153 FERC ¶ 61,292
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Paiute Pipeline Company — Docket Nos. CP14-509-001, RP16-212-000

ORDER ON REHEARING

(Issued December 14, 2015)

1. On May 14, 2015, the Commission issued an order authorizing Paiute Pipeline Company (Paiute) pursuant to section 7(c) of the Natural Gas Act (NGA)[1] to construct and operate its Elko Area Expansion Project.[2] On June 12, 2015, Paiute timely filed a request for rehearing of the May14 Order. As discussed below, this order grants rehearing in part and denies rehearing in part. This order also addresses Paiute's filing in Docket No. RP16-212-000, filed on November 20, 2015, as it pertains to findings made in this order.

I. Background

2. The May 14 Order authorized Paiute to construct and operate approximately 35.2 miles of 8-inch-diameter pipeline extending from a new interconnection with Ruby Pipeline, LLC's existing Wieland Flat Compressor Station to Paiute's Elko City Gate (the Adobe Lateral) and to modify facilities at its Elko City Gate. The Elko Area Expansion Project will enable Paiute to provide 21,994 dekatherms (Dth) per day of incremental firm transportation service to two shippers, Southwest-Northern Nevada (Southwest-NN) and Newmont Mining Corporation (Newmont).

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[1] 15 U.S.C. § 717f(c) (2012).

[2] *Paiute Pipeline Co.*, 151 FERC ¶ 61,132 (2015) (May14 Order).

II. Discussion

A. Request for Rehearing

1. Administrative and General Expenses

3. The May 14 Order rejected Paiute's proposal to include $689,061 of estimated overhead costs as administrative and general (A&G) expenses attributable to the Elko Area Expansion Project.[3] This rejection was based on Paiute's failure to identify in Exhibit N to its application any new overhead costs that will be incurred by its parent, Southwest Gas Corporation (Southwest Gas), attributable to the incremental Elko Area Expansion Project. Noting that overhead costs are normally recovered through base (system) rates, the May 14 Order found that permitting Paiute to recover such costs through the incremental Elko Area Expansion Project rates could result in their double recovery.

4. Paiute contends that the Commission made three errors in rejecting its proposal to include $689,061 of estimated overhead costs as A&G expenses attributable to the Elko Area Expansion Project.[4] First, Paiute states Commission policy does not require exclusion of all common A&G expenses from the cost of service used to derive an incremental firm recourse rate.[5] Paiute maintains that the requirement for it to exclude "all common administrative and general expenses from the incremental recourse rate" will "produce unreasonable results." Paiute states that it is not seeking to reallocate either existing system facilities' costs or common A&G costs already allocated to system shippers in existing rates. Rather, Paiute states that its proposed Elko Area Expansion Project A&G estimates are reasonable and based on the application of the Commission-accepted Modified Massachusetts Formula (MMF).[6]

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[3] *See* May 14 Order, 151 FERC ¶ 61,132 at PP 36-37.

[4] Paiute Rehearing at 4-16.

[5] Paiute Rehearing at 7-9.

[6] Paiute Rehearing at 4-7, 13-16. The Modified Massachusetts Formula is used to allocate overhead costs (expenses that are incurred by, and charged from, parent companies and/or service companies to subsidiaries and affiliates) among corporate subsidiaries when the costs cannot be directly allocated to specific subsidiaries. *See Distrigas of Mass. Corp.*, 41 FERC ¶ 61,205, at 61,555-57 (1987).

5. Second, Paiute states there are increases in direct labor, margin, and gross plant costs associated with pipeline expansions, and to exclude all estimated A&G expenses from the proposed project's incremental rate would underprice the expansion and cause Paiute to under-recover its costs.[7] Paiute asserts there definitely will be a change in the allocation of corporate A&G expenses to Paiute under the MMF as a result of the project. Paiute explains that each year Southwest Gas recalculates the MMF allocation factor used to allocate corporate A&G costs to its subsidiaries. Each month, Southwest Gas transfers Paiute's allocated portion of A&G expenses to Paiute, which is then recorded on Paiute's books. As a result of the proposed project, Paiute states that higher A&G costs will be allocated to Paiute as direct labor, margin, and gross plant ratios increase. Paiute also notes that the Commission has accepted Paiute's inclusion of estimated A&G costs using the same MMF methodology in two of Paiute's recent expansions.[8] Therefore, Paiute requests "the increase in A&G expenses allocated to it by its parent through the MMF due to the changed allocation factor," be included in its incremental rate.

6. Third and finally, Paiute contends that properly estimated A&G costs associated with an expansion do not create double recovery concerns merely because they involve allocated common costs.[9] Paiute points out in this regard that the Commission has "recognized that pipelines will incur A&G costs in connection with expansion capacity and approved the pipelines' estimate of A&G expenses in initial incremental rates." Therefore, Paiute contends that the Commission misinterpreted the estimated A&G costs provided in Exhibit N of its application and inaccurately concluded that inclusion of Paiute's estimated A&G costs could result in double recovery.

Commission Determination

7. The Commission grants rehearing on this issue. The Commission acknowledges that the MMF is an accepted tool for allocating costs. The Commission also agrees that the Elko Expansion will result in additional allocated common A&G expenses to Paiute from its parent, Southwest Gas. Further, the Commission has previously acknowledged Paiute has no employees, therefore, costs such as A&G labor "represent charges to Paiute for work performed on its behalf by employees of its parent, Southwest Gas Corporation" and such costs are "either assigned directly from Southwest or allocated from Southwest

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[7] Paiute Rehearing at 5.

[8] Paiute Rehearing at 5 (citing *Paiute Pipeline Co.*, 76 FERC ¶ 61,114 (1996); *Paiute Pipeline Co.*, 104 FERC ¶ 61,078 (2003); *Paiute Pipeline Co.*, 132 FERC ¶ 61,156 (2010)).

[9] Paiute Rehearing at 9-13.

to Paiute using the [MMF].”[10] Moreover, the Commission finds that the proposed $689,061 is an adequate estimate of incremental A&G costs associated with the Elko Project. Therefore, consistent with its prior rulings on Paiute’s expansions and to ensure there is no double recovery, the Commission approves Paiute’s initial rates only to the extent that they do not include existing A&G costs but solely include A&G costs associated with the instant Elko Project.

2. Interruptible Transportation Rate

8. The May 14 Order required Paiute to file a new interruptible transportation (IT) rate based on the 100 percent load factor of the incremental recourse rate for the Elko Area Expansion Project. Paiute claims that the Commission erred in requiring it to file a new IT rate because, under Commission policy, pipelines are required to charge their current system IT rate for interruptible service rendered on capacity made available due to integrated expansion facilities.[11] Paiute explains that while it did not identify the specific IT rate for service on the Elko Area Expansion Project facilities, Paiute intended to use its existing system IT rate for service on the proposed project because the project’s facilities are integrated and Paiute uses postage stamp rates.

Commission Determination

9. Paiute’s project will provide upstream access to supply sources through a new transportation path into the Elko, Nevada area to satisfy the growth requirements of the two expansion shippers, Southwest-NN and Newmont. Paiute also claimed that its proposal could result in shippers gaming its imbalance management – a proposition that implied separate rates for different segments of Paiute’s system. Described in that way, the project resembles a stand-alone lateral, in that it is for the benefit of only a small number of customers. However, in its rehearing request, Paiute points out that the Elko Area Expansion Project is physically connected to Paiute’s existing Elko Lateral at the Elko City Gate,[12] that Newmont’s primary delivery point is on Paiute’s existing system,

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[10] *Paiute Pipeline Co.*, 76 FERC ¶ 61,114, at 61,592 (1996).

[11] Request for Rehearing at 17 (citing *Texas Eastern Transmission, LP*, 139 FERC ¶ 61,138, at P 31 (2012), *reh’g denied*, 141 FERC ¶ 61,043, at PP 68-69 (2012), *order amending certificate*, 145 FERC ¶ 61,016 (2013), *petition for review dismissed*, *No Gas Pipeline v. FERC*, 756 F.3d 764 (D.C. Cir. 2014); *Columbia Gas Transmission, LLC*, 146 FERC ¶ 61,069, at P 19 and Ordering Paragraph (C) (2014), *modified on other grounds*, 148 FERC ¶ 61,152 (2014); *Texas Eastern Transmission, LP*, 146 FERC ¶ 61,086, at P 10 and Ordering Paragraph (E) (2014)).

[12] Paiute’s natural gas transmission system extends approximately 226 miles in a

(continued...)

and that Southwest-NN has the right to ship gas to alternate delivery points on the existing system. Moreover, in order to subscribe to service on the proposed project, Paiute states that Southwest-NN turned back transportation service from Paiute's existing Owyhee Receipt Point to various delivery points on the existing Elko Lateral.

10. Based on these statements, the Commission accepts Paiute's explanation that its Elko Area Expansion Project facilities are integrated with its existing Elko Lateral facilities, and grants rehearing on this issue. Paiute is correct that it is the Commission's policy "to require a pipeline to charge its current system IT rate for any interruptible service rendered on additional capacity made available as a result of an incremental expansion that is integrated with existing pipeline facilities."[13] Accordingly, the May 14 Order's requirement that Paiute file a new IT rate based on 100 percent load factor of the incremental recourse rate for the proposed project was not appropriate. Consistent with Commission policy, Paiute is directed to charge its current system IT rate for any new interruptible service on the Elko Area Expansion Project.

<u>Re-examination of Initial Firm Transportation Rates</u>

11. In the May 14 Order, the Commission interpreted Paiute's initial rate design as a request for incremental rates for service on just the Elko Area Expansion Project. However, Paiute has clarified that the proposed pipeline is not a stand-alone lateral, but rather an "operationally integrated lateral." Thus, the Commission must re-examine the May 14 Order's findings with regard to the initial rates applicable to transporting the incremental capacity on Paiute's system.

12. Paiute projected a first year cost of service of $6,429,965.[14] The May 14 Order largely approved Paiute's proposed cost of service but rejected Paiute's proposed incremental corporate overhead costs of $689,061,[15] its inflation adjustments for

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southerly direction from an interconnection with Northwest Pipeline, LLC at the Owyhee Receipt Point near the Idaho-Nevada border. Paiute's Elko Lateral, which begins at a point approximately 100 miles downstream of the Owyhee Receipt Point, extends in an easterly direction for approximately 147 miles to the existing Elko City Gate.

[13] *Texas Eastern Transmission, LP*, 139 FERC ¶ 61,138, at P 31 (2012) (citing *Gulf South Pipeline Co., LP*, 130 FERC ¶ 61,015 (2010); *Kern River Transmission Co.*, 117 FERC ¶ 61,077, at PP 313-314 and 326 (2006)).

[14] May 14 Order, 151 FERC ¶ 61,132 at P 35.

[15] *Id.* P 37.

incremental Operations and Maintenance costs ($6,830), and property taxes ($23,353).[16] Above, the Commission granted Paiute's request for rehearing of the Commission's A&G cost of service finding. Thus, the May 14 Order's finding that the incremental cost of service for the Elko Area Expansion Project is $5,710,721 should be increased by approximately $689,061.[17]

13. Paiute proposes to recover the project's incremental cost of service through incremental firm rates calculated using the Straight Fixed-Variable cost classification methodology. Paiute proposes an incremental monthly reservation charge for Rate Schedule FT-1 firm service of $24.3626 per Dth, and a usage charge of $0.0000 per Dth, a zero fuel retention charge, and a lost and unaccounted for gas retention charge for natural gas transported on the project and applicable surcharges.[18]

14. The Commission's cost of service findings in the May 14 Order and the December 14, 2015 Order in CP14-509-002 and RP16-174-000 (December 14 Amendment Order), which grants Paiute's request to amend its certificate to include updates cost data, will require Paiute to recalculate its initial rates. Notwithstanding, the changes required will not reduce the final reservation charge to approach, much less go below, currently effective Rate Schedule FT-1 system reservation charge of $10.2286 per Dth per month for contracts five years or greater, with a usage charge of $0.0000 per Dth.[19] Under the Certificate Policy Statement, the threshold requirement for applicants proposing new projects is that the applicant must be prepared to financially support the project without relying on subsidization from its existing customers.[20] The initial monthly reservation charge will likely be significantly higher than the currently effective rates existing customers pay. To ensure that existing customers will not subsidize the cost of the incremental capacity, the Commission accepts Paiute's proposal to apply an

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[16] *Id.* P 38.

[17] Concurrently with this order, the Commission is issuing an order granting Paiute's request to amend its certificate to included updated cost data. *Paiute Pipeline Co.* 153 FERC ¶ 61,291 (2015). Thus, the overall cost of service will change.

[18] May 14 Order, 151 FERC ¶ 61,132 at P 12.

[19] Paiute Pipeline Company's FERC NGA Gas Tariff, Paiute Pipeline Company, Statement of Rates, Statement of Rates, 5.0.0.

[20] *Certification of New Interstate Natural Gas Pipeline Facilities*, 88 FERC ¶ 61,227 (1999), *clarified*, 90 FERC ¶ 61,128 (2000), *further clarified*, 92 FERC ¶ 61,094 (2000) (Certificate Policy Statement).

incremental monthly reservation charge for firm service. Paiute's proposed firm service usage charge is the same as its currently effective system usage charge. Thus, the Commission finds that the system usage charge is appropriate as the initial usage charge for the Elko Area Expansion Project capacity. As the reservation charge is an incremental rate, the accounting requirements of Order No. 710[21] apply and the reporting requirements of the May 14 Order remain unchanged.[22]

15. For transportation service using only the expansion facilities, Paiute proposes to charge a zero fuel retention charge and a lost and unaccounted for gas retention charge for gas. Paiute argues that not including a fuel charge is appropriate, as it will not have any compression facilities on the Elko Area Expansion Project extending from the Jade Flats receipt point where gas is received from Ruby Pipeline to the interconnection with the Elko Lateral at the Elko City Gate.[23] This proposed retention charge is lower than Paiute's currently effective system-wide retention charge.[24]

16. The Commission rejects Paiute's proposed fuel retention rate for the expansion facilities. Paiute clarified, as discussed above, that the Elko Area Expansion Project is integrated with, and an extension of Paiute's system. The service to be rendered is not only for transportation over the project's facilities, but also includes any delivery point on Paiute's system. Thus, while fuel may not be used to transport natural gas over the project facilities, it may be used for natural gas delivered elsewhere on the system. Paiute's system fuel rate design is a postage stamp rate design. Such a rate design does not evaluate and bill customers on the basis of their individual fuel use, but instead essentially uses a system average rate. Paiute's proposal to treat transportation over the project facilities as part of its integrated system for reservation and usage charge purposes

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[21] *Revisions to Forms, Statements, and Reporting Requirements for Natural Gas Pipelines*, Order No. 710, FERC Stats. & Regs. ¶ 31,267 (2008).

[22] May 14 Order, 151 FERC ¶ 61,132 at P 44.

[23] *Id.* P 12.

[24] Paiute's currently effective system-wide retention charge is only applied to gas received at certain identified receipt points. Paiute posts the retention charge monthly. The monthly calculated retention charge is based on prior months' actual average daily use of fuel, lost and unaccounted for gas, and the calculated retention charge must be within a defined range of minimum and maximum retention percentages. *See* Paiute Pipeline Company's FERC NGA Gas Tariff, Paiute Pipeline Company, Section 4.2 (c)-(d), GTC - Operating Procedures, 1.0.0 and Section 4.2 (d)(1), GTC - Operating Procedures, 0.0.0, at Section 4.2(d).

is inconsistent with its proposal to not charge project shippers fuel costs, even though these customers will have the right to transport natural gas anywhere on Paiute's system. Paiute's proposal would bill shippers that transport natural gas on the project facilities less than shippers that transport natural gas on other parts of its system. This proposal is unduly preferential to the Elko Area Expansion Project shippers, as compared to Paiute's existing shippers.

17. It is Commission policy to authorize system charges for the initial rates except when it is shown that rolling-in incremental costs may result in existing customers subsidizing the expansion shippers.[25] In this case, Paiute clearly documents that its expected fuel costs will be lower than its currently effective fuel costs. Thus, the Commission will require Paiute to use its system fuel rates for transportation utilizing the Elko Area Expansion Project capacity.

18. At section 4.2(d)(i) of its General Terms and Conditions (GT&C), Paiute proposes to change its existing tariff to reflect the new Elko Area Expansion Project capacity. Paiute's proposed language would create an incremental fuel and lost and unaccounted for gas retention rate for shippers using the project capacity. Consistent with the Commission's finding above that Paiute's fuel retention rate proposal is unduly preferential, the Commission rejects this language in section 4.2(d)(i) of Paiute's GT&C. Further, at *pro forma* Sheet No. 21, Paiute proposes that only the firm expansion "[s]hippers shall be responsible for their proportionate share of any quantities of gas needed to replenish linepack, as requested by Paiute from time to time." This provision may subject the Adobe Lateral firm shippers to two charges for lost and unaccounted for gas. The Commission rejects this provision as unduly discriminatory.

3. <u>Imbalance Trading</u>

19. Paiute's tariff currently provides that shippers on its system may trade imbalances irrespective of where the imbalance occurred on Paiute's system. To the extent the imbalance trade results in an under- or over-payment of transportation revenues, Paiute will either bill or credit the responsible party for the difference.[26] Paiute, in its certificate application, proposed *pro forma* tariff changes to its existing imbalance trading procedures. These changes would prohibit shippers from trading imbalances at delivery

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[25] *Southeast Supply Header, LLC*, 148 FERC ¶ 61,121, at P 20 (2014), *reh'g denied*, 151 FERC ¶ 61,032 (2015).

[26] Paiute Pipeline Company, FERC NGA Gas Tariff, Paiute Pipeline Company, Sections 5.3 (e) - 5.4, GTC - Balancing Penalties - Balancing, 2.0.0, at section 5.3(e).

points which require fuel with delivery points on the Elko Area Expansion Project which do not require fuel. Paiute stated the reason for this proposal is to prevent cross-subsidization from existing customers.

20. The May 14 Order disallowed Paiute's proposal to prohibit shippers from trading imbalances between its existing system delivery points and expansion delivery points. The Commission acknowledged that cross-subsidization is a legitimate concern. Notwithstanding, the Commission found that Paiute's proposal was contrary to our regulations, which state that pipelines "must establish provisions permitting shippers and their agents to offset imbalances accruing on different contracts held by the shipper with the pipeline and to trade imbalances with other shippers where such imbalances have similar operational impact on the pipeline's system."[27] The Commission acknowledged that there may be operational reasons not to permit some imbalance trading, but Paiute made no such claim. The Commission recognized that when imbalance trades within an Operational Impact Area cross rate zones a transportation service can be said to take place.

21. As has been discussed above, in the initial order in this proceeding, the Commission interpreted Paiute's initial rate proposal as a request for an initial rate for transportation solely on the Adobe Lateral. Thus, the Commission stated, charging for imbalances traded across rate zones may be appropriate and will ensure that shippers will not try to game the system to save transportation costs. The Commission rejected Paiute's proposal to prohibit Adobe Lateral shippers from trading their imbalances with imbalances incurred elsewhere on the system. The Commission further stated that if Paiute were to propose a rate applicable to imbalance trades that occur between the two parts of its system, it cannot make that proposal in the instant NGA section 7 certificate proceeding. Such a rate would be applicable to all of Paiute's transportation services and customers, not just those that are the subject of the proposed project. Such a rate proposal would have to be made pursuant to an NGA section 4 tariff filing.[28]

22. Paiute, in its request for rehearing, contends that the proposed changes to its existing imbalance trading procedures are necessary to prevent cross-subsidization from existing customers. Paiute stresses that the gaming that can occur from the imbalance trading requirement relates to the difference in fuel factors, not in zonal transportation rates. Paiute's argument is that its proposed changes would prevent shippers from trading imbalances at delivery points which require fuel with delivery points on the proposed pipeline which do not require fuel.

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[27] 18 C.F.R. § 284.12(b)(2)(ii) (2015).

[28] May 14 Order, 151 FERC ¶ 61,132 at PP 46-48.

Commission Determination

23. The Commission denies Paiute's request for rehearing as moot because, consistent with Paiute's clarification that the Elko Area Expansion Project is integrated with the existing Elko Lateral facilities, the Commission found that shippers utilizing the Elko Area Expansion Project should be subject to the same fuel retention charges as any other shippers on Paiute's system. Thus, there will not be any difference in fuel charges for the Elko Area Expansion Project shippers as compared to shippers utilizing other parts of Paiute's system. As the fuel charge is the same for all shippers on Paiute's system, there is no opportunity for shippers to game imbalance trading to capitalize on a difference in fuel charges. Further, Paiute's tariff already provides that Paiute may charge traded volumes that result in an under-recovery of transportation revenues. Thus, Paiute is not exposed to a cost under-recovery simply because of imbalance trading. Accordingly, Paiute's request for rehearing on this issue is denied.

B. Docket No. RP16-212-000

24. On November 20, 2015, Paiute, in Docket No. RP16-212-000, proposed to prohibit imbalance trading for imbalances incurred on the Adobe Lateral with imbalances incurred elsewhere on Paiute's system. Paiute supported its proposal on the basis that its lateral line rate design for fuel would create an opportunity for gaming the different rates between the rate zones. Paiute also proposed a mechanism that nets the system Gas Used percentage and the lost and unaccounted for percentage for a trade involving the Adobe Lateral to Delivery Location 8 (the end of the Adobe Lateral at Elko, Nevada) and other system deliveries. As a result, Paiute states it will recover the same fuel and lost and unaccounted for gas from its shippers as it would if the trade did not occur and shippers reduced their imbalances through the scheduling process. Paiute submitted examples as to how imbalance trading across its rate zones may result in lost fuel, lost and unaccounted for gas revenues and how its proposal would make Paiute whole.

25. The Commission rejects Paiute's proposal. Above, the Commission granted rehearing and concluded that Paiute's proposed project is not a stand-alone lateral, but rather an "operationally integrated lateral" and therefore, the pipeline must use its system fuel, lost and unaccounted for gas retention rate for the incremental services provided through the Adobe Lateral. Against this ruling, the filing in Docket No. RP16-212-000 becomes moot because the initial rate for fuel, lost and unaccounted for gas will be the same as the system rate, and there is no opportunity for shippers to game imbalance trading to Paiute's disadvantage – the justification for the Docket No. RP16-212-000 filing.

C. Compliance

26. As discussed above, the Commission finds that Paiute did propose an incremental rate for service on its full system, not just the Adobe Lateral; and grants rehearing

permitting Paiute to recover additional A&G overhead through its initial rates. As noted in the December 14 Amendment Order, both of these findings will require aspects of the Docket No. RP16-174-000 compliance tariff records to be modified.

27. Within 15 days of the date of this order, the Commission requires Paiute to file compliance tariff records that reflect the initial incremental Rate Schedule FT-1 rates recalculated consistent with the discussion above. Paiute is required to remove Rate Schedule IT-2 and all references thereto from its tariff. As the Commission found that the applicable initial rate for fuel, lost and unaccounted for gas is Paiute's system retention rate, all references to incrementally calculated gas retention rates must be removed from Paiute's tariff.

The Commission orders:

(A) Paiute's request for rehearing is granted, in part, and denied, in part, as discussed in the body of this order.

(B) Paiute is hereby directed to recalculate the initial firm transportation rate applicable to transporting the incremental capacity on Paiute's system and make its compliance filing within 15 days of the date of this order, as detailed in the body of this order.

(C) Paiute's tariff record filed in Docket No. RP16-212-000 is rejected.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.