UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Gulf South Pipeline Company, LP Docket No. RP05-353-000

ORDER ACCEPTING TARIFF SHEETS SUBJECT TO CONDITIONS

(Issued June 24, 2005)

1. On May 25, 2005, Gulf South Pipeline Company, LP (Gulf South) filed tariff sheets[1] that would allow Gulf South to eliminate the fuel charge on selected transactions. Gulf South's tariff sheets are accepted, effective June 24, 2005, as requested, subject to conditions. Acceptance of this filing benefits Gulf South's existing and potential customers because it will allow Gulf South to compete more effectively with other pipelines in Gulf South's market area and increase throughput on its system.

Background

2. Under its tariff, Gulf South is reimbursed for fuel on an in-kind basis, unless it actually agrees with the customer to be reimbursed in cash. Its current fuel rate is 1.6 percent. In the filing here, Gulf South states that it is steadily losing throughput (170 Bcf since 1999) because of its inability to discount its transportation rate below its fuel rate, which is 1.6 percent of the rising price of natural gas on its system. Gulf South states it competes in a highly competitive market area with numerous intrastate pipelines that do not have the same regulations as Gulf South. Gulf South states that at today's gas prices the established market value for transportation service is less than the fuel rate Gulf South is required to charge. Gulf South states that its inability to eliminate the fuel charge is effectively preventing it from serving certain industrial, power plant and pipeline markets. Gulf South believes that as more LNG is delivered into the Gulf Coast, other entities may have the economic incentive to construct duplicative facilities, rather than fully utilize Gulf South's existing infrastructure.

3. Gulf South currently has authority to charge no fuel for its Lake Charles system.[2] Gulf South filed testimony stating that the Commission accepted Gulf South's proposal

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[1] *See* Appendix.

[2] *See Gulf South Pipeline Co.*, 109 FERC ¶ 61,283 (2004).

after British Gas had already started the process to construct a new pipeline to serve markets that were connected to Gulf South, despite the presence of excess capacity on Gulf South.[3] However, Gulf South states once the Commission accepted Gulf South's proposal to charge no fuel for its Lake Charles system, British Gas entered into a ten-year deal with Gulf South for 200,000 Dth per day. The testimony further states that other customers or potential customers of Gulf South have stated that it would be cheaper for them to build facilities than to transport on Gulf South's system and pay Gulf South's fuel rate on a sustained basis.

Proposal

4. Gulf South requests the flexibility to eliminate its fuel charge on specified transactions posted on its website where, based on Gulf South's operational experience, no incremental fuel is expected to be consumed in the transaction on an aggregate basis at a matrix of receipt and delivery point pairs, and the market value of the posted transaction is less than Gulf South's fixed fuel rate. Gulf South states that it will continue to charge the minimum commodity rate, annual charge adjustment, and the lost and unaccounted for portion of its fuel charges, which is 0.27 percent of gas price. Gulf South states because it does not have a fuel tracker there is no risk of cross subsidization of fuel costs, and states that if a specific no-fuel transaction becomes unprofitable, Gulf South, not its customers, will assume the risk and bear the financial consequences.

5. Gulf South states that Commission policy currently allows pipelines to eliminate the fuel charge only where the pipeline can demonstrate that no fuel is ever used for a specific transaction.[4] However, Gulf South asserts that this policy is too narrow for a reticulated system such as its own, and asks the Commission to consider its unique competitive and operational circumstances.

6. Gulf South has provided testimony[5] which states that Gulf South receives nominations, and then decides how to set up its system, including compression to meet the scheduled nominations. Gulf South proposes to evaluate whether it appears that adding, on an aggregate basis, certain volumes at specific receipt and delivery point pairs would result in incremental fuel being consumed to facilitate those transactions. The affidavit asserts that Gulf South will then be able to estimate on an aggregate basis a group of transactions, which in its reasonable business and engineering judgment will not incur incremental fuel.

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[3] *See* Gulf South May 25 Filing, Affidavit of Stacy Franz.

[4] *See Gulf South Pipeline Co.*, 109 FERC ¶ 61,283 (2004), and *NorAm Gas Transmission Co.*, 70 FERC ¶ 61,269 (1995).

[5] *See* Gulf South May 25 Filing, Affidavit of Kerry Comeaux.

7. Gulf South proposes to post the no-fuel receipt/delivery point pairs matrices on its website for a period of three months, and to post, on a quarterly basis, the volumes that were scheduled using the point pairs listed on the matrix during that three-month period. Gulf South states that each posting will identify the time period during which the fuel charge will be eliminated and the volume of gas that is eligible. Gulf South states that if a customer has contracted for service based on a no-fuel posting, and system operations change so that Gulf South is required to begin to charge fuel, Gulf South will honor its commitment not to charge for fuel for the term of the contract. Gulf South proposes to file with the Commission an annual informational report that summarizes customer usage at these point pairs. Additionally, Gulf South proposes a five-year moratorium on unilaterally seeking to increase its postage stamp fuel charge or modify its fuel rate design. Further, Gulf South proposes that any gas volumes transported under this proposal will be excluded from any fuel rate calculation in a future rate case. Gulf South states that this approach provides future rate certainty while placing the current financial risk on Gulf South.

Notice, Protest and Comments

8. Public notice of Gulf South's filing was issued on May 27, 2005, with comments due on or before June 6, 2005. Notice of interventions and unopposed timely filed motions to intervene are granted under the Rule 214 of the Commission's Rules and Practice and Procedure (18 C.F.R. § 385.214 (2004)). Any untimely motion to intervene filed as of this date of this order is granted. Granting late interventions at this stage of the proceeding will not disrupt the proceeding or place additional burdens on existing parties.

9. On June 6, 2005, Calpine Energy Services, L.P. (Calpine) filed a protest, and United Municipal Distributors Group filed comments. In addition, comments in support of the filing were filed by Mobile Gas Service Corporation , Willmut Gas Company , City of Vicksburg, Bay Gas Storage Company, Ltd. , and CenterPoint Energy Entex. On May 31, 2005, Gulf South filed copies of letters it received from five customers in support of the filing.[6] Gulf South filed an answer responding to Calpine's concerns. We are not persuaded to accept Gulf South's answer and will, therefore, reject it.

10. Calpine states that it would not oppose the filing if the following changes are made to alleviate the potential for cross-subsidization: (1) Gulf South should be required to include the non-fuel usage determinants when deriving fuel rates, thus ensuring that they are not unduly understated, and that the pipeline is aware that it bears the ultimate cost responsibility for any un-recovered fuel; (2) Gulf South should bear the burden of proof in proposing to remove any non-fuel service usage determinants when deriving a future

[6] The five companies are CenterPoint Energy Resources Corp., UMDG, Epoch Energy Group, L.P., Murphy Gas Gathering, Inc., and Air Liquide Large Industries U.S., LP.

fuel rate; (3) Gulf South should reduce its fuel rate by at least 50 percent because its current 1.6 percent fuel rate is overstated; and (4) Gulf South should be required to provide the discount to all "no" or "low" fuel points, and not just those points it believes are competitive.

11. UMDG states that it supports Gulf South's filing premised on several representations made in the filing: (1) Gulf South will conduct its assessment of requests for fuel discounts in an objective and non-discriminatory manner; and (2) Gulf South will not modify the existing 1.6 percent postage-stamp fuel rate, or propose a change to the rate design for the fuel rate for five years. UMDG also supports allowing the fuel discounting authority to lapse at the end of five years, unless Gulf South extends the fuel charge moratorium for an additional period.

12. UMDG is concerned about the long-term effects on captive customers, and urges the Commission to condition its approval of the proposal so that Gulf South may not implement a fuel tracking mechanism while no-fuel transactions are available. Ultimately, UMDG urges the Commission to approve Gulf South's filing, stating that it will provide Gulf South with a means to recapture the dramatic levels of lost industrial and power plant loads, which will enhance Gulf South's ability to serve all customers while placing the financial risks of the no-fuel transactions program on Gulf South.

13. The supporting customers all expressed concern about Gulf South's declining throughput due to Gulf South's inability to compete for load because of its high fuel rate, stating that they support Gulf South's proposal, and calling it "the appropriate approach." They state that approval of Gulf South's proposal will allow Gulf South to price its transportation more competitively to regain lost markets and to increase throughput, while fostering markets for competitively priced transportation alternatives and greater access to new gas supplies entering the U.S. Gulf Coast.

Discussion

14. The Commission finds that Gulf South's proposal will enhance its competitiveness in the highly competitive area in which Gulf South operates to the benefit of its customers and, with the safeguards discussed below, is just and reasonable. In Order No. 436,[7] the Commission announced that it was impermissible for a pipeline to provide service at a rate that would not allow it to recover the variable costs of the service. section 284.10 of the Commission's regulations now codifies this policy, stating that the minimum rate "must be based on the average variable costs which are properly allocated

[7] *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, FERC Stats. and Regs., Preambles 1982-1985 ¶ 30,665 (1985).

to the service to which the rate applies."[8] However, the Commission has allowed pipelines to establish a fuel charge of zero for transportation transactions identified in their tariffs provided they have made a showing that the transactions do not require the use of compressors or consumption or fuel in other gas handling equipment on their systems. Typically, these exemptions have been granted to long-line pipelines for backhauls or at locations where compression is provided by connecting pipelines.[9]

15. The Commission has recognized that Gulf South's system is reticulated, and that it is not possible to chart the specific mileage or fuel use for a specific shipment of gas:

> [I]t is not possible to determine the mileage of a haul of specific gas shipments on [Gulf South's] system. This is due to the web-like configuration of the system and the bi-directional flows that take place on it. Nor is it possible to attribute specific fuel use to any one shipment of gas… Since the mileage gas travels cannot be measured and since fuel use cannot be attributed to specific shipments of gas it is reasonable to use a postage stamp rate for fuel.[10]

The Commission later concluded:

> [Gulf South's] system is a web or grid with interspersed production and market areas rather than a single long line from a production area to a market area. The web like configuration of the system results in gas flows that are bi-directional… For the same reasons, it is not possible to attribute specific fuel use to any one shipment of gas… The actual amount of fuel consumed is a function of all of the transportation transactions which are occurring on the system, not necessarily of the distance of any particular haul. Thus, on [Gulf South], fuel use cannot be attributed to specific shipments of gas or to distance of haul.[11]

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[8] *See* 18 C.F.R. § 284.10(c)(4) and (5) (2004).

[9] *See Mississippi River Transmission Corp.*, 98 FERC ¶ 61,119 (2002) (pressure in Clay County will be provided by Trunkline and/or Natural, not by MRT); *Williams Natural Gas Co.*, 75 FERC ¶ 61,023 (1996) (transactions involved are backhauls requiring no compression or consumption of any incremental fuel).

[10] *See Koch Gateway Pipeline Co*., (predecessor to Gulf South) 84 FERC ¶ 61,143 (1998).

[11] *See Koch Gateway Pipeline Co*., 85 FERC ¶ 61,426 (1998).

16. Although the Commission makes no finding here with respect to Gulf South's claim that it can model its system such that it can determine if certain transactions will not incur incremental fuel, we believe Gulf South should be given the opportunity to implement its proposal in order to be able to compete more effectively with other pipelines including intrastate pipelines in Gulf South's market area. In view of the wide support for the proposal, the concern about the rapidly-dropping throughput level expressed by numerous parties, and because the proposal protects the customers by placing the risk of under-recovery of fuel costs on Gulf South, the Commission will accept Gulf South's proposal, as conditioned below.

17. Regarding Gulf South's proposal to exclude non-fuel volumes from future fuel rate filing calculations, and Calpine's protest thereto, we decline to rule here on the design of future fuel rates as that is an issue more appropriate for a future fuel rate filing proceeding. However, Gulf South is on notice that it bears the risk of under-recovery of fuel costs as a result of the instant rate proposal and bears the burden to prove that any future fuel rate filing proposal is just and reasonable and not unduly discriminatory. As part of that burden, Gulf South will bear the burden to show that its proposed rates do not result in the subsidization of any customer class. In addition, the Commission finds that Calpine's request to reduce Gulf South's existing 1.6 percent fuel rate is unsupported and, accordingly, reject it.

18. We also reject Calpine's request that the Commission require Gulf South to eliminate fuel charges at all "no" or "low" fuel "qualifying points", not just those points that Gulf South considers competitive. Gulf South states in its filing that, because analyzing every possible point pair combination across the system is impractical, its analysis will typically focus on markets that are accessed by both Gulf South and intrastate pipelines coming from incremental receipt points. We decline to require Gulf South to continually analyze every point on its system, including those where the need for a rate reduction is not required to meet competition, to eliminate fuel at all "qualifying points". However, Gulf South must operate its fuel program in a non-discriminatory manner. Should Calpine believe that Gulf South's program is not being operated in a non-discriminatory manner, Calpine can file a complaint with the Commission.

19. The Commission accepts Gulf South's five-year fuel rate moratorium proposal. As a result, Gulf South has promised not to unilaterally seek to increase its postage stamp fuel charge or modify its fuel rate design or file a fuel tracker for a period of five years. However, the Commission retains the right to review and modify Gulf South's fuel rates under section 5 of the Natural Gas Act.

20. Finally, we will not require Gulf South to file an annual report as we find that the quarterly postings it proposes to make are sufficient to monitor its program.

The Commission orders:

The tariff sheets listed in the appendix are accepted, effective June 24, 2005, subject to conditions of this order, as discussed above.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.

APPENDIX

Gulf South Pipeline Company, LP
Docket No. RP05-353-000

FERC Gas Tariff, Sixth Revised Volume No. 1
Tariff Sheets Accepted, Effective June 24, 2005

Tenth Revised Sheet No. 20
Seventh Revised Sheet No. 21
Seventh Revised Sheet No. 22
Seventh Revised Sheet No. 23
First Revised Sheet No. 103
First Revised Sheet No. 104
Second Revised Sheet No. 105
First Revised Sheet No. 106
Second Revised Sheet No. 202
First Revised Sheet No. 203
Second Revised Sheet No. 204
Original Sheet No. 205
Sheet Nos. 206 - 299