted).[8] Judge Jones in *Ulmer* emphasized the importance of permitting producers to deduct post-production costs: "A holding contrary to the one we render today would trigger havoc in a multi-billion dollar industry. More importantly, it would be error." *Id.* at *3 n.1. *See also Puza v. Elexco Land Services, Inc.*, No. 3:09-CV-589, 2010 WL 1791150, at *3 (M.D. Pa. May 3, 2010) (granting motion to dismiss); *Kropa v. Cabot Oil & Gas Corp.*, 716 F. Supp. 2d 375, 378 (M.D. Pa. 2010) (same).

Plaintiffs' Leases, by their plain terms, require the net-back method validated in *Kilmer*: MEPUSA is to calculate the royalty based on the "market value at the well," which "*shall not exceed the amount realized* by LESSEE for

[8] Pursuant to Local Rule 7.1, copies of this and all other unpublished opinions are attached for the Court's convenience at Attachment 1.

such production *computed at the well*." ¶ 145 (emphasis added). The "amount realized" is equivalent to "profits realized," and is calculated using the net-back method – deducting post-production costs from the sale price. *See, e.g., Warren v. Chesapeake Exploration, L.L.C.*, 759 F.3d 413, 417 (5th Cir. 2014) ("The phrase 'amount realized by Lessee, computed at the mouth of the well' means that the royalty is based on net proceeds, and the physical point to be used as the basis for calculating net proceeds is the mouth of the well. … 'the phrase net proceeds' contemplates deductions.'"); *Parnell, Inc. v. Giller*, 372 S.W.2d 627, 628 (Ark. 1963) (holding that expenses for piping and disposing of salt water must be deducted where lease provided royalty on "one-eighth (1/8) of the amount realized from such sale").

In *Pollock v. Energy Corp. of Am.*, the U.S. District Court for the Western District of Pennsylvania, adopting a Magistrate's Report and Recommendation, granted summary judgment for the gas producer on a landowner's breach of contract claim, holding that the applicable royalty provisions – again virtually identical to the royalty provision here – permitted the producer to deduct post-production costs under the net-back method. Civ. No. 10-1553, 2013 WL 275327 (W.D. Pa. Jan. 24, 2013). The Report and Recommendation identified the royalty provision for which the net-back method applied:

> Lessee agrees to pay ... as a royalty for all gas produced and marketed, including all substances contained in such gas, one-eighth (1/8th) of the *net proceeds* received by Lessee from the sale of all gas produced, saved and sold from said premises.
>
> * * *
>
> Lessee covenants and agrees ... [t]o pay Lessor as royalty for all gas and the constituents thereof, (except stored gas and gas produced from any storage horizon), including all liquid, solid or gaseous substances produced and saved from any said sand or sands and/or formations on the lease premises, an amount equal to one-eighth (1/8th) of the *price received by the Lessee from the sale of such gas and the constituents at the well head*.

Pollock v. Energy Corp. of Am., Civ. No. 10-1553, 2012 WL 6929174, at *2 n.2, *3 n.3 (W.D. Pa. Oct. 24, 2012) (Mitchell, U.S.M.J.) (emphasis added). The Report and Recommendation interpreted the language as follows: "all the leases contemplate calculation of royalties by the net-back method which permits [the gas producer] to compute royalties as one eighth of the sale price of the gas minus one-eighth of the post-production costs of getting the gas to market." 2012 WL 6929174, at *2. The District Court disregarded the fact that the lease did not "explicitly identify what particular post-production costs can be deducted," observing that, as "set forth in the Report and Recommendation … *Kilmer*'s recital of post-production costs should not be interpreted as comprehensive and that deduction of marketing costs, generally, is not contrary to law." 2013 WL

275327, at *4; 2012 WL 6929174, at *7.[9]

Thus, Count Five must be dismissed to the extent it alleges that MEPUSA could not deduct post-production costs.

B. Plaintiffs Failed To Plead A Plausible Claim That The Amount of MEPUSA's Deductions Was Somehow Improper.

Plaintiffs' alternative claim – that MEPUSA "violated the implied covenant of good faith and fair dealing inherent in each of the leases … by deducting, or giving effect to the deduction of, purported post-production costs which were and are arbitrary, grossly excessive and unreasonable in amount" (¶ 23) – fails to meet the *Iqbal/Twombly* standard for the simple reason that Plaintiffs failed to plead *any* facts to support this theory. *See* ¶¶ 307, 308. Plaintiffs' failure is particularly inexcusable because the OGLA specifies ten specific pieces of information a lessee/producer is to provide the royalty owner. 58 P.S. § 35.2 (2013). Plaintiffs, however, do not allege any facts showing that MEPUSA failed to provide that information.

Plaintiffs admit that each Lessee Defendant separately calculates

[9] The majority of courts in other gas producing jurisdictions has construed comparable royalty provisions as permitting deductions of post-production costs. *See, e.g., Poplar Creek Dev. Co. v. Chesapeake Appalachia, L.L.C.*, 636 F.3d 235, 243–44 (6th Cir. 2011) (Kentucky law); *Piney Woods Country Life Sch. v. Shell Oil Co.*, 726 F.2d 225, 240 (5th Cir. 1984) (Mississippi law); *Bice v. Petro-Hunt, L.L.C.*, 768 N.W.2d 496, 502 (N.D. 2009); *Heritage Res., Inc. v. NationsBank*, 939 S.W.2d 118, 123 (Tex. 1996); *Atl. Richfield Co. v. State of California*, 262 Cal. Rptr. 683 (Ct. App. 1989).

deductions for post-production costs without coordination with one another. ¶ 4. With only one exception applicable to Statoil (¶ 24), Plaintiffs' Complaint lacks any differentiation among the Lessee Defendants and simply alleges in conclusory and threadbare fashion that the Lessee Defendants "provide Plaintiffs with only cryptic, cursory, incomplete and misleading summaries of the deductions taken in calculating the royalties." ¶¶ 26, 168. Plaintiffs also generally allege in conclusory fashion that the post-production costs "were not charged at arms-length" (¶ 149), "were improper and unreasonable" (¶ 308) or derived from the Chesapeake-Access transaction to which MEPUSA was not a party (¶ 307). Plaintiffs failed to allege facts explaining how or why those conclusions are plausible. And the allegation that MEPUSA "retroactively" "applied [a] new method of calculated royalties" (¶ 305) contradicts earlier allegations in the Amended Complaint showing that other Defendants retroactively calculated royalties but that MEPUSA did not (¶ 24). Plaintiffs did not "allege all claims with particularity as to each defendant," requiring dismissal. *United States v. ex rel. Carter v. Halliburton Co.*, No. 1:08-CV-1162 (JCC), 2009 WL 2240331, at *15 (E.D. Va. July 23, 2009).

V. <u>PLAINTIFFS HAVE NO RIGHT TO DECLARATORY RELIEF</u>.

In Count Nine, Plaintiffs seek a declaratory judgment that Defendants may not deduct post-production expenses or, alternatively, if they can, any such deductions may not exceed "the reasonable market price for the applicable service in a competitive market." ¶ 336(b). Because Plaintiffs' breach of contract claim in Count Five fails as a matter of law, their duplicative request for declaratory relief likewise must fail.

VI. PLAINTIFFS ARE NOT ENTITLED TO AN ACCOUNTING.

Plaintiffs claim that they need an accounting even though: (1) the OGLA identifies the accounting information that producers must provide to royalty owners, 58 P.S. § 35.2 (2013); (2) Plaintiff has not identified any statutorily required information that MEPUSA failed to provide; and (3) Plaintiffs can obtain information concerning calculation of royalties during discovery (if the case is not dismissed, which it should be). Pennsylvania law recognizes two bases for an accounting: legal and equitable. *See Binary Semantics Ltd. v. Minitab, Inc.*, No. 4:07-CV-1750, 2008 WL 763575, at *13 (M.D. Pa. Mar. 20, 2008); *McWreath v. Range Resources – Appalachia, LLC*, No. 13-560, 2015 WL 321651, at *15 (W.D. Pa. Jan. 26, 2015); *Pollock v. Energy Corp. of Am.*, No. 10-1553, 2011 WL 5977422 (W.D. Pa. Nov. 29, 2011). Plaintiffs are entitled to neither.

The right to a legal accounting is incident to a breach of contract claim. *McWreath*, at *15; *Pollock*, at *1; Pa. R. Civ. P. 1021(a). Plaintiffs must prove that MEPUSA "received monies as agent, trustee or in any other capacity whereby the relationship created by the contract imposed a legal obligation upon the defendant to account to the plaintiff for monies received by the defendant" and "that the defendant breached or was in dereliction of his duty under the contract." *Pollock*, at *1-2; *Haft v. United States Steel*, 499 A.2d 676, 677-78 (Pa. Super. Ct. 1985)). Plaintiffs have not alleged that MEPUSA acted as their agent or trustee (it did not) or identified any contractual provision requiring MEPUSA to account. *Iqbal*, 556 U.S. at 678. Setting aside those flaws, Count Six necessarily fails because the OGLA specifies the accounting that producers such as MEPUSA are to provide to Plaintiffs. 58 P.S. § 35.2. The Complaint entirely lacks any facts showing that MEPUSA failed to comply with those provisions.

An equitable accounting likewise is unavailable. A plaintiff may not obtain an equitable accounting in the absence of a fiduciary relationship or when plaintiff possesses an adequate remedy at law. *Minitab*, at *13 (citing *A.M. Skier Agency, Inc. v. Gold*, 747 A.2d 936, 942 (Pa. Super. Ct. 2000)). Plaintiffs have admitted the existence of Leases between them and MEPUSA, so an equitable accounting necessarily fails. *See Harold ex rel. Harold v. McGann*, 406 F. Supp. 2d 562, 578 (E.D. Pa. 2005) (no accounting where parties have contractual relationship); *Casey v. Philadelphia Auto Sales, Co.*, 236 A.2d 800, 802 (Pa. 1968). Moreover, there is no fiduciary relationship; Plaintiffs' fraud allegations fail as a matter of law; Plaintiffs have not alleged any facts showing why the accounts would be complicated; and Plaintiffs may obtain the information they seek through discovery under their breach of contract claim and have an adequate remedy available to them.

VII. PLAINTIFFS' CONVERSION CLAIM FAILS AS A MATTER OF LAW.

Conversion is the "deprivation of another's right of property in, or use or possession of, a chattel, or other interference therewith, without the owner's consent and without lawful justification." *Rahemtulla v. Hassam*, 539 F. Supp. 2d 755, 776 (M.D. Pa. 2008) (quoting *Universal Premium Acceptance Corp. v. York Bank & Trust Co.*, 69 F.3d 695, 704 (3d Cir. 1995)). *See also Gottesfeld v. Mechanics and Traders Ins. Co.*, 173 A.2d 763, 766 (Pa. Super. Ct. 1961). Plaintiffs' claim for conversion fails for two reasons: (1) because Plaintiffs lack a property interest in the amounts that were allegedly converted as MEPUSA was justified to deduct the amounts under the leases; and (2) the gist of the action doctrine bars Plaintiffs' attempt to convert a contract claim into a conversation claim.

First, the "right to payment of money under a contractual agreement does not constitute a property interest for purposes of conversion." *See It's Intoxicating, Inc. v. Maritim Hotelgesellschaft mbH*, No. 11-cv-2379, 2013 U.S. Dist. LEXIS 107149, at *61-62 (M.D. Pa. July 13, 2013) (Mannion, J.); *Rahemtualla*, 539 F. Supp. 2d at 777. Plaintiffs supposedly "were entitled to receive the wrongfully deducted amounts pursuant to their leases." ¶ 318. Plaintiffs thus seek payment of money – received in the first instance by MEPUSA from the sale of gas that MEPUSA alone owned - under a purported contractual agreement to pay a portion of those proceeds to Plaintiffs. ¶¶ 248-249 (Defendants were "not entitled to deduct post-production costs from the proceeds received by them at the point of sale ….") . Those facts, even if true, cannot constitute a property interest under a conversion analysis. *It's Intoxicating*, 2013 U.S. Dist. 107149, at **61-62; *Kia v. Imaging Sciences Int'l, Inc.*, 735 F. Supp. 2d 256, 270 (E.D. Pa. 2010). Moreover, as explained above, MEPUSA properly deducted post-production costs under the express terms of the leases and therefore had consent and lawful justification.

Second, Plaintiffs masquerade their breach-of-contract claim as one for conversion, violating the gist-of-the action doctrine that "operates to preclude plaintiff from re-casting ordinary breach of contract claims into tort claims." *Pittsburgh Constr. Co. v. Griffith*, 834 A.2d 572, 581 (Pa. Super. Ct. 2003). Here, Plaintiffs allege that they were "entitled to receive the wrongfully deducted amounts pursuant to their leases" and that "Defendants wrongfully and intentionally caused authorized or artificially inflated and unreasonable deductions to be taken from royalties otherwise payable to Plaintiffs." ¶¶317-318. Plaintiffs base their breach of contract claim on the same allegations. ¶¶300-301, 303-304, 307. The basis of the duty allegedly breached by the Defendants, as well as the alleged liability of the Defendants, was created by and defined by the oil and gas leases. As a result, there can be no liability. *Pittsburgh Constr. Co.*, 834 A.2d at 584 ("[plaintiff's] tort and breach of contract claims are inextricably intertwined, the success of the conversion claim depending entirely on the obligations as defined by the contract.").

VIII. PLAINTIFFS' CLAIM FOR CIVIL CONSPIRACY FAILS AS A MATTER OF LAW.

To prove a civil conspiracy, Plaintiffs must demonstrate that "two or more persons combined or agreed with intent to do an unlawful act or to do an otherwise lawful act by unlawful means. Proof of malice, i.e., an intent to injure, is essential in proof of a conspiracy. *This unlawful intent must be absent justification*." *Thompson Coal Co. v. Pike Coal Co*., 412 A.2d 466, 472 (Pa. 1979) (emphasis added) (internal citations omitted). "A predicate to any civil conspiracy claim is the presence of an underlying tort." *Festa v. Jordan*, 803 F. Supp. 2d 319, 326 (M.D. Pa. 2011); *McKeeman v. Corestates Bank, N.A., et al.*, 751 A.2d 655, 660 (Pa. Super. Ct. 2000).

First, the Leases and Pennsylvania law permit MEPUSA to deduct Plaintiffs's share of post-production costs, precluding any unlawful conduct.

Second, the conspiracy allegations fail for the reasons set forth above concerning the antitrust and RICO conspiracy claims, *Adams v. Teamsters Local 115*, 214 Fed. App'x 167, 176 (3d Cir. 2007) ("conclusory allegations of 'concerted action,' without allegations of fact that reflect joint action, are insufficient”), and because the conversion claim fails, the civil conspiracy claim likewise fails. *See, e.g., McKeeman*, 751 A.2d at 660. Additionally, “[t]he mere fact that two or more persons, each with the right to do a thing, happen to do that thing at the same time is not by itself an actionable conspiracy.” *Fife v. Great Atlantic and Pacific Tea Co.*, 52 A.2d 24, 39 (Pa. 1947).

Third, Plaintiffs do not allege a factual basis for malice. “‘Malice requires … that the sole purpose of the conspiracy was to injure the plaintiff,’ and that the intent was without justification.” *Festa*, 803 F. Supp. 2d at 327. A “showing that the person acted for professional reasons, and not solely to injure the plaintiff, negates a finding of malice.” *Id.* (emphasis in original)*; Grose v. Procter & Gamble Products*, 866 A.2d 437, 441 (Pa. Super. Ct. 2005) (“Appellant’s Amended Complaint … merely alleges in the most general terms that agents of P&G conspired to intentionally harm Appellant for no reason.”) (affirming grant of preliminary objections); *Raneri v. DePolo*, 441 A.2d 1373, 1376 (Pa. Commw. Ct. 1982) (affirming grant of preliminary objections).

CONCLUSION

For the foregoing reasons, Mitsui E&P USA LLC asks the Court to dismiss the Complaint with prejudice.

Dated: September 18, 2015

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CERTIFICATE OF WORD COUNT

I, John K. Gisleson, hereby certify that this Brief contains 9,976 words and complies with Local Rule 7.8(b)(2), as modified by ECF No. 106.

MORGAN, LEWIS & BOCKIUS LLP

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CERTIFICATE OF SERVICE

I hereby certify that on September 18, 2015, true and correct copies of the foregoing **Memorandum of Law in Support of Defendant Mitsui E&P USA LLC'S Motion to Dismiss** were served on all counsel of record via the Court's CM/ECF Court Filing System as follows:

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