

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

SFPP, L.P.

Docket No. IS05-327-002

ORDER ON REHEARING

(Issued December 12, 2005)

1. On June 30, 2005, the Commission issued an Order Accepting and Suspending Tariffs, Subject to Refund and Conditions (June 30, 2005 Order).¹ The June 30, 2005 Order addressed tariffs filed by SFPP, L.P. (SFPP) pursuant to the Commission's indexing methodology set forth in section 342.3 of the Commission's regulations.²
2. In the June 30, 2005 Order, the Commission found SFPP's filing to be consistent with the Commission's indexing regulations and that Indicated Shippers³ had not shown that the indexed rates proposed by SFPP were so substantially in excess of the pipeline's actual cost increases as to render the resulting rates unjust and unreasonable. However, the Commission ordered SFPP to file an updated Page 700 to its 2003 FERC Form 6, after which the parties could file additional comments. Finally, the Commission rejected Indicated Shippers' assertion that SFPP was not entitled to an income tax allowance in 2004, finding that Indicated Shippers inconsistently applied the tax allowance treatment they advocated.
3. On July 14, 2005, SFPP filed its corrected Page 700. SFPP asserted that the corrected Page 700 reflected a slightly changed 2003 interstate cost of service attributable to a modest change in its depreciation expense.⁴ SFPP stated that the final corrected 2003 cost of service value is \$109,188,314, as compared to the 2004 value of

¹ *SFPP, L.P.*, 111 FERC ¶ 61,510 (2005).

² 18 C.F.R. § 342.3 (2005).

³ BP West Coast Products LLC and ExxonMobil Oil Corporation.

⁴ In SFPP's July 14, 2005 filing, the updated Page 700 reflects changes to line numbers 3, 4, 5, 6, and 8. The footnotes indicate that SFPP is restating the 2003 Cost of Service results to reflect a 100-percent tax allowance.

\$109,594,987, which represents a change of 0.37 percent. According to SFPP, the difference between the change in the index and the change in costs (approximately 3.25 percent) indicates that the rate increase is not so substantially in excess of its cost increases that it renders the increased rate unjust and unreasonable.

4. On July 25, 2005, Indicated Shippers filed comments challenging SFPP's revised Page 700, or in the alternative, seeking rehearing of the June 30, 2005 Order. As discussed below, the Commission is treating Indicated Shippers' filing as a request for rehearing. On August 5, 2005, SFPP filed a reply to Indicated Shippers' comments, and on August 12, 2005, Indicated Shippers filed an answer to SFPP's reply. While the Commission's regulations prohibit answers to requests for rehearing, the Commission finds that the responsive filings provide additional clarification of the parties' positions; therefore, the Commission will accept the responsive filings.

5. As discussed below, the Commission denies rehearing of the June 30, 2005 Order.

Discussion

6. On rehearing, Indicated Shippers argue that, in the June 30, 2005 Order, the Commission rejected their original protest without a reasoned decision based on substantial evidence. Indicated Shippers also contend that the revised Page 700 to Form 6 shows that SFPP does not qualify for indexed rate increases because the increases are so substantially in excess of SFPP's actual cost increases.

A. Whether SFPP Is Entitled to a 100-Percent Income Tax Allowance Under the Commission's Policy Statement on Income Taxes (Policy Statement)⁵

7. Indicated Shippers argue in a variety of ways that the *Policy Statement* does not apply to SFPP, which is part of Kinder Morgan Energy Partners, a master limited partnership (MLP) holding company structure that is a registered tax shelter. Indicated Shippers maintain that they have shown that such MLPs reap vast amounts of income, but flow through little or no taxable income to investors. Indicated Shippers also question whether the Commission has approved a 100-percent corporate income tax allowance for SFPP, which Indicated Shippers maintain would be contrary to the *Policy Statement* and *BP West Coast Products, L.L.C. v. FERC*.⁶

⁵ 111 FERC ¶ 61,139 (2005).

⁶ 374 F.3d 1263, 1288 (D.C. Cir. 2004).

8. Indicated Shippers improperly raise in this proceeding their claims regarding applicability of the *Policy Statement* and whether SFPP is entitled to a 100-percent tax allowance. First, this proceeding involves only proposed indexed increases to rates, and the only relevant issue is whether the amount of the increase in SFPP's indexed rates is so substantially in excess of SFPP's actual cost increases that it renders the resulting rates unjust and unreasonable.⁷ The tax allowance challenged by Indicated Shippers is a component of SFPP's underlying base rates; therefore, it is not properly subject to examination in this proceeding. Moreover, Indicated Shippers have challenged SFPP's entitlement to a 100-percent income tax allowance in Docket No. IS05-230-000, which involves a tariff filing with a cost-of-service justification.⁸ The Commission set that issue for hearing, as well as other issues raised by, *inter alia*, Indicated Shippers, and the matter is currently pending before a Presiding Administrative Law Judge. That rate proceeding, not this proceeding concerning indexed rates, is the proper proceeding in which to address the eligibility for and the level of an income tax allowance.⁹

B. Whether SFPP's Proposed Indexed Rate Increases Are Excessive

9. Indicated Shippers assert that the Commission improperly rejected their original protest partly because it believed Indicated Shippers failed to employ comparable income tax allowance data. On the contrary, argue Indicated Shippers, their protest calculated the change in costs from 2003 to 2004 without any income tax allowance included in either year's figures. Thus, Indicated Shippers contend that their "apples to apples" comparison showed a substantial decrease of \$1,100,195 in SFPP's claimed cost of service. Indicated Shippers maintain that their calculation was fair to SFPP, but the Commission did not

⁷ 18 C.F.R. § 343.2(c)(1) (2005) provides as follows:

A protest or complaint filed against a rate proposed or established pursuant to [the indexing rules] must allege reasonable ground for asserting that the rate violates the applicable ceiling level, or that the rate increase is so substantially in excess of the actual cost increases incurred by the carrier that the rate is unjust and unreasonable

⁸ *SFPP, L.P.*, 111 FERC ¶ 61,299 at P 8-9 (2005). In the June 30, 2005 Order, the Commission also observed that SFPP's base rates are at issue in other proceedings. *SFPP, L.P.*, 111 FERC ¶61,510 at P 15 n.15 (2005).

⁹ In the *Policy Statement*, the Commission specifically addressed the question of whether the partners of MLPs have actual tax liability for any income recognized by the partnership. The Commission cautioned that such matters "can present complex allocation and timing issues that would be addressed in individual rate proceedings." *Policy Statement on Income Tax Allowances*, 111 FERC ¶ 61,139 P 37 n.35 (2005).

address their fundamental arguments that SFPP is not entitled to an indexed rate increase in rates that are already excessive and for the most part no longer subject to grandfathering.

10. Indicated Shippers state that SFPP now claims that its actual cost increase is 0.37 percent. However, Indicated Shippers assert that this percentage rate is 9.7 times greater than the claimed cost increase percentage (.036288/.003725) and cannot be justified. Indicated Shippers submit that it would be arbitrary and capricious to grant a \$4.5 million rate increase to cover an increase in costs of \$0.5 million. Indicated Shippers further claim that, because the rate increase is tied to inflation, which has remained low -- approximately three percent -- the “substantial” test has to be considered within that range.

11. Indicated Shippers continue to misinterpret the Commission’s indexing procedures. It is only the percentage of the indexed increase in rates that is at issue here; therefore, Indicated Shippers’ references to the actual dollar amounts of costs or rates are misleading without reference to the percentages of cost increases and rates they represent. If Indicated Shippers wish to challenge the underlying rates, they may do so by filing a complaint; as stated above, Indicated Shippers’ underlying rates are not properly before the Commission in this order and are being addressed in other proceedings.

12. In the June 30, 2005 Order, the Commission found that the indexed rate increases proposed by SFPP do not violate the applicable ceiling levels, which would permit an increase of approximately 3.63 percent. This percentage is based on the increase in the Producer Price Index for Finished Goods, not the general level of inflation, as Indicated Shippers contend.

13. In the June 30, 2005 Order, the Commission found that SFPP had calculated a 0.43 percent change to its interstate cost of service. SFPP’s revised page 700 reflects a lower increase -- 0.37 percent -- in these costs. SFPP contends that the difference between the change in the index and the change in its costs, approximately 3.25 percent, is not so substantially in excess of its cost increases as to render the resulting indexed rates unjust and unreasonable. The Commission finds that SFPP is correct and that its proposed indexed increases are not so substantially in excess of the increases in its costs as to render the indexed rates unjust and unreasonable.

C. Alleged Discrepancies in SFPP’s Claims

14. Indicated Shippers also argue that internal discrepancies in the July 14, 2005 submission by SFPP constitute reasonable grounds for asserting that the rate increase is substantially in excess of the actual cost increases. Indicated Shippers point to the original and revised Page 700 data relating to Depreciation Expense, noting that there is no change:

<u>Depreciation Expense (line 2)</u>	<u>2004</u>	<u>2003</u>
Original Page 700	9,676,099	8,945,508
Revised Page 700	9,676,099	8,945,508

15. However, Indicated Shippers state that SFPP made a number of changes in the revised Page 700 for 2003, resulting in the following changes in the difference between the 2004 costs and the 2003 costs:

- (a) AFUDC revised by \$9,756
- (b) Amortization of Deferred Earnings revised by -\$75,524
- (c) Rate Base (provided in detail here)

<u>Rate Base (line 5)</u>	<u>2004</u>	<u>2003</u>
Original Page 700	231,394,049	227,766,955
Revised Page 700	231,394,049	211,568,669
Difference	0	-16,198,286

- (d) Return revised by -\$1,698,605
- (e) Income tax allowance revised by \$5,540,249
- (f) Total cost of service revised by \$3,775,876

16. Indicated Shippers argue that SFPP's pleading did not note any such changes, so the Commission must not rely on the representations made in the pleading.¹⁰ In the view of Indicated Shippers, this should shift the burden back to SFPP to justify its rate increase claims. Indicated Shippers maintain that the Commission denies access by shippers to the costs of service underlying the Page 700s of the Form 6, so the Commission cannot find that the shippers fail to meet their burden of alleging "reasonable grounds."

17. According to Indicated Shippers, this is a public utility which, by its own admission, had "excess profit" of \$16,980,012 in 2004, as SFPP's expert witness, Jaffe, defined that term in Docket No. OR96-2, Exhibit No. SFPP-1 at 42, *et al.* This "excess profit" is the amount that revenues exceeded the claimed cost of service.

¹⁰ SFPP responds that it notified the Commission that one of the corrections it would make to Page 700 would be the \$58,000 difference in depreciation expense. According to SFPP, this difference reduced the 2003-2004 cost increase from 0.43 to 0.37 percent.

18. Indicated Shippers maintain that, because almost all of SFPP's rates are no longer grandfathered, that can no longer shield the review of SFPP's rates. Moreover, state Indicated Shippers, they are challenging only the increment, so grandfathering does not come into consideration.

19. Indicated Shippers calculate that the rate of return on equity allowed SFPP by the Commission, even before this latest rate increase, is about 35 percent. Indicated Shippers further emphasize that, if the proposed rate increase were factored in, the Commission would be approving a nominal rate of return on equity of over 41 percent.¹¹

20. Indicated Shippers further argue that SFPP no longer claims that its actual cost increases exceeded the level of the index, now contending that its actual cost increase percentage is less than half a percentage point. However, Indicated Shippers argue that, to shippers and consumers, a percentage increase of over 900 percent of SFPP's claimed actual cost percentage increase is substantial by any standard.

21. Indicated Shippers note that SFPP asks the Commission to remove the conditions set forth in Paragraphs 13 and 15 of the June 30, 2005 Order, which require SFPP to file the updated Page 700 and accept its proposed rates subject to refund and the outcome of other proceedings. Indicated Shippers are concerned that this will lead the Commission to remove the condition that all of SFPP's indexed rates in this docket be subject to refund and subject to the outcome of the other pending SFPP cases. Indicated Shippers also question the need to remove the condition calling for SFPP to file a revised Page 700 in light of the fact that this has been accomplished.

22. The Commission finds no merit to these claims advanced by Indicated Shippers. First, SFPP has met its burden of proof in this proceeding by demonstrating that its proposed indexed rates are within the Commission's allowed index ceilings. Indicated Shippers retain the burden of proof in any challenge to these indexed rates, and they have not carried that burden in this proceeding. Likewise, in a complaint proceeding challenging SFPP's underlying base rates, Indicated Shippers would bear the burden of proof. In a complaint proceeding addressing the underlying rates, or in a proceeding involving a cost-of-service justification advanced by SFPP, Indicated Shippers could investigate the types of costs reflected on Page 700, subject to appropriate discovery rules. As the Commission noted in the June 30, 2005 Order, Page 700 is intended to be no more than a preliminary screening tool that would permit a shipper to compare proposed changes in indexed rates to the pipeline's cost of service.¹² The Commission reiterates that the underlying costs are not subject to challenge in this proceeding.

¹¹ Indicated Shippers attached a workpaper as an appendix to their July 25, 2005 Comments/Request for Rehearing.

¹² *SFPP, L.P.*, 111 FERC ¶ 61,510 at P 13 n. 14 (2005).

23. Moreover, SFPP's alleged rate of return on equity is not before the Commission in this proceeding. Thus, references to testimony or briefs submitted in other proceedings in which the underlying rates are at issue are not persuasive and certainly do not constitute applicable precedent. Until the Commission completes its review of SFPP's underlying rates in other pending proceedings, positions advanced by any of the parties in those proceedings are merely argument and entitled to no weight in this proceeding.

24. Indicated Shippers' concerns regarding the possible removal of conditions imposed in the June 30, 2005 Order are baseless. As Indicated Shippers acknowledge, SFPP met one of the conditions by filing the revised Page 700. However, all tariffs containing rates that are subject to the outcome of other pending proceedings remain subject to that condition.

The Commission orders:

Rehearing of the June 30, 2005 Order is denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.