UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

ANR Pipeline Company — Docket No. RP02-335-002

ORDER ON INITIAL DECISION

(Issued November 3, 2004)

1. On April 12, 2004, the Presiding Administrative Law Judge (ALJ) issued an initial decision[1] in this proceeding to determine a just and reasonable method for addressing shipper imbalances on the interstate natural gas pipeline system of ANR Pipeline Company (ANR). Both Indicated Shippers and ANR filed Briefs on Exceptions and Briefs Opposing Exceptions. As discussed below, the Commission affirms in part and reverses in part the ALJ's initial decision.

2. Specifically, the Commission will affirm the ALJ's acceptance of ANR's proposal to modify its current mechanism. However, we will not require ANR to offer an in-kind option as directed by the ALJ. Therefore, there is no need to adopt the ALJ's recommended transition mechanism. We reverse the ALJ's decision requiring ANR to take primary responsibility for providing PTR shippers[2] with the necessary information to make transportation nominations. We will, however, require ANR to put its commitment concerning when it will purchase replacement volumes in its tariff. Finally, we will affirm the ALJ's rejection of certain of Indicated Shippers' proposals. This decision benefits the public interest because it approves changes to ANR's cashout imbalance mechanism that will give all shippers a fair opportunity to balance their gas balance accounts and avoid cashout penalties.

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[1] *ANR Pipeline Co.*, 107 FERC ¶ 63,006 (2004).

[2] "PTR" is an abbreviation for "Plant Thermal Reduction."

Description of ANR's Imbalance Cashout Mechanism

3. In his initial decision, the ALJ provided an excellent narrative of ANR's imbalance cashout mechanism in section 15 of the General Terms and Conditions (GT&C) of ANR's tariff. A shipper's imbalance on a pipeline system arises when the shipper delivers to the pipeline a different volume of natural gas than the shipper receives from the system. A shipper who takes more gas from the system than it delivered for transportation incurs a "negative" imbalance; a shipper who takes less gas from the system than it delivered to the pipeline incurs a "positive" imbalance. Section 15 of the GT&C provides for the pipeline to cash out its shippers' monthly imbalances by either, in effect, selling gas to shippers with negative imbalances, or buying gas from shippers with positive imbalances, at an index price. This is known as "cashing out" the imbalance.

4. Section 16 of ANR's GT&C currently provides that the index price used for cashouts be determined by using the monthly average of weekly spot price indices for each of the four operational areas on the system.[3] Thus, the applicable index price varies depending upon the geographical area in which the shipper delivered its gas to the pipeline. In addition, the index price is adjusted or "tiered," so that the sales price which shippers with negative imbalances pay to ANR increases above 100 percent the larger the negative imbalance and the purchase price ANR pays to shippers with positive imbalances decreases below 100 percent the larger the positive imbalance.[4]

5. Before the cashout takes place, each shipper is given the opportunity to make up the difference by trading its imbalance with a shipper who has an imbalance in the opposite direction. For example, a shipper who has a negative imbalance may agree with a shipper who has a positive imbalance to set off the two imbalances. If, after the monthly trading period is over, the shipper still has an imbalance, then it must cash out the imbalance pursuant to the above procedures.

6. Even though the cashout process brings the account of each shipper into balance at the end of the month, the pipeline system as a whole may have a gas volume imbalance. That is because the shippers in the aggregate may have either delivered more, or less, gas to ANR than they received. If the volume of gas that ANR uses to operate its system gets

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[3] ANR's gas supply sources lie in two distinct areas. Its Southwest area leg takes gas supply from the Texas panhandle, north-central Oklahoma and southern Kansas. Its Southeast area segment receives gas from offshore Louisiana and onshore Louisiana. The gas is moved through "headstations," where the legs meet the main trunk of the pipeline and is eventually transported to markets in Michigan, Wisconsin, Illinois, Indiana and Ohio. *Id*. at 65,023.

[4] *Id*. at 65,024 and note 1 (detailing the tiered pricing).

either too high or too low, ANR may purchase or sell gas in the open market depending upon operational conditions. Historically, shippers have tended to take more gas from the system than they put on the system, and therefore ANR has on occasion purchased gas in the open market to replenish the gas that shippers took from the system, but it has never had to sell excess gas. ANR's costs of purchasing replacement gas may not equal its net revenues from the shippers' monthly cashouts. That is because the index prices used for the cashouts may not equal the price paid by ANR to purchase replacement gas, particularly since ANR's actual purchases may occur a number of months after some of the shipper imbalances that contributed to ANR's need to purchase replacement gas. In addition, ANR's cashout payments to shippers that left too much gas on the system may not equal its cashout revenues from shippers that took too much gas.

7. To reconcile these disparities, ANR's tariff provides for it to make a filing each May 1 to reconcile its cashout activity for the prior year.[5] That filing reconciles (1) the revenues ANR has received from its cashout sales with (2) the costs it incurred as a result of its cashout purchases from shippers and any open market replacement purchases it made to replenish its gas storage inventory.[6] If the reconciliation filing shows that ANR's cost of operating the cashout program during the preceding year has exceeded its revenues, ANR implements a cashout surcharge, to be effective on June 1, which is paid by shippers who incurred imbalances during the preceding year. In addition, section 15.5(b)(1) of ANR's GT&C provides for it to defer, or carry forward, to the following year the collection of cashout costs equal to ten percent of the gross revenues generated by the cashout activity being reconciled (the 10 percent carry forward provision). Conversely, if revenues exceed costs, ANR would refund the excess through a negative surcharge.[7]

Background of the Instant Proceeding

8. On May 1, 2002, ANR filed its annual cashout price surcharge filing and asked that it be made effective June 1, 2002. The filing reflected an increase in the then effective surcharge from $0.1508 per dekatherm (Dth) to $0.4464 per Dth, in order to allow ANR to collect a balance of $6.9 million in its cashout account. The filing was protested. On May 31, 2002,[8] the Commission accepted and suspended the filing for five

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[5] Unlike the monthly reconciliation that ANR provides to each shipper that is out of balance, the May 1 annual surcharge filing deals with money, not volumes of natural gas.

[6] The reconciliation would also include the revenues from any sales ANR made in the open market to eliminate excess gas. However, it has never had to make such sales.

[7] *Id*. at 65,024.

[8] *ANR Pipeline Co*., 99 FERC ¶ 61,183 (2002).

months, to become effective the earlier of November 1, 2002 or on a date specified in an order issued after a technical conference. The technical conference took place on July 18, 2002.

9. In an order following the technical conference, the Commission determined that ANR's proposed cashout price surcharge had been calculated consistent with its approved tariff, and accordingly allowed the surcharge to become effective at the end of the suspension period. However, the Commission was concerned with the workings of ANR's cashout mechanism. Noting the complexity of how ANR's cashout mechanism works, the Commission stated that the past operation of the cashout mechanism indicated that ANR's current mechanism is unjust and unreasonable in at least two respects.

10. First, the Commission was concerned about the wide swings in the cashout surcharge from year to year. The Commission stated that this was partly due to significant accumulated cashout losses being carried forward in some years, but not others. The Commission explained that the 10 percent carry forward provision defers collection of significant costs without regard to the level of costs to be recovered or the resulting surcharge level. As a result, this provision can defer costs (which likely could have been collected during an annual period when the amount of under collection to be recovered was small) to the subsequent annual period when the level of costs (excluding the carry forward costs) and the resulting surcharge might be much greater.

11. Second, the Commission stated that the current mechanism does not give PTR shippers an adequate opportunity to resolve their imbalances.[9] PTR shippers are shippers who contract with processing plants to remove liquefiable hydrocarbons from their gas. The processing plants are located on ANR's system, but are not owned by ANR. ANR transports the PTR shippers' gas to the processing plants, where the liquefiables are removed and the gas is then reinjected into ANR's pipeline for transportation to its ultimate destination. The processing causes the gas to lose part of its heat content. ANR's tariff requires each PTR shipper to enter into a separate transportation agreement,

[9] The Indicated Shippers had complained that a shipper who delivers gas to the pipeline upstream of a processing plant has no way of learning precisely how much of the gas volume has been removed until long after it has been processed and returned to ANR to be transported. Consequently, the Indicated Shippers complained, they could not bring themselves into balance in a timely fashion before their PTR imbalances created a liability for next year's surcharge. In a subsequent order, in Docket No. RP03-465-000 (in which the Commission rejected outright ANR's proposal to switch to a poorly designed in-kind mechanism), the Commission stated that any imbalance resolution mechanism on ANR's system must take into account the timing of data to PTR shippers and provide them an opportunity to net and trade imbalances. *See ANR Pipeline Co.*, 103 FERC ¶ 61,252 at 61,939 (2002).

under which the shipper agrees to nominate additional make-up gas to replace the shrinkage that took place at the processing plant. The PTR shipper makes these nominations based upon estimates of the Plant Thermal Loss provided by the plant operator. However, the plant operator may not provide final figures for the Plant Thermal Loss until 45 days or more after the end of the month in which the processing took place. As a result, a PTR shipper may not know the exact amount of any imbalance it incurred during a particular month until the middle of the second month after the imbalance took place or later. The Commission was concerned that this makes it difficult for PTR shippers to resolve their imbalances through netting and trading, since ANR's tariff generally required such netting and trading to take place in the month immediately following the month in which the imbalances occurred, before the PTR shipper would finally know the amount, if any, of its imbalance.

12. The Commission said that a well-functioning mechanism should be capable of giving all shippers behaving responsibly a fair opportunity to avoid such payments and that when that object is not achieved, the mechanism should be capable of assessing reasonably incurred costs to those shippers that have incurred them and the accounts should be cleared out as expeditiously as possible. The Commission concluded that ANR's mechanism did not appear to meet these goals.[10] Therefore, the Commission set these issues for negotiation before a settlement judge and if the settlement talks proved unsuccessful, for a trial-type hearing.

13. The Indicated Shippers sought rehearing of this decision, arguing that the Commission erred in allowing ANR's 2002 surcharge filing to remain in effect pending review of the merits of the cashout mechanism. The Commission denied the request for rehearing on the ground that section 5 of the Natural Gas Act (NGA), under which it had undertaken the review, did not permit the Commission to order retroactive changes in ANR's tariff.[11] The settlement proceedings took place; however, the parties were unable to achieve a negotiated settlement. Therefore, on May 7, 2003, the matter was set for hearing. After the hearing proceedings were concluded, the ALJ issued an initial decision on April 12, 2004.

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[10] *ANR Pipeline Co.*, 101 FERC ¶ 61,123 at 61,508 (2002).

[11] *ANR Pipeline Co.*, 103 FERC ¶ 61,065 (2003). An appeal to the U.S. Court of Appeals for the District of Columbia Circuit was lodged, *sub nom.* Texaco *Exploration & Production Co. v. FERC*, No. 03-1153, filed May 30, 2003. It remains pending.

The Initial Decision

14. At the hearing, ANR proposed three modifications of its existing cashout mechanism. First, it proposed to switch from a monthly average index price for cashing out imbalances to a weekly high/low index price. Under this proposal, a shipper with a negative imbalance would pay ANR for the excess gas it had taken based on the highest weekly spot index price for the month. ANR would pay a shipper with a positive imbalance for the gas it left on the system based on the lowest weekly spot index price for the month. ANR stated its current use of the average price for the month allows shippers to engage in arbitrage. That is because during the latter part of a month in which gas prices have either risen or fallen significantly, shippers can be quite certain that the monthly average index price used to cash out their imbalances will be either lower or higher than the actual market price during the latter part of the month. If the cashout price is less than the market price, shippers have an incentive to take excess gas from the pipeline and sell it for the higher market price while paying the pipeline the lower cashout price. If the cashout price is higher than the market price, shippers can purchase gas at the lower market price, leave it on the pipeline, and then receive the higher cashout price by selling gas to the pipeline. ANR contended that its high/low index price proposal would minimize this opportunity for arbitrage. ANR presented evidence that, if its proposal had been in effect since 1997, it would not have had any cost underrecovery in the operation of its cashout mechanism, and therefore it would not have needed to impose any surcharge.

15. Second, ANR proposed to eliminate the 10 percent carry forward provision, consistent with the Commission's concern that that provision contributed to the wide swings in the surcharge from year to year. Third, ANR proposed that it would endeavor to purchase or sell gas as necessary to make up for the customers' net overall monthly imbalance in the month following the month in which the imbalance occurred, as long as it had available the transportation capacity necessary to transport the gas to storage. ANR would no longer wait until such purchases or sales were actually operationally required. ANR proposed tariff changes to implement the first two proposals. The third proposal was simply in the form of testimony by ANR's Director of Rates and Regulatory Affairs.

16. Indicated Shippers proposed to require ANR to provide its shippers an option to elect each year whether to resolve their imbalances through cashouts or on an in-kind basis. In addition, Indicated Shippers proposed to give PTR shippers additional time to make up their imbalances, and made various other proposals discussed below.

17. The ALJ held that ANR should offer its shippers an annual option of resolving imbalances either by cashout or on an in-kind basis. Shippers would be required to exercise this option by October 1 of each year, and their choice would go into effect the

following January 1. A shipper choosing the in-kind option for a particular year would remain liable for any surcharge obligations that had accumulated against it by reason of imbalances incurred in prior periods, as well as making any cashout payments for periods preceding the effective date of the in-kind option.

18. The ALJ also held that ANR should be permitted to adopt its proposal to use a high/low index price for cashing out the imbalances of those shippers who choose the cashout option. The ALJ stated that this will prevent shippers from attempting to "game" the system by indulging in price arbitrage, although it would also have a tendency to over-compensate ANR.[12] The ALJ held that ANR's adoption of a high/low index price should be conditioned on ANR eliminating the surcharge through which it recovers any underrecovery of costs in the operation of its cashout mechanism, since the high/low proposal would create a fund that would compensate ANR for bearing the risk of any underrecovery of its costs.

19. Third, the ALJ approved ANR's proposal to purchase or sell the replacement gas necessary to physically balance its system during the month following the month in which the imbalance occurred, if operationally feasible. The ALJ stated that this would eliminate prudence challenges concerning the timing of ANR's purchases of replacement gas. However, the ALJ held that the Commission should make it mandatory that ANR follow this practice, rather than just accepting ANR's proposal to endeavor to follow this practice.

20. With regard to the Commission's concern that the current mechanism does not provide PTR shippers an adequate opportunity to resolve imbalances on ANR's system by netting and trading imbalances, the ALJ determined that ANR should take primary responsibility for providing PTR shippers with the necessary information to make transportation nominations by keeping them apprised of the processing plant shrinkage levels needed to monitor and control their imbalances.

21. The ALJ rejected Indicated Shippers' proposals to (1) refund/credit revenues from FSS overrun service; (2) refund/credit revenues from sales of excess fuel and lost and unaccounted-for gas (LAUF); and (3) compensate shippers for the use of ANR's facilities to derive such revenues, the ALJ noted that throughout the proceeding Indicated Shippers had requested the Commission to require a number of rigorous structural changes to ANR's tariff provisions dealing with shipper imbalances. These changes included the initiation of a new imbalance account, through which would flow prudently-incurred unrecovered cashout costs arising under ANR's current cashout mechanism as well as such costs that arise in the future, to be set off against revenues from the sale of excess fuel, revenues from the sale of excess LAUF and revenues from FSS overrun services.

[12] Initial Decision at 20, P. 41.

Indicated Shippers wanted the Commission to require ANR to pay a charge for the use of facilities used for the transmission and storage of the excess fuel and LAUF volumes. The ALJ stated that it was not entirely clear whether this charge would also flow through the proposed imbalance account. Nor was it clear to the ALJ what Indicated Shippers intended by the insinuation that the sales of excess fuel and LAUF were uncertificated jurisdictional sales of natural gas in interstate commerce. In any event, the ALJ rejected this entire package of prescriptions as being unlawful and baseless.[13] Finally, the ALJ appended tariff sheets to the initial decision to implement his decision.

Discussion

22. The Commission has found that ANR's existing tariff provisions concerning the resolution of imbalances are unjust and unreasonable in two respects. First, the Commission held that ANR's cashout mechanism leads to unnecessarily large swings in its cashout surcharge from year to year. Second, the Commission stated that the current mechanism does not give PTR shippers an adequate opportunity to resolve their imbalances. The Commission accordingly established the hearing before the ALJ in order to determine a just and reasonable cashout mechanism pursuant to NGA section 5. Below, we first address the changes to ANR's cashout mechanism necessary to minimize large swings in the cashout surcharge. Second we address the changes necessary to give PTR shippers an adequate opportunity to resolve their imbalances.

A. Cashout Surcharge

23. The parties now agree that, at minimum, two of the changes which ANR proposed to its cashout mechanism should be adopted. First, while the ALJ did not address ANR's proposal to eliminate the provision for carrying forward 10 percent of its cashout costs from one year to the next, Indicated Shippers does not oppose that proposal. Second, the ALJ adopted ANR's proposal to endeavor to make any purchases or sales of gas necessary to balance its system in the month following the month in which the imbalance occurred if operationally possible, and the ALJ stated that proposal should be made mandatory. The only exception to that holding was the Indicated Shippers' request that ANR be required to include this policy in its tariff, and ANR did not oppose Indicated Shippers' exception. Therefore, the Commission approves these two changes to ANR's cashout mechanism.

24. The ALJ also approved both (1) ANR's proposal to modify its cashout index price to use high/low weekly index prices, instead of the average price for the month, and (2) Indicated Shippers' proposal that ANR be required to offer shippers the option of

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[13] Initial Decision at 31.

resolving their imbalances in-kind. ANR excepts to the ALJ's decision to require it to offer the in-kind option, in addition to the modifications it had proposed. Indicated Shippers, on the other hand, while not excepting specifically to the approval of ANR's high/low proposal, contend that proposal is only acceptable if ANR also offers the in-kind option. Thus, the issue now before the Commission is whether we should take action under NGA section 5 to require ANR to offer the in-kind option in addition to its own high/low proposal in order to minimize swings in the cashout surcharge.

25. In its Brief on Exceptions, ANR argues that it presented evidence showing that making its proposed three changes to its imbalance resolution mechanism, including the shift to a high/low index price, would be sufficient to address the Commission's concerns about wide swings in the surcharge. In particular, ANR states that it presented evidence showing that, if its high/low index price had been in effect during the period 1997-2002, it would have collected sufficient revenues through the cashout of imbalances that it would not have needed to impose any surcharge in those years.[14] In any event, ANR is concerned about the complexity of implementing an in-kind option, including the need for transition surcharges to shippers shifting from the cashout option to the in-kind option, so that such shippers remain responsible for amounts owed to ANR as a result of actions during the time they were using the cashout option.

26. Indicated Shippers respond in their Brief Opposing Exceptions that the ALJ correctly decided not to accept ANR's high-low cashout proposal as a stand-alone mechanism. Indicated Shippers state that, although initially opposed to using a high/low index price for a variety of reasons, they recognize that some type of high/low cashout pricing has been approved on other pipelines. However, Indicated Shippers contend that the high/low index price proposal could only be found just and reasonable, if ANR is also required to offer an in-kind option. For example, Indicated Shippers point out that ANR proposes to apply its high/low index price to the 0 to five percent imbalance tier, which is cashed out at 100 percent of the applicable index price, as well as other imbalance tiers. Indicated Shippers contend that this would result in an inherent penalty for all imbalance volumes, including the previously penalty free 0 to five percent imbalance tier. Therefore, Indicated Shippers argue that shippers must be given the opportunity to avoid incurring a penalty on such minimal imbalances through the use of the in-kind option.

27. The Commission reverses the ALJ's holding that ANR should be required to offer its shippers an in-kind option for resolving their imbalances and approves ANR's proposal to adopt a high/low index price for cashing out imbalances.

[14] *Citing* Ex. Nos. ANR-1 at 13 and ANR-7.

28. In this proceeding, the Commission is acting under NGA section 5 to require ANR to modify its tariff provisions concerning the resolution of imbalances. Therefore, the Commission bears the burden of showing that the justness and reasonableness of the remedial tariff changes it requires in order to minimize the problem of wide swings in the level of the annual true-up surcharge.[15] Moreover, while the Commission is acting here under NGA section 5, the Commission also takes into account the fact that the NGA delegates to the pipeline the primary initiative to propose the rates, terms, and conditions for its services under NGA section 4. If the rates, terms, and conditions proposed by the pipeline are just and reasonable, the Commission must accept them, regardless of whether other rates, terms and conditions may be just and reasonable.[16] Consistent with this structure of the NGA, the Commission believes it appropriate in this case, where ANR agrees that its current tariff is unjust and unreasonable, to give ANR a similar initiative in proposing remedial tariff provisions. To the extent ANR's proposed remedy is just and reasonable, the Commission will approve that remedy, even though other just and reasonable remedies might exist.

29. ANR has presented evidence showing that its proposed high/low index price, together with its other two proposals approved above, should minimize the wide swings in its annual true-up surcharge, primarily by reducing the cost underrecoveries that are recovered through the surcharge. First, ANR presented evidence[17] showing that, if its proposed high/low index price had been in effect during the years 1997 through 2002, and its shippers' imbalances had been the same as they actually were, its revenues from operating the cashout program would have been sufficient to cover its costs. That is because shippers who took too much gas from the system would have had to pay ANR more for that gas, while ANR would have paid less to shippers who left too much gas on the system. In addition, ANR would have had sufficient funds to purchase the remaining deficient volumes on the spot market. As a result, the annual surcharge calculated each year pursuant to the tariff would have been zero.

30. Second, ANR presented evidence that its current use of the average monthly index price gives shippers an incentive to engage in price arbitrage, and such arbitrage has contributed to the cost underrecoveries that it recovers pursuant to its annual true-up surcharge. For example, ANR's witness Richard Porter testified that, because imbalances are cashed out at the monthly average of weekly index prices, shippers will know towards

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[15] The first prong of the Commission's section 5 burden – to show that the existing tariff provision is unjust and unreasonable – is not at issue here, since the Commission has already made that finding and no party has contested the Commission's finding.

[16] *Consolidated Edison Co. v. FERC*, 165 F.3d 992, 998, 1002-1004 (D.C.Cir. 1999), and cases cited.

[17] Ex. Nos. ANR-1 at 13-14 and ANR-7.

the end of the month whether the current market price will, or is likely to be, greater or less than the average price at which their imbalances will be cashed out.[18] Thus, if a shipper in the last week of the month believes that the current market price will be greater than the average weekly cashout price, the shipper has an incentive to take more gas from the system than it puts on the system. It can then sell the gas at the higher market price, while paying ANR the lower cashout price. Moreover, ANR pointed out that one of the Indicated Shippers stated in response to a data request that, when determining how rigorously to correct imbalances at the end of the month, it considers mid-month pricing trends and anticipated cashout charges.[19]

31. When price arbitrage occurs, the pipeline is, in essence, required to sell gas to its customers at below-market levels or buy gas at above-market levels. This can lead to the pipeline incurring a substantial underrecovery of costs.[20] ANR presented evidence that it has incurred just such an underrecovery, thereby necessitating the imposition of the annual true-up surcharge. For example, ANR showed that since November 1993, the average price at which it made cashout purchases was $2.57, while the average price at which it made cashout sales was $2.33. This meant that, even before ANR purchased any gas to replace its customers' net overall overtakes of gas, its administration of the cashout program had caused it to incur a cost underrecovery of about $11.5 million.[21]

32. As the Commission has held in approving proposals by other pipelines to implement a high/low price index, such a high/low price index should eliminate the opportunity for the type of arbitrage discussed above, and the resulting cost underrecoveries. That is because, during the last week of the month, the shippers should not have any degree of certainty that the cashout price will be higher or lower than market price on the day in question.[22]

33. The Commission concludes, based on all of the above, that ANR's proposal to shift to a high/low index price, together with its other proposals, should largely eliminate the need for it to impose any annual true-up surcharge to recover cost underrecoveries. Had the proposal been in effect from 1997-2002 and had the customers still incurred the same imbalances, the proposal would have produced enough revenue to recover the costs ANR incurred as a result of those imbalances, and for that reason there would have been no need for a surcharge. The Commission also believes it likely that the level of

[18] Ex. No. ANR-1 at 11.

[19] Ex. No. ANR-20 at 5.

[20] *Texas Gas Transmission Corp.*, 97 FERC ¶ 61,349 at 62,634 (2001).

[21] Ex. No. ANR-1 at 10.

[22] *Texas Gas Transmission Corp.*, 97 FERC at 62,632.

imbalances would also have been reduced with the removal of the incentive for arbitrage, and this too would have reduced the cost underrecoveries necessitating the actual surcharges that were imposed during that period.

34. While Indicated Shippers have stated they are willing to accept the change to a high/low price index, they contend that use of such an index price for cashouts would only be just and reasonable if the Commission also affirms the ALJ's decision that ANR also be required to give shippers the option to resolve their imbalance on an in-kind basis. Indicated Shippers suggest that, without the in-kind option, ANR's proposal would be inconsistent with § 284.12(b)(2)(v) of the Commission's regulations, adopted by Order No. 637, which provides that pipelines are only permitted to assess penalties "to the extent necessary to prevent the impairment of reliable service." Indicated Shippers point out that ANR proposes to apply its high/low index price to the 0 to five percent imbalance tier, which is cashed out at 100 percent of the applicable index price, as well as other imbalance tiers. Indicated Shippers contend that this would result in an inherent penalty for all imbalance volumes, including the previously penalty free 0 to five percent imbalance tier. Therefore, Indicated Shippers argue that shippers must be given the opportunity to avoid incurring a penalty on such minimal imbalances through the use of the in-kind option.

35. The Commission will not adopt the ALJ's in-kind recommendation. While in-kind resolution of imbalances can be just and reasonable, the Commission has not required other pipelines to offer that method to resolve imbalances, and many pipelines require shippers to cash out any imbalances that remain after netting and trading has been completed.[23] We recognize that ANR is proposing to apply the high/low index price to all imbalances, including those in the 0 to five percent tier. The Commission finds, based on the record in this case, that this aspect of ANR's proposal is not inconsistent with Order No. 637.

36. The Commission in Order No. 637 recognized a need to minimize arbitrage on pipeline systems and determined that, to the extent that changes to a cashout mechanism are necessary to remove the incentive for arbitrage, a pipeline could implement such changes. Specifically, in Order No. 637, the Commission stated that pipelines "could change the methods by which they cash out imbalances to eliminate the incentives for shippers to borrow gas from the pipeline because the cashout price is less than the market price for gas."[24] As the Commission found in *Northern Natural*,[25] shippers may incur

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[23] In addition, the Commission believes it best not to make too many changes at this time since the proposed changes we are accepting may be sufficient to cure the problems that rendered ANR's mechanism unjust and unreasonable in the first place.

[24] FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 at 31,607. *See also* Order No. 637-A at 31,608.

imbalances in the initial tier cashed out at 100 percent of the applicable monthly average cashout index price for the purpose of arbitrage, just as they can incur greater imbalances for that purpose. Indeed, it is in this tier that shippers would have the greatest incentive to engage in arbitrage. That is because in the higher tiers the percentage adjustment to the index price would tend to reduce any price differential between the cashout price and the index price.

37. This is illustrated by the situation where the market price increased during the month, so that an average monthly price used to cashout imbalances was lower than the market price. As previously discussed, in this situation the shipper has an incentive to take excess gas from the system and sell it for the higher end of month market price, while paying ANR the lower monthly average price used to cash out the excess takes. However, in the higher tiers, ANR would charge the shipper more than 100 percent of the index price in order to cash out the imbalance, thereby reducing or eliminating any differential between the cashout price and the index price.

38. Thus, the goal of minimizing arbitrage, which Order No. 637 endorsed, supports the use of the high/low pricing method for all imbalances, not just those in the excess of a tolerance level, such as ANR's five percent tolerance, even if using high/low pricing for cashing out first tier imbalances might be considered in some senses to be a penalty. For that reason, the Commission has approved the use of the high/low pricing method for all imbalance tolerance levels for other pipelines, including where there is no in-kind option.[26] This is particularly appropriate here, where there is evidence that shippers do take into account mid-month pricing trends and the projected cashout price in determining how rigorously to correct imbalances that may have been developed during the course of the month. Moreover, ANR offers a number of imbalance management services to its customers as an alternative to resolving their imbalances by cashout.[27] The imbalance management services offered by ANR and approved by the Commission in ANR's Order No. 637 compliance filing include ANR amending its tariff to facilitate shippers' access to third-party storage to (1) make clear that it will not inhibit access to third-party storage and imbalance management service providers and (2) provide its shippers with three additional intraday nomination opportunities. Other imbalance management services offered by ANR include (1) interruptible parking and lending, (2) interruptible wheeling, (3) no-notice and (4) market balancing services which allow shippers to manage their delivery point imbalances without incurring penalties.

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[25] 107 FERC ¶ 61,252 (2004).

[26] *See* 107 FERC ¶ 61,252 at P 23-24 (2004).

[27] *See ANR Pipeline Co.,* 97 FERC ¶ 61,323 (2001).

39. Accordingly, the Commission finds that ANR's proposed use of a high/low index price, without offering an in-kind option, is just and reasonable. That proposal, together with ANR's other two proposals, should be sufficient to minimize the wide swings in the annual true-up surcharge by minimizing the need for any surcharge to recover costs ANR might incur as a result of its administration of its cashout mechanism. The high/low price should reduce the level of imbalances, and, to the extent imbalances are incurred, it should recover revenues sufficient to cover the costs of cashing out those imbalances. ANR's commitment to make any actual gas purchases necessary to replace its working gas within a month of the incurrence of the imbalances requiring such purchases should also help ensure that ANR's gas purchase costs are generally in line with its cashout prices. In addition, ANR will eliminate the current 10% carryforward provision, which the Commission previously found contributed to the wide swings in the annual true-up surcharge.

40. The Commission also will not adopt the ALJ's proposal to require ANR to eliminate any provision for an annual true-up surcharge as a quid pro quo for approving its high/low proposal. Both the ALJ and Indicated Shippers expressed concern that adoption of the high/low proposal might result in ANR overrecovering any costs it incurs as a result of imbalances, contrary to the consistent cost underrecoveries it suffered under its current tariff provisions. The annual true-up mechanism will ensure that ANR must return any such overrecoveries to its customers.

41. Because the Commission is not adopting the in-kind option on ANR's system, there is no need to address the issues raised concerning the transition mechanism adopted by the ALJ as a means to require shippers who switch to the in-kind option to pay any costs they caused ANR to incur while they were under the cashout mechanism. Since shippers will not have the option to switch to an in-kind method, there will be no need for any such transition mechanism.

42. Finally, Indicated Shippers argue that the ALJ improperly rejected their proposal to offset revenues from the sale of excess fuel and lost and unaccounted for (LAUF) gas against any attempt to pass through unrecovered cashout costs and debit volumes in ANR's existing cashout accounts at the time a new imbalance mechanism is placed into effect.[28] Indicated Shippers explain that under their proposal all cashout charges in the future would be paid through the Imbalance Account, which would also be credited with revenues that ANR derived from other sources (FSS overrun Service and sales from excess Fuel and LAUF). Indicated Shippers' witness attempted to establish a link between these revenues and ANR's management of its cashout program.

[28] Indicated Shippers Brief on Exceptions at 25-29.

43. ANR responds, in its Brief Opposing Exceptions, that the ALJ appropriately rejected Indicated Shippers' proposed Imbalance Account which was designed to permit refunds in prohibition of the ALJ's ruling which prohibited refunds. ANR identifies and discusses each of the ALJ's reasons for rejecting Indicated Shippers' theories.[29]

44. For the reasons set forth in the initial decision, we affirm the ALJ's rejection of Indicated Shippers' proposals relating to (1) refunds/credits of revenues derived from FSS overrun service; (2) refunds/credits of revenues from sales of excess fuel and LAUF; and (3) compensation for the use of ANR's facilities to derive such revenues.

B. PTR Shippers

45. As discussed above, the Commission also found that ANR's current cashout mechanism does not give PTR shippers an adequate opportunity to resolve their imbalances, particularly through netting and trading. That is because the operator of the plant where a PTR shipper's gas is processed may not provide final figures for the plant thermal loss until 45 days or more after the end of the month in which the processing took place. As a result, a PTR shipper may not know the exact amount of any imbalance it incurred during a particular month until the middle of the second month after the imbalance took place or later. The Commission was concerned that this makes it difficult for PTR shippers to resolve their imbalances, for example through netting and trading, since ANR's tariff generally required such netting and trading to take place in the month immediately following the month in which the imbalances occurred, before the PTR shipper would finally know the amount, if any, of its imbalance.

46. At the hearing, ANR contended that tariff changes the Commission approved in a separate docket (Docket No. RP01-612-000) have resolved this problem. On December 26, 2002, the Commission accepted revised tariff language filed by ANR that allows all of its shippers to net and trade imbalances relating to any prior service month after having received a prior period adjustment.[30] The purpose of that change was to permit PTR shippers to trade imbalances after learning of a change in their imbalance activity, even if the imbalance to which the adjustment related occurred more than one month before the adjustment. While the Commission accepted ANR's Docket No. RP01-612-000 tariff change, the Commission also stated that the parties could consider in the instant proceeding whether any other tariff changes were necessary to address the PTR shipper issue.

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[29] *See* ANR Brief Opposing Exceptions at 13-19.

[30] *ANR Pipeline Co.*, 101 FERC ¶ 61,375 (2002).

47. At the hearing, Indicated Shippers contended that ANR should be required to obtain from the processing plants and provide to each PTR shipper up-to-date information about its individual plant shrinkage percentage. Indicated Shippers contended that this information would help them adjust their nominations during a month so as to minimize incurring any imbalance that would need to be resolved by netting or trading or cashing out. Indicated Shippers also asserted that, to the extent the information provided by ANR proved inaccurate, the PTR shippers should not be subject to any penalty for the resulting imbalance. ANR opposed this proposal on the ground that the PTR shippers should themselves be responsible for obtaining such information directly from the processing plants.

48. The ALJ required that ANR assume primary responsibility for providing processing plant data concerning shrinkage to PTR shippers and ensure the data's accuracy. Although the ALJ found that both Indicated Shippers and ANR have contracts with the plant operators and several of the Indicated Shippers stated they do a fairly accurate job of keeping account of their plant shrinkage percentage, the ALJ found that ANR's contract had better terms than the Indicated Shippers' contract, and thus gave ANR better access to the information needed to make the most accurate PTR nominations. He therefore concluded that ANR must play a larger role in keeping PTR shippers apprised of their status with respect to imbalances because ANR is in a better position to provide PTR shrinkage percentages to PTR shippers.

49. ANR excepts to this holding. ANR argues that, based on the record, there is no reason to require ANR to assume primary responsibility for providing processing plant data to PTR shippers and ensuring the data's accuracy. ANR contends that it has already addressed the Commission's concern about PTR shippers' ability to net and trade imbalances through the tariff changes approved in Docket No. RP01-612-000. It also contends that the ALJ's decision (1) conflicts with prior a Commission decision which held that PTR shippers should have primary responsibility for obtaining information from plant processors; (2) is inconsistent with the evidence establishing that PTR shippers are able to obtain this data directly from the plants; and (3) is in conflict with the ALJ's finding that PTR shippers currently have the tools to monitor plant shrinkage and do a good job of doing so.[31] ANR also contends that PTR shippers should not be exempted from penalties simply because the estimated plant shrinkage percentages ANR supplies to them may be inaccurate. ANR contends that PTR shippers can obtain sufficiently accurate information to be able to keep their monthly imbalances within the zero to five percent tolerance range that is cashed out at 100 percent of the applicable index price, and in any event now have an increased ability to net and trade imbalances so as to avoid penalties.

[31] ANR Brief on Exceptions at 20-32.

50. Indicated Shippers argue in support of their position that the ALJ properly required ANR to have primary responsibility for providing processing plant data to PTR shippers and that this decision is based on record evidence.[32] In opposing ANR's exceptions, Indicated Shippers respond that giving ANR the primary responsibility for informing its PTR shippers regarding PTR percentages is a critical part of the initial decision and must be upheld to enable PTR shippers to make better nominations and reduce imbalances on ANR's system. Indicated Shippers argue that the ALJ correctly determined that ANR is in the best position to provide PTR percentages to PTR shippers because ANR has better access to information needed to make the most accurate PTR nominations possible, including the fact that plant operators provide ANR with data that shippers need to make the most accurate PTR nominations.

51. However, Indicated Shippers except to the ALJ's decision on the ground that it did not make clear exactly what information ANR must communicate to its PTR shippers. They suggest that ANR calculate the individual PTR shipper's percentages for the current month of operation based upon the corresponding operational mode used in a previous month. They believe that all PTR shippers should receive from ANR a PTR shrinkage percentage to nominate by receipt meter. If ANR receives communication from the plant that the operational mode has changed during the month, Indicated Shippers state that ANR should adjust the PTR shippers' shrinkage percentages accordingly to reflect the plant's new operational mode.

52. ANR responds to Indicated Shippers' exception by maintaining its position that PTR shippers should be responsible for obtaining and utilizing shrinkage percentages from the plants that process their gas.[33] ANR contends that, in any event, under no circumstances should it be required to calculate individual percentages for specific PTR shippers. Because the plant operators do not provide ANR with shrinkage percentages by shipper, ANR argues that it should not be required to make such calculations. ANR further argues that it should also not be required to be the transferor of any other "pertinent information" provided by the plant or be required to determine what each such shipper should actually nominate.[34]

53. The Commission will not adopt the ALJ's decision requiring ANR to have primary responsibility for providing estimated shipper-by-shipper plant shrinkage information to PTR shippers. The Commission finds that the Indicated Shippers have not satisfied their burden under NGA section 5 to show that ANR's failure to act as an intermediary between the plant operators and the PTR shippers for the purpose of

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[32] Indicated Shippers Brief Opposing Exceptions at 12-16.

[33] ANR Brief Opposing Exceptions at 10.

[34] ANR Brief Opposing Exceptions at 12.

providing this information is unjust and unreasonable or to show that requiring ANR to provide this information is just and reasonable. The Commission's primary concern about the timing of data to PTR shippers was to ensure that PTR shippers, like other shippers, would have an opportunity to net and trade imbalances in order to avoid penalties. As ANR states, the revised tariff sheets approved in Docket No. RP01-612-000 provide PTR shippers with sufficient time to net and trade imbalances because PTR shippers would be given a further opportunity to net and trade after the PTR shippers are informed of any changes in their plant shrinkage percentages for prior months.

54. The Commission recognizes that the PTR shippers have an interest in obtaining on a real time basis as accurate as possible information concerning their individual plant shrinkage percentages. Such information permits them to adjust their nominations to avoid a net imbalance for the month, thereby minimizing any need to net and trade thereafter. However, the relevant information is possessed, in the first instance, by the third party processing plants, not ANR. Thus, the issue is whether the PTR shippers should obtain the information directly from the processing plant operators or should ANR be required to act as an intermediary between the two. The Indicated Shippers have not made a sufficient showing of an inability to obtain the information directly from the plant operators to justify imposing this additional burden on ANR. For example, ANR provided evidence that at least some of the Indicated Shippers currently receive from the plant operators estimated shrinkage percentages at the beginning of each month, as well as updated information concerning changes in operation that might occur during the month.[35] As the ALJ stated in his initial decision, "[c]learly, the Indicated Shippers we encounter in this proceeding have the tools to monitor the shrinkage that their production undergoes in the processing plants. They are some of the largest energy firms in the world, and they do not lack for resources."[36]

55. The ALJ hoped that by placing more of the information gathering and sharing burden on ANR, a means could be found to make more accurate information available to shippers on a more rapid timetable. However, based upon the record before us, it does not appear that this can be accomplished simply by giving ANR the primary responsibility of providing information to PTR shippers. As the record reflects, regardless of whether ANR or the PTR shippers get data from the plant operators during the month, the information that either of them will get will be estimates, as actual data will not be available until after the month in which the relevant imbalances were incurred.

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[35] Ex. No. ANR-18 at 2-4. Ex. No. ANR-19.

[36] 107 FERC at 65,037.

56. The ALJ stated that ANR had more favorable contract terms with plant operators then the PTR shippers. However, PTR shippers have the ability to negotiate with the plant operators the same or more favorable terms in their contracts. In light of ANR's proposed tariff changes which we are accepting, we will not require ANR to be responsible for providing data to PTR shippers as this may cause more problems to arise. Under the plan approved here, PTR Shippers will have more time to trade after obtaining PTR data. The Commission finds that the modifications we are accepting here should be sufficient to address our concerns about PTR shippers.

The Commission orders:

(A) The ALJ's decision is affirmed in part and reversed in part.

(B) ANR's proposal to modify its current mechanism by switching its pricing mechanism for cashing out imbalances from an average weekly index price to a weekly high-low pricing mechanism and eliminating the current 10% carryforward provision is accepted.

(C) ANR is not required to offer an in-kind option, to adopt a transition mechanism or to take primary responsibility for providing PTR shippers with data on PTR shrinkage.

(D) ANR is directed to revise its tariff to reflect the change in its former practice in which operational considerations were the primary driver for determining when to purchase or sell replacement gas in order to reflect its proposed practice of purchasing or selling gas to balance the system in the month following the creation of the imbalance, to the extent such purchases or sales are operationally practicable.

(E) Within 30 days of this order's issuance, ANR is directed to file tariff sheets consistent with the discussion in the body of this order and these ordering paragraphs.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.