

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeen G. Kelly.

Kern River Gas Transmission Company Docket Nos. RP04-274-000,
RP04-274-001 and
RP04-274-002

ORDER ON CLARIFICATION AND REHEARING AND ACCEPTING
COMPLIANCE FILING

(Issued October 13, 2004)

1. Kern River Gas Transmission Company (Kern River) requests clarification or rehearing of the Commission's order of May 28, 2004 suspending its rate increase filing to reflect an increase of approximately \$40.1 million in its jurisdictional cost of service, to a total of approximately \$347.4 million.¹ Kern River requests its 2005 rates be effective January 1, 2005 rather than June 1, 2005. The Rolled In Customer Group² filed a request for clarification that Kern River's filing in Docket No. RP04-274-001 of its supplemental federal income tax data did not require an additional protest. High Desert Power Trust (High Desert) filed a request for rehearing claiming the Commission erred and should have required an immediate reduction in Kern River's Facility Charge.

¹107 FERC ¶ 61, 215 (2004).

²The Rolled-In Customer Group includes Aera Energy LLC, Anadarko E&P Company LP, Anadarko Petroleum Corporation, Chevron USA Inc., Nevada Cogeneration Associates # 1 and # 2, Coral Energy Resources, L.P., Occidental Energy Marketing, Inc., Sempra Energy Trading Corporation, Southwest Gas Corporation and Shell Oil Company (Customer Group).

2. In this order we grant the clarifications requested by Kern River and the Customer Group and deny High Desert's request for rehearing. We continue to find that issues related to Kern River's rates must be dealt with in the investigation and hearing pending before the Administrative Law Judge.

A. Background

3. Kern River requested effective dates of June 1, 2004, and January 1, 2005³ and waiver of the requirement to submit Schedule H-3(2) since Kern River had yet to prepare its 2003 federal income tax return which would reconcile its book depreciable plant, tax depreciable plant and accumulated provision for deferred income taxes.

4. The Commission conditionally accepted and suspended the proposed tariff sheets for five months, to be effective November 1, 2004, and June 1, 2005, as indicated, or an earlier date set by subsequent Commission order, subject to refund, and the outcome of a hearing. Further, the Commission denied Kern River's requested waiver of section 154.312(m)(2) of the Commission's regulations pertaining to the submittal of Schedule H-3(2) and required Kern River to file tax data estimates within 15 days of the date of its order. The Commission found that the order provided the parties with an opportunity to determine just and reasonable rates through the hearing process.

5. Specifically, Protesters had maintained that return on equity, depreciation rates for transmission and compressor engines, inflation factor, rate base, negative salvage amounts, blended IT fuel rate, accumulated deferred income tax, market-oriented revenue credits, gas sales revenue from Park and Loan service, High Desert monthly incremental facility charge, rate design, and throughput adjustments may be inappropriate. Protesters also had argued that Kern River's proposed cost allocation needs to be examined to determine its justness and reasonableness.

6. High Desert had requested that the Commission direct Kern River to file revisions to High Desert's monthly incremental facility charge and upon filing of such re-determination, suspend the rates for a minimal period subject to refund to be effective June 1, 2004. High Desert argued that Kern River had not reflected any change in its currently effective incremental facility charge and that such re-determination was required pursuant to its currently effective negotiated rate

³ Kern River stated that the June 1, 2004, effective date reflects rates calculated based on 366 days for leap year 2004 and that the rates proposed to become effective January 1, 2005, were calculated based on 365 days per year.

contract with Kern River at such time as it filed its next general section 4 rate case. Finally, High Desert had contended that the currently effective monthly incremental facility charge of \$391,432 is approximately 400 percent higher than actual costs needed to operate and support the High Desert lateral.

7. The Commission found that all issues raised by Kern River's filing, including but not limited to those concerning rate derivation and cost-of-service, such as Kern River's proposed cost of service, cost allocation, billing determinants, fuel tracker rates, inflation factor, High Desert incremental facility charge, and other rate issues should be explored at a hearing established by its order. Based upon a review of the filing, the Commission found that the rates proposed reflected increases from test period adjustments which are estimates. Further, the proposed rates reflected a substantial increase in depreciation and a reduction in rate design volumes. Accordingly, the Commission accepted the revised tariff sheets for filing and suspended their effectiveness for five months, and permitted them to become effective, November 1, 2004, subject to refund and conditions.⁴

B. Kern River Request for Clarification or Rehearing

8. Kern River states that it filed two sets of tariff sheets reflecting its proposed rate increase because daily rates during 2004 would be computed on the basis of 366 days and 2005 rates would be based on 365 days. The cost of service and billing determinants used in both cases are the same for Kern River's computation of 2004 and 2005 rates. The Commission suspended the 2004 rates until November 1, 2004 and the 2005 rates until a June 1, 2005 effective date, five months after the requested dates. Kern River now urges that the Commission may have misunderstood the nature of the proposed tariff sheets because the only reason for the 2005 rates being different from the 2004 rates was to reflect the difference between a leap year and a non-leap year computation. Kern River does not contest the five-month suspension of the 2004 rates from June 1, 2004 to November 1, 2004; however, Kern River objects to the five-month suspension of the 2005 rates from January 1, 2005 to June 1, 2005 as needless and duplicative of the 2004 suspension. Therefore, Kern River asks that the May 28, 2004 Order be clarified and the 2005 rates be suspended, subject to refund, effective January 1, 2005, citing the Commission's discretion to order suspensions less than five months where such suspensions would lead to harsh and inequitable results. Kern River contends that the continuation of the 2004 daily rates into 2005 would impose an inequitable revenue loss on Kern River. Should the Commission decline to clarify its order, Kern River requests rehearing.

⁴ The 2005 rates were suspended to be effective June 1, 2005.

9. Upon review of Kern River's request, the Commission concludes that it should exercise its discretion and suspend the 2005 rates to be effective January 1, 2005 subject to refund. Suspension of these rates to June 1, 2005 is unnecessary to protect the ratepayers and the rates will be suspended subject to refund. We accept Kern River's assertion that the only difference between the two sets of rates is the number of days in each year. Because of our clarification, it is unnecessary to consider Kern River's request for rehearing.

C. Customer Group Request for Clarification

10. On April 30, 2004, Kern River requested waiver of the requirement in the regulations to submit Schedule H-3(2) with its rate increase supporting data. Kern River stated that it was unable to prepare a meaningful reconciliation of its book depreciable plant and tax depreciable plant and accumulated provision for deferred income taxes since Kern River had not yet prepared its 2003 federal income tax return. Kern River stated that it did not intend to file its 2003 federal income tax return until September 2004. Kern River claimed that preparation of Schedule H-3(2) using 2002 tax return information would not be meaningful since the 2002 return did not reflect the investment in Kern River's 2003 Expansion or the related bonus depreciation expenses and their effects on accumulated deferred income taxes. Kern River stated that it was willing to submit the schedule when the necessary information to do so became available.

11. The Commission determined that the parties were disadvantaged by the delay in filing Schedule H-3(2). The Commission denied waiver of section 154.312(m)(2) of its regulations pertaining to the submittal of Schedule H-3(2) and required Kern River to file an estimate, within 15 days of the date of the order, justifying its claim of taxes. Kern River was also required to file in this docket and submit Schedule H-3(2) to all parties to this proceeding, based on actuals, at such time Kern River files its 2003 federal tax return.

12. On June 14, 2004, Kern River submitted Schedule H-3(2) to accompany its rate case filing. Kern River made its filing based on estimated amounts for calendar year 2003 of its book and tax depreciable plant and accumulated deferred federal income taxes. Kern River stated it would file final 2003 data after filing its 2003 federal income tax return. The filing was noticed on June 18, 2004 with protests due on June 28, 2004.

13. On June 28, 2004, the Customer Group filed its request for clarification, stating that it assumed this filing will be incorporated with all other evidence and issues set for hearing in the rate case and the failure to file an independent protest to the compliance filing should not be deemed an acceptance of the filing or prejudice Customer Group's ability to object to these matters in the rate case.

14. Whether Kern River's tax data is appropriate as a basis for setting Kern River's rates is a matter to be decided in the hearing. A protest to a compliance filing would be appropriate only if there was an issue as to whether the pipeline complied with the Commission's order.⁵ As specified above, Kern River was directed to file information on its federal tax data within 15 days of the date of issuance of our order. The Customer Group has not asserted that Kern River failed to comply with our order. Kern River complied with our order. Accordingly, protests are not necessary. The filing of estimated tax data by Kern River is not an independent filing requiring protests to be filed by existing parties who might be affected by it in the rate case hearing, as this exhibit along with all other rate case submittals, is subject to the investigation and hearing on Kern River's proposed rates. This ruling also applies to Kern River's filing of actual 2003 tax data after it files its 2003 federal tax return. Clarification of the status of Kern River's June 14th filing is granted for the reasons set out above.

D. High Desert Request for Rehearing

15. High Desert entered into a negotiated rate contract with Kern River on June 5, 2003 and Kern River expended approximately \$29 million to construct a supply lateral to deliver gas to High Desert. The contract contains provisions for determining the rates for the cost of the lateral facility and for the transportation of gas to High Desert, coincident with Kern River's section 4 rate proceedings, such as the filing in this proceeding. High Desert argues that the Commission erred by failing to provide rate relief to High Desert, effective June 1, 2004, the proposed effective date for new rates requested by Kern River, assertedly because High Desert is paying excessive rates during the five-month suspension period. The Commission is asked to rectify its error by directing Kern River to redetermine the Facility Charge, which it states is likely to result in a significant rate decrease, consistent with High Desert's negotiated rate contract dated June 5, 2003 and put the redetermined rates into effect subject to refund pursuant to section 4.2 of the contract. High Desert argues that Kern River's rates are subject to review as each Kern River general rate increase case is filed with the Commission. The current monthly Facility Charge of \$391,432 was set in Kern River's original certificate proceeding and High Desert claims Kern River's current operating and maintenance costs and debt costs are less than those costs used in the certificate proceeding. High Desert also alleges that the allocation of administrative and general expenses is now less and High Desert is being overcharged approximately \$46,500 per month based in part on projected costs.

⁵ See, e.g., *Great Lakes Gas Transmission, L.P.*, 108 FERC ¶ 61,308 at P 11 (2004); *East Tennessee Natural Gas Co.*, 108 FERC ¶ 61,135 at P 4 (2004).

16. While Kern River filed to reduce High Desert's recourse rate, it did not file to reduce the negotiated Facility Charge. High Desert argues that Commission precedent requires rate relief as soon as possible, i.e., June 1, 2004, as required by its contract with Kern River. High Desert points to section 4.1 of its contract as stating that shippers will not be charged in excess of the Facility Charge applied for in any general rate case filing. High Desert also asserts that section 4.1 of the contract requires that the Facility Charge be redetermined at the time the Commission acts on the suspension of Kern River's general rate filing, and as Kern River failed to file a redetermined Facility Charge, the Commission should have ordered Kern River to do so and redetermine the Facility Charge High Desert is paying during the five-month suspension period.

17. The Commission denies rehearing for the following reasons. First, the allegations that Kern River's operating and maintenance and debt costs and its allocated share of administrative and general expenses are significantly less than those used to set its initial Facility Charge in the certificate proceeding are facts in dispute presently pending before the Administrative Law Judge. The Commission does not have the record before it to make findings of fact to satisfy High Desert's request for immediate rate relief. Second, High Desert has asked for an interpretation of its negotiated rate contract on the issue of Kern River's obligation to file a redetermined Facility Charge in conjunction with its section 4 rate change filing. Section 2.3 of the contract states:

The levelized Annual Incremental Facility Charge will be re-determined, if necessary coincident with the effectiveness of new rates pursuant to a general rate case filed by Transporter or coincident with any change to Transporter's system-wide rate.

18. Section 4.1 of the contract states:

General Principles—The true-up and re-determination of the Annual Incremental Facility Charge (and the associated monthly billings) and Rate Schedule KRF-L1 Monthly Reservation Charge will be calculated coincident with a final order in future Transporter general rate cases resolved. . . . The Facility Charge and KRF-L1 Reservation rate will be re-determined at the time rate changes reflected in a general rate case proposing changes in Transporter's rates under Section 4 of the Natural Gas Act are permitted to become effective. . . .

19. Our interpretation of the High Desert contract, specifically, sections 2.3 and 4.1 cited above, leads us to the conclusion that its Facility Charge is to be redetermined at the same time as all other Kern River rates in the pending rate proceeding. Our order of May 28, 2004 specifically suspended the effectiveness of Kern River's rate increases to November 1, 2004.⁶ None of Kern River's rates were effectively changed on June 1, 2004 and therefore there was no obligation on Kern River to change the Facility Charge on that date. High Desert's arguments ignore the provisions of its negotiated rate contract that its Facility Charge changes would be coincident with all other rate changes proposed by Kern River, both as to the suspension rates and the final rates. Kern River's motion to place rates into effect, when filed, on or after November 1, 2004, and January 1, 2005, we anticipate will include a showing of a redetermined Facility Charge, which will be subject to refund until the issuance of a final order in this proceeding.

20. High Desert claims that section 4.2 requires that the redetermined Facility Charge be placed into effect on June 1, 2004. We do not agree. Section 4.2 of the contract, cited by High Desert, states that:

During each rate case billing period (referred to as the "subject to refund" period) Transporter shall initially bill Shipper on the basis of the rates of return on debt and equity and capital structure included in Transporter's subject to refund base tariff rate for this service.

21. Our interpretation of this provision leads us to conclude that the Facility Charge is to be determined at the same time as all of Kern River's transportation rates. Kern River's subject to refund billing period begins on November 1, not June 1, 2004. The parties clearly intended that during the subject to refund period, beginning on November 1, 2004, Kern River will bill High Desert in the same manner as it bills all other shippers.

22. We reject High Desert's claim that the Commission should have reduced the Facility Charge on June 1, 2004. Accordingly, we deny the request for rehearing.

⁶ Order Paragraph (A).

The Commission orders:

(A) Kern River's request for clarification of the May 28, 2004 Order suspending its 2005 rates is granted, as explained above. The Commission accepts and suspends Fourteenth Revised Sheet No. 5, Tenth Revised Sheet No. 5-A, Twelfth Revised Sheet No. 6, Third Revised Sheet No. 7, and Second Revised Sheet No. 8 to Kern River's FERC Gas Tariff, Second Revised Volume No. 1, to be effective January 1, 2005, subject to refund, the outcome of the hearing

established by our prior order, and pursuant to Ordering Paragraph (C) of our prior order in this proceeding.

(B) Customer Group's request for clarification regarding Kern River's filing of tax related data is granted as explained above.

(C) Kern River's compliance filing in Docket No. RP04-274-001 of its supplemental federal income tax data Schedule H-3(2) is accepted subject to our discussion above.

(D) High Desert's request for rehearing is denied for the reasons stated above.

By the Commission.

(S E A L)

Linda Mitry,
Acting Secretary.