FIVE-YEAR REVIEW OF THE OIL PIPELINE INDEX
FERC Docket No. RM15-20-000
Technical Conference
July 30, 2015

Preliminary Outline and Preview of Comments
The Canadian Association of Petroleum Producers

- Given the passage of time and evolution of the oil pipeline industry since the issuance of Order No. 561, the Commission may wish to:
    - Take into account intervening, changed circumstances since 1993
    - Take note of the results of these and other developments relating to indexing in the larger context

- Intervening, Changed Circumstances since 1993: The Rise of "Customized" Oil Pipeline Rates
    - Order 561 implemented not just indexing, but also:
        - Settlement Rates as alternative to cost-based rates;
        - Market Based Rates
    - Contract rates emerged as an adjunct of common carriage (beginning with *Express*, 1996) Use of "committed" rates grows, becoming a norm rather than an exception
    - Increased use of surcharge mechanisms for discrete projects and investments

- Unintended Consequences of These Changes
    - The data captured via the Kahn methodology now encompass costs incurred in connection with negotiated and other customized oil-pipeline rates
    - The Kahn methodology effectively imports non-cost based rates into the indexing of cost based rates.
    - The index effectively imposes these costs on services for which no negotiations or other customized circumstances apply
    - Given the proliferation of customized rates, the data may be more reflective of non-indexed services than indexed-rate services

- Illustration: A pipeline negotiates with its customers to implement a surcharge to replace or modernize facilities. The same pipeline continues to charge indexed rates for its base services. The costs of the surcharged project are captured in, and influence the outcome of, the Kahn methodology
- Illustration: Pipelines or services that have not undergone expansions, modernization nor implemented customized rates experience continuing cost increases traceable to the increasing costs of pipelines that have done so. Kahn methodology had no reason to take these into account and does not do so.

- Similar Potential Anomalies in "Cost" Data
  The repricing of assets in connection with new projects – due to corporate transfer, lease, or similar transactions – may also result in distortions of cost data

- Illustrative "Big Picture" Consequences
  - Costs of capital from original indexed rates, circa 1993, remain embedded in indexed rates
    - Equity 13% (approximate)
    - Debt 10% (approximate)
  - Cost characteristics of customized projects have disproportionate impact throughout industry
    - Increase net plant 2009-2014= 55%
    - Increase in barrel miles = 7.7%

- Potential Solutions?
  - Additional data screens; and or
  - Benchmark checks on reasonableness of Kahn results