

120 FERC ¶ 61,245  
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.

SFPP, L.P.

Docket No. IS06-356-003

ORDER ON REHEARING

(Issued September 20, 2007)

1. On June 29, 2006, the Commission accepted, but did not suspend, SFPP, L.P.'s (SFPP) oil pipeline index filing to be effective July 1, 2006, for the index year July 1, 2006, to June 30, 2007.<sup>1</sup> The filing was made pursuant to the Commission's indexing regulations at 18 C.F.R. § 342.3 and the *Notice of Annual Change in the Producer Price Index for Finished Goods* issued on May 18, 2006.<sup>2</sup> SFPP's East Line rates were among those increased through this index filing. On December 6, 2006, the Commission granted a partial rehearing of the June 29 Order in this proceeding and required SFPP to rescind its July 1, 2006 indexed-based increase to its East Line rates.<sup>3</sup> SFPP filed a request for rehearing of the December 6 Order, which the Commission denies.

**Background**

2. In the December 2006 Order, the Commission granted rehearing on the grounds that protester Western Refining had alleged reasonable grounds under section 343.2 of the Commission's regulations to conclude that the resulting indexed East Line rates were so substantially in excess of the actual cost increases incurred by the carrier that the rate

---

<sup>1</sup> *SFPP, L.P.*, 115 FERC ¶ 61,388 (2006) (June 29 Order).

<sup>2</sup> 115 FERC ¶ 61,295 (2006).

<sup>3</sup> *SFPP, L.P.*, 117 FERC ¶ 61, 271 (2006) (December 6 Order).

increase was unjust and unreasonable. The Commission held that when new East Line rates SFPP filed in May 2006 (Docket No. IS06-283-000) became effective on June 1, 2006, those rates became the ceiling rates against which the index factor was applied on July 1, 2006.<sup>4</sup> SFPP had correctly applied the index factor for calendar year 2005 to these new East Line rates and had correctly proposed an effective date of July 1, 2006 for the indexed rates. The December 6 Order therefore held that the issue raised was whether that indexed-based increase was so substantially in excess of SFPP's actual cost increases that the resulting rates were unjust and unreasonable.

3. Examining SFPP's 2006 index filing, the December 6 Order concluded that there were no cost increases to SFPP's East Line rates in 2005 because the level of those rates was based on SFPP's actual 2005 costs and its projected East Line volumes, as adjusted to September 30, 2006, for known and measurable changes. Thus, as with all new rate filings, the new East Line rates at issue were based on the specific regulatory costs rather than industry wide inflation-driven costs. The new East Line rates were designed to recover all operating and capital costs given the throughput stated in SFPP's May 2006 rate filing, including the equity and total returns.

4. The December 6 Order therefore concluded that the additional revenue from the 2006 indexed increase of 6.15 percent would result in an over-recovery of SFPP's specific East Line costs in SFPP's May 1, 2006 filing.<sup>5</sup> The real equity return contained in that filing was 9.20 percent and the overall weighted real return was 7.80 percent. As all other 2005 East Line rate costs were covered in the new East Line rates, the application of the 6.15 percent index factor would flow directly to the return component of those rates. This increased the real equity return to 15.35 percent and the overall return to 13.95 percent.<sup>6</sup> The December 6 Order therefore concluded that additional returns of this size result in East Line rates that are not just and reasonable given that the East Line rates effective May 31, 2006, were presumed just and reasonable when filed

---

<sup>4</sup> See *SFPP, L.P.*, 115 FERC ¶ 61, 283 (2006) for the order accepting and suspending the new East Line rates SFPP filed in May 2006.

<sup>5</sup> June 29 Order at P 6.

<sup>6</sup> While the allowed regulatory return is a weighted return of debt and equity, the debt component is fixed by contract and does not change when additional revenue flows to SFPP's net income line. Thus the additional return is properly added to the equity cost component as well as the total allowed regulatory return without further weighting of the debt component.

and were based on actual 2005 costs, including the allowed equity and total regulatory returns.<sup>7</sup>

5. On rehearing SFPP asserts that the December 6 Order misapplies the Commission's indexing regulations and effectively amends them without proper notice and opportunity for hearing. It also asserts that the interpretation in the December 6 Order effectively vitiates the indexing regulations for all new rate filings. Finally, it asserts that the Commission improperly ordered refunds because it failed to suspend and investigate the indexed East Line rates at the time those rates became effective on July 1, 2006.

### **Discussion**

6. As discussed in the December 6 Order, SFPP filed its new East Line rates in May 2006 and those rates became effective on May 31, 2006. The Commission's indexing methodology provides that the index year is from July 1 to June 30. The December 6 Order squarely held that SFPP's new East Line rates fell within the index year ended June 30, 2006 and would be part of the ceiling rates for that year. Under section 342.3(d)(5), the new East Line rates filed during the index year became the ceiling rate for that year. Given this, SFPP argues that the December 6 Order arbitrarily interprets section 343.2(c)(1) in a way that creates a direct conflict with section 342.3(d)(5) of the Commission's indexing methodology. It argues that the cost of service justification for its new 2005 East Line rates was its 2004 calendar year costs. Thus, the practical effect of the December 6 Order is to hold that any increase in a ceiling rate for any rate filed in the first half of 2005 would necessarily be unjust and unreasonable. It asserts this would be true for any new rate filed during the index year since such a rate would be supported by a cost of service year that abuts or overlaps the year in which the ceiling rate applied. Thus, a pipeline would always be denied the inflation increase due it under the Commission's indexing regulations. It therefore argues that the December 6 Order undercuts the indexing regulations and amends section 342.3(d)(5) without a rulemaking proceeding, including a notice and opportunity for comment.

7. There are two answers to this argument. First, it is not true in practice given some of SFPP's recent filings and the Commission's response. On April 28, 2005, SFPP filed tariff SFPP FERC No. 111 in Docket No. IS05-230-000 establishing new interstate cost-

---

<sup>7</sup> Under the Interstate Commerce Act newly filed rates are presumed just and reasonable because they are presumed to be based on the carrier's costs. This presumption does not relieve the carrier of its burden to prove that new rates are in fact just and reasonable if the filing is protested and the case proceeds to hearing.

of-service rates for shipping of petroleum products on its North Line between Richmond, California, and Reno, Nevada. The Commission accepted and suspended the proposed tariff, effective June 1, 2005, and set the case for hearing.<sup>8</sup> On May 31, 2005, SFPP filed in Docket No. IS05-327-000 to index all of its rates pursuant to the Commission's annual indexing methodology, including the revised North Line rates. The Commission accepted this second 2005 filing subject to refund on June 29, 2005.<sup>9</sup>

8. Relying on the December 6 Order, several shippers filed complaints in Docket Nos. OR07-3-000 and OR07-6-000 asserting that SFPP's various filings to increase its North Line rates raised the same issues discussed in the December 6 Order, *i.e.*, that SFPP's indexing of the North Line rates in 2005 and 2006 resulted in an increase so substantially in excess of SFPP's actual cost increase that the resulting rate was unjust and unreasonable. SFPP answered that even with the indexed-based increase in July 2005, the resulting rates yielded revenues that would not recover the cost of service that underpinned its new June 29, 2005 North Line rates. Thus, it argued, the resulting rates could not be unjust and unreasonable since SFPP was not recovering its costs.

9. The Commission accepted this argument and dismissed the complaints.<sup>10</sup> SFPP's position in the cited North Line complaint dockets, and the outcome, belies its argument here that interpretation in the December 6 Order will always deprive a pipeline of its inflation increase. Moreover, SFPP's more general assertions are inconsistent with basic math. If a pipeline files a new rate in September of the index year (September 2005) and chooses to use the calendar year 2004 as the test year for its cost of service, it would receive a full year's index in July 2006 by comparing the increase in costs in 2005 over the 2004 test year it used to justify its cost of service. In any event, the December 2006 Order does not preclude adopting a proportional increase where the facts suggest that would be an appropriate solution.

10. The result in the North Line complaint cases further demonstrates that the Commission did not *de facto* amend its indexing regulations without notice and opportunity for comment. As explained in the December 2006 Order, the hallmark of the

---

<sup>8</sup> *SFPP, L.P.*, 111 FERC ¶ 61,299 (2005).

<sup>9</sup> *SFPP, L.P.*, 111 FERC ¶ 61,510 (2005), *order on reh'g*, 113 FERC ¶ 61,253 (2005).

<sup>10</sup> *BP West Coast Products, LLC, et al. v. SFPP, L.P.*, 118 FERC ¶ 61,261 (2007).

Commission's indexing system is simplicity.<sup>11</sup> This is because the indexing approach allows rates to be changed without a detailed and comprehensive presentation and examination of the individual pipeline's cost of service in each case.<sup>12</sup> By this means pipelines are able to adjust rates to just and reasonable levels for inflation-driven costs without the need for strict regulatory review of the pipeline's individual cost of service.<sup>13</sup> In fact, under this regulatory regime some divergence between the actual cost changes experienced by individual pipelines and the changes permitted by the index is inevitable.<sup>14</sup> Moreover, the Commission uses Page 700 of FERC Form No. 6 as a screen to compare aggregate revenues, costs, and volumes in one year with the subsequent year. While the indexing method is an efficient method to recover the inflation-driven cost increases occurring in a given year, it is not normally adequate to determine whether any specific rate is just and reasonable and a complaint must normally be filed to challenge the increase to a specific rate. However, as the Commission explained in the December 6 Order, these rates involved only a single line and one cost of service. As such, the analysis here is a mathematical one based on known cost factors specific to the service at issue.<sup>15</sup> As such, the Commission did not improperly amend its regulations, but construed them to deny an increase that would result in an unjust and unreasonable rate given the context of SFPP's East Line 2006 index filing.

11. Second, the result here provides administrative efficiency. As previously discussed, the Commission's indexing methodology normally requires a complaint to attack the cost factors, and thus the level, of the individual rate. However, in this case the return embedded in the rate, and presumed to be just and reasonable until further action

---

<sup>11</sup> Order No. 561 at 30,948. *Revisions to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, FERC Stats. & Regs., Regs. Preambles January 1991- June 1996 ¶ 30,985 (1993), 58 Fed. Reg. 58753 (Nov. 4, 1993), Order No. 561; *order on reh'g*, Order 561-A, FERC Stats. & Regs., Regs. Preambles January 1991- June 1996 ¶ 31,000 (1994), 59 Fed. Reg. 40242 (Aug. 8, 1994); *aff'd*, *Association of Oil Pipe Lines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996); *aff'd* *Association of Oil Pipe Lines v. FERC*, 281 F.3d 239 (D.C. Cir. 2002) *order on remand*, *Five-Year Review of Oil Pipeline Pricing Index*, 102 FERC ¶ 61,195 (2003).

<sup>12</sup> *Id.* 30,946.

<sup>13</sup> *Id.* 30,948.

<sup>14</sup> *Id.* 30,949.

<sup>15</sup> *See* SFPP, L.P., 111 FERC ¶ 61,510 (2005); SFPP, L.P., 107 FERC ¶ 61,334 (2004); SFPP, L.P., 102 FERC ¶ 61,344 (2003); SFPP, L.P., 96 FERC ¶ 61,332 (2001).

by the Commission, is specifically known. If the index methodology is applied in these circumstances, an unjust and unreasonable rate results because the resulting return substantially exceeds that which SFPP itself states is just and reasonable in its own cost filing. Moreover, while the new 2006 underlying East Line rates are subject to suspension and might be reduced, the mathematical problem here remains even if the base rate were reduced. This would virtually compel a subsequent complaint by the complaining shippers, and one that would have a good probability of success because the 2006 index increase would have resulted in a return notably greater than the one embedded in the initial filing. It is simpler to address the matter here given that the resulting rate levels have returns that would support accepting a complaint on its merits. Here the goal of administrative efficiency embedded in the indexing methodology works against itself and does not justify SFPP's retaining a regulatory windfall.<sup>16</sup>

12. Finally, SFPP argues that the Commission improperly ordered refunds in this proceeding. It asserts that the Commission may not do so because it failed to suspend SFPP's 2006 index in the relevant June 29 Order. This argument is specious. The Commission's indexing regulations provide that if the underlying rates are under investigation and subject to refund, any increase under an index filing is subject to refund. The December 6 Order clarified this point even though it was not necessary given the literal structure of the indexing regulations.<sup>17</sup> Since SFPP's 2006 new East Line rates are subject to suspension, investigation, and refund, the index component of those rates would be also. For the reasons stated, SFPP's request for rehearing is denied.

The Commission orders:

SFPP's request for rehearing is denied for the reasons stated in the body of the order.

By the Commission

( S E A L )

Nathaniel J. Davis, Sr.,  
Acting Deputy Secretary.

---

<sup>16</sup> Cf. *BP West Coast Products v. FERC*, 374 F3d. 1263 at 1294 (2004).

<sup>17</sup> See 18 C.F.R. § 342.3(a) (2007) and Order No. 561, *supra* and December 2006 order at P 7.