108 FERC ¶ 61,028
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

ANR Pipeline Company Docket No. RP04-327-000

ORDER ACCEPTING CERTAIN TARIFF SHEETS
SUBJECT TO CONDITIONS, AND REJECTING OTHERS

(Issued July 8, 2004)

1. On June 8, 2004, ANR Pipeline Company (ANR) filed certain tariff sheets listed in the Appendix, to make generally available to its customers three new options in the General Terms and Conditions (GT&C) of its tariff. One of these options would permit discounted rates based on published gas price indices. The second option would permit discounted rates based on the negotiation of a "must-flow" provision within the service contract. The third option would permit ANR to offer a "linked contract," whereby ANR could satisfy a shipper's request for service it would otherwise have to deny due to prevailing operating conditions. For reasons discussed more fully in the body of this order, the Commission accepts ANR's proposal to offer discounted rates based on published gas price indices, effective July 8, 2004, subject to condition. The other two options are rejected without prejudice to ANR filing new rate schedule(s) containing those options.

2. Public notice of the filing was issued on June 14, 2004. Interventions and protests were due as provided in section 154.210 of the Commission's regulations (18 C.F.R. § 154.210 (2003)). Pursuant to Rule 214, 18 C.F.R. § 385.214, all timely motions to intervene and any motions to intervene out-of-time filed before the issuance date of this order are granted. Granting late intervention at this stage of the proceeding will not disrupt this proceeding or place additional burdens on existing parties. ProLiance

Energy, LLC, the Indicated Shippers[1] and Virginia Power Energy Marketing, Inc. (VPEM) filed comments or protests. ANR filed an answer to Indicated Shippers and VPEM. The details of these pleadings are discussed below.

Details of the Instant Filing

Index or Formula-Based Discounts

3. ANR is proposing to add a new GT&C section 32(b), to provide for a type of discount category that would allow ANR and a shipper to agree to a discounted rate that is calculated using formulas based on published index prices for specific receipt and/or delivery points or other mutually agreed to pricing reference points. ANR states that this type of discount arrangement provides shippers with the option to tailor their service requirements on ANR with their hedging programs and gas supply cost management, while allowing ANR the flexibility to compete with other similar and competitively priced transportation and storage services. ANR asserts that such discounts can fluctuate during the discount period, but that for the discount period, the shipper would not pay any less than it would have paid if it had paid the minimum applicable rates, or pay any more than it would have paid if it had paid the maximum applicable rates. Additionally, ANR states that any discounted rate agreement utilizing an index based rate will identify what rate component is being discounted (i.e., reservation charge or usage charge or both), and any formula will provide a reservation rate per unit of contract demand. Finally, ANR claims that its proposed tariff provision is consistent with the Commission's recent orders approving similar tariff provisions. In support of this, ANR cites *Panhandle Eastern Pipe Line Company, LLC*, 106 FERC ¶ 61,194 (2004), and *Northern Natural Gas Company*, 105 FERC ¶ 61,299 (2003).

Discounts Based on Must Flow Conditions

4. On September 15, 2003, ANR filed a service agreement with Interstate Gas Supply, Inc. ("IGS") as a non-conforming service agreement. The agreement contained a must-flow provision that allowed ANR to require IGS to flow a certain quantity of gas on any given day. On October 15, 2003, the Commission rejected ANR's filing in a Letter

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[1] The Indicated Shippers consist of BP America Production Company, BP Energy Company, ChevronTexaco Natural Gas, a division of Chevron U.S.A. Inc., and ConocoPhillips Company.

Order on the grounds that the must-flow provision was a term and condition of service not authorized in ANR's tariff. [2] In the Letter Order the Commission stated that its rejection of ANR's filing was without prejudice to ANR's right to file an application to provide this service under a new generally applicable rate schedule.

5. ANR sought clarification of the Letter Order, arguing that the Commission had not explained why its must-flow proposal had to be provided in a new rate schedule. In its Order on Clarification issued on March 29, 2004, the Commission noted that it would continue to evaluate and approve requests for innovative proposals to increase capacity that are just and reasonable and not unduly discriminatory. The Commission stated that when a pipeline files a proposal that contains terms and conditions of service that are not part of a pipeline's existing tariff or rate schedules, a pipeline must file appropriate revisions to its tariff and/or rate schedule, or file a new rate schedule that incorporates such provisions.[3] The Commission also afforded ANR an opportunity to conduct an experiment to determine if it is feasible for it to offer a must flow service on a generic basis, but ANR declined to do so.

6. Instead, ANR elected to make the instant filing that included the additional services in the discount provisions of the general terms and conditions portion of its existing tariff. It added a new GT&C section 32(c) that would allow ANR and a shipper to agree to a discounted rate based on the shipper agreeing to nominate and flow up to an agreed-to level of gas at specified receipt and/or delivery points upon demand by ANR. ANR states that proposed new section 32(c) provides the specific contract language by which a shipper who receives this type of discount will be bound, with the only "fill-in blanks" being the amount of notice required, the applicable volume, and the applicable receipt and delivery points. ANR also states that, as specified in section 32(c), any terms and conditions agreed to as part of the fill-in blanks will be posted on ANR's GEMStm system as part of the discounted rate.

7. ANR asserts that its inclusion of the must-flow provision into the GT&C addresses the Commission's previously expressed concern in an earlier proceeding with Interstate Gas Supply, Inc. (IGS), regarding negotiated terms and conditions of service different

[2] *ANR Pipeline Co.,* 105 FERC ¶ 61,062 (2003).

[3] *ANR Pipeline Co.,* 106 FERC ¶ 61,313 (2004) at P8.

from those in the tariff and the associated risk of undue discrimination.[4] Moreover, ANR contends that it is appropriate to consider the must-flow condition within the framework of a discount provision given that this would be the only context within which a shipper would find such a contract attractive, and recognizing the Commission's acknowledgement that certain types of contracts (e.g. backhaul) may create additional capacity on the pipeline, the benefits of which may be recognized in a lower rate.

8. ANR states that it intends for the must-flow contract(s) to create incremental capacity that it can sell on a primary firm basis. ANR states that the sale of such capacity must be contingent on the continued effectiveness of the must-flow contract. For example, ANR states that while the must-flow shipper may release or amend the must-flow contract, the must-flow shipper is not relieved of its underlying obligations regarding flowing gas, unless such obligations are assumed by a Replacement Shipper. Similarly, ANR states that if the must-flow contract is extended past the expiration of its original term, any contract(s) sold in reliance on the must-flow contract can be extended as well. However, ANR states that if the must-flow contract is not extended past its original contract term, ANR will not be in the position to continue service under the contracts sold in reliance on the must-flow contract. ANR modified its tariff accordingly.

The Linked Agreement Option

9. ANR states that in reviewing whether it was prepared to proceed with offering "must-flow" contracts to create incremental capacity, it also considered the option of "linked contracts." ANR describes "linked contracts" as where the shipper takes service with primary receipt and delivery points on one service agreement that allowed flow in one direction, and the flow has the effect of allowing additional volumes to flow on ANR and for deliveries to be made at separate delivery points under a second service agreement with the same shipper. ANR states that without the flows under the first service agreement, ANR would not be able to sell the Shipper the capacity for the second service agreement due its inability to guarantee deliveries. ANR states that a linkage between two contracts in these circumstances is beneficial to both to ANR's system and to the particular shipper since it enables ANR to provide, and for the shipper to receive primary firm service at guaranteed levels. ANR states that the benefits of such an arrangement were realized in agreements between ANR and Michigan Consolidated Gas

[4] ANR cites *ANR Pipeline Company*, 105 FERC ¶ 61,062 (2003) and 106 FERC ¶ 61,313 (2004), *order granting clarification*.

Company at the Georgetown and Sparta-Muskegon delivery points on ANR's system, and which the Commission approved.[5]

10. ANR states that now it can provide the same type of option to other shippers that it provided to Michigan Consolidated Gas Company. In new section 36 of the GT&C, ANR proposes that if it has insufficient available and uncommitted capacity to perform a request for new firm transportation service under existing operating conditions, ANR may nevertheless perform the requested service, provided a shipper is willing and able to maintain gas flows on another service agreement. ANR states the shipper may elect for ANR to perform the requested new service, subject only to the condition that the shipper maintain the linkage between the two contracts, including any extensions, if the shipper wishes ANR to continue to provide service under the linked agreements.

ANR's Answer

11. As noted, ANR filed an answer. While the Commission rules do not permit answers to protests, the Commission will accept ANR's answer because it further clarifies the scope of this proposal. In its answer, ANR states that the must flow provision appropriately belongs in the GT&C as opposed to a separate rate schedule because ANR does not propose to limit the availability of this type of discount to only one type of customer. Regarding VPEM's concern that ANR be required to perform under contracts that might be affected when a "must flow" customer defaults, ANR clarifies that that it will continue to perform under the terms of service under the contracts.

Discussion

12. For the reasons discussed below, the Commission accepts ANR's proposal concerning discounts based on price indices, subject to conditions, but rejects the remainder of ANR's proposal.

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[5] ANR cites a Letter Order issued on October 10, 2002 in Docket No. GT02-41-000.

Index or Formula-Based Discounts

13. In its filing, VPEM acknowledges that the Commission has already permitted discounts based on published indices. VPEM states that these discounts have been permitted as long as two conditions were met: (1) the rate must be "collared" by the filed maximum and minimum tariff rates, and (2) the resulting rate must conform to the pipeline's existing approved rate design. VPEM asserts that ANR's proposal appears to violate the first condition. Rather than restricting the rate resulting from the formula to the filed maximum and minimum rates, it asserts that ANR proposes only that the amount paid over the term of the discount be bound by the amount the shipper would have paid at the maximum and minimum rates. VPEM concludes that as a result, under ANR's proposal, there may be times during the term of the discount when, for example, the rate the shipper actually pays exceeds the filed maximum rate, as long as there are other periods during the term of the discount when the rate is low enough to act as a sufficient offset. In its comment ProLiance states that it would be useful for ANR to explain in further detail the type of formulas it intends to use for its indexed-based discount.

14. The Commission finds that ANR's proposed tariff language regarding index or formula-based discounts is generally consistent with Commission policy, which permits discounts based on price indices.[6] However, as VPEM points out, the Commission's regulations require that discounted rates must fall within the range established by the pipeline's maximum and minimum rates.[7] Accordingly, in *Northern Natural*, the Commission held that formula-based discounts using price indices " are permissible so long as the rate remains within the range established by the maximum and minimum rates set forth in the pipeline's tariff."[8] ANR's proposed tariff language provides that "For the period of the Agreement, in no event shall shipper pay to Transporter more than Shipper would have paid if Shipper had paid the maximum rates applicable to the service provided under the Agreement, or less than Shipper would have paid if Shipper had paid the minimum rate applicable to the service provided under the Agreement." The Commission agrees with VPEM that, as written, this language could permit ANR to

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[6] *See* Substitute Seventh Revised Sheet No. 303 to Northern Natural Gas Company's FERC Gas Tariff, Fifth Revised Volume No. 1. *See Northern Natural Gas Company*, 105 FERC ¶ 61,299 (2003).

[7] 18 C.F.R. § 284.10(c)(5) (2003).

[8] 105 FERC at 62,445.

charge more than the maximum rate during some portions of the period the agreement is in effect, so long as it charges less during other portions of the overall period the discount agreement is in effect. This is contrary to Commission policy. Accordingly, the Commission accepts ANR's proposed section 32(b), effective July 8, 2004, subject to ANR revising that section to make clear that at no time will the shipper be required to pay more than the maximum rate or be permitted to pay less than the minimum rate.

15. The Commission will not require ANR to explain in further detail the type of formulas it intends to use for its indexed-based discount, as requested by ProLiance. The Commission has not required this in other cases, and believes that the parties to a discount agreement should be given flexibility to develop any formulas they choose, so long as the rate remains at all times within the maximum and minimum rates set forth in the pipeline's tariff and there is no variation from the pipeline's rate design.

Discounts Based on Must Flow Conditions and the Linked Agreement Option

16. Indicated Shippers protest that ANR's proposal to implement a must-flow service should be made through the filing of a new rate schedule with all of the necessary support that is required under the Commission's regulations. Indicated Shippers state that, when a pipeline files a new rate schedule, it must provide, among other things, a description of the service, the necessity for the service, how the existing service will differ from existing services, impact of the new service on existing firm and interruptible customers, adequacy of existing capacity, effect on receipt and delivery point flexibility, work papers detailing the proposed rate or an explanation if an existing rate is used, and a justification similar to testimony filed in a section 4 rate case that explains why the proposed rate design and proposed cost allocation are just and reasonable. Indicated Shippers assert that these are the types of support that ANR should give for its proposal.

17. Indicated Shippers further note that ANR has included in its proposed GTC § 32(c) specific language that would be included in each contract for must-flow service. Indicated Shippers state that the proposed language contains blanks to be filled in regarding (i) the number of hours of notice that ANR must provide the shipper that the shipper must flow the specified amount of gas; (ii) the amount of gas covered by the must-flow obligation; and (iii) the receipt and delivery points between which the "must-flow" gas must flow. Indicated Shippers assert that this is the type of language that would appropriately be included in a pipeline's Form of Service Agreement for a rate schedule, and this is where ANR should include this language.

18. VPEM also asserts that under the second type of proposed discount, the "must flow" discount, a shipper gets a reduced rate in exchange for the commitment to flow gas between certain receipt and delivery points. VPEM notes that ANR claims that its system operations are such that there are many instances in which additional capacity and services could be offered if it knew that certain other flows would occur. VPEM asks: what happens if ANR gives a "must flow" discount to Shipper A (the primary agreement), sells a firm service to Shipper B (the secondary agreement) in reliance on Shipper A's performance, and then Shipper A defaults. VPEM requests that ANR clarify that under such circumstances, ANR is still required to perform under the secondary agreement. It argues that firm shippers on ANR should not be exposed to the hidden credit and general performance risks associated with any secondary agreements that they may have unknowingly entered into with ANR.

19. VPEM states that this clarification is particularly important given the details of ANR's "linked agreement" proposal. VPEM characterizes this concept as almost identical to the "must flow" discount, except now both agreements are held by the same shipper. VPEM notes that ANR proposes that it shall not be held liable for its failure to perform under the "linked" subsidiary agreement. In light of this, VPEM concludes that ANR's performance obligations under the "must flow" discount proposal must be made more transparent.

20. ProLiance states that ANR should provide details regarding the operational or other conditions under which ANR would need an agreed upon level of flow from a shipper, whether the required level of flow is a minimum or maximum level the shipper can flow, and how such an arrangement would increase operational efficiency, marketing opportunities or decrease the likelihood of ANR issuing an OFO. Finally, ProLiance states that ANR's proposed linked agreement option may be a useful tool, but further details regarding the operational use of the affected points is still needed.

21. The Commission rejects ANR's proposed tariff provisions concerning discounts based on must flow conditions and linked agreements. In the instant filing, ANR seeks to make discounts available based on a "must flow" condition. This creates an entirely different quality of service than firm service provided under ANR's existing FTS rate schedules. The Commission finds that the "must flow" condition is an element of the character or quality of the transportation service, and that compliance with the "must-flow" condition is a necessary condition to both obtain and retain the service. Additionally, the decision to require gas to flow is vested entirely with ANR, unlike any other services under ANR's existing firm service rate schedules. Under other discounted rate provisions, if the provision is not complied with, the shipper may lose the discount, or may not obtain it in the first place, but under the "must flow" provision, if the shipper does not flow the volume of gas directed by ANR, it not only loses any discount, but is

subject to liquidated damages up to $25.00. Given these distinctions, the proposed "must-flow" service is not properly included under GT&C discount provisions, but must be provided under a separate rate schedule. This conclusion is consistent with our direction in the order rejecting ANR's proposed negotiated rate agreement with IGS that, if it wanted to offer such a service, it must offer it in a new rate schedule. Accordingly, the Commission rejects ANR's proposal to modify GT&C section 32 to make discounts available based on a "must flow" condition without prejudice to ANR's right to file an application, with supporting explanations, to provide this service under a new generally applicable rate schedule.

22. For similar reasons, the Commission also rejects the linked agreement option. In its transmittal letter to the instant filing, ANR writes how the "must flow" condition creates or increases incremental capacity as part of ANR's segue to discussing its "linked contracts" option. In its discussion of the "linked contracts" option, ANR cites a letter order in which a non-conforming service agreement was accepted. This non-conforming service agreement contained a "must flow" provision, and was "linked" to another service agreement. ANR's representation seems to suggest there is some relation between its "must flow" provision with its "linked contracts" option. However, upon further review of the proposed tariff language in ANR's new GT&C Section 36, the Commission finds there is no explicit relation between the two features.

23. Nevertheless, ANR's "Linked Agreement Option" offers a different character of service than that available under any existing rate schedule. Specifically, in order to take service under one contract, a shipper must take service under two contracts, and that the shipper's actions under the one have a direct effect on the service taken under the second. Such a condition of service is not properly included under a new section in ANR's GT&C, but must be provided under a separate rate schedule. Accordingly, the Commission rejects ANR's proposal to offer "linked contracts" without prejudice to ANR's right to file an application, with supporting explanations, to provide this service under a new generally applicable rate schedule.

<u>The Commission orders</u>:

(A) ANR's proposal to allow it and a shipper to agree to a discounted rate calculated on formulas based on published index prices for specific receipt and/or delivery points or other mutually agreed to pricing reference points, is accepted, subject to the conditions discussed above.

(B) ANR's proposal to make discounts available based on a "must flow" condition, is rejected.

(C) ANR's proposal to offer "linked contracts," is also rejected.

(D) The two proposals discussed in ordering paragraphs B and C are rejected without prejudice to ANR's right to file an application, with supporting explanations, to provide these services under new generally applicable rate schedules.

(E) As set forth in the Appendix to this order, certain tariff sheets in the instant filing are accepted subject to the conditions discussed above, and other tariff sheets are rejected. ANR is directed to file revised tariff sheets within fifteen days of the date of this order.

By the Commission. Commissioner Brownell concurring with a
separate statement attachment.

(S E A L)

Magalie R. Salas,
Secretary.

APPENDIX

ANR Pipeline Company
FERC Gas Tariff, Second Revised Volume No. 1

Docket No. RP04-327-000

Accepted Subject to Conditions,
Effective July 8, 2004:

Fifteenth Revised Sheet No. 2
Seventh Revised Sheet No. 102
Sixth Revised Sheet No. 103
Third Revised Sheet No. 162.01
Tenth Revised Sheet No. 191
Third Revised Sheet No. 191A
Second Revised Sheet No. 191B

Rejected:
Fourth Revised Sheet No. 193
Third Revised Sheet No. 194
Second Revised Sheet No. 195
First Revised Sheet No. 196
First Revised Sheet No. 197

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

ANR Pipeline Company Docket No. RP04-327-000

(Issued July 8, 2004)

BROWNELL, Commissioner, concurring:

1. I fully support rejection of the proposed "must flow" and "linked agreement" tariff provisions, as discussed in the order. Our rejection is without prejudice to ANR's right to file an application, with supporting explanations, to provide these services under a new generally applicable rate schedule.

2. If ANR elects to file these proposals as new services, ANR's supporting explanations need to address a number of questions that are raised by such service structures. Do these types of services promote, or are they at least consistent with, a competitive gas supply market? Is vesting the decision to require gas to flow entirely with the pipeline, consistent with the unbundling principles of Order No. 636 such as access to multiple supply sources through flexible receipt and delivery points? Are additional competitive concerns present where affiliate marketers and/or producers are involved? Is the purpose and level of the penalty ($25 per dt) for failure to flow gas consistent with Order No. 637? Are these new services effectively a "take and pay" contract? How will our capacity release and segmentations programs be accommodating under the new rate schedules? The fundamental issue is striking the right balance between providing new, innovative services and not stifling competition.

Nora Mead Brownell
Commissioner