IN THE SUPERIOR COURT OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

STATOIL MARKETING & TRADING (U.S.) INC. Plaintiff, v. WESTERN REFINING YORKTOWN, INC. Defendant.	C.A. No. 08C-03-170 RRC

Submitted: December 3, 2009
Decided: December 15, 2009

On Plaintiff's Motion to Dismiss Defendant's
Fourth, Fifth, and Sixth Counterclaims
DENIED.

MEMORANDUM OPINION

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I. INTRODUCTION

This non-jury case arises from a multi-million dollar purchase/sale agreement of 66 million barrels of Grane crude oil between Plaintiff Statoil Marketing & Trading (US) Inc. ("Statoil") and Defendant Western Refining Yorktown, Inc. ("Western"). While the case is largely a case of competing breach of contract claims, Western has asserted three additional counterclaims, two of which sound in products liability and the third in negligent misrepresentation. These three counterclaims stem from Western's allegation that Statoil failed to warn Western about certain hazardous properties of the Grane crude oil, and, as a consequence of that failure, Western suffered substantial damage to its refinery.

The issues raised by Statoil's motion to dismiss these counterclaims are (1) whether crude oil can be a "product" for purposes of products liability law, (2) whether Statoil had a duty to warn Western about the alleged hazardous properties of Grane crude oil, and (3) whether Statoil had a duty to disclose all material facts about the corrosive properties of Grane to Western despite the fact that the contract entered into by the parties was an arms-length business transaction between two sophisticated parties.

Because the Court finds that further discovery is needed to resolve all of these issues, the Court denies Statoil's motion to dismiss and will allow the parties to take discovery on these claims.

II. FACTUAL AND PROCEDURAL HISTORY

In February 2004, Western's predecessor[1] and Statoil entered into an agreement whereby Statoil was to supply Western's refinery in Yorktown, Virginia with 66 million barrels of Grane crude oil (the "Agreement"). Apparently, no refinery had ever commercially refined Grane,[2] which is a high acid crude oil.[3] During negotiations of the Agreement, Statoil provided Western with an assay setting forth the acidity of Grane (the "Preproduction Assay"). The Agreement, however, provided that the quality of Grane may vary from the Preproduction Assay. Specifically, the assay stated:

> Both parties recognize that the quality of Grane may vary from the quality of Grane defined in the Preproduction Assay and as included as Appendix II. A significant variation in the quality of Grane from the Preproduction Assay to subsequent assays will result in an adjustment of the price as set out in Appendix I.[4]

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[1] For purposes of this motion, the Court will refer to both Western Refining Yorktown, Inc. and its predecessor Giant Yorktown, Inc. as "Western."
[2] Def. Ans. Brief, at 4.
[3] The acidity of crude oil is indicated by its "TAN" or total acid number. According to Statoil, "Grane is sometimes referred to as an 'opportunity crude' because it can be purchased for a lower price than lower-TAN, or otherwise easier-to-refine, 'benchmark crudes.'" Pl. Mot. to Dismiss, at 3-4.
[4] Exhibit 1 of Pl. Mot to Dismiss (the "Agreement"), at Art. 3.2.

The Agreement further provided that "[t]he Oil to be supplied under this Agreement shall be Grane crude oil of normal export quality."[5]

The warranty section of the Agreement stated in part that:

> Seller warrants good title to the Oil sold under this Agreement and warrants it conforms to the quality specifications set forth in Article 3 and shall be free from all royalties, taxes, liens, claims and other charges and encumbrances. **HOWEVER, SELLER MAKES NO WARRANTY AGAINST INFRINGEMENT OF ANY PATENT, TRADEMARK OR COPYRIGHT. FURTHER, EXCEPT AS PROVIDED HEREIN, SELLER MAKES NO OTHER REPRESENTATION OR WARRANTY, WRITTEN OR ORAL, EXPRESS OR IMPLIED, INLCUDING BUT NOT LIMITED TO, ANY REPRESENTATION OR WARRANTY THAT THE OIL SOLD TO BUYER WILL BE MERCHANTABLE OR FIT FOR A PARTICULAR PURPOSE, OR WILL CONFORM TO MODELS OR SAMPLES, OR THAT IT WILL MEET SPECIFICATIONS OTHER THAN THOSE EXPRESSLY PROVIDED HEREIN.**[6]

In addition, Section 32.4 provided that "no representations or warranties shall be implied or provisions added in the absence of a written agreement to such effect between the Parties" and that "[n]o promise, representation or inducement has been made by any party that is not embodied in this Agreement . . . ."[7]

In order for Western's refinery to be able to accommodate Grane crude oil, Western upgraded the refinery. However, a 2007 inspection of a crude oil processing tower allegedly revealed extensive corrosion. Consequently, Western began to reduce the amount of Grane crude oil

[5] *Id*. at Art. 3.1.
[6] *Id*. at Art. 26.
[7] *Id*. at Art. 32.4.

processed on a daily basis,[8] and ultimately declared "Force Majeure" on January 29, 2008. Force Majeure is defined under the Agreement as "any cause or event reasonably beyond the control of a Party . . . whether or not foreseeable."[9] The Agreement further provided that "[n]either Party shall be liable to the other if it is rendered unable by an event of Force Majeure to perform in whole or in party any obligation or condition of this Agreement."[10]

In March 2008, Statoil filed a breach of contract complaint against Western in this Court seeking damages in excess of $100,000,000. The complaint alleges that Western repudiated the Agreement and improperly declared Force Majeure. In May 2008, Western filed an answer denying Statoil's claims and asserting claims for declaratory relief and breach of contract. In September 2009, Western amended its answer in order to add its fourth, fifth, and sixth counterclaims—(4) failure to warn (strict liability); (5) failure to warn (negligence); and (6) negligent misrepresentation. Statoil has moved to dismiss these three counterclaims.

[8] Under the Agreement, the delivery of Grane was at the initial rate of 20,000 barrels per day, which was then increased to 40,000 barrels per day following Western's upgrades to the refinery. Agreement, at Art. 4.2.
[9] *Id*. at 2.1.
[10] *Id*. at 7.3.

III. THE CONTENTIONS

The parties agree that the legal issues in this motion are governed by the law of New York, as provided in the Agreement.

A. Plaintiff's contentions

Statoil argues that the Court should dismiss Western's fourth and fifth counterclaims, which are products liability claims, because crude oil is not a "product" for purposes of products liability law. In support of this argument, Statoil relies on Black's Law Dictionary, which defines "product" as something that is "usually . . . the result of fabrication or processing."[11] Citing to a U.S. Department of Energy website, Statoil contends that:

> Crude oil is a mixture of liquid hydrocarbons found in natural underground reservoirs that is commonly understood to have been formed from the remains of plants and animals that lived hundreds of millions of years ago. With no human intervention, this material was gradually covered with layers of sediment, and with extreme pressure and high temperatures over hundreds of millions of years, transformed into the mix of liquid hydrocarbons known today as crude oil.[12]

Therefore, Statoil asserts that because crude oil is a not the result of "fabrication or processing,"[13] crude oil is not a product. Statoil further

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[11] BLACK'S LAW DICTIONARY 1125 (7th ed. 1999).
[12] Pl. Mot. to Dismiss, at 2-3 (citing "Where Our Gasoline Comes From." Energy Information Administration, *publically available at* http://www.eia.doe.gov/bookshelf/brochures/gasoline/index.html). Statoil contends that the Court may take judicial notice of this website.
[13] *Id*. at 9.

contends that the public policy underlying products liability law would not be served by permitting Western's fourth and fifth counterclaims to go forward in this case because crude oil is not sold to members of the public.

In the alternative, Statoil claims that even if crude oil is deemed a product, Statoil had no duty to warn Western about its properties because crude oil poses "obvious risks" such as the "potential corrosive effect . . . on refining equipment."[14] Therefore, Statoil contends that "a warning about the corrosive nature of Grane would have provided no benefit to [Western] because as a refiner it was clearly aware of the obvious corrosion risks posed by processing crude oil."[15]

Moreover, Statoil contends that it had no duty to warn Western of the dangers of Grane because Western had actual knowledge of the hazards associated with refining Grane. Statoil claims that the Preproduction Assay it provided to Western before entering into the Agreement "plainly shows that Grane is highly acidic."[16] Statoil further asserts that Western's "metallurgical upgrades to various equipment and units of the Yorktown

[14] *Id*. at 14.
[15] *Id*.
[16] *Id*. at 16

refinery" demonstrate that Western knew of the high acid content as well as the potential corrosive affect of Grane.[17]

Finally, Statoil contends that Western's sixth counterclaim, which alleges negligent misrepresentation, must be dismissed because Statoil had no duty to disclose all of the material facts about the corrosive properties of Grane. Specifically, Statoil asserts that "none of the limited situations in which a New York court would recognize a duty to disclose between parties to an arms-length business transaction applies."[18]

B. Defendant's contentions

Western alleges that crude oil is a product pursuant to the Restatement (Third) of Torts, which provides that "[m]ost courts treat raw materials as products for the purposes of strict products liability in tort, provided that the injury resulted from an identifiable defect in the raw material."[19] Western further contends that even if the Court were to accept the Black's Law Dictionary of the word "product," crude oil does undergo some amount of "processing" before it reaches the refinery, and thus should be considered a "product."

[17] *Id*. at 18
[18] *Id*. at 19.
[19] RESTATEMENT (THIRD) OF TORTS: *Prod. Liab*. § 19 (1998).

Western cites a textbook on crude oil as well as Statoil's own website for the proposition that crude oil as sold is a result of some "processing."[20] Western contends that the Court should decline to take judicial notice of the U.S. Department of Energy website to which Statoil cites for the proposition that crude oil is not a result of "processing." Western further contends, however, that if the Court does rely on this website, and converts this motion to dismiss to a motion for summary judgment, that further discovery would be needed before Western could respond to the motion. Specifically, according to an affidavit submitted by Western's counsel pursuant to Superior Court Civil Rule 56(f), discovery would be needed on, among other things, "the extent to which Grane crude oil is processed by Statoil prior being shipped for sale."[21]

In addition, Western claims that Statoil had a duty to warn Western of the dangers of refining Grane because those dangers were not obvious, and that "Western should be entitled to prove through discovery that the particular naphthenic acids present in Grane crude oil were latent dangers

[20] Def. Ans. Brief, at 8 (citing FRANCIS M. MANNING & RICHARD E. THOMPSON, OILFIELD PROCESSING: CRUDE OIL (OILFIELD PROCESSING OF PETROLEUM), 1-4 (Pennwell Books 1995)).

[21] Farnan Aff., at 3 (providing that "a thorough development of the record is needed before Statoil's Motion, if converted to a motion for summary judgment, can be briefed and ultimately considered by the Court").

giving rise to a duty to warn."[22] Furthermore, Western contends that it did not have actual knowledge of all the hazards associated with refining Grane; rather Western claims that it "did not fully appreciate the dangerous qualities of the Grane crude oil."[23] Western also states that "[t]he extent of Western's knowledge—particularly as compared to Statoil's—is far from undisputed."[24]

Finally, Western asserts that it has stated a claim for negligent misrepresentation because "Statoil had superior knowledge and that, had Western been aware of all material facts know to Statoil, it would have not agreed to process Grane crude oil a[t] such a high percentage of the Yorktown refinery's crude oil slate."[25]

IV. STANDARD OF REVIEW

A motion to dismiss under Rule 12(b)(6) requires the Court to determine whether a claimant may recover "under any reasonably conceivable set of circumstances susceptible of proof."[26] When deciding a motion to dismiss, the Court accepts as true all well-pleaded allegations, and

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[22] Def. Ans. Brief, at 15.
[23] *Id*. at 17.
[24] *Id*. *See also* Farnan Aff., at 3 (requesting an opportunity to conduct discovery, *inter alia*, on "Statoil's knowledge of the proper processing of Grane crude oil."
[25] Def. Ans. Brief, at 19.
[26] *Spence v. Funk*, 396 A.2d 967, 968 (Del. 1978).

draws all reasonable inferences in favor of the claimant.[27] Therefore, dismissal will only be warranted where the Court finds that under no reasonable interpretation of the facts alleged could the claim entitle the claimant to relief.[28]

V. DISCUSSION

A. The products liability claims

Western's fourth and fifth counterclaims are products liability claims. In order for Western to obtain relief pursuant to these claims, crude oil must be a "product" for purposes of New York products liability law and Statoil must have had a duty to warn Western of Grane's hazardous properties.

i. Is crude oil a "product" for purposes of New York products liability law?

The parties have not cited, nor has the Court found, any cases from any jurisdiction that directly hold that crude oil is a "product" in the context of a products liability claim.[29] Black's Law Dictionary defines the word "product" as:

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[27] *Ramunno v. Crawley*, 705 A.2d 1029 (Del. 1998).
[28] *Luscavage v. Dominion Dental USA, Inc.*, 2007 WL 901641, at *2 (Del. Super.).
[29] Western claims that the court in *Hobart v. Sohio Petrolem Co.*, 255 F. Supp. 972, 973 (N.D. Miss. 1966) implicitly decided that crude oil was a product because in that case there was a trial on the plaintiff's products liability claims. Because the Court does not determine as a matter of law on this motion to dismiss whether crude oil is a "product" the Court need not decide the import of this case on this motion.

> Something that is distributed commercially for use or consumption and that is usually (1) tangible personal property, (2) the result of fabrication or processing, and (3) an item that has passed through a chain of commercial distribution before ultimate use or consumption.[30]

Under this definition, Statoil asserts that crude oil cannot be a product because it is not the result of "fabrication or processing."

Statoil relies on a U.S. Department of Energy website for the proposition that:

> With no human intervention, this material [remains of plants and animals] was gradually covered with layers of sediment, and with extreme pressure and high temperatures over hundreds of millions of years, transformed into the mix of liquid hydrocarbons know today as crude oil.[31]

Statoil contends that the Court can take judicial notice of this website because the facts contained therein are "not subject to reasonable dispute."[32]

On the other hand, Western, quoting a secondary authority, asserts that "crude oil . . . must be processed before sale, transport, reinjection or disposal."[33] Western also cites to Statoil's own website, which describes the terminal where Grane is loaded for shipment as a "production facility."[34] It appears to the Court that at this stage of the proceedings, the question of

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[30] BLACK'S LAW DICTIONARY 1125 (7th ed. 1999), cited in Pl. Mot. to Dismiss, at 9.
[31] Pl. Mot. to Dismiss, at 3 (citing "Where Our Gasoline Comes From." Energy Information Administration, *publically available at* http://www.eia.doe.gov/bookshelf/brochures/gasoline/index.html).
[32] *Id*. at 3, n. 1 (citing D.R.E. 201(b)).
[33] Def. Ans. Brief, at 11 (quoting FRANCIS M. MANNING & RICHARD E. THOMPSON, OILFIELD PROCESSING: CRUDE OIL (OILFIELD PROCESSING OF PETROLEUM), 1-4 (Pennwell Books 1995)).
[34] *Id*. at 11. *See* http://www.statoil.com/en/ouroperations/terminalsrefining/stureterminal/pages/default.aspx.

what, if any, "processing" that crude oil undergoes before arrival at a refinery is a disputed and undeveloped factual issue. Therefore, the Court declines to take judicial notice of whether crude oil offered for sale results from "processing or fabrication" because that fact, at least at this stage, seems "subject to reasonable dispute."[35]

The Restatement (Third) of Torts: *Products Liability* defines a "product," and the Court notes that New York "generally follows the guidelines set forth in the Restatements with respect to products liability."[36] The Restatement definition states, in pertinent part, that

> A product is tangible personal property distributed commercially for use or consumption.[37]

Additionally, the Reporters' Note to section 19 provides:

> Most courts treat raw materials as products for the purposes of strict liability in tort, provided that the injury resulted from an identifiable defect in the raw material.[38]

Notably, the comment to section 19 also states that:

> Raw materials are products, whether manufactured, such as sheet metal; processed, such as lumber; or gathered and sold or distributed in raw condition, such as unwashed gravel and farm product.[39]

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[35] D.R.E 201(b) (providing that "[a] judicially noticed fact must be one not subject to reasonable dispute in that it is . . . capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned").
[36] *Tenuto v. Lederle Lab.*, 695 N.Y.S.2d 259, 262 (N.Y. Sup. Ct. 1999).
[37] RESTATEMENT (THIRD) OF TORTS: *Prod. Liab.* § 19 (1998).
[38] *Id.* at Reporters' Note.
[39] *Id.* at cmt. b.

As one court has noted, under the Restatement, "strict products liability applies to suppliers of articles that have not undergone any processing."[40] As such, assuming (but not now deciding) that this Court will, at some later point when discovery is concluded, apply the Restatement approach, crude oil might, as Western argues, be a "product" for purposes of Western's fourth and fifth counterclaims, regardless of whether the crude oil has undergone any processing, if Western can show "an identifiable defect in the raw material."

This Court, at this juncture, declines to express any opinion on whether or not this particular Grane crude oil is a "product" as a matter of New York law. As stated earlier, no case has been located by either of the parties or this Court holding explicitly that crude oil is or can be a "product." Further discovery on Western's fourth and fifth counterclaims is needed in order for any such determination to be made.

ii. Did Statoil have a duty to warn Western of Grane's hazardous properties?

Both of Western's products liability claims are also dependent on whether Statoil had a duty to warn Western of Grane's hazardous properties.

[40] *Southwest Pet Prods., Inc. v. Koch Indus.*, Inc., 273 F. Supp. 2d 1041, 1052 (D. Ariz. 2003) (holding that strict liability could apply to wheat containing high levels of vomitoxin even though "vomitoxin is a 'naturally occurring condition in the wheat,' rather than a result of 'something that went wrong during the manufacturing process'").

Under New York law, there are two situations where a court may decide a failure to warn claim as a matter of law. First, some "hazards need not be warned of as a matter of law because they are patently dangerous or pose open and obvious risks."[41] Second, "where the injured party was fully aware of the hazard through general knowledge, observation or common sense . . . lack of a warning about that danger may well obviate the failure to warn as a legal cause of an injury resulting from that danger."[42]

The Court, however, cannot dismiss Western's failure to warn claim at this time under either of these theories. In order to dismiss the claim under the first theory, the dangers of crude oil must be "open and obvious." Statoil relies on *Hobart v. Sohio Petroleum Co.* for the proposition that crude oil is "patently dangerous and poses obvious risks."[43] In *Hobart*, the Court stated that "[c]rude oil is, for more than one reason, an inherently dangerous substance."[44] However, in *Hobart*, the dangerous properties of crude oil at issue were its "fire hazard" and its "suffocation hazard," which are not at issue here. Moreover, *Hobart* was decided after a bench trial, with the benefit of a developed factual record, whereas here, on this motion to dismiss, the Court can only rely on the pleadings.

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[41] *Liriano v. Hobart Corp.*, 700 N.E.2d 303, 308 (N.Y. 1998).
[42] *Id.*
[43] Pl. Mot. to Dismiss, at 13.
[44] 255 F. Supp. at 975.

Western has pled that "the information that [Statoil] failed to disclose concerning the dangerous and corrosive nature of Grane crude oil was not open and obvious . . . ."[45] On this motion to dismiss, the Court must accept this allegation as true. Therefore, the Court cannot conclude as a matter of law that the dangers of Grane were open and obvious and that Statoil had no duty to warn Western. Rather, Western is entitled to take discovery on this issue in attempt to support its claim.

In addition, the second alternative theory would require that Western have "actual knowledge" of the dangers. Statoil cites to the Agreement to demonstrate Western's knowledge. The Preproduction Assay, which Statoil provided to Western before entering into the Agreement, indicates that Grane is highly acidic. Moreover, the Agreement provides that "the quality of Grane may vary from the quality of Grane defined in the Preproduction Assay."[46]

Western has pled, however, that it "did not fully appreciate the dangerous qualities of the Grane crude oil."[47] Although the Court notes that the phrase "fully appreciate" implies that Western had some knowledge of Grane's dangerous properties, without the benefit of discovery the Court

[45] Def. Ans. and Counterclaim, at ¶ 102.
[46] Agreement, at 3.2
[47] Def. Ans. and Counterclaim, at ¶ 100.

cannot determine at this stage of the proceedings exactly what knowledge Western had and what knowledge it was entitled to have. Therefore, the Court will allow the parties to take discovery as to Western's fourth and fifth counterclaims.

B. The negligent misrepresentation claim

In order to plead negligent misrepresentation under New York law, a claimant must allege that: "(1) the parties stood in some special relationship imposing a duty of care on the defendant to render accurate information, (2) the defendant negligently provided incorrect information, and (3) the plaintiff reasonably relied upon the information given."[48] While some New York courts have stated that New York recognizes "the ancient rule of *caveat emptor*," there are some situations where courts applying New York law have found that a party to a business transaction has a duty to disclose certain facts material to the transaction.[49] For example, such a duty exists "where one party possesses superior knowledge, not readily available to the

[48] *Tomoka Re Holdings, Inc. v. Loughlin*, 2004 WL 1118178, at *6 (S.D.N.Y.).
[49] *See Brass v. Am. Film Techs., Inc.*, 987 F.2d 142, 150 (2d Cir. 1993).

other, and knows that the other is acting on the basis of mistaken knowledge."[50]

Statoil claims that it had no duty to disclose all the material facts concerning Grane's corrosive properties, and that Western has failed to sufficiently plead negligent misrepresentation under Superior Court Civil Rule 9(b). The Court finds, however, that Western has sufficiently pled each of the elements required for a negligent misrepresentation claim. Western claims that (1) Statoil "had knowledge and experience relating to the properties of Grane crude oil which was superior to that of Western,"[51] (2) Statoil "negligently failed to disclose" material information to Western,[52] and (3) Western "relied on the information provided by [Statoil] and did not know the information was incomplete."[53]

Further discovery is needed for the Court to determine whether Statoil in fact had any "superior knowledge" (at least to the extent that might expose Statoil to potential liability). Therefore, the Court will not dismiss Western's sixth counterclaim.

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[50] *Creative Waste Mgmt., Inc. v. Capitol Envtl. Servs., Inc.*, 429 F. Supp. 2d 582, 609 (S.D.N.Y.) (applying New York law). *See also Century Pac., Inc. v. Hilton Hotels Corp.*, 2004 WL 868211, at *9 (S.D.N.Y.) (stating that there is a "tendency in New York to apply the rule of 'superior knowledge' in an array of contexts in which silence would at one time have escaped criticism").
[51] Def. Ans. and Counterclaim, at ¶ 98.
[52] *Id.* at ¶ 115.
[53] *Id.* at ¶ 116.

VI. CONCLUSION

For the reasons stated above, Plaintiff's motion to dismiss Western's fourth, fifth, and sixth counterclaims is **DENIED**. Statoil will have the opportunity to reassert these claims as motions for partial summary judgment pursuant to Superior Court Civil Rule 56 upon completion of the factual record pertinent to the issues raised by these counterclaims.

IT IS SO ORDERED.

Richard R. Cooch

oc: Prothonotary