Consumer Watchdog's Analysis for The California Attorney General and California Energy Commission's Petroleum Market Advisory Committee

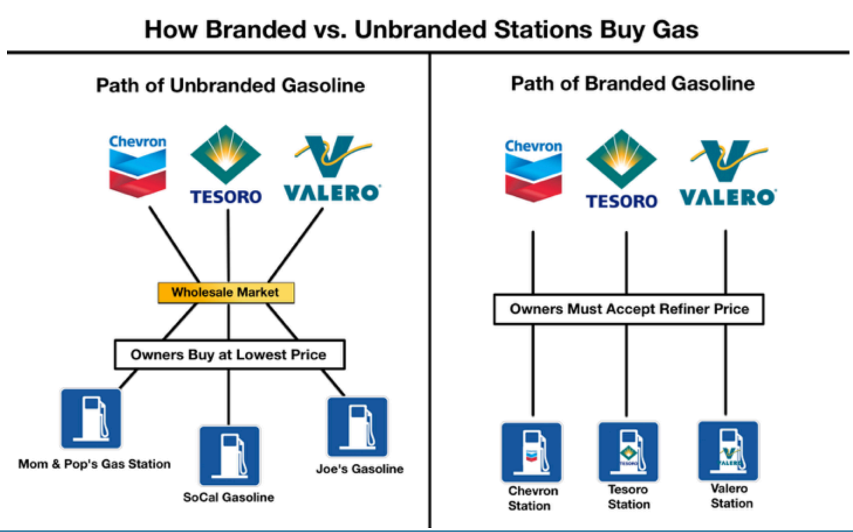
Presented Tuesday June 30, 2015

This analysis documents new evidence that oil refiners are artificially raising California gasoline prices, potentially in violation of previous agreements and anti-trust laws.

Consumer Watchdog presents this evidence in the hopes that a serious investigation and prosecution will ensue.

Typically, branded and unbranded (or independent) gas stations pay only a slightly different price for the wholesale gasoline they purchase. This price is known as the wholesale or rack price. According to CEC data analyzed by Consumer Watchdog, since 1999 the average gap between branded and unbranded stations in California has been 3 cents.

Currently, rack pricing shows that refiners are using their contractual leverage over branded stations to charge gas prices that are 30 cents higher than what unbranded stations pay. Since 1999, only 34 weeks out of 815 averaged a price when branded stations paid over 20 cents more than unbranded stations. Until June 2015, during the last 16 years there has been no period greater than one week during which branded stations were charged 30 cents or more than unbranded stations, and the 30 cents price point has been breached three times. Los Angeles rack prices for the last two weeks reflect a 30-cent differential between branded and unbranded prices – an unprecedented event.



Los Angeles rack price data below shows the refiners' bold move. The price difference was relatively stable throughout May, but increased rapidly coming into June. Some refiners increased their rack prices more than others, but below is the Los Angeles average for dates below.

Date	Amount Extra That Branded Stations Pay
6/25/15	**$0.26**
6/22/15	**0.29**
6/18/15	**0.31**
6/15/15	**0.29**
6/11/15	**0.32**
6/8/15	**0.27**
6/4/15	**0.27**
6/1/15	0.24
5/28/15	0.23
5/25/15	0.08
5/21/15	-0.02
5/18/15	-0.06
5/14/15	-0.10
5/11/15	-0.05
5/7/15	-0.05
5/4/15	0.03

Valero Rack prices for regular gasoline in Southern California show this trend:

Date:	6/11/15
Valero unbranded:	$2.17
Valero branded:	$2.48
Difference:	$0.31

Date:	6/18/15
Valero unbranded:	$2.15
Valero branded:	$2.46
Difference:	$0.31

Date:	6/22/15
Valero unbranded:	$2.16
Valero branded:	$2.46
Difference:	$0.30

Date:	6/23/15
Valero unbranded:	$2.11
Valero branded:	$2.42
Difference:	$0.31

Industry insiders have told Consumer Watchdog that this is an unprecedented pricing strategy to keep California gasoline prices artificially high. According to the Lundberg Survey this week, in the United States the average price difference between branded and unbranded stations is 5 cents.

Branded stations are generally larger, in more visible locations, offer additional services and use national marketing to develop brand loyalty. Unbranded stations are generally smaller and in less desirable and convenient locations, making a major shift in consumer purchasing unlikely even if the independents' retail pricing is noticeably lower.

The wholesale price gap at ARCO stations is of particular concern because of a deal Tesoro made with the California Attorney General after purchasing BP's Southern California Assets. According to a letter from the California Attorney General to the California Energy Commission dated May 17th, 2013, Tesoro, the second largest refiner in California, specifically agreed to continue to charge its branded ARCO stations low prices as a condition of the BP purchase. Anti-Trust chief Kathleen Foote, on behalf of Kamala Harris, wrote:

> *The ARCO brand plays an important role as the value leader in the market for branded retail gasoline in Southern California. It is important to our office that consumers continue to reap the benefits of ARCO's lower prices for years to come. Accordingly,* ***Tesoro has agreed to maintain ARCO's status as a low cost fuel provider.*** [Emphasis added]

The Federal Robinson-Patman Act prohibits charging different prices for the same product when costs are not different. The law came about when producers began charging discounted prices to large chain grocery stores, pushing family-owned retailers out of business. While costs to branded stations are often slightly different, due to certain cost considerations, consistent 30-cent differentials are a clear manipulation of prices in the state.

Tesoro and Valero may not be the only companies engaging in this overpricing. Other refiners may be engaged as well. Chevron is charging similar prices to its branded stations.

Rack prices are typically shielded from public view by pay walls, but have been provided to us by concerned industry insiders and can easily be obtained by government sources to confirm the data.

Oil refiners in California are being watched by this committee after industry documents showed the companies were working together to undermine global warming laws through scare tactics about higher gasoline prices.

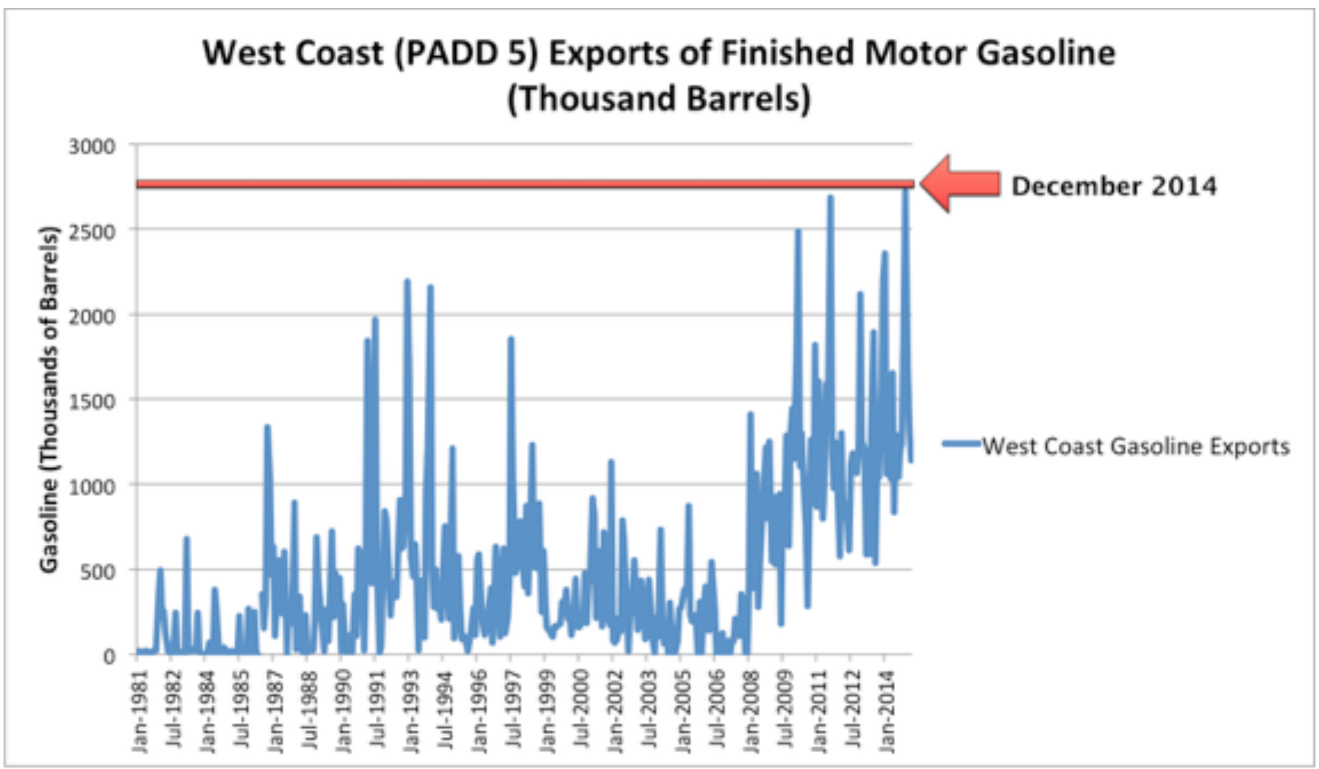
Since February, after the last meeting of the PMAC, California retail gasoline prices have risen by over $1.25 per gallon. In Southern California the gap with average US gasoline prices hit an unprecedented $1.30 per gallon.

A series of reports by Consumer Watchdog since the latest PMAC meeting have chronicled how oil refiners in the state have dried the market and reaped profits through unprecedented exports of gasoline to foreign nations and an unprecedented number of refineries taken offline for maintenance. By controlling and shrinking local supplies of gasoline, the refiners steadily increase their California profits even as drivers elsewhere enjoy steadily moderate prices.

Below is a summary of this research and new information we have received to bolster it.

Exports

- West Coast refineries exported the most gasoline in history in December of 2014 setting the table for the "supply shortage" that caused California's record price spike.
- June 2015 appears to be a record export month as well based on initial industry data that bears further investigation.
- Read the release: http://www.consumerwatchdog.org/newsrelease/west-coast-oil-companies-exported-record-amount-gasoline-foreign-nations-month-%E2%80%9Csupply-s



Profits

- Analysis of SEC filings showed that the first quarter of 2015 was one of the most profitable for California refiners in recent history. Despite refiners' claims that their costs were rising, profits per barrel of gasoline in California actually increased by a staggering amount – disputing industry assertions that higher costs were merely being passed to consumers.
- Valero, the state's fourth largest refiner, nearly quadrupled its typical quarterly profits in the first quarter of 2015.
- Tesoro, the state's second biggest refiner, shut down its Martinez refinery in early February and had to buy gasoline on the spot market to fulfill contracts, yet it still made a first quarter 2015 profit of $119 million.
- Our Consumer Watchdog report: *Refining Profits: How Californians Get Fleeced at the Pump,* can be read here: http://www.consumerwatchdog.org/resources/refiningprofits.pdf

CEOs of California's major refiners stated on investor calls that California and the West Coast saw huge profits from refinery maintenance and the tightening of supplies that the companies control. For instance:

Jeff Gustavson, General Manager, Chevron:

- "Margins increased earnings by $435 million driven by unplanned industry downtime and tight product supply on the US West Coast." - http://www.thestreet.com/story/13135723/3/chevron-cvx-earnings-report-q1-2015-conference-call-transcript.html

Greg Garland, Chairman, CEO, Phillips 66:

- "Well we like the West Coast this quarter" - http://www.thestreet.com/story/13135507/4/phillips-66-psx-earnings-report-q1-2015-conference-call-transcript.html

Greg Goff, CEO, Tesoro:

- "In California, crack spreads [different between crude oil costs and wholesale prices] have improved related to the unplanned and planned refinery maintenance activities" - http://www.thestreet.com/story/13145435/2/tesoro-tso-earnings-report-q1-2015-conference-call-transcript.html
- "There's no question that during the first quarter with what happened to Tesoro as a result of the disruption at the Martinez refinery because of the labor disruption and then with other operating and planned maintenance things across the whole system, it

was very supportive to the margin environment there." - http://www.thestreet.com/story/13145435/2/tesoro-tso-earnings-report-q1-2015-conference-call-transcript.html

Simon Henry, CFO, Shell:

- "On the Downstream side, refining margins around the world were supported by lower crude, and higher levels of industry planned and unplanned downtime, particularly in the United States." - http://www.thestreet.com/story/13135496/1/royal-dutch-shell-rdsa-earnings-report-q1-2015-conference-call-transcript.html

The Rigged Market

- Oil refiners in California keep less supply of gasoline on hand than the nationwide average, leaving the state vulnerable to price spikes.
- Over the last decade, many of the state's largest price spikes have come from clusters of refinery outages combined with tight supplies.
- Our Consumer Watchdog report: *Price Spiked: How Oil Refiners Gouge Californians on Their Gasoline*, can be read here: http://www.consumerwatchdog.org/resources/PriceSpiked.pdf

Refinery Closures

- In a letter to California's four United States Attorneys, Consumer Watchdog laid out eleven suspicious refinery closures that occurred in the first half of 2015. The full list can be found in our letter: http://consumerwatchdog.org/resources/ltrusattorneyspricemanip5-21-15ltrhd2_1.pdf

Conclusion:

California oil refiners, who have made a political agreement to undermine state environmental laws through claims of high gasoline prices, have used every trick in their playbook to raise gasoline prices artificially this year. They exported unprecedented amounts of finished gasoline to dry up the market, took down an unprecedented number of refineries offline in spring/summer drive time, and have propped up prices through manipulation of their price leverage at branded stations by 30 to 40 cents.

The Attorney General may have power to prosecute Tesoro on the last tactic under previous agreements made following the BP buyout and to prosecute other refiners under federal and state anti-trust laws that guarantee the like and kind products be made available to all at similar prices.

The Attorney General should appoint an independent prosecutor to investigate the necessity and reasonableness of the unprecedented refinery outages as many publicly stated reasons for these outages do not comport with industry understanding of them. The information received by the Commission is insufficient to make determinations as to whether the public was defrauded.

According to Gordon Schremp, chief petroleum analyst at the Commission, CEC does does not collect information on gasoline transactions, profit margins, inventory at gasoline terminals, and refinery maintenance schedules. Schremp stated about refinery maintenance schedules:

> *They're not required to report to us planned maintenance activities that are coming up so we know we're going to have a pretty heavy fourth quarter later this year, or first quarter 2015. … what we want to be doing is looking at those refiners when they're coming out of their planned maintenance and they have a problem, that's when in the past we've seen a pretty healthy price spike.*

An independent prosecutor overseen by the Attorney General could subpoena refiner records necessary to make such a determination.