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BEFORE THE WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND)
TRANSPORTATION COMMISSION,)
)
Complainant,)
)Docket No. TO 011472
vs.)Volume XXV
)Pages 2766 to 2952
OLYMPIC PIPELINE COMPANY, INC.,))
)
Respondent.)

A hearing in the above matter was held on June 25, 2002, at 9:30 a.m., at 1300 South Evergreen Park Drive Southwest, Room 206, Olympia, Washington, before Administrative Law Judge ROBERT WALLIS, CHAIRWOMAN MARILYN SHOWALTER, COMMISSIONER RICHARD HEMSTAD, and COMMISSIONER PATRICK OSHIE.

The parties were present as follows:

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Court Reporter

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 BENCH REQUESTS (NONE)

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PROCEEDINGS

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JUDGE WALLIS: Good morning. Let's be on the record for our Tuesday June 25, 2002 session in the matter of Commission Docket TO 011472.

7

8

9

10

By way of preliminary matters this morning, parties indicated as follows: The Staff intends to present some exhibits on cross examination based on the depositions that occurred.

11

12

13

14

15

16

Tesoro intends to offer the depositions that occurred on Monday, yesterday, into the record. And Staff has discovered some minor errors in its exhibit, and, if necessary, will provide an errata sheet that indicates those as to each of the affected exhibits.

17

18

Is there anything else of a preliminary nature?

19

(No response.)

20

21

JUDGE WALLIS: Let the record show there's no response.

22

23

By arrangement, we begin today with the testimony of Larry Peck on behalf of Olympic.

24

25

Mr. Peck, would you please stand and raise your right hand.

2773

1

2

LAWRENCE PECK,

3

produced as a witness in behalf of Olympic Pipeline,

4

having been first duly sworn, was examined and testified

5

as follows:

6

7

JUDGE WALLIS: In conjunction with

8

Mr. Peck's appearance there has previously been

9

marked his rebuttal testimony LP1-T as Exhibit 501-T

10

in this proceeding.

11

CHAIRWOMAN SHOWALTER: Can you wait just

12

one second.

13

(Brief recess.)

14

15

DIRECT EXAMINATION

16

17

BY MR. BEAVER:

18

Q Dr. Peck, could you please state your full

19

name?

20

A My full name is Lawrence B. Peck.

21

Q And do you have a doctorate?

22

A Yeah, I have a Ph.D., yeah.

23

Q What is that in?

24

A In chemical engineering.

25

Q Do you prefer "Mr." or "Dr."?

2774

1 A Everyone calls me "Mr." except my
2 mother-in-law.

3 Q Mr. Peck, do you have in front of you
4 Exhibit 501-T?

5 A I do.

6 Q That is your prefiled rebuttal testimony?

7 A Yes, it is.

8 Q And you have reviewed that?

9 A I have reviewed it again, yes.

10 Q If the questions in Exhibit 501-T were
11 asked you today, would the answers as set forth in
12 that exhibit be your answers today?

13 A Yes, they would.

14 Q Do you have any changes you would like to
15 make to Exhibit 501-T?

16 A No, no changes.

17 Q Do you adopt the testimony set forth in
18 Exhibit 501-T as your testimony?

19 A Yes.

20 MR. BEAVER: Your Honor, we offer Exhibit
21 501-T.

22 JUDGE WALLIS: Is there objection?

23 (No response.)

24 JUDGE WALLIS: Let the record reflect
25 there is no objection, and 501-T is admitted.

2775

1

(EXHIBIT ADMITTED)

2

MR. BEAVER: Thank you. Your Honor,

3

Mr. Peck is now available for cross examination.

4

5

CROSS EXAMINATION

6

7

BY MR. TROTTER:

8

Q Good morning, Mr. Peck.

9

A Good morning.

10

Q At page 1 of Exhibit 501-T you indicate you

11

are the general manager of the products business

12

line for BP Pipelines, as well as chairman of the

13

board of directors of Olympic Pipeline Company; is

14

that correct?

15

A That's correct.

16

Q Do you have input into any decision that BP

17

ARCO would make to either loan additional money, or

18

infuse equity into Olympic so that it might carry

19

out its obligations as a public service company?

20

A I would have input, yes.

21

Q Would that be in your role as the general

22

manager of the product business line?

23

A Correct.

24

Q Do you have input into the decision that

25

Olympic would make to ask BP ARCO for additional

2776

1 money by way of loan or equity infusion so it may
2 carry out its obligations as a public service
3 company?

4 A Yes. That request would have to come from
5 Olympic via vote of the board of directors, so I
6 would have one of five votes.

7 Q How many votes do you have with respect to
8 the decision by BP ARCO to loan additional money, or
9 provide equity capital to Olympic?

10 A I don't get any votes in that decision. I
11 only get to recommend.

12 Q And who do you recommend to?

13 A The recommendation would be to various
14 levels in the management of BP, depending on the
15 size of the money involved. So up to 10 million
16 dollars it's local within the United States
17 management. Above that, it goes to London.

18 With the size of money being talked about
19 here, it would obviously be a decision made in
20 London.

21 Q Has London -- and by London, I take it you
22 means that's the location of BP ARCO's headquarters?

23 A That is our headquarters, yes.

24 Q So we can call that London?

25 A Yeah, that's what I call it.

2777

1 Q Has London given you any written criteria
2 under which it will loan additional money to Olympic
3 or infuse equity into Olympic?

4 A No. And that's really not the way it
5 works. It is a request that would come from us for
6 approval by them, so --

7 Q Has the request been made?

8 A For additional funds?

9 Q Yes.

10 A No, not as yet.

11 Q Please turn to page 3 of your testimony,
12 line 23. You state, quote, "BP ARCO has, as a
13 shareholder has made loans to Olympic in good faith,
14 with safety as our first priority," unquote. Do you
15 see that?

16 A Yes.

17 Q By the word "our" are you referring to both
18 BP ARCO and Olympic?

19 A Yes, that's both.

20 Q So are you testifying here for both BP ARCO
21 and Olympic?

22 A Well, I am testifying here, I suppose, on
23 behalf of both, depending on some questions asked,
24 because I have both roles in my position.

25 Q To the extent BP ARCO made loans to Olympic

2778

1 and the money was used by Olympic for capital
2 improvements, those capital improvements would be
3 recorded on the company's books as assets necessary
4 to provide service for the public; is that correct?

5 A Let me make sure I understand the question.
6 They are recorded on Olympic's books as assets, yes.
7 It's a separate entity.

8 Q I meant -- when I said the company's books,
9 I meant Olympic's books.

10 A Okay.

11 Q At the bottom of page 3 and over to page 4
12 you say, quote, "Ultimately we must also answer to
13 shareholders for the returns they necessarily expect
14 to receive on their investments," unquote. Do you
15 see that?

16 A Yes, I do.

17 Q And by the word "we" are you referring to
18 Olympic and BP ARCO both?

19 A No. This really -- this sentence here is
20 speaking to the BP ARCO view of a further investment
21 via loans to Olympic. I mean, Olympic would have
22 the same questions and make sure they were
23 delivering returns to their shareholders of which
24 there are only two, but in my testimony here, I was
25 really thinking of it more from a BP ARCO

2779

1 perspective.

2 Q So the "we" here refers to BP ARCO?

3 A Right. So that's maybe a little confusing
4 versus the other.

5 Q When you talk about they necessarily expect
6 to receive on their investments, those would be --

7 A Shareholders and BP.

8 Q And by return on their investments, or
9 returns on BP ARCO's investments, are you referring
10 to a return on the 150 million in debt Olympic has
11 on its books, or only the debt issues by Olympic to
12 BP Company?

13 A BP's shareholders certainly expect a return
14 on their money invested in BP. Olympic's
15 shareholders, I suppose, might like to have a return
16 on their investments.

17 Q So --

18 A But at this time, it's relatively unlikely.

19 Q So for purposes of your testimony here, are
20 you only referring to the loans that BP itself made
21 to Olympic?

22 A As opposed to what else? I'm not sure I
23 understand.

24 Q As opposed to the rest of the loans that
25 make up the 150 million in debt currently

2780

1 outstanding.

2 A Well, each of those loans are made by
3 somebody who expects a return. But I would speak on
4 behalf of BP.

5 Q I will represent to you on page 726 in the
6 hearing in this case, Mr. Batch, the president of
7 Olympic Pipeline stated, quote, "The shareholders
8 are looking at Olympic as a stand-alone corporate
9 entity that needs to make a profit on its own
10 standing," unquote. Do you agree with that
11 testimony?

12 A Yes. The shareholders being BP and Shell.
13 That would be their view. I am sure -- I mean, I
14 can't speak for Shell, but I expect that would be
15 their view.

16 Q You mentioned Shell. Has Shell taken over
17 Equilon Corporation?

18 A Yes.

19 Q When did that occur?

20 A Within the past six months.

21 Q You recommend this Commission should look
22 at Olympic as a stand-alone company in this case?

23 A Yes, I believe Olympic needs to be viewed
24 as a stand-alone company.

25 Q On page 4 of your testimony, line 10 --

2781

1 A Okay.

2 Q You are referring to a potential refund
3 liability of approximately 17 million dollars by
4 September of this year. Do you see that?

5 A I do.

6 Q Are you advocating that as a reason for
7 this Commission to grant Olympic's 62 percent rate
8 increase so there would be no refund liability?

9 A Well, I guess I am certainly advocating a
10 substantial tariff increase as necessary for Olympic
11 to continue to do what it needs to do. I would say
12 my expectation is that we will not achieve a 62
13 percent increase, so we will have to deal with some
14 type of refund issue. These numbers would be if
15 there was no increase or a half percent increase.

16 Q But I take it you would agree that the
17 Commission needs to address the issues of cost of
18 service on the merits, and not be guided by whether
19 or not refunds will result from whatever order they
20 issue. Would you agree with that?

21 A Well, I think the Commission needs to
22 consider all the ramifications of the decision they
23 will make as they look at the tariff that Olympic is
24 allowed to charge. And so if that decision includes
25 the requirement of a refund, then that refund is

2782

1 part of the cash needs that the company will have.
2 So I would think that would need to be considered.

3 Q Isn't it correct that Olympic asked that
4 the interim rate that it requested before this
5 Commission be granted subject to refund?

6 A Well, I think -- at least it was my
7 understanding that that was all that was available,
8 the same as at the FERC, is an interim rate that is
9 refundable.

10 Q So it's not your understanding that every
11 other interim rate relief grant, except for Olympic
12 and one other case, were not subject to refund? You
13 did not have that understanding?

14 A I did not know that, if that's true.

15 Q In your testimony you indicate that of the
16 17 million, three million is related to this
17 jurisdiction?

18 A Right. And you know, those numbers I have
19 to take from someone else. I believe those to be
20 the right numbers.

21 Q On line 17 of page four of your testimony
22 you indicate that Olympic has not paid dividends
23 since 1997; is that correct?

24 A To the best of my knowledge, that's
25 correct. I have only been on the board since 2000

2783

1 and BP, of course, was not an owner until 2000. But
2 I believe that's correct.

3 Q I want to be precise. Olympic, in fact,
4 paid dividends in 1997, but not thereafter?

5 A Not thereafter. I think that's right.

6 Q And that was before the Whatcom Creek
7 explosion, right?

8 A Sometime before that, yeah.

9 Q And shortly before the Whatcom explosion,
10 Olympic was making major investments in both the
11 Bayview terminal and the Cross Cascades project,
12 correct?

13 A That's correct.

14 Q And 1996 and '97, Olympic spent of 27
15 million on construction, and it was planning to
16 spend over 25 million in 1998 primarily for those
17 projects, correct?

18 A Maybe I am not the best person to ask about
19 history, but those numbers sound about right.

20 Q At the top of page 3 of your testimony you
21 indicate -- that actually starts on page 2, quote,
22 The real rate of return expected by large oil
23 companies like Olympic's owner and most of its
24 shippers is in excess of 15 percent, far above the
25 modest 7 percent which BP ARCO and Shell are

2784

1 charging for their loans, interest that, up-to-date,
2 is not being paid, unquote. Do you see that?

3 A Yes.

4 Q Do Olympic's owners expect to recover
5 through rates interest rates attributable to past
6 periods that have been deferred and accumulated by
7 Olympic?

8 A I would say, yes.

9 Q Does Olympic expect to recover costs, the
10 recovery of which would constitute retroactive
11 making?

12 A Well, I am not sure I know how to answer
13 that.

14 Q Now, the approximate seven percent interest
15 rate BP ARCO and Shell are charging for loans to
16 Olympic is the cost of that debt, is it not?

17 A It would be an approximation of the debt --
18 it's the cost of the debt to Olympic, for sure, and
19 it's an approximation of the cost of the debt to the
20 big company that loans it money.

21 Q If BP ARCO required a 15 percent return,
22 why did it loan money at 7 percent?

23 A Well, the money loaned so far was loaned to
24 accomplish a number of things really aimed at
25 improving the safe operation of the pipeline and

2785

1 allowing us to restart the north end of the pipeline
2 that had been shut down. And that restart of the
3 north end created a return beyond 7 percent for BP
4 as a whole, and so it was worth it to BP at that
5 time to invest the money that was required to get to
6 where we are today.

7 Q And that's because Olympic would invest in
8 plant and services, and through the rate making
9 process it would a return on that investment. Is
10 that what you have in mind regarding the greater
11 return later?

12 A Olympic hasn't really earned much of a
13 return as yet. It's still running in the red. But
14 BP, through the restart of the north end of the line
15 that was shut down, was able to earn more than it
16 otherwise would have had the line stayed down. So
17 that gives BP a return beyond the 7 percent that it
18 hopes to get on the loan to make up the difference.

19 Q So what you are saying is that by
20 restarting the line up to 80 percent pressure, BP
21 ARCO has benefited a shipper through substantially
22 reduced transportation costs?

23 A That's correct.

24 Q And they were substantially reduced
25 compared to water-borne alternatives; is that

2786

1 correct?

2 A That's correct.

3 Q And do you know how much they were
4 substantially reduced?

5 A No, not right offhand. Someone at ARCO
6 would be better qualified to answer that question,
7 but water-borne is typically a lot more expensive.

8 Q So it's not a cost effective alternative
9 for BP ARCO, is it?

10 A Well, it is a cost effective alternative,
11 and we use it even when the pipeline is running.

12 Q Well, let me ask it this way. If pipeline
13 capacity is available, water-borne transportation is
14 not an effective alternative?

15 A That's not your first line; you would
16 rather use the pipeline.

17 Q That's because it is substantially cheaper?

18 A Correct.

19 Q So when you refer to the 15 percent return,
20 are you referring to -- I take it you are not
21 referring to return on rate base established through
22 the rate setting process; is that correct?

23 A That's correct. It would be the return
24 that BP would see on its investment.

25 Q And that would include the benefits BP gets

2787

1 as a shipper?

2 A Correct.

3 Q In the interim rate relief phase of this
4 case, we discussed the note Olympic issued to
5 Prudential. Are you familiar with that note?

6 A I have some familiarity.

7 Q We can ask Mr. Batch, so if you wish to
8 defer to him, feel free to do so. But I will start
9 with you.

10 A Okay.

11 Q That note is still outstanding, is it not?

12 A It is.

13 Q Are you aware that there's a condition that
14 precludes Olympic from incurring any debt from
15 either external or internal sources?

16 A I am aware that there is a condition in the
17 note to that effect. I don't know the details.

18 Q Do you know whether that condition has been
19 waived or not?

20 A I know it has been waived for the most
21 recent borrowing that Olympic did from BP.

22 Q And was that the June 22nd, 2001 ARCO note
23 setting up the credit line?

24 A Right, yes.

25 Q And that June 22nd, 2001 ARCO note was a

2788

1 revolving credit line, and the remaining credit
2 balance available to Olympic is around 20 million
3 dollars; is that correct?

4 A The note was written, I believe, for 30
5 million dollars, and BP has so far loaned 10. But
6 the note isn't -- it's not a revolver the way you
7 talked about it in the sense that Olympic has no
8 demand on the rest of the money.

9 Q Right. But -- and you were focusing on my
10 use of the word "available"?

11 A Right. In other words, it's BP's choice
12 whether or not to loan the rest of that 30 million.

13 Q Let's be precise. The loan was a maximum
14 amount of 30 million, and 10 million has been
15 released to Olympic?

16 A Correct. Correct.

17 Q So there's 20 million dollars sitting
18 there, and it's up to BP to determine whether or not
19 Olympic will get it. Is that a fair statement?
20 It's BP's choice?

21 A It would be BP's choice whether to loan any
22 additional funds or not under that particular note.

23 Q So other than that 20 million dollars, as
24 you understand the condition of that Prudential
25 note, there could be no other loans to Olympic,

2789

1 either externally or internally, correct?

2 A I believe that was the condition in the
3 note, yes.

4 Q Are you aware of any conditions in writing
5 issued by ARCO under which it will permit Olympic to
6 access the remaining 20 million dollars on the June
7 22nd, 2001 ARCO note?

8 A I don't believe there's any other
9 conditions in writing other than the note itself.

10 Q And the note itself gives BP ARCO
11 discretion on whether to loan that additional money?

12 A Yes.

13 Q And are you aware of anything ARCO has put
14 in writing as to how it will exercise that
15 discretion, or what specifically Olympic needs to do
16 to get that money?

17 A No, there's nothing I am aware of.

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

20 JUDGE WALLIS: Mr. Brena.

21

22 CROSS EXAMINATION

23

24 BY MR. BRENA:

25 Q Good morning, Mr. Peck. I apologize, but I

2790

1 am curious. What does your mother-in-law call you?

2 A She calls me Dr. Peck.

3 Q Do you believe this Commission should set
4 higher rates in this proceeding to help Olympic pay
5 for the 66 million dollars in future capital
6 improvements that you describe in your testimony?

7 A I believe that the rates need to reflect
8 that need for capital, let me answer the question
9 that way.

10 Q So the rates that are set in this proceeding
11 should be sufficient in order to meet those future
12 capital improvement needs, cash needs?

13 A To the extent that the rates are set high
14 enough to both cover some of Olympic's cash flow
15 deficit it would have without a rate increase, and
16 also to encourage BP to continue to loan money, if
17 that is necessary, then, yes, that's what the rates
18 need to reflect.

19 Q You said to incent BP to loan money.
20 Do you believe this Commission should set rates
21 based on regulatory principles, or based on the
22 amount that is necessary to get BP to loan money if
23 they are different?

24 A Well, I think the Commission has to take --
25 as I said before, the Commission has to take into

2791

1 account all of the circumstances affecting Olympic.
2 And to me, it is a very unique situation, and then
3 use their judgment to put the Olympic Pipeline
4 Company in the position it needs to be in. I
5 don't know if I answered your question very well.

6 Q Well, let me return to it. Let's say
7 there's a gap between the two. Let's say regulatory
8 principles would say rates should be set at \$1, but
9 that in order for BP to loan money, BP says
10 that rates should be set at \$2. What should this
11 Commission do?

12 A Well, I think the Commission needs to look
13 at more than simply theoretical calculational
14 methods of determining what a rate would be, I
15 guess, would be my answer. So I think they would
16 need to look at both of those pieces of information
17 to make a good decision.

18 Q So to the degree that it is necessary, the
19 Commission should abandon regulatory principles and
20 take into consideration an incentive program to get
21 the owner to invest?

22 A Well, I would assume, in general, the
23 regulatory principles are designed to encourage
24 owners to invest in facilities in the state. So to
25 me, I don't think that is an either/or.

1 Q Then you would encourage this Commission to
2 apply those regulatory principles in setting the
3 rates, whatever they may be, and not to deviate from
4 them as though this situation were an exception
5 rather than the rule?

6 A I am not sure I am understanding your
7 question. Again, you are saying as if it's a simple
8 math problem, and all we have to do is solve the
9 math, and come up with the answer. And I don't
10 view it as anything like that simple.

11 Q Well, should this Commission, or should it
12 not, set rates based on standard regulatory
13 principles in this case?

14 A I would assume they should set rates based
15 on good standard regulatory principles in all cases,
16 but I think each case is going to be different on
17 its own merits. So I am not, by any stretch, a
18 regulatory or rate-making expert, so --

19 Q But you are not, by your testimony,
20 intending to encourage this Commission to abandon
21 regulatory principles? You are merely asking them
22 to take into consideration the circumstances in
23 applying those regulatory principles; is that
24 correct?

25 A Yes, I think that's fair.

2793

1 Q Is BP Pipelines currently operating Olympic
2 safely?

3 A I believe BP Pipelines is operating Olympic
4 very safely, yes, or it wouldn't be operating.

5 Q When you say very safely, in your judgment
6 does BP Pipelines operate a pipeline above, below,
7 or average to the industry standards?

8 A First, it's an average industry standard.
9 I believe BP Pipelines, both here and everywhere
10 else we operate, operate well above the average of
11 the industry.

12 Q So is it fair to characterize that it's
13 your judgment that BP's current operation of Olympic
14 Pipeline is well above the industry standard?

15 A That would be my judgment.

16 Q Is it your intention that BP would continue
17 to operate the Olympic pipeline to those same
18 standards, regardless of the outcome of this
19 proceeding?

20 A Well, I am not sure of the answer to that,
21 because if we don't have the money as Olympic -- and
22 let me talk about Olympic will have to look at
23 this -- if Olympic doesn't have the money to pay for
24 the kind of operation that BP, as a pipeline
25 operator would expect to do, it's going to put

2794

1 Olympic in a really tough place. And it's going to
2 put BP Pipelines in a tough place, because I think
3 there's a standard below which BP Pipelines won't
4 operate. And if that costs more than the money
5 Olympic has, then we're in a bad place and I can't
6 tell you what would happen.

7 Q Well, that's my question.

8 A It wouldn't be good.

9 Q What bad place are we in?

10 A Well, at some point, I suppose, if we were
11 unable to attract further funding from our London
12 office, which is certainly conceivable, and Olympic
13 doesn't have the funds to pay BP's operating
14 standard, I think probably what would have to happen
15 is BP would have to resign as the operator and
16 Olympic would have to look for someone else. And we
17 could find someone else -- Olympic could find
18 someone else to operate at a lower standard.

19 Q In your judgment, was the prior operator
20 operating at a lower standard?

21 A In my judgment, yes.

22 Q Now, I mean, it's fair to say either as the
23 operator or the owner of a pipeline -- I mean, you
24 are here as chairman of the board of Olympic, as
25 well as other positions -- there's a huge risk in

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1 cost associated with unsafe operation, isn't there?

2 A There is.

3 Q So when BP, the big company, was
4 considering whether or not to advance funds, is it
5 fair to say they wouldn't only look at the return on
6 those funds, they would also look at the likely
7 consequences of not investing those funds, would
8 they not?

9 A We do on all the pipelines that we own and
10 operate, yes.

11 Q Would it be your testimony that ARCO would
12 have its oil flowing through an unsafely operated
13 line after BP resigned as the operator, and that
14 that would be a cost effective solution for BP and
15 the family of companies?

16 A Well, it would be not unusual for BP or
17 ARCO to be a shipper in a pipeline that is operated
18 to a standard not as high as BP Pipelines operates.
19 There are many, many pipelines in this country. We
20 don't operate anything like all of them. We ship in
21 many that we don't operate. And some of those are
22 not operated to our standard. All of those things
23 are true.

24 Q Do you ship in any line in which you are a
25 majority owner in which you are not the operator?

2796

1 A No.

2 Q So every pipeline in the United States and
3 in the world that BP is the majority owner in, it is
4 the pipeline operator of?

5 A I can't speak for the world.

6 Q Every pipeline that you are aware of.

7 A In the United States those pipelines where
8 we are a majority owner, we are also the operator.

9 Q When you become a majority owner, do you
10 also become the operator when you take over lines?

11 A It isn't necessarily the identical thing.

12 Q Has it ever happened that you have acquired
13 a majority interest in a pipeline and you have not
14 become the operator?

15 A No. Typically it goes the other way.

16 Q Now, I am going to ask you some questions.
17 I am going to try and persuade you that investing in
18 Olympic safety is a good investment for BP the
19 family. Okay?

20 A You bet.

21 Q Do you understand that there is no party in
22 this proceeding that has opposed a single penny of
23 capital improvements relating to safety?

24 A No, I don't understand that.

25 Q Do you understand that Tesoro is saying

2797

1 that Olympic should not recover a single penny of
2 the capital expenditures it has put into safety so
3 far?

4 A It's hard for me to understand what the
5 motivation of the Interveners is. I don't know what
6 their point is on that. I can't answer that.

7 Q And I am just focused on, you are talking
8 about 66 million in future improvements and whether
9 you will get it back, right?

10 A Right.

11 Q So let's talk about that. Is it your
12 understanding that any party in this proceeding has
13 opposed, has suggested taking out of rate base a
14 single penny of capital improvements that were for
15 safety?

16 A Well, I am not sure I know the answer to
17 that. Again, what I have seen is requests for rates
18 that don't support the level of investment that we
19 believe is required for safe operation. So is that
20 the same thing?

21 Q Well, I don't think so.

22 A Okay.

23 Q What I am focused on, if you go put 10
24 million dollars into unit A that increases the
25 safety of the line, are you aware of the fact that

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1 no party in this proceeding has said you shouldn't
2 be able to add that 10 million dollars to your rate
3 base and get the 10 million dollars back, plus a
4 return, plus a tax allowance, plus a return of an on
5 investment? Are you aware of that?

6 A Well, I think that's -- if that is the
7 case, that is a good start.

8 Q So with regard to BP's decision whether to
9 invest money, would it matter to that decision that
10 if it were true that this Commission, and none of
11 the parties -- and I am just, this is a
12 hypothetical -- would say that if you put capital
13 improvements into safety, we will give you an
14 opportunity to get those back. We will give you an
15 opportunity to get your investment back, plus a
16 return on your investment, plus an income tax
17 allowance on the equity portion of the investment,
18 would that matter to you?

19 A If you are asking would BP view this on a
20 stand-alone basis so a simple return on just safety
21 related investments, I do not believe we would view
22 it that way.

23 Q Let me say, all capital expenditures. Are
24 you aware of any capital expenditure that Tesoro has
25 suggested that this Commission disallow, safety or

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1 not safety?

2 A I guess I am not aware either way. I don't
3 know.

4 Q One way or the other?

5 A I don't know.

6 Q Now, if it's true that this Commission can
7 guarantee you that you will get your capital
8 improvements back under traditional rate making
9 related to safety under traditional rate making
10 principles, would you put the money in?

11 A I don't think it's that simple, because
12 this Commission can't guarantee BP it's going to get
13 its money back. I mean, there are over a half
14 billion dollars of outstanding claims against
15 Olympic, not counting the debt that's already on its
16 books. And there is just no way -- that is a very,
17 very high risk situation for anybody to be thinking
18 about investing in.

19 Q In my question I didn't mean to say
20 guarantee. I said an opportunity to recover. Does
21 that change the answer, or is it essentially the
22 same?

23 A I certainly didn't expect a guarantee of
24 return. That's not how business works. But we will
25 view it in the context of the entire situation of

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1 the pipeline, not simply a small incremental
2 investment and a small incremental return.

3 Q Now, with regard to the liabilities that
4 Olympic has, would you agree that a lot of those
5 liabilities are associated with the unfortunate
6 Bellingham Whatcom Creek incident?

7 A Well, many of them are certainly associated
8 with that, or its aftermath, yes.

9 Q With regard to those, the costs that BP has
10 incurred and will incur related to those, would you
11 agree that those costs should not be borne by
12 Olympic's rate payers?

13 A I believe we're not asking for those costs
14 to be borne by Olympic's rate payers.

15 Q Then I am trying to make the full circle.
16 You said in determining whether to invest you would
17 take into consideration the high risk environment
18 created by all of those losses, which I believe you
19 agreed should not be borne by the rate payers.

20 Is It somehow your testimony that the rates
21 in this proceeding need to be high enough so that BP
22 will get a total return, taking into consideration
23 all of those risks that were realized in Whatcom
24 Creek or not?

25 A No. We're not looking for a return to

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1 compensate us for the money that was spent because
2 of the accident. I think what I was trying to
3 explain was Olympic, the company, has outstanding
4 claims against it that are more than sufficient to
5 bankrupt the company. And thus you have to take
6 that into context when you think about making an
7 investment in a company in terms of trying to
8 understand whether it can pay back a return on that
9 investment.

10 Q That is why BP has now required security
11 for any loans that it's making?

12 A In the last most recent loan, we worked
13 with Prudential -- I assume that is what you are
14 referring to -- to add our loan to the same type of
15 security relating to shipper guarantees that
16 Prudential has. It's essentially pretty much
17 a parent guarantee, so the people loaning the money
18 are making the guarantee.

19 Q Why would BP require that to advance any
20 additional sums they would require a security
21 interest?

22 A It was more to put those loans in a more
23 formal and business-like format, which we thought
24 was appropriate in dealing with what are separate
25 legal entities.

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1 Q Did it occur to you that as secured
2 creditors, in the event of bankruptcy, you would be
3 in a preferred position relative to this huge amount
4 of outstanding unsecured claims that are out there?

5 A I don't know enough about bankruptcy to
6 know that for sure. I know shareholders go last.

7 Q Do you know that shareholders go last, and
8 unsecured creditors go next, and secured creditors
9 go first?

10 A No, I didn't know.

11 Q Everything I know about bankruptcy law is
12 the banks win. Is that your understanding?

13 A Yes.

14 Q Has BP put itself in the position of being
15 the bank by securing its interest?

16 A I think it probably tried to make itself
17 look more like a bank than it did before. I don't
18 know how successful that would be.

19 Q What was BP, the entire company's rate of
20 return, as a result of the opening of the north end
21 of the pipeline?

22 A I don't think I know that answer for sure.
23 I would say it probably met our 15 percent return
24 type target, but it wasn't a -- it wasn't like a new
25 oil well. It wasn't a huge winner. It was an

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1 appropriate return.

2 Q Your best memory is it's above the 15
3 percent hurdle rate?

4 A I am sure it met our hurdle rate, or we
5 would not have made the investment. And the
6 pipeline opening occurred on the schedule we
7 forecast, so we should have met our planned return.
8 So it was probably less than 20 and more than 15,
9 and that's where most investments we make have to
10 be.

11 Q Now, would you agree or not that generally
12 an investment in a regulated entity is a lower risk
13 investment than a non-regulated entity, all other
14 things being equal?

15 A Generally that is true, yes.

16 Q When you talk about -- is it your belief
17 that this Commission should set rates based on the
18 owner's internal hurdle rates, or based on what is
19 an appropriate rate for the risks of the pipeline on
20 a stand-alone basis?

21 A I would expect, in general, that the
22 Commission would set rates that are designed to
23 attract capital to the kind of investments that are
24 required. So in general, in a utility type
25 investment, the return would be lower.

2804

1 Q Did you file this testimony with the FERC?

2 A Well, I personally didn't, no.

3 Q Was your testimony filed at the FERC as
4 well as this Commission?

5 A I don't know the answer to that.

6 Q Did you draft your testimony?

7 A I did.

8 Q Okay.

9 A And I edited it.

10 Q Who owns Olympic Pipeline?

11 A Who are the shareholders?

12 Q Yes.

13 A BP Pipelines North America, Inc., and an
14 entity of Shell, but I can't tell you which.

15 Q If I were to tell you that BP Pipelines,
16 Inc. does not own Olympic Pipeline, and ask you
17 again who owns Olympic Pipeline, would you care
18 to --

19 A No. I would guess I would have to say I
20 must be mistaken, and I don't know the answer.

21 Q And I am not trying to play hide-the-ball
22 on you. Let me show you Exhibit 641-C, which was an
23 exhibit we prepared for Mr. Batch. And I will show
24 you a page of 641-C that is called Olympic Pipeline
25 Company Stock Certificates.

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1 A (Reading document.) Okay.

2 Q Okay. Based on your review of that
3 document, would you care to --

4 A That document appears to show that the
5 shares are owned by ARCO Midcon, LLC, which in turn
6 is a subsidiary of BP Pipelines North America, Inc.

7 Q Are you familiar with ARCO Midcon LLC?

8 A I have some familiarity in it.

9 Q I notice the shares were transferred into
10 it on 1/01/02, so January 1 of this year. Were you
11 aware of that transaction?

12 A Obviously not that specific one, because I
13 answered the question wrong. We made a number of
14 corporate entity organizational changes at the start
15 of this year as a part of cleaning up all of the
16 entities that exist within BP, because of all the
17 mergers and acquisitions that it's gone through. So
18 a number of changes like that were made right at the
19 start of this year.

20 Q Would you tell me what other assets ARCO
21 Midcon -- well, first, do you know if ARCO Midcon,
22 LLC is a new LLC?

23 A ARCO Midcon, LLC was created at the time of
24 the ARCO acquisition, in part to deal with the sale
25 of a portion of ARCO's pipeline assets required by

2806

1 the Federal Trade Commission.

2 Q Do you know what assets ARCO Midcon, LLC
3 has?

4 A Well, obviously not, since I didn't know it
5 had Olympic. So, no, I don't know the answer.

6 Q Do you know if it has any assets other than
7 Olympic?

8 A No, I don't know. I could look it up.

9 Q How would -- okay. Why won't -- well, let
10 me ask about Shell. Is it your understanding that
11 Shell is willing or not willing to advance equity
12 investment into Olympic?

13 A We gave Shell -- and at the time it was
14 Equilon -- the opportunity to participate the last
15 time we went out for borrowing under the same terms
16 that BP made the most recent loan. And they
17 declined to participate. So I would take that to
18 mean they are not interested.

19 Q And by the terms, you mean the ARCO 30
20 million dollar revolving credit line that is secured
21 in a second position under the through-put and
22 deficiency agreement?

23 A Correct.

24 Q Have you asked Equilon to put equity in?

25 A We have -- there is a finance subcommittee

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1 at Olympic, and they have discussed -- and this is
2 made up of people that work in BP Pipelines and
3 Shell Pipelines now with financial backgrounds. And
4 we certainly have discussed equity investment or
5 even equity conversion of some of the existing
6 loans.

7 But as it stands today, they have, to my
8 knowledge, not expressed any willingness to make any
9 further investment in Olympic.

10 Q I want to be sure I understood what it is
11 that has been discussed between the shareholders.
12 You have discussed both putting in additional equity
13 as well as converting some of the debt to equity?

14 A And additional loans. So all three of
15 those things, additional loans from shareholders,
16 equity investment, incremental new equity
17 investment.

18 Q Not the conversion?

19 A And the conversion of the existing
20 shareholder debt to equity. All three of those have
21 been discussed.

22 Q And those discussions were between -- you
23 were you a participant in those?

24 A I actually was not. They were actual
25 discussions between financial representatives at the

2808

1 shareholders --

2 Q Would these discussions have taken place
3 within the finance committee meetings?

4 A Typically it's a phone call, but yes.

5 Q Are there minutes from the finance
6 committee meetings?

7 A No, I don't believe so. It's more
8 discussional.

9 Q So far as you are aware, to date, Shell has
10 been unwilling to do any of the above?

11 A That's my understanding, yes.

12 Q Were they willing to do any of the above
13 before BP Pipelines took over the operation of this
14 line?

15 A Equilon was supporting -- Equilon was
16 supporting the cash needs of Olympic during the time
17 before BP became first an owner, and then the
18 operator.

19 Q So by that, we're talking about the 45
20 million dollars that is in litigation between the
21 shareholders that Equilon contributed to fund the
22 cash needs of Olympic before Whatcom Creek?

23 A Before and after.

24 Q And the before, you are talking about the
25 additional funding of the Cross Cascades project

2809

1 after ARCO declined to participate further?

2 A At least that.

3 Q Does BP, the parent, have any intention or
4 plan to put Olympic into bankruptcy?

5 MR. BEAVER: I am going to object to the
6 extent that it may require the discussion of
7 privileged information.

8 THE WITNESS: There's probably privilege, I
9 suppose, around Olympic. BP certainly has no plan
10 to put Olympic into bankruptcy. And of course, a
11 shareholder can't put a company into bankruptcy.
12 That's not how it works.

13 Q BY MR. BRENA: Is it fair to say that the
14 exposure arising from Whatcom Creek reaches beyond
15 Olympic alone, to also its shareholders and owners?

16 A It certainly has that potential.

17 Q So if Olympic were to go through
18 bankruptcy, it might solve Olympic's problems with
19 regard to these contingent liabilities, but it would
20 not solve the owners' problems with regard to these
21 contingent liabilities arising from Whatcom Creek.
22 Is that fair?

23 A I am not probably an expert enough in those
24 kinds of things to give a confident answer, but I
25 think some problems would remain, would certainly be

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1 fair.

2 Q Now, in your rebuttal case you indicated
3 that your existing authority was exhausted?

4 A Yes.

5 Q Can London approve the 30 million dollar
6 revolving credit line?

7 A The approval we have is for a larger total
8 than that, and that 30 million actually would cover
9 existing approval, and not-yet-approved amounts. So
10 BP has loaned more than 50 million dollars already,
11 of which only 10 is covered in the latest note.

12 Q Okay. I need to sort through loans and
13 loans, so bear with me for a minute. I am wondering
14 about when ARCO put in place the 30 million dollar
15 revolving credit and secured it under the
16 through-put and deficiency agreement, was that
17 authorized by London or not?

18 A Specifically, it did not have to be.

19 Q Why not?

20 A Because the first 10 of it was already
21 included in the authorization we had.

22 Q So you had authorization up to and
23 including the first 10?

24 A Yes.

25 Q But the authorization expired?

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1 A It just has been exhausted. When we get
2 authority to spend, it is for a total amount of
3 money. And we have now spent that total amount of
4 money. So the last little bit of which came through
5 that note.

6 Q Okay. So when ARCO put in place the 30
7 million dollar line of credit, it put it in place,
8 but it only had approval to loan under it, 10
9 million?

10 A Correct. That's correct.

11 Q Has London been contacted about an increase
12 in the authorization?

13 A No.

14 Q There hasn't been an e-mail or there hasn't
15 been any formal request for increasing the existing
16 authorization for Olympic?

17 A No, there has not. Not as yet.

18 Q What would that process be?

19 A We write what is known as a finance
20 memorandum that is signed off by a number of parties
21 as recommenders, and ultimately by someone as an
22 approver.

23 Q Have you had conversations with London
24 concerning increasing that?

25 A We certainly have had general conversations

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1 with our management, including those in London,
2 around the financial situation at Olympic and its
3 continuing cash needs, and the difficulty we face in
4 trying to raise that cash. So they are aware
5 that --

6 Q That there's a cash problem?

7 A Yes, that there's a cash problem. Yes.

8 Q You understand, don't you, that Olympic is
9 proposing rates based on their current level of
10 through-put?

11 A Yes. I mean, that is how the rates have
12 been proposed, yes.

13 Q Would you agree that there is the potential
14 for a windfall to Olympic if its rates are set on
15 its current through-put levels, and it returns to
16 normal operating through-put levels?

17 A Well, I suppose -- I don't know if I call
18 it a windfall, but obviously as the through-put goes
19 up at a given tariff, the revenue goes up. I mean,
20 Olympic has an awful lot of debt that needs to be
21 paid down.

22 Q If this Commission sets a just and
23 reasonable rate based on current through-put, would
24 you agree with me that that would need to be
25 revisited when the through-put increased, and it

2813

1 returned to normal operations?

2 A Absolutely. And I would expect that -- I
3 mean, I would expect that if we achieve the rate we
4 need to achieve with the through-put we have today
5 at 80 percent, when we get through all of the work
6 that has to be done to get the through-put higher to
7 100 percent, I mean, we absolutely would expect to
8 come back and revisit what the rate should be
9 at that higher through-put as opposed to just
10 keeping all of the extra money.

11 Q So if a condition for this Commission's
12 approval for a rate were that you come back in and
13 refile based on that change of through-put, you
14 would not oppose such a condition?

15 A Not at all. As soon as we're back to a
16 higher through-put, 100 percent rate, we would be
17 happy to come back and revisit the tariff. That
18 seems only appropriate.

19 Q Do you agree, or not, that a lot of the
20 prior loans have funded what are essentially losses,
21 prior losses?

22 A Well, in some sense, I suppose you could
23 characterize it that way. I mean, Olympic has run
24 at a deficit since 1999. And part of the cash
25 shortfall was for capital spending, and part of the

2814

1 cash shortfall was for operations. So if you would
2 like to call the operations part of that a deficit,
3 then, yes.

4 Q Well, Mr. Trotter asked you a legal
5 question with regard to retroactive rate making, and
6 you responded that you didn't know exactly what that
7 meant.

8 But do you think that future rates in any
9 way should be set based on prior losses?

10 A Well, again, I mean, I would have to come
11 back to my same old answer. To me, the future rates
12 need to be based on the condition of the company,
13 and/or what it needs to do the work it has to do.
14 You are asking about technical things around rate
15 making, and I am looking at it in kind of a
16 different way, I think.

17 Q If I were to represent to you that that
18 would be retroactive rate making, that if the
19 Commission established future rates based on a
20 period based on historic losses, rather than the
21 likelihood of future costs of service, then if that
22 is true would you agree -- well, let me rephrase the
23 question, please.

24 Are you asking this Commission to set a
25 higher rate in the future because of losses prior to

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1 now?

2 A I don't think that's what we're asking,
3 unless I am confused about the question. But what
4 we're asking is for the rates to cover the cash
5 needs that we have going forward, including, I mean,
6 probably continued borrowing.

7 But I don't have the expectation that the
8 rate outcome as good as I hoped they could be will
9 be sufficient in themselves to cover Olympic's
10 future cash needs. So there will probably still
11 have to be further borrowing for at least a year or
12 two. The spend level is still very, very high to
13 complete all of the integrity work that has to be
14 done.

15 Q Now, let me pose this as a hypothetical.
16 Let me say that an owner of a company takes 50
17 million dollars out of the company in cash
18 dividends, and they invest another 50 million
19 dollars in projects that don't go anywhere. So they
20 waste 100 million dollars. But their cash needs
21 are, going into the future, that they need 50
22 million dollars for capital improvements.

23 Do you think that it's fair for this
24 Commission to take into consideration the 50 million
25 dollars in dividends that they had taken out and the

2816

1 50 million dollars in bad projects that they had
2 invested in in trying to determine how to solve
3 their cash problems into the future?

4 A I mean, certainly it would be fair. And if
5 you could punish the guy that did that bad thing, it
6 would certainly be something that I would think was
7 within the realm of fairness.

8 In this case, whoever did those is long
9 gone, and BP is the one who is here. And so for us
10 it's -- I mean, looking at BP in terms of our cash
11 investment, it's really kind of a forward-based
12 look.

13 Q So now who is it that distributed those
14 dividends? Well, in the hypothetical, it would be
15 the regulated company that distributed the
16 dividends, correct?

17 A Correct.

18 Q The regulated company is still here, isn't
19 it?

20 A Yes, it is.

21 Q Who made those investments? It would be
22 the regulated company that made those investments,
23 isn't it?

24 A Yes.

25 Q They are still here, aren't they?

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1 A Olympic, the entity, does still exist, you
2 bet.

3 Q So with regard to my example of a wasted
4 100 million dollars, the public service company that
5 made those decisions, as you called it, the bad
6 actor -- and I wouldn't call it bad or good.
7 I would just say they wasted 100 million dollars --
8 that bad actor is still here in this room asking for
9 a rate increase from its rate payers?

10 A Well, it's asking for a rate increase from
11 the current and future shippers, yes.

12 MR. BRENA: I have nothing further. Thank
13 you.

14

15 CROSS EXAMINATION

16

17 BY MR. FINKLEA:

18 Q Good morning, Mr. Peck. I am Ed Finklea on
19 behalf of Tosco. My first question goes to what has
20 been marked for identification as 501-T, your
21 rebuttal testimony. And I am at line 22. You have
22 the observation, "Without new tariff revenues and
23 without new loans, Olympic will not be able to
24 initiate many new capital projects, including the
25 remaining capital projects in the 2002 capital

2818

1 project budget."

2 And then you go on to say, "Over the next
3 three years, Olympic needs about 66 million for
4 capital projects, and I know of no way to fund that
5 amount if Staff's and Interveners' recommendations
6 are accepted."

7 Is it the case that Olympic needs the
8 revenue level that is put forward by Mr. Collins of
9 approximately 56 and a half million dollars to
10 pursue these capital projects over the next three
11 years, or does Olympic need a revenue level that is
12 in excess of its operating expenses so it has a
13 positive cash flow?

14 A Well, I mean, obviously the best thing for
15 Olympic would be to have a positive cash flow. I
16 mean, to have a survivable entity, that's really
17 what you need to have over time is something that
18 generates a positive cash flow, because a negative
19 cash flow entity over time goes away.

20 But I think that we have some belief that
21 the spend level that we have been experiencing over
22 the past couple of years, and we expect to continue
23 into the next couple of years, will eventually
24 decline, and we will have done an awful lot of the
25 work that is less frequent that needs to be done.

1 And so I think there's a case where there's
2 a solution where the tariffs recover -- or the
3 tariffs cover part of those needs, and loans from
4 one or ideally both shareholders cover part of those
5 needs over the short term. And then in the end, the
6 cash flow, when it goes positive, can pay down the
7 debt, of which there is a lot.

8 Q Is it your testimony that if the Commission
9 accepts either the Staff's case, or Tosco's case, or
10 Tesoro's case as the proper level for setting rates,
11 that Olympic will operate at a negative cash flow?

12 A Well, Olympic, this year, with about 50
13 million of forecast revenue, was forecast to operate
14 at a negative 30 million cash flow. And we covered
15 that by the sale of the Sea-Tac terminal, which I
16 think the Commission is familiar with, and with the
17 hope of further borrowing.

18 Q Now, when you say you operated in a
19 negative cash flow, you are not discussing covering
20 service from the current operations. You are saying
21 the company is in a negative cash flow because of
22 these investments in new capital projects; isn't
23 that correct?

24 A Well, if we were making no capital
25 investment, it would then be, I think, almost cash

2820

1 neutral. It would be slightly negative still. I
2 think our capital improvement investment is about 25
3 million dollars for 2002.

4 Q So when you talk about operating at a
5 negative cash flow, your focus is how do you cover,
6 through current rates, or current rates and a
7 combination of that and borrowing, the capital
8 improvements that your company wants or needs to
9 make. You are not talking about a situation
10 where -- and this Commission has faced recently
11 situations where utilities are literally operating
12 at a negative cash flow on current operations.

13 Do you understand the difference?

14 A I mean, to me, cash flow is a thing that is
15 one thing. So whether the cash that is being spent
16 is being accounted for as a capital investment, or
17 whether it's being accounted for as an expense is an
18 accounting thing. But either way, it's cash.

19 In answer to your question, I think things
20 would be even worse at Olympic than they are today
21 if we couldn't cover our current operating expense.
22 I think that the tariff we have coming in now -- and
23 of course, we have right now a lot of tariff revenue
24 on the FERC interstate tariff side, which almost
25 certainly some of which will have to be refunded --

2821

1 we are pretty much able to cover the operating
2 needs, but it doesn't cover the capital investment
3 needs. If that's was the question you were asking.

4 Q That's where I am focusing in on. I want
5 to explore this a little more.

6 There's a statement by Mr. Talley in his
7 FERC testimony and I want to read it to you, and
8 then have you react.

9 Mr. Talley states that Olympic needs a
10 healthy positive cash flow from operations to
11 provide it with a financial ability to pursue these
12 very important capital improvement and maintenance
13 projects.

14 And my question is, how do you, in your
15 mind, square that with the notion that you need the
16 56 million dollars to pursue capital projects? Help
17 me understand here, if you are wholesaling the same
18 thing, or is there a difference?

19 A Well, I believe we're saying the same
20 thing. And that is, if you talk about operating
21 cash flow, to me that is the cash that is generated
22 as the difference between revenue, or in this case,
23 tariff income and operating expense. Which, if you
24 are going to invest capital, has to be a positive
25 number. You have to have money created through your

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1 operations, and that would be operating cash flow.
2 And you can then, in turn, invest that.

3 I mean, it's what BP does. BP is a huge
4 corporation. It runs a lot of businesses. Those
5 businesses generate revenue. And after expense it
6 has a profit, and it reinvests, then, a portion of
7 that profit, and the rest of it is paid as
8 dividends, plus or minus debt.

9 So that's all there is. So, you know, in
10 Olympic's case, of course, dividends are out of the
11 question. Olympic will not pay dividends for
12 decades in my sense. So the shareholders are
13 essentially already holding worthless shares.

14 The debt itself will probably, my sense is,
15 probably still continue to rise for another year or
16 two. And then assuming we have the majority of
17 capital improvements behind us, if we're allowed to
18 continue to make a small positive operating cash
19 flow that's larger than the capital investment
20 needed, we can pay down the debt and get Olympic
21 back to a more reasonable capital structure that is
22 not so heavily burdened with debt.

23 Q Mr. Peck, are you familiar with the notion
24 that in -- particularly in utilities, we often refer
25 to investments as being lumpy in the sense that this

1 year you have to make a very large investment, and
2 then over time that investment pays off? And my
3 question for you is when a utility is in this lumpy
4 investment stage, is it your company's position that
5 it is the obligation of the regulatory system to see
6 to it that rates provide enough cash to fund the
7 lumpy investment through current cash flow?

8 A No, I would not expect that to be the case.
9 And you can take, as an example, if we had to build
10 a loop, in other words build a parallel line on
11 another piece of line, that would be a very high
12 expense. And it did that sometime in its past
13 between -- because there's two lines between
14 Ferndale and Renton. And that money would have to
15 be invested in some fashion up front, and a return
16 earned over time.

17 So presumably, Olympic either borrowed it
18 or the shareholders at the time invested equity to
19 make that happen. That would be pretty typical.

20 Really, the same thing has happened here.
21 BP has put in 50 plus million dollars in loans, much
22 of which has gone for what you were calling lumpy
23 investment. But I think what I would also tell you,
24 based on what I am seeing right now, that investment
25 need is going to continue for certainly longer than

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1 I originally thought it would. There's a lot of
2 work to do to get the line to where people in the
3 state of Washington want it to be.

4 Q Going back to your example of when you
5 looped your line, when you looped your line
6 presumably you made an investment in year one, and
7 it may have taken two or three years to complete the
8 looping project.

9 As you made those investments, as you
10 understand how rate making works, isn't it the case
11 that the utility makes the investment, and once the
12 project is what we call used and useful, then the
13 utility files for an increase in rates to recoup
14 that investment?

15 A Sure. I mean that would make sense, the
16 same way that non-utilities do things; invest the
17 money, and then you make a return.

18 Q In our parlance, we sometimes refer to that
19 as regulatory lag. Does that make sense?

20 A The term doesn't mean anything to me, but I
21 can understand why you might use it.

22 Q There's a lag between the investment and
23 the time the regulatory process sees that the rates
24 give you back your money?

25 A Right.

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1 Q And in many respects, that's what we are
2 wrestling with, isn't it?

3 A Well, I think maybe beyond a lag is more
4 the question around whether it will ever be
5 returned, is really the crux of the issue here. So,
6 I mean, if we look at a company that is already
7 generating annual cash deficits of 20 to 30 million
8 dollars with, from what I can see, no clear end in
9 sight -- it's out there somewhere, but it's years
10 out given the workload -- with that situation, plus
11 the very large number of outstanding claims, the
12 situation of the company itself is just very dire.

13 And so, again, I think what we're looking
14 for is some sense that not all the cash flow needs
15 are going to be covered by tariff -- because I think
16 that's unrealistic. I don't think that's going to
17 happen -- but that enough of the cash flow needs are
18 going to be covered by tariff, that rather than
19 seeing this mountain of debt increase by 30 million
20 a year, if there's some sense that it's going to
21 slow down and remain below a level -- at some point,
22 of course, when the debt gets so high, there's no
23 chance to ever pay it back, and the company is
24 forced to be insolvent and bankrupt.

25 Right now, our view, Olympic's view is that

1 there is still a chance to have this entity survive,
2 and that really is best for everybody if it does.
3 There's lots of creditors, there's lots of things
4 that Olympic owes that it needs to take care of.

5 And a lot of those things will never be
6 paid if it goes through bankruptcy. And that's
7 certainly not what we would prefer. What we would
8 like to see is to get this thing into a position
9 that looks like an entity that will survive over the
10 long term, but it can only do that if the debt stops
11 growing so fast. And for that to happen, the tariff
12 has to be sufficient that the incremental cash needs
13 are substantially less than they are today. Did
14 that make sense?

15 Q I don't testify in this these proceedings.

16 A Okay.

17 CHAIRWOMAN SHOWALTER: Mr. Finklea,
18 could you not click your pen?

19 Q BY MR. FINKLEA: I am looking in particular
20 at the 56 million, or 56 and a half that seems to be
21 the recommendation of your company in the rebuttal
22 testimony.

23 Am I not correct that of that 56 and a half
24 million, that there's approximately 12 million of it
25 that is return on equity, so that isn't equity -- or

1 cash need. That's a return on your current
2 investment. And then depreciation expenses of
3 nearly 3 million. And depreciation, while it occurs
4 on the books, again, isn't really a cash need. And
5 then another almost million that is an amortization
6 of deferred earnings. So those three figures alone,
7 if my math is right, are approaching 15 million
8 dollars, almost 16.

9 Isn't -- under the rebuttal case there's at
10 least that much. And all of the Interveners have
11 certainly put forward a case that is above a
12 negative cash flow on an operating basis.

13 So isn't the real decision here for the
14 Commission, and the debate in this proceeding, is
15 where do you fall in this range well above anything
16 that would make the utility actually be in the red,
17 but obviously less than you would like, if you are
18 trying to fund most of your capital improvements
19 with capital cash? Isn't that really the focus
20 here?

21 A That was a really long question.

22 Q I understand.

23 A So let me try -- I mean, you have a table
24 of numbers there that I don't have, but let me try
25 to do a little bit of the math in my head that you

1 just talked about.

2 If what you have said is, gosh, I can go
3 through this whole thing, and I can find 15 million
4 of what you are using to justify your rate base cost
5 numbers that isn't really money that is being spent,
6 that is where the money will come from to fund the
7 capital.

8 So if you take revenue, you subtract off
9 the actual cash spent, there's money left. And when
10 you do accounting of P&Ls, you have depreciation and
11 such. But in the cash accounting all that gets
12 added back to get cash, but then your capital
13 investment gets taken out of that.

14 So if the capital needs of the company
15 continue at 25 million a year, and we're collecting
16 enough money that there's 15 left after we actually
17 pay all the cash expenses, then I am only 10 million
18 short.

19 And that 10 million might be a reasonable
20 amount to be covered by loans. Because I think
21 at that scale, with another year or two of only 10
22 million of loans, we have a reasonable chance of
23 this entity surviving and surviving and ultimately
24 paying down its debt.

25 Now, I may have lost the thread of the

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1 question, but at least that was my try to answer the
2 first part.

3 Q Well, then, let's -- if you will accept my
4 notion that we have got at least 15 million that
5 will be -- at the company's case, that you will be
6 above your cash flow needs, and there's legitimate
7 regulatory debate about whether Staff's way of
8 calculating the return on equity or the company's
9 way of calculating the return on equity, other
10 issues like capital structure, there's specific
11 regulatory issues, as you understand, that are in
12 the proceeding, correct?

13 A Well, I understand there's a lot of
14 regulatory issues, yes.

15 Q And is it your testimony that certainly
16 unless the Commission sides with the company on
17 every one of these issues, you don't get to a number
18 that winds up with enough cash for you to ever
19 recommend that the owners lend more money?

20 A Well, I think at an increase of half a
21 percent, which was the last I saw the recommendation
22 from the Staff, yeah, it doesn't get close to what
23 we would need to see.

24 Q But there's a lot of millions of dollars
25 between a half percent and 60 percent, right?

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1 A Yeah. And I think we clearly are not
2 expecting to receive 60 percent.

3 Q And you discussed earlier in your colloquy
4 with Mr. Trotter and Mr. Brena about essentially the
5 half billion dollar problem that exists from the
6 conditions that -- the outstanding lawsuits, and the
7 issues surrounding the accident at Whatcom Creek.
8 That's a problem that is just there. That's not a
9 problem you are asking this Commission to solve,
10 correct?

11 A That's correct. I mean, that's a problem
12 we're trying to solve, but we certainly are not
13 asking for the Commission for any help in solving
14 those.

15 Q And that's a problem that existed when BP
16 acquired Olympic, correct? The accident had already
17 happened?

18 A BP had acquired our ownership in Olympic,
19 when BP, the large company, acquired ARCO, the large
20 company. So that was all present at the time that
21 that very large merger was done.

22 MR. FINKLEA: I have no further questions.

23 JUDGE WALLIS: Let's take a recess until
24 11:15, please.

25 (Brief recess.)

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1 JUDGE WALLIS: Let's be back on the
2 record, please.

3 Questions from the Commission.

4

5

EXAMINATION

6

7 BY CHAIRWOMAN SHOWALTER:

8 Q Good morning, Mr. Peck.

9 A Good morning.

10 Q I am trying to separate in my mind
11 analytically what I will call the ghosts of the
12 past, and ghosts of the future, and ghosts of the
13 present, and how we might look at it for regulatory
14 purposes, and how the company might look at those
15 same things from the company's point of view. And I
16 suppose, in part, I mean, Olympic Pipeline Company,
17 and maybe in part I mean the owners. So I will try
18 to distinguish what I mean, or you can distinguish
19 in your answers.

20 A Sure. Sure.

21 Q What I am hearing so far is that while the
22 Commission may make whatever decision it thinks is
23 reasonable, when all is said and done, that is, when
24 that is said and done, BP will make a judgment of
25 its own on what to do about Olympic Pipeline. And

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1 it will look at the company and its revenue from its
2 own point of view, its own business point of view,
3 not our regulatory point of view. Is that more or
4 less what you were saying?

5 A That's very succinct and accurate.

6 Q And when it is looking at Olympic Pipeline
7 from its point of view, am I correct that one of its
8 major concerns is cash flow?

9 A Absolutely. That is one major concern.

10 Q When it's looking at that, is it correct to
11 say that some of the major contributors to the cash
12 flow problem are -- and let me name -- some of the
13 potential liability from Whatcom Creek would be one?

14 A Well, yes and no. And let me see if I can
15 be clear. I mean, I think we view the potential
16 liabilities out there that are directly Whatcom
17 Creek related, like fines and penalties, and those
18 sorts of things.

19 And they are, for sure, a cash flow issue.
20 But in some senses that we have kind of cashed that
21 out and set that aside and said, there's no way that
22 current shippers are going to pay for that. I mean,
23 that is what it is, and that's why the value of our
24 shares is zero.

25 But what we're looking at in cash for needs

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1 for the future from a revenue standpoint are really
2 excluding those large fines and penalties and such.

3 Q And I am not trying to imply anything one
4 way or the other that you are or aren't asking for
5 that. I am just saying from BP's point of view,
6 when they look at Olympic, don't they look at that
7 big liability sitting there, as well as some of the
8 other issues we have talked about?

9 A Yes, absolutely. BP has to. When it looks
10 at Olympic itself, and whether or not to invest more
11 in it, it has to make its judgment on the whole of
12 Olympic, and will it survive to pay back its
13 investment or not. And that equation has in it all
14 of the uncertainties around the very, very large
15 outstanding claims.

16 Q And if we remove from that equation the
17 liabilities, from BP's point of view, would BP need
18 to see less in the way of revenue? Let's say a
19 fairy godmother comes along and wipes out all of
20 the liabilities due to Whatcom Creek. It's off the
21 table. It's taken care of. It's just not there.

22 Would you say, under those circumstances,
23 again, from BP's point of view, a lower amount of
24 revenue coming in to Olympic Pipeline would suffice
25 for BP to say, yes, we will continue to invest in

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1 this company?

2 A I think the answer is yes. In other words,
3 if we were looking at a different pipeline company
4 that had cash needs, but didn't have all of these
5 very large and unknowable liabilities, we would view
6 that as a less risky type of investment.

7 And thus, if you are looking for cash flow
8 coverage on loans when you try to decide whether to
9 loan money or not, you will put up with less cash
10 flow because there's less risk that big disruptions
11 of that cash flow would cause it not to pay back.

12 Q Now, I want to continue down my own list of
13 contributors to cash flow problems. Isn't another
14 one reduced revenue -- lost revenue due to reduced
15 through-put in the last two years?

16 A Yes. I mean, the lack of through-put, or
17 the failure to raise the tariff, that lowered
18 through-put, has caused a part of the existing debt
19 to be there. I mean, the existing cash deficit.

20 Q And by failure to raise the tariff, at
21 least in my question I am referring now, looking
22 backwards, not forward. So the tariff has -- prior
23 to our interim increase, the tariff was what it was,
24 through-put was reduced --

25 A Substantially.

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1 Q -- and that meant lower revenues?

2 A Yes.

3 Q And that is a part of the cash flow
4 picture, isn't it, that BP looks at when it looks at
5 Olympic Pipeline?

6 A It's a part of how we got where we are
7 today. And so that, I mean, the cash flow picture
8 that we would look at before investing new money is
9 really forward looking. The money we have put in is
10 the money we have put in. And I think what we will
11 look for is the chances of the entity surviving and
12 being able to repay any future loans.

13 Q And I guess what I am trying to get at is
14 what starting point BP has in its eyes when it is
15 looking forward; that is, is it a starting point
16 that doesn't see the Whatcom liability or lost
17 revenues, or is it a starting point that does see
18 those things?

19 A I would say it's a starting point that
20 includes all of that in its view.

21 Q And then continuing on the list of things
22 that it may see that are somewhat past related, is
23 it the case that it also looks at what it put into,
24 I will use that term, meaning loaned for projects
25 that are now either suspended or delayed or called

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1 off?

2 A Well, of course, now BP came after any of
3 that, if you are talking about Cross Cascades. We
4 arrived on the scene long after that was over.

5 And so I don't think we would view -- I
6 mean, what we will start with is the company's
7 current position with all of the good and bad, and
8 whatever it is, and then trajectory forward from
9 there. So those projects, whatever they are, are a
10 part of its current position. So that's part of
11 what we will look at.

12 Q Yes. And I think my question was not well
13 put.

14 When BP looks at Olympic's current
15 position, does BP see debt owed on those projects?

16 A We see debt owed, and we see those
17 projects, or what is left of Cross Cascades on the
18 books. I mean, specifically to Cross Cascades, it's
19 likely to be mostly written off this year.

20 Q And I suppose one thing that Bonneville --
21 BP. I am used to BPA being Bonneville -- that BP
22 doesn't see, because it's not there, is dividends
23 that may have been paid out in the past. And had
24 those not been paid out in the past and were somehow
25 otherwise used within the company, the picture might

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1 look different to BP today; is that correct?

2 A Well, I am not sure it would look
3 different. I mean, you would have to try to
4 understand, during the time Olympic was paying
5 dividends -- I assume the way most pipelines work it
6 pays dividends because it doesn't have need of the
7 cash for further investment. So it's generating
8 more cash than it requires in terms of capital.

9 And the difference in these little
10 companies, it's typically paid back to the owners.
11 And then conversely, as we talked about earlier,
12 when large capital needs come up, these little
13 companies go back to the owners to borrow the money.
14 So it's an independent corporate entity, but it's
15 very kind of reliant on the parents. So the extra
16 money goes to the parent, or if there's money
17 needed, it comes from the parents.

18 Q But in terms of when money is needed versus
19 dividends being paid out, that's a judgment, isn't
20 it, of, in the first instance, the company itself,
21 Olympic Pipeline?

22 A Correct.

23 Q But isn't it also a judgment and decision
24 that's heavily influenced by the owners,
25 shareholders in Olympic Pipeline?

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1 A Yes.

2 Q And as an aside, while we're on the topic
3 of dividends, in my lay way of thinking, I would
4 have thought that dividends would be something
5 generally that would be paid on, or would assume the
6 equity had been put into the company in the first
7 place. I understand legally that wouldn't
8 necessarily have to be. But isn't the idea of a
9 dividend a return on your investment, meaning
10 something has been invested?

11 A That would be my understanding of it, yes.

12 Q And -- okay.

13 A And certainly the people who built the
14 pipeline originally put a lot of money in.

15 Q Now, back to these contributing factors, to
16 the starting point or the current position of the
17 company. If the rate that we approve includes
18 enough for, let me say A, B, C, D, E and F. Where A
19 through D are operating expenses, future things,
20 basically not the past, but that it is not enough
21 for E and F, E and F being the amounts necessary to
22 make up for some of those past problems, is what I
23 hear you saying is that maybe from a regulatory
24 point of view, or somebody's regulatory point of
25 view, it's sufficient to have a rate that covers A

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1 through D. But, again, BP is going to look at is it
2 enough to cover E and F when making their decision
3 to invest or not invest?

4 A I believe what you said is exactly right.
5 In other words, you can use, I suppose, a variety of
6 regulatory theories or methods to determine what an
7 appropriate rate ought to be, and that will result
8 in the revenue stream.

9 But I think BP, as a -- in thinking about
10 loaning further money will be looking well beyond
11 regulatory theories of rate making, and really will
12 be looking more at the actual condition of the
13 company, and its likelihood of survival, and the
14 likelihood that they will get a return.

15 Q I would like to go back to one of those
16 contributing factors, and that is lost revenue. The
17 revenue began to be lost, am I right, on June 10 or
18 11 -- June 10, 1999?

19 A Correct.

20 Q And when did BP become the operator of
21 Olympic?

22 A BP became the operator on July 1 of 2000.

23 Q And when did BP become the majority owner
24 of Olympic?

25 A It was in the fall of 2000, September or

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1 October, I believe.

2 Q And how long have you been on the board of
3 Olympic?

4 A I came on the board in April of 2000.

5 Q So you came on the board as president of
6 the board?

7 A No. I came on the board -- I was the first
8 person from BP to come on the board after BP bought
9 ARCO, and I came on as a board member.

10 Q I am sorry. Give me the month and year
11 again.

12 A That was in April of 2000. That was when
13 the acquisition of ARCO by BP was closed. And at
14 that point, BP became the owner of the shares that
15 ARCO had owned. And at that point I became a member
16 of the board of directors of Olympic.

17 Q All right. I think I am getting mixed up
18 on my years.

19 A If that was --

20 Q In terms of chronology of the three dates I
21 just asked you --

22 A Yes.

23 Q -- was your coming on the board the first
24 thing --

25 A First.

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1 Q -- in April of 2000?

2 A Right.

3 Q And then July of 2000 BP became operator?

4 A Correct.

5 Q And then September of 2000 BP became a
6 majority owner?

7 A Correct.

8 Q And then in April of 2001, you became the
9 chairman of the board?

10 A Yes.

11 Q From the time that you were on the board,
12 anyway, April of 2000, to May, and then really
13 later, October of 2001, Olympic did not ask this
14 Commission for any rate increase due to lost
15 revenues. Am I correct on that?

16 A You are correct.

17 Q And why? In other words, if a significant
18 element of this dynamics that we have described is
19 lost revenues due to reduced through-put, isn't it
20 the responsibility of the company to come and ask
21 for that increased revenue, or eat the costs and not
22 consider it when it's making any other decision? In
23 other words -- let me stop with that question.

24 A If you ask me in hindsight, the day I came
25 on the board, should I have started pushing to get a

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1 tariff increase, probably.

2 So I think at the time there was just a lot
3 going on, and our focus was -- I mean, certainly
4 when BP came on our focus was almost entirely on
5 safe pipeline operations, and what to do about the
6 fact that the north end of the pipeline was out of
7 service.

8 And so it probably was just not -- you
9 know, the financial structure of the entity and how
10 we were going to get where we needed to go
11 financially was probably not as clear then as it is
12 now. But, I mean, it would have been a good thing
13 to do.

14 Q Well, but you have put us in the position,
15 I think, of saying, well, even though we, Olympic
16 Pipeline, didn't ask for this rate increase until
17 October, nevertheless it's a big contributing factor
18 to the pickle we're in. And if you don't give us
19 enough money to give BP an incentive to give Olympic
20 a loan, which perspective includes the loss of that
21 revenue, then BP may just shut down Olympic.

22 And where is BP's or Olympic Pipeline -- I
23 am not sure which -- where is their responsibility
24 to stand up to that decision not to ask for a rate
25 increase?

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1 A Well, I don't know. I don't know. The
2 fact -- I mean, BP's viewed its responsibility as
3 coming in to try to do the right thing as a pipeline
4 operator, and in a sense, to make up the cash needs
5 to Olympic.

6 And I am not a person who's real familiar
7 with rate making, and certainly things are quite
8 different in the state of Washington than some of
9 the other states where we operate. So I think, in
10 our mind, it probably was not a bad thing to have BP
11 loaning the money early on while we sorted things
12 out with the idea that we could collect it over
13 time, sort of like other people have talked about.
14 You have to put the money in up front, and collect
15 it later. No different than any other type of
16 investment that was required to deliver service.

17 Q Your comments, and then some of Mr. Batch,
18 emphasize that Olympic's first concern was safety,
19 and that was where their priority was with the
20 implication, or maybe express statement, that
21 Olympic didn't pay so very much attention to its
22 finances.

23 I mean, the implication of the statement is
24 we could not both pay attention to safety and to
25 fiscal responsibility, and I don't know why there

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1 should be a conflict between those. It seems to me,
2 actually, the two go hand-in-hand; fiscal
3 responsibility and safety are necessary to one
4 another, both directions.

5 A Sure. Well, I think without a fiscally
6 sound entity over time you can't do what you need to
7 do to operate safely. So I mean, your statement is
8 correct in that sense. Again, I think what we were
9 probably looking at at the time was we're making
10 these investments, and over time these investments
11 will be paid back. And the actual form of how that
12 was all done, and did we do it right with the
13 correct permissions, and all, and obviously we just
14 missed some of that.

15 Q We have had other utilities that are in
16 distress, and they are right in here, as soon as
17 they think they are in distress, and filing a
18 deferred accounting petition. We want to start
19 counting the dollars later, but they want to be sure
20 that we know they may come and ask us for these
21 amounts.

22 I take it Olympic either was focused on
23 other things, or was unaware of the practice to do
24 that?

25 A Yeah, I think maybe it would be helpful to

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1 clarify. I mean, Olympic is an oil pipeline. And I
2 am assuming most of the other public utilities that
3 come here looking for rate increases and such are
4 like electric utilities, and gas utilities, and
5 such.

6 And oil pipelines are, in my understanding
7 anyway, just really different. I mean, our
8 customers are other big companies. They are not the
9 public. And the way our economics are regulated in
10 general, most places is the same, and it's the
11 FERC's methods.

12 So that was the mindset we had arriving
13 here, from not being a pipeline operator in
14 Washington before, thinking about it with that hat
15 on, thinking okay, FERC methodology and oil pipeline
16 kind of rules.

17 So maybe we were not very clever or maybe
18 we didn't get as much advice as we needed, but
19 really we just weren't thinking about the state
20 regulatory function in that first year or so.

21 Q I wanted to ask you a little bit about your
22 statements about BP's investment in the company.
23 And I guess you are looking at BP's loans as
24 investments in the company?

25 A Yes.

1 Q The basic question is, why didn't BP invest
2 equity into the company? What went into the
3 decision, either of Olympic to elect a loan versus
4 equity, or in BP to give a loan instead of equity?

5 A It would have -- as you look at Olympic as
6 an entity and do the accounting around it, it would
7 have been, I think, extraordinarily difficult for
8 Olympic to come up with a case where an equity
9 investment in Olympic would pay a 15 plus percent
10 return. Which to get an equity investment in a
11 corporate entity, that's what we have to take in
12 terms of our approval process.

13 We have to compete for equity with people
14 drilling oil wells in deep water Gulf of Mexico, and
15 people building gas stations. The competition is
16 among all the businesses that BP is in. And that
17 competition requires you to show you can generate a
18 15 plus percent return to have access to capital for
19 equity investment.

20 What we did instead was we parsed it into
21 looking at it in a couple of pieces, one of which
22 was a more nominal return on the loan made to
23 Olympic, and at the same time, then, the return that
24 flows through the refinery and its improved
25 performance. So that once you have earned a return

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1 from the refinery piece, then there's just a small
2 piece left to be paid back by Olympic, which we
3 thought there was a reasonable chance could happen.

4 Q So if you look at page 3 of your testimony,
5 when you are talking about the modest 7 percent on
6 the loan, you were saying that if it's a loan that
7 has a 7 percent return -- that you may or may not
8 receive -- nevertheless, as a shipper, you are going
9 to meet your hurdle of 15 percent?

10 A As a shipper and refinery owner.

11 Q If that same amount were not a loan but
12 equity, and you were making this same trade-off
13 between the equity this time and the value to you as
14 a shipper, what would be different, equity versus
15 loan?

16 A I am not sure it would be terribly
17 different. And like we have talked about earlier,
18 we looked at conversion of these loans to equity,
19 and really it doesn't make a whole lot of difference
20 in terms of our view of the situation.

21 I mean, I think we would view our loans to
22 Olympic as being pretty close to the same risk level
23 as an equity investment. I think in any sort of
24 proceeding where you are sorting out who the top
25 creditors are, and that sort of thing, then

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1 shareholder loans, no matter their form, are
2 probably suspect, and likely they look more like
3 equity.

4 Q But would you agree that compared to
5 unsecured third-party creditors, the secured loan is
6 probably better than equity?

7 A The one secured loan might be, yeah. It
8 might be. But, again, I am not an expert on those
9 kinds of things. And that's only 10 million
10 dollars.

11 Q On page 2 of your testimony, line 22 --

12 A Okay.

13 Q You are taking Staff to task, and you say
14 their solution is to expect investors to place
15 additional equity at risk. And I just circled the
16 word "additional." Is there any equity that has
17 been put at risk, or were you meaning really to say
18 loans?

19 A Well, certainly the shareholders at one
20 time put their equity at risk. And as it turns out,
21 they lost it.

22 Q When was that? Do you know when the last
23 time is that any of the shareholders put in equity?

24 A No. I am sorry. I don't.

25 Q Do you think as an end state, an Olympic

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1 Pipeline that has equity in the company versus only
2 loans from its shareholders is a preferable
3 condition for Olympic? And let's just say the
4 five-year plan.

5 A Yeah. I am not sure you get there in five
6 years, but it absolutely is the preferable state, is
7 to pay down the debt and then have an entity that
8 has in it more equity, obviously, than it does
9 today.

10 So that is where we would like to get it
11 to. That's where Olympic would like to go, and I
12 think that's probably where both shareholders would
13 like to see it go.

14 Q But given the amount of current debt,
15 wouldn't it virtually be necessary to write some of
16 it off, or disregard it? And by disregard, I mean
17 both the company and the owner to say there were
18 some bad investments, or bad decisions or
19 unfortunate accidents, whatever the cause, and the
20 owner, either as an owner or as a company -- you
21 simply cannot carry this burden well into the future
22 if we're ever going to get this end state?

23 A Well, what you say is true in the sense
24 that it's a serious concern. The high level of debt
25 is a problem for the company. And that's one reason

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1 that if you are looking in from the outside thinking
2 about making up more loans, I mean, significantly
3 more loans are going to put the company at a place
4 where it may not be able to pay those loans back.

5 I think as it sits today, depending on the
6 outcome of our tariff cases, there is a chance that
7 it can turn the corner and be able to pay the debt
8 back down, and get into a kind of more normal,
9 strong financial position.

10 As far as the shareholders go, there's no
11 real reason why the shareholders should feel like
12 the money that they loaned to Olympic shouldn't be
13 paid back.

14 Q Well, but let me -- I would like to inquire
15 about that, because Bonneville -- I am sorry, BP
16 took over ARCO, am I right -- no?

17 A I mean, you could just say BP.

18 Q But BP took on Olympic when it merged
19 with --

20 A When we purchased ARCO.

21 Q -- when you purchased ARCO. And you took
22 on whatever ARCO's assets, liabilities, et cetera
23 were. And one of them was Olympic Pipeline. And
24 you take it as you find it.

25 So I am not sure that BP is in a position

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1 to proclaim claim its innocence. It may be
2 innocent. And yet, it made a decision -- its own
3 decision to purchase ARCO with whatever ARCO had,
4 which includes Olympic Pipeline. And if you look at
5 what Olympic Pipeline was when BP acquired it, it
6 was this entity that had been managed in a certain
7 way, had bad luck in a certain way.

8 Why isn't it correct for BP to say, well,
9 this is the company as it stands. We better write
10 off some of this debt. We cannot expect the rate
11 payers of the future to fund this debt. And we're
12 starting at a bad starting point, but we can't
13 really expect that bad starting point to be made up
14 out of future revenues.

15 A Well, I guess the only way I could answer
16 it is to say BP will make whatever decision it can
17 make at the time it can make it. So when BP bought
18 ARCO we bought what we bought, and Olympic was what
19 it was.

20 During the time between then and now, BP
21 really kind of early on made the decision that has
22 gotten us to where we are today. So there was an
23 approval process we went through, and it included
24 becoming the operator and buying the majority
25 shares, and making the loans up until where we are

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1 today. All of that was approved back in 2000. And
2 now we are where we are.

3 So while, yeah, you could say, gosh, BP you
4 ought to write off some of this investment and take
5 your medicine, at the same time, I think, when we go
6 off to London, they are going to say if you are
7 asking for more money, I want to understand what
8 happened to the previous money, and what are the
9 chances that this next round is going to be just as
10 bad?

11 Q And wouldn't one answer be to them, well,
12 you know, of the many assets we got when we got
13 ARCO, we got a dog?

14 A Yeah, probably more than one.

15 But, again, the reality is what we got at
16 the time we got it is over and done. And the
17 decision will be made looking at the condition of
18 the company, its cash needs going forward, and the
19 likelihood that those cash needs can get covered,
20 and that they can recover their money.

21 Now, I think it is likely, even though it
22 might seem unfair, that BP will consider what
23 happened to the last money that it put in before it
24 puts in more. So if what you are saying is, well,
25 look that 50 million you put in so far, bad luck

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1 guys. That was just part of what you bought with
2 ARCO. That would be -- I can't say you can't look
3 at it that way, but I think BP may look at it
4 differently.

5 Q One last question, and that is about Shell
6 and BP's relationship with Shell. Do the
7 shareholders have no ability to affect each other in
8 terms of the investments, either equity or loans
9 that they make?

10 A Absolutely no ability to affect each other,
11 other than discussion. I mean BP and Shell are
12 different companies. There is nothing, I mean, any
13 more than all the shareholders at Enron. Nobody
14 came to them asking them for money to clean up
15 Enron's mess. Your shareholder is an independent
16 body, and can make its own judgment.

17 Some of these small pipeline companies like
18 Olympic have shareholder agreements that bind the
19 shareholders to a way of behaving toward each other.
20 Olympic actually had one of those at one time, but
21 it's long expired.

22 Q Is a member of Shell on the board of
23 Olympic, or expected to be on the board?

24 A Olympic has five board members: three from
25 BP, and two from Shell.

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1 CHAIRWOMAN SHOWALTER: Thank you.

2 EXAMINATION

3

4 BY COMMISSIONER HEMSTAD:

5 Q I was interested in your question and
6 answer with Mr. Brena, and looking at my notes I
7 believe you indicated that BP Pipeline would have to
8 resign as the operator if the rates set are not high
9 enough. We have this issue about what should be
10 included in rates, and I take it the company's
11 position is that there should be included in rates
12 amounts sufficient to pay for future safety, capital
13 improvements.

14 Assuming, for the purpose of this question,
15 that rates are not set at a level to address future
16 capital improvements. Would it be your
17 recommendation then that Olympic Pipeline, or
18 ultimately British Petroleum, resigned as the
19 operator?

20 A It certainly wouldn't be the first choice
21 or first thing we would look at. In some sense it
22 would be the last resort. But at some point if
23 Olympic, as an entity, can't attract more money from
24 BP, and you know, just take that for what it's
25 worth. For whatever reason we go through a process

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1 to solicit further funding from BP and it's turned
2 down. Then Olympic is in a tough spot, because it
3 has kind of cash needs that are higher than its cash
4 flow, and it just has to make some choices about
5 what to do about that.

6 The first set of things that would be done,
7 I expect, is we would come back to the WUTC, and the
8 Department of Ecology, DOE, and the Office of
9 Pipeline Safety on the Federal level, and show them
10 all of the work that we have sort of promised to do,
11 and talk about if there's any of that work that we
12 can not do, and/or defer. And that affects the
13 capital spend. And that would be the first way to
14 try to close the gap.

15 But if you get to where there's general
16 agreement about what all the work that needs to be
17 done, and it costs more than the cash generated by
18 the company, then you have to kind of look for other
19 alternatives. So Olympic would have to look to
20 other alternatives.

21 I am certain that we could find an operator
22 that is a cheaper than BP. BP is a good operator
23 and we're not terribly expensive as a pipeline
24 operator, but there's probably some things we do
25 that other operators wouldn't feel they needed to do

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1 while still being the operator. So that would be a
2 way to help close that gap.

3 And Olympic, of course -- this is not
4 necessarily a thing that BP would like. And
5 obviously BP will have to think about that as they
6 think about what to do about loaning more money.
7 But at the end of the day, if the pipeline is
8 running here in Washington State, BP has what it
9 needs as a large entity. So if it's operated by
10 Kinder Morgan, or if it's operated by -- pick some
11 pipeline names out of a hat -- as long as it is
12 running, that's what BP needs.

13 Q Well, I was going to ask one more question
14 about you resigning as an operator, and the new
15 operator would face the same issues. And you are
16 suggesting they might be able to be somewhat more
17 efficient, or operate at somewhat of a lower cost,
18 but it would still have the same problems that BP,
19 as the operator, faces. I mean, the problems at
20 least as you perceive them, wouldn't go away?

21 A I don't think they would go away. It would
22 just be one of the things we would have to look at
23 to try to close the gap of cash for Olympic.

24 Q All right. Now, another option would be
25 either to attempt to sell the company, Olympic

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1 Pipeline, or to sell the underlying assets --

2 A Right.

3 Q -- of the company?

4 A And those would probably be looked at, too.

5 Q And if Olympic Pipeline is not generating
6 the kind of return that BP feels it needs to have as
7 alternative investments, that's a typical response,
8 isn't it, from any company with multiple functions.
9 It will sell the losers?

10 A Right. And so, yeah, I mean, what you
11 suggest is another thing that for sure would be
12 looked at. Along with a change of operator there
13 may actually be an outright sale.

14 Q But with the current capital structure of
15 the company, and the liabilities and such, would you
16 receive any positive dollar amount from that sale?

17 A Well, I certainly cannot imagine anybody
18 paying us money for our shares today. So that type
19 of a sale, I think, would be unlikely. There may be
20 a case where Olympic, the company, could sell some
21 of its assets, like Olympic's Sea-Tac terminal. If
22 you had Olympic, the company, sell the whole of the
23 pipeline asset and keep the liabilities, I mean,
24 that starts to look like a bankruptcy proceeding.
25 So I don't know exactly what it looks like, but

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1 that's among the things that would have to be looked
2 at.

3 Q But were that to occur, in effect, the
4 liabilities of the company would be taken into
5 account, and the asset values would be, in effect,
6 written down?

7 A Right, by the outstanding liabilities, yes.
8 And, of course, the value of the asset, not counting
9 the rest, is really determined by the amount of
10 money it makes. And that, in turn, for the asset
11 would be determined by the tariff. So at least --

12 Q A couple of other brief questions. Is it
13 your view that the pipeline operating at 80 percent
14 of capacity, would you consider that to now be a
15 normal operation?

16 A It's certainly not normal. It's
17 acceptable. In other words, it's safe and it's
18 filling a good part of the need of the
19 transportation that is necessary here. I think all
20 of the shippers and the owner would like to see it
21 back at 100 percent, because the demand for that
22 capacity exists.

23 Q And it would be your expectation that at
24 some point, properly run and funded, it could
25 operate at 100 percent?

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1 A That would certainly be our intent if the
2 money is there to make the return, yes.

3 Q What kind of operational risk do you give
4 to Olympic Pipeline? I am not talking about
5 regulatory risk, but operational risk. Do you
6 consider it below normal, or below average, or above
7 average, or average?

8 A I guess I have to try to understand what --
9 in what context you want to put that. We believe in
10 its current condition that Olympic Pipeline is a
11 very safe pipeline.

12 There's a lot of work still to do to get
13 all of the assets into the condition they need to be
14 to operate at 100 percent pressure, and there's a
15 reasonable amount of work left to do to meet some of
16 the standards we have been asked to meet here around
17 secondary leak containment, and things that aren't
18 necessarily dangerous to life and limb, but are one
19 extra step to help protect the environment, types of
20 spend.

21 So there's a level where Olympic still has
22 to go that's even higher than it is today. But to
23 me, the steel is basically in very good condition,
24 the operations are safe, the people are well
25 trained. So I mean, in that sense, I think it's a

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1 pipeline -- a safe pipeline.

2 It is in an area of the country that is
3 more difficult, because you have seismic activity
4 among other things. I mean, a pipeline through the
5 middle of West Texas where there's not any people
6 and there's not any seismic activity is -- all else
7 being equal, the seriousness side of the risk
8 equation is obviously smaller.

9 Q How about market risk?

10 A Market risk, I am not sure I understand
11 what you mean.

12 Q Competitive risk.

13 A Olympic here, its major competitors are
14 barging and trucks. So most pipelines compete well
15 against barges and trucks. I think there's little
16 chance of another pipeline being built to serve the
17 function that Olympic is serving, unlike Colonial
18 and Plantation that compete head to head. Olympic
19 has probably less risk than that.

20 The bigger risk to Olympic, to me, is
21 really around its future uncertainties financially,
22 and to some extent, I suppose, what else goes on
23 here and the economy of Washington state.

24 COMMISSIONER HEMSTAD: Thank you. That's
25 all I have.

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EXAMINATION

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BY COMMISSIONER OSHIE:

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Q I really have only one question, and that is, if the shippers, through their rates, essentially cover the cost of your capital budget, does that make the shippers an owner of the company, at least to those capital assets that are funded by the cost recovered through rates?

A Well, I don't think it exactly does, anymore than a renter who is paying rent to cover renovations of the building becomes an owner of a building. They are still a renter.

Q What if the renter is actually covering the costs for the owner?

A I think, typically, they do over time. And I think, you know, make it clear, we're not expecting that the entire capital need of Olympic is going to get paid out of pocket in current year by the shippers.

I think what we're expecting is that some of the difference will be paid by the shippers, such that the on-going cash demands are smaller, and the chances of Olympic being able to pay that back are

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1 higher.

2 COMMISSIONER OSHIE: Thank you.

3 JUDGE WALLIS: I would like to ask a quick
4 follow-up to one of your statements.

5

6 EXAMINATION

7

8 BY JUDGE WALLIS:

9 Q If I recall correctly, did you say that the
10 investment in the Cross Cascade Pipeline may be
11 written off?

12 A I believe most of that will be written off
13 in this business year.

14 Q Who would actually take the action to write
15 it off?

16 A It probably would involve an action by the
17 board of directors. But really we're right now, as
18 you are probably aware, we're working really hard to
19 get audited books for year 2001 with Ernst and
20 Young. And my expectation is that the auditors will
21 make us write it down at the end of 2001 to really
22 reflect its true value at that time.

23 Q So action by Olympic's board; is that
24 correct?

25 A Yes.

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1 Q Would that have any result on any
2 outstanding debt that the company has that was
3 associated with that project?

4 A Not in and of itself. And, you know, as
5 you are probably aware, there's a bit of a
6 disagreement between Olympic and Equilon as to the
7 exact nature of their notes and how much of that
8 money is really owed. But that's a separate issue.
9 It won't be involved by the writedown of Cross
10 Cascades.

11 Q Other than that disagreement, are there any
12 effects on loan obligations?

13 A I don't believe so.

14 JUDGE WALLIS: Very well. Let's take our
15 noon recess at this point, and reassume at 1:30,
16 please.

17 (Lunch recess taken.)

18 JUDGE WALLIS: Let's be back on the record
19 following our noon recess.

20 In terms of administrative matters,
21 Mr. Marshall, (sic) you used a document that had
22 previously been marked for identification, 641, in
23 conjunction with Mr. Batch's appearance. Do you
24 wish to move that at this time?

25 MR. BRENA: I believe you referred to

1 Mr. Marshall, but, yes. This is Mr. Brena, and I do
2 wish to move 641-C into the record. And I would ask
3 that the confidentiality of it be waived.

4 MR. BEAVER: Your Honor, we are trying to
5 figure out where this document came from. There are
6 even references to me as being a source of
7 information concerning the ownership history of
8 Olympic. And unless I can clarify it, I think
9 we would object.

10 MR. BRENA: Well, it was produced in
11 discovery to us from them, and it is my
12 understanding --

13 JUDGE WALLIS: The time for making
14 objection to -- well, of course, these documents
15 were not available at the time of the prehearing, so
16 I guess it is timely.

17 Let's defer that, and get into the
18 questions and answers and we can take this up on a
19 break, or at our next administrative conference.

20 MR. BRENA: And if I could just point out,
21 they are out of the audit papers. Ernst and Young
22 has Bates stamp EY 00686 stamp in the lower
23 right-hand corner. That indicates they are part of
24 the audit packages that were produced to us.

25 JUDGE WALLIS: Very well. Let's return to

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1 the questioning. We had another question from the
2 bench.

3

4

EXAMINATION

5

6 BY CHAIRWOMAN SHOWALTER:

7 Q I wanted to follow up on my own questions,
8 and also Commissioner Hemstad's in terms of how BP
9 decides what to do from here. We discussed the past
10 costs or the starting point. Isn't it the case that
11 those are sunk costs at this point? It's simply a
12 matter of what the Commission does on a forward
13 going basis. Nothing is going to change whatever
14 the existing obligations are, right?

15 A Well, that's correct. Nothing would change
16 the current state that the Commission will do going
17 forward. And in general, I would agree with your
18 statement that said BP will basically be looking
19 point forward, and you can look at what has been put
20 into this point as a sunk cost in the economic
21 analysis you do around a future investment. And
22 that would be pretty typical.

23 But I do think normally we look at previous
24 investments in the same business, or the same entity
25 as indicative of what might be expected. So, I

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1 mean, I think we would have to roll into our
2 thinking the uncertainty created by our
3 difficulties, if we have difficulties, in achieving
4 tariff results in our thinking about the return on
5 any future investments. So in that sense only would
6 it be involved.

7 Q All right. But a couple of months from now
8 you will know what your starting point is from your
9 point of view. You will know what rates the
10 Commission has approved, and with those two big
11 pieces of information, aren't your options, A, keep
12 going under those circumstances, B, sell, and C,
13 bankruptcy? Are those --

14 A Right and --

15 Q And I recognize BP doesn't declare
16 bankruptcy, but BP might be able to cause
17 bankruptcy.

18 A In some sense, yeah, for Olympic its
19 options are really what it can do to close the gap
20 in costs versus revenue.

21 For BP, its choices are to put more money
22 into Olympic or not. Pretty much as simple as that.
23 And there are also choices BP can make around its
24 position as the operator.

25 Q But have I covered the options: keep

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1 going, sell, or bankruptcy? Are those the basic
2 options?

3 A Right. We spoke a little bit earlier
4 whether BP would continue as the operator. And
5 clearly if we were to sell, we would no longer be
6 the operator.

7 Q As between sale and bankruptcy, from BP's
8 point of view, is there much difference? When you
9 were answering Commissioner Hemstad's questions, I
10 took you to say since there is so much debt, you
11 probably wouldn't get any real price for the sale.
12 And it was unclear to me whether, between those two
13 options, there would be much difference to BP?

14 A Yeah, I think I would answer that best by
15 saying we would have to do some work to understand
16 what our best options were, because we have not done
17 a lot of work looking at sale or bankruptcy or
18 anything like that.

19 We have been kind of working on that
20 assumption path forward that this would survive, and
21 we would stay. That certainly has been our approach
22 up to now, so very limited work.

23 I think the sale of the shares, I think,
24 would be unlikely, because there's not going to be a
25 buyer. The chances of the shares having a value any

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1 time soon is very small. So it's really more
2 around, is there a way out where you are selling
3 assets. And I am not sure that is even possible
4 without some sort of reorganization. So I think --

5 Q All right.

6 A So I think, to answer your question, I
7 think you have covered the options.

8 Q And sale and bankruptcy may be close in
9 terms of their consequences to BP. I don't know.
10 But in any event, wouldn't BP be looking in the end
11 whether it's better to keep going with whatever we
12 give the company, versus not? And it may not be an
13 easy equation, but that's essentially what you will
14 be doing.

15 A That's exactly what we will have to do.
16 And those are the two choices.

17 Q So if BP is better off, as a company,
18 keeping going, under the circumstances it likely
19 will. And by company, I meant the overall view of
20 the company, including the company as shipper -- BP
21 as a company, as shipper?

22 A Yes. That would certainly enter the
23 equation to some extent.

24 Q Versus ending Olympic, or your relationship
25 to Olympic in some manner, and still looking at your

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1 position as a shipper, and then as a seller or
2 shareholder?

3 A Right. I mean, in any case, as long as the
4 pipeline continues to run, which is probably a
5 descent assumption, BP is likely to still be a
6 shipper, no matter who the operator is or who the
7 owner is because we will still have the refinery at
8 the north end.

9 Q All right.

10 CHAIRWOMAN SHOWALTER: I have no further
11 questions. Thank you.

12 JUDGE WALLIS: Mr. Trotter.

13 MR. TROTTER: Thank you, Your Honor.

14

15 RE CROSS EXAMINATION

16

17 BY MR. TROTTER:

18 Q Mr. Peck, there was some discussion about
19 the 15 percent hurdle rate. My question is, does BP
20 require all investment opportunities to produce the
21 same rate of return, regardless of the rate of risk
22 of the investment?

23 A The short answer is not quite. But BP as a
24 corporation is less discriminating that way than
25 Amoco where I worked before Amoco became a part of

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1 BP. Within BP, typically all of the investments are
2 held to a high hurdle standard, even if there is an
3 argument that can be made that the investment is
4 more likely to return than some other one. So it is
5 less volatile.

6 Q So a less risky investment than one that
7 would produce a 15 percent return would have a hard
8 time competing for capital at BP; is that correct?

9 A If there was a lower risk investment that
10 would produce, say, a 10 percent, I think the BP
11 group view is that's not the type of investment that
12 BP shareholders expect us to make.

13 Q You mentioned that some loans from BP to
14 Olympic were quote, "suspect," unquote. And I think
15 this goes into the questions about the nature of
16 loans versus debt versus equity. Do you remember
17 that testimony?

18 A No. You have to find it for me to know
19 what I was talking about.

20 Q Then I will ask it more directly. Isn't it
21 correct that all of the 150 million in loans that
22 are currently outstanding for Olympic are reported
23 in Olympic's FERC form 6 as debt?

24 A I have not reviewed FERC form 6 for
25 Olympic, so I can't -- don't know the answer to

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1 that.

2 Q Can you accept that subject to check?

3 A Sure.

4 Q Can you accept, subject to check, that they
5 are not reported as equity in your FERC form 6?

6 A Yeah, I believe that's true.

7 Q Are you aware of any note to any financial
8 statement ever issued by Olympic that has ever
9 characterized any of its debt as suspect?

10 A No, I wouldn't know of anything like that.

11 Q You mentioned FERC, and other regulatory
12 agencies in your testimony. And let me ask you
13 this: as far as you know, has FERC or any other
14 state -- start over.

15 Has FERC or any state regulatory agency
16 ever approved a rate that permitted a pipeline to
17 recover a past loss through a future rate?

18 A Well, I am not aware that there are or
19 aren't. I am not a historian of that.

20 Q So you weren't relying on any such
21 precedent in the past?

22 A No, I think we were relying on general FERC
23 style rate making, because that's what we were used
24 to. And as I understand, that's what was used here.
25 But beyond that --

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1 Q And is it your understanding that the FERC
2 trended original cost methodology permits you to
3 recover a past loss in a future rate?

4 A I couldn't answer that. I am not a rate
5 specialist.

6 MR. TROTTER: That's all I have. Thank
7 you.

8 JUDGE WALLIS: Mr. Brena.

9

10 RE CROSS EXAMINATION

11

12 BY MR. BRENA:

13 Q Originally Commissioner Hemstad asked a
14 series of questions about Olympic's choices, and
15 Chairwoman Showalter just followed up on that, and
16 was quite specific about the choices.

17 In your response to Chairwoman Showalter,
18 you said it was a decent assumption that Olympic
19 would continue to operate. Would you explain why?

20 A Well, because I think the economic effects
21 on the state of Washington if the pipeline was not
22 operating would be devastating. So I don't think it
23 would last very long if it wasn't operating.
24 Something would have to give.

25 Q Is one of the reasons that it would be a

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1 safe assumption to say it would continue to operate
2 is because of ARCO's tremendous investment in Cherry
3 Point Refinery and the economic incentive it would
4 have to continue to transport product to the market
5 at the lowest possible price?

6 A All the refiners would have some incentive
7 to get the problem solved.

8 Q Looking just at ARCO's incentive, or BP's
9 incentive --

10 A They would have some.

11 Q Can you quantify that amount?

12 A Not easily sitting here, no. It would be
13 significant.

14 Q It's a substantial incentive to have
15 Olympic continue to operate, isn't it?

16 A Certainly for all the shippers there's a
17 large incentive for it to continue to operate, and
18 for the state. So that's why I say it will, in one
19 way or another, continue to operate.

20 Q Now, the other options that there are --
21 and I think we were discussing three -- continue to
22 operate, sale, or bankruptcy. In either of the sale
23 or bankruptcy, all of the affiliated debt would be
24 cleaned off of Olympic, correct?

25 A Well, in some fashion everything would be,

1 if you go through a bankruptcy proceeding,
2 addressed, and creditors either paid or told they
3 won't be paid.

4 Q So the only possibility for the recovery of
5 the affiliated debt that is burdening Olympic today
6 is to keep going as it is?

7 A Well, I mean some of that affiliated debt
8 could be paid back if the asset value is higher than
9 the liabilities. Isn't that how it works?

10 Q You mean in a bankruptcy?

11 A Uh-huh.

12 Q Well, okay. You are asking -- I guess they
13 have a large secured creditor that would probably
14 take control of the pipeline, I would imagine.
15 Would you?

16 A To be honest, I wouldn't venture a guess as
17 to how it would proceed, because we haven't really
18 looked into it very hard.

19 Q Earlier Chairwoman Showalter initiated a
20 line of questioning with regard to why you didn't
21 come in for a rate increase earlier. And I don't
22 mean to mischaracterize what you said, but in part I
23 understood you to say we wish we would have had a
24 little greater sophistication than we had at the
25 time?

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1 A In terms of our understanding of how things
2 work in the state of Washington, we, BP Pipelines,
3 who are trying to take care of this, just didn't
4 know, perhaps, certainly as much as we know now.

5 Q Okay.

6 A Now, we started the process a reasonable
7 amount of time before we actually have shown up here
8 now, trying to get the increase.

9 Q If --

10 A It's been long.

11 Q If I were to show you a board of directors
12 minutes, which I understand confidentiality has been
13 waived on the page that I am about to quote from --

14 MR. BRENA: Can I confirm that, please, on
15 the record?

16 MR. BEAVER: Tell me the exhibit number, if
17 it's the one you showed me.

18 MR. BRENA: Exhibit 626, page C. And
19 I will quote from pages 3 and 5 of the Exhibit 3,
20 just to reference the board of directors minutes.

21 MR. BEAVER: This one?

22 MR. BRENA: Yes.

23 MR. BEAVER: Yes.

24 JUDGE WALLIS: Does that waiver apply to
25 the entire document, or just those pages?

1 MR. BEAVER: Those are the only pages I
2 read, because that is all I was asked about.

3 JUDGE WALLIS: Very well.

4 MR. BRENA: That is sufficient for the
5 purposes of my cross examination.

6 Q BY MR. BRENA: If I were to read to you --
7 and I will show it to you if you like -- from the
8 June 5, 2000 board of directors meeting --

9 MR. BEAVER: Can I hand the exhibit to the
10 witness?

11 JUDGE WALLIS: Please do.

12 MR. BRENA: And 630 as well, if you would.

13 Q BY MR. BRENA: In part it says, on page
14 5 --

15 A Page 5?

16 Q Yes. And by page 5, I am referring to the
17 exhibit page number in the upper right-hand corner
18 of the document.

19 A Okay. I am with you.

20 Q Okay. And it says, "Mr. Peck suggests that
21 the finance committee explore non-debt solutions to
22 the financing issue." Do you see that language?

23 A Yes.

24 Q And what did Mr. Peck mean by non-debt
25 solutions to the financing issue?

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1 A Well, it really is the sort of thing that I
2 have already talked about where the finance
3 committee met to talk about further equity
4 investment, or in some sense, sale of assets as
5 another non-debt solution to closing the financial
6 gap.

7 Q Is raising rate payers' rates, is that a
8 non-debt solution that was intended by this
9 language?

10 A You know, I don't think so. I don't
11 believe that was in our thinking at this time, but I
12 can't promise you.

13 Q And then I will just direct your attention
14 to page 1. This is June 5, 2000, correct?

15 A Yes.

16 MR. BRENA: Could the witness have a copy
17 of Exhibit 630-C, please?

18 MR. BEAVER: It's already up there.

19 Q BY MR. BRENA: Now, when BP became an
20 operator, it submitted a fixed bid to the board of
21 directors; is that correct?

22 A Yes, for a portion of the fees.

23 Q Right. And this package that I have handed
24 you, the fixed bid and financial review, that was
25 part of BP's presentation to the board in becoming

2878

1 an operator; is that correct?

2 A Let me look at it for a minute and I will
3 be sure.

4 Q Sure.

5 A (Reading document.) And what was the
6 question again?

7 Q Is this part of the packet that BP
8 presented to the board when it was becoming the
9 operator?

10 A I am not absolutely sure if this was
11 something that was presented in advance of being
12 chosen as the operator, or if this is a review of
13 the situation shortly after being chosen as the
14 operator. It looks like the latter, but I don't
15 remember.

16 Q But you do recognize it as a document
17 created by BP Pipeline and presented to the board of
18 directors for Olympic?

19 A Yes.

20 Q I would like to draw your attention to page
21 6 of that exhibit, the financial review under volume
22 assumptions.

23 A Okay.

24 Q And in it, in part, it has when you expect
25 your return to normal operations; is that correct?

2879

1 A It does, but --

2 Q When you see --

3 A -- let me back up.

4 Q Okay.

5 A It has what the assumptions were.

6 Q At the time?

7 A At the time. More an assumption than an
8 expectation.

9 Q I understand. And I wasn't trying to
10 suggest that you were suggesting something
11 different. I was looking at this point in time what
12 was being assumed by the parties. We both
13 understand your case before the Commission is
14 different than these assumptions.

15 Do you see what is scratched out on the
16 page?

17 MR. BEAVER: I am going to object. I
18 believe this is beyond the scope, at least on
19 anything I heard from the Commissioners.

20 MR. BRENA: I will tie it directly back to
21 the line of questioning that I indicated I was
22 pursuing, which is why didn't they pursue a tariff
23 rate increase. In the language that is scratched
24 out here, says, "No tariff changes projected during
25 this time frame." It shows a specific consideration

2880

1 of whether or not to file a tariff increase, and the
2 rejection of that option. It's directly on point.

3 JUDGE WALLIS: The objection is overruled.

4 Q BY MR. BRENA: Do you see that scratched
5 out language that I just quoted, and can you read it
6 to say it is what I said it is?

7 A Given you told me what you think it says,
8 it does appear to say that. I would agree.

9 Q I would like to draw your attention to page
10 9 of that exhibit.

11 A Okay.

12 Q Well, excuse me, page 7 next. And you
13 don't know of any reason that that could have been
14 scratched out, do you, the no tariff change?

15 A Not offhand, although if we go further into
16 this document it might make sense.

17 Q Okay. Page 7. Page 7 there's an
18 assumption. The first assumption for the financial
19 review when BP became operator was assumed a tariff
20 increase of 10 percent in the year 2002. Do you see
21 that assumption?

22 A Yes.

23 Q When BP became an operator, it specifically
24 had in its financial plan at the time that there
25 would be a 10 percent tariff increase in 2002; isn't

2881

1 that correct?

2 A Well, apparently in this particular review
3 that assumption was made, yes.

4 Q And if I could draw your attention to page
5 9, which is a financial forecast and statement of
6 income. And if I could draw you to the bottom
7 column, it says Fiscal Year 2000, it says cash flow
8 at the very bottom?

9 A Yes.

10 Q So at the time BP became the operator, and
11 was projecting a 10 percent increase in 2002, it was
12 also projecting a negative cash flow of 34.4 million
13 dollars from Olympic; is that correct?

14 A In 2000, yes.

15 Q And then 2001, at the time it was
16 projecting a 10 percent increase in 2002, it was
17 projecting for 2001 a negative cash flow of 35.4
18 million; isn't that correct?

19 A Yes.

20 Q And in 2002, then, this would -- so let me
21 ask you this way: I mean, as I understood it, I
22 mean, there's 70 million bucks that you guys knew
23 you were going to lose in cash flow before you
24 planned to even come in and file a 10 percent rate
25 increase.

2882

1 Now, are you asking this Commission to
2 somehow allow you now to recover that 70 million
3 bucks that you knew you were going to leave behind?

4 A Well, I don't know that I would agree with
5 the word "lose." I think what we knew was, let's
6 think about when this was, for one thing. This was
7 in around about June of 2000. We had, prior to
8 April of 2000, been precluded from learning anything
9 about Olympic, because of the merger prohibitions
10 about discussing things with people who are
11 competitors before you buy them.

12 So we had from the end of April until the
13 first of June to come up with financial projections.
14 My expectation of the way we did that was to use the
15 financial projections of the people who had been
16 there before. So I don't think there's any
17 implication that we went out and did a thorough
18 study to find out what these numbers were going to
19 be --

20 Q I am sorry. I don't mean to cut off your
21 answer.

22 A And we --

23 MR. BEAVER: If it's possible, if the
24 witness could just finish answering the question.

25 MR. BRENA: And that's fine. And I don't

2883

1 mean to interrupt the witness.

2 There's feedback coming through the system.

3 Is there some steps we could take to correct that,

4 please?

5 JUDGE WALLIS: Let's be off the record for

6 a minute.

7 (Discussion off the record.)

8 JUDGE WALLIS: Let's be back on the record.

9 Q BY MR. BRENA: Do you have my question in
10 mind?

11 A I want to finish addressing your use of the
12 words "lose 70 million dollars." I think there was
13 some recognition that the company was in a cash flow
14 negative position, and thus there was recognition
15 that short term we would have to find a way to cover
16 that cash flow.

17 But there certainly was no -- any
18 assumption that that method would involve large
19 losses of this size by BP, or anyone else.

20 Q On the line above for capital expenditures
21 it shows that from 2000 through 2002 that there
22 would be the necessity to fund 61 million dollars in
23 those three years in capital expenditures. Do you
24 see that?

25 A I do.

2884

1 Q And this is something that BP was fully
2 aware of shortly after or in mid 2000, correct?

3 A That's correct.

4 Q Now, I am trying to understand your answer
5 to me earlier having to do with blocks by the
6 merger. Is it your testimony that you didn't do due
7 diligence on Olympic prior to the acquisition of
8 ARCO?

9 A We did not.

10 Q So you just took ARCO with all its warts?

11 A There was due diligence done on ARCO by the
12 BP acquisition team, but it did not include Olympic.

13 Q Now, Commissioner Oshie asked you some
14 questions, and I believe the analogy went to renters
15 and landlord. And I was just trying to -- and I
16 believe you were saying that you believe capital
17 improvements would be made from the income stream
18 that the renters produced. Do you recall that line
19 of questioning?

20 A Yes. I am not sure those were my exact
21 words. I remember the questioning.

22 Q And in that line of questioning I think
23 that you tried to clarify that you weren't looking
24 to the shippers to pay the entire cash need for the
25 current year to do the capital improvements. Did I

2885

1 understand your answer to him correctly?

2 A Yes.

3 Q How much cash does Olympic have now, today?

4 A In the bank?

5 Q Yeah.

6 A As best -- well, let me say the last I knew
7 it was about 9 million dollars.

8 Q And what are its current accounts
9 receivable that it expects to receive within the
10 next 12 months?

11 A There would be the normal monthly accounts
12 receivable from the shippers who have been billed.
13 I don't know what that is.

14 Q If I were to say there were roughly 34
15 million dollars in receivables, many of them having
16 to do with insurance receivables expected to come in
17 over the next 12 months, would that change your
18 answer?

19 A Half of what you said is right. There's 34
20 million dollars that we have no expectation that any
21 of that will be paid.

22 Q Is it your testimony today that the
23 accounts receivable have been improperly booked by
24 Olympic under current receivables?

25 A It is my expectation that, again, like the

1 Cross Cascades work in progress project, the
2 insurance receivables will be largely written off as
3 a result of completing the audit. Most of that
4 receivable was on the books when we took over as
5 operator.

6 Q Now, are you saying that you don't expect
7 to have any insurance receivables under the claims
8 associated with Whatcom Creek?

9 A I am not sure I would go that far. We are
10 certainly pursuing insurance coverages from various
11 avenues, but I don't think we have anything like the
12 certainty that would be required to record it as a
13 balance sheet item.

14 Q Well, you understand it is recorded?

15 A Yes, I think that's probably incorrect.

16 Q And you understand that your case is built
17 on the assumption that 60 percent of your insurance
18 claims will be paid by insurance? Do you understand
19 that?

20 A Yes, right. I suppose -- well, let me back
21 up and say I don't know.

22 MR. BEAVER: Excuse me. I am going to
23 object. That mischaracterizes Olympic's claim. I
24 don't believe that is an accurate statement at all.

25 JUDGE WALLIS: Mr. Brena.

2887

1 MR. BRENA: Well, the witness is certainly
2 capable of responding if I ask a question that
3 contains a misrepresentation.

4 THE WITNESS: Well, why don't you try
5 again.

6 MR. BRENA: I would be happy to rephrase.

7 JUDGE WALLIS: Thank you.

8 Q BY MR. BRENA: If I could just have a
9 moment.

10 Mr. Peck, you were at the board of
11 directors meeting at which your insurance consultant
12 came in and indicated that he expected you to have a
13 60 percent recovery, were you not?

14 A I remember the meeting with our insurance
15 person present, and we talked about what we expected
16 to recover going forward, which was what the
17 discussion was about, as opposed to the past.

18 Q And it was his representation that that
19 would be 60 percent of the claims?

20 A Right.

21 Q Okay.

22 A And probably that's about what it was over
23 the short period there.

24 MR. BRENA: I have nothing further.

25 MR. FINKLEA: No additional questions from

2888

1 Tosco.

2 JUDGE WALLIS: For Olympic?

3 MR. BEAVER: Yes.

4

5 REDIRECT EXAMINATION

6

7 BY MR. BEAVER:

8 Q Mr. Peck, just to clarify the last couple
9 of questions with regard to insurance receivables,
10 this 30 some million dollar receivable that you
11 mentioned, to your knowledge, was that for monies
12 already spent by Olympic?

13 A Yes.

14 Q With regard to the insurance claims that
15 are pending, do you have an understanding that those
16 are for contingencies, such as lawsuits against
17 Olympic stemming from the Whatcom Creek matter?

18 A Short answer is yes, we are looking for
19 insurance coverage from a variety of sources, all of
20 them really related back to the Whatcom Creek
21 incident.

22 Q For example, the business interruption
23 claims that we have talked about?

24 A Right.

25 Q And to your knowledge, are all of those

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1 claims for which Olympic is trying to obtain
2 insurance coverage excluded from this tariff
3 proceeding by Olympic?

4 A To my knowledge, all of that is excluded,
5 yes.

6 Q You provided some testimony early on
7 comparing operators. Do you remember that
8 testimony?

9 A Yes.

10 Q I would like to explore a little bit your
11 ability to, in fact, make a comparison. Could you
12 give us a brief synopsis of your career in the
13 pipeline industry?

14 A Well, I have been associated with the
15 pipeline industry since 1995, first with Amoco
16 Pipeline and now with BP Pipelines.

17 And I had a career before that in a variety
18 of other parts of what was Amoco Corporation
19 associated with research and development, and
20 refining, and the supply function, which is the
21 people who ship inside pipelines.

22 At the pipeline company over the past six
23 years, I have served on several different boards of
24 directors of pipelines operated by other companies,
25 as well as spent time in a lot of industry groups

2890

1 like the American Petroleum Institute, and ALPO
2 Association of Oil Pipelines, where you have an
3 opportunity to understand how everybody else does
4 things.

5 So I have had really quite a bit of
6 exposure to a variety of operators, and their
7 practices.

8 Q Mr. Peck, the pipelines that you currently
9 are on the board of, what are those?

10 A It's only three. There's this one,
11 Olympic, Colonial Pipeline, and Longhorn Pipeline,
12 which is currently not operating.

13 Q And BP is not the operator of either of the
14 other two?

15 A It is not.

16 Q Could you describe from your perspective
17 BP's operating philosophy?

18 A The real simple philosophy people have
19 probably heard a lot is no accidents, no harm to
20 people, and no damage to environment. That is
21 really the high-level statement against which all of
22 our operating practices are built. And then into a
23 lot of detail, depending on what it is. We have
24 standard procedures and practices that we follow in
25 trying to achieve that goal.

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1 Q From your perspective in being associated
2 with these different pipelines, has the cost of
3 doing business in the petroleum pipeline industry
4 changed at all over the last three years?

5 A It has changed fairly substantially. And
6 certainly not just here in Washington state, but
7 everywhere. For instance, in our overall large
8 pipeline company our capital expenditures have
9 probably increased by two- to three-fold as a result
10 of the OPS regulations as a high consequence area
11 rules, integrity management plan rules, operator
12 qualification rules.

13 All of these things aimed at setting a
14 standard that all of the industry has to follow to
15 make pipelines very safe, and not necessarily a bad
16 thing. But, yes, costs have gone up fairly
17 dramatically.

18 Q And how many miles of petroleum pipeline
19 does BP Pipelines operate?

20 A We operate approximately somewhere between
21 15,000 and 20,000 miles of pipelines.

22 Q We had some discussions about when BP
23 became the operator of Olympic. Was BP the majority
24 owner of Olympic at that time?

25 A We became the operator while we were still

2892

1 a minority owner, a 37 and a half percent owner.

2 Q To your knowledge, was there a pending sale
3 GATX sale to BP at the time it became the operator
4 of Olympic?

5 A No, there was not a pending sale at that
6 time.

7 Q And I think you testified that BP became
8 the operator of Olympic on July 1, 2000; is that
9 correct?

10 A Correct.

11 Q Do you know when the operating agreement
12 with the prior operator expired?

13 A It was long before that, but I don't know
14 when.

15 Q Okay.

16 A There actually was an argument about
17 whether it was expired or not, and whether it was in
18 effect or not with the previous operator and
19 Olympic's board. So we went through the minutes.
20 You will find we went through the process that would
21 be required to terminate the existing operator in
22 case it proved to be true that they still had a
23 contract, which wasn't clear.

24 Q And was it not clear simply because the
25 agreement to operate the pipeline was with Texaco,

2893

1 and this, of course, was Equilon?

2 A Right. And it wasn't obvious that they had
3 followed the very clear procedures in the agreement
4 to transfer that.

5 Q And how many entities bid to operate
6 Olympic at the time that BP submitted the bid?

7 A Just two.

8 MR. BRENA: Objection; scope.

9 MR. BEAVER: I believe there were quite a
10 few questions relating to when BP became the
11 operator, including what BP's ownership interest of
12 Olympic was. So I am simply following up on those
13 questions.

14 MR. BRENA: Well, it doesn't include
15 soliciting whether the process was a competitive bid
16 or non-competitive bid. There were no questions
17 that went to that.

18 JUDGE WALLIS: I think the question is
19 reasonably within the scope. The witness may
20 respond.

21 THE WITNESS: There were two who bid.
22 Three were invited to bid. The board did not go
23 outside of the three owners to look for a non
24 owner-operator, assuming that there was no chance
25 that would happen.

2894

1 Q BY MR. BEAVER: Why was it that the
2 assumption that it would not happen?

3 A Because there was no way any company would
4 want to insert itself in the middle of all of the
5 problems that Olympic had at that time. It just
6 wasn't reasonable.

7 Q And what was the other entity that bid to
8 operate Olympic?

9 A Equilon and BP were the two, GATX declined
10 to bid to operate. And they certainly had a plan to
11 exit their ownership when they could.

12 Q And do you happen to know why BP's bid was
13 selected?

14 A No. Because obviously I only have one of
15 six votes, so I don't know why the other directors
16 voted the way they did.

17 Q Could you tell us why you voted the way you
18 did?

19 A For me it was a fairly clear distinction
20 between the capability offered by the two operators
21 in terms of their demonstrated ability to deliver
22 them. The operating model we asked for was one that
23 BP was currently using, and it was one that Equilon
24 was not currently using. And our confidence -- my
25 confidence level, put it that way, we could deliver

2895

1 was higher for BP than for Equilon. BP was by a
2 little bit, though, more expensive.

3 Q And Mr. Peck, just to clarify, I think
4 earlier you indicated that the Olympic board was
5 composed of five individuals; is that correct?

6 A It is today.

7 Q And apparently at this time it was composed
8 of six?

9 A Right. At that time there were three owner
10 companies. Each owner company had two directors.
11 And at the time, shortly after BP acquired the
12 shares from GATX, later that year we reduced the
13 number of directors by one down to five.

14 Q And Mr. Peck, I believe there was some
15 testimony early on this morning where you indicated
16 that the shareholders perceived Olympic as being a
17 stand-alone company. Do you remember that
18 testimony?

19 A Yes, certainly, as in a Delaware company.

20 Q To your knowledge, does Olympic have the
21 ability, and has it had the ability, to survive
22 without its parent?

23 A Not since the accident in '99.

24 Q And can you explain why that is?

25 A Well, because its needs for cash were far

1 more than the money it had coming in, and there was
2 nobody besides the owner who would put that money
3 in. So it was, in some sense, completely dependent
4 on the shareholders for its survival. Without
5 shareholder loans, Olympic would have been bankrupt
6 by the end of '99, probably.

7 Q Now, Mr. Peck, what, if any, assumptions
8 did Olympic make regarding how future tariff rates
9 would be set when it made various commitments to the
10 communities that are up and down the pipeline
11 corridor with regard to corridor safety improvements
12 and operations?

13 A I think, in general, we kind of expected
14 that Olympic, like everywhere else we operate, would
15 follow a FERC type of approach in setting tariffs
16 since that was really all we had seen, or had
17 experience with. And actually, as I understand it,
18 that's what Olympic had used in the past.

19 Q And are you familiar with how the FERC
20 deals with capital structure of an entity like
21 Olympic?

22 A And --

23 MR. BRENA: Your Honor, this is going so
24 far afield --

25 MR. TROTTER: I join the objection --

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1 MR. BRENA: -- of cross examination.

2 MR. TROTTER: I join the objection. It's
3 beyond the scope.

4 MR. BEAVER: Could I respond? I am
5 actually following up on some questions of Mr. Peck
6 about what he expected this Commission to do, and
7 this is a preface for my question which certainly
8 gets into that very issue. And that's the only
9 reason I asked that question.

10 JUDGE WALLIS: Very well.

11 THE WITNESS: Answer?

12 JUDGE WALLIS: Yes, answer.

13 THE WITNESS: Do you want to try the
14 question again so I make sure I get it right?

15 Q BY MR. BEAVER: Are you familiar with how
16 FERC deals with capital structure of an entity like
17 Olympic?

18 A The company, like Olympic, would look to
19 the capital structure of the parents in ratio to
20 their ownership in setting the capital structure for
21 the company.

22 Q And in follow-up to a question that you
23 were asked on cross, what do you understand this
24 Commission's task is in this proceeding with regard
25 to selecting a particular rate making scheme or

2898

1 methodology or system?

2 A Well, I mean, I would assume that the
3 Commission needs to choose among a number of -- or
4 make a number of choices about how the rates are
5 calculated and set. And that, in turn, then, will
6 result in whatever tariff increase is approved for
7 Olympic.

8 Q From your perspective, do you see any down
9 side or harm to Olympic, and even the community it
10 serves if, in fact, there is a significant change in
11 the methodology used to select rates for Olympic?

12 MR. BRENA: Your Honor, I would renew my
13 objection. That is, not only this line of
14 questioning is not only beyond the scope of cross
15 examination, but it's beyond the scope of his
16 testimony.

17 They have not offered this witness as an
18 expert with regard to FERC methodology. They have
19 not offered this witness that there's any reliance
20 on the FERC methodology, or much less the way that
21 FERC determines capital structure. None of that is
22 in his testimony, and yet he's sitting here trying
23 to bolster up, after the fact, Mr. Schink's theories
24 of the case.

25 And it's beyond his testimony, and beyond

2899

1 any cross examination that I have heard today. And
2 at some point, it's enough.

3 MR. TROTTER: I will join the objection.
4 It's simply beyond his expertise, and beyond his
5 testimonial capacity. And if he's going to be
6 subjected to cross examination on the FERC
7 methodology, then we should proceed to do that.

8 MR. BRENA: Then let's do it.

9 JUDGE WALLIS: Mr. Beaver.

10 MR. BEAVER: This was in direct response to
11 a question Mr. Brena asked Mr. Peck, what he
12 expected the Commission to do, and whether, in his
13 view, the Commission should follow traditional rate
14 making procedures that this Commission used.

15 And I will -- at the time he asked it, I
16 thought about objecting, because it was beyond the
17 scope. But I am following up on that question.

18 JUDGE WALLIS: I think Mr. Peck indicated
19 when he responded that he was talking on the basis
20 of an assumption, rather than his own knowledge.
21 And because the witness has indicated that he does
22 not have knowledge of the topic, I will sustain the
23 objection.

24 Q BY MR. BEAVER: Mr. Peck, you were also
25 asked some questions about why it was if BP had a 15

2900

1 percent requirement as far as return, it would loan
2 money to Olympic at 7 percent. Do you remember
3 that?

4 A Yes.

5 Q And then there was some discussion about BP
6 looking at this globally as opposed to vis-a-vis
7 Olympic. And could you explain what you meant by
8 that? In other words, what was the other part of
9 this component that BP was looking at in deciding
10 whether or make this loan?

11 A What BP was looking at, beyond the actual
12 pipeline itself, was the result that occurred by
13 shipping through the pipeline, and restarting the
14 north end.

15 So the way BP's refinery -- Cherry Point
16 was operating at that point -- all of the crude oil
17 comes in across the docks there at the refinery.
18 All of the products ship back out at that point
19 across the docks, because it wasn't connected to the
20 pipeline, and a little bit goes up by truck.

21 And we talked about the fact that the
22 pipeline is less expensive way to ship. So
23 everybody wants to choose that first, and they did
24 not have that at as an alternative. So they spent a
25 lot more money on transportation.

2901

1 In addition to that, the refinery itself
2 was capable of running at a given rate in hundreds
3 of thousands of barrels per day. And the rate at
4 which the crude oil could come in across the docks,
5 and the rate at which the products could leave
6 across the docks added together was too much for the
7 docks to handle, so the sought refinery had to run
8 at a reduced rate.

9 And so not unlike Olympic's case where
10 Olympic's revenue was less because the through-put
11 was down, the same thing was going on at the
12 refinery. Its through-put was down, and the revenue
13 was less by quite a bit.

14 So there was a large incentive for BP at
15 the time to step in and try to get things going in
16 the right direction, and get the pipeline restarted.
17 And that's where that incentive came from.

18 Q And --

19 A And it doesn't flow to the pipeline,
20 obviously. It flows to the refinery.

21 Q And Mr. Peck, to your knowledge is there
22 the same incentive for BP in getting the pipeline up
23 to 100 percent operating pressure, as opposed to
24 getting the 16-inch line restarted?

25 A It would be much, much smaller incentive

2902

1 for BP to go from 80 to 100. There would be some
2 incentive, because you save transportation costs.
3 But nothing like the incentive that existed before.

4 Q Mr. Brena asked you questions about the
5 incentive on the part of BP to get the pipeline
6 restarted, or continue to operate.

7 To your knowledge, would Tesoro have any
8 less incentive than BP to have the pipeline continue
9 to operate?

10 A I think from where it is today, Tesoro
11 would have the same incentive on a per-gallon basis
12 that BP would have the line continue to operate.

13 Q And would the same be true with regard to
14 Tosco?

15 A Yes. Any shipper, really, would have the
16 same incentive based on their through-put through
17 the pipeline. So a smaller refinery is
18 proportionally smaller, percentage wise.

19 So really all the shippers should have a
20 high incentive to have the pipeline keep operating.

21 Q Mr. Peck, during the nearly two years that
22 the 16 inch pipeline was either completely shut down
23 or partially shut down, to your knowledge was the
24 rest of the pipeline system prorated? In other
25 words, did it have more nominations to ship than

2903

1 capacity?

2 A To my knowledge, no. That is to say there
3 was excess capacity, because two of the four
4 refineries were not connected. So there was more
5 space in the pipeline than users, shippers.

6 Q So the two that were connected, then, would
7 have had complete access to the pipeline to ship
8 their product?

9 A Absolutely, yeah. They had as much space
10 as they wanted.

11 Q Who were those two shippers?

12 A Those were Equilon and Tesoro.

13 CHAIRWOMAN SHOWALTER: What was the time
14 period you were just talking about?

15 THE WITNESS: From 1999 when the accident
16 occurred, June 10, 1999, up through the restart of
17 the north end of the pipeline, which occurred, I
18 believe, in February of 2001. Not quite two years.

19 Q BY MR. BEAVER: Do you recall that the
20 entire 16 inch line was not restarted until June 1
21 of 2001?

22 A The rest of the line, there is a piece of
23 16-inch line that runs from up by where the
24 refineries are down to Ferndale. And then there's a
25 16-inch and 20-inch line that are parallel that run

2904

1 from Ferndale down to the Seattle area.

2 And the first piece that we restarted was
3 the piece to the north. So everything still flowed
4 through the 20-inch line once it got to Ferndale.
5 The 16-inch line was restarted, the parallel piece,
6 in the summer. And it took longer for that piece,
7 because we did a hydro test.

8 Q And that was --

9 A That's something that I think people were
10 glad about.

11 Q And we have actually heard about a hydro
12 test that was done in September of 1999 in the
13 general vicinity of Bellingham. The one you are
14 talking about was in a different part of the
15 pipeline?

16 A Right. It was the part to the south
17 that runs in parallel with the 20-inch line.

18 Q Anything happen during that hydro test?

19 A Yeah, we had a failure of the pipe.

20 Q Was that another ERW seam failure?

21 MR. BRENA: Your Honor, I would object.

22 They are not even trying to tie this to cross.

23 JUDGE WALLIS: We are getting quite a bit
24 afield. I trust the company will have witnesses who
25 are addressing this in their testimony. And in

2905

1 light of our time pressure, I think it might be
2 better to focus this witness on the areas of his
3 direct and his cross.

4 Q BY MR. BEAVER: Mr. Peck, you were asked by
5 Commissioner Hemstad about operational risks of the
6 pipeline. Do you remember that testimony?

7 A Yes.

8 Q And I believe your response related to the
9 safety of Olympic Pipeline?

10 A Right. Uh-huh.

11 Q If you were asked about financial risks of
12 an investment today in Olympic Pipeline, what would
13 your response be?

14 A Well, the financial risk -- I mean, first
15 of all, we talked a little bit about the, kind
16 of all the large unknown liabilities out there that
17 could affect the likelihood of that financial risk
18 to have a return.

19 And then we kind of talked about setting
20 those aside, and looking at, how about the rest? In
21 that sense, the financial risk that you face at
22 Olympic is that it's kind of a one-trick pony. It
23 isn't a large portfolio of pipelines like BP
24 Pipeline North America.

25 So if it had another serious incident like

2906

1 the one we had before, it's subject to obviously a
2 serious interruption of revenues. It has only four
3 refineries feeding it. So if one of those
4 refineries has a serious problem, then sort of by
5 definition Olympic does.

6 As you look at -- well, if you take -- not
7 unlike a stock portfolio, if you only have one
8 pipeline in your company, it's a riskier or higher
9 uncertainty for return than if you have 10 and
10 spread the risk across many investments. So in that
11 sense it would be a riskier investment to make.

12 Q As far as size goes, how does Olympic
13 compare with Colonial, one of the other pipelines
14 you said you were on the board of?

15 A Colonial is the largest single pipeline in
16 the United States. It is huge. Olympic is a very
17 small pipeline.

18 Q As far as miles go, is there a way to
19 quantify?

20 A I believe --

21 MR. BRENA: Your Honor, if I may object.
22 Now we're doing financial risk factors, comparing
23 pipelines in size. This should sound very familiar
24 to Mr. Schink's testimony. Doesn't sound at all
25 familiar to me with regard to Mr. Peck's testimony,

2907

1 or the cross of any witness. They just seem to want
2 to be using this witness to go through and bolster
3 Mr. Schink and his analysis, and it's beyond the
4 scope of this redirect.

5 MR. BEAVER: Your Honor, there actually
6 were several questions of Mr. Peck about a risk, one
7 of which was from Commissioner Hemstad, and I am
8 following up on that. I thought the question was
9 actually a little bit different and intended to be
10 different than the safety response that Mr. Peck
11 gave. So I am trying to get into the other risks
12 that I thought the question was pertaining to.

13 MR. BRENA: The questions were not related
14 to financial risk factors. They were related to
15 operational risk.

16 JUDGE WALLIS: I think that if his answer
17 had not addressed the question, there would have
18 been a follow-up. So I am content to let this topic
19 die, if you are.

20 MR. BEAVER: Okay. That's fine with me.

21 Q BY MR. BEAVER: Mr. Peck, you had testified
22 about, in your view, the need for Olympic to get a
23 rate increase to get -- to attract capital. And I
24 want to clarify, were you referring to the ability
25 to pay for prior loans, or to attract new loans?

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1 A Well, Olympic's capital needs are future
2 needs, not past needs. So certainly this is about
3 new loans in the future, or new investments.

4 Q You were asked some questions about an
5 exhibit, which is, I believe, 630. Do you remember
6 those questions?

7 A Those are the questions about the fixed bid
8 proposal?

9 Q Yes.

10 Q Yes. And one of the questions related to
11 attempting to read something that was apparently
12 scratched out. Do you remember that?

13 A I remember that, yes.

14 Q And I believe -- what is scratched out is
15 "No tariff changes projected during this time
16 frame." Do you know why this was crossed out?

17 A I have no idea even which copy it was
18 crossed out on.

19 Q Do you know if it was crossed out at the
20 board meeting?

21 A I don't know.

22 Q Now, also on the action items of this
23 exhibit, is there an action item that related to
24 tariffs?

25 A (Reading document.)

2909

1 MR. BRENA: Excuse me. Could you refer to
2 what page of the exhibit you are referring to.

3 THE WITNESS: There's a page of the exhibit
4 entitled Action Items at the top, and it is page 8
5 of 9 in the top corner.

6 In the list of action items the third item
7 says, "Lay ground work for cost productions and
8 tariff increase."

9 Q BY MR. BEAVER: And also on this document,
10 which is page 9 of 9.

11 A This is the one with the little print.

12 Q Is there any indication as to whether there
13 was an assumption as to through-put?

14 A Yes, there is a through-put assumption on
15 here.

16 Q Could you just indicate -- this is on page
17 9; is that correct?

18 A On page 9, yes.

19 Q What is the assumption?

20 A The through-put assumption in 2000 was 64
21 million barrels, or 175,000 barrels a day.

22 For 2001, it was 88 million barrels, or
23 242,000 barrels a day.

24 And for 2002, it is 96 and a half million
25 barrels, or 264,000 barrels a day.

2910

1 Q Mr. Peck, I just have a couple of more
2 questions. One, I think this was responded to, but
3 what entity owns ARCO Midcon?

4 A ARCO Midcon is wholly owned by BP Pipelines
5 North America.

6 Q And you were also asked some questions
7 about the security for 10 million dollars of an ARCO
8 loan. Do you remember that testimony?

9 A Yes.

10 Q There was discussion about this through-put
11 and deficiency agreement as being the security; is
12 that correct?

13 A That's correct.

14 Q And do you understand that the ARCO loan is
15 secondary in line behind Prudential?

16 A Yes, that was what Prudential insisted on,
17 which is no surprise.

18 Q And what is ARCO's obligation under that
19 through-put and deficiency agreement to pay for any
20 shortfall in Olympic's ability to repay the ARCO
21 note?

22 A Well, there's essentially two guarantors,
23 which are the two owner shippers, ARCO and Equilon.
24 So under that deficiency agreement, ARCO would be
25 required to pay its ownership share, or two-thirds

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1 of the deficiency. So it's a guarantee of itself.
2 And Equilon would have the other one-third.

3 MR. BEAVER: That's all I have.

4 JUDGE WALLIS: Any other questions?

5 (No response.)

6 JUDGE WALLIS: Let the record show there's
7 no response.

8 Mr. Peck, thank you for your time today.
9 You are excused from the stand at this time.

10 Let's be off the record for a few moments
11 while Mr. Batch steps forward.

12 (Brief recess.)

13 JUDGE WALLIS: Let's be back on the record,
14 please.

15 Olympic has called to the stand at this
16 time its witness, Robert Batch.

17 Mr. Batch, would you please raise your
18 right hand.

19 Mr. Batch, have you appeared previously in
20 this proceeding?

21 THE WITNESS: Yes, I have.

22 JUDGE WALLIS: I will note that you are
23 under oath on a continuing basis.

24 Let me note that the exhibits have been
25 prenumbered for this witness at the administrative

2912

1 prehearing conference that was held on June 13,
2 2002, and the record contains the exhibit numbers
3 601-T through 623.

4 In addition, I would like to note that
5 Tesoro has presented additional exhibits for this
6 witness, which are numbers 624 through today's
7 addition 667. And I will ask the reporter to copy
8 into the record at this point the information that
9 appears on the Commission's Exhibit List for those
10 numbers as the description for the record.

11 (Exhibit 624, BCB - Olympic's response to
12 Tesoro's interrogatory No. 28 re: payments to BP as
13 operator, with AP, Payroll, Transition Costs,
14 Management Fees, (2 pages Tesoro); Exhibit No.
15 625HC, BCB - Olympic's response to Tosco's DR No. 18
16 re: salaries, benefits and payroll taxes for OPL
17 employees - F11779-83 and F117886-94 (14 pages)
18 Highly Confidential (Tesoro); Exhibit 626HC, BCB -
19 Minutes of Meetings fo Board of Directors, May 11,
20 2000, June 5, 2000, and June 16, 2000, F7462, 72
21 (OPO3237-47 (11 pages) Highly Confidential (Tesoro);
22 Exhibit 627, BCB - Olympic's response to Tosco's DR.
23 Nos. 68 & 69 re: management fee and moving control
24 center - F1211, 12, 13 & 15 (4 pages) (Tesoro);
25 Exhibit 628HC, BCB - Affiliated Payments (BCB)

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1 Amounts Paid to BP w/explanation F9465-74
2 (OP12269-76 and OPO2447 &48) (10 pages) Highly
3 Confidential (Tesoro); Exhibit 629, BCB - (1)
4 Management Agreement, Texaco & Olympic 7/1/91 (13
5 pages), (2) Memo to increase service charge on
6 Agreement 8/6/96 (2 pages) (Tesoro) (No dates stamps
7 on Agreement) (Memo OPL 1132358-359) (15 pages
8 total) (Tesoro); Exhibit 630C, BCB - Olympic
9 Pipeline - Fixed Bid and Financial Review (no date
10 stamps) (9 pages) Confidential (Tesoro); Exhibit
11 631, BCB - Olympic's response to WUTC Staff's DR No.
12 51 re: potential to expand system - F14361 (1 page)
13 (Tesoro); Exhibit 632C, BCB - Board of Directors
14 Meeting of Minutes of 5/11/00 re: "Termination of
15 the Operating Arrangement with Equilon" and "Annual
16 Property Insurance Premiums" (2 pages) Highly
17 Confidential (Tesoro); Exhibit 633C, BCB - Board of
18 Directors Meeting Minutes of 6/16/00 re: "Acceptance
19 of BP Amoco's Bid to become Olympic's Operator and
20 its Costs (5 pages) Highly Confidential (Tesoro);
21 Exhibit 634C, BCB - OPL Response to WUTC DR 306 re:
22 the "Fixed Bid Items" on the 2002 Proposed Income
23 Budget (8 pages) Confidential (Tesoro); Exhibit
24 635C, BCB - OPL Response to WUTC DR 365 re: "when
25 Olympic expects to have Audited Financials for 1999,

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1 2000, and 2001" (2 pages) Confidential (Tesoro);
2 Exhibit 636C, BCB - OPL Response to WUTC DR 369 re:
3 "2001 actual and 2002 projected level of management
4 fees paid to BP Pipelines" (1 page) (Tesoro);
5 Exhibit 637, BCB - Olympic's response to John Brown
6 supporting documents WUTC Staff DR No. 2 requesting
7 a Schematic Diagram of Pipeline System F12245-47
8 (OP00127 & 28 diagrams) (3 pages); Exhibit 638HC,
9 BCB -- One-Time Exp. - (BCB) Report by BP - Health,
10 Safety and Environmental Aspects of Olympic
11 Pipeline; assessment conducted July 10-14, 2000 -
12 F9442-61 (20 pages) Highly Confidential (Tesoro);
13 Exhibit 639, BCB - One-Time Expense - Explanation of
14 Integrity Plan (3 pages) (Tesoro); Exhibit 640C, BCB
15 - OPS Corrective Action Order - Tesoro WUTC DR 158
16 (3 pages) Confidential (Tesoro); Exhibit 641C, BCB -
17 Ownership Chronology May 1965 - Sept. 2000 and list
18 of Stock Certificates - EY 000686 & F12255 (2 pages)
19 Confidential (Tesoro); Exhibit 642, BCB - Dec. 28,
20 1998, notice to Olympic shippers and subscribers re:
21 new tariffs FERC No. 24 and WUTC No. 20 and
22 transmittal letter to FERC with No. 24 - OPL1111355,
23 356, 357, 358 (4 pages) (Tesoro); Exhibit 643C, BCB
24 - Salaries - Olympic's response to Tosco DR Nos. 55
25 & 129 re: lists of employees - F12197, F9270071,

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1 EY013388 (4 pages) last page is Confidential
2 (Tesoro); Exhibit 644C, BCB - Olympic's response to
3 WUTC Staff DR. No. 328 re: Olympic's customer base.
4 Resp: 70 shippers, etc. (1 page) W4007 Confidential
5 (Tesoro); Exhibit 645C, BCB - Olympic's response to
6 WUTC Staff DR. No. 326 re: proration of Olympic's
7 pipeline capacity (1 page) W4001 Confidential
8 (Tesoro); Exhibit 646, BCB - Olympic's response to
9 Tosco's DR No. 6 re: when pipeline will return to
10 normal operating pressure (3 pages) F10031, F10033,
11 F10034 (Tesoro); Exhibit 647C, BCB - Pipeline
12 Automated Scheduling System, (PASS) Confidential -
13 OP12785, 86, & 87 and April 4 letter from Larry
14 Miller to Robin Brena, see page 2, para #1 re: PASS
15 manual (total of 7 pages) (Tesoro); Exhibit 648, BCB
16 - Olympic's response to WUTC Staff DR No. 8 re:
17 overall capacity utilization from 1995 through 2001
18 (1 page) F9512 (Tesoro); Exhibit 649C, BCB -
19 Whatcom - Corrective action Order, Amendment, Second
20 Amendment (OPL 1069204-208) (OPL 1069209-216) (OPL
21 1069217-224) Confidential (21 pages) (Tesoro);
22 Exhibit 650, BCB - Byron Coy's Grand Jury Exhibits
23 (1) Assessment of SCADA Computer System by Byron Coy
24 (2) Assessment of Pipeline Control Methodology &
25 SCADA System by Byron Coy (GJEX0000500-506) and

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1 (GJEX 0005915-921) (14 pages) (Tesoro); Exhibit 651,
2 BCB - OPS Docs - Letter dated Jan. 14, 2000, from
3 Olympic to the DOT enclosing (1) portion of
4 Olympic's revised operations manual, and (2) Summary
5 identifying prior responses to the CAO (12 pages)
6 (Tesoro); Exhibit 652, BCB - Letter dated Aug. 19,
7 1999 from DOT to Equilon requesting a report
8 containing additional scenarios on June 10, 1999
9 accident (2 pages) (Tesoro); Exhibit 653, BCB -
10 Letter from DOT to Equilon, May 8, 2000, Notice of
11 Probable Violation and Proposed Civil Penalty,
12 setting out "probably violations of Title 49, CFT,
13 Part 195." (4 pages) (Tesoro); Exhibit 654, BCB -
14 Letter from DOT to Carl Gast of Equilon/Olympic,
15 June 2, 2000, NOTice of Probable Violation and
16 Proposed Civil Penalty, setting out \$3,050,000 in
17 penalties w/attached "procedures for responding" (16
18 pages) (Tesoro); Exhibit 655, Letter from DOT to
19 Mayor of City of Renton, Nov. 2, 1999, addressing
20 the Mayor's concerns regarding pipeline safety and
21 discussing the CAO. FO 10000436-437 (2 pages)
22 (Tesoro); Exhibit 656, BCB - Letter to Zak Barrett
23 of OPS from Bellevue Mayor, Sept. 20, 1999, thanking
24 him for hi presentation to Governor Locke's Fuel
25 Accident Prevention Team - FO 10000443 (1 page)

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1 (Tesoro); Exhibit 657 BCB - Letter from DOT to Mayor
2 of the City of Bellevue, Oct. 8, 1999, addressing
3 the Mayor's concerns regarding pipeline safety and
4 discussing the CAO - FO 10000441-442 (2 pages)
5 (Tesoro); Exhibit 658, BCB - Response, Equilon
6 Pipeline Company, LLC on behalf of Olympic Pipeline
7 Company, Correction Action Order CPR No 595050h, (12
8 pages) (Tesoro); Exhibit 659, BCB - Letter from
9 Olympic to DOT dated Sept. 18, 1999 re: Failure
10 During Pressure up of Hydro-test Section #2, Sept.
11 18, 1999 - OPL 1037310 (1 page) (Tesoro); Exhibit
12 660, BCB - Equilon's response, Equilon Pipeline
13 Company LLC on behalf of Olympic Pipeline Company to
14 Amended Corrective Action Order (8 pages) (Tesoro);
15 Exhibit 661, BCB - Letter from DOT to Olympic dated
16 Jan. 28, 2000, re: Hydro-testing Lone Star Steel
17 Pipe with attached pipe segment chart - OPK
18 1121254-255 (5 pages) (Tesoro); Exhibit 662, BCB -
19 Letter from DOT to Bob Talley of Olympic dated Aug.
20 25, 2000 re: Safety Management Review "systemic
21 Olympic Pipeline management concerns were identified
22 by OPS Inspectors ... that appear to have
23 contributed to the cause and magnitude of the
24 Bellingham accident." OPL 1109903-915 (13 pages)
25 (Tesoro); Exhibit 663, BCB - Letter from Olympic to

2918

1 DOT dated Feb. 29, 2000, re: Hydro-test of Kaiser
2 low frequency ERW pipe OPK 0021254-255 (2 pages)
3 (Tesoro); Exhibit 664, BCB - Fax correspondence re:
4 16" discharge switch, 16" control switch - OPL
5 1000585-587 (3 pages) (Tesoro); Exhibit 665, BCB -1T
6 Direct Testimony; Exhibit 666, Olympic Response to
7 Staff Data Request #17 (Tesoro); Exhibit 667 -
8 (N/A).

9 (EXHIBIT IDENTIFIED.)

10 JUDGE WALLIS: So with that, please
11 proceed.

12 MR. LEYH: Thank you, Your Honor.

13 JUDGE WALLIS: Excuse me. For the record,
14 I wonder if we might have counsel introduced.

15 MR. BEAVER: Your Honor, with me, and the
16 attorney who is going to be handling Mr. Batch's
17 testimony is Tim Leyh from the law firm of Danielson
18 Harrigan and Tollefson.

19 JUDGE WALLIS: Could we have appearance
20 information for you, please? Your office address,
21 your telephone number, your fax number, your e-mail
22 address?

23 MR. LEYH: Yes, Your Honor. I gave the
24 reporter a card, but I can put it on the record.

25 JUDGE WALLIS: Please do.

2920

1 record, please.

2 A Robert Charles Batch.

3 Q What is your business address?

4 A 2201 Linda Avenue, Southwest, Renton,
5 Washington, 98055.

6 Q What is your current position at Olympic,
7 Mr. Batch?

8 A I am currently president of Olympic
9 Pipeline Company.

10 Q And are you testifying here on behalf of
11 Olympic?

12 A Yes, I am.

13 Q Are you sponsoring Exhibit Numbers 601-T,
14 602, and supporting Exhibits 610 through 623?

15 A Yes.

16 Q And you have previously offered written
17 testimony to the Commission, have you not?

18 A Yes, I have.

19 Q Do you have any corrections to make to that
20 testimony?

21 A I have two minor corrections to my
22 substituted rebuttal testimony.

23 Q Would you please read those into the
24 record?

25 A Yes. BCB 32-D on page 6, line 4, replace

2921

1 BCB- with a blank with BCB 22-T at 9.

2 CHAIRWOMAN SHOWALTER: Our versions have no
3 lines. Is that true of yours?

4 COMMISSIONER HEMSTAD: (Nods head.)

5 CHAIRWOMAN SHOWALTER: Which may prove to
6 be problematic if you are referring to page and line
7 numbers. Do we have any copy that does have lines?

8 MR. LEYH: Your Honor -- or Commissioner,
9 we have just two corrections. One is at line 4 and
10 the other is line 1. I wonder if we just read them
11 into the record, it would be possible just to count
12 down and get to the right place.

13 CHAIRWOMAN SHOWALTER: We can do that, but
14 what about other questions?

15 MR. BEAVER: We're definitely going to find
16 out what happened.

17 CHAIRWOMAN SHOWALTER: In other words, if
18 any of the counsel is going to be making references
19 to page and line numbers, we're not going to be able
20 to follow. So it might be better to get a copy with
21 line numbers before we start.

22 MR. BRENA: We don't have line numbers
23 either, so we can't make those kinds of references.

24 MR. FINKLEA: That's true on all of the
25 counsel.

2922

1 MR. TROTTER: We will phrase our questions
2 in terms of paragraphs and locations in the
3 paragraph. That's the best we can do.

4 JUDGE WALLIS: And I will ask that while
5 Mr. Leyh is examining this witness, that he be the
6 company's attorney for matters involving the
7 witness.

8 MR. LEYH: Very well, Your Honor. We're
9 trying to determine whether we have another set of
10 those with the lines, and apparently we do not here.
11 I would propose that we can give substituted
12 testimony tomorrow.

13 CHAIRWOMAN SHOWALTER: Well, actually, that
14 will be more confusing. If we're stuck with what we
15 have, you will just have to make reference to the
16 question and how many lines under the question it
17 is.

18 MR. LEYH: Very well, Your Honor.

19 MR. BEAVER: Unfortunately, neither of us
20 was involved in getting that testimony to the
21 Commission, so we're still trying to find out what
22 happened.

23 JUDGE WALLIS: Let's proceed at this
24 juncture. It does appear we're stuck with the
25 unnumbered lines.

2923

1 MR. LEYH: Okay.

2 Q BY MR. LEYH: Mr. Batch, would you read
3 into the record the two corrections you wanted to
4 make to your testimony?

5 A On page 6 -- do you have page numbers? On
6 page 6, replace BCB- blank with BCB 22-T at 9.

7 JUDGE WALLIS: Would it be possible, Mr.
8 Batch, to use the current exhibit numbers from our
9 exhibit list? I think that would be very helpful to
10 us if you could.

11 THE WITNESS: That actually might take more
12 time.

13 JUDGE WALLIS: Very well.

14 THE WITNESS: And the second and last
15 change was on page 8, line 1. And it was to replace
16 my Exhibit No. BCB- and blank, with Exhibit No.
17 BCB-33.

18 MR. BRENA: 33 is 602.

19 JUDGE WALLIS: Are you ready to proceed?

20 MR. LEYH: Yes, Your Honor.

21 Q BY MR. LEYH: With those two changes,
22 Mr. Batch, do you adopt the testimony that you have
23 submitted as your own today?

24 A Yes, I do. I would point out, though, in
25 my exhibit book the rebuttal testimony that is in

2924

1 the exhibit book, Exhibit, I believe, 601-T, is
2 different than the substituted rebuttal testimony
3 that I am prepared to authorize at this point.

4 CHAIRWOMAN SHOWALTER: Well, we should make
5 sure our 601-T does say substituted rebuttal, so we
6 really do want to know that we're all on the same
7 page.

8 THE WITNESS: Right.

9 MR. BRENA: So does Tesoro, Chairwoman.

10 MR. LEYH: Is that what you have?

11 THE WITNESS: No.

12 MR. LEYH: Okay. I believe we're ready to
13 proceed, Your Honor.

14 JUDGE WALLIS: Very well.

15 MR. LEYH: I apologize for the confusion.

16 Q BY MR. LEYH: With those changes, do you
17 adopt the testimony you have provided as your own
18 today?

19 A Yes, I do.

20 Q And if you were asked those questions today
21 on the stand, would your testimony be in your
22 written testimony?

23 A Yes, it would.

24 MR. LEYH: Mr. Batch is available for cross
25 examination.

2925

1 MR. TROTTER: Thank you, Your Honor.

2 CROSS EXAMINATION

3

4 BY MR. TROTTER:

5 Q Welcome back, Mr. Batch.

6 A Thank you.

7 MR. TROTTER: Your Honor, I would like to
8 move into evidence the deposition testimony of
9 Mr. Batch of April 22nd, 2002, and the accompanying
10 Exhibits 603 through 609. I note two of those
11 exhibits, 605 and 606 have been designated by
12 Olympic as confidential.

13 CHAIRWOMAN SHOWALTER: Mr. Trotter, can I
14 ask you to speak up. I am having trouble hearing.
15 I notice everyone's voices have dropped in the
16 afternoon.

17 JUDGE WALLIS: Is there objection?

18 MR. LEYH: No objection, Your Honor.

19 JUDGE WALLIS: And just as a preliminary
20 matter, as to those items which are designated
21 confidential, is the company going to waive
22 confidentiality?

23 MR. LEYH: Can you give me the pages,
24 again, please?

25 JUDGE WALLIS: Exhibits 605, 606 and 607-C.

1 MR. TROTTER: Your Honor, it's only 605 and
2 606 that's confidential, as I understand it.

3 MR. LEYH: Are there particular parts of
4 the exhibits that you intend to use, because they
5 are rather lengthy exhibits?

6 MR. TROTTER: No, but I covered them in the
7 deposition, and the testimony is not confidential.
8 And I don't intend to reask the same questions.

9 MR. LEYH: We will waive the
10 confidentiality.

11 JUDGE WALLIS: Thank you. So noted in the
12 record. Mr. Trotter.

13 MR. TROTTER: Thank you.

14 (Exhibits 601-609 Admitted)

15 Q BY MR. TROTTER: Mr. Batch, Olympic
16 received a 62 percent increase in its interstate
17 rates effective August 2001; is that correct?

18 A Are you referring to the FERC rates.

19 Q Yes?

20 A I believe we received rates. I believe
21 that went into effect in September, but I believe
22 FERC did issue them in August, yes.

23 Q And Olympic received a 24.3 percent
24 increase in interim rates in this state effective in
25 February of this year; is that correct?

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1 A That's correct.

2 Q Is Olympic Pipeline still overnominated
3 after those increases were put into effect?

4 A Could you just elaborate a little bit on
5 your terminology, "overnominated"?

6 Q Are you transporting less volume than your
7 shippers are asking to you ship?

8 A To the extent that the shippers, I believe,
9 would like to ship more than they can, the system
10 has been prorated for some time. And those prices
11 are based on historical volumes. So to the extent
12 that they are held to their historical volumes based
13 on capacity issues, yes, that's true.

14 Q At any time since August 2001 has Olympic
15 Pipeline not been prorated?

16 A Not to my knowledge.

17 Q If the pipeline is restored to 100 percent
18 pressure, is there any doubt in your mind that you
19 will have enough product offered by shippers to
20 transport at the 100 percent pressure?

21 A I am sorry. Could you ask that question
22 again, please?

23 Q If the pipeline is restored to 100 percent
24 pressure, is there any doubt in your mind that
25 pipeline will be actually transporting at its fully

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1 rated capacity within operational limits of down
2 time, and so on?

3 A It's my understanding that if we can get to
4 100 percent pressure, we will be able to run more
5 product through the line.

6 Q And you are making your investments based
7 on that assumption, aren't you? In other words, if
8 you didn't expect any more through-put by increasing
9 pressure to 100 percent, you wouldn't be doing it,
10 would you?

11 A I think it's important to get to 100
12 percent so that we can increase the through-put on
13 the line, yes, sir.

14 Q And increase your revenues accordingly?

15 A Absolutely.

16 Q I would like to ask you to update us on
17 some of the financial issues that we have studied
18 with you before, and in your deposition that were
19 not addressed by Mr. Peck today.

20 Has there been any substantial changes in
21 the amount of debt Olympic has outstanding
22 currently, around the 150 million dollars?

23 A No substantial changes that I am aware of.

24 Q So the table that you set forth, if you
25 recall, in your interim rate case testimony,

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1 Rebuttal Exhibit 3-T, page 3, that table is still
2 essentially correct today?

3 A It is. We have a principal payment due to
4 Prudential, I believe, this week for about one and a
5 half million dollars, and paid out interest in May.
6 But by and large, it is still accurate.

7 Q And are you going to make that payment this
8 week?

9 A Yes, we plan to.

10 Q Would you accept, subject to check, that at
11 the end of 2001 the total amount of Olympic's net
12 carrier property, including Bayview and Cross
13 Cascades, was about 117.8 million?

14 A Could you repeat the question?

15 Q Yes. The amount of Olympic's net property
16 reported on its FERC form 6, which includes Bayview
17 and Cross Cascades was 117.8 million dollars?

18 A I would accept that subject to check.

19 Q And am I correct that Cross Cascades
20 project is approximately 21.5 million?

21 A I believe that's what I recall.

22 Q So net of Cross Cascades, the amount of
23 Olympic's net carrier property would be 96.3
24 million?

25 A Again, subject to check.

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1 Q Did you hear Mr. Peck testify that Olympic
2 will be writing off Cross Cascades shortly?

3 A I did hear him refer to Cross Cascades in
4 the context of the audit that is going to be
5 performed, and the probability that the auditors
6 will require that to happen.

7 Q That is consistent with your understanding?

8 A Actually, it was new information to me.

9 Q If we take 150 million in debt, and
10 subtract 96.3 million in net carrier property, would
11 you agree with my arithmetic that that means your
12 debt exceeds net carrier property by 54.7 million?

13 A Subject to check, doing the arithmetic,
14 and -- I am not able to do it in my head right
15 now -- yes, sir.

16 Q Is Olympic seeking in this case to recover
17 that 54.7 million dollars?

18 A I think what Olympic is looking for are
19 rates that are fair, just, reasonable, and
20 sufficient so that we can attract capital under
21 reasonable terms.

22 Q And in doing so, is Olympic expecting rate
23 payers to pay for 54.7 million dollars in the
24 process?

25 A I am not sure. I would need to check with

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1 someone.

2 Q Who would you need to check with?

3 A Probably someone who has been working the
4 financials of the case. Mr. Howard Fox might be
5 someone I would like to check with.

6 Q So you don't know, today, the answer to
7 that question?

8 A I am not sure of the answer to that
9 question.

10 Q Olympic's current owners have not made any
11 equity investment in Olympic to date, have they?

12 A Well --

13 MR. LEYH: I object to the form. I think
14 that mischaracterizes the evidence.

15 MR. TROTTER: Without specificity, I ask
16 the witness to respond. If it mischaracterizes the
17 evidence, in his knowledge, he can correct it.

18 THE WITNESS: I am not sure the context of
19 your question. Are you asking if any equity has
20 been put into the company?

21 Q BY MR. TROTTER: Yes.

22 A In what time frame?

23 Q Since BP purchased an interest in Olympic
24 Pipeline.

25 A I am not aware of any.

2932

1 Q What about Equilon? Did they provide any
2 equity capital to Olympic since their ownership?

3 A I don't know.

4 Q Will you accept, subject to check, that the
5 answer is no, or none? Is that something you can
6 check?

7 A Yeah, I think that's something I can check.
8 Yes.

9 Q I would ask you to accept that, subject to
10 check. Turn to page 2 of your Exhibit 601-T.

11 A (Complies.)

12 Q Last paragraph, the last two sentences. I
13 am going to focus on the second to last sentence.
14 It says, "BP ARCO loaned Olympic 53 million dollars
15 starting in June of 2000, and that at least 36
16 million was used for new capital spending." Do you
17 see that?

18 A What page, again?

19 Q Page 2.

20 A Yes.

21 Q Does it follow, then, that 17 million of
22 the 53 million was not used for new capital
23 spending?

24 A To my knowledge, the rest was used for
25 major maintenance projects or safety projects, and

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1 other regulatory requirements.

2 Q Would those other items be operating
3 expenses?

4 A Depends on how you characterize it. Not
5 being an accountant, I am not sure what bucket it
6 would go in. But it would include projects like
7 tank painting, corrosion protection, right-of-way
8 maintenance, and those sorts of projects.

9 Q Was any of it used to deal with the Whatcom
10 Creek incident, the 17 million?

11 A Not to my knowledge, no.

12 Q You then state, quote, "This also allowed
13 Olympic to bring all segments of the system to full
14 operating capability and to implement the higher
15 level of O&M costs necessitated by new Federal
16 regulations and requirements." Do you see that?

17 A Yes, I do.

18 Q By full operating capabilities, you mean 80
19 percent pressure?

20 A What I mean is that all of the lines would
21 be operating at 80 percent pressure, yes.

22 Q So would it be correct that the company's
23 2001 results of operations would reflect its
24 compliance with Federal regulations that were
25 applicable at that time?

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1 A Yes.

2 Q So unless costs of compliance with new
3 regulations are removed by any party to this
4 proceeding, they would remain reflected in Olympic's
5 per book results of operating; is that correct?

6 A I am not sure what you are asking.

7 Q Well, I am focusing your testimony.

8 A Yes.

9 Q That the money BP invested allowed Olympic
10 to implement the higher level of O&M costs necessary
11 to date by new Federal regulations and other
12 requirements.

13 A Yes.

14 Q So you spent more money to comply with new
15 safety regulations? That is the point of this
16 testimony?

17 A We spent a lot of money, including the high
18 consequence area rules, and the operator
19 qualification rules, yes.

20 Q And that money was spent during the year
21 2000 and 2001, is that correct, this 53 million?

22 A I am sorry?

23 Q When was the 53 million dollars that were
24 loaned after June of 2000 -- or beginning in June of
25 2000?

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1 A Yes, it would have been June 2000, and
2 2001, and perhaps some in 2002.

3 Q So to the extent that you incurred higher
4 and O&M costs necessitated by new Federal
5 regulations in the year 2001, your results of
6 operations will reflect your payment for those
7 additional requirements, correct?

8 A Yes.

9 CHAIRWOMAN SHOWALTER: Are we talking about
10 a calendar year, or a June -- July to July year
11 right now?

12 Q BY MR. TROTTER: When I -- Mr. Batch, I
13 intended my reference to 2001 to mean calendar year
14 2001. Did you understand it to mean that?

15 A I wasn't exactly sure what period of time
16 you were referring to.

17 Q Is your answer the same, if you understand
18 that my question relates to your results of
19 operations for calendar year 2001, that they would
20 reflect the additional O&M costs necessitated by new
21 Federal regulations, and other requirements?

22 A To the extent that we had significant
23 safety requirements that we had to put into effect,
24 it would have been -- half would have been done
25 2000-2001 and beyond.

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1 Q And just focusing on calendar year 2001, to
2 the extent you had additional and higher O&M costs
3 necessitated by new Federal regulations and other
4 requirements, those would be reflected in your
5 results for that year, correct?

6 A It would be reflected in that year and
7 subsequent years.

8 Q And were they substantially higher in the
9 year 2001 than in prior years; that is, your costs
10 necessitated by new Federal regulations and other
11 requirements?

12 A Again, I can only speak for after BP took
13 over operations of Olympic. And when we came in
14 there was certainly a lot of investment that needed
15 to be made, both capital investment as well as
16 projects relating to maintenance and other
17 regulatory projects that were required.

18 Q Was Olympic not complying with new Federal
19 regulations and other requirements prior to BP
20 taking over as operator?

21 MR. LEYH: Object, Your Honor. No
22 foundation.

23 MR. TROTTER: I can lay it, if it's
24 necessary.

25 JUDGE WALLIS: The witness may respond.

2937

1 THE WITNESS: Again, I can't really speak
2 to what the prior operator was doing before we got
3 here.

4 MR. TROTTER: Those are all my questions,
5 Mr. Batch. Thank you.

6 MR. FINKLEA: Just to mix things up,
7 Mr. Brena and I are going to switch the number 2 and
8 3 slots.

9

10 CROSS EXAMINATION

11

12 BY MR. FINKLEA:

13 Q Good afternoon, Mr. Batch. I am Ed Finklea
14 on behalf of Tosco. My first questions go to your
15 prepared direct testimony, which has been marked for
16 identification as Exhibit 611.

17 CHAIRWOMAN SHOWALTER: Mr. Finklea, would
18 you give a little more energy to your questions?

19 Q BY MR. FINKLEA: Turning to page 2 of your
20 testimony, you identified yourself as the president
21 of the company. Who is your immediate supervisor?

22 A Mr. Peck is my supervisor.

23 Q And as I understand it, Olympic has a board
24 of directors?

25 A Yes, that's true.

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1 Q And Mr. Peck has identified himself as
2 being a member of the board. Who are the other
3 members of the board?

4 A There are three BP members of the board,
5 and two Shell. The other members of the board are
6 Don Kinstra with BP -- and unfortunately, I am
7 drawing a blank here -- Steve Pankhurst from
8 BP.

9 The Shell members the board are Bob
10 Eastlake and Denise Burch.

11 Q In your professional qualifications you
12 identify your degrees. I take it from this you are
13 not an economist?

14 A I am not.

15 Q And I also take it, then, that you are not
16 an expert in FERC pipeline rate making methodology.
17 Is that fair to assume here?

18 A Yes, that is correct.

19 MR. BEAVER: I hate to butt in. We now
20 have numbered testimony.

21 JUDGE WALLIS: Let's be off the record for
22 a minute, please.

23 (Discussion off the record.)

24 JUDGE WALLIS: Thank you. Let's be back
25 on the record, please.

1 MR. FINKLEA: And I will note as I am going
2 through I will do like Mr. Trotter did, and try to
3 lead us to the right part of the page. I think it
4 works fine.

5 Q BY MR. FINKLEA: On page 3 when you talk
6 about the history of how BP wound up with Olympic,
7 who were the other bidders to operate Olympic in the
8 year 2000?

9 A I believe it was Equilon Pipeline.

10 Q And was it -- we may be going over ground
11 we covered with Mr. Peck. It was the board of
12 directors of Olympic that made the selection; is
13 that correct?

14 A That's my understanding, yes.

15 Q If you could turn to page 5 of the same
16 exhibit.

17 A I am sorry. Which exhibit are we on again?

18 Q We're on what has been marked as Exhibit
19 611. It was your direct testimony which was filed
20 here, as well as filed with the Federal Energy
21 Regulatory Commission. I think it was originally
22 marked as BCB 9 for identification.

23 A Yes.

24 Q I am on page 5 now. Page 5 has lines.
25 Line 19 is where my focus is at the moment. I

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1 believe it's only the rebuttal testimony that
2 doesn't have lines.

3 Is it your testimony that Olympic did not
4 include all of its 1998 new investment in rate base
5 used in its rate filing at that time?

6 A That's what the testimony says, yes.

7 Q How much new investment was not included?

8 A As I state in the testimony, moreover it's
9 my understanding that when Olympic filed for cost
10 based interstate and intra-state rate base increase
11 at the end of 1998 to recoup a substantial
12 investment made that year, it did not attempt to
13 recoup the full amount of that investment projecting
14 a total cost of service for 1999 of 47.328 million,
15 and projected operating revenue subsequent to the
16 increase of only 44.508 million, approximately 6
17 percent below Olympic's cost of service.

18 Q And is it your position that Olympic was
19 entitled to recoup the full amount of its 1998 new
20 investment and its 1999 cost of service?

21 A I would defer that to Brett Collins who
22 will follow me who is kind of our financial person
23 who is looking into these cost of service numbers.

24 Q If you could turn next to page 6 -- or I
25 guess we're still on 6, up at line 3?

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1 A (Complies.)

2 Q There's additional discussion on the next
3 line about substantial safety related investments.
4 A similar question I want to ask, is it your
5 position that Olympic was entitled to include the
6 safety investments you are mentioning there in its
7 rate base at that time?

8 A Again, I am not exactly sure at which time
9 you are referring.

10 Q Well, I am focused on exactly the ones you
11 are discussing at pages 5 and 6 of your direct
12 testimony, and the reference to the 1999 cost of
13 service study.

14 A I am not sure in this testimony that I am
15 trying to link the two thoughts here.

16 Q Well, first, could you just read for --
17 reread your sentence that starts at line 3.

18 A Sure. "Olympic's profitability plunged
19 further as a result of the substantial safety
20 related investments made after the Bellingham or
21 Whatcom Creek incident, and significantly reduced
22 revenue caused by reduced through-put."

23 Q Two questions. Was it -- is it your
24 position that those safety related investments
25 belonged in your rate base in your 1999 cost of

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1 service?

2 A I am not making any claims one way or the
3 other. That might, again, be a better question for
4 Brett Collins.

5 Q Are those safety related investments that
6 were made at that time recurring expenses, which
7 Olympic would be entitled to include in a cost of
8 service study today?

9 A Again, you are talking about a time frame
10 of 1999; is that correct?

11 Q I am talking about your reference to 1999
12 cost of service study, yes.

13 A Again, I am not trying to relate safety
14 improvements that Olympic has made since BP has
15 become the operator to this 1999 study.

16 Q So it's your position that if those safety
17 related investments were made outside of a rate
18 period, then the company has no particular
19 regulatory right to recoup those investments until
20 it files another rate case; is that correct?

21 A Again, I am not a regulatory specialist, so
22 I don't have an opinion on that.

23 Q Could we turn next to page 11 of this same
24 direct testimony?

25 JUDGE WALLIS: What exhibit is that,

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1 Counsel?

2 MR. FINKLEA: Your Honor, I am still on
3 what has been marked for identification as Exhibit
4 611. When it was originally filed, it was marked
5 BCB 9, Mr. Batch's direct testimony in this
6 proceeding, which also is the direct testimony he
7 has filed with the Federal Energy Regulatory
8 Commission, as I understand it.

9 CHAIRWOMAN SHOWALTER: His direct testimony
10 here is 610, and then the attachment which is his
11 direct testimony at the FERC is 611.

12 MR. FINKLEA: You are correct,
13 Commissioner. And the way, at least, that we have
14 been reading this is 611 is essentially offered to
15 be incorporated by reference into this docket. It
16 has a cover sheet that says, Before the Washington
17 Utilities and Transportation Commission, and it's
18 marked as Batch Olympic Pipeline General Rate Case.

19 But then the first page of it is marked
20 with a caption, United States of America, Before the
21 Federal Energy Regulatory Commission.

22 CHAIRWOMAN SHOWALTER: Let's call it 611
23 instead of direct. It would be clearer for the
24 record.

25 MR. FINKLEA: That's fine.

1 Q BY MR. FINKLEA: What we have been
2 discussing, Mr. Batch, is prepared direct testimony
3 that you have offered at the Federal Energy
4 Regulatory Commission, and offered in this
5 proceeding as an exhibit; is that correct?

6 A Yes.

7 Q So if we could turn again to page 11, and I
8 am looking in particular at a statement that begins
9 at line 20.

10 A (Complies.)

11 Q If you could just refresh your recollection
12 by rereading -- you don't have to read it into the
13 record -- but rereading line 20 of page 11 through
14 line 2 of page 12. You discuss there a number of
15 corrective actions that Olympic has undertaken.

16 A (Reading document.) Yes, I have got it.

17 Q Is deformation inspection tools one of the
18 three state-of-the-art devices used to verify the
19 integrity and safety of a pipeline system?

20 A Deformation tool is a tool that looks for
21 dents or anomalies within the system, yes. That is
22 one of the -- one of a few different types of
23 technology smart-pick devices that are used.

24 Q And how frequently are these inspection
25 tools used, the deformation one?

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1 A At Olympic, I think we have made a
2 commitment to run the deformation tool every year
3 since we became the operator for at least three
4 years, because of the significant problems we have
5 seen with third-party damage, and top side dents
6 from excavators that choose not to use the One-Call
7 System. So we made a recognition of up front that
8 this was a risk and exposure to this pipeline that
9 required some extensive inspection and possible
10 repair.

11 Q Now, the next one you mention is the
12 magnetic flux tool, and that's another -- as I take
13 it, another state-of-the-art inspection device; is
14 that correct?

15 A Yes.

16 Q And then you also mention the transverse
17 flux inspection tool?

18 A Yes.

19 Q And regarding the magnetic flux, how often
20 is that used?

21 A We have a periodic time table. I believe
22 we are running those now in two to three year -- two
23 to three year increments, every two to three years.

24 Q And how about transverse flux?

25 A That is the inspection tool that looks at

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1 the longitudinal seams of the pipe, significantly
2 important with regard to ERW pipe seams. That's
3 being run for the first time end of last year. And
4 I believe we completed our final run last week of
5 this year.

6 Q Did I take it that's not something you
7 would do annually the way you -- is it "deformation"
8 or "defamation" tool?

9 A Deformation tool.

10 Q Am I correct that the magnetic flux and
11 transverse flux are not something that have to be
12 done annually?

13 A We made a commitment to look at Olympic's
14 pipeline with all the technology that's available to
15 us. Again, because of the exposure to third-party
16 hits, we felt deformation tool was necessary to run
17 every year.

18 Historically, I think the industry is
19 nowhere near that level of frequency in running
20 inspection tools. With regard to the TFI tool, that
21 is still a relatively new piece of technology that I
22 think Olympic, and a few other companies, have run.
23 And we're just pretty much trying to understand the
24 value and the benefit of the TFI tool, what it's
25 going to show us.

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1 Q Do you know -- this would call for you to
2 have in front of you what has been marked for
3 identification as Exhibit 819. It's Ms. Hammer's
4 original cost of service study, I think also
5 referred to as OPL 31. And my questions go both to
6 that, and then to the rebuttal case.

7 Is the cost of inspection, using first the
8 magnetic flux tool, included in the total operating
9 expenses that Olympic is now requesting rate
10 treatment now on for the test period?

11 A I am not completely sure whether the
12 inspection tools are categorized as capital or
13 expense, and how we're claiming that within our
14 case.

15 JUDGE WALLIS: Mr. Finklea -- excuse me,
16 Mr. Batch -- could we have a repeat citation to
17 Exhibit 819.

18 MR. FINKLEA: Yes. The citation to 819, as
19 I understand it, it was originally marked as OPL 31.
20 And I was looking in particular at schedule 12 of
21 that exhibit. It has been marked for identification
22 at this time as Exhibit 819. It was also known as
23 CAH-4, cost of service case 2.

24 MR. LEYH: Your Honor, I don't believe the
25 witness has a copy of that, and I don't believe it

1 was listed in the cross exhibits for Tosco.

2 MR. FINKLEA: Well, I am not offering it as
3 an exhibit. The company is already offering it as
4 an exhibit.

5 JUDGE WALLIS: Well, we expect the company
6 to offer it. And our convention is an exhibit that
7 has been marked for identification by the company
8 may be inquired into.

9 MR. LEYH: I wonder if we could give the
10 witness a copy of that exhibit.

11 JUDGE WALLIS: May we do that, please.

12 Q BY MR. FINKLEA: Do you have that now in
13 front of you, Mr. Batch?

14 A I have the exhibit, yes.

15 Q Is the cost of inspection using the
16 magnetic flux tool included in the total operating
17 expenses for the base period -- or the test period
18 in OPL -- first of all in OPL 31, or what has been
19 marked for identification as Exhibit 819? And I am
20 on schedule 12 of that exhibit.

21 A This is a level of detail that I am not
22 sure I can properly speak to.

23 Q Well --

24 A Certainly inspection costs need to be
25 recovered. I mean, it's part of the safety efforts

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1 for this pipeline. But as far as the level of
2 detail that you are asking, I don't really think I
3 have the answers for you. I think I would defer
4 that to Ms. Hammer, since this is one of her
5 exhibits.

6 Q Well, let's talk about this in general,
7 then. Is it the company's position that the
8 magnetic flux inspection, as you said, only occurs
9 every two or three years? Is that, in your opinion,
10 something that should be included as an operating
11 expense for purposes of setting rates here, or
12 should it be capitalized, or should it be amortized
13 over a number of years? What is your company's
14 position on that?

15 A Again, I am not a rate specialist or an
16 accountant, and I would, frankly, prefer to defer
17 those questions to the right people who can answer
18 that question.

19 Q And that would be Ms. Hammer or
20 Mr. Collins, or both?

21 A Perhaps both.

22 Q And I will -- I assume the answers would be
23 the same if I am asking about the transverse flux
24 inspections?

25 A Yes.

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1 Q But you do agree that both the magnetic
2 flux and the transverse flux is not something that
3 is done annually?

4 A Yes, that's correct.

5 Q Again, on page 12 of the same exhibit, 611,
6 there's a statement regarding visual inspections on
7 lines -- starting at line 5 in the middle. Does
8 your company's visual inspection program cover the
9 entire pipeline system?

10 A Yes, it does.

11 Q And has a visual inspection program been
12 completed for the entire system?

13 A Visual inspections have been done with
14 the -- in conjunction with the repair program. And
15 the process -- and I might just lay out the process
16 a little bit. We plan to run an internal inspection
17 tool. We run the internal inspection tool. We have
18 some time that we need to spend to analyze the
19 results of the internal inspection tool.

20 That tool correlates various findings,
21 features, and anomalies that it picks up inside of
22 the pipe, and correlates that externally to the real
23 world to where that pipe actually is.

24 At that point, once we have those
25 correlations made, we then have to get proper

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1 permits for fill and grade to be able to physically
2 dig the pipeline -- because primarily most of the
3 pipeline is underground -- to that feature or
4 finding that the tool is indicated and visually
5 inspect what the tool was seeing.

6 So in that context, yes. For every anomaly
7 that we need to inspect, we have to dig it up and
8 visually inspect it before the repair.

9 Q And has the visual inspection program been
10 completed for the entire system at this time?

11 A No. I mean, that's an ongoing process.
12 Certainly the first several rounds of internal
13 inspection and visual information and repair are
14 complete, but we're just completing now the TFI
15 inspection runs, and in the process of analyzing the
16 data that the TFI tools have found.

17 And once we analyze the data, again, we
18 will need to make correlations to the pieces of the
19 pipeline that it has found something. And we will
20 have to go and start digging those areas to visually
21 inspect those locations.

22 Q In your opinion, have all the appropriate
23 repairs from those inspections been completed?

24 A Which inspections?

25 Q From the visual inspections?

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1 A If we have gone through the effort and
2 expense of digging it up, permitting it and digging
3 it up and identifying what the anomaly is, yes, I am
4 confident that we have made the proper repairs.

5 JUDGE WALLIS: Mr. Finklea, may I ask how
6 we're doing on your cross?

7 MR. FINKLEA: I am about 40 percent of the
8 way there.

9 JUDGE WALLIS: Let's take a 15-minute
10 break, then, please.

11 END OF AFTERNOON SESSION AT 3:30 P.M.

12

13