UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Northwest Pipeline Corporation Docket No. RP06-394-001

ORDER REJECTING TARIFF SHEETS AND DIRECTING COMPLIANCE FILING

(Issued December 26, 2006)

1. On July 24, 2006, Northwest Pipeline Corporation (Northwest) submitted supplemental information, as required by the Commission's July 14, 2006 Order in this proceeding,[1] to explain proposed changes to its load-factor-based discounted reservation option. Upon further review of Northwest's tariff, the Commission finds Northwest's proposed tariff revisions and its load-factor-based discounted reservation option to be inconsistent with the Commission's rate design policy for reservation charges, and therefore unjust and unreasonable. Accordingly, the Commission rejects Northwest's proposed tariff sheets, and pursuant to section 5 of the Natural Gas Act (NGA),[2] the Commission directs Northwest to submit, within 10 days of the issuance of this order, revised tariff sheets, effective on the date of issuance of this order, to bring its tariff into conformance with Commission policy, as discussed below.

I. Background

2. Under established rate design principles, a two-part rate may have a reservation charge component that is based on contract demand (the capacity the contract entitles the shipper to take) and a volumetric charge that is based on throughput (the shipper's actual usage). Pipelines may enter into discounted rate agreements that use formulas to produce fluctuating transportation rates. However, said rates must conform to the Commission's rate design policy as reflected in the pipeline's tariff. Northwest's tariff has what it calls a "load-factor-based discounted reservation rate option," which has a hybrid reservation charge component that includes a contract demand factor but which varies based on volumetric usage.

[1] *Northwest Pipeline Corp.*, 116 FERC ¶ 61,034 (2006) (July 14, 2006 Order).

[2] 15 U.S.C. § 717d (2000).

3. On June 16, 2006, Northwest filed revised tariff sheets[3] to amend its load-factor-based discounted reservation rate option under section 3.5(a) of Rate Schedule TF-1, and to revise certain discounted reservation rate parameters.[4]

4. Northwest's Rate Schedule TF-1 currently provides for a load-factor-based discounted reservation rate that is equal to a stated amount per Dth times the actual daily load factor for a shipper's use of its contract demand.[5] In its June 16, 2006 filing, Northwest proposed to revise the load-factor-based discounted reservation rate to specify that the actual daily load factor, up to 100%, would be based on the aggregate use of a shipper's contract demand by the shipper and by any capacity release replacement shippers.[6] Northwest stated that it rarely uses the load-factor-based discount option to market available capacity because a shipper with such a rate could avoid paying Northwest for contracted capacity. Northwest explained that a shipper could release its capacity and eliminate its payment obligation to Northwest because its load factor usage would be zero, while at the same time the releasing shipper would retain the right to receive credits for all reservation revenues paid by the replacement shipper.

5. In the July 14, 2006 Order, the Commission accepted the proposed tariff provisions subject to conditions and further explanations. It was not clear how such load-factor-based discounts would operate, and whether a release of capacity under such a contract is appropriate. Releases of capacity are allowed under Commission policy only if the underlying contract rate is a two-part rate with a reservation charge component under which the shipper is reserving the capacity, but not allowed in the case of a one-

[3] FERC Gas Tariff, Third Revised Volume No. 1, Ninth Revised Sheet No 19-A, Third Revised Sheet Nos. 302-C and 302-D.

[4] Those other changes were intended to provide several new "fill-in-the-blank" choices including: (1) a percent of maximum tariff rate under the load factor based discounted rate option; (2) a percent of maximum tariff rate under the fixed discount rate option; (3) a fixed dollar amount less than the maximum tariff rate under the fixed discount rate option; (4) specified time period(s) for the various discounted rate options; and (5) explicit clarification that various combinations of the discounted rate options and specified time periods for these options may be used as many times as needed to define a specific discounted recourse rate transaction.

[5] In other words, if the volumetric usage on a particular day is zero, that day's reservation charge would be zero.

[6] Northwest proposed, in the alternate, to change its tariff to preclude release of capacity that is subject to such to a load-factor-based discounted reservation rate.

part volumetric rate under which there is no such reservation of capacity. Because it was not clear from Northwest's filing if the underlying contract rate was an appropriately designed two-part rate, we conditioned acceptance of Northwest's tariff revisions on Northwest explaining how a releasing shipper can eliminate its payment obligation to Northwest for contracted capacity. In addition, we stated that if no payment is due when the shipper moves no gas or releases the capacity for use by a replacement shipper, then Northwest should explain how the underlying rate is not a one-part rate, and how such a contract would qualify for capacity release under current Commission policy. We directed Northwest to file the required explanatory information within ten days from the date of issuance of the July 14, 2006 Order.

II. Explanatory Filing

6. Notice of the Northwest's July 24, 2006 explanatory filing was issued on July 27, 2006. Interventions and protests were due as provided in section 154.210 of the Commission's regulations, 18 C.F.R. § 385.210. Pursuant to Rule 214, 18 C.F.R. § 385.214 (2006), all timely filed motions to intervene and any motions to intervene out-of-time filed before the issuance date of this order are granted. Granting late intervention at this stage of the proceeding will not disrupt this proceeding or place additional burdens on existing parties. No protests or adverse comments were received.

7. Northwest explains that the discounted reservation rate is computed by dividing the reservation revenues payable (pursuant to a volumetric formula) by the shipper's contract demand. In other words, the discounted daily reservation rate equals a stated amount per Dth times the actual daily load factor for the shipper's use of its contract demand.[7] Northwest states that the resulting discounted reservation rate varies daily based on actual daily load factor. Under the proposed tariff revision, the load factor component of this formula would be based on the aggregate volumetric use of the shipper's contract demand by the shipper and by any replacement shippers. Northwest sought this change so Northwest would be ensured full payment under the hybrid reservation charge.

[7] By way of illustration, Northwest offers the following hypothetical contract with a three-day term:

- Contract Demand = 100 Dth
- Reservation Charge (per Dth of CD) = $0.05 x actual load factor
- Scheduled Deliveries = 50 Dth (Day 1); 0 Dth (Day 2); 100 Dth (Day 3)
- Actual Load Factor = 50% (Day 1); 0% (Day 2); 100% (Day 3)
- Daily Reservation Charge (per Dth of CD) = $ 0.025 (Day 1); $0.00 (Day 2); $0.05 (Day 3)

8. Northwest further explains that its tariff does not currently prohibit a shipper with a load-factor-based discounted reservation rate contract from releasing its capacity to a replacement shipper. According to Northwest, although the load-factor-based discounted reservation rate option results in a reservation rate that varies daily based upon volumetric usage, the reservation component remains separate from the volumetric charge component of the two-part rate. Northwest acknowledges that capacity release shippers paying a one-part volumetric rate are ineligible to release capacity because such shippers are not paying a reservation charge. However, Northwest states that is unclear whether or not this policy applies to contracts subject to its two-part volumetric rates with both a volumetric bid reservation charge plus a volumetric charge under Northwest's tariff.[8]

9. Finally, Northwest argues that, if two-part volumetric-based rate contracts are deemed to be contrary to Commission policy, presumably the rationale for prohibiting releases under such contracts is the lack of a guaranteed revenue stream for reserved capacity. Northwest states that if that is the test, then any contract that simply has its reservation rate discounted to zero, leaving it subject only to the volumetric charge, would also be precluded from making a capacity release, while a contract with a reservation rate discounted to a non-zero negligible rate (*e.g.* $0.00001) would remain eligible for capacity releases.

III. Commission Determination

10. A reservation charge by definition is based on contract demand. Northwest's hybrid reservation charge has a nominal contract demand basis, but varies with usage. In *Northern Natural Gas Company,*[9] the Commission did allow pipelines to enter into discounted rate agreements that use formulas which produce fluctuating transportation rates during the term of the agreement.[10] The Commission stated that such fluctuating transportation rates must reflect the same rate design as the pipeline's tariff.[11] The Commission required Northern Natural to revise its proposal to ensure that all such discount agreements use the same rate design as the pipeline's tariff rates, and provide that any service agreement containing such a discount identify what rate component (*i.e.*, reservation charge or usage charge or both) is discounted.

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[8] *Citing Northwest Pipeline Corp.*, 79 FERC ¶ 61,259 (1997).

[9] 105 FERC ¶ 61,299 (2003) (*Northern Natural*).

[10] *Id.* at P 12.

[11] *Id.* at P 20.

11. The Commission finds that Northwest's load-factor-based reservation option alters its underlying tariff rate design, contrary to the policy established in *Northern Natural*. Section 3.1 of Northwest tariff, applicable to Rate Schedule TF-1 firm transportation service provides for a daily reservation charge, which is charge per Dth of a T-1 shipper's contract demand.[12] Under Northwest's Rate Schedule TF-1 a shipper's contract demand is fixed by its contract and does not vary from day to day. Assuming there are no rate changes, the shipper's overall reservation charge payment for each day's service would remain constant through the term of its contract. On the other hand, Northwest's discounted load-factor-based daily reservation rate is computed by multiplying the stated amount per Dth times the actual daily load factor for the shipper's use of its contract demand. Unlike the underlying tariff reservation charge, which is based on contracted demand, the load-factor-based reservation charge varies based on the actual daily load factor. This formula rate changes the rate design resulting in a purely volumetric (one-part) rate because the discounted reservation charges are assessed based on usage. In practice, this rate is effectively a volumetric rate formula that varies with usage. Accordingly, the Commission finds that Northwest's discounted load-factor-based reservation option does not conform to Commission policy for formula discounts or reservation charge design. To the extent the firm reservation charge is discounted, the formula-based discounted reservation rate must produce a rate per unit of contract demand to ensure that the discounted reservation charge will always be billed based on the shipper's contract demand, as is appropriate for a reservation charge.[13]

12. Northwest states that although the load-factor-based discounted reservation option results in a reservation rate that varies daily based upon volumetric usage, the reservation component remains separate from the volumetric charge component of the two-part rate. However, under Northwest's formula for calculating the discounted rate, when a shipper moves no gas or releases its capacity for use by a replacement shipper, (*i.e.*, load factor

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[12] Section 3.1 of Northwest tariff provides, in pertinent part:

> 3.1 Reservation Charge. (a) For TF-1 (Large Customer) service, the Reservation Charge is the sum of the daily product of Shipper's Transportation Contract Demand as specified in the executed Service Agreement and the Base Tariff Reservation Charge stated on Sheet No. 5 of this Tariff that applies to the customer category identified in the Service Agreement. FERC Gas Tariff, Third Revised Volume No. 1, Ninth Revised Sheet No. 18.

[13] *See Northern Natural*, 105 FERC at P 20.

equals zero) the resulting reservation rate is zero.[14] As noted above, the practical effect of the formula is the elimination of one of the two-components of the two-part rate. Therefore, we reject Northwest's proposed tariff sheet revisions, and find that Northwest's load-factor-based reservation option is inconsistent with Commission policy, is unjust and unreasonable, and Northwest must revise its tariff accordingly.

The Commission orders:

(A) Northwest's proposed tariff sheets are hereby rejected, for the reasons discussed herein.

(B) Northwest is directed to file revised tariff sheets, effective on the date of issuance of this order, eliminating the load-factor-based discounted reservation rate provisions from its tariff, within 10 days of the date of issuance of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.

[14] Northwest's hypothetical about a fixed reservation charge being discounted to virtually nothing is unlikely as it would impair the pipeline's ability to recover the costs for which the shippers have already committed to pay.