

DRAFT

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA
ENERGY DIVISION

ITEM # 6 I.D. # 8947
RESOLUTION O-0050
DATE: December 17, 2009

R E S O L U T I O N

Resolution O-0050; Chevron Pipeline Company (CPL) requests authority to remove the New Kettleman Station Truck Unloading Facility from CPL's public utility accounts and further authority to transfer ownership to an unregulated affiliate.

PROPOSED OUTCOME: CPL's request is approved. CPL shall record the annual cost of service of the Kettleman Unloading Facility that is embedded in rates in a memorandum account, and shall apply the amount accumulated in that account as an offset against the revenue requirement adopted in CPL's next General Rate Case.

ESTIMATED COST: None.

By Advice Letter 40 filed on June 12, 2009

SUMMARY

This resolution approves Chevron Pipeline Company's (CPL) request for authority to transfer ownership of its New Kettleman Truck Unloading Facility to its unregulated affiliate, Chevron USA, Inc. (CUSA). The facility is not used or needed by CPL to carry out its public utility obligations as a common carrier, and thus the costs of the facility have erroneously been included in the CPL rate base. CUSA seeks ownership of the facility.

Because the facility was included in Chevron's rate base in error, was never needed or used for shipments on CPL's pipeline, and was included in CPL's rate base when it submitted its last General Rate Case (GRC), CPL shall record the annual cost of service of the Kettleman Unloading Facility that is embedded in rates in a memorandum account, and shall apply the amount accumulated in that account as an offset against the revenue requirement adopted in CPL's next General Rate Case. The effect of this would be to reduce the revenue requirement

adopted in CPL's next general rate case by the amount accumulated in the memo account.

This advice letter satisfies the conditions specified in Resolution ALJ-202, a pilot program instituted by this Commission to expedite review of transactions that fall under the control of Public Utility Code §851.¹

BACKGROUND

CPL owns and operates the KLM Pipeline System (KLM Pipeline), and provides common carrier transportation services to a variety of shippers on the KLM Pipeline. These common carrier services are tariffed and subject to Commission jurisdiction. Kettleman Station provides the KLM Pipeline with intermediate pump boosting for crude oil movements from southern receipt points on the pipeline system to destinations in the San Francisco Bay Area.

CUSA is not regulated by this Commission and "is a major subsidiary of Chevron Corporation. CUSA and its subsidiaries manage and operate most of Chevron's U.S. businesses. Assets include those related to the exploration and production of crude oil, natural gas and natural gas liquids and those associated with the refining, marketing, supply and distribution of products derived from petroleum, excluding most of the regulated pipeline operations of Chevron. CUSA also holds the company's investment in the Chevron Phillips Chemical Company LLC joint venture..."²

The New Truck Unloading Facility is located at Kettleman Station and was constructed in 2005 at the request of CUSA. This truck unloading facility, along with an older truck unloading facility, allows crude oil to be removed from trucks, transferred to a storage tank and then ultimately commingled with other crude oil received into the Kettleman Station.

CPL states the New Kettleman Truck Unloading Facility is neither necessary nor useful for CPL to carry out its public utility obligations. CPL said that the

¹ All Code citations are to the Public Utilities Code, unless otherwise stated.

² *Chevron Annual Report 2008*, Note 4 to the Consolidated Financial Statements.

sole purpose for the construction and operation of the New Kettleman Truck Unloading Facility was, and is, to provide service to CUSA and that CUSA is the only entity making use of the New Kettleman Truck Unloading Facility. Further, CPL believes that the inclusion of the costs for the New Kettleman Truck Unloading Facility, for purposes of public utility rate base calculations, was erroneous. CPL said it is not in the business of offering or providing common carrier service on the truck loading facilities and the KLM Pipeline tariff does not offer a truck unloading service.

CPL states that CUSA requested that CPL upgrade the New Kettleman Truck Unloading Facility to enable receipt of larger volumes of crude oil at the Kettleman Station. CPL's attempt to find interests of other entities in increased truck capability brought no indication of interest of any entity other than CUSA. CUSA represented to CPL that it was willing and able to unilaterally commit the necessary funding for expansion of the New Kettleman Truck Unloading Facility.

CPL and CUSA concluded that ownership of the New Kettleman Truck Unloading Facility should reside with CUSA, which will upgrade and expand the facility. CPL states that it disclosed to shippers whose crude oil enters the KLM Pipeline at Kettleman Station of its intent to request approval of transfer of the ownership of the New Kettleman Truck Unloading Facility to CUSA. No shipper expressed any opposition to the proposed transfer.

REQUIREMENTS OF RESOLUTION ALJ-202

Utilities proposing to sell, lease, dispose of, or otherwise encumber property are governed by and must comply with §851. Ordinarily, such a proposal would entail a full Application to the Commission, including a review pursuant to the California Environmental Quality Act (CEQA) or a demonstration that such a review is not necessary. The Commission on August 25, 2005, issued Resolution ALJ-186 which initiated a 24-month pilot program providing an expedited process for certain transactions meeting criteria specified in the Resolution. Under this program utilities may file for authority to proceed with such transactions through the advice letter process rather than by formal Application, provided the transaction meets the criteria specified in the Resolution. On August 23, 2007, the Commission extended this pilot program for an additional three years (Res. ALJ-202).

Res. ALJ-202 requires that the transaction meet certain restrictions to qualify for this expedited review under the Commission's advice letter process. In its advice letter, the utility must provide information, statements, and documentation regarding the transaction to show compliance with both §851 and Res. ALJ-202. We list the pertinent requirements listed in Res. ALJ-202 here. The filing utility must provide:³

1. A complete description of the financial terms of the proposed transaction;
2. A description of how the financial proceeds of the transaction will be distributed;
3. A statement of the impact of the transaction on ratebase and any effect on the ability of the utility to serve customers and the public reliably and at reasonable rates;
4. For sales of real property and depreciable assets, the original cost, present book value, the present fair market value, and a detailed description of how the fair market value was determined (e.g., appraisal);
5. If the transaction results in a transfer of real property, evidence that the property does not have a fair market value in excess of \$5 million, and;
6. A statement addressing whether the proposed transaction will require environmental review by this Commission under CEQA. If this transaction is exempt from such review, filer must provide a complete explanation, including documentation, supporting the claimed exemption.

CPL asserts compliance with §851 and General Order (GO) 96-B.

CPL notes that §851 enables a utility to transfer interests in utility property by the advice letter process for certain transactions valued at \$5 million or less. CPL added the cost of the New Kettleman Truck Unloading Facility to its accounting

³ Res. ALJ-202, Appendix A, pp. 2-4.

records on September 1, 2005, in the amount of \$87,925.69. CPL reported the remaining book value of this facility to be \$74,210.65 as of May 31, 2009.

Energy Industry Rule 5.3(b) of GO 96-B enables public utilities to submit a Tier 3 advice letter for purposes of withdrawing a service or abandoning service within an area. (Advice letters are filed as Tier 3 when the utility expects or requests a Commission Resolution to address its advice letter.) AL 40 requests formal abandonment of public utility service from the New Kettleman Truck Unloading Facility.

CPL further notes that Res. ALJ-202 directed that, even if valued at less than \$5 million, transactions are not eligible to use the advice letter process if the removal of the rate will materially impact the rate base of the utility. In its Application 08-08-002, CPL represented the rate base of the KLM Pipeline and two other regulated pipelines to be over \$45 million. Since the book value of the New Kettleman Truck Loading Facility is less than \$75,000, less than 0.2% of the \$45 million rate base, CPL asserts that the transfer of the facility will not materially affect its rate base.

CPL states that no review by this Commission under CEQA is required for this proposed transaction. CUSA intends to expand this facility to deliver increased volumes of crude to the KLM Pipeline. However, CPL states that the expansion is subject to the oversight and environmental regulation of the San Joaquin Valley Air Pollution control District (SJVAPCD). CPL obtained two Authorities to Construct (ATC) from SJVAPCD, providing authorization to CPL to construct additional truck unloading facilities. Upon Commission approval of the transfer of ownership, CPL states the operating permits will be transferred to CUSA, or reissued with submittal of a brief application form. CPL concludes that no additional environmental assessment is required of the Commission under CEQA for this proposed transaction. Both ATCs are attached to the advice letter.

CPL states that there is no gain on sale associated with the transfer.

The Commission requires applicants seeking to sell utility property under §851 to report any gain on the disposition.⁴ CPL reports that there will be no gain on the transfer described herein since CUSA has agreed to purchase the facility “at

⁴ See D.06-05-041, as modified by D.06-12-043.

“the actual remaining book value of the facilities, as of the date of the actual transfer.” This final sale amount will be less than the original price.

CPL asserts that the proposed transfer is in the public interest.

CPL states the transfer is in the public interest because it is disposing of an asset that is not used or useful in carrying out its public utility responsibilities. CPL adds that CUSA’s expansion of the New Kettleman Truck Unloading Facility would facilitate and improve the reliability of movements of additional supplies of crude into pipelines for shipment to California refineries, thereby providing economic benefits of higher shipment volumes.

CPL responded on September 21, 2009, to a data request by the Energy Division transmitted in telephone conversations during the week of

September 14, 2009. This response provided further information on two issues. First, asked by staff to elaborate on the nature of the property CPL proposed to transfer to CUSA, CPL states that this proposed transaction does not involve real property, only the equipment and machinery comprising the New Kettleman Truck Rack Unloading Facility. CPL “is retaining ownership of the real property on which the truck rack unloading facility is located.

Second, asked to more thoroughly explain why it believes the book value of the facility is no less than its fair market value, and thus this transaction does not subsidize its unregulated affiliate at the cost of the ratepayers, CPL states that the “facility is dependent on it being physically able to deliver crude oil from production fields into an oil pipeline; other than for scrap, the equipment has no value in a freestanding mode.” The company continues,

Prior to filing the Advice Letter, CPL disclosed to all shippers whose crude oil enters the KLM Pipeline at Kettleman Station of its intent to request Commission approval to transfer ownership of the New Kettleman Truck Unloading Facility to its affiliate. CPL also sought expressions of interest from these shippers in having the truck unloading capability of the New Kettleman Truck Unloading Facility increased. In response to these inquiries, no shipper, other than CPL’s affiliate, expressed any interest in increasing the capability of the New Kettleman Truck Unloading Facility,

and no shipper has expressed any opposition to the proposed transfer of the New Kettleman Truck Unloading Facility to CPL's affiliate.⁵

NOTICE

Notice of AL 40 was made by publication in the Commission's Daily Calendar. CPL states that a copy of the advice letter was mailed and distributed in accordance with Section 4 of General Order 96-B.

PROTESTS

No party filed a protest to this advice letter.

DISCUSSION

The transfer of ownership of the New Kettleman Truck Unloading Facility from CPL to CUSA is approved. The transfer satisfies the requirements of §851. Under the criteria specified in Res. ALJ-202, this authority may be sought from this Commission through its advice letter process.

The facility is not used or needed by CPL to perform its common carrier transportation obligations on the KLM Pipeline, and inclusion of the New Kettleman Truck Unloading Facility in CPL's rate base was apparently an error. CPL said that sole purpose for construction of the New Kettleman Truck Unloading Facility is to provide service to CUSA, and CUSA is the only entity making use of that facility.

CPL demonstrated that filing Advice Letter 40 to request the transfer of ownership under §851, G.O. 96-B Energy Rule 5.3(6), and Res. ALJ-202 was appropriate and in the public interest. The sale of the New Kettleman Truck Unloading Facility will not result in any physical impacts to the environment. Thus, the transfer itself will not require environmental review by the CPUC as a lead or responsible agency under CEQA.

⁵ E-mail data request response to staff on September 21, 2009, from Steven F. Greenwald of Davis Wright Tremaine LLP, counsel for CLP.

The transfer will not have an adverse effect on the public interest or on the ability of CPL to provide safe and reliable service to customers at reasonable rates. The facility costs far less than \$5 million, and CPL never apparently offered the truck unloading service in the first place. We also find that there is no material impact on CPL's rate base. The rate base associated with the facility (\$75,000) is less than .002 of CPL's total rate base (\$45 million). While the dollar and percentage amounts are quite small, these amounts still could be significant enough to require an application if they have a clear impact on rates. In CPL's most recent rate proceeding, the Commission adopted in D.08-12-046 a settlement of rates that were significantly below CPL's initially proposed rates. The reduction in annual revenues from CPL's initially proposed rates was \$1.7 million (from \$8.1 million to \$6.4 million), or about a 21% reduction. It is doubtful that the exclusion of the New Kettleman Truck Unloading Facility from rate base now would have a further material impact on reasonable rates for CPL, especially one that would be significant enough to require a new application. We also place some weight on the fact that there were no protests from shippers to CPL's proposal in AL 40.

This transaction involves the transfer of no real property, as explained by CPL in its response to the staff's data request. Res. ALJ-202 requires:

For sales of real property and depreciable assets, the original cost, present book value, and present fair market value, and a detailed description of how the fair market value was determined (e.g., appraisal).

CPL explains that this transfer involves no real property. Its depreciable assets have no value separate from its current location outside of its scrap value, and no shipper outside of its own affiliate has expressed interest in obtaining these assets. Under these circumstances, it is unlikely that the fair market value of the facility is greater than its current book value.

There is no gain on sale on the proposed transfer since the New Kettleman Truck Unloading Facility will be transferred at book value.

D.06-05-041 provides guidelines on the allocation of gains realized through the sale of utility property. This proposed transaction results in no gain, however, as the assets are being transferred at book value.

CPL concedes that the facility was placed into rate base erroneously, and was never needed or useful for making pipeline shipments. However, the costs associated with this facility were included in CPL's 2008 GRC rate base, and is embedded in the rates adopted in the Commission's 2008 GRC decision for CPL, D.08-12-046.

CPL acknowledges that the sole purpose for the facility was and is to provide service to CUSA, and that the facility is neither necessary nor useful for CPL to carry out its public utility obligations on the KLM Pipeline. CPL executed a lease agreement with CUSA for the use of the facility, and CUSA is the only entity making use of the facility.

CPL asserts that the inclusion of these assets in its rate base has had no discernible impact on rates. This may be true, as we discussed above, but there is no denying the fact that the facility's costs were embedded in rates since December 1, 2008 (when the rates adopted in D.08-12-046 became effective) even though the impact on rates may be imperceptible.. CPL included these costs in its rate base in its request for a rate increase in its 2008 GRC, A.08-08-002.

Although the rates adopted in D.08-12-046 were based on a settlement of the rates and CPL was not granted its full requested revenue requirement, we can not ignore the fact that rates were essentially based on a rate base amount that included the cost of service associated with this facility, including at least depreciation and maintenance expense as well as rate of return. (D.08-12-046 concluded that a 5.79% rate of return was reasonable for CPL.) The current CPL rates, that are essentially based on these costs, will be in effect until CPL's next GRC.

CPL shall record the annual cost of service of the Kettleman Unloading Facility that is embedded in rates in a memorandum account, and shall apply the amount accumulated in that account as an offset against the revenue requirement adopted in CPL's next General Rate Case.

At that time, CPL shall apply the amount accumulated in the memo account as an offset to the total cost of service revenue requirement adopted in CPL's next GRC which will have the effect of reducing CPL's then adopted revenue requirement by the accumulated amount in the memo account. CPL is required to specifically note this amount in its next GRC application.

COMMENTS

On November 9, 2009, CPL submitted comments on the Draft Resolution (DR). CPL objected to the DR's Ordering Paragraph (OP) #2 which states: CPL shall refund to shippers the difference between the original cost and the current book cost of the facility at the time of the transfer.

The primary points presented by CPL in its opposition to OP #2 are these:

- Even though the purchase price of the Kettleman facility was placed in rate base in 2005, rates were not changed until December, 2008 by D.08-12-046. The full depreciation costs for the facility have therefore not yet been recovered in rates paid by their shippers. According to CPL, assuming a return on equity (ROE) of 7.52%, application of the ROE to the additional rate base of \$87,925.69 for these six months \$2790. CPL argues that this should be the limit of the refund to shippers.
- The cost of the facility (\$87,925.69 according to AL 40) is an insignificant addition to their rate base of over \$45 million (as of its A.08-08-002).
- OP #2 unlawfully modifies "a rate case settlement approved by the Commission" in D.08-12-046. Changes in rate base between general rate cases do not trigger or mandate a change in rates charged by the utility.
- The Commission's Pilot Program (Resolution ALJ-202) "provides that if the applicant demonstrates that the removal of the asset 'will not have a material impact on rate base,' no prospective rate reduction need be considered. Any rate adjustment...is thus deferred until the next general rate case." (Comments, p. 3)

Thus, while CPL argues that a refund using the methodology in the Draft Resolution is incorrect, and that rates weren't impacted by the inclusion of the facility costs in its GRC, it also argues that, even assuming that its current rates reflect the full facility costs, any refund to shippers should be based on shipper overpayments only for the the time period after the 2008 GRC rates became effective, i.e. after December 1, 2008.

Upon consideration of CPL's comments, we have made some changes to the Draft Resolution. As discussed above, we do not require CPL to refund to shippers the difference between the original cost and the current book cost of the

facility at the time of the transfer. Rather, we require CPL to return to shippers the cost of service associated with the facility, including depreciation, maintenance, and other costs associated with this facility, that is embedded in rates for the period after December 1, 2008. This will be specified as an offset to the total cost of service revenue requirement adopted in CPL's next GRC. CPL will document and submit to this Commission a showing of how the rates resulting from this next GRC reflect this required offset.

FINDINGS

1. Chevron Pipeline Company (CPL) submitted AL 40 seeking authority to transfer ownership of New Kettleman Truck Unloading Facility to its unregulated affiliate Chevron USA (CUSA).
2. No party has filed a protest to this advice letter.
3. CPL submitted AL 40 appropriately under PU Code 851, General Order 96-B, and Resolution ALJ-202.
4. CPL added the cost of the New Kettleman Truck Unloading Facility to its accounting records on September 1, 2005, in the amount of \$87,925.69. CPL reported the remaining book value of this facility to be \$74,210.65 as of May 31, 2009.
5. The New Kettleman Truck Unloading Facility is neither necessary nor useful for CPL to meet its public utility obligations.
6. No CEQA review is necessary because the transfer of this existing facility will have no physical impacts on the environment.
7. The transaction will not have an adverse effect on the public interest or on the ability of CPL to provide safe and reliable service to customers at reasonable rates.
8. No real property will be transferred from CPL to CUSA, only the equipment and machinery necessary to perform the function of the New Kettleman Truck Unloading Facility.

9. There is no gain on sale associated with this transaction, as the facility will be sold to CUSA at its book value at the time of the transfer.
10. The sole purpose of the New Kettleman Truck Unloading Facility is to provide service to CUSA.
11. The sale will be at an amount far less than \$5 million, and will not have a material impact on rate base.
12. CPL sought expressions of interest from all shippers whose crude oil enters the KLM Pipeline at Kettleman Station in having the truck unloading capability of the New Kettleman Truck Unloading Facility increased. Only its affiliate CUSA expressed any interest in this.
13. No shipper is opposing the proposed transfer of ownership of this facility.
14. CPL erroneously placed the facility costs in rate base, and those costs are embedded in CPL's current rates.
15. CPL should record the annual cost of service of the Kettleman Unloading Facility that is embedded in rates in a memorandum account, and should apply the amount accumulated in that account as an offset against the revenue requirement adopted in CPL's next General Rate Case.
15. CPL should document and submit to this Commission a showing of how the rates resulting from this next GRC reflect this required offset.

THEREFORE IT IS ORDERED THAT:

1. Chevron Pipeline Company's (CPL's) Advice Letter 40 is approved. CPL may sell its New Kettleman Truck Unloading Facility to its unregulated affiliate Chevron USA and remove it from its public utility accounts.
2. CPL shall record the annual cost of service of the Kettleman Unloading Facility that is embedded in rates in a memorandum account, and shall apply the amount accumulated in that account as an offset against the revenue requirement adopted in CPL's next General Rate Case.

3. For the purpose of this memorandum account, the cost of service shall include at least annual depreciation expense plus a 5.79% return on the declining property balance for the New Kettleman Truck Rack Facility included in CPL's 2008 rate case filing and included in the rates approved by the Commission in D.08-12-046 from December 2008 onward.
4. This memorandum account shall be updated on November 30th of each year prior to Chevron Pipeline Company's next General Rate Case, and shall include interest on the balance of the account. The interest rate shall be the 3-month Commercial Paper rate on November 30th of each year.
5. CPL shall specifically discuss the accumulated amount in its next GRC application and explain that the accumulated amount will be a reduction to the revenue requirement adopted by the Commission in that GRC.
6. CPL shall file an advice letter within 30 days of the effective date of this resolution showing in its tariff the creation of this memo account.
7. CPL will document and submit to this Commission a showing of how the rates resulting from this next GRC reflect this required offset.
8. No review by this Commission under CEQA is required for this transaction, as explained herein.
9. 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 December 17, 2009, the following Commissioners voting favorably thereon:

Paul Clanon
Executive Director

