UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Nora Mead Brownell, and Suedeen G. Kelly.

Bay Gas Storage Company, Ltd. Docket No. PR04-9-003

ORDER DENYING REHEARING

(Issued April 14, 2006)

1. On December 8, 2005, Bay Gas Storage Company, Ltd. (Bay Gas) requested clarification or, in the alternative, rehearing of the Commission's order dated November 8, 2005 (November 8, 2005 Order).[1] Bay Gas contends that order erroneously reversed the Commission's previous order[2] accepting its proposal to roll in the Whistler spur facilities. We will deny rehearing, as discussed below.

I. Background

2. Bay Gas began operations of its original facilities in 1994.[3] The original facilities include a 22-mile 20-inch diameter pipeline that runs due south from Bay Gas's storage facilities at McIntosh, Alabama, to its Salco Station, located north of Mobile, at Axis, Alabama. They interconnect with Gulf South Pipeline Company, L.P. (Gulf South) and Mobile Gas Service Corporation (Mobile Gas) at Salco Station. In 2002, Bay Gas constructed the Whistler spur facilities, which generally run southwest from Salco Station 17.5 miles to Whistler Junction, where there is another interconnection with Gulf South and Mobile Gas.

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[1] *Bay Gas Storage Co., Ltd.*, 113 FERC ¶ 61,140 (2005) (November 8, 2005 Order).

[2] *Bay Gas Storage Co., Ltd.*, 111 FERC ¶ 61,345 (2005) (June 2, 2005 Order).

[3] *Bay Gas Storage Co., Ltd.*, 66 FERC ¶ 61,354 (1994) (approving market-based rates for original facilities).

3. Before this rate case, Bay Gas had separate transportation rates for service on each set of facilities. On March 9, 2004, as supplemented on April 9, 2004, Bay Gas sought approval of rolled-in rates for firm and interruptible transportation services on the combined facilities, both the 22-mile original facilities and the 17.5-mile Whistler spur facilities, under the Natural Gas Policy Act of 1978 (NGPA) section 311.[4]

4. Southern Company Services, Inc. (Southern), on behalf of its subsidiary Alabama Power Company (Alabama Power), requested the Commission to clarify that, if the rates to be paid by shippers on the older pipeline are to include the costs of the formerly incrementally-priced Whistler spur facilities, then those shippers—including Southern/Alabama Power—should be given flexible point rights throughout the system. Absent this clarification, Southern opposes Bay Gas's roll-in proposal.

5. Following a staff panel proceeding to permit parties an opportunity to present oral views, data, and arguments, the Commission has issued two orders addressing the merits of Bay Gas's roll-in proposal, the first on June 2, 2005[5] and the second on November 8, 2005.[6] In both those orders, the Commission held that the rolled-in rate issue in this case should be decided based on the current policy concerning rolled-in versus incremental rates on interstate pipelines, as set forth in our 1999 Pricing Policy Statement.[7] Under that policy statement, the Commission changed the focus of its policy so that the primary goal is to achieve efficient pricing signals to expansion shippers and existing pipeline customers, while remaining within the pipeline's revenue requirement. When an expansion to an interstate pipeline project is certificated, the Commission requires that existing shippers not be required to subsidize the expansion shippers. This generally means that expansions will be priced incrementally so that expansion shippers will have to pay the full costs of the project, without subsidy from the existing customers through rolled-in pricing. This will help ensure that the market finds the project viable, because either the expansion shippers or the pipeline must be willing to fully fund the project.

6. Subsequently, however, when a pre-expansion shipper's existing contract expires it could be required to pay a higher rate than its existing vintage rate. This would occur where the pipeline is fully subscribed and there is a competing bid higher than the pre-

[4] *Bay Gas Storage Co., Ltd.*, 97 FERC ¶ 61,020 (2001) (approving rates for Whistler spur facilities); 99 FERC ¶ 61,263 (2002) (approving rates for non-Whistler spur facilities).

[5] June 2, 2005 Order, 111 FERC ¶ 61,345 (2005).

[6] November 8, 2005 Order, 113 FERC ¶ 61,140 (2005).

[7] *Policy Statement concerning Certification of New Interstate Natural Gas Pipeline Facilities*, 88 FERC ¶ 61,227 (1999), 90 FERC ¶ 61,128 (2000), *order on reh'g*, 92 FERC ¶ 61,094 (2000) (1999 Pricing Policy Statement).

expansion rate. In addition, the Commission has suggested rolled-in rates could be approved before the expiration of current contracts if (1) the facilities are needed to improve service for existing customers, (2) the increase in rates is related to improvements in service, and (3) raising existing customers' rates does not constitute a subsidy of an expansion by existing customers.

7. Consistent with that policy, the June 2 and November 8 Orders both considered whether Bay Gas's rolled-in rate proposal would require the shippers on the original system to subsidize the Whistler spur expansion. The June 2 Order found that there would be no subsidy, because rolling in the costs of the Whistler spur facilities would produce a lower maximum rate for service on Bay Gas's original facilities than if service on the Whistler spur facilities continued to be priced on an incremental basis. However, the November 8 Order found that the rate calculations upon which the holding in the June 2 Order had been based were in error, and in fact rolling in the costs of the Whistler spur facilities would produce a higher maximum rate for service on Bay Gas's original facilities. The November 8 Order concluded that the Whistler spur facilities did not provide sufficient benefits to existing customers to justify the rate subsidy caused by a roll-in.

8. The difference in result between the June 2 and November 8 Orders turned on the billing determinants used to calculate the maximum rates for service on the original facilities with and without roll-in of the Whistler Spur facilities. The June 2 Order used total billing determinants of 415,600 MMBtu to design Bay Gas's rates, based on Bay Gas's October 14, 2004 responses to data requests by the Staff Panel. Those responses used incremental billing determinants for the original facilities of 259,900 MMBtu per day and incremental billing determinants for the Whistler spur facilities of 155,700 MMBtu per day. The Whistler spur billing determinants were calculated based on 90 percent of the design capacity of the Whistler spur facilities of 173,000 MMBtu per day.

9. On rehearing, however, Bay Gas pointed out that the resulting 415,600 MMBtu in billing determinants was greatly in excess of its system capacity available for interstate service. Bay Gas stated that, while its current system capacity is 438,000 MMBtu per day, only 261,433 MMBtu per day is available for the transportation-only NGPA section 311 service that is at issue here. Bay Gas contended that the Commission should have designed its rates using the billing determinants of 304,400 MMBtu per day which Bay Gas proposed in its March 9, 2004 rate filing. That 304,400 level was based on firm transportation-only contract demand of 285,200 MMBtu per day and an imputed interruptible contract amount of 19,200 MMBtu per day. Bay Gas stated that its contract demand for firm service exceeds its available design capacity due to the location of the specific firm receipt and delivery points.

10. In the November 8 Order, the Commission agreed with Bay Gas that its rates should be designed using the billing determinants proposed in Bay Gas's original March 9, 2004 petition and not its October 14, 2004 data response. The Commission pointed out that, although the Whistler spur facilities extend the length of the system, they do not increase the total capacity of the existing system. The after-discount adjustment billing determinants based on Bay Gas's March 9, 2004 proposal were 1,252,800 MMBtu, as compared to the 2,587,200 MMBtu after-discount adjustment billing determinants used in the June 2 Order. Based on these lower billing determinants, the November 8 Order determined that rolling in the costs of the Whistler spur facilities would result in maximum rates of $2.7120 per MMBtu for firm transportation-only service, and $0.0892 per MMBtu for interruptible transportation-only service. These re-calculated rolled-in rates were higher than the maximum rates for service on the original facilities if the rolled-in rate proposal is rejected. As discussed in the June 2 Order in P 25, "if Bay Gas's rolled-in rate proposal were rejected, the maximum rates for service on the original facilities would be $1.5991 per MMBtu for firm transportation-only service, and $0.0526 per MMBtu for interruptible transportation-only service."

11. Consequently, the Commission reversed its decision to approve a rolled-in approach for Bay Gas's original system and Whistler spur facilities. The Commission stated that Bay Gas had not shown sufficient benefits to shippers on the original facilites to justify the $1.1130 per MMBtu increase in the maximum rate for firm transportation-only service that roll-in would cause. The Commission also found that Bay Gas's assertion that no existing original facilities firm shippers' rate would be impacted negatively by the use of rolled-in rates because they presently hold heavily discounted rates for the terms of their contracts to be misplaced. Commission precedent requires that the pipeline's approved maximum rates be fair and equitable. Because the rolled-in rates would exceed the maximum rates applicable to service on the original facilities, we found the rolled-in rates not to be fair and equitable.

II. Request for Rehearing

12. Bay Gas states that it assumes the lawful NGPA section 311(a)(2) rates are those calculated in the June 2, 2005 Order as incremental rates for the original facilities (*i.e.*, $1.5990 for FT, $0.0526 for IT) and for the Whistler spur facilities (*i.e.*, $1.2033 for FT, $0.0396 for IT) from March 9, 2004, to March 8, 2007,[8] though it states this is not clear from the June 2, 2005 Order.

13. Bay Gas contends, however, that the Commission's determination that rolling in the Whistler spur facilities would cause an increase in the maximum rates for service on the original facilities was based on an incorrect comparison. Bay Gas contends that the

[8] *Citing* June 2, 2005 Order, 111 FERC at 62,531-32.

rate impact of a roll-in must be determined independently of a discount adjustment. Bay Gas maintains that the appropriate methodology is to compare rolled-in maximum rates, independent of the discount adjustment, with non-rolled-in maximum rates for original facilities service. Thus, Bay Gas asserts that the Commission should determine the maximum rolled-in rate based on the "approved cost of service, without a discount adjustment, of $4,857,581," and "transportation-only cost of service billing units of 3,652,800" in Schedule I-1 of its March 9, 2004 filing (Schedule I-1). This calculation produces a rolled-in FT rate of $1.3298 per MMBtu per month and an IT rate of $0.0437 per MMBtu per day. Hence, Bay Gas concludes, rolled-in rates without a discount adjustment are lower for the original facilities shippers than their non-rolled-in rates. Therefore, it asserts, any rate increase is due not to roll-in, but to the discount adjustment, according to Bay Gas.

14. Bay Gas also reiterates that there is no subsidy by original shippers because all original facilities shippers receive service under discounted rate current contracts that will not change after roll-in. Moreover, Bay Gas asserts that there are sufficient benefits to justify a roll-in. It states that the cost of service the Commission has approved in this proceeding includes annual regulatory commission expenses of approximately $30,000. It states that rejection of its roll-in proposal will require it to continue to file separate triennial rate petitions for each part of its system, whereas with roll-in it would only need to file a single triennial rate petition for its entire system. Bay Gas accordingly asserts that approval of its roll-in proposal would halve its regulatory expenses.

15. Bay Gas also asserts that the Whistler spur facilities provide a number of other benefits to all shippers. These include: increased access to additional gas supplies, increased access to storage facilities on other systems, and increased reliability.

III. Discussion

16. The Commission denies Bay Gas's request for rehearing. The Commission reaffirms its prior holdings that rolling in the costs of the Whistler spur facilities would increase the maximum rate applicable to service on the original facilities, and that the Whistler spur facilities do not provide sufficient benefits to justify roll-in.

17. First, rolling in the costs of the Whistler spur facilities would increase the maximum rate applicable to the original facilities, regardless of whether the rate impact comparison is made with or without a discount adjustment. Bay Gas's assertion that, if the discount adjustment is excluded from the analysis, a roll-in would decrease the maximum rate for service on the original facilities is based on an incorrect comparison. Bay Gas compares a rolled-in rate of $1.3298 per MMBtu determined without a discount adjustment, to a non-rolled-in rate for the original facilities of $1.5990 per MMBtu determined with a discount adjustment. There is no justification for such an apples-to-oranges comparison.

18. Bay Gas has proposed to design its rates in this proceeding using billing determinants that are adjusted to reflect discounts. Therefore, the rates approved in this proceeding will reflect a discount adjustment whether or not the Commission approves the rolled-in rate proposal. It follows that, in determining whether the rolled-in rate proposal would lead to an increase in the maximum rates for service on the original facilities, it is appropriate to include a discount adjustment in the calculation of those rates both with and without a roll-in. However, if the rate impact determination were to be made excluding a discount adjustment, then consistency would require excluding the discount adjustment from the calculation of both the rolled-in rates and the non-rolled-in rates. Excluding the discount adjustment in this manner would result in a rolled-in rate of $1.3298 for service on the original facilities and a non-rolled-in rate for service on these facilities of $0.8366.[9] Thus, even excluding the discount adjustment from the analysis, there would be a rate increase of $0.4932 per MMBtu. As a result, under either scenario, whether the discount adjustment is included or excluded from the comparison of maximum rates for service on the original facilities with and without a roll-in, a rate increase results from a roll-in that would require shippers on the original facilities potentially to subsidize the Whistler spur expansion shippers.

19. Bay Gas contends that roll-in does not change either the current contract discounted rates or services for any shipper on Bay Gas's original facilities. Thus, the Commission's no-subsidy policy in the 1999 Pricing Policy Statement is met on these facts, according to Bay Gas.[10] Bay Gas asserts that the 1999 Pricing Policy Statement and *Transcontinental Gas Pipe Line Corporation*, 106 FERC ¶ 61,299, at P 57 (2004) (*Transco*), state that when pre-expansion shippers' current contract rates expire they could be required to pay a higher rate than their current rate. Bay Gas accordingly asserts that, given the discounted rates that the existing shippers are receiving under their current contracts, its rolled-in rate proposal only requires that the existing shippers pay a rolled-in rate after the expiration of the current contracts, consistent with the policy set forth in *Transco* and the Commission's 1999 Pricing Policy Statement.

20. The Commission rejects this contention. The 1999 Pricing Policy Statement clarifies that a shipper with an expiring contract

> could be required to match a bid up to a maximum rate higher than the historic maximum rate applicable to its capacity in certain limited circumstances…. Application of this approach could lead to rates for shippers … that are higher than their existing vintaged rate. But this will

[9] The non-rolled-in rate for the original facilities (excluding discount adjustment) of $0.8366 is calculated by dividing the total system cost of service of the original facilities ($2,609,342) by the total billing units for the original facilities (3,118,800).

[10] *See* 1999 Pricing Policy Statement, 90 FERC at 61,392.

> occur only if the preconditions are met—the pipeline is full and there is a competing bid higher than the pre-expansion rate so that a higher rate is needed to allocate available capacity—and the Commission has accepted the pipeline's mechanism for determining rates as just and reasonable.[[11]]

However, under Bay Gas's rolled-in rate proposal, it could require its existing shippers to pay a rolled-in rate upon expiration of their current contracts, regardless of whether the preconditions in the 1999 Pricing Policy Statement are met. Moreover, Bay Gas has proposed no tariff mechanism "for reallocating costs between the historic and incremental rates so all rates remain within the pipeline's cost-of-service,"[12] as required by the policy statement.

21. We also find that Bay Gas has not shown that the roll-in of costs proposed in Bay Gas's March 9, 2004 filing is beneficial to shippers on the system. With respect to Bay Gas's contention that roll-in of the Whistler spur facilities will reduce regulatory commission expense by approximately $30,000 annually, we find that this minor savings is a negligible benefit to system shippers and does not justify roll-in. Further, we note that in our June 2, 2005 Order in this proceeding,[13] we directed Bay Gas to file on or before March 9, 2007, a new application for rate approval to justify its existing rates or establish a new maximum rate for both parts of its system. Thus, contrary to Bay Gas's contention, it will not have to make two separate petitions, but rather one petition covering both systems. There appears to be no reason why Bay Gas should incur more expenses filing a petition using an incremental rate design as opposed to one using a rolled-in rate design.

22. Bay Gas contends that existing shippers will benefit from the Whistler spur facilities because those facilities will give the existing shippers access to additional gas supplies and third party storage services through interconnections between the Whistler spur facilities and Gulf South and Mobile Gas. As the Commission stated in the November 8, 2005 Order, access to additional gas supplies and flexibility "cannot be considered a benefit for those shippers in light of the fact that Bay Gas has stated it will not permit those shippers to use the Whistler spur facilities under their existing contracts."[14] This case is similar to *Tennessee Gas Pipeline Company*, 80 FERC ¶ 61,070, at 61,225-26 (1997), in which the Commission found the alleged benefit of additional supply effectively was not available to pre-expansion shippers through capacity release even on a short term firm basis, because expansion shippers used the

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[11] *Id.* at 61,394-95.

[12] *Id.* at 61,394 (footnote omitted).

[13] June 2, 2005 Order, 111 FERC ¶ 61,345, at ordering para. (C).

[14] November 8, 2005 Order, 113 FERC ¶ 61,140 at P 23.

new capacity at such a high load factor. Bay Gas's alleged benefit here is even less available to existing shippers, since Bay Gas will not permit its existing shippers to use secondary points on the Whistler spur facilities. Nor does Bay Gas's statement of operating conditions allow for capacity release.

23. For the same reasons, Bay Gas reliance on *Northern Border Pipeline Company*, 76 FERC ¶ 61,141 (1996), *reh'g denied*, 80 FERC ¶ 61,152 (1997), is misplaced. In that case, the Commission pointed out that the pre-expansion shippers would be able to use the expansion through use of secondary points and capacity release.[15] As already pointed out, under Bay Gas's proposed roll-in existing shippers may not obtain released capacity over the incremental facilities, nor may existing shippers make use of secondary delivery points on the Whistler spur facilities.[16] Moreover, in *Northern Border* there was evidence that the expansion would reduce bottlenecks that had resulted in curtailment of the pre-expansion shippers' service.[17] By contrast, Bay Gas does not contest our finding that "Bay Gas has not shown that the shippers on the original system have been subject to curtailment or interruption of service in the past," nor does Bay Gas clarify "how the existence of the Whistler spur facilities would help the shippers on the original system in case of [such] an interruption of service."[18]

24. Bay Gas's reliance on *Eastern Shore Natural Gas Company*, 87 FERC ¶ 61,168, at 61,664 (1999), is also misplaced. In that case, the Commission found that the revenues from the expansion shippers would exceed the cost of the expansion. Therefore, no issue of an inappropriate subsidy was presented. Finally, with regard to Bay Gas's citation of *El Paso Natural Gas Company*, 113 FERC ¶ 61,183, at P 29-31 92005), "all" shippers (including the existing shippers) do not benefit from enhanced reliability, because original facilities shippers cannot use the Whistler spur facilities under their current contracts.

25. Accordingly, we continue to find that incremental rate treatment of the Whistler spur (expansion) facilities is appropriate, and therefore deny Bay Gas's request for rehearing.

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[15] *Northern Border*, 76 FERC at 61,774-75; *Northern Border*, 80 FERC at 61,631-32.

[16] *Northern Border*, 76 FERC at 61,775.

[17] *Northern Border*, 80 FERC at 61,628.

[18] November 8, 2005 Order, 113 FERC ¶ 61,140 at P 23.

<u>The Commission orders:</u>

Bay Gas's request for rehearing is hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.