

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Kern River Gas Transmission Company

Docket No. RP05-254-000

ORDER ON TECHNICAL CONFERENCE

(Issued May 24, 2006)

1. On July 26, 2005, the Commission accepted a report filed by Kern River Gas Transmission Company (Kern River) supporting its gas compressor fuel and lost and unaccounted-for gas factors for 2004, subject to the outcome of a technical conference.¹ On September 21, 2005, the Commission held a technical conference to further explore Kern River's compressor fuel allocation methodology, which was followed by comments from the parties. The instant order addresses proposals and comments originating from the technical conference proceeding, and, as discussed below, accepts Kern River's current methodology for allocating gas compressor fuel between rolled-in and incremental shippers as shown in its March 31, 2005 report.

Background

2. In its certificate order in Docket Nos. CP01-31-000, *et al.*,² the Commission determined that Kern River should be allowed to roll-in the cost of its 2002 expansion project because the result would be a lower rate for existing pre-2002 expansion shippers. However, when Kern River applied for a certificate for its subsequent 2003 expansion project in Docket No. CP01-422-000, it proposed, and the Commission approved, incremental rates for the new 2003 expansion project.³ Consistent with the approval of incremental rates for the 2003 expansion project, the Commission required that, in

¹ *Kern River Gas Transmission Co.*, 112 FERC ¶ 61,132 (2005).

² *Kern River Gas Transmission Co.*, 96 FERC ¶ 61,137, at 61,581-82 (2001) (2002 Expansion Certificate Order).

³ *Kern River Gas Transmission Co.*, 98 FERC ¶ 61,205 (2003 Expansion Preliminary Determination Order), *reh'g*, 100 FERC ¶ 61,056 (2002) (2003 Expansion Certificate Order).

designing its fuel reimbursement mechanism, Kern River must maintain the principle that the existing rolled-in shippers not be required to subsidize any fuel costs attributable to the 2003 expansion project.⁴ Accordingly, Kern River's tariff includes a method for allocating fuel between the rolled-in shippers⁵ and the 2003 expansion shippers, which the Commission approved in April 2003.⁶

3. Under this method, actual fuel used at a given compressor station during any month is allocated between rolled-in and expansion shippers. Kern River's gas compressor fuel allocation methodology is derived from average design day studies under pre- and post-2003 expansion project scenarios for a typical August and January, assuming the maximum available operational capacity. These months are used because they purportedly have the lowest and highest available capacity, respectively, due to the typical temperatures during these months. The average fuel factors derived from the pre-2003-expansion design day models were compared to the average fuel factors from the post-2003-expansion design day models to develop weighting factors for each compressor. In turn, the weighting factors were used to allocate compressor fuel between the two shipper groups; namely, the rolled-in and expansion shippers. The design day studies made certain assumptions with respect to the location of gas receipts and deliveries on the system. Further, the design day models assume that both the rolled-in shippers and the expansion shippers utilize 100 percent of the designed operational capacity.

4. The quantities scheduled by the expansion shippers are adjusted by a weighting factor specific to each compressor station to reflect that the incremental portion of the system requires relatively more compression per unit of capacity than the rolled-in system and, therefore, the incremental shippers must bear a proportionately larger share of the total fuel consumed.⁷ The weighing factors were intended to ensure that the rolled-in shippers do not subsidize the fuel use of the expansion shippers regardless of the nominated receipts and deliveries.

⁴ 2003 Expansion Preliminary Determination Order, 98 FERC at 61,724.

⁵ "Rolled-in shippers" include those taking service on Kern River's original and 2002-expansion facilities. "Expansion shippers" include those taking service post-construction of the 2003 expansion.

⁶ *Kern River Gas Transmission Co.* 103 FERC ¶ 61,102 (2003).

⁷ This finding was based on design day studies performed by Kern River in the 2002 certificate proceeding in Docket No. CP01-422-000.

5. The expansion shippers' weighting factor for each compressor station is derived by dividing the average design day incremental fuel factor by the average design day rolled-in fuel factor. For example, the Muddy Creek compressor station weighting factor is 1.56 (0.81/0.52). If for example, the Muddy Creek compressor station has scheduled monthly nominations of 20 Bcf under rolled-in rate agreements and 30 Bcf under incremental rate agreements, and 0.35 Bcf of fuel is used, the following allocation would be made by Kern River: The 30 Bcf under incremental agreements would be multiplied by the weighing factor of 1.56, which would result in an adjusted scheduled quantity of 46.8 Bcf. The 46.8 Bcf would be added to the 20 Bcf scheduled by rolled-in shippers to compute an adjusted total scheduled quantity of 66.8 Bcf for that particular month. The expansion shippers would be responsible for 70 percent of the adjusted total scheduled quantity (46.8/66.8) of fuel, while the rolled-in shippers would be responsible for 30 percent (20/66.8). These percentages would be applied to the 0.35 Bcf monthly fuel use at Muddy Creek compressor to calculate the responsibility of each group. In this example, 0.245 Bcf would be attributable to expansion shippers (.70 x 0.35) and 0.105 Bcf would be attributable to rolled-in shippers (.30 x 0.35).

6. Section 12 of the General Terms and Conditions (GT&C) of Kern River's tariff permits it to post revised fuel retention factors each month. Section 12.10 requires Kern River to file an annual report with the Commission by March 31 of each year, supporting the fuel and lost and unaccounted for gas factors used during the previous calendar year. On March 31, 2005, Kern River filed such a report, wherein Kern River reported, *inter alia*, fuel allocation and collection amounts from the rolled-in and expansion shippers. Calpine Energy Services, L.P. (Calpine) protested Kern River's report, stating that it reflects a continuing over-collection of actual fuel costs by Kern River, and that Kern River is improperly charging separate and higher incremental fuel rates to expansion shippers as compared to rolled-in rate shippers.

7. On July 26, 2005, the Commission accepted Kern River's compressor fuel and lost and unaccounted-for gas factor report as satisfying the requirement of section 12.10 of the GT&C for the calendar year 2004, subject to a technical conference. The technical conference was held on September 21, 2005, to address the allocation of compressor fuel between rolled-in and expansion shippers, particularly regarding the compressor weighting factors in GT&C section 12.6 of Kern River's tariff, which was an issue raised by Calpine.

Comments on Technical Conference

8. On October 12, 2005, Calpine filed initial comments on the technical conference, reiterating its previous comments that Kern River's current compressor fuel allocation methodology yields unjust and unreasonable results. Calpine argues that, after examining actual system utilization figures and pre- and post-2003-expansion flow patterns of the

rolled-in shippers, and after correcting an inherent mathematical flaw in Kern River's weighting approach, it has concluded that there is a significant subsidy provided to the rolled-in shippers by the expansion shippers, with resulting inaccurate market price signals. Accordingly, Calpine argues that Kern River's methodology is inappropriate and should be changed. Additionally, Calpine submitted calculations that purport to show that the incremental shippers have been over-charged \$17 million from the commencement of the expansion service date to August 2005 (assuming a \$9 MCF average price of natural gas). Calpine proposes two alternate methods which it believes would produce a more reasonable allocation of compressor gas fuel costs. The first allocation method would fix the rolled-in shippers' fuel percentages at each compressor at the levels experienced immediately prior to the 2003 expansion project, with the incremental shippers being responsible only for the compressor fuel consumed above historical levels. A second, alternative method would require Kern River to utilize a pre-2003-expansion model to determine the fuel to be allocated to the rolled-in shippers for the past month at each compressor, with the incremental shippers being responsible for the difference.

9. On October 26, 2005, Kern River, BP Energy Company (BP Energy), and the Rolled-In Customer Group (Rolled-In Customers)⁸ filed reply comments opposing Calpine's proposal. Kern River states that a just and reasonable fuel allocation methodology is one that is equitable among the shipper groups by ensuring that there is no subsidization of fuel costs attributable to the 2003 expansion by the rolled-in shippers. Kern River notes that, due to the 2003 expansion, system capacity increased by 105 percent but the fuel requirement increased by 229 percent. Therefore, Kern River argues the present methodology prevents the rolled-in shippers from subsidizing the incremental shippers because of the weighted factors, and serves to keep Kern River whole for the actual fuel consumed during system operations. Kern River concludes that Calpine has failed to prove that the present methodology is unjust and unreasonable.

10. BP Energy comments that Kern River is currently engaged in a general rate case initiated under section 4 of the NGA.⁹ The final decision in that proceeding may significantly affect the way capacity is utilized by the 2003 expansion shippers. Therefore, BP Energy states that changing Kern River's fuel allocation methodology before a final order is issued may be counterproductive. BP Energy argues that Calpine's proposal would allocate 100 percent of the benefit from changes in the way the system

⁸ The Rolled-In Customers include: Area Energy, LLC; Anadarko E & P Company LP; Anadarko Petroleum Corporation; Chevron U.S.A., Inc.; Coral Energy Resources, L.P.; Occidental Energy Marketing, Inc.; and Southwest Gas Corporation.

⁹ Docket No. RP04-274.

now operates solely to the 2003 expansion shippers and potentially result in the subsidization of the expansion shippers by the rolled-in shippers. Finally, BP Energy states that Calpine's proposal to adjust the fuel costs on a monthly basis to reflect the prior month's actual activity would add additional complexity to the system and also reflects an element of retroactive ratemaking.

11. The Rolled-In Customers contend that Calpine has failed to meet its burden under NGA section 5 to demonstrate that the existing allocation methodology is unjust and unreasonable and made no showing that its proposals would ensure that rolled-in shippers would not subsidize any of the fuel costs attributed to the 2003 system expansion. Finally, the Rolled-In Customers state that Calpine did not describe how its proposed tracker methodology would operate and if there would be prospective true-ups or retroactive adjustments.

12. On November 2, 2005, Calpine filed reply comments. Calpine first addressed Kern River's, BP Energy's, and the Rolled-In Customers' (collectively, the Commentors) belief that Calpine's proposals would create an improper subsidy from Kern River's rolled-in customers to its expansion shippers. Calpine states that it does not want to create a fuel cost subsidy in favor of any Kern River shipper group but rather proposes to eliminate an ongoing fuel subsidy from Kern River's expansion shippers to its rolled-in shippers. Calpine also claims that such subsidies run counter to the Commission's policy goal of sending accurate pricing signals regarding the pipeline's 2003 expansion capacity. Accordingly, Calpine asserts that Kern River's existing fuel allocation methodology is unjust and unreasonable and therefore must be replaced.

13. Calpine states that the Commission need not wait for a decision in Kern River's ongoing section 4 general rate proceeding to act here, because allowing Kern River to continue to over-collect fuel from expansion shippers while Kern River's section 4 rate case remains pending would result in unjust and unreasonable fuel rates continuing for an indefinite period into the future. Calpine argues that the level of utilization that Kern River has chosen to assume in its fuel allocation methodology diverges so significantly from actual capacity utilization on its system that it produces overstated fuel charges for the expansion shippers. Calpine then restates that the rolled-in shippers' flow patterns were essentially unchanged after the 2003 expansion, and that just as expansion-related fuel costs should be allocated exclusively to the incremental shippers, so too should any fuel-related benefits created by the expansion. Calpine contends that, in light of the actual experience gained with regard to Kern River's fuel methodology, sufficiently changed circumstances exist so that the Commission's earlier 2001 Certificate Order poses no bar to modifying that methodology.

Discussion

14. In this proceeding, Kern River has reported its allocation of 2004 fuel usage between its rolled-in and expansion shippers. It is undisputed that Kern River allocated these costs consistent with the method set forth in its tariff. However, Calpine has challenged the reasonableness of that allocation method. Since Kern River did not propose to change its current allocation method, Calpine bears the burden under section 5 to show that the existing method of allocation is unjust and unreasonable, and to support a just and reasonable replacement methodology.¹⁰ As discussed below, we find that Calpine has not met its burden under section 5 of the NGA.

15. The Commission finds that the evidence Calpine presented is insufficient to justify a finding that the expansion shippers are subsidizing the rolled-in shippers on the Kern River system. The Commission required Kern River to establish and maintain separate fuel charges under its fuel tracking mechanism as part of its approval of incremental rates for the 2003 expansion. Thus, Kern River had to develop a method for allocating system fuel usage that both (1) keeps Kern River whole for actual fuel consumption and (2) results in no subsidization of expansion shippers by the rolled-in shippers. We find that Kern River's current fuel allocation methodology reasonably accomplishes both requirements. We note that Kern River's design day studies indicate that its 2003 expansion increased its fuel requirements by 229 percent, while increasing system transportation capacity by only 105 percent. The incremental shippers, therefore, must bear a proportionately larger share of the total fuel consumed at each compressor station.

16. Developing a fuel charge that accurately reflects each shipper's usage is a daunting task for any pipeline. This is because fuel use at any compressor is not linear (*i.e.*, does not increase proportionately with throughput), and is affected by a number of external factors, such as suction and discharge pressures, and ambient air temperatures. Absolute precision from an allocation methodology, however, is not required. As the

¹⁰ In their reply comments, the Rolled-In Customers pointed out that Calpine failed to include in its post-technical conference comments a separate section titled "Statement of Issues" in violation of section 385.203(a)(7) of the Commission's procedural regulations as revised by Order No. 663, *Revision of Rules of Practice and Procedure Regarding Issue Identification*, 70 Fed. Reg. 55,723 (Sept. 23, 2005), FERC Stats. & Regs. ¶ 31,193 (2005). However, subsequently in Order No. 663-A, 71 Fed. Reg. 14,640 (Mar. 23, 2006), FERC Stats. & Regs. ¶ 31,193 (2006), the Commission eliminated the requirement in section 385.203(a)(7) that all pleadings contain a statement of issues, and instead modified section 385.713 to establish such a requirement solely for requests for rehearing. Accordingly, the Commission accepts Calpine's comments.

courts have stated, “[a]llocation of costs is not a matter for the slide-rule. It involves judgment on a myriad of facts.”¹¹ Accordingly, there may be several allocation methodologies that are just and reasonable.

17. The Commission further finds that Kern River’s current fuel allocation methodology, which is based on a comparison of design day studies before and after the 2003 expansion, has not been shown to be unreasonable. It reflects the 2003 expansion facilities, which were designed and constructed to provide service for additional gas volumes on the system. As stated above, Kern River’s present Commission-approved fuel allocation methodology compares the pre- and post-2003-expansion compressor fuel factors to determine the weighted factor for each compressor. The compressor fuel costs are then allocated among the rolled-in and expansion shippers using the weighting factors in the tariff to assign costs to expansion shippers.¹² This is consistent with Kern River’s obligations to all of its shippers.¹³ Further, the Kern River’s proposed charge is also both predictable and not burdensome on the pipeline to administer.

18. Calpine’s argument that the incremental shippers are being allocated excessive fuel costs is predicated on the fact that, since Kern River’s methodology is based on design day studies, it effectively assumes that both the rolled-in and expansion shippers make full use of the contract demand amounts, but currently the rolled-in shippers are taking less than their contract demand amounts. We recognize that this fact pattern may result in a higher unit charge for incremental rate shippers, than if both sets of customers made the same use of their capacity. However, this fact pattern is subject to change on a day-to-day and month-to-month basis. Since the allocation of fuel costs between the rolled-in and expansion shippers can never reflect more than a rough approximation of

¹¹ *Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581, 589 (1945).

¹² Section 12.6 of Kern River’s GT&C, states:

Total fuel used at each compressor each month will be allocated between rolled-in and incremental rate groups on a *pro rata* basis using actual receipt quantities at each compressor, with the receipt quantities attributable to the incremental rate group adjusted by the following weighting factors: Muddy Creek – 1.56%; Painter – 1.00%; Anschutz – 1.00%; Coyote Creek – 2.00%; Salt Lake – 2.00%; Elberta – 1.89%; Fillmore 2.13%; Veyo – 2.00%; Dry Lake – 2.00%; Goodsprings – 2.12%.

¹³ See 2002 Expansion Certificate Order, 96 FERC at 61,582; 2003 Expansion Preliminary Determination Order, 98 FERC at 61,724.

the relative fuel use caused by each customer class, the Commission finds that the added complexity of trying to take into account such changing usage patterns outweighs the benefit of whatever added accuracy could be achieved.

19. Calpine's alternative fuel recovery proposal, like Kern River's, uses both estimates and allocations. It assumes that system utilization and flow patterns for the rolled-in shippers have not changed and will not change from the pre- to post-2003-expansion periods, and that these are the two most important factors in determining fuel usage. Based on these assumptions, Calpine argues that the proper allocation of fuel should be based on pre-2003-expansion, historical usage percentages for the rolled-in shippers, and the incremental shippers should be assigned the difference between total fuel costs and the rolled-in shippers' fuel costs. While this approach could produce reasonable results, it suffers from the same infirmity that Calpine has lodged against Kern River; namely, those results would only continue to be accurate to the extent that the existing shippers' usage and flow patterns remain constant. Therefore, we find that Calpine has failed to demonstrate that Kern River's present methodology for allocating fuel costs between its rolled-in and incremental (*i.e.*, expansion) shippers is unjust and unreasonable. Accordingly, Calpine's proposed rate treatment is rejected.

The Commission orders:

Kern River's report supporting its gas compressor fuel and lost and unaccounted-for gas factors for 2004 is hereby accepted.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.