122 FERC ¶ 61,055
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Rockies Express Shippers, Complainants

v.

Northern Natural Gas Company, Respondent

Docket No. RP08-29-000

ORDER ON COMPLAINT AND ESTABLISHING HEARING

(Issued January 25, 2008)

1. On October 24, 2007, as amended October 30, 2007, the Rockies Express Shippers (REX Shippers)[1] filed a complaint against Northern Natural Gas Company (Northern). REX Shippers assert that Northern violated its tariff, as well as Commission regulations and policies, in conducting an open season for capacity that will be available through a new interconnection with the Rockies Express Pipeline LLC (REX Pipeline). The REX Shippers ask the Commission to invalidate the July 2007 open season and require Northern to conduct a second open season for the new capacity so that Market Area shippers will have an opportunity to realign their firm transportation service by designating the new interconnection as a primary receipt point.

2. Northern filed answers to the REX Shippers' allegations and asked the Commission to dismiss the complaint. As discussed below, the parties raise issues of material fact that cannot be resolved on the basis of the existing record. Accordingly, the Commission establishes an investigation and hearing procedures to address the contested issues.

[1] The Rockies Express Shippers are Ultra Resources, Inc. (Ultra), and Sempra Rockies Marketing, LLC (SRM). Northern points out that these are only two of approximately 10 shippers on the REX Pipeline.

Background

3. REX Pipeline is a new pipeline being built in three phases that will extend from the Rocky Mountain production area to eastern Ohio. Phase II of the new REX Pipeline crosses Northern's system approximately 17 miles from its Beatrice, Nebraska compressor station and that crossing point is the site of the new interconnection at issue in this proceeding. It is in the upper part of Northern's system, above the "Demarc" or demarcation line dividing the more constrained upper Market Area of its system from the lower, less-constrained Field Area of the system.[2]

4. On March 22, 2007, Northern posted notice on its website that its agreement with REX Pipeline provided for construction of the new interconnection that would accommodate 200,000 Dth/day. The posting advised that, because of capacity constraints through the Demarc North Group, Northern anticipated that the open season would be only for firm service from the new REX receipt point to Demarc. The open season commenced July 9, 2007, and the open season posting stated that Northern would not be accepting realignment requests at that time, although if unsold capacity remained at the close of the open season, Northern would post it as generally available for incremental requests and realignments. Northern set no minimum rate in the open season, but it advised shippers that the bid evaluation methodology would be the highest net present value (NPV) per unit of capacity for the period from January 1, 2008, through October 31, 2008.

5. Northern posted the results of the open season on July 20, 2007. According to Northern, it received 28 bids for the capacity, seven of which totaled 630,000 Dth/day and were at Northern's maximum tariff rate for firm transportation service. Northern allocated the available 200,000 Dth/day as provided in its tariff, awarding pro rata shares of the capacity to those who bid the maximum rate. Neither of the REX Shippers submitted a bid, although an affiliate of SRM submitted a bid at a discounted rate, so it was not awarded capacity.

6. REX Shippers (Ultra and SRM) will be firm shippers on the REX Pipeline, and each has contracted for 200,000 Dth/day of firm transportation capacity on that pipeline.[3] The REX Shippers contend that Northern unreasonably demanded payment of an

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[2] Demarc is the boundary between Northern's Field and Market Areas. According to Northern, the Demarc point is a physical location on its system that is available as both a primary and alternate receipt and delivery point. The Demarc North Group includes the area of its mainline north of Demarc into the Market Area.

[3] REX Shippers further state that Ultra holds 50,000 Dth/day and SRM holds 5,830 Dth/day of primary firm delivery point capacity at the REX interconnect with Northern.

additional charge to Northern for what the REX Shippers term “phantom” backhaul service before accepting deliveries at the new interconnection. The REX Shippers argue that this charge will disadvantage their gas supplies delivered to Northern’s system on the REX Pipeline as compared to gas supplies delivered to Demarc through Northern’s Field Area facilities, which will not incur the added backhaul charge.

Summary of the Complaint

7. The REX Shippers allege that

A. Northern improperly failed to post the REX receipt point capacity as available for realignment of receipt point capacity by existing Northern shippers holding firm forward-haul transportation in Northern’s Market Area or for designation as a primary receipt point under Northern’s Rate Schedule MPS (pooling) service;

B. Northern improperly tied the availability of firm receipt point capacity at the REX receipt point to shippers subscribing to a new firm backhaul service;[4]

C. Northern did not have the right to offer the new firm backhaul capacity because doing so contravenes the limitations on segmentation that are in place on Northern’s system;

D. Northern discriminated against gas delivered to its Market Area through the REX receipt point by subjecting such gas to limitations, i.e., access to firm receipt point capacity only through backhaul service, to which similarly-situated gas delivered through the interconnection with Trailblazer Pipeline Company (Trailblazer) is not subject;[5]

E. Northern’s charge for backhaul service from the REX receipt point to Demarc is unjust and unreasonable; and

F. Northern’s backhaul charge violates Order No. 587-F[6] and Commission regulations.

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[4] The new REX receipt point will be on the segment of Northern’s system that runs from Demarc to Beatrice and on to Palmyra, Nebraska.

[5] The Northern/Trailblazer interconnection is also located on the Demarc/Palmyra segment at a short distance from the new REX receipt point.

[6] *Standards for Business Practices of Interstate Natural Gas Pipelines*, Order No. 587-F, FERC Statutes and Regulations ¶ 32,527 (1997).

Notices, Interventions, Comments, and Answers

8. Notice of the complaint was issued October 25, 2007, and notice of the amended complaint was issued November 6, 2007. Interventions, protests, and Northern's answer were due as provided in the Commission's regulations.[7] Pursuant to Rule 214,[8] all timely-filed 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 this proceeding or place additional burdens on existing parties.

9. In answers filed November 13 and November 27, 2007, Northern challenges the REX Shippers' allegations, asserting that it conducted the open season in accordance with its tariff, as well as applicable laws and regulations, and Commission policies. Northern argues that:

A. Transportation capacity constraints from the REX receipt point north into the Market Area, particularly during the winter months, cause Demarc to be the desired delivery point, as well as the only primary firm delivery point available for this service. Northern asserts that it conducted the open season pursuant to its tariff in the same manner as it conducted previous open seasons for available capacity from its interconnection with Trailblazer at Beatrice, which is located in the same geographic area as the new REX receipt point.

B. Northern's Market Area segmentation provisions have no relevance to its offer of this capacity in the open season.

C. Newly-available transportation capacity is always provided to shippers that value it the most. The REX receipt point open season resulted in bids at Northern's maximum tariff rate for more than three times the available capacity. If unsold capacity had remained after the open season, Northern would have posted it as capacity generally available to existing shippers.

D. The successful bidders in the open season were maximum tariff rate shippers that will have complete and full access to Northern's entire Market Area for realignments and alternate point scheduling, subject to the availability of capacity. All Market Area shippers have access to the REX receipt point on an alternate basis.

[7] 18 C.F.R. §§ 385.211, 385.214 (2007).

[8] 18 C.F.R. § 385.214 (2007).

10. On November 16, 2007, the REX Shippers field a motion for leave to file answer and an answer to Northern's answer of November 13, 2007. Northern's November 27, 2007 answer responds to the REX Shippers' answer. The Commission's Rules of Practice and Procedure prohibit answers to answers unless otherwise ordered by the decisional authority.[9] In this case, the Commission finds that the answers of Northern and the REX Shippers provide additional information that supplements the record, and the Commission will accept the answers.

11. BP Canada Energy Marketing Corp. (BP Canada) intervened and filed comments. While BP Canada takes no position on the REX Shippers' allegations, it strongly objects to the proposed remedy of voiding the previous open season and requiring a new open season. BP Canada maintains that such an action would harm the shippers that successfully bid for the new capacity and relied on that in structuring commercial arrangements. ConocoPhillips Company intervened and filed an answer in support of BP Canada's comments. EnCana Marketing (USA) Inc. did not intervene, but submitted a letter asking the Commission to consider the effects of Northern's actions on the Commission's policies regarding receipt point allocation, as well as how such actions might discourage future infrastructure projects.

The Pleadings

A. The Complaint

12. The REX Shippers assert that Northern's posting wrongly prohibited Market Area shippers from designating the REX receipt point as a primary receipt point under their existing firm transportation and/or Mileage Indicator District (MID) Pooling Service (MPS) agreements. The REX Shippers contend that Northern's action violated Order No. 636[10] and section 284.13(d)[11] of the Commission's regulations, as well as sections 18 and 26 of the General Terms and Conditions of Northern's tariff.[12]

13. The REX Shippers dispute Northern's claim that it offered the receipt point capacity in connection with a "new" service. The REX Shippers assert that the alleged new service exists only because Northern prevents its other customers from segmenting

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[9] 18 C.F.R. § 385.213(a)(2) (2007).

[10] *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636, FERC Stats. & Regs. ¶ 30,939, at 30,415 (1992).

[11] 18 C.F.R. § 284.13(d) (2007).

[12] Northern Natural Gas Company, FERC Gas Tariff, Sixth Revised Sheet No. 221 and Substitute 13 Revised Sheet No. 252.

their firm capacity on that portion of mainline by claiming that its Market Area experiences "bi-directional flows" of gas and is a "reticulated system." According to the REX Shippers, this violates the flexible point and segmentation rights afforded shippers under Order No. 637.[13]

14. The REX Shippers further contend that Northern's action in tying the new receipt point capacity to an obligatory but unnecessary backhaul service inhibits the creation and development of market pooling centers, contrary to the requirements of Order Nos. 636, 636-A, and 636-B.[14] Specifically, REX Shippers claim that Northern precluded its MPS customers from utilizing their existing MPS pooling service to achieve the same result as the imposed backhaul arrangement.

15. REX Shippers essentially maintain that the phantom backhaul service is actually a pooling service, not significantly different from the service provided under Northern's MPS Rate Schedule. However, unlike the MPS pooling service for which Northern may not impose a charge, Northern will collect its full Market Area tariff rates for the phantom backhaul service, which is obligatory for shippers seeking to use the new REX receipt point as a primary point. REX Shippers estimate that the financial impact to consumers on Northern's system will be from $26.8 million to $36.4 million annually for a pooling service for which they should not be required to pay.

16. The REX Shippers also contend that Northern's backhaul charge violates Order No. 587-F, which makes it clear that shippers must be able to deliver from receipt points into at least one pool and to receive volumes at a delivery point from at least one pool.[15] Additionally, the REX Shippers point to the Commission's statement that "[c]urrent Commission policy as enunciated in Order No. 587-F is to permit a transportation charge to a pool or from a pool, but not both."[16] REX Shippers thus claim that Northern's action

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[13] *Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services*, Order No. 637, FERC Stats. & Regs. ¶ 31,091 (2000).

[14] *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636-B, 61 FERC ¶ 61,272 (1992).

[15] *Standards for Business Practices of Interstate Natural Gas Pipelines*, Order No. 587-F, FERC Statutes and Regulations ¶ 32,527, at 33,351 (1997).

[16] *Transcontinental Gas Pipeline Corp.*, 112 FERC ¶ 61,170, at P 173 (2005).

inhibits the development of a market center in violation of Order Nos. 636 and 636-B and section 284.7(b)(3) of the Commission's regulations.[17]

17. REX Shippers state that Ultra contacted the Commission's Enforcement Hotline, which advised it to file a complaint. REX Shippers further state that Ultra unsuccessfully attempted to address its concerns directly with Northern. REX Shippers assert that Commission intervention is necessary to achieve a satisfactory remedy, although they do not believe that alternative dispute resolution procedures will be adequate. On the other hand, they ask the Commission to require settlement judge procedures. They also ask the Commission to initiate an investigation under section 5 of the Natural Gas Act (NGA) to void the July 2007 open season and to require Northern to conduct another open season for the new capacity without tying it to mandatory phantom backhaul service.

B. Northern's Answer to the Complaint

18. Northern challenges all the REX Shippers' allegations and maintains that settlement judge procedures would be inappropriate in this case so the Commission should dismiss the complaint.

19. Northern contends that it posted and allocated the available capacity in accordance with its tariff and Commission regulations. Further, as required by section 284.7(b) of the Commission's regulations,[18] it offered the capacity to all parties, and it awarded the capacity to the parties bidding the highest NPV. According to Northern, the added gas supply from the REX point cannot go north into the Market Area incrementally on a primary firm basis during the winter because of capacity constraints, but that it can go south to Demarc via backhaul.

20. In response to the claim that it should have made the receipt point available to existing customers, Northern states that it does not sell capacity at individual points. Northern emphasizes that all the transportation service it provides includes at least one receipt point and at least one delivery point, and shippers then have access to all other receipt and delivery points on an alternate basis at the maximum tariff rate.

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[17] 18 C.F.R. § 284.7(b)(3) (2007).

[18] Northern states that 18 C.F.R. § 284.7(b) (2007) provides in part as follows:

> [a]n interstate pipeline or intrastate pipeline that offers transportation service on a firm basis . . . must provide such service without undue discrimination, or preference, including undue discrimination or preference in the quality of service provided, the duration of service, the categories, prices, or volumes of natural gas to be transported, customer classification, or undue discrimination or preference of any kind.

21. Northern insists that, prior to the open season, it made shippers aware that its system was constrained through the Demarc North Group (i.e., receipts at the REX receipt point could not go into the Market Area absent a backhaul). Northern rejects the term "phantom backhaul," contending that backhauls, which are contemplated by the Commission's regulations and Northern's tariff, mean only receipt and delivery in the opposite direction from the typical flow of gas and are neither mysterious nor phantom.

22. Northern asserts that the segmentation program for its Market Area is similar to those approved by the Commission for other pipelines where physical segmentation is unworkable[19] and that the Commission has deemed this "virtual segmentation." Northern points out that transportation on the Delivery Segment is subject to all applicable Market Area transportation rates and mainline fuel charges, and the Delivery Segment uses the Market Area Segmentation Point as its receipt point.

23. Northern also responds to the REX Shippers' claim that pooling service is not available at the REX receipt point. Northern maintains that this receipt point will be treated the same as any other receipt point in its Market Area, including the interconnection with Trailblazer. Northern explains that MPS is its MIDS Pooling Service, which allows a shipper to nominate from any receipt point in the pool to the MID pooling point at no charge. Northern contends, however, that under its tariff, MPS agreements do not contain any primary firm receipt and delivery points.

24. Northern also disagrees that its sale of REX-to-Demarc capacity precludes the development of market centers in its Market Area or reduces the value of the gas at the REX receipt point. According to Northern, the overall dynamics of the MidContinent market determine whether a market center is created, and other market dynamics will determine the value of the gas at the REX receipt point. Northern maintains that it has treated the REX interconnection exactly as it has treated the Trailblazer interconnection. It states that it has not limited the gas delivered to either receipt point to firm receipt capacity available only by backhaul service.

25. Northern next claims that transportation to Demarc is not a pooling transaction and that the REX Shippers' argument is inconsistent with the pipeline's tariff and the Commission's regulations. Northern emphasizes that the Commission specifically recognizes backhaul as "transportation," a term which also includes storage, exchange, displacement, and other methods. Northern claims that shippers acquiring the new capacity are able to use the REX receipt point in the same manner as any other receipt point in Northern's Market Area, including nominating it as an alternate receipt point, using other Market Area receipt and delivery points on an alternate basis, and using the MPS service to pool volumes. In particular, continues Northern, shippers with primary

[19] Northern cites *Dominion Transmission, Inc.*, 95 FERC ¶ 61,316 (2001); *Gulf South Pipeline Company, LP*, 98 FERC ¶ 61,278 (2002).

capacity at the REX interconnection will be able to utilize an MPS agreement and nominate to the MID 17 pool. Northern emphasizes that the REX Shippers have not contracted for firm capacity anywhere on its system and, therefore, will not be able to utilize the REX point as either a primary or an alternate point. However, Northern observes that SRM's affiliate has an interruptible service agreement and an MPS pooling agreement, and Ultra has submitted a request to enter into the same types of agreements, so they will be able to nominate the MID 17 pool on an interruptible basis, but use of the MID 17 pool requires a counter party and a downstream contract in order to deliver the volume to a market.

26. Northern states that the REX Shippers assume that none of the shippers awarded the capacity wish to have their gas transported to a liquid-indexed point like Demarc that has far greater transparency and depth than the REX receipt point. In fact, states Northern, the successful bidders elected to bid for the transportation service so that their gas will be physically available at Demarc on a primary basis. Northern asserts that the REX Shippers' theory that pipelines should not sell transportation from a receipt point because it prevents development of a market center would mean that shippers would never be able to buy transportation on any pipeline from any new interconnection to a point other than for end-use.

27. Northern also addresses the issue raised in the amendment to the complaint -- that the charge for the transportation service to Demarc violates Order No. 587-F and NAESB Standard 1.3.18. Northern contends that this argument relies on the REX Shippers' mistaken belief that Demarc falls into the ABC Rate Zone in the Market Area. Northern points out that Demarc is not in the Market Area and thus is not located in Operational Zone ABC; instead, it is located in a stand-alone MID referred to as MID 16B. Thus, continues Northern, transportation rates to Demarc from the Field Area are different from transportation rates to the Market Area from the Field Area.

C. <u>REX Shippers' Answer</u>

28. The REX Shippers filed an answer to Northern's answer. They dispute the notion that incremental firm transportation has priority over realignments. The REX Shippers challenge Northern's reliance on tariff provisions authorizing use of the NPV methodology to award capacity, agreeing that this is generally appropriate for awarding receipt point capacity in connection with forward haul capacity, but that it is not the case with backhaul service. REX Shippers assert that the associated mainline capacity marketed by Northern here is a backhaul that is available only because Northern has reserved the right to segment capacity for its own purposes.

29. REX Shippers argue that the only reason the "firm backhaul" service could be offered by Northern is because it previously convinced the Commission to approve tariff language denying the Market Area shippers the right to segment their capacity under Order No. 637. According to REX Shippers, had Northern's tariff authorized the same

segmentation rights that firm shippers on other pipelines enjoy, the firm backhaul service would not be available for Northern to offer, but instead would be controlled by its Market Area Shippers, who already paid demand charges for the capacity.

30. According to the REX Shippers, the addition of the REX receipt point between Demarc and the reticulated portions of Northern's system downstream from Palmyra represents a change in circumstances such that segmentation of the mainline between Demarc and the REX receipt point (and likely Palmyra) is now operationally feasible, or Northern could not have offered the "new" backhaul service in its open season.

31. REX Shippers defend their characterization of the service as a "phantom backhaul," because that characterization reflects the two remaining questions: whether the capacity was Northern's to sell and whether, under the unique facts of this case, any service (backhaul or otherwise) is actually provided. They insist that, unlike legitimate backhauls, the artificial service for which Northern seeks to charge its maximum tariff rates is not necessary for the gas to flow from the REX receipt point to ultimate delivery points downstream in Northern's Market Area.

D. Northern's Answer to the REX Shippers' Answer

32. Northern renews its request that the Commission dismiss the complaint, contending that the REX Shippers' answer presents no new facts or arguments. Northern reiterates that its tariff contains one methodology for selecting winning bids that is applicable to all forms of transportation.

33. Northern contends that the REX Shippers have identified no change in circumstances that would require a change to the Commission-approved Market Area segmentation provisions of its tariff. Northern insists that the addition of the REX receipt point does not change the nature of its system or the gas flow on it. Northern states again that its firm transportation contracts provide only for receipt point capacity and delivery point capacity, not path capacity. Finally, Northern states that the Trailblazer receipt point is similar in location and function to the REX receipt point and that the Trailblazer point existed at the time the Commission authorized Northern's virtual segmentation.

Commission Determination

34. The REX Shippers have raised serious questions arising from Northern's open season for the additional capacity to be available through the new interconnection with REX Pipeline. The existing record in this proceeding is insufficient to allow the Commission to make a reasoned decision on any of the issues that have been raised, which include, but are not limited to, whether a backhaul should be required for delivery at the new REX point, whether market center development would be inhibited by such requirement, and whether the posting violated Commission regulations and policy so as to be unjust and unreasonable. Accordingly, the Commission will set the complaint for

hearing.[20] The presiding administrative law judge (ALJ) may make a recommendation as to a remedy, if any, at the conclusion of the hearing.

The Commission orders:

(A) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Energy Regulatory Commission by section 402(a) of the Department of Energy Organization Act and by the NGA, particularly sections 4, 5, 8, and 16 thereof, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the NGA, a public hearing shall be held concerning whether Northern's actions in conducting an open season for the new capacity at the REX interconnection and in awarding the capacity to certain shippers were unjust, unreasonable, or otherwise unlawful.

(B) The ALJ shall, within thirty (30) days of the date of this order, convene a prehearing conference in this proceeding in a hearing room of the Federal Energy Regulatory Commission, 888 First Street, NE, Washington, DC 20426. Such conference shall be held for the purpose of establishing a procedural schedule. The ALJ is authorized to establish procedural dates and to rule on all motions (except motions to dismiss), as provided in the Commission's Rules of Practice and Procedure.

(C) The Commission directs the ALJ to issue an initial decision in this proceeding within 12 months of the commencement of the hearing procedures.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

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[20] Though the Commission is not directing this matter to a settlement judge at this time, the Commission consistently encourages parties to settle disputed issues to avoid the burden and expense of a hearing. In particular, this proceeding may especially benefit from a prompt settlement of the issues due to the uncertainty over the validity of the open season results.