120 FERC ¶ 61,223
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Pan Gas Storage, LLC
d/b/a Southwest Gas Storage Company

Docket No. CP07-69-000

ORDER ISSUING CERTIFICATE AND APPROVING ABANDONMENT

(Issued September 7, 2007)

1. On January 26, 2007, Pan Gas Storage, LLC d/b/a Southwest Gas Storage Company (Southwest) filed an application in Docket No. CP07-69-000 under section 7(b) of the Natural Gas Act (NGA) seeking abandonment authority to decrease the certificated total storage capacity of the North Hopeton storage field located in Woods County, Oklahoma, from 21.6 Bcf to 18.1 Bcf and to decrease the field's certificated working gas capacity from 10 Bcf to 3.5 Bcf. Southwest seeks certificate authority under section 7(c) of the NGA to increase its authorized base gas level in the North Hopeton storage field from 11.6 Bcf to 14.6 Bcf and acquire the difference by purchasing 3 Bcf of gas. As discussed below, the Commission finds that approval of Southwest's proposal is required by the public convenience and necessity. Therefore, the Commission grants Southwest's requested authorizations, subject to the conditions set forth below.

I. Background and Proposal

2. Southwest, a limited liability company, is a natural gas company as defined by the NGA and primarily engaged in the business of underground natural gas storage in interstate commerce. Southwest currently operates underground natural gas storage facilities in Kansas, Oklahoma, Illinois, and Michigan.

3. The North Hopeton storage facilities were certificated in 1976.[1] Prior to development as a gas storage field, North Hopeton was a production field. Upon initial

[1] *Panhandle Eastern Pipe Line Company* (Panhandle), 56 FPC 942 (1976). The field was acquired by Southwest from Panhandle in 1998. *Southwest Gas Storage Company*, 85 FERC ¶ 61,328 (1998).

injection of storage volumes into the field, injection rates were lower than expected. Testing revealed that the lower storage zone had been swept by water during previous production operations, altering the formation's gas permeability and making it difficult to move the water back into the aquifer by gas injection. As a result, wells were recompleted in an attempt to isolate the lower zone and measures were taken to force gas into the lower zone and build gas saturation. It was determined that additional injection pressure was needed, and the Commission authorized an increase in the shut-in reservoir pressure from 2,976 psig to 3,515 psig and the installation of additional compression.[2]

4. During the early 1980s, dewatering operations were performed by producing large quantities of water from wells in the middle of the field in an attempt to expand the gas bubble. Over the years, high volumes of water produced in conjunction with withdrawals of storage gas caused the individual wells to rapidly lose gas deliverability. The field's single salt disposal well did not have the capacity to handle high volumes of water for extended periods of time, and the gas withdrawal rate was reduced to limit water production. Subsequently, a second salt water disposal well was added to keep the storage wells in withdrawal status longer. The salt water disposal lines were replaced in 2003, and the original disposal well was recompleted in 2005 to further increase disposal capacity. This work was performed in an effort to increase the field's working gas capacity by improving the facility's ability to dispose of water.

5. Southwest states that despite the above-described efforts, it is unable to reduce the amount of water in the North Hopeton reservoir. Consequently, while the certificated maximum storage volume is 21.6 Bcf, Southwest states that the average total storage capacity since the summer of 2004 has been 18.1 Bcf and the average minimum inventory has been 14.6 Bcf. The difference, 3.5 Bcf, represents the actual average level of working gas that Southwest has been able to recycle. Therefore, while the storage field contains 6.5 Bcf of gas owned by Panhandle Eastern Pipeline Company (Panhandle), Southwest's parent and only firm customer at the North Hopeton storage field, 3 Bcf of Panhandle's gas is actually serving as base gas to sustain the field's actual working capacity of 3.5 Bcf.

6. In view of the above considerations, Southwest seeks abandonment authority to reduce its certificated total storage capacity from 21.6 Bcf to 18.1 Bcf and its certificated maximum working gas level from 10 Bcf to 3.5 Bcf. Further, to sustain the 3.5 Bcf of working gas capacity, Southwest states that base gas levels need to be increased from 11.6 Bcf to 14.6 Bcf and therefore seeks certificate authority to acquire the difference by purchasing 3 Bcf of gas to serve as base gas. Exhibit K to Southwest's application shows a cost estimate of $22.5 million to purchase the 3 Bcf of gas at $7.512 per Dth, the natural gas futures price on January 23, 2007 for April 2007 delivery. Southwest intends to finance the gas purchase by internally generated funds.

[2] *Panhandle Eastern Pipe Line Company*, 11 FERC ¶ 62,208 (1980).

7. Southwest states that approval of its proposal to reflect the actual 3.5 Bcf of working gas capacity at the North Hopeton storage field will not prevent it from meeting its 10 Bcf firm service obligation to Panhandle under Rate Schedule FSS. Southwest explains that it will acquire 6.5 Bcf of off-system working gas storage capacity and transportation capacity from third parties, as authorized under its tariff, to satisfy its firm service obligation to Panhandle.[3] Southwest estimates that its will incur annual costs of approximately $16.5 million to acquire third-party storage and transportation services to provide the remaining 6.5 Bcf of storage service for Panhandle.

II. Notice and Interventions

8. Notice of Southwest's application was published in the *Federal Register* on January 30, 2007.[4] ProLiance Energy, LLC and the Panhandle Complainants[5] filed timely unopposed motions to intervene. Each of the Panhandle Complainants also filed a separate timely motion for leave to intervene in this proceeding. Timely, unopposed motions to intervene are granted by operation of Rule 214 of the Commission's regulations.[6] The Missouri Public Service Commission (MoPSC) filed a timely notice of intervention. Pursuant to Rule 214(a)(2), a state commission is a party to any proceeding upon filing a timely notice of intervention.[7]

9. Missouri Gas Energy, a division of Southern Union Company (MGE); Kansas Gas Service, a division of Oneok, Inc. (Kansas Gas Service); Mewbourne Oil Company (Mewbourne) and the Kansas Corporation Commission (KCC) filed untimely motions for leave to intervene. MGE's, Kansas Gas Service's, Mewbourne's and the KCC's motions show that they have direct and substantial interests in this proceeding. Further, granting intervention at this stage of the proceeding will not cause undue delay or unfair prejudice

[3] Second Revised Sheet No. 147 to FERC Gas Tariff, First Revised Volume No. 1, effective July 8, 2001. *See Southwest Gas Storage Co., et al.*, 96 FERC ¶ 61,025 (2001).

[4] 72 Fed. Reg. 5,690.

[5] The Panhandle Complainants are American Forest & Paper Association; American Iron and Steel Institute; American Public Gas Association; Anadarko Petroleum Corporation and Anadarko Energy Services Company; Citizens Utility Board of Illinois; ConocoPhillips Company; ExxonMobil Gas & Power Marketing Company, a division of Exxon Mobil Corporation; Independent Petroleum Association of America; and Process Gas Consumers Group.

[6] 18 C.F.R. § 385.214(c)(1) (2007).

[7] 18 C.F.R. § 385.214(a)(2) (2007).

to other parties. Therefore, the Commission finds good cause to grant these late motions for intervention.[8]

10. Panhandle Complainants, the MoPSC and the KCC protest Southwest's proposal. The MoPSC and the KCC request a technical conference. Southwest filed an answer to the protests. Although the Commission's Rules of Practice and Procedure do not permit answers to protests, the Commission finds good cause to waive Rule 213(a) to admit Southwest's answer, as its provides information that has assisted in the decision-making process.[9]

III. Protesters' Arguments and Southwest's Answer

A. Panhandle Complainants' Protest

11. Panhandle Complainants are customers of Panhandle, which is Southwest's parent and only firm storage customer. Panhandle holds a firm contract for approximately 61 Bcf of annual storage capacity, essentially Southwest's entire working gas capacity, which Panhandle uses in rendering both transmission services and storage services for its customers.

12. On October 25, 2006, Panhandle Complainants filed a complaint in Docket No. RP07-34-000 alleging that Southwest's rates are unjust and reasonable and requesting that the Commission initiate a proceeding under section 5 of the NGA to investigate Southwest's rates. In Docket No. RP07-34-000, Panhandle Complainants are seeking reductions in Southwest's rates that would result in Panhandle's annual payments to Southwest being reduced by approximately $17 million, savings which the Panhandle Complainants argue should ultimately flow through to Panhandle's customers, including members of the Panhandle Complainants. On December 21, 2006, the Commission issued an order setting the issues raised by Panhandle Complainants for evidentiary hearing before an administrative law judge.[10]

13. Panhandle Complainants assert that the real purpose of Southwest's proposal in this proceeding is to use the associated costs to support its rates being investigated in the on-going section 5 complaint proceeding in Docket No. RP07-34-000. In support of this assertion, Panhandle Complainants state that in 2006 Southwest reported that it had 62

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[8] 18 C.F.R. § 384.214(d) (2007).

[9] 18 C.F.R. § 385.213(a)(2) (2007).

[10] *Panhandle Complainants v. Southwest Gas Storage Company*, 117 FERC ¶ 61,318 (2006).

MMDt of working gas storage capacity but had only cycled approximately 36 MMDt.[11] Based on this information, Panhandle Complainants assert that Southwest had 26 MMDt of unused working gas capacity last year, and that Southwest therefore can meet its firm service obligations to Panhandle without incurring significant costs to purchase additional base gas for the North Hopeton storage field and third-party storage and transportation services. Panhandle Complainants also emphasize that Southwest's periodic capacity and operations reports have not identified the North Hopeton operational problems described in its application in this proceeding.[12] The Panhandle Complainants also emphasize that in recent years Panhandle has not been using all the firm storage service for which it has contracted with Southwest.

14. Even if Southwest's proposal were justified on the grounds that it is necessary in order for Southwest to stand ready to meet all of its firm storage service obligations to Panhandle, the Panhandle Complainants argue that Southwest's application failed to adequately explain and justify its estimated costs to purchase additional base gas for the North Hopeton storage field and to contract for third-party storage and transportation services. The Panhandle Complainants object that Southwest estimated its additional cost of service using a 100 percent equity capital structure and a 13.25 percent rate of return, both of which the Panhandle Complainants are challenging in the section 5 proceeding in response to their complaint in Docket No. RP07-34-000.

15. The Panhandle Complainants also object that Southwest failed to identify the companies that will provide the third-party storage and transportation services or provided assurance that such services will offer the same degree of operational flexibility.

B. The MoPSC's and the KCC's Protests

16. In view of the ongoing section 5 complaint proceeding in Docket No. RP07-34-000, the MoPSC and the KCC, like the Panhandle Complainants, question the timing of Southwest's proposal in this proceeding and whether Southwest really needs to add base gas to its North Hopeton storage field and, in addition, pay for third-party storage and transportation services in order to meet its service obligations to its parent Panhandle. Arguing that the costs associated with this proposal will have a direct impact in the ongoing section 5 proceeding, the MoPSC and the KCC request a technical conference to

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[11] *Citing* Southwest's FERC Financial Report, FERC Form 2A: Annual Report of non-Major Natural Gas Companies and Supplemental Form 3-Q: Quarterly Financial Report at p. 552.1 (filed April 18, 2006).

[12] *Citing* Southwest's annual capacity reports filed on March 1, 2005 and on March 1, 2006 in compliance with Docket No. RM85-1-000. *See, e.g., FERC Stats & Regs* 1982—1985 at ¶ 30,665 (Order No. 436, *et seq*.).

allow the parties to seek additional information to better understand the need for the instant proposal.

C. Southwest's Answer to Protests

17. In its March 1, 2007 answer, Southwest emphasizes that its January 26, 2007 application's description of the North Hopetown storage field's operational history clearly explains why the field's actual working gas capacity is only 3.5 Bcf, notwithstanding all of the efforts over the years to increase working gas to the certificated 10 Bcf level. Southwest also argues that its application clearly explains that it needs to increase its authorized base gas level from 11.6 Bcf to 14.6 Bcf and therefore needs to acquire 3 Bcf of additional base gas to sustain the current 3.5 Bcf level of working gas. Southwest further asserts that the $7.512 per Dth and total estimated costs of $22.5 million to purchase the 3 Bcf of gas are reasonable because it based the costs on the natural gas futures price on January 23, 2007 for April 2007 delivery.

18. Southwest acknowledges that Panhandle has not always requested its full contractual level of storage service, but Southwest emphasizes that it nevertheless is obligated to provide the full contract volumes upon reuest. Since the field's actual working capacity is only 3.5 Bcf and Panhandle's current entitlement is 10 Bcf of storage service, Southwest asserts that it is prudent to seek firm contracts for third-party storage and transportation services for up to 6.5 Bcf. While Southwest estimates annual costs of approximately $16.5 million to arrange for these third-party storage and transportation services, Southwest advises in its answer that it is still negotiating with off-system service providers.[13] However, Southwest is not seeking any authorization here for these services, since it is authorized under its tariff to enter into such agreements.

19. In response to the protesters' speculation that Southwest's real motivation for this proposal is to incur additional costs in support of the cost of service underlying its rates at issue in the section 5 proceeding in docket No. RP07-34-000, Southwest counters that the timing of its application is driven only by the deterioration of the North Hopeton storage field. Southwest states that the rate issues raised by Panhandle Complainants are already

[13] The Commission notes that on June 22, 2007, after the protests and Southwest's answer were filed in this proceeding, Southwest filed testimony in the section 5 proceeding in Docket No. RP07-34-000 that it has entered into a contract with Tenaska Gas Storage, LLC (Tenaska) for sufficient additional storage service to ensure that Southwest will meet its full firm service obligations to Panhandle. Under the contract, Tenaska will provide 5,800,000 Dt of working storage capacity and charge Southwest $1,015,000 per month or $12,180,000 annually. Prepared Answering Testimony of Michael T. Langston on behalf of Southwest Gas Storage Company, at pp. 15 - 17.

at issue in the on-going section 5 rate proceeding, and that proceeding is the proper forum to address such concerns.

IV. Discussion

20. While the North Hopeton storage field's currently certificated maximum storage capacity and working gas capacity are 21.6 Bcf and 10 Bcf, respectively, Southwest clearly describes the operational problems encountered at the North Hopeton storage field. The storage field is limited to its operationally proven total storage capacity of 18.1 Bcf and working gas capacity of 3.5 Bcf, notwithstanding that Southwest and its predecessor, Panhandle, made several attempts to correct the field's water saturation problems. Based on the information provided in the application and responses to two Commission data requests, staff analysis confirms the operational limitations of the North Hopeton storage field.[14] While the protesters question the timing of Southwest's proposal, they do not dispute Southwest's representations regarding the storage field's actual overall capacity and working gas capacity. In view of these considerations, the Commission finds that the public convenience and necessity permit approval of Southwest's abandonment proposal in order to accurately reflect the storage field's capabilities.

21. Further, Southwest explained that it needs to purchase 3 Bcf of gas to increase base gas levels in the North Hopeton storage field to sustain the storage field's current working gas level of 3.5 Bcf. The protesters' skepticism as to whether Southwest needs to purchase this additional base gas is based on their speculation, based on past history, that Panhandle may not need all of the storage capacity for which it has contracted, not because they dispute Southwest's assertion that additional base gas is necessary to maintain the storage field's current 3.5 Bcf working gas level. The Commission agrees with Southwest that prudence requires it to take steps that ensure it can meet the full level of its firm service obligations to Panhandle, regardless whether Panhandle has fully utilized its entitlements in the past. However, if Panhandle Complainants believe that Panhandle has contracted for more storage service than it needs from Southwest, they may raise costs associated with any underutilized capacity as an issue in Panhandle’s next section 4 rate case.

22. The Commission further finds that Southwest’s proposal to purchase the additional 3 Bcf of base gas at $7.512 per Dth is reasonable, in view of Southwest's explanation in its January 26, 2007 application that it based this price on the natural gas futures price on January 23, 2007 for April 2007 delivery. In view of these considerations, the Commission also will grant Southwest certificate authority to increase its authorized base

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[14] Staff data requests were submitted to Southwest on March 29, 2007 and May 1, 2007. Southwest's responses were filed on April 19, 2007 and May 7, 2007.

gas level from 11.6 Bcf to 14.6 Bcf and approve its proposal to acquire the difference by purchasing 3 Bcf of additional base gas.

23. As discussed above, Panhandle Complainants filed a complaint on October 25, 2006 to initiate an investigation of Southwest's rates in Docket No. RP07-34-000. In that section 5 proceeding, Southwest's arguments to defend its currently effective rates have included testimony to support inclusion in rate base of its estimated costs for the additional base gas proposed in this certificate proceeding and its costs for third-party storage and transportation services to stand ready to provide Panhandle with its full contract volumes. Further, on August 1, 2007, Southwest filed under section 4 in Docket No. RP07-541-000 to propose rates based a revised cost of service that also reflects its estimated costs for the additional base gas and third-party services. On August 31, 2007, the Commission issued an order consolidating the section 4 and section 5 proceedings, suspending Southwest's proposed rates until February 1, 2008, and establishing hearing procedures.[15] Accordingly, while the Commission finds in this order that the natural gas futures price that Southwest proposes to rely on reasonably supports its request for section 7 certificate authority to acquire additional base gas, this finding is not a finding that the proposed cost of gas is appropriate for purposes of establishing a just and reasonable rate under section 4 or 5 of the NGA, nor does this finding create a presumption of rolled-in rate treatment for the estimated costs of the additional base gas.[16] Further, while Southwest's tariff makes it unnecessary for it to seek authority to enter into third-party storage and transportation service agreements, the Commission's caveat that this order creates no presumption of rolled-in rate treatment also applies to Southwest's estimated costs to acquire such services.

24. Thus, the Commission's action in this proceeding in no way prejudices the ability of the Panhandle Complainants in the section 5 proceeding to challenge the level of proposed costs to acquire additional base gas and third-party storage and transportation services that Southwest seeks to include in its rates. The Panhandle Complainants may present arguments that Southwest failed to exercise due diligence in securing competitive contracts for the base gas and third-party services, resulting in costs that are unreasonably high. Further, the section 5 proceeding addresses the Panhandle Complainants' arguments that Southwest's 100 percent equity capital structure and 13.25 percent rate of return reflected in its currently effective rates are not appropriate. Any changes to these

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[15] 120 FERC ¶ 61,207 (2007).

[16] *Cf. Columbia Gas Transmission Corporation and Hardy Storage Company*, 113 FERC ¶ 61,118 (2005) at P 55 (finding Hardy Storage Company's valuation of native gas reasonable and appropriate to support approval of its use of native gas as base gas but nevertheless stating that it had an obligation under the NGA to be prudent in incurring costs and that any costs would be subject to review and challenge in its general rate cases).

or other pertinent cost of service factors as a result of the section 5 proceeding will be reflected in Southwest's estimated costs to acquire base gas for the North Hopeton storage field and third-party services to meet its firm service obligations to Panhandle.

25. Based on the above discussion and findings, the Commission finds that there are no disputed issues of fact material to the Commission's determination on the proposal in this proceeding. The Commission therefore will deny the KCC's and the MoPSC’s requests for a technical conference.

26. Because Southwest provides for the abandonment of working gas storage capacity by converting such capacity to base or cushion gas capacity and no construction or ground disturbance is involved, the Commission finds that approval of this proposal qualifies for the categorical exclusion set forth in section 380.4(a)(31) of the regulations. Therefore, environmental review of the proposal is not necessary.

27. The Commission, on its own motion, received and made part of the record in this proceeding all evidence, including the application and exhibits thereto, submitted in support of the authorizations sought herein, and upon consideration of the record,

The Commission orders:

(A) Permission for and approval of the abandonment of 6.5 Bcf of working gas capacity and 3 Bcf of total capacity at the North Hopeton storage field, as described above and in the application, are granted.

(B) Upon the terms and conditions of this order, a certificate of public convenience and necessity is issued to Southwest authorizing it to increase base gas levels in the North Hopeton storage field from 11.6 Bcf to 14.6 Bcf and to acquire 3 Bcf of gas to serve as the additional base gas.

(C) The certificate issued in Ordering Paragraph (B) is conditioned upon Southwest’s compliance with all applicable Commission regulations under the Natural Gas Act, particularly the general terms and conditions set forth in Parts 154, 157 and 284, and paragraphs (a), (e) and (f) of section 157.20 of the regulations.

(D) Southwest shall not operate the North Hopeton storage field above the following certificated levels: Working gas – 3.5 Bcf; Base Gas – 14.6 Bcf; Total Capacity – 18.1 Bcf.

(E) MGE’s Kansas Gas Services’s, Mewbourne’s and the KCC’s untimely motions to intervene are granted.

(F) The KCC's, the MoPSC's and the Panhandle Complainants' protests are denied.

(G) The MoPSC's and the KCC's requests for technical conference are denied.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.