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PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Agenda ID # 12905

ENERGY DIVISION **RESOLUTION O-0058**

May 1, 2014

R E S O L U T I O N

Resolution O-0058 Ellwood Pipeline, Inc. requests approval of a rate and tariff terms and conditions for crude oil transportation service on a new pipeline.

PROPOSED OUTCOME: This Resolution approves the rules and regulations and rate tariffs for transportation service on Ellwood Pipeline, Inc.'s Los Flores pipeline.

SAFETY CONSIDERATIONS: The transportation of crude petroleum and indirect products of oil and gas wells involves inherent safety risks. It is the utility's responsibility to adhere to all commission rules, decisions, General Orders, and statutes, including Public Utility Code Section 451, to take all actions " . . . necessary to promote the safety, health, comfort, and convenience of its patrons, employees and the public."

ESTIMATED COST: Unknown.

By Advice Letter 4 filed on February 27, 2013.

SUMMARY

This Resolution authorizes Ellwood Pipeline, Inc.'s (Ellwood) rate and rules and regulations tariffs for crude oil transportation service on the newly constructed Los Flores pipeline. Advice Letter (AL) 4 proposes a transportation service rate of $4.88 per barrel (bbl.).

The only current shipper on the pipeline is Conoco Phillips.

Although the State Lands Commission protested the rate proposed in AL 3, the State Lands Commission did not protest AL 4, and sent a letter to the Energy Division stating that the tariff proposed by Ellwood in AL 4 is acceptable to it.

The proposed rate was calculated considering costs, updated from those presented in AL 3 and using a higher rate of throughput. The method used to calculate the rate is not a formal or complete cost of service analysis as may be required in future proceedings. Neither the State Lands Commission nor ConocoPhillips protested AL 4. The Commission approves the tariffs in AL 4.

BACKGROUND

On February 17, 2012 Ellwood filed Advice Letter (AL) 3 to institute a crude petroleum transportation service on its Las Flores pipeline.[1] The Las Flores pipeline is newly constructed with an origin point at the Ellwood Onshore Processing Facility, Santa Barbara County, and a destination point 8.1 miles away, at the Tautrim tie-in to Plain's All American Pipeline, Santa Barbara County. Previously moving the oil intended for Las Flores required the use of barges. Connecting to the All American Pipeline via Las Flores will allow product to be shipped to market without the use of barges.

The only product shipped on the Las Flores line is produced pursuant to and governed by two leases between the State Lands Commission and Venoco, Inc. the parent company of Ellwood. The leases provide for Venoco's payment of royalties to the State of California on all oil produced from these leases. The amount paid is based on a percent of the "market price." The market price provides for certain offsets/deductions, including offsets/deductions for transportation. That is, higher offsets/deductions reduce the "market price" and therefore reduce the amount of the royalties received by the State Lands Commission.

ConocoPhillips is the only shipper on the pipeline.

AL 3, included a rules and regulations tariff, Cal. P.U.C. No. 1 and a transportation service rate in Cal. P.U.C. No. 2. AL 3 was timely protested by the State Lands Commission. The State Lands Commission protest asserted that the proposed transportation rate of $7.58 per barrel (bbl.) was artificially high and did not reflect throughput volumes for the pipeline. The protest noted that the rate would reduce the market price of product (through transportation cost offsets/deductions) thereby reducing the royalty amounts due. The protest also

[1] AL 3 is identical to AL 1 submitted by Ellwood on January17, 2012. AL 1 was incorrectly numbered.

asserted that Ellwood was including in its rate certain costs otherwise prohibited by the leases.

The Energy Division's review of AL 3 found that: (1) the rate proposed by Ellwood was significantly higher than other crude oil transportation rates;[2] (2) the proposed rate was based on throughput equaling only 13 percent of the line's capacity, and (3) Ellwood did not adequately break down costs as would be required in a full cost of service analysis and did not adequately respond to an Energy Division data request asking for additional information. **Based on its review, the Energy Division, on May 25, 2012, rejected AL 3 without prejudice.**

On February 27, 2013, Ellwood filed AL 4. AL 4 proposes two tariff schedules, Cal. P.U.C. No. 1 which incorporates proposed rules and regulations governing the pipeline transportation service, and Cal. P.U.C. No. 2, which presents a new rate of $4.88/bbl. for transportation of crude petroleum products on the pipeline. Ellwood asserts that AL 4 proposes significant revisions to what was presented in AL 3. It contends that the revisions address the policy issues raised by Commission staff and seek to resolve the concerns raised by the State Lands Commission. Specifically Ellwood states that "Advice Letter No. 4 provides the following:

(1) Justification for the initial sizing of the Las Flores Line and related rate base investment as well as adjustment of the forecasted throughput and anticipated utilization of pipeline capacity.

(2) A full cost of service presentation in support of the proposed rate of $4.88 per barrel.

(3) Description of the proposed rate and rate mechanism that reasonably address concerns previously raised by [State Lands Commission]."[3]

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[2] Energy Division Staff reviewed 27 transportation rates on oil pipelines and found that the proposed Ellwood rate of $7.58 was significantly above all 27 existing rates. The next highest rate was $1.71/bbl. charged on the All American line. The highest rate then charged for short distance service, i.e. under 20 miles, is $1.58/bbl. The review of other rates was intended to provide perspective on the magnitude of the proposed rate and was not a specific evaluation of the Ellwood Cost of Service analysis.

[3] Advice Letter No. 4 of Ellwood Pipeline, Inc. February 27, 2013. p. 3.

On August 22, 2013, the State Lands Commission submitted a "letter as comment on Ellwood Pipeline Inc.'s ('Ellwood') Advice Letter No. 4." The letter states that "At present . . . Ellwood's proposed tariff for the Las Flores pipeline . . . is acceptable to the [State Lands Commission] . . . "

NOTICE

Notice of Advice Letter 4 was made by publication in the Commission's Daily Calendar. Ellwood Pipeline Inc. states that a copy of the Advice Letter was sent via First Class U.S. Postal Service, or other means of agreed upon transmission to the representatives of the sole shipper on the Las Flores Line as well as to the California State Lands Commission in accordance with Section 3.14 of General Order 96-B.

PROTESTS

There were no protests to Advice Letter 4.

DISCUSSION

Ellwood's AL 4 should be authorized. The AL, including the proposed rate and rules and regulations tariffs was not protested by the line's only shipper, ConocoPhillips.[4] Further, the State Lands Commission, in its letter commenting on the AL, accepts the tariffs as presented.

Notwithstanding authorization of the proposed tariffs in this advice letter, the Commission does not fully agree with Ellwood's assertion that the analysis used in arriving at the approved rate represents a full cost of service analysis. As such, the analysis provided in AL 4 does not establish a precedent for the requirements of a cost of service analysis as may be required in future rate determinations. Ellwood has not provided all of the necessary information for a full cost of service analysis. While the analysis provides estimates for several parts of its inputs, it again fails to provide costs for several operating expense categories. In response to the data request for AL 4, Ellwood relied on statements that, given its short operating experience, these costs were not known. Ellwood should be able to provide at least reasonable estimates of its operating

[4] In Ellwood's August 9, 2013 response to an Energy Division data request, Ellwood stated that ConocoPhillips has been the only shipper since service was initiated and that it does not know at this time of any other potential shippers on the line.

costs, and its apparent inability (or unwillingness) to do so means that its analysis does not rise to the requirements of a full cost of service analysis.

Ellwood's explanation of the sizing of the pipeline does not address the concern that the current shipper, providing only a small part of the capacity of the line, is being burdened with the full costs of the line. Ellwood provides its rationale for the capacity/sizing of the pipeline contending that the low incremental costs justified building a line with greater capacity than currently needed. That argument may make economic sense for Ellwood, but it does not address this concern.

The 'volume adjustment' (to allow adjustments in the rate for actual pipeline throughput) in the proposed rules and regulations tariff also does not resolve issue of throughput relative to capacity. Under the proposed 'volume adjustment' a decrease in throughput results in an even higher rate, thus aggravating the problem identified in AL 3. On the other hand, if Venoco production increases, or if any new shippers add volumes to the pipeline, the rate would fall.

Ellwood does, however, correctly assert that the proposed rate and rate mechanism satisfies the concerns of State Lands Commission. This is evidenced by the State Lands Commission's letter to the CPUC finding the proposed rate tariff acceptable.

ConocoPhillips did not protest AL 4. ConocoPhillips is a very large corporation, and can fully represent its interests before the Commission.

In summary, Ellwood has arrived at a rate for transportation service acceptable to the parties with a direct interest. The fact that this was arrived with less than a full cost of service analysis does not make the rate less acceptable. And the approval of the rate by the Commission does not mean that, should a future proposed rate change be challenged, the incomplete analysis used in AL 4 would be sufficient for approval. Further, the Commission notes that the use of the adjustment factor does not relieve Ellwood from the requirements of Cal. Public Utilities Code section 455.3 concerning rate increases and the requirement that Ellwood file new tariffs reflecting any rate changes with the Energy Division.

COMMENTS

This is an uncontested matter in which the resolution grants the relief requested. Accordingly, pursuant to PU Code 311(g)(2), the otherwise applicable 30-day period for public review and comment is being waived.

FINDINGS AND CONCLUSIONS

1. On February 7, 2012 Ellwood Pipeline Inc. (Ellwood) filed Advice Letter (AL) 3 requesting approval of a rules and regulations tariff and a rate tariff to initiate a new crude oil products transportation service on its newly built Las Flores pipeline.
2. Product on the Los Flores pipeline is produced from and governed by two leases between the California State Lands Commission (State Lands Commission) and Venoco, Inc. Venoco, Inc. is the parent company of Ellwood. The leases provide for Venoco to pay the State Lands Commission royalties on oil produced from the leases. The royalties are based on the market price of the product net of certain offsets/deductions for transportation.
3. The State Lands Commission protested Ellwood AL 3 asserting that (a) the proposed rate of $7.58 was artificially high; (b) the rate sought to reduce the market price used to determine royalties; and (c) the rate sought to pass on costs otherwise prohibited by the leases.
4. On May 25, 2012, the Energy Division rejected AL 3 without prejudice. The Energy Division's review of the AL identified that (1) the rates for the Line were based on recovering the full capital costs of the Line but a throughput of less than 13 percent of the Line's full capacity; and (2) the AL did not breakdown the cost of service into all of the required accounts nor did Ellwood provide further detail when requested. Based on this and the protest of the State Lands Commission, the Commission determined that evidentiary hearings would be required.
5. On February 7, 2013, Ellwood filed AL 4. AL 4 proposes a new rate of $4.88/bbl. and revises its rules and regulations tariff to incorporate a provision adjusting the rate each year based upon the prior year's throughput. The AL asserts that the new rate and revisions address both the issues raised by the Commission and the concerns of the State Lands Commission relative to AL 3.
6. Ellwood, in arriving at the proposed rate in AL 4, did not provide adequate information as required for a full cost of service analysis. Approval of the proposed rate does not set a precedent for the use of the analysis presented in AL 4 in any future proceedings requiring a cost of service analysis.

7. AL 4 was not protested either by the line's only shipper, ConocoPhillips, or by the State Lands Commission. The State Lands Commission provided the Commission with a letter as comment on the AL stating that the tariffs are acceptable to it.
8. The proposed tariffs should be authorized.
9. Approval of the proposed rate does not set a precedent for the use of the analysis presented in AL 4 in any future proceedings requiring a cost of service analysis.
10. The adjustment factor based on annual volumes and used to calculate new rates does not relieve Ellwood of the requirements of California Public Utilities Code Section 455.3.
11. The proposed tariffs should be authorized.

THEREFORE IT IS ORDERED THAT:

1. The tariffs proposed in Ellwood Pipeline Inc.'s Advice Letter 4 are approved.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on, May 1, 2014; the following Commissioners voting favorably thereon:

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Paul Clanon
Executive Director