

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

COMMISSION ADVISORY
AND COMPLIANCE DIVISION
Energy Branch

RESOLUTION O-0002
February 8, 1995

R E S O L U T I O N

RESOLUTION O-0002. CHEVRON PIPELINE COMPANY REQUESTS APPROVAL OF TARIFFS WHICH GOVERN THE TRANSPORTATION AND DELIVERY OF CRUDE PETROLEUM AS DESCRIBED IN CAL. P.U.C. NO.18 CANCELLING CAL. P.U.C. NO. 1.

BY ADVICE LETTER NO. 8 filed June 8, 1994.

SUMMARY

1. Chevron Pipeline Company (Chevron) filed Advice Letter No. 8 on June 8, 1994, which requests authority to cancel Cal. P.U.C. No. 1 and to replace it with Cal. P.U.C. No.18 which contains tariffs governing the rates, rules and regulations for transporting and delivering crude petroleum on the Chevron's KLM pipeline system.
2. Cal P.U.C. No.18 limits shipment in the KLM pipeline system common stream to virgin crude oil and direct liquid products of oil and gas wells, and specifies that tenders to the system must be indigenous San Joaquin Valley crudes of certain defined characteristics. The tariff also includes various word changes which are comparable to those contained in Chevron's Federal Energy Regulatory Commission Rules and Regulations Tariff No. 338.
3. Protests to Advice Letter No. 8 were filed by Tosco Refining Company (Tosco) and Koch Industries, Inc. (Koch). Shell Oil Company (Shell) filed a letter in support of the proposed revisions. Protestants allege the geographic limitation is discriminatory.
4. On September 22, 1994, Chevron filed Advice Letter Supplement No. 8-A, which provided expanded explanation for the geographic limitations contained in Cal. P.U.C. No. 18. Chevron responds that without the geographic limitation the oil of other shippers would be degraded.
5. Koch filed a protest in response to Advice Letter Supplement No. 8-A on October 19, 1994, in which it asserted that objective testing was a reasonable method to protect the quality of crude oil shipments. Chevron responded to Koch on November 3, 1994. According to Chevron, the two refineries on the KLM pipeline system (Shell and Tosco) had not been able to

agree on a set of quality standards for crude oil shipments, and thus Chevron was placed in a position wherein it had to establish acceptable quality standards, ie. the geographic limitation.

6. Shell filed a letter on November 10, 1994, in support of Advice Letter Supplement No. 8-A and in response to Koch's protest of October 19, 1994 and the Chevron response of November 3, 1994. Shell believes that Chevron's proposed geographic limitation would not exclude shippers, rather it would only exclude types of crude oil and would thus be an objective standard.

7. Koch filed a letter on November 15, 1994, responding to the Chevron response of November 3, 1994. Koch believes that Chevron is attempting to protect its largest customer, Shell, and that objective standards can be used to protect quality.

8. Shell filed a letter on December 12, 1994, responding to Koch's letter of November 15, 1994. Shell reiterates that it is trying to protect the integrity of the crude oil it receives on the pipeline and that while the quality of San Joaquin crudes does indeed vary, such variations have been acceptable to Shell's refining capabilities.

9. This resolution grants Chevron's request and denies the protests.

BACKGROUND

1. Chevron files its tariffs for the transport and delivery of crude petroleum pursuant to the Pipeline Dedication Agreement dated August 26, 1991, which was the settlement agreement stemming from a lawsuit between the City of Long Beach and Chevron. The lawsuit also involved other oil pipeline companies which now file tariffs with the Commission, as well.

2. Issues pertaining to the quality of liquid products transported on Chevron's system were raised by shippers (Shell and Tosco) after Chevron filed Cal. P.U.C. No.1. The shippers expressed concern over the sulfur content of the delivered product, as well as changes in the specific gravity. Chevron has conferred with the shippers and now proposes various revisions in Cal. P.U.C. No. 18 to resolve the shipper's concerns.

3. The KLM pipeline, which has been dedicated to public use as a common carrier is known as a "common stream" pipeline. This means that all liquid petroleum products introduced into and carried by the pipeline are transported in a common stream and that mixing of different products from different origin points will occur. When high quality crude oil and low quality crude oil are carried in the same common stream, the quality of the higher grade oil at the destination point may be degraded, while the quality of the lesser grade may be improved. Similarly, crudes which simply bear different characteristics can mix in a

common stream pipeline, again resulting in a delivery of crude oil bearing characteristics which may not resemble those of the crude at the origin points.

4. A solution to the problem of mixing on common stream pipelines is to transport the crude oil in batches, such that crudes of differing characteristics are physically separated and the pipeline transports individual batches one at a time. This involves the use of large holding tanks which are located at points of origin and destination and which are adequately sized to hold the volumes selected for transportation in a given batch.

5. The KLM pipeline has limited facilities for providing batching services, but does not have the facilities to provide batching services for all points of origin and destination. Thus most of the transport occurs in a common stream.

6. Another solution to the problem of maintaining quality of crude oil transported in the common stream is to limit shipments to those which satisfy an objective set of measureable standards or characteristics, such as gravity and sulfur content.

NOTICE

Public notice of Advice Letter No. 8 was made by mailing copies to all tariff subscribers and adjacent utilities in accordance with section III of General Order 96-A and by publication in the Commission Calendar.

PROTESTS

1. The Commission Advisory and Compliance Division (CACD) has received two protests to Chevron's Advice Letter No.8.

2. Koch submitted a protest dated June 20, 1994, and Tosco submitted a protest dated June 27, 1994.

3. On July 12, 1994, Chevron submitted its response to both protests.

4. Koch filed a protest in response to Advice Letter Supplement No. 8-A on October 19, 1994. Chevron responded to Koch on November 3, 1994.

5. Shell filed a letter on November 10, 1994, in support of Advice Letter Supplement No. 8-A and in response to Koch's letter of October 19, 1994 and the Chevron letter of November 3, 1994.

6. Koch filed a letter on November 15, 1994, responding to the Chevron response of November 3, 1994.

7. Shell filed a letter on December 12, 1994, responding to Koch's letter of November 15, 1994.

DISCUSSION

1. Chevron proposes revisions to its tariffs to resolve the general issue of maintaining the quality of petroleum products transported on its pipelines. In order to assure shippers that high quality, low-sulfur petroleum products will not be degraded by the introduction of lesser quality products, Chevron proposes to limit shipments by place of origin. It would limit the shipments to virgin crude oil and direct liquid products of oil and gas wells, with the additional requirement that the liquid products be indigenous to the San Joaquin Valley crudes, whose distillation range, quality, and general characteristics are typical of San Joaquin Valley crudes.

2. Chevron also proposes to implement a gravity bank which is designed to monetarily compensate shippers for changes in the specific gravity of petroleum products being shipped which may result during shipping because of the effects of mixing liquids of differing gravities.

3. Koch objects to the geographic limitations, and suggests that such limitations are discriminatory and will not adequately solve the problems they are designed for. Koch does not comment on the proposed gravity bank.

4. Tosco objects to the geographic limitations, as well. It suggests that the limitations are discriminatory, but offers alternative specifications for assuring the quality of petroleum products introduced into Chevron's pipelines. Further, Tosco indicates that the specifications it offers are currently used by Four Corners Pipeline Company (FCPL). Tosco does not propose any changes to the tariff regarding the gravities of petroleum products introduced to the pipeline system.

5. Shell, which is Chevron's largest customer on the KLM system, supports the proposed tariff changes in Cal. P.U.C. No. 18. Shell does not believe the geographic limitation is discriminatory, but rather that it establishes an objective standard for quality of crudes tendered for shipment on the KLM pipeline.

6. Chevron's response to the protests of Koch and Tosco addresses the issue of discriminatory service and the justification for its proposed tariff changes. Chevron believes that the geographic limitation is its best solution for protecting the quality of shipments in its pipelines, which serves the economic interests of its shippers. It indicates that it endeavored to negotiate an adequate solution for all San Joaquin area producers, but could not achieve a common solution satisfactory to all. Instead, Chevron proposes its geographic limitation, and it also indicates that it has offered to ship petroleum products of various mixed blends on a segregated basis so as to isolate them from indigenous common stream shipments.

7. Chevron also responds to Tosco's offer of using a set of specifications for shipments in Chevron's pipelines which are

apparently being used by FCPL. Chevron notes that the types of oil carried by FCPL vary significantly from those carried by Chevron.

8. Chevron indicates in Advice Letter Supplement No. 8-A that an alternative to batching is to conduct quality testing at all points of origin. It also notes that such testing is not only expensive, but that some procedures are not sufficiently established to be standardized and recognized by the American Society for Testing and Materials (ASTM). The ASTM has standardized testing for some characteristics of crude oils, but the demands of today's oil refineries have become highly sensitive and require new and costly tests. Hence, it is Chevron's opinion that the concept of objective standards and testing as a means to assure preservation of quality during common stream transport is technically infeasible.

9. Chevron acknowledges that batched transportation service for non-San Joaquin Valley crude oil could be employed to assure quality in the common stream on the KIM pipeline. It notes, however, that demand for batching does not justify the expense to Chevron to study the feasibility and assume the financial risk of investing in the necessary facilities. It also indicates that its major direct competitor currently has the capability to provide batching services.

10. CACD sees the central problem as follows. When common stream transportation involves, for example, two grades of crude oil, the shipper of the higher grade oil is harmed by the degradation in quality which results when the lesser grade is mixed with the higher grade in the common stream. On the other hand, the shipper of the lesser grade oil sees an improvement in the quality of its shipment. The shipper of the lesser grade oil is enriched at the expense of the shipper of the higher grade oil.

11. The potential solutions to protect the quality of oil during transport include batch shipping or objective quality standards and testing at origin and destination points throughout the pipeline system. Based on the information provided by Chevron in its advice letter and supplemental advice letter, CACD believes that the testing option is neither economically nor practically feasible.

12. The option to provide batching services appears to be a potentially viable solution to the extent that it is practicable; however, CACD believes it would be unreasonable to require Chevron to invest in the necessary storage facilities to provide batching services. Chevron indicates that a competing pipeline exists which is capable of providing batching services from the San Joaquin Valley area to the Bay area. This would suggest that there are options available for shippers who need batching services.

13. The filings made by Koch on October 19 and November 15, 1994 reiterate Koch's belief that objective standards are a

feasible means to assure the quality of petroleum products transported on the KLM line. CACD has reviewed all the filings made by Koch, Tosco, Shell and Chevron, and the parties agree that the central issue is that of the quality of the petroleum products shipped on the KLM line. CACD believes that the demands of the refineries which receive the shipments should guide the solution to this issue. It is reasonable for a refinery to expect that the petroleum products it ships on the KLM line will arrive at their destination without significant degradation in quality. The materials provided by Chevron and Shell indicate that objective testing of the characteristics of the petroleum products is not sufficiently feasible to protect quality. Chevron indicates that its efforts to develop common standards for objective testing have been fruitless to date, and further indicates that certain characteristics are either too expensive to test or cannot be tested reliably. Tosco and Koch assert that such testing is feasible and acceptable and cite the use of such testing on competing pipelines. CACD notes that other pipelines are not necessarily comparable since they carry different products and may have differing capabilities, i.e. batching facilities. For these reasons, CACD recommends that the geographic limitation for shipments on the KLM line be approved at this time. This is not an optimal solution, but rather one that protects the interests of the refineries which process the common stream petroleum products.

14. Although the solution proposed by Chevron of imposing a geographic limitation on the source of petroleum products to be shipped on the KLM system may serve to preserve the quality of crude oils transported on the KLM line today, it is expedient and limited at best. For the future, CACD encourages Chevron and its shippers to pursue options such as shared financing of necessary batching facilities and/or objective testing protocols. At this time, however, CACD does not believe that Chevron should bear the full cost of batching facilities, nor does it view testing as a currently viable option, in part due to the fact that Tosco and Shell have not been able to agree on a common set of quality standards.

FINDINGS:

1. Chevron Pipeline Company (Chevron) filed Advice Letter No. 8 on June 8, 1994, which requests authority to cancel Cal. P.U.C. No. 1 and to replace it with Cal. P.U.C. No. 18 which contains tariffs governing the rates, rules and regulations for transporting and delivering crude petroleum on the Chevron pipeline system.
2. The rules and regulations in Cal. P.U.C. No. 18 revise those contained in Cal P.U.C. No. 1 which relate to the transport of petroleum on Chevron's KLM pipeline system. Specifically, Cal. P.U.C. No.18 limits shipment in the KLM pipeline system common stream to virgin crude oil and direct liquid products of oil and gas wells, and specifies that tenders to the system must be indigenous San Joaquin Valley crudes of certain defined characteristics. The tariff also includes

various word changes which are comparable to those contained in Chevron's Federal Energy Regulatory Commission Rules and Regulations Tariff No. 338.

3. Protests to Advice Letter No. 8 were filed by Tosco Refining Company (Tosco) and Koch Industries, Inc. (Koch). The protests allege that the geographic limitation is discriminatory.

4. Chevron's responses to the protests indicate that without the geographic limitation the oil of other shippers would be degraded.

5. On September 22, 1994, Chevron filed Advice Letter Supplement No. 8-A, which provided expanded explanation for the geographic limitations contained in Cal. P.U.C. No. 18.

6. Koch filed a protest in response to Advice Letter Supplement No. 8-A on October 19, 1994. Chevron responded to Koch on November 3, 1994.

7. Shell filed a letter on November 10, 1994, in support of Advice Letter Supplement No. 8-A and in response to Koch's letter of October 19, 1994 and the Chevron letter of November 3, 1994.

8. Koch filed a letter on November 15, 1994, responding to the Chevron response of November 3, 1994.

9. Shell filed a letter on December 12, 1994, responding to Koch's letter of November 15, 1994. Shell does not believe the geographic limitation is discriminatory, but rather that it establishes an objective standard for quality of crudes tendered for shipment on the KLM pipeline.

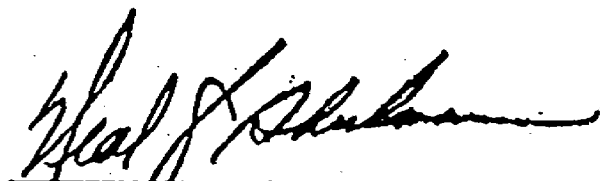
10. Chevron's request to replace CAL. P.U.C. No. 1 with CAL. P.U.C. No. 18 is reasonable and nondiscriminatory in light of the circumstances described above.

February 8, 1995
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THEREFORE, IT IS ORDERED that:

1. Chevron Pipeline Company is authorized to cancel its tariff CAL. P.U.C. No. 1 and replace it with CAL. P.U.C. No. 18 which would limit shipments on the KLM pipeline system to virgin crude oil and direct liquid products of oil and gas wells, and specify that tenders to the system must be indigenous San Joaquin Valley crudes.
2. Advice Letter No. 8 and Advice Letter Supplement No. 8-A and the accompanying tariff sheets shall be marked to show that they were approved by Commission Resolution O-0002.
3. The protests of Koch and Tosco are denied.
4. This Resolution is effective today.

I hereby certify that this Resolution was adopted by the Public Utilities commission at its regular meeting on February 8, 1995. The following Commissioners approved it:


NEAL J. SHULMAN
Executive Director

DANIEL WM. FESSLER
President
NORMAN D. SHUMWAY
P. GREGORY CONLON
JESSIE J. KNIGHT, JR.
Commissioners