

129 FERC ¶ 61,130
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Sudeen G. Kelly, Marc Spitzer,
and Philip D. Moeller.

The Dow Chemical Company, Dow Pipeline Company Docket No. PR09-31-000
and Dow Hydrocarbons and Resources LLC

ORDER ON REQUEST FOR DECLARATORY ORDER

(Issued November 19, 2009)

1. On August 19, 2009, The Dow Chemical Company (Dow Chemical), Dow Pipeline Company (Dow Pipeline), and Dow Hydrocarbons and Resources LLC (Dow Hydrocarbons) (collectively, Dow) filed a petition for declaratory order that authorizes Dow Hydrocarbons to link an assignment of firm intrastate pipeline capacity on the Dow Pipeline system, to be used for firm interstate transportation service under section 311(a)(2) of the Natural Gas Policy Act of 1978 (NGPA),¹ with an assignment of some or all of Dow Chemical's capacity rights at the liquefied natural gas (LNG) import terminal owned and operated by Freeport LNG Development, L.P. (Freeport LNG). As discussed below, the Commission grants Dow's request for declaratory order, subject to conditions.

I. Background

2. According to Dow's petition, Dow Chemical owns and operates a large petrochemical manufacturing facility in Freeport, Texas that is dependent upon natural gas supplies. Dow Pipeline and Dow Hydrocarbons are each indirect, wholly-owned subsidiaries of Dow Chemical. Dow states that Dow Pipeline owns and operates an intrastate pipeline system in the state of Texas. That pipeline was originally constructed in the 1970s as a means of enhancing Dow Chemical's access to supplies of natural gas needed for fuel and feedstock purposes at Dow Chemical's manufacturing facility in Freeport, Texas. Dow states that the Dow Pipeline system includes approximately 60-70 miles of pipeline extending in a southeasterly direction from its upstream terminus at the Katy Hub west of Houston to its downstream terminus near Dow Chemical's facility.

¹ 15 U.S.C. §§ 3371(a)(2) (2006).

Dow states that this portion of the system is and will be interconnected with a number of intrastate and interstate pipelines. Dow states that Dow Pipeline currently provides intrastate and interruptible NGPA section 311 transportation service, but does not provide NGPA firm section 311 transportation service.²

3. Dow states that Dow Hydrocarbons sells natural gas to Dow Chemical at its Freeport manufacturing facility. In order to transport that natural gas to Dow Chemical, Dow Hydrocarbons has a contract with Dow Pipeline for 100 percent of its firm intrastate transportation capacity. Historically almost all of the service provided by Dow Pipeline involved the transportation of natural gas to Dow Chemical's facility.

4. In 2004 and 2006, the Commission authorized the construction and expansion of an LNG import terminal by Freeport LNG on Quintana Island, southeast of the City of Freeport, in Brazoria County, Texas.³ The Commission, pursuant to section 3 of the NGA, authorized Freeport LNG to site, construct, and operate a LNG import, storage, and vaporization terminal and an associated 9.6 mile send-out pipeline extending from the terminal to the Stratton Ridge meter station in Brazoria County, Texas. Following the expansion, the terminal's send-out capacity should increase from 1.5 billion cubic feet per day (Bcfd) to 4.0 Bcfd. Freeport LNG's facilities are not subject to the Commission Part 284, open access regulations.⁴

² Section 311(a)(2) of the NGPA allows the Commission to authorize the transportation of natural gas by intrastate pipelines on behalf of interstate pipelines and local distribution companies served by interstate pipelines. Section 601(a)(2) of the NGPA exempts transportation service authorized under NGPA section 311 from the Commission's Natural Gas Act (NGA) jurisdiction. The Commission's regulations governing interstate transportation services by intrastate pipelines under section 311(a)(2) of the NGPA are set forth in Part 284, subpart C of the Commission's regulations, 18 C.F.R. § 284.121 *et seq.* (2009).

³ See *Freeport LNG Development, L.P.*, 107 FERC ¶ 61,278 (2004); *Freeport LNG Development, L.P.*, 116 FERC ¶ 61,290 (2006).

⁴ As the Commission noted in Order No. 712-A, LNG facilities approved pursuant to NGA section 3, such as the Freeport LNG facility, are not open access, as permitted by the Commission's *Hackberry* policy. By contrast, facilities approved pursuant to section 7 of the NGA provide Part 284 open access service and are subject to the Commission's capacity release rules. See Order No. 712-A, *Promotion of a More Efficient Capacity Release Market*, 73 Fed. Reg. 72692 (Dec. 1, 2008) FERC Stats. & Regs. ¶ 31,284 (2008) (citing *Hackberry LNG Terminal, L.L.C.*, 101 FERC ¶ 61,294 (2002)).

5. Dow states that the Freeport LNG terminal is located only a few miles from Dow Chemical's Freeport facility. Dow states that Dow Chemical contracted with Freeport LNG for 0.5 Bcf of terminal capacity for a 20-year period that commenced in July 2008.⁵ This amounts to slightly more than four LNG cargoes per month. Dow states that Dow Chemical can receive revaporized natural gas from the Freeport LNG terminal via a 0.6 mile pipeline, currently owned and operated by Dow Chemical, which extends from an interconnection with Freeport LNG's send-out pipeline at the Stratton Ridge meter station to a 20 inch line, also owned and operated by Dow Chemical, which continues to Dow Chemical's manufacturing facility. Dow states that it should be assumed that, when the service described in its petition is provided by Dow Pipeline, a direct connection will have been established at the Stratton Ridge meter station between Dow Pipeline and Freeport LNG, through the sale of the 0.6 mile interconnecting pipeline and related facilities by Dow Chemical to Dow Pipeline

II. Request for Declaratory Order

6. Because of difficulties Dow Chemical has experienced in its efforts to locate economically-attractive supplies of LNG, Dow states that Dow Chemical has been exploring alternatives for efficient use of its capacity at the Freeport LNG terminal, including alternatives involving the release or assignment of terminal use rights to one or more third parties. Dow states that a third party is interested in acquiring some or all of Dow Chemical's capacity at the Freeport LNG terminal, but the third party has advised that, if it were to acquire some or all of Dow Chemical's capacity at the Freeport LNG terminal (including capacity on Freeport LNG's 9.6 mile send-out line), it would also require an equivalent level of firm transportation rights on the Dow Pipeline system to transport regasified LNG to downstream markets.

7. To accommodate this request, Dow is proposing that Dow Hydrocarbons would assign some or all of its firm intrastate capacity on Dow Pipeline to the third party, conditioned on the third party also accepting an assignment of an equivalent level of capacity at the Freeport LNG terminal. In addition, Dow states that Dow Pipeline will file to implement firm intrastate service pursuant to NGPA section 311 on the portion of its system from Stratton Ridge to Katy Hub, but Dow Pipeline will likely wish to place a limit on the quantity of firm section 311 service to be made available in order to protect the jurisdictional status of Dow Pipeline's system as an intrastate pipeline, while also ensuring that Dow Chemical continues to be able to rely on Dow Pipeline to transport natural gas supplies to its manufacturing facility. Dow states that the assigned Dow Pipeline capacity would be available for use either as firm section 311 transportation

⁵ ConocoPhillips contracted with Freeport for the remaining 1.0 Bcf of pre-expansion terminal capacity.

service or firm intrastate transportation service. Dow states that the section 311 firm service would most likely be provided by displacement with regasified LNG flowing to Dow Chemical's plant in Freeport and displacing supplies that would otherwise be transported to Dow Chemical from upstream pipelines that are interconnected to Dow Pipeline.

8. Dow requests that the Commission declare that it is authorized to engage in the transactions described above. Dow acknowledges that Dow Pipeline requires Commission authorization to implement firm NGPA section 311 service, but states that neither the firm section 311 service nor the Freeport LNG terminal service is subject to the capacity release rules applicable to interstate pipelines, including those relating to tying arrangements. As a result, Dow requests waiver, to the extent required, to allow it to link Dow Hydrocarbons' assignment of firm intrastate pipeline service on Dow Pipeline with Dow Chemical's assignment of terminal service at Freeport LNG.⁶

9. Dow also states that its request will not compromise any of the Commission's open access policy goals. Dow states that, to begin with, it can stipulate that the third party or parties with whom Dow Chemical and Dow Hydrocarbons will consummate the linked assignment of pipeline and LNG capacity will not be affiliated with Dow Chemical. Further, Dow states that the negotiations that have occurred and that will occur in the future will be conducted on a fully arms-length basis. Dow also stipulates that the assignment of Dow Pipeline capacity will be structured to assure that the assignee agrees to pay Dow Pipeline's prevailing maximum rate for the firm section 311 transportation service. Dow argues that this should remove any concerns over potential subsidies of such transportation service by any of Dow Pipeline's other transportation customers in the future.

10. Dow requests that the Commission not condition a favorable ruling on any obligation by Dow Chemical to conduct some form of competitive bidding or open season process to enable interested parties to compete to acquire some or all of Dow Chemical's Freeport LNG capacity. Dow states that there are only a handful of LNG market participants in the world that would be in a position to take on the remainder of Dow Chemical's 20-year firm commitment to Freeport LNG, and Dow Chemical firmly believes that its best chance of reaching a successful conclusion in this effort will be to allow it to finish the negotiations it has already started.

⁶ Dow states that, in this regard, the arrangement contemplated by Dow is distinguishable from both of those considered in Order Nos. 712 and 712-A because the pipeline capacity that is to be linked with the release of LNG import capacity is capacity on an intrastate pipeline rather than an interstate pipeline.

11. Dow argues that there is no public interest purpose to be served by denying Dow the ability to link the pipeline and LNG transactions discussed above. Without this ability, Dow argues that Dow Chemical will have no incentive to authorize Dow Hydrocarbons to assign capacity to anyone to be used for section 311 transportation purposes, but will instead continue its historical practice of insuring that such firm capacity is safeguarded to meet Dow Chemical's needs. In contrast, Dow argues, by facilitating the ability of Dow Pipeline to offer this limited form of firm section 311 service, the Commission will be acting to open the gate to more efficient use of terminal capacity at the Freeport LNG terminal and increase the odds that LNG will be imported into that terminal in the future and eventually into interstate commerce, where it can help lower prices and reinforce U.S. supply security.

III. Public Notice, Interventions and Comments

12. Notice of Dow's filing was issued on September 9, 2009. Interventions and protests were due as provided in section 154.210 of the Commission's regulations, 18 C.F.R. § 154.210 (2009). Pursuant to Rule 214, 18 C.F.R. § 385.214 (2009), all timely filed 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. No protests or comments were filed.

IV. Discussion

13. As discussed in more detail below, the Commission finds that, in this case, Dow has presented sufficient information about the proposal to justify granting Dow Chemical, Dow Hydrocarbons, and Dow Pipeline the necessary authority to (a) link Dow Hydrocarbon's assignment of firm intrastate pipeline capacity on the Dow Pipeline system, to be used for firm interstate transportation service under section 311(a)(2) of the NGPA, with an assignment of some or all of Dow Chemical's capacity rights at the Freeport LNG terminal, subject to conditions; and (b) limit the quantity of firm interstate section 311 transportation service Dow Pipeline will make available, subject to conditions.

14. As described above, the Commission regulates intrastate pipelines pursuant to section 311 of the NGPA. One purpose of the NGPA was to encourage intrastate pipelines to participate in the interstate pipeline grid by ensuring that it would not be unduly burdensome to do so.⁷ This participation by intrastate pipelines eliminates the

⁷ See *Associated Gas Distributors v. FERC*, 824 F. 2d. 981, 1001-3 (D.C. Cir. 1987); and *EPGT Texas Pipeline, L.P.*, 99 FERC ¶ 61,295, at 62,252 (2002), *reh'g denied*, 106 FERC ¶ 61,184 (2004) (*EPGT*).

need for duplication of facilities between interstate and intrastate markets. Consistent with the NGPA's goal of encouraging intrastate pipelines to provide interstate service, the Commission has not imposed on intrastate pipelines all of the Part 284 requirements imposed on interstate pipelines. For example, the Commission exempted NGPA section 311 pipelines from any requirement to offer firm interstate transportation service.⁸ The Commission did this to minimize the concern of intrastate pipelines and responsible state authorities that a requirement that NGPA section 311 pipelines offer firm service to out-of-state shippers could lead to the pipeline being progressively being turned into an interstate pipeline.⁹ In addition, the Commission exempted intrastate pipelines from the requirements of Order No. 636, including capacity release, electronic bulletin boards (now internet websites), and flexible receipt and delivery points.¹⁰

15. In this case, Dow seeks, in essence, an authorization for Dow Pipeline to offer a firm NGPA section 311 transportation service that would be limited to shippers who also take an assignment of Freeport LNG terminal capacity. Dow states that the only reason Dow Pipeline is considering offering firm NGPA section 311 service is to facilitate assignment of Dow Chemical's Freeport LNG terminal rights, and that it will likely limit the quantity of firm interstate transportation service it offers under NGPA section 311 to the quantity of terminal capacity Dow Chemical assigns to third parties.

16. Ordinarily, the Commission would not permit an intrastate pipeline to require a shipper contracting for firm NGPA section 311 transportation service also to contract for another distinct service, such as the LNG terminal service at issue here. Although

⁸ See *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 436, FERC Stats. and Regs. Regulations Preambles 1982-1985, ¶ 30,665, at 31,502; Order No. 436-A, FERC Stats. & Regs. Regulations Preambles 1982-1985 ¶ 30,675 (1985). See also *Transok, Inc.*, 56 FERC ¶ 61,275, at 62,083 (1991) (*Transok*); *Northern Illinois Gas Co.*, 95 FERC ¶ 61,452, at 62,644 (2001); and *Oasis Pipeline, LP*, 127 FERC ¶ 61,263, at P 16 (2009).

⁹ See Order No. 436, FERC Stats. and Regs. Regulations Preambles 1982-1985 ¶ 30,665 at 31,502.

¹⁰ *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636, FERC Stats. & Regs. ¶ 30,939, at 30,407 n.89, *order on reh'g*, Order No. 636-A, FERC Stats. & Regs. ¶ 30,950, *order on reh'g*, Order No. 636-B, 61 FERC ¶ 61,272 (1992), *order on reh'g*, 62 FERC ¶ 61,007 (1993), *aff'd in part and remanded in part sub nom. United Distribution Cos. v. FERC*, 88 F.3d 1105 (D.C. Cir. 1996), *order on remand*, Order No. 636-C, 78 FERC ¶ 61,186 (1997).

intrastate pipelines are not required to offer firm interstate service under NGPA section 311, the Commission has held that, if an intrastate pipeline offers such service, it must do so without “undue discrimination or preference of any kind.”¹¹ This includes not discriminating based on “customer classification.”¹² Limiting firm section 311 service to customers contracting for a separate LNG terminal service could be considered undue discrimination based on customer classification. In addition, the Commission generally favors the unbundling of distinct services, even in the case of section 311 services,¹³ and Dow is effectively proposing to bundle firm section 311 transportation service, with an assignment of capacity rights at the Freeport LNG terminal.

17. However, in the unique circumstances of this case, we find that the benefits of granting Dow Pipeline the requested authorizations outweigh concerns about the limits Dow proposes to place on the availability of firm section 311 transportation service. Dow Chemical currently holds capacity in the Freeport LNG terminal which it purchased for the purpose of obtaining natural gas for use in its chemical manufacturing facility. However, it has been unable to locate economically attractive supplies of LNG, and thus it has no need for its capacity at the terminal. Based upon the information provided by Dow, replacement shippers interested in Dow Chemical’s terminal rights require reliable access to an equivalent quantity of firm downstream transportation capacity to access interstate natural gas markets as a condition for taking assignment of Dow Chemical’s terminal rights. Therefore, authorizing Dow Pipeline to provide firm section 311 service to assignees of Dow Chemical’s LNG terminal capacity should result in more efficient use of terminal capacity at the Freeport LNG terminal, and increase the likelihood that LNG will be imported into that terminal in the future and make its way into interstate commerce.

18. Moreover, given that Dow Pipeline is under no obligation to offer firm section 311 service, it does not appear that these benefits would be achieved without granting the requested authorizations. As Dow states, without the authorization to tie these two transactions, Dow Hydrocarbons will have no incentive to assign its firm intrastate capacity on Dow Pipeline to be used for firm section 311 interstate transportation

¹¹ See Section 284.7(b) of the Commission’s regulations. 18 C.F.R. § 284.7(b) (2009). See also Order No. 436-A, FERC Stats. & Regs. Regulations Preambles 1982-1985 ¶ 30,675 at 31,694; and *Transok*, 56 FERC ¶ 61,275 at 62,082 (1991).

¹² See Section 284.7(b)(1) of the Commission’s regulations. 18 C.F.R. § 284.7(b)(1) (2009).

¹³ See *EPGT*, 99 FERC ¶ 61,295.

purposes. Instead, it will retain all the capacity on Dow Pipeline for the purpose for which it purchased it – supplying Dow Chemical’s plant.

19. It also appears from the information provided by Dow that granting the necessary authorizations will not have an adverse effect on open access competition. No party has protested the request or claimed that it would be harmed by the transaction. Moreover, no entity filed to state that it has an interest in obtaining firm section 311 transportation on Dow Pipeline without also obtaining capacity at the Freeport LNG terminal. Dow stipulates that the transaction will be structured to ensure that the assignee of Dow Hydrocarbon’s transportation capacity pays Dow Pipeline’s prevailing maximum rate for transportation service, thereby eliminating any potential subsidies by Dow Pipeline customers in the future. Dow also stipulates that the third party or parties with whom Dow Hydrocarbons and Dow Chemical consummate the proposed transactions will not be affiliated with Dow Chemical, the parent company of Dow Hydrocarbon and Dow Pipeline.

20. Therefore, given the unique circumstances here and the potential public benefit of this proposed transaction, we will grant Dow the necessary authorizations to proceed with the proposed transactions, subject to the Commission’s approval of Dow Pipeline’s request to provide firm section 311 service.

The Commission orders:

The Commission grants Dow’s request for declaratory order as discussed in the body of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.