

Colonial Pipeline Co.
92 FERC ¶ 61,144 (2000)

The Commission established in this proceeding that cost studies were required to justify proposed alternative sources of transportation in an origin market similar to the cost study requirements in a destination market. For an origin market, the Commission adopted a “netback” cost analysis that required a comparison of the price a shipper receives for selling its products when using the applicant pipeline and when using proposed alternative sources of transportation. The Commission also followed the detailed cost study formulation established in the TEPPCO proceeding that used a threshold price increase to compare proposed alternative sources. The Commission in this case did not make a finding on the appropriate threshold price increase, however, instead relying on a range of different price increases to gauge the competitiveness of proposed alternatives. In addition, the Commission signaled in this proceeding that it would now principally cite to the market share and market concentration statistics in its determination of market power. Other factors that the Commission had cited in prior proceedings, such as excess capacity, begin to be omitted in the reasoning for the Commission’s findings on market power.

UNITED STATES OF AMERICA 92 FERC ¶ 61,144
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: James J. Hoecker, Chairman;
William L. Massey, Linda Breathitt,
and Curt Hébert, Jr.

Colonial Pipeline Company

Docket No. OR99-5-000

ORDER ON APPLICATION FOR MARKET POWER DETERMINATION AND
ESTABLISHING A CONFERENCE

(Issued August 1, 2000)

On March 26, 1999, Colonial Pipeline Company (Colonial) filed an application for a market power determination pursuant to Part 348 of the Commission's regulations.¹ Colonial seeks permission to charge market based rates in its Gulf Coast origins and destinations. As discussed below, the Commission finds that the Lafayette, Louisiana, and the Beaumont-Port Arthur, Texas destination markets are uncontested. In addition, the Commission finds that Colonial lacks significant market power in the Jackson, Mississippi, and the Baton Rouge-New Orleans destination markets. The Commission will permit Colonial to implement market based rates in these markets. The Commission also will direct its staff to convene a conference to explore the facts and issues regarding the Western Gulf Coast and Baton Rouge-New Orleans Origin Markets.

I. Background

¹18 C.F.R. Part 348 (1999).

Colonial is a common carrier pipeline, constructed in 1962 as a joint venture among the affiliates of 10 major oil companies.² Colonial transports refined petroleum products, e.g., gasoline, distillate, kerosene and jet fuel, from origins on the Gulf Coast to the New York Harbor (and intermediate points) over a system that includes 2,886 miles of mainlines, 2,196 miles of stublines, and 192 miles of delivery lines. Colonial is a bulk delivery pipeline that delivers to marine and truck distribution terminals, airports, other pipelines, power generating plants, and Department of Defense facilities. Most of the petroleum product volumes shipped by Colonial are delivered to large distribution terminals. The average distance a barrel of petroleum product is transported on Colonial is slightly less than 1,000 miles.

The Gulf Coast region of Colonial's system serves primarily as an origin on the pipeline. There are large shipper-owned bulk storage facilities that can also serve as destination points on the pipeline. At its origin in Houston/Pasadena, Colonial receives petroleum products from a large number of pipeline and refinery connections that it transports eastward in two parallel 40-inch and 36-inch pipelines to Herbert, Texas, where Colonial interconnects with lateral connections to Beaumont and Port Arthur, Texas. At Herbert, Colonial receives product from a number of refineries located in Beaumont and Port Arthur, and also delivers product to TE Products Pipeline, L.P. (TEPPCO), for further movement to the Midwest.

The next origin on Colonial is at Lake Charles, Louisiana where Colonial receives product from Conoco's Westlake refinery and CITGO's Lake Charles refinery from a connection with the shipper-owned Lake Charles pipeline. At Krotz Springs and Baton Rouge, Louisiana, Colonial receives product from several refineries and can make deliveries at Opelousas, Louisiana, to a Chevron storage facility. In Collins, Mississippi, Colonial makes deliveries for further transportation on Plantation Pipeline and to an Amerada Hess storage facility in Collins.

II. The Instant Filing

²Colonial's current stockholders are Amoco Pipeline Holding Company (14.32 %), Atlantic Richfield Company (1.58 %), Citgo Pipeline Investment Company (13.98 %), Conoco Pipeline Company (7.55%), Koch Petroleum Corporation (6.46%), Marathon Oil Company (2.50%), Mobil Pipeline Company (11.49 %), Phillips Petroleum International Investment Company (7.10%), Texaco Trading and Transportation Inc. (14.27%), and Union Oil Company of California (20.75%).

With this application, Colonial seeks permission to file market-based rates on shorter movements between origins and destinations in its Gulf Coast region, *i.e.*, Texas, Louisiana and Mississippi. Colonial proposes to charge market-based rates for movements from origins in Pasadena and Houston, Texas; Hebert (*i.e.*, Beaumont and Port Author), Texas; Lake Charles, Louisiana; Krotz Springs and Baton Rouge, Louisiana; and Collins Mississippi, to destinations in and around Beaumont and Port Author; Opelousas, Baton Rouge, and Lafayette, Louisiana; and Collins and Meridian Mississippi. Colonial defines the relevant product market as pipelineable refined petroleum products, which consist of motor gasoline, distillates, kerosene, and jet fuel.

III. Protests and Interventions

Colonial filed its application on March 26, 1999. On May 10, 1999, Transmontaigne Product Services, Inc. (TPSI) filed a motion requesting a two-week extension of time, *i.e.* until June 8, 1999, to file protests, if necessary. On June 8, 1999, TPSI filed its protest and motion to intervene. Chevron also filed a motion to intervene on June 8, 1999. Colonial filed a motion for summary disposition, which included supplemental testimony from Dr. George R. Schink, on July 19, 1999. On July 21, 1999, TPSI requested a three-week extension of time to respond to Colonial's motion for summary disposition. TPSI filed its reply to Colonial's motion for summary disposition on August 24, 1999. On August 25, 1999, Chevron also replied to Colonial's motion for summary disposition.

TPSI remonstrates that Colonial's application is undermined by the use of suspect methodology and a lack of evidentiary support. TPSI states that the Commission should deny Colonial's application. To be more specific, TPSI levels the following objections against Colonial's subject filing: (1) Colonial's definition of the Jackson and Baton Rouge destination markets is unsupported; (2) Colonial's HHI calculations of its market power in the Jackson and Baton Rouge markets is artificially understated; (3) Colonial's reliance on the 10% rule regarding waterborne competition is misplaced; and (4) Colonial's conglomeration of numerous BEAs into two large origin markets is improper.

TPSI states Colonial has expanded the definition of its destination markets well beyond the relevant BEAs without adducing any evidence to support, much less justify, such an expansion. For example, TPSI argues that Colonial presumes that all sources of product within a 75-100 mile straight-line radius of the border of the Jackson BEA provide effective competition within the entire BEA. However, contends TPSI, Colonial does not explain its use of the border of the BEA, as opposed to the major population center in the middle of the BEA, as the measure of the competitive reach of external sources. Furthermore, adds TPSI, Colonial presents no truck surveys or cost studies to

show that these external sources currently compete, are economically feasible, or could effectively constrain a "small but significant and nontransitory increase in price" (SSNIP) by Colonial.

TPSI presents data that it states it collected through a preliminary truck survey conducted in the Jackson BEA, which it claims illustrates that Colonial's use of a 75-100 mile radius from the border of the Jackson BEA substantially overstates the reach of external sources. In addition, continues TPSI, a study undertaken by TPSI to determine the "laid in" cost for truck shipments into the Jackson BEA demonstrates that the external sources upon which Colonial seeks to rely are not economically feasible alternatives and could not act as a check on Colonial's market power in the Jackson BEA.

TPSI states that Colonial should provide evidentiary support for its contention that sources of supply from outside each relevant BEA could act as a competitive constraint on Colonial's exercise of market power within the BEA. Since TPSI asserts that Colonial has failed to do so, TPSI contends Colonial's attempt to expand the destination market beyond the boundaries of the relevant BEA should be rejected out of hand. Also, TPSI maintains that with the studies and analysis presented in its protest, the relevant destination markets for Jackson and Baton Rouge should be limited to the boundaries of the Jackson and Baton Rouge BEAs.

TPSI asserts that Colonial makes unsupported assumptions about the Baton Rouge destination market. Specifically, TPSI states Colonial has arbitrarily combined the Baton Rouge and New Orleans BEAs into a single destination market for the purposes of its market power analysis. TPSI believes that the only apparent purpose of combining the Baton Rouge and New Orleans BEAs is to reduce Colonial's market share as well as its delivery-based and effective-capacity HHIs.

TPSI argues that Colonial's HHI calculations artificially understate its market power in the Jackson and Baton Rouge markets. TPSI further states that Colonial has included competitors from outside the relevant BEA -- despite the absence of any evidence in its application that these external sources provide effective competition to Colonial within the BEA -- as a means to dilute Colonial's market share and artificially deflate the HHI applicable to the BEA market under scrutiny.

Colonial's treatment of waterborne deliveries within the Jackson BEA, argues TPSI, arbitrarily reduces the effective capacity HHI for the Jackson market. TPSI avers that Colonial's effective capacity analysis assumes, without explanation, that local consumption will be served first by using all waterborne deliveries before product from any other source is consumed. TPSI argues there is no reason to assume that waterborne

deliveries are absorbed by the market any differently than product delivered via pipeline or truck. Moreover, continues TPSI, Colonial assumes that all waterborne deliveries in the BEA are consumed within the BEA. TPSI argues that based on its recent discussions with trucking companies operating out of the Vicksburg port terminal, a substantial portion of the product arriving at the Vicksburg facility exits the Jackson BEA, primarily to destinations north and northwest of the Jackson BEA.

TPSI states that Colonial calculates its own market share for the Jackson BEA as 23%, despite the fact that its actual 1998 deliveries into the market are more than twice that amount. Although Colonial contends that all of its deliveries to Meridian, Mississippi leave the Jackson BEA on two other pipelines, TPSI claims that Colonial provides no evidence to demonstrate that this assertion is true. TPSI believes that based on its preliminary truck survey, Colonial's assertion is erroneous.

According to TPSI, Colonial asserts that tank trucks deliver 6.2 kBD (thousand barrels a day) into the Jackson BEA based upon Colonial's estimate that "net supply" differs from "net demand" by this amount. TPSI states the arbitrary attribution of this differential to truck competition from external sources is completely unsupported by any evidence of truck movements into the Jackson BEA from external sources. TPSI believes the effect of this assumption is to artificially lower the HHI applicable to the Jackson BEA.

TPSI states when the delivery and effective capacity-based HHIs are calculated without Colonial's unsupported and unwarranted assumptions, the HHIs are dramatically higher than suggested in Colonial's application. TPSI contends that the delivery-based HHI for the Jackson BEA is 3086, while the effective capacity HHI for the Jackson BEA is 2347. Similarly, adds TPSI, Colonial's unsupported decision to combine the Baton Rouge and New Orleans BEAs also results in a substantial unwarranted reduction in the HHI calculation. According to TPSI, the effective capacity based HHI for the Baton Rouge BEA itself is 3010.

TPSI states Colonial has produced no evidence to demonstrate that all of the waterborne deliveries arriving at Vicksburg remain in the Jackson BEA. Colonial has estimated that waterborne deliveries in the Jackson BEA total approximately 11% of the effective capacity. TPSI argues that with Colonial's estimate of waterborne deliveries at only 11%, if even a small portion of the products arriving at Vicksburg leave the Jackson BEA, waterborne deliveries would fall below the 10% threshold. In addition, TPSI maintains that the 10% rule requires that the capacity of the waterborne competition must be readily expandable to ensure that it could provide enough product to defeat any SSNIP implemented by Colonial. TPSI remonstrates that Colonial has not provided any credible

evidence that the Vicksburg facility could be readily expanded to constrain an exercise of market power by Colonial. TPSI states the substantial capital cost of expanding the Vicksburg facility, as well as the environmental requirements, are formidable barriers to expansion. Furthermore, TPSI argues that Colonial's delivery data demonstrates that throughput at the Vicksburg terminal has been virtually unchanged since the early 1990s. If expansion of the Vicksburg facility to meet the growing demand of the Jackson BEA could be economically justified, TPSI posits that one would expect to see the volumes at Vicksburg grow along with the regional demand for refined products. TPSI believes the fact that Vicksburg deliveries have remained static is a strong indication that the Vicksburg terminal is not readily expandable.

Based on a preliminary analysis by TPSI personnel familiar with the Vicksburg facility, TPSI asserts that the current level of throughput at the Vicksburg terminal is near capacity, absent a significant capital investment in excess of \$1,000,000. TPSI states that the requirement that a substantial capital investment be made in order to expand the Vicksburg facility undercuts its effectiveness as a competitive constraint on Colonial's exercise of market power. Furthermore, TPSI maintains that even if waterborne deliveries marginally exceeded 10% today, the available data shows that the Vicksburg facility's market share is shrinking in the face of static deliveries and a growing market. Therefore, TPSI states there is substantial reason to believe that Vicksburg will not be able to provide more than 10% of the Jackson BEA consumption in the near future.

Chevron argues cost information is lacking in Colonial's application. Chevron asserts Colonial's application fails to address the cost and availability of possible competing transport options between the exact pairs of origins/destinations defined by Colonial. Chevron believes relying exclusively on low origin HHIs and low destination HHIs, without regard to cost and availability of exactly competing transport options between pairs of origins/destinations, does not address key considerations in evaluating whether this pipeline should be accorded market-based rates in its markets. Chevron states that low HHIs are a necessary condition, but are not sufficient to conclude that competition will keep prices down. In addition, in its response to Colonial's motion for summary disposition, Chevron argued that a hearing should be established whereby the shippers have the opportunity to challenge Colonial's claim of effective competition in certain origin and destination markets in the Gulf Coast, including Texas, Louisiana, and Mississippi.

IV. Discussion

A. Regulatory Framework

In Farmers Union Central Exchange, Inc. v. FERC (Farmers Union),³ the Court held that a particularized showing based on empirical evidence is required to prove that market forces can be relied upon to keep rates at a just and reasonable level:

³Farmers Union Central Exchange, Inc. v. FERC, 734 F.2d 1486 (D.C. Cir. 1984), cert. denied sub nom. Williams Pipeline Company v. Farmers Union Central Exchange, Inc., 469 U.S. 1034 (1984).

In setting extraordinarily high price ceilings as a substitute for close regulation, FERC assumed that, with the wide exposed zone between the ceiling and the "true" market rate, existing competition would ensure that the actual price is just and reasonable. Without empirical proof that it would, this regulatory scheme, however, runs counter to the basic assumption of statutory regulation, that "Congress rejected the identity between the 'true' and the 'actual' market price." ⁴

In other words, under Farmers Union, the Commission cannot simply presume the existence of competition or that a market-based price will be within a just and reasonable range. ⁵

In Order No. 572, the Commission established procedures to enable the Commission to comply with Farmers Union by not permitting market-based rates until there is an affirmative showing that the oil pipeline lacks market power in the relevant markets. ⁶ In order to ensure that market-based rates are not charged in the absence of such an affirmative showing, the Commission placed the burden of proving effective competition in the relevant markets on the pipeline requesting market-based rates. ⁷ The pipeline has the burden of defining and justifying the relevant market, whether it chooses to use BEAs or some other measure of the appropriate market. Similarly, the burden is on the oil pipeline to justify its inclusion of transportation alternatives and other competition in its market power analysis. Failure to make the requisite showing for any

⁴Id. at 1510 (citation omitted) (quoting *FPC v. Texaco*, 417 U.S. at 399 (1974)).

⁵Market-Based Ratemaking for Oil Pipelines, Order No. 572, 59 FR 59148 (Nov. 16, 1994), FERC Stats. & Regs. (Regulations Preambles, 1991-1996) ¶ 31,007 at 31,183 (Oct. 28, 1994), order denying rehearing, Order No. 572-A, 69 FERC ¶ 61,412 (Dec. 28, 1994).

⁶Id.

⁷The Commission is requiring no more than that an oil pipeline bear its burden of proof in a fashion that ensures that there is no reliance on presumed market forces. Id. at 31,186.

of the relevant markets will preclude the Commission from being able to approve market-based rates for the markets in question.⁸

B. Origin Markets

⁸Section 348.1 of the Commission's regulations requires pipelines requesting permission to charge market based rates to (1) define the relevant geographic and product markets (including both destination and origin markets), (2) identify the competitive alternatives for shippers, including potential competition and other competition constraining the pipeline's ability to exercise market power, and (3) compute the market concentration (HHI) and other market power measures based on the information provided about competitive alternatives.

Colonial defines its origin markets by identifying the refineries or inbound port facilities that do or could use the outbound pipeline being analyzed. The location of the refineries and the port facilities, and the local areas served by these facilities, establishes the areas to be included in the origin markets. According to Colonial, the location of refineries and pipeline interconnections in the area from the Texas Gulf Coast through Alabama militates that the Colonial receipt points at issue here be agglomerated into two separate origin markets: (1) the Western Gulf Coast Origin Market, with seven BEA Economic Areas (BEAs)⁹ (Beaumont-Port Arthur, Austin-San Marcos, Houston-Galveston-Brazoria, Corpus Christi, McAllen-Edinburg-Mission, San Antonio, Texas; Lake Charles, LA) extending from the Corpus Christi, Texas area through the Lake Charles, Louisiana area; and (2) the Baton Rouge-New Orleans Origin Market, with six BEAs (Jackson, Biloxi-Gulfport-Pascagoula, Mississippi; Mobile, Alabama; New Orleans, Baton Rouge, and Lafayette, Louisiana).

Colonial states that it will face competition for the pipelineable petroleum products from other pipelines, waterborne transportation, and local consumption in its origin market. In the Western Gulf Coast origin market (Corpus Christi, TX; Houston, TX; Beaumont-Port Arthur, TX; and Lake Charles, LA areas) Colonial maintains that additional competition in origin markets will come from other pipelines that can carry refined products out of the origin market and from local consumption that can be served by truck. Colonial claims that many refineries have the alternative of waterborne shipments from their own docks generally located close to their refineries. All refineries have alternatives provided by at least two pipelines. In the Baton Rouge-New Orleans, LA origin market, the refineries can dispose of their products locally through their truck terminals. Also, waterborne shipments are an alternative for all the refineries in this origin market.

TPSI claims that Colonial conflates thirteen BEAs extending hundreds of miles from Texas to Mississippi, and then arbitrarily divides this vast geographic area into two large origin markets (Western Gulf and Baton Rouge-New Orleans origin markets). TPSI states Colonial's definition of origin markets as an amalgam of BEAs is unsupported by any evidence to demonstrate that shippers located at one end of such a large origin market could cost effectively access transportation alternatives a great distance away at the other end of the origin market. TPSI further argues that Colonial has offered no cost studies or other proof to show that it would be feasible for shippers in such vast origin

⁹Each BEA is an "Economic Area" defined by the Bureau of Economic Analysis of the U.S. Department of Commerce. These areas were redefined in 1995 to reflect more current commuting and trading patterns.

markets to move their products onto other transportation alternatives located substantial distances away. TPSI states if the Baton Rouge BEA is considered by itself, the effective capacity-based HHI is over 4200.

Conceptually, the question to ask in defining origin markets is what are the "good" economic alternatives to shippers that would be putting products on the pipeline at each of Colonial's origin terminals for shipment to destination terminals by Colonial. The focus is on good alternatives to the shipper for getting the product out of a particular location or disposing of the product elsewhere. Thus, in determining whether proposed alternatives are good alternatives in terms of price, it is the netback to the shipper (price to shipper after all costs of delivery) that should be compared in determining good alternatives for origin markets. If the netback to the shipper from using a given potential alternative is not high enough to prevent Colonial from exercising market power, that alternative is not a good alternative and should not be included in the relevant origin geographic market.

It appears that Colonial's shipment-based and capacity-based HHIs and market share results do not indicate the presence of market power in the Western Gulf Coast and Baton Rouge-New Orleans Origin Markets. On the other hand, the TPSI asserts that Colonial has improperly enlarged the market and overstated the good alternatives so that its HHIs for this market are too low. Accordingly, the Commission will direct its staff to convene a conference to explore the facts and issues regarding the Western Gulf Coast and Baton Rouge-New Orleans Origin Markets.

C. Destination Markets

Colonial claims its destination markets comprise the geographic BEA areas of Beaumont-Port Arthur, TX; Lafayette, LA; Baton Rouge-New Orleans, LA (two BEAs); and Jackson, MS. Each of these BEAs contains refineries and terminals. In establishing BEAs as the appropriate definition of its destination markets, Colonial states it considered the destination market definition used in Buckeye,¹⁰ Williams,¹¹

¹⁰Buckeye Pipeline Company, Opinion No. 360 53 FERC ¶ 61,473 (1988), order on reh'g, Opinion No. 360-A, 55 FERC ¶ 61,084 (1991).

¹¹Williams Pipeline Company, Opinion No. 391, 68 FERC ¶ 61,136 (1994), order on reh'g, Opinion No. 391-A, 71 FERC ¶ 61,291 (1995).

Longhorn,¹² and Kaneb.¹³ In particular, Colonial cites Kaneb's application for market-based rates as an example of the Commission accepting BEAs as an appropriate definition for the geographic destination markets. Colonial states the BEAs it proposes are more typical of the size as defined by the Commission in the foregoing orders. According to Colonial, the BEAs served by its pipeline are centered on substantial cities and only include the areas in the immediate vicinity of these cities. Colonial contends that its delivery locations are near the central cities of the BEAs.

Colonial cites the Commission's statement in Kaneb that all external supply sources that are within 75 miles of the BEA border are appropriate to include in the market share and market concentration analyses, in addition to the supply sources located within the BEAs' borders.¹⁴ Furthermore, Colonial argues that the Commission has found in some circumstances that external supply sources located 100 miles or more from a BEA were valid competitors within the BEA. As a result, Colonial has included external supply sources that are within 75 to 100 miles of a BEA as external suppliers to the BEA. Thus, although Colonial states its destination markets are defined as BEAs, Colonial is really defining its destination markets to include competitive alternatives outside the destination BEAs as well as within the BEAs. With two exceptions in supplemental testimony, Colonial presents no market power statistics for the BEAs only.

Colonial states that it faces competition from other inbound pipelines, refineries, and inbound waterborne shipments in each of the destination markets. In the Beaumont-Port Arthur BEA, Colonial contends that it competes with four refineries, three inbound pipelines and waterborne deliveries, and another 13 refineries in the expanded 75-mile external supply area around the Beaumont-Port Arthur BEA. In the Lafayette BEA, Colonial claims it competes with two refineries, substantial waterborne deliveries, and eleven additional refineries within the 75-mile external supply area. In the Baton Rouge-New Orleans BEA, Colonial maintains that it faces competition from ten refineries, including one that opened in 1998, waterborne deliveries, and three additional refineries in the 75-mile external supply area. Finally, Colonial asserts that it faces competition at its Jackson, MS destination BEA from four inbound pipelines, waterborne deliveries, six refineries and two terminals in the 75-mile external supply area, and six refineries in the 100-mile external supply area.

¹²Longhorn Partners Pipeline, L.P., 83 FERC ¶ 61,345 (1998).

¹³Kaneb Pipeline Company, 83 FERC ¶ 61,183 (1998).

¹⁴Id. at 61,761.

1. Market Power Measures

Colonial's first methodology¹⁵ is the delivery-based method, which represents the applicant's estimated percentage of actual deliveries to the market(s) at issue. Colonial states its delivery-based results clearly demonstrate no market power in any of the destination markets. According to Colonial, all of the Herfindahl-Hirschman indexes (HHI's) are below 1800 and its maximum market share is just over 23%. Further, in two markets, Colonial currently makes no deliveries.

Colonial's second methodology reflects an "effective capacity," which is the smaller of (1) a competitive alternative's capacity to transport or produce or (2) local consumption minus waterborne deliveries. Colonial contends that for all of its destination markets, the effective-capacity based HHIs are, at most, 2075 (Jackson BEA). For all other markets, adds Colonial, the HHIs are below 1800. In addition, Colonial states that its market share in all markets is below 23% and is less than 15% in three of the four markets. The excess capacity ratio,¹⁶ claims Colonial, is 3.9 or higher for all destination markets. Colonial avers that the foregoing statistics clearly indicate that these markets are highly competitive; therefore, Colonial could not profitably raise its rates above competitive levels.

Colonial's third methodology is the U.S. Department of Justice (DOJ) Adjusted Capacity Method. Under the DOJ Adjusted Capacity Method, it is assumed that each supplier has an equal probability of making a delivery into the market in question, regardless of the size of its pipeline or refinery. Theoretically, each supplier captures an equal share of demand. If each supplier has the capability of supplying an equal share, then each supplier will be assigned a capability to supply this amount. If all suppliers have at least an unadjusted capacity at or above whatever is required to supply an equal share, then under the DOJ Adjusted Capacity Method each supplier is assigned a capacity to supply a particular market, giving each an equal market share. Waterborne deliveries are not adjusted since it is an estimated delivery rather than a capacity figure. Colonial claims that this method yields HHIs no higher than 1147 (Jackson BEA) and market shares that do not exceed 16.2% (Jackson BEA). Furthermore, continues Colonial, the

¹⁵The HHI and market share calculations for all three methodologies employed by Colonial are predicated on the assumption that the anticipated Exxon/Mobil merger occurs, and they include 75-100 mile external suppliers.

¹⁶Excess capacity is computed by dividing the effective capacity by consumption.

lowest excess capacity ratio is 3.9, and waterborne deliveries constitute more than 10% of consumption in all four markets, which by itself should be sufficient to conclude that these markets are workably competitive.

2. Jackson Destination Market

In the Jackson and Baton Rouge destination markets, TPSI argues that Colonial has expanded the definition of its destination markets well beyond the relevant BEAs without adducing evidence to support the expansion. As with origin markets, the Commission requires applicants to justify alternatives outside the boundary of the BEA containing a delivery terminal by comparative delivered price studies showing that these external alternatives are good alternatives in terms of price:

In a market power analysis, the Commission must determine the oil pipeline's ability to exercise market power over this transportation service. However, a market power analysis in general cannot be made solely in the context of transportation rates. Where competitive alternatives constrain the applicant's ability to raise transport prices, the effect of such constraints are ultimately reflected in the price of the commodity transported. Hence, the delivered commodity price (relevant product price plus transportation charges) generally will be the relevant price to be analyzed for making a comparison of the alternatives to a pipelines' service.¹⁷

The use of delivered price studies to justify competitive alternatives external to a BEA has two benefits. First, it ensures that actual costs, rather than rules-of-thumb based on mileage, are used to reflect transportation costs. Second, it accounts for the importance of the price of the product, e.g., price of gasoline, in determining whether an external source is a good alternative. The price of the product is likely to vary depending on location. An external source may not be a good alternative because of a high product price, even though it is located very close to a BEA.

¹⁷Market-Based Ratemaking for Oil Pipelines, Order No. 572, 59 FR 59148 (Nov. 16, 1994), FERC Stats. & Regs. (Regulations Preambles, 1991-1996) ¶ 31,007 at 31,189 (Oct. 28, 1994).

In supplemental testimony, Colonial presents a cost study, attempting to justify external alternatives beyond the border of the Jackson BEA.¹⁸ This study ostensibly results in acceptable market power statistics based on Commission precedent in other cases (HHIs = 1736 and 1399; Colonial 's market share = 20.59% and 18.00% for cases where external supplies are cheaper or not more expensive than ½ cent per gallon, respectively, than internal sources; excess capacity ratios = 4.3 or higher). However, TPSI maintains that Colonial's study is flawed because (1) the trucking costs are based on information from the Williams case¹⁹ and are not accurate and (2) the price increase threshold of one half cent allowed for a good alternative is too high.²⁰

In fact, TPSI performed its own cost study, and the results show that sources outside the Jackson BEA would capture less than 4% of consumption, even if Colonial and other sources within the BEA instituted a delivered price increase equivalent to a 45% increase in Colonial's transportation rate.²¹ TPSI contends that the ability to serve only 4% or 5% of the market is not enough to justify including these external alternatives in the relevant geographic market. Similarly, the Commission finds that Colonial has not justified why an alternative that is alleged to be a good alternative only for a fringe area of the BEA is in fact a good alternative for a shipper that takes delivery of the product shipped on Colonial at the Collins and Meridian terminals, which may be some distance away from the fringe area.

¹⁸See Motion for Summary Disposition (Motion); Exhibits 18 & 19.

¹⁹Williams Pipeline Company, Opinion No. 391, 68 FERC ¶ 61,136 (1994), order on reh'g, Opinion No. 391-A, 71 FERC ¶ 61,291 (1995).

²⁰In demonstrating good alternatives in terms of price, the Commission typically requires that the alternatives be no higher than some threshold price, which is a given amount above the competitive or some other appropriate base price. The increase in price above the base price is the price increase threshold. For example, in Buckeye the Commission stated that the price increase threshold was a 15% increase in the delivered price of the product. Buckeye Pipeline Company, Opinion No. 360, 53 FERC ¶ 61,473 at 62,666 (1988) .

²¹Jones Rebuttal Testimony at 11-14.

Colonial presents capacity-based market power statistics in Exhibit 20 of the supplemental testimony of Dr. George Schink for sources located in the Jackson BEA alone.²² The effective capacity HHI is 2347, Colonial's market share is 24.23% and the excess capacity ratio is 3.7.²³ If valid, these market power statistics may be acceptable based on Commission precedent in other cases.²⁴ TPSI does not criticize this study, except to say that the HHI is higher than the 1800 HHI standard put forth in the DOJ Merger Guidelines.

Colonial also contends that it lacks market power because waterborne movements through the Vicksburg terminal account for over 11% of the demand in the market.²⁵ However, TPSI challenges this assertion based on Dr. Jones' (TPSI's witness) testimony that (1) a substantial share of barrels arriving at Vicksburg leave the Jackson BEA for other markets, rather than being consumed there and (2) expansion of capacity at Vicksburg may be costly, meaning that expanded shipments through Vicksburg may not be a good alternative to Colonial in terms of price in the future.²⁶

²²Motion, Exhibit 20.

²³Id.

²⁴ See Buckeye Pipeline Company, Opinion No. 360, 53 FERC ¶ 61,473 (1988), order on reh'g, Opinion No. 360-A, 55 FERC ¶ 61,084 (1991).

²⁵In Williams, the Commission found that lack of market power existed in one market where waterborne capacity was expandable and waterborne movements accounted for 10% or more of the demand in the market. In such a case, it might be argued that expanded waterborne shipments could defeat any attempt by the pipeline to exercise market power. Williams Pipeline Co., 58 FERC ¶ 63,004 at 65,014 (1992).

²⁶Transmontaigne Protest (Protest); Dr. Jones Testimony at 22-26.

TPSI states there are four petroleum facilities at Vicksburg, but only one facility handles the pipelineable refined petroleum products at issue.²⁷ That facility, operated by Citgo Petroleum (Citgo), has nine storage tanks with an approximate capacity of 180,000 barrels, and a three-bay truck loading rack.²⁸ The Citgo facility has a maximum throughput capacity of approximately 15 kBD. In order to increase its capacity above 15 kBD, TPSI contends that the Citgo facility would have to add additional storage tanks, as well as additional loading bays.²⁹ However, TPSI states that there is no room at the Citgo facility to add additional storage tanks or loading bays, and the Citgo facility is locked in by businesses on both sides. Accordingly, TPSI claims that Citgo would have to either build a new facility or buy out its neighbors to expand its capacity to handle any substantial additional volume of refined petroleum products. The cost of building a new facility capable of handling up to 15 kBD of gasoline, diesel fuel, and jet fuel, would be approximately \$5-7 million.³⁰

TPSI also argues that Vicksburg is a high cost supplier of refined product within the Jackson BEA. TPSI maintains that the posted product price for gasoline at the Vicksburg facility is currently 1.28 and 1.47-cents per gallon higher than the comparable posted price at Meridian and Collins.³¹ Thus, TPSI posits that the Vicksburg facility cannot compete with Colonial in the major population centers of the Jackson BEA. The facility can economically serve less than 5% of the consumption of the Jackson BEA. TPSI asserts the substantial costs associated with expanding Vicksburg's capacity would only increase the cost disadvantage the Vicksburg facility suffers relative to Colonial, making it even less competitive.

²⁷Reply of Transmontaigne to Motion for Summary Disposition (Reply) at 20.

²⁸Id.

²⁹Id.

³⁰Id. at 21.

³¹Id. at 22.

Notwithstanding the arguments raised by TPSI, in light of the additional information provided by Colonial in Exhibit 20 of its supplemental testimony by Dr. George Schink, the Commission finds that Colonial has demonstrated that it lacks market power for deliveries at Collins and Meridian, MS. This is Colonial's sole exhibit presenting potential competitive alternatives located only within the Jackson BEA, and this exhibit was not directly challenged by TPSI. Nevertheless, to be conservative in our analysis, the Commission has modified the exhibit by eliminating waterborne sources of supply as competitive alternatives because of general concerns expressed by TPSI about Colonial's use of waterborne statistics.³² As a result, Colonial's market share is 25%, and the effective capacity and adjusted capacity HHIs are 2500. Based on market power statistics in destination markets in other cases where the Commission has found lack of market power, the Commission believes its conservative modification of Colonial's statistics, based on the Jackson BEA alone, merits a lack of market power finding.

3. Baton Rouge-New Orleans Destination Market

TPSI also raises several valid concerns regarding Colonial's definition of its Baton Rouge-New Orleans destination market. TPSI criticizes Colonial for combining the Baton Rouge and New Orleans BEAs into one large destination market, and then making it even larger by including external supply sources from truck radii of 75 and 100 miles. Colonial proffers the following as justification for conflating the two BEAs: the close proximity of the central cities of the two BEAs (approximately 82 road miles apart); all the refineries in the two BEAs are located on the Mississippi River and have active barge docks that allow all of these refineries to supply locations throughout the two BEAs; pipelines link four of the eight refineries in the New Orleans BEA to the city of Baton Rouge; and all ten of the refineries in the two BEAs are located within 100 road miles of the cities of Baton Rouge and New Orleans. TPSI states if the Baton Rouge BEA was considered a destination market by itself, it calculates an effective capacity HHI of 3051 and market share of 33%, compared to less than 1200 and 14% respectively for the combined BEAs.

TPSI performed a "small but significant and nontransitory increase in price" (SSNIP) test that demonstrated supply alternatives in the New Orleans BEA could not

³²These concerns as related to Vicksburg are discussed above. Also, TPSI is critical of Colonial's assumption in calculating capacity-based market power statistics that local consumption is first served by waterborne alternatives, with the remainder assigned to other alternatives.

effectively compete with Colonial's pipeline in the Baton Rouge BEA. The results of the study are shown in the following three tables:

I. Delivered product costs

| | Baton Rouge | Convent/Garyville | New Orleans |
|------------------------------|--------------|-------------------|--------------|
| OPIS posted price | 42.47 | 42.86 | 42.63 |
| Truck freight to Baton Rouge | 0.00 | 1.85 | 2.35 |
| Laid in price at Baton Rouge | 42.47 | 44.71 | 44.98 |

II. Delivered product costs following a 15% Colonial tariff increase

| | Baton Rouge | Convent/Garyville | New Orleans |
|---------------------------------|---------------|-------------------|---------------|
| OPIS posted price (Adjusted) | 42.59 0.00 | 42.86 1.85 | 42.63 2.35 |
| Truck freight to Baton Rouge | | | |
| Laid in price at Baton Rouge | 42.59 | 44.71 | 44.98 |

III. Delivered products costs following a .5 cent/gallon Colonial tariff increase³³

| | Baton Rouge | Convent/Garyville | New Orleans |
|---------------------------------|---------------|-------------------|---------------|
| OPIS posted price (Adjusted) | 42.97 0.00 | 42.86 1.85 | 42.63 2.35 |

³³Posted prices and truck freights in cents/gallon. OPIS reports Convent, LA and Garyville, LA as a single price. Trucking rates differ. A simple average was calculated to create a single trucking rate.

| | | | |
|------------------------------|--------------|--------------|--------------|
| Truck freight to Baton Rouge | | | |
| Laid in price at Baton Rouge | 42.97 | 44.71 | 44.98 |

The tables above give the delivered cost of shipping product to Baton Rouge by tank truck from Garyville and Convent, LA (the two refineries that have the closest refinery truck racks to Baton Rouge) and terminals near the city of New Orleans. A comparison of the laid-in cost of product trucked from these origin points with the posted price in Baton Rouge indicates that product cannot be economically trucked from the New Orleans BEA into Baton Rouge. This is evident when one compares the laid-in price with the posted price from the analysis of the above tables. TPSI states that Garyville, Convent and New Orleans still cannot economically serve Baton Rouge, even when a 15% SSNIP is added to the Colonial tariff in Baton Rouge. The SSNIP test is repeated using Colonial's 0.5 cent per gallon differential in place of a SSNIP equal to 15% of Colonial's tariff. TPSI finds that even using Colonial's larger price differential, product trucked in from the New Orleans BEA cannot compete effectively in the Baton Rouge BEA.

Colonial did not present any market power statistics related to the Baton Rouge BEA, alone, in its original application. However, in Colonial's Motion for Summary Disposition, Colonial presents supplemental testimony with capacity-based market power statistics for sources located only in the Baton Rouge BEA, as well as statistics including external sources located within 75 and 100 miles of the BEA. Colonial does not make deliveries to its Baton Rouge terminal, so no delivery statistics were presented.

Colonial states that when only intra-BEA sources are included, the effective capacity-based HHI for the Baton Rouge BEA destination market is 1,022 (including waterborne receipts and inbound pipelines) and Colonial's capacity-based market share is 14.3%. The adjusted capacity-based HHI is 223 and the excess capacity ratio is 2.3. Colonial argues the low HHI results produced do not even provide a complete picture of the competitive situation within the Baton Rouge BEA because these calculations exclude inbound truck movements from the refineries in the New Orleans BEA and from refineries in the area to the west of the Baton Rouge BEA.

In Colonial's analysis using a 75-mile trucking radius for external suppliers, the effective capacity-based market share is 7.8%, the effective capacity-based HHI is 616, the DOJ-adjusted capacity HHI is 93, and the excess capacity ratio is 4.3. When a 100-mile trucking radius is used for external supply sources, Colonial's effective

capacity-based market share is 7.4%, the effective capacity-based HHI is 616, the DOJ adjusted-capacity HHI is 93, and the excess capacity ratio is 4.5. These calculations are performed assuming that the Exxon-Mobil merger occurs. Colonial concludes that these statistical results clearly demonstrate that the Baton Rouge BEA destination market is highly competitive.

However, there may be some question about the accuracy of Colonial's waterborne capacity used in developing the above-mentioned market power statistics related to the Baton Rouge BEA. Although addressing a somewhat different issue, TPSI, in the supplemental testimony of Mark Huff, questions whether all of the barge capacity is appropriately assigned to refined products (the relevant product in this case) versus other products such as blend or feedstock products used by refineries and petrochemical companies in producing other products.³⁴

³⁴Reply, Mark Huff Testimony at 6-7.

In this case, there have been significant protests to Colonial including alternative supply sources located outside of single BEAs. The Commission believes that if Colonial wants to use relevant markets containing alternatives external to a BEA, Colonial must demonstrate that the external sources are indeed good alternatives based on cost studies. In Order No. 572, the Commission clearly stated that market-based rate applicants must include pertinent data about transportation alternatives and other competitive alternatives.³⁵ For example, the oil pipeline would have to include data similar to that provided for its own facilities and services, including cost and mileage data in specific reference to the oil pipeline's terminals and major consuming markets.³⁶ The burden is on the pipeline to justify its inclusion of transportation alternatives and other competition in its market analysis. Moreover, as has already been stated, adopting some standard radius (e.g., 75 miles) for accepting external sources as good alternatives completely disregards the importance of the price of the product (e.g., price of gasoline) in determining whether an external source is good alternative.

Notwithstanding TPSI's protests, the Commission finds that the data in Exhibit 7 of Colonial's supplemental testimony by George Schink does demonstrate that Colonial lacks significant market power for deliveries at Baton Rouge, LA. This is Colonial's sole exhibit presenting potential competitive alternatives located only within the Baton Rouge BEA, and this exhibit was not directly challenged by TPSI. Nevertheless, to be conservative, the Commission modified the exhibit by eliminating waterborne sources of supply as competitive alternatives because of general concerns expressed by TPSI about Colonial's use of waterborne statistics.³⁷ As a result of the foregoing modification, Colonial's market share is 20.52 %; the effective capacity HHI is 2006; and the DOJ adjusted capacity HHI is 2000. Based on market power statistics in destination markets

³⁵Market-Based Ratemaking for Oil Pipelines, Order No. 572, 59 FR 59148 (Nov. 16, 1994), FERC Stats. & Regs. (Regulations Preambles, 1991-1996) ¶ 31,007 at 31,191 (Oct. 28, 1994).

³⁶Id.

³⁷TPSI criticizes Colonial's waterborne data for the Baton Rouge/New Orleans market, and some of these concerns may raise questions about the accuracy of the waterborne data for the Baton Rouge BEA only. Also, TPSI is critical of Colonial's assumption in calculating capacity-based market power statistics that local consumption is first served by waterborne alternatives, with the remainder assigned to other alternatives.

in other cases where the Commission has found a lack of significant market power, the Commission believes its conservative modification of Colonial's statistics, based on the Baton Rouge BEA alone, supports a finding of lack of market power.

4. Uncontested Markets

TPSI did not protest the Beaumont-Port Arthur, TX and Lafayette, LA destination markets. However, in its reply to Colonial's motion of summary disposition, Chevron suggests that shippers should have the opportunity to challenge Colonial's claim of effective competition in certain origin and destination markets in Texas, Louisiana, and Mississippi. No substantive protests have been filed alleging that Colonial has market power in these destination markets.

Chevron challenges Colonial's definition of separate origin and destination markets by contending that the application lacks evidence of the cost of transportation alternatives in the discrete corridor between origins and destinations. However, the Commission rejected the corridor approach in Williams.³⁸ By rejecting the corridor approach, the Commission recognized that if geographic markets were limited to specific origin/destination pairs, this would fail to recognize the economic concerns of the shippers as well as eliminate from consideration competitive suppliers who bring product into the markets without utilizing the specific corridors.

After analyzing Colonial's application for market-based rates, the Commission concludes that the Lafayette, LA and the Beaumont-Port Arthur, TX destination markets are not at issue. In addition, while the Baton Rouge-New Orleans, LA and Jackson, MS destination markets were heavily contested, the Commission concludes that Colonial lacks significant market power in these markets. Colonial will be permitted to implement market-based rates in the uncontested destination markets as well as the destination markets where the Commission found it lacked market power

The Commission orders:

(A) Colonial's application for a market power determination is granted to the extent discussed in the body of this order. Colonial may file to implement market based

³⁸Williams Pipeline Company, 68 FERC ¶ 61,136, at 61,660-61 (1994).

rates in the Beaumont-Port Arthur, Texas, Jackson, Mississippi, and Lafayette and Baton Rouge-New Orleans destination markets.

(B) The Commission's staff is directed to convene a conference to explore the facts and issues regarding the Western Gulf Coast and Baton Rouge-New Orleans origin markets and to report the results of the conference to the Commission.

By the Commission.

(S E A L)

David P. Boergers,
Secretary.