NERA
ECONOMIC CONSULTING

Case & Project Experience

The First Alberta Oil to the Texas Gulf Coast: NERA's Role in *Energy Transfer Partners vs. Enterprise Product Partners and Enbridge Inc.*

Overview

Energy Transfer Partners (ETP) and Enterprise Products Partners entered into an unwritten partnership in April 2011 to market the construction of a new pipeline linking the traditional US crude oil hub of Cushing, Oklahoma to the Gulf Coast of Texas—completing the last link in the economic chain tying Alberta crude oil to the largest of North America's refining complexes on the Texas Gulf Coast. In August 2011, ETP/Enterprise attracted a major oil company, Chesapeake Energy Corp., to sign onto their venture. Almost simultaneously, however, and without consulting ETP, Enterprise announced the dissolution of that venture to pursue a similar project with Enbridge, Inc. ETP immediately filed suit in Texas court to recover damages due to Enterprise's breach of its fiduciary duty in abandoning its original pipeline venture. ETP retained NERA to analyze the economic similarities between the ETP/Enterprise pipeline and the Enterprise/Enbridge pipeline and to compute the value of the lost opportunity to ETP if the court found a fiduciary breach with regard to the ETP/Enterprise partnership.

Background

The crude oil transportation business has changed rapidly in the past five years as new oil sands and oil shale plays have been developed in Alberta, the North Dakota Bakken region, and West Texas. In the past, imported crude oil came by tanker to the Texas Gulf Coast refineries before being piped north, as refined products, throughout the US. As with North American natural gas—where unconventional development from the Marcellus field has changed traditional pipeline flows—the new sources of crude oil created a new demand for crude oil pipeline capacity south to those same Texas refineries to displace imported tanker cargoes. The lack of a pipeline from Cushing to the Gulf Coast caused oil to pile up in the tank farms there; a glut that drove the US domestic West Texas Intermediate price index nearly $20 per barrel below the world price of similar crude oil (priced at the Brent index). Given the historical and institutional problems involved in building new crude oil lines (because of century-old legislation, the federal government does not regulate the route or capacity of such lines, in contrast to natural gas lines), the first mover to link Cushing southward to those Texas Gulf Coast refineries would capture that spread.

By signing Chesapeake, the ETP/Enterprise joint venture held a credible first-mover advantage over other firms trying to affect such a southward crude oil pipeline link to the Texas Gulf Coast. The value of being a first mover in such a pipeline market, and the extent to which joint-venture duties had been breached, was the crux of the trial.

NERA's Role

ETP retained NERA Senior Vice President Jeff D. Makholm to assess pipeline markets in the region, the value of first-mover status in the changing crude oil markets in North America, and the value the lost opportunity for ETP if a jury found that fiduciary duties had been breached. Dr. Makholm is NERA's long-time expert on the economics of gas and oil pipelines. Among other writings, Makholm published his monograph *The Political Economy of Pipelines: A Century of Comparative Institutional Development* (University of Chicago Press, 2012) to describe how institutional factors in various parts of the world—with which Dr. Makholm has first-hand experience—affect pipeline development, economics, and pricing.

Dr. Makholm and his staff performed an economic analysis of the first-mover link in that region, finding the entire project as eventually modified and expanded by Enterprise/Enbridge to be worth more than $2 billion. He also determined the value to ETP of the alleged breach, presenting both economic valuations to the Dallas jury. An important element in Dr. Makholm's evidence was the value of the "anchor tenant" represented by Chesapeake and the potential for that opportunity to bode well for a successful ETP/Enterprise pipeline venture.

The Result

In a decision that the *Dallas Morning News* (4 March 2014) called a "potential landmark verdict," the jury, in a 10-2 decision, ordered Enterprise to pay ETP $319 million in damages for violating "the corporate version of a common law marriage." The jury computed the size of the award on the "anchor tenant" value of the Chesapeake commitment to what they found to be a valid ETP/Enterprise joint venture.

This case redefined the characterization of a partnership between firms in Texas, while also setting a precedent for the size of a Texas jury award in a major case involving the modern movement of oil and gas in competitive North American energy markets.

About NERA

NERA Economic Consulting (**www.nera.com**) is a global firm of experts dedicated to applying economic, finance, and quantitative principles to complex business and legal challenges. For over half a century, NERA's economists have been creating strategies, studies, reports, expert testimony, and policy recommendations for government authorities and the world's leading law firms and corporations. We bring academic rigor, objectivity, and real world industry experience to bear on issues arising from competition, regulation, public policy, strategy, finance, and litigation.

NERA's clients value our ability to apply and communicate state-of-the-art approaches clearly and convincingly, our commitment to deliver unbiased findings, and our reputation for quality and independence. Our clients rely on the integrity and skills of our unparalleled team of economists and other experts backed by the resources and reliability of one of the world's largest economic consultancies. With its main office in New York City, NERA serves clients from more than 25 offices across North America, Europe, and Asia Pacific.

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