

130 FERC ¶ 61,070
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
and John R. Norris.

The State of Alaska

Docket No. RP10-145-000

ORDER ON PETITION FOR WAIVER

(Issued January 28, 2010)

1. On November 12, 2009, the State of Alaska (State) filed a petition for a limited waiver of the Commission's capacity release regulations and related rules regarding the State's ability to transport royalty gas on any Alaska Gas Pipeline Project authorized by the Commission. In advance of open seasons announced by proponents of potential projects, the State is seeking permission to obtain pre-arranged capacity releases for transporting its royalty gas without posting the releases for bidding. Subject to the conditions explained below, the Commission grants the requested waiver.

Background

2. In 2004, Congress passed the Alaska Natural Gas Pipeline Act (ANGPA) in order to encourage the construction of an Alaska natural gas pipeline. Such a pipeline would transport natural gas from producing areas in Alaska to the border between Alaska and Canada. Among other things, the ANGPA provides that, as long as the rates of existing shippers are not increased, the Commission, upon a request by the State, may provide for reasonable access to pipeline capacity "for the transportation of royalty gas of the State for the purpose of meeting local consumption needs within the State."¹

3. TransCanada Alaska Company, LLC, Foot Hills Pipe Lines, Ltd., and ExxonMobil (jointly "TransCanada") and Denali, a BP and ConocoPhillips partnership, are currently in the pre-filing process with respect to separate proposed Alaska pipeline projects. Both partnerships have announced that they plan to initiate open-seasons during 2010. Denali proposes to construct a natural

¹ ANGPA section 103(h)(1).

gas pipeline with a capacity of up to 4.0 billion cubic feet (Bcf) per day of natural gas, while TransCanada proposes to construct either an Alaska-to-Canada pipeline with a capacity of up to 4.5 Bcf/day or an alternative 3 Bcf/day project to a projected LNG terminal in Valdez, depending on market support.²

4. In 2007, the State passed the Alaska Gasline Inducement Act (AGIA) to encourage an applicant to file for a FERC certificate authorizing an Alaska project. Under the AGIA, the State can award a qualified project sponsor an exclusive and enforceable license. The AGIA licensee is entitled to matching contributions from the State of up to \$500 million during the planning and preparation of a FERC certificate application and related permits for the pipeline. In exchange, the licensee must agree to State requirements intended to maximize the exploration and development of the North Slope and apply to the Commission for a certificate of public convenience and necessity by a certain date, regardless of the outcome of the licensee's initial open season. The AGIA also provides that, before the start of the first binding open season to be conducted by the licensee, the state commissioner of natural resources must adopt regulations concerning payment of royalties to the state. Among other things, those regulations must establish the terms under which the state will exercise its right to switch between taking royalties in kind or in value "for gas committed for firm transportation in the first binding open season of the project." Those regulations must ensure that the state's actions do not unreasonably cause the lessee or other person to bear disproportionate transportation costs. The state has not yet adopted those regulations. In November 2007, TransCanada applied for an AGIA license, which the State granted in 2008.³

The State's Petition

5. The State has leased to various producers the right to produce natural gas on Alaska's North Slope, and under those leases, the State has the right to take its royalties (approximately 12.5 percent, depending on the lease) either in kind or in value. The State also has the right to switch back and forth between the in-kind and in-value options from time to time, at its discretion. As a result, the State asserts that it will need to transport its in-kind royalties on the pipeline; however,

² Both entities also propose to construct a gas treatment plant.

³ The AGIA establishes a regime for State financial support of a proposed project. However, this state statute cannot limit the Commission's federal authority to consider any application for a proposed Alaska project (whether developed under AGIA or not), nor can it in any way affect the Commission's consideration of proposed projects.

when the State receives royalties in value, it will not need the pipeline capacity because producer-shippers will be responsible for transportation. For periods when the State elects to receive royalties in kind, the State proposes to enter a pre-arranged capacity release with producer-shippers to use the capacity that the producer-shippers normally would use for the royalty volumes. The release would require the State to pay the pipeline the same rate paid by the producer-shippers, and this amount would be credited against the pipeline's bill to the producer-shippers. The capacity would then revert back to the producer-shippers when the State switches back to the in-value option. In other words, the capacity would follow the royalty gas.

6. The Commission's current capacity release regulations require all pre-arranged capacity releases to be posted for bidding, unless certain exemptions apply.⁴ The State asserts that the releases at issue here generally will not qualify for those exemptions. It claims that unless the Commission grants permission for pre-arranged capacity releases without bidding, the producers holding capacity on the pipeline would bear significant risk of stranded capacity. To the extent the State could obtain capacity for its in-kind volumes by turning to interruptible transportation, traditional capacity releases from other shippers, or an expansion, the producer-shippers from which the State took its royalties in-kind would not receive any capacity release credits,⁵ and thus could be exposed to the risk of stranded capacity. The State contends this potential for stranded capacity will dissuade bidders from participating in any open season or, at least, will cause them to condition their bids on the resolution of this issue.

7. The State proposes that the waiver should at least cover any producer-shipper that obtains capacity during the initial open season and believes it would be most beneficial if the waiver extends to any firm contract, including expansions, for shippers that produce gas under a lease with the State. Furthermore, the State suggests that the waiver should apply to either of the currently-proposed projects, or to any other Alaska pipeline that may be built, including any capacity associated with an LNG project.

8. The State contends that its request is consistent with ANGPA and Commission precedent. By granting the waiver, the State asserts, the Commission would facilitate the timely development of an Alaska pipeline because it would

⁴ 18 C.F.R. § 284.8(c)-(e) and (h) (2009).

⁵ Section 284.8(f) of the Commission's regulations requires that the pipeline credit the net proceeds from any replacement shipper in any capacity release to the releasing shipper's reservation charge.

provide greater certainty to shippers. This, in turn, would reduce the risk associated with bidding on firm capacity in any open-season. Furthermore, the waiver would assure the State reasonable access for transportation of the State's royalty gas. The State argues that *North Baja Pipeline, LLC*, 111 FERC ¶ 61,119 (2005) and *North Baja Pipeline, LLC*, 128 FERC ¶ 61,082 (2009), are examples of prior Commission determinations granting a limited waiver of the posting and bidding requirements in analogous circumstances.

Public Notice, Comments, and Protests

9. Public notice of the State's filing issued on November 16, 2009, providing for comments on or before November 24, 2009.⁶ Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §385.214 (2009), all timely-filed motions to intervene and any motion 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. On December 10, 2009, BP Exploration (Alaska) Inc. (BP Exploration), ExxonMobil Gas & Power Marketing Company (ExxonMobil), TransCanada, and Anadarko Petroleum Company (Anadarko) all filed comments in general support of the waiver. However, ExxonMobil and Anadarko condition their support on the Commission imposing further requirements on the State's request. Denali – The Alaska Pipeline Company LLC (Denali) and ConocoPhillips Alaska Inc. and ConocoPhillips Company (collectively, ConocoPhillips) filed adverse comments or protests.

10. ExxonMobil requests the Commission to limit the State's request by requiring that, if and when the State elects the in-kind option, the State must accept the capacity release at the corresponding contract transportation rate. Similarly, ExxonMobil argues the Commission should require the producer-shipper to accept a capacity release from the State at the corresponding contract rate. According to ExxonMobil, this condition should also apply if the State makes a sale of the in-kind gas to a buyer at the wellhead. ExxonMobil asserts that if the State does not accept a release of capacity from the producer-shipper in return for the waiver, the producer-shipper could be left with stranded capacity.

11. Anadarko requests that the Commission not limit the State's waiver to only producer-shippers that acquire capacity in the initial open season. Anadarko believes the risk of stranded capacity is not unique only to producer-shippers participating in the initial open season, but all producer-shippers, regardless of the

⁶ The comment period was extended to December 11, 2009, by a notice issued November 19, 2009.

date they commit their production to the pipeline. Moreover, Anadarko asserts that limiting the applicability of the waiver to the initial open season producer-shippers would create an uneven playing field and undermine the goal of promoting future exploration, development, and production of Alaskan natural gas.

12. Denali filed comments and ConocoPhillips a protest with some overlapping concerns. First, both companies contend the State's request for waiver is premature and there is not enough information at this point to grant it. In particular, the State has not issued regulations providing certainty with regard to in-kind/in-value switching, as required by the AGIA. Second, both companies argue that the State's petition is inconsistent with the Commission's capacity release rules and policies and its policy respecting waivers. Denali states the petition is unique in that it does not identify any specific transactions to which the requested waivers will apply; rather, the waivers would apply to a number of potential transactions. ConocoPhillips asserts the Commission generally reserves waiver for transactions where a replacement shipper is permanently acquiring all of a substantial portion of the natural gas assets of a releasing shipper exiting the natural gas business, or transactions where commitments and monetary considerations have been negotiated between the parties.

13. Denali also requests that, if the Commission grants a waiver, it should attach the following conditions: (1) any waiver will only apply to gas used in Alaska; (2) the Commission should require the State to waive its Eleventh Amendment of sovereign immunity, so the State can be held accountable if the pipeline is damaged as a result of any waiver; (3) a minimum timeframe on the frequency of switching, such as annual, quarterly, or monthly should be set and any switching should be limited to no less frequently than once a year with a minimum of 90 days' advance written notice; and, (4) the State should comply with all provisions of the pipeline's approved tariff or applicable contract that are not specifically impacted by the waiver. In addition, Denali is concerned about the pipeline carrying the financial burden of the capacity release because it plans to charge distance-based rates on its system and will earn less revenues for in-kind royalties that are delivered instate. Denali claims that these conditions would ensure that the pipeline remains financially indifferent to any capacity release transaction, and that the pipeline is not unduly burdened by any capacity release transaction.

14. ConocoPhillips protests the State's petition and requests the Commission to deny the waiver. The company claims the State wants to use the waiver addressing fiscal and royalty matters in commercial negotiations with producers. Furthermore, the waiver would facilitate the ability of the State to avoid taking firm capacity and force producer-shippers to underwrite the State's switching

options. For instance, it is not known how the State and its producer-lessees will address any of the stranded capacity costs on the Canadian portion of the pipeline. ConocoPhillips is also concerned that the waiver will provide the AGIA-sponsored pipeline with an advantage over its competitors since certain offers by the State concerning the reduction of stranded capacity costs would only apply to shippers acquiring capacity during the AGIA pipeline initial open season.

15. In addition, ConocoPhillips requests the Commission deny the waiver based on the merits of the petition. As mentioned above, ConocoPhillips states that granting the capacity release waiver would be inconsistent with prior Commission determinations. ConocoPhillips argues that the first *North Baja* case is not applicable in this scenario since the Commission there granted a one-time right to permanently reassign all or a portion of the long-term agreements, not a re-occurring reassignment of capacity. Similarly, ConocoPhillips asserts the reference to *North Baja II* is misplaced. In that case, the Commission denied the waiver request because the petitioners failed to adequately explain why the release could not go forward without the waiver. ConocoPhillips reasons that the State's petition suffers from the same infirmity because the State failed to demonstrate that its in-kind goals and local markets cannot be adequately served without the waiver. In fact, ConocoPhillips notes that nothing in the ANGPA provides for the Commission to issue a waiver of its capacity release rules and policies.

16. In the alternative to denying the petition, ConocoPhillips requests the Commission refrain from taking any action that would influence the commercial negotiations between the State and the producer-shippers or the selection of a pipeline until after the following: (1) commercial negotiations have concluded, (2) more progress has been made on the pipeline, and (3) all relevant facts and circumstances are known.

Answer to Protest and Comments

17. On December 23, 2009, the State filed answers to the comments and ConocoPhillips' protest. On January 6, 2010, ConocoPhillips responded to the State's answer. On January 8, 2010, the State responded to ConocoPhillips' response. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2009), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept the State's and ConocoPhillips' answers because they provided information that will assist us in our decision-making process.

18. Among other things, the State accepts the condition put forth by ExxonMobil and will accept capacity releases from the releasing producer-shipper at the corresponding contract transportation rate. The State also accepts

Anadarko's suggestion that the waiver apply to any capacity on any Alaska Gas Pipeline Project, including expansions to such systems. The State, however, opposes Denali's request to narrow the waiver to gas transported solely within Alaska, since it would limit the State's ability to address in-state demand and storage fluctuations. Nevertheless, the State asserts the predominant use of the waiver will be for in-state needs and any other use will be incidental. The State also opposes Denali's request for limits on the frequency and notice requirements on usage of its in-kind/in-value switching rights, claiming that capacity release transactions would occur more frequently on most other pipelines than the State's in-kind related transactions would. Finally, the State rejects the notion that it should waive sovereign immunity because of the unusual nature of the proposal and because Denali fails to explain what damage could be incurred due to the waiver.

19. The State requests that the Commission reject ConocoPhillips' protest. First, the State contends that the waiver is not premature and ConocoPhillips (and Denali) fail to present a valid reason to deny the request. The State reiterates its claim for clarity before the open-seasons begin and its dependence on the waiver to transport its in-kind volumes. In addition, the State questions ConocoPhillips' argument that the waiver will interfere with commercial discussions and related issues because the issues of royalties and taxes, among others, are not within the Commission's jurisdiction.⁷ Second, the State asserts that ConocoPhillips' complaint regarding stranded capacity along the Canadian portion of the pipeline does not fall under the Commission's jurisdiction and does not constitute a basis to defer action on the waiver request. Third, the State argues that the inducements granted under the AGIA have no relevance to the issue of whether the Commission should grant the waiver, nor do they interfere with the Commission's jurisdiction. Finally, the State asserts that ConocoPhillips fails to prove that the waiver would confer any commercial advantage to the State. The State maintains that, if the Commission grants the State's waiver request, it will remove the ability of any party to gain potential leverage in commercial negotiations with regard to capacity associated with royalty gas.

20. In ConocoPhillips' January 6, 2010 response to the State's answer it reiterates the arguments from its protest. It also states that the only way the Commission could assure that any waiver would be neutral would be to condition

⁷ While, as discussed below, we find Conoco's arguments unpersuasive on their merits, the fact that we might lack jurisdiction to remedy certain matters that are arguably consequences of a Commission action does not mean that we would not consider those matters in determining whether our action was in the public interest.

the waiver to require the State to apply the terms of the waiver equally to shippers participating in any open season on any Alaska Gas Pipeline Project. In its January 8, 2010 answer, the State responded that it would be amenable to these conditions.

Discussion

21. Due to the unique circumstances of the Alaska Gas Pipeline Project, the State's royalty switching rights, and local consumption needs within Alaska, the Commission grants the limited waiver requested by the State, subject to the following conditions: (1) if the State uses the waiver to take a capacity release from one producer, then it must offer to do the same with other similarly-situated producers on any Alaska Gas Pipeline Project; and (2) the waiver must apply to all firm capacity held by producer-shippers and is not limited to firm capacity acquired by a producer-shipper during the initial open season. In its pleadings, the State maintains it will not discriminate against any producer-shipper and the waiver would apply to either pipeline project. Thus, the condition holds the State to its agreement and should alleviate the concerns of certain parties, such as Conoco and Denali, concerning potential discrimination.

22. The Commission agrees with the State that the waiver could eliminate some risk associated with making a firm transportation commitment due to royalty payment switching by the State and would ensure that capacity follows the royalty gas. Moreover, the ANGPA regards the pipeline as in the national interest and recognizes Alaska's need for reasonable access to pipeline capacity for transporting its royalty gas for the purpose of "meeting local consumption needs within the State." That being the case, contrary to Conoco's argument, it is not premature to grant a limited waiver with the aforementioned conditions.

23. The Commission also finds that various conditions requested by Denali are not necessary and will be rejected. The Commission will not restrict the waiver to apply only to gas used in Alaska. This condition is not necessary because the State indicates that out-of-state uses will be incidental. That fact that ANGPA provided for the State's reasonable access to the pipeline to transport royalty gas for local consumption does not preclude the State's transportation of royalty gas out-of-state. No party will be harmed if the gas is used out-of-state because Alaska will pay for the released capacity at the contract rate. The Commission also will not establish a minimum timeframe on the frequency of switching. The State's right to switch between royalty payment methods is governed by its contracts with the producers. Denali did not give a reason for the Commission to limit the frequency of switching. The Commission is only waiving the posting and bidding requirements and not other capacity release rules. Thus, both the pipeline

and the State have to abide by any pipeline's Commission-approved tariff, including capacity releases on short notice by the pipeline consistent with Commission regulations. A condition requiring that the State be required to comply with all provisions of the pipeline's approved tariff, is unnecessary because all shippers must comply with the pipeline's tariff, and, in any case, the State agrees to comply with all applicable Commission-approved tariff provisions, subject to its right to protest any proposed tariff provisions.

24. With regard to Denali's concern about remaining fiscally neutral for short haul shipments associated with in-kind royalty gas, section 284.8(f) of the Commission's capacity release regulations provides that, unless the pipeline agrees otherwise, the contract of the shipper releasing capacity will remain in full force and effect. Therefore, the producer remains liable for the full amount of its payments, to the extent that liability is not offset by credits for the State's payments to the pipeline for its released capacity. Therefore, the capacity releases to the State cannot reduce pipeline revenues and Denali's concern is unfounded.

25. Finally, the Commission will not require the State to waive its Eleventh Amendment right of sovereign immunity as a condition of the waiver. Denali did not give a reason why sovereign immunity should be waived or give any indication what damage it might suffer absent such a waiver. As already discussed, the producer-shipper will remain fully liable under its contract with the pipeline for all amounts not offset by the State's payments to the pipeline.

The Commission orders:

(A) The State's petition for a limited waiver of the Commission's capacity release regulations and related rules regarding the State's ability to transport royalty gas on any Alaska Gas Pipeline Project is granted, subject to the following conditions:

- (1) If the State uses the waiver to take a capacity release from one producer, then it must offer to do the same with other similarly situated producers on any Alaska Gas Pipeline Project that is completed and provides interstate service.

(2) The waiver must apply to all firm capacity held by producer-shippers and is not limited to firm capacity acquired by a producer-shipper during the initial open season.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.