

127 FERC ¶ 61,217  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Sudeen G. Kelly, Marc Spitzer,  
and Philip D. Moeller.

Tuscarora Gas Transmission Company

Docket Nos. RP09-8-000  
RP09-8-001

ORDER APPROVING SETTLEMENT, SUBJECT TO CONDITIONS

(Issued June 3, 2009)

1. On February 12, 2009, Tuscarora Gas Transmission Company (Tuscarora) filed a Stipulation and Agreement (Settlement) in the above-referenced docket. As discussed in more detail below, the Commission approves the Settlement, subject to conditions.

**I. Background**

2. On October 1, 2008, Tuscarora Gas Transmission Company (Tuscarora) filed a revised tariff that incorporated numerous changes to rate schedules as well as to the General Terms and Conditions (GT&C) (Initial Filing).<sup>1</sup> Tuscarora's filing proposed numerous changes to its then-existing tariff, including proposals to (1) implement a new service option, limited firm transportation service under proposed Rate Schedule LFS; (2) clarify the method for evaluating bids and selling firm capacity; (3) update the creditworthiness provisions; (4) revise the balancing penalties and penalty crediting provisions; (5) add operational flow order provisions; (6) modify the uniform pressure and quantity provisions; (7) update the capacity release provisions; (8) update the right of first refusal provisions; (9) incorporate an additional type of permissible discount; (10) request negotiated rate authority; (11) implement provisions allowing for the reservation of capacity for expansion projects; (12) request authority to sell excess gas; (13) modify certain Form of Service Agreements that will help implement the above changes; and (14) make miscellaneous housekeeping changes to the entire tariff.

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<sup>1</sup> Tuscarora, October 1, 2008 Filing (proposing Tuscarora, FERC Gas Tariff, First Revised Volume No. 1 to replace Original Volume No. 1).

3. On October 14, 2008, Sierra Pacific Power Company (Sierra) filed a protest and Southwest Gas Corporation (Southwest) filed a joint protest with Paiute Pipeline Company (Paiute) (collectively, Protesters). On October 24, 2008, Tuscarora filed an answer to the protests.

4. On October 31, 2008, the Commission accepted and suspended the filing for five months, subject to refund and conditions, and subject to the outcome of a technical conference.<sup>2</sup> The Commission directed its staff to convene a technical conference to address the proposed services and terms and conditions. A conference was noticed and twice postponed at the behest of the parties, who informed staff that they were conducting settlement talks and nearing an agreement.<sup>3</sup> Ultimately, the parties did reach agreement, and Tuscarora filed the Settlement and revised *pro forma* tariff sheets with the Commission on February 12, 2009.

## II. Description of the Settlement

5. The Settlement, as proposed, would resolve all of the issues in this proceeding. The principle terms of the Settlement are summarized here.

6. Article I of the Settlement defines the terms “Issues,” which includes all issues raised in Tuscarora’s initial filing and set for technical conference by the Commission, and “Consenting Parties,” which refers to the three Protesters listed in Paragraph 3 above.

7. Article II provides that, upon the effective date of the Settlement, all of the Issues will be resolved, and upon the date the Commission accepts the tariff filing defined in Article III, the proceedings in Docket No. RP09-8-000 will be terminated with prejudice.

8. Article III provides that within seven business days of the effective date of the Settlement, Tuscarora will file with the Commission a Tariff Filing that sets forth tariff sheets substantively identical to the *pro forma* tariff sheets filed as part of the Settlement (listed in Exhibit 2 of the Settlement) and those tariff sheets filed as part of Tuscarora’s Initial Filing that remain unchanged by the Settlement (listed in Exhibit 3 of the Settlement). The effective date of this Tariff Filing will be the first day of the month following the date Tuscarora submits the Tariff Filing.

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<sup>2</sup> *Tuscarora Gas Transmission Co.*, 125 FERC ¶ 61,133, at P 44 (2008) (October 31, 2008 Order).

<sup>3</sup> As part of its requests to postpone the technical conference to accommodate settlement talks, Tuscarora agreed not to move its proposed tariff sheets into effect until June 1, 2009. *See* Tuscarora, January 12, 2009, Request for Deferral of Technical Conference, Docket No. RP09-8-000.

9. Article IV sets forth reporting and other requirements applicable to Tuscarora. Such reporting requirements include a penalty revenue crediting report, informational postings on Rate Schedule LFS agreements, and a one-time report after Rate Schedule LFS has been in effect for a year. Other requirements include certain accounting standards, as well as a standard for applying discount-type adjustments for certain specified negotiated rate agreements (i.e., that it is necessary to meet competition).
10. Article V establishes the effective date of the Settlement as the date on which Tuscarora receives either a final Commission order approving the Settlement as filed and without condition, if no opposition to the Settlement is filed, or a final Commission order, no longer subject to rehearing or appeal, approving the Settlement as filed and without condition if opposition to the Settlement is filed.
11. Article VI.1 provides that the Settlement represents a negotiated settlement of the issues in the proceeding and that the benefits accruing to both Tuscarora and the Consenting Parties represent compromises by the parties to achieve a balance between competing interests.<sup>4</sup>
12. Article VI.2 provides that Commission approval of the Settlement constitutes a resolution of all issues in the proceeding in Docket No. RP09-8-000 as of the effective date of the Settlement, and constitutes any and all waivers of the Commission's rules and regulations that may be necessary to effectuate the Settlement.
13. Article VI.3 provides that Tuscarora and the Consenting Parties retain their full rights under sections 4 and 5 of the Natural Gas Act, and the standard of review in any future section 4 or 5 proceeding will be the "just and reasonable" standard.
14. Article VI.4 provides that any and all discussions related to the Settlement are privileged and not admissible in evidence unless the Settlement becomes effective.
15. Article VII contains representations, warranties and covenants by the parties regarding their ability to enter into the Settlement and the actions they will take in supporting the Settlement before the Commission.
16. Tuscarora and Sierra filed comments in support of the Settlement.

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<sup>4</sup> Article VI.1 further provides that resolution of any matter by the Settlement is not deemed to be a "settled practice" as that term was interpreted and applied in *Public Service Commission of New York v. FERC*, 642 F.2d 1335 (D.C. Cir. 1980).

### III. Discussion

17. The Commission will approve the Settlement, subject to conditions relating to Tuscarora's proposal for evaluating bids for firm capacity with terms of one year or more in proposed section 3.2 of its GT&C.<sup>5</sup> In acting on an uncontested settlement, the Commission has a duty to provide "independent consideration of fairness, reasonableness, and the public interest."<sup>6</sup> While the Settlement satisfies these criteria with respect to the majority of the issues listed in Paragraph 2, above, proposed section 3.2 contains a bid evaluation methodology that (1) inappropriately devalues the net present value (NPV) of bids submitted by creditworthy shippers, and (2) requires the posting of collateral greater than what is justified by the NPV bid evaluation formula used by the pipeline.<sup>7</sup> We therefore approve the Settlement, subject to the condition that Tuscarora revise section 3.2 of its GT&C consistent with the discussion below.

18. As proposed in both the Initial Filing and the Settlement, Tuscarora would evaluate bids for firm capacity with terms of one year or more using an NPV analysis. The purpose of using NPV to determine the value of a bid is to simplify the stream of future cash flows to a single, present-day dollar figure. All else being equal, funds to be received in the future are worth less than funds received presently, and the present value formula permits a fair comparison of bids that may contain differences in rate and terms of service.

19. Tuscarora's NPV methodology would reflect the total value to the pipeline of any given bid, taking into consideration the rate per Dth, the duration of the proposed service agreement, and the time value of money. After calculating the NPV of a bid, Tuscarora would then multiply the NPV by a Risk of Default Factor. The Risk of Default Factor is defined by the Standard & Poor's *Cumulative Average Default Rate by Rating* table.<sup>8</sup> Using the credit rating of a bond issuer as the row (x-axis) and the time horizon in years as the column (y-axis), the Standard & Poor's table shows at their intersection the rate at which, historically, companies with those ratings have tended to default at any time

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<sup>5</sup> Tuscarora, FERC Gas Tariff, First Revised Volume No. 1, Proposed Original Sheets No. 69-70. These tariff sheets, proposed in Tuscarora's Initial Filing, remain unchanged by the Settlement.

<sup>6</sup> *Petal Gas Storage, LLC v. FERC*, 496 F.3d 695, 700 (D.C. Cir. 2007).

<sup>7</sup> See *Saltville Gas Storage Co., LLC*, 126 FERC ¶ 61,181 (2009) (*Saltville*) (conditionally approving three uncontested settlements that contained a similar collateral requirement, but applying the requirement only to non-creditworthy shippers).

<sup>8</sup> See *infra* Paragraph 31 for an excerpt of this table.

within a given number of years. Tuscarora thus devalues the NPV of a bid by simply multiplying the NPV by one minus the Risk of Default Factor from the Standard & Poor's table.

20. The NPV formula proposed in both the Initial Filing and the Settlement, which includes the above-mentioned adjustment based on the shipper's credit status, would apply to both creditworthy and non-creditworthy bidders. In its Initial Filing, Tuscarora cited the Commission's *Creditworthiness Policy Statement* as support for adjusting bids in this way.<sup>9</sup> Tuscarora argued that its proposal to include shippers' credit quality in the bid evaluation process will enable Tuscarora to award capacity to those shippers who are in the best position to fulfill their long-term contractual obligations, limit the ability of relatively high-default risk bidders to secure capacity by bidding unrealistically long terms, and encourage shippers to use the highest possible credit quality to support their bids.

21. As indicated above, we find that Tuscarora's proposed method for determining the NPV of shippers' bids for long-term capacity inappropriately devalues the NPV of bids submitted by creditworthy shippers, and requires the posting of collateral greater than what is justified by the NPV bid evaluation formula used by the pipeline. We therefore find that proposed section 3.2 (as reflected in both the Initial Filing and the Settlement) is not "fair, reasonable and in the public interest" as part of the Settlement. Accordingly, our approval of the Settlement is conditioned on Tuscarora's revising that section, consistent with the discussion herein.

**A. Risk of Default Adjustments for Creditworthy Shippers**

22. In conditionally approving the Settlement, we reject proposed section 3.2 of the GT&C due to the fact that creditworthy shippers, under the criteria specified in Tuscarora's proposed tariff, would be subject to a bid adjustment based on the shipper's individual bond rating, thereby requiring those creditworthy shippers to post collateral in order to have the full value of their bids recognized. We find that this method of bid valuation inappropriately adjusts creditworthy shippers' bids for capacity despite the fact that such shippers are considered creditworthy under the pipeline's tariff and serves to undermine the basic concept of non-discriminatory access to transportation capacity. Thus, we find that Tuscarora's proposed section 3.2 of its GT&C, as applied to creditworthy shippers, runs counter to Commission policy, as explained below.

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<sup>9</sup> Tuscarora, October 1, 2008 Initial Filing at 6 (citing *Policy Statement on Creditworthiness for Interstate Natural Gas Pipelines*, FERC Stats. & Regs. ¶ 31,191 (2005) (*Creditworthiness Policy Statement*)).

23. The 2005 *Creditworthiness Policy Statement* is not clear on the applicability of a risk of default factor, and after considering this issue in a number of cases, we find it inappropriate to permit the adjustment of bids by creditworthy shippers based on their risk of default. In the *Creditworthiness Policy Statement*, the Commission explained that, as a general matter, the ongoing credit risk of pipelines' customers is a business risk of the pipeline that should be reflected in its rate of return on equity.<sup>10</sup> The Commission also stated:

The Commission needs to consider on a case-by-case basis any pipeline proposal to take into account a shipper's credit status in determining whether more than three months collateral can be required when shippers are bidding for available capacity on the pipeline's existing system.... A shipper's credit status may be a relevant factor in assessing of the value of its bid as compared with bids by more creditworthy shippers, and in determining the amount of collateral that a non-creditworthy shipper must provide to have its bid considered on an equivalent basis.<sup>11</sup>

24. We interpret this statement as allowing pipelines to take into account credit status only with respect to bids of shippers who fail to meet the pipeline's creditworthiness criteria and are already subject to posting collateral to obtain transportation service. Accordingly, we affirm that Commission policy permits pipelines to incorporate a *non-creditworthy* shipper's probability of default into the calculation of the NPV of that shipper's bid for existing long-term capacity; however, pipelines may not incorporate a *creditworthy* shipper's probability of default into the calculation of the NPV of their bids.<sup>12</sup>

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<sup>10</sup> *Creditworthiness Policy Statement*, FERC Stats. & Regs. ¶ 31,191 at P 11 (citing *Ozark Gas Transmission Co.*, 68 FERC ¶ 61,032, at 61,107-08 (1994) (business and financial risk determine where the pipeline should be placed within the zone of reasonableness); *Williston Basin Interstate Pipeline Co.*, 67 FERC ¶ 61,137, at 61,360 (1994) ("Bad debts are a risk of doing business that is compensated through the pipeline's rate of return").

<sup>11</sup> *Id.* P 15.

<sup>12</sup> In a situation in which the pipeline applies the risk of default and the best bid available is that of non-creditworthy shipper, the pipeline must allocate that capacity to the non-creditworthy shipper with no more than three months collateral.

25. Requiring pipelines to treat bids of all creditworthy shippers on an equal footing will continue to foster open access and the development of competitive markets. As we explained in the *Creditworthiness Policy Statement*, “the Commission is concerned that any such proposal not impede open access, non-discriminatory transportation as well as competition and market development by reducing the pool of potential shippers that can acquire capacity.”<sup>13</sup> Applying the risk of default to creditworthy shippers will result in capacity not being available to all creditworthy shippers on an equal basis. Such a result would provide the shippers with the highest credit rating an undue preference as to other similarly situated creditworthy shippers by allowing them to acquire capacity despite making a lower bid. Our requirement that all creditworthy shippers’ bids be considered on an equal basis is justified by the beneficial effects on open access, and a resulting impact on competition for the supply of natural gas,<sup>14</sup> as it would prevent pipelines from making it more difficult for certain creditworthy shippers to secure capacity to the detriment of other creditworthy shippers.

26. Moreover, in the *Creditworthiness Policy Statement*, the Commission indicated that while pipelines could propose methods of incorporating shippers’ credit status in the valuation of their bids for existing capacity, collateral requirements stemming from such proposals would apply to non-creditworthy shippers, and would be permitted only to the extent necessary to have such non-creditworthy shippers’ bids considered equivalent to creditworthy shippers’ bids.<sup>15</sup> Similarly, we find that where a shipper meets a pipeline’s creditworthiness criteria, its bid should not be adjusted based on its individual credit rating. Instead, by meeting a pipeline’s creditworthiness standards, a shipper poses a sufficiently limited risk of default to the pipeline that its bid should be considered on par with all other creditworthy shippers’ bids. Moreover, business risks, including risk of default, are already factors considered in establishing the pipeline’s overall return on equity, which Tuscarora does not propose to revisit here.<sup>16</sup>

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<sup>13</sup> *Creditworthiness Policy Statement*, FERC Stats. & Regs. ¶ 31,191 at P 16.

<sup>14</sup> *Gas Transmission Northwest Corp. v. FERC*, 504 F.3d 1318, 1321 (D.C. Cir. 2007).

<sup>15</sup> *Creditworthiness Policy Statement*, FERC Stats. & Regs. ¶ 31,191 at P 15-16 (discussing additional collateral requirements only with respect to non-creditworthy shippers and indicating that the pipeline “may need to apply a reasonable limit on the amount of collateral a *non-creditworthy* shipper would have to provide in order to have its bid considered equivalent to that of *creditworthy* shippers”) (emphasis added).

<sup>16</sup> *Id.* P 11.

27. On the other hand, a determination by a pipeline that a shipper is non-creditworthy implies that selling capacity to such a shipper carries with it a significantly added business risk. In light of the additional risk that attends doing business with non-creditworthy customers, we find it reasonable for pipelines to incorporate such non-creditworthy shippers' risk of default in determining the NPV of their bids for pipeline capacity on a long-term basis vis-à-vis other competing bids.

28. Subsequent to the *Creditworthiness Policy Statement*, the Commission has encountered bid valuation methodologies similar to the one included in the Settlement, but has not found such a bid mechanism just and reasonable. In three other cases in which such a proposal has been made, the issue was heavily protested, and Commission set the issue for technical conference.<sup>17</sup> In each such case, the Commission conditionally accepted a settlement, which as here, applied the risk of default only to non-creditworthy shippers. In only one case did the Commission accept a provision similar to Tuscarora's proposed section 3.2; however, this case preceded the other three, and the Commission accepted the provision as part of an uncontested settlement.<sup>18</sup> In looking at the issue again in light of the concerns voiced in the other three cases, we have reconsidered the reasonableness of such provisions even as part of uncontested settlements as to creditworthy shippers, because they may adversely affect similarly situated shippers across the grid and potentially undermine the concept of open-access, non-discriminatory transportation.

29. Thus, we reject Tuscarora's proposed method of calculating the NPV of creditworthy shippers' bids for long-term capacity consistent with our determination in *Saltville*.

#### **B. Determination of Collateral Requirements**

30. We also find that the Settlement's method of determining the collateral required by shippers at the full contractual value by year is not consistent with our policy governing the use of NPV to value bids. As discussed in the *Creditworthiness Policy Statement*, the collateral requirements stemming from the use of a shipper's credit status in determining the NPV of its bid must be reasonably related to the risk posed by the non-creditworthy shipper.<sup>19</sup> In the proposed Settlement, we find that the collateral

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<sup>17</sup> *Saltville*, 126 FERC ¶ 61,181 at P 3, 24 (addressing the three different settlements involving three pipelines and their respective customers).

<sup>18</sup> *Gas Transmission Northwest Corp.*, 122 FERC ¶ 61,012 (2008) (*GTN*).

<sup>19</sup> *Creditworthiness Policy Statement*, FERC Stats. & Regs. ¶ 31,191 at P 16.

requirements are not reasonably related to the added business risks faced by Tuscarora, as discussed below.<sup>20</sup>

31. Under the proposed Settlement, bids for capacity would be reduced based on data contained in Standard & Poor's *Cumulative Average: Default Rate by Rating Modifier* table. This Standard & Poor's table shows the risk of default (at any time during the term of the contract) for a company with each credit rating for a contract of a specified number of years. Thus, on a 10-year contract, the risk of default for a BBB- shipper is 6.91 percent, while the credit rating for a BB+ shipper is 10.21 percent.

Time Horizon (Years)												
Rating	1	2	3	4	5	6	7	8	9	10	11	12
BBB-	0.31	1.02	1.78	2.78	3.74	4.60	5.25	5.87	6.33	6.91	7.42	7.94
BB+	0.52	1.41	2.85	4.20	5.41	6.71	7.88	8.41	9.36	10.21	10.82	11.41

32. Under the Settlement, the NPV of a 10-year bid by the BBB- shipper would be reduced by 6.91 percent and the NPV of the same bid by the BB+ shipper would be reduced by 10.21 percent. Under the Settlement, if the BB+ shipper wanted to have its bid considered on the same footing as the BBB- shipper, it would have to put up the contract value for the number of years sufficient to move its risk of default to a number equal to or less than the risk of default for a BBB- shipper. In this example, it would have to put up four years of collateral to reduce its risk of default to equal to or less than that of a BBB- shipper (6.91 percent).

33. By requiring payment of the full contract price for four years to have a BB+ shipper's bid considered equivalent to a BBB- shipper's bid, Tuscarora ignores the fact that this additional collateral entirely eliminates the risk of default in the early years. If this cash were recognized in the NPV formula as of the time the collateral is received, its impact on the present value would be at its greatest and it would reduce the level of risk faced by the pipeline. Thus, the Settlement's methodology for determining collateral requires collateral in excess of what is necessary to compensate for the additional risk of default, as it treats collateral as separate from the NPV calculation, rather than adjusting the future cash flow for the probability of default.

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<sup>20</sup> Our determination here reflects the same reasoning discussed in *Saltville*, 126 FERC ¶ 61,181 at P 21-25, in which the NPV bid adjustment was applied only to non-creditworthy shippers.

34. We therefore will approve the Settlement, subject to the condition that Tuscarora revise the methodology for determining the amount of collateral a non-creditworthy shipper would need to provide in order to ensure that the NPV of its bids considered on a more equitable basis.

35. Accordingly, the Settlement is approved, subject to Tuscarora's filing, within 30 days of the date this order issues, the Settlement Tariff Filing, reflecting the conditions and modifications to section 3.2 of its GT&C consistent with this order.

The Commission orders:

The Settlement is approved, subject to the conditions set forth in the body of the order.

By the Commission.

( S E A L )

Kimberly D. Bose,  
Secretary.