

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Northern Natural Gas Company

Docket Nos. RP04-94-000
RP04-94-001

ORDER ACCEPTING COMPLIANCE FILING

(Issued July 26, 2005)

1. On April 9, 2004, Northern Natural Gas Company (Northern) filed an explanation to comply with the Commission's March 25, 2004 Letter Order (March 25 Order).¹ This order accepted Northern's January 20, 2004, informational filing subject to Northern filing an explanation addressing the concerns of Northern Municipal Distributors Group and Midwest Region Gas Task Force Association (NMDG/MRGTF). Northern's April 9, 2004 explanation complies with the March 25 Order and is accepted for filing.

Background

2. Northern has used its System Balancing Agreement (SBA) surcharge to recover the costs of purchasing system supply gas for packing, drafting, peaking, and no-notice service. On December 30, 2003, in Docket No. RP04-94-000,² the Commission conditionally approved Northern's SBA cost recovery surcharge for 2004, subject to Northern filing additional information necessary to evaluate the costs included in the 2004 surcharge. After Northern filed the information, the Commission directed Northern to file an explanation addressing the concerns expressed in the February 4, 2004 comments of NMDG/MRGTF. Specifically, the March 25 Order directed Northern to explain what circumstances prompted it to reduce the quantity and term parameters in its solicitation for bids from potential suppliers of the gas it would use in its system operations. Northern filed its explanation on April 9, 2004. On April 21, 2004,

¹ 106 FERC ¶ 61,287 (2004).

² 105 FERC ¶ 61,395 (2003).

NMDG/MRGTF protested Northern's April 9, 2004 filing. On May 6, 2005, Northern filed an answer to the protest.³

3. On November 24, 2004, Northern filed a Partial Settlement agreement in Docket Nos. RP03-398-000 and RP04-155-000, its consolidated general section 4 rate increase proceedings. Among other things, the Partial Settlement provided for the termination of the existing SBA surcharge mechanism effective January 1, 2005. Thereafter, Northern would recover these costs in its Market Area base tariff rates. On February 14, 2005, the Commission approved the Partial Settlement as uncontested.⁴ NMDG/MRGTF requested a rehearing of the Partial Settlement order. In its June 2, 2005 rehearing order,⁵ the Commission noted that the Partial Settlement, at Article I, section A, Paragraph 2, provides, in part, that the parties shall retain the right to challenge the level of SBA costs for the period November 2003 through the last month that the SBA surcharge was in effect. Accordingly, the Commission granted rehearing to modify the Partial Settlement order to eliminate the termination of Docket No. RP04-94-000 and stated that it would act on NMDG/MRGTF's April 21, 2004 protest in that proceeding.

Northern's Explanatory Filing

4. Northern states that on July 21, 2003, it held its initial SBA bid solicitation for the upcoming annual SBA period of November 2003 through October 2004, incorporating historical quantity and term parameters that Northern has followed since it implemented the SBA provisions. Northern received the SBA bids on August 15, 2003, and asserts the bids resulted in SBA costs of \$10 million that exceeded previous years' \$6 million to \$8 million of SBA costs and were much higher than anticipated. Northern further asserts that as a result, it rejected all the bids and, after discussions with its customers, decided to hold a revised bid solicitation. Northern contends that it learned from bidding parties that extreme price volatility experienced during the prior heating season caused the increased prices. Northern then discussed with its shippers the possibility of reducing the number of pack and draft and peaking months. Northern asserts that it recognized that the possibility that reduced quantity and term SBA bid parameters could result, for example, in the calling of more System Overrun Limitation (SOL) days but that Northern could still effectively operate its system.

³ The Commission's Rules of Practice and Procedure do not permit answers to protests (18 C.F.R. § 385.213(a)(2) (2005)). However, the Commission finds good cause to admit the answer by Northern since it will not delay the proceeding, will assist the Commission in understanding the issues raised and will ensure a complete record on which the Commission may act.

⁴ 110 FERC ¶ 61,149 (2005).

⁵ 111 FERC ¶ 61,339 (2005).

5. Northern asserts that it posted a revised bid solicitation on August 21, 2003, which slightly revised the SBA bid parameters, to mitigate the impact of high volatility and reduce the SBA bid prices. Northern reduced the parameters for gas that it would use for peaking and drafting from 3.78 Bcf for nine months to 2.94 Bcf for seven months over the 12-month SBA period. Northern's bid package to provide peaking service remained at 1.35 Bcf, but reduced the term by two months to December through March instead of November through April. Northern received SBA bids of approximately \$7.65 million which were significantly lower than the original bids of \$10 million.

6. Northern asserts that it based the decision to reduce both the quantity of SBA gas it needed to purchase by .84 Bcf and the purchase term by two months on higher than expected costs received in response to its original SBA bid solicitation. Northern further asserts that its rejection of such bids and posting of a revised bid solicitation with slightly reduced quantity and term parameters was reasonable. Northern contends that, although the revised bid parameters called for less purchases over a slightly shorter term, this does not in any way mean that the level included in the original solicitation was somehow unreasonable. It opines that system balancing agreements are but one tool used to balance its system. For example, continues Northern, other tools include the use of operational storage, the Carlton Resolution, and liquefied natural gas and the precise mix of how much Northern will rely on each tool each year is not a fixed obligation. Northern asserts that, as a result, at the time it revised the SBA bid package, Northern knew other balancing tools existed that it could rely upon if necessary in order to effectively operate its system. Northern further asserts that it evaluated all of its operating conditions and available balancing tools and determined that it was reasonable to reduce the level of SBA services in order to reduce overall SBA costs for the benefit of its customers.

7. Northern notes that, when the initial bids were received, it communicated to NMDG/MRGTF the steps it intended to take to contain SBA costs without any objection until their February 4, 2004 protest. Northern argues that there is no merit to NMDG/MRGTF's criticism for its exercise of reasonable business practices. In any event, it fails to see how NMDG/MRGTF has been harmed by the decision to solicit revised bids that resulted in lower SBA costs. Northern further argues that the revised parameters were the result of discussions with customers, including NMDG/MRGTF, to achieve lower SBA costs while still ensuring the reliable operation of its system. Northern contends that it followed its tariff with respect to establishing the 2004 SBA surcharge and has explained the basis for its revised bid solicitation.

NMDG/MRGTF's Protest

8. NMDG/MRGTF argues that Northern does not address the central issue of whether Northern overstated, in this filing or in the past, the level of SBA service required to meet the needs of the system and its shippers. NMDG/MRGTF questions, if

Northern could effectively operate its system within the revised and lower cost parameters, why Northern did not initially include the revised parameters in the original bid package. NMDG/MRGTF argues that Northern initially attempted to contract for an unnecessarily high level of SBA services for 2004. NMDG/MRGTF further argues that all of Northern's tools to reduce its SBA needs were in place when it issued the original bid package and none of those tools changed between that time and when Northern issued the revised bid package only one month later. NMDG/MRGTF contends that Northern appears to confirm that given the panoply of operational tools available to it, Northern did attempt to oversubscribe SBA services for 2004 and has consistently overstated its SBA requirements.

9. NMDG/MRGTF contends that there was a 23 percent reduction in the required quantity and a two month term reduction of the pack and draft SBA service and the term of the peaking SBA service in the revised bid package. NMDG/MRGTF questions why the revised parameters were not the original parameters; what standards did Northern apply to determine that the bids made in response to the original bid package were too high; how did Northern conclude that the bids received in response to the revised bid package are not "too high" as well; and how can the Commission and the shippers determine that the amount of SBA service provided under the revised bids is not too high. NMDG/MRGTF argues that to the extent there were increased prices as compared to 2003, the increased prices affected both the original and the revised bid package, and that what changed was the substantial reduction in the quantity and term parameters for SBA service between the original and revised bid packages. Finally, NMDG/MRGTF contends that, while Northern argues that it communicated with NMDG/MRGTF without objection, Northern is responsible for defending its SBA practices. NMDG/MRGTF requests that the Commission reject Northern's filing to increase the SBA surcharge for 2004 and institute further proceedings to review Northern's operational tools and investigate its SBA bidding and contracting practices to determine whether the SBA mechanism truly minimizes costs, or whether Northern consistently over-subscribes these services.

Northern's Answer

10. Northern argues it explained that it revised its original bid solicitation because of inordinately high SBA costs and primarily, the extreme volatility experienced during the prior heating season. Northern asserts that, as a result of discussions with its customers, it determined that it was reasonable to revise the historical SBA bid parameters to reduce the overall SBA costs while still ensuring the reliability of its system and that no customers questioned Northern's actions. Northern argues that the reason it did not initially include the revised parameters is irrelevant for purposes of this proceeding because Northern filed for recovery of the SBA costs based on the second bid solicitation which resulted in lower SBA costs. Northern further argues that NMDG/MRGTF has not challenged the \$7.65 million of SBA costs resulting from the revised bid solicitation

and, thus, there is no basis to reject Northern's proposed 2004 SBA surcharge. Northern contends that, in any case, there was nothing inappropriate with its' original bid solicitation which was consistent with the historical bid parameters used in prior SBA filings approved by the Commission.

11. Northern argues that it based its previous SBA requirements on historical parameters approved by the Commission. Northern asserts that it explained the availability of other operational tools to demonstrate that the precise mix and use of each tool each year is not fixed. Moreover, Northern maintains that it could rely upon varying amounts of other balancing tools, if necessary, to effectively operate its system. Northern further asserts that it evaluated all of its operating conditions and available balancing tools and determined that it was reasonable to reduce the level of the SBA bid solicitation in order to reduce overall SBA costs for the benefit of its customers.

12. In response to NMDG/MRGTF's request that the Commission institute further proceedings, Northern argues that NMDG/MRGTF's real issue is not so much with the specific SBA costs filed in this proceeding but the level of SBA services as they relate to the other operational tools. Northern contends that the proper forum for discussing the proper mix and related costs of balancing tools is in its pending consolidated rate case proceedings, not here where Northern followed its tariff to establish the 2004 SBA surcharge and explained the basis for its revised bid solicitation.

Discussion

13. The Commission accepts Northern's April 9, 2004 explanatory filing. NMDG/MRGTF's assertions regarding the 2004 SBA surcharge are rejected as vague and unsupported. As Northern points out, its 2004 SBA cost recovery surcharge filing in this proceeding seeks to recover the SBA costs associated with the second bid solicitation which resulted in lower SBA costs. NMDG/MRGTF's challenge concerns the revision of the original solicitation. Northern's proposed 2004 SBA surcharge was not based on the original solicitation, but on the revised bid solicitation. Northern, in any case, has satisfactorily explained the circumstances of its revision to the original bid solicitation which resulted in the revised gas purchase bids that reduced costs to its customers. Therefore, no basis has been presented upon which to reject Northern's proposed SBA surcharge for 2004.

14. In addition, we deny NMDG/MRGTF's request for further proceedings to investigate Northern's SBA bidding and contracting practices. The Partial Settlement in Northern's consolidated rate proceedings allows a challenge only to the level of the SBA costs for the period November 2003 through the last month the surcharge is in effect. The Partial Settlement also requires Northern to terminate the existing SBA surcharge mechanism effective January 1, 2005. Further, the Commission previously stated that it would not examine the underlying structure and rationale of the SBA charge outside of

the context of the general section 4 rate case proceeding in Docket No. RP03-398-000 and that NMDG/MRGTF may pursue the issue of the SBA charge in that proceeding.⁶ Therefore, there is no need for further proceedings to investigate Northern's terminated SBA mechanism.

The Commission orders:

Northern's April 9, 2004 explanatory filing is accepted as in compliance with the Commission's March 25 Order.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.

⁶ 104 FERC ¶ 61,162 at 61,584 (2003).