

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Hardy Storage Company, LLC

Docket No. CP05-150-002

ORDER AMENDING CERTIFICATE AUTHORITY

(Issued March 15, 2007)

1. On October 26, 2006, Hardy Storage Company, LLC (Hardy Storage) filed an application pursuant to section 7(c) of the Natural Gas Act (NGA) to amend the certificate issued on November 1, 2005, authorizing the development and operation of underground gas storage facilities in Hampshire and Hardy Counties, West Virginia.¹ Hardy Storage's requested certificate amendment would implement an uncontested settlement agreement, executed by Hardy Storage and all of its customers, to revise Hardy Storage's initial rates approved by the November 1, 2005 Order.² Hardy Storage also seeks amended certificate authority to change certain wells from observation wells to injection/withdrawal wells and vice versa and to modify the lines associated with these wells. In addition, Hardy Storage seeks amended certificate authority in order to operate the Lost River Reservoir and the Inkerman Reservoir on an integrated basis with an aggregate maximum storage level for the two reservoirs, rather than a maximum storage level for each reservoir.

2. As discussed below, we find that Hardy Storage's proposal to revise its initial rates is fair and reasonable and in the public interest. Therefore, we will grant the request for amended certificate authority consistent with the agreement of the parties. We also find that the public convenience and necessity require approval of Hardy Storage's request for amended certificate authority to revise the certificated use of certain wells. We will deny the request for amended certificate authority to operate the Lost River Reservoir and the Inkerman Reservoir with a combined maximum storage level, rather than individual maximum storage levels that add up to the certificated capacity for Hardy Storage.

¹ *Columbia Gas Transmission Corporation, et al.*, 113 FERC ¶ 61,118 (2005).

² The settlement agreement was executed in October 2006 by Hardy Storage, Baltimore Gas & Electric Co., Washington Gas Light Company, Piedmont Natural Gas Company and the City of Charlottesville on various dates.

I. Background and Proposals

A. Revision of November 1, 2005 Order's Approved Initial Rates

3. The November 1, 2005 Order authorizing Hardy Storage's storage facilities approved as initial section 7 rates Hardy Storage's proposed firm (Rate Schedule HSS) and interruptible (Rate Schedule IHSS) recourse storage service rates. The approved rates were based on the design capacity of the storage facility for each year during the phase-in period and the then-projected cost of service during each phase.³

4. Hardy Storage has prepared an updated cost estimate using the actual prices from contracts that Hardy Storage executed with suppliers and contractors. Hardy Storage states that costs have risen because of increased demand for skilled labor, material, and equipment. Hardy Storage asserts that this increased demand is being driven by many factors beyond its control, including repair work necessitated by Hurricanes Katrina and Rita, which hit the Gulf Coast region a few months after the cost estimate accepted in the November 1, 2005 Order was prepared; dramatically expanded oil and gas exploration and production activities nationwide and in the Appalachian region; and industry-wide pipeline integrity work, much of which must be completed by December 7, 2007, under U.S. Department of Transportation regulations.

5. Hardy Storage now estimates that the total cost of the Hardy Storage Field will be \$164 million. This represents a \$43 million increase over the \$121 million in estimated costs considered in the November 1, 2005 Order. Hardy Storage is authorized to phase in storage levels, with the Hardy Storage Field operating at 57 percent of capacity in its first year of operation (beginning in April 2007), 85 percent of capacity in its second year of operation, and 100 percent of capacity in its third year of operation.

6. Hardy Storage and all of its customers executed the October 2006 settlement agreement to address the increased construction costs in Hardy Storage's phased initial rates for the first three years of operation of the Hardy Storage Field. The uncontested settlement agreement states that it is to be effective until the date Hardy Storage files a cost and revenue study, on or before October 1, 2010.⁴ Under the October 2006

³ 113 FERC ¶ 61,118 at P11. The November 1, 2005 Order also approved Columbia Gas Transmission Corporation's (Columbia) construction of facilities and initial rates for the transportation of gas to and from Hardy Storage's facilities.

⁴ October 2006 settlement, Article 1.2. Hardy Storage proposed to begin the first phase of service in April 2007. 113 FERC ¶ 61,118 at P 10. The November 1, 2005 Order directed Hardy Storage to file a cost and revenue study at the end of its first three years of actual operation to determine whether its then-existing recourse rates are just and reasonable. *Id.* at P 43.

settlement agreement, the parties agree that during the period covered by the settlement agreement, Hardy Storage will not file under section 4 of the NGA to revise the settlement rates, except as provided by the terms of the settlement agreement, and no customer will file under section 5 of the NGA to seek a reduction in or to otherwise modify the stipulated rates. Under the settlement agreement, the phased initial rates for Hardy Storage's first three years of operation are to be based on an updated estimate of Hardy Storage's actual costs, plus applicable surcharges, including retainage, and Hardy Storage's actual cost of debt.

7. Additionally, as provided in the October 2006 settlement, Hardy Storage's Year 3 firm and interruptible recourse rates would be (a) reduced by \$0.02/Dth; (b) adjusted to reflect 100 percent of any difference between the estimated and actual costs of the contingency wells; and (c) adjusted pursuant to a sharing mechanism that will allow the parties, including Hardy Storage, to share the risks and benefits of actual differences between estimated and actual initial project costs. Specifically, the sharing mechanism provides that Hardy Storage will calculate the rate impact of the difference between actual project costs and estimated project costs. If the rate impact would be an increase, Hardy Storage will absorb 60 percent of the increase and the Year 3 rates will be increased by 40 percent of the difference between actual project costs and estimated project costs. If the rate impact would be a decrease, the Year 3 rates will be decreased by 60 percent of the difference between actual project costs and estimated project costs.

8. The October 2006 settlement provides that Hardy Storage will file tariff sheets no later than 30 days prior to the commencement of Year 1 service, and no later than 30 days prior to the commencement of Year 2 service, to incorporate Hardy Storage's actual cost of debt. The October 2006 settlement also provides that Hardy Storage will file tariff sheets to reflect the reductions in the Year 3 firm recourse rate as provided for in the settlement agreement and to set forth rates to be placed into effect on the first day of Year 3 service no later than 30 days prior to the commencement of Year 3 service. Additionally, the October 2006 settlement provides that Hardy Storage will file a reconciliation report to implement rate adjustments to reflect the rate impacts of the Risk Sharing Adjustment and the Contingency Well Adjustment on or before October 1, 2009. In order to implement these adjustments, Hardy Storage will also submit tariff sheets to apply a temporary surcharge or credit, to be effective November 1, 2009 through March 31, 2010.

9. The October 2006 settlement provides that customers may challenge the calculations contained in the reconciliation report, the categorization of costs as Initial Project Costs or as Contingency Well Costs, and the calculation of the resulting Risk Sharing Adjustment and Contingency Well Adjustment. However, customers may not challenge: (a) the prudence of Initial Project Costs or Contingency Well Costs; (b) Hardy Storage's right to implement the revised rates as of November 1, 2009; or (c) Hardy

Storage's right under the settlement agreement to collect a surcharge to collect the difference between its present rate revenues and its revised rate revenues for Year 3 of service.⁵

B. Proposed Changes in Operation of Certain Wells

10. Hardy Storage also seeks amended certificate authority to revise the use of four wells as described in and authorized by the November 1, 2005 Order. Hardy Storage states that after interpreting the results of seismic surveys and recent well testing, Hardy Storage has determined that Well 9255 and Well 9058 would serve better as observation wells than as injection/withdrawal wells. It was also determined that Well 9447 and Well 9368 would serve better as injection/withdrawal wells than as observation wells. Consequently, Hardy Storage seeks amended certificate authority to change the status of these four wells. Changing Wells 9255 and 9058 to observation wells will make unnecessary construction of the authorized 0.58-mile, 4-inch-diameter well line from Well 9255 and the 0.02-mile, 4-inch-diameter well line from Well 9058. To change Wells 9447 and 9368 to injection/withdrawal wells, Hardy Storage will need to construct an approximately 0.3-mile, 4-inch-diameter well line from Line X78-F3 to Well 9447 and an approximately 0.06-mile, 6-inch-diameter well line from Line X78-F1 to Well 9368. Hardy Storage seeks amendment of its construction authority under its certificate to accommodate these changes. Hardy Storage will construct the lines to Wells 9447 and 9368 in existing right-of-way, after removing old production-related pipe.

C. Operation of Lost River Reservoir and Inkerman Reservoir

11. The Hardy Storage project consists of two distinct storage reservoirs, Lost River Reservoir and Inkerman Reservoir. As conditioned by the November 1, 2005 Order, the maximum combined inventory in these two reservoirs in combination shall not exceed 29,600 MMcf. As further conditions, the November 1, 2005 Order provides that 17,350 MMcf shall be the maximum inventory in the Lost River Reservoir and 12,250 MMcf shall be the maximum inventory in the Inkerman Reservoir, both at 14.73 psia and 60 degrees Fahrenheit.⁶ In the instant application, Hardy Storage requests authorization to operate its storage field with no individual limits on the Lost River Reservoir and Inkerman Reservoirs so long as their combined inventory does not exceed 29,600 MMcf.

⁵ October 2006 settlement agreement at section 2.5.2.5.7.

⁶ 113 FERC ¶ 61,118 at Ordering Paragraph (J).

II. Notice and Comment

12. Notice of Hardy Storage's application for amendment of its certificate authorization was published in the *Federal Register* on November 9, 2006 (71 Fed. Reg. 65,792). Comments were due on or before November 20, 2006. The City of Charlottesville, Virginia filed comments in support of the application. No protests were filed.

III. Discussion

A. Certificate Policy Statement

13. In the November 1, 2005 Order, the Commission found that Hardy Storage's proposal satisfied the criteria for certification of new facilities set forth in the Commission's Certificate Policy Statement.⁷ The requested amendments to Hardy Storage's certificate authorization do not affect the bases for the findings supporting that conclusion. As discussed in the November 1, 2005 Order,⁸ since Hardy Storage is a new natural gas company, it has no existing customers which could subsidize the new construction, thereby satisfying the Certificate Policy Statement's threshold requirement. Since there are no existing customers, there also can be no degradation of service or other negative impacts on existing customers. Further, no service on any other pipeline will be displaced and therefore no other pipeline's customers will be adversely impacted. Rather, Hardy Storage's facilities will satisfy the increased demand for storage service by customers served by Columbia Gas Transmission Corporation (Columbia), which will transport gas to and from Hardy Storage's facilities.

14. As the Commission also found in the November 1, 2005 Order, Hardy Storage's project will confer financial and timing benefits to its customers. By converting the production field to storage prior to its total depletion, the reservoir will be able to provide a higher value service to the gas industry as a high performance storage field by delivering 176,000 Dth during periods of peak demand, as compared with an average daily output of only 5,000 Dth or less per day as a production field. Additionally, converting the approximately 5.9 Bcf of native gas remaining in the production field to storage cushion gas is an economical and efficient way to achieve the total of 17.6 Bcf of base gas required for reliable operation of the Hardy Storage Field. This difference in performance from the same reservoir (with additional facilities for storage) will have the potential for a greater positive impact on Hardy Storage's customers' financial and

⁷ *Certification of New Interstate Natural Gas Pipeline Facilities* (Certificate Policy Statement), 88 FERC ¶ 61,227 (1999), *order on clarification*, 90 FERC ¶ 61,128 (2000), *order on clarification*, 92 FERC ¶ 61,094 (2000).

⁸ 113 FERC ¶ 61,118 at PP 33-38.

operational management of their winter gas requirements. Hardy Storage has designed the storage facility in a manner which utilizes and upgrades existing facilities acquired from Columbia to enhance the new facilities that Hardy Storage is constructing. Further, being located within Columbia's system grid, Hardy Storage will improve the reliability and flexibility of Columbia's services in the Mid-Atlantic region. Finally, Hardy Storage's design of its project minimizes impacts on landowners and communities, since Hardy Storage had storage rights in the reservoir and protective acreage areas under lease and anticipates that it would need resort to eminent domain proceedings for only four percent of the approximately 500 acres of land needed for its project.

B. Revision of Initial Rates Approved by the November 1, 2005 Order

15. The November 1, 2005 Order authorizing Hardy Storage's facilities also authorized Hardy Storage to provide open-access storage services under its proposed firm Rate Schedule HSS and interruptible Rate Schedule IHSS. Since Hardy Storage's services will be phased-in, the Commission approved phased-in rates for Hardy Storage's firm storage services. The approved initial cost-based rates were based on Hardy Storage's then- estimated project cost of \$121,980,205 and then-projected annual costs of service for the first three years of operation of \$18,659,866, \$18,266,535, and \$18,574,835, respectively.

16. Based on the then-projected costs of service, the initial rates approved by the November 1, 2005 Order were: Year 1 - \$7.676 per Dth per month for firm storage service under Rate Schedule HSS and \$0.3624 per Dth for interruptible storage service under Rate Schedule IHSS; Year 2 - \$5.038 per Dth per month under Rate Schedule HSS, and \$0.2376 per Dth under Rate Schedule IHSS; and Year 3 - \$4.355 per Dth per month under Rate Schedule HSS and \$0.2062 per Dth under Rate Schedule IHSS.

17. Hardy Storage states that due to increased costs, the originally estimated total cost of Hardy Storage's project has increased to \$164 million, and its revised annual costs of service for the first three years of operation therefore have increased to \$24,671,346, \$24,136,817, and \$24,592,466, respectively. The uncontested October 2006 settlement agreement between Hardy Storage and all of its customers provides for recalculation of Hardy Storage's initial rates using these updated costs-of-service amounts, which reflect the November 1, 2005 Order's approved capital structure, return on equity, depreciation rate and cost of debt.⁹

⁹ The October 2006 settlement provides for the revised initial rates to reflect Hardy Storage's actual cost of debt. This is consistent with the November 1, 2005 Order's directing Hardy Storage to use its actual debt cost when it files to implement its initial rates for the Hardy Storage project. 113 FERC ¶ 61,118 at P 47.

18. As provided for in the October 2006 settlement, Hardy Storage's recalculated initial recourse rates are: Year 1 - \$10.205 per Dth per month under Rate Schedule HSS and \$0.4815 per Dth under Rate Schedule IHSS; Year 2 - \$6.655 per Dth per month under Rate Schedule HSS and \$0.3148 per Dth under Rate Schedule IHSS; and Year 3 - \$5.780 per Dth per month under Rate Schedule HSS and \$0.2730 per Dth under Rate Schedule IHSS, with Year 3 rates being subject to adjustment as provided for in the October 2006 settlement agreement.

19. Hardy Storage proposes to file tariff sheets at least 30 days prior to the commencement of each year of service. Hardy Storage also proposes to file a reconciliation report and tariff sheets on or before October 1, 2009. Whereas the November 1, 2005 Order directed Hardy Storage to file a cost and revenue study after its first three years of operation, which would be at the end of the storage withdrawal season in March 2010 based on Hardy Storage's plan to commence service in April 2007, the settlement agreement provides that Hardy Storage will file a cost and revenue study on or before October 1, 2010.

20. The Commission finds the October 2006 settlement to be fair and reasonable and in the public interest.¹⁰ As in previous cases, the Commission recognizes the benefits of certainty and of avoiding costly and time consuming litigation that the settlement agreement provides.¹¹ Additionally, we find that Hardy Storage's approach of sharing the costs of any overrun on the initial project costs with its customers is consistent with the Commission's determination in the Certificate Policy Statement that the risks of construction cost over-runs "should be apportioned between the pipeline and the new customers in their service contracts."¹² Accordingly, the Commission will amend Hardy Storage's initial rates and certificate authority consistent with the agreement of the parties.

C. Changes in the Operation of Certain Wells

21. As discussed above, Hardy Storage requests amended certificate authority to revise the status of four wells. As authorized by the November 1, 2005 Order, Well 9255

¹⁰ See *El Paso Natural Gas Co.*, 115 FERC ¶ 61,259 at P30. The Commission elaborated on the appropriate standard of review for uncontested settlements, explaining that it "determines whether the uncontested settlement rates are fair and reasonable and in the public interest."

¹¹ See, e.g., *Dominion Transmission, Inc.*, 111 FERC ¶ 61,285, at P30 (2005).

¹² 88 FERC ¶ 61,227 at 61,747.

and Well 9058 were to be used as injection/withdrawal wells and Well 9447 and Well 9368 were to be used as observation wells. As described above, Hardy Storage now seeks, after interpreting the results of seismic surveys and recent well testing, amended certificate authority to use Well 9255 and Well 9058 as observation wells rather than as injection/withdrawal wells, and to use Well 9447 and Well 9368 as injection/withdrawal wells rather than as observation wells. Hardy Storage seeks amended authority so that it can remove existing production-related lines and construct new lines to Wells 9447 and 9368 since it is proposing to use them as injection/withdrawal instead of as observation wells.

22. Since all of the wells at issue were previously used for gas production, there are existing lines to the wells. Hardy Storage's proposed activities to remove and construct well lines will occur in these previously disturbed rights-of-way in the area studied for purposes of the environmental assessment (EA) prepared for Hardy Storage's proposed storage project and issued on August 5, 2005 in Docket No. CP05-150-000. Hardy Storage's proposed activities to change the operation of these wells do not alter the bases for any of our findings in the EA, and the Commission will grant amended certificate authority to accommodate Hardy Storage's proposed changes.

D. Operation of the Lost River and Inkerman Reservoirs

23. As discussed above, the Hardy Storage project consists of two distinct storage reservoirs, Lost River Reservoir and Inkerman Reservoir. Pursuant to Ordering Paragraph (J) of the November 1, 2005 Order, the maximum combined inventory in these two reservoirs in combination shall not exceed 29,600 MMcf, and the individual maximum inventory limits for the Lost River Reservoir and the Inkerman Reservoir are 17,350 MMcf and 12,250 MMcf, respectively, both at 14.73 psia and 60 degrees Fahrenheit.

24. Hardy Storage requests authorization from the Commission to operate the Lost River and Inkerman Reservoirs with no individual maximum inventory limits, so long as both reservoirs' inventory does not exceed 29,600 MMcf. The maximum inventory limits imposed by the November 1, 2005 Order were based upon the reservoir characteristics and conditions as represented in Hardy Storage's application for the Hardy Storage project. Since these reservoirs have not yet been used for gas storage, Hardy Storage lacks an operational history that could provide data to indicate that, if not individually limited, the two reservoirs may be operated in an integrated manner as requested by Hardy Storage. Thus, the Commission will deny Hardy Storage's request, and maintain the condition that inventory at the Lost River Reservoir not exceed 17,350 MMcf and that inventory at the Inkerman Reservoir not exceed 12,250 MMcf, both at 14.73 psia and 60 degrees Fahrenheit.

E. Use of Certain of Hardy Storage's Pipeline Facilities by Hampshire Gas Company

25. Although Hardy Storage has not yet placed its storage facilities in service, it has leased Hampshire Gas Company (Hampshire Gas) capacity in existing pipeline facilities on the storage field property that were previously used to transport production from the now largely depleted wells being converted to storage service. Hampshire Gas has leased this pipeline capacity to transport gas for Washington Gas Light Company (WGL). On September 20, 2006, the Director of the Division of Gas Environment and Engineering of the Commission's Office of Energy Projects found that Hardy Storage was in compliance with the relevant conditions of the November 1, 2005 Order and therefore granted clearance for Hardy Storage to commence service for Hampshire Gas. In the instant application, Hardy Storage states that it, Hampshire Gas and WGL are renegotiating their agreement and that when final agreement is reached, Hardy Storage will file for any necessary authorizations to lease or transfer old production-related pipeline facilities to Hampshire Gas.

26. In view of this information, the Commission reiterates the November 1, 2005 Order's statement that any agreement for Hampshire Gas' lease of capacity in Hardy Storage's pipeline facilities must be approved by the Commission and Hampshire Gas must have a rate schedule on file with the West Virginia State Public Service Commission that it can rely on for any service using capacity leased from Hardy Storage.¹³ Since Hardy Storage indicates that it is now considering transferring facilities to Hampshire Gas, the Commission also emphasizes that prior authorization from the Commission will be necessary for Hardy Storage to effect such an abandonment of facilities. In addition, the Commission notes that while the Director's September 20, 2006 letter cleared Hardy Storage's commencement of service for Hampshire Gas under their capacity lease agreement, that clearance stated that Hardy Storage must separately request clearance to commence service for its storage customers using the pipeline facilities in which capacity is being leased to Hampshire Gas.

The Commission orders:

(A) Hardy Storage's application to amend its initial rates as authorized in the Commission's November 1, 2005 Order in this proceeding is granted, consistent with the agreement between Hardy Storage and its customers. Hardy Storage's certificate is also amended to authorize changes in operation of certain wells and the construction of associated well lines, as discussed in the body of this order. In all other respects, the certificate authorization is unchanged.

¹³ 113 FERC ¶ 61,118 at P 88.

(B) Hardy Storage's request for amended certificate authority to operate the Lost River and Inkerman reservoirs on an integrated basis is denied.

(C) Hardy Storage is directed to file actual tariff sheets to implement its revised rates no sooner than 60 days and no later than 30 days before service commences.

(D) Except as provided herein, the terms and conditions of Hardy Storage's certificate authorization granted on November 1, 2005 are unchanged.

By the Commission.

(S E A L)

Philis J. Posey,
Acting Secretary.