148 FERC ¶ 61,228
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Cheryl A. LaFleur, Chairman;
Philip D. Moeller, Tony Clark,
and Norman C. Bay.

Hiland Crude, LLC Docket No. OR14-38-000

ORDER ON PETITION FOR DECLARATORY ORDER

(Issued September 25, 2014)

1. On August 8, 2014, Hiland Crude, LLC (Hiland), an affiliate of Hiland Partners, LP, filed a Petition for a Declaratory Order (Petition) requesting approval of the proposed rate structure and prorationing terms for Hiland's proposed Double H pipeline expansion project (Double H Expansion). After the expansion the Double H pipeline will be able to transport 74,000 barrels per day (bpd), an increase of 28,000 bpd.

2. Hiland explains that the Project will create much needed additional pipeline capacity to transport Bakken crude oil from points in North Dakota and Montana to pipeline connections at Guernsey, Wyoming. Hiland anticipates that the Double H Expansion project will commence operation in the fourth quarter of 2014.

3. As discussed below, the Commission grants the requested declaratory order.

<u>Background and Description of the Project</u>

4. Crude oil production from the Bakken region in North Dakota and Montana has increased dramatically in recent years. Production from the Bakken formation has reached over one million bpd, and significant additional production is expected from the region. Hiland explains that the rapidly increasing production has resulted in a shortage of pipeline capacity to U.S. refineries, which in turn has caused significant prorationing of existing pipelines from the Bakken region.

5. In response to this dramatic increase in production, Hiland is undertaking two projects, the Double H pipeline and the Double H expansion. The Double H pipeline consists of two segments: the H1 segment which transports gathered volumes of Bakken crude to a terminal in Baker, Montana, and the H2 segment which transports Bakken crude from Baker to Guernsey, Wyoming. At Guernsey, there are various interconnections including one with Pony Express, which enables pipeline transport to Cushing, Oklahoma. Hiland is constructing the Double H pipeline at a cost of $375 million.

6. Hiland's Double H Expansion involves (1) construction of four additional pump stations, utilizing approximately 2,000 horsepower per station; (2) construction of four additional pigging stations; and (3) upgrading four existing stations, adding redundancy with approximately 2,000 horsepower. Hiland states that following expansion, the Double H Pipeline will be able to transport approximately 74,000 barrels per day with the capability to further expand the capacity. Hiland expects the Double H Expansion will cost approximately $47 million.

7. Hiland explains that it required shipper commitments to make the expansion project economically viable. Hiland states that it held an open season from March 17 to April 30, 2014, for binding daily volume commitments for a five-year term. Hiland emphasizes that the open season was widely publicized and reported in the press and that all interested parties had an equal opportunity to participate. Hiland states that during the open season, Hiland provided prospective shippers a Throughput and Deficiency Agreement (T&D Agreement) and a *pro forma* tariff.

Key Terms of the T&D Agreement and the *pro forma* tariff

8. Hiland states that the T&D Agreement requires each Committed Shipper to ship a monthly minimum volume commitment or to make a deficiency payment if the Committed Shipper fails to meet its commitment. The initial contract period is five years. Hiland states that each shipper may make one-time election to extend the contract term by an additional five years, during which time shippers may also elect to reduce their minimum volume commitment by up to 20 percent. The T&D Agreement also provides for a volume incentive rate for committed volumes based on the committed volume shipped each month. Hiland explains that according to the T&D Agreement, Committed Shippers may elect to pay a premium rate on their shipments of at least $0.01 more than the rate payable for Uncommitted volumes to the same delivery point, which conforms to Commission precedent.[1] Hiland states that the initial tariff rate for Committed Volumes and the Volume Incentive Rates may vary as reflected by the annual FERC indexing methodology.[2]

9. Hiland's proposal reserves 90 percent of capacity for Committed Shipper volumes while ensuring that Uncommitted Shippers have access to at least 10 percent of capacity. Hiland states that when combined with shipper commitments for the joint committed rates in connection with Pony Express, Hiland has commitments for approximately 89 percent of the capacity on the H-2 segment. This leaves 11 percent of H-2 capacity for Uncommitted shippers and a greater percentage for Uncommitted capacity on H-1

[1] *See Kinder Morgan Pony Express Pipeline LLC*, 141 FERC ¶ 61,249 at PP 30-31 (2012) (*Pony Express*).

[2] 18 C.F.R. § 342.3 (2014).

segment. Hiland states that according to the proration provisions, Committed Shippers who elect to pay a premium rate shall not be subject to prorationing unless Hiland's overall monthly capacity available for transportation is reduced.

Hilands' Requested Rulings

10. Hiland requests a declaration that confirms the following:

i) The key provisions of the T&D Agreement will be upheld and applied during the term of the agreement.

ii) The filing of committed rates – including the initial committed rates and any adjustments thereto pursuant to the Commission's indexing methodology as settlement rates under 18 C.F.R. § 342.4(c) during the term of the T&D Agreement.

iii) The tiered committed rate discounts.

iv) The prorationing and related rate components, including:

(a) Hiland's proposed historically-based prorationing policy;

(b) Establishment of the initial Committed Shipper line history at the level of Committed Shipper's volume commitments; and

(c) Priority capacity, whereby a committed shipper may elect to receive priority capacity during periods of pipeline prorationing in exchange for premium rate.

v) The option of Committed Shippers to extend the term of the T&D Agreement for an additional five-year term.

vi) The option to use a revenue crediting mechanism for the rate design of Uncommitted rates.

Hiland's Supporting Statements

11. Hiland states that the Commission has a well-established policy that recognizes the value of providing advance guidance for significant infrastructure through its declaratory order process.[3] Hiland states that the expansion will require substantial capital outlays by Hiland and that the Committed Shippers provide revenue necessary to support the expansion.

[3] *See, e.g. Express Pipeline P'ship,* 76 FERC ¶ 61,245 (1996).

12. Hiland requests that the Commission confirm that it will uphold and apply the key provisions of the T&D Agreement during the term of that agreement, and asserts that this request comports with Commission precedent.[4] Hiland says that such approval is warranted to provide the pipeline and shippers with the appropriate level of regulatory certainty in light of the substantial commitments that are being made.

13. Hiland seeks authorization to file the committed rates, including the initial committed rates and any adjustments thereto, pursuant to the Commission's indexing methodology as settlement rates under 18 C.F.R. § 342.4(c) during the term of the T&D Agreement. Hiland states that although the Commission's regulations do not specifically provide for a negotiated rate with agreed-to subsequent rate changes, in cases where shippers have signed throughput and deficiency agreements and committed to pay for the contract volumes over a period of years, the Commission has treated these rates as effectively achieving the role of the settlement rates described in section 342.4(c) of the Commission's regulations.

14. Hiland states that its tiered committed rate discounts are consistent with Commission precedent. Committed Shippers had the option in the open season to commit to a tiered committed rate structure with lower rates applicable to greater volume commitments.[5] Hiland states that shippers making larger volume commitments are not similarly situated to shippers with smaller volume commitments because the level of costs, liabilities and risks are not comparable. Accordingly, the tiered committed rate discounts are appropriate.

15. Hiland maintains that its prorationing and related rate proposals are also consistent with Commission precedent. Hiland states that the Commission has previously approved historically-based prorationing policies that allocate 90 percent of available capacity to historical shippers and set aside 10 percent of capacity to new shippers.[6] Furthermore, Hiland states that the Commission has also permitted pipelines to grant committed

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[4] *Pony Express*, 141 FERC ¶ 61,249 at P 20 (citing *Mid-America Pipeline Co., LLC*, 136 FERC ¶ 61,087, at P 9 (2011); *Enbridge Pipelines (Southern Lights) LLC*, 122 FERC ¶ 61,170, at P 13 (2008)); *see also Centerpoint Energy Bakken Crude Services, LLC*, 144 FERC ¶ 61,130, at P 17 (2013).

[5] *Pony Express*, 141 FERC ¶ 61,249 at P 22. The Commission stated as follows:

> The Commission previously has recognized that it is appropriate for shippers committing to larger volumes to pay discounted rates, versus shippers that do not commit to transport larger volumes.

[6] *See, e.g. Marketlink, LLC*, 144 FERC ¶ 61,086, at P 16 (2013).

shippers initial history at the level of their volume commitments on the in-service date.[7] Finally, Hiland states that the Commission has approved requests to provide Committed Shippers with discounts relative to Uncommitted shippers when the pipeline is not in prorationing, along with the ability to elect priority capacity not subject to prorationing when the pipeline is under prorationing.[8]

16. Hiland says these proposals represent a reasonable, non-discriminatory means of balancing the needs of the pipeline, Uncommitted shippers, and Committed Shippers. Hiland receives the commitments necessary to undertake the Double H Expansion and attracts new volumes to its system. Committed Shippers receive a discount when the pipeline is not under prorationing. In exchange for their volume and term commitments, Committed Shippers may elect to receive priority capacity during periods of prorationing at a premium rate, which means that the pipeline's capacity is awarded to those who value it most. Uncommitted shippers are still eligible to ship on the Double H pipeline but are free to choose not to ship every month and do not have to provide commitments. Uncommitted shippers remain eligible to build line history under Hiland's historically based prorationing policy.

17. Hiland says that its proposed term extension provision is consistent with Commission precedent. Hiland points out that the five-year contract term, with the five-year extension right, includes the right to reduce committed volumes by 20 percent during the extension term. Hiland claims that such a term extension provision is appropriate and reasonable given that it provides shippers with an option - but not a requirement – to renew and reduce their commitments.[9]

18. Hiland says that its proposed revenue crediting mechanism for the design of Uncommitted rates is consistent with Commission precedent as well. Hiland states that it supports its initial Uncommitted rates with a cost of service presentation; it requests the flexibility to design Uncommitted rates using a revenue crediting mechanism. Under this approach, Hiland would develop a cost of service for the Double H Pipeline and then subtract revenues generated by Committed Shippers. The difference would then be divided by the Uncommitted barrels for purposes of deriving Uncommitted rates. While this approach may result in Uncommitted shippers bearing a higher share of the

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[7] *Id*.

[8] *See, e.g. Enterprise TE Products Pipeline Co., LLC,* 144 FERC ¶ 61,092, at P 16 (2013); *Explorer Pipeline Co.,* 140 FERC ¶ 61,098 (2012).

[9] *See, e.g., Enbridge Energy Co., Inc.*, 110 FERC ¶ 61,211, at P 10 (2005).

pipeline's costs on a per unit basis, Hiland states that the Commission has previously concluded that such a result is not unjust or unreasonable.[10]

Public Notice and Interventions

19. Notice of the filing was issued August 12, 2014, with interventions and protests due August 29, 2014. Pursuant to Rule 214 of the Commission's regulations,[11] all timely-filed motions to intervene and any unopposed motion to intervene out-of-time before the issuance date of this order are granted. Granting late intervention at this stage of the proceeding will not delay or disrupt the proceeding or place additional burdens on existing parties. The petition is unopposed.

Commission Analysis

20. The Commission grants the rulings requested in the Petition. Granting these rulings will provide regulatory certainty for an important expansion project that will transport Bakken oil to markets and refining centers.

21. The Commission will grant the requested ruling on upholding the key provisions of the T&D Agreement as consistent with Commission precedent. The Commission has elsewhere approved the terms of the agreements executed by committed shippers (including the agreed-to tariff, rate, and priority service structure) and confirmed that these terms would be applied during the established terms of the agreements between the pipeline and the shippers that made volume commitments during the open season.[12]

22. The Commission will approve Hiland's request for a tiered committed rate discount because it is consistent with Commission policy and precedent. The Commission has previously recognized that it is appropriate for shippers committing to larger volumes to pay discounted rates.[13]

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[10] *See TransCanada Keystone Pipeline, LP*, 125 FERC ¶ 61,025, at P 25 (2008).

[11] 18 C.F.R. § 385.214 (2014).

[12] *See, e.g., Mid-America Pipeline Co., LLC*, 136 FERC ¶ 61,087, at P 9 (2011), cited in *Pony Express*, 141 FERC ¶ 61,249 at P 20; *see also Enbridge Pipelines (Southern Lights) LLC*, 122 FERC ¶ 61,170, at P 13 (2008) ("[T]he Commission clarifies that the agreed-upon terms of the TSA will govern the determination of the Committed shippers' rates over the term of the TSA[.]").

[13] *See, e.g., Plantation Pipe Line Co.*, 98 FERC ¶ 61,219 (2002); *Williams Pipe Line Co.*, 80 FERC ¶ 61,402 (1997).

23. The Commission will approve Hiland's prorationing policies because they appear consistent with Commission policy and precedent.[14]

24. The Commission will approve Hiland's request for a contract extension option of T&D Agreement for Committed Shippers. The Commission has approved similar contract extension/rollover rights in prior declaratory orders addressing new pipeline capacity.[15]

25. The Commission will grant the requested ruling on the revenue crediting mechanism for Uncommitted rates because it is consistent with Commission policy and precedent, such as the mechanisms approved in *TransCanada Keystone*.[16] In that case, the Commission stated that revenue-crediting mechanisms recognize the fact that committed shippers have assumed significant risk by committing volumes under long-term contracts - risks that Uncommitted shippers do not bear. Thus, Committed and Uncommitted shippers are not similarly situated. Finally, the Commission also approves the general concept of designing Uncommitted Shipper rates by subtracting the revenues provided by Committed Shippers in order to derive the costs to be recovered from Committed Shippers.[17]

<u>The Commission orders</u>:

The Petition for a Declaratory Order is granted, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

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[14] *See, e.g., Marketlink, LLC*, 144 FERC ¶ 61,086, at P 16 (2013).

[15] *See Pony Express*, 141 FERC ¶ 61,249 at P 39.

[16] *TransCanada Keystone Pipeline, LP*, 125 FERC ¶ 61,025, at P 25 (2008).

[17] However, the actual uncommitted rates must, if challenged, be supported as just and reasonable.