FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, D.C. 20426

January 6, 2006

In Reply Refer To:
Eastern Shore Natural Gas Company
Docket No. RP06-144-000

Eastern Shore Natural Gas Company
417 Bank Lane
Dover, Delaware 19904

Attention: Ronald A. Craig

Reference: Revisions to Penalty Provisions

Dear Mr. Craig:

1. On December 9, 2005, Eastern Shore Natural Gas Company (Eastern Shore) filed revised tariff sheets[1] to replace its existing fixed price penalties with penalties that are the higher of a fixed price or a multiple of a daily index price. The proposed revised penalties apply to shippers who violate Operational Flow Orders (OFO) and to shippers who take unauthorized overrun volumes resulting in a threat to operational integrity of the pipeline, or to Eastern Shore's ability to render reliable service. For good cause shown, waiver of the notice period is granted and the tariff sheets are accepted effective December 21, 2005, as proposed.

2. Eastern Shore proposes two changes to its unauthorized overrun penalty during periods when curtailment is not in effect. Currently, the penalty for unauthorized overrun volumes when curtailment is not in effect is $2.50 per Dth for overruns up to 50 Dth, and $25 for any additional overrun volumes taken on that Gas Day. Eastern Shore proposes to: (1) eliminate the $2.50 per Dth penalty for overruns up to 50 Dth and (2) charge a penalty of the higher of (i) $50 per Dth or (ii) two times the mid-point range of prices reported for Transco Zone 6 non-N.Y. published in the Daily price survey by Platt's Gas Daily per Dth for all unauthorized overrun quantities taken on that Gas Day.

[1] Fourth Revised Sheet No. 162, First Revised Sheet No. 173C, and Original Sheet No. 173C.01 to FERC Gas Tariff, Second Revised Volume No. 1.

3. The current penalty for unauthorized overrun volumes when curtailment is in effect is $25.00 per Dth. Eastern Shore proposes to change that penalty to the higher of (i) $50 per Dth or (ii) three times the mid-point of the range of prices reported for Transco Zone 6 non-N.Y. published in the Daily price survey by Platt's Gas Daily, per Dth. Eastern Shore's tariff provides that Eastern Shore will waive any penalties against shippers in circumstances where the imposition of the penalty is not necessary to protect the operational integrity of the system or Eastern Shore's ability to render reliable service.

4. Eastern Shore also proposes to change its penalties for violations of Levels One, Two and Three OFOs from $25 per Dth to the higher of (i) $50 per Dth or (ii) three times the mid-point of the range of prices reported for Transco Zone 6 non-N.Y. published in the Daily price survey by Platt's Gas Daily for the day on which the OFO is in effect, per Dth. Eastern Shore requests waiver of the notice requirements in section 154.207 of the Commission's regulations, 18 C.F.R. §154.207 (2005), to permit a December 21, 2005 effective date.

5. Eastern Shore states that these revisions are necessary due to higher prices in the current natural gas market, and that in order for penalties to serve as a deterrent to behavior that may threaten system integrity, they must be at a sufficiently high level to actually deter that behavior. Thus, Eastern Shore proposes to increase its penalties to reflect the higher prices in the current market for natural gas. Eastern Shore notes that both of its upstream interconnecting pipelines have been granted Commission authorization to increase penalty levels.[2]

6. Notice of Eastern Shore's filing was issued on December 15, 2005, with interventions and protests due as provided in section 154.210 of the Commission's regulations, 18 C.F.R. § 154.210 (2005). Pursuant to Rule 214, 18 C.F.R § 385.214 (2005), all timely motions to intervene and any motions to intervene out-of-time filed before the issuance date of this order are granted. Granting late intervention at this stage of the proceeding will not disrupt the proceeding or place additional burdens on existing parties. Easton Utilities Commission (Easton) protested the filing. Pivotal Utility Holdings, Inc., d/b/a Elkton Gas (Elkton) filed comments stating that while it does not protest Eastern Shore's filing, it does support the comments filed by Easton in its protest. The protest is discussed below.

7. Easton protests Eastern Shore's attempt to eliminate the two tiered structure of the current unauthorized overrun penalty and to replace it with a single tier. Easton states that Eastern Shore has not provided any justification for this change in the penalty structure and notes that Transcontinental Gas Pipeline Corporation (Transco), which also

[2] *Transcontinental Gas Pipe Line Corp.*,, 113 FERC ¶ 61,224 (2005); *Columbia Gas Transmission Corp.*, 113 FERC ¶ 61,191 (2005).

has a tiered penalty structure for unauthorized overruns, retained that tiered structure when it increased its penalties. Easton argues that Eastern Shore's proposal represents not only and an increase in penalties, but also a change in the penalty structure itself, which goes beyond the types of penalty level increases the Commission has approved for other pipelines.

8. The Commission denies Easton's protest, and accepts Eastern Shore's proposal. The recent increases in natural gas prices have decreased the deterrent value of existing penalty levels on some pipeline systems and the Commission has approved increased penalty levels for that reason. That same reasoning holds true in Eastern Shore's case. Although Easton argues that Transco instituted a similar increase but did not eliminate the tiered structure of its penalties, this has little bearing on what Eastern Shore did or did not propose. Eastern Shore is within its right to eliminate the two tiered structure in favor of a single penalty structure. Under the statutory scheme set forth in the Natural Gas Act, the pipeline has the initiative through a section 4 filing to propose rates, terms, and conditions for the service it provides.[3] If the pipeline shows that its proposal is just and reasonable, the Commission must accept it, regardless of whether other rates, terms, or conditions might also be just and reasonable.[4] Therefore, the fact the Commission has accepted as just and reasonable Unauthorized Overrun Penalties that do consist of a two-tiered structure does not show that Eastern Shore's elimination of a tiered structure is not just and reasonable. Furthermore, the Commission has recently approved another proposal to eliminate a tiered penalty structure in favor of a level penalty structure in *Guardian Pipeline, LLC,* 113 FERC ¶ 61,086 (2005).

9. Penalties are designed to deter shipper behavior that could threaten the pipeline's operational integrity. To that extent, it matters little if the overrun is 50 Dth or 1000 Dth. In either case, if operational integrity is threatened, it has an impact on other shippers on the system through no fault of their own. Eastern Shore waives Unauthorized Overrun Penalties if its operational integrity or ability to render reliable service is not threatened, pursuant to section 22(c) of its tariff. Furthermore, section 22(b) of Eastern Shore's tariff permits shippers to exceed their Authorized Daily Quantity by an Overrun Tolerance Quantity of three percent (October – April) or five percent (May – September) of their Authorized Daily Quantity before any penalty applies. Finally, penalties are not a profit center for pipelines, and Eastern Shore is required by section 36 of its tariff to refund

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[3] *See United Pipeline Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956).

[4] *See Western Resources, Inc. v. FERC*, 9 F.3d 1568, 1578 (D.C. Cir. 1993).

penalty revenues net of costs. Therefore, there is no incentive for Eastern Shore to assess penalties other than to protect the operational integrity of its system. The Commission accepts Eastern Shore's proposal effective December 21, 2005.

By direction of the Commission.

Magalie R. Salas,
Secretary.

cc: All Parties

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