Decision _____

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Pipeline System LLC for Authorization to Increase Its Rates and Charges for Crude Oil Transportation Services on Its Line 63 System Effective November 1, 2004.	Application 04-10-002 (Filed October 1, 2004)

O P I N I O N

1. Summary

Pacific Pipeline System LLC (Pacific Pipeline) applied for Commission authority to increase its rates and charges for all crude oil transportation services on its Line 63 System by 9.5%, effective November 1, 2004. The requested increase of $2.033 million would provide Pacific Pipeline an opportunity to earn an overall return of 6.97% and a 6.99% return on equity for its Line 63 System. The application is approved.

2. Background

Pacific Pipeline is a Delaware Limited Liability Company authorized to do business in California.[1] Its principal place of business is in Long Beach, California.

[1] In D.02-06-069, dated June 27, 2002, the Commission approved an indirect change of control of Pacific Pipeline through an internal restructuring establishing a master limited partnership form of ownership.

Pacific Pipeline owns and operates two separate common carrier crude oil pipeline systems. Each system has a separate set of tariffs on file with the Commission. One system, Line 2000, or the Pacific System, consists of a 130-mile, 20-inch insulated pipeline that extends from Kern County to the Long Beach and El Sequndo areas. The requested increase in rates in this application is not applicable to the Pacific System, Line 2000.

The second system is the Line 63 System. The Line 63 System includes a 118-mile, 16-inch and 14-inch trunk line from Kern County to the City of Carson, with an average pumping capacity of approximately 105,000 barrels per day. The Line 63 System also includes gathering and distribution lines. Gathering lines gather oil from various locations in the San Joaquin Valley. This gathered oil is transported north to Bakersfield area refineries and south into the Los Angeles Basin. The new rates requested in this application are applicable solely to the Line 63 System.

The history of the company is in its application[2] and also in the last rate setting Decision (D.) 01-01-006 dated January 4, 2001. In that decision, the Commission authorized Pacific Pipeline to increase its rates and charges for all crude oil transportation services on its Line 63 System by 5%, effective October 1, 2000, which provided an opportunity to earn an overall return of 7.56% and an equity return of 7.1%. Based on the projected throughputs for that test year, the request increased annual revenues by approximately $1.04 million. Subsequently, the Commission authorized Pacific Pipeline to further increase rates by approximately $2.1 million to recover rising electricity costs, as

[2] Application, pp. 2-3.

requested in Advice Letter 12 and as revised in 12-A, effective August 1, 2001. The Energy Division approved implementation of Advice Letter 12 and 12-A by letter dated August 21, 2001, pursuant to delegated authority in General Order 96-A.

3. Requested Increase In Rates

A. Operating Expenses

Applicant states that average throughput volumes on Line 63 have steadily decreased, a trend that has continued since Application (A.) 00-08-052, so that for the test year September 1, 2004 to August 31, 2005, throughput on Line 63 is expected to decrease to 55,700 barrels per day compared to approximately 66,600 barrels per day forecast for August 1, 2000 through July 31, 2001.

Pacific Pipeline asserts that a $1.4 million increase is attributable to increases in right-of-way and line lease expenses, currently $1.5 million higher than those costs as forecast in the last proceeding.[3] In total, the company forecasts operating expenses of $16,991,000 plus other costs including taxes, interest and the full reasonable return on equity, for a total cost of service of $29,083,000.[4]

B. Rate of Return

In D.02-06-069, the Commission authorized an indirect change of control and approved, pursuant to § 854(a), an internal restructuring establishing a

[3] Application, p. 6

[4] Ex. 11, line 15, and various work papers supporting the application.

master limited partnership form of ownership.[5] Pacific Pipeline is currently earning less than the 7.56% rate of return authorized in D.01-01-006. Applicant seeks adoption of an overall rate of return of 6.97%, net of a reduction in rates due to competitive pressures, lowering the requested before-tax return on equity from 14.5% to 6.99%.

Proposed Capital Structure and Cost of Capital[6]			
	Weight[7]	Cost	Weighted Cost
Debt	45.71%	6.95%[8]	3.18%
Equity	54.29%	6.99%[9]	3.79%
	100.00%		6.97%

Pacific Pipeline points out that the rate of return for petroleum pipelines is determined on an infrequent basis, and offered the comparisons shown below for both pipelines and less-risky utility operations.[10] Pacific Pipeline argues that a return on equity of 14.5% would be reasonable based on the comparable risks of other pipelines and the greater risk compared to an electric or natural gas utility.

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[5] Pacific Energy Partners, LP (Pacific LP), a limited partnership was formed pursuant to the Delaware Revised Uniform Limited Partnership Act. Pacific LP became the sole owner of Pacific Energy Group LLC (PEG). Pacific Energy GP, Inc. (Pacific GP) is a Delaware corporation and the general partner of Pacific LP. (D. 02-06-069, *mimeo.*, p. 1.)

[6] Application, p. 7.

[7] Work papers, Schedule 8.

[8] Work papers, Schedule 9.

[9] Application, p. 8.

[10] Application, p. 7.

Comparison of Rates of Return on Equity			
Oil Pipelines			
SFPP, LP	CPUC	Pending	15.86%
SFPP, LP	CPUC	D.92-05-018	13.54%
SFPP, LP	FERC	Opinion No 435	14.40%
TAPS	Alaska	Order 151	13.10% - 14.75%
Energy Utilities			
Southwest Gas	CPUC	D.04-3-034	10.90%
PG&E Edison Sierra Pacific SDG&E	CPUC	D.02-11-027	11.22% 11.60% 10.90% 10.90%

C. Competitive Influences

Pacific Pipeline asserts that it faces competition from other pipelines and alternative markets to transport a declining supply of crude oil. In effect, Pacific Pipeline seeks a market-based rate for transportation service.[11] The requested $2.033 million increase reflects the use of the 6.99% return on equity, not 14.5%. Pacific Pipeline proposes a unique cap to its rate request: while it argues an equity return of 14.5% is otherwise justified, it requests approval of a reduced return of 6.99% on equity, unless any test year forecast operating expenses are disallowed. If adopted test year expenses are less than requested, then applicant requests that the return on equity correspondingly increase so that test year revenues at adopted rates remain constant. Thus, Pacific Pipeline has determined what it perceives to be the competitive rate for its services and concedes the difference in its return on equity.

Adopted Results of Operations Test Year September 1, 2004 to August 31, 2005 (Source: Work Papers)	
Revenue at Current Rates	$21,397,000
Non-Tariff Revenue	2,513,000
Requested Rate Increase	2,033,000
Total Revenue	25,943,000
Cost of Service	
Operating Expenses	$16,991,000
Interest Expense	1,488,000
Depreciation - Plant	4,106,000
Amortization of AFUDC	289,000
Income Taxes	2,523,000
Return on Equity (14.5%)	3,686,000
Cost of Service - Forecast	$29,083,000
Foregone Revenues – Equity at 6.99%	($3,140,000)

4. Protest

There were no protests. EOTT Energy Operating Limited (EOTT) protested Pacific Pipeline's last application, A.00-08-052. EOTT is no longer in business[12] and thus Pacific Pipeline did not serve a copy of this application on EOTT.

5. Discussion

This application is filed pursuant to Pub. Util. Code § 454. Consistent with Pub. Util. Code § 455.3, Pacific Pipeline gave all shippers no less than 30 days' notice of the rate change. Following that notice, a pipeline corporation is entitled

[11] Application, p. 8.

[12] A representation of counsel for Pacific Pipeline, by letter dated October 13, 2004.

to change its rates prior to Commission approval, barring suspension or other action by the Commission.

Pacific Pipeline has made a *prima facie* showing that its request is reasonable. The applicant's request would make permanent the energy cost increases authorized when Advice Letter 12 and 12-A were approved, and would include the majority of the identified increases in right-of-way and line lease expenses that have occurred since the last test year result was adopted. Pacific Pipeline's request for a $2.033 million increase is justified by the increased costs and the need for a reasonable rate of return. A return on equity of 6.99% is well below recent comparable returns authorized for regulated natural gas utilities in California and significantly below returns authorized by the Federal Energy Regulatory Commission and other jurisdictions for oil pipelines.

The application is approved.

6. Waiver of Comment Period

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

7. Assignment of Proceeding

Susan P. Kennedy is the Assigned Commissioner and Douglas M. Long is the assigned Administrative Law Judge in this proceeding.

8. Categorization and Need for Hearings

Notice of this Application appeared in the Commission Daily Calendar on October 5, 2004. In Resolution ALJ 176-3140, dated October 7, 2004, the

Commission preliminarily categorized this proceeding as ratesetting, and preliminarily determined that hearings were necessary. Based on the record, we now conclude that a public hearing is not necessary, but we affirm the proceeding is ratesetting.

Findings of Fact

1. The rate increase sought by Pacific Pipeline applies only to the Line 63 System and not to the Pacific System.

2. The last increase in Line 63 System rates occurred in 2001, when the Commission approved Advice Letter 12 and 12-A to reflect increased electricity costs.

3. Average throughput on Line 63 has decreased from 66,600 in 2000 - 2001 to 55,700 barrels per day in 2004 - 2005.

4. The reasonable return on equity is 14.5% for Line 63 for the test year October 1, 2004 to September 31, 2005.

5. Competitive pressures in its market limit Pacific Pipeline's ability to charge rates that reflect the full return on equity it argues would be reasonable: 14.5%.

6. The increase of $2.033 million Pacific Pipeline formally requests in this application will afford it the opportunity to earn an overall return of 6.97% and an equity return of 6.99%.

7. Pursuant to Pub. Util. Code § 455.3, Pacific Pipeline has given the Commission and all shippers no less than 30 days' notice of the rate change and it has made the change effective as of November 1, 2004.

8. No party protested this application and evidentiary hearings are not required.

Conclusions of Law

1. The application should be approved because Pacific Pipeline demonstrated that the request is just and reasonable.

2. The Commission's preliminary determination that evidentiary hearings are required should be changed.

O R D E R

IT IS ORDERED that:

1. Pacific Pipeline System LLC (Pacific Pipeline) is authorized to increase its rates and charges for all crude oil transportation services on its Line 63 System by $2.033 million annually, effective November 1, 2004.

2. Pacific Pipeline shall file an advice letter to conform its tariffs within 21 days of this order.

3. This is a final determination that evidentiary hearings are not required.

4. Application 04-10-002 is closed.

This order is effective today.

Dated _____, at San Francisco, California.