111 FERC ¶ 61,236
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Marathon Oil Company

v. Docket No. RP05-234-000

Trailblazer Pipeline Company

ORDER DENYING COMPLAINT

(Issued May 20, 2005)

1. On March 22, 2005, Marathon Oil Company (Marathon) filed a complaint against Trailblazer Pipeline Company (Trailblazer) alleging that the rates charged under two of Marathon's Expansion 2002 negotiated rate transportation contracts are the product of Trailblazer's exercise of market power in violation of the Commission's Alternative Rate Policy Statement,[1] the Natural Gas Act (NGA), the Commission's regulations, and Trailblazer's tariff. Marathon also alleges that the rates charged under these service contracts are unduly discriminatory in violation of NGA section 4. It requests the Commission direct Trailblazer to disgorge and return all revenues collected under those contracts in excess of the applicable maximum recourse rates, plus interest. Marathon also requests that the Commission invalidate the existing negotiated contracts and require Trailblazer to provide service in the future at the current recourse rate or at the lowest existing negotiated rate charged any Expansion 2002 shipper.

[1] *Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines and Regulation of Negotiated Transportation Services of Natural Gas Pipelines*, 74 FERC ¶ 61,076, *reh'g and clarification denied*, 75 FERC ¶ 61,024, *reh'g denied*, 75 FERC ¶ 61,066 (1996), *petition for review denied, Burlington Resources Oil & Gas Co. v. FERC*, Nos. 96-1160, 1998 U.S. App. Lexis 20697 (D.C. Cir. 1998)(*Alternative Rate Policy Statement)*.

2. The Commission finds that Trailblazer did not violate Commission policy and regulations in effect when Trailblazer held its open season and executed the contracts for the Expansion 2002 service. Further, the Commission finds insufficient justification to initiate further action under NGA section 5 to invalidate and change the negotiated rate in the Expansion 2002 contracts. For these reasons, we find that it is in the public interest to deny Marathon's complaint.

PROCEDURAL ISSUES

3. Notice of Marathon's complaint was published in the *Federal Register* on March 31, 2005 (70 Fed. Reg. 16,496). Numerous parties filed timely, unopposed motions to intervene.[2] All timely, unopposed motions to intervene are granted by operation of Rule 214 of the Commission's regulations.[3] The Natural Gas Supply Association filed comments stating, in short, that the Commission should continue to adhere to the current policy requiring pipelines to provide a recourse rate during open seasons for new capacity.

4. Trailblazer filed an answer to Marathon's complaint, and Marathon filed an answer to Trailblazer's answer.[4] While section 385.231(b) of the Commission's regulations does not permit answers to protests, we will waive that provision and accept Marathon's answer as it may aid in the disposition of the issues raised in the complaint.

5. Marathon also filed a motion that requests the Commission order Trailblazer to admit or deny, specifically and in detail, each material allegation contained in Marathon's complaint in accordance with section 385.213(c) of the Commission's regulations. We have a sufficient record before us to address the complaint on the merits in this order. Therefore, we deny Marathon's request.

---

[2] They are: Hasting Utilities, Tenaska Marketing Ventures, BP America Production Company and BP Energy Company, Duke Energy Trading and Marketing America, L.L.C. and Duke Energy Marketing America L.L.C., Natural Gas Supply Association, Devon Energy Production Company, L.P., Western Gas Resources, Inc., and The Williams Companies, Inc.

[3] 18 C.F.R. § 385.214 (2004).

[4] While Marathon styled its answer as a cross-motion for summary disposition and opposition to Trailblazer's request for summary motion, it is, in essence, an impermissible answer.

BACKGROUND

6. Production of coalbed methane in the Powder River Basin in the Rocky Mountain Region area has been expanding for many years. In 2000, the Energy Information Administration (EIA) reported that production had outpaced the development of longhaul capacity to carry the gas to end-use markets.[5] In response, several interstate natural gas pipelines announced proposals to construct new pipeline capacity in that area, including Trailblazer.

7. Trailblazer is an interstate pipeline company that owns and operates approximately 436 miles of 36-inch pipeline that extends eastward from an interconnection with Wyoming Interstate Company, Ltd. near Rockport, Colorado. Trailblazer's system delivers gas to Natural Gas Pipeline Company and Northern Natural Gas Company at Beatrice, Nebraska, which, subsequently transport gas into Chicago and north-central cities.

8. Trailblazer held two open seasons in 2000. First, in June 2000, it announced a proposed extension and/or expansion of transportation capacity on its system. Trailblazer proposed an extension to Glenrock, Wyoming or Rockport, Colorado, or both. It also proposed an expansion project for its existing facilities.[6] Trailblazer states that it terminated the June open season because no bidders that submitted acceptable bids executed any contracts. In August 2000, Trailblazer announced a second open season for 300,000 Dth/d of new capacity on its existing system.[7]

9. The August 2000 open season required bids of at least $0.17 per Dth for expansion capacity. Trailblazer stated that this criterion was a minimum and that it would not accept bids for less than that amount. It also stated that it would only pursue the project if it obtained fixed-price contracts with minimum terms of 10 years. Additionally, it stated that the contracts would be filed with the Commission as negotiated rate transportation contracts.

[5] *Natural Gas Monthly*, October 2000, at vii.

[6] *See* Open Season materials in Exhibit 3 of Marthon's complaint.

[7] *See* Open Season materials in Exhibit 4 of Marthon's complaint.

10. Subsequently, on January 10, 2001, Trailblazer filed an application in Docket No. CP01-64-000 for a certificate of public convenience and necessity requesting authorization to construct and operate facilities that would expand its transportation capacity from Colorado to Nebraska to provide 324,000 dekatherms per day (Dth/d) of new firm, long-term transportation service commencing July 2002 (Expansion 2002).[8]

11. Trailblazer's application for the Expansion 2002 capacity included signed, binding precedent agreements for all of the Expansion 2002 capacity at negotiated rates. Trailblazer also proposed an incremental recourse rate of 12.19 cents Dth/d. Notice of Trailblazer's application was published in the *Federal Register*. While several parties filed protests, none of the protests raised issues relating to Trailblazer's open season or its proposed recourse rate. Marathon did not intervene in the certificate proceeding or protest the application.

12. On May 18, 2001, the Commission issued Trailblazer a certificate to construct and operate the proposed Expansion 2002 facilities. In the order, the Commission found that the firm shippers supporting Trailblazer's Expansion 2002 elected to pay negotiated rates. The order also approved Trailblazer's proposed 12.19 cents/Dth recourse rate. No party challenged the Commission's findings concerning Trailblazer's recourse rate or filed a request for rehearing of the May 18, 2001 order.

13. As required by the May 18 certificate order, Trailblazer made a tariff filing on March 8, 2002, to implement, among other things, its 12.19 cents/Dth recourse rate. Additionally, as required, Trailblazer filed a list of the shippers that agreed to negotiated rate contracts and the rates. The shippers and rates were as follows:

[8] After the open season for the 300,000 Dth/d on new capacity, Trailblazer's engineers determined that it could construct the facilities to create an additional 24 MDth/d of capacity.

Shipper Name	Quantity (Dth/d)	Rate (Dth/d)
Western Gas Resources, Inc	57,500	$ 0.2252
J.M. Huber Corp.	41,000	0.2287
CMS Energy Marketing, Services and Trading Company	100,000	0.2401[9]
Williams Production RMT Co.	70,000	0.1782
Devon Energy Production Co.	33,000	0.1836
Marathon	22,500	0.1783[10]
Total	324,000	

No protests were filed in response to the compliance filing, and the Commission accepted the filing in an unpublished letter order issued on May 23, 2002.

14. On November 29, 2002, Trailblazer filed tariff sheets initiating its first rate case under NGA section 4 following the in-service date of its 2002 expansion project.[11] The Commission accepted the filing, subject to refund, and set it for hearing before an Administrative Law Judge. On January 23, 2004, the Commission issued an order approving a settlement in the rate proceeding.[12] In that order, the Commission severed Marathon (as a member of Indicated Shippers) from the settlement to allow it to "litigate the reasonableness of the rate applicable to any contracts in which they have a direct interest."[13] On March 1, 2004, Marathon notified the Commission that it had agreed to become a consenting party to the settlement agreement.

---

[9] CMS permanently released its capacity to Marathon in May 2002.

[10] Marathon states that its rate under the executed contract for this capacity is 18.25 cents/Dth. In Trailblazer's compliance filing, and the agreement filed by Marathon in Exhibit 12 to the complaint, the stated monthly reservation charge for that capacity is $5.4243. When the monthly reservation charge is multiplied by 12 months and divided by 365 days, Marathon's rate equals 17.83 cents/Dth. While Marathon also states the initial executed agreement was subsequently amended, it provides no documentation to support the 0.42 cent/Dth difference.

[11] *Trailblazer Pipeline Co.*, 101 FERC 61,405 at P21 (2002)

[12] *Trailblazer Pipeline Co.*, 106 FERC ¶ 61,034 (2004).

[13] *Id.* at Ordering Paragraph (B).

15. Marathon is a natural gas producer that owns, among other things, natural gas producing properties in the Powder River Basin in Wyoming. While Marathon did not submit a bid in Trailblazer's August 2000 open season, it holds 122,500 Dth/d of firm capacity on Trailblazer's Expansion 2002 facilities. Specifically, Marathon holds 22,500 Dth/d of capacity at 17.83 cents/Dth (FTSX Agreement No. 919467) that it succeeded to when it acquired Pennaco Energy Inc.(Pennaco) before the Expansion 2002 facilities were completed. While it was Pennaco that entered into a binding precedent agreement for the Expansion 2002 capacity, it was Marathon that executed the final service agreement with Trailblazer. In May 2002, Marathon acquired by permanent capacity release, effective June 1, 2002, CMS Energy Marketing, Services and Trading Company's (CMS Energy) 100,000 Dth/d of capacity at 24 cents/Dth (FTSX Agreement No. 927144).[14]

16. Marathon states that when it was negotiating to acquire CMS Energy's Expansion 2002 capacity, Trailblazer was unwilling to allow the permanent capacity release until Marathon agreed to assume the entire contract for the entire term at the 24 cent/Dth rate agreed to by CMS Energy. Marathon states that it subsequently entered into firm transportation contract FTSX Agreement No. 927144, effective June 1, 2002, for 100,000 Dth/d of Expansion 2002 capacity at 24 cents/Dth.

PARTIES POSITION

A. Marathon's Complaint

17. Marathon contends that neither the Pennaco nor the CMS Energy contract was freely negotiated because Trailblazer exercised its market power during the August 2000 open season by threatening to withhold much needed capacity and pressuring shippers to outbid other shippers to maximize Trailblazer's profits. Marathon asserts that Trailblazer held the earlier June 2000 open season to test the market to determine the price that shippers were willing to pay. Marathon suggests that Trailblazer used the information gained from the June 2000 open season, in conjunction with the gas commodity basis differentials between the Rocky Mountain area and the Mid Continent during the summer of 2000, in deciding to announce that it would not consider bids for less than 17 cents/Dth during the subsequent August 2000 open season.

[14] Marathon also acquired production properties from CMS Energy.

18. Marathon states that the letter announcing the August 2000 open season did not offer potential shippers a cost-of-service recourse rate alternative. It contends that the letter clearly stated that: (1) Trailblazer would not build the expansion unless it received fixed-price negotiated rates of at least 17 cents/Dth for contracts of at least 10 years; (2) capacity would be awarded to bidders offering the highest value based on rate and term; and (3) maximum rate cost-of-service bids would be rejected. For these reasons, Marathon concludes that Trailblazer designed its August 2000 open season to encourage prospective shippers to unnecessarily bid up the price of the capacity.

19. Marathon contends that a fundamental predicate to the authority of a pipeline to negotiate rates under the negotiated rate policy is that the pipeline and its shippers mutually agree to negotiated rates. Marathon alleges that when a pipeline dictates that the only way it will provide a particular service is if the rates are negotiated, sets a minimum rate that shippers must bid, and demands that the rate remain fixed for the entire term of the contract without regard to the Commission-approved cost-based recourse rate, there can be no voluntary agreement by the shipper to forgo cost-of-service rates in favor of negotiated rates.

20. Marathon states that to ensure that a shipper's agreement to pay a negotiated rate instead of a cost-of-service rate is voluntary and is not the product of the pipeline's market power, the Commission's negotiated rate policy requires that the pipeline affirmatively offer the shipper the option of declining to negotiate and, instead, electing to submit a bid at the Commission-approved, cost-of-service recourse rate. Marathon argues that because Trailblazer did not offer a recourse rate during its August 2000 open season, it violated the Commission's negotiated rate policy.

21. Marathon states that in accepting Trailblazer's recourse rate in the certificate proceeding, the Commission stated that Trailblazer agrees to negotiate rates for its transportation services in accordance with the Commission's Alternative Rate Policy Statement. Marathon also states that at the time of the Expansion 2002 open season in the summer of 2000, Trailblazer violated section 38.1 of its tariff's General Terms & Conditions. Specifically, it contends that when Trailblazer filed to include section 38.1 in its tariff, it represented that the tariff provision was to implement a negotiated rate provision in its tariff.

22. Marathon asserts that the Commission's acceptance of Trailblazer's tariff sheet was premised on the Commission's understanding that the language of the tariff sheet, providing for a recourse rate option for all shippers receiving service under Trailblazer's blanket certificate, was consistent with the Alternative Rate Policy Statement. Marathon contends that because Trailblazer did not offer a recourse rate during its August 2000 open season, Trailblazer violated section 38.1 of its tariff.

23. Further, Marathon concludes that Trailblazer deliberately hid the fact that it did not offer a recourse rate during its open season from the Commission. It states that the certificate application did not disclose that the minimum fixed reservation rate that it demanded from the expansion shippers during the open season was five cents higher than the proposed initial maximum recourse reservation rate it subsequently filed in its certificate application, and that it did not allow the expansion shippers to bid a cost-based recourse rate. Marathon also asserts that Trailblazer did not disclose to the Commission that Trailblazer conditioned its construction of the facilities on its obtaining negotiated-rate, fixed-price contracts with a minimum term of ten years. Marathon asserts that the certificate application misrepresented what transpired during the open season by implying that the negotiated rate shippers had the opportunity during the open season to choose recourse rates over negotiated rates.

24. Marathon suggests that because Trailblazer violated the Commission's Alternative Rate Policy Statement and the terms of its tariff in conjunction with exercising market power to extract higher prices for Expansion 2002 service, it has no legal authority to charge Marathon negotiated rates under its two existing service agreements for the Expansion 2002 capacity. Marathon surmises that the highest lawful rate that Trailblazer should charge under those agreements is the recourse rate.

25. As such, Marathon requests the Commission require Trailblazer to refund the profits over the applicable recourse rate earned under the negotiated contracts. Specifically, Marathon calculates that during June 2002 to February 2004, Trailblazer collected $13,641,390 and $1,715,580 under FTSX Agreements 927144 and 919467, respectively, above the revenues that Trailblazer would have collected under the maximum recourse rate applicable to the Expansion 2002 service. Further, Marathon anticipates that over the 10-year term of the contracts, Trailblazer will over-collect by $63,085,078. Marathon alleges that these are windfall profits that the Commission should disallow.

26. Additionally, Marathon argues that by charging Marathon negotiated rates that are higher than the negotiated rates charged to similarly situated shippers, Trailblazer is charging unduly discriminatory rates in violation of NGA section 4, section 284.7(b) of the Commission's regulations, and the Commission's negotiated rate policy. It contends that shippers with the same receipt and delivery points under the same rate schedule are paying markedly different rates for exactly the same service on the same pipeline. Marathon states that this establishes a *prima facia* case of discrimination. Marathon requests that if the Commission denies its request for continued service at the maximum applicable recourse rates, the Commission should, instead, require that Trailblazer provide service under Marathon's negotiated rate contracts at the lowest rate charged under any other negotiated rate contract for the Expansion 2002 service.

B. Trailblazer's Answer

27. Trailblazer states that in 2000, it began exploring the possibility of expanding its system. On June 12, 2000, it announced and posted on its electronic bulletin board a non-binding open season intended to gauge market support for multiple expansion scenarios. Trailblazer contends that it proposed a possible expansion of its existing system and extension of its system from Glenrock, Wyoming, Rockport, Colorado or both, to Gage County, Nebraska. Trailblazer states that while it received a number of acceptable bids for different combinations of capacity, none of the winning bidders would execute binding agreements.

28. Trailblazer states that it held another open season on August 7, 2000, for an expansion project to add 300 MDth/d of capacity. The open season specified that a fixed-rate bid of 17 cents was the minimal acceptable economic criterion. The open season also stated that Trailblazer would award the capacity using the net present value method. Trailblazer states that no recourse rate was set out in the open season. It contends that the open season package was sent to numerous prospective shippers, reported in the trade press, and posted on Trailblazer's web site. Trailblazer asserts that no one challenged the lack of notice of the prospective recourse rate in the open season.

29. Trailblazer states that it received bids for capacity in excess of the 300 MDth/d of capacity. It stated that it received several bids above the 17 cents minimum acceptable bid and awarded capacity to the shippers who valued it most.

30. Trailblazer contends that its open season fully complied with the Commission's policy as it existed at the time of the open season. It states that at the time it held its open season, the case-by-case development of the Commission's policy on negotiated rates had not yet reached the issue of the availability of recourse rates during open seasons for expansion capacity.

31. Specifically, Trailblazer contends that prior to the Commission's October 31, 2002 decision in *Natural Gas Pipeline Co. of America* (*Natural*),[15] the Alternative Rate Policy Statement applied only to existing pipeline capacity. It argues that in the *Natural* case, which was issued two years after it held its open season, over a year after the Commission issued the Expansion 2002 certificate order, and more than five months after the facilities were placed into service, the Commission for the first time held that the requirement to offer a recourse rate applied to new, as well as existing capacity.

[15] 101 FERC ¶ 61,125 (2002).

Trailblazer states that the Commission subsequently recognized that the requirement for a recourse rate in an open season became effective for the first time in the *Natural* decision.[16]

32. Trailblazer points out that at the time it held its open season, other pipelines had announced their own proposals to move gas along the same general route as Trailblazer.[17] Trailblazer contends that in this environment, Marathon's assertion that Trailblazer threatened to withhold capacity to drive up rates is baseless. Trailblazer reasons that it initially proposed a larger project, but it was the shippers, not Trailblazer, who refused to execute agreements. Trailblazer concludes that far from withholding capacity, it was competing for business with Williams Gas Pipeline Central, Inc., Colorado Interstate Gas Company, and Kern River Gas Transmission Company.

33. Trailblazer contends that there is no requirement for a pipeline to construct facilities under the NGA. It states that it was under no obligation to build the expansion facilities, but it did. It states that in the open season it stated that it would construct a project if it received sufficient fixed-rate contracts for at least 17 cents/Dth. Further, Trailblazer contends that a majority of the interested shippers bid higher rates than the minimum rate requested by Trailblazer. It asserts that its actions were open and transparent and that it told the marketplace exactly what it required to proceed with the project.

---

[16] *Citing Kinder Morgan Interstate Gas Transmission, L.L.C.,* 104 FERC ¶ 61,266, P 5 n. 1 (2003).

[17] Trailblazer refers to a Williams Gas Pipeline Central, Inc. announcement to commence an open season for 540 Dth/d for fixed rate 10-year contracts in the mid-20 cent range. *Citing WIC, Williams Central, Trailblazer Offer New Capacity in Rockies,* Inside FERC, Aug. 14, 2000. It also states that the following month Colorado Interstate Gas Co. announced an open season for a similar project that CIG discussed with its shippers before the open season. *Citing Expansion in East and West Under Scrutiny With Open Season Scheduled by Dominion Transmission (Formerly CIG) and Colorado Interstate,* Foster's Natural Gas Report, Sept. 28, 2000 at 8. Finally, Trailblazer refers to the Kern River Gas Transmission Co. proceeding to move gas west out of the Rocky Mountains. *Kern River Gas Transmission Co.*, 98 FERC ¶ 61,205, *order on reh'g and issuing certificate*, 100 FERC ¶ 61,056, *order on reh'g*, 101 FERC ¶ 61,042 (2002): *Kern River Gas Transmission Co.,* 96 FERC ¶ 61,147, *order on remand*, 97 FERC ¶ 61,080 (2001).

34. Trailblazer states that after the open season, its engineers determined that it could construct the project with an additional 24MDth/d. It contends that instead of holding a supplemental open season, it offered the capacity at 17 cents/Dth to the open season bidders. Trailblazer claims that if it had been pressuring shippers to bid higher prices to maximize profits, it would not have offered this capacity for 17 cent/Dth.

35. Trailblazer states that it executed precedent agreements with six parties. It states that each of the precedent agreements committed the shippers to enter into negotiated rate contracts at fixed rates for a fixed period. Trailblazer asserts that each shipper bid a different rate and each shipper is paying a rate based on its bid.

36. Trailblazer points out that it filed its certificate application on January 10, 2001, and that the application included a proposed 12.19 cent/Dth recourse rate. It states that notice of the application was published in the *Federal Register* on January 24, 2001. Trailblazer states that while Marathon had already announced its acquisition of Pennaco, which had successfully bid for Expansion 2002 capacity, Marathon did not intervene in the proceeding to protect its interests.

37. Trailblazer points out that the Commission issued Trailblazer a certificate for its Expansion 2002 project on May 17, 2001, approving Trailblazer's proposed recourse rate of 12.19 cents/Dth as an initial NGA section 7 rate. Trailblazer states that it filed a tariff sheet setting forth the relevant terms of all negotiated rates contracts on March 8, 2002. It asserts that there were no protests to the Commission's acceptance of the tariff sheets. Trailblazer states that it commenced Expansion 2002 service on May 7, 2002.

38. Trailblazer contends that Marathon closed on the Pennaco acquisition in March 2001, at which time it states Marathon had the open season materials and, therefore, presumably knew that a recourse rate had not been included. Further, Trailblazer states that Marathon executed the negotiated rate contract for the capacity awarded to Pennaco on July 9, 2002, after the Commission had approved the recourse rate in the issued certificate order. Trailblazer states that Marathon never complained that it should have been offered a recourse rate or that its negotiated rate was too high.

39. Trailblazer states that in May 2002, Marathon acquired additional Expansion 2002 capacity from CMS Energy via capacity release. Trailblazer disagrees with Marathon's representation that Trailblazer was not cooperative in agreeing to release CMS Energy from its transportation contract. Trailblazer states that it recognizes that under the Commission's regulations, firm shippers must be permitted to release their capacity without restrictions on the terms or conditions of the release.[18] Trailblazer states that

[18] *Citing* 18 C.F.R. § 284.8(b)(2004).

when Marathon executed its agreement with CMS Energy, Marathon ratified the negotiated rate provision of CMS Energy's contract with Trailblazer. Trailblazer asserts that the ratification took place a year after the Commission approved the recourse rate and that Marathon did not complain about the lack of recourse rate in the open season or about not being able to avail itself of the recourse rate as a replacement shipper for CMS Energy.

40. Trailblazer states that on November 29, 2002, it filed a rate case in Docket No. RP03-162. Trailblazer asserts that it served Marathon a copy of the filing and that Marathon protested as a member of Indicated Shippers. Trailblazer states that the filing included a proposed recourse rate for the Expansion 2002 capacity. It contends that Marathon's petition to intervene and protest did not mention the lack of a recourse rate in Trailblazer's open season in August 2000.

41. Trailblazer states that during its rate case, Marathon did assert that the Commission should take into account the fixed negotiated rates paid by the Expansion 2002 shippers in setting Trailblazer's return on equity, but Marathon did not challenge the negotiated rates themselves. Trailblazer states that the first time Marathon ever raised the issue of lack of a recourse rate in the open season before the Commission was in rebuttal testimony Marathon submitted later in the rate case on September 22, 2003.

42. Trailblazer asserts that for three years after the August 2000 open season, and for over a year after the Expansion 2002 facilities went into service, Marathon remained silent on the question of whether a recourse rate should have been offered in the open season. Trailblazer states that throughout that time, basis differentials between CIG-Rocky Mountains and NGPL Amarillo Receipt were far greater than the transportation rate Marathon was contractually obligated to pay Trailblazer.[19] Specifically, Trailblazer contends that: (1) in August 2000, at the time of the open season, the average monthly basis differential was $1.18; (2) at the time Trailblazer entered into the precedent agreements in December 2000, the basis differential was $1.07; (3) at the time it filed its certificate application the basis differential was 34 cents; (4) at the time Marathon acquired Pennaco and its expansion capacity the basis differential was 79 cents; (5) at the time Marathon agreed to pay the 24 cent rate to succeed to the CMS Energy contract the basis differential was $1.60; and (6) at that time Trailblazer filed its rate case the basis differential was $1.33. Trailblazer asserts that

[19] Trailblazer states that its basis differentials were calculated using monthly averages of data from Gas Daily for commodity prices between "CIG, Rocky Mountains" and "NGPL Amarillo Receipt". Trailblazer's differential calculations are set out in Exhibit 3 of its answer.

Marathon raised the issue for the first time after the basis differential dropped to 48 cents in August 2003 and 40 cents in September and October 2003. Trailblazer concludes that once the profitability of Marathon's contracts with Trailblazer were reduced because of the changes in the basis differentials, Marathon, through Indicated Shippers, sought Commission intervention to reduce the transportation rates.

43. Trailblazer states that Marathon, the largest oil producer in Wyoming and the largest coalbed methane leaseholder in the Power River Basin, is not an unsophisticated consumer. Trailblazer states that Marathon reaped substantial profits because its negotiated fixed rate contracts with Trailblazer contains rates well below the basis differentials that have generally prevailed since the Expansion 2002 went into service. Trailblazer calculated that through March 2005, Marathon had the opportunity to make over $68 million in profits based solely on the basis differential. Trailblazer concludes that because the market conditions have changed so that Marathon is unable to make as much money as before, Marathon devised its strategy of seeking a Commission order reducing Marathon's transportation rates for the Expansion 2002 capacity. Trailblazer asserts that the Commission should not countenance Marathon's attempt to eviscerate freely negotiated contracts.

44. Trailblazer emphasizes that different rates for different shippers are not *per se* unduly discriminatory. Specifically, it argues that in the context of a capacity auction for an incrementally priced project, different rates should be expected. Trailblazer states that the Commission previously found that under the NGA, discrimination is undue and therefore violates the NGA when "there is no underlying factual or equitable basis for the difference."[20] It further states that the "mere fact of a rate disparity [between customers receiving the same service] does not establish unlawful rate discrimination", and that "rate differences may be justified and rendered lawful by facts."[21]

45. Trailblazer contends that Marathon, and all the Expansion 2002 shippers, are paying rates based on the open season bids, which were filed with the Commission. It states that the shipper's bids were based on their level of interest in the proposed expansion project, the amount of capacity they anticipated needing, the anticipated value-added that capacity on the expansion facilities would provide to them as shippers, as well as other considerations unique to each individual shipper. Trailblazer asserts that

[20] *Citing Great Lakes Transmission Limited Partnership,* 62 FERC ¶ 61,101 at 61,720 (1993).

[21] *Citing Cities of Bethany v. FERC*, 727 F.2d 1131, 1138 (D.C. Cir. 1984).

awarding capacity to the highest bidder is consistent with the Commission's goal of ensuring that capacity goes to shippers who value it the most.[22] Trailblazer states that there is nothing to suggest that Marathon's negotiates rates are unduly discriminatory.

46. Trailblazer states that no shipper at any point in the Expansion 2002 certificate proceeding raised any concerns regarding the lack of an opportunity to bid a recourse rate during the August 2000 open season. It states that under Commission precedent it is well settled that any complaint about an open season should be made at the time the certificate application is filed.[23] Trailblazer argues that any assertion by Marathon that it did not know that no recourse rate was offered in the open season is implausible. It states that Marathon announced its acquisition of Pennaco in December 2000 and completed the acquisition before the Commission issued the Expansion 2002 certificate order. Trailblazer contends that Marathon could have reviewed the contracts held by Pennaco prior to acquiring that company. Trailblazer further asserts that by not seeking rehearing of the certificate order, Marathon is precluded from subsequently challenging that order.

47. Trailblazer states that the Commission should dismiss Marathon's complaint because it does not provided documentation specifically relevant to the complaint. It claims that there are numerous allegations that are not supported by evidence. Specifically, Trailblazer stated that the court affirmed dismissal of claims because the "allegations, upon analysis, were just that. They were assertions of counsel, not evidence."[24] Trailblazer states that the Commission has held likewise.[25]

48. Trailblazer asserts that if pipelines cannot rely on deals agreed to by the customers and approved by the Commission, pipelines cannot make long-term commitments to construct new capacity. It contends that while the Commission is permitted to revise its policy, it should not do so in a manner that retroactively undoes freely negotiated, Commission-approved contracts.

---

[22] *Citing Northern Natural Co.,* 109 FERC ¶ 61,388 (2004).

[23] *Citing Kern River Gas Transmission Co.,* 96 FERC ¶ 61,012 (2001).

[24] *Citing Brown v. Immigation and Naturalization Serv.* 775 F.2d 383, 388 (D.C. Cir. 1985).

[25] *Pacific Gas and Elec. Co.,* 108 FERC ¶ 61,304 at P 9 (2004).

ISSUES

49. The issues raised by the complaint may be framed as follows:

> (1) Did Trailblazer's failure to offer a recourse rate during its open season for its Expansion 2002 service violate the Commission's Alternative Rate Policy Statement and Trailblazer's tariff.
>
> (2) Should the Commission, under NGA section 5, modify the negotiated rate contracts.

DISCUSSION

A. Trailblazer's Open-Season

50. As stated, Marathon argues that Trailblazer violated the Commission's Alternative Rate Policy Statement and its tariff by not providing a recourse rate during its August 2000 open season for the Expansion 2002 capacity. Trailblazer contends that prior to the Commission's October 31, 2002 decision in *Natural*, the Alternative Rate Policy Statement applied only to existing pipeline capacity.

51. In response, Marathon argues that the Commission's Alternative Rate Policy Statement addressing negotiated rates made no distinction between existing and expansion capacity and that no rational distinction can be made. Marathon contends that the Commission assumes the existence of market power in any transaction in which rates are negotiated.[26] Therefore, Marathon concludes that a pipeline's market power must be mitigated if it intends to negotiate rates and that the Alternative Rate Policy Statement places great emphasis on the fact that shippers must retain their ability to choose cost-of-service based recourse rates any time a pipeline seeks to negotiate rates.

52. Marathon emphasizes that the Commission rejected arguments in the *Natural* proceeding similar to Trailblazer's argument that the Alternative Rate Policy Statement was not intended to apply to new capacity. Therefore, Marathon argues that there never was an exception for expansion service, as the authority to negotiate any rate for any service is predicated on the availability of a recourse service.

---

[26] *Citing Trunkline Gas Co.*, 78 FERC ¶ 61,012 at 61,051 (1997).

53. When the Commission issued the Alternative Rate Policy Statement in 1996, it stated that it was exploring the criteria it should use when evaluating rates established through methods other than the traditional cost-of-service ratemaking method. While the Policy Statement stated that requests may be made for new or existing contracts, it also stated that pipelines:

> must use their *existing* Commission approved tariff rates applicable to the service as their recourse rates . . . . The recourse rate will be available for *existing* capacity holders that do not negotiate a rate with the pipeline, thereby ensuring that *existing* customers will always have a cost-of-service based rate available for capacity they have under contract.[27]

54. The Alternative Rate Policy Statement also specifically stated that the Commission intended to apply its negotiated/recourse rate programs on a "shipper by shipper" basis.[28] On rehearing, the Commission stated:

> The purpose of the Policy Statement was to provide the industry with guidance by stating the criteria the Commission will consider when evaluating proposals for alternative ratemaking methodologies. In stating the evaluation criteria, the Policy Statement also conveyed the Commission's intent to evaluate the specific proposals based on the facts and circumstances relevant to the applicant and to address any concerns regarding the application of the criteria on a case-by-case basis.[29]

---

[27] *Alternative Rate Policy Statement,* 74 FERC at 61,241(emphasis added).

[28] *Id.*

[29] *Alternative Rate Policy Statement,* 75 FERC ¶ 61,024 at 61,076 (1996).

55. As such, the Commission opted to implement the policy and address various issues and arguments concerning negotiated/recourse rates in specific cases where those issues became apparent.[30] The court subsequently affirmed the Commission's intent to implement its negotiated rate policy on a case-by-case basis.[31]

56. Subsequently, in response to a protest filed in *Natural*, the Commission, for the first time, addressed the issue of requiring a recourse rate during an open season for new capacity made available at a negotiated rate. The Commission determined in *Natural,* as a matter of policy and thereby creating precedent, that shippers should have a recourse rate option during an open season in which a pipeline was seeking negotiated rate agreements for new capacity. Prior to the *Natural* order, the Commission had not specifically addressed the issue of the availability of a recourse rate during an open season in which the pipeline was soliciting negotiated rates. The Commission confirmed this in a footnote in a subsequent order issued in *Kinder Morgan Interstate Gas Transmission LLC.*,[32] where the Commission stated:

> Kinder Morgan held a second open season because its initial open season, which only solicited negotiated fixed rate bids, *preceded the Commission's decision* requiring that a pipeline soliciting negotiated fixed rate bids in an open season must also provide the option of recourse rate bids.[33]

57. In Pacific Gas and Electric Company v. FPC,[34] the court stated that:

> An administrative agency has available two methods for formulating policy that will have the force of law. An agency may establish binding policy through rulemaking procedures by which it

---

[30] *See, e.g., Algonquin Gas Transmission Co.,* 91 FERC ¶ 61,169 (2000)(stating it is within the Commission's discretion to apply its policy prospectively).

[31] *Burlington Res. Oil & Gas Co. v. FERC,* No. 96-1161,1998 U.S. App. Lexis 20697 (D.C. Cir. July 20, 1998). In an unpublished opinion, the court stated that the Alternative Rate Policy Statement is just a general statement of policy having neither a binding legal effect nor a significant and immediate impact. *Id.,* at * 29-30.

[32] 104 FERC ¶61,266 (2003).

[33] *Id*. at n.1 (emphasis added).

[34] 506 F.2d 33 (D.C. Cir. 1974).

> promulgates substantive rules, or through adjudications which constitute binding precedents. A general statement of policy is the outcome of neither a rulemaking nor an adjudication; it is neither a rule nor a precedent but is merely an announcement to the public of the policy which the agency hopes to implement in future rulemakings or adjudications. A general statement of policy, like a press release, presages an upcoming rulemaking or announces the course which the agency intends to follow in future adjudications.[35]

58. The court further explains that a statement of policy does not create a binding norm. It does not determine issues or rights that it addresses and the agency cannot apply or rely on a statement of policy as law.[36] The court stated that:

> A policy statement announces the agency's tentative intentions for the future. When the agency applies the policy in a particular situation, it must be prepared to support the policy just as if the policy statement had never been issued. An agency cannot escape its responsibility to present evidence and reasoning supporting its substantive rules by announcing binding precedent in the form of a general statement of policy.[37]

59. Trailblazer held its open season in August 2000, filed its application on January 10, 2001, received authorization to construct the facilities from the Commission in May 2001, constructed the facilities and commenced service in May 2002. The *Natural* order was issued in October 2002.

60. As stated, in the Alternative Rate Policy Statement, the Commission stated its intention to develop its negotiate/recourse rate policy on a case-by-case basis. The *Natural* proceeding was a case of first impression. It was the first time the Commission introduced and specifically required a recourse rate during an open season for new pipeline capacity. While we found in the *Natural* decision that the objectives of the Alternative Rate Policy Statement made it appropriate to require that a recourse rate be available as a bid option during an open season in which a pipeline was seeking negotiated rates for expansion capacity, we do not find Trailblazer's interpretation of the

[35] *Id.* at 38 (footnotes omitted).

[36] *Id*.

[37] *Id.* at 38-39 (footnote omitted).

Alternative Rate Policy Statement unreasonable. In fact, the *Natural* proceeding demonstrates that there was confusion and uncertainty as to the whether a recourse rate was necessary during an open season for new incremental capacity.

61. When Trailblazer announced its open season without identifying a recourse rate, any interested person had the opportunity to seek guidance from and intervention by the Commission. When Trailblazer filed its proposed recourse rate with its certificate application, all parties received sufficient notice and opportunity to raise their concerns in that proceeding. All contracting parties, including Marathon, knew or should have known the applicable recourse rate before entering into final contracts for the Expansion 2002 capacity. Therefore, we conclude that Trailblazer's failure to provide a recourse rate during its open season does not warrant a finding that it violated its tariff or the Commission's policy at that time

B. Negotiated Rate Contracts

62. Marathon contends that the rates under its contracts for the Expansion 2002 capacity were the direct result of Trailblazer's exercise of market power, and that the Commission, therefore, should invalidate the rate charges under those contracts and require that Trailblazer provide service under the applicable recourse rate. Marathon states that if the Commission does not grant its request to require Trailblazer to continue service at the current recourse rate, the Commission should find that the rates in Marathon's contracts for the Expansion 2002 capacity are unduly discriminatory. In that case, Marathon requests that the Commission lower the rates under the contracts to 17.8 cents/Dth, the lowest negotiated rate awarded to an Expansion 2002 shipper.

63. To modify the rates in Marathon's existing negotiated rate contract, the Commission would have to take action under NGA section 5. Based on the reasons set forth below, we find that Marathon has failed to provide sufficient justification for the Commission to exercise its discretion to invoke NGA section 5 to invalidate Marathon's negotiated rate contracts.[38] The Commission permits negotiated rates that exceed a pipeline's recourse rates,[39] and has determined there are legitimate reasons for shippers to choose negotiated rates that exceed the maximum recourse rate.[40] Moreover, the

[38] *See General Motors Corp. v. FERC*, 613 F.2d 939, 944 (D.C.Cir. 1979) (finding an administrative agency's decision whether to exercise its authority under NGA section 5 is committed to the agency's discretion).

[39] *Missouri Interstate Gas, LLC*, 100 FERC ¶ 61,312 at P 44 (2002).

[40] *PG&E Transmission*, 100 FERC ¶ 61,291 at P 22 (2002).

Commission has determined that under the Commission's negotiated rate policy "the option to pay a rate that deviates from the recourse rate is the customer's, and accordingly, would be considered reasonable."[41] Further, the courts have held the mere fact of a rate disparity does not establish unlawful discrimination, as long as the contracts were entered into in good faith and did not involve improper conduct.[42]

64. Absent a compelling reason, the Commission does not believe it should second-guess the business and economic decisions between knowledgeable business entities when they enter into negotiated rate contracts. Pipelines rely on their contracts and the integrity of the Commission's process in deciding whether to construct new facilities. As such, the Commission is reluctant to upset the expectations of pipelines when they make investment decisions in reliance on the commitments by their customers and the Commission's approval. The Commission is particularly reluctant to upset those expectations after a customer foregoes numerous opportunities to raise issues concerning its contracts in reasonably timely manner in a more appropriate forum.

65. The terms and conditions of Trailblazer's open season, as Trailblazer points out, were widely publicized. The open season announcement was sent to numerous prospective shippers, reported in the trade press, and posted on Trailblazer's web site. The shippers that bid on the available capacity were knowledgeable companies amply aware of the Commission's policies and procedures. As such, the rates in the negotiated contracts were the result of bids tendered under a valid open season. The bids were offered by the shippers who used their own economics and analyses to arrive at these capacity values. The contract rates reflect the bids agreed to by the shipper regardless of what the Commission determined would be the recourse rate.

66. The shippers that negotiated the contracts were not captive customers that needed to rely solely on Trailblazer's expansion project. As noted above, at the time of and shortly following Trailblazer's August 2000 open season, there were several other proposals to increase the pipeline infrastructure in the area, which offered alternatives to Trailblazer's project at comparable rates. Marathon opted to acquire the Pennaco and CMS capacity, arguably based on its belief that the rates under those contracts were not unreasonable. Based on the above reasons, we find the contracts were entered into in good faith as the result of lawful conduct and are not unduly discriminatory.

---

[41] *Id.*

[42] *United Municipal Distributors Group v. FERC*, 732 F.2d 202, at 211-13 (D.C. Cir 1984). *See also Cities of Bethany v. FERC,* 727 F.2d 1131, 1138-1140 (D.C. Cir. 1984).

67. Moreover, we note that during the five years since Trailblazer held it open season in August 2000, Marathon, or any other Expansion 2002 negotiated rate shipper, has had a number of opportunities to raise market power allegations in more appropriate forums before the Commission. First, at the time of the proposed open season, any prospective shipper could have filed a complaint requesting that the Commission require Trailblazer to offer a recourse rate as part of its open season.[43] Second, when Trailblazer filed its certificate application and proposed a recourse rate below the negotiated rates, any negotiated rate shipper could have raised the issue of the absence of a recourse rate as a bid option during the open season.

68. Third, when the Commission issued the certificate order and approved the recourse rate as the initial rate, any party could have filed a request for rehearing of that decision. Fourth, when Trailblazer filed its compliance filing specifically disclosing the applicable recourse rates, upon seeing the differences in rates, any party could have raised the issue of the legality of these rates.[44] Fifth, any party could have raised and pursued issues relating to the absence of an open-season recourse rate in Trailblazer's NGA section 4 rate proceeding.[45] As discussed above, on November 29, 2002, Trailblazer filed tariff sheets initiating its first rate filing less than a year after its 2002 expansion project became operational.[46] Marathon chose to act at none of those junctures, waiting until now to file a complaint.

69. Marathon advocates that it is an integrated energy business and a top-five U.S. oil company with exploration and production activities in several countries.[47] Marathon is a knowledgeable customer that should be well aware of the Commission's policies and procedures. While Marathon did not participate in the open season or intervene in the Trailblazer proceeding, before it committed to purchasing Pennaco it could have

[43] Similarly, any party could have also filed a complaint in response to the June 2000 open season, which also failed to provide a recourse rate.

[44] *See Tennessee Gas Pipeline Co.*, 110 FERC 61,047 at P38 (2005) (noting that when a pipeline files the negotiated rates tariff sheets or contracts under NGA section 4, interested parties may protest if they believe the rates are discriminatory).

[45] *Alternative Rate Policy Statement*, 74 FERC at 61,242.

[46] *Trailblazer Pipeline Co.*, 101 FERC 61,405 at P21 (2002).

[47] http://www.marathon.com/Our_Business/Marathon_Oil_Company/

investigated all the facts and circumstance relating to Pennaco's contractual commitments. Further, it should have been aware of the circumstances behind Trailblazer's open season before it entered into the final service agreement with Trailblazer for the Expansion 2002 capacity reserved by Pennaco under a precedent agreement. Finally, we note that Marathon acquired the CMS Energy capacity in plenty of time to raise its concerns, in a timely manner, during Trailblazer's NGA section 4 rate proceeding, but chose not to.

70. Therefore, in view of the above considerations, we find that Marathon has not provided sufficient justification for the Commission to exercise its discretion to invoke NGA section 5 to invalidate Marathon's negotiated rate contracts. Accordingly, Marathon's complaint is denied.

The Commission orders:

(A) As discussed in the body of this order, the Commission denies Marathon's complaint.

(B) Marathon's answer is accepted into the record.

(C) Marathon's motion requesting that the Commission order Trailblazer to admit or deny, specifically and in detail, each material allegation contained in Marathon's complaint in accordance with section 385.213(c) of the Commission's regulations is denied.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.