UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Discovery Gas Transmission LLC	Docket No. CP03-342-002
Discovery Producer Services LLC	Docket No. CP03-343-002
Texas Eastern Transmission, LP	Docket No. CP04-50-001

ORDER GRANTING REHEARING

(Issued July 13, 2004)

1. On May 25, 2004, Discovery Gas Transmission LLC, (Discovery) filed a request for rehearing of the Commission's May 6, 2004 Order in this proceeding.[1] The May 6 Order authorized Discovery's Market Expansion facilities in Louisiana and approved Discovery's proposed initial rates for incremental service, requiring a 100 percent load factor IT rate provision in its tariff crediting 100 percent of all IT and overrun revenue to firm and interruptible shippers. For the reasons discussed herein, the Commission will grant Discovery's request for rehearing of the May 6 Order.

Background and Request for Rehearing

2. Discovery requests rehearing of the May 6 Order solely on the issue of whether the Commission properly required Discovery to credit 100 percent of all IT revenue to firm and interruptible customers. The May 6 Order stated that Commission policy regarding new interruptible service requires either a crediting of revenues, net of variable costs, to firm and interruptible customers, or an allocation of costs to this service. The order found that a revenue crediting provision is appropriate because this is a new service without actual experience upon which to base a cost allocation.

3. Discovery states that a 100 percent revenue crediting provision is not appropriate under the circumstances of the project at issue in this proceeding. Instead, Discovery proposes to credit to its customers 90 percent of the combined firm and interruptible transportation revenues that exceed Discovery's approved cost of service of $4.4 million.

[1] Discovery Gas Transmission LLC, 107 FERC ¶ 61,124 (2004).

4. Under Discovery's proposal, transportation service will be provided through the Market Expansion facilities only pursuant to Discovery's firm Rate Schedule FT-2 (Market Expansion) and Rate Schedule IT (Market Expansion). In return for committing quantities of gas for the life of specified leases to firm service on Discovery, shippers are not charged a reservation fee, but instead pay only a usage fee under Rate Schedule FT-2 (Market Expansion). This is the same rate methodology used in the design of Discovery's initial rates and is consistent with the rate structure of its existing FT-2 rate schedule. Discovery states that it did not propose a more traditional monthly reservation charge using a straight-fixed variable (SFV) rate design under Rate Schedule FT-1 because no shipper requested such service from Discovery, and it does not anticipate having any Rate Schedule FT-1 shippers for its Market Expansion facilities.

5. Discovery explains that, because its rate design for service through the Market Expansion facilities is based solely on usage rates and there are no reservation fees, it will have no guaranteed stream of revenue and will be at risk for recovery of any return on its investment in the Market Expansion facilities. Discovery states that the usage rate is based on the total firm capacity of the Market Expansion facilities (150,000 Dth/day) without regard to whether the service provided will be on a firm or interruptible basis.

6. Emphasizing that it does not charge reservation fees, Discovery states that, in proceedings where either IT revenue crediting or cost allocation has been required, the pipeline has been guaranteed revenue through the collection of reservation fees.[2] Discovery argues that, since its proposed Market Expansion project does not involve this kind of situation, a 100 percent revenue crediting mechanism is inappropriate and should not be applied to Discovery.[3] Further, it notes that the Commission did not impose an IT revenue crediting mechanism or cost allocation in approving Discovery's existing rates.[4]

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[2] Citing AES Ocean Express, 103 FERC ¶ 61,030 (2003); SCG Pipeline, Inc., 99 FERC ¶ 61,345 (2002); Independence Pipeline Co., 89 FERC ¶ 61,283 (1999); and Maritimes & Northeast Pipeline, L.L.C., 81 FERC ¶ 61,166 (1997).

[3] Discovery notes that the Commission's policy of crediting revenue or allocating costs to interruptible service has not been imposed even on certain offshore pipelines that do charge reservation fees, citing Dauphin Island Gathering Partners, 82 FERC ¶ 61,136 (1998); Destin Pipeline Company, LLC, 79 FERC ¶ 61,395 (1997); and Shell Gas Pipeline Company, 76 FERC ¶ 61,126 (1996).

[4] Discovery Gas Transmission LLC, 78 FERC ¶ 61,194 (1997), order on rehearing, 96 FERC ¶ 61,114 (2001), order on rehearing, 97 FERC ¶ 61,023 (2001).

7. Discovery states that, depending on daily market conditions on its system, it could transport very little gas through its Market Expansion facilities under Rate Schedule FT-2 (Market Expansion), and instead be requested to provide mostly interruptible service under Rate Schedule IT (Market Expansion).[5] Discovery notes if it were required to return all IT revenue to its customers, it might not recover its capital costs in the Market Expansion project and earn its allowed rate of return. Discovery states that although it projects it will deliver approximately 100,000 Dth/day under Rate Schedule FT-2 (Market Expansion) through the Market Expansion facilities, this level is still far less than the 150,000 Dth/day billing determinants on which its Rate Schedule FT-2 (Market Expansion) usage rate is based.

8. Discovery argues that, if the Commission requires a revenue crediting mechanism, it should recognize the total usage revenue collected by Discovery. Discovery states that it recognizes the Commission's concern that Discovery may over-collect its cost of service and exceed its allowed rate of return if the level of interruptible service on the Market Expansion turns out to be significant and Discovery is able to collect more transportation revenue than the maximum usage rate times the 150,000 Dth/day billing determinants underlying the rate. Discovery states, however, that there is little likelihood that such over-collection will occur because it does not expect to average more than 150,000 Dth/day of combined firm and interruptible service on the Market Expansion project and because it will rarely be able to collect its maximum rate from the Market Expansion shippers. Discovery submits that a revenue crediting condition that takes into account the total amount of FT and IT revenue that Discovery is able to collect would address the Commission's concern and give Discovery a reasonable opportunity to recover its costs and earn the allowed rate of return on its investment.

9. Specifically, Discovery requests that it be required to credit revenue to its firm and interruptible customers only to the extent that its combined FT and IT revenues from service through the Market Expansion facilities exceed its approved, annual cost of service of $4.4 million, and that it be permitted to retain 10 percent of the revenues above the cost of service. Discovery submits that its proposed alternative revenue crediting mechanism would prevent any over-collection of revenues while permitting Discovery a reasonable opportunity to recover its allowed rate of return, as well as an incentive to market interruptible service even at discounted rates.

[5] The rate for Rate Schedule FT-1 (Market Expansion) is the same as the rate for Rate Schedule IT (Market Expansion), because the Commission rejected Discovery's proposed 50 percent load factor rate for Rate Schedule IT (Market Expansion).

10. Discovery submits that retaining 10 percent of revenue above costs is reasonable and would give it the incentive to provide additional transportation in the event additional compression is available and transportation opportunities on the Market Expansion facilities are significantly higher than projected. Discovery states that this percentage was approved by the Commission in Order No. 636 proceedings in restructuring rates in a way that would deter any over-recovery of costs while maintaining incentives to provide interruptible transportation at greater than projected levels.[6]

Discussion

11. Discovery states that it will deliver approximately 100,000 Dth/day through its Market Expansion project. We note, however, that Discovery has precedent agreements with three shippers for 112,000 Dth/day (75 percent of the total firm capacity of the Market Expansion facilities of 150,000 Dth/day). Further, Discovery states in its application that two other shippers requested firm service under Rate Schedule FT-2 (Market Expansion) for up to 100,000 Dth/per day, even though they wanted short-term contracts without the commitment of gas for the life of their leases as required under Rate Schedule FT-2 (Market Expansion). Nevertheless, Discovery states that it expects to be able to deliver gas for these and other shippers on an interruptible basis under Rate Schedule IT (Market Expansion).

12. In addition, Discovery notes that, under the compression services agreement with Discovery Producer Services LLC (Discovery Producer), Discover Producer may be able to provide an additional 50,000 Dth/day of compression services for Discovery. Thus, on those days, Discovery has the potential to transport more than 150,000 Dth/day. Indeed, Discovery submits in its application that the new delivery points will provide incremental value to Discovery's existing shippers and enhance its ability to attract incremental gas supplies and associated shippers. By extending its pipeline system to four new pipeline interconnections, Discovery has expanded its system to reach additional markets, which could generate additional transportation service through the Market Expansion facilities.

13. All this suggests a potential for Discovery to exceed its projected throughput level of 150,000 Dth/day and over-recover its cost of service. In its rehearing request, however, Discovery proposes to credit 90 percent of FT and IT transportation revenues to firm and interruptible customers after Discovery has recovered its annual cost of service

[6] Citing Trunkline Gas Company, 62 FERC ¶ 61,199 (1993); Iroquois Gas Transmission System, LP, 62 FERC ¶ 61,167 (1993); Arkla Energy Resources, 62 FERC ¶ 61,076 (1993); and Texas Eastern Transmission Corporation, 62 FERC ¶ 61,015 (1993).

of $4.4 million. Discovery's proposal would allay the Commission's concerns regarding the potential for cost over-recovery, as well as give Discovery the incentive to provide additional transportation when additional compression is available and transportation opportunities on the Market Expansion facilities enable Discovery to exceed its projected level of service. Accordingly, the Commission will grant rehearing and accept Discovery's alternative proposal and require Discovery to file such a revenue crediting mechanism in its tariff when it makes its compliance filing.

The Commission orders:

(A) Discovery's request for rehearing is granted.

(B) Discovery's revised rates, to be filed not less than 30 nor more than 60 days prior to implementing the market expansion project, shall include a revenue crediting mechanism in its tariff that credits 90 percent of all FT and IT transportation revenue to firm and interruptible shippers after Discovery has recovered its annual cost of service of $4.4 million.

By the Commission.

(S E A L)

Linda Mitry,
Acting Secretary.