

UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;  
Sudeen G. Kelly, Marc Spitzer,  
Philip D. Moeller, and Jon Wellinghoff.

SFPP, L.P.

Docket No. IS06-356-001

ORDER ON REHEARING

(Issued December 6, 2006)

1. On June 29, 2006, the Commission accepted, but did not suspend, SFPP's oil pipeline index filing to be effective July 1, 2006, for the index year July 1, 2006, to June 30, 2007.<sup>1</sup> The filing was made pursuant to the Commission's indexing regulations at 18 C.F.R. § 342.3 and the *Notice of Annual Change in the Producer Price Index for Finished Goods* issued on May 18, 2006.<sup>2</sup> SFPP's East Line rates were among those increased through this index filing. SFPP had also previously filed on May 1, 2006, to increase those rates to reflect the construction costs of replacing and expanding the capacity of its East Line. In Docket No. IS06-283-000, the Commission accepted and suspended those rates, subject to refund, to be effective June 1, 2006.<sup>3</sup> As discussed below, the Commission grants rehearing of the index increase of SFPP's East Line rates contained in the June 29, 2006 Order and makes certain of SFPP's July 2006 index increases subject to refund as provided in 18 C.F.R. § 342.39(a) (2006).

**The Requests for Rehearing**

2. Requests for rehearing were filed by Western Refining Company, L.P. (Western Refining) and ConocoPhillips and Valero Marketing and Supply Company, filing jointly (ConocoPhillips/Valero). Western Refining asserts that in this case indexing the East Line rates on June 30, 2006, was arbitrary and capricious and makes no sense under the

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<sup>1</sup> *SFPP, L.P.*, 115 FERC ¶ 61,388 (2006) (Index order).

<sup>2</sup> 115 FERC ¶ 61,295 (2006).

<sup>3</sup> *SFPP, L.P.*, 115 FERC ¶ 61, 283 (2006).

Commission's regulations.<sup>4</sup> It states that new East Line rates were placed in effect on May 31, 2006, and were based on SFPP's actual calendar year 2005 cost-of-service adjusted through September 30, 2006, for known and measurable changes. Western Refining argues that the increase under the index procedures is intended to compensate SFPP for cost increases in 2005 over the costs reported to the Commission for 2004 without having to file a general rate increase. Western Refining argues that since SFPP's rates in effect on June 30, 2006, were based on its actual 2005 costs, there was no increase in costs in that year over East Line costs incurred in 2004. Navajo concludes that this increases the new 2005 East Line rates to a level that is not just and reasonable. ConocoPhillips/Valero argue that the Commission erred in not making the instant index filing subject to refund since most of SFPP's current ceiling rates are subject to refund.

### **Discussion**

3. The Commission will grant rehearing on the grounds that Western Refining has alleged reasonable grounds under section 343.2 of the Commission's regulations to conclude that the resulting East Line rates are so substantially in excess of the actual cost increases incurred by the carrier that the rate increase is unjust and unreasonable. To recapitulate, the Commission's indexing regulations apply an annual index factor to the ceiling rate in effect on June 30 of each year. Because new East Line rates were effective on June 1, 2006, these rates became the ceiling rates against which the index factor was applied on July 1, 2006. SFPP correctly applied the index factor to the new East Line rates. Therefore the only issue is whether the resulting rates were so in excess of the actual cost increases incurred by the carrier that the increase was unjust and unreasonable.

4. The hallmark of the Commission's indexing system is simplicity.<sup>5</sup> This is because the indexing approach allows rates to be changed without a detailed and comprehensive presentation and examination of the individual pipeline's cost of service in each case.<sup>6</sup> Thus, pipelines are able to adjust rates to just and reasonable levels for

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<sup>4</sup> See 18 C.F.R. 342.3 (2006).

<sup>5</sup> Order No. 561 at 30,948. *Revisions to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, FERC Stats. & Regs. [Regs. Preambles, 1991-1996] ¶ 30,985 (1993), 58 F.R. 58753 (Nov. 4, 1993), Order No. 561; *order on reh'g*, Order 561-A, FERC Stats. & Regs. [Regs. Preambles, 1991-1996] ¶ 31,000 (1994), 59 F.R. 40242 (Aug. 8, 1994); *aff'd*, *Association of Oil Pipe Lines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996); *aff'd* *Association of Oil Pipe Lines v. FERC*, 281 F.3d 239 (D.C. Cir. 2002) *order on remand*, *Five-Year Review of Oil Pipeline Pricing Index*, 102 FERC ¶ 61,195 (2003)

<sup>6</sup> *Id.* 30,946.

inflation-driven costs without the need for strict regulatory review of the pipeline's individual cost of service.<sup>7</sup> In fact, under this regulatory regime some divergence between the actual cost changes experienced by individual pipelines and the changes permitted by the index is inevitable.<sup>8</sup> Moreover, the Commission uses Page 700 of FERC Form No. 6 as a screen to compare aggregate revenues, costs, and volumes in one year with the subsequent year. While the indexing method is an efficient method to recover the inflation-driven cost increases occurring in a given year, it is not normally adequate to determine whether any specific rate is just and reasonable. This is because a reasonableness determination requires the detailed regulatory review of the pipeline's individual cost of service and the allocation of those costs among the different services and rates stated in the pipeline's tariff. Thus, the determination Navajo urges here is not normally possible in the context of index proceeding because the specific costs necessary for such a determination are not available. For this reason, the Commission has consistently required a complaint under section 13(1) of the ICA<sup>9</sup> to pursue a determination whether specific rates are just and reasonable.<sup>10</sup>

5. The situation is different here. First, there were no cost increases to SFPP's East Line rates in 2005 because the level of those rates is based on SFPP's actual 2005 costs and its projected East Line volumes, as adjusted to September 30, 2006, for known and measurable changes. Second, as with all new rate filings, the new East Line rates at issue are based on the specific regulatory costs rather than industry wide inflation-driven costs. These new East Line rates are designed to recover all the relevant operating and capital costs based on the throughput stated in SFPP's May 2006 rate filing, including the allowed equity and total regulatory returns. Thus, the additional revenue from the 2006 indexed increase of 6.15 percent results in an over-recovery of SFPP's specific East Line costs in SFPP's May 1, 2006 filing.<sup>11</sup> The real equity return contained in that filing was 9.20 percent and the overall weighted real return was 7.80 percent. As all other 2005 East Line rate costs were covered in the new East Line rates, the application of the 6.15 percent index factor flows directly to the return component of those rates. This increases

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<sup>7</sup> *Id.* 30,948.

<sup>8</sup> *Id.* 30,949.

<sup>9</sup> 49 U.S.C. App. §13(1) (1988).

<sup>10</sup> *See* SFPP, L.P., 111 FERC ¶ 61,510 (2005); SFPP, L.P., 107 FERC ¶ 61,334 (2004); SFPP, L.P., 102 FERC ¶ 61,344 (2003); SFPP, L.P., 96 FERC ¶ 61,332 (2001).

<sup>11</sup> Index order at P 6.

the real equity return to 15.35 percent and the overall return to 13.95 percent.<sup>12</sup> Returns of this size result in East Line rates that are not just and reasonable given that the East line rates effective May 31, 2006, were presumed just and reasonable when filed and are based on actual 2005 costs, including the equity and allowed regulatory returns.<sup>13</sup>

6. As has been discussed, the indexing procedure assures that the carrier does not have to file a general rate increase to recover cost increases that occur from inflation-driven industry-wide costs increases. Since the costs contained on Page 700 of the FERC Report No. 6 reflect the carrier's total costs and revenues, these cannot be used to determine the reasonableness of a specific rate and a shipper must file a complaint to challenge the reasonableness of a specific rate. However here the level of the rate and the embedded return is premised on the carrier's creation of a specific rate that is designed to recover its specific costs. Thus, a complaint proceeding is unnecessary to determine whether the increase to this specific rate was so in excess of the actual cost increases incurred by the carrier that the rate is unjust and unreasonable. SFPP is directed to rescind the indexed increase to its East Line rates and to make refunds accordingly.

7. As noted, ConocoPhillips/Valero argue that SFPP's West Line, North Line, East Line and Sepulveda rates in effect on June 30, 2006 were subject to investigation and refund and that the Commission's regulations require that the index rate be subject to refund.<sup>14</sup> They assert that since the June 29 Order did not make the filing subject to refund, this was error. While the cited regulations speak for themselves, the Commission will amend the Index order to provide that the index increases to West Line, North Line, East Line, and Sepulveda rates are subject to refund. The holding here does not apply to the Oregon Line rates, which were not subject to refund on July 1, 2006.

The Commission orders:

(A) The Commission grants rehearing as stated in the body of this order.

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<sup>12</sup> While the allowed regulatory return is a weighted return of debt and equity, the debt component is fixed by contract and does not change when additional revenue flows to SFPP's net income line. Thus the additional return is added solely to the equity cost component and the total allowed return without further weighting of the debt component.

<sup>13</sup> Under the Interstate Commerce Act newly filed rates are presumed just and reasonable because they are presumed to be based on the carrier's costs. This presumption does not relieve the carrier of its burden to prove that new rates are in fact just and reasonable if the filing is protested and the matter proceeds to litigation.

<sup>14</sup> Citing 18 C.F.R. § 342.3(a) (2006) and Order No. 561, *supra*.

(B) Within 30 days after this order issues, SFPP shall rescind the indexed-based increase to its East Line rates effective July 1, 2006, and make refunds accordingly.

By the Commission.

( S E A L )

Magalie R. Salas,  
Secretary.