

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION
100 FERC ¶ 61,254

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, Linda Breathitt,
and Nora Mead Brownell.

Shell Offshore Inc.

Docket No. RP02-99-000

v.

Transcontinental Gas Pipe Line Corp.,
Williams Gas Processing - Gulf Coast Co., L.P.,
Williams Field Services Company, and
Williams Gulf Coast Gathering Co., L.L.C.,

Superior Natural Gas Corporation and
Walter Oil & Gas Corporation

Docket No. RP02-144-000

v.

Williams Gas Processing - Gulf Coast Co., L.P.,
Williams Field Services Company, and
Williams Gulf Coast Gathering Co., L.L.C.

ORDER ON INITIAL DECISION

(Issued September 5, 2002)

Appearances

Thomas J. Eastment, Esq., Charles J. McClees, Jr., Esq., Steven R. Hunsicker, Esq. and Mark J. O'Brien, Esq. on behalf of Shell Offshore Inc.

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Docket Nos. RP02-99-000 and RP02-144-000

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Lorna J. Hadlock, Esq., William J. Collins, Esq., and Arnold H. Meltz, Esq. on behalf of the Federal Energy Regulatory Commission Trial Staff

Philip L. Chabot, Jr., James M. Costan, Esq., and T. Alana Deere, Esq. on behalf of Producer Coalition

Stephen Teichler, Esq., Jennifer Cook, Esq., and Douglas W. Rasch, Esq. on behalf of Exxon Mobil

John W. Wilmer, Jr., Esq., W. Jonathan Airey, Esq., and Jason J. Kelroy, Esq. on behalf of the Independent Petroleum Association of America

1. This proceeding is before the Commission on exceptions to an Initial Decision issued in this proceeding on June 4, 2002 (Initial Decision or I.D.).¹ In this order, we generally affirm the findings of the presiding administrative law judge (ALJ). We affirm the ALJ's findings that Transcontinental Gas Pipe Line Corporation (Transco) and its gathering affiliate, Williams Field Services Company (WFS): (1) acted in concert in offering offshore gathering service to Shell Offshore Inc. (Shell) on the subject spundown North Padre Island (NPI) facilities; and (2) in a manner that frustrates the Commission's effective regulation of Transco.

2. On the basis of the record and the circumstances presented in this case, the Commission finds it necessary to reassert jurisdiction over WFS's gathering rates and services under Sections 4 and 5 of the Natural Gas Act (NGA), 15 U.S.C. §§ 717c, 717d. Accordingly, the rates and services related to the subject spundown NPI facilities will again be considered part of Transco's jurisdictional rates and services that applied before the spindown of these facilities. As discussed below, the Commission finds that an unbundled gathering rate for service on the subject NPI facilities of 1.69 cents per Dth² falls within a zone of reasonableness and will be established pursuant to NGA Section 5.

¹Shell Offshore Inc. v. Transcontinental Gas Pipe Line Corp., Williams Gas Processing-Gulf Coast Company, L.P., Williams Field Services Company, and Williams Gulf Coast Gathering Company, L.L.C., 99 FERC ¶ 63,034 (2002).

²See Appendix.

Accordingly, the Commission directs Transco to file revised tariff sheets to reflect the Commission's approved unbundled gathering rate for the subject NPI facilities, effective as of the date of this order. The Commission also directs Transco to file a proposed rate schedule and form of service agreement for the subject services and all contracts that govern service on the subject NPI facilities.

3. This order benefits customers by ensuring that the Commission's unbundling and gathering policies are not used to circumvent effective regulation of interstate transportation of natural gas.

I. Background

4. The following description of the background of this proceeding is a condensed version of that provided by the ALJ in the Initial Decision, as modified where appropriate. Transco historically designed, constructed and operated its systems in order to perform a bundled service, *i.e.*, purchasing and aggregating gas supplies and transporting those supplies for sale to local distribution companies at the city gate.³ Following its restructuring and transition to an open-access transportation-only pipeline, with respect to service on the NPI system, Transco charged Shell a bundled rate (IT-feeder rate) for its bundled Outer Continental Shelf (OCS) transportation and gathering services. However, as part of an effort to unbundle its gathering services, on November 20, 2000, Transco and its affiliate, Williams Gas Processing-Gulf Coast Company, L.P. (WGP), submitted an application and related petition, in Docket Nos. CP01-32-000 and CP01-34-000, to spin down, *inter alia*, portions of Transco's NPI system located offshore Texas.⁴

5. With respect to the NPI system, Transco sought to spin down its offshore pipeline facilities upstream of NPI Block 956. These facilities consist of two small offshore

³Transcontinental Gas Pipe Line Corp., 96 FERC ¶ 61,115 at 61,432 (2001).

⁴Transco initially sought to abandon a large number of its facilities to become non-jurisdictional gathering pipelines, including the NPI spindown facility at issue here, in February 1999, in Docket No. CP96-206-000. On September 25, 1996, the Commission dismissed Transco's application to abandon all of these facilities as gathering without prejudice to filing a proposal requesting Commission consideration of discrete portions of the facilities. Transcontinental Gas Pipe Line Corp., 76 FERC ¶ 61,317 at 62,542-43 (1996), order denying reh'g, 95 FERC ¶ 61,396 (2001), review pending, Case No. 01-1327 (D.C. Cir.).

pipelines (subject NPI facilities) that converge in the OCS at NPI Block 956 where they both deliver gas into a Transco pipeline. One leg consists of 3.83 miles of 10-inch pipeline that begins on the upstream end in NPI Block 967 and ends at NPI Block 956. The other leg consists of 18.79 miles of 20-inch pipeline that begins in NPI Block A-42 and also ends at NPI Block 956. Shell's production originating from NPI Blocks 969 and 976 is delivered into the 20-inch line via a Shell undersea gathering pipeline interconnect in NPI Block 948 that is 3.08 miles from the Transco jurisdictional pipeline in Block 956. These pipelines deliver gas into a 24-inch NGA-regulated Transco IT-feeder rate transmission pipeline at the common point of interconnection on the OCS for transportation to onshore points in Texas.⁵ The NPI system also includes an 18.75 mile 16-inch pipeline that transports gas from Chevron Platform Block A-31 Mustang Island to the Amerada Hess Platform in Block A-42, connecting with the upstream end of the spudown WFS 20-inch line on this platform. This line always has been classified as gathering and has never been considered a jurisdictional part of the interstate transmission system. Accordingly, it is referred to as the "always gathering" line. The volumes of the upstream "always-gathering" line producers (such as Apache Corporation and Houston Exploration) flow into the NPI spudown gathering line which serves Shell.

6. In an order issued on July 25, 2001, the Commission approved Transco's application to abandon the facilities located at or upstream of NPI Block 956 to its affiliate, WGP (WFS's parent company).⁶ The Commission also granted WGP's request to declare that the facilities, upon transfer to WGP, would be gathering facilities and services, exempt from the Commission jurisdiction pursuant to NGA Section 1(b). All facilities located downstream of NPI Block 956, which includes approximately 230 miles of Transco's NGA jurisdictional IT-feeder line that interconnects with Transco's mainline at Station 30, continued to be classified as transmission.

7. Representatives of Shell and WFS met to discuss the spindown in November 2001, but were unable to agree on a higher gathering charge or other terms and

⁵Transcontinental Gas Pipe Line Corp., 96 FERC ¶ 61,115 at 61,430 (2001).

⁶Transcontinental Gas Pipe Line Corp., 96 FERC ¶ 61,115 (2001), reh'g denied, 97 FERC ¶ 61,296 (2001), review pending, Amerada Hess Corp., et al. v. FERC, Case No. 02-1053, et al. (filed Feb. 11, 2002). WGP later transferred the facilities to its other affiliate, WFS.

conditions proposed by WFS.⁷ WFS offered Shell an 8-cent gathering rate that would be charged in addition to the pre-existing IT-feeder rate of 8 cents per Dth and result in a 16-cent rate for gathering and IT-feeder service from NPI Block 948 to Station 30 instead of the pre-spin-down IT-feeder rate of 8 cents per Dth. The gathering and transmission services provided on the NPI system would remain the same as the transmission service provided prior to the spindown.⁸ The total haul from NPI Block 948 to Station 30 is about 230 miles. The additional gathering rate would be imposed on a 3.08-mile portion of the total haul to Station 30.⁹ As a result of the egregious rates and anti-competitive terms and conditions of service in the proposed gathering agreement, Shell shut in its gas.

8. On November 30, 2001, Shell filed a complaint against Transco and its affiliates, WGP, Williams Field Services Company (WFS) and Williams Gulf Coast Gathering Company, L.L.C. (collectively, WFS or Williams), in Docket No. RP02-99-000. In its complaint, Shell alleged that Transco and its affiliates were acting in concert in an anti-competitive manner in connection with the transportation of gas in interstate commerce, by requiring that Shell enter into a gathering agreement for service on the NPI facilities that would impose unjust and unreasonable rates and would require anti-competitive terms and conditions of service. The terms and conditions of service included a condition requiring that Shell dedicate all its reserves to WFS and a condition requiring Shell to agree not to take action that would result in a reassertion of NGA jurisdiction (referred to as the "jurisdictional impact" clause). Shell requested that the Commission reassert its jurisdiction under the NGA over the NPI facilities upstream of NPI Block 956 that were abandoned and spun down by Transco to its non-jurisdictional affiliate.

9. On January 15, 2002, Superior Natural Gas Corporation and Walter Oil & Gas Corporation (collectively, Walter) filed a joint complaint against Williams in Docket No. RP02-144-000. Walter alleged that Williams is imposing anti-competitive and discriminatory rates and terms and conditions for gathering service on a non-jurisdictional portion of the NPI system in violation of the Outer Continental Shelf Lands Act (OCSLA), 43 U.S.C. §§ 1301-1356, and the Commission's implementing regulations.

⁷Id. at 65,231, Exh. SOI-6, Shell Brief Opposing Exceptions at 7.

⁸See Tr. 1008 (Malmquist); see also Exh. SOI-4 at 7 (Harris); Exh. SOI-11 at 5 (Harris).

⁹See Exhibit SOI-11 at 5 (Harris); Tr. 1008 (Malmquist).

10. On March 6, 2002, the Commission established an expedited hearing in this proceeding to develop the factual record "to determine if Transco and its affiliates acted in concert with one another in offering gathering services on the North Padre system and in a manner that frustrates the Commission's effective regulation of Transco."¹⁰ The March 6, 2002 order deferred to future orders the Commission's determination of whether the rates, terms and conditions of service for the gathering services are unjust and unreasonable, or otherwise unlawful under the NGA, and what remedies, if any, may be appropriate under the NGA. In addition, the March 6, 2002 order set for hearing whether the open and nondiscriminatory access requirements of Section 5 of the OCSLA have been violated and any appropriate remedies that may be available under the OCSLA.

11. The hearing began on April 8, 2002. In briefs filed with the ALJ, Shell alleged that Transco and WFS acted in concert in implementing the abandonment and spindown in a manner that frustrates the Commission's objective to foster competition in the gathering industry by unlawfully using their market power to impose upon Shell unjust and unreasonable gas transportation rates and anti-competitive conditions to Shell's access to the essential NPI facilities. Shell requested that the Commission reassert jurisdiction under the NGA over the pipeline facilities upstream of the platform in NPI Block 956 that were ultimately abandoned by transfer to Transco's affiliate, WFS.

12. In Transco's separate, but related general NGA Section 4 rate proceeding in Docket No. RP01-245-000, the Commission issued an order on December 19, 2001 requiring Transco to remove all costs associated with the abandoned NPI gathering facilities from its rates, effective December 1, 2001.¹¹ On January 18, 2002, in Docket No. RP01-245-007, Transco filed proposed revised tariff sheets to remove the costs of the NPI gathering facilities from its rates, as directed. In an order issued on February 28, 2002, in Docket No. RP01-245-007, the Commission consolidated the issues raised with regard to Transco's January 18, 2002 compliance filing with the ongoing hearing

¹⁰Shell Offshore Inc. v. Transcontinental Gas Pipe Line Corp., Williams Gas Processing-Gulf Coast Company, L.P., Williams Field Services Company, and Williams Gulf Coast Gathering Company, L.L.C., 98 FERC ¶ 61,253 at 62,017 (2002), reh'g denied, 99 FERC ¶ 61,153 (2002).

¹¹Transcontinental Gas Pipe Line Corp., 97 FERC ¶ 61,302 (2001).

proceeding in that docket.¹² On April 12, 2002, Transco filed a partial settlement agreement, in Docket No. RP01-245-008, to resolve, among other things, issues related to Transco's rates reflecting a settled cost of service, overall throughput level and mix of throughput for the Docket No. RP01-245 rate period.¹³ The agreement also resolved all issues concerning Transco's January 18, 2002 compliance filing in Docket No. RP01-245-007.

13. Shell states that, subsequent to the close of the record in this case, the Mineral Management Service of the United States Department of the Interior (MMS) informed Shell that it would allow Shell to suspend its production from the NPI leases, only through June 30, 2002.¹⁴ Shell states that it therefore resumed production from its leases and entered into a month-to-month gathering agreement with WFS, terminating December 31, 2002, subject to refund based on the outcome of this proceeding, but that this temporary agreement does not obviate the need to resolve the issues presented in this case.

II. ALJ's Decision

14. As directed in the March 6, 2002 order, the ALJ relied on the two-part test set forth by the Commission in Arkla Gathering Services Co. (Arkla),¹⁵ in analyzing whether the Commission may disregard separate corporate structures and exert control over the gathering activities of Transco's affiliated gatherer, WFS. Specifically, the ALJ considered whether: (1) Transco and its affiliates acted in concert with one another in offering gathering services on the NPI system (2) and in a manner that frustrates the Commission's effective regulation of Transco. In sum, the ALJ found that The Williams

¹²Transcontinental Gas Pipe Line Corp., 98 FERC ¶ 61,225 (2002).

¹³The Commission accepted the partial settlement in a letter order issued on July 23, 2002. Transcontinental Gas Pipe Line Corp., 100 FERC ¶ 61,085 (2002).

¹⁴Shell Brief Opposing Exceptions at 21-22.

¹⁵67 FERC ¶ 61,257 at 61,871 (1994), order on reh'g, 69 FERC ¶ 61,280 (1994), reh'g denied, 70 FERC ¶ 61,079 (1995), reconsideration denied, 71 FERC ¶ 61,297 (1995).

Companies (TWC)¹⁶ affiliates, Transco and WFS, acted in concert in offering gathering services and abused their monopoly market power in a manner that frustrates the Commission's effective regulation of Transco and the interstate transportation of natural gas from the NPI system.¹⁷ Based on these findings, the ALJ concludes that reassertion of jurisdiction by the Commission under the NGA would remedy the concerted abusive monopoly market power actions planned and taken by the Williams affiliates which have frustrated the Commission's effective regulation of Transco and the interstate transportation of natural gas from the NPI system.¹⁸

15. With respect to the first part of the Commission's two-part test, the ALJ finds concerted action between Transco and its affiliates. The ALJ finds that, through the corporate structure and in association with their collective parent, the TWC affiliates, WFS and Transco, act as one entity for purposes of gathering and transporting of natural gas in interstate commerce in association with services they provide for Shell.¹⁹ The ALJ states that the record is replete with facts of ongoing cooperative activities between WFS and Transco. These activities include: WFS and Transco working together in planning and implementing the spindown of the NPI facilities; WFS acting as Transco's agent in contracting for transmission services across the Transco production area supply laterals for IT and IT-feeder services; and WFS operating the physically integrated NPI WFS gathering and Transco jurisdictional production area facilities, including day-to-day operation and maintenance of meters, valves, compressors and other facilities.²⁰ The ALJ concludes that these concerted actions raised rates for the NPI service to monopolistically egregious levels and permitted WFS to command other terms and conditions of service not desirable to the producer/shipper. In this case, the ALJ finds

¹⁶TWC is the common parent of Transco and WFS, holding 100 percent of the interest in both affiliates.

¹⁷Id. at 65,230, 65,260.

¹⁸Id. at 65,260.

¹⁹Id. at 65,243.

²⁰Id. at 65,240-41.

that the producer/shipper no longer has countervailing negotiating strength at NPI and thus lacks the power to protect itself.²¹

16. Furthermore, the ALJ states that perhaps more significant than the continued operational and integration cooperative activities of WFS and Transco, is the inter-affiliate transfer and corporate plan. The ALJ states that the concerted action between TWC, Transco and WFS began with the planned spindown of the NPI project from Transco in 1994-1995 (including the sale of the NPI facilities to WFS), and the associated business plan from their corporate parent TWC, and continues through the enactment and enforcement of the current Operating Agreement between the two affiliates.²² Thus, with respect to Shell, the ALJ concludes that the services on NPI are essentially one continuous transaction.²³ The concerted action among the affiliates, according to the ALJ, enabled them to exercise and abuse their market power, which resulted in the frustration of the Commission's NGA regulation of Transco's interstate transportation of natural gas.²⁴

17. According to the ALJ, WFS and Transco currently have a monopoly on the gathering and transportation of natural gas on the NPI system because producers must flow gas produced on the NPI system through WFS's gathering pipeline and into Transco's NGA jurisdictional IT-feeder transmission pipeline in order to get downstream

²¹Id. at 65,241.

²²For example, the ALJ finds that WFS and Transco collectively reviewed the WFS Business Plan that incorporated a consultant firm's report (McKinsey Report) regarding the value associated with NPI gathering services to customers with no other service options. The ALJ states that the McKinsey Report also included an analysis of the opportunity to collect "IT-feeder rents" in gathering rates upon a shift in Transco's rate design, which TWC tried to capture by creating WFS as a non-jurisdictional gathering provider. The ALJ finds that WFS would not have been able to capture the increased rents for the combined gathering and transmission service from captive producers lacking a good alternative if the facilities remained under the Commission's jurisdiction. Id. at 65,241.

²³Id. at 65,241.

²⁴Id. at 65,249.

to onshore markets.²⁵ The ALJ finds that, based on the record, WFS's proposed 8-cent per Dth rate precludes consideration of a bypass to Transco's IT-feeder line, while at the same time, demonstrating the exercise of market power by WFS and Transco in demanding the anti-competitive 8-cent rate.²⁶

18. In finding that WFS and Transco have abused their market power, the ALJ focuses on WFS's price term as the most significant aspect. The ALJ rejects arguments by WFS and Transco that an NGA-regulated rate is not a fair competitive market rate or WFS's alternative argument that an NGA cost-of-service type rate would be close to 8 cents for its gathering service. The ALJ also rejects arguments by Transco and WFS that gathering rates on the non-jurisdictional lines through the Gulf of Mexico, including on the NPI system, should be used for comparison, and that those rates are competitive with 8 cents.²⁷ Instead, the ALJ generally agrees with Shell, the Staff and their supporters, that an NGA-regulated rate is a good approximation of a fair competitive market rate.²⁸ The ALJ thereby concludes that the 8-cent gathering rate demanded by WFS, in addition to the almost 8-cent IT-feeder NGA-regulated rate which Shell must continue to pay to Transco, is an abuse of market power.²⁹ The ALJ adopts the Staff's NGA-regulated unit rate for gathering on the subject spundown facilities of 2.5 cents as a fair approximation

²⁵Id. at 65,243, citing Tr. 721-27 (Johnston); SOI-4 at 3-4, 8 (Harris); SOI-1 at 5-6 (Means).

²⁶Id. at 65,244-45.

²⁷Id. at 65,246-47.

²⁸Id. at 65,247.

²⁹Id. at 65,247. The ALJ also notes that in a competitive market, alternative service providers tend to drive rates down toward the cost of providing service plus a reasonable return. Citing SOI-1 at 9-10 (Means); SOI-10 at 7 (Means); Tr. 1484-85, 1731-32, 1741-42 (Sullivan); Tr. 600 (Harris); and *Interstate Natural Gas Assoc. of America v. FERC*, 285 F.3d 18 at 30 (D.C. Cir. Apr. 5, 2002) ("the basic premise of the NGA is the understanding that natural gas pipeline transportation is generally a natural monopoly . . . so that without regulation the rates of pipeline companies would exceed competitive rates, i.e., ones approximating cost").

of a market rate for gathering service on the spundown facilities.³⁰ However, the ALJ states that it is sufficient to confirm WFS's and Transco's obvious market power over NPI gathering and transmission, and the abuse of that power, simply to compare the doubling to Shell of the combined gathering and transportation rate from 8 to 16 cents.³¹

19. The ALJ rejects WFS's argument that the rates charged for gathering on other Gulf of Mexico gathering lines are a relevant measure of a reasonable competitive market price for WFS's facilities, and therefore concludes that such rates are not pertinent to whether WFS and Transco have abused their monopoly market power.³² The ALJ finds that, under the present circumstances, Shell has no viable alternatives to WFS providing needed gathering service and the fair market unit price for gathering on a particular line is subject to the specific cost conditions at the location (including water depth), levels and proximity of reserves, and competitive circumstances (*e.g.*, distance to any number of existing pipelines with capacity) at the location and time of construction or abandonment of the line.³³ In addition, the ALJ notes that it could be that many of the other gathering rates, whether the result of deals between affiliate producers and gatherers or between non-affiliates, do not reflect competitive, non-discriminatory situations. The ALJ notes that there are too many differences among gathering lines, even on the NPI system, to determine whether other gathering rates are competitive.³⁴

20. The ALJ finds that the record contains no demonstrated, direct effect on the downstream market for purchasers of natural gas at pooling points, such as Station 30 on Transco's IT-feeder transmission line resulting from WFS's and Transco's abuse of

³⁰*Id.* at 65,249. Staff's approximation is based on Transco's data for annual cost of service of the subject spundown facilities of \$937,142, including Transco's as-filed rate of return in Docket No. RP01-245 of 12.25%. Staff uses current throughput, including Shell's shut-in volumes of about 100,000 Dth per day. *I.D.* at 65,247.

³¹*Id.* at 65,249.

³²*Id.* at 65,250.

³³*Id.* at 65,250, *citing* SOI-11 at 3, 10-12 (Harris); Tr. 431, 657-660 (Harris).

³⁴*Id.* at 65,250-51.

market power over gathering of Shell's gas on the NPI system.³⁵ However, the ALJ finds that the "WFS NPI gathering grip" may ultimately harm consumers because the distortions of price signals by monopoly abuse of ratepayer producers could ultimately distort production and development decisions.³⁶

21. After finding that the concerted actions of Transco and WFS have resulted in an abuse of market power, the ALJ turns to the second part of the Commission's two-part test, *i.e.*, whether this concerted action has frustrated the Commission's effective regulation of the NGA-regulated pipeline, Transco. The ALJ concludes that the concerted actions of the corporate family and the fact that service across NPI is collectively a single service traversing the gathering and transmission systems, allow Transco's affiliated corporate family to benefit from collecting monopoly rents it could not extract if it were subject to Commission regulation.³⁷ The ALJ explains that, since WFS is currently unregulated, the corporate family collects the upside monopoly premium through the unchecked gathering rates portion of the collective NPI gathering and transportation service for the benefit of WFS and Transco.³⁸ The ALJ states that this abuse of market power, by itself, frustrates the Commission's effective regulation of Transco, but that there are also other examples of such frustration. These examples include: (1) WFS's and Transco's use of a "push-down" premium (a goodwill premium above book value paid by TWC to Transco for acquiring its facilities) which effectively caused ratepayers to pay for the same facility more than once; (2) Staff's assertions that Transco has not adequately audited its books to ensure that non-jurisdictional costs are not transferred to jurisdictional rates;³⁹ (3) undue discrimination favoring the pre-existing "always-gathering" shippers that use WFS's upstream gathering service by not charging them any additional rates for gathering service in the spundown facilities across the

³⁵Id. at 65,251, citing T/WFS-3 at 2-6 (Johnston).

³⁶Id. at 65,252, citing SOI-1 at 12-13 (Means).

³⁷Id. at 65,254.

³⁸Id. at 65,254-55.

³⁹As an example of Transco's apparent misassignment of costs among its various NPI-area enterprises, the ALJ states that Transco erroneously labeled \$320,756 attributable to painting a platform on the "always-gathering" facilities as part of the costs for the spin-down facilities and appears to have carried this error through to include that cost as part of the spindown facilities' cost of service. *I.D.* at 65,247 n.37.

spundown facilities (for a service of 18.79 miles) while attempting to charge Shell, which uses its own upstream gathering services for service on these facilities (for a service of 3.08 miles).

22. Moreover, the ALJ finds that WFS's initial proposed agreement contained an explicitly "non-negotiable" rate term. In addition, the ALJ finds that the agreement contained a "non-negotiable" dedication of reserves term, and a condition stating that, if "any action" resulted in reinstatement of NGA jurisdiction, the parties would rework the contract to bring each to its original condition.⁴⁰ The ALJ concludes that, under these circumstances, the 100 percent rate increase for the same combined service Shell received before spindown, along with the restrictive conditions (e.g., dedication of reserves and jurisdictional impact clauses) are in fact exclusionary and anti-competitive and violate the Commission's pro-competitive initiatives for the OCS gathering industry.⁴¹

III. Briefs on Exception

23. Transco and WFS filed briefs on exception and requests for oral argument. On exception, Transco argues that the Initial Decision erroneously finds frustration of NGA regulation by assuming that gathering is part of an "interstate transportation path" even though the path contains a gathering part that is exempt from NGA jurisdiction and an IT-feeder part that is subject to NGA regulation.⁴² Transco argues that, even if the gathering/IT-feeder path is the proper basis for assessing monopoly power, the record contains only market power analysis of the NPI spindown facilities instead of the broader "delivered gas" market, extending to the downstream market centers and pooling points (such as Station 30).⁴³

⁴⁰Id. at 65,258-59.

⁴¹Id. at 65,260.

⁴²Transco Brief on Exceptions at 20-25, citing Id. at 65,254-55.

⁴³Transco Brief on Exceptions at 26-29. Transco states that the broader "delivered gas" market dynamics reveal gas flows competing side-by-side for deliveries to these downstream pooling points or market centers, and in the long run, producers such as Shell and gatherers such as WFS have incentives to fairly negotiate prices and terms which will allow their shared stream of gas to compete and flow to these market centers;

(continued...)

24. Transco and WFS argue that the ALJ erroneously applied the standards set forth in Northern Natural Gas Co. v. FERC (Northern Natural)⁴⁴ and Conoco Inc. v. FERC (Conoco)⁴⁵ to support asserting NGA jurisdiction over spudown gathering facilities. Transco states that the Northern Natural court was concerned that a bundled, merchant pipeline could use its own gathering facilities to discriminate in favor of its own gas to the disadvantage of third-party shippers, a concern that does not apply here because there is no allegation that Transco has sought to use the gathering facilities to discriminate in favor of its own gas.⁴⁶ Transco also asserts that the Conoco court's decision only mentioned the Commission's possible ability to assert jurisdiction over gathering "as an abstract matter."⁴⁷ Similarly, WFS asserts that the ALJ relies upon dicta in various appellate cases.⁴⁸ WFS states that the Commission decisions invoked by the ALJ note that the Commission lacks jurisdiction over entities not engaged in either sales for resale, or transmission in interstate commerce, because such entities are not natural gas companies within the meaning of the NGA.⁴⁹

25. WFS also argues that Shell's allegations fall outside the scope of conduct that would trigger Commission jurisdiction under the two-part test and disputes the ALJ's finding that the alleged abuse in this case is "directly related to the affiliate's unique

⁴³(...continued)

otherwise neither Shell or WFS (nor Transco) derive any revenues from gas that is shut-in. Citing Transcontinental Gas Pipe Line Corp., 96 FERC at 61,435 (WFS and the existing shippers have a vested interest in reaching mutually agreed upon terms and conditions and WFS has incentive to negotiate fairly with Transco's existing shippers).

⁴⁴929 F.2d 1261 (8th Cir. 1991), cert. denied, 502 U.S. 856 (1991).

⁴⁵90 F.3d 536 (D.C. Cir. 1996), cert. denied sub nom., Amoco Energy Trading Corp. v. FERC, 519 U.S. 1142 (1997).

⁴⁶Citing 929 F.2d at 1270.

⁴⁷90 F. 3d at 549.

⁴⁸WFS Brief on Exceptions at 85-86.

⁴⁹Citing Arkla, 67 FERC at 61,870-71; Mid Louisiana Gas Co., et al., 65 FERC ¶ 61,166 (1993), reh'g denied, 67 FERC ¶ 61,255 at 61,852-53 (1994), reh'g denied, 69 FERC ¶ 61,303 (1994).

relationship with the interstate pipeline."⁵⁰ Transco argues that an unaffiliated purchaser of the NPI facilities could have demanded the 8-cent rate and the other proposed contractual terms and conditions demanded by WFS.⁵¹ WFS argues that Shell raised concerns about the potential for the abuse of market power in the abandonment and spindown proceeding for the NPI facilities, but that the Commission's spindown order relied on its oversight responsibilities under the OCSLA rather than the NGA.⁵²

26. WFS argues that the ALJ's analysis of the "in concert" activity prong of the test is flawed because some concerted activities are unavoidable in the context of a spindown of gathering facilities from a jurisdictional interstate pipeline to its non-jurisdictional gathering affiliate.⁵³ Transco and WFS argue that the ALJ gave undue weight to the significance of the McKinsey Report⁵⁴ and gave no weight to the fact that Transco personnel played no direct role in the negotiation for gathering rates.⁵⁵

27. With respect to the second part of the Commission's two-part test, WFS argues that its conduct in offering Shell an 8-cent gathering rate, in trying to negotiate contract clauses, and in dealing with the "always gathering" producers, has been reasonable.⁵⁶ Therefore, maintains WFS, its conduct does not frustrate the Commission's NGA regulation of NGA facilities. WFS argues that none of the examples provided in Arkla describing circumvention of the Commission's regulations has occurred here. WFS asserts that if the Commission were to adopt the formulation in the Initial Decision regarding whether the corporate parent will benefit, then every spindown in which costs are reduced, or earnings are enhanced, will satisfy the concerted activity standard, and thereby jurisdiction will re-affix to most spindowns. More importantly, maintains WFS,

⁵⁰WFS Brief at 18, citing I.D. at 16 (quoting Arkla, 67 FERC at 61,871).

⁵¹WFS Brief on Exceptions at 18, 92-93.

⁵²WFS Brief on Exceptions at 95.

⁵³WFS Brief on Exceptions at 69.

⁵⁴WFS Brief on Exceptions at 71-75; Transco Brief on Exceptions at 43-45.

⁵⁵WFS Brief on Exceptions at 18, 82; Transco Brief on Exceptions at 39-40.

⁵⁶WFS Brief on Exceptions at 61.

there has been no harm to consumers because NPI volumes would not affect market prices.⁵⁷

28. Transco argues that the Initial Decision misconstrues and misapplies the Commission's policy of prohibiting write-ups on property acquired at a premium. Transco asserts that the Initial Decision does not consider that the "gain" of \$4 million has never been paid by ratepayers but is the premium the shareholders paid in the first instance to acquire the assets and they have been fully at risk thereafter as to whether the assets would retain such value upon ultimate sale.

29. WFS disputes the ALJ's finding that the rate treatment of "always gathering" shippers compared to the rate treatment of Shell represents undue discrimination among shippers at NPI.⁵⁸ WFS states that the "always gathering" shippers generally pay more for WFS NPI gathering service than WFS offered Shell but that the ALJ focuses on the fact that the "always gathering" producers did not have their pre-spindown gathering rates increased for the post-spindown elongation of their NPI gathering service. WFS also states that it is totally consistent with the zone rate concept for the always gathering shippers to pay nothing extra to ship farther in an expanded NPI zone and for Shell, who was paying no gathering charge in WFS' NPI zone to incur a new gathering charge in its new contract to begin gathering service in the NPI zone.⁵⁹

30. With respect to the 8-cent gathering rate offered to Shell, WFS states that such a rate does not frustrate the Commission's regulation of Transco. WFS states that, assuming the Commission reasserted NGA regulation, Transco would be subject to the Commission's NGA regulation and may adjust its current systemwide gathering rate of 19 cents per Dth to account for the costs and throughput of the NPI spindown facilities, but that there is no evidence in the record to show that the current Transco 19-cent gathering rate would be reduced anywhere close to 8 cents.⁶⁰ WFS states that a transfer of netback revenue to the seller of transport services is the same result which the Commission actively promoted when it lifted the rate ceiling for short-term capacity release transactions. In addition, WFS states that the record shows that Shell's NPI gas

⁵⁷WFS Brief on Exceptions at 64.

⁵⁸WFS Brief on Exceptions at 57, citing Id. at 65,257.

⁵⁹WFS Brief on Exceptions at 60.

⁶⁰WFS Brief on Exceptions at 47.

volumes have no discernible impact on the competition to sell Gulf of Mexico gas to gas consumers.⁶¹ Furthermore, WFS states that the ALJ erred in using an NGA-regulated rate as a surrogate for a competitive rate for gathering service because the gathering facility is exempt from NGA jurisdiction and the 8-cent rate is a "below-market" and "reasonable" rate for gathering service when compared to other gathering rates in the NPI region.⁶² WFS states that the relevant market is for gathering as a service that takes a producer's gas from the producing platform to the interstate pipeline grid where NGA-regulated rates begin to apply.⁶³ Therefore, argues WFS, viewed in the context of the total cost to get to the Commission-regulated interstate pipeline, the WFS offer to Shell of 8 cents for gathering is a commercially reasonable gathering cost. WFS also disputes the ALJ's findings that the conditions of services, *i.e.*, the dedication of reserves and jurisdictional impact clauses are anti-competitive, stating that they were initial offers subject to negotiation with Shell.⁶⁴

31. Moreover, Transco argues that reasserting NGA jurisdiction over the subject gathering would undermine the Commission's Order No. 636 unbundling policies designed to encourage gathering facility spin downs or spin offs by pipelines.

IV. Briefs Opposing Exceptions

32. Shell, Staff, Apache Corporation, Exxon Mobil Corporation, Producer Coalition⁶⁵ and Independent Petroleum Association of America (IPAA) filed briefs opposing exceptions in support of the Initial Decision and the Commission's reassertion of NGA jurisdiction.

⁶¹WFS Brief on Exceptions at 50.

⁶²WFS Brief on Exceptions at 20.

⁶³WFS Brief on Exceptions at 36-37.

⁶⁴WFS Brief on Exceptions at 51.

⁶⁵For purposes of this proceeding, the Producer Coalition consists of: Devon Energy Corporation, Dominion Exploration & Production, Inc., Forest Oil Corporation, the Houston Exploration Company, Newfield Exploration Company, and TotalFinaElf E&P U.S.A. Inc.

33. Shell urges the Commission to adopt the Initial Decision and, as recommended by the ALJ, reassert NGA jurisdiction over the spundown NPI gathering facilities because the concerted actions of WFS and Transco have frustrated the Commission's effective regulation of Transco. In general, Shell argues that WFS and Transco have acted together to generate monopoly rents from captive producers based on a change in the regulatory regime governing their facilities for gathering and transmission services now provided on the NPI system that are the same as the transmission service provided prior to the spindown.⁶⁶ According to Shell, the only change is that one piece of the unitary service provided on the integrated NPI system is now deemed gathering and one piece is deemed transmission, even though there is no actual ability for shippers to unbundle the gathering and transmission components of this unitary service since gas that enters the spundown gathering facilities must be transported on Transco's transmission facilities.

34. Shell states that the ALJ correctly determined that the Commission may reassert NGA jurisdiction over a gathering company affiliated with an interstate pipeline based on Northern Natural and Conoco.⁶⁷ Shell states that this precise jurisdictional result was reached in Northern Natural based on the Eighth Circuit's reading of Colorado Interstate Gas Co. v. FPC⁶⁸ and the Conoco court expressly agreed that "such jurisdiction" was supported by applicable Supreme Court precedent.⁶⁹

35. Shell contends that the ALJ correctly applied the standard for "in concert" activity and that there is overwhelming evidence of concerted actions. Shell argues that the joint operating and business arrangements and the physical integration of the gathering and transmission facilities allow Transco's agent, WFS, to have complete control over the total rate offered for the gathering and transmission service on the NPI system, which allows WFS to exact monopoly rents for both transmission and gathering service by ostensibly adding such rents to the rate for the gathering portion of the overall integrated

⁶⁶Shell Brief Opposing Exceptions at 23, citing Tr. 1008 (Malmquist); Exh. SOI-4 at 7 (Harris); Exh. SOI-11 at 5 (Harris).

⁶⁷Shell Brief Opposing Exceptions at 42.

⁶⁸324 U.S. 581 (1945).

⁶⁹90 F.3d at 546.

service.⁷⁰ In response to WFS's argument that the evidence of concerted actions reflect an effort to make money for shareholders, Shell states that, while it may be the objective of corporations to maximize revenues for shareholders, it is equally the responsibility of the Commission to constrain the corporate profits of pipeline companies, which are natural monopolies.⁷¹

36. With respect to the concerted action part of the Commission's two-part test, Staff notes that the record establishes that the planning and implementation of the spindown of the subject NPI gathering facilities points to concerted activities between WFS and Transco. In addition, Staff asserts that the record establishes that WFS and Transco acted in concert to physically operate the Transco IT-feeder system and the spundown NPI gathering facilities through an operating agreement under which WFS agrees to act as Transco's agent to operate and maintain Transco's IT feeder system. The services provided under the agreement by WFS include: pressure and flow control, maintaining monitoring and communication equipment, submitting and maintaining all non-FERC licenses and permits to governmental agencies, communicating with shippers regarding routine business matters, the negotiation of gathering and transmission service contracts on the Transco IT-feeder facilities and the NPI facilities, and platform lease and interconnection agreements. Furthermore, Staff states that WFS and Transco acted in concert by using the same WFS personnel to negotiate transmission service contracts for Transco's IT feeder facilities and gathering service contracts on the NPI facilities.

37. Staff also asserts that WFS and Transco acted in concert in a manner that allowed non-jurisdictional NPI gathering costs to be passed through to and collected from Transco's jurisdictional transportation customers. In particular, Staff notes that \$320,756 of non-jurisdictional Operation & Maintenance (O&M) costs incurred by WFS in painting a platform on the "always-gathering" NPI pipeline were mistakenly charged to Transco.⁷² These non-jurisdictional NPI costs were included in Transco's recent rate increase filing in Docket No. RP01-245, which became effective September 1, 2001, and were subsequently removed from Transco's rates effective December 1, 2001, in compliance with a Commission order requiring Transco to remove the costs of the NPI

⁷⁰Shell Brief Opposing Exceptions at 58.

⁷¹Id.

⁷²Staff Brief Opposing Exceptions at 17-18.

spindown facilities from rates upon the effective date of the transfer of NPI to WFS.⁷³ Therefore, for a period of three months, the non-jurisdictional costs were included in Transco's rates. Staff notes that, while Transco may not have intended to collect non-jurisdictional costs through its rates, its affiliate relationship with WFS provided no incentive to carefully check the costs of WFS.⁷⁴

38. Shell agrees with the ALJ's conclusion that WFS and Transco currently have monopoly power in the market for the gathering and transportation of natural gas on the NPI system and that the market power is currently constrained only to the extent the Commission is able to effectively regulate the transmission of gas.⁷⁵ Shell argues that WFS and Transco have abused their market power by placing demands that are based on exploiting regulatory change rather than enhancing service; by demanding rates far above their costs; by demanding anti-competitive terms and conditions; by making demands that are not fair nor commercially reasonable; that Transco's gathering rate is irrelevant; and that the rates demanded by WFS are unduly discriminatory.

39. Shell rejects Transco's and WFS's arguments that it does not have, or has not abused, market power. For example, Shell rejects WFS's contention that the relevant market to be considered is the service of transporting gas from the platform to an interstate pipeline, thereby comparing its 8-cent offer to other rates for bringing gas from platforms to interstate pipelines in the Gulf of Mexico.⁷⁶ Shell argues that such a broad definition of the relevant market suggests that gathering service for gas produced from one area is competitively relevant to the gathering service produced from another field.⁷⁷ Shell states that the relevant market for gathering here is no larger than the market for gathering gas produced in the NPI area that can be transported on the NPI system. Therefore, comparing WFS's 8-cent rate demand for gathering on the NPI system with gathering rates charged even for service in the deepwater far from the NPI system does not determine whether WFS and Transco possess market power or whether they are abusing such power. Similarly, Shell rejects Transco's argument that the relevant market

⁷³Transcontinental Gas Pipe Line Corp., 97 FERC ¶ 61,302 (2001).

⁷⁴Staff Brief Opposing Exceptions at 18.

⁷⁵Shell Brief Opposing Exceptions at 50, citing Id. at 65,243.

⁷⁶Shell Brief Opposing Exceptions at 64.

⁷⁷Id.

is the delivered gas sales market onshore, countering that it is no defense to an abuse of market power in one market that another downstream market is competitive.⁷⁸

40. Shell also argues that Transco and WFS possess monopoly power over the transportation and gathering of natural gas on the NPI system because there are no good alternatives to the use of the NPI facilities. Specifically, Shell states that there are no potential competitors that would provide a good alternative to WFS's gathering service and that a 3.08-mile bypass extending from NPI Block 948 to NPI Block 956 may be potentially futile and too costly. Shell also asserts that it does not have countervailing market power as a monopsonist.

41. Shell asserts that WFS and Transco have abused their market power.⁷⁹ Shell states that WFS and Transco: (1) extracted exorbitant profits by exploiting a change in the jurisdictional status of their facilities; (2) demanded an 8-cent per Dth rate, which is over four times the cost of service of about 1.7 cents per Dth; and (3) demanded anti-competitive terms and conditions, such as the life-of-the-reserves commitment and a condition eliminating Shell's rights to request that the Commission to assert NGA jurisdiction over the NPI gathering facilities. Moreover, Shell asserts that WFS's demands are neither fair nor commercially reasonable. Finally, Shell contends that WFS and Transco abused their market power by unduly discriminating in favor of shippers in the "always gathering" portion of the NPI system by not seeking a gathering charge from them for a haul of 18.79 miles in the spundown facilities, whereas WFS demanded that Shell pay 8 cents for a haul of 3.08 miles on the same facilities.

42. With respect to the ALJ's finding that the Commission's effective regulation of Transco and the interstate gas transportation market has been frustrated, Staff states that the record evidence clearly establishes that the gathering rate offered to Shell bears no relationship to WFS's costs. A monopolist like WFS, maintains Staff, can sustain a price that is far above its cost by exercising market power. According to Staff, now that NGA regulation has been removed subsequent to the construction of a gathering system and after gas reserves have been substantially depleted, Shell has been left subject to WFS's unconstrained market power.⁸⁰ Staff states that, by shifting non-jurisdictional gathering costs to Transco's jurisdictional ratepayers for recovery, WFS and Transco effectively

⁷⁸Shell Brief Opposing Exceptions at 65-66.

⁷⁹Shell Brief Opposing Exceptions at 79-94.

⁸⁰Staff Brief Opposing Exceptions at 41 citing Exhibit No. SOI-1 at 6-8, Tr. 1531-35.

manipulated the costs of gathering, thereby frustrating the Commission's effective regulation of Transco.

V. Commission Decision

43. The Commission generally affirms the Initial Decision. As discussed below, the Commission finds that the ALJ's analysis of the facts established in the record is generally well-reasoned and provides a sound basis for reasserting NGA jurisdiction over the subject rates and services provided on the spundown NPI gathering facilities. The record establishes that Transco, a jurisdictional pipeline, and WFS, its nonjurisdictional gathering affiliate, acted as a single entity with respect to offering gathering rates and services on the NPI gathering system and did so in a manner that frustrates the Commission's effective regulation of Transco. As a result, the Transco/WFS single entity (Transco/WFS) was able to demand rates, terms and conditions of service that are unjust, unreasonable and unduly discriminatory, in violation of Sections 4 and 5 of the NGA. In addition, the gathering rates, terms and conditions of service constitute a barrier to open and nondiscriminatory access under OCSLA Section 5. Therefore, the Commission will reassert NGA jurisdiction, and thereby re-regulate the rates, terms and conditions of the subject spundown gathering service on the NPI system, pursuant to Sections 4 and 5 of the NGA. The Commission also finds that it has the jurisdiction, pursuant to Section 5 of the OCSLA, to enforce the open and nondiscriminatory access requirements of that statute over the rates and services demanded for the subject gathering services on the NPI system.

44. Because the record reflects that Transco and WFS acted in concert with each other, we will treat WFS as if it were a division of Transco. Accordingly, the rates and services of the NPI spundown facilities will again be considered part of the rates and services of Transco's system, and Transco will be directed to file revised tariff sheets to reflect this ruling.

A. Authority to Reassert NGA Jurisdiction

45. The Commission affirms the ALJ with respect to his ruling on the Commission's NGA jurisdiction.⁸¹ The ALJ's analysis is well-reasoned and hereby adopted. The Commission does not assert jurisdiction over companies that perform only a gathering function because the NGA defines "natural gas companies" that are subject to the NGA

⁸¹See I.D. at 65,233-38.

to be companies engaged in the "transportation" of natural gas. However, the Commission has authority to assert NGA jurisdiction over an otherwise nonjurisdictional gathering affiliate in particular circumstances where such action is necessary to fulfill the Commission's obligations with respect to the transportation of natural gas in interstate commerce.⁸² By permitting spindown as an extension of its Order No. 636 unbundling policies, the Commission did not foreclose its future ability to exercise its authority to reassert NGA jurisdiction in particular circumstances or prevent aggrieved parties from filing a complaint when such circumstances arise.

B. Application of the Commission's Two-Part Test

46. As set forth in Arkla, and supported in dicta by the D.C. Circuit Court in Conoco,⁸³ the Commission uses a two-part test to determine whether the Commission may exert control over the gathering activities of affiliated gatherers in particular circumstances where such action is necessary to accomplish the Commission's policies for the transportation of natural gas in interstate commerce. The two-part test provides that the Commission may disregard the corporate form and treat the pipeline and gatherer as a single natural gas company if: (1) an affiliated gatherer acts in concert with its pipeline affiliate in connection with the transportation of gas in interstate commerce; and (2) in a manner that frustrates the Commission's effective regulation of the interstate pipeline.⁸⁴

47. Although we diverge slightly from the ALJ in how to apply the two-part test, we affirm the ALJ's findings that, under the present circumstances, Transco and WFS acted in concert in offering gathering services in a manner that frustrates the Commission's effective regulation of the jurisdictional pipeline, Transco. As the evidence in the record suggests, the effect of Transco's and WFS's concerted actions and abuse of market power

⁸²See, e.g., Independence Pipeline Co., 89 FERC ¶ 61,283 at 61,842 (1999), order issuing certificate, 91 FERC ¶ 61,102 (2000), order issuing certificates, 92 FERC ¶ 61,022 (2000), order denying reh'g, 92 FERC ¶ 61,268 (2000).

⁸³The Court stated that "[a]s an abstract matter, we have no reason to doubt the Commission's conclusion that a nonjurisdictional entity could act in a manner that would change its status by enabling an affiliated interstate pipeline to manipulate access and costs of gathering....". Conoco, 90 F.3d at 549.

⁸⁴Arkla, 67 FERC ¶ 61,237 at 61,871.

was a demand for gathering rates, terms and conditions so anti-competitive that Shell jeopardized its OCS reserves by shutting them in and risked the loss of its MMS leases.

1. Concerted Action

48. In applying the first part of the Commission's test, *i.e.*, whether WFS, a nonjurisdictional affiliate, acted in concert with the jurisdictional pipeline, Transco, in connection with the transportation of gas in interstate commerce, we find that the record reveals concerted action and adopt the ALJ's decision on that issue. For example, the record shows that Transco and WFS acted in concert by planning and implementing the spindown of Transco's offshore assets, with WFS continuing to operate the physically integrated NPI WFS gathering and Transco production area facilities in essentially the same manner after the spindown as before the spindown. WFS's operational responsibilities continued to include daily operation and maintenance of the meters, valves, compressors and other facilities. In addition, Transco and WFS acted in a concerted manner, pursuant to a corporate business plan, in not allowing for the sale of the NPI facilities on the open market, which would have allowed non-affiliated gathering service providers to buy the spin-down assets. Furthermore, Transco and WFS acted in concert by using WFS personnel to negotiate contracts for transmission service on the IT-feeder system as well as to negotiate gathering contracts on the WFS gathering system. Thus, WFS acted as if it were a division of Transco, rather than a separate company, which effectively maintained the bundled transportation and gathering services that existed prior to the spindown.

2. Frustration of the Commission's Regulation of Transco

49. The second prong of the Commission's two-part test is whether the concerted action frustrates the Commission's effective regulation of the interstate pipeline, Transco. Predicated on the Commission's finding above that WFS and Transco have in fact acted in concert, the Commission may pierce the "corporate veil" if the concerted action has frustrated the Commission's effective regulation of the jurisdictional pipeline, Transco. Because their actions have been found to have been conducted on a concerted basis, the actions of WFS can be attributed to Transco, and *vice versa*, as if the facilities were still part of the Transco system. Thus, our inquiry under the second part of the Commission's two-part test is to determine whether the rates and terms and conditions of service exacted directly by WFS, and indirectly by Transco, for the subject gathering services, are unjust and unreasonable or unduly discriminatory, as the result of Transco's and WFS's monopoly power, such that a reassertion of direct NGA regulation is warranted.

50. The record evidence shows that Transco and WFS possess monopoly market power with respect to the gathering and transportation of natural gas on the NPI system. This monopoly market power stems from the fact that producers have no reasonable alternative but to flow their gas through WFS's gathering pipeline and into Transco's NGA jurisdictional IT-feeder transmission pipeline in order to access downstream gas markets. Transco and WFS abused their monopoly market power by doubling Transco's previous combined rate for providing gathering and transmission service from 8 cents to 16 cents within the relevant market of gathering on the NPI spundown facilities and by demanding anti-competitive, unduly discriminatory terms and conditions of service. For example, as part of its offer to Shell, WFS demanded a non-negotiable dedication of reserves condition. In effect, this condition would lock in Shell as a captive customer and discourage possible future competitive alternatives for Shell's production. Furthermore, if WFS demands such a dedication of reserves condition from all of its NPI producers, it would protect its monopoly leverage to demand egregious rates in the future. If all NPI producers are prevented cumulatively from having their production gathered by a new entrant, then Shell and all NPI future production would never be able to avoid the Transco/WFS monopoly, absent regulation.⁸⁵ Such a condition frustrates the Commission's goal of fostering competition on the OCS in the Gulf of Mexico. In addition, through the "jurisdictional impact" clause in the proposed gathering agreement, WFS sought to condition access to the gathering service by requiring Shell to agree not to take action that would result in the Commission's reassertion of NGA jurisdiction. Such a condition would impede lowering the rate to a just and reasonable level.

51. By demanding a monopolistically egregious rate in conjunction with anti-competitive terms and conditions of service, Transco and WFS tried to obtain monopoly rents from the nonjurisdictional gathering that the Commission's regulation would prohibit.⁸⁶ As such, the single entity, Transco/WFS, frustrated the Commission's regulation over the rates and services provided on Transco.

52. WFS argues an unaffiliated gatherer could charge the same gathering rates and impose the same terms and conditions of service that it [WFS] did, without being subject to the reassertion of the Commission's NGA jurisdiction. However, in the case of an unaffiliated gatherer, there is no tie-back to the regulated pipeline, which could result in the frustration of the Commission's effective regulation of the pipeline. Further, we are

⁸⁵See Id. at 65,258.

⁸⁶See Id. at 65,252, citing SOI-1 at 11-12 (Means); SOI-10 at 12 (Means); SOI-4 at 9 (Harris).

affirming the ALJ's finding that non-affiliated gatherers' rates are not relevant here because of differences in the location, proximity of reserves, competitive positions, and so forth, of the gatherers.⁸⁷

53. WFS and Transco contend that any market power, and any abuse thereof, would result only in harm to Shell's netback revenue but not to consumers. However, we agree with the ALJ that even if the most direct victim of such behavior may be Shell and other producers on the NPI system, if such behavior happens repeatedly it may have a significant cumulative effect on downstream consumers markets by distorting producers' price signals.⁸⁸ The public would thereby suffer from the reduced competition in the interstate transportation and sale of natural gas. Further, these distortions of production and development decisions could also have a negative economic impact. Therefore, under these circumstances, reassertion of NGA jurisdiction is appropriate.

54. We also reject WFS's and Transco's arguments that reasserting jurisdiction constitutes a collateral attack on the orders approving spindown. While the Commission anticipated some increase in gathering prices after a spindown,⁸⁹ the Commission did not intend the spindown to result in an exercise and abuse of market power by Transco/WFS that raised gathering rates to egregious levels.

C. OCSLA Jurisdiction

55. Pursuant to Section 5(f) of the OCSLA, a pipeline must provide "open and nondiscriminatory access to both owners and nonowner shippers."⁹⁰ Accordingly, the March 6, 2002 Order set for hearing the issues of whether the rates, terms and conditions of service offered to Shell constitute a violation of the open and nondiscriminatory access provisions of the OCSLA, and any appropriate remedies.

⁸⁷See *Id.* at 65,250-51.

⁸⁸See *Id.* at 65,252.

⁸⁹Transcontinental Gas Pipe Line Corp., 97 FERC at 62,382.

⁹⁰43 U.S.C. § 1334(f).

56. In light of our findings that Transco and WFS, in concert, have abused their monopoly power to exact monopolistically egregious gathering rates and impose anticompetitive terms and conditions of service, the Commission finds that Transco has violated the open and nondiscriminatory access requirement of the OCSLA.⁹¹ Therefore, the Commission will also assert OCSLA jurisdiction over the rates and services provided by Transco/WFS.⁹² Accordingly, the remedy imposed here also serves to fulfill the Commission's responsibilities under Section 5 of the OCSLA.

D. Remedies

57. The Commission reasserts NGA jurisdiction and hereby re-regulates the rates and terms and conditions of the subject spundown gathering service on the NPI system, *i.e.*, over the 3.83-mile and the 18.79-mile pipelines that end in NPI Block 956, pursuant to NGA Sections 4 and 5. The Commission finds Transco/WFS's proposed 8-cent gathering rate to be unjust and unreasonable, and otherwise unlawful under the NGA. As a result, Transco must file revised tariff sheets to reflect the approved unbundled

⁹¹See *Shell Oil Company v. FERC*, 47 F.3d 1186 (D.C. Cir. 1995) (based on Commission's finding that the oil pipeline's refusal to transport a shipper's oil violated the open and nondiscriminatory access requirement under the OCSLA, the Commission had authority under the OCSLA to order an interconnection).

⁹²On appeal of the Commission's reporting requirements for OCS pipelines under the OCSLA, the D.C. District Court found that the Commission lacks the authority to promulgate reporting requirements under the OCSLA. However, the Court leaves intact the Commission's authority to pursue remedies under the OCSLA where the Commission has ruled, as is the case in the current proceeding, "in the context of an adjudicative proceeding, whether certain conduct violates the open access provision of the OCSLA." Regulations under the Outer Continental Shelf Lands Act Governing the Movement of Natural Gas on Facilities on the Outer Continental Shelf, Order No. 639, FERC Stats. & Regs., Regs. Preambles, 1996-2000, ¶ 31,097, order on reh'g and clarification, Order No. 639-A, FERC Stats. & Regs., Regs. Preambles, 1996-2000 ¶ 31,103, order denying requests for clarification, 93 FERC ¶ 61,274 (2000), vacated and enjoined, *Chevron U.S.A., Inc., et al. v. FERC*, 193 F. Supp. 2d 54, 72 (D.D.C. 2002), appeal docketed, *FERC v. The Williams Companies, et al.* No. 02-5056 (D.C. Cir. Feb. 5, 2002).

gathering rate of 1.69 cents for the subject gathering facilities, to be effective the date of this order.

58. Based on the record, we find a just and reasonable gathering rate to be 1.69 cents per Dth.⁹³ Commission policy favors separately stated gathering and transmission rates for interstate pipelines.⁹⁴ Since Transco does not currently have an unbundled gathering rate in its tariff, it must file revised tariff sheets to reflect the approved unbundled gathering rate of 1.69 cents per Dth for service on the subject gathering facilities, effective as of the date of this order. Transco must file a proposed rate schedule and form of service agreement for the subject gathering services. Finally, Transco must file all contracts that govern service on the subject NPI gathering facilities.

E. Requests for Oral Argument

59. With respect to the motions for oral argument requested by Transco and WFS, the Commission finds that the record is sufficient to support our findings. Accordingly, we deny the motions for oral argument.

F. Walter Complaint in Docket No. RP02-144-000

60. On April 11, 2002, counsel for Walter and WFS announced on the record that they had reached a settlement in principle regarding all of the issues raised in Walter's complaint in Docket No. RP02-144-000. On April 25, 2002, WFS requested that the Motions Commissioner (Chairman Pat Wood, III) permit an interlocutory appeal of the ALJ's ruling to produce, pursuant to a protective order, the settlement agreement entered into between WFS and Walter/Superior (Walter settlement) due to its apparent relevance and materiality to the Docket No. RP02-99-000 proceeding. The Motions Commissioner denied this request on May 2, 2002. On May 10, 2002, Walter and WFS filed a joint motion seeking to dismiss with prejudice Walter's complaint and withdraw certain pleadings and testimony in Docket No. RP02-144-000 regarding the NPI facilities. On May 28, 2002, Producer Coalition filed an answer opposing the dismissal of the Walter

⁹³See Appendix for derivation of this rate.

⁹⁴See 18 C.F.R. § 284.10(c)(1) (2002). The Commission has previously expressed its concern that including gathering costs in transportation rates would unfairly disadvantage those customers who desire to purchase gas off-system and may inhibit the development of market centers contrary to the intent of Order No. 636. See El Paso Natural Gas Co., 60 FERC ¶ 61,109 at 61,353-54 (1992).

complaint unless the Walter settlement is made public. IPAA joined in the Producer Coalition's answer. WFS and Walter filed separate answers to Producer Coalition's answer, opposing the condition of public disclosure.

61. On June 12, 2002, the ALJ issued an order granting the joint motion to dismiss the Walter complaint without the condition of public disclosure. The ALJ stated that the OCSLA or the Commission's presently effective regulations do not require public disclosure and that the settlement deserves protection consistent with the Commission's policy to promote settlements of litigation. On July 2, 2002, Producer Coalition filed exceptions to the ALJ's June 12, 2002 order, stating that the ALJ erred in not requiring public disclosure of the Walter settlement, in violation of the Commission's policy promoting transactional transparency under the OCSLA. On July 17, 2002, WFS filed a brief opposing the Producer Coalition's exceptions, requesting that the Commission affirm the ALJ's decision to dismiss the complaint, in Docket No. RP02-144-000, without any condition to publicly disclose the Walter settlement.

62. The Commission affirms the ALJ's decision to dismiss Walter's complaint in Docket No. RP02-144-000 with prejudice. In light of the fact that the ALJ did not rely on the Walter settlement in making his findings in the Initial Decision, and disclosure of settlements is not required under the Commission's regulations, the Commission also affirms the ALJ's ruling not to condition the dismissal by requiring disclosure of the Walter settlement in the public record.

The Commission orders:

- (A) The Initial Decision is affirmed, as discussed in the body of this order.
- (B) Within 7 days of the date of this order, Transco must file revised tariff sheets to reflect the approved unbundled gathering rate of 1.69 cents per Dth for the subject gathering facilities, to be effective as of the date of this order.
- (C) Within 30 days of the date of this order, Transco must file a proposed rate schedule and a form of service agreement for the subject gathering services, and all contracts that govern service on the subject NPI gathering facilities.
- (D) The Commission affirms the ALJ's ruling to dismiss the complaint by Walter against WFS, in Docket No. RP02-144-000, without disclosing the settlement in the public record.

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(E) WFS's motion to dismiss Shell's complaint, in Docket No. RP02-99-000, is denied.

By the Commission.

(S E A L)

Linwood A. Watson, Jr.,
Deputy Secretary.

Appendix

Transcontinental Gas Pipeline Corporation
Docket Nos. RP02-99-000 and RP02-144-000

Calculation of Cost of Service and Rates for North Padre Island Spindown Facilities

Line No.	Column (1) <u>Description</u>	(2) <u>Amount</u>
1	O&M Expenses 1/	\$137,458
2	A&G Expenses 2/	101,292
3	Depr., Depl., and Amortization 3/	210,760
4	Return 3/	111,318
5	Income Taxes 3/	55,558
6	Revenue Credits 3/	<u>0</u>
7	Total Cost of Service	\$616,386
8	Volumes - 100,000 Mcf/day * 365 4/	36,500,000
9	Rate per MCF (Line 7 / Line 8)	\$0.0169

1/ O&M expenses from Transco's compliance filing in Docket No. RP00-245-007, Appendix B, Schedule 1 at 2 (\$458,214 was reduced by \$320,756, i.e., the removal of improperly assigned costs allocated to the subject NPI facilities - Tr. at 913-914).

2/ As-filed Cost of Service Items from Docket No. RP01-245-007- Appendix B, Schedule 1 at 2 - A&G Expense Allocation.

3/ As filed Cost of Service Items from Docket No. RP01-245-007- Appendix B.

4/ Volumes derived using April 17, 2002 testimony in Docket No. RP02-99-000, et al., Tr. at 1479 (Sullivan) and Tr. at 772 (Johnston).