

PART I

Items 1 and 2. *Business and Properties*

General

We are a publicly traded Delaware limited partnership, formed in 1998 and engaged in interstate and intrastate crude oil transportation, and crude oil gathering, marketing, terminalling and storage, as well as the marketing and storage of liquefied petroleum gas and natural gas related petroleum products. We refer to liquefied petroleum gas and natural gas related petroleum products collectively as "LPG." We have an extensive network of pipeline transportation, storage and gathering assets in key oil producing basins and at major market hubs in the United States and Canada. Our operations can be categorized into two primary business activities:

- *Crude Oil Pipeline Transportation Operations.* As of December 31, 2004, we owned approximately 15,000 miles of active gathering and mainline crude oil pipelines located throughout the United States and Canada, of which approximately 13,000 miles are included in our pipeline segment. Our activities from pipeline operations generally consist of transporting crude oil for a fee, third party leases of pipeline capacity, barrel exchanges and buy/sell arrangements.
- *Gathering, Marketing, Terminalling and Storage Operations.* As of December 31, 2004, we owned approximately 37 million barrels of active above ground crude oil terminalling and storage facilities, including approximately 23.4 million barrels of tankage that are associated with our pipeline operations within our pipeline segment. These facilities include a crude oil terminalling and storage facility at Cushing, Oklahoma. Cushing, which we refer to in this report as the Cushing Interchange, is one of the largest crude oil market hubs in the United States and the designated delivery point for NYMEX crude oil futures contracts. We utilize our storage tanks to counter-cyclically balance our gathering and marketing operations and to execute various hedging strategies to stabilize profits and reduce the negative impact of crude oil market volatility. Our terminalling and storage operations also generate revenue at the Cushing Interchange and our other locations through a combination of storage and throughput charges to third parties. We also own approximately 1.7 million barrels of LPG storage. Our gathering and marketing operations include:
 - the purchase of U.S. and Canadian crude oil at the wellhead and the bulk purchase of crude oil at pipeline and terminal facilities, as well as foreign cargoes;
 - the transportation of crude oil on trucks, barges and pipelines;
 - the subsequent resale or exchange of crude oil at various points along the crude oil distribution chain; and
 - the purchase of LPG from producers, refiners and other marketers, the storage of LPG at storage facilities owned by us or third parties and the sale of LPG to wholesalers, retailers and industrial end users.

Business Strategy

Our principal business strategy is to capitalize on the regional crude oil supply and demand imbalances that exist in the United States and Canada by combining the strategic location and distinctive capabilities of our transportation and terminalling assets with our extensive marketing and distribution expertise to generate sustainable earnings and cash flow.

We intend to execute our business strategy by:

- increasing and optimizing throughput on our existing pipeline and gathering assets and realizing cost efficiencies through operational improvements;
- utilizing our Cushing Terminal and our other assets to service the needs of refiners and to profit from merchant activities that take advantage of crude oil pricing and quality differentials;
- utilizing assets we have recently acquired along the Gulf Coast and our Cushing Terminal to increase our presence in the importation of foreign crude through Gulf of Mexico receipt facilities to U.S. refiners;
- selectively pursuing strategic and accretive acquisitions of crude oil transportation assets, including pipelines, gathering systems, terminalling and storage facilities and other assets that complement our existing asset base and distribution capabilities;
- optimizing and expanding our Canadian operations and our presence in certain areas of the U.S. to take advantage of anticipated increases in the volume and qualities of crude oil produced in these areas as well as increased foreign crude import activities in the Gulf Coast area; and
- prudently and economically leveraging our asset base, knowledge base and skill sets to participate in energy businesses that are closely related to, or significantly intertwined with, the crude oil business.

To a lesser degree, we also engage in a similar business strategy with respect to the wholesale marketing and storage of LPG.

Financial Strategy

Targeted Credit Profile

We believe that a major factor in our continued success is our ability to maintain a competitive cost of capital and access to the capital markets. We have consistently communicated to the financial community our intention to maintain a strong credit profile that we believe is consistent with an investment grade credit rating. We have targeted a general credit profile with the following attributes:

- an average long-term debt-to-total capitalization ratio of approximately 55% or less;
- an average long-term debt-to-EBITDA ratio of approximately 3.5x or less (EBITDA is earnings before interest, taxes, depreciation and amortization); and,
- an average EBITDA-to-interest coverage ratio of approximately 3.3x or better.

Based on our 2004 results, we were slightly above our targeted metric for long-term debt-to-EBITDA primarily due to acquisitions made at various times throughout the year, and the inclusion of less than a full year's results in EBITDA. In order for us to maintain our targeted credit profile and achieve growth through acquisitions, we intend to fund acquisitions using approximately equal proportions of equity and debt. In certain cases, acquisitions will initially be financed using debt since it is difficult to predict the actual timing of accessing the market to raise equity. Accordingly, from time to time we may be outside the parameters of our targeted credit profile.

Credit Rating

As of February 2005, our senior unsecured rating with Standard & Poors and Moody's Investment Services was BBB- stable and Baa3 stable, respectively, both of which are investment grade. We cannot assure you that these ratings will remain in effect for any given period of time or that one or both of these ratings will not be lowered or withdrawn entirely by a rating agency. Note that a credit rating is not a recommendation to buy, sell or hold securities, and may be revised or withdrawn at any time.

Competitive Strengths

We believe that the following competitive strengths position us to successfully execute our principal business strategy:

- ***Our pipeline assets are strategically located and have additional capacity.*** Our primary crude oil pipeline transportation and gathering assets are located in well-established oil producing regions and are connected, directly or indirectly, with our terminalling and storage assets that service major North American refinery and distribution markets where we have strong business relationships. In many instances, these assets are strategically positioned to maximize the value of crude oil by transporting it to major trading locations and premium markets. Certain of our pipeline networks currently possess additional capacity that can accommodate increased demand without significant additional capital investment.
- ***Our Cushing Terminal is strategically located and operationally flexible.*** Our Cushing Terminal interconnects with the Cushing Interchange's major inbound and outbound pipelines, providing access to both foreign and domestic crude oil. Our Cushing Terminal is one of the most modern large-scale terminalling and storage facilities at the Cushing Interchange, incorporating operational enhancements designed with the ability to safely and efficiently terminal, store, blend and segregate large volumes and multiple varieties of crude oil as well as with extensive environmental safeguards. Since becoming operational in late 1993, we have completed four separate expansion phases, increasing the Cushing Terminal's tankage to 6.3 million barrels. In January 2005, we announced the commencement of our Phase V expansion that will increase the Cushing Terminal's capacity by approximately 1.1 million barrels. In addition, we own approximately 31 million barrels of above-ground crude oil terminalling and storage assets elsewhere in the United States and Canada that are used in our pipeline operations or that complement our Cushing Terminal and enable us to serve the needs of our customers.
- ***We possess specialized crude oil market knowledge.*** We believe our business relationships with participants in various phases of the crude oil distribution chain, from crude oil producers to refiners, as well as our own industry expertise, provide us with an extensive understanding of the North American physical crude oil markets.
- ***Our business activities are counter-cyclically balanced.*** We believe that our terminalling and storage activities and our gathering and marketing activities are counter-cyclical. We believe this balance of activities, combined with our pipeline transportation operations, has a stabilizing effect on our cash flow from operations.
- ***We have the financial flexibility to continue to pursue expansion and acquisition opportunities.*** We believe we have significant resources to finance strategic expansion and acquisition opportunities, including our ability to issue additional partnership units, to borrow under our credit facilities and to issue additional notes in the long-term debt capital markets. As of December 31, 2004, we had approximately \$420.2 million available under our committed credit facilities, subject to covenant compliance.
- ***We have an experienced management team whose interests are aligned with those of our unitholders.*** Our executive management team has an average of more than 20 years industry experience, with an average of over 15 years with us or our predecessors and affiliates. Members of our senior management team own a 4% interest in our general partner and collectively own approximately 650,000 common units. In addition, through grants of phantom units and options, the senior management team also owns significant contingent equity incentives that generally vest upon achievement of performance objectives, continued service or, in certain cases, both.

Organizational History

We were formed as a master limited partnership in September 1998 to acquire and operate midstream crude oil businesses and assets. We completed our initial public offering in November 1998. Since June 2001, our 2% general partner interest has been held by Plains AAP, L.P., a Delaware limited partnership. Plains All American GP LLC, a Delaware limited liability company, is Plains AAP, L.P.'s general partner. Unless the context otherwise requires, we use the term "general partner" to refer to both Plains AAP, L.P. and Plains All American GP LLC. Plains AAP, L.P. and Plains All American GP LLC are essentially held by seven owners. See "Security Ownership of Certain Beneficial Owners and Management and Related Unitholders' Matters—Beneficial Ownership of General Partner Interest."

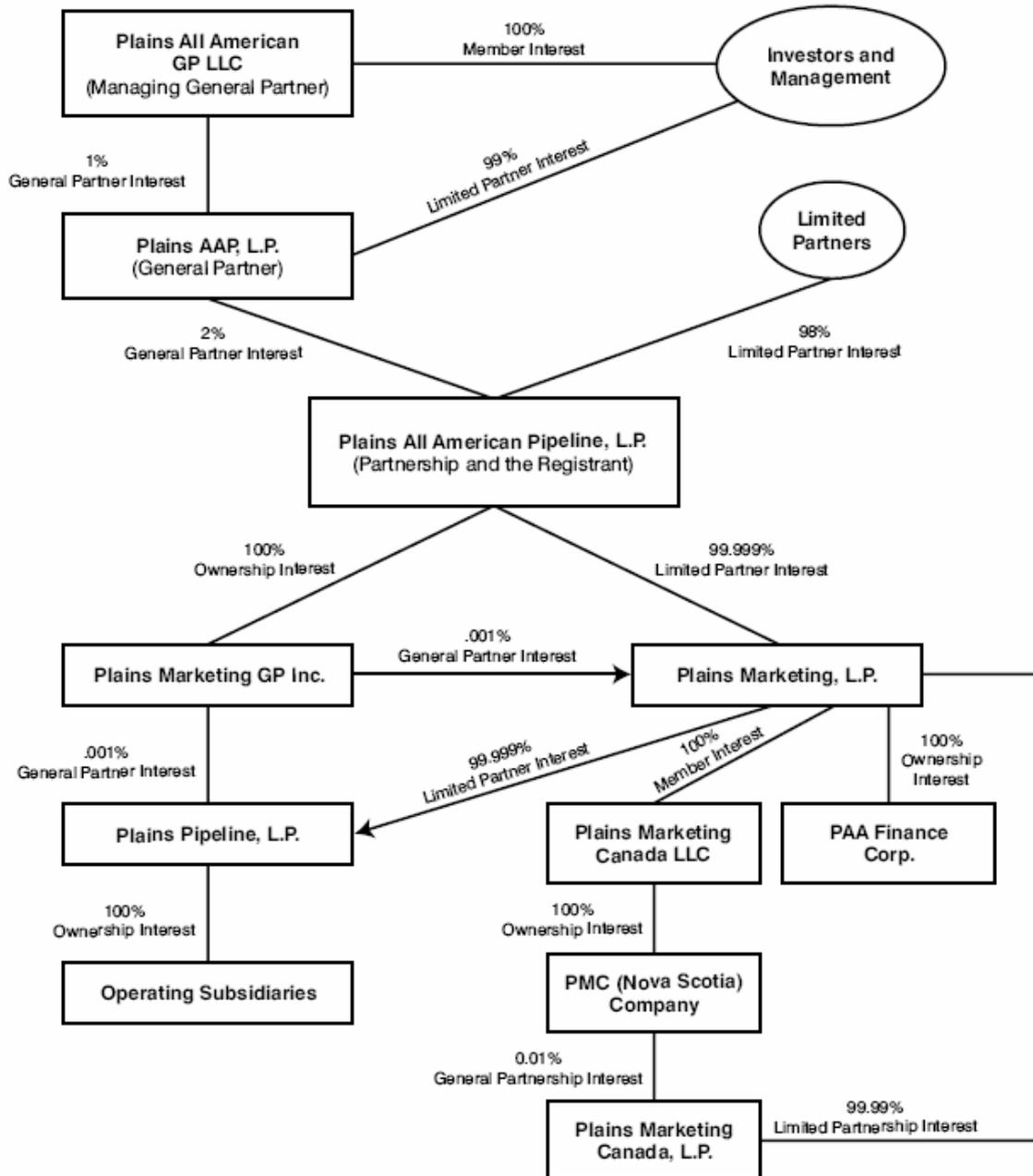
Partnership Structure and Management

Our operations are conducted through, and our operating assets are owned by, our subsidiaries. We own our interests in our subsidiaries through two operating partnerships, Plains Marketing, L.P. and Plains Pipeline, L.P. Our Canadian and LPG operations are conducted through Plains Marketing Canada, L.P.

Our general partner, Plains AAP, L.P., is a limited partnership. Our general partner is managed by its general partner, Plains All American GP LLC, which has ultimate responsibility for conducting our business and managing our operations. Plains All American GP LLC is governed by an eight-member board of directors. As amended in July 2004, the limited liability company agreement provides that four directors are designated by the four owners that hold 9% or greater of the outstanding membership interests of Plains All American GP LLC, one director is the Chairman and CEO and three independent directors are elected by majority vote of the membership owners of Plains All American GP LLC. Our general partner does not receive a management fee or other compensation in connection with its management of our business, but it is reimbursed for all direct and indirect expenses incurred on our behalf.

The chart on the next page depicts the current structure and ownership of Plains All American Pipeline, L.P. and certain subsidiaries.

Partnership Structure



Acquisitions

An integral component of our business strategy and growth objective is to acquire assets and operations that are strategic and complementary to our existing operations. Such assets and operations include crude oil related assets and LPG assets, as well as energy assets that are closely related to, or intertwined with, these business lines, and enable us to leverage our asset base, knowledge base and skill sets. We have established a target to complete, on average, \$200 million to \$300 million in acquisitions per year, subject to availability of attractive assets on acceptable terms. Since 1998, and through December 31, 2004, we have completed numerous acquisitions for an aggregate purchase price of approximately \$1.9 billion. In addition, from time to time, we have sold assets that are no longer considered essential to our operations.

The following table summarizes selected acquisitions that we have completed over the past five years:

Acquisition	Date	Description	Approximate Purchase Price (in millions)
Schaefferstown Propane Storage Facility	August 2004	Storage capacity of approximately 0.5 million barrels of refrigerated propane	\$32
Cal Ven Pipeline System	May 2004	195-miles of gathering and mainline crude oil pipelines in northern Alberta	\$19
Link Energy LLC	April 2004	The North American crude oil and pipeline operations of Link Energy, LLC ("Link")	\$332
Capline and Capwood Pipeline Systems	March 2004	An approximate 22% undivided joint interest in the Capline Pipeline System and an approximate 76% undivided joint interest in the Capwood Pipeline System	\$158
South Saskatchewan Pipeline System	November 2003	A 158-mile mainline crude oil pipeline and 203 miles of gathering lines in Saskatchewan	\$48
ArkLaTex Pipeline System	October 2003	240 miles of crude oil gathering and mainline pipelines and 470,000 barrels of crude oil storage capacity	\$21
Iraan to Midland Pipeline System	June 2003	98-mile mainline crude oil pipeline	\$18
South Louisiana Assets	June 2003 and December 2003	Various terminalling and gathering assets in South Louisiana, including a 100% interest in Atchafalaya Pipeline, L.L.C.	\$18

Acquisition	Date	Description	Approximate Purchase Price (in millions)
Iatan Gathering System	March 2003	West Texas crude oil gathering system	\$24
Red River Pipeline System	February 2003	334-mile crude oil pipeline along with 645,000 barrels of crude oil storage capacity	\$19
Shell West Texas Assets	August 2002	Basin Pipeline System, Permian Basin Pipeline System and the Rancho Pipeline System	\$324
Canadian Operations	May/July 2001	The assets of CANPET Energy Group (crude oil and LPG marketing) and substantially all of the Canadian crude oil pipeline, gathering, storage and terminalling assets of Murphy Oil Company Ltd. (560 miles of crude oil and condensate mainlines along with 1.1 million barrels of crude oil storage and terminalling capacity)	\$232

The following is a more in-depth discussion of selected acquisitions completed in 2004:

Schaefferstown Propane Storage Facility

In August 2004, we completed the acquisition of the Schaefferstown Propane Storage Facility from Koch Hydrocarbon, L.P. The total purchase price was approximately \$32 million, including transaction costs. In connection with the transaction, the Partnership also acquired an additional \$14.2 million of inventory. The transaction was funded through a combination of cash on hand and borrowings under the Partnership's revolving credit facilities. The storage facility is located approximately 65 miles northwest of Philadelphia near Schaefferstown, Pennsylvania, and has the capacity to store approximately 0.5 million barrels of refrigerated propane. In addition, the facility has 19 bullet storage tanks with an aggregate capacity of approximately 14,000 barrels. Propane is delivered to the facility via truck or pipeline and is transported out of the facility by truck. In addition, the transaction also included approximately 61 acres of land and a truck rack. The results of operations and assets from this acquisition have been included in our consolidated financial statements and our gathering, marketing, terminalling and storage operations segment since August 25, 2004.

Cal Ven Pipeline System

On May 7, 2004, we completed the acquisition of the Cal Ven Pipeline System from Cal Ven Limited, a subsidiary of Unocal Canada Limited. The total purchase price was approximately \$19 million, including transaction costs. The Cal Ven Pipeline System includes approximately 195 miles of 8-inch and 10-inch gathering and mainline crude oil pipelines. The system is located in northern Alberta and has the ability to deliver crude oil into the Rainbow Pipeline System. The results of operations and assets from this acquisition have been included in our consolidated financial statements and our pipeline operations segment since May 1, 2004.

Link Energy LLC

On April 1, 2004, we completed the acquisition of all of the North American crude oil and pipeline operations of Link Energy LLC ("Link") for approximately \$332 million, including \$268 million of cash (net of approximately \$5.5 million subsequently returned to us from an indemnity escrow account) and approximately \$64 million of net liabilities assumed and acquisition-related costs. The Link crude oil business consists of approximately 7,000 miles of active crude oil pipeline and gathering systems, over 10 million barrels of active crude oil storage capacity, a fleet of approximately 200 owned or leased trucks and approximately 2 million barrels of crude oil linefill and working inventory. The Link assets complement our assets in West Texas and along the Gulf Coast and allowed us to expand our presence in the Rocky Mountain and Oklahoma/Kansas regions. The results of operations and assets from this acquisition have been included in our consolidated financial statements and both our pipeline operations and gathering, marketing, terminalling and storage operations segments since April 1, 2004.

Capline and Capwood Pipeline System

In March 2004, we completed the acquisition of all of Shell Pipeline Company LP's ("SPLC") interests in two entities for approximately \$158.0 million in cash (including a \$15.8 million deposit paid in December 2003) and approximately \$0.5 million of transaction and other costs. The principal assets of the entities are: (i) an approximate 22% undivided joint interest in the Capline Pipeline System, and (ii) an approximate 76% undivided joint interest in the Capwood Pipeline System. The Capline Pipeline System is a 633-mile, 40-inch mainline crude oil pipeline originating in St. James, Louisiana, and terminating in Patoka, Illinois. The Capline system is one of the primary transportation routes for crude oil shipped into the Midwestern U.S., accessing over 2.7 million barrels of refining capacity in PADD II. Capline has direct connections to a significant amount of sweet and light sour crude production in the Gulf of Mexico. In addition, with its two active docks capable of handling 600,000-barrel tankers as well as access to LOOP, the Louisiana Offshore Oil Port, the Capline System is a key transporter of both domestic and foreign crude to PADD II. The total system operating capacity is 1.14 million barrels per day, with approximately 248,000 barrels per day subject to the interest acquired. Since we acquired this asset, throughput on the interest we acquired averaged approximately 147,000 barrels per day.

The Capwood Pipeline System is a 57-mile, 20-inch mainline crude oil pipeline originating in Patoka, Illinois, and terminating in Wood River, Illinois. The Capwood system has an operating capacity of 277,000 barrels per day of crude oil. Of that capacity, approximately 211,000 barrels per day are subject to the interest acquired. Since we acquired this asset, throughput on the interest we acquired averaged approximately 120,000 barrels per day. The Capwood System has the ability to deliver crude at Wood River to PADD II refineries and pipelines. Movements on the Capwood system are driven by the volumes shipped on Capline as well as Canadian crude that can be delivered to Patoka via the Mustang Pipeline. Since closing, we have assumed the operatorship of the Capwood system from SPLC.

Ongoing Acquisition Activities

Consistent with our business strategy, we are continuously engaged in discussions with potential sellers regarding the possible purchase by us of assets and operations that are strategic and complementary to our existing operations. Such assets and operations include crude oil related assets and LPG assets, as well as energy assets that are closely related to, or intertwined with, these business lines, and enable us to leverage our asset base, knowledge base and skill sets. Such acquisition efforts involve participation by us in processes that have been made public, involve a number of potential buyers and are commonly referred to as "auction" processes, as well as situations in which we believe we are the only party or one of a very limited number of potential buyers in negotiations with the

potential seller. These acquisition efforts often involve assets which, if acquired, would have a material effect on our financial condition and results of operations.

Dispositions

Shutdown and Sale of Rancho Pipeline System

We acquired an interest in the Rancho Pipeline System from Shell in August 2002. The Rancho Pipeline System Agreement dated November 1, 1951, pursuant to which the system was constructed and operated, terminated in March 2003. Upon termination, the agreement required the owners to take the pipeline system, in which we owned an approximate 50% interest, out of service. Accordingly, we notified our shippers and did not accept nominations for movements after February 28, 2003. This shutdown was contemplated at the time of the acquisition and was accounted for under purchase accounting in accordance with SFAS No. 141 "Business Combinations." The pipeline was shut down on March 1, 2003 and a purge of the crude oil linefill was completed in April 2003. In June 2003, we completed transactions whereby we transferred our ownership interest in approximately 241 miles of the total 458 miles of the pipeline in exchange for \$4.0 million and approximately 500,000 barrels of crude oil tankage in West Texas. In August 2004, we sold our interest in the remaining portion of the system for approximately \$0.9 million, including the assumption by the purchaser of all liabilities typically associated with pipelines of this type. We recognized a gain of approximately \$0.6 million on this transaction.

All American Pipeline Linefill Sale and Asset Disposition

In March 2000, we sold the segment of the All American Pipeline that extends from Emidio, California to McCamey, Texas for \$129.0 million. Except for minor third-party volumes, one of our subsidiaries, Plains Marketing, L.P., was the sole shipper on this segment of the pipeline since its predecessor acquired the line from the Goodyear Tire & Rubber Company in July 1998. We realized net proceeds of approximately \$124.0 million after the associated transaction costs and estimated costs to remove equipment. We used the proceeds from the sale to reduce outstanding debt. We recognized a gain of approximately \$20.1 million in connection with the sale.

We had suspended shipments of crude oil on this segment of the pipeline in November 1999. At that time, we owned approximately 5.2 million barrels of crude oil in the segment of the pipeline. We sold this crude oil from November 1999 to February 2000 for net proceeds of approximately \$100.0 million, which were used for working capital purposes. We recognized an aggregate gain of approximately \$44.6 million, of which approximately \$28.1 million was recognized in 2000.

Description of Segments and Associated Assets

Our business activities are conducted through two primary segments, Pipeline Operations and Gathering, Marketing, Terminalling and Storage Operations ("GMT&S"). Our operations are conducted in approximately 40 states in the United States and six provinces in Canada.

Following is a description of the activities and assets for each of our business segments:

Pipeline Operations

As of December 31, 2004, we owned approximately 15,000 miles of active gathering and mainline crude oil pipelines located throughout the United States and Canada. Approximately 13,000 miles of these pipelines are used in our pipeline operations segment with the remainder used in our GMT&S segment. Our activities from pipeline operations generally consist of transporting crude oil for a fee and third-party leases of pipeline capacity, as well as barrel exchanges and buy/sell arrangements.

Substantially all of our pipeline systems are controlled or monitored from one of two central control rooms with computer systems designed to continuously monitor real-time operational data, including measurement of crude oil quantities injected into and delivered through the pipelines, product flow rates, and pressure and temperature variations. The systems are designed to enhance leak detection capabilities, sound automatic alarms in the event of operational conditions outside of pre-established parameters and provide for remote controlled shut-down of pump stations on the pipeline systems. Pump stations, storage facilities and meter measurement points along the pipeline systems are linked by telephone, satellite, radio or a combination thereof to provide communications for remote monitoring and in some instances control, which reduces our requirement for full-time site personnel at most of these locations.

We perform scheduled maintenance on all of our pipeline systems and make repairs and replacements when necessary or appropriate. We attempt to control corrosion of the mainlines through the use of cathodic protection, corrosion inhibiting chemicals injected into the crude stream and other protection systems typically used in the industry. Maintenance facilities containing equipment for pipe repairs, spare parts and trained response personnel are strategically located along the pipelines and in concentrated operating areas. We believe that all of our pipelines have been constructed and are maintained in all material respects in accordance with applicable federal, state, provincial and local laws and regulations, standards prescribed by the American Petroleum Institute, the Canadian Standards Association and accepted industry practice. See "—Regulation—Pipeline and Storage Regulation."

Major Pipeline Assets

All American Pipeline System

The All American Pipeline is a common carrier crude oil pipeline system that transports crude oil produced from certain outer continental shelf, or OCS, fields offshore California via connecting pipelines to refinery markets in California. The system extends approximately 10 miles along the California coast from Las Flores to Gaviota (24-inch diameter pipe) and continues from Gaviota approximately 126 miles to our station in Emidio, California (30-inch diameter pipe). Between Gaviota and our Emidio Station, the All American Pipeline interconnects with our San Joaquin Valley, or SJV, Gathering System as well as various third-party intrastate pipelines. The system is subject to tariff rates regulated by the FERC.

The All American Pipeline currently transports OCS crude oil received at the onshore facilities of the Santa Ynez field at Las Flores and the onshore facilities of the Point Arguello field located at Gaviota. ExxonMobil, which owns all of the Santa Ynez production, and Plains Exploration and Production Company ("PXP") and other producers that together own approximately 75% of the Point Arguello production, have entered into transportation agreements committing to transport all of their production from these fields on the All American Pipeline. These agreements, which expire in August 2007, provide for a minimum tariff with annual escalations based on specific composite indices. The producers from the Point Arguello field that do not have contracts with us have no other means of transporting their production and, therefore, ship their volumes on the All American Pipeline at the filed tariffs. Volumes attributable to PXP are purchased and sold to a third party under our marketing agreement with PXP before such volumes enter the All American Pipeline. See "Certain Relationships and Related Transactions—Transactions with Related Parties—General." The third party pays the same tariff as required in the transportation agreements. For 2003 and 2004, the tariffs averaged \$1.71 per barrel and \$1.81 per barrel, respectively. Effective January 1, 2005, based on the contractual escalator, the average tariff increased to \$1.88 per barrel. The agreements do not require these owners to transport a minimum volume.

A significant portion of our revenues less direct field operating costs is derived from the pipeline transportation business associated with these two fields. The relative contribution to our revenues less

direct field operating costs from these fields has decreased from approximately 24% in 2000 to 11% in 2004, as we have grown and diversified through acquisitions and organic expansions and as a result of declines in volumes produced and transported from these fields. Since our acquisition in 1998, the volume decline has been substantially offset by an increase in pipeline tariffs. Over the last several years, transportation volumes received from the Santa Ynez and Point Arguello fields have declined from 92,000 and 60,000 average daily barrels, respectively, in 1995 to 44,000 and 10,000 average daily barrels, respectively, for 2004. We expect that there will continue to be natural production declines from each of these fields as the underlying reservoirs are depleted. A 5,000 barrel per day decline in volumes shipped from these fields would result in a decrease in annual pipeline segment profit of approximately \$3.2 million, based on a tariff of \$1.88 per barrel.

In October 2004, PXP announced that it had successfully completed an initial development well into the Rocky Point field that is accessible from the Point Arguello platforms and that drilling operations are underway on a second development well. If successful, such incremental drilling activity could lead to increased volumes on our All American Pipeline System in future periods. However, we can give no assurance that our volumes transported would increase as a result of this drilling activity.

The table below sets forth the historical volumes received from both of these fields for the past five years:

	Year Ended December 31,				
	2004	2003	2002	2001	2000
	(barrels in thousands)				
Average daily volumes received from:					
Point Arguello (at Gaviota)	10	13	16	18	18
Santa Ynez (at Las Flores).....	44	46	50	51	56
Total	<u>54</u>	<u>59</u>	<u>66</u>	<u>69</u>	<u>74</u>

Basin Pipeline System

The Basin Pipeline System, in which we own an approximate 87% undivided joint interest, is a primary route for transporting Permian Basin crude oil to Cushing, Oklahoma, for further delivery to Mid-Continent and Midwest refining centers. We acquired the Basin Pipeline System in August 2002. Since acquisition, we have been the operator of the system. The Basin system is a 515-mile mainline, telescoping crude oil system with a capacity ranging from approximately 144,000 barrels per day to 394,000 barrels per day depending on the segment. System throughput (as measured by system deliveries) was approximately 265,000 barrels per day (net to our interest) during 2004. Within the current operating range, a 20,000 barrel per day decline in volumes shipped on the Basin system would result in a decrease in annual pipeline segment profit of approximately \$1.8 million.

The Basin system consists of three primary movements of crude oil: (i) barrels are shipped from Jal, New Mexico to the West Texas markets of Wink and Midland, where they are exchanged and/or further shipped to refining centers; (ii) barrels are shipped to the Mid-Continent region on the Midland to Wichita Falls segment and the Wichita Falls to Cushing segment; and (iii) foreign and Gulf of Mexico barrels are delivered into Basin at Wichita Falls and delivered to a connecting carrier or shipped to Cushing for further distribution to Mid-Continent or Midwest refineries. The system also includes approximately 5.8 million barrels (5.0 million barrels, net to our interest) of crude oil storage capacity located along the system.

In 2004, we expanded a 424-mile section of the system extending from Midland, Texas to Cushing, Oklahoma. With the completion of this expansion, the capacity of this section has increased approximately 15%, from 350,000 barrels per day to approximately 400,000 barrels per day. The Basin

system is subject to tariff rates regulated by the Federal Energy Regulatory Commission (the "FERC"). TEPPCO Partners, L.P. owns the remaining approximately 13% interest in the system.

Capline/Capwood Pipeline Systems

The Capline Pipeline System, in which we own a 22% undivided joint interest, is a 633-mile, 40-inch mainline crude oil pipeline originating in St. James, Louisiana, and terminating in Patoka, Illinois. The Capline Pipeline System is one of the primary transportation routes for crude oil shipped into the Midwestern U.S., accessing over 2.7 million barrels of refining capacity in PADD II. Capline has direct connections to a significant amount of crude production in the Gulf of Mexico. In addition, with its two active docks capable of handling 600,000-barrel tankers as well as access to LOOP, it is a key transporter of sweet and light sour foreign crude to PADD II. With a total system operating capacity of 1.14 million barrels per day of crude oil, approximately 248,000 barrels per day are subject to our interest. Since we acquired this asset in March 2004, throughput on the interest acquired has averaged approximately 147,000 barrels per day. A 10,000 barrel per day decline in volumes shipped on the Capline system would result in a decrease in annual pipeline segment profit of approximately \$1.5 million.

The Capwood Pipeline System, in which we own a 76% undivided joint interest, is a 57-mile, 20-inch mainline crude oil pipeline originating in Patoka, Illinois, and terminating in Wood River, Illinois. The Capwood Pipeline System has an operating capacity of 277,000 barrels per day of crude oil. Of that capacity, approximately 211,000 barrels per day are subject to our interest. The system has the ability to deliver crude oil at Wood River to several other PADD II refineries and pipelines. Movements on the Capwood system are driven by the volumes shipped on Capline as well as Canadian crude that can be delivered to Patoka via the Mustang Pipeline. PAA assumed the operatorship of the Capwood system from SPLC. Since we acquired this asset in March 2004, throughput net to our interest acquired has averaged approximately 120,000 barrels per day.

Our significant pipeline systems are discussed on the previous pages. Following is a tabular presentation of all of our active pipeline assets in the United States and Canada, grouped by geographic location and including the aforementioned major pipeline assets:

<u>Region</u>	<u>Pipeline</u>	<u>Ownership Percentage</u>	<u>Pipeline Mileage</u>	<u>2004 Average Net Volumes</u>
Southwest US	Basin	87.0%	515	265,000
	West Texas Gathering	100.0%	717	80,000
	Permian Basin	100.0%	919	46,000
	Dollarhide	100.0%	24	6,000
	Mesa	8.8%	79	28,000
	Iraan	100.0%	98	23,000
	Iatan	100.0%	360	22,000
	New Mexico	100.0%	1,185	50,000
	Texas	100.0%	1,276	80,000
	Lefors	100.0%	68	2,000
Merkel	100.0%	128	1,000	
Western US	All American	100.0%	136	54,000
	San Joaquin Valley	100.0%	86	74,000
US Rocky Mountains.....	Butte	22.0%	370	15,000
	North Dakota	100.0%	620	39,000
US Gulf Coast	Sabine Pass	100.0%	33	15,000
	Ferriday	100.0%	570	7,000
	La Gloria	100.0%	114	23,000
	Red River	100.0%	567	12,000
	ArkLaTex	100.0%	161	7,000
	Atchafalaya	100.0%	35	14,000
	Eugene Island	100.0%	66	12,000
	Bridger Lakes	100.0%	17	3,000
	Capline	22.0%	633	123,000
	Capwood/Patoka	76.0%	57	109,000
	Pearsall	100.0%	62	2,000
	Mississippi/Alabama	100.0%	686	29,000
Southwest Louisiana	100.0%	267	4,000	
Central US	Oklahoma	100.0%	1,498	56,000
	Midcontinent	100.0%	1,196	22,000
Canada.....	Cal Ven	100.0%	177	11,000
	Manito	100.0%	101	71,000
	Milk River	100.0%	11	106,000
	Cactus Lake	14.9%	55	3,000
	Wascana	100.0%	114	9,000
	Wapella	100.0%	79	14,000
	South Sask	100.0%	158	49,000

Gathering, Marketing, Terminalling and Storage Operations

The combination of our gathering and marketing operations and our terminalling and storage operations provides a counter-cyclical balance that has a stabilizing effect on our operations and cash

flow. The strategic use of our terminalling and storage assets in conjunction with our gathering and marketing operations generally provides us with the flexibility to maintain our margins irrespective of whether a strong or weak market exists. Following is a description of our activities with respect to this segment.

Gathering and Marketing Operations

Crude Oil. The majority of our gathering and marketing activities are in the geographic locations previously discussed. These activities include:

- purchasing crude oil from producers at the wellhead and in bulk from aggregators at major pipeline interconnects, trading locations as well as foreign cargoes brought in by tanker;
- transporting crude oil on our own proprietary gathering assets and our common carrier pipelines or, when necessary or cost effective, assets owned and operated by third parties;
- exchanging crude oil for another grade of crude oil or at a different geographic location, as appropriate, in order to maximize margins or meet contract delivery requirements; and
- marketing crude oil to refiners or other resellers.

We purchase crude oil from many independent producers and believe that we have established broad-based relationships with crude oil producers in our areas of operations. Gathering and marketing activities involve relatively large volumes of transactions often with lower margins than pipeline and terminalling and storage operations.

The following table shows the average daily volume of our lease gathering and bulk purchases for the past five years:

	Year Ended December 31,				
	2004	2003	2002	2001	2000
	(barrels in thousands)				
Lease gathering.....	589	437	410	348	262
Bulk purchases.....	148	90	68	46	28
Total volumes per day	<u>737</u>	<u>527</u>	<u>478</u>	<u>394</u>	<u>290</u>

Crude Oil Purchases. We purchase crude oil from producers under contracts, the majority of which range in term from a thirty-day evergreen to three years. In a typical producer's operation, crude oil flows from the wellhead to a separator where the petroleum gases are removed. After separation, the crude oil is treated to remove water, sand and other contaminants and is then moved into the producer's on-site storage tanks. When the tank is approaching capacity, the producer contacts our field personnel to purchase and transport the crude oil to market. We utilize our truck fleet and gathering pipelines as well as third-party pipelines, trucks and barges to transport the crude oil to market. We own or lease approximately 400 trucks used for gathering crude oil.

We currently have a marketing agreement with PXP for certain of its equity crude oil production and that of its subsidiaries. The marketing agreement provides that we will purchase PXP's equity crude oil production for resale at market prices, for which we charge a fee of \$0.20 per barrel. For any new contracts for the sale of the crude oil entered into after January 1, 2005, the marketing fee will be adjusted to \$0.15 per barrel, subject to further adjustment in November 2007 based upon then existing market conditions. See "Certain Relationships and Related Transactions—Transactions with Related Parties—General."

Bulk Purchases. In addition to purchasing crude oil at the wellhead from producers, we purchase crude oil in bulk at major pipeline terminal locations. This oil is transported from the wellhead to the

pipeline by major oil companies, large independent producers or other gathering and marketing companies. We purchase crude oil in bulk when we believe additional opportunities exist to realize margins further downstream in the crude oil distribution chain. The opportunities to earn additional margins vary over time with changing market conditions. Accordingly, the margins associated with our bulk purchases will fluctuate from period to period.

Crude Oil Sales. The marketing of crude oil is complex and requires current detailed knowledge of crude oil sources and end markets and a familiarity with a number of factors including grades of crude oil, individual refinery demand for specific grades of crude oil, area market price structures for the different grades of crude oil, location of customers, availability of transportation facilities and timing and costs (including storage) involved in delivering crude oil to the appropriate customer. We sell our crude oil to major integrated oil companies, independent refiners and other resellers in various types of sale and exchange transactions. The majority of these contracts are at market prices and have terms ranging from one month to three years.

We establish a margin for crude oil we purchase by selling crude oil for physical delivery to third-party users, such as independent refiners or major oil companies, or by entering into a future delivery obligation with respect to futures contracts on the NYMEX or over-the-counter. Through these transactions, we seek to maintain a position that is substantially balanced between crude oil purchases and sales and future delivery obligations. From time to time, we enter into various types of sale and exchange transactions including fixed price delivery contracts, floating price collar arrangements, financial swaps and crude oil futures contracts as hedging devices. Except for pre-defined inventory positions, our policy is generally to purchase only crude oil for which we have a market, to structure our sales contracts so that crude oil price fluctuations do not materially affect the segment profit we receive, and to not acquire and hold crude oil, futures contracts or other derivative products for the purpose of speculating on crude oil price changes that might expose us to indeterminable losses. In November 1999, we discovered a significant violation of this policy. As a result, we incurred an aggregate loss of approximately \$181 million in unauthorized trading losses, including associated costs and legal expenses.

Crude Oil Exchanges. We pursue exchange opportunities to enhance margins throughout the gathering and marketing process. When opportunities arise to increase our margin or to acquire a grade of crude oil that more closely matches our physical delivery requirement or the preferences of our refinery customers, we exchange physical crude oil with third parties. These exchanges are effected through contracts called exchange or buy-sell agreements. Through an exchange agreement, we agree to buy crude oil that differs in terms of geographic location, grade of crude oil or physical delivery schedule from crude oil we have available for sale. Generally, we enter into exchanges to acquire crude oil at locations that are closer to our end markets, thereby reducing transportation costs and increasing our margin. We also exchange our crude oil to be physically delivered at a later date, if the exchange is expected to result in a higher margin net of storage costs, and enter into exchanges based on the grade of crude oil, which includes such factors as sulfur content and specific gravity, in order to meet the quality specifications of our physical delivery contracts.

Producer Services. Crude oil purchasers who buy from producers compete on the basis of competitive prices and highly responsive services. Through our team of crude oil purchasing representatives, we maintain ongoing relationships with producers in the United States and Canada. We believe that our ability to offer high-quality field and administrative services to producers is a key factor in our ability to maintain volumes of purchased crude oil and to obtain new volumes. Field services include efficient gathering capabilities, availability of trucks, willingness to construct gathering pipelines where economically justified, timely pickup of crude oil from tank batteries at the lease or production point, accurate measurement of crude oil volumes received, avoidance of spills and effective management of pipeline deliveries. Accounting and other administrative services include securing

division orders (statements from interest owners affirming the division of ownership in crude oil purchased by us), providing statements of the crude oil purchased each month, disbursing production proceeds to interest owners, and calculation and payment of ad valorem and production taxes on behalf of interest owners. In order to compete effectively, we must maintain records of title and division order interests in an accurate and timely manner for purposes of making prompt and correct payment of crude oil production proceeds, together with the correct payment of all severance and production taxes associated with such proceeds.

Liquefied Petroleum Gas and Other Petroleum Products. We also market and store LPG and other petroleum products in the United States and Canada. These activities include:

- purchasing LPG (primarily propane and butane) from producers at gas plants and in bulk at major pipeline terminal points and storage locations;
- transporting the LPG via common carrier pipelines, railcars and trucks to our own terminals and third party facilities for subsequent resale by them to retailers and other wholesale customers; and
- exchanging product to other locations to maximize margins and /or to meet contract delivery requirements.

We purchase LPG from numerous producers and have established long-term, broad based relationships with LPG producers in our areas of operation. We purchase LPG directly from gas plants, major pipeline terminals, refineries and storage locations. Marketing activities for LPG typically consist of smaller volumes and generally higher margin per barrel transactions relative to crude oil.

LPG Purchases. We purchase LPG from producers, refiners, and other LPG marketing companies under contracts that range from immediate delivery to one year in term. In a typical producer's or refiner's operation, LPG that is produced at the gas plant or refinery is fractionated into various components including propane and butane and then purchased by us for movement via tank truck, railcar or pipeline.

In addition to purchasing LPG at gas plants or refineries, we also purchase LPG in bulk at major pipeline terminal points and storage facilities from major oil companies, large independent producers or other LPG marketing companies. We purchase LPG in bulk when we believe additional opportunities exist to realize margins further downstream in our LPG distribution chain. The opportunities to earn additional margins vary over time with changing market conditions. Accordingly, the margins associated with our bulk purchases will fluctuate from period to period.

LPG Sales. The marketing of LPG is complex and requires current detailed knowledge of LPG sources and end markets and a familiarity with a number of factors including the various modes and availability of transportation, area market prices and timing and costs of delivering LPG to customers.

We sell LPG primarily to industrial end users and retailers, and limited volumes to other marketers. Propane is sold to small independent retailers who then transport the product via bobtail truck to residential consumers for home heating and to some light industrial users such as forklift operators. Butane is used by refiners for gasoline blending and as a diluent for the movement of conventional heavy oil production. Butane demand for use as heavy oil diluent has increased as supplies of Canadian condensate have declined.

We establish a margin for propane by transporting it in bulk, via various transportation modes, to terminals where we deliver the propane to our retailer customers for subsequent delivery to their individual heating customers. We also create margin by selling propane for future physical delivery to third party users, such as retailers and industrial users. Through these transactions, we seek to maintain a position that is substantially balanced between propane purchases and sales and future delivery

obligations. From time to time, we enter into various types of sale and exchange transactions including floating price collar arrangements, financial swaps and crude oil and LPG-related futures contracts as hedging devices. Except for pre-defined inventory positions, our policy is generally to purchase only LPG for which we have a market, and to structure our sales contracts so that LPG spot price fluctuations do not materially affect the segment profit we receive. Margin is created on the butane purchased by delivering large volumes during the short refinery blending season through the use of our extensive leased railcar fleet and the use of our own storage facilities and third party storage facilities. We also create margin on butane by capturing the difference in price between condensate and butane when butane is used to replace condensate as a diluent for the movement of Canadian heavy oil production. While we seek to maintain a position that is substantially balanced within our LPG activities, as a result of production, transportation and delivery variances as well as logistical issues associated with inclement weather conditions, from time to time we experience net unbalanced positions for short periods of time. In connection with managing these positions and maintaining a constant presence in the marketplace, both necessary for our core business, our policies provide that any net imbalance may not exceed 250,000 barrels. These activities are monitored independently by our risk management function and must take place within predefined limits and authorizations.

LPG Exchanges. We pursue exchange opportunities to enhance margins throughout the marketing process. When opportunities arise to increase our margin or to acquire a volume of LPG that more closely matches our physical delivery requirement or the preferences of our customers, we exchange physical LPG with third parties. These exchanges are effected through contracts called exchange or buy-sell agreements. Through an exchange agreement, we agree to buy LPG that differs in terms of geographic location, type of LPG or physical delivery schedule from LPG we have available for sale. Generally, we enter into exchanges to acquire LPG at locations that are closer to our end markets in order to meet the delivery specifications of our physical delivery contracts.

Credit. Our merchant activities involve the purchase of crude oil and LPG for resale and require significant extensions of credit by our suppliers of crude oil and LPG. In order to assure our ability to perform our obligations under crude oil purchase agreements, various credit arrangements are negotiated with our suppliers. These arrangements include open lines of credit directly with us, and standby letters of credit issued under our senior unsecured revolving credit facility.

When we sell crude oil and LPG, we must determine the amount, if any, of the line of credit to be extended to any given customer. We manage our exposure to credit risk through credit analysis, credit approvals, credit limits and monitoring procedures. If we determine that a customer should receive a credit line, we must then decide on the amount of credit that should be extended.

Because our typical crude oil sales transactions can involve tens of thousands of barrels of crude oil, the risk of nonpayment and nonperformance by customers is a major consideration in our business. We believe our sales are made to creditworthy entities or entities with adequate credit support. Generally, sales of crude oil are settled within 30 days of the month of delivery (in the case of foreign cargoes, typically 10 days after delivery), and pipeline, transportation and terminalling services also settle within 30 days from invoice for the provision of services.

We also have credit risk with respect to our sales of LPG; however, because our sales are typically in relatively small amounts to individual customers, we do not believe that we have material concentration of credit risk. Typically, we enter into annual contracts to sell LPG on a forward basis, as well as sell LPG on a current basis to local distributors and retailers. In certain cases our customers prepay for their purchases, in amounts ranging from approximately \$2 per barrel to 100% of their contracted amounts. Generally, sales of LPG are settled within 30 days of the date of invoice.

Terminalling and Storage Operations

We own approximately 37 million barrels of terminalling and storage assets. Approximately 13.6 million barrels of capacity are used in our GMT&S segment, and the remaining 23.4 million barrels are used in our Pipeline segment. Our storage and terminalling operations increase our margins in our business of purchasing and selling crude oil and also generate revenue through a combination of storage and throughput charges to third parties. Storage fees are generated when we lease tank capacity to third parties. Terminalling fees, also referred to as throughput fees, are generated when we receive crude oil from one connecting pipeline and redeliver crude oil to another connecting carrier in volumes that allow the refinery to receive its crude oil on a ratable basis throughout a delivery period. Both terminalling and storage fees are generally earned from:

- refiners and gatherers that segregate or custom blend crudes for refining feedstocks; and
- pipeline operators, refiners or traders that need segregated tankage for foreign cargoes.

The tankage that is used to support our arbitrage activities positions us to capture margins in a contango market (when the oil prices for future deliveries are higher than the current prices) or when the market switches from contango to backwardation (when the oil prices for future deliveries are lower than the current prices).

Our most significant terminalling and storage asset is our Cushing Terminal located at the Cushing Interchange. The Cushing Interchange is one of the largest wet-barrel trading hubs in the U.S. and the delivery point for crude oil futures contracts traded on the NYMEX. The Cushing Terminal has been designated by the NYMEX as an approved delivery location for crude oil delivered under the NYMEX light sweet crude oil futures contract. As the NYMEX delivery point and a cash market hub, the Cushing Interchange serves as a primary source of refinery feedstock for the Midwest refiners and plays an integral role in establishing and maintaining markets for many varieties of foreign and domestic crude oil. Our Cushing Terminal was constructed in 1993, with an initial tankage capacity of 2 million barrels, to capitalize on the crude oil supply and demand imbalance in the Midwest. The Cushing Terminal is also used to support and enhance the margins associated with our merchant activities relating to our lease gathering and bulk purchasing activities. See "—Gathering and Marketing Operations—Bulk Purchases." Since 1999, we have completed four separate expansion phases, which increased the capacity of the Cushing Terminal to a total of approximately 6.3 million barrels. The Cushing Terminal now consists of fourteen 100,000-barrel tanks, four 150,000-barrel tanks and sixteen 270,000-barrel tanks, all of which are used to store and terminal crude oil. In January 2005, we announced the commencement of our Phase V expansion that will add approximately 1.1 million barrels of storage capacity to our Cushing Terminal. The Cushing Terminal also includes a pipeline manifold and pumping system that has an estimated throughput capacity of approximately 800,000 barrels per day. The Cushing Terminal is connected to the major pipelines and other terminals in the Cushing Interchange through pipelines that range in size from 10 inches to 24 inches in diameter.

The Cushing Terminal is designed to serve the needs of refiners in the Midwest. In order to service an increase in volumes and varieties of foreign and domestic crude oil projected to be transported through the Cushing Interchange, we incorporated certain attributes into the original design of the Cushing Terminal including:

- multiple, smaller tanks to facilitate simultaneous handling of multiple crude varieties in accordance with normal pipeline batch sizes;
- dual header systems connecting most tanks to the main manifold system to facilitate efficient switching between crude grades with minimal contamination;

- bottom drawn sumps that enable each tank to be efficiently drained down to minimal remaining volumes to minimize crude oil contamination and maintain crude oil integrity during changes of service;
- mixer(s) on each tank to facilitate blending crude oil grades to refinery specifications; and
- a manifold and pump system that allows for receipts and deliveries with connecting carriers at their maximum operating capacity.

As a result of incorporating these attributes into the design of the Cushing Terminal, we believe we are favorably positioned to serve the needs of Midwest refiners to handle an increase in the number of varieties of crude oil transported through the Cushing Interchange. The pipeline manifold and pumping system of our Cushing Terminal is designed to support more than 10 million barrels of tank capacity. Our tankage in Cushing ranges in age from less than a year old to approximately 11 years old and the average age is approximately 5 years old. In contrast, we estimate that of the approximately 21 million barrels of remaining tanks in Cushing owned by third parties, the average age is approximately 50 years and of that, approximately 9 million barrels has an average age of over 70 years. We believe that provides us with a competitive advantage over our competitors.

Our Cushing Terminal also incorporates numerous environmental and operational safeguards. We believe that our terminal is the only one at the Cushing Interchange in which each tank has a secondary liner (the equivalent of double bottoms), leak detection devices and secondary seals. The Cushing Terminal is the only terminal at the Cushing Interchange equipped with aboveground pipelines. The Cushing Terminal is operated by a computer system designed to monitor real-time operational data and each tank is cathodically protected. In addition, each tank is equipped with a high-level alarm system to prevent overflows; a double seal floating roof designed to minimize air emissions and prevent the possible accumulation of potentially flammable gases between fluid levels and the roof of the tank; and a foam dispersal system that, in the event of a fire, is fed by a fully automated fire water distribution network.

We also own LPG storage facilities located in Alto, Michigan, Schaefferstown, Pennsylvania and Claremont, New Hampshire. The Alto facility is approximately 20 miles southeast of Grand Rapids. The Alto facility was acquired from Ohio-Northwest Development Inc. in 2003 and is capable of storing over 1.2 million barrels of LPG. The Schaefferstown facility is approximately 65 miles northwest of Philadelphia and is capable of storing over 0.5 million barrels of propane. The Claremont facility is on the Vermont border and has the capacity to store approximately 17,000 barrels of propane. In addition, the Claremont facility has two truck loading stations and two rail unloading stations. We believe these facilities will further support the expansion of our LPG business in Canada and the northern tier of the U.S. as we combine the facilities' existing fee-based storage business with our wholesale propane marketing expertise. In addition, there may be opportunities to expand these facilities as LPG markets continue to develop in the region.

Crude Oil Volatility; Counter Cyclical Balance; Risk Management

Crude oil prices have historically been very volatile and cyclical, with NYMEX benchmark prices ranging from a high of over \$55 per barrel in October 2004 to as low as \$10 per barrel over the last 20 years. Segment profit from terminalling and storage activities is dependent on the crude oil throughput volume, capacity leased to third parties, capacity that we use for our own activities, and the level of other fees generated at our terminalling and storage facilities. Segment profit from our gathering and marketing activities is dependent on our ability to sell crude oil at a price in excess of our aggregate cost. Although margins may be affected during transitional periods, these operations are not directly affected by the absolute level of crude oil prices, but are affected by overall levels of supply and demand for crude oil and relative fluctuations in market related indices.

During periods when supply exceeds the demand for crude oil, the market for crude oil is often in contango, meaning that the price of crude oil for future deliveries is higher than current prices. A contango market has a generally negative impact on marketing margins, but is favorable to the storage business, because storage owners at major trading locations (such as the Cushing Interchange) can simultaneously purchase production at current prices for storage and sell at higher prices for future delivery.

When there is a higher demand than supply of crude oil in the near term, the market is backwardated, meaning that the price of crude oil for future deliveries is lower than current prices. A backwardated market has a positive impact on marketing margins because crude oil gatherers can capture a premium for prompt deliveries. In this environment, there is little incentive to store crude oil as current prices are above future delivery prices.

The periods between a backwardated market and a contango market are referred to as transition periods. Depending on the overall duration of these transition periods, how we have allocated our assets to particular strategies and the time length of our crude oil purchase and sale contracts and storage lease agreements, these transition periods may have either an adverse or beneficial affect on our aggregate segment profit. A prolonged transition from a backwardated market to a contango market, or vice versa (essentially a market that is neither in pronounced backwardation nor contango), represents the most difficult environment for our gathering, marketing, terminalling and storage activities. When the market is in contango, we will use our tankage to improve our gathering margins by storing crude oil we have purchased for delivery in future months that are selling at a higher price. In a backwardated market, we use less storage capacity but increased marketing margins provide an offset to this reduced cash flow. We believe that the combination of our terminalling and storage activities and gathering and marketing activities provides a counter cyclical balance that has a stabilizing effect on our operations and cash flow. References to counter-cyclical balance elsewhere in this report are referring to this relationship between our terminalling and storage activities and our gathering and marketing activities in transitioning crude oil markets.

As use of the financial markets for crude oil has increased by producers, refiners, utilities and trading entities, risk management strategies, including those involving price hedges using NYMEX futures contracts and derivatives, have become increasingly important in creating and maintaining margins. Such hedging techniques require significant resources dedicated to managing these positions. Our risk management policies and procedures are designed to monitor both NYMEX and over-the-counter positions and physical volumes, grades, locations and delivery schedules to ensure that our hedging activities are implemented in accordance with such policies. We have a risk management function that has direct responsibility and authority for our risk policies, our trading controls and procedures and certain other aspects of corporate risk management.

Our policy is to purchase only crude oil for which we have a market, and to structure our sales contracts so that crude oil price fluctuations do not materially affect the segment profit we receive. Except for the controlled trading program discussed below, we do not acquire and hold crude oil futures contracts or other derivative products for the purpose of speculating on crude oil price changes that might expose us to indeterminable losses.

While we seek to maintain a position that is substantially balanced within our crude oil lease purchase and LPG activities, we may experience net unbalanced positions for short periods of time as a result of production, transportation and delivery variances as well as logistical issues associated with inclement weather conditions. In connection with managing these positions and maintaining a constant presence in the marketplace, both necessary for our core business, we engage in a controlled trading program for up to an aggregate of 500,000 barrels of crude oil. This controlled trading activity is monitored independently by our risk management function and must take place within predefined limits and authorizations.

In order to hedge margins involving our physical assets and manage risks associated with our crude oil purchase and sale obligations, we use derivative instruments, including regulated futures and options transactions, as well as over-the-counter instruments. In analyzing our risk management activities, we draw a distinction between enterprise level risks and trading related risks. Enterprise level risks are those that underlie our core businesses and may be managed based on whether there is value in doing so. Conversely, trading related risks (the risks involved in trading in the hopes of generating an increased return) are not inherent in the core business; rather, those risks arise as a result of engaging in the trading activity. We have a Risk Management Committee that approves all new risk management strategies through a formal process. With the exception of the controlled trading program, our approved strategies are intended to mitigate enterprise level risks that are inherent in our core businesses of crude oil gathering and marketing and storage.

Although the intent of our risk-management strategies is to hedge our margin, not all of our derivatives qualify for hedge accounting. In such instances, changes in the fair values of these derivatives will receive mark-to-market treatment in current earnings, and result in greater potential for earnings volatility.

Geographic Data; Financial Information about Segments

See Note 14 "Operating Segments" in "Notes to the Consolidated Financial Statements."

Customers

Marathon Ashland Petroleum ("MAP") accounted for 10%, 12% and 10% of our revenues for each of the three years in the period ended December 31, 2004. BP Oil Supply Company also accounted for 10% of our revenues for the year ended December 31, 2004. No other customers accounted for 10% or more of our revenues during the three years ended December 31, 2004. The majority of the revenues from Marathon Ashland Petroleum and BP Oil Supply Company pertain to our gathering, marketing, terminalling and storage operations. We believe that the loss of these customers would have only a short-term impact on our operating results. There can be no assurance, however, that we would be able to identify and access a replacement market at comparable margins.

Competition

Competition among pipelines is based primarily on transportation charges, access to producing areas and demand for the crude oil by end users. We believe that high capital requirements, environmental considerations and the difficulty in acquiring rights-of-way and related permits make it unlikely that competing pipeline systems comparable in size and scope to our pipeline systems will be built in the foreseeable future. However, to the extent there are already third-party owned pipelines or owners with joint venture pipelines with excess capacity in the vicinity of our operations, we will be exposed to significant competition based on the incremental cost of moving an incremental barrel of crude oil.

We face intense competition in our gathering, marketing, terminalling and storage operations. Our competitors include other crude oil pipeline companies, the major integrated oil companies, their marketing affiliates and independent gatherers, brokers and marketers of widely varying sizes, financial resources and experience. Some of these competitors have capital resources many times greater than ours, and control greater supplies of crude oil.

Regulation

Our operations are subject to extensive regulations. We estimate that we are subject to regulatory oversight by over 70 federal, state, provincial and local departments and agencies, many of which are authorized by statute to issue and have issued laws and regulations binding on the oil pipeline industry,

related businesses and individual participants. The failure to comply with such rules and regulations can result in substantial penalties. The regulatory burden on our operations increases our cost of doing business and, consequently, affects our profitability. However, except for certain exemptions that apply to smaller companies, we do not believe that we are affected in a significantly different manner by these laws and regulations than are our competitors. Following is a discussion of certain laws and regulations affecting us. However, due to the myriad of complex federal, state, provincial and local regulations that may affect us, directly or indirectly, you should not rely on such discussion as an exhaustive review of all regulatory considerations affecting our operations.

Pipeline and Storage Regulation

A substantial portion of our petroleum pipelines and storage tanks in the United States are subject to regulation by the U.S. Department of Transportation ("DOT") with respect to the design, installation, testing, construction, operation, replacement and management of pipeline and tank facilities. In addition, we must permit access to and copying of records, and must make certain reports available and provide information as required by the Secretary of Transportation. Federal pipeline safety rules also require pipeline operators to develop and maintain a written qualification program for individuals performing covered tasks on pipeline facilities. Comparable regulation exists in some states in which we conduct intrastate common carrier or private pipeline operations, as well as in Canada under the National Energy Board ("NEB") and provincial agencies.

Since 2000, the DOT has adopted a series of rules requiring operators of interstate pipelines transporting hazardous liquids or natural gas to develop and follow an integrity management program that provides for continual assessment of the integrity of all pipeline segments that could affect so-called "high consequence areas," including high population areas, areas that are sources of drinking water, ecological resource areas that are unusually sensitive to environmental damage from a pipeline release, and commercially navigable waterways. Segments of our pipelines transporting hazardous liquids in high consequence areas are subject to these DOT rules and therefore obligate us to evaluate pipeline conditions by means of periodic internal inspection, pressure testing, or other equally effective assessment means, and to correct identified anomalies. If, as a result of our evaluation process, we determine that there is a need to provide further protection to high consequence areas, then we will be required to implement additional spill prevention, mitigation and risk control measures for our pipelines. The DOT rules also require us to evaluate and, as necessary, improve our management and analysis processes for integrating available integrity related data relating to our pipeline segments and to remediate potential problems found as a result of the required assessment and evaluation process. Costs associated with this program were approximately \$1.0 million in 2003 and approximately \$5 million in 2004. Based on currently available information, our preliminary estimate for 2005 is approximately \$8 million. The relative increase in program cost over the last few years is primarily attributable to pipeline segments acquired in 2003 and 2004 (including the Link assets), which are subject to the new rules and for which assessment commenced in 2004. Certain of these costs are recurring in nature and thus will impact future periods. We will continue to refine our estimates as information from our assessments is collected. Our estimates do not include the potential costs associated with assets acquired in the future. Although we believe that our pipeline operations are in substantial compliance with currently applicable regulatory requirements, we cannot predict the potential costs associated with additional, future regulation.

The DOT is currently considering expanding the scope of its pipeline regulation to include certain gathering pipeline systems that are not currently subject to regulation. This expanded scope would likely include the establishment of additional pipeline integrity management programs for these newly regulated pipelines. The DOT is in the initial stages of evaluating this initiative and we do not currently know what, if any, impact this will have on our operating expenses. However, we cannot assure you that future costs related to the potential programs will not be material. However, even if the DOT does not

expand the scope of its pipeline regulation to include pipeline systems not currently regulated, we may still need to upgrade or expand our existing pipeline integrity management programs to remain in compliance with the Federal Water Pollution Control Act and other environmental laws. We could be required to spend substantial sums to ensure the integrity of and upgrade our pipeline systems to maintain environmental compliance, and in some cases, we may take pipelines out of service if we believe the cost of upgrades will exceed the value of the pipelines. We cannot provide any assurance as to the ultimate amount or timing of future pipeline integrity expenditures for environmental compliance.

States are largely preempted by federal law from regulating pipeline safety but may assume responsibility for enforcing federal intrastate pipeline regulations and inspection of intrastate pipelines. In practice, states vary considerably in their authority and capacity to address pipeline safety. We do not anticipate any significant problems in complying with applicable state laws and regulations in those states in which we operate.

The DOT has adopted API 653 as the standard for the inspection, repair, alteration and reconstruction of existing crude oil storage tanks subject to DOT jurisdiction (approximately 83% of our 37 million barrels are subject to DOT jurisdiction). API 653 requires regularly scheduled inspection and repair of tanks remaining in service. Full compliance is required by 2009. Costs associated with this program were approximately \$3 million in 2004. Based on currently available information, we anticipate we will spend an approximate average of \$6 million per year from 2005 through 2009 in connection with API 653 compliance activities. Such amounts incorporate the costs associated with the assets acquired in 2003 and 2004. Our estimates do not include the potential costs associated with assets acquired in the future. We will continue to refine our estimates as information from our assessments is collected.

We have instituted security measures and procedures, in accordance with DOT guidelines, to enhance the protection of certain of our facilities from terrorist attack. We cannot assure you that these security measures would fully protect our facilities from a concentrated attack. See "—Operational Hazards and Insurance. "

In Canada, the NEB and provincial agencies such as the Alberta Energy and Utilities Board and the Saskatchewan Industry and Resources have promulgated regulations similar to the domestic pipeline integrity management rules and API 653 standards. We spent approximately \$4.1 million in 2004 in compliance activities. Our preliminary estimate for 2005 is approximately \$5.1 million. In addition, we expect to incur compliance costs under other regulations related to pipeline and storage tank integrity, such as operator competency programs, regulatory upgrades to our operating and maintenance systems and environmental upgrades of buried sump tanks. Our preliminary estimate for such costs for 2005 is approximately \$0.5 million. Certain of these costs are recurring in nature and thus will impact future periods. We will continue to refine our estimates as information from our assessments is collected. Our estimates do not include the potential costs associated with assets acquired in the future. Although we believe that our pipeline operations are in substantial compliance with currently applicable regulatory requirements, we cannot predict the potential costs associated with additional, future regulation.

Asset acquisitions are an integral part of our business strategy. As we acquire additional assets, we may be required to incur additional costs in order to ensure that the acquired assets comply with the regulatory standards in the U.S. and Canada.

Transportation Regulation

General Interstate Regulation. Our interstate common carrier pipeline operations are subject to rate regulation by the FERC under the Interstate Commerce Act. The Interstate Commerce Act

requires that tariff rates for petroleum pipelines, which includes both crude oil pipelines and refined product pipelines, be just and reasonable and non-discriminatory.

State Regulation. Our intrastate pipeline transportation activities are subject to various state laws and regulations, as well as orders of state regulatory bodies.

Canadian Regulation. Our Canadian pipeline assets are subject to regulation by the NEB and by provincial agencies. With respect to a pipeline over which it has jurisdiction, each of these agencies has the power, upon application by a third party, to determine the rates we are allowed to charge for transportation on, and set other terms of access to, such pipeline. In such circumstances, if the relevant regulatory agency determines that the applicable terms and conditions of service are not just and reasonable, the agency can amend the offending provisions of an existing transportation contract.

Energy Policy Act of 1992 and Subsequent Developments. In October 1992, Congress passed the Energy Policy Act of 1992 ("EPAct"), which among other things, required the FERC to issue rules establishing a simplified and generally applicable ratemaking methodology for petroleum pipelines and to streamline procedures in petroleum pipeline proceedings. The FERC responded to this mandate by issuing several orders, including Order No. 561. Beginning January 1, 1995, Order No. 561 enables petroleum pipelines to change their rates within prescribed ceiling levels that are tied to an inflation index. Rate increases made pursuant to the indexing methodology are subject to protest, but such protests must show that the portion of the rate increase resulting from application of the index is substantially in excess of the pipeline's increase in costs. If the indexing methodology results in a reduced ceiling level that is lower than a pipeline's filed rate, Order No. 561 requires the pipeline to reduce its rate to comply with the lower ceiling unless doing so would reduce a rate "grandfathered" by EPAct (see below) below the grandfathered level. A pipeline must, as a general rule, utilize the indexing methodology to change its rates. The FERC, however, retained cost-of-service ratemaking, market based rates, and settlement as alternatives to the indexing approach, which alternatives may be used in certain specified circumstances. The EPAct deemed petroleum pipeline rates in effect for the 365-day period ending on the date of enactment of EPAct that had not been subject to complaint, protest or investigation during that 365-day period to be just and reasonable under the Interstate Commerce Act. Generally, complaints against such "grandfathered" rates may only be pursued if the complainant can show that a substantial change has occurred since the enactment of EPAct in either the economic circumstances of the oil pipeline, or in the nature of the services provided, that were a basis for the rate. EPAct places no such limit on challenges to a provision of an oil pipeline tariff as unduly discriminatory or preferential.

On July 20, 2004, the United States Court of Appeals for the District of Columbia Circuit ("D.C. Circuit") issued its opinion in *BP West Coast Products, LLC v. FERC*, which upheld FERC's determination that the rates of an interstate petroleum products pipeline, SFPP, L.P. ("SFPP"), were grandfathered rates under EPAct and that SFPP's shippers had not demonstrated substantially changed circumstances that would justify modification of those rates. The court also vacated the portion of the FERC's decision applying the *Lakehead* policy, under which the FERC allowed a regulated entity organized as a master limited partnership to include in its cost-of-service an income tax allowance to the extent that entity's unitholders were corporations subject to income tax. On December 2, 2004, the FERC issued a Notice of Inquiry that called for comments regarding whether *BP West Coast* applies broadly or only to the specific facts of that case. We are uncertain what action the FERC ultimately will take in response to the court's disapproval of the FERC's *Lakehead* policy and what effect, if any, such action might have on our rates should they be challenged.

Additionally, in *BP West Coast*, the court remanded to the FERC the issue of whether SFPP's revised cost-of-service without a tax allowance would qualify as a substantially changed circumstance that would justify modification of SFPP's rates. Because the court remanded to the FERC and because the FERC's ruling on the substantially changed circumstances issue will focus on the facts and record presented to it, it is not clear what impact, if any, the opinion will have on our rates or on the rates of other FERC-jurisdictional pipelines organized as tax pass-through entities. Moreover, it is not clear to what extent FERC's actions taken in response to *BP West Coast* will be challenged and, if so, whether they will withstand further FERC or judicial review.

In a subsequent FERC proceeding involving SFPP, certain shippers again challenged SFPP's grandfathered rates on the basis of substantially changed circumstances since the passage of EPAct. On March 26, 2004, the FERC issued an order in that case, finding that some of SFPP's rates were not grandfathered and that there were substantially changed circumstances on certain of their systems. Several of the participants in the proceeding have requested rehearing of the FERC's order, and several participants have filed petitions with the D.C. Circuit for review of the order. FERC and court action on those petitions is pending. We are uncertain whether FERC's order will remain intact and, if it does, what effect, if any, that order might have on our grandfathered rates should they be challenged.

Our Pipelines. The FERC generally has not investigated rates on its own initiative when those rates have not been the subject of a protest or complaint by a shipper. Substantially all of our segment profit on transportation is produced by rates that are either grandfathered or set by agreement with one or more shippers.

Trucking Regulation

We operate a fleet of trucks to transport crude oil and oilfield materials as a private, contract and common carrier. We are licensed to perform both intrastate and interstate motor carrier services. As a motor carrier, we are subject to certain safety regulations issued by the Department of Transportation. The trucking regulations cover, among other things, driver operations, maintaining log books, truck manifest preparations, the placement of safety placards on the trucks and trailer vehicles, drug and alcohol testing, safety of operation and equipment, and many other aspects of truck operations. We are also subject to the Occupational Safety and Health Act, as amended ("OSHA"), with respect to our trucking operations.

Our trucking assets in Canada are subject to regulation by both federal and provincial transportation agencies in the provinces in which they are operated. These regulatory agencies do not set freight rates, but do establish and administer rules and regulations relating to other matters including equipment and driver licensing, equipment inspection, hazardous materials and safety.

Cross Border Regulation

As a result of our Canadian acquisitions and cross border activities, we are subject to regulatory matters including export licenses, tariffs, Canadian and U.S. customs and tax issues and toxic substance certifications. Regulations include the Short Supply Controls of the Export Administration Act, the North American Free Trade Agreement and the Toxic Substances Control Act. Violations of these license, tariff and tax reporting requirements could result in the imposition of significant administrative, civil and criminal penalties. Furthermore, the failure to comply with U.S., Canadian, state, provincial and local tax requirements could lead to the imposition of additional taxes, interest and penalties.

Environmental, Health and Safety Regulation

General

Our operations involving the storage, treatment, processing, and transportation of liquid hydrocarbons including crude oil are subject to stringent federal, state, provincial and local laws and

regulations governing the discharge of materials into the environment or otherwise relating to protection of the environment. As with the industry generally, compliance with these laws and regulations increases our overall cost of business, including our capital costs to construct, maintain and upgrade equipment and facilities. Failure to comply with these laws and regulations may result in the assessment of administrative, civil, and criminal penalties, the imposition of investigatory and remedial liabilities, and even the issuance of injunctions that may restrict or prohibit our operations. Environmental laws and regulations are subject to change, and we cannot provide any assurance that compliance with current and future laws and regulations will not have a material affect on our results of operations or earnings. A discharge of hazardous liquids into the environment could, to the extent such event is not insured, subject us to substantial expense, including both the cost to comply with applicable laws and regulations and any claims made by neighboring landowners and other third parties for personal injury and property damage.

Water

The U.S. Oil Pollution Act ("OPA") and analogous state and Canadian federal and provincial laws subject owners of facilities to strict, joint and potentially unlimited liability for containment and removal costs, natural resource damages, and certain other consequences of an oil spill, where such spill is into navigable waters, along shorelines or in the exclusive economic zone of the U.S. The OPA establishes a liability limit of \$350 million for onshore facilities. However, a party cannot take advantage of this liability limit if the spill is caused by gross negligence or willful misconduct, resulted from a violation of a federal safety, construction, or operating regulation, or if there is a failure to report a spill or cooperate in the cleanup. We believe that we are in substantial compliance with applicable OPA requirements.

The U.S. Clean Water Act and analogous state and Canadian federal and provincial laws impose restrictions and strict controls regarding the discharge of pollutants into navigable waters of the United States and Canada, as well as state and provincial waters. Permits must be obtained to discharge pollutants into these waters. The Clean Water Act imposes substantial potential liability for the removal and remediation of pollutants. Although we can give no assurances, we believe that compliance with existing permits and compliance with foreseeable new permit requirements will not have a material adverse effect on our financial condition or results of operations.

Some states and all provinces maintain groundwater protection programs that require permits for discharges or operations that may impact groundwater conditions. We believe that we are in substantial compliance with any such applicable state requirements.

In addition to the costs described above we could also be required to spend substantial sums to ensure the integrity of and upgrade our pipeline systems as a result of oil spills, and in some cases, we may take pipelines out of service if we believe the cost of upgrades will exceed the value of the pipelines. We cannot provide any assurance as to the ultimate amount or timing of future pipeline integrity expenditures for environmental compliance.

Air Emissions

Our operations are subject to the U.S. Clean Air Act and comparable state and provincial laws. Under these laws, permits may be required before construction can commence on a new source of potentially significant air emissions and operating permits may be required for sources already constructed. We may be required to incur certain capital expenditures in the next several years for air pollution control equipment in connection with obtaining or maintaining permits and approvals for sources of air emissions. While we believe that our operations are in substantial compliance with these laws in those areas in which we operate, we can provide no assurance that future compliance obligations will not have a material adverse effect on our financial condition or results of operations.

Canada is a participant in the Kyoto Protocol of the United Nations Framework Convention on Climate Change. The Kyoto Protocol requires participating developed nations such as Canada to reduce their emissions of carbon dioxide and other "greenhouse gases" to five percent below 1990 levels by 2012. As a result, already stringent air emissions regulations applicable to our operations in Canada will be replaced, by 2010, with even stricter requirements. We are currently monitoring the impact on our operations of proposed changes in regulations that will be necessary as a result of Canada's participation in the Protocol.

Solid Waste

We generate wastes, including hazardous wastes, that are subject to the requirements of the federal Resource Conservation and Recovery Act ("RCRA") and comparable state and provincial laws. We are not required to comply with a substantial portion of the RCRA requirements because our operations generate primarily oil and gas wastes, which currently are excluded from consideration as RCRA hazardous wastes. However, it is possible that in the future the exclusion of oil and gas wastes from regulation as RCRA hazardous wastes may be eliminated, in which event, our wastes as well as the wastes of our competitors in the oil and gas industry will be subject to more rigorous and costly disposal requirements, resulting in additional capital expenditures or operating expenses for us and the industry in general.

Hazardous Substances

The federal Comprehensive Environmental Response, Compensation and Liability Act, as amended ("CERCLA"), also known as "Superfund," and comparable state and provincial laws impose liability, without regard to fault or the legality of the original act, on certain classes of persons that contributed to the release of a "hazardous substance" into the environment. These persons include the owner or operator of the site or sites where the release occurred and companies that disposed of, or arranged for the disposal of, the hazardous substances found at the site. Under CERCLA, such persons may be subject to strict joint and several liability for the costs of cleaning up the hazardous substances that have been released into the environment, for damages to natural resources, and for the costs of certain health studies. It is not uncommon for neighboring landowners and other third parties to file claims for personal injury and property damage allegedly caused by hazardous substances or other pollutants released into the environment. In the course of our ordinary operations, we may generate waste that falls within CERCLA's definition of a "hazardous substance," in which event we may be held jointly and severally liable under CERCLA for all or part of the costs required to clean up sites at which such hazardous substances have been released into the environment.

OSHA

We are subject to the requirements of OSHA, and comparable state statutes that regulate the protection of the health and safety of workers. In addition, the OSHA hazard communication standard requires that certain information be maintained about hazardous materials used or produced in operations and that this information be provided to employees, state and local government authorities and citizens. We believe that our operations are in substantial compliance with OSHA requirements, including general industry standards, record keeping requirements and monitoring of occupational exposure to regulated substances. OSHA has also been given jurisdiction over enforcement of legislation designed to protect employees who provide evidence in fraud cases from retaliation by their employer.

Similar regulatory requirements exist in Canada under the federal and provincial Occupational Health and Safety Acts and related regulations. The agencies with jurisdiction under these regulations are empowered to enforce them through inspection, audit, incident investigation or public or employee complaint. Additionally, recent legislation directly ties corporate accountability to the Criminal Code of Canada. This legislation enables occupational health and safety ("OH&S") regulators to prosecute

organizations and individuals criminally for violations of the regulations. We believe that our operations are in substantial compliance with applicable OH&S requirements.

Endangered Species Act

The federal Endangered Species Act ("ESA") restricts activities that may affect endangered species or their habitats. Although certain of our facilities are in areas that may be designated as habitat for endangered species, we believe that we are in substantial compliance with the ESA. However, the discovery of previously unidentified endangered species could cause us to incur additional costs or operation restrictions or bans in the affected area, which costs, restrictions, or bans could have a material adverse effect on our financial condition or results of operations. Similar regulation (the Species Risk Act) applies to our Canadian operations.

Hazardous Materials Transportation Requirements

The DOT regulations affecting pipeline safety require pipeline operators to implement measures designed to reduce the environmental impact of oil discharge from onshore oil pipelines. These regulations require operators to maintain comprehensive spill response plans, including extensive spill response training for pipeline personnel. In addition, DOT regulations contain detailed specifications for pipeline operation and maintenance. We believe our operations are in substantial compliance with such regulations. See "—Regulation—Pipeline and Storage Regulation."

Environmental Remediation

We currently own or lease properties where hazardous liquids, including hydrocarbons, are being or have been handled. These properties and the hazardous liquids or associated generated wastes disposed thereon may be subject to CERCLA, RCRA and analogous state and Canadian federal and provincial laws. Under such laws, we could be required to remove or remediate hazardous liquids or associated generated wastes (including wastes disposed of or released by prior owners or operators), to clean up contaminated property (including contaminated groundwater) or to perform remedial operations to prevent future contamination.

We maintain insurance of various types with varying levels of coverage that we consider adequate under the circumstances to cover our operations and properties. The insurance policies are subject to deductibles and retention levels that we consider reasonable and not excessive. Consistent with insurance coverage generally available in the industry, in certain circumstances our insurance policies provide limited coverage for losses or liabilities relating to gradual pollution, with broader coverage for sudden and accidental occurrences.

In addition, we have entered into indemnification agreements with various counterparties in conjunction with several of our acquisitions. Allocation of environmental liability is an issue negotiated in connection with each of our acquisition transactions. In each case, we make an assessment of potential environmental exposure based on available information. Based on that assessment and relevant economic and risk factors, we determine whether to negotiate an indemnity, what the terms of any indemnity should be (for example, minimum thresholds or caps on exposure) and whether to obtain insurance, if available. In some cases, we have received contractual protections in the form of environmental indemnifications from several predecessor operators for properties acquired by us that are contaminated as a result of historical operations. These contractual indemnifications typically are subject to specific monetary requirements that must be satisfied before indemnification will apply and have term and total dollar limits.

The acquisitions we completed in 2003 and 2004 include a variety of provisions dealing with the allocation of responsibility for environmental costs that range from no or limited indemnities from the sellers to indemnification from sellers with defined limitations on their maximum exposure. We have

not obtained insurance for any of the conditions related to our 2003 acquisitions, and only in limited circumstances for our 2004 acquisitions.

For instance, in connection with the Link acquisition, we identified a number of environmental liabilities, for which we received a purchase price reduction from Link. A substantial portion of these environmental liabilities are associated with the former Texas New Mexico ("TNM") pipeline assets. On the effective date of the acquisition, we and TNM entered into a cost-sharing agreement whereby, on a tiered basis, we will bear \$11 million of the first \$20 million of pre-May 1999 environmental issues. We will also bear the first \$25,000 per site for new sites which were not identified at the time we entered into the agreement (capped at 100 sites). TNM will pay all costs in excess of \$20 million (excluding the deductible for new sites). TNM's obligations are guaranteed by Shell Oil Products ("SOP"). We recorded a reserve for environmental liabilities of approximately \$17.0 million in connection with the Link acquisition.

In connection with the acquisition of certain crude oil transmission and gathering assets from SOP in 2002, Shell purchased an environmental insurance policy covering known and unknown environmental matters associated with operations prior to closing. We are a named beneficiary under the policy, which has a \$100,000 deductible per site, an aggregate coverage limit of \$70 million, and expires in 2012. Shell has recently made a claim against the policy; however, we do not believe that the claim will substantially reduce our coverage under the policy.

In connection with our 1999 acquisition of Scurlock Permian LLC from MAP, we were indemnified by MAP for any environmental liabilities attributable to Scurlock's business or properties which occurred prior to the date of the closing of the acquisition. This indemnity applied to claims that exceeded \$25,000 individually and \$1.0 million in the aggregate. For the indemnity to apply, we were required to assert any claims on or before May 15, 2003. In conjunction with the expiration of this indemnity, we reached agreement with respect to MAP's remaining indemnity obligations. Under the terms of this agreement, MAP will continue to remain obligated for liabilities associated with two Superfund sites at which it is alleged that Scurlock Permian deposited waste oils. In addition, MAP paid us \$4.6 million cash as satisfaction of its obligations with respect to other sites. During 2002, we had reassessed previous investigations and completed environmental studies related to environmental conditions associated with our 1999 acquisitions. As a result of that reassessment, we established an additional reserve of \$1.2 million.

Other assets we have acquired or will acquire in the future may have environmental remediation liabilities for which we are not indemnified. We have in the past experienced and in the future will likely experience releases of crude oil into the environment from our pipeline and storage operations, or discover releases that were previously unidentified. Although we maintain a program designed to prevent and, as applicable, to detect and address such releases promptly, damages and liabilities incurred due to environmental releases from our assets may substantially affect our business.

At December 31, 2004, our reserve for environmental liabilities totaled approximately \$19.8 million (approximately \$12.7 million of this reserve is related to liabilities assumed as part of the Link acquisition). Approximately \$9.3 million of our environmental reserve is classified as current and \$10.5 million is classified as long-term. At December 31, 2004, we have recorded receivables totaling approximately \$6.3 million for amounts recoverable under insurance and from third parties under indemnification agreements.

In some cases, the actual cash expenditures may not occur for three to five years. We believe that this reserve is adequate, and in conjunction with our indemnification arrangements, should prevent remediation costs from having a material adverse effect on our financial condition, results of operations, or cash flows. Our estimates used in these reserves are based on all known facts at the time and our assessment of the ultimate outcome. Among the many uncertainties that impact our estimates are the necessary regulatory approvals for, and potential modification of, our remediation plans, the

limited amount of data available upon initial assessment of the impact of soil or water contamination, changes in costs associated with environmental remediation services and equipment and the possibility of existing legal claims giving rise to additional claims. Therefore, no assurances can be made that any costs incurred in excess of this reserve or outside of the indemnifications would not have a material adverse effect on our financial condition, results of operations, or cash flows.

Operational Hazards and Insurance

Pipelines, terminals, trucks or other facilities or equipment may experience damage as a result of an accident or natural disaster. These hazards can cause personal injury and loss of life, severe damage to and destruction of property and equipment, pollution or environmental damage and suspension of operations. Since we and our predecessors commenced midstream crude oil activities in the early 1990s, we have maintained insurance of various types and varying levels of coverage that we consider adequate under the circumstances to cover our operations and properties. The insurance policies are subject to deductibles and retention levels that we consider reasonable and not excessive. However, such insurance does not cover every potential risk associated with operating pipelines, terminals and other facilities, including the potential loss of significant revenues. Consistent with insurance coverage generally available to the industry, in certain circumstances our insurance policies provide limited coverage for losses or liabilities relating to gradual pollution, with broader coverage for sudden and accidental occurrences. Over the last several years, our operations have expanded significantly, with total assets increasing over 400% since the end of 1998. At the same time that the scale and scope of our business activities have expanded, the breadth and depth of the available insurance markets have contracted. Notwithstanding what we believe is a favorable claims history, the overall cost of such insurance as well as the deductibles and overall retention levels that we maintain have increased. As a result, we have elected to self insure more activities against certain of these operating hazards and expect this trend will continue in the future. Certain aspects of these conditions were exacerbated by the events of September 11, 2001, and their overall effect on the insurance industry have adversely impacted the availability and cost of certain coverages. Due to these events, insurers have excluded acts of terrorism and sabotage from our insurance policies and on certain of our key assets, we have elected to purchase a separate insurance policy for acts of terrorism and sabotage.

Since the terrorist attacks, the United States Government has issued numerous warnings that energy assets, including our nation's pipeline infrastructure, may be future targets of terrorist organizations. These developments expose our operations and assets to increased risks. We have instituted security measures and procedures in conformity with DOT guidance. We will institute, as appropriate, additional security measures or procedures indicated by the DOT or the Transportation Safety Administration. However, we cannot assure you that these or any other security measures would protect our facilities from a concentrated attack. Any future terrorist attacks on our facilities, those of our customers and, in some cases, those of our competitors, could have a material adverse effect on our business, whether insured or not.

The occurrence of a significant event not fully insured, indemnified or reserved against, or the failure of a party to meet its indemnification obligations, could materially and adversely affect our operations and financial condition. We believe we are adequately insured for public liability and property damage to others with respect to our operations. We believe that our levels of coverage and retention are generally consistent with those of similarly situated companies in our industry. With respect to all of our coverage, no assurance can be given that we will be able to maintain adequate insurance in the future at rates we consider reasonable, or that we have established adequate reserves to the extent that such risks are not insured.

Title to Properties and Rights-of-Way

We believe that we have satisfactory title to all of our assets. Although title to such properties are subject to encumbrances in certain cases, such as customary interests generally retained in connection with acquisition of real property, liens related to environmental liabilities associated with historical operations, liens for current taxes and other burdens and minor easements, restrictions and other encumbrances to which the underlying properties were subject at the time of acquisition by our predecessor or us, we believe that none of these burdens will materially detract from the value of such properties or from our interest therein or will materially interfere with their use in the operation of our business.

Substantially all of our pipelines are constructed on rights-of-way granted by the apparent record owners of such property and, in some instances, such rights-of-way are revocable at the election of the grantor. In many instances, lands over which rights-of-way have been obtained are subject to prior liens that have not been subordinated to the right-of-way grants. In some cases, not all of the apparent record owners have joined in the right-of-way grants, but in substantially all such cases, signatures of the owners of majority interests have been obtained. We have obtained permits from public authorities to cross over or under, or to lay facilities in or along water courses, county roads, municipal streets and state highways, and in some instances, such permits are revocable at the election of the grantor. We have also obtained permits from railroad companies to cross over or under lands or rights-of-way, many of which are also revocable at the grantor's election. In some cases, property for pipeline purposes was purchased in fee. All of the pump stations are located on property owned in fee or property under leases. In certain states and under certain circumstances, we have the right of eminent domain to acquire rights-of-way and lands necessary for our common carrier pipelines.

Some of the leases, easements, rights-of-way, permits and licenses transferred to us, upon our formation in 1998 and in connection with acquisitions we have made since that time, required the consent of the grantor to transfer such rights, which in certain instances is a governmental entity. We believe that we have obtained such third party consents, permits and authorizations as are sufficient for the transfer to us of the assets necessary for us to operate our business in all material respects as described in this report. With respect to any consents, permits or authorizations that have not yet been obtained, we believe that such consents, permits or authorizations will be obtained within a reasonable period, or that the failure to obtain such consents, permits or authorizations will have no material adverse effect on the operation of our business.

Employees

To carry out our operations, our general partner or its affiliates employed approximately 1,950 employees at December 31, 2004. None of the employees of our general partner were represented by labor unions, and our general partner considers its employee relations to be good.

Summary of Tax Considerations

The tax consequences of ownership of common units depends in part on the owner's individual tax circumstances. However, the following is a brief summary of material tax consequences of owning and disposing of common units.

Partnership Status; Cash Distributions

We are classified for federal income tax purposes as a partnership based upon our meeting certain requirements imposed by the Internal Revenue Code (the "Code"), which we must meet each year. The owners of common units are considered partners in the Partnership so long as they do not loan their common units to others to cover short sales or otherwise dispose of those units. Accordingly, we pay no federal income taxes, and a common unitholder is required to report on the unitholder's federal income tax return the unitholder's share of our income, gains, losses and deductions. In general, cash

distributions to a common unitholder are taxable only if, and to the extent that, they exceed the tax basis in the common units held.

Partnership Allocations

In general, our income and loss is allocated to the general partner and the unitholders for each taxable year in accordance with their respective percentage interests in the Partnership (including, with respect to the general partner, its incentive distribution right), as determined annually and prorated on a monthly basis and subsequently apportioned among the general partner and the unitholders of record as of the opening of the first business day of the month to which they relate, even though unitholders may dispose of their units during the month in question. A unitholder is required to take into account, in determining federal income tax liability, the unitholder's share of income generated by us for each taxable year of the Partnership ending within or with the unitholder's taxable year, even if cash distributions are not made to the unitholder. As a consequence, a unitholder's share of our taxable income (and possibly the income tax payable by the unitholder with respect to such income) may exceed the cash actually distributed to the unitholder by us. At any time incentive distributions are made to the general partner, gross income will be allocated to the recipient to the extent of those distributions.

Basis of Common Units

A unitholder's initial tax basis for a common unit is generally the amount paid for the common unit. A unitholder's basis is generally increased by the unitholder's share of our income and decreased, but not below zero, by the unitholder's share of our losses and distributions.

Limitations on Deductibility of Partnership Losses

In the case of taxpayers subject to the passive loss rules (generally, individuals and closely held corporations), any partnership losses are only available to offset future income generated by us and cannot be used to offset income from other activities, including passive activities or investments. Any losses unused by virtue of the passive loss rules may be fully deducted if the unitholder disposes of all of the unitholder's common units in a taxable transaction with an unrelated party.

Section 754 Election

We have made the election provided for by Section 754 of the Code, which will generally result in a unitholder being allocated income and deductions calculated by reference to the portion of the unitholder's purchase price attributable to each asset of the Partnership.

Disposition of Common Units

A unitholder who sells common units will recognize gain or loss equal to the difference between the amount realized and the adjusted tax basis of those common units. A unitholder may not be able to trace basis to particular common units for this purpose. Thus, distributions of cash from us to a unitholder in excess of the income allocated to the unitholder will, in effect, become taxable income if the unitholder sells the common units at a price greater than the unitholder's adjusted tax basis even if the price is less than the unitholder's original cost. Moreover, a portion of the amount realized (whether or not representing gain) will be ordinary income.

Foreign, State, Local and Other Tax Considerations

In addition to federal income taxes, unitholders will likely be subject to other taxes, such as foreign, state and local income taxes, unincorporated business taxes, and estate, inheritance or intangible taxes that are imposed by the various jurisdictions in which a unitholder resides or in which we do business or own property. We own property and conduct business in Canada as well as in most

states in the United States. A unitholder may be required to file Canadian federal income tax returns and to pay Canadian federal and provincial income taxes, as well as to file state income tax returns and to pay taxes in various states. A unitholder may be subject to penalties for failure to comply with such requirements. In certain states, tax losses may not produce a tax benefit in the year incurred (if, for example, we have no income from sources within that state) and also may not be available to offset income in subsequent taxable years. Some states may require us, or we may elect, to withhold a percentage of income from amounts to be distributed to a unitholder who is not a resident of the state. Withholding, the amount of which may be more or less than a particular unitholder's income tax liability owed to the state, may not relieve the nonresident unitholder from the obligation to file an income tax return. Amounts withheld may be treated as if distributed to unitholders for purposes of determining the amounts distributed by us.

It is the responsibility of each prospective unitholder to investigate the legal and tax consequences, under the laws of pertinent states and localities, including the Canadian provinces and Canada, of the unitholder's investment in us. Further, it is the responsibility of each unitholder to file all U.S. federal, Canadian, state, provincial and local tax returns that may be required of the unitholder.

Ownership of Common Units by Tax-Exempt Organizations and Certain Other Investors

An investment in common units by tax-exempt organizations (including IRAs and other retirement plans), regulated investment companies (mutual funds) and foreign persons raises issues unique to such persons. Virtually all of our income allocated to a unitholder that is a tax-exempt organization is unrelated business taxable income and, thus, is taxable to such a unitholder. Furthermore, no significant amount of our gross income is qualifying income for purposes of determining whether a unitholder will qualify as a regulated investment company, and a unitholder who is a nonresident alien, foreign corporation or other foreign person is regarded as being engaged in a trade or business in the United States as a result of ownership of a common unit and, thus, is required to file federal income tax returns and to pay tax on the unitholder's share of our taxable income. Finally, distributions to foreign unitholders are subject to federal income tax withholding.

Unauthorized Trading Loss

In November 1999, we discovered that a former employee had engaged in unauthorized trading activity that resulted in significant losses and litigation and had a temporary, but material adverse impact on our liquidity and our relationship with our customers. A full investigation into the unauthorized trading activities by outside legal counsel and independent accountants and consultants determined that the vast majority of the losses occurred in 1999, but also extended into 1998 and required restatements of our financial statements for the applicable periods. Including litigation settlement costs, the aggregate losses associated with this event totaled approximately \$181 million. All of the cases were settled and paid. Additionally, based on recommendations from experts involved in the investigation, we made significant enhancements to our systems, policies and procedures and developed and adopted a written policy document and manual of procedures designed to enhance our processes and procedures and improve our ability to detect any activity that might occur at an early stage. We can give no assurance that the above steps will serve to detect and prevent all violations of our trading policy; however, we believe that such steps substantially reduce the possibility of a recurrence of unauthorized trading activities, and that any material unauthorized trading that does occur would be detected at an early stage.

Available Information

We make available free of charge on our website (www.paalp.com) our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file the material with, or furnish it to, the Securities and Exchange

Commission. We also have on our website our Code of Ethics for Senior Financial Officers, our Code of Business Conduct and our Governance Guidelines. Any waiver of the Code of Ethics for Senior Financial Officers and any waiver of our Code of Business Conduct on behalf of an executive officer or director will also be posted on our website. We also have on our website the committee charters for our Audit, Compensation and Governance Committees. Print versions of the foregoing are available to any unitholder upon request. You can also access Section 16 reports through our website. On September 15, 2004, our Chief Executive Officer submitted to the New York Stock Exchange ("NYSE") the annual certification required by Section 303A.12(a) of the NYSE's Listed Company Manual.

Item 3. Legal Proceedings

Export License Matter. In our gathering and marketing activities, we import and export crude oil from and to Canada. Exports of crude oil are subject to the "short supply" controls of the Export Administration Regulations ("EAR") and must be licensed by the Bureau of Industry and Security (the "BIS") of the U.S. Commerce Department. In 2002, we determined that we may have violated the terms of our licenses with respect to the quantity of crude oil exported and the end-users in Canada. Export of crude oil except as authorized by license is a violation of the EAR. In October 2002, we submitted to the BIS an initial notification of voluntary disclosure. The BIS subsequently informed us that we could continue to export while previous exports were under review. We applied for and received several new licenses allowing for export volumes and end users that more accurately reflect our anticipated business and customer needs. We also conducted reviews of new and existing contracts and implemented new procedures and practices in order to monitor compliance with applicable laws regarding the export of crude oil to Canada. As a result, we subsequently submitted additional information to the BIS in October 2003 and May 2004. In August 2004, we received a request from the BIS for additional information. We have responded to this and subsequent requests, and continue to cooperate fully with BIS officials. At this time, we have received neither a warning letter nor a charging letter, which could involve the imposition of penalties, and no indication of what penalties the BIS might assess. As a result, we cannot reasonably estimate the ultimate impact of this matter.

Alfons Sperber v. Plains Resources Inc., et al. On December 18, 2003, a putative class action lawsuit was filed in the Delaware Chancery Court, New Castle County, entitled *Alfons Sperber v. Plains Resources Inc., et al.* This suit, brought on behalf of a putative class of Plains All American Pipeline, L.P. common unitholders, asserted breach of fiduciary duty and breach of contract claims against us, Plains AAP, L.P., and Plains All American GP LLC and its directors, as well as breach of fiduciary duty claims against Plains Resources Inc. and its directors. (Plains Resources, Inc. is a unitholder and an interest owner in our general partner. See "Security Ownership of Certain Beneficial Owners and Management and Related Unitholders' Matters.") The complaint sought to enjoin or rescind a proposed acquisition of all of the outstanding stock of Plains Resources Inc., as well as declaratory relief, an accounting, disgorgement and the imposition of a constructive trust, and an award of damages, fees, expenses and costs, among other things. This lawsuit has been settled in principle. The court has approved the settlement and, assuming no appeals are filed, the settlement will become final in March 2005.

Pipeline Releases. In December 2004 and January 2005, we experienced two unrelated releases of crude oil that reached rivers located near the sites where the releases originated. In late December 2004, one of our pipelines in West Texas experienced a rupture that resulted in the release of approximately 4,500 barrels of crude oil, a portion of which reached a remote location of the Pecos River. In early January 2005, an overflow from a temporary storage tank located in East Texas resulted in the release of approximately 1,200 barrels of crude oil, a portion of which reached the Sabine River. In both cases, emergency response personnel under the supervision of a unified command structure consisting of representatives of Plains Pipeline, the U.S. Environmental Protection Agency, the Texas

Commission on Environmental Quality and the Texas Railroad Commission conducted clean-up operations at each site. Approximately 4,200 barrels and 980 barrels were recovered from the two respective sites. The unrecovered oil has been or will be removed or otherwise addressed by us in the course of site remediation. Aggregate costs associated with each release, including estimated remediation costs, are estimated at approximately \$1.7 million and \$1.4 million, respectively. We continue to work with the appropriate state and federal environmental authorities in responding to the releases and no enforcement proceedings have been instituted by any governmental authority at this time.

Other. We, in the ordinary course of business, are a claimant and/or a defendant in various other legal proceedings. We do not believe that the outcome of these other legal proceedings, individually and in the aggregate, will have a materially adverse effect on our financial condition, results of operations or cash flows.

Item 4. *Submission of Matters to a Vote of Security Holders*

On January 20, 2005, we held a special meeting of our unitholders. At the meeting, our unitholders approved the following matters:

- A proposal to approve (a) a change in the terms of our Class B common units to provide that each Class B common unit is convertible into one of our common units and (b) the issuance of additional common units upon such conversion (36,457,148 "For," 486,532 "Against," 197,686 "Abstain");
- A proposal to approve (a) a change in the terms of our Class C common units to provide that each Class C common unit is convertible into one of our common units and (b) the issuance of additional common units upon such conversion (36,448,165 "For," 492,779 "Against," 200,422 "Abstain");
- A proposal to approve the terms of our 2005 Long-Term Incentive Plan (the "2005 LTIP"), which provides for awards of common units, options to purchase common units and other rights to our employees, officers and directors (39,864,363 "For," 1,336,929 "Against," 493,061 "Abstain"); and
- Any proposal to adjourn the special meeting to a later date, if necessary, to solicit additional proxies if there were not sufficient votes in favor of the foregoing proposals (38,273,033 "For," 3,185,226 "Against," 235,995 "Abstain").

See "Certain Relationships and Related Transactions—Transactions with Related Parties—Class B Common Units" and "Certain Relationships and Related Transactions—Transactions with Related Parties—Class C Common Units" for a discussion of the Class B and Class C common units.