149 FERC ¶ 61,030
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Cheryl A. LaFleur, Chairman;
Philip D. Moeller, Tony Clark,
and Norman C. Bay.

Transcontinental Gas Pipe Line Corporation	Docket Nos. RP06-569-008 RP07-376-005 (consolidated)

ORDER REQUESTING BRIEFS AND ESTABLISHING SETTLEMENT JUDGE PROCEDURES

(Issued October 16, 2014)

1. On February 21, 2014, the United States Court of Appeals for the District of Columbia Circuit (Court) issued an opinion in *BNP Paribas Energy Trading GP v. FERC*,[1] vacating and remanding the Commission's decision to accept Transcontinental Gas Pipe Line Corporation's (Transco)[2] proposal to charge BNP Paribas Energy Trading GP (Paribas)[3] and South Jersey Resources Group, LLC (South Jersey) (collectively, replacement shippers) a new incremental rate for service under Rate Schedule Washington Storage Service-OA service, higher than the rate paid by Transco's historic shippers. Specifically, the Court held that the Commission failed to offer a reasoned basis for its decision to accept Transco's incremental rate proposal. As discussed below, the Commission establishes a paper hearing on the issues raised by the Court, suspends the briefing schedule on these issues, and establishes settlement judge procedures for the parties.

[1] 743 F.3d 264 (2014) (*BNP Paribas*).

[2] Transco has since changed its name to Transcontinental Gas Pipe Line Company, LLC.

[3] *Transcontinental Gas Pipe Line Corp.*, 130 FERC ¶ 61,043 (2010) (Opinion No. 507), *reh'g denied*, 139 FERC ¶ 61,002 (2012) (Opinion No. 507-A). In the underlying proceedings at the Commission, the Commission used the name Fortis Energy Marketing & Trading GP or "Fortis" because that was the previous name of the company Paribas before it changed its name. However, because the Court uses the name "Paribas" in *BNP Paribas*, the Commission will also use this name when referring to the company.

I. Background

A. Proceedings Before the Commission

2. A full discussion of the background of these proceedings and the establishment of the Washington Storage Field was included in Opinion No. 507 and Opinion No. 507-A. Therefore, we will not repeat those discussions at length herein.

3. Transco's Washington Storage Service originated in the mid-1970s. On February 26, 1975, the Commission approved a Settlement (1975 Settlement) proposed by Transco and issued a certificate to provide individually certificated contract storage service at the Washington Storage Field under Rate Schedule WSS.[4] At that time, Transco faced severe supply problems, and its curtailment of service to its high priority industrial customers had "reached extraordinary proportions."[5] The Commission found that development of the Washington Storage Field was the best available means of providing extra volumes of gas during the winter heating season.

4. The 1975 Settlement provided that Transco's customers desiring WSS service would provide the base gas volumes necessary to support their top gas storage capacity entitlements.[6] As agreed to in the settlement, section 9.1 of the Rate Schedule WSS provided that Transco would inform each WSS customer (historic shipper) of the quantity of base gas to be supplied by that customer for each increment of its storage capacity. Each historic shipper would then supply the required base gas volumes from volumes that would otherwise be available to it for purchase under Transco's then existing bundled firm sales rate schedules. The customers' firm entitlements to purchase gas would be temporarily reduced by the amount of base gas being supplied, coupled with a credit to their sales reservation charges. In addition, pursuant to the 1975 Settlement, section 9.5 of Rate Schedule WSS provided that Transco would be the owner of the base gas injected into the Washington Storage Field (and incur the gas purchase cost), but the historic

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[4] *Transcontinental Gas Pipe Line Corp.*, 53 FPC 628 (1975) (*Transco*). Amendments to Rate Schedule WSS were subsequently authorized by the following orders: 56 FPC 1351 (1976); 58 FPC 1960 (1977); 1 FERC ¶ 61,172 (1977); 4 FERC ¶ 61,271 (1978); 6 FERC ¶ 61,232 (1979); 11 FERC ¶ 62,003 (1980); 12 FERC ¶ 62,287 (1980); 16 FERC ¶ 62,212 (1981).

[5] *Transco*, 53 FPC at 631.

[6] *Id.* at 630; *see also Transcontinental Gas Pipe Line Corp.*, 87 FERC ¶ 61,184, at 61,704 (1999) (1999 Conversion Order).

shippers would have the right to purchase their respective share of the base gas at historical cost from Transco at the time the customer terminated service from the field.[7]

5. Transco injected the original base gas volumes into the Washington Storage Field, consistent with these provisions of the 1975 Settlement and the WSS Rate Schedule. Transco expanded the capacity of the storage field several times between 1975 and 1981, each time buying gas that the historic shippers had been entitled to take themselves and giving those shippers the right to repurchase the gas at historic cost on terminating service.[8] On the above occasions, Transco's costs were rolled into its rate base.

6. After its Order No. 636 restructuring proceeding, Transco continued to provide only an individually certificated, non-open access service at its Washington Storage Field until 1998. In 1998, Transco proposed to implement a new Rate Schedule WSS-OA to permit its shippers to convert from the existing Rate Schedule WSS firm storage service to open access service at the Washington Storage Field under Transco's blanket certificate and Part 284 of the Commission's regulations. The Commission accepted that proposal subject to various modifications.[9] As finally approved, Transco's proposal allows each historic WSS customer, including those converting to WSS-OA service, to retain its existing right to repurchase the specific volume of base gas that it supplied as part of the development of the Washington Storage Field if the customer terminated service from the field. New WSS-OA customers are not required to supply base gas, but in turn, these shippers do not have the WSS base gas repurchase rights that historic shippers possess under the tariff.[10] Transco's tariff provides that it has an ongoing obligation to maintain sufficient base gas to support the total top gas requirements of its customers.

7. Because Transco's Washington Storage Field is fully subscribed, the need to purchase base gas would only arise if one of the field's historic shippers exited the field

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[7] *See Transco*, 53 FPC at 630. This base gas arrangement was listed in section 9.1 and section 9.5 of Transco's then existing WSS tariff on file with the Commission.

[8] A certificate for the final increase in top gas storage capacity was issued to Transco for the Washington Storage Field on September 30, 1980, increasing its capacity to 75 million Mcf. *See Transcontinental Gas Pipe Line Corp.*, 12 FERC ¶ 62,287 (1980). The total top gas storage capacity, and thus the total base gas required to support that capacity, have remained unchanged since the completion of that expansion.

[9] *Transcontinental Gas Pipe Line Corp*., 85 FERC ¶ 61,119 (1998), *order on reh'g*, 87 FERC ¶ 61,184 (1999).

[10] *Id.* at 61,707-61,708.

along with its share of base gas along with the arrival of a replacement shipper at the field. However, if a historic shipper withdrew its base gas entitlement from the Washington Storage Field and no replacement shipper sought to take that shipper's place, Transco would not automatically be required to purchase base gas.

8. During the period 2005-2006, two of Transco's historic shippers permanently released their Washington Storage Field rights. PSEG Energy Resources and Trade (PSEG) released its capacity to Paribas, and South Jersey Gas Company (South Jersey Gas) released its capacity to its affiliate, South Jersey. Both PSEG and South Jersey Gas also exercised their right to purchase approximately 3.4 million Dekatherms (Dth) of base gas at its historic cost of approximately $0.89 per Dth. At this time, the price of gas was approximately $6.00 per Dth. To support the top gas needs of its shippers at the Washington Storage Field, Transco purchased approximately 3.4 million Dth of base gas.

9. On August 31, 2006, Transco filed a NGA general section 4 rate case in which it proposed, among other things, new bifurcated tariff rates for service at its Washington Storage Field. The historic shippers would continue to pay a rate based on their proportionate share of the historic base gas and the replacement shippers would pay an incremental rate based on the cost of replacing 3.4 million Dth of natural gas. Transco and the parties settled the proceeding except for the issues related to the appropriate rate treatment for the cost of replenishing the base gas for Paribas and South Jersey. These issues were the subject of hearing in July 2008 before the presiding Administrative Law Judge (ALJ).

10. On November 21, 2008, the ALJ issued a decision and certified that decision to the Commission.[11] With regard to Transco's NGA general section 4 rate proposal, the ALJ ruled that Transco's incremental rate proposal was not a just and reasonable method to allocate costs for the replenishment of base gas at the Washington Storage Field. Specifically, the ALJ reasoned that all base gas serves the top gas deliverability of all shippers; therefore, it was impossible to attribute any portion of base gas to any one or more customers other than pro rata according to each customer's top gas volume. In addition, the ALJ stated that the principle of cost causation supported the imposition of rolled-in rate treatment for the replenishment of the base gas for both historic and incremental customers receiving storage service for Transco's Washington Storage Field, because no one customer's top gas requirement can be said to cause more base gas cost than any other customer's. Accordingly, the ALJ held that Transco's incremental rate proposal violated section 4 of the NGA because it was unlawfully discriminatory against the replacement storage customers.

[11] *Transcontinental Gas Pipe Line Corp.*, 125 FERC ¶ 63,020 (2008).

11. Several parties filed exceptions to this decision with the Commission. In Opinion No. 507, the Commission reversed the ALJ's decision,[12] and in Opinion No. 507-A,[13] the Commission denied Paribas and South Jersey's request for rehearing of Opinion No. 507. The Commission stated that, under the statutory scheme set forth in the NGA, the pipeline has the initiative through a section 4 filing to propose how it will recover its costs and, if the pipeline shows that its proposed rates are just and reasonable, the Commission must accept those rates, regardless of whether other just and reasonable rates may exist.[14] The Commission also pointed out that in *ConEd* the court recognized that, "while incremental treatment may be required at one end of the rate-setting continuum, and rolled-in pricing required at the other, in between the two extremes lie a series of intermediate points in which both these recovery methods would satisfy section 4's just and reasonable test."[15] The Commission found that Transco had satisfied its section 4 burden to show that its proposed incremental rates were just and reasonable, and therefore, the Commission accepted Transco's proposal.

12. The Commission rejected Paribas and South Jersey's contention that Transco's use of an incremental rate base is contrary to the ratemaking principle set forth in *KN Energy* that "all approved rates reflect to some degree the costs actually caused by the customer who must pay them."[16] The Commission stated that, as is generally true in cases involving a choice between incremental and rolled-in rates for integrated pipeline services, this case presented alternative methods of analyzing cost causation, depending upon whether the focus is on the pipeline's operations or on the events enabling each customer to join the system. On the one hand, because Transco operates the Washington Storage Field on an integrated basis, all base gas injected into the field serves the top gas deliverability needs of all WSS/WSS-OA customers, regardless of when each shipper joined the system. On the other hand, the Commission stated, the permanent capacity releases to Paribas and South Jersey were the "most immediate and proximate" cause of

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[12] *Transcontinental Gas Pipe Line Corp.*, 130 FERC ¶ 61,043 (2010) (Opinion No. 507).

[13] *Transcontinental Gas Pipe Line Corp.*, 139 FERC ¶ 61,002 (2012) (Opinion No. 507-A).

[14] *See Western Resources, Inc. v. FERC*, 9 F.3d 1568, 1578-1579 (D.C. Cir. 1993), and *Consolidated Edison Co. v. FERC*, 165 F.2d 992 (D.C. Cir. 1999) (*ConEd*).

[15] *Id*.

[16] *KN Energy, Inc. v. FERC*, 968 F.2d 1295, 1300 (D.C. Cir. 1992).

Transco's need to purchase new base gas in 2005 and 2006.[17] Those releases enabled PSEG and South Jersey Gas to exercise their right to purchase the approximately 3.4 million Dth of base gas attributable to them, thereby requiring Transco to purchase replacement base gas so that it could serve the top gas deliverability rights transferred to Paribas and South Jersey.

13. The Commission stated that, because these alternative analyses of cost causation are both factually accurate, the relative weight to be given to each in resolving the rolled-in versus incremental rate issue turns on equitable factors and other public interest considerations. The Commission held that equitable factors supported Transco's proposed incremental rates. These included the fact the historic shippers provided essential support for Transco to proceed with the Washington Storage Field by providing the necessary base gas out of their gas purchase entitlements during a period of severe gas shortages. In addition, PSEG and South Jersey Gas' capacity releases to Paribas and South Jersey did not improve the quality of the historic shippers' service. The historic shippers received the same service before and after the base gas injections required by PSEG and South Jersey's exit from the system.

14. Similarly, the Commission found that it was not unduly discriminatory for Transco to charge the replacement shippers a different rate from the historic shippers. The Commission held that the two customer classes were not similarly situated because the historic shippers, unlike the replacement shippers, had contributed base gas for Transco's use necessary for the establishment and expansion of the storage field.

15. Finally, the Commission rejected Paribas' and South Jersey's argument that the Commission's approval of Transco's incremental rate proposal is inconsistent with its policy concerning the interconnection of new electric generation resources to the existing transmission network. The Commission stated that policy is not relevant to this case, because the resolution of this case turns on equitable considerations arising from the unique circumstances concerning the development of the Washington Gas Storage Field during a period of severe gas shortages.

B. <u>Proceedings Before the Court of Appeals</u>

16. Paribas appealed Opinion Nos. 507 and 507-A to the Court and South Jersey intervened in support of Paribas' appeal.

17. In *BNP Paribas*, the court vacated and remanded the Commission's underlying decisions. Specifically, the Court stated that the Commission failed to explain:

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[17] Citing the statement in *KN Energy* that the Commission traditionally focuses on "the most immediate and proximate cause of the cost incurred." *See id.* at 1302.

> how its decision manifested the cost causation principle. It particularly failed to explain how or why or in what sense the historic customers' *continued demand* did not share, *pro rata*, in causing the need for the new base gas, or, to put the same issue in terms that the Commission often treats as equivalent, how or what or in what sense the historic customers did not share proportionately in the benefits provided by the new base gas.[18]

The Court found two flaws in the Commission's rationale for holding that Transco's proposed incremental rates were consistent with the principle of cost causation, that the Court described as requiring that rates reflect to some degree the costs actually caused by the customer who must pay them.

18. First, the Court found that the Commission had not supported its finding that the case presents two factually accurate methods of analyzing cost causation, depending on whether the focus is on the pipeline's operations or on the events enabling each customer to join the system.[19] The Court was not persuaded that the exiting historic shippers' releases to the replacement shippers could be viewed as the most immediate and proximate cause of Transco's need to purchase base gas to be able to serve the replacement shippers. The Court explained,

> [o]n its face, this alternative focus on the exiting shippers' release doesn't seem to support the Commission's idea that the *replacement shippers'* demand is *the* cause of the need for the additional 3.4 million dekatherms of base gas. It still places the replacement shippers in the position of any new customer whose demand, *coupled with that that of the prior customers,* necessitates some new investment. Thus the Commission's characterization of *both* alternative views as "factually accurate" seems highly questionable.[20]

As a result, the Court found the Commission's "chosen bridge to reliance on equity is shaky."[21]

19. Second, the Court held that the Commission had failed to explain why the historic customers' earlier support for the project, which left them entitled to buy back their gas

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[18] *BNP Paribas,* 743 F.3d at 266.

[19] *Id*. at 268.

[20] *Id.* (emphasis in original).

[21] *Id*. at 269.

and resell it at current prices, gives them a special equitable claim in perpetuity. The Court stated,

> [e]quity's conscience is famously "as long as the chancellor's foot"; to reconcile its use with the APA's rejection of arbitrariness requires both that the justification for shifting to "equity" and the reasons that make an outcome equitable be set forth with clarity and logic. They are missing here, and the Commission doesn't really advance its judgment that the replacement shippers' demand can be viewed as the sole cause of the base gas need by pinning on that demand the undefined label "immediate and proximate cause."[22]

20. Next, the Court asserted the Commission failed to address a specific point raised by Paribas in the proceeding regarding the Commission's general policy in the electric sector of requiring rolled-in cost allocation for network upgrade costs. The Court indicated that Paribas had argued that the Commission's decision in the Transco proceeding was inconsistent with its application of the cost causation principles in the electricity sector when integration of a new electricity generator requires upgrades to the transmission network.[23] The Court stated that Paribas had argued before the Commission that the Commission in those cases inquires whether the upgrade benefits all users of the grid or just the additional generator, and does not require the new generator to bear costs incurred for the development of equipment that benefits all users of the network.[24] The Court stated that, instead of addressing this inconsistency, the Commission stated that the matter was not relevant to the facts of this proceeding. The Court stated that Transco, in support of the Commission's underlying orders, suggested that the failure of the Commission to address this inconsistency is immaterial because the Commission permits incremental rates in network upgrades in certain circumstances. Nevertheless, the Court found that, even assuming the circumstances for allowing incremental rates are present here, the Commission did not address the issue and allow Paribas to argue against the

[22] *Id.*

[23] Paribas cited *Midwest Indep. Transmission Sys. Operator and the Midwest ISO Transmission Owners*, 129 FERC ¶ 61,060, at PP 53-56 (2009); *Standardization of Generator Interconnection Agreements and Procedures*, Order No. 2003, FERC Stats. & Regs. ¶ 31,146 (2003), *order on reh'g*, Order No. 2003-A, FERC Stats. & Regs. ¶ 31,160, at PP 585-586, *order on reh'g*, Order No. 2003-B, FERC Stats. & Regs. ¶ 31,171 (2004), *order on reh'g*, Order No. 2003-C, FERC Stats. & Regs. ¶ 31,190 (2005), *aff'd sub nom. Nat'l Ass'n of Regulatory Util. Comm'rs v. FERC*, 475 F.3d 1277 (D.C. Cir. 2007); and *Public Serv. Co. of Colorado*, 62 FERC ¶ 61,013, at 61,061 (1993).

[24] *BNP Paribas*, 743 F.3d at 269-270.

applicability of incremental rates in this case. The Court stated that it was not suggesting that the Commission regulates, or should regulate, the natural gas and electric industries identically because it often does not. However, the Court stated that the Commission must point to distinguishing factors and not dismiss a material argument.

21. Finally, the Court opined that, although it was vacating and remanding the Commission's decision, it was not suggesting that the Commission should ignore the complex history of the Washington Storage Field in its deliberations.[25] The Court then stated:

> [t]he historic shippers have consistently refrained from leaving the field and reaping the potential windfall from exercising their contingent option to purchase their share of the base gas. By so refraining, they annually incur, as a cost of continuing to take service, the foregone return on the proceeds of selling that gas. It may be that the Commission could, consistent with regarding all shippers as causing the need for the purchase of additional base gas in proportion to their use of the field, nevertheless require the replacement shippers to pay the incremental cost, while allowing the historic shippers to pay the previously calculated rate and continue to forego the annualized return from exercise of their buy-back option. If this analysis is correct, such a rate treatment could subject all shippers to similar incentives for similar use of the field.[26]

The Court stated, however, that because the Commission did not broach such an inquiry, it would be improper for the Court to adopt it.

C. <u>The Parties' Post-Remand Pleadings</u>

22. On June 6, 2014, Paribas filed a motion (June 6 filing) requesting that the Commission issue an order on remand directing payment of refunds and other relief consistent with the Court's order vacating and remanding Opinion Nos. 507 and 507-A. Paribas specifically requests that the Commission: (1) affirm, in all respects, the ALJ's decision in the Initial Decision that Transco's proposed direct allocation of base gas purchase costs to Paribas and South Jersey is unlawful; and (2) direct Transco to make the immediate payment of full refunds, with interest per the Commission's regulations to Paribas and South Jersey.

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[25] *Id*. at 270.

[26] *Id.*

23. On June 23, 2014, South Jersey filed an answer supporting Paribas' June 6 filing and further requesting that the Commission direct Transco to revise its WSS-OA Rate Schedule by removing the incremental rates for the replacement shippers. On June 23, 2014, Transco[27] and the WSS Customer Group both filed in opposition to Paribas' June 6 filing. On July 8, 2014, South Jersey filed a motion to reply to Transco's opposition.[28]

II. Discussion

24. Before we issue an order on remand, the Commission reopens the record for the purpose of allowing the participants in this proceeding an opportunity to present written evidence and argument concerning the issues raised by the court's decision. In particular, the Commission is interested in hearing the parties' views on: (1) the court's alternate theory by which Transco's incremental rate proposal might be found just and reasonable; and (2) the consistency of Transco's incremental rate proposal with Commission policy concerning incremental rate treatment of electric network upgrades. However, in order to give the parties an opportunity to settle the issues raised by the Court's remand, the Commission suspends the briefing schedule on these issues, and establishes settlement judge procedures. If the settlement procedures are unsuccessful, interested participants are directed to file briefs on the issues listed below within 60 days of the date the Chief Administrative Law Judge terminates the settlement procedures and reply briefs are due within 90 days of the termination of settlement procedures.

A. Alternative Method(s) for Finding Incremental Rates Just and Reasonable

25. As described above, at the end of its decision, the Court stated it was not suggesting that the Commission should ignore the complex history of the Washington Storage Field. The Court then posited an alternate theory by which the Commission might have found Transco's incremental rate proposal just and reasonable. The Court suggested that, by refraining from exercising their base gas purchase rights, the historic shippers annually incur, as a cost of continuing to take service, the foregone return on the proceeds of selling that gas. As a result, it may be that, consistent with regard to all shippers causing the need for the purchase of additional base gas in proportion to their

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[27] Transco asserts that it has been authorized to state that the Transco Municipal Group, an active party to the proceeding, supports incremental rates for the replacement shippers and the instant opposition filed by Transco.

[28] Rule 213(a)(2) of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.213(a)(2) (2014)) prohibits answers unless ordered by the decisional authority. In this case, the Commission will accept South Jersey's answer because it has assisted the Commission in our decision-making process.

use of the field, the Commission could require the replacement shippers to pay the incremental cost, while allowing the historic shippers to pay the previously calculated rate *and* continue to forego the annualized return from exercise of their buy-back option.

26. In its June 6 filing, Paribas asserts that the Court's analysis was not broached by the Commission or any party and is inapplicable to the factual record and issues presented in the proceeding. First, Paribas argues that the "foregone return" is not a cost of continuing to take service because historic customers have no ability to exercise the purchase option while also taking service. Paribas asserts that the purchase option is exercisable only when the contract ends and is controlled by the contract term and not the customers. Paribas contends, therefore, that "refraining" from exercising the purchase option is not an opportunity cost to historic customers of taking storage service; rather, they are both incidents of the historic customer having an effective storage service contract in place. Next, Paribas argues that, in reality, the existence of the purchase option can only be viewed as a massive, deferred rate discount that is enjoyed solely by the historic shippers when their service is terminated. Paribas states that the value of this benefit varies over time with the movement of gas prices in the gas commodity market.

27. Transco responds that the Court correctly observed that, because of the arrangements made under the 1975 Settlement, the historic shippers have incurred and will continue to incur as long as they continue to take service under Rate Schedule WSS a significant opportunity cost related to the unrealized gain on the base gas they contributed to the field. Transco argues that Paribas erroneously contends that the historic shippers face no such opportunity cost because historical customers have no ability to exercise the purchase option while also taking service. In fact, Transco states it is precisely because the choice to continue service forecloses exercise of the purchase option that the foregone gains on the historic customers' shares of the base gas are an opportunity cost attributable to continuing their Washington Storage Field service.

28. The WSS Customer Group argues that historic shippers have incurred opportunity costs in maintaining their Washington Storage Field service over a period of more than 30 years and in not exercising their base gas repurchase rights during that period. Moreover, the WSS Customer Group states that, since the inception of service, historic customers have foregone their right to purchase their base gas entitlements and have paid Transco's rate of return, plus associated income tax, on that base gas which is not subject to depreciation. Because Paribas and South Jersey have not paid these costs, the WSS Customer Group claims that they are not similarly situated and have not incurred these opportunity costs.

29. While the Court vacated and remanded our approval of Transco's incremental rate proposal, it also made clear that, on remand, we should not ignore the complex history of the Washington Storage Field, and the Court also suggested an alternative analysis that might justify approval of Transco's proposal. The pleadings filed by the parties raise factual and other issues concerning the Court's alternative analysis which the

Commission finds should be addressed in a paper hearing where all participants will have an opportunity to present written evidence and argument.

30. The Court's alternative analysis focuses on the historic shippers' *current* decisions not to leave Washington Storage Field and exercise their contingent option to purchase their share of the based gas, rather than the historic shippers' past support for the project in the late 1970s and early 1980s. Paribas contends that the Court's analysis is incorrect, asserting that the historic shippers have no current ability to leave the field until their existing contracts expire. By contrast, Transco and the WSS Customer Group argue that the historic shippers are incurring a current opportunity cost, as the court suggested. The participants' written evidence and argument should address all issues relevant to the Court's alternative analysis, including whether the historic shippers are incurring a current opportunity cost and, if so, how that fact supports Transco's incremental rate proposal. Among other things, participants should address whether South Jersey Gas' 2005 capacity release to its marketing affiliate South Jersey, enabling South Jersey Gas to exercise its contingent purchase option, supports a finding that the other historic shippers are incurring a current opportunity cost by refraining from taking a similar course. In addition, Transco and the WSS Customer Group should specify when the current terms of each of the historic WSS customers' contracts expire and therefore, give them the opportunity to terminate those contracts.

B. Consistency with Electric Policy Concerning Incremental Rates

31. As referenced above, the Court stated the Commission failed to address a material argument raised by Paribas on the difference in the way the Commission treated the replacement shippers and how it treats new electric generators seeking to connect to an existing transmission network. The Court stated, "when Paribas pointed out the apparent inconsistency between FERC's action here and its management of the electricity sector the Commission brushed it off as not relevant to this case."[29] The Court also noted that Transco, intervening in support of the Commission, suggested that there was no inconsistency because the Commission permits incremental rates for electric network upgrades in certain circumstances. However, the Court stated that the Commission did not rely on that rationale for rejecting Paribas' reliance on its analogy to the Commission's electric network upgrade policy, and therefore, the Commission's decision could not be affirmed on that basis.

32. In its June 6 filing, Paribas states that it has explained and the Court has agreed that the Commission treated similarly situated parties differently. Paribas argues that the Commission has made a policy determination that the costs of new electric transmission upgrades should be allocated to all users of the network, and that doing so is consistent

[29] *BNP Paribas*, 743 F.3d at 269.

with the Commission's basic cost causation and allocation principles. Therefore, Paribas avers that the same principles should be applied in this proceeding to preclude Transco from allocating base gas costs on a selective basis to the replacement shippers when all Washington Storage Field customers benefit equally from the purchase and use of that base gas.

33. In its opposition, Transco states that Paribas' June 6 filing repeats the incorrect assertion that the Commission erred because it did not reconcile its acceptance of Transco's incremental rates, which assigned the cost of base gas to the replacement shippers, with its policy of permitting rolled-in rate treatment for the cost of electric transmission upgrades when those upgrades are required for the interconnection of new electric generation facilities. Transco states that, while the Court found in *BNP Trading* that the Commission failed to address this argument adequately, Paribas' June 6 filing provides no basis for the Commission to reach a different conclusion on remand. Transco avers the Commission had already ruled in Opinion No. 507 that the *1999 Certificate Policy Statement*[30] did not apply to this proceeding because it covers natural gas facility expansions,[31] and this ruling was not challenged by Paribas on rehearing.[32] Transco contends that it was correct for the Commission to determine that the rate treatment for transmission upgrades for generation interconnections is even less relevant to the proceeding because it covers expansions and construction of electric transmission facilities. In any event, Transco contends that the Commission does permit incremental rates for electric network upgrades in order to protect native load from subsidizing such upgrades, and therefore Transco's incremental rate proposal is consistent with the Commission's rate policies for network upgrades.

34. In its opposition, the WSS Customer Group states, even assuming the Commission's electric interconnection pricing policy is applicable to the natural gas industry, it does not apply in this proceeding because that policy is focused on additions to the electric grid; however, the WSS Customer Group argues that this situation only involves the replacement of a commodity that was removed from an existing storage field by departing shippers who were immediately replaced by Paribas and South Jersey. The WSS Customer Group asserts that no new facilities or expansion of capacity resulted from these transactions. As such, the WSS Customer Group avers that there is no

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[30] *Certification of New Interstate Natural Gas Pipeline Facilities* 88 FERC ¶ 61,227 (1999), *clarified*, 90 FERC ¶ 61,128, *further clarified*, 92 FERC ¶ 61,094 (2000) (*1999 Certificate Policy Statement*).

[31] Transco Opposition at 7 (citing Opinion No. 507, 130 FERC ¶ 61,043 at P 63).

[32] *Id*. at 8 (citing Paribas and South Jersey Rehearing of Opinion No. 507 at 24).

reasonable basis to apply a policy directed at how to allocate the costs of new and additional facilities where no new or additional facilities exist.

35. The Commission requests that the participants address in their written evidence and briefs the issue of the consistency of Transco's incremental rate proposal with the Commission's policy concerning incremental rate treatment of electric transmission network upgrades. In Order No. 2003-A, the Commission summarized that policy as follows:

> [U]nder our interconnection pricing policy, the Transmission Provider continues to have the option to charge a transmission rate that is the higher of an incremental cost rate for network upgrades required to interconnect its generating facility or an embedded cost rate for the entire transmission system (including the cost of the Network Upgrades. . . Allowing transmission providers to charge the higher of an incremental cost rate or an embedded cost rate ensures that other transmission customers, including the Transmission Provider's native load, will not subsidize Network Upgrades required to interconnect merchant generation.[33]

36. Order No. 2003-A also rejected a proposal that the Commission permit the cost of network upgrades to be directly assigned to the interconnection customer. The Commission explained that direct assignment is not permitted, because even if the interconnection customer can be said to have caused the addition of the network upgrade, the addition represents a system expansion used by and benefitting all users due to the integrated nature of the grid. Order No. 2003-A stated that, for this reason, the Commission has consistently priced the transmission service of a non-independent transmission provider based on the cost of the grid as a whole, and has rejected proposals to directly assign the cost of network upgrades.

37. However, Order No. 2003-A then explained that this does not mean that native load customers must subsidize the cost of the network upgrades:

> [w]hen rolling in the cost of Network Upgrades would cause the embedded cost rate paid by existing transmission customers to increase, we permit the non-independent Transmission Provider to charge an incremental rate (i.e., the rate associated with the costs of the Network Upgrades divided by the Interconnection Customer's units of service) to the Interconnection Customer. This will fully insulate existing customers from the cost of the Network Upgrades. We emphasize, however, that an incremental rate is not the same as direct assignment; the Interconnection Customer that pays

[33] Order No. 2003-A, FERC Stats. & Regs. ¶ 31,160 at P 580.

> an incremental rate is paying for Transmission Service over the entire Transmission System. Charging both the incremental cost of the Network Upgrades and an embedded cost transmission rate would be charging twice for the same service, i.e. 'and' pricing, and we do not permit such pricing for the Transmission Services of a non-independent Transmission Provider.[34]

38. The electric network upgrade pricing policy described above is consistent with the Commission's pricing policy for natural gas pipeline expansions, as established in the *1999 Certificate Policy Statement*. In that policy statement, the Commission changed the focus of its rolled-in versus incremental rate policy so that the primary goal is to achieve efficient pricing signals to expansion shippers and existing pipeline customers, while remaining within the pipeline's revenue requirement. Under this policy, when a project is first certificated, the Commission requires that existing shippers not be required to subsidize the expansion. This generally means that expansions will be priced incrementally so that expansion shippers will have to pay the full costs of the project, without subsidy from the existing customers through rolled-in pricing. The Commission has stated that policy will help ensure that the market finds a project viable, because either the expansion shippers or the pipeline must be willing to fully fund the project.[35] In addition, the Commission stated that rolled-in rates may be permissible if the facilities are needed to improve service for existing customers, the increase in rates is related to improvements in service, and raising existing customers' rates does not constitute a subsidy of an expansion by existing customers.[36]

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[34] *Id.* P 586.

[35] Pursuant to this policy, the Commission has approved incremental rates for expansions of storage fields, with the cost of additional base gas required for the expansion included in the incremental rate. *Columbia Gas Transmission, LLC*, 122 FERC ¶ 61,021 (2008). *Natural Gas Pipeline Co. of America*, 124 FERC ¶ 61,154, at PP 24-25 (2008).

[36] *Transcontinental Gas Pipe Line Corp*., 95 FERC ¶ 61,388, at 62,450 (2001). *Transcontinental Gas Pipe Line Corp*., 112 FERC ¶ 61,170, at P 35 (2005). As also described in these orders, the Commission has stated that, subsequently, when a pre-expansion shipper's existing contract expires, the pipeline could require the existing shipper to pay a higher rate than its existing vintaged rate if: (1) the pipeline is fully subscribed; and (2) there is a competing bid higher than the pre-expansion rate. However, a pipeline must include a rate adjustment mechanism in its tariff in order to do this, and no pipeline has done so.

39. Thus, the Commission's rolled-in vs. incremental rate policies for electric network upgrades and pipeline expansions both permit incremental rates for new facilities when rolling in the costs of those facilities would increase the rates being paid by existing customers (or "native load"). Moreover, in both cases, the Commission designs the incremental rates for the new shipper based solely on the costs of the new facilities and does not include the costs of existing facilities in the incremental rate. As described by Order No. 2003-A, an incremental rate for a network upgrade is based on the costs of the network upgrade divided by the Interconnection Customer's units of service; existing facility costs embedded in the current electric transmission rate are not included in the incremental rate. Similarly, an incremental rate for a natural gas pipeline expansion is designed based on costs associated with the new facilities divided by the expansion shipper's units of service; existing facility costs embedded in the pipeline's current transportation rates are not included in the incremental rate. For example, when a pipeline increases the capacity of its mainline by adding pipeline looping, the costs of the new looping will be included in the incremental rate, but not the costs of the existing pipeline facilities.[37]

40. The Commission directs that the participants address in the written evidence and argument required by this order whether or not Transco's proposed rates for Paribas and South Jersey are consistent with the Commission's incremental rate policies applicable to electric network upgrades. Specific questions to be addressed by the participants include: Is it reasonable for Transco to use incremental rates to protect its historic storage customers from subsidizing base gas purchases to serve Paribas and South Jersey, similar to the Commission's approval of incremental rates to protect native load from subsidizing electric network upgrades? Has Transco proposed to design Paribas and South Jersey's rates in a manner similar to the incremental rates the Commission has permitted to be charged to electric interconnection customers, so that costs associated with preexisting facilities are excluded? Alternatively, has Transco proposed to include costs of preexisting facilities in those rates in a manner that is inconsistent with the Commission's policies concerning the design of incremental rates described above? If so, what adjustments in Transco's rate proposal would be necessary to render it consistent with the Commission's incremental rate design policies? Is there a reason why inclusion of the costs of existing facilities in Paribas and South Jersey's incremental rates is reasonable, even if seemingly inconsistent with the policies described above?

41. In this case, if Transco had not replaced any of the base gas taken by PSEG and South Jersey Gas when they released their storage capacity to Paribas and South Jersey, Transco would not have been able to provide its historic storage customers the full amount of the contracted service. Thus, a portion of the subject base gas purchases was

[37] *See Northwest Pipeline Corp.*, 71 FERC ¶ 61,253, at 61,976 (1995).

necessary to provide service to the historic storage customers. The participants should address whether and how this fact should be taken into account in determining a just and reasonable allocation of the costs of the base gas purchases.

III. Settlement Judge Procedures

42. While we are establishing a paper hearing in this remand proceeding, we encourage the parties to make every effort to settle their longstanding dispute over these issues before the paper hearing procedures are commenced. We are mindful of the fact that the parties have previously engaged in settlement discussions on a bilateral and multilateral basis, but no accord could be reached between them on the appropriate rate treatment for Paribas and South Jersey. However, in light of the court's remand and the need for further procedures before the remanded issues can be resolved on the merits, we believe a renewed effort to resolve this dispute through settlement is in the interest of all concerned. To aid the parties in their settlement efforts, we will hold the paper hearing in abeyance and direct that a settlement judge be appointed, pursuant to Rule 603 of the Commission's Rules of Practice and Procedure.[38] If the parties desire, they may, by mutual agreement, request a specific judge as the settlement judge in the proceeding; otherwise, the Chief Judge will select a judge for this purpose.[39] The settlement judge shall report to the Chief Judge and the Commission within 30 days of the date of the appointment of the settlement judge, concerning the status of settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions or terminate the settlement procedures.

The Commission orders:

(A) Pursuant to Rule 603 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.603 (2014), the Chief Administrative Law Judge is hereby directed to appoint a settlement judge in this proceeding within 15 days of the date of this order. Such settlement judge shall have all powers and duties enumerated in Rule 603 and shall convene a settlement conference as soon as practicable after the Chief Judge designates the settlement judge. If the parties decide to request a specific judge, they must make their request to the Chief Judge with 5 days of the date of this order.

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[38] 18 C.F.R. § 385.603 (2014).

[39] If the parties decide to request a specific judge, they must make their joint request to the Chief Judge by telephone at (202) 502-8500 within five days of this order. The Commission's website contains a list of Commission judges available for settlement proceedings and a summary of their background and experience (http://www.ferc.gov/legal/adr/avail-judge.asp).

(B) Within 30 days of the appointment of the settlement judge, the settlement judge shall file a report with the Commission and the Chief Judge on the status of the settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions, if appropriate, or terminate the settlement judge procedures. If settlement discussions continue, the settlement judge shall file a report at least every 60 days thereafter, informing the Commission and the Chief Judge of the parties' progress toward settlement.

(C) If the settlement judge reports that settlement procedures have failed and the paper hearing is to be conducted, the Chief Judge shall terminate the settlement judge procedures. The participants are directed to file briefs on the issues listed above within 60 days of the date the Chief Administrative Law Judge terminates the settlement procedures and reply briefs are due within 90 days of the termination of settlement procedures. Each participant's presentation in its initial and reply briefs should separately state the facts and arguments advanced by the participant and include any and all exhibits, affidavits and/or prepared testimony upon which the participant relies. The statement of facts must also include citations to supporting exhibits, affidavits, and/or prepared testimony. All materials must be verified and subscribed as set forth in 18 C.F.R. § 385.2005 (2014).

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.