UNITED STATES OF AMERICA 114 FERC ¶61,269
FEDERAL ENERGY REGULATORY COMMISSION

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

Southern Star Central Gas Pipeline, Inc. Docket Nos. RP05-668-002
RP05-668-001

ORDER ON REHEARING AND COMPLIANCE FILING

(Issued March 16, 2006)

1. On October 31, 2005, the Commission issued an order[1] in this proceeding. That order conditionally accepted Southern Star Central Gas Pipeline, Inc.'s (Southern Star) filing to revise the list of permissible discounts included in its General Terms and Conditions (GT&C), among other things. BP America Production Company and BP Energy Company (collectively BP) filed a timely request for rehearing of the October 31, 2005 Order. As discussed below, BP's request for rehearing is denied.

2. In addition, on November 14, 2005, Southern Star made a filing to comply with the October 31, 2005 Order. As discussed below, the Commission accepts the compliance filing effective November 1, 2005.

Background

3. On September 14, 2005, Southern Star filed to revise the list of permissible discounts included in its GT&C. Southern Star proposed in section 30.1(vii) to permit discounts based on a formula including, but not limited to, published index prices for specific receipt or delivery points or other agreed-upon pricing reference points for price determination. In addition, proposed section 30.1(viii) would permit Southern Star to include in discounted rate agreements a provision for increasing (or decreasing) a discounted rate for service under one rate schedule to make up for a decrease (or increase) in the maximum rate for a separate service provided under another rate schedule to the same customer.

[1] *Southern Star Central Gas Pipeline, Inc.*, 113 FERC ¶ 61,110 (2005).

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4. On October 31, 2005, the Commission issued a letter order conditionally accepting Southern Star's tariff filing, effective November 1, 2005. The October 31, 2005 Order directed Southern Star to file tariff revisions to ensure that all discounts based on formulas use the same rate design as the pipeline's tariff rates. The order stated, "Southern Star must provide that any service agreement containing such a discount identify what rate component (*i.e.* reservation charge or usage charge or both) is discounted. Also, Southern Star must provide that, to the extent it discounts the firm reservation charge, the basis differential rate formula will produce a rate per unit of contract demand."[2] Southern Star filed to comply with this provision on November 14, 2005.

Notice and Protests

5. Notice of Southern Star's compliance filing was issued on November 17, 2005, providing for the filing of protests by November 29, 2005, in accordance with Rule 211 of the Commission's Rules of Practice and Procedure. 18 C.F.R. § 385.211 (2005). No protests or adverse comments were filed.

Discussion

6. BP requests rehearing of the Commission's acceptance of proposed section 30.1(viii) of Southern Star's GT&C, permitting Southern Star to enter into discount agreements providing for increasing (or decreasing) the discounted rate for service under one rate schedule to make up for a decrease (or increase) in the maximum rate for a separate service provided to the same shipper under another rate schedule. BP refers to this as a "shifting discount" and argues that such a discount constitutes a negotiated rate and should be rejected.

7. BP asserts that Southern Star's shifting discount proposal raises serious concerns. BP objects that the shifting discount would allow Southern Star to effectively nullify Commission decisions that require the pipeline to reduce its maximum rate for a service. BP explains, for example, that if a shipper is paying the maximum tariff reservation rate for production area transportation under Rate Schedule FTSP and a discounted rate for market area transportation under Rates Schedule FTSM and the Commission requires a reduction of the FTSP reservation rate by three cents, a "shifting discount" agreement would require the shipper to pay three cents more for its discounted service under Rate

[2] *Southern Star Central Gas Pipeline, Inc.*, 113 FERC ¶ 61,110 at P 7 (2005).

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Schedule FTSM. BP states that this would be contrary to the Commission's statutory duty under the NGA to protect against excessive rates and charges.[3]

8. BP claims that the risk a shifting discount could nullify a Commission ordered rate decrease is a special concern on Southern Star because Southern Star has a straight-fixed-variable rate design allowing the pipeline to recover all its fixed costs regardless of throughput. BP states that Southern Star recovers 94 percent of its operating revenue from reservation charges so a firm shipper has no real opportunity to reduce its transportation costs during the term of the contract.

9. BP also contends that a shifting discount should be treated as a negotiated rate because a shifting discount involves a complicated rate structure. BP states that the Commission found that a discount proposed by Natural Gas Pipeline Company of America (Natural), "is not a simple discount situation but is the sort of complicated transaction that may be entered into only pursuant to a negotiated rates provision in the pipeline's tariff."[4] BP submits that the same reasoning applies here because a shifting discount would allow Southern Star to adjust rates by essentially shifting costs among a shipper's different contracts involving different services, perhaps with a different rate structure, and possibly different facilities. BP argues that treating a shifting discount as a negotiated rate would ensure that the Commission could review whether the shifting discount properly transfers costs between different services, because Southern Star would have to file the contract or a tariff sheet describing the contract for Commission approval before the contract takes effect.[5] BP states that in contrast a pipeline is not required to seek Commission approval of a discount contract but need only post the discount after gas flow has commenced.[6]

10. BP submits that the complicated nature of a shifting discount could create a risk of undue discrimination and treating a shifting discount as a negotiated rate would reduce

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[3] *Citing Atlantic Refining Co. v. Public Service Commission of the State of New York*, 360 U.S. 378, 388 (1959).

[4] *Citing Natural*, 86 FERC ¶ 61,144 at 61,506-07 (1999).

[5] *Citing* Southern Star's GT&C § 31.5 Original Sheet No. 304.

[6] *Citing ANR Pipeline Co.*, 102 FERC ¶ 61,235 at P 12 (2003).

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the risk of discriminatory practices or the impermissible tying of services[7] because of the opportunity for Commission and shipper review. BP contends that a pipeline could try to use a shifting discount agreement to tailor a discount to the unique portfolio of pipeline services that a specific shipper utilizes to provide a special discount to that shipper alone. In addition, BP claims a shifting discount could give a pipeline leverage to compel a prospective shipper to subscribe to multiple services on the pipeline in order for the shipper to get a discount or the shipper might subscribe to multiple services to qualify as a similarly situated shipper to obtain a discount. Finally, BP argues that treating a shifting discount as a negotiated rate would ensure that Southern Star could not shift to other shippers the revenue forfeited due to the fact that a shifting discount is lower than the recourse rate.[8]

11. The Commission denies BP's rehearing request. A discounted rate agreement permitting the discounted rate for one service to be increased to affect a reduction in the maximum rate for another service would not nullify NGA protections against unjust and unreasonable rates. Under Southern Star's proposal, the resulting rates for each service would remain between the maximum and minimum rate in Southern Star's tariff applicable for the service provided. Since the Commission has found that the maximum and minimum rates in the pipeline's tariff are just and reasonable, the resulting rates under a shifting discount agreement are by definition just and reasonable. We also disagree that a shifting discount would nullify Commission decisions that require a pipeline to reduce its maximum rate for a service. In BP's example the pipeline lowers the maximum rate for the specified service as the Commission requires. This is not changed by the fact that the pipeline may be able to raise the discounted rate, up to the maximum tariff rate, for a separate service based on a discount agreement mutually agreed to by the pipeline and its customer. As long as the increase in the rate charged the customer for the separate service does not increase the rate above the maximum rate for that service, the customer is being charged a just and reasonable rate to which it has consented.

12. The Commission also rejects BP's argument that a shifting discount must be treated as a negotiated rate because it involves a complicated rate structure. In support of its argument, BP cites a 1999 Order in *Natural Gas Pipeline Company of America* (*Natural*), where the Commission stated that Natural's request for flexible rate

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[7] *Citing Natural*, 94 FERC ¶ 61,310 at 62,142 (2001); *Arkla Gathering Services Co.*, 67 FERC 61,257 at 61,871 (1994); and *Williams Natural Gas Co.*, 74 FERC ¶ 61,103 at 61,334 (1996).

[8] *Citing, Texas Eastern Transmission, LP*, 101 FERC ¶ 61,120 at P 29 (2002).

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components should be filed as a request for negotiated rates due to the complicated nature of the transaction in support of its argument.[9] However, after the cited *Natural* order, the Commission modified the policy against the use of formulas in discounted rates reflected in the *Natural* order. In 2003, the United States Court of Appeals for the District of Columbia, in *Northern Natural Gas Co. v. FERC (Northern)*, vacated the Commission's rejection of Northern's proposal to offer discounts based on published index prices for specific receipt or delivery points or other agreed-upon pricing reference points.[10] The Court found unpersuasive the argument that a complicated rate structure may only be used in a negotiated rate and not in a discounted rate. The Court also specifically stated that the Commission reached its conclusion in the *Natural* case without a reasoned explanation.[11] The Court accordingly found that the Commission failed to provide a reasoned explanation why the formula discount rate Northern proposed could only be offered as a negotiated rate. Additionally, the Court stated that the Commission had never clarified the distinction between discounted and negotiated rates. In the Commission's order on remand (Remand Order), the Commission modified its policy to permit pipelines to offer discounts based on formulas and clarified the distinction between discounted and negotiated rates.[12] In the order, the Commission stated that discounted rates "must stay within the maximum and minimum rates in the pipeline's tariff and be based on the same rate design as the tariff rates. Negotiated rates are not so limited."[13] Southern Star's so-called "shifting discount" proposal is consistent with this policy since the discounted rate must always remain within the maximum and minimum rate for the service in question and will use the same rate design.

13. BP argues that circumstances involved in the *Northern* remand order and another Northern order[14] the Commission cited in accepting Southern Star's proposed shifting

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[9] *Citing Natural*, 86 FERC ¶ 61,144 at 61,506-07 (1999).

[10] 335 F.3d 1089 (D.C. Cir. 2003). The Commission had rejected the discount rate because it was a formula rate and did not provide for a rate that was fixed. *See Northern Natural Gas Co.*, 90 FERC ¶ 61,064 (2000), *reh'g denied*, 98 FERC ¶ 61,106 (2002).

[11] *Northern Natural Gas Co. v. FERC*, 335 F.3d 1089, 1094 (D.C. Cir. 2003).

[12] *Northern Natural Gas Co.*, 105 FERC ¶ 61,299 (2003).

[13] *Northern Natural Gas Co.*, 105 FERC ¶ 61,299 at P 12 (2003).

[14] *Northern Natural Gas Co.*, 105 FERC ¶ 61,229 (2003) and *Northern Natural Gas Co.*, 111 FERC ¶ 61,223 (2005).

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discount are distinguishable from the circumstances in this case. BP contends that the Northern cases involved a discount based on gas index prices and the pertinent tariff language required that the discounted rate remain between the maximum and minimum tariff rate. BP is correct that the Northern orders the Commission cited in the October 31, 2005 Order involved discounts based on gas index prices. However, BP fails to mention that the second Northern order cited by the Commission[15] also accepted the same type of shifting discount as Southern proposes here. Southern Star's proposed shifting discount is not distinguishable from the Northern shifting discount accepted by the Commission. Moreover, the Commission required Southern Star to revise its tariff to clarify that the discounted rate will use the same rate design as the pipeline's tariff rates, consistent with the *Northern* remand order.

14. BP observes that in contrast to a negotiated rate, where a pipeline would have to file with the Commission the contract or a tariff sheet describing the contract allowing the Commission to review whether the shifting discount properly transfers costs between different services before the contract takes effect, a pipeline need only post a discount after gas flow has commenced. The Commission's regulations require Southern Star to post the details of all discounted rate agreements, so that similarly situated shippers will be able to evaluate the discounts and avail themselves of the discounted rates if they so choose.[16] This considerably reduces concerns regarding improper shifting of costs between services and undue discrimination. Further, section 30.1 of Southern Star's GT&C expressly provides that Southern Star must discount on a not unduly discriminatory basis. If a shipper is not similarly situated, Southern Star may not charge the shipper more than the just and reasonable recourse rate set forth in Southern Star's tariff.

15. Finally, BP's argument regarding the shifting of costs between customers is misplaced. The Commission has repeatedly held that the purpose of its discounted rate program is to allow pipelines to compete for customers who have alternatives. The Commission has found that this allows the pipeline to generate greater throughput over which to spread its fixed costs, thus benefiting all customers.[17] Formula-based discounts

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[15] *Northern Natural Gas Co.*, 111 FERC ¶ 61,223 (2005).

[16] 18 C.F.R. § 284.13 (2005).

[17] *Policy Statement Providing Guidance with Respect to the Designing of Rates*, 47 FERC ¶ 61,295 at 62,046 n. 44 (1989), *citing* Order No. 436 at 31,546 n.1. Order No. 436-A, FERC Stats. & Regs., Regulations Preambles 1982-1985 ¶ 30,675 at 31,679 (1985). *Southern Natural Gas Co.*, 67 FERC ¶ 61,155 at 61,456-58 (1994). *Williston Basin Interstate Pipeline Co.*, 85 FERC ¶ 61,247 at 62,028-29 (1998).

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provide the pipeline an additional tool to meet competition, consistent with the underlying purpose of the Commission's discount policy. We find that Southern Star's proposed shifting discount is consistent with the Commission's discount policy since it allows shippers additional flexibility and provides Southern Star with an additional tool to meet competition.

16. On November 14, 2005, Southern Star filed Substitute First Revised Sheet No. 300 to its FERC Gas Tariff, Original Volume No. 1, to comply with the Commission's directive in the October 31, 2005 Order that Southern Star file tariff revisions to ensure that all discount agreements use the same rate design as the pipeline's tariff rates. Specifically, Southern Star proposes to revise section 30.1 of its GT&C to add tariff language that ensures all discount agreements use the same rate design as the pipeline's tariff rates. Southern Star also clarifies that any service agreement containing a basis differential discount will identify what rate component is discounted. Also, to the extent the firm reservation charge is discounted, the index price differential rate formula will produce a rate per unit of contract demand. Southern Star's November 14, 2005 filing fully complies with the Commission's directive in the October 31, 2005 Order.

The Commission orders:

(A) BP's request for rehearing is denied, as discussed in the body of this order.

(B) Southern Star's November 14, 2005 filing is accepted, effective November 1, 2005, as in compliance with the October 31, 2005 Order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.