142 FERC ¶ 61,162
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Buckeye Pipeline Company, L.P. Docket No. OR13-3-000

ORDER ON MARKET-BASED RATE APPLICATION ESTABLISHING HEARING PROCEDURES

(Issued February 28, 2013)

1. On October 15, 2012, Buckeye Pipeline Company L.P. (Buckeye), pursuant to Part 348[1] of the Commission's regulations, filed an "Application for Authority to Charge Market-Based Rates in the New York City Market." The application requests authority to charge market-based rates[2] for its transportation service of all refined petroleum products to destinations located in the New York BEA.[3] Buckeye asserts that it lacks significant market power in the New York BEA, which in this case is both the origin and destination market.

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[1] *See* 18 C.F.R. Part 348 (2012).

[2] Buckeye states that the application seeks market-based rate authority for transportation rates under two current tariffs: (1) Buckeye's FERC No. 440.3.0, for transportation of aviation turbine fuel from Linden, Sewaren, and Port Reading, New Jersey to Newark International Airport, New Jersey, and to J.F. Kennedy International Airport JFK and LaGuardia Airport, New York City, New York (Long Island System), and Inwood, New York; and (2) Buckeye's FERC No. 439.2.0, for transportation of refined petroleum products from Linden, New Jersey to Inwood and Long Island City, New York City, New York.

[3] Each BEA is an "Economic Area" defined by the U.S. Department of Commerce's Bureau of Economic Analysis. BEA's economic areas generally represent regions of related economic activity surrounding urban centers, and which the Commission has frequently employed as a geographic unit for purposes of analyzing market power.

2. The application was protested by the Airlines,[4] arguing that Buckeye's analysis was incorrect and incomplete. As discussed below, the Commission sets this matter for hearing.

Description of Filing

3. Buckeye seeks market-based rate authority for the transportation from its Linden, Port Reading and Sewaren origins in northern New Jersey to destinations on Buckeye's Long Island System, consisting of its delivery points at various New York City area airports and Inwood, New York.[5]

4. Buckeye requests market-based rate authority to gain greater flexibility in setting rates to Buckeye's destinations in the New York City market, superior to either Buckeye's current ratemaking methodology established by Opinion No. 360 and a subsequent settlement in 1991[6] or to the Commission's index regulation, which the Commission has suggested as an alternative to the Buckeye program in its Show Cause Order[7] issued in Docket No. IS12-185-000. Additionally, Buckeye contends market-based rates would provide it with greater certainty regarding future revenues for purposes

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[4] Delta Air Lines, Inc. (Delta), Continental Airlines, Inc. (Continental), JetBlue Airways Corporation (JetBlue), United Air Lines Inc. (United), and US Airways Inc. (US Airways); "Airlines" or "Joint Protesters."

[5] Newark International Airport, New Jersey; J.F. Kennedy International Airport, New York; and LaGuardia Airport, New York (New York City airports).

[6] *See Buckeye Pipe Line Co., L.P.*, Opinion No. 360, 53 FERC ¶ 61,473 (1990), *reh'g granted in part and denied in part*, Opinion No. 360-A, 55 FERC ¶ 61,084 (1991) (collectively, Buckeye experimental program or the "Cap and Link" program). Pursuant to Opinion Nos. 360 and 360-A issued on December 31, 1990 and April 18, 1991, respectively, the Commission authorized Buckeye to implement an experimental program for interstate rate regulation (Experimental Rate Program), allowing Buckeye to determine rate changes based on whether its markets were established to be competitive or not.

[7] *See Buckeye Pipe Line Co., L.P.*, 138 FERC ¶ 61,239 (2012) (Show Cause Order). On March 1, 2012, Buckeye submitted tariffs in Docket No. IS12-185 for the transportation of jet or aviation turbine fuel to the New York City Destinations. The tariffs were protested, and on March 30, 2012, the Commission rejected Buckeye's tariffs and ordered Buckeye to "show cause why the rates in its experimental program should not be rescinded and replaced with rates filed pursuant to the ratemaking methodologies contained in Part 342 of the Commission's regulations."

of determining whether to invest in potential substantial increases in capacity for the benefit of the three New York City airports over the next several years.

5. Buckeye also maintains market-based rate authority would foreclose the continuing litigation regarding whether the rates to the New York City airports are just and reasonable, which has been raised in the Airlines' complaint in Docket No. OR12-28-000. At a minimum, Buckeye contends, market-based rate authority would eliminate further litigation over the prospective justness and reasonableness of its rates.

6. Section 348.1(c) of the Commission's regulations require a refined petroleum product pipeline seeking market-based rates to: (1) define the relevant product and geographic markets, including both destination and origin markets; (2) identify the competitive alternatives for shippers, including potential competition and other competition constraining the pipeline's ability to exercise market power; and (3) compute the market concentration and other market power measures based on the information provided about competitive alternatives.[8]

A. Product Market

7. Buckeye asserts that the relevant product market in this case is the transportation of all the "pipelineable refined petroleum products," which include motor gasoline, distillates, and jet fuel that it transports or could transport, consistent with Commission precedent. Buckeye notes that since Opinion No. 360, the Commission has recognized that shippers determine the mix of pipelineable refined petroleum products transported by a refined petroleum products pipeline; thus it is appropriate to include in the product definition all of the products that the pipeline applicant could transport.

B. Origin Market/Destination Markets

8. In the context of a refined petroleum products pipeline seeking market-based rates, an applicant must define two types of geographic markets: (1) the pipeline's destination market into which the pipeline makes inbound movements; and (2) the pipeline's origin market from which the pipeline makes outbound movements.

9. Buckeye's expert witness Dr. George Schink asserts that Buckeye's New York origin market is appropriately defined geographically as the area contained in the New York BEA.[9] Buckeye states that the New York BEA is a highly competitive origin market, and Buckeye's market share of volumes exported from the BEA is not high. Dr.

[8] 18 C.F.R. § 348.1(c) (2012).

[9] Buckeye's application defines the geographic market to include all 36 counties in the New York City BEA, a 14,823 square mile area.

Schink further states that under the Commission-approved Cap and Link program,[10] Buckeye has market-based rate authority for its transportation service for volumes exported from all its receipt points located in the New York BEA.

10. Buckeye states that its receipt points in the New York BEA are located at three locations—the Linden, New Jersey area; the Macungie, Pennsylvania area; and the New Haven, Connecticut area. Buckeye states that the Linden area is a receipt point for Buckeye's Eastern Products system and for its Long Island System, and the movements from the Linden area on the Eastern Products System go to Macungie and then either northward to the Scranton, Pennsylvania area and Upstate New York or westward to the Harrisburg and Pittsburg, Pennsylvania areas. Buckeye notes that the Macungie receipt point also obtains pipelineable refined petroleum products from the Philadelphia, Pennsylvania area, and the New Haven receipt point is supplied off-the-water by barge or tanker.

11. Buckeye asserts the appropriate geographic market for both the origin and destination markets is the New York BEA.[11] Buckeye defines the New York City market as "encompassing Buckeye's transportation service of all refined petroleum products to destinations located in the New York BEA."[12] Buckeye states that the service to all of the destinations for which market-based rate authority is sought are intra-BEA movements of short distances, located within one of the largest and most active ports in North America, and in an area of northern New Jersey densely populated by petroleum terminals and pipelines, as well as two refineries.

12. Buckeye states that it provides virtually no deliveries into the New York BEA, and that the New York BEA is a highly competitive destination market. Buckeye notes that its delivery locations in this destination market, for which it does not currently have market-based rates under the Buckeye experimental program,[13] are located in the immediate vicinity of New York City which is the population center for the New York BEA. Further, Buckeye notes that the delivery locations in the New York BEA where Buckeye does not have market-based rates under the experimental program are all on Buckeye's Long Island System (Newark, Long Island City, LaGuardia, Inwood, and JFK). Buckeye states it also has receipt points at Port Reading, New Jersey and Sewaren,

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[10] *See* Footnote 6.

[11] *See* Application at 1 and 3. Buckeye relies on the affidavit of Dr. George Schink for these assertions.

[12] *See* Application at 1.

[13] *See* Footnote 6.

New Jersey from which refined petroleum products are transported into Linden for movement to all the delivery locations on Buckeye's Long Island System.

C. <u>Competitive Alternatives</u>

13. Buckeye states that it faces significant competition in both its proposed origin and destination markets. Buckeye contends that shippers in its New York origin market "all have several alternatives available to move their pipelineable petroleum products to ultimate consumers."[14] Buckeye contends that each of the refineries connected to its pipeline have competition alternatives, including the option of waterborne transportation, Colonial Pipeline Company (Colonial), and local consumption.

14. Buckeye states that in the New York BEA destination market, Buckeye faces competition from two local refineries with truck racks, two inbound pipelines connected to terminals in New York, the Colonial and Sunoco Logistics Partners L.P. pipelines, and substantial port facilities.

15. Dr. Schink testifies that the New York City airports exist in a market rich with active competitive alternatives in the form of adjacent pipelines and competitive barge traffic, and it only requires some investment in facilities for these airports to access those alternative supplies efficiently and economically. Specifically, Dr. Schink testifies that "the recent and planned Colonial pipeline capacity expansions and increased waterborne receipts and shipments in Buckeye's New York destination market indicate that further new entry would occur when needed in this market."[15] Buckeye also states that its market based rate application fully meets the evidentiary standards required by the Commission's regulations under Order No. 572, *Market-Based Ratemaking for Oil Pipelines*.[16]

16. Buckeye also asserts that it faces potential competition in the origin and destination markets via potential entry and the recent and planned Colonial pipeline capacity expansions and increased waterborne receipts in Buckeye's markets. Further, Buckeye asserts that the ability of existing competitors to take business from Buckeye if it were to attempt to exercise market power is reflected in the amount of excess capacity in the marketplace.

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[14] Application at 13.

[15] *Id.* at 18.

[16] FERC Stats. & Regs., Regulations Preambles January 1991 – June 1996 ¶ 31,007 (1994).

17. Buckeye states that product exchanges within the New York Harbor area make all inbound transportation alternatives and local refiners competitive to Buckeye in its destination market and all outbound transportation and local consumption alternatives competitive to Buckeye in its origin market.

18. Buckeye further argues that its Long Island System's receipt and delivery points are all located within the New York Harbor area, and for the four delivery locations on that system, three also have access to refined petroleum product barge dock facilities at Buckeye's Long Island City and Inwood delivery locations and operating refined petroleum product barge dock facilities in the vicinity of LaGuardia and JFK. Buckeye states there is a substantial volume of refined petroleum product barge movements within the Port of New York, as well as substantial barge movements up the Hudson River and up the East Coast to New England ports. Buckeye points out that potential alternatives to the intra-market transportation services to each of the three airports could be constructed in a reasonable time frame and operated at or very near to Buckeye's current charges.

D. Market Power Analysis

19. The Commission generally calculates market power through the Herfindahl-Hirschman Indexes (HHI) of market concentration for the markets to be served.[17] The recommended threshold set forth by the U.S. Department of Justice in its Oil Pipeline Deregulation Study for permitting an oil pipeline to be totally deregulated is an HHI of 2,500.[18] Buckeye notes that the Commission has declined to set a threshold level for maximum HHIs consistent with a competitive market, and even at HHIs at or above 2,500, the Commission has found markets sufficiently competitive to allow market-based

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[17] HHI equals the sum of the squared market shares of all competitors in the market. The statistic takes into account the number and relative size of the market. A market that is a monopoly, for example, has an HHI of 10,000.

[18] The Herfindahl-Hirschman Index (HHI) measures the likelihood of a pipeline exerting market power in concert with other sources of supply. One derives an HHI by squaring the market shares of all the firms competing in a particular geographic market and adding them together. The HHI can range from just above zero, where there are a very large number of competitors in the market, to 10,000, where only a single monopolist serves the market.

A high HHI indicates significant concentration. A high HHI also suggests a pipeline may exercise market power either unilaterally or through collusion with rival firms in the market. An HHI of 1,800 would reflect a market served by between five and six equally sized competitors. An HHI of 2,500 would indicate a market served by four equally sized competitors. *Magellan Pipeline Co., L.P.*, 132 FERC ¶ 61,016, at P 7 n.6 (2010).

rates if market shares are not excessive. The Commission has found that barge and tanker shipments of pipelineable refined products are highly competitive with pipeline movements.[19]

20. Additionally, two statistics can be calculated to measure the amount of excess capacity in the markets: (1) the excess capacity ratio; and (2) the ratio of excess capacity held by the applicant pipeline's competitors to the volumes transported by the applicant oil pipeline.[20]

21. Buckeye asserts that in the litigation leading up to Opinion No. 360, the only contested issue regarding the New York BEA was whether deliveries to the New York City airports were competitive, and based on the record, at that time the Commission did not reach a determination as to whether the transportation was competitive or non-competitive. Because the Commission made no finding and left the market to be treated as being subject to Buckeye's market power and right to litigate the issue in the future, Buckeye states that this proceeding is the response to that invitation.

22. Buckeye asserts that its origin market faces large competition from large outbound waterborne movements and large amounts of local consumption in the New York origin market, which is defined as the New York BEA. Buckeye states the unadjusted capacity-based HHI is 552, and its unadjusted capacity based market share is less than 23.5%. Buckeye states that the excess capacity ratio equals total unadjusted capacity divided by the capacity of the local refineries to produce pipelineable refined petroleum products. The excess capacity ratio equals 6.34, indicating that the capability of the New York origin market to absorb pipelineable refined petroleum products is 6.34 times the capability of the local refiners to produce these products. Buckeye states that the very high excess capacity ratio insures that neither Buckeye nor any other market participant could profitably exercise market power, and the capacity based statistics indicate that

[19] *See Williams Pipe Line Co.*, 71 FERC ¶ 61,291, at 62,141-143 (1995).

[20] *See Enterprise Products Partners, L.P. and Enbridge Inc.*, 139 FERC ¶ 61,099, at P 10 n.5 (2012) (The excess capacity ratio measures the total capacity available in the market relative to the total demand capacity in a market. An excess capacity ratio of 1.2 or higher indicates substantial excess capacity, which in turn implies that it is highly unlikely that the applicant pipeline could profitably sustain a tariff rate above competitive levels. The "excess capacity held by others" ratio measures capacity of the market and the unutilized capacity present. For the "excess capacity held by others" ratio, given that the pipeline in question is not yet operational and its future capacity utilization is unknown, the alternative calculation was done based on an assumption that the pipeline would be 90 percent utilized.).

Buckeye could not profitably increase its tariff rates above competitive levels in its New York origin market.[21]

23. Buckeye contends the HHI for the destination market is low. Buckeye states in the New York Area BEA in the destination market include local refineries, inbound refined products pipelines serving racket terminals and waterborne deliveries. Buckeye asserts that no competitors located outside the New York BEA were included in the analysis because the internal competitors were sufficient to demonstrate that the market is highly competitive. Buckeye states that the excess capacity ratio of the destination market is 1.45, the effective capacity based HHI is 462, and the adjusted capacity based HHI is 61. Buckeye additionally states that its effective and adjusted capacity based market shares are both less than 3.5%, and the excess capacity ratio is 1.45%. Buckeye states that Buckeye's delivery-based market share in its New York destination market is extremely low and the ratio of excess capacity held by others to Buckeye's deliveries for location consumption is over 550, demonstrating that Buckeye's New York destination market is highly competitive.

Interventions and Protests

24. Pursuant to section 348.2(g) of the Commission's regulations,[22] interventions or protests to the application were required to be filed by December 14, 2012. The Airlines filed a timely joint protest and motion to intervene.

25. The Airlines urge the Commission to dismiss Buckeye's application as facially deficient, or, in the alternative, to set the application for hearing. The Airlines assert that based on their analysis, good cause exists to believe that Buckeye currently exercises, and will continue to exercise, market power with respect to the transportation of jet fuel to the New York Harbor area.

26. The Airlines point out that Buckeye currently supplies 100 percent of the jet fuel consumed at Newark, LaGuardia, and JFK. The Airlines further assert that Buckeye's application depends on redefining the markets involved and the alternatives available to consumers.[23] The Airlines take issue with Buckeye's definition of the geographic market,

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[21] Application at 17.

[22] 18 C.F.R. § 348.2(g) (2012).

[23] For example, the Airlines state that, contrary to Buckeye's definition of the relevant product market (including all refined products, including diesel, gasoline, and jet fuel), a consumer of jet fuel cannot substitute gasoline or diesel fuel for their jet fuel needs, and will not react to price changes in the transportation of gas or diesel fuel, resulting in a definition that is overly broad and unreasonable.

noting that because jet fuel is only received at the New York airports, Buckeye's definition is overly broad.

27. The Airlines also charge that Buckeye's good alternatives analysis is entirely speculative, as Buckeye did not identify a single "good" alternative for the transportation of jet fuel to any of the New York airports. The Airlines assert that Buckeye's argument that numerous alternatives could be used if Buckeye were to raise its rates above the competitive level is erroneous for two reasons. First, the Airlines state that Buckeye's rates are already above the competitive level, and Buckeye still enjoys market share. Second, the Airlines state that it is unreasonable to believe that the potential alternatives identified by Buckeye could be permitted and constructed within a reasonable time and at the cost suggested by Buckeye, and so these alternatives are not "good alternatives."

28. The Airlines state that the relevant definition of "market power" is the ability to profitably sustain a small but significant price increase above a competitive price level for a significant period of time.[24] The Airlines state that if Buckeye were to raise its transportation rate to one of the New York airports, it is only a shipper or consumer of jet fuel that could respond to the rate increase, and only alternatives for transporting jet fuel to one of the New York airports would be potential competitive alternatives, rather than Buckeye's claim that the relevant product market should include "all of the products that (Buckeye) could transport."[25]

29. Further, the Airlines argue because Buckeye provides transportation service for different refined products to different destinations at different rates, there could be a different set of good economic alternatives in terms of availability, quality, or price for the transportation of each refined product. The Airlines contend Buckeye charges different and unequal rates for the transportation of different refined products, and has the ability to adjust prices independently; meaning that jet fuel and other refined products are separate markets.

30. The Airlines maintain because Buckeye's definitions of the competitive price level bear no relation to the costs Buckeye incurs in providing the transportation in question, the definitions are inconsistent with long-established Commission and federal court precedent as well as regulatory economic theory. The Airlines state that Buckeye's costs, rather than other proxies, should first be used to determine a proxy for a competitive price level.

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[24] *See Mobil Pipe Line Co. v. FERC*, 676 F.3d 1098, 1100 (D.C. Cir. 2012).

[25] *See* Protest at 41-42.

31. The Airlines argue that Buckeye has failed to identify any alternatives for the transportation of jet fuel to the New York airports. The Airlines state that none of the alternatives identified by Buckeye currently supply any jet fuel to the New York airports. The Airlines state that because jet fuel is not, and cannot be, trucked to or between airports, each New York airport should be treated as a separate destination market, and Buckeye's market power in each of those markets should be evaluated based on the alternatives available to the consumers of jet fuel at each airport.

32. On January 14, 2013, Buckeye filed an answer requesting rejection of the Airlines' intervention and requesting summary disposition as to the destinations for which no opposition had been filed. The Airlines responded to Buckeye's answer on January 29, 2013.

Commission Analysis

33. Rule 385.213(a)(2) of the Commission's Rules of Practice and Procedure prohibits answers to answers unless otherwise ordered by the decisional authority. In the instant case, the Commission will accept the answer filed by Buckeye in the instant docket, as well as the pleading submitted by the Airlines, which assisted the Commission in its determination.

34. The Commission denies Buckeye's request for summary disposition as to the destinations for which no opposition has been filed—specifically the destinations of Inwood and Long Island City.[26] Buckeye defined its origin and destination markets as the New York BEA. The Airlines protested Buckeye's stated origin and destination markets. Buckeye did not break out specific destinations in its application; therefore, these destinations cannot be separated unless the application is amended.

35. The Commission's preliminary analysis indicates that the protest raises issues about Buckeye's request for market-based rates, which cannot be resolved on the basis of the record at this point. Therefore, the Commission will set the application for hearing.

36. The Commission notes that the Airlines' complaint against Buckeye in Docket No. OR12-28-000 regarding the New York Airport rates has similar facts and issues as the instant docket. The Commission will leave it to the Chief Administrative Law Judge's (ALJ) discretion as to how they would like to proceed with the common issues present in both cases, and if consolidation is appropriate.

[26] *See* Answer of Buckeye Pipe Line Company, L.P. to Protest and Request for Rejection of Airline Intervenors and Request for Summary Disposition as to Destinations for Which No Opposition Has Been Filed, filed January 14, 2013.

<u>The Commission orders</u>:

(A) Pursuant to the authority conferred on the Commission by the ICA, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the ICA, a public hearing shall be held concerning the Airlines' protest against Buckeye Pipe Line's market-based rate application.

(B) A Presiding ALJ, to be designated by the Chief ALJ within 15 days of this order, shall within 15 days of the date of the Presiding ALJ's designation, convene a prehearing conference in these proceedings in a hearing room of the Commission, 888 First Street, NE, Washington, DC 20426. Such a conference shall be held for the purpose of establishing a procedural schedule. The Presiding ALJ is authorized to establish procedural dates and to rule on all motions (except motions to dismiss) as provided in the Commission's Rules of Practice and Procedure.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.