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October 14, 2022

Via Electronic Mail

Mr. Bryan J. Lethcoe
Director, Southwest Region
Office of Pipeline Safety
Pipeline and Hazardous Materials Safety Administration
U.S. Department of Transportation
8701 S. Gessner, Suite 630
Houston, TX 77074

Re: Phillips 66 Pipeline LLC
Notice of Probable Violation and Proposed Civil Penalty, CPF 4-2022-006-NOPV
Request for Settlement Conference and Hearing

Dear Mr. Lethcoe:

Phillips 66 Pipeline LLC (Phillips 66 or the Company) received the above-referenced Notice of Probable Violation (NOPV) and Proposed Civil Penalty issued by the Pipeline and Hazardous Materials Safety Administration (PHMSA or the Agency) on September 16, 2022. The NOPV sets forth three (3) probable violations of the federal pipeline safety regulations, including two (2) allegations with associated proposed civil penalties (totaling \$552,800) and one (1) warning item. With this letter, Phillips 66 respectfully requests the opportunity for an informal settlement meeting with PHMSA in order to attempt to reach an agreement outside of a hearing. In the event the parties are unable to resolve the issues and in order to preserve the Company's rights, Phillips 66 is timely filing the attached request for hearing, written response, and statement of issues, pursuant to 49 C.F.R. §§ 190.208 and 190.211.

The two (2) NOPV items associated with civil penalties (Items 1 and 2) relate to a release of 6.50 barrels of crude oil involving Breakout Tank #1401 at the Helena Terminal in Karnes County, Texas. After discovering the release, the Company timely reported it to the National Response Center (NRC) and initiated its own investigation to determine the cause of the failure. The two (2) NOPV allegations (Items 1 and 2) associated with civil penalties arise out of that investigation. The remaining warning item (Item 3) relates to an alleged violation associated with hydrostatic testing of tanks at facilities located in Wink and Crane, Texas and is not related to or associated with the release at the Helena Terminal.

The Company is contesting the allegations in the NOPV and the associated civil penalties. Phillips 66 believes that the allegations under NOPV Item 1 and 2 are duplicative and that the warning item is based on a misapplication of the facts and law. The Company requests that PHMSA withdraw the allegations. In the alternative, Phillips 66 requests that PHMSA adjust the associated civil penalties for NOPV Items 1 and 2 to more accurately reflect the statutory and regulatory penalty assessment criteria required under 49 U.S.C. § 60122(b) and 49 C.F.R. § 190.225.

Because Phillips 66 believes that these issues can be resolved without resort to a hearing, the Company respectfully requests an informal settlement conference to more fully discuss the allegations and the proposed civil penalties. While the Company is confident that these issues can be resolved informally, Phillips 66 is also requesting a hearing to preserve its rights and asks that a hearing be postponed in order to allow the parties a meaningful opportunity to convene a settlement meeting(s). To the extent the parties proceed to a hearing, Phillips 66 expects to be represented by outside counsel.

I. Background

Phillips 66 owns and/or operates a network of more than 22,000 miles of pipeline and dozens of storage terminals throughout the United States. The Company is committed to pipeline safety and operating its system and assets in accordance with the federal pipeline safety regulations and within a robust safety management system that conforms to API RP 1173. As evidence of its commitment, the Company was recently recognized by its peers for the second year in a row as a winner of the 2021 API Distinguished Pipeline Safety Award for its “deep commitment” to pipeline safety and “making zero incidents a reality.”¹

The tank at issue with respect to NOPV Items 1 and 2, Breakout Tank #1401, is located at the Helena Terminal in Karnes County, Texas. Breakout Tank #1401 and the Helena Terminal are a part of the Gray Oak Pipeline system, a crude oil system of over 800 miles of pipe and associated terminals and facilities, which is owned by Gray Oak Holdings, LLC, a joint venture entity. Phillips 66 is the operator of the Gray Oak Pipeline system through a contractual relationship with Gray Oak Holdings, LLC.

On March 10, 2020, Phillips 66 discovered a release of 6.50 barrels of crude oil at the Gray Oak Helena Terminal in Karnes County, Texas. The release was fully contained within the facility’s property and did not result in any injury, fatality or impacts outside of the facility. The Company determined that the release was associated with Breakout Tank #1401, a newly constructed tank that was put into service just four (4) days prior to the discovery. The Company properly notified the NRC of the release in a timely manner as required by 49 C.F.R. § 195.52 and began to remove product from the tank.

¹ American Petroleum Institute, “BP, Colonial and Phillips 66 Win 2021 API Distinguished Pipeline Safety Awards” (May 3, 2022), available at <https://www.api.org/news-policy-and-issues/news/2022/05/03/2021-api-distinguished-pipeline-safety-awards>.

Phillips 66 also initiated its own investigation to identify the cause of the release. The Company completed a root cause analysis (RCA) on April 8, 2020 and determined that the release was caused by “pin holes in tank bottom caused by lack of proper weld clean up per API 650.” The Company further determined that welders contracted to construct Breakout Tank #1401 failed to properly comply with Phillips 66 procedures and the requirements of API Standard 651, despite providing inspection records verifying their compliance with the requirements. As a lesson learned and to ensure that future breakout tanks are properly constructed as required by the Company’s procedures and API Standard 650, the RCA indicated that the Company would require 100% third party inspections of all first pass welds during new breakout tank construction. Phillips 66 provided a copy of the RCA to PHMSA on April 14, 2020.

In addition to the RCA, PHMSA requested additional documentation, which was provided by the Company. To Phillips 66’s knowledge, the investigation related to the release and NOPV Items 1 and 2 was limited to the review of documentation provided by the Company and there were no physical inspections of Breakout Tank #1401 or the Helena Terminal. PHMSA’s inspection lasted from March 11, 2020 through June 4, 2021 and resulted in the issuance of the above-referenced NOPV, which is based, in large part, on the RCA submitted by Phillips 66.

With respect to Item 3, it is unclear when PHMSA identified the alleged warning item. The allegation relates to failure to hydrostatically test breakout tanks at terminals unrelated to the Helena Terminal or the release at issue in NOPV Items 1 and 2. PHMSA conducted separate construction inspections of the terminals located in Wink and Crane, Texas. At the conclusion of those construction inspections, however, PHMSA indicated that there were no findings of violations associated with the Gray Oak Pipeline system.

II. Written Responses to NOPV Allegations

A. Item 1 – 49 C.F.R. § 195.202 (Proposed Civil Penalty - \$276,400)

1. PHMSA Allegation

§ 195.202 Compliance with specifications or standards

Each pipeline system must be constructed in accordance with comprehensive written specifications or standards that are consistent with the requirements of this part.

Phillips 66 failed to construct Breakout Tank #1401 in Karnes County, Texas, in accordance with comprehensive written specifications as required by § 195.202. Specifically, Phillips 66 failed to follow its own procedure, Aboveground Atmospheric Storage Tank (P66 MEP 4510, Rev. 1, 10/26/2017) and the written procedure of manufacturer of the tank, Smith Tank & Steel Inc., NDE Procedure, Vacuum Testing Procedure (STS-VBT-001), Section 5.0 Surface Preparation as required by API Std 650.

On March 10, 2020, Phillips 66 notified the National Response Center of a leak from the newly constructed and recently commissioned breakout tank. This failure resulted in the unintentional release of 6.50 barrels of crude oil. A post-accident investigation by Phillips 66 determined that weld defects on the bottom of the tank that had not been detected by the required testing and examinations caused the accident. The visual examination and vacuum box testing performed during the failure investigation revealed 28 indications with 17 confirmed indications that required repairs. Phillips 66 failed to properly remove weld slag, debris and conduct visual inspections before pre-commissioning vacuum box testing. These failures masked the defects that resulted in the release and were causal to the reported accident.

In addition, Phillips 66 failed to construct Breakout Tank #1401 in accordance with § 195.132(a)(3). This regulation states that storage tanks must be designed and constructed in accordance with API Std 650. Section 6.6 of API Std 650 states that “[v]acuum testing shall be performed in accordance with a written procedure prepared by the manufacturer of the tank.” Phillips 66 used the procedures of Smith Tank & Steel, Inc. but failed to follow section 5.2 which states that “[w]elds shall be clean and free of slag and loose debris.”

Therefore, Phillips 66 failed to construct Breakout Tank #1401 in accordance with its comprehensive written specifications as required by §§ 195.202 and 195.132(a)(3).

2. Phillips 66 Response

Phillips 66 contests NOPV Item 1 as characterized by PHMSA and the associated proposed civil penalty. The Company’s RCA confirms that the release was caused by improper welding practices performed by a contractor. The Company, however, takes exception to the NOPV’s implication that it disregarded its procedural processes and the applicable regulatory requirements. To the contrary, Phillips 66 made a good faith effort to comply with its procedures and the applicable regulatory requirements; rather, the construction issues associated with Tank #1401 are more appropriately characterized as a contractor workmanship issue.

Pursuant to 49 C.F.R. §§ 195.202; 195.313, the Company requires breakout tanks to be constructed in accordance with its Aboveground Atmospheric Storage Tank (P66 MEP 4510, Rev. 1, 10/26/2017) procedure and API Standard 650, which include requirements for cleaning welds and inspecting welds for defects. When constructing Breakout Tank #1401, Phillips 66 hired a properly qualified contractor, who failed to adequately clean a portion of the welds in the tank bottom as required by the Company’s procedures. Subsequently, the contractor inspected the welds, but failed to identify any defects. The contractor provided records documenting these inspections. In good faith, Phillips 66 relied on these inspection records and did not otherwise have cause to believe that there were any weld defects on the tank bottom until discovering the release. Moreover, the tank passed a successful vacuum box floor inspection and hydrostatic test before the coating was installed and before being placed into service. As part of the surface preparation process to install floor coating, the tank floor was blasted in preparation for coating. During the blasting process weld flux covering the pin holes was removed exposing the pin holes

prior to coating activities. Records of these inspections were provided to PHMSA on March 3, 2020.

Given the nature of the release and alleged violation at issue, PHMSA’s proposed civil penalty fails to accurately reflect the statutory and regulatory penalty assessment criteria required by 49 U.S.C. § 60122(b) and 49 C.F.R. § 190.225. Most notably, the proposed penalty fails to account for the nature of the release, including that there was no impact to the public. When calculating the proposed civil penalty, PHMSA misapplied the factors for circumstances, history of prior offenses, good faith, duration, and other factors as justice may require. *Id.* Further, this alleged violation is disproportionately high as compared to similar enforcement actions. *See PHMSA Pipeline Safety Enforcement Procedures*, Sec. 3, Selection of Administrative Enforcement Actions at 1 (Sep. 15, 2020) (providing that the purpose of the enforcement manual is to “improve PHMSA’s consistency in implementing the pipeline enforcement program” and to ensure that the Agency applies the enforcement tools at its disposal “as consistently as possible”). As a result, Phillips 66 requests that the Agency reduce the proposed civil penalty.

For the reasons set forth above, Phillips 66 requests that PHMSA withdraw Item 1 of the NOPV or, in the alternative, substantially reduce the associated civil penalty.

B. Item 2 – 49 C.F.R. § 195.581(a) (Proposed Civil Penalty - \$276,400)

1. PHMSA Allegation

§ 195.579 What must I do to mitigate internal corrosion?

(d) Breakout tanks. After October 2, 2000, when you install a tank bottom lining in an aboveground breakout tank built to API Spec 12F (incorporated by reference, see § 195.3, API Std620 (incorporated by reference, see § 195.3), API Std 650 (incorporated by reference, see § 195.3), or API Std650’s predecessor, Standard 12C, you must install the lining in accordance with API RP 652 (incorporated by reference, see § 195.3). However, you don’t need to comply with API RP 652 when installing any tank for which you note in the corrosion control procedures established under § 195.402(c)(3) why compliance with all or certain provisions of API RP 652 is not necessary for the safety of the tank.

Phillips 66 failed to install the tank bottom lining in Breakout Tank #1401 in accordance with API RP 652 as required by § 195.579(d) and its written procedures. Specifically, Phillips 66 failed to conduct adequate surface preparation, improperly applied the tank bottom epoxy liner, failed to properly visually inspect the epoxy liner for holidays after installation, and failed to repair the defects in the epoxy liner.

The failure investigation determined that the bottom lining had been installed over bottom plate welds that did not have slag and debris removed, there were visible defects in the lining that were

not repaired, and that the lining was damaged during installation. The failure investigation also determined that there were pinholes through the welds.

Section 7 of API RP 652 requires adequate surface preparation prior to installation of tank bottom liners. Section 9 of API RP 652 requires inspections during all phases of lining installation to ensure proper installation. In addition, Phillips 66's written procedures, Application of Internal Coating on Storage Tanks and Vessels specification (P66-MEP-5070, Rev 1, Effective Date 2017-11-14) sections 8.4 and 9.9 include specific surface preparation, application, visual inspection, and coating holiday inspection requirements.² Sections 12.8 and 13.2 contain specific requirements to visually inspect the liner after curing and to repair any defects.³ Phillips 66 failed to follow all of the above listed requirements. Phillips 66 failed to adequately prep the surface by removing slag and debris, failed to inspect the liner during all phases of installation, and failed to repair visible defects in the liner.

After the release, the tank was taken out of service, cleaned, and photographed. Photographs showed pores in the tank bottom epoxy lining where it was applied over welds containing irregularities, weld slag, and debris. The photographs also indicated that the welds were not ground smooth and rounded according to the section 8.4 of Phillips 66's procedure. Despite applying the epoxy lining over the entire welded steel tank bottom, post-accident testing determined the welds contained pinholes that, along with visible defects in the tank bottom epoxy lining, allowed the tank to leak. Phillips 66's failure to follow API RP 652 and its procedures was causal to the accident.

Post-accident photos also showed footprints on the tank bottom prior to the epoxy being cured, resulting in coating defects (holidays) that compromised the coatings effectiveness. This photographic evidence indicates that Phillip 66 failed to adequately inspect the liner after installation and repair defects in the liner according to sections 12.8 and 13.2 of its procedures.

Therefore, Phillips 66 failed to construct Breakout Tank #1401 in accordance with § 195.579(d) and its written procedures.

2. Phillips 66 Response

Phillips 66 is contesting NOPV Item 2 because it is duplicative of NOPV Item 1. As such, PHMSA must withdraw the underlying violation. Although NOPV Item 2 alleges that Phillips 66 failed to properly "install the tank bottom lining in Breakout Tank #1401," the basis for the allegation originates from the same set of facts at issue in NOPV Item 1, poor workmanship and a failure to remove all slag and debris and to properly inspect welds. *See Blockburger v. United States*, 284 U.S. 299, 304 (1932) ("requires a determination of whether there are two offenses or only one"); *In re Colo. Interstate Gas*, Final Order, CPF No. 5-2008-1005, 2009 WL 5538649, at **11-13 (D.O.T Nov. 23, 2009) ("The relevant test is to determine whether the multiple alleged violations "each require proof of any additional fact or have their own 'evidentiary basis.'"). The very purpose of the internal coating under 49 C.F.R. § 195.579(d) is to protect against corrosion, which

was not a factor in this incident. Coating imperfections identified in the investigation following the release were a workmanship issue and were a concern for long-term corrosion protection, and not causal to this incident.

In the event that PHMSA does not withdraw the underlying violation, the associated civil penalty should be significantly reduced to more properly reflect the statutory and regulatory penalty assessment criteria and account for the factors related to (1) gravity, (2) history of prior offenses, (3) good faith, (4) duration, and (5) other matters as justice may require. The Company requests that PHMSA consider the duplicative nature of this violation when compared to NOPV Item 1. As currently structured, Phillips 66 is being unfairly heavily penalized twice for the same contractor workmanship issue.

For the reasons set forth above, Phillips 66 requests that PHMSA withdraw Item 2 of the NOPV or, in the alternative, substantially reduce the associated civil penalty.

C. Warning Item 3 – 49 C.F.R. § 195.307(c)

1. PHMSA Allegation

§ 195.307 Pressure testing aboveground breakout tanks.

(c) For aboveground breakout tanks built to API Std 650 (incorporated by reference, see § 195.3) and first placed in service after October 2, 2000, testing must be in accordance with sections 7.3.5 and 7.3.6 of API Standard 650 (incorporated by reference, see § 195.3).

§ 195.202 Compliance with specifications or standards

Each pipeline system must be constructed in accordance with comprehensive written specifications or standards that are consistent with the requirements of this part.

Phillips 66 failed to perform a hydrostatic test in accordance with its written procedures and API Standard 650 as required by § 195.307(c) for its breakout tanks at the Wink and Crane, Texas terminals. Specifically, Phillips 66 failed to receive proper approval for deviation from hydrostatic testing because practical access to water was available.

API Standard 650, Section 7.3.5 (2) provides for an exemption of hydrostatic testing if there is a lack of sufficient water to fill the tank for hydrostatic testing. Phillip 66's written procedure Hydrostatic Testing - Atmospheric Storage Tanks (P66-MPR-6202, Rev 5, Effective Date 2017-10-24 provides for hydrostatic testing and the requirements for approval of exemptions from testing, as permitted by API Standard 650. Specifically, section 9.1.1.2 of Phillips 66's procedure states that "[w]hen practical access to water is not readily available, a deviation requesting an exemption for hydrostatic testing shall be submitted to the Phillips 66 Tank and Facility Integrity Group. The decision to use other methods in lieu of hydrostatic testing for new

tanks requires approval by the President of Transportation.”

Phillips 66 determined that a deviation from hydrostatic testing was required “due to insufficient water in the area, but also due to the economic impact of getting water to the site.” However, Phillips 66 recently conducted hydrostatic testing on the pipelines that directly connect to the Wink and Crane terminals. Therefore, there was sufficient water available for the hydrostatic testing of the tanks because Phillips 66 could use the same source of water it used for the connecting pipelines.

Therefore, Phillips 66 failed to perform a hydrostatic test in accordance with §§ 195.202 and 195.307(c).

2. Phillips 66 Response

Phillips 66 contests this warning item and PHMSA’s mischaracterization of the Company’s decision not to hydrostatically test the breakout tanks at the Wink and Crane, Texas terminals, an issue which is entirely unrelated to the release at issue in NOPV Items 1 and 2. In accordance with its procedures, Phillips 66 received proper approval to deviate from the requirement to hydrostatic test the relevant breakout tanks in accordance with the allowance in API 650 Section 7.3.5. The Company’s MPR6202 procedure requires approval by the Phillips 66 President of Transportation, a title which was changed in a prior company reorganization and is now called VP, Phillips 66 Midstream Operations. The VP, Phillips 66 Midstream Operations, is also the President of Phillips 66 Pipeline LLC, the operator of Gray Oak pipeline and the individual who approved the deviation from the hydrostatic testing requirement. Put another way, the same person – regardless of the title change – was responsible for approving the deviation. For additional clarity, Procedure MPR 6202 has been updated to reflect current titles.

Further, the Company stands by the approval to deviate from the hydrostatic testing requirements and maintains that it was fully compliant with the allowance in API 650 Section 7.3.5 and the requirements at 49 C.F.R. § 195.307. The Company applied additional safeguards in its procedures to follow API 650 Section 7.3.6.2 (13th Edition) to carefully monitor initial tank filing. PHMSA’s allegation is based on an oversimplification and inaccurate assumptions. Although the Company hydrostatically tested pipelines that connect to the terminals, the Company still did not have any practical access to water for several reasons, including:

- The volume of water required to test the tanks at the relevant terminals is seven (7) times more than the volume of water used to hydrostatically test the pipelines. Additionally, the source used to hydrostatically test the pipelines could not provide enough water to accommodate the increased volume of the tanks.
- The Company did not have landowner permission to construct disposal ponds to impound test water.

- The Company determined that it would have required roughly 3,200 truckloads of water transported from 66 miles away at a cost of \$1.1 million dollars to transport the amount of required water to test the tanks by truck.

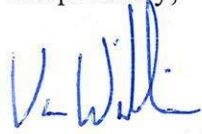
For these reasons, Phillips 66 respectfully requests that NOPV Item 3 be withdrawn.

III. Statement of Issues

- A. Whether NOPV Items 1 and 2, including the associated proposed civil penalties, are duplicative in that both allegations arise out of and are based on the same set of issues with the poor workmanship of a qualified contractor upon whom Phillips 66 relied in good faith and should be modified accordingly.
- B. Whether based on the facts and applicable law, PHMSA has met its burden to prove by a preponderance of the evidence that Phillips 66 did not comply with procedures as it relates to the requirements to hydrostatically test breakout tanks at its Wink and Crane, Texas terminals as alleged by NOPV Warning Item 3.
- C. Whether PHMSA provided due process and fair notice, as required by the U.S. Constitution and the Administrative Procedure Act, in issuing alleged violations for NOPV Items 1, 2, and 3 based on the facts and the applicable law.
- D. Whether PHMSA's allegations of noncompliance under NOPV Items 1, 2 and 3 are arbitrary and capricious, an abuse of discretion, or otherwise not in accordance with law in violation of the Administrative Procedure Act, 5 U.S.C. § 706(2).
- E. Whether the proposed civil penalties associated with NOPV Items 1 and 2 should be withdrawn or substantially reduced to accurately reflect the statutory and regulatory penalty assessment criteria required under 49 U.S.C. § 60122(b) and 49 C.F.R. § 190.225 and to align with penalties issued in prior relevant PHMSA enforcement.

Thank you for your consideration of this request for a settlement meeting and request for hearing, and for your cooperation in response to this matter. If you have any questions, please do not hesitate to contact me.

Respectfully,



Van P. Williams

cc: Manny Cortez (Phillips 66)
Doug Sauer (Phillips 66)
Catherine D. Little, Esq. (Bracewell)