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BEFORE THE WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND)Docket No. TO-011472
TRANSPORTATION COMMISSION,)Volume X
Complainant,)Pages 952-1206
)
v.)
)
OLYMPIC PIPE LINE COMPANY,)
INC.,)
Respondent.)
_____)

A hearing in the above matter was held on January 16, 2002, at 9:35 a.m., at 1300 Evergreen Park Drive Southwest, Olympia, Washington, before Administrative Law Judges ROBERT WALLIS and THEODORA MACE, Chairwoman MARILYN SHOWALTER, and Commissioner PATRICK OSHIE.

The parties were present as follows:

OLYMPIC PIPE LINE COMPANY, INC., by Steve Marshall, Attorney at Law, One Bellevue Center, Suite 1800, 411 108th Avenue, N.E., Bellevue, Washington 98004, and Patrick W. Ryan, Attorney at Law, Perkins Coie, 1201 Third Avenue, Suite 4800, Seattle, Washington, 98101.

TESORO, by Robin Brena, Attorney at Law, 310 K Street, Suite 601, Anchorage, Alaska 99501.

Barbara L. Nelson, CSR
Court Reporter

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1 TOSCO CORPORATION, by Edward A.
2 Finklea, Attorney at Law, 526 N.W. 18th Avenue,
3 Portland, Oregon 97209.

4 THE COMMISSION, by Donald Trotter
5 and Lisa Watson, Assistant Attorneys General, 1400
6 Evergreen Park Drive, S.W., P.O. Box 40128, Olympia,
7 Washington 98504-0128.

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1 JUDGE WALLIS: Let's be on the record,
2 please, for the Wednesday, January 16, 2002 hearing
3 session in the matter of Commission Docket Number
4 T0-011472. We're going to begin this morning's
5 session by interrupting the testimony of Mr. Elgin to
6 bring Mr. Schink to the stand to accommodate his
7 scheduling needs. Mr. Schink, would you please stand
8 and raise your right hand?
9 Whereupon,

10 GEORGE SCHINK,
11 having been first duly sworn, was called as a witness
12 herein and was examined and testified as follows:

13 JUDGE WALLIS: Please be seated.

14 Mr. Marshall.

15 MR. MARSHALL: Thank you.

16

17 D I R E C T E X A M I N A T I O N

18 BY MR. MARSHALL:

19 Q. Mr. Schink, do you have before you your
20 testimony in this matter, which is marked as Exhibit
21 101-T?

22 A. Yes, I do.

23 Q. Do you have any corrections to make to that
24 prefiled testimony?

25 A. There are some typos, which I guess we're

00958

1 going to handle by errata. The only thing I should
2 note, on page nine, Mr. Fox made some small changes
3 in his numbers, which affect the numbers in a small
4 way in lines seven to 13 on that page, and I think
5 that's the bulk of it.

6 MR. MARSHALL: Okay. Would the Commission
7 like those changes to those numbers or would that be
8 fine for an errata sheet, as well?

9 JUDGE WALLIS: Are they likely to be
10 matters of significance during the presentation?

11 THE WITNESS: They don't change any of the
12 conclusions or affect them in any way.

13 MR. BRENA: That would be acceptable. As I
14 recall Mr. Fox's change, it was \$100,000 in the \$9
15 million item, and that's inconsequential.

16 JUDGE WALLIS: Very well.

17 Q. That's the change you had in mind?

18 A. That's the change I had in mind.

19 JUDGE WALLIS: Let's use errata sheet for
20 that purpose.

21 Q. With those corrections in mind, if asked
22 the questions in 101-T as set forth, would you give
23 the same answers under oath today?

24 A. Yes, I would.

25 MR. MARSHALL: We move for the admission of

00959

1 the testimony and offer the witness for
2 cross-examination.

3 JUDGE WALLIS: Is there objection to the
4 exhibit? Let the record show that there is no
5 objection, and the witness is available for
6 cross-examination. Mr. Brena.

7

8 C R O S S - E X A M I N A T I O N

9 BY MR. BRENA:

10 Q. Good morning, Mr. Schink.

11 A. Good morning.

12 Q. With regard to your background and
13 experience, have you ever given cost of -- have you
14 ever given cost of capital testimony in an oil
15 pipeline case?

16 A. I've submitted written testimony, yes.

17 Q. And was the written testimony, did it
18 concern the cost of capital under a traditional cost
19 of service model?

20 A. Well, it was using the FERC's 154(b)
21 methodology, which is what you use before the Federal
22 Energy Regulatory Commission.

23 Q. And have you done that several times or a
24 single time or how many times?

25 A. I've done it five or six times.

00960

1 Q. Have you ever, in your experience, directly
2 negotiated the placement of debt in the debt
3 marketplace?

4 A. No, I have not.

5 Q. Have you ever rated or participated
6 directly in the placement of debt by a utility?

7 A. No, I've not.

8 Q. Have you ever directly negotiated the terms
9 of debt with a lender?

10 A. Other than my mortgage, no.

11 Q. What was the amount of your mortgage?

12 A. Several hundred thousand dollars.

13 Q. Was it for your house?

14 A. It was for my house, yes.

15 Q. So other than for a house loan, you have
16 never negotiated the terms of debt?

17 A. I have never negotiated terms of debt for a
18 business, no.

19 Q. Have you ever attended a Standard and
20 Poor's bond rating seminar?

21 A. I have not.

22 Q. Do you know of companies which participate
23 in the debt marketplace without audited books and
24 records?

25 A. I can't answer that. It's unusual, but I

00961

1 can't say there aren't any.

2 Q. Do any come to mind?

3 A. No, they don't.

4 Q. Do you know of any companies that
5 participate in the debt marketplace with zero equity
6 and no corporate guarantees or some other form of
7 financial assurances from third parties?

8 A. Yes.

9 Q. And what company is that?

10 A. Colonial Pipeline, Explorer Pipeline,
11 Express Pipeline.

12 Q. Those three pipelines participate in the
13 debt marketplace and they have no corporate
14 guarantees?

15 A. That's right. They're backed by -- on some
16 of the loans for Colonial and Explorer, they do, but
17 a lot of it is backed by T&D agreements.

18 Q. Throughput and deficiency agreements?

19 A. Throughput and deficiency, I apologize.

20 Q. So those are financial assurances from
21 third-party owner/shippers that they will have a
22 certain level of throughput on the line; correct?

23 A. No, just shippers. There are -- some are
24 owners and some are not.

25 Q. Okay. Let me restate my question. Are you

00962

1 aware of any company that participates in the debt
2 marketplace without some sort of financial assurances
3 from a third party and has zero equity?

4 A. No, it's either a parent guarantee or
5 throughput and deficiency.

6 MR. BRENA: No further questions.

7 JUDGE WALLIS: Mr. Finklea, you have no
8 questions for this witness; is that correct?

9 MR. FINKLEA: That is correct, Your Honor.

10 JUDGE WALLIS: Mr. Trotter.

11 MR. TROTTER: We have no questions of Mr.
12 Schink.

13 JUDGE WALLIS: Commissioners.

14

15 E X A M I N A T I O N

16 BY CHAIRWOMAN SHOWALTER:

17 Q. Well, I have some questions about the
18 concept of a throughput and deficiency company or
19 structure. What I'm trying to see here is where are
20 the risks placed in an entity like that, both
21 financial and maybe other risks?

22 From listening to this so far, it seems to
23 me that if you have a company with no equity, and no
24 guarantees by the shareholders or parents, no
25 recourse to them, but you do have the throughput and

00963

1 deficiency type of agreements, that -- in effect,
2 that pushes the risk of disaster or financial
3 hardship or various other things onto the shippers.
4 Am I right on that?

5 A. Well, it's -- there are force majeure
6 clauses in these T&Ds. If a pipeline can't transport
7 it, the shippers aren't responsible. I mean, so
8 they're not -- but so long as the pipeline is
9 operating and is capable of moving the committed
10 barrels by the shippers, they -- the shippers have to
11 do it. Would it help if I explained the reasoning
12 behind these agreements or --

13 Q. Go ahead.

14 A. The shippers are under -- basically, the
15 shippers, on refined product pipelines, own
16 refineries that are going to be there for a long time
17 and want to have assurance of the ability to
18 transport product via pipeline to the various
19 locations that they're supplying from their refinery.
20 It is -- to, in essence, in part to ensure their
21 ability to do the shipping and in part to basically
22 ensure that pipeline's capacity will be available,
23 they will enter into these agreements, in some cases,
24 for as many as 15 years, that they will ship a
25 minimum amount of barrels, usually per year, per

00964

1 month, but -- and they will pay a tariff as specified
2 in the agreement.

3 They enter into it because it's in their
4 interest to have this transportation, and it's become
5 sort of the standard practice in the pipeline
6 industry to do things this way, because the oil
7 companies often are owners of these pipelines, they
8 don't want to -- they want to make sure everybody
9 who's using it in some sense participates, and so
10 these throughput and deficiency agreements are
11 brought up, so essentially everybody contributes or
12 makes a guarantee, essentially, of revenue to the
13 company, which then they can take to lenders and
14 borrow money for operating purposes and expansion.

15 I think the most impressive use of these is
16 Express Pipeline, which is a crude oil pipeline from
17 Canada into Wyoming, which was financed entirely by
18 throughput and deficiency agreements. It was built
19 with, you know, with these as collateral, so --

20 Q. Okay. So is it a fair summary to say that,
21 in those instances, that the shippers are closer to
22 the concept of an owner in that, because they have an
23 interest in this pipeline remaining there and being
24 there for them, they are more willing to take on more
25 risk?

00965

1 A. Precisely.

2 Q. Because -- am I right that a T&D
3 arrangement with no equity on the part of the owners
4 does place more responsibility or risk on the
5 shippers?

6 A. The owners are typically shippers, also,
7 and would also enter into a similar agreement. So
8 it's not just the shippers, but it's the
9 owner/shippers, also.

10 Q. But it's the owners, as shippers, as
11 opposed to the owners, as owners?

12 A. That's correct.

13 Q. Okay. Now, so your recommendations here
14 are in part posited on the soundness of such an
15 arrangement?

16 A. These financial practices are widespread
17 within the industry. It occurs when major oil
18 companies, either one company or a group of oil
19 companies, owns a pipeline. They are sound financial
20 arrangements, in essence, because there is a -- there
21 is a fairly steady expected revenue stream. The
22 problem, in Olympic's case, is not the way it's
23 capitalized; the problem is a lack of revenue.

24 Q. Okay.

25 A. And that would be true independent of

00966

1 whether it had, you know, all debt, no debt, or
2 50/50. It's -- the problems that -- the financial
3 problems that Olympic is having have nothing to do
4 with its capital structure; it has to do with a lack
5 of revenue.

6 Q. Well, I'd like to explore that. If the
7 owners' risk is really no more than the risk that the
8 customers' shippers take on, where is the incentive
9 for the owners to manage the company? Or put another
10 way, these shippers, as shippers, as customers only,
11 can't manage the company. Am I right on that?

12 A. That's correct.

13 Q. All right. So with whatever incentives
14 they have, they can't translate that directly to a
15 management responsibility?

16 A. That's correct.

17 Q. All right. Then, if we take the owners
18 now, if their interest is no greater than the
19 shippers, where is the incentive to manage the
20 company appropriately?

21 A. One of the incentives the T&D agreements
22 require, that the pipeline be operating and so on and
23 so forth, and they don't manage it properly and it
24 fails for some reason, force majeure takes over and
25 the shippers no longer have responsibility. So if

00967

1 they fail to manage it properly, the guarantees
2 provided by these other people disappear and it will
3 tend to fall back on the pipeline.

4 Q. But where does it fall? Let's assume -- I
5 don't want to get too close to the actual Olympic
6 Pipe Line situation, because I don't know all of the
7 facts, but let's posit a situation that may be close
8 to that. Let's assume that a pipeline company -- a
9 pipeline was mismanaged.

10 A. Right.

11 Q. And as a result of mismanagement, an
12 accident occurred. I don't want to say that's
13 Olympic's situation.

14 A. No, I understand it's a hypothetical.

15 Q. But it could happen.

16 A. It's a hypothetical.

17 Q. All right. So the pipeline stops
18 functioning or is shut down. Now, from what you just
19 said, the shippers no longer have a responsibility,
20 because the pipeline is shut down?

21 A. And the owner/shippers don't have a similar
22 out. They can't walk away from it.

23 Q. Right. But where is the equity -- who
24 ponies up the money for whatever disaster unfolds?

25 A. Well, typically, if the company -- the

00968

1 companies don't want to lose control of the pipeline,
2 because if they operate it properly, they do get a
3 return, an income, and companies are in business to
4 earn an income. They have the incentive to run it
5 right to earn the income.

6 Secondly, they don't really want -- you
7 know, they don't want the pipeline -- assuming the
8 pipeline is financially healthy, that the revenues
9 are there and, you know, beyond this problem, the
10 revenues will be there sufficient to cover costs,
11 they will, in fact, make interim loans or whatever's
12 necessary to get it through.

13 I think the difference between the typical
14 situation here is that -- well, the caveat here, and
15 the problem with Olympic, is that right now the
16 expectations of revenues aren't there to give them
17 the incentive to put the additional money in.

18 Q. But couldn't one say that in a typical T&D
19 arrangement with no equity in the company, there's
20 not as much incentive to -- because the owners don't
21 have that equity at stake -- to make certain that
22 that pipeline is operated in a way so as not to
23 jeopardize the equity. There's no equity to
24 jeopardize. There's only the pipeline functioning,
25 which has an interest to the shipper and the

00969

1 owner/shipper as a shipper.

2 A. Well, ultimately, they -- whether they have
3 equity in the pipeline or not, they are the owners of
4 that asset, and to the extent it has value, they want
5 to retain it, and to the extent they let the company,
6 say, slip into bankruptcy, they would lose control of
7 that asset and possibly, you know, lose a lot of
8 value.

9 Q. But what value is there that belongs to the
10 owner if all the value is in either the debt or the
11 shippers?

12 A. Well, I think the problem is that the
13 lenders use the T&Ds as security for loans, but the
14 actual -- whether or not there is equity capital in
15 the pipeline or not, the owners are still the owners.
16 If it were sold, they would get the money for it.

17 Q. What makes you say that, if this is a
18 regulated entity where apparently the ratepayers have
19 put in all of the value, other than loans, where is
20 the -- where is the ownership value there?

21 A. The ownership value is created essentially
22 by, you know, the money put into it, you know, by the
23 company, the effort put into the company, the
24 management and the rest of it. The fact that there
25 isn't equity in the capital structure doesn't mean

00970

1 that the company hasn't made a commitment and
2 wouldn't suffer a financial loss if, in fact, the
3 pipeline were to slip into bankruptcy.

4 Q. Well, if the pipeline company slips into
5 bankruptcy, what loss is there if they have no equity
6 in it?

7 A. I think one of the things is that the
8 company -- well, the companies are putting money in
9 via either debt or equity, they have money in it, and
10 they're going to lose that money. And typically, the
11 owners have debt claims against the pipeline, which
12 are -- which they will lose if the pipeline goes
13 under.

14 So it doesn't really make any difference
15 financially to the owners if the claim is labeled
16 debt and they don't -- and they lose that amount of
17 money or it's labeled equity and they lose that
18 amount of money. The owners typically have loaned
19 large amounts of money to the pipeline as
20 owner/shippers, and therefore have basically -- and
21 would lose that, you know, would be liable for a
22 large portion of it.

23 Q. Well, but no more than what they're owed?

24 A. Well, what they're owed is typically as
25 much as 50 or more percent of the debt, which is no

00971

1 different than having 50 percent as equity.

2 Q. Okay. I'd like to stop on that point,
3 then. Is there a difference between being owed \$50
4 million in a loan from the owner/shipper to the
5 company versus a contribution of \$50 million in
6 equity? Do you see a difference in those two?

7 A. There may be a slight difference for tax
8 purposes. In terms of having capital risk, there's
9 none. There may be a tax advantage to doing it this
10 way, but in terms of risk to capital, there's no
11 difference.

12 Q. Does your recommendations -- this
13 recommendation here about what we should do depend on
14 the FERC methodology? In other words, is it a given
15 that you are operating or assuming the FERC
16 methodology for purposes of your --

17 A. In terms of the immediate hearing?

18 Q. Uh-huh.

19 A. No, it's not contingent on that. I
20 basically have taken the Staff's approach and made
21 what I thought are appropriate adjustments to it. I
22 think the Staff methodology is appropriate. I
23 disagree with some of their assumptions, which I've
24 spelled out in my testimony. In that, my analysis,
25 to that extent, is merely just making adjustments to

00972

1 the Staff's approach. The requested amount of tariff
2 that -- in the general case is, in fact, based on
3 FERC methodology.

4 Q. Okay. But in your view, this Commission
5 doesn't need to elect or endorse one methodology or
6 another in order to grant the company the relief it's
7 requesting?

8 A. No, not at all. It has no effect on that.

9 Q. Let me ask you, on page six of your
10 testimony, line 14, you say, Olympic's cost of debt
11 is based on the creditworthiness of its parents, and
12 I would like to know why that is the case. I can
13 understand if BP is rated an AA plus, it would go out
14 and get a loan based on that. Why would -- why is
15 Olympic Pipe Line in that same situation?

16 A. Basically, the -- if you're going to rate
17 the company as such, it is viewed as if it were, even
18 though the legal arrangements are different, as if it
19 were a wholly-owned subsidiary of its owners.

20 Q. But if that's the case, why would it be so
21 difficult for Olympic to get a loan right now?

22 A. Basically, the parents have to extend a
23 guarantee to the lenders for them to do that. And
24 for BP -- it's not unusual for the owners -- the T&Ds
25 are a very common way. There are also instances

00973

1 where the parents extend the guarantee to a loan for
2 -- taken out by the company, but the reality is that
3 these companies make these guarantees, are willing to
4 extend these guarantees only when they believe that
5 there is sufficient revenues in the pipeline company
6 itself, so their expectation is they won't have to
7 make the interest payments and their expectation is
8 they won't have to repay the loan.

9 These companies, BP or Equilon or all the
10 major oil companies are international companies, they
11 have -- they only make investments or are willing to
12 -- and they would view backing this or offering a
13 guarantee on this debt as if making an investment.
14 They only make an investment if they can expect a
15 reasonable return. And by backing a loan where there
16 wasn't an expectation of sufficient revenue to meet
17 the interest payments or to repay the principal is,
18 you know, not the kind of thing that the boards in
19 BP's case, in London, are going to approve.

20 They won't invest where they get no return
21 and they're going to lose the money they invest.
22 They have to have a legitimate expectation that a
23 loan taken by Olympic will, in fact, be paid both in
24 terms of interest and principal when revenue is
25 generated by Olympic.

00974

1 Q. I asked a witness earlier whether, if we
2 granted the increase requested -- I take that back.
3 I think that was about whether the company would
4 proceed with its capital plan.

5 Do you have any knowledge of whether, if we
6 grant the request, the parents will guarantee or just
7 that there's a better prospect that they will?

8 A. I really can't speak for the company. I
9 think what Mr. Fox said yesterday is -- I think he
10 said he would recommend it. I think -- I can't speak
11 to it, because I'm not an employee of the company.

12 Q. Thank you.

13 A. You're welcome.

14 JUDGE WALLIS: Mr. Marshall.

15

16 R E D I R E C T E X A M I N A T I O N

17 BY MR. MARSHALL:

18 Q. Mr. Schink, you mentioned Colonial and
19 Explorer. Could you describe a little bit about
20 Colonial, what it is?

21 A. Colonial is a refined products pipeline
22 that begins in Houston and goes along the Gulf Coast,
23 picking up refined products from all the large
24 refineries on the Gulf Coast, and it transports it to
25 Atlanta, north through the Carolinas, Washington,

00975

1 D.C., and finally into essentially New York City. It
2 goes to Linden, New Jersey, which is right across the
3 river.

4 Q. And how big is Colonial?

5 A. It has a capacity of 2.1 million barrels a
6 day, which is like six or seven big refineries.

7 Q. Is it one of the biggest, if not the
8 biggest, oil pipeline in the United States?

9 A. I think it may well be the biggest refined
10 products pipeline in the world by quite a bit. The
11 next biggest are five and six hundred thousand a day.

12 Q. What's Colonial's method of financing?
13 Does it have a hundred percent or nearly a hundred
14 percent debt?

15 A. I looked at their FERC Form 6. The oil
16 pipeline companies have to file financial reports
17 with the Federal Energy Regulatory Commission, and
18 it's called FERC Form 6. And I looked at Colonial's
19 for the year 2000, and their debt-to-capital ratio
20 was 116 percent, so they had negative equity in the
21 year 2000, yet they're one of the most profitable oil
22 pipelines in the world. They're very, very
23 profitable.

24 Q. Have you done work for Colonial and
25 Explorer and other pipelines?

00976

1 A. Yes, I've worked, I think, for over 20 oil
2 pipeline companies.

3 Q. Mr. Hanley said yesterday that he didn't
4 know about Colonial. How is that possible?

5 MR. BRENA: Objection. This is beyond the
6 scope.

7 MR. MARSHALL: I'll withdraw the question.

8 JUDGE WALLIS: Thank you.

9 Q. Throughput and deficiency agreements, you
10 said, are common in the industry?

11 A. That's correct.

12 Q. Are there other analogies that you have in
13 mind for other industries where financing
14 arrangements have grown up over time and have created
15 expectations among lenders and owners and users?

16 MR. BRENA: Objection, relevancy and scope.

17 THE WITNESS: Yes.

18 JUDGE WALLIS: The witness may respond.

19 THE WITNESS: A throughput and deficiency
20 agreement used as a guarantee against the loan is
21 really pledging expected future income or future
22 revenue as guarantees -- to guarantee the payment of
23 the loan. It's common, for example, in the movie
24 industry to finance the making of moving pictures
25 with pledges of revenues from the movie using,

00977

1 usually not as a guarantee.

2 For someone who owns a patent and is going
3 to license to others and collect royalties, the
4 company can take the expected royalties from that
5 patent and use that as security to obtain a loan. So
6 it's used widely in the industry wherever you can, in
7 fact, identify a stream of -- expected future stream
8 of revenues that's certain enough that the lenders
9 will accept it as security against a loan.

10 Q. Chairwoman Showalter asked some questions
11 about risk and management. Have you seen any
12 evidence in this case that BP Pipelines, as operator
13 of Olympic, is doing any less than it could to get
14 the throughput levels back up as rapidly as possible
15 on this pipeline?

16 MR. BRENA: Objection, scope. This issue
17 wasn't discussed at all.

18 MR. MARSHALL: I believe the risk issues
19 about operations really are a central question here.

20 JUDGE WALLIS: The witness may respond.

21 THE WITNESS: It's my understanding that
22 the company, in fact, is making all the investments
23 necessary to ensure that the pipeline will operate
24 properly and is, in fact, staffing it properly and
25 doing the other things necessary to make sure that

00978

1 the pipeline will run on a steady and consistent
2 basis in the future. And once that happens, then
3 people who would like to loan money to it would have
4 confidence that, you know, it would continue to run
5 and operate and generate revenues.

6 If shippers think there's a risk that the
7 pipeline will have an accident or break, they're less
8 willing to advance loans based on T&Ds, because
9 there's a concern that the revenue, in fact, won't be
10 forthcoming. They have to be confident that the
11 pipeline will be reliable and operate and be safe.

12 MR. MARSHALL: No further questions.

13 JUDGE WALLIS: Mr. Brena.

14

15 R E C R O S S - E X A M I N A T I O N

16 BY MR. BRENA:

17 Q. Mr. Schink, have you reviewed Colonial
18 Pipeline's throughput and deficiency agreements?

19 A. I haven't reviewed them specifically. I've
20 talked -- I know some of them exist and I've talked
21 to the people about them. I haven't reviewed them in
22 any detail.

23 Q. Have you reviewed -- have you read the
24 throughput and deficiency agreements for Olympic?

25 A. I have only seen the one that Tesoro, I

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1 think, had signed relative to Cross Cascades. I have
2 not read it carefully.

3 Q. Have you read the ones that the affiliates
4 have in place?

5 A. I have not.

6 Q. Have you read any other ones that they may
7 have?

8 A. No, I have not.

9 Q. Have you participated directly in arranging
10 financing for an oil pipeline?

11 A. No, I have not.

12 Q. Would you name for me a single throughput
13 and deficiency agreement for Colonial by a shipper
14 who is not also an owner?

15 A. I don't know if I could or not. I don't
16 remember whether -- I mean, I don't remember if there
17 is one or not.

18 Q. For Explorer?

19 A. Same answer. I don't know if there's one
20 there or not.

21 Q. For Express?

22 A. I can't name them, but I know they existed,
23 because I worked for Express when they were, in fact,
24 trying to get financing, and they had about half from
25 owners and half from non-owners.

00980

1 Q. Would you name a single non-owner/shipper
2 that provided a throughput and deficiency agreement
3 for Express?

4 A. I can't name them now.

5 Q. Do you know whether or not they were part
6 of the ultimate finance package for Express?

7 A. I know that these agreements were part of
8 the finance package, because that was the reason they
9 were working so hard to get the FERC approval.

10 Q. Isn't it fair to say that throughput and
11 deficiency agreements are typically advanced in the
12 industry by owner/shippers to fund the initial
13 construction of a pipeline?

14 A. That's a common use. It's certainly not
15 the only use.

16 Q. How many throughput and deficiency
17 agreements have you read in your career?

18 A. I've probably looked at several dozen over
19 the course of -- in my career.

20 Q. For what lines?

21 A. I looked at -- I've looked at one of them
22 for Tapco, I've looked, over the years, at some of
23 them for Explorer, I've looked at them for Longhorn
24 Pipeline, I've looked at them for Express. There may
25 be others. I can't remember.

00981

1 Q. Was there a single one that comes to mind
2 that was offered by a non-shipper/owner which you can
3 name?

4 A. I can't name them, but I know the ones in
5 Express involve -- some of the ones that I'm looking
6 at involve non-shippers.

7 Q. Only in Express? That's the only one that
8 you know of that there may have been one?

9 A. I know there are ones with other pipelines.
10 The only ones I can recall having actually seen are
11 the ones for Express.

12 Q. Do you know whether or not Olympic's
13 throughput and deficiency agreements that it has with
14 Prudential and the owners require it to continue to
15 operate?

16 A. Usually, the owners' agreements don't have
17 force majeure, because they're supposed to be --
18 well, they don't have agreements of the sort that a
19 third party one would have. I'm not aware
20 specifically of those. I have not read the agreement
21 carefully, so I can't tell you.

22 Q. Are you aware whether Prudential's loan
23 assurances require Olympic to continue to operate the
24 line?

25 A. I can't say that. I don't know.

00982

1 Q. Would you expect it to be a reasonable loan
2 term to continue to operate the line?

3 A. When you're an owner and a shipper --

4 Q. Excuse me. For Prudential?

5 A. For Prudential. Prudential would probably
6 not let -- to the extent it would not allow the
7 company to get out of the agreement based on whether
8 the pipeline was running or not. It would not make
9 sense for them to do so.

10 Q. Now, a shipper on a common carrier has a
11 right to tender shipments and to have them received
12 on a nondiscriminatory basis; correct?

13 A. Correct.

14 Q. Regardless of whether they provide a
15 throughput or deficiency agreement, that shipper is
16 entitled to the same pro rata share of throughput
17 through the line; correct?

18 A. In most cases, yes.

19 Q. Are you suggesting that a common carrier
20 can discriminate among shippers based on whether
21 they're willing to provide security for the owner's
22 loans?

23 A. No, but with FERC approval, I know a part
24 of the arrangement that Express made said that they
25 could guarantee the space to the people who made the

00983

1 upfront commitments, because they had made a 15-year
2 commitment of throughput, but it has to be an
3 exception and it has to be subject to the approval of
4 Federal Energy Regulatory Commission, absent such
5 exceptions, yes.

6 Q. Did I understand you to state to Chairwoman
7 Showalter that an owner's equity in a secured
8 creditor's capital bore the same risk?

9 A. I'm not sure that's exactly what I said.
10 What I was saying that to the extent that the owner's
11 able to either put in equity into a pipeline or they
12 lend it money, that money is at risk. And if the
13 pipeline fails, they'll lose the money in either
14 case.

15 Q. Well, let's explore that. Let me give you
16 a hypothetical. Let's say that there's some owners
17 that anticipate some large unsecured judgments to be
18 entered against their facility as a result of a
19 tragedy. And let's say they take their money out and
20 then loan -- take their equity out and then loan
21 money back as secured creditors. And let's say, in
22 my hypothetical, that the judgments are entered and
23 they go into bankruptcy. Now, in bankruptcy -- and
24 I'll ask you to assume that all of bankruptcy law
25 boils down to secured creditors win and end up with

00984

1 the assets. Is the owner's equity in bankruptcy --
2 where is that in line in comparison with the secured
3 debt?

4 A. The owner's equity is the last in line.

5 Q. So if there is bankruptcy and there is only
6 the Olympic's owners who have secured credit at that
7 time, and let's say that their secured debt happens
8 to be in the same proportion as their ownership
9 interest, roughly, then who is going to end up with
10 this line after bankruptcy, in your judgment?

11 A. I really don't know. I would -- I'm not a
12 lawyer and I'm certainly not a bankruptcy law expert,
13 but it seems to me that if, following your
14 hypothetical, if the owners had switched their equity
15 for debt just before or pending some judgment like
16 that, that there would be a number of suits
17 suggesting that wasn't proper.

18 Q. The point that I'm raising is does a
19 secured creditor, does an owner that puts himself in
20 a position of being a secured creditor and securing
21 the underlying asset, is that money really at risk if
22 it goes into bankruptcy? Is that money at risk at
23 all?

24 A. The fact that you have long-term debt with
25 a company that's supposedly secured by something, the

00985

1 money isn't there, you don't get any money back.
2 That's just a question of what order you get paid in,
3 and if -- so --

4 Q. Okay. Hypothetical. Hundred million
5 dollars in secured debt, hundred million dollar
6 asset, a single secured creditor. Isn't that secured
7 creditor going to end up with that asset?

8 A. Absent any -- yes, in a purely hypothetical
9 situation.

10 MR. BRENA: May I have a minute off the
11 record, please?

12 (Recess taken.)

13 MR. BRENA: May I go back on the record?

14 JUDGE WALLIS: Please continue, Mr. Brena.

15 Q. In my hypothetical, I was comparing the
16 risk of secured debt with owner's equity. Does
17 unsecured debt also -- is that also repaid before the
18 owner's equity is realized?

19 A. Yes.

20 MR. BRENA: I'm sorry, if I can go off the
21 record for a minute.

22 JUDGE WALLIS: Technically, I don't think
23 we need to go off the record if you're just taking a
24 moment to --

25 MR. BRENA: Thank you.

00986

1 JUDGE WALLIS: -- evaluate your notes.

2 MR. BRENA: I have no further questions.

3 Thank you.

4 JUDGE WALLIS: Mr. Finklea.

5 MR. FINKLEA: I did have just a couple of
6 questions that were sparked by the colloquy with the
7 Chairwoman.

8

9 C R O S S - E X A M I N A T I O N

10 BY MR. FINKLEA:

11 Q. Mr. Schink, I am Ed Finklea, representing
12 Tosco. I see from your resume that you have some
13 familiarity with natural gas pipelines, as well as
14 oil; is that correct?

15 A. That's correct.

16 Q. Are you familiar with the FERC policy of
17 straight fixed variable rate design on interstate
18 natural gas pipelines?

19 A. Yes.

20 Q. And am I correct that under a straight
21 fixed variable rate design, shippers on interstate
22 pipelines pay most of the fixed costs of an
23 interstate pipeline through what are called demand
24 charges, as opposed to volumetric charges?

25 A. Yes, and gas pipelines are run differently

00987

1 than oil. In gas pipelines, shippers can actually
2 reserve space, and the payment for reserving that
3 space on a pipeline is called a demand charge. In
4 oil pipelines, this can't be done, and it's basically
5 if there's more demand than supply, you have to
6 ration the supply among the demanders.

7 Q. In the case of natural gas pipelines, when
8 a pipeline does have its customers under long-term
9 contracts and has a straight fixed variable rate
10 design, isn't, from an economic standpoint, the
11 result very similar to a throughput and deficiency
12 agreement on an oil pipeline, in that the pipeline
13 has been guaranteed a stream of revenue based on
14 those demand charges over the life of the contract?

15 A. In a sense that they both provide a
16 guaranteed revenue stream, yes.

17 Q. And in your experience with the natural gas
18 pipeline industry, are natural gas pipelines financed
19 a hundred percent with debt?

20 A. Generally not, but then they're generally
21 stand-alone companies, as opposed to the wholly-owned
22 by major oil companies. In fact, I think they're
23 almost all stand-alone companies.

24 MR. FINKLEA: I have nothing further.

25 JUDGE WALLIS: Mr. Trotter.

00988

1 C R O S S - E X A M I N A T I O N

2 BY MR. TROTTER:

3 Q. Mr. Schink, you were asked some questions
4 from the Bench, and you talked about parent companies
5 investing in a pipeline where they will get a return.
6 Do you recall that?

7 A. Yes.

8 Q. And am I correct that that is why they
9 typically invest money in a company for construction
10 to build hard assets that will eventually go in rate
11 base and earn a return?

12 A. They invest because they expect to get a --
13 what they consider to be a fair or reasonable return
14 on the investment, yes.

15 Q. And the investment is what is put in the
16 ground to provide service to the public; correct?

17 A. That's correct.

18 MR. TROTTER: Thank you. That's all I
19 have.

20 JUDGE WALLIS: Is there anything further of
21 the witness?

22 MR. MARSHALL: Yes, I wanted to do one
23 follow-up on one of Mr. Brena's hypotheticals.

24

25 R E D I R E C T E X A M I N A T I O N

00989

1 BY MR. MARSHALL:

2 Q. If you assume hypotheticals where there are
3 some debt holders that have security that are
4 subordinate to other debt holders, obviously the
5 people who come second would come second. In this
6 case, assume that there are third party loans
7 outstanding and that loans from any kind of owner are
8 subject to coming second from that, does that place
9 -- under that hypothetical, would that place that
10 loan capital at significant risk in the event of a
11 bankruptcy?

12 A. Yes, it would put it behind the secured
13 debt of everyone else, and in front of -- just in
14 front of unsecured debt.

15 MR. MARSHALL: Okay. I don't have anything
16 further. Thank you.

17 MR. BRENA: I have one question with regard
18 to that.

19

20 R E C R O S S - E X A M I N A T I O N

21 BY MR. BRENA:

22 Q. In this case, do you understand that Mr.
23 Fox, in his supplemental rebuttal, has proposed that
24 the proceeds from the sale of the Sea-Tac terminal be
25 used to pay off that superior debt?

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1 MR. MARSHALL: Well, object to the
2 hypothetical or the assumption. There's both Chase
3 and Prudential, so Mr. Brena has forgotten one of the
4 loans.

5 MR. BRENA: I will rephrase my question.

6 MR. MARSHALL: A significant loan.

7 JUDGE WALLIS: Mr. Brena.

8 Q. Do you understand that Mr. Fox has proposed
9 that, from the sale of the Sea-Tac terminal, that the
10 Prudential note will be paid off?

11 A. I'm -- I've read his testimony. I'm aware
12 that's what he said in it, yes.

13 MR. BRENA: Thank you.

14 CHAIRWOMAN SHOWALTER: I want to follow up
15 on the hypotheticals, too.

16

17 E X A M I N A T I O N

18 BY CHAIRWOMAN SHOWALTER:

19 Q. I guess assume Mr. Brena's original
20 hypothetical, but let's just assume that the owners
21 never did put in much equity, that is, it's a typical
22 -- rather than switch at the last minute, which might
23 be legally suspect, they just operated under these
24 T&D agreements.

25 If you have that situation, and then the

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1 company, for whatever reason, needs to spend a lot of
2 money -- may have been past mismanagement, may have
3 been some kind of disaster, but in any event, they
4 need to spend a lot of money to get the pipeline up
5 and running again. So at a certain point, isn't it
6 the case that the choice is, under that structure,
7 either -- either the rates need to be raised very
8 high in order to pay all that money -- that is, you
9 put the risk of all those expenditures onto the
10 customers -- or bankruptcy?

11 In that it's really the owner who,
12 depending on the rate, will make that choice, because
13 the owner doesn't have equity; the owner has -- the
14 owner/shipper has a loan outstanding, which may be
15 second to some other people's loans. So instead of
16 the risk being assigned say between, you know, the
17 ratepayers and the equity owners; it's the ratepayers
18 versus a decision, really, of the owners and where
19 they stand, either as a debtor -- I mean, a
20 creditor --

21 A. Right.

22 Q. -- versus a shipper. Then they'll make
23 some kind of judgment.

24 A. Well --

25 Q. Have I got -- is that really -- is that the

00992

1 situation we're in?

2 A. No, I think the situation -- well, sort of.
3 Let me try to -- the situation that's occurred, or my
4 interpretation of it, is that there have been
5 increased costs, not due -- you know, not for the
6 Whatcom Creek, but for all the safety and upgrades
7 and other things that were done to the rest of the
8 system.

9 And in general, BP came in and, in essence,
10 just determined, as Mr. Batch has said, to run it
11 according to their standards. It means they're going
12 to basically invest -- put money into upgrading the
13 system, make sure it's safe, and putting personnel in
14 place and procedures in place, which increases the
15 operating costs of the company and also involves an
16 infusion of capital for investment.

17 As a result of this change, the costs are
18 higher and they would need a revenue increase to do
19 it. This has been combined with a drop in revenue
20 because of the sharp drop in throughput. The result
21 has taken a company that was in reasonable financial
22 -- reasonably healthy financial shape, not great
23 financial shape, but at least healthy at the end of
24 1998, to one that's really financially in trouble.

25 And what is necessary, I think, from the

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1 owner's perspective, is to have some assurance that
2 the revenues necessary to, over time, you know,
3 generate a reasonable return on what they put in and
4 then to repay the loans and to actually generate
5 ultimately some return on what's put in now will be
6 forthcoming. And I think the company really wants
7 that -- or is looking for some assurance that that's
8 there.

9 Now, it's -- one of the problems with the
10 new era of mega companies is that Mr. Batch and Mr.
11 Fox, while they're relatively senior, I think, in the
12 U.S. company, ultimately have to get approval for all
13 this from the board in London. And the BP board is
14 looking at moving money to where the return is. And
15 I think for them to be able to get the funds -- and I
16 think Mr. Batch has said he wants to get the funds,
17 he wants to make the investment -- he has to be able
18 to go back to the board with some assurance or some
19 likelihood that, in fact, if the money's put in,
20 that, in fact, there will ultimately be a return and
21 recovery of that money.

22 Q. Well, and your answer got to the actual
23 facts of this case. And one reason I want to stick a
24 little bit on the hypothetical side is that, when
25 looking at the structure of a company or how sound it

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1 is, I don't know whether it is a good idea to look at
2 who is actually in charge. This particular company,
3 Olympic Pipe Line, has had different operators and
4 different owners over different periods of time, and
5 some could be dedicated to safety, some might be more
6 dedicated to returning dividends, some could be poor
7 managers.

8 Shouldn't we be -- when we're making
9 assumptions on which to base a sound or reasonable
10 rate increase, whether it's interim or general,
11 shouldn't we be bearing in mind a generally sound
12 structure? That's what we do when we have a
13 hypothetical capital structure. And it seems like,
14 in part, we do that because we're trying to assume a
15 structure that has the best balance of incentives and
16 risks and rewards --

17 A. Okay.

18 Q. -- to have a well-managed company.

19 A. Right.

20 Q. But we don't -- when we're just talking
21 about structure, we don't know in the particular if
22 it's going to be, you know, sound managers or not.
23 You want to set it up so basically reward follows
24 risks --

25 A. Right.

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1 Q. -- and there are the appropriate incentives
2 in place to operate the pipeline in the public
3 interest.

4 A. Right. Well, in terms of rate structure, I
5 think, in the context of the general rate case, there
6 will -- I mean, the Commissioners will have to
7 determine -- I mean, given that we have a hundred
8 percent debt structure in the actual company and the
9 Federal Energy Regulatory Commission faces this with
10 a number of companies, what they do in that instance
11 is first look to the capital structure of the owners
12 and form a weighted average of that and then
13 determine what a weighted average of the capital
14 structures of the owners, based on their ownership
15 shares, or alternative -- and if they feel that
16 that's inappropriate for whatever reason, they will
17 then look to the capital structures of the five
18 stand-alone oil pipelines, five master limited
19 partnership oil pipeline companies in the U.S. now,
20 and they have a range of capitalization, I think
21 running from 40 percent to a little over around 60
22 percent debt, and they may position the company in
23 that, they may -- they haven't, in cases when they
24 felt that the pipeline was risky, moved it beyond
25 that, but they in essence determine a hypothetical

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1 capital structure that they deem appropriate to the
2 risk, business risk faced by the company.

3 Now, I mean, certainly this Commission
4 doesn't have to follow the FERC in that regard,
5 but it seems to me that the only way you can sort of
6 bring over conventional rate of return regulation and
7 apply it to Olympic is to somehow or other determine
8 a hypothetical capital structure that's appropriate
9 and apply it. I don't think you have any other way
10 of dealing with it.

11 We have recommended one, which is that --
12 the parents, staff, and major oil company intervenors
13 will probably suggest something else, but I think
14 these are all matters for the rate case. I think
15 that -- I think the company of Olympic has put in, I
16 think, a thick volume of testimony attempting to
17 justify their rate request. It's -- it will
18 certainly be challenged, questioned, what have you,
19 but these are all issues for the rate case. It's not
20 a request that's not based on a lot of thought, a lot
21 of analysis.

22 Q. And I don't want to -- don't want to
23 litigate the rate case here, but I am somewhat
24 confused, I think, as to how much of these issues
25 are, in fact, relevant to the interim request. And

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1 we have to have at least some discussion of it in
2 order to entertain the arguments about what's
3 relevant on the interim request, which we'll then
4 decide.

5 A. Right, right.

6 CHAIRWOMAN SHOWALTER: Thank you.

7 JUDGE WALLIS: Is there anything further?

8 MR. MARSHALL: Yes, I do have something
9 further.

10

11 R E D I R E C T E X A M I N A T I O N

12 BY MR. MARSHALL:

13 Q. Some of these hypotheticals have assumed
14 that there has been no equity input. Subject to
15 check, do you understand that BP bought 25 percent of
16 the equity of Olympic following the Whatcom Creek
17 accident in September of 2000 from GATX?

18 A. Yes, I'm aware of that.

19 Q. Is there any reason that you know of that
20 others, including the intervenors here, could not
21 have bought any equity interest in Olympic at that
22 time, in September of 2000?

23 A. No, it's -- GATX made it widely known that
24 they wanted to sell their interest, and I'm sure
25 would have accepted offers from anyone who wanted to

00998

1 make one.

2 Q. And subject to check, do you understand
3 that the GATX shares, the 25 percent of the company,
4 was sold for approximately \$7 million in September of
5 2000?

6 MR. BRENA: Objection at this point. I
7 fail to see how this responds to any question that
8 this witness has been asked.

9 JUDGE WALLIS: Mr. Marshall.

10 MR. MARSHALL: It's designed to show what
11 the equity amounts were and what the equity at that
12 time of the company could reasonably have been
13 without -- and this goes to the various hypotheticals
14 that Mr. Brena has. I'm going to ask a couple of
15 questions about the other notes that were outstanding
16 as of that time, too, and then tie it up.

17 JUDGE WALLIS: Is this a matter as to which
18 the witness has personal knowledge? In your
19 question, you offered the information regarding the
20 price for the -- or reputed price for the sale of the
21 interest in the company. Mr. Schink, is this a
22 matter as to which you do have personal knowledge?

23 THE WITNESS: I worked for BP as -- when
24 they were in fact -- supported them when they were,
25 in fact, in the process of buying GATX.

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1 JUDGE WALLIS: Very well. You may
2 continue.

3 Q. So you have personal knowledge of that
4 transaction?

5 A. Yes, I do.

6 Q. You actually worked on that deal?

7 A. Yes.

8 Q. Okay. And at that time, I'm asking you to
9 assume that, on June 6th of the year 2000, three
10 months prior, that Chase made a loan of \$30 million,
11 and ask you to assume that on June 13th of that same
12 year, three months prior to the purchase, Equilon
13 made a loan of \$43 million. Would all of that equity
14 amount purchased from GATX by BP have been subject to
15 those loans and all others that preceded that, for
16 that matter?

17 A. Yes, they would be taking a responsibility
18 for the repayment of those loans.

19 Q. Okay. And was there any interest, when you
20 were working on that purchase of GATX on behalf of
21 BP, expressed by any of the other major oil
22 companies, including owners of the two refineries
23 here, Tosco and Tesoro, that are intervenors in this
24 matter?

25 A. My understanding is that essentially BP was

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1 the only interested buyer at that time.

2 MR. MARSHALL: Okay. No further questions.

3

4 R E C R O S S - E X A M I N A T I O N

5 BY MR. BRENA:

6 Q. Does BP own an interest in Olympic Pipe
7 Line?

8 A. BP/ARCO does, I think is the -- I don't
9 know the exact corporate structure. BP ultimately is
10 the ultimate parent.

11 Q. Who is the owner of Olympic Pipe Line?

12 A. I thought it was BP/ARCO, or was one of the
13 owners, and the other one was Equilon.

14 Q. Is that the name, BP/ARCO, or Atlantic
15 Richfield Company?

16 A. I can't say that.

17 Q. Whatever was paid for GATX's interest, was
18 that an equity contribution into Olympic?

19 A. No, it was -- but, in essence, it was an
20 investment by BP to acquire an equity interest.

21 Q. Did the equity of GATX change -- I mean,
22 did the total equity investment in Olympic Pipe Line
23 change a penny as a result of that entire
24 transaction?

25 A. No, it did not.

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1 MR. BRENA: Thank you.

2

3 E X A M I N A T I O N

4 BY CHAIRWOMAN SHOWALTER:

5 Q. I'm confused by your answer. I thought you
6 first said the transaction was not an equity
7 interest, and then I thought I heard you say it was
8 either the same as or something like an equity
9 interest.

10 Earlier, I had thought I heard that BP
11 bought 25 percent, I thought, of an equity interest.
12 So can you just -- you don't need to clarify your
13 answers. I just want to know, did that transaction
14 equate to an equity interest by BP in Olympic Pipe
15 Line?

16 A. It --

17 Q. Or ARCO, whichever one it is?

18 A. It expanded their percentage ownership in
19 the company, but it wasn't an infusion of capital
20 into the pipeline itself. The money that was paid to
21 GATX, GATX kept, I guess.

22 What we were talking about earlier are
23 infusions of capital from BP into Olympic per se.
24 The GATX transaction is essentially BP paying GATX
25 for its 25 percent interest in the pipeline. The

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1 money didn't go to the pipeline; it went to GATX.

2 Q. But as a result of that transaction, did BP
3 acquire a greater equity in the company or just
4 ownership of the company?

5 A. It acquired a greater ownership interest --
6 well, it has -- usually the ownership interests are
7 described as equity interests. I think we've been
8 using equity in two different ways here. The company
9 -- the ownership shares, if you will, are considered
10 equity interests in the company, but when we're
11 talking about capital structure of Olympic, we're
12 talking about the money put into the company, whether
13 it be loans or an equity infusion from the owners
14 into Olympic per se, which is a different kind of use
15 of the word equity.

16 Q. Right, and I think that -- isn't that
17 because normally owners have placed equity into the
18 company and so we tend to think of the two as the
19 same, but am I right that, in this case, the owner,
20 whoever that is, and I'm a little unclear who the
21 legal owner is, but whoever it is could be a legal
22 owner without having any or very much equity in the
23 company, as if I bought a car, for example --

24 A. Okay.

25 Q. -- but didn't pay any money down. I would

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1 be the owner, but I would not have equity into the
2 car.

3 A. Well, you can think of it this way. What
4 BP did when it bought GATX is a lot like buying
5 shares. But this ownership is not like stocks so
6 much as in fact, in a sense, buying partnership
7 shares. And partners -- I mean, this isn't a legal
8 structure, mind you, but partners typically take
9 dividends out and, when the company needs money, put
10 investments in.

11 Now, it can be done in a form of just an
12 equity infusion, it can be done -- into the company,
13 it can be done in terms of loans. It's typical, in
14 the oil pipeline industry, for pipelines that are
15 owned by major oil companies, for the infusion of
16 money into the pipeline company to be made in the
17 form of loans, as opposed to equity infusions.

18 CHAIRWOMAN SHOWALTER: Thank you.

19 JUDGE WALLIS: Is there anything further of
20 the witness?

21 MR. MARSHALL: Just one thing, to make sure
22 that we're all on the same page on the clarification
23 here.

24

25

R E D I R E C T E X A M I N A T I O N

01004

1 BY MR. MARSHALL:

2 Q. The amounts that BP paid in September of
3 2000, those amounts were placed at additional risk in
4 terms of their ever being able to get that amount
5 that they paid for those shares back out of the
6 company. And that comes at the end of the line,
7 insofar as creditors and everything else would go; is
8 that true?

9 A. That's correct. The returns that the
10 companies get for buying the shares in the company
11 are in the form of dividends, which, as Mr. Fox said,
12 I think haven't been paid since 1997, and he doesn't
13 expect them to be paid in the foreseeable future.

14

15 R E C R O S S - E X A M I N A T I O N

16 BY MR. BRENA:

17 Q. At the risk of -- did Atlantic Richfield
18 Company acquire control of Olympic with that
19 purchase?

20 A. The -- well, whoever the owner -- I'm
21 sorry, I mean --

22 Q. Please assume, for the purposes of my
23 questions, that Atlantic Richfield Company is the
24 proper name of the proper owner for Olympic Pipe
25 Line.

01005

1 A. I will -- I'm not sure that's correct, but
2 I will go along with your assumption, yes. They did
3 acquire control, yes.

4 Q. And since they've acquired control, do you
5 know how much BP Pipelines has received in total fees
6 as a result of the change of operators?

7 A. No, I do not. Fox has discussed this.

8 MR. MARSHALL: Wait, I have an objection,
9 because the questions assume BP Pipelines --

10 MR. BRENA: I withdraw my question.

11 MR. MARSHALL: -- had been given a
12 management contract after the control changed, when,
13 in fact, BP Pipelines was awarded the management
14 contract before that transaction occurred, so --

15 MR. BRENA: I withdraw the question.

16 MR. MARSHALL: Okay. Fair enough.

17 JUDGE WALLIS: Thank you.

18 MR. BRENA: I'm done.

19 JUDGE WALLIS: Mr. Schink, I believe we're
20 done with you for today. I want to thank you for
21 appearing before us today. We will take a 15-minute
22 recess at this time, resuming shortly after 11:00,
23 and we will take up then with the conclusion of the
24 testimony of Mr. Elgin.

25 (Recess taken.)

01006

1 JUDGE WALLIS: Let's be back on the record
2 following our morning recess. Mr. Elgin has resumed
3 the stand. Mr. Elgin, I will merely remind you that
4 you've previously been sworn. We will take up with
5 questioning by Mr. Brena, as Mr. Finklea has
6 indicated that he has concluded his examination.

7 Mr. Brena

8

9 C R O S S - E X A M I N A T I O N

10 BY MR. BRENA:

11 Q. Good morning, Mr. Elgin.

12 A. Good morning.

13 Q. I wanted to ask you a few questions about
14 Bayview, if I may. Would you agree that if the
15 Bayview terminal had never been placed in service, so
16 that it was used and useful for the transportation of
17 petroleum products, that it should not have been
18 included in Olympic's rate base?

19 A. I would agree that there would probably be
20 no basis for including it in rate base; that's
21 correct.

22 Q. And if that were the case, then it should
23 not have been depreciated?

24 MR. MARSHALL: Well, I object to the
25 hypothetical, because it assumes a fact not in

01007

1 evidence. I mean, it was. I mean, this is asking
2 him to make assumptions, well, if it were dark
3 outside, what would you be doing, and I think that
4 those assumptions are incorrect.

5 CHAIRWOMAN SHOWALTER: It is dark outside.

6 MR. MARSHALL: I stand corrected.

7 JUDGE WALLIS: I do think that -- I do
8 think that the subject --

9 MR. MARSHALL: It just seems like it.

10 JUDGE WALLIS: Yes, I do think that the
11 subject is more than an abstract hypothetical. It's
12 based on the witness' testimony and his responses on
13 examination. He did testify as to the terminal and
14 the nature of his decision, and I think that these
15 questions are appropriate in light of that.

16 MR. BRENA: Thank you, Your Honor.

17 Q. Do you have my question in mind?

18 A. Yes. If it was not a plant in service,
19 there would be no basis for depreciation, as I
20 understand your question.

21 Q. Nor the collection of any rate with regard
22 to that facility; is that fair?

23 A. That's fair, and that was the entire
24 premise of the Staff analysis, to adjust. Olympic's
25 rates previously were under the Staff's assumption

01008

1 that that facility would be used and useful and put
2 in rate base; that's correct.

3 Q. Can I direct you to Exhibit Number 25? Do
4 you have the exhibits?

5 A. They're in my book. Right here. No, in
6 that pile right there.

7 JUDGE WALLIS: Let's be off the record,
8 please.

9 (Recess taken.)

10 JUDGE WALLIS: Let's be back on the record.
11 The witness now has the document; is that correct,
12 Mr. Elgin?

13 THE WITNESS: Yes.

14 JUDGE WALLIS: Thank you.

15 Q. If I could direct your attention to page
16 three of Exhibit Number 25, the bottom two
17 paragraphs, titled Bayview, and specifically the
18 language, Bayview is totally tied in and awaiting
19 product availability and the scheduling program. Do
20 you see that language?

21 A. Yes.

22 Q. And if I could direct your attention to
23 page one of that exhibit, which that was prepared
24 sometime after the first quarter of 1999, do you see
25 that at the top?

01009

1 A. That's what it purports to say, yes.

2 Q. Okay. Now, would you agree that if a
3 facility has only been tested, but has never been
4 actually used for the transportation of petroleum
5 products, that it would not properly be considered in
6 service?

7 A. I'm a little -- I'm a little uncomfortable
8 with answering that question, just because of my
9 knowledge of this facility and what it -- the
10 operational characteristics and how it is to be used,
11 and so it's getting beyond my knowledge.

12 Q. Okay. Please allow me to restate my
13 question. I'm not now asking a question on Bayview;
14 I am asking that if -- when a facility would be
15 considered placed in service. If it were only used
16 for testing and were never used, in fact, for the
17 transportation of petroleum products, would you
18 consider that plant facility to be used and useful
19 for a shipper or not?

20 A. Under that hypothetical, I would say that
21 that facility, if it's not providing service to
22 shippers, then it would raise serious questions about
23 whether or not it would be considered used and useful
24 property.

25 Q. Thank you. I have a few questions. Are

01010

1 you aware of any case in which this Commission has
2 given emergency relief when the underlying financial
3 position of the company was improving?

4 A. No, my review of the prior Commission
5 treatments for interim rate relief in a general rate
6 case was that the company's financial condition was
7 continuing -- was declining and the prospects were
8 continuing to decline.

9 Q. Would you agree that, in the past six
10 months, that Olympic's financial position has
11 improved?

12 A. The company, in the last six months, has,
13 as I've testified, improved its utilization of the
14 facility, and our analysis attempted to capture that
15 improving revenue picture of Olympic.

16 Q. Should this Commission be concerned with
17 the message that's being sent or the potential
18 precedential value of granting emergency relief to a
19 company with an improving financial condition?

20 A. Well, this is precisely what the Staff
21 recommendation boils down to, is the explicit
22 acknowledgement of that improving financial
23 condition. And I might add that the critical factor
24 that Staff is proposing in its recommendation is for
25 the Commission to consider the facilities that are

01011

1 there in place serving the public, and attempting to
2 provide an interim rate solution on those facilities
3 that are devoted to public service and serving the
4 shippers on Olympic's pipeline system.

5 So one other point I did want to add is
6 that our analysis of the interim standards clearly
7 gave us a problem, because the traditional kind of
8 PNB analysis assumed that the utility had
9 publicly-traded securities and the traditional kind
10 of PNB analysis could be accomplished. So we were
11 hampered by our inability to apply that type of
12 analysis with respect to the outstanding securities
13 and the restrictions on issuing new debt.

14 So I think that the Commission can consider
15 improving financial conditions as a utility, if you
16 will, turns around, but we have carefully put some
17 protections into the circumstances in this case and
18 how it should be applied, and the critical principle
19 is look at the plant in service and what are the
20 facilities there serving the public, and looking how
21 the company has financed those and then provide some
22 reasonable earnings protection so the company can
23 finance those facilities.

24 Q. Please allow me to restate and perhaps
25 better focus my question. My question is not

01012

1 intended to go to question Staff's recommendation.
2 My question was, as a general proposition, should
3 this Commission -- is it a legitimate concern for
4 this Commission to be concerned about the signal they
5 send to the industry or the precedent they establish
6 if they start granting emergency relief to a company
7 whose financial prospects are improving?

8 A. Yes. As I understand your question, the
9 Commission should consider that, and that's a part of
10 the Staff recommendation, that, in its evaluation of
11 what is in the public interest, that factor should be
12 considered.

13 Q. Are you aware of any case in which this
14 Commission has granted emergency relief for a company
15 when the relief requested would have no substantial
16 impact on a company's ability to attract market -- to
17 attract debt or capital in the commercial
18 marketplace?

19 MR. MARSHALL: This is all legal argument,
20 I think, for closing. I would object. I don't think
21 this is going to shed any light on anything. And he
22 can't look at the cases and make the argument in
23 closing.

24 JUDGE WALLIS: It strikes me that the
25 question is not argument, but asks the witness'

01013

1 opinion, and I think it should be allowed.

2 Q. Do you have my question in mind or would
3 you like for me to restate it? It was rather
4 lengthy.

5 A. Yes, would you please restate it?

6 Q. I would be happy to. Are you aware of a
7 case in which this Commission has given emergency
8 relief when the relief that was sought and granted
9 would not help the company attract capital in the
10 commercial marketplace?

11 A. No. As I previously testified, that was
12 one of the problems we had with this case, is that
13 these securities are not publicly traded. Olympic is
14 precluded by the Prudential note from going to
15 external sources, and that the only real source of
16 additional capital for this company was the revolving
17 line of credit that we had previous testimony and
18 discussions about the nature of that and how Mr. Fox
19 would access those additional funds under that
20 revolving line of credit.

21 Q. Is that -- should the Commission be
22 concerned with the message sent to the industry or
23 the precedential value of granting emergency relief
24 when it doesn't help the company attract capital in
25 the commercial marketplace?

01014

1 A. Yes, the Commission needs to consider that
2 factor and the circumstances in this case and
3 evaluate the recommendations and look at how we
4 attempted to craft a solution to this particular
5 circumstance and should consider that.

6 Q. Are you aware of any case in which this
7 Commission has given emergency relief based on
8 financial books and records which have not been
9 subject to audit?

10 A. Well, I don't know of any, and I think what
11 you mean in your question, subject to audit, is
12 whether or not the company is able to issue a
13 financial statement that has an unqualified opinion
14 attached to it?

15 Q. Yes, sir.

16 A. So with that clarification of your
17 question, I would answer, generally, no, that has
18 been the traditional kinds of -- publicly-traded
19 companies have audited statements that are
20 unqualified and that the financial community that is
21 making the loans have those statements to form a
22 basis as to assess the credit worthiness of the loan
23 applicant.

24 Q. Would you agree that Olympic's
25 unwillingness or inability to get an unqualified

01015

1 audit opinion raises the legitimate issue of whether
2 the financial books and records it's advancing are
3 accurate and proper?

4 A. There is concern about Olympic's books and
5 records and its ability to get an unqualified
6 opinion.

7 Q. Is that a legitimate concern that this
8 Commission should consider with regard to the message
9 it's sending to the industry or the precedential
10 value of this case?

11 A. Again, because these securities are not
12 publicly traded, in the circumstance it were, I would
13 say that that would have significant precedential
14 value. In this circumstance, I'm not as concerned
15 about that.

16 Q. Okay. Is it a legitimate concern for the
17 Commission to have?

18 A. Again, the Commission should evaluate that
19 and look at the books and records and understand the
20 circumstances surrounding this company and should
21 evaluate the weight it gives to Olympic's inability
22 to get a qualified -- an unqualified financial
23 statement.

24 Q. Are you aware of any case in which this
25 Commission has granted emergency relief when the

01016

1 owners have no equity?

2 A. No, there have been no cases. Generally,
3 what has happened in those circumstances is that the
4 continuing losses have been causing the company's
5 equity to erode, and the purpose of interim rate
6 relief is to turn that circumstance around.

7 Q. Is that a legitimate concern for this
8 Commission to consider?

9 A. Yes, it is, and my recommendation took that
10 into account as to how and the reason why I chose to
11 provide interest expense on those facilities that are
12 devoted to public service.

13 Q. And again, my questions are not intended,
14 by implication or otherwise, to question the
15 recommendation; only to probe what is a legitimate
16 issue for this Commission to consider in the messages
17 it sends the industry or the precedential value of
18 the case.

19 MR. TROTTER: Your Honor, I'll object to
20 Counsel testifying. He can ask his questions, but
21 Mr. Elgin should be permitted to answer.

22 MR. BRENA: I stand properly corrected.

23 JUDGE WALLIS: Mr. Brena.

24 Q. Are you aware of any case in which the
25 Commission has granted emergency relief when the

01017

1 company has a hundred percent payout dividend policy?

2 MR. MARSHALL: Well, you know, I'm going to
3 have to object at this time. The last time a
4 dividend was made was 1997. There were cases that
5 occurred after that time when these intervenors could
6 have intervened about dividends. There's no evidence
7 about a hundred percent payout policy or not. I
8 think that misstates the evidence. I mean, this is
9 entirely improper and assumes facts not in evidence
10 and is argumentative.

11 MR. BRENA: My question had no relationship
12 whatsoever to Olympic's particular facts. I was
13 probing this witness' knowledge and familiarity with
14 prior Commission precedent.

15 MR. MARSHALL: Well, then, I find that
16 irrelevant and not connected to the facts in this
17 case and will make that further objection. It seems
18 to be misleading, as well, because I certainly got
19 the implication that that's what you were driving at.
20 Maybe that's --

21 MR. BRENA: Well, in fact, we put into
22 evidence exhibits in which owners of Olympic Pipe
23 Line have stated that their dividend policy was a
24 hundred percent payout, but we will argue that in
25 closing.

01018

1 I am just -- my question to this witness is
2 is he aware of any case in which emergency relief has
3 been granted in which the owners had a hundred
4 percent dividend policy.

5 JUDGE WALLIS: It strikes me that Mr.
6 Brena's line of questioning does identify areas of
7 potential concern and asks the witness' knowledge as
8 to prior occurrence, and asks for the witness' view
9 on whether that's a matter for the Commission to
10 consider the witness' responding to those questions.
11 It might -- unless you're near the end of that list,
12 they are repetitive in structure, and responses seem
13 to be similar, so you might consider, as you proceed,
14 lumping them.

15 MR. BRENA: I will try. I'm somewhat
16 concerned with having different answers to different
17 factors.

18 JUDGE WALLIS: Very well. Please proceed.

19 Q. Do you have my question in mind, Mr. Elgin?

20 A. Yes.

21 Q. Are you aware of any -- I guess you said
22 yes. I'm sorry.

23 A. No, generally speaking, most investor-owned
24 utilities do not have a policy of paying out a
25 hundred percent of dividends. Quite frankly,

01019

1 utilities traditionally have high-dividend payout
2 policies. That has been the tradition. There have
3 recently been some exceptions to that rule. The
4 other factor, though, to consider is that from time
5 to time the utilities may, because of earnings,
6 suffer and be forced to pay out -- to keep stable
7 dividends, pay out more than a hundred percent. So
8 the question is almost confusing, what is and what
9 ought in regards to policy.

10 Generally, dividend policy would not be a
11 hundred percent payout ratio. That would be an
12 imprudent thing to do. But at times, boards of
13 directors may be forced to pay out a hundred percent
14 of earnings and dividends and have a policy that
15 would pay out a hundred percent or even 120 percent
16 or 150 percent to keep a stable dividend, but,
17 generally speaking, no, there have not been instances
18 in prior cases where utilities have had a stated
19 policy that we will pay out all earnings in
20 dividends, as I understand your question, Mr. Brena.

21 Q. Yes, you did understand my question. Is
22 that a legitimate issue that the Commission should
23 consider?

24 A. Yes.

25 Q. Are you aware of any case in which this

01020

1 Commission has granted emergency relief when the
2 company did not have a financial plan supporting that
3 relief?

4 A. I generally believe that, for most of the
5 utility cases, the energy cases that I'm aware of,
6 there was a financial plan, and that included, as
7 part of their request for interim, as I testified,
8 included the plan to balance the financings to -- in
9 other words, how much debt, how much preferred
10 equity, and how much common equity.

11 And generally speaking, the history is that
12 the utilities, because of earnings and because of a
13 need for interim, they could not issue additional
14 equity because of several factors, and primarily was
15 -- excuse me, the dilutive effect of additional --
16 issuing additional equity and the fact that equity
17 would be -- they would issue additional equity below
18 book value.

19 So that's the history in terms of looking
20 at a financial plan, so that, in most circumstances,
21 the only practical solution was to issue additional
22 debt, build up the book equity so that the utility
23 down the road could issue additional equity.

24 Q. Would you agree that Olympic has not
25 advanced a financial plan in this case?

01021

1 A. I have not seen one.

2 Q. Is that a legitimate issue for the
3 Commission to consider?

4 A. Yes.

5 Q. Are you aware of any case in which the
6 Commission has granted emergency relief so that a
7 company could add over 30 percent to its net plant in
8 a single year?

9 A. If I understand your question, is that --
10 is there an interim case where the amount of relief
11 sought equaled the increase in facilities the company
12 planned to ask to add in the future and make --
13 somehow say we need to spend \$20 million, and we need
14 20 million in relief to fund it? There is no such
15 case that I know of in the energy industry. There
16 may -- I'm not as familiar with some of the
17 circumstances in the water industry.

18 Q. What is Olympic's net plant in service?
19 Just roughly. I'm not looking for an exact number.

20 A. Net carrier properties, at the end of 2000,
21 was approximately 97 and a half million, including
22 construction work in progress.

23 Q. And is construction work in progress used
24 or useful?

25 A. No, it's -- that's precisely what it means,

01022

1 it's still -- it's not classified as plant in
2 service.

3 Q. So net plant in service would be how much,
4 roughly?

5 A. The Form 6 identified, I think,
6 approximately 30 million in construction work in
7 progress, so it would be about 67 and a half million
8 of what we'd call plant in service.

9 Q. And the amount -- and your understanding is
10 is that they're requesting emergency relief so they
11 can add \$24 million of plant in service over the next
12 year? Is that part of what -- your understanding of
13 they're requesting?

14 A. Their request states that they plan to
15 spend, in 2002, an additional \$24 million.

16 Q. Is this a legitimate factor that the
17 Commission should consider?

18 A. Yes, I think -- I think it is, and it's
19 precisely because of the magnitude of the proposed
20 rate increases. A 62 percent increase is substantial
21 and it deserves careful consideration by the
22 Commission.

23 Q. Are you aware of any case in which a
24 company had an obligation to and did not notify the
25 Commission of the debt that it incurred and, through

01023

1 the emergency relief, it was asking for support of
2 that debt?

3 A. No, as I pointed out in my testimony, the
4 traditional kinds of things that we have seen in the
5 context of interim rate requests are this
6 intertwining of these processes that the Commission
7 has, and that is the budgets, the financing
8 applications, so that the Commission is notified in
9 terms of what financings the company is doing.

10 And those financings are critical, because
11 there's only three categories of uses of proceeds
12 that the statute provides for, and in my mind, that's
13 an important factor, because when the utility issues
14 long-term securities, there's generally that
15 connection between the money that you're going to
16 issue in terms of a security and facilities to serve
17 the public, so there's that connection, and then
18 ultimately their long-term financial plan and then
19 what rates support those facilities and what is
20 needed in terms of interim rate relief.

21 Q. Would you agree that Olympic has not
22 notified the Commission of much of the debt that it
23 is seeking here to support through emergency relief?

24 A. There -- for none of the ARCO loans -- for
25 all but one of the outstanding -- or I misspoke. All

01024

1 but two, I believe, there have been no security
2 applications filed.

3 Q. Are you aware of any case in which the
4 Commission has granted emergency relief for the
5 purpose of supporting debt incurred for expenses
6 unrelated to its plant in service?

7 A. No, I do not. In fact, that was, as I
8 previously mentioned, that's the fundamental
9 principle of the Staff case, is that there has to be
10 a connection. The Staff recommendation is, in terms
11 of that principle, the connection between the interim
12 relief and the facilities serving the public.

13 Q. Would you agree that Olympic is requesting
14 relief in part to support debt which is unrelated to
15 plant in service?

16 A. That's my concern, yes. And that's the
17 fatal flaw in their proposal, is that there is no
18 connection between the interim rate relief that
19 they're requesting and the interest expense that they
20 have incurred and the amount of debt that they have
21 outstanding and the facilities that are there to
22 serve the public. There is no connection and I can't
23 make one and I can't find any financial information
24 that would enable me to put something together to
25 reconcile those, those factors.

01025

1 Q. And you would agree that that's a
2 legitimate concern that the Commission should
3 consider in terms of the messages it sends to the
4 industry and the precedential value of this
5 proceeding?

6 A. Yes, and it's a factor that I considered,
7 as well, in my recommendation.

8 Q. Are you aware of any case in which the
9 Commission has granted emergency relief when there
10 are a great deal of expenses and debt that are
11 affiliated in nature, which the parties or the
12 Commission have had no opportunity to thoroughly
13 review?

14 A. Well, and that's -- yes, and that's
15 precisely why I did what I did. I had to make the
16 assumption that there was that connection between the
17 debt that I could identify that reasonably appeared
18 to be connected to the facilities in service.

19 Q. I think perhaps I misspoke. Let me ask my
20 question again, the way that I intended to. I'm not
21 sure that I asked it correctly. Are you aware of any
22 case in which the Commission's granted emergency
23 relief in which there are a great deal of affiliated
24 transactions in which the parties and the Commission
25 hasn't had adequate time to thoroughly review?

01026

1 A. Well, if there were affiliated transactions
2 that were included in the cost and they weren't
3 reviewed, that would be a concern, yes.

4 Q. And that would be a legitimate concern with
5 regard to -- that this Commission should consider?

6 A. Yes, although I think you and I probably
7 might be using the term affiliate in different
8 senses.

9 Q. Please, please explain.

10 A. I think you're using the term affiliate in
11 the context of an owner or in relationship to a
12 subsidiary, and my understanding of the term
13 affiliate transactions has to do with transactions
14 between subsidiary companies of a common ownership,
15 so I use that term a little bit differently in the
16 sense of how our affiliated interest statutes are
17 constructed and work.

18 Q. I was thinking about the series of
19 affiliated relationships. Are you aware of the
20 series of affiliated relationships between Olympic
21 and BP Pipelines who is not an owner?

22 A. I'm not aware of them, and I understand and
23 I heard the testimony that -- about the different
24 hats that the officers and the employees of the
25 companies wear, and I don't fully understand all

01027

1 those transactions and how they --

2 Q. Are you aware of any case in which this
3 Commission has granted emergency relief for a company
4 that did not meet the PNB test since it was adopted?

5 A. No, and as I testified, the PNB case can't
6 be applied in this circumstance, but I attempted to
7 apply it in the spirit of the test.

8 Q. Should the Commission be concerned with the
9 potential precedential impact of granting emergency
10 relief under a new standard other than the PNB test?
11 Is that a legitimate concern that this Commission
12 should consider?

13 A. Well, yes. And that is precisely what I
14 did, is to provide a recommendation that captures all
15 these factors that should be considered, and for the
16 Commission, as a recommendation, to provide interim
17 relief that is, in my mind, in the public interest.

18 Q. Thank you. I just have a few more
19 questions. Are you aware of any circumstance in
20 which financial ratios have been used to determine
21 emergency relief for a company that has zero equity?

22 A. No, and in fact, in fact, a ratio analysis
23 in this context makes little sense, because of the
24 fact that the company has no equity. Those financial
25 ratios are all established with the premise that

01028

1 there is equity and that the coverages are minimum
2 targets based on the fact that there has to be some
3 protection on the downside, and that is the company's
4 equity investment in the facilities serving the
5 public.

6 Q. Are you aware of any circumstance in which
7 financial ratios have been used to determine the
8 emergency need for a company with unaudited books and
9 records?

10 MR. MARSHALL: This has been asked and
11 answered, Your Honor.

12 MR. TROTTER: I'll join that objection,
13 Your Honor.

14 MR. BRENA: If I may, my question went to
15 whether he was aware of any case in which emergency
16 relief had been granted with unaudited books and
17 records. This question went to whether he's aware of
18 circumstances in which financial ratios have been
19 used to determine an emergency need for a company
20 with unaudited books and records.

21 JUDGE WALLIS: With that clarification--

22 MR. TROTTER: Counsel -- may I ask Counsel
23 if he means financial ratios to mean an equity ratio?
24 Because a financial ratio could be a coverage test or
25 something else, so I don't know.

01029

1 MR. BRENA: I was intending it broadly to
2 include whatever this witness' understanding of
3 financial ratios included.

4 MR. TROTTER: Okay.

5 Q. Do you have the question in mind?

6 A. Yes, I do. For the same reason that
7 Prudential has the issue with the qualified nature or
8 the inability of Olympic to issue an unqualified
9 statement, if you would calculate financial ratios,
10 you have to have financial information. And so if
11 you don't have an unqualified statement and you
12 calculate ratios based on income or equity or book
13 value, and you don't know whether or not those are
14 meaningful figures, the ratios are just as well
15 meaningless. You don't have that connection.

16 MR. BRENA: Thank you. I have nothing
17 further.

18 JUDGE WALLIS: Questions from the Bench?

19

20 E X A M I N A T I O N

21 BY CHAIRWOMAN SHOWALTER:

22 Q. Now, my first question is does your
23 recommendation depend on an adoption or endorsement
24 or acceptance of either the FERC methodology or a
25 different methodology? In other words, in the

01030

1 general rate case, what methodology is appropriate is
2 an issue, and I'm wondering if, in your opinion, it's
3 an issue in this case or, to be more precise, whether
4 your recommendation depends on methodology?

5 A. No, it does not, Your Honor.

6 Q. Okay.

7 A. Chairwoman.

8 Q. Either one's fine.

9 A. Yes, I'm sorry.

10 Q. I always did like -- Commissioner Hemstad
11 once called me Chairwalter. Nice contraction. I
12 know it's a mouthful, so Madam Chair works well off
13 the tongue.

14 Well, my next question is is the issue of
15 this company being a debt only, no equity company, is
16 that -- is the soundness of that an issue in whether
17 we grant interim rate relief or --

18 A. Ultimately, in my recommendation, no. But
19 at the same time, though, I was mindful of that very
20 fact and mindful of the very fact of the testimony
21 you've seen by others of this disconnect between what
22 they have here in the interim and what they're asking
23 for in the general rate case, because there is a
24 total disconnect.

25 And it's a concern that as I get into this

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1 pipeline rate-making, I'm very concerned about, and
2 that is the fact that you have a company that's all
3 debt, or very little equity, but the basis for rates
4 presumes that there's equity. And it enables a
5 company to generate tremendous amounts of cash, and
6 you've also heard, seen testimony about what they
7 call the dividending up of the cash to the parent.
8 And if there's an -- if there is an accident and
9 there is something that you need this financial
10 cushion, what do you do?

11 Q. You've said if there is an accident? I
12 thought you said if there isn't an accident.

13 A. Yes, if there is an accident.

14 Q. Okay.

15 A. So you don't have that financial cushion,
16 and so what should be done? And it seems to me that
17 the testimony of Mr. Hanley, to some extent, was
18 persuasive, is that somebody has to step up.

19 You have a history where this pipeline was
20 -- had very low equity investment and it generated
21 tremendous amounts of cash when everything was going
22 well. The accident happened. Now, all of a sudden,
23 there was no money, there was no equity, and now it
24 has all these expenses to reassure the public that
25 it's a safe pipeline, a new operator that's bringing

01032

1 in new practices and procedures that cost more, and
2 the fact that they want to make safety improvements.
3 So you need to spend all this money, but there's no
4 equity. There's nothing there to support those
5 losses, because they're truly losses.

6 Q. Right, but does your -- I want to stick to
7 the subject of what premises are implicit in your
8 recommendation or in the other parties'
9 recommendation.

10 A. Okay.

11 Q. So do I understand that you are taking as a
12 given, for purposes of your recommendation, that this
13 is a company with no equity?

14 A. That's correct.

15 Q. And does your recommendation assume or not
16 assume that the owners will respond in some way to
17 the rate increase you recommend? And by some way, I
18 mean does it assume that they will put in more money,
19 for example, more equity?

20 A. It assumes that -- the one and a half times
21 coverage that I recommend, it assumes that the
22 facilities that are there serving the public, they
23 can provide debt service, and over time have
24 sufficient revenues as things turn around to
25 eventually build up some equity in this company.

01033

1 Q. All right. But we're just talking about
2 the interim here. And so if we accept your
3 recommendation and authorize a 20 percent increase,
4 in your opinion, is that alone enough to carry this
5 company through the interim in a state of financial
6 condition that at least won't deteriorate?

7 A. It -- first of all, the financial condition
8 is beginning to improve because of the ability of the
9 company to move volumes on its system at 80 percent
10 pressure, 91 percent utilization.

11 What I think my recommendation will do
12 would be enable the company now to take, with these
13 increased revenues, and produce a pro forma income
14 statement and balance sheet sufficient to show that
15 it can provide a way, a light at the end of the
16 tunnel. You can't turn it around overnight, but what
17 I attempted to do was move the company in the
18 direction, provide a light at the end of the tunnel,
19 and that the company would be able to put those
20 financials together and then Mr. Fox would be able
21 to, in his capacity, make the call and get the money
22 to make those improvements between now and the end of
23 the interim, and then we can get on with the rate
24 case and resolve the issues about rate base and rate
25 of return and produce final rates and really move

01034

1 this company forward.

2 Q. I want to digress for a minute to the word
3 improvement. It's a relative term, but it means that
4 a company's doing better than it was before, but a
5 company could be improving from one of almost
6 jeopardy to being sound, or of in bad shape to less
7 than bad shape, or absolutely miserable shape to bad
8 shape.

9 Doesn't the absolute state of a company
10 make a difference in our determination on whether to
11 grant an increase or not? Aren't we -- isn't the
12 goal to get a company on sound financial footing and
13 sound management; not just to go from very, very bad
14 to kind of bad?

15 A. In the context of the interim case, I think
16 what I've recommended here is moving from bad to not
17 so bad, if I can use those kind of characteristics.

18 Q. Okay.

19 A. And we think it's improving. We've
20 incorporate -- and Mr. Colbo can talk to you more
21 about this, in terms of his best shot at what the
22 near-term prospects of Olympic will be because of the
23 turnaround. And that's what we're attempting to do,
24 just to get us like, as I just said, bad to not so
25 bad, and we at least put together a pro forma

01035

1 financial that should say here's a light at the end
2 of the tunnel. We're moving in the right direction.

3 My problem with the company's case is they
4 want 62 percent, they want it now, and they want,
5 because of that, in an interim case, 60 percent
6 change in rates increase, and let's solve it all
7 right now. And I'm very uncomfortable with that and
8 I'm very -- and I'm very uncomfortable because I
9 can't tie it to -- those securities to anything
10 that's remotely close to facilities that are there in
11 the ground serving the public, and that's the big
12 disconnect I have. And that's why I just, you know,
13 I just can't get to anywhere near what the company is
14 saying is a reasonable outcome of the interim case.

15 Q. In a way, isn't the company saying the
16 company as a whole, with all of its liabilities and
17 difficulties and expenditures, is in bad shape, and
18 unless they can get completely out of that bad shape,
19 they can't spend the necessary money for what is in
20 the ground? In other words, aren't they, in effect,
21 saying we've got to look at the whole company,
22 because you can't address part of the company without
23 -- or if we only address a part of the company or a
24 part of its assets and don't deal with the rest, the
25 owners, in this case, or lenders won't be satisfied?

01036

1 A. That's their case.

2 Q. Well, I mean, to take it into a different
3 context, maybe, take a utility that has regulated and
4 unregulated components, and supposing the unregulated
5 side nearly ruins the company. And therefore, the
6 company can't borrow or it's difficult for its
7 regulated side to function very well. Then, in that
8 instance, don't we get similar arguments, that unless
9 we somewhat take the whole company into account,
10 we're not going to make very much progress on the
11 regulated side? On the other hand, the ratepayers
12 shouldn't bear all that risk of that unregulated
13 side. Is this a similar situation, but slightly
14 different than the regulated/unregulated aspects?

15 A. It's similar, but I would say that you
16 still have to -- what makes it dissimilar is at least
17 there, on the regulated utility front, you could try
18 to cordon off and sequester the regulated operations.
19 In this circumstance, it's just so hopelessly
20 intertwined that I just don't know how to unwind it,
21 whereas in the Avista case that we were involved in,
22 we had some testimony about how to do that, and Mr.
23 Schoenbeck had some recommendations that I think had
24 a lot to go for it. You kind of divide up the
25 utility, look at some comparable groups and make

01037

1 rates and, you know, that's all you can do. In this,
2 in a way, I've tried to also incorporate that, saying
3 what is truly there in money spent for the utility.

4 And so my analysis, looking at the balance
5 sheet and the plant accounts, saying yeah, that
6 should be financed and that should have a return and
7 the company should have a reasonable ability to pay
8 debt service on that. That's how I tried to do a
9 similar and a parallel analysis for purposes of this
10 interim case.

11 Q. But by the time you add up your shoulds of
12 this is justified or this should happen, you added it
13 up and you got to approximately a 20 percent
14 increase.

15 If you step one step back and we authorize
16 that increase, but no more than that increase or no
17 other conditions, I hear you say that should be
18 enough to get them on footing, but another question
19 is will it. And what degree of confidence should we
20 have that that will get it off or, you know, continue
21 to get it back on track, and what if we're wrong?

22 A. Well, I think your question is if you're
23 wrong -- in the Avista case, and to some extent, we
24 -- the Commission fashioned a solution and tried --
25 at least I read your order as saying we thought this

01038

1 was reasonable and this would prevent a downgrade,
2 but the downgrade happened, and things go on. It may
3 be that this isn't enough and -- but I think, in my
4 estimation, I've looked at the documents and looked
5 at the source of financing, and the only reasonable
6 source is that additional 20 million under the
7 Olympic -- under the ARCO revolver. And I think that
8 telling the company that interim, based on some
9 semblance of plant in service, is all we can do, and
10 you'll get -- the attorneys will make arguments
11 about, you know, the legal constraints and whatnot,
12 but practically, I just can't say that 62 percent is
13 right, as the company's saying, because it just seems
14 to me that providing enough relief to completely fund
15 a capital program is not the right thing to do. It's
16 not to ask the shippers to pay all the costs of the
17 2002 construction program.

18 It may not be enough and it may be -- as I
19 testified in Avista, sometimes in receivership is the
20 answer, but -- and this was caused by the fact that
21 the company had no equity. And you know, as the
22 Commissioner and trying to figure out what's in the
23 public interest and put myself in your shoes, I think
24 that our analysis is clearly one that is principled,
25 it is, in my estimation, the right signal, it's

01039

1 moving the company towards building up some equity.
2 And if that's not enough, then we'll have to see what
3 falls out from that, but it may be that there is no
4 solution but for -- even 62 percent may not be
5 enough, is my concern, and I heard testimony the
6 other day that said without equity, who's going to
7 loan. You can't borrow a penny without having some
8 equity.

9 So we have to move forward, we have to get
10 this company in the right direction, but a 62 percent
11 increase just doesn't cut it, and I think that our 20
12 percent increase, and given the fact that the
13 company's beginning to turn around, we're moving in
14 the right direction, and I'm fairly confident that
15 this will be the right signal.

16 CHAIRWOMAN SHOWALTER: All right, I have a
17 few more questions, but I think we should wait till
18 after lunch.

19 JUDGE WALLIS: Very well. Let's be in
20 recess until 1:30, please.

21 (Lunch recess taken from 12:00 to 1:30
22 p.m.)

23 JUDGE WALLIS: Let's be on the record,
24 please. At the prehearing conference last Thursday,
25 Mr. Marshall made an inquiry about a document that

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1 the Commission had received, and I made inquiries on
2 Friday and located the document and was told that the
3 document had been received and a reply sent.

4 It turned out that that was in error and
5 that the reply had not been sent, but the process
6 that the Commission uses when a letter is sent
7 regarding a pending matter is to hide that from the
8 Commissioners. And as of today, neither the
9 Chairwoman nor Commissioner Oshie have seen the
10 letter in question, and the issue at this point is
11 how to deal with it.

12 Mr. Brena has suggested that we just let
13 the matter drop as it is and not take it further.
14 Mr. Marshall?

15 MR. MARSHALL: I brought it to Your Honor's
16 attention because I'd just been informed that day and
17 haven't yet seen the letter myself, but there might
18 be one out there that needed to be brought up in the
19 context that if it had been reviewed, then it should
20 be made available to all parties, so they would have
21 an opportunity to respond to it.

22 I think it's like any other letter. So
23 long as all parties have it, I think that satisfies
24 the Commission's rules, and that's why I thought I
25 ought to bring it to your attention. How the

01041

1 Commission wants to handle it is entirely up to the
2 Commission. I don't have a viewpoint as to whether
3 the Commission should read it or should not read it.
4 To me, it's -- I still haven't seen it, by the way,
5 so I don't know what it is in terms of any more than
6 a -- you know, to who -- from whom and to whom.

7 JUDGE WALLIS: We did provide a copy to all
8 parties this morning.

9 MR. MARSHALL: I did see that, but I
10 haven't read it, actually. I was going to, and I
11 haven't even read it myself.

12 JUDGE WALLIS: It would not, under ordinary
13 circumstances, either be delivered to the
14 Commissioners, nor made a part of the record. And Mr.
15 Brena, as I take it, is suggesting that we just leave
16 it with that. Is there any comment from others?

17 MR. TROTTER: That treatment is appropriate
18 from Staff's viewpoint.

19 MR. FINKLEA: I conclude with Staff and
20 Tesoro.

21 JUDGE WALLIS: Very well. Mr. Marshall, if
22 you have any alternative suggestions, then I believe
23 we'll leave it with that and that will be the status
24 of it.

25 MR. MARSHALL: That's fine by me. As I

01042

1 say, it's entirely at your discretion.

2 JUDGE WALLIS: Very well. If the letter
3 had been delivered and if it had been received by a
4 Commissioner, then our process would have been to
5 follow the ex parte contact rules and to make it a
6 part of the record.

7 As it has not been delivered, then I don't
8 notice that the Commissioners are sitting next to me
9 wondering what's going on, but it not having been
10 delivered, there has been no contact, and we'll just
11 leave it with that.

12 MR. MARSHALL: That's fine.

13 CHAIRWOMAN SHOWALTER: I just want to
14 clarify one thing. You said that neither
15 Commissioner Oshie nor I have read the letter, and I
16 don't think you meant to imply that Commissioner
17 Hemstad has.

18 JUDGE WALLIS: I did not mean to imply
19 that, no. I'm just looking to my right and seeing
20 who's here.

21 CHAIRWOMAN SHOWALTER: I just have a
22 question on this subject. When we receive letters
23 from members of the public in general rate cases,
24 they tend to be collected in a pile and delivered to
25 the Office of Public counsel, or at least maybe not

01043

1 delivered to, but reviewed by or handled or managed
2 by.

3 JUDGE WALLIS: Yes.

4 CHAIRWOMAN SHOWALTER: And I guess I'm
5 unclear myself what that process is and whether there
6 are two processes, one for some type of general
7 letter and another for other letters, or are we
8 dealing with the same process? We have no Office of
9 Public Counsel in this case, but I don't know if that
10 makes a difference or not.

11 COMMISSIONER OSHIE: I have the same
12 question. I concur with the Chair. You know, what
13 is the process for a letter of this nature and why is
14 it different than other public comment that we
15 receive?

16 JUDGE WALLIS: In a similar matter, letters
17 are provided to Public Counsel, public letters, and
18 Public Counsel, as a matter of routine, makes them
19 available to the Commission by offering them as a
20 group as illustrations of public sentiment. If a
21 letter is received that is of a different character,
22 then Public Counsel, as counsel for the public, is
23 able to take those and pursue them.

24 In this proceeding, we have no Public
25 Counsel. In similar proceedings in the past, the

01044

1 Assistant Attorney General has taken on those
2 responsibilities. As far as I know, this is the only
3 such letter that the Commission has received
4 regarding this particular docket.

5 MR. TROTTER: I might just offer that,
6 having been Public Counsel at one time, those are
7 often offered into the record for illustrative
8 purposes only. There's also -- Public Counsel
9 solicits public comment generally and does not filter
10 it as such, and there are some concerns -- I know, in
11 a recent Puget Sound Energy case, where
12 communications come in and they may be solicited by
13 the company initially in some manner. I don't know
14 if this particular one was, but usually these letters
15 don't come in of this nature we're talking about here
16 completely out of the blue, and so there is that
17 concern that -- again, I'm not alleging anything, but
18 that if the utility is behind the effort to influence
19 you, that that's a different level than a consumer
20 hearing about the case and writing their opinions to
21 you. And that being just used as illustrative of
22 public sentiment. So those are the competing
23 concerns.

24 In terms of the strict ex parte rule, I
25 believe it speaks to parties, and this particular

01045

1 letter was not from a party, but I commend the
2 Commission for being cautious about it, but I do
3 think it may be worth inquiring into the ground rules
4 on a more formal basis and try to figure out a system
5 that maybe works better than what we have now.

6 MR. BRENA: If I may, just briefly, to
7 respond to Commissioner Oshie's concern. My concern
8 is on the last day of a hearing and a letter comes in
9 that I was unaware of, I have no opportunity to
10 cross-examine on any of its contents, none of the
11 normal procedural due process that would be available
12 to me, if it were timely received or if I had an
13 opportunity to go to the author or I had an
14 opportunity to voir dire him or put him on the stand,
15 ask him for the basis for the letter and how it came
16 to be and the origin, none of those procedural
17 safeguards are available with regard to this
18 particular letter, and that was the basis for my
19 recommendation, just to keep that stuff completely
20 out of the hearing room.

21 CHAIRWOMAN SHOWALTER: All right. And I --
22 we are at a bit of a disadvantage here, but I gather
23 every party here has been able to assemble the
24 evidence that each party wants to present and have
25 that subject to the other party's scrutiny. In other

01046

1 words, we're talking about additional comments from
2 non-parties, which really don't affect the ability of
3 all of the parties to present whatever evidence they
4 deem relevant for our consideration.

5 MR. FINKLEA: I think that's correct.

6 MR. TROTTER: Yes, I think the concern is
7 that if the letter should be used for substantive
8 evidentiary purposes, there's a problem. I don't
9 think the Commission has ever done that, or if they
10 did, they'd allow process. But to the extent it's in
11 the record and you're looking at it, sometimes it's
12 hard to divorce those two types of approaches, so
13 that's the gist of the problem, I think.

14 MR. MARSHALL: We may have made this more
15 mysterious than it should be, and again, I think it's
16 up to the Commission. I think this is one of those
17 kinds of things that if there were Public Counsel,
18 this probably would have come out in some manner,
19 even though it's not from the public, per se.

20 I've just been shown that the reply letter
21 indicates it had been entered into the record in this
22 case.

23 JUDGE WALLIS: That is incorrect, and
24 considering the views of Counsel, it will not be, and
25 we will advise the writer of the letter to that

01047

1 effect.

2 MR. MARSHALL: Good.

3 JUDGE WALLIS: Very well. We now resume
4 the examination of Mr. Elgin.

5 BY CHAIRWOMAN SHOWALTER:

6 Q. Well, I'm trying to remember where we were
7 before lunch. You are not a lawyer, so I don't want
8 you to worry about whether the Commission can or
9 cannot do this. We can ask for legal briefing on
10 legal questions. But if the Commission were to
11 condition a rate increase, a temporary rate increase
12 on other actions of the company, would that increase
13 the likelihood that this ratcheting up that we want
14 to achieve could be achieved? And by ratcheting it
15 up, I mean, it seems to be your sentiment that
16 everyone needs to take steps to get the company on a
17 firmer footing.

18 A. That's correct.

19 Q. And your recommendation of a rate increase
20 is one of those steps?

21 A. Yes.

22 Q. Well, what are the other steps? If the
23 rate increase -- if the interim rate increase is step
24 one, what would step two or three be?

25 A. Step two would be clearly the company

01048

1 continue with its --

2 Q. I think your mike isn't on.

3 A. I'm sorry. Yes. Step two would be the
4 company continue with its 2002 capital program, and
5 get the pipeline operating up to a hundred percent
6 pressure to enable it to further increase throughput.

7 The second -- third step would be bring the
8 Commission a financing plan, some kind of long-term
9 financing plan as to how it would plan to finance and
10 operate this business on a long-term basis. Clearly,
11 as I previously stated, if the company is given some
12 kind of, for rate-making purposes, a hypothetical
13 capital structure and we provide rates based on that
14 hypothetical and the company continues to finance
15 with a hundred percent debt, that would be some kind
16 of concern down the road, but, you know, as part of
17 the financing plan, if they said we would be moved to
18 -- let's just say, for argument purposes, a 50/50
19 debt equity ratio, some kind of plan to get there,
20 and how the rate relief would fit into that and what
21 kind of series of steps over time they would take to
22 get to there.

23 And then the other thing, it seems to me,
24 is clearly looking at the company's balance sheet,
25 what role does its investment in Cross Cascades play.

01049

1 In other words, should those facilities be sold or is
2 there any long-term impact to ratepayers of
3 continuing to have that on its books. And I think
4 for now, that's about the only things that come to
5 mind.

6 Q. Well, those are five other steps.
7 Supposing we did condition our rate increase on firm
8 evidence that those steps were underway? I don't
9 know to what degree, but let's say they were
10 satisfactorily underway.

11 If we had that kind of evidence, would it
12 justify a higher interim rate increase, in your mind?
13 In other words, is your recommendation in some way
14 constrained by the absence of these five steps and
15 would be less constrained if there was more evidence
16 of these steps?

17 A. I'm just going to answer this, because I
18 haven't run the numbers, but clearly, the 62 percent
19 increase that they're asking for in the interim and
20 the general, the thing that drives that is -- and you
21 asked me previously, does this recommendation get --
22 prejudice the issue or get to the issue about FERC
23 methodology.

24 But clearly I have some constraints in my
25 recommendation, because I don't necessarily agree

01050

1 with the trended rate base methodology that the
2 company's proposing. And clearly I have a concern
3 about the disconnect between the way the company's
4 financed today and what they're proposing for an
5 equity ratio with a general rate case. So to that
6 extent, I have constrained my recommendation to
7 recognize the realities of how this company is
8 financed. So in that regard, I have not run the
9 numbers.

10 But in a general rate case, the nature of
11 these costs and the nature of the company's cost of
12 service is driven principally by investments, return
13 on rate base, and the components of that, and that
14 would be return on equity and capital structure.
15 Those are tremendous cost drivers in the company's
16 total cost of service.

17 So I think the answer to your question,
18 yes, that this recommendation would be different had
19 they been financed probably differently.

20 Q. All right. Well, then, would it justify an
21 order that says if you do nothing more, you get a 20
22 percent increase -- this is from your point of view
23 -- but if you do various steps, it would justify a
24 higher rate of increase, interim? Does that make any
25 sense?

01051

1 A. For interim purposes, no.

2 Q. Okay.

3 A. But for the conclusion of the rate case and
4 where we're going in terms of a long-term solution to
5 this company's problems, I think it does.

6 Q. Okay. I want to get back to something you
7 just said, because it seemed to imply that, in fact,
8 you are somewhat constrained in your recommendation
9 by, in effect, rejecting the FERC methodology; is
10 that right? Or is it because you don't agree with
11 the FERC methodology that, in part, your
12 recommendation is only 20 percent?

13 A. No.

14 Q. No?

15 A. No, what I was saying is that -- I thought
16 I understood your question to say am I constrained
17 now and in the context of what would be the
18 conditions in this long-term solution to the problem.

19 What I was getting at in term of my
20 analysis now and my constraint was I had to look at
21 what was really there and what I felt comfortable
22 about, the nature of the company's investment in
23 actual facilities, and then how they finance that, so
24 that was my constraint.

25 And then, as we move and transition from

01052

1 the interim to the general, and even the long-term
2 solution to this company's problems are all, in my
3 mind, tied to how they finance it and what's really
4 there serving the public. What are the facilities.

5 Q. All right. The reason I'm asking this
6 question is that I am unclear to what extent anyone's
7 recommendations depends on the acceptance or
8 rejection of FERC methodology, and this is interim
9 only, and if, if -- and it's an if -- if the
10 Commission has accepted in its last rate approval a
11 FERC methodology, then I'm not sure we should be
12 amending that methodology in an interim proceeding.
13 That's for the general.

14 And so if the status quo -- if the status
15 quo is kind of a FERC methodology because we have
16 previously approved something based on it -- and all
17 those are ifs -- but if that's the case, I think we
18 shouldn't revise that until we've had a full hearing.
19 And I want to understand what I'm being asked to do,
20 either by Staff or the other parties, in terms of any
21 revisions of that methodology. If it's not an issue,
22 that's fine.

23 A. Let me make it very clear that my
24 recommendation, the recommendation of the shippers,
25 and the recommendation of the company have nothing to

01053

1 do with FERC methodology.

2 Q. Okay.

3 A. So in adopting any -- any one of the range
4 of solutions that are out there proposed, nobody's
5 asking you to decide that issue.

6 Q. All right. That's good. Let me shift,
7 then, to the issue of the throughput and deficiency
8 model. Is the presence or absence or acceptance or
9 rejection of a throughput and deficiency model, and
10 coupled maybe with a no equity element, is that
11 related to the FERC methodology or not?

12 A. It's not at all related to the FERC
13 methodology.

14 Q. Okay. This demonstrates that I don't know
15 anything about the FERC methodology, which is a good
16 thing, since this is only the interim case.

17 I wanted to ask you about your comments --
18 I think it's on page 10 of your testimony.

19 A. I have that.

20 Q. It's your comment that we should be making
21 sure that the 2002 expenditures are for essential
22 expenditures, and what that means. I guess my
23 question is, if you have an ongoing company who's
24 needing to make reasonable expenditures, why wouldn't
25 the appropriate range be reasonable expenditures to

01054

1 keep the company going, as opposed to do essential
2 expenditures? Why would we be restricting what
3 should be spent from reasonable down to essential?

4 A. Well, there's two factors to consider. One
5 is is the timing right to finance the project.
6 Sometimes timing makes a considerable difference.
7 And then the second thing is that if you are in an
8 emergency and you have constraints on capital and
9 cash flows, the prudent thing to do is to look at
10 every -- leave no stone unturned with respect to what
11 is absolutely essential and necessary.

12 Going back in the history of the
13 Commission's cases on interim relief, quite a few of
14 them had to do with ongoing construction projects for
15 large thermal generation, particularly the electric
16 companies. And then, in some instance, in other --
17 it's -- so in my mind, there was a shortage of power,
18 the companies had to have access to capital markets,
19 they had to continue these projects, they had to get
20 these long-lived assets built, and so there was this
21 kind of this assurance that everything -- the company
22 looked at every possible means of saying we had to
23 spend this money. There was -- the public demanded
24 the service, we're short of power, or some situation
25 like that.

01055

1 And so in my mind, I looked at their budget
2 and I couldn't tell whether or not one element or
3 another was essential, and so in my review of the
4 prior cases, this was one of the criteria that the
5 Commission looked at. And so on page 12 of my -- on
6 page 10, line 12, that was the point.

7 Q. Okay. But if you have expenditures that
8 let's say are reasonable, but not essential, but need
9 to be done sometime, maybe unlike a go, no-go
10 decision on a big plant, doesn't it just defer these
11 reasonable expenditures to a later time period, in
12 which case you're more or less frontloading what's
13 needed in the next rate period?

14 A. But the interim rate relief standard is in
15 an emergency, and so if something can be deferred,
16 then to get us through the emergency and to get us to
17 a point where we can determine the revenue
18 requirements and the cost of service on an ongoing
19 basis and will prove the company's cash flow on a
20 rate-making basis, then that would be the time for
21 the company, now, to begin to deal with those
22 expenditures that are necessary, but not essential.

23 Q. All right. But once we figure out the
24 permanent fair, just, and reasonable rate on a going
25 forward basis, wouldn't it now have to cover more

01056

1 expenditures in the first several months or year of
2 the rate period because those expenditures had not
3 been carried on in a normal way in the previous
4 period?

5 A. You have those, they're deferred, so
6 assuming that you have the continuing accumulation of
7 ongoing expenditures, but now you have the cash flow,
8 and now you have the ability to not only have a
9 balanced capital budget, but you have a balanced
10 financial plan as to how you're going to finance it
11 on an ongoing basis in a reasonable manner, which
12 would include debt, preferred equity, and common
13 equity.

14 So you'd have all the pieces in place so
15 that, on an ongoing basis, you have the cash flows,
16 you have the balance equity capital structure, and
17 you have a financially sound utility on a going
18 forward basis, can go ahead and finance those
19 operations.

20 Q. Well, I don't think I'm speaking of the
21 current situation; I'm just speaking theoretically.
22 That if you push out of one period into another
23 period reasonable expenditures, don't you necessarily
24 raise the revenue requirement?

25 A. No.

01057

1 Q. And why not?

2 A. Because primarily what you're doing is just
3 deferring a capital expenditure to the time that you
4 have the revenues to support the investment. In a
5 purely theoretical situation in finance, any utility
6 is capital constrained. So the capital budget in
7 question for a financial officer of a company is
8 amongst competing projects where I'm capital
9 constrained where I could defer something, but do
10 something else. Relative speaking, I'm not costing
11 me anything more; I'm just rationing my capital.

12 And I think the interim case is -- isn't
13 analogous to that situation. That we deal with the
14 emergency, what's essential, we put the company on
15 financial footing that's sound, and now the company
16 can go and finance, issue new debt, issue preferred,
17 issue common and finance those projects, but by
18 deferring something, it's possible that you could
19 increase some expense, like if you defer maintenance
20 on something, but then that comes in question of
21 degree, and is it essential or can it reasonably be
22 deferred.

23 And I think that those are the kinds of
24 decisions -- and this is what my testimony's about,
25 is we don't have that in front of us now. I just

01058

1 don't know.

2 Q. I might be forgetting what I asked you
3 before lunch versus after lunch, but do you have an
4 opinion on there being a difference between debt and
5 equity of an owner, and let's assume that we're
6 comparing an equitable interest by an owner versus a
7 loan which perhaps is second in line behind some
8 other loans. We had testimony earlier this morning
9 that both of them represent risk, but are they the
10 same?

11 A. Yes, and I'm not sure I understood what --
12 fully the import of Mr. Schink and what he was trying
13 to distinguish there. In my mind, at least what I
14 understood your question, is that this was some other
15 questions, I believe, of Mr. Batch, as well, is that
16 if you own, have an equity interest in something and
17 you have something to lose, clearly the ability for
18 you to secure financing, in my mind, is enhanced.

19 Q. Okay. But -- oh, maybe you were going to
20 keep going?

21 A. No, I think that that's -- that's my
22 understanding. Now, what Mr. Schink was trying to
23 say in that discussion you had with him earlier this
24 morning, I'm not sure I understood. I think what
25 he's saying, at the most fundamental level, is that

01059

1 any project has risk, and whether it's financed with
2 debt or equity, irrespective of that, capital's at
3 risk. And that's as far as I understood what he was
4 saying.

5 The other thing I understood him saying is
6 that it clearly didn't matter how it was financed,
7 because the only thing that mattered was more
8 revenues to Olympic, and so, other than that, I'm not
9 sure I really can go much further with that.

10 Q. Well, I wasn't really asking you to
11 interpret his comments, but just ask you whether you
12 see a difference in \$50 million of equity versus a
13 \$50 million loan from an owner?

14 A. Yes, because the owner -- the owner is
15 putting it all at risk, that his interest clearly
16 becomes secondary to a bond holder. And so at the
17 most fundamental level, \$50 million of debt and \$50
18 million equity is a risk, but if I'm a note holder
19 and I can have some claim to the assets as a note
20 holder before equity owners, I'm in a preferred
21 position.

22 Q. Right, but what if there are no equity
23 owners? So I mean, in effect, has the owner/lender,
24 who comes second after non-owner/lenders, is that
25 owner/lender in the last position anyway, because

01060

1 there's no equity to be above?

2 A. That's right.

3 Q. So then, is there a difference? Isn't --
4 in each case, isn't the owner last in line, either as
5 an equity holder or as a lender with no equity below
6 the lender?

7 A. Well, and this is why I had the trouble
8 figuring out what the discussion was. I mean, and I
9 think part of it traded on the ambiguity of the word
10 equity. This company has no equity. In fact, its
11 equity is negative. So for purposes of -- just
12 because I have equity interest in the company, if I
13 look at the balance sheet, there's nothing there.
14 There's no book value. There's nothing there that I
15 can claim ownership of, other than I have a piece of
16 paper that says I had a 70 percent interest in the
17 equity, but there's none. So if I continue to loan
18 money --

19 Q. Well, could that be the answer? I don't
20 know. But maybe the answer is once you get into a
21 negative equity, then doesn't the lender, the
22 owner/lender stand above somebody who -- one way or
23 another, the company got to a negative equity, which
24 I assume means there's somebody holding a bag
25 somewhere, an empty bag. And if that someone were no

01061

1 one other than the owner/lender, I guess it wouldn't
2 make any difference, but if the someone includes
3 somebody other than the owner/lender, then doesn't
4 the owner/lender stand in a better position than the
5 one who otherwise would have introduced equity and
6 then lost it?

7 A. Well, yes. I mean, if you had a company
8 that has negative equity, that means that there's
9 more claim in loans than there are assets to be
10 pledged, and there is no ownership interest
11 whatsoever, and so that, on liquidation -- I mean,
12 I'm no expert in how this gets all sorted out in a
13 receivership situation, but clearly it's a problem,
14 and it's a problem that I identified, and there is no
15 easy solution.

16 And the thing that compounds it is that it
17 appears that what the company did is issue debt to
18 pay ongoing operating expenses. And that is just
19 really not good business practice, that if you're
20 going to issue debt, you better have something to
21 show for it.

22 Q. Okay. Moving to just a couple other areas,
23 I thought I heard you answer a question regarding
24 financial ratios, that it doesn't really make sense
25 for a company that has no equity to be using them or

01062

1 for us to analyze the company that way. I'm not sure
2 what you said, but what I was getting to is that you
3 do have this 1.5 ratio, covered ratio factor?

4 A. Mm-hmm.

5 Q. Tell me the right terminology.

6 A. It's a pre-tax coverage.

7 Q. Okay. Does it make sense to use that,
8 whether it's 1.5 or 2.5, in this case when the
9 company has no equity?

10 A. Yes, it does.

11 Q. And why?

12 A. The question from Mr. Brena had to do with,
13 if you don't have a financial statement that's
14 unqualified and you calculate some ratios, well, the
15 unqualified nature of the financial statement now
16 says that the ratios that you calculate have meaning.
17 So in other words, if I use an income figure to
18 calculate a coverage ratio or if I use an income
19 figure to calculate earned return on equity or if I
20 calculate a book value or any kind of financial
21 analysis that I would do with those statements, the
22 analysis has credibility. So that was the line of
23 questioning I had with Mr. Brena.

24 If you turn to -- what I've done here is
25 make a couple of assumptions that is premised on

01063

1 sound financial theory. And that is that the balance
2 sheet has assets and liabilities, and basic
3 accounting principles, the assets has to equal the
4 liabilities. And the corollary to that is that if
5 you have long-life assets, you have long-lived
6 financing.

7 So take that fundamental financial
8 principle and apply it to the assets on the books and
9 say that has to be financed somehow. And since this
10 company is a hundred percent debt, it's reasonable to
11 assume that it needs to cover the interest cost of
12 those assets, plus with some extra.

13 So -- and the one and a half times comes
14 out of the kinds of things that you see in firms that
15 have publicly-traded securities, preferred equity
16 covenants, first mortgage indentures. Those are
17 protective covenants that basically say if your
18 pre-tax earnings fall below one and a half, you are
19 restricted from the articles of incorporation from
20 issuing any more debt. It's a basic, most
21 bottom-line protection measure for both the preferred
22 owners and the existing bond holders.

23 Q. So -- I just don't want you to get too far.

24 A. Okay.

25 Q. So is what you're saying is that a 1.5

01064

1 coverage is more or less rock bottom, and that to get
2 higher than that, you need to have -- be on a
3 different footing than you believe this company is?

4 A. Right, to get higher than that, you need to
5 not only move up your coverages, but then also those
6 coverages then have to do with the amount of equity
7 that's invested. And that's the fallacy of Mr.
8 Schink's rebuttal testimony, where he says, Well,
9 you've got to have a 2.6. He's forgetting the other
10 half of the coin was, when you get to that point,
11 those are typically companies that have 40 to 50
12 percent of equity investment in, in the company.

13 So I've calculated a rock bottom, some room
14 to spare, let's provide that level of interim relief
15 and then let's sort out the remainder in the general
16 rate case, is what my recommendation is.

17 Q. Okay. I want to fill in just a couple more
18 blanks. You testified that Olympic has not notified
19 the Commission of all but two security applications.
20 This is my notes.

21 A. Mm-hmm.

22 Q. What were the two where the Commission was
23 notified?

24 A. I believe it's the Chase note and the
25 Prudential note. Let's see, which exhibit? There is

01065

1 -- it would be the most recent -- the most recent
2 financing application we've had for this company is
3 in the exhibit, and I left that over at -- here, I
4 could provide that to you, if I could get my --

5 JUDGE WALLIS: Let's be off the record for
6 a moment.

7 (Recess taken.)

8 JUDGE WALLIS: Let's be back on the record,
9 please. Mr. Elgin, are you prepared to proceed now?

10 THE WITNESS: Yes. It's BCB-30, and that
11 is, I thought, Exhibit 16. It's Exhibit 16, BCB-30.

12 JUDGE WALLIS: Yes.

13 THE WITNESS: That is the last application
14 this Commission received with respect to the
15 financings of Olympic Pipe Line Company. None of the
16 ARCO notes that were identified in Mr. Batch's
17 original testimony, BCB-5, Exhibit T-2, on page
18 three, none of the ARCO short-term notes were ever
19 brought before the Commission in light of the filing
20 requirements of 81.08, our security statute. So I
21 believe just the Prudential note, and I'm not sure
22 about the Chase note, because that was -- it's a
23 rolling over situation. Whether that was originally
24 filed when it was first entered into, I'm unsure
25 about that, but those would be the only two.

01066

1 Q. All right. Can you turn to page 20 of your
2 testimony?

3 A. Yes.

4 Q. And on lines 19 through 22, you say that
5 you took into account that Olympic is not in default
6 of the Chase and Prudential notes. Is that still
7 your premise and assumptions?

8 A. Correct.

9 Q. And another general question. When you are
10 doing your analysis and making your recommendation,
11 are you putting blinders on the interstate operations,
12 and the FERC-approved 62 percent interim rate
13 increase, or are you not? Are you taking that into
14 account in any way in terms of the company's health?

15 A. We have done an analysis that says
16 Washington intrastate stands alone, that the FERC
17 jurisdiction stands alone, so how Mr. Colbo adjusted
18 the recommendation, Washington intrastate stands
19 alone.

20 Q. Put another way, if FERC had not approved
21 its interim increase, would your recommendation be
22 any different?

23 A. No, it would not. That it's -- my
24 understanding of reading the prior -- some prior
25 Commission orders, is that the Commission has said

01067

1 that it will, for interim purposes or a surcharge,
2 look at Washington and Washington's responsibilities
3 and the other jurisdictions have -- you separate
4 them. You -- Washington stands alone.

5 Q. All right.

6 A. And I want to clarify. You used FERC
7 interim. The FERC rates are -- so they're, in
8 effect, subject to refund, and it's really --

9 Q. I recognize that terminology was probably
10 wrong.

11 A. Okay.

12 Q. What FERC did last September. I'll call it
13 that.

14 A. Yeah, okay.

15 Q. But your answer is the same; correct?

16 A. It's the same, yes.

17 Q. There is another point in your testimony
18 when I don't think you completed the thought. You
19 were talking about things being very intertwined, and
20 you mentioned budgets and financing applications, and
21 you made mention of three elements or three factors,
22 and you didn't enumerate the three. I'm wondering if
23 you remember what I was talking about? This was on
24 the stand this morning.

25 A. Yes.

01068

1 Q. And what those three were.

2 A. Let me see if I can find it quickly here in
3 my direct testimony. I would ask you to turn to page
4 nine, please. And the Q&A beginning on line nine, I
5 think, is pretty much a complete description of the
6 intertwining kinds of thing that I was talking about.

7 Q. So what were these three elements that you
8 -- you alluded to three, but didn't end up telling
9 what the three were.

10 A. Okay. First off, there is -- there's a
11 problem with the earnings, and the company has
12 essential capital needs, needs to access to capital
13 markets and it's constrained, that there is kind of a
14 long-term financing plan before us, and that there's
15 a connection between the relief and the ability to
16 finance.

17 Q. Okay. I see what you're talking about now.
18 I think that's all the questions I have. Thank you.

19 A. You're welcome.

20

21 E X A M I N A T I O N

22 BY COMMISSIONER OSHIE:

23 Q. Mr. Elgin, in your earlier discussions and
24 your testimony, there were issues raised by the
25 Chair, particularly with regard to the company's

01069

1 financial improvement and the five steps that you
2 believe would be required to move forward.

3 You did, just as a matter of clarification,
4 you talked about the Cross Cascades pipeline
5 investment, and whether it was appropriate to keep
6 the facilities on the books. And my question really
7 goes to whether there are actually facilities that
8 were constructed as a result of the -- of that
9 project, of the Cross Cascades project?

10 A. I don't know what was specifically
11 constructed or whether there are actual facilities.
12 I do know that there's \$21 and a half million of
13 investment, so you would think that something was
14 done and there's something of value related to that
15 \$21 and a half million expenditure. Whether it's
16 specific facilities, pipe in the ground or switches
17 or whatever, I don't know.

18 Q. Okay. I want to follow up a little bit on
19 one of the questions that was asked also by the
20 Chair. And this has to do with your recommendation,
21 at least, that at least as far as capital
22 expenditures, that the only expenditures or the only
23 capital projects that should be funded for 2002
24 should be those that are considered to be essential
25 by the company.

01070

1 And my question really goes to whether you
2 believe that there is capital projects that would be
3 required under the Office of Pipeline Safety's
4 corrective action orders and its amendments would be
5 considered to be essential or required?

6 A. I think the distinction would be in the
7 interim case, if you -- if the requirements were
8 those kinds of expenditures to get the company up to
9 a hundred percent pressure, those are things that
10 might be able to be deferred in non-essential. The
11 things that are necessary to ensure the safe
12 operation of the pipeline, as it's operating now,
13 would be considered essential, but again, I don't
14 know what's specifically required.

15 Q. So I guess if the projects that would be
16 required under the corrective action order and its
17 amendments, if it would be required for the continued
18 operation of the pipeline, then you would consider it
19 to be essential?

20 A. That's correct, but, again, the question is
21 the timing. We're talking about a 2002 budget which
22 goes from, you know, till the end of 2002.

23 So I would not think that all those
24 expenditures would for the entire year, and
25 furthermore, even what might be in the near term, the

01071

1 question of could that be deferred until from, say,
2 theoretically second quarter of 2002 to third
3 quarter, after the general.

4 But I would note that my analysis assumes
5 -- and I want to make it so that the record's clear,
6 what they have spent in 2001, even though they
7 haven't shown is essential, I've included in my
8 calculation for interim relief. The entire 25
9 million that they spent in 2001 is included in my
10 analysis.

11 The question now goes to the propriety of
12 continued capital expenditures through 2002, and
13 that's the 24 million.

14 Q. Do you think that the -- that actions taken
15 to comply with the corrective action order of the
16 Office of Pipeline Safety is directly or indirectly
17 related to the Whatcom Creek incident?

18 A. I believe many of the expenditures that the
19 company has today, in terms of what is being
20 required, are -- let me take that back.

21 It's my sense that a lot of what this
22 company has to do and some of the things are because
23 of the Whatcom Creek incident, and there's just this
24 question about -- I lost my train of thought here for
25 a second. I'm trying to assimilate this in the

01072

1 context of what I know and what is kind of like from
2 going through all these documents and the discovery
3 in this case, what I've surmised from reading this,
4 but it just seems to me a lot of what the company's
5 facing are items and things related to Whatcom Creek.

6 There's clearly the direct expenses, but
7 then there's this whole series of costs and
8 expenditures that, while not directly related to
9 Whatcom Creek, Whatcom Creek is indirectly affecting
10 the company's cost, and how that all gets sorted out
11 is going to be a complex task. That's the best way I
12 can put it.

13 Q. Is that something that you believe should
14 be better deferred to the general rate case?

15 A. Yes, sir.

16 Q. One other area that I'd like to ask you a
17 few questions about deals with the Bayview terminal.
18 I noted in your testimony that you've determined that
19 the assets and service of Olympic Pipe Lines is
20 approximately \$98 million; is that correct?

21 A. Yes, sir.

22 Q. And you believe that it's appropriate to
23 include the Bayview terminal in that \$98 million
24 figure; is that also correct?

25 A. For purposes of calculating the interim

01073

1 relief, yes, sir.

2 Q. Now, I guess I have some questions that
3 really go to when Bayview was placed into service,
4 and maybe you know or you don't know, Mr. Elgin, but
5 that is -- perhaps better I should rephrase the
6 question. Do you know when the Bayview terminal
7 assets were placed into service by the company?

8 A. Yes, that's -- we have an exhibit already
9 in the record. It's from Mr. Batch's rebuttal. It's
10 BCB-28. I believe that's Exhibit 18. Excuse me,
11 it's not 18; it's --

12 JUDGE WALLIS: Exhibit 14.

13 THE WITNESS: Fourteen. It would be --
14 these pages aren't numbered, but it would be -- on
15 the sixth page back, there's a memorandum from Mr.
16 Colbo, so in 1998, it was placed in service.

17 Q. Is it your opinion that the Bayview
18 terminal's still in service at the present time?

19 A. It's unclear as to if it's in service, as
20 to what the original intent and how it's described in
21 this memorandum is being used for that purpose. My
22 understanding, now it's serving as a support for some
23 of the testing procedures that the company's doing
24 when it runs water through the line and when it runs
25 water and does hydro testing to ensure the integrity

01074

1 of the main trunk line facility, the water becomes
2 contaminated and they needed to store that water. So
3 in the process of the hydro testing and some of the
4 ongoing testing procedures, they're using Bayview,
5 but Bayview is not being used as it was originally
6 intended, and that is to enable the pipeline to
7 increase capacity and improve the operational
8 flexibility of its mainline system. So it's not
9 being used for that purpose, but for another purpose.

10 Q. Is that the reason why you have the opinion
11 why it should be included as assets in service, in
12 public service, then?

13 A. I have concluded that -- it's in my
14 calculation, because it's a facility that's on the
15 company's balance sheet, and that the company has
16 taken depreciation and it's been in service, but
17 whether or not it has continued to operate and what
18 would be the proper rate-making treatment of this
19 facility, I have not come to a conclusion yet.

20 But for purposes of this case, I've
21 included it in a reasonable -- in a reasonable level
22 of assets to provide a calculation of the amount of
23 plant that's serving the public for purposes of this
24 interim case. So in the general, the actual
25 treatment of that is reserved, is what I'm

01075

1 suggesting.

2 Q. At least for purposes of this case, is it
3 that -- I guess the distinction, then, that the Cross
4 Cascades asset is not being depreciated by the
5 company on its books and that the Bayview terminal
6 asset's depreciation has been taken on that asset?

7 A. That's the distinction I've made, sir.

8 COMMISSIONER OSHIE: I don't have any other
9 questions.

10

11 E X A M I N A T I O N

12 BY CHAIRWOMAN SHOWALTER:

13 Q. I just have a followup on the Whatcom
14 issues. I think it's fair to say that the explosion
15 itself certainly generated certain liabilities and
16 expenses directly. It also generated a heightened --
17 you might say hypersensitivity in Office of Pipeline
18 Safety and our agency and the legislature and
19 Congress and the Bellingham community about pipeline
20 safety issues.

21 And I think if one used a but-for test, one
22 could fairly say, but for the Bellingham explosion,
23 all of that activity and sensitivity would not be
24 present. But it is present, and so there may be
25 requirements or laws or other reactions that have now

01076

1 became embedded in either our community or our laws.
2 And it's that realm of activities and the company's
3 response to those activities that I'm interested in.

4 Ultimately, we have a public interest test
5 here, and the public, in the vicinity of the
6 Bellingham -- of the, excuse me, the Olympic Pipe
7 Line, not only in Bellingham, but elsewhere, is
8 clearly much more interested in this pipeline and
9 activity than my guess is any citizenry is
10 interested in any other pipeline. That might not be
11 true, but it must be close to true.

12 So how do we take into account either the
13 new paradigm or new plane of concern that would not
14 be present but for the Bellingham explosion, but that
15 has taken on somewhat of a life of its own?

16 A. Well, I think we have. Mr. Colbo describes
17 his accounting analysis that takes into account a
18 preliminary analysis of those increased level of
19 expenses. And I think the Staff recommendation for a
20 20 percent increase in the interim I think is part
21 and parcel to take into account to that, to recognize
22 the company has increased expenses, it has need to
23 access capital, and so we've attempted to take into
24 that -- that into account, and the specific
25 adjustments and how Mr. Colbo calculated a

01077

1 representative test year for interim purposes, you
2 could take that up with him.

3 And so I think the Staff recommendation as
4 a whole attempted to account for that, and we have
5 included those expenses and we have included what we
6 believe is a representative level of those kinds of
7 things, but the ultimate outcome of where's a
8 reasonable level of expenses for rate-making is a
9 rate case issue.

10 But to the extent that they are facing this
11 company now in this interim case, we've tried to
12 account for those. And how Mr. Colbo adjusted that
13 test period and made a representation of the
14 company's resultant operations, ask him those types
15 of questions.

16 Q. All right. But so, for example, have you
17 allowed more public education, public outreach
18 expenses than you might have five years ago?

19 A. I believe he has.

20 Q. Okay.

21 A. But the specifics of those levels of
22 expenses, he's had the opportunity to look at those
23 accounts and can go into further detail with you on
24 that.

25 Q. All right. And then, likewise, in thinking

01078

1 about the 2002 capital expenditures, is it
2 appropriate to take into consideration, in terms of
3 what is essential, the heightened sensitivity that
4 the public has?

5 A. And I think, to some extent, we have,
6 because we have included all of 2001 capital
7 expenditures.

8 Q. Well, I was asking about 2002. In other
9 words, when we decide what is essential, if we, in
10 fact, get into that exercise, but you have
11 recommended that we gauge what is essential and what
12 isn't. Is a factor in determining what is essential
13 the public expectation?

14 A. Well, to be quite candid, I think what I
15 was saying in my testimony is the company has not put
16 forth the evidence to say what's essential. But our
17 analysis is to try to provide, based on what they
18 have spent and what's out there in service and
19 provide a reasonable level of earnings that they
20 should be able to fund and finance 2002 in this
21 interim case.

22 Q. I see. So you're saying because you did
23 take that kind of factor into account in allowing for
24 the 2001 expenses, it carries that over into an
25 allowance of that type of factor, the 2002?

01079

1 A. Correct.
2 CHAIRWOMAN SHOWALTER: Okay. Thank you.
3 JUDGE WALLIS: Mr. Trotter.
4 MR. TROTTER: Thank you, Your Honor.

5
6 R E D I R E C T E X A M I N A T I O N
7 BY MR. TROTTER:
8 Q. Mr. Elgin, with respect to the 2002 budget,
9 did your analysis assume any reduction in that
10 budget?

11 A. No.
12 Q. With respect to your testimony about a
13 showing of those projects that are essential and
14 cannot be deferred, did the company provide such a
15 showing?

16 A. No, it did not.
17 Q. Did you participate in the recent Avista
18 docket, 010395, in which interim -- excuse me,
19 emergency rate relief was involved?

20 A. Yes, I did.
21 Q. Did Avista provide an analysis of budget
22 and expense items that they could reduce or defer?
23 A. Yes, it did. And I might add, to that
24 extent, the company went so far as to even sell its
25 interest in -- half of its interest in a major

01080

1 generating facility.

2 Q. Now, is it your understanding that the
3 general rate case will be resolved by the end of July
4 or August?

5 A. Yes.

6 Q. If a project was to be deferred for the
7 interim period, are you recommending that -- or would
8 such project need to be deferred any longer than
9 that?

10 A. No.

11 Q. You listed some steps in response to the
12 Chair's question regarding the steps that the company
13 would need to take to move forward, in your judgment.
14 Would the provision of an unqualified audit
15 statement, would that be appropriate to include on
16 that list?

17 A. Yes, it would.

18 Q. You were asked several questions by Mr.
19 Brena regarding prior orders of the Commission on
20 interim rate relief, and various characteristics of
21 the company's operations that were involved in those
22 dockets. Do you recall that, generally?

23 A. Yes.

24 Q. Did you answer those questions based on the
25 best of your knowledge?

01081

1 A. Yes.

2 Q. Do those orders that the Commission has
3 issued speak for themselves on the subjects that Mr.
4 Brena raised with you?

5 A. Yes.

6 Q. Are you aware that the Commission has
7 resolved requests for interim relief from solid waste
8 companies and water companies?

9 A. Yes.

10 Q. What is your understanding of the nature of
11 those companies?

12 A. Many of those companies subject to the
13 Commission's jurisdiction are small, owner-operated,
14 and almost invariably they have financial statements
15 that are unaudited.

16 Q. As a general matter, are the debt
17 securities or other securities of those companies
18 publicly traded, to your knowledge?

19 A. No, they're not.

20 MR. TROTTER: Those are all my questions,
21 Your Honor. Thank you. Oh, I did have one other
22 line. I'm sorry.

23 Q. Mr. Elgin, you were asked some questions,
24 and you responded, about your 1.5 times interest
25 coverage number?

01082

1 A. Yes.
2 Q. I'd like to ask you a couple of
3 hypotheticals, and I'd like you to assume that a
4 utility is financed -- excuse me, has \$100 of total
5 plant, and that it has a 50/50 debt ratio. Do you
6 have that in mind?
7 A. Yes, I have those figures down.
8 Q. What would be the amount of total debt?
9 A. Fifty dollars.
10 Q. And if the cost of that debt was \$10, what
11 would be the total interest expense?
12 A. If the cost --
13 Q. Ten percent, excuse me. What would be the
14 total interest expense?
15 A. Five, \$5.
16 Q. Assume that you used a 2.6 pre-tax interest
17 coverage.
18 A. Yes.
19 Q. What would the minimum earnings before
20 income tax be in that hypothetical?
21 A. Thirteen dollars.
22 Q. How did you derive that?
23 A. I multiplied 2.6 times \$5, the interest
24 expense, and that's \$13.
25 Q. Now, let's assume you have a utility

01083

1 financed exclusively with debt and one hundred
2 percent debt ratio and the same total plant. How
3 much total debt would there be for that company?

4 A. A hundred dollars.

5 Q. Assuming the same 10 percent interest rate,
6 what would be the interest expense?

7 A. Ten dollars.

8 Q. In order to produce the same earnings
9 before income tax of \$13 for that utility, what would
10 the pre-tax coverage ratio be?

11 A. One point three, because 1.3 times \$10
12 equals \$13.

13 Q. Does that demonstrate that any analysis of
14 pre-tax coverage should consider the effects of total
15 debt on the utility's books?

16 A. Well, what it really shows is that, for all
17 intents and purposes, my 1.5 recommendation is --
18 if you assume a 50/50 capital structure, for all
19 intents and purposes, produces the same amount of EBIT,
20 or earnings before interest and taxes, that would be
21 equivalent to 3.0. So it's a -- it takes into
22 account implicitly the fact that this company has no
23 equity, in terms of providing a level of earnings to
24 support debt.

25 MR. TROTTER: I have nothing further.

01084

1 Thank you.

2 JUDGE WALLIS: Is there further
3 examination?

4 MR. MARSHALL: Yes, Your Honor.

5

6 R E C R O S S - E X A M I N A T I O N

7 BY MR. MARSHALL:

8 Q. Mr. Elgin, in terms of capital at risk, the
9 two owners of Olympic have approximately \$97 million
10 of loans to Olympic, do they not?

11 A. Yes.

12 Q. And that's all capital at risk; is that not
13 true?

14 A. Yes, it's money that they've loaned to
15 Olympic.

16 Q. And whether that was in terms of equity or
17 loans, capital at risk means what you have into the
18 company. So if the company doesn't do well, that's
19 at risk; true?

20 A. That's -- that was my answer to the
21 Chairwoman's question.

22 Q. And of that \$97 million, is any of it
23 secured, to your knowledge?

24 A. No, it's unsecured.

25 Q. So everybody comes ahead of that that might

01085

1 have security or other claims prior?

2 MR. TROTTER: I'll object to the question
3 to the extent it assumes that equity owners would
4 come prior to that.

5 Q. No, okay. Equity holders wouldn't come
6 prior to that?

7 A. No, they would not.

8 Q. So the two owners wouldn't come prior to
9 themselves in this hypothetical, would they?

10 A. No, they are unsecured creditors, and to
11 the extent that there is creditors that have
12 security, they would come first.

13 Q. So in terms of capital at risk, it doesn't
14 matter to them whether it's equity or a loan, from
15 the standpoint of what they have to lose?

16 A. To them, it doesn't matter, but to
17 ratepayers, it makes a difference.

18 Q. And to ratepayers, it makes a difference
19 because they have less capital at risk?

20 A. No, because of the cost to them, and in
21 terms of what is -- what an equity owner has invested
22 and what his interest is in the company. Equity
23 capital, because of the higher return, assumes risks,
24 and it could be because they get the higher risk, the
25 higher rate of return, they accept the risk that they

01086

1 could lose their entire investment.

2 Q. And they could lose the entire loan?

3 A. That's -- that may well be, but --

4 Q. Any --

5 A. But let me -- they could lose the entire
6 loan, but there are approximately a hundred million
7 dollars of investments, facilities on the books. So
8 in a receivership, they would have equal entitlement
9 to all those facilities as any other unsecured
10 creditor, whereas an equity owner may not have any
11 entitlement to anything.

12 Q. Are there any other unsecured creditors you
13 know of?

14 A. No.

15 Q. Okay. You just said equity costs more than
16 debt?

17 A. That's correct.

18 Q. So financing this through equity, not
19 having any dividends go to the owners, is actually a
20 less expensive way for an interim basis, isn't it?

21 A. I don't understand your question.

22 Q. Well, equity owners are entitled to more of
23 a premium on their investment than just mere debt in
24 a typical case; right?

25 A. Typically, equity investors get a higher

01087

1 rate of return than debt investors because of their
2 secondary position on the claim of the assets.

3 Q. Right. And do you know, how many basis points
4 are we talking about here in general, between debt
5 and equity, in terms of higher rates of return
6 generally allowed?

7 A. Well, the -- it can range, depending on the
8 enterprise, it can range from anywhere from very
9 small premiums to very large premiums. Depends on
10 the enterprise.

11 Q. So the current applications before the
12 Commission now, I know those haven't been ruled on,
13 what are utilities asking for in rate of return on
14 their equity today, this year?

15 A. They're asking for 13 and a half to 14
16 percent, the energy companies.

17 Q. Roughly double the seven percent that's the
18 highest note interest that you have here in this
19 case; is that true?

20 A. That's correct math.

21 Q. And you would agree that there haven't been
22 any dividends paid by this company since 1997 to
23 their shareholders; is that correct?

24 MR. BRENA: Asked and answered.

25 JUDGE WALLIS: The witness may respond.

01088

1 THE WITNESS: Well, I don't know why you
2 would -- why the company would want to limit it to
3 just that time period. If you want to go back, let's
4 go back --

5 Q. I'm just asking if there -- isn't it
6 correct that there have not been any dividends paid
7 since 1997?

8 A. That's correct.

9 Q. There have been rate cases since that time;
10 correct?

11 A. By Olympic?

12 Q. By Olympic?

13 A. There's been the -- if you would call what
14 happened in 1998, when Bayview -- Bayview went into
15 service, that would be a rate application. I
16 wouldn't characterize that as a rate case. But there
17 has been a change in rates when Bayview went into
18 service.

19 Q. And at that time, people -- and you say
20 you're concerned about the intervenor types here --
21 could have intervened and asked about all these
22 things we're talking about today?

23 MR. TROTTER: I'll object, Your Honor.

24 This is way beyond anything Mr. Elgin has testified
25 to, and his speculation on what intervenors might or

01089

1 might not have done is adding nothing to this record.

2 MR. MARSHALL: I'm going to get to the
3 specifics of Cross Cascades and Bayview after this
4 question is answered.

5 JUDGE WALLIS: Well, I'm concerned also
6 that it's speculative and of questionable relevance,
7 so I think we should not ask the witness to respond
8 to it.

9 Q. Let's talk about Cross Cascades for a
10 moment. Are you aware that the Cross Cascades
11 project was supported by the shippers and they -- the
12 shippers, including intervenors here, Tosco and
13 predecessors of Tesoro, had signed throughput and
14 deficiency agreements to support and finance debt and
15 encourage Olympic to go out and obtain the debt to
16 start that project?

17 A. I'll accept your representation that that
18 is what they did. I have no knowledge of that.

19 Q. Well, if -- have you ever had a situation
20 in an interim case where some of the people
21 protesting the interim case were also associated with
22 encouraging the debt that they now want to disregard?

23 A. I don't think that that's a fair
24 characterization of what the shippers are doing in
25 this proceeding. I --

01090

1 Q. They don't want to disregard the debt
2 associated with Cross Cascade in the coverage
3 analysis that you have?

4 A. No, it's the analysis that I did. I'm not
5 saying that -- I'm saying, for purposes of interim,
6 we're not providing it in our calculation, but I
7 don't think that --

8 Q. Would it be a relevant factor to you if
9 people who are intervening in the case and protesting
10 interim rate relief were in part responsible for the
11 incurring of large amounts of debt for a project?

12 MR. BRENA: I object to this whole line of
13 questioning. First of all, there's no evidence in
14 the record whatsoever that Tesoro encouraged this at
15 all. I noticed that he modified it to say Tesoro's
16 successor. Tesoro is the intervenor here, so there
17 isn't any foundation for that.

18 Secondly, this is beyond the scope of his
19 testimony, beyond the scope of his knowledge with
20 regard to these matters, so -- and I don't see that
21 it's at all relevant if a shipper stands up on top of
22 the Seattle Tower, screaming, Go borrow the money, go
23 borrow the money. That has nothing to do with the
24 rate treatment that should be afforded to the
25 ultimate expenditure and with regard to whether it's

01091

1 prudently incurred.

2 MR. MARSHALL: That's why I think it is
3 relevant, Your Honor. I think that if shippers have
4 encouraged projects and have participated in that,
5 they need to step up and assume some of the
6 responsibility for the associated debt.

7 JUDGE WALLIS: My sense is that, to the
8 extent that is your position, that the position has
9 been made clear. If you want to argue that, you're
10 free to do that. The witness apparently has no
11 independent knowledge of that, and there may well be
12 a question of relevance.

13 Q. Have you gone back through the prior rate
14 case filings for Olympic to understand how the Cross
15 Cascade project got going?

16 A. No, but I have been through the past
17 financial statements of the company, and I was quite
18 surprised to see how the company capitalized itself
19 and how it conducted its finances and managed its
20 balance sheet through the period 1990 to the present.
21 But I've not done specifically any analysis on the
22 rate case.

23 Q. So your testimony is you have not looked at
24 any of the rate case filings prior to this case in
25 the Commission's files?

01092

1 A. That's correct.

2 Q. Including any of Mr. Colbo's analysis from
3 1983 onward?

4 A. I have had no need to. I have not.

5 Q. So did you look at the rate tariff with
6 respect to Bayview, other than when it occurred in
7 Mr. Batch's testimony, which I believe was Exhibit --

8 A. Fourteen.

9 Q. -- 14? That's the only one you looked at?

10 A. For purposes of this cross, I don't
11 remember -- I've looked at so much stuff in this
12 case, it's just -- it's been quite overwhelming, so I
13 can't say specifically. I know I've seen some things
14 related to Bayview, but I have not specifically gone
15 down to the Commission's Record Center and the Staff
16 work papers and pulled out the work papers and
17 analyzed them. I have not done that. I have -- what
18 I have done is gone back and looked at the company's
19 financial statements and books since 1990, its FERC
20 Form Sixes.

21 Q. So are you aware that there have been cases
22 before this Commission, tariff cases, from 1983 on
23 regarding Olympic Pipe Line?

24 MR. TROTTER: Your Honor, I'll object to
25 the characterization of a case. There have been

01093

1 filings and they've been resolved without suspension.
2 That doesn't constitute a case.

3 Q. Have you been aware that, since 1983, there
4 have been filings asking the Commission to approve
5 tariffs on behalf of Olympic since 1983?

6 A. Yes, I am aware. And then the financial
7 consequences of those tariffs and the revenues and
8 expenses that would produce would be reflected in the
9 company's financial statements that are on file that
10 I have analyzed since 1990.

11 Q. Now, have you known, since the Commission
12 has analyzed since 1983, the fact that the FERC
13 methodology produces a different outcome than the
14 traditional utility for essential services?

15 MR. TROTTER: Your Honor, I'm going to
16 object. It's been very clearly stated so far no
17 party is -- that the FERC methodology is not
18 relevant. No one's recommending it be adopted in
19 this phase of the proceeding, it hasn't been used in
20 this phase of the proceeding. This may be relevant
21 to the next phase. I'll object to it being asked
22 about now.

23 JUDGE WALLIS: Mr. Marshall.

24 MR. MARSHALL: Oh, yes. What I want to
25 establish, and we'll get to that in a minute, that

01094

1 what has been done in the past with regard to FERC
2 methodology and the overall financing methodologies
3 used by oil pipeline companies is distinct, unique,
4 and therefore I'm just trying to get this witness'
5 background on whether he knows that the two different
6 methodologies produce a different result and that the
7 Staff has analyzed that since 1983.

8 JUDGE WALLIS: What is the relevance to
9 this inquiry?

10 MR. MARSHALL: Again, I think the relevance
11 will be shown in another couple of connecting
12 questions. All I really want to know is does he know
13 that distinction, that difference. It's a yes or no
14 answer.

15 MR. TROTTER: Your Honor, part of the
16 problem here is that the Commission allowed those
17 tariffs to go into effect. There's no finding of
18 fact by this Commission that FERC methodology is
19 appropriate, there's no conclusion of law finding
20 that the FERC methodology, which has changed over
21 time, is appropriate, and so I don't even know what a
22 FERC financing methodology is, quite frankly, having
23 read FERC orders. But it's not an issue in this
24 phase, period. I'll object for that reason.

25 MR. MARSHALL: I'll move on. Maybe I can

01095

1 come back to this after I tie it up here.

2 Q. In a question asked by the Chair, you
3 mentioned that you recommended a level that, in your
4 view, would not try to solve it all right now, it
5 would not completely fund the 2002 capital budget.
6 Do you remember those statements in general?

7 A. I don't believe that was my testimony at
8 all. I didn't say anything about completely funding
9 the 2002 capital budget. I think that -- I don't
10 recall that testimony at all.

11 Q. Do you recall the testimony where you said
12 let's not try to solve it all right now?

13 A. That I do recall.

14 Q. And what did you mean by that?

15 A. What I meant was that the Staff
16 recommendation is an effort to -- I use the phrase a
17 light at the end of the tunnel. It's so that the
18 company could possibly go forward with a pro forma
19 financial statement that could show improved
20 earnings, that could show ability to service debt,
21 that could possibly get an unqualified financial
22 opinion, and reasonably make an effort to tie the
23 relief to an ability to finance so that Mr. Fox could
24 make that call and secure the additional financing
25 available under the revolving line of credit. I

01096

1 believe that was my testimony.

2 Q. Do you also recall saying that you did not
3 want to provide a level of rate relief for the
4 interim that would, quote, completely fund the 2002
5 capital budget?

6 A. Yes, I believe that the 60 percent increase
7 that the company's asking for, coupled with what
8 they've requested at FERC, would ostensibly do that.

9 Q. Okay. Let's break that down. The amount
10 that they got from FERC is -- how much do you have in
11 mind when you gave that answer? Let's just assume 14
12 million, subject to check. Close enough for this.
13 And your thought was that the WUTC amount would be
14 around nine million. So you add the two together and
15 you get 23. Is that roughly your idea?

16 A. Yes.

17 Q. Okay. Now, that's for a full year;
18 correct?

19 A. Yes.

20 Q. And we're talking about interim relief for
21 a half a year; correct?

22 A. No, we're talking about interim relief as a
23 total.

24 Q. Up until August 1st?

25 A. Yes.

01097

1 Q. Okay. That's half a year from now?

2 A. Right.

3 Q. Okay.

4 A. And rateably, I would think that the
5 capital program would be rateably -- mirror the same
6 time frame. That would be my assumption.

7 Q. So it wouldn't be 23; it would be half of
8 that that you're talking about for half a year?

9 A. Right.

10 Q. Okay. In that example, when you referred
11 to this in your testimony, you were relying on the
12 FERC interim part, the \$14 million, giving that
13 answer; true?

14 A. Well, of course.

15 Q. Right. And --

16 MR. TROTTER: Excuse me, Your Honor. The
17 witness should be able to explain his answer.

18 Q. Is there any further explanation?

19 A. Well, that's precisely what our analysis
20 did, is we had the FERC jurisdiction stand on its own
21 and, for purposes of calculating our level of
22 interim, we removed the FERC increase.

23 Q. Now --

24 A. So Washington is providing its share, which
25 I believe is the fair amount, to go forward.

01098

1 Q. So FERC is providing 14 million, and what
2 is the share that you're going to provide for the
3 intrastate share?

4 A. Well, I think you're mischaracterizing what
5 my testimony is, Mr. Marshall. What I'm saying is
6 that we've removed the FERC jurisdiction amount --

7 Q. Okay.

8 A. -- and put the total company, and then
9 allocated a Washington portion based on my
10 methodology.

11 Q. On the 23 million, if FERC puts in 14,
12 what's your recommendation going to do for the
13 intrastate part? How much?

14 A. I don't understand your question.

15 Q. How much are you recommending in total
16 dollars between now and August 1st for interim if you
17 have your nearly 20 percent amount? Do you know?

18 A. Well, on an annual basis, it's -- I don't
19 have Mr. Colbo's exhibit right in front of me. It's
20 a 20 percent increase, approximately.

21 Q. A 60 percent increase gets you nine million
22 and 20 percent increase gets you how much?

23 A. Well, if it's rateable, about 1.8 million.

24 MR. TROTTER: Excuse me, Your Honor. Could
25 I just direct the witness to the first page -- the

01099

1 first page of his testimony has the number. Maybe we
2 could short-circuit this a bit. Just refer to page
3 one, line 18.

4 And also, I'm going to object to this line
5 of questioning. This could all have been asked on
6 the initial round. It's all been in the testimony.
7 We're just getting highly repetitive of the direct
8 case at this point, so I'm going to object.

9 MR. MARSHALL: Well, I think this goes to
10 the whole statement that Mr. Elgin has made, that
11 they're not relying on FERC money in any way, shape
12 or form. And we're going to go -- this goes to that
13 attempt, to try to distinguish the two, which I don't
14 think that distinction works.

15 MR. TROTTER: But, Your Honor, he's
16 testified and Mr. Colbo will testify we pulled out
17 the FERC revenue, so we're not relying on what FERC
18 has done. The Staff could have said they're getting
19 that money, let's include it in our analysis of the
20 financials. They didn't do that, in order to have
21 the state stand on its own.

22 That's been asked and answered numerous
23 times, and any suggestion to the contrary is false.
24 So I don't know what point is being advanced. The
25 relevance of this line of inquiry has yet to be

01100

1 demonstrated.

2 JUDGE WALLIS: Mr. Marshall, you may

3 continue.

4 Q. So if the Commission were to grant your
5 recommendation of 20 percent, how much would that
6 provide toward the \$23 million of -- basically, of
7 the 2002 capital budget that you added up a moment
8 ago?

9 A. It would provide -- just that piece would
10 provide, rateably, half of 2.7 million or 1.35
11 million, and that does -- that amount alone, in terms
12 of the Staff analysis, has to be considered in the
13 context of all the other adjustments and the critical
14 factor that the throughput of the company is
15 increasing.

16 Q. Okay. So --

17 A. So it's not that -- you cannot just say
18 that -- the problem I'm having with your testimony is
19 that you're trying to characterize it as saying only
20 the piece that we're recommending goes to the capital
21 budget, and that's a faulty assumption, and that's
22 the premise of your question, and that's incorrect.

23 Q. I'm working from the premise of your
24 response, which said that if you gave the full
25 amount, that would then completely take care of the

01101

1 2002 capital budget. So I'm inquiring into that,
2 so --

3 MR. TROTTER: I'll object, Your Honor.
4 That was not Staff's testimony.

5 JUDGE WALLIS: Mr. Marshall, I don't
6 believe that that correctly characterizes the
7 witness' testimony.

8 Q. In any event, rather than \$9 million
9 available from the state in intrastate rates, you
10 would only have 1.3 million available under your
11 recommendation; is that correct?

12 A. No, you're mixing apples and oranges again,
13 Mr. Marshall.

14 Q. Instead of \$9 million, as requested by the
15 company, your recommendation would provide 1.3; is
16 that true?

17 A. No, it's not true. That's not what we're
18 saying.

19 Q. What's the total amount that your
20 recommendation produces?

21 A. On an annual basis, it would produce 2.719
22 million. Rateably, over six months, it would produce
23 half of that, assuming that that's how the system
24 would operate. You know, half of the throughput
25 would go between now and when the general rate would

01102

1 be determined.

2 Q. Now, as to the facilities in the 2002
3 capital budget, have you gone through to determine
4 which facilities can be separated from intrastate
5 versus interstate, or do many of the facilities, and
6 perhaps the largest majority of facilities, serve
7 both interstate and intrastate products?

8 A. I would -- I would expect that none of them
9 could be identified as purely intrastate, that they
10 would almost all be for -- support both operations.

11 Q. So to support the 2002 capital budget or
12 anything else, the people paying interstate rates are
13 providing full support at the 60 percent level; is
14 that a fair statement right now?

15 A. No.

16 Q. Starting in September?

17 A. No, it's not. They're paying a rate
18 subject to refund, and it may well be an excessive
19 rate.

20 Q. So assuming it doesn't get refunded.

21 A. Hypothetically.

22 Q. They are paying for their full 60 percent
23 share, if you want, they have a rate increase right
24 now going toward capital and operating and wherever's
25 it's going; true?

01103

1 A. If that's a fair rate, yes.

2 Q. And you're right, it could be subject to
3 refund.

4 A. It's not could be; it is.

5 Q. Well, it could be refunded. It's subject
6 to refund?

7 A. Yes.

8 Q. I'll go with you on that. We'll get to
9 that part in a minute.

10 A. Okay.

11 Q. Since September of this past year,
12 testimony has been from the intervenors that
13 Olympic's prospects and financial condition is
14 improving, and that's composed of the two parts,
15 right, the increased throughput and the FERC rates?
16 Look at the financial statements. Do you find that
17 FERC rate built into the -- when you multiply that by
18 the throughput?

19 MR. BRENA: Objection. He is now
20 cross-examining this witness not on his testimony,
21 either live or written; he's cross-examining this
22 witness on the other intervenors' testimony.

23 Q. Let me rephrase that. When you say that
24 the financial condition of Olympic is improving, did
25 you mean to say it's improving if you disregard the

01104

1 FERC rates?

2 A. Yes, that is the Staff analysis. Mr.
3 Colbo's analysis shows that unequivocally.

4 Q. And that's because throughput is increased
5 a little bit?

6 A. A little bit. Substantially. It's -- the
7 company is at a 91 percent utilization factor, where,
8 before it went up to that, it was, for all intents and
9 purposes, shut down. It's not -- it's just a
10 dramatic change in the operation of that facility.

11 Q. And if you take out the FERC rates for the
12 last three months of last year, you don't get a
13 positive income; you get losses continuing, don't
14 you?

15 A. I don't have that analysis. I can't
16 respond. I can tell you what Mr. Colbo's analysis
17 shows, is if you take out the FERC rate and you apply
18 our recommended increase, the company earns on its
19 facilities approximately one and a half times its
20 interest expense on those facilities, and that's what
21 we did. We've taken it out.

22 It's a very conservative analysis to
23 recognize the fact that, if you will, that the
24 financial condition of Olympic is turning around and
25 heading back up because of increased throughput. And

01105

1 if you want to know exactly how that adjustment was
2 made, I think Mr. Colbo is the right person to talk
3 to with that.

4 Q. Can you say, even subject to check, that
5 the fourth quarter 2001 cash flow with FERC increase
6 is a negative four and a half million, and without
7 the FERC increase, is a negative 7.7 million?

8 A. Let me tell you what I can.

9 Q. If you can't say that, just say, I don't
10 know, and then we'll move on.

11 A. Okay. I don't know.

12 Q. Do you know what the cash flow is of
13 Olympic for the fourth quarter 2001?

14 A. Well, that's what I was about to go to. It
15 looks to me -- it appears to me, from Exhibit 27,
16 that but for -- ah, here it is. Page two of five.
17 But for casualty and the other losses in the 2001
18 test period, but for the way the company's booked
19 these casualty and other losses, which I assume are
20 exclusively related to Whatcom Creek, and that
21 includes six months when the pipeline was down, for
22 all intents and purpose, the company had no -- was in
23 a break-even position, that -- so that that would
24 tell me that if you would take out the first six
25 months, that, on a going forward basis, the company

01106

1 would have positive cash flow but for the booking of
2 the Whatcom Creek. That's what Exhibit 27, page two
3 tells me.

4 Q. My question was fourth quarter 2001, do you
5 know what the cash flow is on that? Not what's
6 booked, but --

7 A. Wait a second.

8 Q. Not what's booked, but what --

9 A. You've asked the question. Give me a
10 chance here to pull these figures together, okay.

11 Q. Just trying to make sure you understand.

12 JUDGE WALLIS: Mr. Marshall.

13 THE WITNESS: In the fourth quarter,
14 Exhibit 27, page two of five, tells me that, but for
15 Whatcom Creek, the company has positive cash flow.
16 And that, I was adding figures in my head. That's
17 the best I can do on the stand pulling these figures
18 together.

19 Q. So when you refer to their improving
20 financial condition, you refer to pulling out, at
21 least mentally, in your mind, Whatcom Creek?

22 A. Yes, because the company's own testimony
23 says that for purposes of both the interim and the
24 general rate case, they're not asking for any
25 recovery of Whatcom Creek.

01107

1 Q. Does that exhibit have December on it?

2 A. Yes, it does.

3 MR. TROTTER: Your Honor, if I might, could
4 we have a recess? The witness has been on the stand
5 now for a long time, and maybe this will give Counsel
6 an opportunity to perhaps consider where they want to
7 go from here.

8 JUDGE WALLIS: Very well. Let's take our
9 afternoon recess at this time. I think we should be
10 conscious of the ground that we have yet to cover and
11 the time that we have available to do it in.

12 (Recess taken.)

13 JUDGE WALLIS: Let's be back on the record,
14 please, following a brief recess. Mr. Elgin, you've
15 noticed a typographical error in one of the
16 documents; is that correct?

17 THE WITNESS: Yes. When I previously was
18 asked a question about when Olympic Pipe Line's
19 Bayview terminal went into service, the Staff
20 memorandum indicated January 27th, 1998, and that
21 should be January 27th, 1999.

22 JUDGE WALLIS: Thank you, Mr. Elgin.

23 THE WITNESS: You're welcome.

24 MR. MARSHALL: We could, if the Commission
25 wants, put in the actual, actual date that it went

01108

1 into service and provide other details. I know this
2 Bayview issue has come up kind of late in the game,
3 but it's just up to the Commission.

4 JUDGE WALLIS: If any different -- if you
5 believe that any difference in date from the date
6 mentioned in the Staff memo, as corrected, would be
7 significant to the Commission in its decision, then
8 you may offer the correction.

9 MR. MARSHALL: It's an earlier date. I
10 don't know how significant it is. I'll consult.
11 Okay. It's December of '98, so it's not that
12 significant.

13 JUDGE WALLIS: Very well. Mr. Marshall,
14 are you ready to proceed?

15 MR. MARSHALL: I am.

16 Q. We were last referring to Exhibit 27, and
17 that, I believe, is based on estimates for the last
18 couple of months of 2001; is that correct?

19 A. Yes, I believe it has estimates for
20 November 1st and December 1st.

21 Q. Okay. And of course, as those financials
22 -- as the books are closed for the end of the year,
23 and all those financials will come in as actuals,
24 rather than estimates?

25 A. Correct.

01109

1 Q. Okay. Now, we were talking about whether
2 the system could be divided in terms of its component
3 parts between things devoted just to interstate
4 versus intrastate. You said you didn't believe that
5 they could be divided up.

6 When you're trying to do a capital project
7 requiring an investment for 2002, and you have some
8 FERC money that's available subject to refund and you
9 have some Commission money at an amount that's at a
10 percentage less, assuming that your recommendation is
11 followed through, does that create a concern of yours
12 that the intrastate shippers are relying on
13 interstate shippers to accomplish that project? Is
14 there a jurisdictional question and a potential
15 federalism issue involved in that situation?

16 MR. TROTTER: I'll object to the question,
17 to the extent it calls for legal conclusion.

18 Q. Or do you know?

19 JUDGE WALLIS: Mr. Marshall, may we assume
20 in your question that you're not asking for a legal
21 conclusion on the part of the witness?

22 MR. MARSHALL: Yes, that's correct.

23 THE WITNESS: In my opinion, it does not.
24 We do this all the time in utility rate-makings, is
25 we separate both interstate and intrastate, and as

01110

1 well as between all kinds of jurisdictions. It's not
2 uncommon and I don't believe it involves any issue of
3 federalism. In fact, my reading of some of the case
4 law in the pipelines and some of the rate cases that
5 came out is that there is always a difference between
6 how the federal government makes rates and state
7 commissions make rates for oil pipelines. So it's
8 not uncommon to see that result.

9 Q. Let's just focus on interim rate cases.
10 Mr. Brena asked you a series of questions about what
11 would give you a concern in an interim case. Have
12 you -- first of all, I take it that there have been
13 no interim rate cases involving oil pipelines in
14 Washington State before, so this is new?

15 A. No, and in fact, that was one of the things
16 that I did in my testimony, is an analysis of Title
17 81 and Title 80, to see whether or not what the
18 Commission has done in prior utility cases could
19 reasonably be applied to common carriers operating
20 under Title 81, and -- because there have been no
21 cases.

22 Q. And in any of the other cases, had there
23 ever been a situation where interim rates have been
24 requested where the federal portion has granted an
25 interim rate and the State of Washington has either

01111

1 not granted an interim rate or granted a lesser
2 interim rate, that you know of?

3 A. Well, first off --

4 Q. Are there --

5 A. -- we've had the --

6 JUDGE WALLIS: Mr. Elgin, could you begin
7 by responding to the direct question that was asked?
8 I believe it called for a yes or no answer.

9 THE WITNESS: Yes, sir. He's -- I can't
10 answer it yes or no, because he's mischaracterizing
11 what FERC does with respect to rates. FERC doesn't
12 have interim rates. So he keeps talking about FERC
13 interim rates, and I can't -- I'm having trouble with
14 those questions, because it's presuming something
15 that isn't there. So that's my difficulty with it.
16 So if he could rephrase the question, I'd be glad to
17 answer it yes or no.

18 Q. Sure. Has there been any situation here in
19 the state of Washington where a federal agency, like
20 the FERC, has given a rate subject to refund at the
21 same time the Commission is considering an interim
22 rate of the same nature, the same type of a system,
23 and comes up with either a lesser amount or no
24 amount?

25 A. I don't know of any and I -- if it

01112

1 happened, it would not be unusual, but I don't know
2 -- your specific question is no, I don't know of any
3 cases.

4 Q. When you say if it happened, it would not
5 be unusual, you know of no cases here in Washington
6 State --

7 A. No.

8 Q. -- where that exists. Now, if somebody
9 wants to make plans for the 2002 capital budget, and
10 let's say do some of the things that are listed in --
11 I believe Mr. Batch has an exhibit. Can you refer to
12 Exhibit 10 and turn to the last few pages of that,
13 where you'll find a listing of all of the capital
14 improvement budget items for 2002? Are you familiar
15 with that exhibit?

16 A. Yes.

17 Q. And you've reviewed that exhibit?

18 A. Yes.

19 Q. Yes. So that goes through and --

20 A. This -- I think this is the same exhibit
21 that was prepared when -- in response to the request
22 from Staff to produce such a document, as I recall,
23 or something similar to this.

24 Q. Well, I'm asking you to take a look at the
25 last seven pages, which is called Tab Three in that

01113

1 exhibit.

2 A. Yes, I have that.

3 Q. Okay. Actually, I have an easier copy for
4 people to take a look at. It's the same thing. Why
5 don't you hand that out, if you wouldn't mind. It
6 might be easier to refer to that. The copy that we
7 have in our witness notebook is not as clear as the
8 copy here, so that might aid everybody in looking at
9 this.

10 MR. BRENA: If I may.

11 JUDGE WALLIS: Mr. Brena.

12 MR. BRENA: The copies which -- well, go
13 ahead.

14 MR. MARSHALL: So if you look at various
15 valve upgrades that are partially related to, say,
16 corrective action orders on this, if you were to try
17 to start getting permits and start ordering the parts
18 and so forth, in order to do this in 2002, you'd
19 pretty much have to do this -- now, there's a window
20 of time to start getting permits and order materials
21 to do the things in 2002. Is that a fair statement
22 of general ways that construction and capital budgets
23 are done?

24 A. I wouldn't know how that would be done for
25 this particular company.

01114

1 Q. Does that sound reasonable?

2 A. I mean, if the company would have provided
3 something, that would have given me an opportunity to
4 analyze that, yes, but I don't know.

5 MR. TROTTER: Your Honor, I'm going to
6 object at this point. This is re-cross, Your Honor.
7 Mr. Marshall had his turn yesterday, and now this is
8 whole new areas that he could have crossed on
9 yesterday and elected not to.

10 Mr. Elgin has not got into the details of
11 permitting for any valve replacement or otherwise.
12 He asked the company, he suggested the company had a
13 burden in which it prove what was essential and what
14 could be deferred and come up with some plan for
15 dealing with an alleged financial emergency, and they
16 didn't produce it. That's all he's saying.

17 Now we're being treated to this. I'm going
18 to object and ask this line of questioning be
19 terminated.

20 MR. BRENA: And may I join in the objection
21 and point out that we have three more witnesses to go
22 today, and this witness. So I mean, I'm going to try
23 to make my questions just as focused as I possibly
24 can, and so allowing more in that isn't within the
25 appropriate scope of the line of questioning seems to

01115

1 me to be a little much at this point. I don't want
2 my witnesses on at 11:00 at night.

3 JUDGE WALLIS: Mr. Marshall.

4 MR. MARSHALL: There were a number of
5 questions asked by the Commissioners on what was
6 essential and what was necessary, what was the
7 timing, and whether the Commission Staff was relying
8 in part on money from the FERC. This is just going
9 to those issues.

10 And I'm not trying to redo things. I'm
11 trying to clarify, first, that there is a relevance
12 and has to be, out of necessity, on the FERC monies.
13 Second, in response to what things were necessary,
14 this exhibit, which was provided in the rebuttal
15 testimony, 3-T, was in fact provided, was reviewed by
16 Mr. Elgin. Mr. Batch wasn't asked any questions at
17 all about this exhibit when he was up.

18 But it shows what's essential and it also
19 proves the point that these are combined largely
20 between intrastate and interstate projects. So I
21 think it's fair to ask Mr. Elgin now to clarify what
22 he's just testified to in response earlier today.

23 JUDGE WALLIS: Very well. You may
24 continue.

25 Q. So is it fair to assume that if you're

01116

1 going to start these projects and get them finished
2 in 2002, you're going to have to get them going and
3 you're going to have to rely on some amount of money
4 from someplace to do that, if they're going to be
5 done?

6 A. Yes.

7 Q. And are you familiar with 49 CFR 195.450,
8 for example? Have you looked at those federal
9 standards?

10 A. No, no.

11 Q. So when you say you reviewed this document,
12 you have not made a review of the material that's
13 been presented to you in the testimony of Mr. Batch
14 insofar as what things are required and what things
15 are not by law?

16 A. No. Again, I think that's a
17 mischaracterization of my testimony. What my
18 testimony said was that the company's affirmative
19 case did not make that assessment as to what was
20 essential, and it wasn't until Staff went and asked
21 for this information was it eventually produced, and
22 then I relied on these figures for the 2001 figures
23 that was provided to Staff, and then subsequently
24 used those in my calculation of a recommended
25 increase.

01117

1 So I think that you're making out my
2 testimony to be something that it is not by going
3 through this.

4 Q. Perhaps I did misapprehend your testimony
5 when you said that you didn't think the company had
6 proven what was essential or necessary, but
7 apparently it has in this exhibit, would you agree?

8 A. Again, you've mischaracterized my
9 testimony, Mr. Marshall. I would direct you to page
10 10, Q&A that begins on line 10.

11 CHAIRWOMAN SHOWALTER: Of which exhibit?

12 THE WITNESS: Exhibit 131-T. The question
13 says, In your opinion, does Olympic's direct
14 testimony provide support for its request for interim
15 relief similar to that provided in Cause Number
16 U-8111? And I said, No.

17 Q. Then you --

18 A. Then you asked the question, What would the
19 company have to provide to provide such analysis,
20 because the company said 8111 is the authority, and
21 we are like 8111, provide us the interim relief.

22 And I said the answer, which begins on line
23 11, An 8111 analysis would provide these -- the
24 company, in its direct case, would have been required
25 to provide these types of things. That's what my

01118

1 testimony is.

2 Q. And so Mr. Batch, if you would turn to
3 Exhibit 3-T, at page three -- do you have that in
4 front of you, Mr. Batch's Exhibit 3-T?

5 A. Yes.

6 Q. He quotes from your page 10, just that
7 statement, and then proceeds on for the next several
8 pages to explain what's prudent, necessary,
9 essential, and to that, attaches, at page eight,
10 Exhibit Number 10, which is identified here as BCB
11 24; is that correct?

12 A. That's what he has done. He's attempted to
13 take one piece and show that the expenditures for
14 2002 are essential. That's -- in its rebuttal case,
15 is what he's done. That's --

16 Q. Mr. Batch is available for
17 cross-examination on this exhibit. Was there
18 anything in here that you thought you should ask Mr.
19 Batch that was not necessary or essential in 2002
20 capital budget?

21 A. No, and I did not take exception to any of
22 the items. I think what you've done is
23 mischaracterized my testimony and then tried to
24 create something that isn't there, is what I'm
25 saying.

01119

1 Q. But I didn't intend to mischaracterize your
2 testimony. I thought that I heard you say that the
3 company had not proven, but now you're suggesting --

4 MR. TROTTER: Excuse me, Your Honor. I'm
5 going to object to the colloquy. Could we just have
6 questions, please?

7 MR. MARSHALL: Fair enough.

8 MR. TROTTER: I'll ask that Counsel be
9 directed to ask questions, or not.

10 Q. There was, in that same testimony by Mr.
11 Batch, in 3-T, the idea that expenditures relating to
12 increasing the throughput could be deferred.

13 A. I heard him say that.

14 Q. Does Staff recommend that any of those
15 items with regard to increasing throughput should be
16 deferred?

17 A. We're not making any recommendations about
18 anything to be deferred. That's not our case. I
19 don't know where I've testified to that or any member
20 of Staff. We're not saying that something has to be
21 deferred.

22 Q. Well, let me just ask you straight out. Do
23 you think that it's a prudent and wise idea to do all
24 that could be done in the 2002 capital budget with
25 regard to increasing throughput, even if it's not

01120

1 required by a federal, state, or local law?

2 A. If -- I guess if the company can manage its
3 cash without a 60 percent increase and do other
4 things necessary to get to that point, that would be
5 a prudent thing to do. It may not.

6 Q. Okay. So it wouldn't be prudent to do if
7 we didn't get a 60 percent increase; is that the
8 reverse of what you just said?

9 A. No, I don't believe that's what I said at
10 all.

11 Q. Okay. Now, in the Avista testimony -- you
12 referred to your testimony in the Avista case here
13 just a little bit ago. Do you recall that?

14 MR. TROTTER: I'll object. I asked whether
15 he testified in the Avista case. I didn't refer to
16 his testimony, but rather his understanding of the
17 evidence in that case.

18 Q. Okay. You referred to the evidence that
19 you presented in that case?

20 A. Yes.

21 Q. And you presented evidence that Avista
22 might not be able to get all of its requested
23 increase because of the potential for rate shock. Do
24 you remember that testimony?

25 A. Yes.

01121

1 Q. Is there any evidence of rate shock in this
2 particular interim request?

3 A. Yes.

4 Q. Rate shock for whom?

5 A. Shippers.

6 Q. Tosco and Tesoro?

7 A. No, all the shippers.

8 Q. And have you, apart from talking to Tosco
9 and Tesoro, have you talked to any shippers that are
10 concerned?

11 A. I've seen an additional letter that voiced
12 concern about the magnitude of the increase from a
13 small shipper, so I would think that any other
14 shipper would share that concern, as well. It's -- a
15 60 percent increase is a dramatic increase, and I
16 think, by anybody's reasonable definition of the term
17 rate shock, that would qualify.

18 Q. And up here on the board, we have what this
19 interim rate increase would be in Mr. Batch's
20 testimony. Do you see that on this chart?

21 A. Yes, we went through that.

22 MR. MARSHALL: Okay. I don't have any
23 further questions.

24 JUDGE WALLIS: Mr. Finklea.

25 MR. FINKLEA: I just have one line of

01122

1 questions.

2 C R O S S - E X A M I N A T I O N

3 BY MR. FINKLEA:

4 Q. You were asked some questions by Mr.
5 Marshall about the Cross Cascades project. Allow me
6 a hypothetical where an electric utility proposes to
7 construct a windmill project for new electric
8 generation and a hundred percent of their ratepayers
9 support the project. The utility goes forward with
10 the project, but about halfway through it, abandons
11 the project and the windmill never becomes
12 operational.

13 Under Washington law, is that investment
14 considered an investment that is serving the public?

15 MR. TROTTER: Your Honor, I just have the
16 objection to the extent it calls for a conclusion of
17 law.

18 MR. MARSHALL: And also an objection about
19 assumptions of abandonment and so on. I don't think
20 there's any testimony that the Cross Cascades project
21 was abandoned; just to the contrary. So I don't know
22 where this is going. It's assuming a fact not in
23 evidence.

24 JUDGE WALLIS: Mr. Finklea, do you want to
25 rephrase your question?

01123

1 MR. FINKLEA: Sure, I'll rephrase it.

2 Q. Assume, again, staying with the
3 hypothetical, that the utility gets halfway through
4 the project and then the project isn't completed and
5 the project does not generate electricity. Is the
6 fact that the utility's customers supported the
7 project at the outset relevant to the consideration
8 of whether the project should ever be put in the
9 utility's rate base?

10 A. No, but that doesn't mean necessarily that
11 -- the history of this Commission on plant
12 abandonment is varied and it depends on the magnitude
13 of it, the project. But to actually put it into rate
14 base, it's been the practice of this Commission to
15 not include it in rate base.

16 MR. FINKLEA: That's all I had, Your Honor.

17 JUDGE WALLIS: Mr. Brena.

18 MR. BRENA: Yes. I have some questions,
19 Your Honor.

20

21 R E C R O S S - E X A M I N A T I O N

22 BY MR. BRENA:

23 Q. Mr. Elgin.

24 A. Good afternoon, again.

25 Q. For every question that I'm about to ask, I

01124

1 would like you to assume that the public interest is
2 in allowing Olympic to go forward with its 2002
3 capital improvements. Do you understand the
4 assumption?

5 A. Okay. Yes, I have that.

6 Q. Assuming it's in the public interest to
7 have those improvements done, is it also in the
8 public interest to require the ratepayers fund those
9 in advance simply because the owner is unwilling to?

10 A. Well, no, but we have situations where
11 contributions that aid in construction are deemed
12 appropriate, depending on the circumstance of the
13 capital improvement and the circumstances of specific
14 customers. But as a general proposition, the concept
15 that all ratepayers forward funds to fund capital
16 projects is not in the public interest, is not
17 traditional utility rate-making.

18 And I want to say -- I have so much
19 experience, I just said utility rate-making, but
20 we're dealing with common carriers under Title 81, so
21 -- but I would think that the same practice would
22 apply.

23 Q. Okay. In struggling to find what the
24 balance of the public interest is, not whether the
25 improvements get made, but in who should pay for

01125

1 them, what if 20 percent is too much? Then isn't it
2 fair to characterize the amount that the shippers
3 have been paid as a forced capital contribution to a
4 pipeline in which they have no ownership interest?

5 A. I don't know that I would characterize it
6 that strongly, but I would say that the typical way
7 is for the utility to make the investment and then,
8 once the plant goes into service and the utility does
9 not have sufficient stream of revenues to pay a fair
10 return on and of capital, that a rate application
11 would be made and that the utility would change its
12 rates in order to be given an opportunity to earn a
13 fair return on that investment to serve the public.
14 That's the traditional paradigm.

15 Q. Now, if this Commission decides that the
16 public interest is in having the shippers pay \$24
17 million, the entire \$24 million, so the capital
18 improvements can get made, then isn't it true that
19 the shippers would pay for those same capital
20 improvements twice when they include them in rate
21 base and take depreciation and also pay for a return
22 and a tax allowance on that in the future?

23 A. That would be one way to look at it. The
24 other way to look at it would be the shippers would
25 now have an equity interest. That would be the other

01126

1 alternative.

2 Q. How many times do you think it's in the
3 public interest to have shippers pay for capital
4 improvements, once or twice?

5 A. They pay for it as they use the service and
6 ostensibly they pay for it once.

7 Q. They should pay for it once, shouldn't
8 they?

9 A. Yes.

10 Q. And the problem with deviating from the
11 traditional approach to funding capital improvements
12 is that the shippers pay for the improvements today,
13 but they're also going to be asked to pay for them in
14 the future. Is that a problem that could occur?

15 A. Yes, under your hypothetical, the way you
16 characterized it, I would agree with that.

17 Q. Would you agree that this Commission should
18 deny all emergency relief if it could be demonstrated
19 that Olympic could fund the capital improvements out
20 of their own resources?

21 A. Well, I believe that that's, again, a
22 corollary to the question you just asked me, is that
23 how should -- what's the traditional paradigm for
24 utilities or common carriers to fund capital
25 improvements, and then how shippers or customers pay

01127

1 for services rendered.

2 Q. If I could show you that they could make
3 all of the 2002 capital improvements with no
4 emergency relief, would your recommendation change to
5 that they should be denied emergency relief?

6 MR. MARSHALL: Well, I'd have to object.
7 The time for putting in testimony to that extent has
8 passed. If he wants to ask something specific, then
9 I think he ought to.

10 MR. TROTTER: I will join the objection.
11 It's too speculative, too imprecise to be of use.

12 MR. BRENA: I don't -- this witness was
13 asked a very broad ranging series of questions,
14 primarily by the Madam Chair, in which he was trying
15 to balance what the public interest was and how it
16 should be borne and whether 20 percent was too much
17 or not enough, and so, you know, I'm well within the
18 scope of the questions that this witness has been
19 asked.

20 JUDGE WALLIS: I think the question is
21 permissible and the witness may respond.

22 Q. Do you have the question in mind?

23 A. Yes. As I understand your question, is
24 that if I had evidence that clearly demonstrated the
25 company could access the capital on reasonable terms,

01128

1 that -- and the issue was whether or not it could
2 fund those ongoing projects, my recommendation would
3 change.

4 Q. Okay. Are you aware of Mr. Fox's testimony
5 in which he has proposed that, from the sale of
6 Sea-Tac, that they pay off the entire Prudential debt
7 of \$15 million?

8 A. I read that testimony, yes.

9 Q. Okay. Does it concern you that, in
10 rebuttal, that the company is proposing to pay off
11 \$15 million in debt when the only event of default is
12 that they have unaudited books and records, but
13 they're here requesting, on an emergency basis, four
14 or \$5 million from their shippers?

15 A. Well, I would say that, first off, if they
16 can sell it for that amount and improve their cash
17 flow, that would be something for the Commission to
18 consider. And so at this late date, in the context
19 of how that's factored into the equation, that is
20 something that would be of concern.

21 And again, my testimony and my
22 recommendation is premised on the fact that the only
23 reasonable source of capital, additional capital I
24 see from the company, is that \$20 million revolver
25 under the ARCO promissory note, so that is something

01129

1 new and I have not had sufficient opportunity to put
2 that into my calculus and figure out how that all
3 fits into what I've done in the Staff recommendation.

4 Q. Isn't it reasonable to assume -- wouldn't
5 it be a reasonable position for this Commission to
6 take, why don't you go out and get your books audited
7 so that you comply with the terms of your existing
8 debt and then take that \$11 million that your
9 president has testified will be available in January
10 and apply 40 percent of it to your capital
11 improvements instead of having emergency relief.
12 Wouldn't that be a reasonable position for this
13 Commission to take?

14 MR. MARSHALL: I'm going to object to the
15 question, assuming facts not in evidence. He didn't
16 say that they were going to get any amount of money
17 in January. That is a thing that's being
18 negotiated --

19 MR. BRENA: I would allow the record to
20 speak for itself.

21 MR. MARSHALL: We have to get permission
22 from the Commission to sell these assets, under what
23 circumstances Mr. Trotter gave testimony. This is
24 just one thing that they were looking at in terms of
25 trying to resolve a problem with a Prudential note.

01130

1 So I would object that it mischaracterizes --

2 MR. BRENA: I withdraw the question and --

3 Q. Okay. Assuming that this money becomes
4 available --

5 MR. MARSHALL: May I have a clarification
6 of which money?

7 Q. The Sea-Tac \$11 million. And were you
8 present in the room when Mr. Trotter indicated to Mr.
9 Fox that, under this Commission's policies and
10 regulations and law, that when the ratepayer pays for
11 those funds and -- those facilities and there's gain
12 associated with those facilities, that those are
13 properly credited to the ratepayer?

14 A. Yes, I heard that line of cross-examination
15 from Mr. Trotter and I heard Mr. Fox's response.

16 Q. Now, assuming that that is true, as it
17 stands today, when they sell the Sea-Tac terminal,
18 the gain associated with that sale should go to the
19 ratepayers' benefit, should it not?

20 A. That has been the traditional Staff
21 position and -- in most property -- sale of property
22 cases and when there is a gain.

23 Q. So again, assuming a sale in the first
24 quarter of the next year, we have \$11 million that
25 their case did not take into consideration that

01131

1 should go -- that's ratepayer money that's flowing
2 into this company with zero emergency relief. Would
3 that be correct?

4 A. No, that's --

5 MR. MARSHALL: I object to the question, .
6 even though it sounded like the answer was going to
7 be no, on the basis that it was assuming facts not in
8 evidence, because Mr. Fox --

9 MR. BRENA: I withdraw the question.

10 MR. MARSHALL: -- Mr. Fox said, if that's
11 the case, so we don't want to sell it.

12 JUDGE WALLIS: The question is withdrawn.

13 MR. MARSHALL: We don't have to sell --
14 okay.

15 Q. Now, I heard you mention that you
16 considered, as an assumption in your case, that the
17 only available source of funds was the ARCO revolving
18 line of credit?

19 A. Yes.

20 Q. Did I properly characterize your testimony?
21 Well, why doesn't Mr. Fox make a call to the chairman
22 of Olympic and get the money that they need to make
23 the improvements?

24 MR. MARSHALL: Object, argumentative. He's
25 asking this witness to speculate about some --

01132

1 MR. BRENA: I'll rephrase the question.

2 MR. TROTTER: Your Honor, I'd like to raise
3 an objection here. This is re-cross again, and this
4 could have been raised in the initial round and was
5 not. And I think we're at the point of diminishing
6 returns here, so I'm going to enter an objection.

7 MR. BRENA: It is not re-cross. This
8 witness' specific testimony, in response to a
9 question from Chairwoman Showalter, was is that this
10 was the only reasonable source of funds. That was
11 the first time he used that phrase, and I'm exploring
12 the truth of that phrase.

13 MR. TROTTER: I believe he testified to it
14 earlier, but it's also in his direct.

15 MR. MARSHALL: I would concur with Mr.
16 Trotter's observations.

17 JUDGE WALLIS: We think the area is
18 permissible to explore, and Mr. Brena may continue.

19 Q. Why -- well, do you believe the company has
20 demonstrated that that credit facility is not
21 available?

22 A. No, I think that that's -- that's the one
23 source that's available, and that's where this
24 company will go. And Mr. Fox's testimony did not do
25 anything to convince me to the contrary, that Olympic

01133

1 could not access that additional 20 million. And
2 I've -- I just think that that's where they're going
3 to have to go.

4 Q. Did you consider \$30 million in accounts
5 receivable?

6 A. Indirectly, yes, we did.

7 Q. Is that another source that the company
8 could go?

9 A. Their companies -- I have seen companies
10 that have sold their receivables, but at the same
11 token, the company's payables also have changed over
12 time, so -- but like I've said, we've indirectly
13 connected those, because in our revenue analysis,
14 receivables are just another form of revenue, and
15 it's just a matter of timing for cash purposes, but
16 indirectly we have considered those.

17 Q. But this is a company -- do you agree that
18 the definition of a receivable as a current asset is
19 revenue that's expected within the next 12 months?

20 MR. MARSHALL: Your Honor, this was all
21 gone into with Mr. Fox, and he explained the \$30
22 million.

23 MR. BRENA: Excuse me.

24 MR. MARSHALL: The explanation was there.

25 This witness does not know what's composed of that in

01134

1 detail. Mr. Fox does. I think these are questions
2 that are now argumentative and assuming facts not in
3 evidence and mischaracterizing prior testimony as to
4 what constitutes those receivables, which are mostly
5 just insurance recoveries that Mr. Fox and Mr. Batch
6 testified to in detail.

7 MR. BRENA: The question that I asked the
8 witness is is it his understanding that the
9 definition of receivables was money that would be
10 received within the next 12 months.

11 JUDGE WALLIS: The question is permissible.

12 THE WITNESS: General -- yes, or 12 months
13 or sooner. And also, to the extent that it's booked,
14 it's likely that it will be -- there's a high
15 likelihood that it will be. And if it's not, then it
16 becomes impaired, and the company has an obligation
17 to take it off its books. So there's kind of a
18 two-factor test, the timing and then the likelihood
19 of recovery, and those are things that the company
20 needs to be assessing.

21 Q. Okay. Now, I have a couple questions about
22 Bayview terminal, but I hope just a couple, so if
23 you'll bear with me. You indicated to Commissioner
24 Oshie that the date of that memo is when you
25 considered the Bayview terminal to be in service;

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1 correct?

2 A. Yes.

3 Q. And that date that you corrected was, I
4 believe, January 27th, 1999?

5 A. That was --

6 Q. As corrected?

7 A. Yes, that was the date of the memo, so
8 sometime preceding that, it would have had to have
9 been placed in service, so in that time frame.

10 Q. Well, that's what I wanted to explore. I
11 had shown you Exhibit 25 on page three, which was a
12 report written referring to the first quarter of
13 1999, which was after the Staff memo was written, and
14 it said Bayview was totally tied in and awaiting
15 product availability in the scheduling program.

16 So we -- isn't it fair to say that we have
17 a memo in the record that shows that a few months, at
18 least, after Staff's memo, that it still wasn't in
19 service yet?

20 A. Well, again, what in service means is
21 something that operationally is a question that I'm
22 not prepared to say one way or the other, but what I
23 mean, in service, is it's gone from construction work
24 in progress, it's on the company's books and plant
25 accounts, and there is depreciation charged, and also

01136

1 then the company gets cash flow from deferred tax
2 from the difference between tax and book
3 depreciation, and all those kind of capital recovery
4 factors begin to -- and furthermore, for once it goes
5 into plant in service, then I would ask you to take
6 this up further with Mr. Colbo, but then how things
7 become treatment for abandonment or whatever may
8 happen to that facility, now there's other rules, so
9 -- but that's the critical distinction. If it's
10 placed in plant in service, book depreciation and tax
11 depreciation was taken on the facility.

12 Q. So in your responses to Commissioner Oshie,
13 you were just saying when, on their books, it was
14 considered plant in service?

15 A. That's correct.

16 Q. Okay. You were not intending to suggest
17 that it was actually being used for transportation or
18 used and useful?

19 MR. TROTTER: I'll object to the question,
20 Your Honor. The exhibit says it's totally tied in
21 and awaiting product availability. There's a legal
22 question there. It's obviously tied into the system,
23 it's ready to go. Is that used and useful? That's a
24 legal question. It could very well be, and there may
25 be an argument to the contrary. But at that point,

01137

1 we have the facts, or at least a piece of paper that
2 states a fact, and the rest is a conclusion of law.
3 So I object to the question.

4 MR. MARSHALL: I object, as well. If
5 questions were needed to be asked about Bayview when
6 it went into service, Mr. Batch could have been asked
7 those questions. That's one reason why we objected
8 to that supplemental exhibit by Mr. Finklea when it
9 came in, because that did put us in a spot where we
10 couldn't respond effectively, but I can represent
11 what Mr. Batch would say if called upon, if the
12 Commission would like, and I think it's at odds with
13 what Mr. Brena is trying to suggest.

14 JUDGE WALLIS: Let's focus now on the
15 question that Mr. Brena has asked. I'm concerned
16 about the phrasing of the question.

17 MR. BRENA: I'll withdraw it and rephrase
18 it.

19 Q. Okay. Perhaps all the facts are in. Do
20 you recall Mr. Batch's testimony with response to my
21 cross and the question of whether Bayview was in
22 service?

23 MR. MARSHALL: The question, I think, is
24 when did Bayview go into service, and Mr. Batch was
25 not asked that by Mr. Brena. Was he?

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1 MR. BRENA: Do you recall -- is that an
2 objection?

3 JUDGE WALLIS: Mr. Brena.

4 MR. BRENA: I'm sorry. What was the
5 objection?

6 MR. MARSHALL: That was my objection. I --

7 JUDGE WALLIS: That your question does not
8 correctly characterize the Q&A between yourself and
9 the witness, the prior witness.

10 MR. BRENA: I asked if he recalled -- I'll
11 rephrase the question.

12 Q. Do you recall my cross-examination of Mr.
13 Batch with regard to the use of the Bayview terminal?

14 A. Yes.

15 Q. With the exception of diesel for testing
16 and water storage associated with hydro testing, did
17 he indicate that the Bayview terminal had ever been
18 used for any other purpose in your memory?

19 A. That is my recollection of his testimony,
20 but I --

21 Q. Okay. I'll move on.

22 A. It's not as clear as I would like it to be.

23 MR. MARSHALL: I think at this time I would
24 like to strike that question, because the witness
25 shows that he doesn't have foundation to make

01139

1 speculation on what that colloquy was. The record
2 will speak for itself.

3 MR. TROTTER: Your Honor, the witness
4 simply said the extent of his recollection, so the
5 record will speak for itself, we agree, but I don't
6 think it needs to be stricken.

7 JUDGE WALLIS: The motion's denied.

8 Q. If the goal of the -- if part of our
9 purpose here is to determine whether or not -- well,
10 I'm sorry. Let me ask a preliminary question first.

11 In anywhere in the company's case did it
12 separate the costs or revenues associated with the
13 different jurisdictions that this pipeline serves?

14 A. No, it did not, and I don't even recall
15 that it did it for its general case, as well.

16 Q. In terms of a company's ability to attract
17 capital from the capital markets or Olympic's ability
18 to attract capital from its own affiliated companies,
19 do you think that they will look at that on a total
20 company basis?

21 A. Yes, it will finance itself on a total
22 company basis.

23 MR. BRENA: I have nothing further.

24 MR. TROTTER: No questions.

25 JUDGE WALLIS: Is there anything further of

01140

1 the witness? It appears that there's not. Mr.
2 Elgin, thank you for appearing. You're excused from
3 the stand at this time. Let's be off the record,
4 please.

5 (Recess taken.)

6 JUDGE WALLIS: Let us be back on the
7 record, please. At this point, we're going to take
8 up the testimony of Commission Staff witness Robert
9 Colbo. Mr. Colbo, could you please rise, raise your
10 right hand?
11 Whereupon,

12 ROBERT COLBO,
13 having been first duly sworn, was called as a witness
14 herein and was examined and testified as follows:

15 JUDGE WALLIS: Please be seated. Mr.
16 Trotter.

17 MR. TROTTER: Thank you.

18

19 D I R E C T E X A M I N A T I O N

20 BY MR. TROTTER:

21 Q. Mr. Colbo, would you please state your name
22 for the record?

23 A. Robert Colbo.

24 Q. And are you employed by the Commission as a
25 transportation program consultant?

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1 A. Yes.

2 Q. In the course of your duties, did you have
3 cause to prepare testimony and exhibits in this
4 docket?

5 A. Yes.

6 Q. Turning your attention to Exhibit 135-T, is
7 that your direct testimony?

8 A. Yes.

9 Q. If I asked you the questions that appear
10 there, would you give the answers that appear there?

11 A. Yes.

12 Q. In the course of that exhibit, you refer to
13 two exhibits prepared by you, 136 and 137; is that
14 right?

15 A. Yes.

16 Q. Are those true and correct, to the best of
17 your knowledge?

18 A. Yes.

19 MR. TROTTER: I move the admission of
20 Exhibits 135-T, 136 and 137.

21 JUDGE WALLIS: Is there objection? Let the
22 record show that there is none, and those exhibits
23 are received in evidence. The witness is available
24 for cross-examination. Mr. Marshall.
25

01142

1 C R O S S - E X A M I N A T I O N

2 BY MR. MARSHALL:

3 Q. Mr. Colbo, you've been the analyst for the
4 Commission on oil pipeline since when, 1983, or
5 before?

6 A. Well my title is analyst, yes. We haven't
7 gone into a great deal of depth in oil pipeline
8 analysis filings, generally.

9 CHAIRWOMAN SHOWALTER: Mr. Colbo, I think
10 you're going to need to move your microphone more in
11 line between you and Mr. Marshall.

12 THE WITNESS: Okay, thank you.

13 Q. To the extent there's been any analysis of
14 oil pipeline tariffs, have you been the one to do
15 that since 1983?

16 A. Yes, yeah.

17 Q. Okay. And you wrote a memorandum in 1983,
18 at least at that time, about the differences in
19 methodology between what the Commission utility rates
20 approach were and the FERC, what used to be the ICC
21 rates, methodology would have been?

22 A. Yes, I did.

23 Q. Okay. And your conclusion then was that
24 there was a significant difference between the two
25 methodologies?

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1 A. There was a difference, yes.

2 Q. And the FERC methodology produced a higher
3 rate than using a utility rate method that was used
4 for utility cases in the state?

5 MR. FINKLEA: Your Honor, I'm going to
6 object. I don't believe this is touched on in Mr.
7 Colbo's testimony.

8 MR. TROTTER: I'll object, also, Your
9 Honor. This is an issue for the general rate case.
10 I think all witnesses have testified, including the
11 company's, that the interim rate case does not depend
12 on any difference between state and FERC
13 methodologies.

14 MR. MARSHALL: I'm going to tie it up with
15 this next question if he answers that one.

16 JUDGE WALLIS: Very well.

17 THE WITNESS: What was the question, sir?

18 MR. MARSHALL: Could you repeat the
19 question to the witness?

20 (Record read back.)

21 THE WITNESS: That's right.

22 Q. Okay. Now, the FERC also has an approach
23 to putting rates into effect fairly quickly subject
24 to refund; is that correct?

25 MR. BRENA: Objection. What does how what

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1 the FERC does with its rate filings have to do with
2 the emergency standard of this Commission?

3 JUDGE WALLIS: Mr. Marshall.

4 MR. MARSHALL: Address this regarding Mr.
5 Colbo's recommendation that the rates be subject to
6 refund and what the standard might be if you use the
7 approach used by the federal government versus
8 approaches used by the state.

9 MR. TROTTER: Your Honor, the issue of
10 subject to refund is Mr. Elgin's subject area, as Mr.
11 Colbo clearly states in his testimony.

12 MR. BRENA: And I would just like to make
13 the practical observation that if we're going to get
14 done tonight, we can't go down very many more rabbit
15 holes.

16 JUDGE WALLIS: Mr. Marshall, I don't think
17 this is an area that this witness is offered for.

18 MR. MARSHALL: Okay. Well, it is in his
19 testimony, but I'll move on. I can tie that up at a
20 later time.

21 Q. Now, you've also analyzed the rates that
22 had been filed with respect to Bayview; is that
23 right? You were the analyst on that?

24 A. Yes.

25 Q. Okay. And you were also the analyst that

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1 received different applications for the funding and
2 the proposals relating to Cross Cascades pipeline; is
3 that correct?

4 A. There was a filing made regarding potential
5 -- potential funding arrangement with respect to the
6 Cross Cascades pipeline. Myself and my supervisor,
7 Mr. Eckhardt, worked on that case. It was
8 subsequently withdrawn by the company.

9 Q. Now, in this testimony that you've given,
10 you've taken out all protection for debt associated
11 with Cross Cascade pipeline; is that right?

12 A. Well, I think Mr. Elgin did.

13 Q. But that's what your testimony supports in
14 your various schedules and analysis; correct?

15 A. I used the number Mr. Elgin gave to me,
16 yes.

17 Q. But you were involved in those discussions
18 about Cross Cascades, not Mr. Elgin, in the
19 mid-1990s; is that true?

20 A. That filing was withdrawn.

21 Q. Mr. Elgin was not involved in those
22 discussions and you were; right?

23 A. That's true.

24 MR. TROTTER: Well, Your Honor, the
25 question assumes there were discussions. Mr. Colbo

01146

1 has said a filing was made and withdrawn. I'll
2 object to the question on that basis.

3 Q. In addition to filings, there were letters
4 that included throughput and deficiency agreements to
5 finance that project; correct?

6 A. There were drafts proposed.

7 Q. And you also received copies of those
8 letters regarding the throughput and deficiency
9 agreements that were going to support the Cross
10 Cascades pipelines, including that from Tosco, from
11 Texaco, and perhaps others; is that right?

12 A. I don't recall what the status of that was.
13 I know it was withdrawn, it was subsequently
14 withdrawn.

15 Q. Well, to refresh your recollection, do you
16 remember getting a letter, for example, dated October
17 10th, 1995? And just look at the back page on that
18 letter, just for purposes of --

19 MR. FINKLEA: Your Honor, I object. This
20 is, again, well beyond the scope of the witness'
21 testimony.

22 JUDGE WALLIS: Mr. Marshall, can you point
23 us to an area within the witness' testimony?

24 MR. MARSHALL: It's regarding the
25 appropriateness of taking out the Cross Cascade

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1 pipeline from the debt protection and to show that it
2 was intervenors who supported that, intervenors who
3 entered into throughput and deficiency agreements
4 with regard to that project.

5 MR. BRENA: I join in the objection and
6 would point out that this witness has already
7 testified that that decision -- that he used a number
8 by Mr. Elgin in his calculation, but that the
9 judgment was Mr. Elgin's, who has already been
10 cross-examined on this point.

11 And I'd also raise the objection that what
12 relevance does it have whether or not a shipper
13 supported or didn't support the project with regard
14 to whether it should be included today?

15 MR. TROTTER: I'll join the objection.
16 Also, Your Honor, the company is not seeking to earn
17 a return on the Cross Cascades pipeline in its
18 general case, and as far as we can tell, they're not
19 asking for a recovery of it in the interim case. So
20 it's irrelevant and it is Mr. Elgin's responsibility.
21 Mr. Colbo took the figure from Mr. Elgin.

22 JUDGE WALLIS: The objection is sustained.

23 Q. Are you familiar with throughput and
24 deficiency agreements as a method of financing in the
25 oil pipeline business?

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1 MR. FINKLEA: Same objection.

2 MR. BRENA: Perhaps he could direct me to
3 part of this witness' direct case, in which this is
4 an issue.

5 MR. MARSHALL: Well, let me ask it a
6 slightly different way.

7 Q. Is there anybody on the Commission Staff,
8 other than yourself, that knows about any type of
9 financing for oil pipelines?

10 A. Other than who?

11 Q. Other than yourself?

12 A. I certainly don't consider myself to be an
13 expert on financings from oil pipeline companies, and
14 Mr. Elgin presumably did some work in that regard in
15 connection with his presentation of his case.

16 MR. MARSHALL: I don't have any further
17 questions.

18 JUDGE WALLIS: Very well.

19 MR. FINKLEA: Your Honor, in light of the
20 hour, we have decided that we have no questions.

21 JUDGE WALLIS: Very well. Mr. Brena.

22 MR. BRENA: We includes me.

23 JUDGE WALLIS: Are there questions from the
24 Bench?

25

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1 E X A M I N A T I O N

2 BY CHAIRWOMAN SHOWALTER:

3 Q. My only question is about the source or
4 sources of your information that you have in your
5 testimony. You make a number of calculations. Are
6 these calculations based on the information that you
7 got from the company in the course of this
8 proceeding --

9 A. Yes.

10 Q. -- through discovery?

11 A. Yes.

12 Q. Are there other reports that the company
13 files on any kind of regular basis about its
14 financial condition?

15 A. In general terms, we have adopted the FERC
16 form, in terms of annual reporting, and so they file
17 a copy of the FERC report with us once a year.

18 Q. But that was not the basis for any of these
19 calculations?

20 A. That's correct.

21 CHAIRWOMAN SHOWALTER: Okay. Thank you.

22 MR. TROTTER: No redirect.

23 JUDGE WALLIS: Very well. Mr. Colbo, thank
24 you for appearing. You're excused from the stand.
25 And let's be in recess while Mr. Colbo steps down and

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1 the next witness steps up. Would that be Mr. Brown
2 or Mr. Grasso?

3 MR. BRENA: That would be Mr. Brown.

4 JUDGE WALLIS: Mr. Brown.

5 (Recess taken.)

6 JUDGE WALLIS: Let's be back on the record,
7 please. Mr. Brown, would you stand and raise your
8 right hand, please?
9 Whereupon,

10 JOHN BROWN,
11 having been first duly sworn, was called as a witness
12 herein and was examined and testified as follows:

13 JUDGE WALLIS: Please be seated. Mr.
14 Brena.

15

16 D I R E C T E X A M I N A T I O N

17 BY MR. BRENA:

18 Q. Good afternoon.

19 A. Good evening.

20 Q. Did you prepare and do you adopt testimony
21 and exhibit labeled JFB 113-T(C)?

22 A. Yes, I did.

23 MR. BRENA: And just for the record, the C
24 can be removed from this testimony, as the
25 confidentiality of the document in its entirety has

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1 been waived by the company.

2 JUDGE WALLIS: So noted, and we are
3 removing that designation.

4 MR. BRENA: He is available for cross.

5 JUDGE WALLIS: Are you offering the exhibit
6 at this time, Mr. Brena?

7 MR. BRENA: Yes.

8 JUDGE WALLIS: There being no objection,
9 Exhibit 113-T is received in evidence.
10 Cross-examination, Mr. Marshall.

11

12 C R O S S - E X A M I N A T I O N

13 BY MR. MARSHALL:

14 Q. Please turn to page eight of your
15 testimony, Mr. Brown, line 15 to 16. Do you have
16 that in front of you?

17 A. Yes, I do.

18 Q. Where you say Olympic's revenues and cash
19 flows have also increased substantially recently due
20 to both dramatically increasing throughput and
21 increasing rates. Do you see that?

22 A. I see that.

23 Q. And the rates you mean by that are the FERC
24 rates that went into effect September 1st; is that
25 correct?

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1 A. That's correct.

2 Q. Okay. And have you tried to break out in
3 any of your analysis, any of your testimony here, can
4 you point to me what contribution that makes from the
5 FERC?

6 A. That's a question I think you can ask Mr.
7 Grasso. He is the one that has put the schedules
8 together.

9 Q. I see. Now, have you been retained by
10 Tosco, Tesoro, with respect to the FERC matter?

11 A. I've been retained by Tesoro, and I'm not
12 sure about Tosco. I don't know the answer to that.
13 I'm sorry.

14 Q. Had you been retained by Tesoro prior to
15 Tesoro's opposition to the FERC interim rates?

16 A. Yes.

17 Q. I call them interim rates, but you know
18 what I mean. Those are rates that go into effect
19 subject to refund. So whenever I say that, please
20 make that mental transposition.

21 A. All right. And I want you to make one
22 mental transition, too, or consideration, and that is
23 that, in my credentials, I show that I'm a licensed
24 attorney in the state of Missouri. But I am not --

25 Q. You'll have to show me.

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1 A. I'm not here as an attorney, I'm not here
2 to give legal opinions, so whatever I say is not
3 based on a legal opinion.

4 Q. Okay. Were you involved directly in the
5 opposition by Tesoro to those interim -- as I call it
6 -- rates at the FERC?

7 MR. BRENA: Objection, relevance.

8 JUDGE WALLIS: These are preliminary
9 questions, and I will give --

10 MR. MARSHALL: Goes to credibility --

11 JUDGE WALLIS: -- Mr. Marshall some
12 latitude.

13 MR. MARSHALL: -- bias and so on.

14 THE WITNESS: You asked about opposition,
15 and my recollection is that Olympic made a filing
16 with the FERC --

17 Q. I'm just asking whether you were involved
18 or not in the opposition, not the details.

19 MR. BRENA: Please allow my witness to
20 complete his answer, and if there's something
21 inappropriate with the answer, we can address it at
22 that time.

23 MR. MARSHALL: It's just preliminary.

24 JUDGE WALLIS: Yes, let's let the witness
25 respond, please.

01154

1 THE WITNESS: There was a filing made at
2 the FERC earlier in the year, and Tesoro protested
3 that filing. Ultimately, the --

4 Q. Were you involved in that?

5 A. Ultimately, the FERC rejected that filing
6 and I was involved in that. I participated in a
7 couple of phone calls in connection with their
8 protest, but that was about the extent of the
9 involvement.

10 Q. And after the FERC granted these rates
11 subject to refund to go into effect in September of
12 2001, were you involved in Tesoro's efforts at a
13 rehearing to try to once again oppose those rates
14 going into effect?

15 A. No, I was not.

16 Q. You have been retained, however, on the
17 FERC general rate case matter; is that true?

18 A. Yes.

19 Q. Okay. And have you done any preliminary
20 analysis whatsoever of any type, had any preliminary
21 discussions where you've come to any conclusions with
22 regard to whether any part of those rates ought to be
23 refunded?

24 A. I haven't come to any particular firm
25 conclusion. I do know that the question of the

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1 capital structure and the rate of return are items
2 that have been raised here in this proceeding, and
3 I'm sure that Mr. Hanley will address those matters
4 in the proceeding at the FERC.

5 Obviously, to the extent that there's a
6 different capital structure and different rate of
7 return that is used, that's going to have an effect
8 on the filing. There are, of course, matters, and I
9 don't have all of the details of this, I think Mr.
10 Grasso may have those details, but there are
11 questions about the level of the rate base, questions
12 such as the Bayview terminal. I'm not sure, but I
13 believe that the Cross Cascades pipeline costs may be
14 included. I said may. I'm not sure of that. But to
15 the extent they are, that will be an issue that needs
16 to be addressed.

17 There are questions about the costs that
18 are included in connection with the Whatcom Creek
19 matter, and of course those items will have to be
20 addressed, but I haven't come to any conclusion about
21 those, because we don't have all of the information
22 about the rate filings.

23 Q. My question was fairly broad. Have you
24 come to any conclusion, tentative or otherwise, that
25 any amount of that FERC rate ought to be refunded?

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1 In your own mind, as you sit here today, are you
2 saying that you have come to absolutely no conclusion
3 that any part of that should be refunded?

4 A. I guess if you wanted to put a quantity on
5 it, should you have a penny to be refunded, probably
6 so. Should you have no refund, probably not. But I
7 don't know in between and I haven't come to any
8 conclusion about the level of the amount of refund,
9 if any there should be.

10 Q. I'm not sure I understood your answer.
11 It's between a penny and nothing to be refunded?

12 A. That's my own view, that there's going to
13 be some refund, but I haven't come to a conclusion as
14 to how much.

15 Q. Is it more than a penny?

16 A. Probably.

17 Q. Is it more than \$50 million?

18 A. I haven't looked into the details of that.
19 I haven't been asked to look into the details of
20 that.

21 Q. You said that Mr. Hanley will address that
22 at the FERC. How do you know that Mr. Hanley will
23 address that before the FERC? Have you spoken to him
24 about that rate case?

25 MR. BRENA: Your Honor, I understand that

01157

1 these started out to be preliminary in nature. I
2 fail to see how this line of questioning or that last
3 question has anything to do with this at all.

4 MR. TROTTER: I'll join the objection.
5 This is very remote.

6 JUDGE WALLIS: Mr. Marshall.

7 MR. MARSHALL: Mr. Hanley said yesterday
8 that he had absolutely no opinions about this issue,
9 either, and apparently he's had conversations with
10 this witness. And it's interesting, and I think
11 their testimony's informative on if they truly
12 haven't any conclusion whatsoever as to any amount
13 that should be refunded, I'd like to know that, but I
14 don't believe that that's true, and I'd like to find
15 out what conclusions they have and what -- even a
16 ballpark amount that they believe needs to be
17 refunded. It has a direct bearing on whether this
18 2002 capital budget can be financed.

19 MR. TROTTER: Your Honor, what they believe
20 or will even testify to is not relevant. It's
21 whatever FERC orders is what's relevant. So I think
22 it's very, very remote relevance. Continuing
23 objection.

24 MR. BRENA: I would also like to add that
25 whatever work product or impressions that my experts

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1 may share with me within the context of their
2 engagement in another rate case is protected by the
3 work product privilege. And this isn't an
4 opportunity to probe my witnesses with regard to
5 their opinions in other cases. That's not what we're
6 here for. And I've allowed this to go on, and in
7 fact, I've waived the privilege so certain documents
8 can be produced, but, you know, enough with regard to
9 the work that my experts do in other cases at my
10 request.

11 MR. MARSHALL: This is a case that has
12 direct bearing on what we're talking about. It's not
13 some unrelated case.

14 JUDGE WALLIS: We're going to sustain the
15 objection to these inquiries. We think that there is
16 a concern about work product. We think that the
17 preliminary views of the witnesses are of only remote
18 relevance to the ultimate decision that the federal
19 agency might reach, and we have a level of concern
20 about the Commission's authority, in any event, to
21 consider the FERC decision, subject to parties'
22 argument in briefs, whatever it may be in setting
23 intrastate rates.

24 Q. Are you familiar at all with accounting
25 principles that require an amount to be recorded as

01159

1 income to be relatively certain not only of
2 collection, but of not being subject to refund?

3 A. I am familiar with the fact that amounts
4 can be recorded, even if they're subject to refund,
5 and ordinarily there, if they are subject to refund,
6 there will be a footnote somewhere in the financial
7 statements indicating that the revenues are being
8 collected subject to refund.

9 Q. And that's a caution to any investor, that
10 don't count on this necessarily?

11 A. All right. I'll accept that.

12 Q. And in your testimony here, at page eight,
13 are you counting on the increased rates from the FERC
14 in your analysis or not?

15 A. Let me explain that testimony, and maybe I
16 can explain the FERC procedure and the Washington
17 procedures and we can kind of clear things up in this
18 regard.

19 Q. I just wanted to know if you're relying on
20 that or not?

21 A. I am relying on that testimony for the
22 following reasons: The FERC procedure is one in
23 which the FERC accepts the filing and makes it
24 subject to refund. They then have a schedule, and in
25 this case, I believe that they have scheduled a

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1 hearing that is in July. I think that's the date
2 that has been established. There is no schedule at
3 all before the FERC for FERC to issue a decision.

4 They will have, in fact, the procedure,
5 unlike here, is that they will have a hearing, judge,
6 administrative law judge hear the proceeding. And
7 ordinarily those matters then will be briefed before
8 the judge. And there will be exceptions taken to the
9 briefs. And from then, after all of that goes
10 through, then the FERC will take the case up for
11 consideration before the full Commission.

12 I have no idea when that will occur. It
13 could be a year after the hearing, it could be six
14 months after the hearing, it could be two years after
15 the hearing. It's not unusual, in fact, I think in
16 the -- there's a case that is SFFP, I think, is the
17 designation of the case, that they have used, I
18 believe, 1994 data, and the FERC, just in the year
19 2000 issued a decision in that case.

20 Now, until the order is final and no longer
21 subject to appeal, there's no refund that is
22 required. And ultimately, there may be a refund,
23 there may not be a refund. And yet, here in
24 Washington, as I understand the procedure, you have a
25 period of time in which you are required to hear and

01161

1 decide the case. And as I understand it, there is a
2 hearing that is to take place in May, and there's
3 some question about whether July 1 or whether August
4 1 is the date that you will have to issue your
5 decision.

6 Now, I do not know the procedures beyond
7 that point, whether appeals can be taken to the
8 procedures -- or to the order that you issue and if
9 refunds are due, when those refunds would be made.
10 But there certainly is a far shorter period of time
11 to deal with the question of the rate proceeding that
12 you have here in Washington than they have in
13 Washington, D.C.

14 And from the standpoint of, you know, why
15 are we here, well --

16 MR. MARSHALL: I don't believe I asked that
17 question. My question was very limited, and it
18 sounds like -- I really wanted to get this witness on
19 and off quickly, and I think it's way beyond the
20 question, which is deserving a yes or no answer. I
21 think he's lost track of what it is. Can you tell me
22 what my question was?

23 MR. BRENA: Excuse me.

24 JUDGE WALLIS: Let's let Mr. Brena respond,
25 please.

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1 MR. BRENA: First, the characterization of
2 a witness' losing track of something, I think is
3 inappropriate. Secondly, this witness said that he
4 relied on it and was giving the reasons why he relied
5 on it. He was responding to the question. Third, I
6 do not like my witness cut off in mid answer. If he
7 goes on longer than Mr. Marshall thinks appropriate
8 and if he includes information which is inappropriate
9 to respond, he has the procedural option of asking
10 for a motion to strike. And if Your Honor agrees,
11 then that portion will be struck. He should not have
12 the procedural option of interrupting my witness in
13 mid answer.

14 JUDGE WALLIS: The process that we use at
15 the Commission, I believe, allows Counsel to
16 interject if they believe that the witness' response
17 is far beyond the question, and to raise that point
18 at the time and we will deal with it. Sometimes it
19 can save an extended answer.

20 In this case, I'm not sure that we've
21 reached the point yet where the witness' testimony is
22 not responsive to the question. So we will allow the
23 witness to conclude his response.

24 THE WITNESS: I was going to say that, as
25 far as why we're here, what we're talking about is

01163

1 they've asked for an interim increase in rates, based
2 on their full filing, but you're going to be deciding
3 that in just a short while. And so I question, you
4 know, why are we here for this interim rate
5 proceeding when you already have scheduled a full
6 hearing that will be heard on the merits of the case.

7 Q. Do you recall what my question was?

8 A. Your question was specifically related to
9 lines 15 and 16 of my testimony on page eight, and
10 you were asking questions about the refund of the
11 revenues attributable to the increasing rates and --

12 Q. The --

13 A. And my answer was directed to your
14 question.

15 Q. Okay. And the increasing rates were only
16 the FERC rates in lines 15 and 16; correct?

17 A. That is correct.

18 Q. Okay. Nothing to do with the rate increase
19 that you just now testified to at the state level?

20 A. Nothing to do, except for the fact that
21 I've been sitting here listening to all of the
22 testimony of everyone and I have had in my own mind a
23 question as to why we're here, and yes, I was
24 addressing the increased rates, but there is a
25 relevance to the question of whether or not an

01164

1 emergency has been shown, and you haven't shown an
2 emergency.

3 MR. MARSHALL: Your Honor, I move to strike
4 the witness' last response and his prior response.
5 It didn't respond to my question, and I don't know
6 how I can try to shorten this up. I'd like to keep
7 this very short, unless I move to strike.

8 MR. BRENA: Could I have the court reporter
9 read back the last question, please?

10 (Record read back.)

11 MR. BRENA: He was asked a broad question
12 about whether it had anything to do with the state
13 case at the broad level. I would suggest that if Mr.
14 Marshall speed this up, that he ask more specific
15 questions.

16 JUDGE WALLIS: My take on this is that the
17 question did call for a yes or no answer. I am going
18 to ask the witness, if you have personal reservations
19 about the purpose of this proceeding, that's a matter
20 for the Commission. You've indicated that you're not
21 one of the attorneys in this case. What I would ask
22 you to do is listen to the questions carefully and
23 respond to the questions to the best of your ability.
24 Let's move on.

25 Q. Now, your last response said, as you were

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1 sitting in the room here, you thought to yourself why
2 have an interim case at all, why don't we just go to
3 a general case in this matter.

4 Let me ask you this question. Why couldn't
5 we do in this state exactly what they do at the FERC
6 and have the rates go into effect immediately, as
7 they do at the FERC, and then go to the general case
8 and solve all the problems of the time that we've
9 spent on this?

10 JUDGE WALLIS: Mr. Marshall, I'm not sure
11 that this witness is qualified to answer that, which
12 appears to be a question relating to the processes
13 available under state law.

14 MR. MARSHALL: I was trying to respond to a
15 question that he asked himself and answered himself
16 on the stand as to why we are here. And I guess I --

17 JUDGE WALLIS: We have indicated that we've
18 asked him not to engage in those kinds of questions
19 on our record.

20 Q. Please turn to page nine of your testimony,
21 Mr. Brown, and look at line 11. Of the receivable
22 amount, do you know how many millions of dollars in
23 receivables are due to insurance recoveries and are
24 associated with costs that are not being requested by
25 Olympic? Do you know?

01166

1 A. No, I don't.

2 Q. Okay. And do you know what percentage of
3 insurance recoveries are likely to be made? Do you
4 know anything about those issues at all?

5 A. I'm going to answer, and then I would like
6 an explanation of that answer. The answer is no,
7 specifically, I do not know. However, the receivable
8 has been recorded on the books, there is no reserve
9 that's been established on the books for a
10 non-recovery of a receivable, and it's been
11 classified on the books as a current asset.

12 That means to me that the company expects
13 to recover that money, one hundred percent of the
14 money. There's no reserve that's set up for it. And
15 so I'd say that it is something that would be
16 recovered in the next 12 months.

17 Q. Assuming that a great bulk of this money
18 that you have here in that line is insurance recovery
19 money. Were you here to hear the testimony of Mr.
20 Batch or Mr. Fox about what percentage of the
21 insurance recoveries are likely to occur, in fact?

22 A. I heard some mention of a figure, but,
23 again, you're asking about recovery of that money,
24 and you've classified or the company has classified
25 it on its books as a current asset, and that means

01167

1 that you're going to recover that money. You expect
2 to recover it. Otherwise, you would have a reserve
3 set up.

4 I don't know, for example, that -- let's
5 assume that -- and I think the figure was 60 percent.
6 It may very well be that what's been recorded on the
7 books is 60 percent of the amount of the insurance.
8 I don't know that. I do know that you have recorded
9 on the books \$39.7 million, or \$37 million, I think
10 is the figure for the receivables that's recorded on
11 the books. And that would indicate to me that you
12 expect to recover that amount of money.

13 Q. My specific question is did you hear the
14 testimony of Mr. Batch and Mr. Fox as to the exact
15 number that they testified to that they thought the
16 insurance coverage would be?

17 A. And I answered that. I said no, that I did
18 not know the exact number. However, I was going to
19 explain my answer, and I explained the answer.

20 Q. Do you know whether those insurance
21 recoveries go against costs that have been requested
22 or not in this matter, or do you have an opinion on
23 that?

24 A. My opinion --

25 Q. Let me restate that, withdraw it. I'm

01168

1 going to try to make this very precise. I may have
2 made a mistake here. Do you know the dollar amount
3 of costs against which the insurance recoveries go?

4 A. No, I do not, but again, I have to say that
5 it is a receivable that is reported on the books, and
6 if you recorded it on the books as a receivable,
7 there's no footnote indicating that it is subject to
8 some percentage of recovery, there's no reserve
9 that's been set up for non-recovery, it is a
10 receivable. And under accounting rules, a receivable
11 that is expected to be recovered within 12 months
12 will be recorded as a current asset.

13 Q. My question, Mr. Brown, was not about the
14 receivable, but the cost against which the
15 receivables would go. And my question was a very --
16 I thought, precise one, which is do you know the
17 dollar amount of the cost against which the
18 receivables for insurance recoveries would go if
19 recovered?

20 A. I don't have any information about that. I
21 do know that the money would be coming into the
22 company and would be a source of cash.

23 Q. Now, do you know, because you don't know
24 about the costs against which these insurance
25 recoveries go, you don't know whether the costs are

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1 included in any of these financial statements or in
2 this case, do you?

3 A. I guess that I would have to answer that
4 no, I don't know, and that may be the reason that
5 there aren't audited financial statements.

6 Q. Okay. With regard to whether the financial
7 statements are audited or not, these financial
8 statements are also preliminary and forecasts for the
9 most part, particularly for the last two months of
10 2001; isn't that correct?

11 A. I don't believe that is correct. At least
12 that's not my understanding. I understood that the
13 financial statements that were presented were actual
14 through November with an estimate for December. I
15 may be mistaken about that. But the 2000 financials
16 are actual figures and you have actual figures at
17 least through October.

18 Q. Would you agree that the best evidence of
19 financials would be the testimony given here by Mr.
20 Fox because -- at least you've admitted that December
21 is not in. Do you agree that the books are --

22 A. Do you really want me to answer that
23 question?

24 Q. No, I'll withdraw that, due to the lateness
25 of time. Did you attend any of Mr. Fox's examination

01170

1 in this matter?

2 A. I certainly did.

3 Q. Okay. And were there any questions asked
4 about the insurance receivables and the costs to Mr.
5 Fox that you can recall?

6 A. I believe that there were questions that
7 were asked, but I'm not -- I don't recall the exact
8 questions and answers.

9 Q. Okay, thank you. Page 12 of your
10 testimony, line 19, you say, Olympic's owners have a
11 large and direct financial stake in Olympic's
12 continuing proper operation due to their large
13 investment in refineries.

14 Just focusing on refineries. Do you know
15 how many refineries there are in Washington State?
16 And if you don't know, just please say, I don't know.

17 A. Well, the difficulty is that I do recall
18 seeing an exhibit that was attached to Mr. Batch's
19 testimony. It mentioned four refineries, but I don't
20 know if that is all of the refineries in the state of
21 Washington. There were four refineries that were
22 mentioned in that exhibit.

23 Q. Do you know where any of the four are
24 physically located in the state?

25 A. They're on the -- on or tied to the Olympic

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1 system.

2 Q. Do you know whether they're north of
3 Seattle, east of Seattle, south of Seattle?

4 MR. BRENA: Objection.

5 THE WITNESS: Well, the line begins in --
6 I'm not a Washington -- a native of the state of
7 Washington, so I don't know the exact names of the
8 cities, but there is the refinery of -- I believe it
9 is ARCO's refinery that is up near the
10 Washington-Canadian boarder. I'm going to class it
11 as that. And then I believe that Tosco has a
12 refinery that is either there or just slightly south
13 of there, and then Tesoro and Equilon have refineries
14 that are south of there, and those are all north of
15 Seattle, as I understand it.

16 MR. MARSHALL: I don't have anything
17 further of this witness.

18 JUDGE WALLIS: Commission Staff.

19 MR. TROTTER: Staff has no questions of Mr.
20 Brown.

21 JUDGE WALLIS: From the Bench.

22

23

24

25

E X A M I N A T I O N

BY CHAIRWOMAN SHOWALTER:

Q. Could you turn to page 22 of your

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1 testimony, and I'm looking at line 20. And this is
2 one of a few places that you make your point, but
3 here you say Olympic and its owners are perfectly
4 capable of assuming financial responsibility for the
5 difficulties they have created. And that's a
6 compound there.

7 And assume for the moment that Olympic
8 itself is not capable, but that its owners are
9 capable of assuming responsibility. What do we do if
10 the owners are capable, but elect not to assume that
11 responsibility that you've mentioned here?

12 A. Going back to the question that was just
13 asked, I don't understand, and I think it's
14 completely -- I'll use a word Mr. Hanley used
15 yesterday in his testimony, or whenever it was, day
16 before -- preposterous that they would not.

17 Because, again, you're looking at rates for
18 barge and rail shipment, truck shipment of refined
19 products that are twice the rates for the pipeline
20 company, and if -- if indeed the owners decided that
21 they were not going to put the money into the
22 pipeline and basically let it go belly up, that's
23 cutting off the nose to spite the face. It's, again,
24 having to -- I believe that the figures that were
25 used, ARCO's refinery had capacity of 222,000 barrels

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1 a day, and it's my understanding, from some things
2 I've either seen or heard, that they've increased
3 that capacity by another 40,000 barrels a day. We're
4 looking at, then, 262,000 barrels a day of refinery
5 capacity. The Equilon refinery has a capacity that
6 is like 150,000 barrels a day, I think that's the
7 figure that was used in that exhibit I referenced.

8 Doesn't make any sense that they would not
9 come up with the dollars to keep the pipeline going
10 and use the pipeline to move their products.

11 Q. So in your view, we should proceed on the
12 assumption that the company -- or no, the company's
13 owners will contribute, and it's a contested issue as
14 to what rate, if any, might induce them or -- to act
15 that way?

16 A. In my view, I think you should proceed on
17 the basis that they will put the money into the line.
18 In the first place, as far as this line is concerned,
19 Mr. Batch said, I believe, that the pipeline is
20 running in a safe mode. Now, there's been a lot of
21 talk about the 2002 capital expenditures. Those
22 capital expenditures are those that the company says
23 they need to make to provide continued safety of the
24 pipeline.

25 Some of those capital expenditures, if you

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1 look at the list of projects that are included,
2 include boring under a river to put the pipeline
3 there and to avoid the possibility that an earthquake
4 or a landslide will occur. You know, that may be
5 something that ought to be done from a safety
6 standpoint, but certainly I don't believe that it's
7 something that is going to affect the outcome of this
8 case. You're not dealing with 2002 capital
9 expenditures.

10 Q. I'm sorry, but my question really doesn't
11 go at all to the expenses. I'm simply inquiring and
12 only wanted to talk about the relationship of the
13 owners to the company, not which expenses are
14 reasonable or not reasonable.

15 A. Well, but getting back to the Olympic and
16 its owners, Olympic could look, and I think Staff
17 suggested this in its -- in their testimony, that
18 Olympic could look at those items that are necessary
19 and those items that are desirable. I think Staff
20 called it essential. Now, again, we're talking about
21 2002 capital expenditures, and your question had to
22 do with, as I thought, what are you going to do if
23 the owners don't put up the money. And I don't see
24 that as a possibility.

25 They've asked for a signal, and they say,

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1 Okay, give us a signal from the interim proceeding.
2 You're going to be dealing with resolution of this
3 case in four months. What if you give a signal and
4 give them an increase at this time, and then find
5 that, in four months' time, they're not entitled to a
6 thing. What kind of signal is that?

7 I think you're better off to proceed to the
8 hearing. And from the standpoint of an interim
9 increase, that doesn't help -- it doesn't help the
10 financing. You're talking about, you know, I think,
11 according to Mr. Elgin's figures, something less than
12 \$2 million for the next six months, maybe \$2.7
13 million. But that's not going to be enough to
14 provide them the capability of financing. They need
15 to make their corporate guarantees or they need to
16 come up with something other than just this interim
17 increase that they're requesting to get the company
18 in the right position financially and the owners to
19 put the money up.

20 CHAIRWOMAN SHOWALTER: Okay. Thank you.

21 JUDGE WALLIS: Mr. Brena.

22

23 R E D I R E C T E X A M I N A T I O N

24 BY MR. BRENA:

25 Q. Have you heard any testimony in this

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1 proceeding that the owners have refused to put the
2 money up?

3 A. No, I haven't.

4 MR. MARSHALL: I think this is beyond
5 cross.

6 JUDGE WALLIS: I think it's --

7 MR. MARSHALL: He just answered it, so I'll
8 withdraw that.

9 Q. Mr. Brown, you were asked some questions
10 about costs that the insurance was intended to go
11 against. Is there some sort of compartmentalization
12 of costs that would be appropriate with regard to
13 those receivables where some costs should have
14 priority over the safety improvements that they're
15 asking for?

16 A. None that I'm aware of.

17 Q. Madam Chair asked a question with regard to
18 inducing owners to put equity into the company. Do
19 you think, as a regulatory matter, that it's
20 appropriate to charge a ratepayer higher than a just
21 and reasonable rate to induce an owner to add equity
22 into a company that has none?

23 MR. MARSHALL: I object. It's leading
24 and --

25 JUDGE WALLIS: In light of the hour and

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1 need to expedite, we will allow some latitude.

2 MR. BRENA: Thank you, Your Honor.

3 THE WITNESS: Does that mean I answer?

4 JUDGE WALLIS: Yes.

5 Q. Yes.

6 A. Okay. No, I don't think that the
7 regulatory body should do anything other than
8 establish just and reasonable rates based on the
9 costs presented, and those just and reasonable rates
10 would be decided in the full proceeding.

11 Q. Now, you testified, in response to her
12 question, that you didn't think there was any
13 possibility that the owners wouldn't ultimately put
14 up the money. Why is that?

15 A. Well, as I said, I think that they have
16 their refineries that are operating. You know, I
17 don't see that ARCO would spend money to expand the
18 capacity of its refinery by 40,000 barrels a day
19 expecting that it's going to shut the line down. And
20 to the extent that it needs to make the capital
21 expenditures, I see that the owners would do that.

22 I think that the pipeline company has made
23 a commitment, for example, to the city of Bellingham
24 that it's going to operate a safe pipeline, and to
25 the extent that they need to abide by that -- to the

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1 extent they need to make the capital expenditures,
2 they'll do so, at least I would think that they would
3 do so, to abide by that commitment, they have the
4 corrective action orders of the OPS, and I'm fairly
5 certain that they've made commitments under those
6 corrective action orders to put the pipeline in safe
7 condition and keep it in safe condition. And there
8 may be even conditions required in their right-of-way
9 agreements. I don't know that, but there may be
10 conditions in the right-of-way agreement that they
11 will have to continue operating the pipeline.

12 Q. Now, if they do put the money up for the
13 capital improvements in 2002, who ultimately is going
14 to pay for those improvements?

15 MR. MARSHALL: This is beyond cross, Your
16 Honor.

17 MR. BRENA: No, I am exploring with this
18 witness an owner's incentive to put money up for
19 capital improvements is that he gets his money back
20 from ratepayers through appropriate rate adjustments,
21 including a rate of return on that equity invested.

22 MR. MARSHALL: That would be in a general.

23 MR. BRENA: That is a direct motivation for
24 an owner to come up with money when he knows that
25 he's going to get it back, plus return.

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1 JUDGE WALLIS: Mr. Brena, you don't need to
2 telegraph the answer.

3 MR. MARSHALL: Also, it's --

4 JUDGE WALLIS: Respond to the objection. I
5 do think, however, that this topic was touched on in
6 the examination and it is not beyond the pale.

7 MR. MARSHALL: But it is a general rate
8 case issue, Your Honor, and I think, in the interest
9 of time, they ought to at least apply to the interim
10 issues.

11 MR. TROTTER: Your Honor, I join the
12 objection of Mr. Marshall in effect. Mr. Brown does
13 testify to this very topic on page nine, beginning on
14 line 15. It does seem to me it's been asked and
15 answered.

16 JUDGE WALLIS: Perhaps that resolves it,
17 that reference.

18 MR. BRENA: Let me just review my notes,
19 please. I have no further questions.

20 JUDGE WALLIS: Is there anything further
21 for the witness?

22 MR. MARSHALL: No, Your Honor.

23 JUDGE WALLIS: Very well. Mr. Brown, thank
24 you for appearing. You're excused from the stand at
25 this time. Let's be off the record for a scheduling

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1 discussion.

2 (Discussion off the record.)

3 JUDGE WALLIS: Let's be back on the record,
4 please. Following a very brief recess, an
5 administrative matter, I acknowledge receipt of
6 Exhibit 83-R, for revision, under today's date, an
7 update of Mr. Fox's Exhibit 83, which incorporates
8 the changes to which he testified in his supplemental
9 testimony.

10 Our next witness is Mr. Gary Grasso. Mr.
11 Grasso, would you please stand, raise your right
12 hand?

13 Whereupon,

14 GARY GRASSO,
15 having been first duly sworn, was called as a witness
16 herein and was examined and testified as follows:

17 JUDGE WALLIS: Thank you. Please proceed.

18 Mr. Brena.

19

20 D I R E C T E X A M I N A T I O N

21 BY MR. BRENA:

22 Q. Mr. Grasso, did you prepare and are you
23 adopting testimony and exhibits labeled GG-114-TC,
24 through and including GG-121-C?

25 A. I am.

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1 MR. BRENA: I would make a note for the
2 record that all of the designations in Mr. Grasso's
3 testimony and exhibits are stamped with C, and it's
4 my understanding that they've all been waived by the
5 company and that this is public information.

6 JUDGE WALLIS: That is consistent with our
7 understanding, and the initial C will be stricken and
8 these documents will not be considered to be
9 confidential.

10 MR. BRENA: Mr. Grasso is available for
11 cross.

12 JUDGE WALLIS: You're offering the exhibits
13 at this time?

14 MR. BRENA: Yes.

15 THE WITNESS: I have an errata.

16 MR. BRENA: Oh.

17 JUDGE WALLIS: Is it a matter of substance?

18 THE WITNESS: No, but it's only one word,
19 and it's a matter of context. And if I may, it's on
20 page two of my testimony.

21 JUDGE WALLIS: Page two?

22 THE WITNESS: Yes, at line 13. I have
23 September in there, and that should be August.

24 JUDGE WALLIS: Very well. There being no
25 objection, the exhibits are received. Mr. Marshall,

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1 were we correct in our understanding of the company's
2 withdrawal of the concerns relating to
3 confidentiality of these documents?

4 MR. MARSHALL: Yes, Your Honor.

5 JUDGE WALLIS: Thank you. The witness is
6 available for cross-examination. Mr. Marshall.

7

8 C R O S S - E X A M I N A T I O N

9 BY MR. MARSHALL:

10 Q. Mr. Grasso, you indicated in your resume
11 that you were most recently involved in Trans-Alaska
12 Pipeline System rate case proceeding before the
13 Regulatory Commission of Alaska.

14 A. Correct.

15 Q. Is that work that you're doing for Mr.
16 Brena?

17 A. For Tesoro Alaska, yes.

18 Q. And Mr. Brena?

19 A. Yes.

20 Q. Okay. And it also indicates that you're
21 currently directing your firm's litigation support
22 for an oil refinery client in a major oil pipeline
23 rate case being prosecuted before a state regulatory
24 commission. Is that the same thing?

25 A. Yes, it is.

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1 Q. Okay. And have you also been retained by
2 Tesoro and Mr. Brena to work on the FERC case, the
3 federal part of the same matter that we have here?

4 A. Yes, I have.

5 Q. And have you formed any conclusions about
6 any of those amounts that you think should be
7 refunded from that case?

8 A. I have done no analysis of that type. I've
9 been focusing heavily on this interim case and have
10 just been getting around to looking at the testimony
11 that's been filed in the general case.

12 Q. Were you involved in opposing that FERC
13 rate from going into effect in September of this past
14 year?

15 A. Could you define opposing, because I think
16 of an attorney as presenting the opposition, as
17 opposed to providing advice to my --

18 Q. Let me ask it very broadly. I thank you
19 for that.

20 A. Okay.

21 Q. Were you involved in any way, shape or form
22 in that proceeding which resulted in Tesoro filing an
23 objection, and then a motion for rehearing on that
24 FERC rate going into effect in September?

25 A. I was certainly asked to review the initial

01184

1 filings that were made. Other than the fact that it
2 was, I think initially, a 76 percent increase, which
3 was rejected by the FERC, and then later on, there
4 was a 62 percent rate increase, and so each time I
5 was asked to look to see what was done.

6 Q. And in May of last year, the throughput
7 amount was still a little uncertain as to what
8 Olympic would be able to put down its system at
9 reduced pressures; is that a fair statement?

10 A. I can look at the exhibit and look at the
11 actual throughput. I don't know whether that's the
12 case or not. I wasn't -- wasn't here.

13 Q. The difference between the earlier request
14 for rate increase and the later rate request was
15 reduced because of an increase in throughput; is that
16 a fair statement?

17 A. Well, yeah, that's a fair statement. I
18 didn't want to mischaracterize -- or if I did, no.

19 Q. And in general terms, because of the high
20 fixed costs that a pipeline has, the more throughput
21 you have means the lower the cost per barrel, isn't
22 that a truism?

23 A. That's a truism, yes.

24 Q. And so the faster this pipeline can get its
25 throughput increased, the lower the tariff rate will

01185

1 be on a per-barrel basis; correct?

2 A. That would be the general proposition, yes.

3 Q. Okay.

4 A. You mean, as soon as you can get it up to
5 one hundred percent?

6 Q. Sure. And in your testimony, you included,
7 I believe, a couple of exhibits. And in fact, one
8 exhibit that puts the -- I believe you've got the
9 actual throughput numbers for '97 through '01, and
10 maybe even before. I put them up here in blue, just
11 for reference. Do you see that on this chart?

12 A. Logistics are there. Yes, I do.

13 Q. Okay. And do those correspond to what you
14 understand, in '97, the throughput was about 116
15 million barrels a year; '98, it was 116; '99, 87?

16 A. Yes.

17 Q. 2000, 63; and in 2001, 83; correct?

18 A. Yes, and noting that 2001, I believe the
19 numbers we were using that were provided by Olympic
20 were, I think, estimates for December and possibly
21 November.

22 Q. Correct.

23 A. But in that regard, I doubt -- I'm not
24 going to say I doubt they were that much higher, that
25 much off, but --

01186

1 Q. They could be. They were just estimates?

2 A. They were just estimates.

3 Q. Do your best and make estimates.

4 A. Absolutely.

5 Q. That's what was done in May in that rate
6 filing, they were trying to make estimates of what
7 the throughput would be. Is that your understanding
8 at the time that you were involved in that
9 proceeding?

10 A. At the FERC, I would say what they were
11 doing was trying to present a representative year of
12 throughput.

13 Q. Right. And when they had actuals, they
14 could do a better job?

15 A. Well, not necessarily would that impact the
16 rate case or the rate filing. If no one had
17 protested a rate filing and certain throughput was
18 used and that went into effect without refund,
19 certainly if the throughput went up 10 percent in the
20 next two months, I doubt they would come back in and
21 say, Gee, our rates should be adjusted downwards
22 because our throughput went up.

23 Q. Now, in '97 and '98, when the throughput
24 was 116 million barrels, and let's say you had costs
25 of a certain amount, whatever that amount might be.

01187

1 A. Right.

2 Q. Then you go off into the next three years
3 and you have throughput significantly less. Those
4 fixed costs have to necessarily be recovered from a
5 much smaller number of barrels, thereby increasing
6 fairly dramatically the cost per barrel of shipping;
7 is that correct?

8 A. Or those fixed costs could be reduced in
9 some manner.

10 Q. But all other things being equal, the fewer
11 barrels you have, the higher the cost per barrel?

12 MR. BRENA: Asked and answered.

13 MR. MARSHALL: Okay. I'll move on to the
14 next question.

15 Q. Then what I'd like to show you is -- I
16 think it's your exhibit with a graph, it's 115, and
17 I'm going to --

18 A. Thank you.

19 Q. I'm going to ask you --

20 A. I was given two copies.

21 Q. Yes. I was going to ask you to mark on
22 this extra copy of your Exhibit 115 where it was that
23 BP took over operation under the contract with
24 Olympic to operate Olympic Pipe Line?

25 A. I believe that was June 2000, subject to

01188

1 check.

2 Q. Okay. Could you just draw a line extending
3 upward through that graph, June 2000?

4 A. How far would you like me to go?

5 Q. Just all the way up to the top of that
6 shaded area.

7 A. Got it.

8 Q. Then do you know when it was that BP
9 acquired the 25 percent of the GATX shares?

10 A. I believe I've seen September 2000 in the
11 Form Six that was filed as the date.

12 Q. Could you draw a line up from that, just
13 label that GATX? Now, do you have any information in
14 any of the materials here that BP Pipelines, as
15 operator of Olympic, has done anything less than to
16 try to get the throughput up as rapidly as possible
17 to restore the pipeline to a level where the price
18 per barrel could be reduced?

19 A. Could you repeat that?

20 Q. Sure. Maybe I'll make it more simple for
21 you.

22 A. Yeah, good.

23 Q. Do you know any evidence that BP Pipelines,
24 as the operator of Olympic, has not been doing all it
25 can to try to get the throughput back up to

01189

1 historically normal levels?

2 A. Do you mean are they responding to the
3 orders of the Office of Pipeline Safety to do what
4 needs to be done?

5 Q. Yes, are they doing all they can, in your
6 opinion?

7 A. I have really no opinion or not as to
8 whether they are doing all they can.

9 Q. Do you have any opinion to the contrary,
10 that they're doing less than --

11 A. Oh, no.

12 Q. -- everything possible?

13 A. No, I'm not an engineer, so I don't know
14 whether they're doing everything they -- I'm just
15 assuming that they're meeting the requirements that
16 have been set down to get the pipeline back online,
17 and I think it's a reasonable assumption that they'd
18 want to get it to one hundred percent of where it was
19 before.

20 JUDGE WALLIS: I'm going to interject here,
21 ask to go off the record for just a moment.

22 (Discussion off the record.)

23 JUDGE WALLIS: Let's be back on the record,
24 please. Mr. Marshall, you wish to have the document,
25 page three of three of the witness' Exhibit Number

01190

1 115 marked as a separate exhibit, the document that
2 the witness has marked; is that correct?

3 MR. MARSHALL: Yes, Your Honor, if we could
4 mark it 115-A or R or whatever.

5 JUDGE WALLIS: Are the parties content with
6 calling that 115-A?

7 MR. TROTTER: That's fine.

8 JUDGE WALLIS: Let's do so. Is there
9 objection to its receipt?

10 MR. BRENA: There is none.

11 JUDGE WALLIS: Let the record show that
12 there is no objection and the exhibit is received.
13 May we have the exhibit, please? Mr. Marshall, does
14 that conclude your questioning?

15 MR. MARSHALL: Yes, it does, Your Honor.

16 JUDGE WALLIS: For Commission Staff.

17 MR. TROTTER: No questions of Mr. Grasso.

18 JUDGE WALLIS: From the Bench.

19

20 E X A M I N A T I O N

21 BY CHAIRWOMAN SHOWALTER:

22 Q. Mr. Grasso, thank you for staying here till
23 the bitter end.

24 A. You're certainly welcome.

25 Q. It seems that any time I ask a question, it

01191

1 generates a round of other cross-examination, so I'm
2 going to begin very safely, with your address. I
3 notice that you operate out of Bethesda, Maryland?

4 A. Yes, I do.

5 Q. Which is where I grew up.

6 A. Oh, my.

7 Q. I'm a graduate of Walt Whitman High School.

8 A. Oh, wow.

9 Q. And I can see Mr. Marshall's thinking -- he
10 can ask about if we went to the same law school. I
11 do -- I want to draw your attention to page seven of
12 your testimony.

13 A. I am there.

14 Q. Line 17, you say, In the last three months.
15 What months were those?

16 A. Those were the months of September, October
17 and November. Those are the months on the
18 spreadsheets that I was working from.

19 Q. Okay. And then, are the figures there,
20 lines 17 and 18, do they include revenues that
21 resulted from the FERC-authorized increase?

22 A. Yes, they do.

23 Q. And is your answer the same for the
24 paragraphs that are at the bottom of page seven and
25 then going on through the middle two-thirds of page

01192

1 eight?

2 A. Yes, in using the company's financial
3 statements that were provided to me, it included all
4 revenue, all expenses.

5 Q. Okay.

6 A. Or it included the figures they included,
7 which included the FERC revenue.

8 CHAIRWOMAN SHOWALTER: Okay. Thank you. I
9 have no further questions.

10 JUDGE WALLIS: Is there anything further of
11 the witness?

12 MR. MARSHALL: I forgot that question.
13 Thank you.

14 MR. BRENA: I have a couple questions.

15

16 R E D I R E C T E X A M I N A T I O N

17 BY MR. BRENA:

18 Q. Mr. Grasso, what was the company's
19 throughput in July of 2001?

20 MR. MARSHALL: It's in the testimony, Your
21 Honor, so it's just repetitive.

22 MR. BRENA: So was every question Mr.
23 Marshall asked with regard to the dates. I'd just
24 ask for your indulgence. It's a preliminary
25 question.

01193

1 JUDGE WALLIS: Very well. Under the
2 representation that there are few questions and in
3 order to have the information tied together on one
4 page, the witness may respond, if the witness knows
5 the answer.

6 THE WITNESS: I have, in millions of
7 barrels, 9.6, approximately, for the month. If I can
8 get my calculator, I can give you the daily. That's
9 probably around 310,000, possibly.

10 Q. You were asked whether the company was
11 doing all it can to get its throughput up, but when I
12 look at this chart, its throughput in that month
13 spikes above any throughput that it's had since, so
14 my question to you is does that suggest that the
15 company isn't doing all it can to keep its throughput
16 up?

17 MR. MARSHALL: You know, it's a leading
18 question. This witness actually stated on cross that
19 he didn't have any opinion that the company was doing
20 anything less than it could possibly do. Now the
21 Counsel is suggesting another answer to the witness.

22 MR. BRENA: I'm exploring the witness'
23 answer, that's correct. I'm not sure that's an
24 objection to redirect, though.

25 MR. MARSHALL: It's an objection to the

01194

1 leading question. It suggests the --

2 JUDGE WALLIS: I think it's not an
3 objection to redirect, but I am concerned that the
4 witness has already stated that he has no knowledge,
5 and on that basis, I think I would sustain the
6 objection.

7 Q. Is there anything in this chart that
8 suggests that the current throughput isn't as high as
9 it could be?

10 MR. MARSHALL: Same objection, particularly
11 given the prior --

12 JUDGE WALLIS: The witness may respond.

13 THE WITNESS: Did you say is there anything
14 in this chart?

15 Q. Yes.

16 A. That could suggest that?

17 Q. Well --

18 A. Well, the fact of the matter is is that
19 there's been nothing as high as July of 2001.

20 Q. Okay.

21 A. Now, that tells me that they were able to
22 get through in July of 2001, and I believe that's
23 when the four refineries all came on, online, that
24 for some reason they were able to get through over
25 300,000 barrels in that particular month. I don't

01195

1 think it's approached 300,000 barrels, and to that
2 extent, well, maybe that would raise a question as to
3 whether they could, at some point right now, approach
4 or on a consistent basis 300,000 barrels or more a
5 month.

6 Q. So far as you're aware, was the pressure
7 restriction in effect during that month?

8 MR. MARSHALL: Well, there's no foundation
9 that he knows what restrictions apply. I think this
10 witness has demonstrated he doesn't have the
11 knowledge necessary to respond to Mr. Brena's
12 suggestions.

13 JUDGE WALLIS: I'm not sure that the
14 witness' knowledge is any more than he indicated
15 earlier, in that his last testimony seemed to be
16 largely speculation. And I think I would sustain the
17 objection.

18 Q. Do you know, do you have knowledge of when
19 the pressure restriction went into effect?

20 A. I have knowledge that the pressure
21 restriction is 80 percent of operating pressure from
22 testimony and from whatever I've read. I also know
23 that they're shipping about 91 percent of the 1998
24 throughput. How soon after that pressure restriction
25 went into effect after the June 1999 accident, I am

01196

1 not aware, but I am sure -- I would say within a few
2 months, if not right away.

3 MR. MARSHALL: Well, I'd move to strike.
4 It's totally speculative. This witness doesn't have
5 any foundation to know when the pressure restriction
6 went into effect.

7 JUDGE WALLIS: The witness indicated that
8 he had no knowledge.

9 Q. Mr. Grasso, when you spoke earlier, I think
10 you said 300,000 barrels a month. Did you mean 300
11 thousand barrels --

12 A. Three hundred barrels a day, yes. I'm
13 sorry.

14 Q. Is it your understanding that the system is
15 over-nominated?

16 A. That is my understanding. And I understand
17 that it's because of that volumes are pro-rated.

18 Q. Okay. Are you aware of any reason
19 whatsoever why this company can't operate at its July
20 levels?

21 MR. MARSHALL: Your Honor, again, I think
22 it's been established that this witness doesn't know
23 enough of the facts. That was the purpose of my
24 cross, was to establish lack of knowledge, and now
25 Counsel is trying to go into an area that I think the

01197

1 witness himself has foreclosed.

2 MR. BRENA: That would -- my question was
3 to test his knowledge. Is he aware of any reason why
4 they can't continue to operate at their July level?

5 JUDGE WALLIS: I do think that that's
6 repetitive of the earlier questioning, and he has
7 indicated that he has no knowledge. And I think the
8 objection should be sustained.

9 Q. Chairwoman Showalter asked you, with regard
10 -- whether you took into consideration total company
11 revenues and total company costs?

12 A. Yes.

13 Q. Do you recall that line of questions?

14 A. Yes, I do.

15 Q. Is there any reason you would take into
16 consideration only a part of the FERC revenues, but
17 all of the FERC cost?

18 A. There's absolutely no reason why I would do
19 that.

20 Q. If there was going to be some sort of
21 jurisdictional pro-ration, wouldn't you expect it to
22 go not only to the revenue side, but also to the cost
23 side?

24 A. Absolutely. I believe the increase at the
25 FERC -- I believe that the rates that are in effect

01198

1 at the FERC are designed to recover -- to recover
2 increased costs, as well, and those are certainly
3 within, I think, Staff's analysis. So if it's there,
4 then I would include the revenue.

5 Q. You were asked about which were the last
6 three months in your testimony. Do you recall that
7 question?

8 A. Yes, I do.

9 Q. And taking into consideration all the
10 company's revenues and all of the company's costs
11 from both jurisdictions in total, is this company
12 making money?

13 A. That's what my exhibit shows, yes.

14 MR. BRENA: No further questions.

15 JUDGE WALLIS: Is there anything further?

16 CHAIRWOMAN SHOWALTER: Just one, and I
17 challenge anyone to ask a question that relates to
18 this.

19 MR. BRENA: The challenge is accepted.

20 CHAIRWOMAN SHOWALTER: Mr. Brena will find
21 a way.

22

23

E X A M I N A T I O N

24 BY CHAIRWOMAN SHOWALTER:

25 Q. But on Exhibit 115, the graph, the chart,

01199

1 on the left-hand access of millions, there actually
2 is no unit here. Can you put in the unit for me?

3 A. Those are monthly barrels.

4 Q. So this is millions of barrels per month?

5 A. That's right.

6 Q. Or it's just -- actually, just millions of
7 barrels?

8 A. That's right.

9 CHAIRWOMAN SHOWALTER: Oh, all right.
10 Thank you.

11 MR. BRENA: I lost that one.

12 JUDGE WALLIS: I don't think the door
13 opened very wide.

14 MR. BRENA: Yes.

15 JUDGE WALLIS: Very well. Mr. Grasso, I
16 think we're done with you, and you may be excused
17 from the stand at this time.

18 THE WITNESS: Thank you very much.

19 JUDGE WALLIS: We do have some
20 administrative matters to address. Let's take a
21 brief recess, and then we will take up those
22 administrative matters.

23 (Recess taken.)

24 JUDGE WALLIS: Let's be on the record,
25 please, following a brief recess for some

01200

1 administrative discussions.

2 We have discussed the pros and cons of
3 various means of dividing time at the oral argument.
4 The Commission has blocked off two hours for that
5 argument on January 23rd in this room, beginning at
6 1:00 p.m., and we have in mind the suggestions of the
7 parties regarding the division of that time.

8 We understand that it is a limited time and
9 we intend to provide a letter of notice to the
10 parties tomorrow by fax that identifies the breakdown
11 of that time. We understand that while Tesoro and
12 Tosco are combined in their presentations to some
13 regard, that there are some differences that they
14 would like to present and argue individually, and we
15 understand, also, that the company would like the
16 time to respond to all of the parties and to provide
17 a rebuttal.

18 Let's move on to the exhibit list. Tesoro
19 has provided a document that identifies which of its
20 proposed exhibits on cross-examination were used in
21 the cross-examination of various witnesses. And it
22 asks that the Commission admit to the record those
23 documents that were used in the examination.

24 Mr. Marshall has indicated some
25 reservations about Exhibit Numbers 43, which is an

01201

1 indictment; 49, which is a reprint of a statute; and
2 Exhibit 54, which is a version of Exhibit 10, which
3 has already been admitted. Mr. Marshall, did I state
4 your concerns with sufficient eloquence or would you
5 like to add to those?

6 MR. MARSHALL: Well, actually, on the
7 Exhibit 49, on the laws here, I've looked at this
8 further and I think they're mixing and matching.
9 They not only have a statute under Chapter 81, but
10 then they have a number of Washington Administrative
11 Codes under Title 80 that they have attached here. I
12 see this is about a nine-page exhibit. I think
13 they've got it confused.

14 With regard to what notice and so forth
15 must be given, I would just as soon not have any of
16 that in and have Counsel make sure he hasn't
17 scrambled the two titles together. It sure looks
18 like it to me. So when ordinarily you wouldn't have
19 any problem with just duplicating a piece of statute,
20 I think having it as an exhibit may provide an
21 implication that just isn't applicable here.

22 JUDGE WALLIS: Very well. Why don't we, in
23 light of that comment, allow Mr. Brena the
24 opportunity to respond by day after tomorrow with
25 whether he believes that the exhibit is an accurate

01202

1 reflection of the RCWs, and we will take it from
2 there.

3 MR. BRENA: As I understand it, it's 43, 49
4 and 54. With regard to 54, his objection is well
5 taken. That it is in complete form in Mr. Batch's
6 Exhibit 10, so with that comment, I would withdraw
7 offering that duplicative record into the record.

8 JUDGE WALLIS: Very well.

9 MR. BRENA: With regard to Number 43, I
10 would ask that it be admitted. From Tesoro's
11 perspective, this is a case about responsibility.
12 And there was testimony with regard to the company's
13 responsibility for Whatcom Creek. I believe that
14 their responding testimony was is that Whatcom Creek
15 was about a contractor that had 24 debts, so there
16 was specific testimony with regard to -- in which, as
17 I saw it, the company tried to distance itself from
18 responsibility for Whatcom Creek.

19 I think that, in addition to the issue of
20 responsibility, which is what I view as one of the
21 central issues in the case, there is the issue of
22 prudence. When you talk about prudently incurred
23 costs being the only ones that a shipper is entitled,
24 is responsible for paying, and you have behavior in
25 which there has been criminally indicted, then it

01203

1 certainly raises and supports the scepter of
2 prudence.

3 So I think I asked the witnesses questions
4 about this. This exhibit goes to some of his
5 responses trying to distance the company from
6 responsibility for Whatcom Creek, and it goes to the
7 prudence of the inclusion of those costs.

8 Now, we can argue what issues should be in
9 what docket, but that is a matter of legal argument,
10 and the best evidence rule applies and our position
11 is different than theirs.

12 JUDGE WALLIS: Mr. Trotter, what are your
13 views on this, if any?

14 MR. TROTTER: Well, Exhibit 43, the
15 indictment was examined. That exhibit was examined
16 during cross, it is what it is. I think the
17 Commission needs to understand it is just an
18 indictment and not a conviction. But it was covered
19 in cross and it is relevant to that.

20 On Exhibit 54, although it's been
21 withdrawn, but I just -- I guess I would ask that it
22 stay in the file and maybe a note be put on that
23 Exhibit 10 is the complete copy, because if the
24 Commission goes to the cross, sees that exhibit
25 reference, goes to the exhibit and there's nothing

01204

1 there, then the record's incomplete. But I don't
2 have any problem with the withdrawal, if that note
3 can be attached to the record.

4 JUDGE WALLIS: Very well. We will make
5 that note on the official exhibit list. And what I
6 would propose is that I will circulate the official
7 exhibit list updated, and the parties, no later than
8 the time of the argument, will have an opportunity to
9 offer corrections to that, and we will consider that
10 to be a part of the record and, in that document, we
11 will provide that cross-reference.

12 Mr. Marshall, would you like to address
13 Exhibit 43?

14 MR. MARSHALL: Absolutely, Your Honor.
15 These are nothing but allegations. They have not
16 been proven. They probably never will be proven.
17 They are, in the essence of federal and state rules
18 of evidence, highly prejudicial. We don't know who
19 made these allegations, with what evidence, we have
20 no foundation for any of the allegations in this
21 case. I objected to it in a timely way during
22 cross-examination, and it was said that we could look
23 at the front sheet of this. But it was not inquired
24 in further in any of the details of the indictment
25 and we didn't want the cross-examination to go into

01205

1 this arena.

2 Mr. Brena elicited from Mr. Batch, over our
3 objections in this area, the question and answer that
4 he made. He can't open the door by himself on his
5 own exhibit here, which, again, is nothing but a
6 collection of prejudicial allegations. So I most
7 strenuously object to this. I don't say strenuously
8 very often, but this one is beyond the pale.

9 JUDGE WALLIS: Very well. What I would
10 propose to do with this is to review the transcript
11 when it's available, in light of your argument this
12 evening. I would say that we are especially blessed
13 to have three Commissioners who are all lawyers and
14 who can, by dint of their training and experience,
15 identify the difference between a conviction and mere
16 indictment. So I don't mean to, by that, signal a
17 ruling, but I do mean to indicate that it's not as
18 though we are sending something to a jury and that we
19 have some very sophisticated and capable
20 commissioners who will be reviewing this evidence.

21 MR. MARSHALL: But it is difficult to take
22 out of your mind something that may have absolutely
23 no factual foundations at all, regardless of
24 training. I can't.

25 JUDGE WALLIS: We will review the record

01206

1 and we'll make a ruling after doing so.

2 MR. BRENA: If I may briefly address Number
3 49. You had asked for me to review that and to see
4 if it was complete and to respond the day after
5 tomorrow, I believe was Your Honor's ruling.

6 JUDGE WALLIS: Yes.

7 MR. BRENA: I'd just say that an option
8 certainly that I would consider, to the degree that
9 there is any confusion in the exhibit, that I would
10 propose to offer a 49-R, which would just have only
11 the information which was cross-examined on and not
12 have extraneous information.

13 JUDGE WALLIS: Very well. After your
14 review, please determine which course you wish to
15 take, and we will respond accordingly. All right.

16 Again, I want to thank everyone and commend
17 you for the level of professionalism and skill that's
18 been demonstrated, and we look forward to seeing you
19 at the time of oral argument on January 23rd, at 1:00
20 in this room.

21 MR. RYAN: Thank you, Your Honor.

22 MR. FINKLEA: Thank you, Your Honor.

23 (Proceedings adjourned at 6:44 p.m.)

24

25

