

131 FERC ¶ 61,118  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Marc Spitzer, Philip D. Moeller,  
and John R. Norris.

Midcontinent Express Pipeline LLC

Docket Nos. CP08-6-005  
CP09-56-001

ORDER GRANTING REHEARING

(Issued May 6, 2010)

1. On July 25, 2008, in Docket No. CP08-6-000, the Commission granted Midcontinent Express Pipeline LLC (Midcontinent) authorization under section 7(c) of the Natural Gas Act (NGA)<sup>1</sup> to construct and operate a new interstate natural gas pipeline extending from southeastern Oklahoma to western Alabama, with a capacity of up to 1,532,500 dekatherms per day (Dth/d) in its system's Zone 1 and 1,200,000 Dth/d in Zone 2, and to lease up to 272,000 Dth/d of capacity on Enogex LLC's Oklahoma intrastate pipeline system.<sup>2</sup> Midcontinent placed Zone 1 into service on April 10, 2009, and Zone 2 into service on August 1, 2009.
2. On September 17, 2009, in an order granting Midcontinent's request to amend its certificate and expand its system in Docket Nos. CP08-6-002 and CP09-56-000, respectively, the Commission determined that Midcontinent failed to justify the accrual of Allowance for Funds Used During Construction (AFUDC) prior to the filing of its certificate application and required Midcontinent to remove the improperly accrued AFUDC from the costs of the project.<sup>3</sup>
3. Midcontinent requests rehearing of the September Order regarding accruing AFUDC. We will grant its rehearing for the reasons discussed below.

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<sup>1</sup> 15 U.S.C. § 717f (2006).

<sup>2</sup> See *Midcontinent Express Pipeline LLC*, 124 FERC ¶ 61,089 (2008), *order denying reh'g and granting clarification*, 127 FERC ¶ 61,164 (2009).

<sup>3</sup> See *Midcontinent Express Pipeline LLC*, 128 FERC ¶ 61,253, at P 37 (2009) (September Order).

## **I. September Order**

4. In its applications to amend and expand its project, Midcontinent proposed to start the accrual of AFUDC in November 2008, three months prior to the January 30, 2009 filing of its certificate application in Docket No. CP09-56-000 (its expansion application), through May 2011. In the Commission's September Order, the Commission relied on its Accounting Release No. 5,<sup>4</sup> which at the time provided that AFUDC should not be accrued for the period prior to the filing date of an application to the Commission for a certificate to construct facilities by a natural gas company unless justified by the company. Relying on this provision, the Commission determined that Midcontinent failed to provide any support to justify the accrual of AFUDC prior to the January 30, 2009 filing of its certificate application. Therefore, the Commission required that Midcontinent remove the AFUDC accrual from November 2008 to the application filing date, January 30, 2009, from the project costs.

## **II. Request for Rehearing**

5. On rehearing, Midcontinent argues that the Commission's AFUDC accrual determination was arbitrary and capricious because it was contrary to Commission precedent and was not supported by the facts.<sup>5</sup>

6. Midcontinent argues that it submitted evidentiary support for its AFUDC accruals in its expansion application, including worksheet computations on a monthly basis to support its AFUDC accruals, which was responsive to Commission staff's May 14, 2009 data request.<sup>6</sup> Midcontinent further points out that the Commission did not seek additional information afterward and did not issue a notice of deficiency or non-responsiveness subsequently.

7. Midcontinent additionally argues that the Commission's September Order that requires Midcontinent to remove the AFUDC accrued prior to the January 30, 2009 filing date from the expansion project's costs would unreasonably deny it the opportunity to recover its costs. According to Midcontinent, regulated pipelines are entitled to recover the cost of financing construction of jurisdictional transportation facilities.<sup>7</sup>

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<sup>4</sup> *Capitalization of Interest During Construction*, Accounting Release No. 5 (Revised), FERC Stats. & Regs. ¶ 40,005 (1968).

<sup>5</sup> See Midcontinent's Request for Rehearing at 6-7.

<sup>6</sup> See *id.* at 5.

<sup>7</sup> See *id.* at 10-11.

### III. Discussion

8. Midcontinent is one of several pipelines that have been denied early accrual of AFUDC on expenditures made prior to the filing of the certificate application.<sup>8</sup> Like Midcontinent, the other pipeline applicants argued that the Commission should allow the accrual of AFUDC on expenditures made prior to the filing of a certification application, particularly for those costs incurred during the pre-filing period. In response, on December 15, 2009, the Commission convened a technical conference seeking input and comments on the continuing propriety of the Commission's then-current policy of limiting the AFUDC accrual, absent specific justification, to expenditures incurred after the filing of an application.<sup>9</sup>

9. Based on the comments received in the technical conference proceeding, the Commission revised its AFUDC policy as described in *Southern Natural Gas Co.* and *Florida Gas Transmission LLC*.<sup>10</sup> In these orders, we acknowledged that the natural gas industry has undergone significant changes since the issuance of AR-5 in 1968.<sup>11</sup> We also noted that since many natural gas pipelines take advantage of the pre-filing process and incur significant project-related costs during this time, they might be at risk of not being able to capture all of the cost of financing their construction projects if they cannot accrue AFUDC on expenditures made prior to the filing of a certificate application.<sup>12</sup> Therefore, in light of the current regulatory landscape in the natural gas industry, the

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<sup>8</sup> See, e.g., *Ruby Pipeline, L.L.C.*, 128 FERC ¶ 61,224 (2009), *reh'g granted in part and denied in part*, 131 FERC ¶ 61,007 (2010); *Florida Gas Transmission Co. LLC*, 129 FERC ¶ 61,150 (2009), *reh'g granted*, 130 FERC ¶ 61,194 (2010); *Southern Natural Gas Co.*, 128 FERC ¶ 61,198 (2009), *reh'g and clarification granted*, 130 FERC ¶ 61,193 (2010); *Fayetteville Express Pipeline LLC*, 129 FERC ¶ 61,235 (2009); *Pacific Connector Gas Pipeline, LP*, 129 FERC ¶ 61,234 (2009); *Texas Eastern Transmission, LP*, 129 FERC ¶ 61,151 (2009).

<sup>9</sup> *Notice of Technical Conference on Commission Policy on Commencement of Accrual of Allowance for Funds Used During Construction*, 74 Fed. Reg. 65,117 (Dec. 2, 2009). Pre-technical conference comments were due December 11, 2009. Post-technical conference comments were due December 29, 2009.

<sup>10</sup> 130 FERC ¶ 61,193 (2010) and 130 FERC ¶ 61,194 (2010), respectively. A full discussion of the comments received in the technical conference proceeding and the Commission's rationale for adopting the new policy can be found in *Southern Natural Gas Co.*, 130 FERC ¶ 61,193, at P 24-40.

<sup>11</sup> See, e.g., *Southern Natural*, 130 FERC ¶ 61,193, at P 33.

<sup>12</sup> See *id.* P 33-34.

certificate application date is no longer an appropriate milestone for determining when construction project-related expenditures begin, and thus when to begin accruing AFUDC.<sup>13</sup>

10. Under the Commission's revised AFUDC policy, natural gas pipelines may begin accruing AFUDC on construction projects when the following two conditions are met: (1) capital expenditures for the project have been incurred; and (2) activities that are necessary to get the construction project ready for its intended use are in progress.<sup>14</sup> The term "activities" includes all actions required to prepare the construction project for its intended use, including actions prior to physical construction, such as the development of plans or the process of obtaining permits from governmental authorities, and costs listed under Gas Plant Instruction No. 3.<sup>15</sup> "Activities" does not include preliminary survey and investigation activities.<sup>16</sup> Although the Commission's revised policy does not identify a bright line for establishing when natural gas pipelines may begin to accrue AFUDC, the date that the Commission approves the request to initiate the pre-filing process is a strong indicator of the initiation of construction project-related activities.<sup>17</sup>

11. Based on our revised AFUDC policy, we grant Midcontinent's request for rehearing and will allow Midcontinent to include its proposed AFUDC in its initial rates, subject to Midcontinent's filing a representation that the proposed AFUDC accruals comply with the requirements set forth above and in our recent orders describing the revised AFUDC policy.<sup>18</sup> Furthermore, if Midcontinent determines that its proposed AFUDC accruals should be revised in light of our revised AFUDC policy conditions, it must revise all cost-of-service items dependant on Gas Plant in Service such as Income Taxes, Depreciation Expense, Return, and Interest Expense. Midcontinent must then file its revised rates and work papers in sufficient time for the Commission to act on the revised rates prior to its filing the tariff sheets to implement those rates.

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<sup>13</sup> *See id.* P 34.

<sup>14</sup> *See id.* P 36.

<sup>15</sup> *See id.*

<sup>16</sup> *See id.* P 37.

<sup>17</sup> *See id.* P 39.

<sup>18</sup> *See Florida Gas*, 130 FERC ¶ 61,194, at P 24-29; *Southern Natural*, 130 FERC ¶ 61,193, at P 36-40.

The Commission orders:

(A) Midcontinent's request for rehearing of the September 17, 2009 Order is granted, as discussed in this order.

(B) Midcontinent shall file a representation that its proposed AFUDC accruals for the project comply with the revised policy conditions. In the alternative, if Midcontinent determines that its proposed AFUDC accruals should be revised in light of the revised policy conditions, it shall revise all cost-of-service items dependent upon Gas Plant in Service, such as Income Taxes, Depreciation Expenses, Return, and Interest Expense, and file its revised rates and workpapers in sufficient time for the Commission to act on the revised rates prior to filing the tariff sheets to implement those rates.

(C) Midcontinent and its representations made with respect to AFUDC accruals are subject to an audit to determine whether they are in compliance with the revised policy and related Commission rules and regulations.

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.