

DEPARTMENT OF ENERGY
Federal Energy Regulatory Commission

18 CFR Part 342

[Docket No. RM20-14-000]

Five-Year Review of the Oil Pipeline Index

June 18, 2020

AGENCY: Federal Energy Regulatory Commission.

ACTION: Notice of inquiry.

SUMMARY: The Federal Energy Regulatory Commission (Commission) invites comments on its proposed index level used to determine annual changes to oil pipeline rate ceilings. The Commission proposes to use the Producer Price Index for Finished Goods (PPI-FG) plus 0.09% as the index level for the five-year period commencing July 1, 2021. The Commission invites interested persons to submit comments regarding this proposal and any alternative methodologies for calculating the index level.

DATES: Initial Comments are due on or before August 17, 2020, and Reply Comments are due on or before September 11, 2020.

ADDRESSES: You may submit comments, identified by docket number, by any of the following methods:

- Agency Web Site: <http://www.ferc.gov>. Documents created electronically using word processing software should be filed in native applications or print-to-PDF format and not in a scanned format. All supporting workpapers must be submitted with formulas and in a spreadsheet format acceptable under the

Commission's eFiling rules.

- Mail/Hand Delivery: Commenters unable to file comments electronically must mail or hand deliver an original to: Federal Energy Regulatory Commission, Office of the Secretary, 888 First Street, NE, Washington, DC 20426.

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SUPPLEMENTARY INFORMATION:

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Five-Year Review of the Oil Pipeline Index

Docket No. RM20-14-000

NOTICE OF INQUIRY

June 18, 2020

1. The Commission annually applies an index to existing oil pipeline transportation rate ceilings to establish new rate ceiling levels.¹ The Commission reexamines the index level every five years.² In this notice of inquiry (NOI), the Commission invites comments on its proposal to use the Producer Price Index for Finished Goods (PPI-FG)³ plus 0.09% as the index level for the next five years beginning July 1, 2021.⁴ This

¹ Indexing allows oil pipelines to change their tariff rates so long as those rates remain at or below certain ceiling levels. 18 CFR 342.3(a).

² The five-year index review process was established in Order No. 561. *See Revisions to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, Order No. 561, FERC Stats. & Regs. ¶ 30,985 (1993), *order on reh'g*, Order No. 561-A, FERC Stats. & Regs. ¶ 31,000 (1994), *aff'd*, *Ass'n of Oil Pipe Lines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996).

³ The PPI-FG is determined and issued by the Bureau of Labor Statistics, U.S. Department of Labor.

⁴ As provided by 18 CFR 342.3(d)(2), “The index will be calculated by dividing the PPI-FG for the calendar year immediately preceding the index year, by the previous calendar year’s PPI-FG.” Multiplying the rate ceiling effective on June 30 of the index year by the resulting number establishes the new rate ceiling for the year beginning the next day, July 1.

proposal is based on the Kahn Methodology established in Order No. 561 and applied in subsequent five-year index review proceedings.⁵

2. As discussed below, commenters are invited to submit comments regarding the Commission's proposal and any alternative methodologies for calculating the index level. Among other issues, these comments may address different data trimming methodologies and whether and how the index should reflect changes to the Commission's policies regarding income tax costs and return on equity (ROE). The Commission will select a final index level at the conclusion of this proceeding.

I. Background

A. Five-Year Review Process

3. In Order No. 561, the Commission established an indexing methodology that allows oil pipelines to change rates based upon an annual index as opposed to making cost-of-service filings.⁶ The Commission committed to review the index level every five years to ensure that the index level chosen by the Commission adequately reflects changes to industry costs.⁷

⁵ *Five-Year Review of the Oil Pipeline Index*, 153 FERC ¶ 61,312, at PP 5, 12-18 (2015) (2015 Index Review), *aff'd*, *Ass'n of Oil Pipe Lines v. FERC*, 876 F.3d 336 (D.C. Cir. 2017); *Five-Year Review of Oil Pipeline Pricing Index*, 133 FERC ¶ 61,228, at PP 5-9, 60-63 (2010) (2010 Index Review), *order on reh'g*, 135 FERC ¶ 61,172 (2011); *see also Five-Year Review of Oil Pipeline Pricing Index*, 114 FERC ¶ 61,293 (2006) (2005 Index Review); *Five-Year Review of Oil Pipeline Pricing Index*, 102 FERC ¶ 61,195 (2003), *aff'd*, *Flying J Inc. v. FERC*, 363 F.3d 495 (D.C. Cir. 2004).

⁶ Order No. 561, FERC Stats. & Regs. ¶ 30,985 at 30,947.

⁷ *Id.*

4. In Order No. 561 and each successive five-year index review, the Commission has calculated the index level based upon a methodology developed by Dr. Alfred E. Kahn.⁸ The Kahn Methodology uses pipeline data from Form No. 6, page 700⁹ from the prior five-year period to determine an adjustment to be applied to PPI-FG. The calculation is as follows. Each pipeline's cost change on a per barrel-mile basis over the prior five-year period (e.g., the years 2014-2019 in this proceeding) is calculated. In order to remove statistical outliers and spurious data, the resulting data set is trimmed to those oil pipelines in the middle 50% of cost changes. The Kahn Methodology then calculates three measures of the middle 50% central tendency: the median, the mean, and a weighted mean.¹⁰ The Kahn Methodology calculates a composite by averaging these three measures of central tendency and measures the difference between the composite and the PPI-FG over the prior five-year period. The index level is then set at PPI-FG plus (or minus) this differential.

⁸ The Commission's use of the Kahn Methodology has been affirmed by the United States Court of Appeals for the District of Columbia Circuit. *Ass'n of Oil Pipelines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996); *Flying J Inc. v. FERC*, 363 F.3d 495 (D.C. Cir. 2004).

⁹ 2015 Index Review, 153 FERC ¶ 61,312 at P 12 (updating the Commission's calculation of the five-year oil pipeline index to use page 700 data to measure changing barrel-mile costs). Page 700 provides summarized interstate barrel-mile and cost-of-service data consistent with the Commission's cost-of-service methodology. *Id.* PP 12-13, 16.

¹⁰ The weighted mean assigns a different weight to each pipeline's cost change based on the pipeline's total barrel-miles.

B. Developments Since the Most Recent Five-Year Review

5. Since the Commission's most recent review of the index in 2015, the Commission has adopted two major changes to the cost-of-service methodology used to populate page 700 data. First, in 2018, the Commission revised its policy concerning the treatment of income taxes and Accumulated Deferred Income Taxes (ADIT) in the rates of master limited partnership (MLP) pipelines (income tax policy change). Following the remand in *United Airlines, Inc. v. FERC*,¹¹ the Commission determined that an impermissible double recovery results from granting MLP pipelines an income tax allowance when using the discounted cash flow (DCF) methodology.¹² Thus, the Commission instructed MLP oil pipelines to eliminate the income tax allowance from page 700 costs filed on April 18, 2018¹³ and clarified that pipelines eliminating an income tax allowance may also eliminate previously-accumulated ADIT from their costs of service.¹⁴ The Commission further stated that it would incorporate the effects of the income tax policy change on industry-wide oil pipeline costs in the 2020 five-year review of the oil pipeline index level.¹⁵

¹¹ 827 F.3d 122 (D.C. Cir. 2016).

¹² *Inquiry Regarding the Commission's Policy for Recovery of Income Tax Costs*, 162 FERC ¶ 61,227, at P 8 (2018) (Income Tax Policy Statement), *reh'g denied*, 164 FERC ¶ 61,030 (2018) (Income Tax Policy Statement Rehearing Order).

¹³ *Id.* P 46.

¹⁴ Income Tax Policy Statement Rehearing Order, 164 FERC ¶ 61,030 at P 13.

¹⁵ Income Tax Policy Statement, 162 FERC ¶ 61,227 at P 46.

6. Second, on May 21, 2020, the Commission issued a policy statement revising its methodology for determining ROE for interstate natural gas and oil pipelines (ROE policy change).¹⁶ The Commission departed from its longstanding policy of determining pipeline ROEs by relying solely on the discounted cash flow model (DCF) and expanded its methodology to afford equal weighting to the results of DCF and Capital Asset Pricing Model (CAPM) analyses.¹⁷ Moreover, the Commission encouraged oil pipelines to file updated Form No. 6, page 700 data for 2019 reflecting the revised ROE methodology, explaining that such data may help the Commission better estimate industry-wide cost changes for purposes of the five-year index review.¹⁸ The Commission explained that following Office of Management and Budget (OMB) approval of this voluntary information collection pursuant to the Paperwork Reduction Act,¹⁹ the Commission will issue a notice affording pipelines two weeks to file updated Form No. 6, page 700 data reflecting the revised ROE methodology.²⁰

¹⁶ *Inquiry Regarding the Commission's Policy for Determining Return on Equity*, 171 FERC ¶ 61,155 (2020) (ROE Policy Statement).

¹⁷ *Id.* PP 18, 28, 50.

¹⁸ *Id.* P 92. The Commission further explained that pipelines that previously filed Form No. 6 for 2019 and choose to submit updated page 700 data should, in a footnote on the updated page 700, either (a) confirm that their previously filed Form No. 6 was based solely upon the DCF model or (b) provide the real ROE and resulting cost of service based solely upon the DCF model as it was applied to oil pipelines prior to the ROE Policy Statement. *Id.*

¹⁹ 44 U.S.C. 3501-21.

²⁰ ROE Policy Statement, 171 FERC ¶ 61,155 at P 93. The Commission clarified that pipelines that have not filed Form No. 6 for 2019 (e.g., pipelines that have received

II. Commission Proposal

7. We propose PPI-FG plus 0.09% as the index level for the five-year period commencing July 1, 2021. This proposal is based on the Kahn Methodology as applied to Form No. 6, page 700 data from the 2014 through 2019 period. The Commission's calculations are included in workpapers available in this docket on the Commission's eLibrary system.²¹ This proposal is subject to change based upon the updated Form No. 6, page 700 data for 2019 and other potential adjustments as supported by the record in this proceeding.

8. We invite interested persons to submit comments regarding the Commission's proposal and any alternative methodologies for calculating the index level for the five-year period commencing July 1, 2021. Commenters may address issues that include, but are not limited to, different data trimming methodologies and whether, and if so how, the Commission should reflect the effects of cost-of-service policy changes in the calculation of the index level.

an extension of the Form No. 6 filing deadline) should file page 700 data consistent with their previously granted extensions and such filings should be based upon the DCF model, which was the Commission's oil pipeline ROE methodology as of April 20, 2020. *Id.* Moreover, upon OMB approval of the information collection in the ROE Policy Statement, those pipelines will have the opportunity to file updated page 700 data reflecting the Commission's revised oil pipeline ROE methodology. *Id.* n.192.

²¹ See *infra* P 17 (discussing the Commission's eLibrary system).

A. Trimming of the Data Set

9. The Commission calculated the proposed index level by trimming the data set to the middle 50 percent of all oil pipelines, consistent with the Commission's practice in the 2010 and 2015 index reviews.²² We encourage commenters to address whether the Commission should continue to trim the data set to the middle 50 or adopt an alternative approach to data trimming, such as returning to the Commission's prior practice of considering the middle 80²³ or any other approach. Commenters should explain why any such alternative approach is superior to the middle 50 and how it would appropriately address outliers and spurious data that could bias the results in either direction.

B. Cost-of-Service Policy Changes

10. As discussed above, the Commission uses the Kahn Methodology to measure changes in pipeline costs using page 700 data from the prior five-year period. Accordingly, the Commission's proposal incorporates the effects of the income tax policy change on industry-wide oil pipeline costs because this policy change is reflected in pipelines' page 700 data. The Commission's proposal does not include the effects of the ROE policy change because page 700 data reflecting that policy change has yet to be filed. However, as explained in the ROE Policy Statement, the Commission will afford

²² 2015 Index Review, 153 FERC ¶ 61,312 at PP 42-44; 2010 Index Review, 133 FERC ¶ 61,228 at PP 60-63.

²³ See, e.g., 2005 Index Review, 114 FERC ¶ 61,293.

pipelines an opportunity to file this data for consideration in this five-year index review.²⁴

As discussed above, interested persons may address whether, and if so how, the Commission should reflect the effects of cost-of-service policy changes (including the income tax policy change²⁵ and the ROE policy change²⁶) in the calculation of the index level.

11. However, this proceeding is not the appropriate forum to litigate the merits of the policy changes themselves. Litigating the merits of cost-of-service policy changes in the five-year index review is inappropriate for several reasons. First, the index adjusts for and the effects of subsequent changes to the Commission's cost-of-service policies which could be incorporated into the index level in the next five-year index review. Second, litigating policy changes in the five-year index review would be impractical because, whereas the Commission's policies are continually evolving, the five-year index review is based upon a snapshot of pipeline cost changes during the applicable review period. Third, litigating policy changes would improperly complicate and prolong the five-year index review by introducing complex cost-of-service issues that can require years to resolve.²⁷ The Commission must complete this five-year index review in order to

²⁴ ROE Policy Statement, 171 FERC ¶ 61,155 at P 93.

²⁵ Income Tax Policy Statement, 162 FERC ¶ 61,227 at P 8.

²⁶ ROE Policy Statement, 171 FERC ¶ 61,155 at P 2.

²⁷ *See, e.g., SFPP, L.P.*, Opinion No. 511-C, 162 FERC ¶ 61,228, at PP 4-7 (2018) (noting that the litigation culminating in the 2018 income tax policy change began in 2008).

establish the index level in sufficient time for it to be used by pipelines in the index filings to be effective July 1, 2021. Finally, cost-of-service rate proceedings, where participants and the Commission have a full opportunity to develop an evidentiary record, are a more appropriate forum for litigating policy changes than the generic, industry-wide proceeding on the five-year index review.

III. Comment Procedures

12. Initial Comments are due on or before August 17, 2020 and Reply Comments are due on or before September 11, 2020. Comments must refer to Docket No. RM20-14-000, and must include the name of the commenter, the organization they represent, if applicable, and their address.

13. We encourage comments to be filed electronically via the eFiling link on the Commission's web site at <http://www.ferc.gov>. The Commission accepts most standard word processing formats. Documents created electronically using word processing software should be filed in native applications or print-to-PDF format and not in a scanned format. All supporting workpapers must be submitted with formulas and in a spreadsheet format acceptable under the Commission's eFiling rules. Commenters filing electronically do not need to make a paper filing.

14. Commenters that are not able to file comments electronically must send an original of their comments to: Federal Energy Regulatory Commission, Secretary of the Commission, 888 First Street, NE, Washington, DC 20426.

15. All comments will be placed in the Commission's public files and may be viewed, printed, or downloaded remotely as described in the Document Availability section

below. Commenters are not required to serve copies of their comments on other commenters.

IV. Document Availability

16. In addition to publishing the full text of this document in the Federal Register, the Commission provides all interested persons an opportunity to view and/or print the contents of this document via the Internet through the Commission's Home Page (<http://www.ferc.gov>). At this time, the Commission has suspended access to the Commission's Public Reference Room, due to the proclamation declaring a National Emergency concerning the Novel Coronavirus Disease (COVID-19), issued by the President on March 13, 2020.

17. From the Commission's Home Page on the Internet, this information is available on eLibrary. The full text of this document is available on eLibrary in PDF and Microsoft Word format for viewing, printing, and/or downloading. To access this document in eLibrary, type the docket number excluding the last three digits of this document in the docket number field.

18. User assistance is available for eLibrary and the Commission's website during normal business hours. For assistance, please contact the Commission's Online Support at (202) 502-6652 (toll free at 1-866-208-3676) or email at ferconlinesupport@ferc.gov, or the Public Reference Room at (202) 502-8371, TTY (202) 502-8659. E-mail the Public Reference Room at public.referenceroom@ferc.gov.

By direction of the Commission.

Secretary

