124 FERC ¶ 61,210
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.

East Tennessee Natural Gas, LLC Docket No. RP08-487-000

ORDER ACCEPTING AND SUSPENDING TARIFF SHEETS
SUBJECT TO REFUND AND OTHER CONDITIONS,
AND ESTABLISHING A TECHNICAL CONFERENCE.

(Issued August 29, 2008)

1. On August 1, 2008, East Tennessee Natural Gas, LLC (East Tennessee) filed proposed changes to certain tariff sheets[1] concerning, among other things, timelines and an allocation methodology for available capacity. East Tennessee requested waiver of the Commission's notice requirements in order to permit the tariff sheets to be effective August 1, 2008. Waiver is denied. As discussed below, we accept and suspend East Tennessee's proposal and the instant tariff sheets, subject to refund and other conditions, and the outcome of a technical conference, effective the earlier of a Commission order in this proceeding, or February 1, 2009.

Details of the Filing

2. East Tennessee currently allocates firm service on a "first-come, first-served" basis. In the instant filing, it proposes to switch to a "net present value" (NPV) allocation methodology, in accordance with current regulatory and market conditions and consistent with the Commission's goal of ensuring that capacity is allocated according to its value to shippers in the marketplace.

3. According to East Tennessee's proposed General Terms and Conditions (GT&C) section 5.8(a)(8), once the quantity, rate, and term factors are accounted for, the resulting figure will be multiplied by the creditworthiness factor to determine the final NPV. East Tennessee defines the creditworthiness factor as one (1) minus the bidder's probability of default for the maximum bid term. The bidder's probability of default is determined based on Standard & Poor's most current "Cumulative Average Default Rates by Rating

[1] *See* Appendix for list of tariff sheets.

Modifier" table for a given credit rating and term. East Tennessee states that proposed GT&C section 5.8(a)(8) also allows for bidders to increase the NPV of their bid by posting additional collateral, as specified under GT&C section 6, prior to the end of the open season. East Tennessee states that its creditworthiness calculation is in accordance with Commission precedent.[2]

4. East Tennessee proposes tariff revisions that would permit it to use an NPV methodology to evaluate bids for allocation of expansion capacity and for changes in primary receipt and delivery points. With regard to the allocation of expansion capacity, East Tennessee states that pursuant to proposed GT&C section 5.8(b)(3), it will have the right, but not the obligation, to reserve for a future expansion project any unsubscribed capacity or capacity under expiring or terminating service agreements where such agreements do not have a right of first refusal or the subject shipper does not exercise its right of first refusal. East Tennessee's proposed language sets forth certain requirements for reserving capacity for a future expansion project, including that East Tennessee first hold an open season in which it states that it is planning to reserve the posted capacity for an expansion to the extent that other potential shippers do not purchase the capacity in that open season (reservation open season). East Tennessee states that the instant proposal is consistent with Commission policy and with provisions recently approved for other pipelines.[3] East Tennessee states that proposed GT&C section 5.8(b)(3) further provides that East Tennessee may, in conjunction with the reservation open season posting, elect to conduct a reverse open season for turnback capacity from East Tennessee's existing shippers. East Tennessee shall post a notice of the reverse open season in accordance with the provisions of new GT&C section 5.8(b)(4) no later than 90 days after the close of the open season for the expansion project.

5. Finally, East Tennessee proposes several miscellaneous revisions to its tariff, in order to conform its tariff with the above identified proposals.

6. East Tennessee states that as of the date of the instant filing, it has one request in queue for firm service under the currently effective first-come, first-served methodology pursuant to GT&C section 5.8(a). East Tennessee proposes to grandfather this request for a one year period. East Tennessee states that to the extent the requested capacity

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[2] East Tennessee August 1, 2008 Application at 3, citing *Gas Transmission Northwest Corporation*, 117 FERC ¶ 61,315 (2006).

[3] East Tennessee August 1, 2008 Application at 5, citing *Gas Transmission Northwest Corporation*, 117 FERC ¶ 61,315 (2006), *Texas Gas Transmission, LLC,* 111 FERC ¶ 61,135 (2005), *Tennessee Gas Pipeline Co.*, 84 FERC ¶ 61,304 (1998), *reh'g and clarification*, 86 FERC ¶ 61,066 (1999).

becomes available before August 1, 2009, it will allocate the capacity to the shipper in the existing queue on the date such capacity becomes available and is posted on the LINK System.

Notice, Interventions and Protests

7. Public notice of the filing was issued on August 6, 2008. Interventions and protests were due as provided in section 154.210 of the Commission's regulations.[4] Pursuant to Rule 214,[5] all timely motions to intervene and any motions to intervene out-of-time filed before the issuance date of this order are granted. Granting late intervention at this stage of the proceeding will not disrupt this proceeding or place additional burdens on existing parties. Hess Corporation (Hess) filed a request for clarification and protest. Sequent Energy Management, L.P. (Sequent) filed a protest, and the East Tennessee Group (ETG)[6] filed comments. Nexen Marketing U.S.A., Inc., filed an out-of-time motion to intervene and an out-of-time protest on August 22, 2008. While we accept Nexen's protest, Nexen makes no substantive arguments that differ from those raised by the other parties. East Tennessee also filed a motion to Answer on August 22, which we allow because it aids in the explication of the issues.[7]

Hess Corporation

8. Hess asserts that East Tennessee's proposed creditworthiness/collateral analysis should apply only to non-creditworthy shippers. In support of this position, Hess cites the Commission's Creditworthiness Policy Statement,[8] in which, Hess contends, the Commission only addressed the credit strength and additional collateral that could be required of non-creditworthy shippers. Hess states that the Commission allows pipelines to require non-creditworthy shippers to put up collateral, and that pipelines are allowed to

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[4] 18 C.F.R. § 154.210 (2008).

[5] 18 C.F.R. § 385.214 (2008).

[6] The East Tennessee Group is an ad hoc, voluntary association of 28 jurisdictional customers of East Tennessee, each of which is engaged in the retail distribution of natural gas.

[7] *See* 18 C.F.R. §385.213(a)(2) (2008).

[8] Hess August 13, 2008 Protest at 4, citing *Creditworthiness Standards for Interstate Natural Gas Pipelines*, 111 FERC ¶ 61,412 (2005) (Creditworthiness Policy Statement).

propose additional measures to address their concerns with non-creditworthy shippers.[9] Hess also notes that in *Algonquin Gas Transmission, LLC*,[10] the Commission discussed non-creditworthy shippers' opportunities when posting bids, and found that non-creditworthy shippers can be required to post collateral to protect against default.

9. Hess argues that allowing East Tennessee to apply a creditworthiness/collateral factor in its NPV determination to creditworthy shippers is likely to have a negative impact on the potential pool of shippers that can effectively compete for capacity while also increasing the costs for end-users acquiring service from shippers that may be effectively required to post collateral for their transportation contracts. Hess states that, in constrained markets, creditworthy shippers with lower credit ratings would be severely disadvantaged.

10. Hess asserts that separating the traditional NPV and the creditworthiness/collateral analyses addresses the conflict that it sees between East Tennessee's proposal and the Creditworthiness Policy Statement, Order No. 712,[11] and *Algonquin*. Hess also asserts that determining an amount of collateral that is not disproportionate to the pipeline's risks can be best made only after the traditional NPV best bid is determined and the terms of the traditional NPV best bid are known.

11. Hess argues that separating the traditional NPV analysis and creditworthiness/collateral analyses would equally protect the pipeline while also minimizing the discount adjustment used to determine East Tennessee's rates in future rate cases.

12. Finally, Hess contends that the Commission should also require East Tennessee to clarify (1) the limitations on how much collateral can be posted; and (2) how collateral will be treated during the applicable contract's term. Specifically, Hess argues that the posting of collateral in and of itself should not allow a shipper to be awarded capacity, but instead should only allow a shipper's bid to match the bids of shippers that did not

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[9] Hess August 13, 2008 Protest at 6, citing Creditworthiness Policy Statement at P 15.

[10] *See* 120 FERC ¶ 61,072, at P 26 and P 28 (2007), *cited in* Hess August 13, 2008 Protest at 4.

[11] In Order No. 712, the Commission recognized and approved various arrangements that would benefit the natural gas market by increasing efficiencies and lowering gas costs, with the benefits inuring to consumers. *See Promotion of a More Efficient Capacity Release Market,* Order No. 712, 123 FERC ¶ 61,286, at P 122-123, 126 (2008), *cited in* Hess August 13, 2008 Protest at 8.

post collateral but have higher credit ratings. With respect to how the collateral will be treated, Hess requests clarification as to whether a shipper's posted collateral will be reduced as the shipper's contract term is reduced, and that East Tennessee will pay interest on the collateral during the term of the contract.

Sequent Energy Management, L.P.

13. Sequent protests two aspects of East Tennessee's filing: (1) its use of the creditworthiness factor in determining NPV, and (2) the wording of one clause concerning reverse open seasons. With regard to its creditworthiness proposal, Sequent begins by arguing that East Tennessee is relying on weak precedent. For example, Sequent notes, the *Gas Transmission Northwest Corporation* case settled, so the Commission did not have an opportunity to confirm or reverse its initial order on rehearing.

14. Sequent states that East Tennessee's proposed tariff language makes clear that the creditworthiness factor is a mathematical component to the NPV calculation, on par with rate and term. Sequent protests that the proposal could therefore lead to anomalous instances where a more-creditworthy party could receive capacity over a less-creditworthy party who was nevertheless willing to pay the same or even a greater rate and/or commit to a longer term.

15. Sequent asserts that potential customers with higher credit ratings, will, solely by virtue of East Tennessee's creditworthiness proposal, be granted an automatic, structural bidding advantage over other bidders. As a result, these higher-rated shippers will be free to propose lower rates or shorter bid terms and yet still win bids against lower-rated shippers. Sequent further asserts that lower-rated shippers cannot upgrade their credit rating in any meaningful time frame, and therefore, they will be forced into a collateral bidding process in order to stay competitive.

16. Sequent argues that this result not only subverts the Commission's allocative efficiency goal that underpins the NPV process, but also undermines the Commission's carefully-crafted policy imposing general limits on the amount of collateral that can be demanded of potential shippers by pipelines. Sequent questions the fundamental validity of the creditworthiness factor, and urges the Commission to reject the factor on that basis alone.

17. If the Commission accepts the proposed creditworthiness language, Sequent asserts that it must at a minimum require East Tennessee to clarify that the creditworthiness factor does not apply if the bidding parties are able to meet East Tennessee's first tier creditworthiness standards under Section 3.4 of its tariff's General Terms and Conditions. Sequent states that once East Tennessee has determined that a potential bidder is minimally creditworthy, there is no need to force that party into an

expensive collateral bidding process designed solely to raise its creditworthiness score; rather, capacity should be allocated to minimally creditworthy parties on the basis of rate and term alone.

18. Sequent's second concern is that the proposed Section 5.8(b) merely states that East Tennessee "may" conduct a reverse open season, giving existing shippers an opportunity to turn back capacity, before seeking an expansion. Sequent contends that, under existing Commission policy, a pipeline *must* conduct a reverse open season before seeking an expansion.[12] Sequent asserts that a reverse open-season provides critical information to a pipeline, and to the Commission, in its determination of the necessity of an expansion. In addition, it provides greater transparency to the market on its system and in the larger market area of the project's geographic region.

East Tennessee Group

19. ETG notes East Tennessee's statement that it has exactly one request pending in its firm service queue, and East Tennessee's offer to grandfather that request under the old allocation system for a further year. ETG states that, to its knowledge, this is a request made by one of its members, Knoxville Utilities Board, whose request has been pending since January 2007. ETG contends that this one year grandfathering is too short, and asserts that East Tennessee should either pledge to satisfy the request of the Knoxville Utilities Board as soon as capacity becomes available, or at least to do so if it becomes available before August 1, 2011.

20. ETG notes that East Tennessee's proposed GT&C sections 5.8(a)(2) and 5.8(b)(3) provide that capacity under expiring or terminating service agreements will be made available through open seasons to the extent such service agreements do not have a right of first refusal or the shipper does not exercise its right of first refusal. ETG urges that the proposed tariff language should be revised to clarify that even shippers having long-term contracts with negotiated or discounted rates have a right to extend their contracts to the extent they agree to pay the maximum rate, and thus their capacity will not be put up for bid in an open season unless they choose not to exercise that right.

21. With regard to East Tennessee's proposed NPV allocation system for requests to change primary receipt or delivery points, ETG characterizes the proposed process as cumbersome, and states that many requests for point changes by existing capacity holders will not add revenues to East Tennessee, and therefore, would have an NPV of zero. ETG contends that East Tennessee should be required to grant requests for point changes

[12] Sequent August 13, 2008 Protest at 5, citing *Certification of New Interstate Natural Gas Pipeline Facilities*, 90 FERC ¶ 61,128, at 61,392 (2000).

to the maximum extent possible, consistent with the Commission's policy objectives of maximizing point flexibility. ETG contends, however, that East Tennessee's proposal would add severe additional strictures to its willingness to accept point changes, as listed in proposed GT&C section 5.7(b)(2). ETG states that these additional strictures appear subjective, overbroad, unnecessary and redundant, and that East Tennessee should not be given the discretion to refuse requested point amendments on the grounds set forth in the proposed GT&C section 5.7(b)(2).

Discussion

22. While the Commission does not require an NPV methodology, we have generally found it to be consistent with our goal of allocating capacity to the highest-valued use in those cases where pipelines have proposed it.[13] The parties have raised many issues that require further review. The particular issue that concerns us is the inclusion of a creditworthiness factor in the proposed NPV evaluation. East Tennessee has failed to provide sufficient evidence for us to justify that aspect of its proposal at this point. Therefore, the Commission denies East Tennessee's request for waiver of its notice requirements, and accepts and suspends the tariff sheets, to become effective February 1, 2009, subject to refund and condition. The Commission also directs Staff to establish a technical conference to examine the issues raised in the instant filing. Staff is further directed to report the results of the technical conference to the Commission within 120 days of the issuance of this order.

23. Based upon a review of this filing, the Commission finds that the proposed tariff language has not been shown to be just and reasonable, and may be unjust, unreasonable, unduly discriminatory, or otherwise unlawful. Accordingly, the Commission accepts East Tennessee's revised tariff language for filing and suspends its effectiveness for the period set forth below.

24. The Commission's policy regarding suspensions is that filings generally should be suspended for the maximum period permitted by statute where preliminary study leads the Commission to believe that the filing may be unjust, unreasonable, or inconsistent with other statutory standards.[14] It is recognized, however, that shorter suspensions may be warranted in circumstances where suspension for the maximum period may lead to

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[13] *See e.g., Tennessee Gas Pipeline Company*, 121 FERC ¶ 61,149, at P 23 (2007); *Northern Natural Gas Company*, 118 FERC ¶ 61,053, at P 51 (2007); *ANR Pipeline Company*, 116 FERC ¶ 61,201, at P 9 (2006).

[14] *See Great Lakes Gas Transmission Co.*, 12 FERC ¶ 61,293 (1980) (five-month suspension).

harsh and inequitable results.[15] Such circumstances do not exist here. Accordingly, the Commission shall suspend the effectiveness of the sheets shown on the Appendix for the full five months, until the earlier of a date set by a subsequent Commission order or February 1, 2009, subject to further Commission order.

The Commission orders:

(A) The tariff sheets in the instant filing are accepted and suspended, subject to refund and condition, and subject to the outcome of a technical conference as established by this order, to become effective February 1, 2009.

(B) Staff shall report the results of the technical conference to the Commission within 120 days of the issuance of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.

[15] *See Valley Gas Transmission, Inc.*, 12 FERC ¶ 61,197 (1980) (one-day suspension).

APPENDIX

East Tennessee Natural Gas, LLC
Docket No. RP08-487-000
FERC Gas Tariff, Third Revised Volume No. 1
Accepted, Subject to Refund and Other Conditions, and Subject to the Outcome of a Technical Conference, Effective February 1, 2009:

Second Revised Sheet No. 313
Second Revised Sheet No. 315
Second Revised Sheet No. 315A
Second Revised Sheet No. 315B
Original Sheet No. 315B.01
Original Sheet No. 315B.02
Original Sheet No. 315B.03
Original Sheet No. 315B.04
Original Sheet No. 315B.05
Original Sheet No. 315B.06
Second Revised Sheet No. 315C
Second Revised Sheet No. 315D
Fifth Revised Sheet No. 317