UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

North Baja Pipeline, LLC — Docket Nos. RP02-363-002, RP02-363-005, RP02-363-006

ORDER DENYING REHEARING AND CLARIFYING PRIOR ORDER
AND ACCEPTING COMPLIANCE FILINGS
SUBJECT TO MODIFICATION

(Issued December 24, 2003)

1. On February 28, 2003, the Commission issued an order[1] wherein, among other things, it acted pursuant to its authority under Section 5 of the Natural Gas Act (NGA) to bring North Baja Pipeline's (NBP) tariff into conformance with the Commission's creditworthiness standards. NBP and the Interstate Natural Gas Association of American (INGAA) filed requests for rehearing and/or clarification of that order. In a separate filing, NBP submitted tariff sheets in compliance with the February 28 Order. The Commission here is clarifying its February 28 Order, denying the requests for rehearing, and accepting the tariff sheets, subject to modification. This order benefits the public interest by ensuring that NBP's tariff is consistent with Commission policy regarding operational procedures and creditworthiness provisions.

I. Background

2. NBP is a new, 79.8-mile pipeline which interconnects with El Paso Natural Gas Company's facilities near Ehrenberg, Arizona and culminates at border-crossing facilities near Mexicali, Baja California, Mexico, where NBP interconnects with Gasoducto Bajanorte, a Mexican pipeline. NBP has a capacity of 512,500 Dth/day and is primarily intended to serve new, gas-fired electric generation supplying the northern Mexico and southern California power grids.

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[1] North Baja Pipeline, LLC, 102 FERC ¶ 61,239 (2003) (February 28 Order).

3. On August 9, 2002, the Commission issued an order[2] conditionally accepting NBP's initial tariff proposal and directing NBP to make further revisions to: (1) limit the amount of collateral required for long-term firm service; (2) limit Operational Flow Orders (OFOs) to critical periods and to address threats to system integrity; (3) require OFO information to be posted as soon as it becomes available; (4) eliminate the need for shippers to use nomination and scheduling procedures to net and trade imbalances; (5) extend the application of right of first refusal (ROFR) rights to multi-year, maximum-rate contracts involving services that are not offered for 12 consecutive months; and (6) propose an alternative mechanism for imbalance resolution.

4. On January 29, 2003, the Commission issued two orders, Northern Natural Gas Company (Northern)[3] and Tennessee Gas Pipeline Company (Tennessee),[4] which clarified Commission policy regarding creditworthiness standards for pipelines. The Northern order notes that the Commission started a generic proceeding to examine certain aspects of creditworthiness by requesting the Wholesale Gas Quadrant of the North American Energy Standards Board to consider whether standards relating to creditworthiness can be developed. The Northern order declined to expand that proceeding to an industry-wide generic proceeding on creditworthiness, but instead explained that the Commission would continue to address the issue on a case-by-case basis. The Northern and Tennessee orders were issued after technical conferences on creditworthiness issues were held in those cases, with the opportunity for comment. Those orders also noted that several cases pending before the Commission involved creditworthiness issues.

5. The August 9 Order also directed NBP to remove tariff language that would have permitted it to include the value of lent gas in the amount of collateral required for PAL-1 service. In the February 28 Order, the Commission addressed NBP's request for rehearing of the August 9, 2002 Order. There, acting under Section 5 of the NGA, the Commission modified NBP's creditworthiness standards to bring it into compliance with the creditworthiness policies established in Northern and Tennessee. The changes which are now at issue concern the amount of security the pipeline can require from its shippers.

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[2] North Baja Pipeline, LLC, 100 FERC ¶ 61,183 (2002) (August 9 Order).

[3] 102 FERC ¶ 61,076 (2003).

[4] 102 FERC ¶ 61,075 (2003).

6. On June 4, 2003, the Commission issued an order[5] on rehearing and compliance in the Tennessee proceeding which, among other things, clarified certain aspects of our February 28 Order in this proceeding, as discussed below.

II. Compliance Filing – Docket No. RP02-363-002

A. Description of the Filing

7. The August 9 Order addressed NBP's proposal for daily imbalance penalties. NBP's original tariff required shippers to balance actual receipts and deliveries on a daily basis, and offered the following remedies for imbalance resolution: (1) flow control by NBP, when possible; (2) shipper nominations; (3) the use of PAL-1 service; and (4) netting and trading. The August 9 Order rejected NBP's proposal for physical imbalances to be automatically transferred to PAL-1 service, finding that the service should be optional. The order also stated that, for shippers not electing PAL-1 service for imbalance resolution, NBP could propose a tiered cashout mechanism, a nominal imbalance penalty for use during non-critical periods, and a higher penalty for imbalances during critical periods.

8. NBP now proposes in Section 16 of its General Terms and Conditions (GT&C) to make PAL-1 service optional for resolving imbalances. Further, NBP proposes a $10/dth penalty on positive or negative daily physical imbalances above a 5% tolerance that shippers have chosen not to resolve through PAL-1 service, and which are unresolved three days after NBP has notified the shipper of the imbalance. The penalty would be applicable during periods when the system is not constrained, its integrity is not threatened, and NBP has not issued an OFO. If not resolved within 45 days of such notice, NBP would assess an additional $10/dth penalty on negative imbalances, and would confiscate and sell a positive imbalance, applying the proceeds to its revenue crediting mechanism.

B. Notice

9. Notice of NBP's filing was published in the Federal Register (67 Fed. Reg. 58,600) with interventions, comments, and protests due by September 23, 2003. No protests or interventions were filed.

C. Discussion

10. NBP has complied with the Commission's directive to make PAL-1 service optional for resolving imbalances. However, NBP must further revise Section 16 to be compliant with Commission policy on penalties. In Order No. 637, et seq., the Commission directed

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[5] Tennessee Gas Pipeline Company, 103 FERC ¶ 61,275 (2003) (Tennessee II).

pipelines away from the use of penalties to deter undesirable shipper behavior during non-critical periods, and instead required them to offer a variety of imbalance management tools. The August 9 Order reflected this policy shift when it stated that, for shippers not electing PAL-1 service for imbalance resolution, NBP could propose a tiered cashout mechanism, a nominal imbalance penalty for use during non-critical periods, and a higher penalty for imbalances during critical periods. NBP's proposed $10/dth penalty on daily physical imbalances during non-critical periods is substantial, and inconsistent with the Commission's current policy on penalties which requires pipelines to narrowly design penalties to deter only conduct that is actually harmful to the system.[6] Therefore, NBP is directed to revise its proposed physical imbalance penalties to be applicable only during critical periods. Also, as stated in the August 9 Order, NBP may propose a nominal penalty for use during non-critical periods.

11. NBP's compliance filing in Docket No. RP02-363-006 makes further revisions to two tariff sheets in the instant proceeding. Therefore, First Revised Sheet Nos. 134 and 135 in this docket are rejected as moot.

III. Rehearing – Docket No. RP02-363-005

A. Requests for Rehearing

12. NBP filed a request for rehearing and clarification of the February 28 Order. INGAA, a trade association representing the interstate pipeline industry, filed a motion to intervene out-of-time and a request for rehearing of the February 28 Order. When late intervention is sought after the issuance of a dispositive order, the prejudice to other parties and burden upon the Commission of granting the late intervention may be substantial. Thus, movants bear a higher burden to demonstrate good cause for the granting of such late intervention.[7] INGAA states that good cause exists to approve its late intervention because it had no reason to know, prior to the February 28 Order, that this proceeding would address issues of substantial importance to the entire pipeline industry.

13. NBP and INGAA argue that the Commission erred in applying the precedents set in Northern and Tennessee to NBP because the facts and circumstances of those cases are substantially different. Specifically, they point to the fact that Tennessee is a very large pipeline with many creditworthy shippers, whereas NBP is a small, new pipeline with few initial shippers, all of which are non-creditworthy. NBP points out that a default by a

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[6] See, e.g., Paiute Pipeline, 96 FERC ¶ 61,167 (2001).

[7] North Baja Pipline LLC, 99 FERC ¶ 61,028 at 61,109-110 (2002).

shipper on Tennessee's system is not likely to have a substantial financial impact, whereas a default by a shipper on NBP's system would, since each shipper represents a much higher percentage of NBP's cash flow.

14. NBP and INGAA both argue that the Commission erred procedurally by acting under NGA Section 5 without first conducting an evidentiary hearing to determine the facts and circumstances relating to NBP. Specifically, they contend that the Commission ignored the critical differences between the risk profiles facing Northern and Tennessee, as compared to NBP.

15. NBP and INGAA note that the February 28 Order states that "requiring security equal to twelve months of service charges is excessive for shippers subscribing to service after the pipeline is in operation."[8] They note also that the February 28 Order goes on to say "a prepayment requirement for any period longer than three months is excessive and should be rejected."[9] NBP and INGAA interpret these statements to mean that once the pipeline becomes operational, NBP can only require no more than 3 months collateral from its original shippers (i.e., shippers who entered into contracts prior to construction of the pipeline), regardless of the collateral requirements specified in those shippers' contracts for service. They argue that this ruling undermines NBP's contracts with its shippers and otherwise shifts an unacceptable amount of financial risk to NBP. They argue that the limitation on the collateral that is allowed for new construction will impede development of infrastructure.

16. NBP seeks clarification that the Commission's prior decisions allowing pipelines to require up to twelve months of collateral for system expansions does not foreclose a pipeline's ability to require greater collateral on a non-discriminatory basis from non-creditworthy shippers subscribing to an expansion. NBP states that this clarification is necessary to ensure that NBP has the flexibility to establish creditworthiness criteria for an expansion consistent with NBP's tolerance for risk. In the alternative, NBP seeks rehearing on this issue.

17. In support of its request for clarification, NBP states that circumstances may exist where one year of collateral does not provide NBP with sufficient assurance to justify its investment in new capacity. In particular, NBP is currently holding an open season to accommodate a potential system expansion for entities contemplating construction of LNG facilities in Baja California, Mexico that would require service on NBP. If the project goes

[8] Supra n. 1 at P 14.

[9] Id. at P 15.

forward, it would bring a significant new source of natural gas into the western U.S. marketplace. However, noting that its potential gain from investing capital is limited by its regulated rate of return, NBP states that it may be unwilling to risk its capital on an expansion to support the risky LNG venture unless it can require collateral in excess of twelve months from the shippers. NBP indicates that such shippers would be non-creditworthy shippers that are located outside the U.S. and that do not have other assets.[10] NBP argues that there is no basis in the instant proceeding for the Commission to arbitrarily impose a twelve month limitation on the collateral which NBP could require for such shippers. Further, NBP argues that without the flexibility for it to negotiate with these shippers for collateral in excess of twelve months, the Commission's goal regarding infrastructure development will not be fully realized.

B. Discussion

18. The Commission is granting the requested clarification. As the Commission stated in Tennessee II, our decision in the February 28 Order with regard to the issue of how much security a pipeline can require from non-creditworthy shippers that request the construction of new facilities has been misinterpreted.[11] In the instant proceeding, NBP requested twelve months of collateral and the Commission found that "requiring twelve months of security may be acceptable in the precedent agreements leading up to the issuance of a certificate."[12] While the Commission has routinely permitted similar levels of security in pipeline expansions, we did not intend to establish a bright-line policy that security for pipeline expansions cannot exceed twelve months of service charges. Indeed, our recent decision in Calpine Energy Services v. Southern Natural Gas Company reflects this position.[13] To the extent a pipeline seeks security requirements in capacity expansions or similar proceedings that exceed 12 months of demand charges, the Commission will review the appropriateness of the security requirements in the context of the certificate application.

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[10] NBP indicates that the LNG developers seek to contract for service on NBP using new, sole purpose corporate entities without other assets.

[11] Tennessee II at Ps 27 and 28.

[12] Supra n. 1 at P 15.

[13] Calpine Energy Services v. Southern Natural Gas Company (Calpine) 103 FERC ¶ 61,273 (2003).

19. In Tennessee II, the Commission also addressed the second issue that NBP and INGAA raise, regarding the three-month collateral requirement.[14] In Tennessee II, it was explained that current Commission policy provides that the amount of collateral a particular shipper is required to provide will depend on whether the shipper is an initial subscriber or a new shipper that takes service after the facilities are placed in service. These differences reflect the relative risks faced by a company proposing to construct new facilities versus an existing pipeline. Once pipeline facilities are constructed, the major risk to the pipeline is the potential loss of reservation charges associated with the contract termination process. The Commission's established three-month collateral requirement provides the pipeline with sufficient protection against this risk. Alternatively, initial subscribers to newly constructed capacity will not have their collateral automatically reduced to three months worth of charges once the facilities enter service. Such a limited amount of collateral would not generally serve to secure the financial commitment made by the pipeline on behalf of the initial subscribers that requested construction of new mainline facilities. Since the Commission has granted clarifications request by NBP, the requests for rehearing are denied. It is unclear whether NBP and INGAA seek rehearing of the 3 month limit on collateral for post-construction new shippers. To the extent that they do, the Commission denies rehearing for the reasons discussed above, and more fully delineated in the contemporaneously issued order in PG&E Gas Transmission, Northwest Corp., Docket Nos. RP03-70-002 and -003.

IV. Compliance Filing - Docket No. RP02-363-006

A. Description of the Filing

20. On March 31, 2003, NBP submitted the tariff sheets listed in the Appendix to this order in compliance with the Commission's February 28 Order. NBP requests an effective date of February 28, 2003, concurrent with the issuance of the Commission's February 28 Order.

21. NBP modified the amount of security required from firm and interruptible shippers subscribing after the in-service date to reflect the Commission's standard of no more than three months of transportation charges. NBP also revised its tariff to provide 30 days notice of termination to a shipper that becomes non-creditworthy. Finally, if a releasing shipper's contract has been terminated, NBP's tariff provides a replacement shipper with the option of continuing service at the lower of the releasing shipper's contract rate or the maximum recourse rate, consistent with the Commission's decision in Northern Border.[15]

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[14] Tennessee II at P 28.

[15] Northern Border Pipeline Company, 100 FERC ¶ 61,125 (2002).

22. Among other things, NBP notes that the February 28 Order indicated that NBP must provide shippers with an opportunity to earn interest on prepayments. NBP states that it will comply with this requirement by paying interest on collateral prepayments (as opposed to giving shippers the option to deposit prepayment funds into an interest-bearing escrow account). NBP states that the interest rate to be paid will be the rate for one-month commercial paper (non-financial) as published in the Federal Reserve statistical Report H.15 for the month immediately ended.

23. With respect to timing for the posting of collateral, NBP states that it is declining to adopt the approach taken in Northern and Tennessee, as the Commission suggested,[16] and instead is choosing to further justify the reasonableness of its original proposal. Specifically, NBP leaves unchanged its provision that a non-creditworthy shipper shall have five business days to post acceptable collateral in an amount up to the maximum collateral that may be required by NBP, consistent with its tariff.

B. Notice, Intervention, and Protest

24. Notice of NBP's filing was published in the Federal Register (68 Fed. Reg. 17,616) with interventions, comments, and protests due by April 14, 2003. Calpine filed a motion to intervene one day out-of-time and a protest. Acceptance of Calpine's late intervention will not delay or disrupt the proceeding, or prejudice any party to it. Accordingly, for good cause shown, the Commission will accept the late intervention.

25. Calpine protests that the tariff filing does not comply with the February 28 Order in two respects. First, Calpine contends that the February 28 Order required NBP to revise its tariff to state that, once the pipeline is in operation, the security requirements from non-creditworthy shippers must be limited to three months of transportation charges. Calpine states that NBP's proposed tariff Section 12.1(b)(ii) would allow NBP to continue to require security equivalent to twelve months of transportation service charges on long-term capacity that was originally subscribed prior to the in-service date of NBP's original facilities, even after NBP's facilities have been placed into service. Calpine requests that the Commission instruct NBP to modify Section 12.1(b)(ii) so as to limit security amounts to up to three months of transportation charges.

26. Second, Calpine argues that NBP's proposed five-day time period to provide security is unjust and unreasonable and burdensome. NBP states that the Commission rejected similar proposals in Tennessee and Northern and that it should do so here as well. Calpine

[16] Supra n. 1 at P 19.

also states that five business days does not provide a sufficient amount of time for the Commission to respond to a complaint by the shipper contending that it was unfairly treated by NBP.

C. Discussion

27. NBP's revised tariff sheets partially comply with the Commission's February 28 Order, but require the following modifications.

1. Collateral Requirements

28. NBP properly revised Section 12.1(b), limiting collateral requirements for shippers that subscribe after the pipeline is in service to three months. However, it added a provision that for long-term firm capacity that was originally subscribed prior to the in-service date of NBP's original facilities, the collateral required is up to one year's worth of transportation charges. Although this provision may accurately reflect the terms of NBP's precedent agreements with its original shippers, the Commission has consistently stated that such a provision does not belong in a pipeline's tariff.[17] NBP may continue to require collateral up to one year's worth of transportation charges for its original shippers, but is directed to delete this provision from its tariff.

29. In addition, Section 12.1(b)(iv) allows a shipper to post "other security acceptable to NBP's lenders as may apply to system expansion capacity." This reference to expansion capacity is unnecessary. We are not acting to negate this provision in the precedent agreement, but reiterating that provisions related to terms agreed to in precedent agreements have no place in a tariff. NBP is directed to remove this language.

30. With respect to Calpine's protest, Calpine confuses initial subscribers for which the new mainline facilities are constructed with shippers that subscribe to take service once the facilities are in service. As we stated in Northern,[18] Commission policy provides that the amount of collateral a particular shipper is required to provide will depend on whether the shipper is an initial subscriber or a new shipper that takes service after the facilities are placed in service. Accordingly, as stated above, initial subscribers will not have their collateral automatically reduced to three months worth of charges once the facilities are

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[17] Supra n. 1 at P 15; see also, PG&E Gas Transmission, Northwest Corp., 103 FERC & 61, 137 at P 39 (2003); Trailblazer Pipeline Company, 103 FERC & 31,225 at P 68 (2003); Tennessee Gas Pipeline Company, 103 FERC & 61,275 at P 26 (2003).

[18] Northern, 103 FERC & 61,276 at P 17 (2003).

placed into service. Such a limited amount of collateral would not generally serve to secure the financial commitment made by the pipeline on behalf of the initial subscribers that requested construction of new mainline facilities.

2. Establishing Creditworthiness and Providing Security

31. NBP's revised tariff sheets still contain the requirement that a non-creditworthy shipper provide security within five business days or face suspension of service. NBP argues that our suggestion of requiring one month of transportation charges be posted within 5 days and the balance of the security within 30 days leaves the pipeline at a disadvantage, should that shipper default on its contract before providing all the required security. NBP further asserts that other standard industry contracts (e.g., the ISDA Master Agreement) require participants to post collateral in two to three business days.

32. We again find this provision potentially too burdensome. NBP has not shown that it is in the same position as other industry participants cited. Allowing a shipper more time to post collateral may increase the pipeline's risk of uncollateralized shipper default, but this risk is captured in the rate of return component of the pipeline's rates. NBP has not demonstrated the reasonableness of this proposal. It must, therefore, propose and justify the reasonableness of another timeline, or adopt the one suggested by the Commission.

3. Interest Paid on Cash Collateral

33. NBP has not demonstrated why it is appropriate to pay shippers for cash collateral NBP holds at the rate for one-month commercial paper (non-financial), as published in the Federal Reserve statistical Report H.15 for the month immediately ended. In a recent order,[19] the Commission required interest on cash collateral to be paid at the FERC interest rate, as specified in Section 154.501 of the Commission's regulations.[20] In addition, the Commission clarified in Tennessee II that the pipeline must pay interest at the FERC interest rate on funds it holds.[21] For these same reasons, NBP is directed to revise this provision to pay interest to shippers at the FERC interest rate.

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[19] e-prime, inc. v. PG&E Gas Transmission, Northwest Corporation, 102 FERC ¶ 61,289 at P 8 (2003).

[20] 18 C.F.R. § 154.501 (2003).

[21] Tennessee II, at P 21.

4. Notification of Creditworthiness Determination

34. Our February 28 Order directed NBP to provide a non-creditworthy shipper with written notification of the reasons why it was deemed non-creditworthy. NBP included this concept in its tariff revisions, but as currently written, such notification would only be provided in the limited instance when the shipper does not have a credit rating and NBP itself performs the rating and creditworthiness analysis.

35. The Commission has found that a pipeline must provide written notice to its shippers explaining the reasons why the shipper was determined to be non-creditworthy, regardless of how the determination was made.[22] NBP is directed to revise its tariff accordingly.

5. Collateral Required for Lending Service

36. The February 28 Order permitted NBP to require collateral for any gas it loans to shippers under its Park and Loan (PAL) lending service. The Commission found that "requiring a prepayment based on the value of the entire amount of gas that might be loaned over a three-month period is excessive."[23] Our order directed NBP to propose a more reasonable time period taking into account the short-term and fluctuating nature of this service.

37. NBP's new proposal would require security up to the shipper's maximum contract quantity times the average annual "SoCal" price, as reported in Gas Daily's Daily Price Survey for the preceding calendar year. NBP's PAL service is different from PAL services offered by most pipelines in that NBP's service specifies a total quantity rather than a maximum daily quantity. The Commission has previously held that a pipeline should be allowed to protect itself from the risk that the loaned gas might not be returned. Including the value of loaned gas in the collateral protects pipelines and their customers against the risk of a shipper withdrawing gas from the system without replacing or paying for it, and the pipelines' desire to obtain sufficient collateral to cover the value of the gas is reasonable. Moreover, in the event of a default, sufficient collateral will protect the other shippers on the system from being affected.[24] A collateral requirement based on the per unit price

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[22] Tennessee 102 FERC & 61,075 at P 46 (2003); Northern 103 FERC & 61,276 at P 43 (2003).

[23] Supra n. 1 at P 11.

[24] February 28 Order at P 9 (2003).

times the maximum quantity of gas the shipper may borrow is an appropriate measure of the security non-creditworthy shippers must post with NBP under its PAL service. Accordingly, the Commission finds NBP's current proposal on collateral amounts reasonable.

38. However, NBP's proposed use of a gas index may be subject to meeting the criteria of the Commission's Policy Statement in Price Discovery in Natural Gas and Electric Markets in Docket No. PL03-3-000 (Policy Statement).[25] In the Policy Statement, the Commission stated that it "will require that any prospective use of any index in its jurisdictional tariffs meet the criteria for price index developers…."[26] NBP, therefore, must make a compliance filing indicating whether its proposed price index is sufficiently reliable to meet the criteria of the Policy Statement in Docket No. PL03-3-000.

The Commission orders:

(A) NBP and INGAA's requests for clarification are granted, as discussed in the body of this order.

(B) NBP and INGAA's requests for rehearing are denied, as discussed above.

(C) The tariff sheets submitted in Docket No. RP02-363-002 and listed in the Appendix to this order are accepted, to become effective August 12, 2002, subject to the modifications discussed herein.

(D) The tariff sheets submitted in Docket No. RP02-363-006 and listed in the Appendix to this order are accepted, to become effective February 28, 2003, subject to the modifications discussed herein.

(E) NBP is directed to submit tariff revisions, as discussed in the body of this order, within 30 days of the date hereof.

By the Commission.

(S E A L)

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[25] 104 FERC ¶ 61,121 (2003).

[26] Id. at P 41.

Linda Mitry,
Acting Secretary.

Appendix

North Baja Pipeline, LLC
FERC Gas Tariff
Original Volume No. 1

Tariff Sheets Submitted in Docket No. RP02-363-002

First Revised Sheet No. 123	
First Revised Sheet No. 130	
First Revised Sheet No. 134	rejected as moot
First Revised Sheet No. 135	rejected as moot
First Revised Sheet No. 151	
First Revised Sheet No. 152	
First Revised Sheet No. 153	
First Revised Sheet No. 155	
First Revised Sheet No. 156	
First Revised Sheet No. 159	
First Revised Sheet No. 160	

Tariff Sheets Submitted in Docket No. RP02-363-006

First Revised Sheet No. 128
First Revised Sheet No. 129
Second Revised Sheet No. 130
First Revised Sheet No. 131
First Revised Sheet No. 132
First Revised Sheet No. 133
Second Revised Sheet No. 134
Second Revised Sheet No. 135
First Revised Sheet No. 136
First Revised Sheet No. 181