

136 FERC ¶ 61,241
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
John R. Norris, and Cheryl A. LaFleur.

Kern River Gas Transmission Company

Docket Nos. RP11-2356-000
RP04-274-029
RP11-2328-000

ORDER ACCEPTING COMPLIANCE FILING AND DENYING MOTION FOR
CLARIFICATION

(Issued September 30, 2011)

1. On August 5, 2011, Kern River Gas Transmission Company (Kern River) filed revised tariff records to comply with the Commission's July 21, 2011 Opinion No. 486-E in Docket No. RP04-274-023.¹ In its filing, Kern River stated that the proposed tariff records reflected (1) eligibility requirements for shippers to pay Period Two rates, to be effective September 1, 2011, and (2) rates for Period Two shipper groups, to be effective October 1, 2011.² On August 29, 2011, the Commission accepted the tariff records related to Period Two Shipper eligibility to be effective on September 1, 2011, subject to conditions.³ In this order, the Commission accepts the tariff record related to Period Two rates to be effective October 1, 2011. The Commission also denies a September 1, 2011 motion by Nevada Power Company d/b/a

¹ *Kern River Gas Transmission Co.*, Opinion No. 486-E, 136 FERC ¶ 61,045 (2011). Kern River's compliance filing was given a new docket number because the underlying filing pre-dates the effective date of eTariff. *See Electronic Tariff Filings*, 130 FERC ¶ 61,047, at P 9-17 (2010). On August 22, 2011, several parties to the instant proceedings filed requests for rehearing of Opinion No. 486-E.

² The tariff record proposed to be effective on October 1, 2011 is Sheet No. 5.01, Statement of Rates, Period Two (Step-Down) Rates, 0.0.0 to Kern River Gas Transmission Company's FERC NGA Gas Tariff.

³ *Kern River Gas Transmission Co.*, 136 FERC ¶ 61,141 (2011).

NV Energy (NVE) for clarification that its September 1, 2011 Notice of Intent to Contract constituted a valid election of Period Two service from Kern River.

I. Background

2. In January 1990, the Commission issued a certificate for Kern River to construct its Original System under the optional expedited certificate regulations.⁴ In that order, the Commission approved initial rates based on, among other things, a levelized cost of service and a 25-year depreciation life. The Commission also authorized Kern River to charge separate levelized rates for three different periods: (1) the 15-Year term of the firm shippers' initial contracts (Period One); (2) the period from the expiration of those contracts to the end of Kern River's depreciable life (Period Two); and (3) the period thereafter (Period Three). The levelized rates for Period One (Period One Rates) were designed to recover approximately 70 percent of Kern River's original investment, an amount about equal to the portion of its invested capital funded through debt.⁵ Since the Period One rates allowed Kern River to recover more invested capital during Period One than Kern River would under ordinary straight-line depreciation for the depreciable life of the project, the rates for the second two periods (the Period Two rates and Period Three rates) would be lower than the Period One Rates.⁶

3. In May 2000, Kern River proposed to lower its rates by refinancing its debt and providing for longer debt recovery periods by extending the terms of its firm contracts. The Commission accepted a settlement containing this proposal (the Extended Term (ET) Settlement).⁷ The ET Settlement provided each of Kern River's firm shippers on the Original System an option to extend their contracts for either five or ten years. Some customers chose the five-year option and entered into revised contracts with ten-year terms (October 1, 2001 to September 30, 2011), while the rest of the Original System firm shippers extended their contract terms by ten years and entered into revised contracts with 15-Year terms (October 1, 2001 to September 30, 2016). The ET Settlement provided that the firm shippers' rates under these contracts would be designed consistent

⁴ *Kern River Gas Transmission Co.*, 50 FERC ¶ 61,069, at 61,150 (1990) (Original Certificate Order).

⁵ *See* Original Certificate Order, 50 FERC at 61,144.

⁶ *Kern River Gas Transmission Co.*, 58 FERC ¶ 61,073, at 61,244 n.38 (1992) (January 1992 Amended Original Certificate Order), *order on reh'g*, 60 FERC ¶ 61,123 (1992) (August 1992 Order).

⁷ *Kern River Gas Transmission Co.*, 92 FERC ¶ 61,061 (2000), *order on reh'g*, 94 FERC ¶ 61,115 (2001).

with the principles stated in the Original Certificate Order, permitting Kern River to recover 70 percent of the costs of the plant being depreciated by the end of the new repayment periods.⁸

4. In May 2002, Kern River completed an expansion project by adding additional compression to its system (2002 Expansion).⁹ The costs associated with the 2002 Expansion were rolled into the Original System costs, creating the Rolled-in System. As before, each of the 2002 Expansion shippers were permitted to choose 10-Year or 15-Year terms for this additional capacity. In May 2003, Kern River completed another expansion project (2003 Expansion).¹⁰ Kern River priced these services on an incremental basis and again permitted each shipper participating in the 2003 Expansion to choose either 10-Year or 15-Year firm contracts. Therefore, after the 2003 Expansion, there were six groups of levelized rate contracts. The shippers under all those contracts are still paying Period One rates, but the Original System ten-year shipper contracts expire on September 30, 2011.¹¹

5. On April 30, 2004, Kern River filed a general rate case under section 4 of the NGA in Docket No. RP04-204-000 (Original Rate Case Filing). Kern River proposed to continue to design its rates based on the levelized rate design methodology approved in Original Certificate Order, as modified in subsequent proceedings. Because Kern River's firm levelized rate contracts expire on six different dates, in its

⁸ *Kern River Gas Transmission Co.*, 92 FERC at 61,059.

⁹ *Kern River Gas Transmission Co.*, 96 FERC ¶ 61,137 (2001) (2002 Expansion Certificate Order).

¹⁰ *Kern River Gas Transmission Co.*, 100 FERC ¶ 61,056 (2002) (2003 Expansion Certificate Order), *order on reh'g*, 101 FERC ¶ 61,042 (2002).

¹¹ The expiration dates of the various contracts are as follows:

Original system – 10-Year contracts (expires September 30, 2011);
Original system – 15-Year contracts (expires September 30, 2016);
2002 Expansion – 10-Year contracts (expires April 30, 2012);
2002 Expansion – 15-Year contracts (expires April 30, 2017);
2003 Expansion – 10-Year contracts (expires April 30, 2013);
2003 Expansion – 15-Year contracts (expires April 30, 2018).

The rates for the Big Horn Lateral and the High Desert Lateral are not at issue in this phase of this proceeding. See *Kern River Gas Transmission Co.*, Opinion No. 486, 117 FERC ¶ 61,077 at P 487-8 (2006).

April 30, 2004 rate case filing, Kern River proposed different levelized Period One rates for each of the six groups of contracts. While the rates approved in the original certificate proceeding included separate, levelized rates for three periods, Kern River's tariff only included rates for Period One, the term of its firm shippers' initial contracts, and Kern River did not propose in this rate case to add Period Two or Three rates to its tariff.

6. In Opinion No. 486,¹² the Commission found that Kern River's proposal to continue its levelized methodology did not result in just and reasonable rates unless the pipeline included tariff sheets reflecting the Period Two step down rates, in addition to its proposed Period One rates. The Commission explained that the Period One Rates are designed to recover 70 percent of Kern River's invested capital, an amount approximately equal to the portion of its invested capital funded through debt. This fact allows Kern River to recover more invested capital during Period One than it would under ordinary straight-line depreciation for the depreciable life of its system. Because Kern River will have an excess recovery of its depreciation expense as of the end of Period One, the Commission held that it could only find the Period One rates to be just and reasonable, if Kern River's tariff also provides for the return of that excess recovery in its Period Two rates.

7. In Opinion No. 486-C, the Commission reaffirmed its holdings in earlier orders that Kern River must include in its tariff levelized rates for Period Two. However, the Commission also established a hearing to determine how levelized Period Two rates should be calculated and what conditions the shipper must satisfy in order to be eligible for the levelized Period Two rates.¹³ On April 14, 2011, the Presiding ALJ issued an Initial Decision regarding the Period Two rates.¹⁴

8. In Opinion No. 486-E, the Commission affirmed the April 14, 2011 Initial Decision on all matters, with one exception.¹⁵ The Commission held that Kern River may require Period One shippers to enter into Period Two contracts with terms of either 10 or 15-Years at the shipper's election and that the entire remaining balance of Kern

¹² Opinion No. 486, 117 FERC ¶ 61,077 at P 37, *order on reh'g*, Opinion No. 486-A, 123 FERC ¶ 61,056 (2008), *order on reh'g*, Opinion No. 486-B, 126 FERC ¶ 61,034 (2009).

¹³ *Kern River Gas Transmission Co.*, Opinion No. 486-C, 129 FERC ¶ 61,240, at P 247 (2009), *order on reh'g*, Opinion No. 486-D, 133 FERC ¶ 61,162 (2010).

¹⁴ *Kern River Gas Transmission Co.*, 135 FERC ¶ 63,003 (2011) (Period Two ID).

¹⁵ Opinion No. 486-E, 136 FERC ¶ 61,045 at P 1.

River's original capital investments may be levelized during the term of those contracts. The Commission clarified that, when those Period Two contracts expire, the shippers will be eligible for reduced Period Three rates. The Commission affirmed the ALJ's approval of Kern River's other proposed eligibility requirements, with the exception of his holding that Kern River may require shippers to take service under Rate Schedule KRF-1, instead of the other open access firm transportation rate schedules under which they are currently taking service.¹⁶ This finding was without prejudice to Kern River filing under NGA section 4 to propose elimination of its other firm service rate schedules in a not unduly discriminatory manner.

9. In the balance of Opinion No. 486-E, the Commission affirmed the ALJ's findings concerning the cost of service and billing determinants to be used in calculating Kern River's Period Two rates. The Commission directed Kern River to file revised tariff records including both the Period Two rates and the eligibility requirements for those rates, consistent with the holdings in this order, on or before August 5, 2011. The Commission determined that the tariff records setting forth the Period Two rates would be effective on October 1, 2011 and the tariff records setting forth the eligibility requirements will be effective September 1, 2011.

10. On August 5, 2011, Kern River filed tariff records to comply with the determinations of Opinion No. 486-E, concerning both the Period Two rates and the eligibility requirements for those rates. The eligibility requirements are set forth in a new section 30 to Kern River's General Terms and Conditions (GT&C), entitled "Contracting for Service Subject to Period Two Rates." On August 29, 2011, the Commission issued an order, accepting Kern River's proposed tariff records containing the section 30 Period Two shipper eligibility requirements, to be effective September 1, 2011, subject to conditions.¹⁷ In so doing, the Commission rejected Kern River's proposal to require all shippers whose Period One contracts expire on the same date to have the same Period Two contract term and required that Kern River revise sections 30.2(a) and 30.2(d) to

¹⁶ The parties have referred to these other rate schedules as the "Self-Contained Rate Schedules." Those rate schedules were established as a result of firm contracts that were negotiated around the time when Kern River's original system was certificated in 1990. Subsequently, the Commission directed Kern River to incorporate the terms of the Self-Contained Contracts within the General Terms and Conditions (GT&C) of its tariff, so all shippers that requested such service might receive service under the same terms and conditions that were available under the terms of those contracts. *Kern River Gas Transmission Co.*, 53 FERC ¶ 61,172, at 61,632-3 (1990), *order on reh'g*, 55 FERC ¶ 61,089, at 61,270 (1991); *Kern River Gas Transmission Co.*, 60 FERC ¶ 61,128, at 61,456 (1992).

¹⁷ *Kern River Gas Transmission Co.*, 136 FERC ¶ 61,141.

remove all provisions related to the requirement that all shippers whose Period One contracts expire on the same date must enter into Period Two contracts of the same duration. The Commission also directed Kern River to eliminate the rate matrices set forth in section 30.2(a) and to revise that section to include the 10-Year and 15-Year Period Two rates for each group of Original System and 2002 Expansion Project shippers upon the commencement of Period Two for that shipper group. The Commission stated that Kern River may also include in its tariff a mechanism under which it may file for approval of an appropriate adjustment to the Period Two rates of the Original System shippers within a reasonable time after each group of 2002 Expansion Project shippers have made their contract duration election.

11. The Commission also accepted proposed section 30.2(d), requiring Original System shippers whose Period One service agreements expire on September 30, 2011 to submit a binding request for transportation service no later than September 1, 2011. The Commission found that the requirement that 10-Year Original system shippers make a binding commitment to execute a Period Two contract by September 1, 2011 was consistent with Opinion No. 486-E. The Commission pointed out that, in Opinion No. 486-E, it had stated:

Kern River must make a compliance filing calculating Period Two rates consistent with the holdings of this order on or before August 5, 2011. In these circumstances, the Commission finds that the 10-year Original System shippers will have sufficient information concerning Period Two contract rates and conditions of service, so that *it is just and reasonable to require them to make a binding and non-conditional commitment on or before September 1, 2011 to execute a service agreement for Period Two service with a term of either 10 or 15 years.*¹⁸

12. The Commission also determined that any shipper with an expiring Self-Contained Contract may choose to receive Period Two service on September 1, 2011, subject to the terms and conditions of service contained within its existing Self-Contained Contract and the corresponding rate schedule. The Commission noted that Period Two service under such a Self Contained Rate Schedule will remain subject to the Commission's action in Docket No. RP11-2328-000, where Kern River has proposed to phase out the Self Contained contracts,¹⁹ as well as the outcome of the Commission's consideration of the

¹⁸ Opinion No. 486-E, 136 FERC ¶ 61,045 at P 84.

¹⁹ *Kern River Gas Transmission Co.*, 136 FERC ¶ 61,140 (2011).

requests for rehearing of Opinion No. 486-E, including Kern River's request for rehearing of that opinion's holdings on this issue.

13. Lastly, the Commission stated that it would issue a subsequent order to discuss the issues surrounding the derivation of the Period Two rates. In the instant order, the Commission will address issues related to the Period Two rates raised by Kern River's August 5, 2011 filing.

14. On September 1, 2011, NVE, which has a Period One contract expiring on September 30, 2011, filed a motion, requesting that the Commission find that its September 1, 2011 Notice of Intent to Contract constitutes a valid election of Period Two service on Kern River's Original System. The Commission also addresses that motion in this order.

Details of Period Two Rate Proposals in the August 5, 2011 Filing

15. As required by Opinion No. 486-E, Kern River's August 5, 2011 compliance filing included a tariff record, to be effective October 1, 2011, setting forth its proposed Period Two rates. Kern River maintained that, consistent with Opinion No. 486-E, its proposed Period Two rates return the excess recovery of depreciation projected to occur during Period One. Kern River also stated that its proposed Period Two rates reflected an 11.55 percent rate of return on equity. Kern River also asserted that: (1) the Period Two reservation rates are calculated based on billing determinants equal to 100 percent load factor subscription and utilization of Kern River's firm, mainline capacity; (2) the Period Two rates are based on a 100 percent equity capital structure; (3) the Period Two rates do not include adjustments to the regulatory asset/liability for deferred depreciation associated with replacements of compressor engines and general plant after the end of the test period for this proceeding (October 31, 2004); and (4) the Period Two rates do not reflect an adjustment for inflation.

16. Kern River also stated that proposed Sheet No. 299D requires that Kern River file *pro forma* Period Three rates at the times specified by the Commission in Opinion No. 486-E. In addition, Kern River states that this section provides for Period Two rates to be adjusted to reflect reductions in revenue credits applicable to rolled-in shippers that will result from the implementation of Period Three rates.

17. As noted in the August 29, 2011 order, several parties filed protests related to the derivation of the Period Two rates.²⁰ In particular, Calpine Energy Services, L.P., (Calpine), and BP Energy Company (BP) filed protests related to the derivation of the Period Two rates. On August 24, 2011 and August 31, 2011, in order to fully address all

²⁰ *Kern River Gas Transmission Co.*, 136 FERC ¶ 61,141 at P 16, 25.

aspects of the proposed rates, the Commission directed Kern River to file additional explanations of its data. Kern River complied with these directives on August 26, 2011 and September 2, 2011. The information provided by Kern River and the objections to the derivation of the Period Two rates in the August 5, 2011 compliance filing are discussed below.

II. Discussion

18. The Commission finds that Kern River's proposed Period Two rates comply with the holdings of Opinion No. 486-E and are just and reasonable. Therefore, the Commission accepts the associated tariff record to be effective October 1, 2011. The Commission also denies NVE's motion for a determination that its September 1, 2011 Notice of Intent to Contract was a valid election of Period Two service.

A. Period Two Rate Disparities

19. In Kern River's August 5, 2011 filing to comply with Opinion No. 486-E, Kern River proposed that current 10-Year and 15-Year shippers on the Original System who execute 10-year contracts for Period Two pay different rates. Specifically, Kern River proposed that a current 10-Year shipper whose Period One contract expires on September 30, 2011, pay a Period Two rate of \$0.2560 per Dt if it elects a 10-year contract term for Period Two. However, Kern River proposed that a current 15-Year shipper whose Period One contract expires on September 30, 2016, pay a Period Two rate of \$0.2182 per Dt if it elects a 10-year contract term for Period Two.²¹

20. BP argues in its protest to Kern River's the August 5, 2011 filing that the Period Two rates proposed by Kern River are unjust, unreasonable and unduly discriminatory with respect to the Original System 10-Year Shippers. BP argues that the rates for the Original System 10-Year Shippers are too high and are higher than the Original System 15-Year Shippers for Period Two contracts of the same duration, particularly for 10-year Period Two contracts. BP requests that the Commission direct Kern River to establish Period Two rates such that the Original System 10-Year Shippers pay no more for Period Two service than the Original System 15-Year Shippers for Period Two contracts of the same duration.

21. On August 24, 2011 the Commission requested Kern River to explain why Kern River's proposed Period Two rates for the Original System 10 year shippers are higher than the rates for the Original System 15 year shippers for Period Two contracts of the

²¹ Sheet No. 299E, Contracting for Service Subject to P2 (Step-Down) Rates, 0.0.0 to Kern River Gas Transmission Company's FERC NGA Gas Tariff.

same duration. Kern River responded on August 26, 2011, stating that in order for the rates to be identical, each shipper group would have to have the same percentage of the total billing units on Kern River's system and stated that because this was not the case for Period One rates, it is not the case for Period Two. On August 31, 2011 the Commission required Kern River to explain how the opening balances for Accumulated Deferred Income Taxes (ADIT) used to design its Period Two rates were derived from its Period One supporting documentation. The Commission directed Kern River to explain "the source and/or cause of the variation between the Original System 10-year and 15-year customers for Accumulated Deferred Income Taxes."

22. On September 2, 2011, Kern River responded and cited to various worksheets in its compliance filing that identify the sources for its use of beginning deferred income taxes for both Period One rates and Period Two rates. Kern River asserted that the difference between the deferred taxes for the Original System 10-year and 15-year shippers is a function of the changes to the beginning balances derived from Ex. KR-100, (included in the test period record in Docket No. RP04-274-000) caused by the subsequent rate base changes stemming from the different amounts of tax depreciation and levelized depreciation generated for each shipper group by Kern River's levelized rate methodology. Kern River asserts that the changes to the ADIT balances for the different shipper groups between the end of the 2004 test period and the expiration of the various Period One contracts are derived from the approved and currently effective Period One rates and therefore form the basis for the beginning of Period Two balance.

23. BP filed comments on Kern River's data responses on September 6, 2011. BP argues that Kern River's proposed Period Two rates rest upon the illogical premise that the Original System 10-Year Shippers should pay substantially more for the same service over the same duration of Period Two when compared to the Original System 15-Year Shippers, even when both sets of shippers are supposedly paying their respective shares of 30 percent of Kern River's original investment in the same set of facilities.

24. BP argues that the rates proposed by Kern River in its August 5, 2011 filing must comport with the Commission's orders to Kern River, including the Original Certificate Proceeding which established certain parameters for Period Two. BP argues that there is no indication in the Original Certificate Proceedings or the ET Settlement proceeding that any party proposed or agreed to materially higher rates for some shippers in Period Two compared to other shippers receiving the same service using the same facilities for the same duration of Period Two.²² BP argues that as of the beginning of Period Two, each

²² BP points out that in the ET Settlement proceeding Kern River represented that that no costs would be shifted between 10-Year and 15-Year shippers because of its ET proposal. BP Comments at 2 (citing, *Kern River Gas Transmission Co.*, 92 FERC ¶ 61,061 at 61,159).

class of shipper must have paid 70 percent of the original plant investment. Both shipper classes should, therefore, pay the same Period Two rates if both agree to take Period Two service for an equal duration. BP asserts that Kern River and its shippers are at the threshold of Period Two and that it is critical to accurately compute the Period Two rates. Therefore, the Period Two rates proposed for Original System 10-Year Shippers should be rejected and modified to a level comparable to the Period Two rates for Original System 15-Year Shippers when both elect the same length of service during Period Two rate and take the same service, and use the same facilities for the same period of time.

25. BP argues that incorrect opening Period Two ADIT balances contribute to the Original System 10-year shippers paying unduly discriminatory and excessive Period Two rates. BP argues that Kern River's methodology of assigning ADIT in calculating its Period Two rates gives one group of shippers virtually the entire benefit of payments made by another group of shippers. It asserts that Original System 10-Year Shippers were assigned less than one percent of the ADIT balances in the calculation of their respective Period Two rates while approximately 99 percent of the ADIT balance was assigned to 15-Year shippers.²³ BP asserts that such an improper assignment is an important contributor to the disparity between Period Two rates for the Original System 10-Year and 15-Year Shippers even when both sets of shippers elect the same service for the same length of Period Two over the same facilities. BP argues that the Commission must require Kern River to re-calculate Period Two rates to reflect the proper realization of such amounts by shipper class.

26. BP argues the Kern River has attempted to justify the difference in Period Two rates based upon work papers underlying its Period One rate calculation which was intended to comply with Opinion No. 486-C and therefore did not address Period Two rates at issue here. BP also argues that the difference cannot be attributed to the difference in the costs of Original System 10-Year and 15-Year Shippers because no costs can be shifted between Original System 10-Year and 15-Year Shippers either before or during Period Two. Further, BP argues that regardless of the merits of Kern River's derivation of Period One rates, BP is contesting here the proposed Period Two rates and seeking a method that accurately attributes cost responsibility for the Original System between the 10-Year and 15-Year Shippers when each begins to receive Period Two service.

Commission Determination

27. The Commission denies BP's protest concerning the difference in the Period Two rates to be paid by current 10-Year and 15-Year Original System shippers who elect Period Two contracts of the same duration. As is clear from the parties' pleadings on this issue, the rate differential results from Kern River's treatment of ADIT for purposes of

²³ BP Comments at 5.

calculating the Period Two rates for the Original System. Therefore, before addressing BP's protest, the Commission first describes the purpose and mechanics of the ADIT adjustment to rate base.²⁴

28. The adjustment is required when there is a difference between the dollar amount of the depreciation and amortization the pipeline reports for tax purposes and the dollar amount of the depreciation and amortization contained in its regulatory cost-of-service. The latter must be straight line depreciation, in the instant case, over 39 years. If the pipeline uses any form of accelerated depreciation or amortization, in the early years the depreciation or amortization reported for tax purposes will exceed the depreciation or amortization contained in the pipeline's regulatory cost-of-service. This reduces taxable income and therefore income tax payments are below what would otherwise have been paid if the pipeline only used straight line depreciation for tax purposes. This means that the income tax allowance embedded in the pipeline's regulatory cost-of-service generates more cash flow than is actually used to pay income taxes. Traditionally, the Commission has viewed this difference between the cash from the income tax allowance and the taxes paid as a tax free loan from the rate payers to the pipeline. The Commission has therefore required the pipeline to create an ADIT account that records the difference between the income taxes actually paid and the cash flow generated by the income tax allowance component of its rates. The amount of the ADIT account is deducted from the rate base of the pipeline and reduces the pipeline's return allowance.

29. However, over time the regulatory depreciation and amortization become greater than that reported for income tax purposes. At that point, the cash flow from the income tax allowance is less than that the pipeline actually pays because taxable income exceeds the regulatory return upon which the income tax allowance is based. Therefore, the positive ADIT balance that began to accrue when the accelerated depreciation was first instituted will decline and eventually reach zero. Once that has happened, the net plant of the pipeline will be the same as if there had been no difference in the annual dollar amount between straight line and accelerated depreciation. Thus, in the first years of an ADIT adjustment the pipeline's rate base is reduced and the shippers normally receive a "benefit" because the pipeline's rates reflect a lower dollar return on rate base. In the latter years, the net rate base begins to increase as the ADIT balance declines. But whatever the particulars of the ADIT adjustment, the shippers must eventually pay the pipeline's income taxes. The specifics are ones of timing and whether some shippers receive a "benefit" is a matter of the rates in effect when a given amount of taxes is paid.

30. Under conventional rate making, these changes are reflected only when the pipeline establishes a new set of rates and modifies its rates to reflect the ADIT balance on its books at the end of the test period. However, in the instant case, the changes that

²⁴ See also Opinion No. 486, 117 FERC ¶ 61,077 at P 228-29.

occur to the ADIT balances over time are reflected in Kern River's rates due to the operation of its levelized rate methodology. This occurs because the changes to ADIT are a direct function of the changes in the annual depreciation rates and dollar depreciation amounts generated by the levelized rate methodology. As Kern River stated, the dollar amount of the ADIT adjustment that accrues for each shipper group is a function of each shipper group's contract term and its relative proportion of Kern River's billing determinants. The Period One rates of the 15-Year Original Shippers reflect a lower annual regulatory depreciation and amortization expense, than the Period One rates of the 10-Year Original System shippers. This lower regulatory and amortization expense generates a larger difference between regulatory and tax depreciation expense for the 15-Year Shippers, causing a higher ADIT balance for that group of shippers. Thus, even though the 10-Year shipper group will be amortizing Kern River's rate base more rapidly during Period One than the 15-Year shipper group, the latter can accumulate a greater ADIT balance during its 15-year Period One, than a 10-year shipper group accumulates during its 10-year Period One.

31. In addition, in the instant case, the 10-Year Original System shippers have billing determinants of 100,033 Dt per day and the 15-Year Original System Shippers have billing determinants of 639,570 Dt per day, a ratio of about 6.39 to 1. Given this, it is not surprising that the dollar amount of the ADIT balances of the Original System 15-Year shipper group were much higher than those of the Original 10-Year Shipper group both at the end of the 2004 test period²⁵ or at the beginning of Period Two.²⁶

32. Having discussed the mechanics of the ADIT balances, the Commission now turns to merits of BP's protest, which is denied on two grounds. First, the protest is untimely in the context of the instant compliance filing, which implements Opinion No. 486-E's rulings regarding Kern River's Period Two rates. In Opinion No. 486-C,²⁷ the Commission rejected Kern River's initial compliance filing concerning its Period Two

²⁵ \$45,743,081 and \$3,220,627 respectively. *See* Kern River's February 1, 2010 Compliance Filing, Schedule J-2 at 51 and 15 respectively.

²⁶ \$101,144,821 and \$1,356,353 respectively. February 1, 2010 Compliance Filing, Schedule J-2 at 46 and 11 respectively. The balances in Kern River's August 11, 2011 compliance filing are \$97,230,740 for the Original 15-Year Shippers and \$1,766,732 for the Original 10-Year Shippers (Schedule J-2 at 62 and 38 respectively). The ADIT balance of the Original 15-Year Shippers declines beginning in 2017. The ADIT balance of the Original 10-Year Shippers increases until 2016 (to \$7,735,374) and then decreases to \$372,387 in 2020. These Period Two schedules assume both groups execute a 10 year contract for their Period Two service.

²⁷ 129 FERC ¶ 61,240 at P 263.

rates and required Kern River to submit a new compliance filing setting forth its proposal for offering shippers levelized Period Two rates. Opinion No. 486-C also established a hearing to consider all issues concerning the calculation of the Period Two rates. On February 1, 2010, Kern River submitted its filing to comply with Opinion No. 486-C's requirements concerning its Period Two rates. In that filing, Kern River proposed Period Two rates for each shipper group levelized over a period of ten years. As here relevant, Kern River proposed that a current 10-Year shipper whose Period One contract expires on September 30, 2011, pay a Period Two rate of \$0.3346 per Dt, but proposed that a current 15-Year shipper whose Period One contract expires on September 30, 2016 pay a Period Two rate of \$0.3052 per Dt.²⁸ Thus, Kern River's February 1, 2010 Opinion No. 486-C compliance filing contained a similar difference in the rates to be paid by current 10-Year and 15-Year Original System shippers for 10-Year Period Two contracts, as in Kern River's August 5, 2011 Opinion No. 486-E compliance filing.²⁹

33. While the rate differential of which BP now complains was clear on the face of the *pro forma* tariff sheets included in Kern River's February 1, 2010 Period Two compliance filing, at no point in the hearing established by Opinion No. 486-C on Kern River's Period Two rates did BP raise any issue with respect to that rate differential. The Commission has reviewed the following that BP filed with regard to Kern River's initial February 1, 2010 compliance filing: BP's initial comments,³⁰ the expert testimony of its witness Elizabeth Crowe,³¹ BP's initial and reply briefs to the ALJ following the hearing, the Period Two ID,³² BP's Briefs on³³ and opposing³⁴ Exceptions to Opinion No. 486-E,

²⁸ See Kern River's February 1, 2010 Compliance Filing, Appendix A, *Pro Forma* Sheet Nos. 5.02 and 5.03, Kern River Gas Transmission Company, FERC Gas Tariff, Second Revised Volume No. 1 issued February 1, 2010.

²⁹ The differential in the February 1, 2010 filing was \$0.0294(*pro forma* Sheet Nos. 5.02 and 5.03) while the differential in the August 5, 2011 filing is \$0.0378 (Sheet No. 299E, Contracting for Service Subject to P2 (Step-Down) Rates, 0.0.0).

³⁰ BP Energy Company's Protest and Preliminary Comments on Kern River's Period Two Compliance Filing dated February 23, 2010.

³¹ Prepared First Round Period Two Rate Testimony of Elizabeth Crowe on behalf of BP Energy Company dated June 29, 2010 (Crowe First Round Testimony).

³² Period Two ID, 135 FERC ¶ 63,003, *passim*.

³³ Brief on Exceptions of BP Energy Company dated May 16, 2011.

³⁴ Brief opposing Exceptions of BP Energy Company dated June 6, 2011.

and its request for rehearing of that opinion. At no point in any of these materials did BP raise the rate differential issue it advances in its comments on Kern River's August 5, 2011 compliance filing. Nor did BP question Kern River's treatment of ADIT in its Period Two levelized rate proposal.³⁵ Moreover, it is not that BP was without notice of the ADIT issue. As previously noted, the difference in the opening ADIT balances for 10-Year and 15-Year Original system shippers was clear on the supporting schedules in the February 1, 2010 compliance filing.³⁶ BP could have raised the issue in its comments or questioned the appropriateness of the opening balances and related calculations by Kern River's levelized model at hearing, but chose not to take such action.

34. BP having chosen not to litigate these issues during the hearing on Period Two rates but instead to concentrate on other issues, it is too late in this already lengthy proceeding for BP now to raise the issue. As is clear from the description above of the purpose and mechanics of the ADIT adjustment, the treatment of ADIT in a pipeline's rates is a very complex issue, and is particularly complex in the context of Kern River's levelized rates. The Commission established a hearing on Kern River's Period Two rates for the very purpose of allowing the parties a full opportunity to present testimony on all issues of interest to them in the determination of Kern River's Period Two rates. BP failed to avail itself of that opportunity with respect to ADIT balances. The Commission will not now entertain contentions that could, and should, have been raised at the hearing, where all parties would have had an opportunity to present evidence with respect to those contentions. Therefore BP's protest to Kern River's August 5, 2011 compliance filing is rejected.

35. Second, the Commission addressed the merits of BP's arguments with regard to the treatment of ADIT during Period One in Opinion Nos. 486 through 486-D, and the ADIT balances as of the end of Period One are necessarily the opening ADIT balances for Period Two. BP first raised the issue of the allocation of ADIT balances as between Original System 10 and 15-Year Shippers in a series of pleadings addressing Kern River's March 2, 2009 filing to comply with Opinion Nos. 486 through 486 through 486-B.- In those pleadings, BP complained that Kern River's filing to comply with the

³⁵ The worksheet included in the First Round testimony of BP's witness Elizabeth Crowe does show an opening ADIT balance for the Original 10-Year Shippers of \$8,887,408, as compared to Kern River's \$1,766,732. Crowe First Round Testimony, Ex. BP-187 at 7. However, at the hearing, BP did not present any testimony in support of its ADIT balances or otherwise raise the issue of this difference in the ADIT opening balances.

³⁶ \$101,144,821 and \$1,356,353 respectively. *See* Kern River's February 1, 2010 Compliance Filing, Schedule J-2 at 46 and 11 respectively.

Commission's rulings with regard to Period One resulted in an increase in the 10-Year Original System Shippers' rates from the rates in effect before this rate case, but a decrease in the 15-Year Original System Shippers' rates. BP argued that all rate factors, including ADIT, should affect the unit rates proportionately between Original System 10-Year Shippers and Original System 15-Year Shippers. In reply, Kern River pointed out that ADIT accumulates faster for the Original System 15-Year Shippers than for the Original System 10-Year Shippers service because of the larger difference between the accelerated tax depreciation and regulatory depreciation included in the Original System 15-Year Shippers' rate. Kern River also explained that because the Original System 15-Year Shippers' accumulated deferred income taxes increase faster, their ADIT balance was built up faster than the Original System 10-Year Shippers' balance from 2002 (the time of the sale of Kern River to MidAmerica Energy Holdings Company (MidAmerica)) until the effective date of Kern River's new rates in Docket No. RP04-274-000.³⁷

36. In Opinion No. 486-C, the Commission rejected BP's concerns stating that:

[A]side from making a general assertion that any rate factors should similarly affect the unit rates of the 10 and 15-year Rolled-in System shippers, BP points to no specific error in Kern River's compliance filing as causing an improper rate disparity. In fact, as Kern River explains, the different remaining contract terms of the two groups of shippers cause various rate factors to affect the rates of the 10 and 15-year shippers differently.³⁸

37. In regard to the differences in ADIT amounts for shippers electing different terms for service, the Commission identified two factors that resulted in different ADIT balances for the Original System 15-Year Shippers and Original System 10-Year Shippers. One was that ADIT balances were set to zero when Kern River was acquired by MidAmerica in 2002. Moreover, even after the adjustment, the ADIT generated reduction in rate base continues to accumulate faster for the Original System 15-Year Shippers than for the Original System 10-Year Shippers service due to the larger difference between tax depreciation and regulatory depreciation included in the Original System 15-Year Shippers' rate.³⁹ This explanation for the calculation of ADIT also

³⁷ Opinion No. 486-C, 129 FERC ¶ 61,240 at P 199-204.

³⁸ *Id.* P 207. The 10 and 15-year Rolled-in System Shippers are more appropriately referred to as the Original System 10-Year Shippers and Original System 15-Year Shippers so the Commission does so here. They are the same for the purpose of the analysis here and the prior analysis in Opinion No. 486-C.

³⁹ *Id.* P 204-05, 208.

explains the differences in the rates between an Original System 15-Year Shippers and a Ten-Year Period One shipper if both opt for 10-Year Period Two terms. At bottom, those shippers did not start with equal amounts of opening and closing ADIT balances at the end of the 2004 test period and it is those test period balances that underpin the revised Period One rates Kern River filed in Docket No. RP04-274-000. As the ADIT calculation moves forward after the end of the 2004 test period the divergence between the ADIT balances for the Original System 15-Year Shippers and Original System 10-Year Shippers reflects the difference in the rates at which ADIT is accrued and then amortized for two different groups of shippers that had different closing ADIT balances at the close of the 2004 test period.

38. The resulting differences in the opening ADIT balances for the Period Two rates are a function of Kern River's levelized rate methodology. As such, they are derived mathematically from the opening and closing ADIT balances contained in Ex. KR-100 and which was the source for the ADIT calculations embedded in Kern River's Period One rates. BP does not claim here that Kern River's levelized rate methodology model incorrectly calculated the changes in ADIT balances that would occur on a going forward basis after the close of the 2004 test period. Rather, BP seeks to attack the ADIT balances for each category of shipper at the beginning of Period Two as unjust and unreasonable arguing that those balances are incorrect due to the factors used to allocate ADIT balances between different shipper groups. But as Kern River states in its September 2, 2011 data request response, Kern River has not modified how those allocations were reflected in the design of its Period One rates. The resulting ADIT balances used to develop the Period Two rates reflect the operation of the allocation factors and ADIT balances that were used to design the Period One rates approved by the Commission in Docket No. RP04-274-000. BP's challenges to both allocations and ADIT balances developed in that docket were rejected by the Commission on substantive grounds in Opinion No. 486-C.⁴⁰

39. On rehearing of Opinion No. 486-C, BP made various new contentions concerning the appropriate method of allocating ADIT and accumulated depreciation between different shipper groups. In Opinion No. 486-D, the Commission rejected these on grounds that BP had failed to raise them in a timely fashion.⁴¹ Again, BP has made an untimely effort to reopen a closed issue in the context of Kern River's Period Two compliance filing. Since Kern River did nothing in that compliance filing to change the ADIT formulas that were approved in Docket No. RP04-274-000 for Period One, BP's protest is without substantive foundation. Therefore, it is denied and the Commission

⁴⁰ *Id.*

⁴¹ Opinion No. 486-D, 136 FERC ¶ 61,162 at P 83-90.

accepts the ADIT balances used to design the Period Two rates for the Original System 15-Year Shippers and Original System 10-Year Shippers.

B. Period Two 2003 Expansion Billing Determinants

40. In this rate case, Kern River proposed to design its Original System rates using reservation and usage billing determinants based on 95 percent of the design capacity of its Original System, despite the fact that during the test period it had firm contracts (including several seasonal contracts) for somewhat more than 100 percent of the design capacity of the Original System. Kern River contended that this proposal was consistent with the so-called 95 percent load factor condition in its Optional Expedited Certificate. It asserted that condition required it to design the Original System rates based on 95 percent of design capacity, regardless of whether it had contracts for more or less than 95 percent of its capacity. In Opinion Nos. 486 through Opinion No. 486-D, the Commission held that the 95 percent load factor condition simply required that Kern River design its original system rates based upon *at least* 95 percent of its design capacity. Accordingly, the Commission held that Kern River's Period One rates for its Original System, as well as the 2002 and 2003 expansions, must be designed based on its actual Period One billing determinants.

41. Despite the Commission's holdings concerning the volumes to be used in designing Kern River's Period One rates, Kern River's February 1, 2010 Period Two compliance filing proposed to design its Period Two rates for all shipper groups based on 95 percent of its design capacity, rather than its actual Period One billing determinants. Kern River contended that this was appropriate because its Period One contracts expire at the end of Period One and it does not currently have contracts with any shippers for Period Two. The other parties protested Kern River's February 1, 2010 Period Two compliance filing, contending that the Period Two rates should be designed based on the same actual 2004 test period billing determinants as the Period One rates.

42. In Opinion No. 486-D, the Commission stated that the parties could address at hearing the issue whether the volumes used to design the Period Two rates and allocate costs should be based upon 95 percent of Kern River's design capacity, a projection that its Period One contracts will be renewed, or some other basis.⁴² In Opinion No. 486-E, the Commission affirmed the ALJ's finding that the Period Two rates should be designed based on the same actual billing determinants as previously adopted by the Commission for Period One.

⁴² Period Two ID, 135 FERC ¶ 63,033 at P 1033 (citing Opinion No. 486-D, 133 FERC ¶ 61,162 at P 198).

43. In its August 5, 2011 filing to comply with Opinion No. 486-E, Kern River proposed to design the Period Two rates for the 2003 Expansion based on total annual reservation billing determinants for 15-Year 2003 Expansion shippers of 279,817,030 dekatherms. In its protest to the August 5, 2011 filing, Calpine asserts that Kern River designed the Period One rates for the 2003 Expansion based on total annual reservation billing determinants for the 15-Year shippers of 282,966,386 dekatherms. It therefore asserts that Kern River's proposed Period Two reservation rates for 15-Year 2003 Expansion shippers appear to be based on reduced billing determinants in contravention to Opinion No. 486-E where the Commission directed the pipeline to derive Period Two rates based on the same billing determinants as used to derive Period One rates.

44. On August 24, 2011, the Commission requested that Kern River explain its proposed choice for the billing determinants used to calculate Period Two reservation rates for 15-Year 2003 Expansion shippers. On August 26, 2011 Kern River responded, stating that it used billing determinants based on a 100 percent load factor of design capacity to calculate its Period Two reservation rates, including those for 15-Year 2003 Expansion shippers. Kern River states that the ID determined that the "100% load factor is a just and reasonable level to be used for cost allocation and rate design of the Period Two rates."⁴³ Kern River states that Opinion No. 486-E framed the issue as whether Period Two rates should be based on the "use of 95 percent rather than a 100 percent load factor,"⁴⁴ and affirmed the ID on this issue.⁴⁵ Kern River states that it explained in its opening testimony that it calculated its illustrative Period Two rates based on 95 percent load factor determinants.⁴⁶ Kern River states that the ID found that it should use the 100 percent load factor and indicated that it was affirming the findings of the ID concerning the billing determinants to be used in calculating Period Two rates.⁴⁷ However, Kern River states that in Opinion No. 486-E the Commission also stated that Kern River should use "the same actual 2004 test period billing determinants as used to design Kern River's Period One rate."⁴⁸ Kern River also states that it has sought clarification that

⁴³ *Citing*, 135 FERC ¶ 63,033 at P 1030.

⁴⁴ *Citing*, Opinion No. 486-D, 133 FERC ¶ 61,162 at P 163.

⁴⁵ *Citing*, *id.* P 1, 189.

⁴⁶ *Citing*, Ex. No. KR-P2-1 at 19, 23; Exh. No. KR-P2-2.

⁴⁷ *Citing*, Opinion No. 486-E, 136 FERC ¶ 61,045 at P 162.

⁴⁸ *Citing*, Opinion No. 486-E, 136 FERC ¶ 61,045 at P 166.

using 100 percent load factor billing determinants, as determined by the ID is compliant with Opinion No. 486-E.⁴⁹

45. In its September 2, 2011 answer, Calpine argues that Kern River's proposed Period Two billing determinants for the 2003 Expansion reflects Period One billing determinants with previously approved volumetric adjustments removed, resulting in Kern River's proposed Period Two reservation billing determinants for 15-Year 2003 Expansion shippers of 279,817,030 dt rather than the 282,966,386 dt approved for use in designing Period One rates. Calpine responds that in Opinion No. 486-E the Commission stated:

Kern River's Period Two rates must be designed based on the same actual 2004 test period billing determinants as used to design Kern River's Period One rate, because Kern River provided **no** evidence of why this should change based on the 2004 test period data.⁵⁰

Calpine argues that the Commission also stated that it "finds that it is just and reasonable to use the same billing determinants to design Kern River's Period Two rates" as were used to design the pipeline's Period One rates,⁵¹ and "affirms the ID's holding that Kern River's Period Two rates should be designed on the same billing determinants as the Commission approved for Period One."⁵²

46. Calpine argues that the 2004 test period billing determinants approved for designing Kern River's Period One rates include the volumetric adjustment that the pipeline now seeks to remove when calculating Period Two rates. Calpine argues that, contrary to Kern River's assertion in its response to the Commission's data request, Opinion No. 486-E actually mandates the calculation of Period Two rates using the same volumetrically adjusted 100 percent load factor billing determinant levels used to set Period One rates.

⁴⁹ *Citing*, Request of Kern River Gas Transmission Company for Clarification and/or Rehearing of Opinion No. 486-E, Docket No. RP04-274, filed August 22, 2011.

⁵⁰ Opinion No. 486-E, 136 FERC ¶ 61,045 at P 166 (emphasis in original).

⁵¹ *Id.* P 88.

⁵² *Id.* P 89.

Commission Determination

47. The Commission denies Calpine's protest. The Commission finds that Kern River properly used actual 2004 test period billing determinants in calculating 15-Year 2003 Expansion shippers' rates.

48. In Opinion No. 486-E, the Commission stated:

Kern River's Period Two rates must be designed based on the same actual 2004 test period billing determinants as used to design Kern River's Period One rate, because Kern River provided **no** evidence of why this should change based on the 2004 test period data.⁵³

The Commission's review of Kern River's work papers shows that it complied with this requirement in calculating the Period Two rates for the 2003 Expansion. First, with respect to the 15-Year Shippers' rates, in its January 29, 2010 Period One compliance filing, Kern River started with the actual 2003 15-Year shippers' billing determinants of 766,622 dt per day as of the end of the 2004 test period (279,817,030 dt per year). The 766,622 dt per day amount represented the actual total of the contract demands under the 15 then-effective contracts with 15-Year 2003 Expansion shippers. Kern River then adjusted the actual billing determinants of the 15-Year 2003 Expansion shippers upward by 8,628 dt per day for purposes of determining the 15-Year 2003 Expansion shippers' Period One rates, while making a downward adjustment in the actual billing determinants of the 10-Year 2003 Expansion shippers. This adjustment, which appears to have been related to discounts provided in two Period One contracts for service on the 2003 Expansion, increased the 15-Year shippers' Period One billing determinants to 775,250 dt per day (282,966,386 dt per year).⁵⁴ No party protested Kern River's January 29, 2010 Period One compliance filing on the issue of these adjustments, and the Commission has approved that filing in orders no longer subject to rehearing.

49. In its February 1, 2010 Period Two compliance filing, Kern River started with the same actual 15-Year shippers' billing determinants of 766,622 dt per day (279,817,030 dt per year) as it did in the Period One compliance filing.⁵⁵ It then reduced those billing

⁵³ Opinion No. 486-E, 136 FERC ¶ 61,045 at P 166 (emphasis in original).

⁵⁴ Kern River's January 29, 2010 Compliance filing in Docket No. RP04-274-021, actual Period One billing determinants for 2003 15-Year shippers shown on Schedule J-1, Part 1, Page 1-A, line 57; discount adjustment of discounted billing determinants shown on Work Paper, pp. 16-18.

⁵⁵ Schedule J-1, Page 1, line 35 of Kern River's February 1, 2010 compliance filing.

determinants down by five percent, consistent with its proposal to design the Period Two rates based on a 95 percent load factor. Kern River did not propose any discount adjustment to the billing determinants used to design its Period Two 2003 Expansion rates.⁵⁶ While parties protested Kern River's proposal in its February 1, 2010 Period Two compliance to design its Period Two rates based upon 95 percent of its design capacity, no party objected to the absence of any other adjustments in those proposed billing determinants, including the absence of a discount adjustment. Similarly, in their testimony at the hearing, the parties focused solely on the issue of whether Kern River's Period Two rates should be designed based on 95 percent of its design capacity or the actual billing determinants in effect at the end of the 2004 test period.

50. Kern River's August 5, 2011 filing to comply with Opinion No. 486-E has properly used actual end of 2004 test period reservation billing determinants to design the Period Two 2003 Expansion rates, without any adjustment. The Period Two rates for that expansion are well below the discounted rates in effect during the 2004 test period. In these circumstances, it is reasonable to project, based on the 2004 test period data, that Kern River will not discount its Period Two rates for the 2003 Expansion. As a result, it is just and reasonable for Kern River to design its Period Two rates for the 2003 Expansion based upon the full level of both the 10-Year and the 15-Year 2003 Expansion shippers' billing determinants. In fact, given the projection that Kern River will not discount its Period Two rates, any discount adjustment would be unjust and unreasonable.

51. Calpine objects to the reduction in Period Two 15-Year shipper billing determinants as compared to Period One 15-Year billing determinants. However, as discussed above, Kern River used the same actual 2004 test period data in designing the rates for the both Period One and Period Two. The only change Kern River made in the August 5, 2011 compliance filing from the billing determinants used to design the Period One rates was to eliminate an adjustment that is not appropriate for Period Two. Accordingly, Kern River utilized the appropriate test period data in calculating its Period Two rates for all shippers.

C. Election of Period Two Service on the Original System

52. As described above, on August 29, 2011, the Commission accepted Kern River's proposed GT&C section 30.2(d), requiring Original System shippers whose Period One service agreements expire on September 30, 2011 to "submit a binding request for [Period Two] transportation service no later than September 1, 2011." The Commission found that tariff provision to be consistent with Opinion No. 486-E's holding that it is just

⁵⁶ *Id.*, at Schedule J-2, p.1 line 3 and J-2, p. 64, line18. See also Kern River's August 24, 2011 Answer at 17-18.

and reasonable to require the Original System shippers “to make a binding and non-conditional commitment on or before September 1, 2011 to execute a service agreement for Period Two service with a term of either 10 or 15 years.”⁵⁷

53. NVE has two 10-year contracts for Period One service on the Original System expiring on September 30, 2011. One of those contracts (Contract No.7650) is for service under Self Contained Rate Schedule MO-1. On September 1, 2011, NVE provided notice to Kern River that it intended to contract for Period Two service at Period Two rates, commencing on October 1, 2011, for the Demand Maximum Daily Quantity of 37,933 Dekatherms, subject to the terms and conditions contained within its existing Self-Contained Contract No.7650 and the corresponding Rate Schedule MO-1.⁵⁸

54. NVE also stated that its notice of intent to contract for Period Two service was subject to NVE obtaining an order from the Commission which would make several findings. Specifically, NVE stated that its notice was conditioned upon findings by the Commission that:

A. Because NVE’s Notice of Intent to contract for Period Two service pursuant to the MO-1 Rate Schedule was specifically authorized by the Commission in its orders in Docket Nos. RP11-2328-000 and RP11-2356 as a valid choice available to NVE under Kern River’s existing tariff records, should the Commission authorize any modifications to the non-rate terms and conditions of the MO-1 rate schedule, then NVE shall have the option to discontinue Period Two service as of the effective date of such Commission determination.

B. Because of the continuing uncertainties surrounding the form and effect of NVE’s choice of Period Two service pursuant to the MO-1 rate schedule, because the Period Two rates are still not final, and because of the nature of the order sought from the Commission by NVE, NVE shall have an appropriate amount of time following issuance of such order to seek any senior management and Board of Directors approvals needed to proceed with execution of Period Two contractual arrangements with Kern River under the terms and conditions authorized by the Commission in the order sought by NVE.

⁵⁷ Opinion No. 486-E, 136 FERC ¶ 61,045 at P 84.

⁵⁸ NVE has chosen not to take Period Two service under its Rate Schedule KRF-1 Original System contract.

C. NVE's September 1, 2011 notice of intent, together with the foregoing determinations, was a valid election of Period Two service.

55. On the same date NVE submitted this notice to Kern River, NVE submitted a motion requesting that the Commission issue an order finding that its Notice of Intent to Contract, with its accompanying terms and conditions, would constitute a valid election of Period Two service from Kern River. NVE asserts that, without such a determination by the Commission, NVE would be unable to contract for Period Two service, because doing so at this time would require it to make a binding long-term contract commitment for service without a final determination of contract length, terms and conditions of service and rates.

56. In Condition A above, NVE requests that the Commission provide it the option to discontinue Period Two service if the Commission approves any modifications to the non-rate terms and conditions of the MO-1 Rate Schedule. NVE argues that this option is necessary, because the service benefits of Rate Schedule MO-1 comprise the key reason why it is interested in Period Two service. However, NVE contends that the Commission's orders have created uncertainty as to whether it will be able to retain those benefits for the full term of its Period Two contract.

57. In Opinion No. 486-E, the Commission rejected Kern River's proposal in the Docket No. RP04-274-000 section 5 proceeding to require all Period One shippers wishing to contract for Period Two service to enter into a new service agreement under its standard firm open access Rate Schedule KRF-1. Opinion No. 486-E held that the record in that proceeding was insufficient for the Commission to satisfy its section 5 burden to show that continued service under the Self Contained Rate Schedules would be unjust and unreasonable. However, the Commission stated that its holding was without prejudice to Kern River proposing under NGA section 4 to eliminate the Self Contained Rate Schedules pursuant to just and reasonable terms and conditions.⁵⁹

58. On July 29, 2011, Kern River proposed pursuant to section 4 to amend several provisions under its Self-Contained Rate Schedules in Docket No. RP11-2328-000. Kern River proposed to limit service under these rate schedules exclusively to the currently effective contracts of shippers taking service under those rate schedules until their current contracts expire. Kern River stated that service to existing customers would continue under the Self-Contained Rate Schedules, but that all new service, including Period Two service, will be offered exclusively under Kern River's Rate Schedule KRF-1. On August 29, 2011, the Commission accepted and suspended Kern River's Docket

⁵⁹ Opinion No. 486-E, 136 FERC ¶ 61,045 at P 117-120.

No. RP11-2328-000 proposal to be effective February 1, 2012, subject to the outcome of a technical conference.⁶⁰

59. In its August 29, 2011 order on the tariff records Kern River filed to comply with Opinion No. 486-E's requirements concerning the eligibility requirements for those rates, the Commission stated that, because it had suspended Kern River's Docket No. RP11-2328-000 proposal, Kern River's section 4 proposal in that docket was not currently in effect. Therefore, the Commission held that NVE or any similarly situated shipper with an expiring Self-Contained Contract may choose to receive Period Two service on September 1, 2011, subject to the terms and conditions of service contained within its existing Self-Contained Contract and the corresponding rate schedule. The Commission then stated:

However, Period Two service under this Self Contained Rate Schedule will remain subject to the Commission's action in Docket No. RP11-2328-000, as well as the outcome of the Commission's consideration of the requests for rehearing of Opinion No. 486-E, including Kern River's request for rehearing of that opinion's holdings on this issue.⁶¹

60. NVE asserts that the Commission's action in the August 29, 2011 order on Kern River's compliance filing means that it has only received a non-final determination by the Commission that it can continue receiving service under Rate Schedule MO-1 during Period Two. It argues that this is because the "However" sentence quoted above places it in the position of potentially losing that right and the service benefits of Rate Schedule MO-1 retroactively to September 1, 2011 based on future actions in Docket No. RP11-2328-000 and from future Commission action on Kern River's pending request for rehearing of Opinion No. 486-E.

61. NVE argues that it should not be forced to make the required commitment for service given the circumstances of this case and the Commission's existing determinations. It points out that currently service under the existing terms and conditions of Rate Schedule MO-1 is available to NVE for Period Two and that is what it chose by its notice. NVE argues that if and when such terms and conditions should become unavailable to NVE it should have the right to decline further service from Kern River at that point. NVE argues that the Commission should determine now that should the basis for NVE's election of Period Two service be modified (i.e. the non-rate terms and conditions of Rate Schedule MO-1), it would be inequitable to require NVE to

⁶⁰ *Kern River Gas Transmission Co.*, 136 FERC ¶ 61,141.

⁶¹ NVE Motion at 5 (citing, 136 FERC ¶ 61,141 at P 55).

continue to be bound to a different service and; therefore, NVE should have the option to discontinue Period Two service at Period Two rates on the date that its service is modified. Therefore, NVE requests that the Commission grant its requested Condition A.

62. In Condition B, NVE requests that the Commission provide NVE a reasonable time after the Commission issues an order approving Condition A to review that order. It argues that such additional time is needed to obtain approval by senior management and Board of Directors to proceed with execution of Period Two contractual arrangements consistent with the terms and conditions authorized by the Commission in the order granting Condition A. It argues that such time is also needed because many of the critical components of Period Two service continue to be attacked in requests for rehearing and therefore the look and cost of that service could be significantly changed by the time the contract documents need to be executed. NVE argues that it is in neither Kern River's nor its shippers' interests to force them to enter into long-term agreements with their significant financial and operational impacts while such critical matters as rates and length of contract remain open.

63. Lastly, NVE requests in Condition C that the Commission find that NVE's September 1, 2011 Notice of Intent was a valid election of Period Two service. NVE states that it recognizes that Ordering Paragraph (D) of Opinion No. 486-E requires NVE to make a binding election whether to execute 10 or 15-year contracts for service under Period Two rates on or before September 1, 2011. NVE's Notice of Intent chose a 15-year term. However, NVE asserts that Ordering Paragraph (D) did not include the requirement to specify the form of contract that would ultimately be available for that service and that issue is still pending before the Commission on rehearing of Opinion No. 486-E and in Docket No. RP11-2328-000. NVE argues that its notice specified that it chose to receive Period Two service under the terms and conditions contained in its existing contract and Rate Schedule MO-1. NVE argues that it did so even though the issues of contract length and the level of Period Two rates have not been finally decided by the Commission. NVE asserts that the risk of changes in these parameters is something that NVE believes is prudent to assume. However, NVE asserts that it cannot make a financial commitment of approximately \$50,000,00, for 15 years for a form of service that may change in the near future to a form that does not meet its needs. Accordingly, NVE requests that the Commission grant the relief requested herein by issuing the three determinations requested herein. NVE argues that absent such relief, NVE is unable at this time to commit to Period Two service for the 38,000 Dekatherms currently under Contract No.7650.

64. On September 6, 2011 Kern River filed an answer to NVE's motion. Kern River argues that there is no merit to NVE's attempt to impose conditions on its service at Period Two rates under Rate Schedule MO-1, and therefore, the Commission should deny NVE's motion outright and determine that Nevada Power has forfeited its right to receive

service at Period Two rates because of its failure to provide a binding, non-conditional commitment by September 1, 2011.

65. Kern River argues that the Commission's orders as cited above make it clear that the 10-year Original System shippers had to make a binding, non-conditional commitment no later than September 1, 2011. Kern River argues that NVE's motion fails to demonstrate any justification for retroactively modifying a Commission order after the time in which NVE was required by the Commission to provide a binding, non-conditional election.

66. Moreover, Kern River argues that the motion is a collateral attack on Opinion No. 486-E, the August 29, 2011 Compliance Order and Section 30 of Kern River's tariff. Kern River asserts that NVE's motion is contrary to the Commission's authority under the NGA. Kern River states that NVE is requesting that the Commission sanction a special, unduly discriminatory right for NVE to obtain Kern River's lowest, most beneficial rates without complying with the conditions applicable to eligibility for those rates. Further, Kern River notes that NVE is also claiming the right to terminate its service in the event this proceeding or any related proceeding fails to be finally resolved to its satisfaction, or if, at any time in the future, the Commission determines that it is just and reasonable to make changes to the MO-1 Rate Schedule.

67. Kern River argues that there is no basis for NVE to request or for the Commission to agree to such conditions given the fact that the Commission has required NVE to provide a binding commitment either for a 10-year or 15-year term by September 1, 2011. Kern River argues that NVE is attempting to claim the lowest 15-year Period Two rates when it failed to provide the binding, unconditional election required by the Commission, and at the same time, has not made any commitment to take or pay for any service at all.⁶²

68. Kern River argues that NVE's claims regarding continuing uncertainties surrounding Period Two is not a compelling justification for refusing to meet the Commission's order requiring binding notice. Kern River argues that the subject Period Two rates are subject to change at any time under section 4 or 5 of the NGA. Kern River asserts that the uncertainty such as that NVE complains of is nothing more than the uncertainty faced by any maximum-rate shipper with regard to the rates, terms and conditions of its service.⁶³ Kern River states that because the Period Two rates are less

⁶² Kern River adds that NVE has also failed to commit to execute a contract prior to October 1, 2011, in order to obtain this unreasonably conditioned service.

⁶³ Kern River points out that the Commission has already found that sufficient certainty exists with respect to the Period Two rates NVE will pay. Kern River Answer at 4, *citing*, 136 FERC ¶ 61,141 at P 84.

than half the rate NVE currently is paying, there is no irreparable harm to NVE, only the prospect that a change in rates could occur to ensure that such rates are, and remain, just and reasonable.

69. Kern River argues that the Commission did not give NVE the option to submit a “non-binding, conditional commitment” for Period Two service, and further it is unfair to permit one party to unilaterally claim a right to walk away from its service at any time after having accepted and received the benefit of the service. Accordingly, Kern River argues that the Commission must find that NVE has forfeited its right to receive service at Period Two step-down rates.

Commission Determination

70. The Commission denies NVE’s motion. First, it is clear that the Commission’s orders in this proceeding required 10-year Original System shippers with contracts expiring on September 30, 2011 to make a binding and non-conditional commitment to take Period Two service by September 1, 2011. In Opinion No. 486-E, the Commission held the following with regard to the 10-year Original System shippers:

This order is resolving all issues concerning the Period Two rates for those shippers and eligibility conditions they must satisfy in order to contract for Period Two service. Kern River must make a compliance filing calculating Period Two rates consistent with the holdings of this order on or before August 5, 2011. In these circumstances, the Commission finds that the 10-year Original System shippers will have sufficient information concerning Period Two contract rates and conditions of service, so that it is just and reasonable to require them to make a binding and non-conditional commitment on or before September 1, 2011 to execute a service agreement for Period Two service with a term of either 10 or 15 years. Opinion No. 486-E, 136 FERC ¶ 61,045 at P 84

In addition to this declaration, the Commission also stated at Ordering Paragraph (D) of Opinion 486-E that:

(D) Firm shippers on the Original System with Period One contracts expiring on September 30, 2011 must make a binding election whether to execute 10 or 15-year contracts for service under Period Two rates on or before September 1, 2011.

71. Further, in its August 29, 2011 order on compliance of Opinion No. 486-E, the Commission accepted certain tariff sheets after a discussion of its finding in Opinion No. 486-E with regard to the type of notice required of shippers such as NVE:

Proposed section 30.2(d) expressly addresses the contracting process for the 10-year Original System shippers whose contracts expire on September 30, 2011, requiring that they submit a binding request for Period Two service by September 1, 2011. . . . Moreover, the requirement that the 10-year Original system shippers make a binding commitment to execute a Period Two contract by September 1, 2011 is consistent with Opinion No. 486-E.⁶⁴

72. In NVE's motion, it concedes that it has not made an unconditional commitment for Period Two capacity as required by the Commission's orders. In fact, NVE states that it "simply cannot make a binding commitment with such critical parts of the service undecided."⁶⁵ Therefore, it is clear that NVE has not made the unconditional, binding commitment to take Period Two service required by Opinion No. 486-E, the August 29, 2011 order, and section 30.2(d) of Kern River's tariff.

73. NVE states that it should not be forced to make the required unconditional, binding commitment to take service during Period Two, because the Commission has not yet made a final determination that it will be able to take that service under Rate Schedule MO-1 for the entire term of Period Two, instead of being required to shift to service under Rate Schedule KRF-1. This argument fails for several reasons. First, the Commission finds that NVE has not presented it with a situation that is different from any other shipper required to recommit to capacity while a section 4 or 5 proceeding is pending in which changes are sought in the terms and conditions of the service at issue. Kern River provides firm transportation service under both Rate Schedules KRF-1 and MO-1.

74. Most of the terms and conditions applicable to those two services are identical. For example, both services have the same scheduling priorities, the same flexible point rights, and the same capacity release rights. According to NVE, the MO-1 Rate Schedule provides certain rights not included in Rate Schedule KRF service, including (1) daily balancing of receipts and deliveries; (2) a longer period to eliminate cumulative imbalances; and (3) the right to match any lower authorized overrun rate offered by Kern River. Even assuming that NVE is correct about the differences in the terms and conditions of the two services,⁶⁶ Kern River's proposal, both on rehearing of Opinion

⁶⁴ *Kern River Gas Transmission Co.*, 136 FERC ¶ 61,141 at P 48.

⁶⁵ NVE September 1, 2011 Motion at 1.

⁶⁶ The Commission has established a technical conference in Docket No. RP11-2328-000 for the purpose of discussing the precise differences in the terms and conditions of service between the Self-Contained Rate Schedules and Rate Schedule KRF-1 and the effects such differences, if any, have on the quality of transportation service provided by Kern River to the subject shippers.

No. 486-E and in its Docket No. RP11-2328-000 NGA section 4 filing, is essentially a proposal to modify certain terms and conditions of an existing firm transportation service, here primarily terms related to eliminating imbalances. It is not uncommon for such proposed changes in the terms and conditions of a pipeline's service to be pending when a shipper's contract for that service expires. If the Commission were to permit shippers to postpone making binding contractual commitments to continue to take a service until such issues are finally resolved, it would seriously interfere with pipelines' marketing of their services.

75. Here, NVE's contract expires on September 30, 2011. As a special accommodation to the two 10-year shippers on Kern River's Original System due to the unique circumstances of this proceeding, Opinion No. 486-E permitted those shippers not to make a binding commitment to take service in Period Two until September 1, 2011, only one month before the Period One contracts expired.⁶⁷ That allowed the shippers over one month to review Opinion No. 486-E and nearly a month to review Kern River's compliance filing before making a binding contractual commitment to take service during Period Two. The Commission recognizes that some uncertainties remain, including the fact that rehearing of Opinion No. 486-E's holdings concerning contract duration and the level of the Period Two rates is pending. However, NVE itself recognizes that "the risk of changes in these parameters is something that NVE believes is prudent to assume, given the Commission's authority over them."⁶⁸

76. Moreover, even at a point where all uncertainty as to the outcome of a currently pending section 4 or 5 proceeding is removed because all Commission determinations in a proceeding are final, there is no guarantee that the pipeline may not exercise its rights under the NGA to file a new section 4 proposal to change the terms, conditions, or rate for a shipper's service. Therefore, contrary to its assertions, NVE is facing no more uncertainty than that faced by any shipper with regard to the rates, terms and conditions of its service. For the Commission to require Kern River to wait to remarket its capacity until all uncertainty is removed from NVE's possible recommitment for such capacity would be unfair to Kern River. The Commission declines to grant any additional rights to NVE such as it has requested. Accordingly, the motion is denied.

⁶⁷ See *Kern River Transmission Co.*, 135 FERC ¶ 61,179 (2011), rejecting Kern River's proposal to require these shippers to make bidding commitments before the Commission had issued an order addressing the contract duration then pending before the Commission on exceptions from the ALJ's Period Two Initial Decision.

⁶⁸ September 1, 2011 Motion at 8.

The Commission orders:

(A) The tariff record listed in footnote no. 2 is accepted effective October 1, 2011.

(B) NVE's September 1, 2011 motion is denied.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.