



*AOPL Business Conference
Newport Beach, California
September 18, 2013*

STRATEGY ROUNDTABLE SESSION

Topic 1
EVOLVING USE of CAOs

Corrective Action Orders (CAOs) are PHMSA's strongest enforcement tool, usually associated with the shutdown of a pipeline facility. PHMSA's use of CAOs is on the rise. Since these are most often issued as unilateral orders (meaning that you have to comply with them before you can contest them), the stakes are often high.

We are seeing certain issues reappearing in recent CAOs, and it is in your best interests to be aware of these issues, as well as your options for response.

DISCUSSION BY PANELISTS BOB HOGFOSS AND CATHERINE LITTLE:

CAOs are provided for in the Pipeline Safety Act; they are a creation of Congress, not PHMSA (although the Agency has promulgated rules to implement the statutory requirements). 49 U.S.C. Section 60112. These tools used to be called 'Hazardous Facility Orders' or HFOs, but PHMSA was persuaded to change the name because of the stigma associated with the term 'hazardous facility.' Unfortunately, before issuing a CAO, PHMSA must make a finding that "a particular pipeline facility is hazardous to life, property or the environment" and that continued operation without immediate corrective action "would result in the likelihood of serious harm." See 49 C.F.R. Part 190.233. The 'hazardous facility' language is in both the statute and the regulations, even if the actions are now called 'CAOs' instead. Although PHMSA can allow for an administrative hearing before issuing a CAO, they are almost always issued on an "emergency" basis, where you must immediately comply before having an opportunity to request a hearing. The government increasingly issues CAOs after virtually all 'significant' incidents associated with reportable releases of oil (not to be confused with

PHMSA's broader 'significant' incident data tracking and trending). There is no definition of 'significant,' though, and it often turns on how much attention the incident has received in the press. Because of the unfortunate 'hazardous facility' language, CAOs are often viewed with concern by local communities, the media and investors. The Agency was persuaded to utilize an alternative "Safety Order" enforcement tool authorized under the Pipeline Safety Act (49 U.S.C. 60117(l)) several years back, but CAOs continue to be the enforcement tool of choice.

Among the issues we have encountered with CAOs recently is that because the Order usually issues within days of an incident, it often contains significant mistakes of fact, and erroneous conclusions about causation. The incorrect information then finds its way into the media and third party litigation, before a company even has a chance to correct even obvious errors. It can require months if not years to correct those statements that were incorrect when made.

Another significant concern about PHMSA's recent use of CAOs is that by the time the Agency has an opportunity to review the cause and impact of an incident, it may realize that the event really did not pose a significant threat sufficient to warrant a 'hazardous facility' finding. This is illustrated by a number of recent incidents where CAOs were issued, but the pipeline was approved for restart almost immediately. It defies common sense how PHMSA can approve a pipeline for restart while at the same issue an order declaring that "continued operation without corrective action makes the pipeline hazardous to life, property or the environment." Operators are increasingly faced with the difficult choice of challenging a CAO finding in light of the Agency's restart approval, or risk not getting a prompt restart approval the next time an incident occurs.

The typical corrective action required in recent years—even after restart is approved – is also troubling. In the past few years the Agency has been requiring that a pipeline subject to a CAO conduct both an inline inspection (ILI) and a hydrotest of the affected segment. The "affected segment" is often very broadly defined (we have seen examples where the corrective action gets applied to adjacent or even lines with similar characteristics across the system). The requirement to conduct both an ILI and a hydrotest is often an unnecessary 'boot and suspenders' approach, at least without a full understanding of causation.

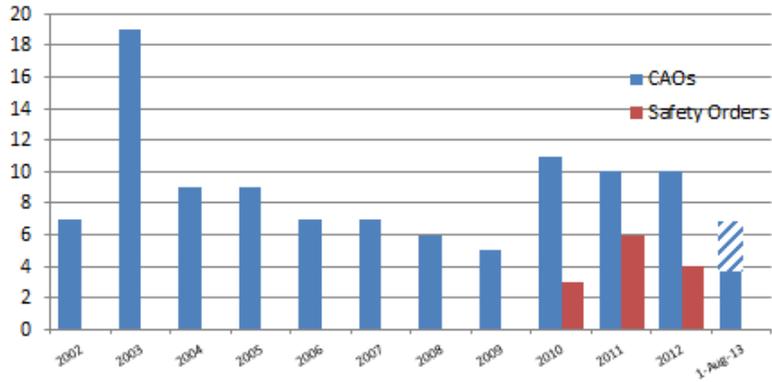
PHMSA is also increasingly requiring operators to include an independent entity in its Root Cause Failure Analysis (RCFA) deliberations. The concern there is that once a third party is included, it is extremely difficult to protect good faith internal

discussions and deliberations through attorney-client or work product privileges. This can have a significant impact on third party litigation.

So what are your response options to these various issues? First, you should consider requesting a hearing, if only to try to correct the record for purposes of addressing any media or third party litigation interest (although PHMSA takes the position that the only issue to be addressed in a Hearing is whether or not a “hazardous finding” was appropriate, typically other issues are also addressed). Second, you should consider objecting to the inclusion of a third party in your RCFA, or at least structure the involvement in a manner that allows you to preserve privilege to the fullest extent possible (remember that facts are never privileged, but discussions about cause and options for response can be). Third, you should press PHMSA (either informally or in a hearing) to allow the RCFA and causation analysis to be completed before determining the required corrective actions, including in particular whether both an ILI and hydrotest (or either) are required.

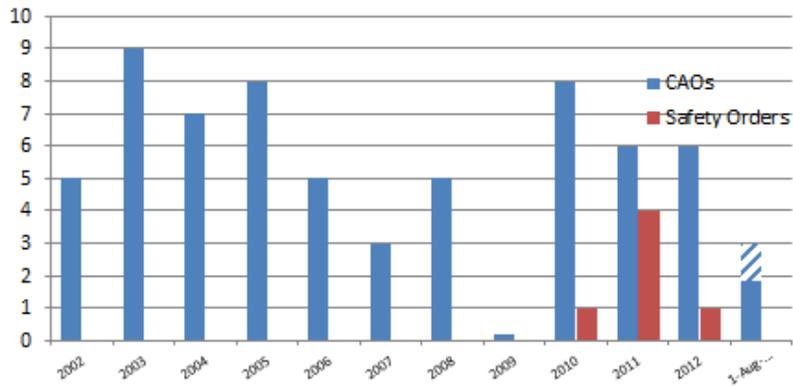
Finally, be aware that whether you request a hearing on a CAO or not, if the Agency directs you to take additional corrective actions not included in the CAO as issued (or expands the scope of the CAO), that action provides you with a new opportunity to request a hearing, and you should.

All Safety Orders and CAOs Initiated 2002 - 2013



Source: PHMSA Safety Monitoring & Reporting Tool for the Pipeline Safety Enforcement Tracking System, August 1, 2013

Safety Orders and CAOs Initiated: Liquid Only 2002 - 2013



Source: PHMSA Safety Monitoring & Reporting Tool for the Pipeline Safety Enforcement Tracking System, August 1, 2013

DISCUSSION TOPICS WITH AUDIENCE

1. Experiences with hearings in response to CAOs.
2. Process of obtaining closure of old HFO or CAO when all actions are complete.
3. Corrective actions typically required by PHMSA in CAOs.
4. PHMSA's requests to involve third parties in root cause analyses.
5. Responsiveness of PHMSA to concerns about privilege and root cause investigations.
6. Claiming privilege over root cause investigation if a third party is involved.

For more information on these topics and the discussion that occurred at the session, feel free to contact
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