Tesoro Refining and Marketing Company et al. v. Calnev Pipe Line L.L.C.

ORDER CONSOLIDATING CERTAIN COMPLAINT PROCEEDINGS AND ESTABLISHING HEARING PROCEDURES

134 FERC ¶ 61,214 (2011), *order denying reh'g*, 136 FERC ¶ 61,083 (2011)

In this case, various shippers filed complaints in 2007 and 2009 challenging, among other things, the grandfathered rate of Calnev Pipe Line LLC. The Commission consolidated the complaint proceedings, set them for hearing, but held the consolidated proceeding in abeyance pending a settlement judge proceeding. In this hearing order, the Commission, among other things, describes at length the return to establish to prove whether the challenged grandfathered rate should lose the presumption that it is just and reasonable due to a substantial change in the economic circumstances that were the basis of the rate. Whether there is a substantial change involves comparing the equity rate of return generated by the grandfathered rate in the complaint year ("C" year) with a comparable measure in the year grandfathering became lawful ("B" year, generally calendar 1992) for the grandfathered rate against the embedded rate of return on equity in the grandfathered rate for the year in which the grandfathered rate was established ("A" year). The Commission notes the pertinent formulaic expression as C-B/A. The Commission denied Calnev's petition for rehearing on procedural grounds.

134 FERC ¶ 61,214
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
John R. Norris, and Cheryl A. LaFleur.

Tesoro Refining and Marketing Company v. Calnev Pipe Line LLC	Docket No. OR07-7-000 (consolidated)
America West Airlines, Inc. and US Airways, Inc. Chevron Products Company Continental Airlines, Inc. Southwest Airlines Co. and Valero Marketing and Supply Company v. Calnev Pipe Line LLC	Docket No. OR07-18-000 (consolidated)
ConocoPhillips Co. v. Calnev Pipe Line LLC	Docket No. OR07-19-000 (consolidated)
BP West Coast Products, LLC v. Calnev Pipe Line LLC	Docket No. OR07-22-000 (consolidated)
Tesoro Refining and Marketing Company v. Calnev Pipe Line LLC	Docket No. OR09-15-000 (consolidated)
BP West Coast Products, LLC v. Calnev Pipe Line LLC	Docket No. OR09-20-000 (consolidated)

ORDER CONSOLIDATING CERTAIN COMPLAINT PROCEEDINGS AND ESTABLISHING HEARING PROCEDURES

(Issued March 17, 2011)

1. This order addresses and consolidates four complaints against Calnev Pipe Line LLC (Calnev) that were filed in 2007 (the 2007 Calnev Complaints), and which raise substantially changed circumstances issues.[1] The Commission is addressing methodological and technical issues involved in the 2007 Calnev Complaints and is setting them for hearing. However, the Commission is not here deciding whether there has been a substantial change to the economic circumstances that were the basis for Calnev's grandfathered rates. The Commission also clarifies the 2007 Calnev Orders[2] in response to one request for rehearing. In addition, the Commission dismisses BP West Coast Product, LLC's amendment of its 2007 Calnev complaint to include Calnev's Las Vegas vapor recovery terminaling charges. This order also addresses the procedural status of two additional complaints that were filed against Calnev's rates in late 2009 (the 2009 Calnev Complaints).[3] The Commission concludes that it will expedite resolution of all current complaints against Calnev's base rates if the 2009 Calnev Complaints are set for hearing and consolidated with the 2007 Calnev Complaints.

2. On the issue of substantially changed circumstances, the Commission makes the following determinations which set the framework to be followed when analyzing whether there are substantially changed circumstances to the grandfathered portion of a pipeline's base rates. First, that in measuring a change in return for purposes of determining substantially changed circumstances, the Commission considers the pipeline's change in profitability, which is measured by the change in the rate of return on equity from that embedded in the grandfathered rate. Second, when calculating the change in return on equity, the change should be quantified in terms of actual dollar amounts of the pipeline's revenues and expenses. Third, when analyzing whether there are substantially changed circumstances the analysis must use total jurisdictional revenues. Fourth, the Commission acknowledges that in considering whether there are

---

[1] ExxonMobil Oil Corporation (ExxonMobil) filed a complaint against Calnev's base rates in Docket No. OR07-5-000. The case settled and ExxonMobil withdrew all of its complaints, protests and interventions on April 18, 2008, which terminated the complaint in Docket No. OR07-5-000. Thus, the remaining 2007 Calnev Complaints are Docket Nos. OR07-7-000, OR07-18-000, OR07-19-000, and OR07-22-000 (collectively the 2007 Calnev Complaint Proceedings).

[2] *America West Airlines, Inc., et al. v. Calnev Pipe Line, L.L.C.*, 121 FERC ¶ 61,241 (2007) (*America West*), *BP West Coast v. Calnev*, 121 FERC ¶ 61,242 (2007) (*BP v. Calnev*) (collectively the 2007 Calnev Orders).

[3] Docket Nos. OR09-15-000 and OR09-20-000. The first complaint proceeding was initiated by Tesoro Refining and Marketing Company (Tesoro) and the second was initiated by BP West Coast Products, LLC (BP West Coast).

substantially changed circumstances, increases in revenues resulting from the pipeline's annual indexing should be considered. Fifth, any change in the embedded rate return on equity must occur after the enactment date of Energy Policy Act of 1992 (EPAct). Sixth, the Commission sets 25 percent as the minimum percentage change in return on equity necessary to establish substantially changed circumstances. If the change in return on equity is 25 percent or greater, the Commission may consider other factors to confirm that the change is not anomalous or unrepresentative. Last, the Commission confirms that a change in return on equity must be measured using the current version of the rate methodology that is applicable to the particular year under analysis.

I. Background

3. The four pending 2007 Calnev Complaints challenge all of Calnev's existing interstate rates, including both the grandfathered portion of those rates as well as the portion of its rates in excess of the grandfathered rate.[4] The grandfathered portion was created when Calnev's 1991 rates had been in effect for the 365 day period preceding the effective date of the EPAct of 1992. Because Calnev's 1991 rates were in effect during that 365 day period, they were deemed just and reasonable and became grandfathered rates under section 1803(a) of EPAct.[5] The 2007 Calnev Complaints also challenge the cost-based and index-based components of Calnev's base rates, which first became effective on September 2, 1991.[6] The Commission requires a complainant to establish reasonable grounds to conclude that the challenged rate is unjust and unreasonable before

---

[4] The complainants are shown for the respective Dockets as follows: Docket No. OR07-7-000, complainant Tesoro; Docket No. OR07-18-000, joint complainants America West Airlines, Inc., Chevron Products Company, Continental Airlines, Inc., Northwest Airlines, Inc., Southwest Airlines Co., U.S. Airways, Inc., and Valero Marketing and Supply Company (collectively, the Airline Parties); Docket No. OR07-19-000, ConocoPhillips Company (ConocoPhillips); and Docket No. OR07-22-000, complainant BP West Coast. All of these complainants are hereinafter collectively referred to as the Calnev Shippers when referring to the pleadings in Docket No. OR07 series of complaints against Calnev.

[5] Section 1803(a) of the Energy Policy Act of 1992, Public L. No. 102-486, 106 Stat. 2276 (1992) (EPAct). Section 1803(a)(2) provides: "any rate in effect on the 365th day preceding the date of such enactment shall be deemed to be just and reasonable . . . regardless of whether or not, with respect to such rate, a new rate has been filed with the Commission during such 365-day period."

[6] *See Revision to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, Order No. 561, FERC Stats. & Regs. ¶ 30,985 (1993), *order on rehearing*, Order

(continued ...)

a complaint will be accepted.[7] The Commission previously held that the 2007 Calnev Complaints met this threshold standard.[8] With respect to a complaint challenging the grandfathered portion of a pipeline's rate, the Commission requires the complainant to establish reasonable grounds to conclude that there may be substantially changed circumstances to the grandfathered portion of a pipeline's base rates.[9] Specifically, section 1803(b) of EPAct requires that a complaint against the grandfathered portion of a base rate establish that a substantial change has occurred after the date of the enactment of EPAct in the economic circumstances of the oil pipeline which were the basis for the rate.[10] In *America West,*[11] the Commission held that two of the 2007 Calnev Complaints did not adequately address the issue of substantially changed circumstances and made a similar finding regarding the other two 2007 Calnev Complaints in *BP v. Calnev* and *ExxonMobil v. Calnev*.[12] The Commission therefore provided the 2007 Calnev complainants an opportunity to amend their complaints. After receiving the amended complaints, the Commission permitted another round of pleadings to further clarify

---

561-A, FERC Stats. & Regs. ¶ 31,000 (1994), *affirmed sub nom. Association of Oil Pipelines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996).

[7] *See ExxonMobil Oil Corporation v. Calnev Pipe Line LLC, et al.*, 120 FERC ¶ 61,075 at P 4 (2007) (*ExxonMobil v. Calnev*); Order No. 561, FERC Stats & Regs. at 30,956, 30,964-65.

[8] *ExxonMobil v. Calnev*, 120 FERC ¶ 61,075 at P 6 (accepting Tesoro's 2007 complaint against Calnev to the extent it challenges Calnev's rates in excess of the grandfathered rate in effect in 1992); *America West*, 121 FERC ¶ 61,241 at P 5 (accepting the portion of the Airline Parties' and Conoco Phillips' complaints against the non-grandfathered portion of Calnev's rates); *BP West Coast v. Calnev*, 121 FERC ¶ 61,242 at P 5, Ordering Paragraph (A).

[9] *America West*, 121 FERC ¶ 61,241 at P 6.

[10] Section 1803(b)(1)(A) of EPAct. The conventional short form for the cited standard is "substantially changed circumstances."

[11] *America West*, 121 FERC ¶ 61,241 at P 7-11.

[12] *BP v. Calnev*, 121 FERC ¶ 61,242 at P 4-7; *ExxonMobil v. Calnev*, 120 FERC ¶ 61,075 at P 5.

the parties' arguments.[13] The additional comments and answers were filed by early April 2008.

4. While the amended 2007 Calnev Complaints were under review, an initial decision (2008 SFPP ID involving a complaint by Chevron Products Co. and several other shippers[14] against SFPP, L.P. (SFPP) in Docket No. OR03-5-001 (SFPP Proceeding) issued on November 18, 2008, which addresses, in part, the issue of substantially changed circumstances.[15] The SFPP Proceeding involved complaints against SFPP's North and Oregon Line rates.[16] The arguments of the SFPP litigant shippers[17] and of SFPP regarding substantially changed circumstances in the SFPP Proceeding are almost identical to those presented in the 2007 Calnev Complaints against Calnev. Prior to this order the arguments in the SFPP Proceeding have never been reviewed by the Commission.[18] Because of the similarity of the substantially changed circumstances issues raised in the 2007 Calnev Complaints and the contemporaneous SFPP Proceeding, the Commission will use the SFPP Proceeding's record and the 2008

---

[13] *See* Notice Permitting Further Answers dated March 6, 2008 in Docket No. OR07-5-000, *et al.*, including the four 2007 Calnev Complaints.

[14] The other shipper litigants include BP West Coast, ExxonMobil and ConocoPhillips.

[15] *Chevron Products Co., et al., v. SFPP, L.P.*, 125 FERC ¶ 63,018, at P 339-436 (2008) (2008 SFPP ID). The complainant shippers in Docket No. OR03-5-001 SFPP Proceeding were BP West Coast, Chevron, and ConocoPhillips. In the SFPP Proceeding, ConocoPhillips and Chevron are collectively known as the CC Shippers.

[16] *Chevron Products Company v. SFPP, L.P.*, Docket No. OR03-5-000 (the SFPP Proceeding).

[17] All of the complainant shippers in the SFPP Proceeding are also the complainants in the 2007 Calnev Complaints.

[18] Subsequently, the SFPP shipper complainants entered into two separate settlements with SFPP that resolved all their respective issues regarding the 2008 SFPP ID including the substantially changed circumstances issues. *See SFPP, L.P.*, 131 FERC ¶ 61,180 (2010) (order approving April 16, 2010 settlement agreement between SFPP and all complaining shippers except Chevron) and *SFPP, L.P.*, 134 FERC ¶ 61,201 (2011) (order approving February 2, 2011 settlement agreement between SFPP and Chevron).

SFPP ID as guidance in making our determination on the issue of substantially changed circumstances.[19]

5. In 2009, ConocoPhillips Company filed a motion requesting that the 2007 Calnev Complaints be set for hearing on rate reasonableness asserting that the complainants had established that there were substantially changed circumstances to Calnev's rates.[20]

6. While the 2007 Calnev Complaints have been pending, Tesoro and BP West Coast filed new complaints against Calnev's base rates on June 30, 2009 and July 31, 2009 respectively (2009 Calnev Complaints). The 2009 Calnev Complaints do not challenge the grandfathered portion of Calnev's base rates. Rather, the 2009 Calnev Complaints challenge Calnev's existing base rates as unjust and unreasonable principally on the grounds that page 700 of Calnev's 2008 FERC Form No. 6 shows a substantial over-recovery of Calnev's 2008 jurisdictional cost-of-service. Specifically, they assert that Calnev's 2008 total cost-of-service was some $46,600,876 and its total revenues were $54,922,230, a substantial over-recovery of some $8.3 million. In addition, they assert that Calnev's cost structure includes inappropriate overhead cost allocations, and an improper capital structure and income tax allowance. Calnev filed replies to the two 2009 Calnev Complaints on July 20 and August 20, 2009, asserting that the 2009 Calnev Complaints do not meet the standards for a complaint challenging a pipeline's rates as unjust and unreasonable.

7. The first part of this order provides a summary of the 2007 Calnev Complaints. The second part discusses the methodology that should be applied at hearing on the issues of substantially changed circumstances, together with some technical issues unique to the 2007 Calnev Complaints. The third part addresses the two 2009 Complaints, including all of BP West Coast's pleadings filed after its initial complaint.

---

[19] As noted, the Calnev Shippers and the CC Shippers make many of the same arguments in the 2007 Calnev Complaints as made in the SFPP Proceeding. When referencing the arguments made in both those proceedings they are referenced as the Shipper Parties.

[20] ConocoPhillips, Motion to Set Complaint for Hearing, Docket No. OR07-19-000 (filed June 2, 2009).

II. Procedural History of the 2007 Calnev Complaints

A. Tesoro

8. Tesoro filed its initial complaint on January 30, 2007 in Docket No. OR07-7-000. Tesoro's complaint asserted that Calnev's rates were unjust and unreasonable and that there were reasonable grounds to conclude that there were substantially changed circumstances. Tesoro asked the Commission to determine that the Calnev's existing rates were unjust and unreasonable, establish just and reasonable rates, and order reparations. Calnev filed an answer on March 1, 2007, and Tesoro filed its reply on March 16, 2007. The Commission's April 2, 2007 order held Tesoro's complaint in abeyance pending clarification of a number of issues then pending before the D.C. Circuit.[21] On July 20, 2007, the Commission issued a second order and found that Tesoro's complaint relied on arguments that were recently rejected by the U.S. Court of Appeals for the D.C. Circuit (Court) in *ExxonMobil*.[22] The Commission therefore granted Tesoro ninety days to amend its complaint to reflect the Court's determinations in *ExxonMobil* on the income tax allowance and substantially changed circumstances issues. The order also accepted Tesoro's complaint against the portion of Calnev's base rates in excess of the grandfathered rates.[23]

9. Tesoro did not file an amended complaint within the 90 day period established by the April 2, 2007 order, but did so on February 8, 2008, purportedly in response to the Commission's December 26, 2007 order in *America West,*[24] citing 18 C.F.R. § 385.215(a)(3)(i) (2007) of the Commission's rules. Tesoro argued that the cited regulation permits a complaint to be amended any time before it is set for hearing. Calnev filed a combined answer to Tesoro's and the other amended 2007 Calnev

---

[21] *Tesoro Marketing and Refining Co. v. Calnev Pipe Line LLC*, 119 FERC ¶ 61,002 (2007) (*Tesoro v. Calnev*).

[22] *See ExxonMobil v. Calnev*, 120 FERC ¶ 61,075 at P 6 (citing *ExxonMobil Oil Corp., et al. v. FERC*, 487 F.3d 945 (D.C. Cir. 2007) (*Exxon Mobil*)).

[23] *ExxonMobil v. Calnev*, 120 FERC ¶ 61,075 at P 1, 4.

[24] In *America West*, the Commission addressed the joint complaint filed by the Airline Parties and ConocoPhillips against Calnev's entire rate. The Commission found certain methodological errors by the complainants regarding their arguments on substantially changed circumstances and provided those complainants forty-five days to amend their complaint in light of the Commission's discussion. *See America West*, 121 FERC ¶ 61,241.

Complaints on March 3, 2008 (March 3 Answer).[25] Calnev argued that Tesoro's February 8 amendment was out-of-time and that it did not meet the threshold standard regarding substantially changed circumstances. Given the opportunity for amendment provided the other complainants on December 26, 2007, and the discussion in *America West*, the Commission accepts Tesoro's February 8, 2008 amended complaint. On April 10, 2008, Tesoro filed its response to Calnev's March 3 Answer as permitted by the Commission's March 6, 2008 notice permitting further comments.

B. The Airline Parties and ConocoPhillips

10. On August 20, 2007, the Airline Parties filed a joint complaint in Docket No. OR07-18-000. Also on August 20, 2007, ConocoPhillips filed in Docket No. OR07-19-000, a complaint that is virtually identical to the Airline Parties' complaint. Both the Airline Parties' and ConocoPhillips' complaints asserted that Calnev's rates were unjust and unreasonable and that the complaints had established reasonable grounds to conclude that there were substantially changed circumstances to support rescission of Calnev's 1991 grandfathered rates. The complaints requested the Commission determine that Calnev's existing rates were unjust and unreasonable, establish just and reasonable rates, provide reparations, and order attorney's fees and costs. Calnev filed an answer to these complaints on September 10, 2007, asserting the complainants had not established that Calnev's rates were unjust and unreasonable. Calnev further argued that the complainants had not established reasonable grounds to conclude that there were substantially changed circumstances to Calnev's grandfathered rates. Calnev asked the Commission to dismiss the two complaints.

11. On December 26, 2007, the Commission issued an order on Airline Parties' and ConocoPhillips' complaints, *America West*, which consolidated the Airline Parties' and ConocoPhillips' complaint proceedings and held that the complainants had established reasonable grounds to conclude that Calnev's rates may be unjust and unreasonable.[26] The order also addressed what the Commission concluded were certain methodological errors by the complainants and provided the complainants forty-five days to amend their complaints in light of the Commission's discussion.[27] In response, the Airline Parties and ConocoPhillips filed separate amended complaints on February 11, 2008. On February

---

[25] Calnev filed its March 3, 2008 Answer to the following 2007 Calnev Complaint Proceedings: Docket Nos. OR07-5-000; OR07-7-000; OR07-18-000; OR07-19-000; and OR07-22-000.

[26] *See America West*, 121 FERC ¶ 61,241.

[27] *Id.* P 8-10.

11, 2008, America West Airlines, Inc. and US Airways, Inc. filed a motion to reflect their consolidation into a single corporation and to substitute US Airways as a complainant, which motion the Commission grants.[28] Calnev responded to the amended complaints with its March 3 Answer. Calnev argues that the complainants fail to meet the Commission's existing standards for establishing reasonable grounds to conclude that there were substantially changed circumstances to Calnev's grandfathered rates. On April 10, 2008, the Airline Parties and ConocoPhillips filed a joint response to Calnev's March 3 Answer pursuant to the Commission's March 6, 2008 notice permitting further comments. Calnev replied on April 25, 2008.

C. BP West Coast

12. On September 13, 2007, BP West Coast filed a complaint in Docket No. OR07-22-000. BP West Coast asserted that Calnev's rates were unjust and unreasonable, including all surcharges to those rates. BP West Coast also asserted that its complaint establishes that there are reasonable grounds to conclude that there were substantially changed circumstances with respect to Calnev's 1991 grandfathered rates. BP West Coast asked the Commission to require Calnev to submit a cost and revenue study, and if the resulting revenues exceeded costs, to require Calnev to make interim reparations. In addition, BP West Coast asked the Commission to find that Calnev's 1991 rates were not grandfathered, to set reasonable rates, to preclude indexing of Calnev's rates, and to award damages.

13. On October 15, 2007, Calnev filed an answer asserting that BP West Coast's complaint did not address the basic elements of the Commission's substantially changed circumstances standard, and further argued that BP West Coast violated an earlier settlement by asserting that Calnev's jet fuel surcharge was unjust and unreasonable. The December 26, 2007 order on BP West Coast's complaint issued concurrently with *America West*, and like *America West*, discusses the deficiencies in the complaint on the issue of substantially changed circumstances. The Commission gave BP West Coast forty-five days to file an amended complaint.[29] On January 25, 2008, BP West Coast

---

[28] The Commission had previously dismissed US Airways as a complainant because it was not shipping fuel over Calnev at the time the August 20 complaint was filed. *Id.* P 18. The February 11, 2008 motion is unopposed and is granted because the consolidation has been completed.

[29] *BP West Coast v. Calnev*, 121 FERC ¶ 61,242, *passim*.

filed a request for rehearing of both the 2007 Calev orders.[30] BP West Coast filed an amended complaint on February 11, 2008. The amended complaint addresses the issue of substantially changed circumstances and withdraws the part of the complaint against Calnev's jet fuel surcharge. Calnev responded to BP West Coast's amended complaint in its March 3 Answer.

14. On April 10, 2008, BP West Coast filed a second amendment to its complaint adding a count challenging Calnev's rate for vapor recovery at its Las Vegas terminal. The second amended complaint also includes a motion for leave to call certain protected materials to the Commission's attention.[31] On April 25, 2008, Calnev filed an answer asserting that Calnev's vapor recovery service was not jurisdictional and, as such, was not within the Commission's jurisdiction. Calnev also argues that even assuming jurisdiction, BP West Coast has not pled a single fact supporting a conclusion that there were substantially changed circumstances. Calnev asks the Commission to dismiss BP West Coast's second amended complaint.

III. The Methodology for Determining Substantially Changed Circumstances

15. The extensive comments filed in response to *America West* disclosed that there are differing interpretations among the parties regarding the Commission's conclusions on substantially changed circumstances.[32] The same matters were more fully explored at hearing in the SFPP Proceeding and were addressed in detail in the 2008 SFPP ID.[33] Upon review of briefs on exception and opposing exceptions to the 2008 SFPP ID, the Commission again finds that SFPP Shippers' and SFPP's arguments regarding the methodology for determining substantially changed circumstances filed in the SFPP Proceeding are essentially the same as those made by the Calnev Shippers's[34] and Calnev

---

[30] *See* BP West Coast, Request for Rehearing and Clarification, , Docket Nos. OR07-18; OR07-19; and OR07-22 (filed Jan. 25, 2008) (seeking rehearing of both *America West*, 121 FERC ¶ 61,241 and *BP West Coast v. Calnev*, 121 FERC ¶ 61,242).

[31] As the Commission is setting the 2007 Calnev Complaints for hearing, there is no need to rule on this motion at this time.

[32] *E.g.*, to what extent did the order intend for revenue increases for annual index adjustments to be considered in determining whether there are substantially changed circumstances. These and other ambiguities in *America West* are clarified *infra.*

[33] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 339-436.

[34] The overlap of between the SFPP Shippers and the Calnev Shippers includes SFPP Shippers Chevron, BP West Coast, and Conoco Phillips. SFPP is affiliated with

(continued ...)

in the 2007 Calnev Complaints proceedings.[35] The Commission finds that the methodologies advanced in the 2007 Calnev Complaints require correction or clarification, thus the cumulative record to date precludes the Commission from making a merit determination of whether there are substantially changed circumstances with respect to Calnev's grandfathered rate. Accordingly, given the similarities between the SFPP Proceeding and the 2007 Calnev Complaints, the Commission addresses in this order the methodological approach related to substantially changed circumstances that should be used at hearing, taking into consideration guidance from the record in the SFPP Proceeding.[36] As was previously stated, this affords the Commission and the parties additional guidance to consider regarding the most appropriate method for determining whether there are substantially changed circumstances. Since the question of whether there are substantially changed circumstances is being set for hearing, the parties will have another opportunity to address the principles discussed in this order.

16. The first part of this order addresses the historical framework for determining substantially changed circumstances, addresses Calnev's pending motions to dismiss, summarizes the parties' theories, and discusses the 2008 SFPP ID's analysis. The Commission emphasizes it is not making a factual determination regarding whether there were substantially changed circumstances herein; that remains a matter to be determined at hearing.

Calnev. Therefore Calnev and SFPP are jointly referred to as Calnev/SFPP when they are making the same or similar arguments in the 2007 Calnev Complaint and SFPP Proceedings.

[35] For example, SFPP used Robert G. Van Hoecke as its lead witness in both the 2007 Calnev Complaints (Exhibit 1 to Calnev's Combined Answer dated March 3, 2008) and the SFPP Proceeding (Ex. SFO-1). Most of the Calnev and SFPP Shipper used Matthew P. O'Loughlin as the lead witness in both proceedings (e.g. Supplemental Affidavit to Amendment to Complaint of ConocoPhillips, *et al.* dated February 11, 2008 in Docket No. OR07-19-000, *et al.* and Ex. CC-1 and Ex. CC-44 in Docket No. OR03-5-001). While the testimony reflected the different cost-of-services and volumes for the different pipeline facilities at issue, there was virtually no difference in the methodological or analytical positions SFPP or Calnev took in 2007 Calnev Complaints and the SFPP Proceeding.

[36] All reference to briefs on or opposing exceptions in this order are to the briefs filed in the SFPP Proceeding, Docket No. OR03-5-001. With respect to references to exhibits, where necessary for clarity, citations to exhibits include references to the relevant docket number.

A. The Historical Framework

17. The Commission's basic legal framework for determining substantially changed circumstances has been relatively constant. The Commission adopted the methodology for determining substantially change circumstances in a March 2004 Order[37] and a June 2005 Order,[38] which was affirmed by the U.S. Court of Appeals, D.C. Circuit in *ExxonMobil v. FERC.*[39] Under this methodology, the Commission first determines the return embedded in the grandfathered portion of the rate at the time the rate was established and is the base rate for the base period, which is called the A period. The Commission then determines the return generated by the challenged rate at the time EPAct became effective, or a reasonably approximate time frame, which, generally, is the return for the calendar year 1992, which is called the B period. The third determination is the return as of the date of the complaint, or some reasonable approximation of that time frame. This is known as the return for the C period.

18. Once the return for each period is determined, the formula for calculating the change is the return for the C period, minus the return for the B period, divided by the A period, or (C-B)/A.[40] Under this (C-B)/A formula, there are a couple of predicates for a finding of substantially changed circumstances. First, there must a positive change in return after the date of EPAct. In other words, if the C-B calculation is negative; there is no need for further analysis because there is no increase in return after the effective date of EPAct. Second, the percentage resulting from (C-B)/A must be positive and must reflect some significant increases. In both the 2007 Calnev Complaints proceedings and in the SFPP Proceeding the parties have debated the definition of the word "return," whether the increase in return required to establish substantially changed circumstances should be greater than 15 or 20 percent, the proper way of calculating the percentage, and related technical issues. The Commission discusses each of these issues below.

---

[37] *ARCO Products Co. v. SFPP, L.P.,* 106 FERC ¶ 61,300, at P 22-26 (2004) (March 2004 Order).

[38] *SFPP, L.P.*, 111 FERC ¶ 61,334, at P 30 (2005) (June 2005 Order).

[39] *ExxonMobil*, 487 F.3d 945, 959-60.

[40] March 2004 Order, 106 FERC ¶ 61,300 at P 22-26, 38; June 2005 Order, 111 FERC ¶ 61,334 at P 37-39, and Appendix, particularly Tables 1-4, 7. *See also BP West Coast Products LLC v. FERC*, 324 F.3d 1263, 1279-80 (2004) (*BP West Coast*).

B. Rulings on Calnev's Motions to Dismiss

19. Calnev has filed motions to dismiss each of the 2007 Calnev Complaints. Calnev makes four central arguments in its motions to dismiss. First, Calnev argues that the Airline Parties and ConocoPhillips utilize a narrow measure of return based on the change in margin between total revenues and expenses rather than the broader measure of return used in the Opinion No. 435 Orders.[41] Calnev asserts that the broader measure of return examines the change in ratio of total revenues to total expenses, as weighted by their relative size in the A period, to assure that the percentage calculated by the (C-B)/A formula properly reflects the different base numbers against which the calculation is performed.[42] The Commission will not dismiss the 2007 Calnev Complaints on this basis because the interpretation of *America West* and the definition of return under that order is the central issue here. As discussed below, the Airline Parties and ConocoPhillips reasonably construe *America West* as requiring a methodology using the change in dollar margins or in the rate of return on equity.

20. Second, Calnev argues that the Airline Parties and ConocoPhillips do not apply the (C-B)/A formula correctly because: (1) they use cost-of-service assumptions that are inappropriate, particularly involving the income tax allowance factors and equity cost of capital, and (2) they assume that Calnev's costs, volumes and revenues for 1992 are essentially the same as 1991. However, the Airline Parties, Chevron, and ConocoPhillips changed certain of the cost assumptions in their joint April 10, 2008 supplemental filing based in the Commission's prior criticisms of their methodology. They should not be penalized for having updated their pleadings in response to the Commission's concerns. Moreover, the Commission is not prepared to dismiss their complaints for failure to use the proper base year given disputes about the availability and accuracy of information for the 12 month period proceeding the date on which EPAct was approved and the methodology to be used.

21. Third, Calnev argues that neither Tesoro nor BP West Coast attempted to apply the (C-B)/A formula to analyze the matters raised by *America West*. Calnev points out that both these parties instead rely significantly on proposed changes in Calnev's over-recovery of its cost-of-service which the Commission has consistently rejected.[43]

---

[41] *SFPP,L.P.*, Opinion No. 435, 86 FERC ¶ 61,022 (1999), Opinion No. 435-A, 91 FERC ¶ 61,135 (2000), Opinion No. 435-B, 96 FERC ¶ 61,281 (2000), *order on clarification and reh'g,* 97 FERC ¶ 61,138 (2001) (collectively Opinion Nos. 435 Order).

[42] Calnev March 3, 2008 Consolidated Response at 11-12, 23-24.

[43] *Id.* at 28-30.

Because there is an extensive debate whether *America West* involved a new methodology and the ambiguities in *America West*, the Commission will not dismiss Tesoro's or BP West Coast's complaints.

22. Fourth, Calnev prepared a cost-of-service for 1991, 1992, 2005, and 2006, and compared them with its achieved return in those years. Based on its cost-of-service analyses, Calnev concludes that its achieved return was 11.39 percent and 11.37 percent in 1991 and 1992 respectively, and that by 2005 and 2006 its overall achieved returns had declined to 7.94 percent.[44] Calnev attributed this change in return primarily to a substantial increase in Calnev's rate base from $43 million in 1992 to over $102 million in 2005. Calnev's analysis further showed that its cost-of-service increased by almost 106.5 percent while its volumes increased by only 64.5 percent. Calnev concludes there can be no substantially changed circumstances given that its achieved return declined since the date EPAct became effective.[45] Pursuant to Rule 217 of the Commission's Rules of Procedure,[46] the Commission may summarily dispose of a complaint if there is no genuine issue of material fact. Calnev's arguments, specifically its cost-of-service assumptions and calculations contain disputed material facts. Accordingly, the Commission will deny Calnev's motions to dismiss and set the 2007 Calnev Complaints for hearing.

C. Summary of the Parties' Methodologies in the SFPP Proceeding

23. In the SFPP Proceeding, SFPP, CC Shippers, and Trial Staff present different methodologies for measuring a change in return within the context of the Commission's (C-B)/A formula for determining whether there are substantially changed circumstances. Below are three examples of how each of the parties in the SFPP Proceeding would perform the C-B calculation to determine a percentage change in return between two different periods. The examples do not address arguments regarding the proper definition of the term "return," the cost-of-service to be used, the appropriate test periods, or the quality of the record.

24. In both the SFPP Proceeding and the 2007 Calnev Complaints, SFPP and Calnev assert that the Commission should measure return through a "broad measure" of the

---

[44] While Calnev's Motion to Dismiss is somewhat unclear, the Commission assumes for purposes of discussion that "achieved return" means the realized return on equity.

[45] *See* Calnev March 3, 2008 Consolidated Response at Ex. 3 at 12.

[46] 18 C.F.R. § 385.217 (2010).

change in the ratio of total revenues and total costs among different time periods.[47] Thus, if in the first year the pipeline's revenues were $110 and its costs were $106, the difference is four percentage points on a ratio of 1.10 to 1.06. If, in a subsequent year, the revenues increase to $112 and costs remain $106, the difference between revenues and costs is now $6, or six percentage points on a ratio of 1.12 to 1.06. This results in a two percentage point change in the ratio of total revenues to total costs, which according to SFPP and Calnev, is a two percent increase in the pipeline's return. They assert this approach replicates the methodology used in the June 2005 Order and is consistent with *America West*.[48]

25. In the SFPP Proceeding, Trial Staff advocated a "margin approach." Specifically, Trial Staff analyzed the change between total revenues and total costs by comparing the difference between actual revenues and costs in the years at issue.[49] Trial Staff defined this change in the numerical difference of revenues and costs as the "change in margin," relying on the use of the term "margin" in *America West*. Thus, if costs were $101 and revenues $105 in the first year, the pipeline's margin would be $4. If costs rise to $105 and revenues were $110 in a subsequent year, the pipeline's margin would now be $5 compared to $4, for a change in margin $1 or 25 percent. Under Trial Staff's "margin approach" the 25 percent change in margin would represent a 25 percent increase in return.

26. CC Shippers' approach in the SFPP Proceeding was to determine the change in the dollar return on equity or the rate of return on equity,[50] a concept that BP West Coast supported but did not elucidate as fully. Under the CC Shippers' approach, if the return in the first year was $10 and the return in a subsequent year was $12, they assert that the $2 increase in return equals a 20 percent increase in the dollar return on equity. Similarly, if the rate of return on equity was 10 percent for the first year and rate of return on equity was 13 percent in a subsequent year, the three percentage point increase would reflect a 30 percent increase in rate of return on equity. The CC Shippers assert the June 2005 Order, *ExxonMobil*, and *America West* focus on rate of return and their method is

---

[47] *See* Calnev March 3, 2008 Consolidated Response at 11-12, 23-24; SFPP Brief on Exceptions at 13-15, 19-20; 2008 SFPP ID, 125 FERC ¶ 63,018 at P 374-375.

[48] Calnev March 3, 2008 Consolidated Response at 10, 14; SFPP Brief on Exceptions at 19-21.

[49] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 362-363.

[50] *Id.* P 340, 345, 350.

the only one that measures a change in the rate of return. The CC Shippers thus oppose SFPP's "broad ratio" and the Trial Staff's "margin" approaches.

D. The 2008 SFPP ID's Analysis

27. In the SFPP proceeding, the Administrative Law Judge (ALJ) in the 2008 SFPP ID reviewed Commission precedent on the issue of substantially changed circumstances and the parties' different methodologies. The 2008 SFPP ID concluded that any calculation of substantially changed circumstances should include all of the pipelines' revenues and expenses in the pertinent years and not just the grandfathered revenues. The 2008 SFPP ID reasoned that if revenues designed to compensate for inflation were excluded from the (C-B)/A calculation, then inflation-driven cost increases should also be excluded.[51] The 2008 SFPP ID also concluded that the threshold for determining whether there are substantially changed circumstances should be 15 percent,[52] that cost-of-service for a given year should reflect the cost-of-service methodology in effect in that year and that Trial Staff's proposed cost-of-service methodology for the 1992 calendar year was the most appropriate method.[53] The 2008 SFPP ID also held that if a complainant party failed to prove substantially changed circumstances, it is unnecessary to consider cost-of-service issues for revenues in excess of those generated by the grandfathered rate because the litigating SFPP shippers had not challenged the portion of the rates that resulted from the Commission's oil pipeline indexing methodology.[54]

28. The 2008 SFPP ID rejected SFPP's "broad ratio" approach on the grounds that it failed to measure a change in the return. The 2008 SFPP ID first explained that SFPP used the ratio of a broad measure of revenues and costs as a proxy for changes to the return on equity at the three different points in time, the base year, 1992, and the complaint year. The 2008 SFPP ID then held that the Commission previously rejected such a proxy approach *America West*.[55] The 2008 SFPP ID further concluded that SFPP failed to present credible evidence addressing the economic basis for the Oregon Line rates when those rates were established in 1985. The 2008 SFPP ID therefore concluded that the Commission should measure any change in return after the effective date of

---

[51] *Id.* P 417.

[52] *Id.* P 418.

[53] *Id.* P 412.

[54] *Id.* P 429-431.

[55] *Id.* P 416.

EPAct against the return of the Oregon Line rates in calendar year 1992.[56] As noted, the 2008 SFPP ID also rejected SFPP's analysis because it did not include the increased revenues resulting from the indexing of SFPP's rates under the Commission indexing methodology.[57]

29. The 2008 SFPP ID rejected CC Shippers' approach on the ground that they used several different definitions of return in their efforts to quantify a change in return, and therefore their approach was not credible. The 2008 SFPP ID also appears to have doubted the quality of CC Shippers' evidence based on the cost-of-service used, and also rejected their analysis as it did not reflect revenue increases caused by inflation.[58]

30. The 2008 SFPP ID accepted Trial Staff's approach as the one most consistent with *America West*.[59] Having concluded that *America West* required a comparison of the change in the pipeline's margins as the proper measure of a change in profitability,[60] the 2008 Chevron ID adopted Trial Staff's margin methodology for determining whether there are substantially changed circumstances. The 2008 SFPP ID also accepted Trial Staff's conclusion that there were no substantially changed circumstances to the North Line rates for the year 2003, but there was such a change to the Oregon Line rates in 2003.[61]

31. On exceptions, SFPP and CC Shippers both asserted the 2008 SFPP ID's use of SFPP's total North and Oregon Line revenues rather than the revenues generated by the grandfathered portion of those rates was inconsistent with *America West*. They both opposed the 2008 SFPP ID's adoption of Trial Staff's margin methodology for determining whether there are substantially changed circumstances, again on the ground that this was inconsistent with *America West*. SFPP and CC Shippers also both opposed the 2008 SFPP ID's rejection of their respective methodologies for determining substantially changed circumstances. SFPP further opposed to the specific finding that there were substantially changed circumstances to the Oregon Line rates and objected to

---

[56] *Id.* P 408-410.

[57] *See* 18 C.F.R. § 342.2 (2010).

[58] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 413-415, 417.

[59] *Id.* P 408.

[60] *Id.* P 409.

[61] *Id.* P 408-409. Trial Staff reached the same conclusions for 2004, but 2004 is no longer at issue due to the April 2010 Settlement that resolved the 2004 complaints.

the 2008 SFPP ID's setting the threshold change in return required to establish substantially changed circumstances at 15 percent.

32. CC Shippers, in their brief on exceptions, opposed the 2008 SFPP ID's finding that there were no substantially changed circumstances to the North Line rates. They also opposed a related holding that it was unnecessary to address the reasonableness of the North Line rates given the finding that there are no substantially changed circumstances to those rates. They further objected to a holding that SFPP Shippers did not adequately challenge the indexed portion of the North and Oregon Line rates in their complaints. CC Shippers similarly asserted that the 2008 SFPP ID erred by holding that the Commission should not review cost-of-service matters relevant to the index-based rate increases that were in excess of the grandfathered rates. They argued this incorrectly limited their reparations of the rates they paid in 2003 and 2004 to the extent that SFPP's revenues for those years exceeded its 2003 and 2004 actual cost-of-service. CC Shippers also asserted the 2008 SFPP ID erred in adopting Trial Staff's proposed 1992 cost-of-service on the grounds that it did not reflect the rate design methodology that was actually in effect in 1992.

E. Commission Analysis

33. Given the different interpretations of the *America West* decision the parties raise in the 2007 Calnev Complaints and the SFPP Proceeding, the Commission first provides below a fuller analysis of the legal framework regarding substantially changed circumstances. Second, the Commission discusses the regulatory issues raised by *America West* focusing on how these issues were analyzed in the SFPP proceeding. Third, the Commission clarifies the method for determining substantially changed circumstances. Fourth, the Commission addresses certain technical issues that are unique to the 2007 Calnev Complaint proceedings.

1. The Legal Framework

34. As noted, in the SFPP Proceeding, SFPP, CC Shippers, and the Trial Staff all assert they have advanced the correct interpretation of the *America West* decision. These assertions are reviewed in light of the Commission's earlier June 2005 Order and the court decision in *ExxonMobil* reviewing that order. The June 2005 Order states:

> The Commission reiterates here that it is changes in return, and hence a pipeline's profit expectations, that ultimately determines whether there has been a change in the economic basis for the rate.[62]

---

[62] June 2005 Order, 111 FERC ¶ 61,334 at P 38.

In reviewing the June 2005 Order, the Court stated:

> FERC interprets the phrase "a substantial change has occurred after the date of the enactment of this Act . . . in the economic circumstances of the oil pipeline which were a basis for the rate" as requiring a substantial change in the overall rate of return of the pipeline, rather than in one cost element, such as a tax allowance .... In other words, it makes little sense to de-grandfather a rate when the pipeline is no more profitable – or perhaps even less profitable – than it was when the rate was grandfathered.[63]

The Court then explained the reasonableness of using a change in the rate of return as the method for determining whether there are substantially changed circumstances:

> Moreover, FERC's reading meshes with the purpose of the EPAct, as gleaned from its text and structure. The grandfathering provision of § 1803 is intended to insulate pre-existing rates from attack by ordaining them to be necessarily "just and reasonable." The most natural understanding of § 1803 is that Congress believed that the then-existing rates of return were not so large as to justify the added litigation costs of subjecting the rates to agency evaluation and judicial review. This inference comports with the streamlining goals of § 1801 and § 1802. It makes good sense, then, to de-grandfather rates only when the rate of return itself has changed. It is unclear why Congress would care if the underlying composition of a pipeline's costs has changed so long as the pipeline's rate of return has remained constant or decreased.[64]

While the June 2005 Order and *ExxonMobil* both speak of a change in profitability, the June 2005 Order uses the term "return" while the court uses the phrase "rate of return." However return and rate of return are not necessarily the same concepts.

35. The distinction between the language in the June 2005 Order and that of the Court in *ExxonMobil* is telling. The word "return" appears in four different contexts under the Commission's Opinion No. 154-B oil pipeline rate making methodology,[65] three of which are terms of art regarding the cost-of-service methodology and one of which is a

---

[63] *ExxonMobil*, 487 F.3d at 959 (emphasis added).

[64] *Id.* at 959-60 (emphasis added).

[65] *Williams Pipe Line Company*, Opinion No. 154-13, 31 FERC ¶ 61,377 (1985) (Opinion No. 154-B).

derivation used for analytical purposes. The first is "allowed total return," which is determined by multiplying the weighted average of the cost of debt and the cost of equity times the net trended original cost rate base, and is reflected on Schedule 1, page 1, line 3 of a standard oil pipeline cost-of-service filing.[66] One of the subtractions from the allowed total return is "debt return" on line 7. Since allowed total return includes a debt component, the total return must be adjusted to eliminate that part of the regulatory return attributable to interest, and as such total return is not an indicia of profitability.

36. There are two additional contexts that the word "return" appears in the Commission's oil pipeline methodology. The most important one here is the "real equity rate of return," which is expressed as a percent at Schedule 1, page 2, line 13 of an oil pipeline cost-of-service.[67] The equity rate of return is derived on Schedule 11 as a percent and is included in the weighted cost of capital.[68] The second context is the so-called allowed dollar return, which is derived by multiplying the equity rate of return times the equity component of the pipeline's rate base.

37. Given this background, the Commission concludes that the Court's holding that profitability is measured by the rate of return on equity is the correct definition of return under EPAct. As the Court implied in its analysis, it is the rate of return that is used to measure profit when designing a just and reasonable rate. Indeed, in its analysis, the Court notes the relationship of rate reasonableness to the pipeline's costs, and by implication to the rate of return embedded in an oil pipeline's regulatory cost-of-service, stating:

> The ICA prohibits pipelines from charging rates that are "unjust or unreasonable" and permits shippers to challenge both pre-existing and newly filed rates. 49 U.S.C. app. §§ 13(1), 15(1), (7). FERC has generally approved just and reasonable rates based primarily on a pipeline's costs.[69]

This explicit reference to rate reasonableness and the pipeline's cost ties directly to the Court's central premise that "[i]t is unclear why Congress would care if the underlying composition of a pipeline's costs has changed so long as the pipeline's rate of return has

---

[66] *See* SFPP Compliance Filing, Docket No. OR92-8-027, *et al.*, at Tab A, Schedule 1, Page 1, Line 3 (filed February 26, 2008).

[67] *Id.* at Tab A, Schedule 1, Page 2, Line 13.

[68] *Id.* at Tab A, Schedule 11.

[69] *ExxonMobil*, 487 F.3d at 956.

remained constant or decreased."[70] Because a pipeline may recover its reasonable operating costs and prudent rate base investments, together with its debt financing costs, it is the equity return over those costs that is the final measure of profitability and places the ultimate limit on the pipeline's revenue requirement and its rates.

38. However, as the three different interpretations of *America West* presented in the SFPP proceeding indicate, the issue the Commission must decide is whether the Court's use of "rate of return" in *ExxonMobil* means that the change in return required to establish substantially changed circumstances is literally the change in the rate of return [on equity], or whether some proxy or simpler form of measurement may be appropriate. As SFPP points out,[71] the June 2005 Order analyzed the percentage change in volumes and the percentage changes in several key cost factors.[72] The June 2005 Order also compared the percentage change in volumes to the change in total costs as checks on the other calculations.[73] The use of this "broad" measure of a change in profitability was challenged, but the Court did not reach such issues because they were not raised to the Commission on rehearing.[74] It was in this context that the Commission made the *America West* decision.

2. ***America West* Revisited**

39. In the December 2007 *America West* decision, the Commission sought to clarify the method for determining substantially changed circumstances. Thus that order is the basis for several issues raised on exceptions in the SFPP Proceeding. These include whether: (1) the Commission should only use actual dollars to quantify any changes in revenue and costs; (2) the Commission should use total revenues or only revenues generated by the grandfathered rate level in any calculations; (3) the Commission should

---

[70] *Id.* at 959-60. For the Commission's emphasis on the return on equity in determining whether a rate is just and reasonable, *see Natural Gas Pipeline Company of America LLC*, 129 FERC ¶ 61,158, at P 5 (2009); *Northern Natural Gas Company*, 129 FERC ¶ 61,159, at P 4 (2009); *Great Lakes Gas Transmission Limited Partnership*, 129 FERC ¶ 61,160, at P 5 (2009).

[71] *See* 2008 SFPP ID, 125 FERC ¶ 63,018 at P 375-376, 398; SFPP Brief on Exceptions at 13-15.

[72] June 2005 Order, 111 FERC ¶ 61,334 at P 36, 39-40.

[73] *Id.* n.56.

[74] *ExxonMobil*, 487 F.3d at 961-62.

base a calculation on revenues that are less than those stated in the pipeline's regulatory cost-of-service in the base year; (4) *America West* intended to change the Commission's prior approach to determining substantially changed circumstances; (5) *America West* adopted a change in margins as the method for determining substantially changed circumstances; and (6) whether *America West* precluded the use of the change in return on equity as a method for determining substantially changed circumstances.

a. Use of Dollars for the Revenue Calculation

40. In *America West,* the Commission concluded that the soundest metric for quantifying changes was the actual amount of the pipeline's revenues and expenses.[75] Moreover, the Commission stated that "if the Complainants choose to amend their complaints, they should compare the change in actual revenues and expenses to determine the change in profit margins."[76] The Commission thereby intended that volumes should not be used as a proxy for revenues in evaluating whether there are substantially changed circumstances. There should be no further debate on this issue given this language requiring the use of revenues and expenses in determining if there are substantially changed circumstances. Moreover, *ExxonMobil* explicitly approved the Commission's decision not to rely on any one cost factor in its determinations because changes to the individual cost factors within a pipeline's cost-of-service structure may offset each other.[77] Notably, all the methodologies presented in the SFPP Proceeding were ultimately grounded in the actual dollar changes to revenues and costs.

b. Use Total or Grandfathered Revenues

41. As noted, the 2008 SFPP ID concluded that the Commission should use total jurisdictional revenues to evaluate whether there were substantially changed circumstances, not just revenues generated by the pipeline's volumes times the initial level of the grandfathered rate.[78] This issue arose because *America West* contains an explanation of several ways an increase in return could manifest given the presence of grandfathered rates, together with a mathematical example. The order stated this could occur if an increase in volumes resulted in greater revenue from the grandfathered rate and this exceeded total costs, if the revenue from the grandfathered rate was constant but

---

[75] *America West*, 121 FERC ¶ 61,241 at P 8.

[76] *Id.*

[77] *ExxonMobil*, 487 F.3d at 961-62.

[78] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 417.

costs declined, or by some combination of a volume driven revenue increase and actual cost decreases.[79] That analysis and example led Calnev, SFPP, and most shipper parties to conclude that the Commission should evaluate substantially changed circumstances by using only the revenue generated by the grandfathered rate compared to current expenses. In contrast to the 2008 SFPP ID, these parties concluded the Commission should exclude the portion of total revenue generated by any indexed-based increases from any calculation of whether there were substantially changed circumstances.[80]

42. Calnev, SFPP, and the shipper parties reasonably read *America West* as excluding from the determination of substantially changed circumstances, revenues generated by the oil pipeline indexing methodology based on the examples attached to that order. However, the 2008 SFPP ID was correct that the analysis in *America West* order should have permitted revenue growth from the indexing methodology, at least as a starting point for the analysis. This is because increased revenue can come from increased volumes at the same rate, from additional revenues generated by the indexed-based rates, or some combination of both. Thus, if revenues are equal to costs over time, this may occur if: (1) one of those two sources of increased revenue equals the increase in costs, (2) a combination of those two sources of revenue increases equals the cost increases, or (3) revenue increases and cost decreases preserve the existing ratio of revenues and expenses.

43. *America West* did not allow for situations where the indexing mechanism might be the means, or one of the means, by which the pipeline's return is sustained or enhanced. For example, it is possible for total costs to increase by a given percent and under the indexing methodology for the rates to increase at the same percent. If volumes remain the same, then revenues will increase in proportion to costs and the pipeline's return will not change.[81] However, if volumes increase over time, the indexed rates will normally generate revenues faster than the cost increase. This is because over time more barrels are moved at those higher per-barrel rates. In this situation, the greater increase in revenues results from both the index-based increase to the rates and the increase in volumes. Thus one would understate the implied increase in return if one excludes any

---

[79] *America West*, 121 FERC ¶ 61,241 at P 12.

[80] *See* 18 C.F.R. § 342.0 through § 342.4 (2010) for the procedures to be applied annually under the indexing methodology.

[81] Under the most rigorous assumptions the statement should also probably assume that the capital structure and rate base remain constant. *Cf.* Calnev March 3, 2008 Consolidated Response at Ex. 3 at 12.

index-based increase in revenue is excluded when determining the change in return, regardless of how the concept of "return" is defined.

44. Moreover, any analysis is further complicated by the fact that both Order No. 561 and the Commission's indexing regulations recognize that revenues generated by rate increases under the indexing methodology may exceed the pipeline's actual cost increases to the point that the resulting rates may be unjust and unreasonable.[82] As Calnev and SFPP each state, if this occurs, the Commission can reduce a rate to the level of the pipeline's actual costs without addressing whether there are substantially changed circumstances to the grandfathered rate. But the Commission also recognized that the reduction of the index-based portion of a rate may not always result in just and reasonable rate if a pipeline's rate base or cost-of-capital decline to the point where the grandfathered rate would exceed the level of a cost-based, going-forward rate resulting from the lower cost structure.[83]

45. The Commission believes *America West* incorrectly implied that one should exclude revenue gains from the indexing methodology from a determination of substantially changed circumstances in all cases. However, another concern was that substantially changed circumstances not be an issue when a simpler proceeding to eliminate an unreasonable over-recovery is available, i.e., a complaint proceeding challenging a cumulative increase based on the indexing methodology. Accordingly, the Commission concludes that when challenging an oil pipeline's rate, particularly the grandfathered portion of a rate, a complainant must first show reasonable grounds to conclude that the rates at issue are unjust and unreasonable.[84] Second, if the complainant seeks a rate that is less than the grandfathered rate, it must also provide reasonable grounds to conclude that the challenged rate must be reduced below the grandfathered rate to obtain a rate that is just and reasonable.

46. The first step in analyzing whether there are substantially changed circumstances is to posit a rate that, when multiplied by the pipeline's current volumes, equals the total cost-of-service on page 700 of the pipeline's annual FERC Form No. 6, and determine whether that rate exceeds the grandfathered rate. If the posited rate is more than the grandfathered rate, and the complainant still believes the existing rate is unjust and unreasonable, the second step is to explain what adjustments to the existing cost-of-

---

[82] *See* Order No. 561, FERC Stats. & Regs. at 30,954.

[83] *See* Opinion No. 435, 86 FERC at 61,067.

[84] *See ExxonMobil v. Calnev*, 120 FERC ¶ 61,075 at P 4; Order No. 561, FERC Stats. & Regs. at 30,956, 30,964-65.

service would warrant a lower rate. Again the analysis must compare the resulting rate to the grandfathered rate. If, in either step one or two, the proposed going-forward rate is less then the grandfathered rate, the complainant must establish that an increase in the rate of return since the effective date of the EPAct supports a finding of substantially changed circumstances under the methodology discussed in this order.

47. Finally, to assure there is no confusion, it should be noted that index-based increases are not grandfathered even if the increase is applied onto a grandfathered rate. Order No. 561 so provides,[85] and the Commission stated in subsequent orders that the indexed portion of index-based rates are subject to challenge if there are reasonable grounds to conclude that pipeline's existing rates are unjust and unreasonable.[86] The EPAct protects shippers from unjust and unreasonable rates, not returns.[87] While the Commission intends its indexing methodology to stabilize returns without the need for frequent and expensive general rate case proceedings, that methodology does not protect rates that diverge from the pipeline's costs to the point they are no longer just and reasonable. Thus the Commission recognizes that a complaint may challenge a pipeline's rates because changes to the cost and revenue factors embedded in its cost-of-service or the cumulative increases from indexing unreasonably exceed the pipeline's actual cost increases, or that an unreasonable rate results from a combination of those factors.[88]

c. Did *America West* Modify the Prior Methodology?

48. The issue discussed is whether the Commission intended its decision in *America West* to change the methodology for determining substantially changed circumstances contained in the June 2005 Order beyond the order's requirement that all revenues and costs be stated in dollars. As noted, the 2008 SFPP ID concluded that *America West*

---

[85] Order No. 561, FERC Stats. & Regs. at 30,941, 30,951, 30,955-56.

[86] *America West*, 121 FERC ¶ 61,241 at P 13; *BP West Coast v. Calnev*, 121 FERC ¶ 61,242 at P 12; *ARCO v. Calnev Pipe Line L.L.C.*, 97 FERC ¶ 61,057, at 61,311 (2001).

[87] Section 1803(b)(1)(A) of EPAct of 1992 states that the change is to "the economic circumstances of the oil pipeline that were the basis for the rate." (emphasis added). Congress did not use the word "return," and if it had, this would imply that the return, and thus the rate, was a just and reasonable rate that was beyond challenge, not just one that was presumed just and reasonable until the threshold standard was met. *See ExxonMobil*, 487 F.3d at 959-60.

[88] *America West*, 121 FERC ¶ 61,241 at P 13.

represented a shift to measuring any change in return after the effective date of EPAct against the return embedded in the rate. The 2008 SFPP ID also held that *America West* did not contemplate a broad proxy such as the change in the ratio of total expenses and total costs advanced by SFPP. The 2008 SFPP ID rejected SFPP's and the CC Shipper's approaches and accepted the Trial Staff's method of comparing the change in margins.[89]

49. On exceptions in the SFPP Proceeding, SFPP asserted the 2008 SFPP ID erred in not adopting SFPP's proposed ratio methodology. SFPP argued that the ALJ should have used its ratio methodology to discern a broad measure of change in return based on the change in the relationship between total revenues and total costs, which SFPP characterized as a gross margin approach. It asserted this approach is consistent with the Commission's historical use of a broad measure of change in the pipeline's return.[90] SFPP maintains its approach follows that used in the June 25 Order, but with two significant changes designed to correct and clarify the June 25 Order approach. First, SFPP stated it used actual revenue dollars and costs. Second, SFPP claims it properly began with the grandfathered revenues and total costs in each of the base, complaint, and 1992 years and expressed those revenues and costs as a ratio. The ratio in the base year is weighted by the relationship of revenues and expenses in that year, and the weighting factor is then applied to the revenues and expenses in future years.

50. While SFPP further asserted that given the Commission's historical use of a broad measure of return, it asserts that SFPP Shippers' use of return or rate of return as the measure of change was incorrect because the change in return would be measured only against the equity rate of return embedded in the pipeline's cost-of-service. SFPP opined that SFPP Shippers' approach results in the use of a narrower denominator for measuring a percentage change than comparing the difference in ratio of revenues and expenses among the periods used to evaluate substantially changed circumstances. SFPP also asserted that Trial Staff's approach may assume an embedded margin of zero, and thus presents a mathematical impossibility.

51. While their methodologies differ, both Trial Staff and SFPP Shippers maintain that *America West* marked a shift to measuring substantially changed circumstances by the change in the pipeline's return. Thus, while *America West* may not have clearly defined the term "return," both agree that SFPP's methodology of comparing the change in the ratio of total revenues to total costs has nothing to do with measuring a change in

---

[89] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 414-417.

[90] SFPP Brief on Exceptions at 27-30.

return.[91] As such, they assert that SFPP's weighting approach does not address the fundamental issue and is of little relevance here. SFPP Shippers and Trial Staff are correct that *America West* did not provide a precise definition of "return" despite the frequent use of the words "return" and "margin." However, *America West* should be read in the light of the use of the phrase "rate of return" in *ExxonMobil*[92] and *America West*'s references to the embedded return.[93] The problem with SFPP's broad measure of change and the one used in the June 2005 Order is that a change in ratio of total revenues to total expenses only indicates the direction of a change in return. However, it does not measure with any precision a change in subsequent returns against the return embedded in the grandfathered rate. As the court stated:

> The grandfathering provision of § 1803 is intended to insulate pre-existing rates from attack by ordaining them to be necessarily "just and reasonable." The most natural understanding of § 1803 is that Congress believed that the then-existing rates of return were not so large as to justify the added litigation costs of subjecting the rates to agency evaluation and judicial review. This inference comports with the streamlining goals of § 1801 and § 1802. It makes good sense, then, to de-grandfather rates only when the rate of return itself has changed.[94]

Given this language, a methodology that lacks a reasonably direct correlation between the embedded rate of return and change in that return over time is unlikely to survive review.

52. The difference between SFPP's methodology and one that actually measures the change from the grandfathered rate of return can be demonstrated by the following. Assume the pipeline has total operating costs of $90 and an equity rate of return of $10, for $100 in total regulatory costs. The equity component of the rate base is $100, which means an equity rate of 10 percent ($100 divided by $10 equals 10 percent). Total revenues are also $100, which means that the pipeline is just recovering its total regulatory cost-of-service of $100. As was previously discussed, under SFPP's approach the ratio of total revenues to total costs is 1.0 to 1.0. If in a subsequent year the revenues become $110 and costs $100, the difference between revenues and costs is now $10, or a

---

[91] ConocoPhillips Brief Opposing Exceptions at 13, 17; BP West Coast Brief Opposing Exceptions at 8-9; Trial Staff Brief on Exceptions at 62-63.

[92] *ExxonMobil*, 487 F.3d at 959-60.

[93] *America West*, 121 FERC ¶ 61,241 at P 9, 12, 14.

[94] *ExxonMobil*, 487 F.3d at 959-60 (emphasis added).

ratio of 1.1 to 1.0. This results in a 10 percentage point change in the ratio of total revenues to total costs, and by SFPP's theory this equals a 10 percent increase in the grandfathered return. However, the actual increase in the rate of return is 100 percent because the total dollar return becomes $20 instead of the original $10.[95] Thus the rate of return is now 20 percent on the equity rate base of $100 ($100 divided by $20 is 20 percent), a level far in excess of the Commission's current target rate of return for jurisdictional gas pipelines[96] or what it has approved for oil pipelines.[97] While the mechanics of SFPP's overall approach are hard to follow, this example supports the 2008 SFPP ID's and the CC Shippers' conclusions that SFPP designed its methodology to dilute any change in return.[98] By using only a broad measure of change in total revenues and total costs, the methodology that SFPP and Calnev both advance neutralizes the impact of any changes in rate base and capital structure that would otherwise be reflected in a change in the rate of return on equity.

53. The Commission recognizes that *America West* did not address the rate of return issue in the detail suggested by the above example. However, *America West* does speak in terms of profitability, margin, and return, and includes an example, while not well articulated, of how a change in return based on actual revenues and expenses could exist. Moreover, *America West* refers to the "embedded return" of the grandfathered rate at least twice.[99] Given the specific language in *ExxonMobil* that the change in the rate of return is the Commission's method and the marked understatement of a change in the rate of return that would occur under SFPP's method, the Commission now clarifies that *America West* should be understood as contemplating a shift away from the broad measure of change advanced by SFPP and from the broad measure of change used in earlier March 2004 and June 2005 Commission orders.[100] Therefore, the Commission

---

[95] CC Shipper's witness Matthew P. O'Loughlin's testimony effectively makes this point. *See* Prepared Rebuttal Testimony of Matthew P. O'Loughlin on Behalf of Chevron Products Co. and ConocoPhillips Co., Docket No. OR03-5-001 at Ex. CC-44 at 37-38, 40-41.

[96] *See Portland Natural Gas Transmission System*, Opinioin No. 510, 134 FERC ¶ 61,129, at P 162 (2011).

[97] *See SFPP, L.P.*, 134 FERC ¶ 61,121 at P 193 (2011) (Opinion No. 511).

[98] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 352-353; Ex. No. CC-44 at 60-61.

[99] *America West*, 121 FERC ¶ 61,241 at P 7, 9.

[100] March 2004 Order, 106 FERC ¶ 61,300 at P 37-38, 53-58, 61-62, 66-67 and Appendix A; June 2005 Order, 111 FERC ¶ 61,334 at P 30, 38-39.

holds that the appropriate method to determine whether there are substantially changed circumstances is to measure the change in the rate of return on equity from that embedded in the grandfathered rate.

d. Does *America West* Require the Use of a Change in Margin as the Method for Measuring a Change in Return on Equity?

54. Above, the Commission concludes that *America West* marks a departure from the "broad measure" of return contained in the March 2004 and June 2005 Orders to one based on the change in the rate of return on equity. However, a related issue is whether the use of a change in dollar margins is an appropriate method for determining the changes in the pipeline's rate of return. The 2008 SFPP ID concluded that Trial Staff's methodology was the one that most closely conformed to *America West* because Trial Staff used a change in margin approach.[101] On exceptions, both SFPP and the CC Shippers assert that Trial Staff's approach is neither a measure of margin nor a measure of return.[102] The CC Shippers in particular argue that measuring the change in the difference between total revenues and total costs does not measure a change in return because Trial Staff's approach does not reflect the rate of return that is embedded in a pipeline's rates.[103] They claim that Trial Staff's approach departs from the premise in *America West* that substantially changed circumstances are determined by changes in return on equity. SFPP argues Trial Staff's approach was incorrect and seeks to revise it to fit its own ratio approach.

55. CC Shippers are correct that *America West* did not intend to substitute "margin" as the method for determining substantially changed circumstances. The relevant language relies on the change in actual revenues and expenses to determine the change in profit margins. The order directs the parties to compare the profit margins, which are net dollars in percentage terms without any mathematical errors. In that discussion, the emphasis is on how to properly measure the difference between revenues and expenses without any such errors.[104] In fact, the next paragraph, while discussing a different point, states the pipeline normally imputes a profit margin equal to or more than the regulatory

---

[101] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 417.

[102] SFPP Brief on Exceptions at 28-29; ConocoPhillips Brief on Exceptions at 12-16.

[103] ConocoPhillips Brief on Exceptions at 13.

[104] *America West*, 121 FERC ¶ 61,241 at P 8.

return embedded in the rate.[105] *America West* thus recognizes that the change measured is the change from the return embedded in the rate. For example, *America West* states that "one measures substantially changed circumstances by relative profit or return" and further notes that "[c]omplainants' approach thus overstates the percentage gain in return."[106] While the mathematical example in the same paragraph may have created some ambiguity, the Commission did not intend to use a change in profit margin as the method to measure a change in return.

56. The complainant shippers in the SFPP Proceeding are also correct that Trial Staff's margin approach fails to reflect either the dollar return or the rate of return embedded in a pipeline's cost-of-service.[107] Neither of these returns is normally embedded in the cost structure of an unregulated company. While *America West* speaks at points of a change in margins, this was not intended as a measure of return. Accordingly, the Commission declines to adopt Trial Staff's method.

e. Adopting the Change in Rate of Return on Equity Methodology

57. As discussed in the previous sections, neither SFPP's broad measure of change methodology nor Trial Staff's margin methodology were appropriate methods for determining whether there are substantially changed circumstances. In the SFPP Proceeding, the CC Shippers argue that its approach is the only one that attempted to calculate a change in the embedded return.[108] SFPP argues in reply that CC Shippers' methodology leads to inconsistent results because it measures a dollar change in return

---

[105] *Id.* P 9.

[106] *Id.*; *see also id.* P 12, 14.

[107] The following illustrates these issues. Assume that the pipeline's total cost-of-service is $100 and includes a 10 percent rate of return on equity, which yields a $10 return on an equity rate base of $100. Thus the other regulatory components of the pipeline's cost-of-service are $90. Now assume the pipeline's total revenues increase to $105 while total costs remain at $100. Trial Staff would say that the margin, and hence the return, had increased by $5 or 5 percent. But the increase of $5 in revenue is added to the $10 equity already embedded in the pipeline's cost-of-service. This provides a total return of 15 percent on the equity rate base, where the equity rate base remains at $100. Since the original return was 10 percent, this is an increase of 50 percent in the embedded rate of return ($5 divided by $10), not five percent as Trial Staff suggests.

[108] ConocoPhillips Brief on Exceptions at 21-25, 32-33.

against the embedded dollar return or the embedded rate of return. SFPP also asserts that the use of a narrower denominator in calculating a change in return will lead to more frequent findings of substantially changed circumstances, and this approach will discriminate against older pipelines. Thus SFPP argued that Trial Staff's approach, if modified, is preferable to that of CC Shippers.

58. Given the court's emphasis on rate of return in *ExxonMobil*[109] and our analysis *supra*, the Commission concludes the change in the rate of return on equity is the proper methodology for determining whether there are substantially changed circumstances. CC Shippers construed *America West* as limiting the analysis to revenues generated by the grandfathered rates and precluded measuring the change in return using a B revenue calculation that is less than the revenues that are included in the base period. While CC Shippers correctly conclude that the change in the rate of return is the best method, the limitations in their analysis preclude its acceptance. SFPP's reservations regarding the Commission's adoption of a rate of return on equity method and some practical implications of that method are examined in the next section.

3. Implementing a Rate of Return on Equity Methodology

59. The Commission concludes that the change in the equity rate of return as outlined here is the most appropriate methodology for determining whether there are substantially changed circumstances. The remaining question is what kind of quantitative standards should the Commission use to determine whether "the rate of return itself has changed."[110] The 2008 SFPP ID concluded that the threshold for measuring a change in return should be 15 percent, citing prior Commission decisions.[111] In the SFPP Proceeding, the litigant shippers and the Trail Staff support this conclusion as the one most consistent with the Commission's earlier decision. In contrast, SFPP notes that in the March 2004 and June 2005 Orders there is only one example of a finding of substantially changes circumstances where the change did not exceed 25 percent and that in all cases the change in return was at least 20 percent.[112] SFPP further asserts that the March 2004 Order rejected a change of 18 percent, which demonstrates that a 15 percent threshold is too low. SFPP posits that there is no basis to find that a 15 percent threshold is appropriate. SFPP further argues this point is important as a rate of return method

---

[109] *ExxonMobil*, 487 F.3d at 959-60.

[110] *Id.* at 959.

[111] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 418-419.

[112] SFPP Brief on Exceptions at 23-24.

likely will result in more frequent findings of substantially changed circumstances because complainants will base the percentage calculation on a much narrower denominator. SFPP therefore asserts the Commission should use a higher threshold if the change in the equity rate of return determines whether there are substantially changed circumstances.

60. The March 2004 and June 2005 Orders adopted a 25 percent threshold with only one exception.[113] Moreover, as SFPP points out, this was in the context of a method that was less likely to result in a finding of substantially changed circumstances than the rate of return method adopted here. As shown by the examples below, the return on equity method adopted here may result in more findings of substantially changed circumstances. Returning to the examples used above, assume under SFPP's broad measure approach revenues and costs are both $100. Thus, the ratio of revenues to total costs is 1.0 to 1.0 in the first year. If in a subsequent year the revenues become $110 and costs remain $100, the difference between revenues and costs is now $10, or a ratio of 1.1 to 1.0. This results in a 10 percentage point change in the ratio of total revenues to total costs. However, as has been discussed, under the Commission's regulatory costing methodology the $100 in costs includes an embedded return on equity of $10. Given a $10 increase in revenues and constant costs, the increase in the rate of return is 100 percent. This is because one measures the $10 increase in the return against the denominator of the $10 return on equity embedded in the cost-of-service. We believe the Commission's methodology adopted here may lead to more findings of substantially changed circumstances. Therefore if this method is to comport with the streamlining goals of EPAct, we will not reduce the minimum standard below the 25 percent generally used in our prior orders.

61. Further, the Commission notes this 25 percent threshold is not a bright-line standard such that any change in the rate of return greater than 25 percent is a conclusive determination that substantial change in circumstances exists. Rather, the Commission will carefully examine any evidence submitted in support of a complaint to assure that the change in the rate of return is in fact "substantial." The dictionary definition of that term addresses quality as well as quantity. The word "substantial" denotes: (1) not imaginary, true, real; (2) solidly built, strong; or (3) ample, sustaining.[114] Thus, in a case where the change in the equity rate of return is greater than 25 percent, the Commission would consider whether the test year reflects an unrepresentative short term or anomalous

---

[113] March 2004 Order, 106 FERC ¶ 61,300 at P 53-54, 57-58, and Appendix B, Tables 2 and 3; June 2005 Order, 111 FERC ¶ 61,334 at P 38-39 and Appendix, Table 3.

[114] American Heritage Dictionary of the English Language; Houghton Mifflin at 1284 (1976).

change in return when determining whether the change is actually "substantial." An unrepresentative change could occur because of minor changes in the balance sheet or capital structure, a spike in expenses or revenues, non-recurring revenue from payments for an accidental loss, or a one time sale or other gain or loss. Therefore in order to sustain a finding of substantially change circumstances, a complainant must show that there has been a consistent and sustainable increase in the pipeline's rate of return prior to the complaint year. Thus a change in an unrepresentative complaint year will not support the required statutory finding.

62. Another possible anomalous result from use of the change in the equity rate of return method may be demonstrated as follows. First, assume an embedded rate of return on equity of 20 percent in the base year (A) and that the 1992 realized rate of return on equity (B) is the same. The rate of return on equity in the complaint year is 25 percent (C), and thus arguably meets the threshold under the (C-B)/A formula if the sustainability criteria are also met.[115] However, if the embedded rate of return on equity in the base year (A) and in year 1992 (B) is 9 percent and the rate of return on equity in the complaint year (C) is 12 percent, the increase in the rate of return on equity is 33 percent.[116] However, the 12 percent return in the complaint year in this example is within the target range of reasonableness reflected in recent a recent gas pipeline complaint proceeding or the nominal return afforded SFPP in a different proceeding.[117] Given the streamlining purposes of the EPAct,[118] it is irrational to investigate the issue of substantially changed circumstances unless there were convincing grounds that the return in the complaint year was unreasonable and there are reasonable grounds to believe the prospective rate will need to be substantially less than the grandfathered rate of return to achieve a just and reasonable prospective rate.

63. Finally, SFPP asserts the use of a return on equity method will more often impact older pipelines because they have lower rate bases, and hence a lower equity component to their rate base, making it more likely to find substantially changed circumstances exists. While this is a likely result, the simple fact is that as the rate base declines the return generated by the historical rates can materially increase. The Commission recognized this possibility in Opinion No. 435. The Commission noted that a significant

---

[115] (25-20)/20 = 25 percent.

[116] (12-9)/9 = 33 percent.

[117] *See* Opinion No. 510, 134 FERC ¶ 61,129, at P 162, Opinion No. 511, 134 FERC ¶ 61,121, at P 193.

[118] *ExxonMobil*, 487 F.3d at 957.

decline in the rate base could lead to substantially changed circumstances.[119] The issue is not one of discrimination against older pipelines as SFPP alleges, but a reflection of how pipelines amortize their rate base and the mechanics of EPAct. Consistent with the caveats discussed above, the Commission concludes the most appropriate method for determining substantially changed circumstances is the degree of change in the equity rate of return embedded in the grandfathered rate at the time that rate was established.

4. Further Cost-of-Service Analysis

64. As noted, the 2008 SFPP ID held it was unnecessary to investigate the reasonableness of the North Line rates given the finding that there were no substantially changed circumstances to those rates.[120] Trial Staff supports the 2008 SFPP ID on the ground that if a rate is grandfathered, the indexed portion of the rate is also grandfathered. As discussed *supra*, this is incorrect.[121] SFPP supports the 2008 SFPP ID on a narrower point and argues the litigant SFPP shippers failed to present any evidence that the revenue indexed portion of the grandfathered rate so substantially exceeded the actual cost increases that the resulting rate is unjust and unreasonable, citing 18 C.F.R. § 343.2.

65. The Commission's indexing regulations provide, in part, that "[a] protest or complaint against a rate proposed or established pursuant to § 342.3 of this chapter must allege reasonable grounds for asserting . . . that the rate increase is so substantially in excess of the actual cost increases incurred by the carrier that the rate is unjust and unreasonable . . . ."[122] SFPP essentially argues this standard applies to every index-based increase taken by a pipeline and includes the entire increase in excess of the grandfathered rate. This argument is without merit for several reasons. First, the indexing methodology operates annually under the provisions of 18 C.F.R. § 342.3 as the cited language itself indicates. There can only be one rate to which section 343.2 applies. That rate is the rate established in a particular index year and against which a complaint is filed in that year. Any cumulative increases are outside the single year increase addressed by the regulations and are the consequences of rates filed in the past. SFPP's incorrectly conflates cumulative over-recoveries that may be caused by the indexing

---

[119] Opinion No. 435, 86 FERC ¶ 61,022 at 61,067; March 2004 Order, 106 FERC ¶ 61,300 at P 16, 29-30.

[120] 2008 SFPP ID, 125 FERC ¶ 63,018 at P 430-431.

[121] *See* SFPP Brief Opposing Exceptions at 30-31.

[122] 18 C.F.R. § 343.2(c) (2010).

methodology with the rate increase in a single year. As Order No. 561 states, shippers may challenge the cumulative increases, like other index increases under section 13(1) of the Interstate Commerce Act (ICA). Indexed rates are only presumed to be just and reasonable.[123]

66. SFPP's argument suffers from an additional flaw. At bottom, it implies that an over-recovery that causes a rate to be unjust and unreasonable stems primarily from indexing. This position has no merit. An over-recovery may be caused by long term revenue growth from increased volumes, a decline in overall costs, the indexing methodology, or some combination of these. In fact, it is possible that the index could decline in a given year while the over-recovery increases due to an increase in volumes. An increase in volumes results in higher revenues, and thus a recovery in excess of costs, even though the indexed rate that applies to those increased volumes was less than it had been in the prior year. Once one moves beyond the focus of a complaint directed against the indexed-based increase of a single year, there can be multiple causes that may result in an over-recovery by the pipeline that may provide reasonable grounds to conclude a rate is unjust and unreasonable. As the Commission has stated elsewhere, a complaint against the base rates may attack the cumulative increases under the indexing methodology, the underlying cost-of-service, or both.[124]

5. The Role of Economic Regulation

67. One additional issue is what regulatory cost methodology to use in the SFPP Proceedings. The issue raised by SFPP on exceptions is whether the Commission should base a cost-of-service on the original version of Opinion No. 154 methodology[125] or on the modifications occurring in later years.[126] SFPP recognizes that the Commission previously stated that regulatory change can be a factor in determining whether there are substantially changed circumstances. It asserts however that such changes should only include those that represent a fundamental change in regulatory philosophy, such as the adoption of the Opinion No. 154-B methodology, but not refinements to that methodology. SFPP asserts incorporating such changes would expose the pipeline industry to changes that had nothing to do with the economic circumstances of the

---

[123] Order No. 561, FERC Stats. & Regs. at 30,951, 30,955-56.

[124] *See BP West Coast Products, LLC v. SFPP, L.P.*, 121 FERC ¶ 61,243, at P 8-10 (2007) (*BP West Coast v. SFPP*).

[125] Opinion No. 154-B, 31 FERC ¶ 61,377.

[126] SFPP Brief Opposing Exceptions at 26-27.

pipeline. Conversely, in the 2007 Calnev Complaints, the complainant Calnev shippers assert the Commission recognizes that a change in methodology can be a factor in determining substantially changed circumstances and, therefore, they maintain the Commission must apply the most recent version of any rate methodology in any particular year under analysis.[127]

68. The Commission concludes that the complainant Calnev shippers are correct. Economic regulation is as much a part of a pipeline's commercial environment as demand, operating costs, the cost of capital, and taxes. All of these can vary from year-to-year and present different opportunities and risk at different times. This is also true of the legal framework within which today's pipelines operate and includes the regulatory methodology for determining the pipeline's costs. Any such methodology can change with experience or to the Commission's policy concerns. The changes in return on equity are to be measured by the regulatory circumstances that the pipeline faced at a given point in time prior to any remedial action by the Commission.

F. Technical Issues Related to the 2007 Calnev Complaints

69. Prior sections of this order explain the limitations in the various approaches to determining substantially changed circumstances since *America West* issued in December 2007 in response to the 2007 Calnev Complaints and the Commission's proposed clarifications and modifications. However, there is one technical issue regarding the 2007 Calnev Complaints that requires our attention prior to a hearing. Namely, how to calculate the return embedded in the grandfathered rates or the return that was actually realized for each year in the (C-B)/A formula. In the case of the initial grandfathered rates filed in 1991, the record contains a detailed justification filed by Calnev in support of those rates. The record reveals Calnev chose to accept a real return on equity of 8.75 percent.[128] Thus, contrary to the initial conclusion in *America West*, this 8.75 percent return controls even if it is less than what Calnev could have justified in its 1991 cost-of-service rate filing. As noted in *ExxonMobil*, oil pipelines often file for a return less than that allowed under the cost-of-service, perhaps due to competitive pressures or the desire to obtain rapid regulatory approval.[129] Calnev's embedded return

---

[127] *See* Amended Joint Complaint of America West Airlines, Inc. *et al.* dated February 11, 2008 at 6-7 and Supplemental Affidavit of Mathew P. O'Loughlin attached thereto at 8-10. This would include the definition of cost-of-service factors that may fall within the formulaic approach of the Opinion No. 154-B methodology.

[128] *See id.* at Attachment A to the Supplemental Affidavit of Matthew P. O'Loughlin.

[129] *ExxonMobil*, 487 F.3d at 961.

reflects the economic circumstances that were actually used to design the rates and not the hypothetical maximum cost-of-service that may have been theoretically available.

IV. Other BP West Coast Pleadings

A. Request for Rehearing or Clarification

70. BP West Coast filed a request for rehearing or clarification of *America West* and *BP West Coast v. Calnev* stating three concerns.[130] The Commission denied BP West Coast's request for rehearing by operation of law. However, the Commission will provide clarification regarding whether *America West* requires complainants to frame their complaints consistent with Commission policy or risk the possible dismissal of the entire complaint. BP West Coast questions whether this effectively precludes it from raising certain cost-of-service issues in a proceeding, and whether this would manifests a denial of due process.

71. In *America West*, which was an initial order on one of the 2007 Calnev Complaints, the Commission was faced with a complaint where complainants premised many of their initial arguments regarding substantially changed circumstances on cost-of-service adjustments that the Commission previously rejected several times. These arguments concerned the granting to a partnership an income tax allowance, as discussed in the December 2007 Order,[131] and the equity cost of capital issues, as discussed in the ROE Policy Statement.[132] There is no due process issue if the Commission rejects a complainant's analysis of substantially changed circumstances based on cost-of-service arguments that the Commission consistently rejects. Thus, as indicated in *America West*, if a party's cost-of-service arguments are wholly inconsistent with prior Commission decisions, the Commission will not make cost-of-service adjustments based on those arguments when determining whether there are substantially changed circumstances.

---

[130] The first is whether complainants may ask the Commission to review all grievances raised without risk of dismissal of an entire complaint. The second is whether the Commission justified a change in the standard for changed circumstances from that established in 2005 and approved in *ExxonMobil*. Third, BP West Coast asserts, that if a change was intended, then the new standard is inconsistent with EPAct.

[131] *SFPP, L.P.*, 121 FERC ¶ 61,240, at P 20-21 (2007) (December 2007 Order).

[132] *Composition of Proxy Groups for Determining Gas and Oil Pipeline Return on Equity*, 123 FERC ¶ 61,048 (2008) (ROE Policy Statement).

B. Amended Complaint Regarding Certain Terminal Charges

72. BP West Coast's second amendment to its 2007 Complaint challenges Calnev's charge for vapor recovery at its Las Vegas terminal. The Commission summarily dismisses this amendment. BP West Coast's amended complaint fails to allege adequate grounds why the vapor recovery charge is jurisdictional, and if so, unjust and unreasonable due to substantially changed circumstances with respect to that rate. BP West Coast is not precluded from filing a separate complaint against Calnev's vapor recovery charge provided it includes an initial analysis of the jurisdictional and reasonableness issues. The ruling here does not extend to terminal charges that are embedded in an interstate transportation rate or which are acknowledged as interstate charges because they are included in Calnev's interstate tariff. Whether these latter services are grandfathered and/or just and reasonable is an issue ripe for examination at hearing.

V. The 2009 Calnev Complaints

73. Tesoro and BP West Coast filed complaints in July 2009 asserting that Calnev's base rates were not just and reasonable based principally on the over-recovery of Calnev's cost-of-service reflected on page 700 of Calnev's 2009 FERC Form No. 6. Tesoro states that Calnev had an over-recovery of its cost-of-service of 37.1 percent in 2007 and 18 percent in 2008. Both Tesoro and BP West Coast question Calnev's overhead cost allocations, its allocation of costs between jurisdictional and non-jurisdictional services, Calnev's equity cost of capital, the method for calculating its rate base, the amortization of deferred earnings, debt cost, income tax allowances, throughput, and indexing. Both complainants request that these issues be set for hearing and request reparations and damages for the over-recoveries.

74. Calnev answered Tesoro's and BP West Coast's 2009 Calnev Complaints asserting that neither complainant has met the two standards for a base rate complaint as they failed to establish either: (1) that the cumulative increases from the index-based increases of the years now exceed the cumulative increases in the pipeline's actual costs to the point that the rates are unjust and unreasonable; or (2) that the components embedded in the pipeline's cost-of-service are improperly defined or no longer accurately measure its costs. It further asserts that the complainants' claims that Calnev's rates no longer accurately reflect its costs are based on items such as income tax allowance, ADIT, return, cost allocation and rate design (including overhead cost allocations) and

volumes, throughput, and indexing, arguments which the Commission has consistently rejected.[133]

75. Calnev also presented a table showing that for the years 2004 through 2008, the cumulative percentage increase in its costs was greater than the cumulative increase in the index in each of the years of that five year period. Calnev thus asserts that BP West Coast provides nothing to substantiate its claims and that Tesoro fails to address the point that Calnev's rate design may not reflect its actual costs. Finally, Calnev asserts that the requests for reparations should be denied because both complainants already have complaints pending for the year 2007 that would address the just and reasonable rates for all, if not most, of the period to which the 2009 Calnev Complaints are directed. Calnev thus concludes that both 2009 Calnev Complaints should be dismissed as neither meets the standards for filing a compliant against base rates.

76. On review, the Commission first notes that page 700 of a pipeline's FERC Form No. 6 is designed to reflect its current costs for the prior year under the Opinion 154-B costing methodology,[134] and thus accurately reflect the pipeline's jurisdictional throughput, revenues, costs, and return under a current, rather than a historical rate design. Calnev is correct that neither Tesoro nor BP West Coast have presented grounds to conclude that Calnev's cost-of-service structure either is inappropriate or that it does not reflect Calnev's costs under the Commission's Opinion No. 154-B methodology.[135]

77. Thus, the Commission would ordinarily find the 2009 Calnev Complaints inadequate except for the evidence of Calnev's continuing over-recoveries in 2007 and 2008. Tesoro correctly points out that in the 2007 *America West* order, the Commission held that there were reasonable grounds to conclude that Calnev's rates were unjust and unreasonable based solely on the approximately $14 million over-recovery of its cost-of-service in 2005 and the approximately $15 million over-recovery of its cost-of-service in 2006.[136] While the over-recovery then declined to approximately $8.3 million, these

---

[133] *BP West Coast v. SFPP*, 121 FERC ¶ 61,243 at P 10, *order on reh'g*, 123 FERC ¶ 61,121 (2008) (*BP West Coast v. SFPP* Rehearing Order).

[134] *See e.g.*, Calnev's 2008 FERC Form No. 6, Page 700, instruction 1, which states in part "[T]he values shall be computed consistent with the Commission's Opinion No. 154-B methodology." To be consistent with this standard the page 700 must reflect the Opinion No. 154-B methodology as applied to a year's cost-of-service components, including changes to the capital structure, equity return, and income tax components.

[135] Opinion No. 154-B, 31 FERC ¶ 61,377.

[136] *America West*, 121 FERC ¶ 61,241 at P 5.

consistently large over-recovery amounts are sufficient to avoid summary dismissal of the 2009 Calnev Complaints. This is because an over-recovery can result from: (1) revenue increases under the Commission's indexing methodology that are in excess of the actual cost increases; (2) a divergence between the pipeline's actual costs and the costs embedded in its existing rate design; and (3) an increase in volume that results in greater revenues and increased returns because the additional revenue generated exceeds the related variable costs.[137] In theory, all three of these could occur simultaneously or at different times and, individually or collectively could result in the jurisdictional over-recovery stated on page 700 of the pipeline's FERC No. 6 report in any given year. Calnev's 2008 page 700 provides reasonable grounds to conclude that Calnev's rates in that year may be unjust and unreasonable and to preclude dismissal of the complaints at this time.[138]

78. Although the 2009 Calnev Complaints have survived summary dismissal, several of Calnev's arguments warrant a fuller discussion; accordingly they are addressed below. Calnev correctly notes that there are currently pending complaints that address Calnev's base rates and its cost-of-service for the years 2006 and 2007. As such, Calnev reasonably asserts that if its rates are reduced in those years, this will likely eliminate any possible reparations under the 2009 Calnev Complaints. Calnev's argument has merit as evidenced below. If Calnev's rates are reduced, reparations may be paid to Tesoro and BP West Coast for the difference between: (1) the rates they paid in 2009 and (2) the new base rates for 2007 as indexed through 2009. This results in new effective rates for Tesoro and BP West Coast in 2009. As noted, Calnev's cost increases since calendar year 2007 have consistently exceeded the maximum allowed under the indexing methodology based.[139] As the oil pipeline indexing methodology is premised on the use of a current Opinion No. 154-B cost-of-service, if a new just and reasonable rate is established for 2007 and is indexed through 2009, it is unlikely that rate levels through

---

[137] *See BP West Coast v. SFPP* Rehearing Order, 123 FERC ¶ 61,121 at n.9, where the Commission recognized that an over-recovery could be caused "by cumulative increases in the index or some more fundamental change in the pipeline's revenues or cost-of-service." Any increase in volumes can be tracked by reviewing several years of page 700 data since the throughput is reflect annual on line 11 of page 700.

[138] *Cf. Cost-of-Service Reporting and Filing Requirements for Oil Pipelines*, Order No. 571, 59 FR 59137 (Nov. 16, 1994), FERC Stats. & Regs. ¶ 31,006, at 31,168, *order on reh'g*, Order No. 571-A, 69 FERC ¶ 61,411 (1994), discussing the preliminary screening function of the page 700 data.

[139] *See* Calnev Pipe Line LLC, Answer to Complaint of BP West Coast Products LLC, Docket No. OR09-20-000 at 6 (filed September 20, 2009).

2009 will be unjust and unreasonable since the resulting rates will be less than the cumulative increase in Calnev's cost-of-service. The Commission recognizes that this cannot be established with certainty until a cost-of-service determination has been made on the 2007 Calnev Complaints.

79. However, the Commission also concludes that resolution of all the outstanding complaints against Calnev's base rates will be advanced if the 2009 Calnev Complaints are set for hearing and consolidated with the 2007 Calnev Complaints. For example, the parties may find it in their interests to negotiate a package settlement for both the 2007 and 2009 Calnev Complaints. Moreover, if at hearing on the 2007 Calnev Complaints the presiding administrative law judge determines there are substantially changed circumstances to Calnev's 2007 base rates and the matter proceeds to a hearing on the issue of rate reasonableness, this would require establishing an appropriate cost-of-service for 2007.[140] It should then be relatively easy to update that cost-of-service in a summary form and to determine whether Calnev's revised revenues, as indexed, exceed the cost-of-service increases in the subsequent years under the Commission's indexing methodology. For these reasons the 2009 Complaint are set for hearing and are consolidated with the 2007 Calnev Complaints.

The Commission orders:

(A) The 2007 Calnev Complaints filed in Docket Nos. OR07-7-000, OR07-18-000, OR07-19-000, and OR07-22-000 are set for hearing on the issues of substantially changed circumstances and the reasonableness of Calnev's base rates in calendar year 2007. Issues of substantially changed circumstances are to be resolved based on the rulings in this order. If the presiding administrative law judge determines that there are substantially changed circumstances to Calnev's 2007 base rates, the 2007 Calnev Complaints shall proceed to hearing on the issue of reasonableness. The hearings on substantially changed circumstances and reasonableness may be combined if the parties and/or the presiding administrative law judge conclude that this would expedite resolution of the instant dockets. The foregoing dockets are consolidated.

---

[140] Proceedings involving substantially changed circumstances are technically bifurcated proceedings because there must be substantially changed circumstances to the rates at issue before the matter may proceed to a determination of reasonableness. However, because cost-of-service evidence is a material component of any such determination, it may be more efficient to have a combined hearing on both issues. As stated in the Ordering Paragraph (A), the parties and/or the presiding administrative law judge may decide to do so.

(B) The 2009 Calnev Complaints filed in Docket Nos. OR09-15-000 and OR09-20-000 are set for hearing on the issue of reasonableness only for the reasons stated in the body of this order, including possible settlement procedures, and are consolidated with Docket Nos. OR07-7-000, OR07-18-000, OR07-19-000, and OR07-22-000.

(C) Pursuant to the section 375.304 of the Commission's regulations, 18 C.F.R. § 375.304 (2010), the Chief Administrative Law Judge shall designate a presiding administrative law judge for the purpose of conducting a hearing. The ALJ is authorized to conduct further proceedings pursuant to this order and to the Commission's Rules of Practice and Procedure.

(D) The hearings established in Ordering Paragraphs (A) and (B) are hereby held in abeyance to provide time for settlement judge procedures, as discussed in Ordering Paragraphs (E) and (F) below.

(E) Pursuant to Rule 603 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.603 (2010), the Chief Administrative Law Judge is hereby directed to appoint a settlement judge in this proceeding within ten (10) days of the date this order. Such settlement judge shall have all powers and duties enumerated in Rule 603 and shall convene a settlement conference as soon a 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 within five (5) days of the date of this order.

(F) Within thirty (30) days of the appointment of the settlement judge, the settlement judge shall file a report with the Commission and 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 assign this case to a presiding judge for a trial-type evidentiary hearing. If settlement discussions continue, the settlement judge shall file a report at least every thirty (30) days thereafter, informing the Commission and Chief Judge of the parties' progress toward settlement.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

Document Content(s)

136 FERC ¶ 61,083
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
John R. Norris, and Cheryl A. LaFleur.

Tesoro Refining and Marketing Company v. Calnev Pipe Line LLC	Docket No. OR07-7-002 (consolidated)
America West Airlines, Inc. and US Airways, Inc. Chevron Products Company Continental Airlines, Inc. Northwest Airlines, Inc. Southwest Airlines Co. and Valero Marketing and Supply Company v. Calnev Pipe Line LLC	Docket No. OR07-18-002 (consolidated)
ConocoPhillips Co. v. Calnev Pipe Line LLC	Docket No. OR07-19-002 (consolidated)
BP West Coast Products, LLC v. Calnev Pipe Line LLC	Docket No. OR07-22-002 (consolidated)
Tesoro Refining and Marketing Company v. Calnev Pipe Line LLC	Docket No. OR09-15-001 (consolidated)
BP West Coast Products, LLC v. Calnev Pipe Line LLC	Docket No. OR09-20-001 (consolidated)

ORDER ON REQUEST FOR CLARIFICATION OR REHEARING

(Issued August 4, 2011)

1. This order addresses Calnev Pipe Line LLC's (Calnev) request for clarification, or in the alternative rehearing, of the paragraphs 78 and 79 of the Commission's March 17, 2011 order in the captioned dockets.[1] As discussed in detail below, the Commission denies the requested clarification and rehearing.

I. Background

2. In its March 2011 Order, the Commission consolidated six complaints against Calnev and set them for hearing. Four of the complaints were filed in 2007.[2] These 2007 complaints challenge all of Calnev's interstate rates, including both the grandfathered portion as well as the portion in excess of the grandfathered rate.[3] The other two complaints, filed in 2009 by BP West Coast and Tesoro, challenge Calnev's existing base rates as unjust and unreasonable.[4]

3. At issue on rehearing are paragraphs 78 and 79 of the March 2011 Order, in which the Commission explained why it set the 2009 complaints for hearing and consolidated them with the 2007 complaints. Specifically, the Commission stated:

> Although the 2009 Calnev Complaints have survived summary dismissal, several of Calnev's arguments warrant a fuller discussion; accordingly they are addressed below. Calnev correctly notes that

---

[1] *Tesoro Refining and Marketing Co., et al. v. Calnev Pipe Line LLC*, 134 FERC ¶ 61,214 (2011) (March 2011 Order).

[2] The 2007 complainant shippers are: Tesoro Refining and Marketing Company (Tesoro); ConocoPhillips Co. (ConocoPhillips); BP West Coast Products, LLC (BP West Coast); and, jointly, America West Airlines, Inc., US Airways, Inc., Chevron Products Company, Continental Airlines, Inc., Northwest Airlines, Inc., Southwest Airlines Co. and Valero Marketing and Supply Company (ACV Shippers) (collectively the "Shippers" or "Shipper Complainants").

[3] Thus, the 2007 complaints raise issues of both substantially changed circumstances and rate reasonableness.

[4] The 2009 complaints do not challenge the grandfathered portion of Calnev's base rates.

there are currently pending complaints that address Calnev's base rates and its cost-of-service for the years 2006 and 2007. As such, Calnev reasonably asserts that if its rates are reduced in those years, this will likely eliminate any possible reparations under the 2009 Calnev Complaints. Calnev's argument has merit as evidenced below. If Calnev's rates are reduced, reparations may be paid to Tesoro and BP West Coast for the difference between: (1) the rates they paid in 2009, and (2) the new base rates for 2007 as indexed through 2009. This results in new effective rates for Tesoro and BP West Coast in 2009. As noted, Calnev's cost increases since calendar year 2007 have consistently exceeded the maximum allowed under the indexing methodology based. As the oil pipeline indexing methodology is premised on the use of a current Opinion No. 154-B cost-of-service, if a new just and reasonable rate is established for 2007 and is indexed through 2009, it is unlikely that rate levels through 2009 will be unjust and unreasonable since the resulting rates will be less than the cumulative increase in Calnev's cost-of-service. The Commission recognizes that this cannot be established with certainty until a cost-of-service determination has been made on the 2007 Calnev Complaints.

However, the Commission also concludes that resolution of all the outstanding complaints against Calnev's base rates will be advanced if the 2009 Calnev Complaints are set for hearing and consolidated with the 2007 Calnev Complaints. For example, the parties may find it in their interests to negotiate a package settlement for both the 2007 and 2009 Calnev Complaints. Moreover, if at hearing on the 2007 Calnev Complaints the presiding administrative law judge determines there are substantially changed circumstances to Calnev's 2007 base rates and the matter proceeds to a hearing on the issue of rate reasonableness, this would require establishing an appropriate cost-of-service for 2007. It should then be relatively easy to update that cost-of-service in a summary form and to determine whether Calnev's revised revenues, as indexed, exceed the cost-of-service increases in the subsequent years under the Commission's indexing methodology. For these reasons the 2009 Complaint [sic] are set for hearing and are consolidated with the 2007 Calnev Complaints.[5]

---

[5] March 2011 Order, 134 FERC ¶ 61,214 at P 78 and 79 (internal footnotes omitted).

II. The Pleadings

4. On April 18, 2011, Calnev filed a request for clarification, or in the alternative rehearing, regarding paragraphs 78 and 79 of the Commission's March 2011 Order. Specifically, Calnev requests clarification that paragraphs 78 and 79 do not preclude Calnev from developing a record at hearing to establish its actual cost-of-service and volume data "for the years at issue," presumably 2008 and 2009, for purposes of analyzing and accurately measuring the appropriate level of reparations that may be owed to the complainants. Calnev asserts that allowing it to fully develop the record concerning its actual costs and volumes would ensure that Calnev is not precluded from establishing that a higher 2008 or 2009 rate would be just and reasonable and that any reparations to be paid in that year should be limited accordingly.[6] Calnev states it is not seeking at this time to determine what reparations methodology might be reasonable, but only to develop a record that could address that issue.[7]

---

[6] Calnev provides the following example:

> If the Commission were to determine that, as of 2007, Calnev's pipeline rate level is no longer grandfathered, then . . . a new cost-based rate would . . . be determined as of that year. Based on Calnev's preliminary application of the Commission's discounted cash flow ("DCF") methodology, the real rate of return on equity for calendar year 2007 would be approximately 7.0 percent, and any cost-based rate calculated based on the 2007 data would utilize that 7.0 percent real equity rate of return. Paragraph 78 also indicates that this new 2007 rate would be indexed forward into the years 2008, 2009, and presumably onward, to determine any reparations owed by Calnev for those years. However, Calnev's preliminary DCF calculations, using actual data, yield a real rate of return on equity for 2008 of over 14.0 percent and approximately 8.8 percent for 2009. The wide variation in these preliminary equity rate of return calculations demonstrate that the application of a 2007 base rate to determine the 2008 or 2009 reparation amounts would likely result in significant overstatements of potential reparations for those years.

Calnev Request at 5.

[7] Calnev further argues that granting its requested clarification would not place an undue burden on the shipper complainants or cause undue delay.

5. In the alternative to the requested clarification, Calnev seeks rehearing of paragraphs 78 and 79. Calnev asserts that denial of its requested clarification would constitute a denial of due process by precluding Calnev from presenting information on its cost-of-service.

All of the Shipper Complainants oppose Calnev's request for clarification and/or rehearing.[8] The Shippers note that the March 2011 Order ruled that the appropriate level of reparations would be determined by establishing a just and reasonable rate for 2007, then "indexing forward" the new 2007 rate to determine the just and reasonable rate for subsequent years. Shippers state that this method of calculating reparations was established by the Commission in its Opinion No. 435 decisions[9] and approved by the U.S. Court of Appeals for the D.C. Circuit.[10] Shippers state that in contrast to this established method, Calnev seeks to introduce cost evidence for the purpose of justifying higher rates (and lower reparations) in the years following 2007 than would be derived by "indexing forward" the new 2007 just and reasonable rate that may be established in these proceedings. The Shippers argue Calnev's proposal is inconsistent with the Commission's indexing methodology[11] and violates the filed rate doctrine's rule against retroactive rate making. They further assert that Calnev's requested clarification would expand the scope of this proceeding by introducing a full evidentiary proceeding for the calendar years 2008 and 2009 (creating essentially a multitude of successive rate cases), which would be unduly burdensome to the parties and the proceeding. They also state that any increase in Calnev's cost of capital in 2008 or 2009 is built into the Commission's indexing methodology and therefore could be recovered through Calnev's indexing of the rates in those years. Finally, the shipper parties assert that the due process argument has no merit and wastes the Commission's resources.

---

[8] Specifically, on May 3, 2011, ConocoPhillips Company (Conoco), individually, and BP West Coast Products LLC, Tesoro Refining and Marketing Co., Valero Marketing and Supply Co., America West Airlines, Inc., Continental Airlines, Inc., Northwest Airlines Inc., Southwest Airlines Co., US Airways, Inc., and Chevron Products Co., jointly, filed answers to Calnev's request for clarification/rehearing. Ordinarily answers to rehearing petitions do not lie, but as the Calnev pleading is alternatively styled as a request for clarification, the answers are allowable and have assisted the Commission.

[9] Joint Shippers Answer at 3; Chevron Answer at 5-6 (*citing SFPP, L.P.*, 86 FERC ¶ 61,022, at 61,113 (1999) (Opinion No. 435) and *SFPP, L.P.*, 91 FERC ¶ 61,135, at 61,516-519 (2000) (Opinion No. 435-A)).

[10] Joint Shippers Answer at 3; Chevron Answer at 5-6 (*citing BP West Coast Products, LLC v. FERC*, 374 F.3d 1263, 1306 (D.C. Cir. 2004)).

[11] 18 C.F.R. § 342.3 (2011).

6. In addition, ConocoPhillips argues that Calnev's request raises an issue which was not previously raised in these proceedings. ConocoPhillips notes that the Commission does not permit new arguments to be raised on rehearing as it is disruptive to the administrative process because it has the effect of a moving target for parties seeking a final administrative decision.[12]

III. Discussion

7. Calnev's clarification/rehearing request does not actually speak to the issues raised in paragraphs 78 and 79 of the March 2011 Order. In the March 2011 Order, the Commission states that if as a result of the 2007 complaint proceedings Calnev's rates are reduced, "reparations may be paid to [shippers] . . . for the difference between: (1) the rates they paid in 2009 and (2) the new base rates for 2007 as indexed through 2009."[13] Those paragraphs recognized that an order reducing the indexed rates in effect in 2009 would likely result in rates that were less than Calnev's actual cost-of-service in 2008 or 2009.[14] And, if this occurred, there would be no practical purpose in proceeding with the 2009 complaints.

8. However, Calnev is not seeking clarification regarding the impact of the resolution of the 2007 complaints on the 2009 complaints. Rather, Calnev seeks advance permission from the Commission to submit evidence of actual cost-of-service and volume data for the years subsequent to 2007 for the purposes of determining reparations that may arise from resolution of the 2007 complaint proceedings. At bottom what Calnev appears to seek is the ability to establish actual cost-of-service rates, not indexed rates, for the calendar years 2008 and 2009 to determine the level of reparations that would be due in either or both of those years. While Calnev's proposal is contrary to the Commission's established method for determining reparations,[15] of concern at this stage in the proceedings is that Calnev is raising a new issue on rehearing – the scope of evidence it may submit in the hearing on the 2007 complaints regarding the appropriate method for calculating reparations. The Commission will not entertain new issues on

---

[12] ConocoPhillips Answer at 4 (*citing County of Butte, California v. California Department of Water Resources*, 129 FERC ¶ 61,133, at P 30 (2009)).

[13] March 2011 Order, 134 FERC ¶ 61,214 at P 78.

[14] The March 2011 Order thus concluded that this particular issue could likely be determined based on a summary review of Calnev's costs in that year. *See* March 2011 Order, 134 FERC ¶ 61,214 at P 78-79.

[15] *See* Opinion No. 435-A, 91 FERC ¶ 61,135 at 61,516-519; *BP West Coast Products, LLC v. FERC*, 374 F.3d 1263, 1306-07.

rehearing.[16] Accordingly, the Commission denies Calnev's requested clarification/rehearing as outside the scope of March 2011 Order.

The Commission orders:

Calnev's request for clarification and rehearing are denied.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.

[16] *See, e.g.*, *PJM Interconnection, LLC*, 126 FERC ¶ 61,030, at P 15 & n.10 (2009) (A request for rehearing of a new issue is outside the proper scope of the rehearing); *Calpine Oneta Power v. American Elec. Power Serv. Corp.*, 114 FERC ¶ 61,030, at P 7 (2006); *Midwest Indep. Transmission Sys. Op., Inc.*, 112 FERC ¶ 61,211, at P 34 (2005) (citing *Baltimore Gas & Elec. Co.*, 91 FERC ¶ 61,270, at 61,922 (2000) and *Baltimore Gas & Elec. Co.*, 92 FERC ¶ 61,043, at 61,114 (2000)).

Document Content(s)