128 FERC ¶ 61,082
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

North Baja Pipeline, LLC | Docket No. RP09-779-000

ORDER ON PETITION FOR WAIVER

(Issued July 23, 2009)

1. On June 25, 2009, North Baja Pipeline, LLC (North Baja), Shell Energy North America (US), L.P. (Shell North America) and Gazprom Marketing & Trading USA, Inc. (Gazprom USA) (collectively Petitioners) filed a petition for a limited case-specific waiver of the Commission's capacity release regulations and policies and Paragraph 19 of the General Terms and Conditions (GT&C) of North Baja's tariff, as well as any other waivers or authorizations deemed necessary, in order to allow a permanent release of a portion of Shell North America's firm transportation capacity on North Baja to Gazprom USA at Shell North America's negotiated rate, as well as a long-term, temporary release of the balance of Shell North America's firm transportation capacity to Gazprom USA at such rate. The Commission grants in part and denies in part the requested waivers, as described more precisely below.

Background

2. On October 16, 2007, Shell North America entered into a firm transportation services agreement with North Baja for 207,000 Dth/day of northbound flow on North Baja's pipeline. The contract has a term of twenty years, beginning January l, 2008, with an expiration date of December 31, 2027. The rate for service under this contract is a negotiated rate, fixed for the term of the contract. The rate is levelized over the term of the agreement. The fixed, levelized rate currently is lower than maximum recourse rate for firm transportation on North Baja.

3. The Petitioners state that as part of a larger commercial transaction between affiliates of Shell North America's parent company, Royal Dutch Shell, and Gazprom USA's parent company, OAO Gazprom, Shell North America desires to permanently release 127,160 Dth/day of its capacity to Gazprom USA under the same terms and conditions as set forth in the firm transportation service agreement. Shell North America also desires to temporarily release the remaining 79,840 Dth/day of its capacity to

Gazprom USA under the same terms and conditions as set forth in the firm transportation service agreement. The Petitioners state that various subsidiaries of Royal Dutch Shell and OAO Gazprom have executed agreements giving OAO Gazprom subsidiaries access to the U.S. market through the Energia Costa Azul LNG import terminal in Baja California, Mexico and the Gasoducto Bajanorte Pipeline to the U.S. border and the interconnection with North Baja.

4. The Petitioners state that the negotiated rate under the firm transportation service agreement is a fixed rate that is currently less than North Baja's maximum recourse rate. The Petitioners state that they desire to preserve that bargain for the remainder of the term of the permanent release and temporary release. Accordingly, the Petitioners request limited waiver of the Commission's capacity release regulations and policies and Paragraph 19 of the GT&C of North Baja's tariff, as well as any other waivers or authorizations deemed necessary, in order to allow Shell North America to permanently release 127,160 Dth/day of the contracted-for capacity, and to temporarily release 79,840 Dth/day of the contracted-for capacity, under, in each case, the negotiated rate currently in effect, with such rate to remain in effect for the remainder of the terms of the permanent and temporary releases. The Petitioners state that the Commission's regulations and policies for which they seek a waiver include the Commission's prohibition against tying the release of capacity to other conditions and the bidding procedures for releases of capacity.

5. The Petitioners assert that the circumstances here are appropriate for the Commission to grant such a limited waiver. The Petitioners submit that the permanent capacity release and temporary capacity release from Shell North America to Gazprom USA are part of a complex, multi-party, multi-national arrangement whereby affiliates of both Shell North America and Gazprom USA will buy LNG from the Sakhalin II project in eastern Russia over twenty years for redelivery to markets in the United States, Asia and Europe. The overall transaction includes a new pipeline supply agreement under which a Shell North America affiliate will receive gas for delivery from Russia to Europe. The transaction also includes agreements under which a Gazprom USA affiliate, through long-term assignment from a Shell North America affiliate and Shell North America, will take: (i) certain capacity in Sempra's Energia Costa Azul LNG import terminal in Baja California, Mexico; (ii) certain pipeline capacity in Mexico on the Gasoducto Bajanorte Pipeline; and (iii) certain capacity on the North Baja Pipeline to ship gas to Southern California and/or Arizona. The Petitioners assert this integrated transaction will facilitate the delivery of additional natural gas supplies to U.S. markets, using existing facilities.

6. The Petitioners assert that the waiver will facilitate the importation of new supplies of natural gas into the United States by providing transactional, financial and regulatory certainty to Shell North America, Gazprom USA and North Baja. The Petitioners state that like virtually all firm shippers on the North Baja system, Shell North

America's capacity is contracted under a negotiated rate contract, one that is structured on a levelized rate basis over the life of the contract (expiring in 2027). The Petitioners need confirmation that the economic underpinnings for their long-term relationships will not be changed and that North Baja's capacity will be awarded to the entity committing to the entire chain of supply and transportation, including commitments to the liquefaction and regasification terminals. The Petitioners assert that the Commission has granted requests for waiver under nearly identical circumstances.[1] The Petitioners submit that in order for Shell North America to be released from its obligations pursuant to the permanent release, and to assure that North Baja will receive the benefit of its long-term bargain under the firm transportation service agreement, it is essential that North Baja be financially indifferent to the release. To ensure that North Baja remains financially indifferent, Shell North America's capacity rights on the North Baja Pipeline must be transferred to Gazprom USA at the existing negotiated rate and adequate credit assurances must be put in place prior to the releases.

7. Shell North America, Gazprom USA and their affiliates closed their transaction on April 30, 2009. Shell North America and Gazprom USA desire to effect the permanent release and temporary release described herein as soon as possible after the closing. Accordingly, the Petitioners request expedited issuance of an order on this petition no later than July 24, 2009. The Petitioners submit that such expedited action by the Commission will assist in facilitating their transactions.

Public Notice and Interventions

8. Public notice of the Petitioners' filing was issued on June 29, 2009, providing for interventions, comments, and protests to be filed by July 2, 2009. Pursuant to Rule 214 (18 C.F.R. § 385.214 (2008)), 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 the proceeding or place additional burdens on existing parties.

9. On July 2, 2009, Virginia Power Energy Marketing, Inc. (Virginia Power Energy Marketing) filed a motion to intervene and comments. Virginia Power Energy Marketing states that as a natural gas marketer that is, among other things, in the business of acquiring released capacity in U.S. markets, it has a direct and substantial economic interest in Commission proceedings that waive existing Commission capacity release regulations and policies, or otherwise impact competition for capacity in the secondary market. Although Virginia Power Energy Marketing states that it has not expressed an

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[1] *North Baja Pipeline, LLC,* 111 FERC ¶ 61,119, at P 6 (2005); *North Baja Pipeline, LLC,* 109 FERC ¶ 61,269, at P 1 (2004).

interest in the specific capacity at issue in this case, the precedential value of a Commission decision granting a waiver in this proceeding cannot be ignored.

10. As an initial matter, Virginia Power Energy Marketing points out that it is not protesting the petition. Rather, Virginia Power Energy Marketing is providing comments to request that the Commission clarify and fully explain its policy of granting waivers of capacity release regulations and policies to facilitate certain transfers of capacity in "complex transactions." Virginia Power Energy Marketing submits that additional clarity in this area is needed, particularly at this time of wide-spread economic uncertainties, when many companies are entering into a multitude of complex transactions designed to protect against impacts associated with the global economic downturn.

11. Virginia Power Energy Marketing recognizes that the Commission recently provided additional guidance on capacity release regulation waivers in *Macquarie Cook Energy, LLC* [2] and in the notice issued in Docket No. RM09-7-000 in *Request for Clarification of Policy Regarding Waivers of Applicable Requirements to Facilitate Integrated Transfers of Marketing Business,*[3] and encourages the Commission to continue to elaborate on the facts and "good cause" created by individual factual circumstances, particularly in the instant case where the applicants have requested a rather novel waiver.

12. Virginia Power Energy Marketing asserts while the letter orders cited by the Petitioners emphasize the same general benefits, the factual underpinnings are entirely different, with the exception that they involve a similar general geographic region and North Baja facilities. Virginia Power Energy Marketing submits that the prior waivers on North Baja involved a limited capacity rationalization program undertaken in anticipation of changing supply patterns and that certain of the processes were initiated by the Mexican government. Virginia Power Energy Marketing is unconvinced that other existing Commission precedent is applicable, as neither party appears to be exiting the natural gas business as part of a merger or acquisition or selling an entire U.S. natural gas trading portfolio. Virginia Power Energy Marketing asserts that it is unaware of any other Commission precedent that speaks to the specific type of waiver requested in this proceeding. For this reason, and given that the Commission recently re-affirmed the importance of evaluating the specific circumstances of individual cases, Virginia Power Energy Marketing requests that the Commission carefully consider whether a waiver is appropriate and, if so, narrowly tailor any such waiver so as to provide precedent that protects the transparency and competitiveness of the markets the Commission has done so much to promote in recent years. Finally, Virginia Power Energy Marketing urges the

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[2] 126 FERC ¶ 61,160 (2009) (*Macquarie).*

[3] 127 FERC ¶ 61,106 (2009).

Commission to explain why the transfer of capacity between Shell North America and Gazprom USA could not otherwise be conducted pursuant to, and in accord with, the Commission's capacity release regulations and policies.

Discussion

13. In the petition, the Petitioners are requesting waivers of the Commission's capacity release regulations and policies to permit Shell North America to release to Gazprom USA 127,160 Dth/day of its North Baja capacity on a permanent basis and 79,840 Dth/day of its North Baja capacity on a temporary basis. Both releases would be at a negotiated, levelized rate that is currently less than North Baja's maximum recourse rate for firm transportation service. North Baja, the affected pipeline, supports the waiver. Virginia Power Energy Marketing, an intervener, questions whether Commission precedent supports the waiver and asserts that the transactions can be accomplished under the applicable capacity release regulations.

14. The Commission grants the Petitioners' request for waiver concerning the 127,160 Dth/day of North Baja capacity to be released on a permanent basis. In a recent *Transcontinental Gas Pipe Line* Corporation order,[4] the Commission granted waivers to allow capacity to be released on a permanent basis at a negotiated rate that was in excess of the pipeline's maximum rate. In *Transco*, the Commission stated that it only requires a pipeline to allow a permanent capacity release where the pipeline will be financially indifferent to the release. The Commission stated that where the releasing shipper is paying a negotiated rate in excess of the maximum rate, waiver of the maximum rate is necessary to render the pipeline financially indifferent to the release. The Commission concluded that denial of a waiver request in those circumstances would unnecessarily inhibit the use of permanent releases to transfer capacity that the releasing shipper no longer needs to a shipper that does need it. While the release here is at a negotiated, levelized rate that is currently less than the maximum rate, the rate could be above the maximum rate later. Therefore, North Baja can reasonably conclude that a continuation of the existing negotiated rate is necessary for it to be financially indifferent to a permanent release of Shell North America's capacity. If the Commission were to require that the long-term permanent release be posted for bidding subject to the maximum recourse rate as required by the capacity release regulations, bidders could not offer to pay the existing negotiated rate for the entire term of the release because such a rate could violate the maximum rate during future periods. Therefore, as in *Transco*, denial of a waiver of the bidding requirement for a permanent release would unnecessarily inhibit the use of a permanent release to transfer capacity the releasing shipper no longer needs or wants.

[4] 126 FERC ¶ 61,086 (2009) (*Transco).*

15. The Commission, however, denies the Petitioners' request for a waiver concerning the 79,840 Dth/day of North Baja capacity to be released on a temporary basis. The principles that the Commission discussed in *Transco* are not applicable here. Because the release is on a temporary basis, it is clear that Shell North America is not transferring capacity that it no longer needs. The Petitioners have not explained why the capacity cannot be submitted for posting and bidding, and awarded to the bidder who values it most. Because Shell North America would remain liable under the contract during a temporary release, North Baja would retain the same revenue no matter at what rate the capacity is released. The Commission is concerned that interested parties may not be aware of the availability of the capacity until it is actually posted for bid pursuant to the capacity release provisions of North Baja's tariff. If no other shipper is interested in bidding on the capacity, then posting for bidding should not be an obstacle to the transaction. If other shippers are interested in bidding, the capacity should and will be awarded to the shipper who values it most.

16. The Commission finds that the Petitioners' assertion that their waiver request is consistent with procedures established for LNG facilities in Order Nos. 712 and 712-A is incorrect.[5] In Order No. 712-A, the Commission determined that it was acceptable for a holder of capacity in an open access LNG terminal to require a replacement shipper to take both terminal capacity and downstream pipeline capacity pursuant to a release. However, the Commission found that the tied releases would only be exempt from bidding if they qualified for either of the standard bidding exemptions of section 284.8(h) for releases of 31 days or less or prearranged releases to an LNG supplier for more than a year at the maximum rate. Otherwise, the capacity holder would have to post the tied release for bidding "to ensure that the tied release is made to the person placing the highest value on the subject capacity."[6] Because the release here is a long-term temporary release not at the maximum rate, neither of the exemptions apply. Bidding is necessary to ensure that the release is made to the person placing the highest value on the subject capacity.

17. The *North Baja* cases cited by the Petitioners are inapplicable here because, as pointed out by Virginia Power Energy Marketing, those cases involved a limited capacity rationalization program undertaken in anticipation of changing supply patterns and that certain of the processes were initiated by the Mexican government. Moreover, the instant petition is unlike recent cases such as *Macquarie, Barclays*[7] and *Bear Energy*[8] where the

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[5]Petition at 2, citing *Promotion of a More Efficient Capacity Release Market*, FERC Stats. & Regs. ¶ 31,271, at P 193 (2008); *order on reh'g*, FERC Stats. & Regs. ¶ 31,284, at P 146 (2008)).

[6] *Id*. at P 145.

[7] *Barclays Bank PLC and UBS AG*, 125 FERC ¶ 61,383 (2008).

Commission granted waivers of various policies and regulations relating to the transfer of interstate pipeline transportation capacity in order to facilitate the transfer of natural gas supply and transportation contracts and other assets as a result of various types of corporate restructurings, including corporate mergers and sales of entire business units. Here, unlike in those cases, Shell North America is not seeking to transfer its entire gas trading business unit to another company, along with other assets.

18. Finally, given the discussion here, as well as the recent order in *Macquarie* and notice in Docket No. RM09-7-000, the Commission finds that it has appropriately defined the scope of the Commission's policy on capacity release waivers as requested by Virginia Power Energy Marketing.

The Commission orders:

The Petitioners' request for waiver is granted in part and denied in part as discussed above.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

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[8] *Bear Energy LP*, 123 FERC ¶ 61,219 (2008).