106 FERC ¶ 61,092
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Iroquois Gas Transmission System, L.P. Docket No. RP04-136-000

ORDER ACCEPTING AND SUSPENDING TARIFF SHEET
SUBJECT TO REFUND AND CONDITIONS AND
ESTABLISHING HEARING PROCEDURES

(Issued January 30, 2004)

1. On January 2, 2004, Iroquois Gas Transmission System, L.P. (Iroquois) filed a tariff sheet[1] to be effective February 2, 2004, to increase the rates on its Eastchester Extension Project (Eastchester) to reflect an increase in the annual revenue requirement for the project of approximately $18 million. As discussed below, this order accepts and suspends the tariff sheet listed in Footnote 1, to be effective July 1, 2004, subject to refund and the outcome of hearing procedure and conditions established herein. This order benefits the public interest by ensuring that Iroquois' recourse rates will be just and reasonable.

**Background**

2. Iroquois' pipeline system extends from the New York-Canadian border near Iroquois, Ontario through New York and Connecticut, terminating near South Commack, New York on Long Island. The Commission recently authorized the Eastchester project which extended Iroquois' system from Northport on Long Island, New York to an interconnect with Consolidated Edison Company of New York, Inc. (ConEd) in the

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[1] Original Sheet No. 4C to Iroquois' FERC Gas Tariff, First Revised Volume No. 1.

Bronx, New York, with a projected capacity of 230,000 Dth per day.[2] The route for the Eastchester project required Iroquois to construct a pipeline from an onshore point at Northport across Long Island Sound and the East River to the onshore terminus at Hunts Point in the Bronx. To complete the Eastchester project, Iroquois constructed over 36 miles of 24-inch pipeline and more than doubled the compression on its system, adding over 54,000 horsepower at various points on Iroquois' existing system, with an estimated construction cost in 2001 of $210 million.

3. The Commission previously denied Iroquois' request for a presumption of rolled-in rate treatment for the Eastchester project. The Commission found that Iroquois had not met the threshold requirement of the Certificate Policy Statement[3] and that Iroquois must be prepared to financially support the project without relying on subsidization from its existing customers not directly involved with the Eastchester facilities.[4] Further, the Commission found that since Iroquois was more than doubling the compression on its system, any shipper moving gas on the Eastchester expansion should be responsible for the fuel cost to operate the compressor stations, thereby providing for the proper matching of costs to the shippers that benefit from the Eastchester expansion.[5] The Commission authorized Iroquois to charge its existing RTS Part 284 rate as an initial rate (currently $0.4234 per Dth)[6] for service on Eastchester. The Commission also ruled that, until Iroquois files to revise its rates, it will be responsible for any underrecovery of costs if the costs to operate the Eastchester project exceed the revenues recovered though the initial Part 284 rate.[7] Further, the Commission addressed the issue of potential cost overruns for the Eastchester project, finding that the issue of risk sharing in the event of

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[2] See Iroquois Gas Transmission System, L.P., 95 FERC ¶ 61,355 (2001); order on reh'g and issuing certificates, 97 FERC ¶ 61,379 (2001); order on reh'g, 98 FERC ¶ 61,273 (2002); order denying reh'g, 101 FERC ¶ 61,093 (2002).

[3] Certification of New Interstate Natural Gas Pipeline Facilities (Certificate Policy Statement), 88 FERC ¶ 61,227 at 61,774 (1999); order clarifying statement of policy, 90 FERC ¶ 61,128 (2000); order further clarifying statement of policy, 92 FERC ¶ 61,094 (2000).

[4] 95 FERC ¶ 61,335 at 62,201 (2001); order on reh'g, 97 FERC ¶ 61,379 at P 33 - 34 (2001).

[5] 97 FERC ¶ 61,379 at P 23 (2001).

[6] See Twenty-Ninth Revised Sheet No. 4 to Iroquois' FERC Gas Tariff, First Revised Volume No. 1.

[7] 97 FERC ¶ 61,379 at P 19 (2001).

cost overruns is an issue that needs to be decided between the pipeline and the shippers.[8] The Commission recently approved a rate settlement which established Iroquois' system rates except for the Eastchester project, permitting Iroquois to submit a limited Section 4 filing to establish rates for service on the Eastchester project.[9] The instant filing is Iroquois' proposal to change the Commission's approved initial rates to recover additional construction and operating costs of the Eastchester project, which Iroquois states has a projected in-service date of February 1, 2004.[10]

**The Filing**

4. Iroquois proposes to increase rates for the Eastchester project to recover increased construction and operating costs not reflected in its certificated initial rate, which is now $0.4234 per Dth, the generally applicable Part 284 daily RTS reservation rate under the recent settlement. Iroquois is proposing an incremental maximum Eastchester daily RTS reservation charge rate of $0.8444 per Dth and a $0.00 usage charge, which is based on a total cost of service of $70.9 million and an annual throughput of 83,950,000 Dth. Iroquois proposes an interruptible rate of $0.8444 per Dth, which is also designed on a 100% load factor basis. The proposed rates and cost of service utilize a 12-month base period ending September 30, 2003, adjusted for known and measurable changes expected to occur during the nine-month test period ending June 30, 2004. While Iroquois acknowledges that it knows of no required waivers, it requests that the Commission grant any waivers of its regulations, policy or precedent that the Commission may deem necessary to make the proposed tariff change effective as proposed.

5. Iroquois is also proposing Secondary Access Rates, providing service for firm shippers on Iroquois' system who are not currently Eastchester shippers, but who want to use service delivery points on the Eastchester project on a secondary basis. For each unit of secondary access service on Eastchester, existing Iroquois shippers will pay an additional amount which, when added to the unit charge for their primary Zone 1 or Zone 2 service on Iroquois, will bring their total charge up to the level of the posted incremental recourse rate for the Eastchester service. The proposed Secondary Access Rates reflect proposed changes effective at various dates in the future.

6. Iroquois states that the proposed cost of service of $70.9 million is based on construction costs of $334 million to complete the Eastchester project. This represents a cost overrun of $124 million, as compared to the costs estimated in the certificate

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[8] Id. at P 37.

[9] Iroquois Gas Transmission System, L.P., 105 FERC ¶ 61,121 (2003).

[10] See page 4 of the Transmittal Letter to the application.

application of $210 million. The $70.9 million cost of service is composed of: $3.1 million for allocated administrative and general (A&G) costs; $1.2 million in direct operation and maintenance (O&M) costs; $9.3 million in depreciation expense reflecting Iroquois' existing approved depreciation rate of 2.77%; $8.9 million for taxes other than income; $34.2 million for return on equity which is based on an overall rate of return of 10.52%, a return on equity of 14.9%, cost of long term debit of 7.369%, and a capital structure of 58% debt and 42% equity; $11.1 million in federal income tax; and $3.1 million in state income taxes.

7. Iroquois states that it has entered into long-term recourse rate contracts for service on the Eastchester project, as well as, long-term negotiated rate with a fixed rate contracts, short-term contracts, and has unsubscribed capacity. Iroquois designed its rates based on design capacity. Iroquois' projected annual test period billing determinates are 83,950,000 Dth, of which 74 percent, 62,050,000 Dth is transported under firm, long-term service agreements. The long term recourse rate contracts provide for a total throughput of 40,150,000 Dth with a demand charge of $0.8444 per Dth. The long term negotiated rate contracts with a fixed charge provide for 21,900,000 Dth of throughput with two different fixed rates. For 18,250,000 Dth, the demand charge rate is $0.4650 per Dth and the remaining 3,650,000 Dth transported has a demand charge of $0.2580 per Dth. Of the remaining 21,900,000 Dth capacity on the Eastchester system, which represents 26% of the throughput, 10,950,000 Dth is subscribed under a variable rate contract scheduled to expire in November 2004 and the other 10,950,000 Dth of capacity is unsubscribed. Iroquois projects a rate of $0.25 per Dth for both the variable rate contract capacity of 10,950,000 Dth and the unsubscribed capacity of 10,950,000 Dth, as compared to the proposed recourse rate of $0.8444 per Dth. The projected revenue is expected to be $48,907,720 as compared to the proposed cost of service of $70.9 million.

8. Iroquois contends that even at the higher proposed Eastchester rates, it is projecting an annual revenue deficiency of $22 million. Iroquois argues that the deficiency results from designing the Eastchester rates using the full project capacity of 230,000 Dth per day, without any adjustments for currently unsubscribed capacity or contracts at less than maximum rate, thereby allocating to Iroquois the full risk of marketing all project capacity at maximum rates. Iroquois contends that the various post-Enron and post-September 11, 2001 changes to energy markets and the economy have affected the Eastchester project, such that the near-term market value of Eastchester capacity is substantially below the proposed maximum rates. Iroquois indicates that it will absorb the substantial revenue deficiency associated with the Eastchester project at the proposed rates.

**Notice of Filing, Interventions, and Protests**

9. Interventions and protests were due as provided in Section 154.210 of the Commission's regulations. Pursuant to Rule 214 (18 C.F.R. ' 385.214), any timely filed

motion to intervene is granted unless an answer in opposition is filed within 15 days of the date such motion is filed. Timely filed motions are also granted in accordance with the conditions of Rule 214. Any motions to intervene out-of-time filed as of the date of this order are granted pursuant to 18 C.F.R. ' 214(d), since the Commission finds that granting intervention at this stage of the proceeding will not disrupt this proceeding or place additional burdens on existing parties.

10. Virginia Power Energy Marketing, Inc. (VPEM) filed comments, KeySpan-Ravenswood, LLC (Ravenswood) requested the full five-month statutory suspension and establishment of hearing proceedings, Public Service Commission of the State of New York (PSCNY) filed a protest and request for maximum suspension period, and Consolidated Edison Company of New York, Inc. (ConEd) (collectively, Protesters) filed a motion to reject, protest, and reply to the waiver request. Iroquois filed an answer opposing the motion to reject the filing.[11] The protests, comments and answer are addressed below.

11. VPEM states that Iroquois is incorrect in asserting that its filing comports with all applicable Commission orders regarding the Eastchester project because (as an example) there is little or no support offered for Iroquois' proposed allocations of O&M and A&G expenses to the project. VPEM also argues that the volume projections used by Iroquois to establish rates for the Eastchester project are not founded on known base period experience. VPEM further asserts that the level of plant expense cannot be known at this time and that given the role of gross plant in the development of the cost of service for the Eastchester project, it is critical that the gross plant figure not be speculative or poorly estimated.

12. PSCNY argues that Iroquois' proposed rate increase is due to the $124 million cost overrun for constructing the Eastchester facilities and Iroquois' request for a 14.9% return on equity. PSCNY argues that a portion of Iroquois' construction cost for the Eastchester facilities reflects costs incurred in constructing facilities that Iroquois may have been compelled to destroy or to duplicate in order to relocate the pipeline in response to applicable regulations. PSCNY states that Iroquois' request for a 14.9% return on equity is not consistent with the Commission's policy announced in Opinion 414-A as applied in recent cases. PSCNY adds that Iroquois' DCF analysis is further flawed because the pipeline has further adjusted its proposed return on equity upward to reflect an adjustment for flotation cost. PSCNY contends that such adjustment is contrary to Commission policy. PSCNY states that in Williston,[12] the Commission

[11] While the Commission's Rules of Practice and Procedure generally prohibit answers to protests or answers, the Commission will accept the answer to allow a better understanding of the issues. See 18 C.F.R. § 385.213(a)(2) (2003).

[12] Williston Basin Interstate Pipeline Co., 104 FERC ¶ 61,036 (2003) (Williston).

expressly rejected an adjustment for flotation cost proposed by the pipeline. As stated by the Commission, "a flotation cost adjustment is only proper if supported by actual test period evidence that such cost can be expected to occur."[13] PSCNY argues that Iroquois has presented no evidence in this case that it can be expected to occur any actual flotation cost and therefore, the adjustment for flotation cost should be summarily rejected in the suspension order. PSCNY requests that the maximum suspension period for the proposed rates begin on the actual in-service date of the Eastchester facilities.

13. ConEd filed a motion to summarily reject Iroquois' proposed rate increase. ConEd argues that Iroquois' instant filing should be rejected because Iroquois has not fully complied with Section 154.301(c) of the Commission's regulations governing rate increases because it contains no estimate of throughput for either the Eastchester secondary access service or the Eastchester interruptible service. ConEd states that Iroquois' rates cannot be computed without billing determinants for all services, including interruptible and secondary access services, and that such rates should not include reservation rates premised on variable costs.

14. In the event that the Commission does not grant ConEd's motion to reject, ConEd proposes that the Commission should address the following issues in hearing procedures: (1) the rate of return of 14.9%; (2) adjustments to the costs for the gas plant in service; (3) allocation of system A&G costs; (4) claimed O&M expenses; and (5) the issues surrounding the construction of Athens compressor station in Docket No. CP02-20.[14]

15. Iroquois filed an answer requesting that ConEd's motion to reject be denied. Iroquois argues that it has shown estimates of revenues from short-term Eastchester services in Schedule G of its filing, and that it has adjusted the assumed revenues from those services to lower the rates that otherwise would have resulted. Additionally, Iroquois argues that it need not classify variable commodity costs into a usage rate for this service because all of the costs for this service are properly classified as fixed costs and are placed in the demand component of the rate pursuant to SFV methodology. Iroquois argues that at most ConEd may argue whether the classification of these costs is correct, but contends that that is a factual matter to be determined at hearing.

16. Iroquois also argues that it has presented substantial evidence supporting its flotation cost adjustment and that Commission policy does not mandate that this adjustment must be summarily rejected. Iroquois argues that at most this issue should be permitted to be explored at hearing along with all other factual issues and adds that the

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[13] Id. at 61,105.

[14] Iroquois Gas Transmission System, L.P., 99 FERC ¶ 61,261 (2002).

Commission is without authority to adopt PSCNY's proposal to tie the suspension period to the in-service date of the facilities.

**Discussion**

17. The protesters have raised a number of issues which can be appropriately explored in a hearing established by this order. During the hearing, the parties can explore the issues raised in their protests and general rate case issues, including but not limited to, rate derivation, cost of service issues, rate of return, allocation of O&M expenses, rate design, and throughput for firm, interruptible, and secondary access service. Further, the parties should be prepared to address the concerns discussed below.

18. Iroquois has incurred significant cost overruns to construct the Eastchester project, with the construction costs increasing from an estimated $210 million to the filed estimate of $334 million. This represents a cost overrun of $124 million. Parties can explore all aspects of the construction costs, including the cost overruns and construction delays. The Administrative Law Judge should determine whether the construction costs were prudently incurred by Iroquois and whether the costs should be recovered from the Eastchester ratepayers or absorbed by Iroquois. Further, in accordance with the Certificate Policy Statement, Iroquois is responsible for the costs of the new capacity created by the Eastchester project that are not fully utilized.[15] Since Iroquois has encountered a number of problems and delays in placing its Eastchester project into service, Iroquois is required within five days of commencing service, to notify the Commission and the parties to this proceeding of the commencement date of service on the Eastchester project.

19. Iroquois, in Statement G of the filing, identified revenues, credits, and billing determinants for the Eastchester project for the 12 month period ending June 30, 2004. In Schedule G-2, Iroquois reported revenues for the base period starting in November 2002 through November 2003 for two of its shippers, Sempra Energy Trading, Corp. (Sempra) with $3,743,110 in revenue and ConEd/Virginia Power with $2,832,606 in revenue.[16] Further, Iroquois indicates that the contracts with Sempra started on

[15] Certification of New Interstate Natural Gas Pipeline Facilities, 88 FERC ¶ 61,227 at 61,747 (1999); order clarifying statement of policy, 90 FERC ¶ 61,128 (2000); order further clarifying statement of policy, 92 FERC ¶ 61,094 (2000).

[16] See Iroquois' filing at Schedule G-2, page 1 of 7 and page 3 of 7.

November 1, 2003, and for ConEd/Virginia Power on November 1, 2002.[17] While Iroquois can enter into contracts prior to the projected February 1, 2004 commencement date for service, Iroquois is reporting revenue of $6,575,716 prior to placing the Eastchester facilities into service. The Administrative Law Judge should examine whether Iroquois improperly billed and collected revenues prior to the commencement of service under its tariff.

20. Iroquois in Exhibit E proposed a cash working capital allowance of $121,156 for the period ending June 30, 2004. Section 154.306 of the Commission's regulations provides that any natural gas company that files a tariff change may not receive a cash working capital adjustment to its rate base except when such adjustments are accompanied by a fully developed and reliable lead-lag study. In order for Iroquois to recover the $121,156 in cash working capital, it must perform a lead-lag study supporting its request consistent with the regulations at Section 154.306.

**Motion to Reject and Secondary Access Service**

21. The Commission denies ConEd's motion to summarily reject Iroquois' proposed rate increase. In the Commission's view, the instant filing has raised issues which can be properly addressed at hearing where they may be fully ventilated. For example, Iroquois has reflected cost overruns of approximately $124 million incurred in constructing its Eastchester pipeline. A hearing will permit parties to explore all aspects of the construction costs, including the cost overruns and construction delays and to determine whether such costs were prudently incurred by Iroquois.

22. However, the Commission also finds that Iroquois has not sufficiently supported several aspects of its filing and the Commission directs Iroquois to supplement its filing. Specifically, Iroquois has proposed secondary access rates without the required supporting cost data, billing determinates, revenue figures, testimony, or impact on the capacity release market. Neither has Iroquois attempted to meet these requirements by providing information as provided for in Section 154.202 of the regulations (18 C.F.R. § 154.202 (2002)). In addition, Iroquois has not proposed service priorities for its proposed transportation services. Correctly prioritized and properly priced secondary access could be beneficial to customers on the Iroquois system and, therefore, the Commission will not summarily reject the proposal but will require Iroquois to provide the requisite support required by the Commission regulations to support its secondary

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[17] See page 3, Exhibit ___(SER-1) of Prepared Direct Testimony of Witness Rupff, which identified the ConEd/Virginia Power contract as No. R-560-04 starting on November 1, 2002 and ending on February 1, 2012 and the Sempra contract as No. R-1710-06 starting on November 1, 2003 and ending on November 1, 2004.

access rates. The Commission also directs Iroquois to file revised tariff sheet(s) proposing service priorities for its proposed transportation services.

**Suspension**

23. Although the Commission authorized Iroquois to charge its Part 284 system rate as the initial incremental rate for service on Eastchester, Iroquois' tariff does not reflect this initial rate charge. Therefore, in order to commence service on the Eastchester system, Iroquois is required within 5 days of the date of this order to file a revised tariff sheet which reflects the initial rate for service as the Part 284 rate which is currently $0.4234 per Dth (100% load factor). This initial rate will remain in effect during the suspension period ordered below for the Eastchester service.

24. Based upon a review of the filing, the Commission finds that the proposed tariff sheet have not been shown to be just and reasonable and may be unjust, unreasonable, unduly discriminatory, or otherwise unlawful. Accordingly, the Commission shall accept the tariff sheet for filing and suspend its effectiveness for the period set forth below, subject to the conditions set forth in this order.

25. The Commission's policy regarding rate suspensions is that rate filings generally should be suspended for the maximum period permitted by statute where preliminary study leads the Commission to believe that the filing may be unjust, unreasonable, or that it may be inconsistent with other statutory standards. See Great Lakes Gas Transmission Co., 12 FERC & 61,293 (1980) (five-month suspension). It is recognized, however, that a shorter suspension period may be warranted in the circumstances where suspension for the maximum period may lead to harsh and inequitable results. See Valley Gas Transmission, Inc., 12 FERC & 61,197 (1980) (one-day suspension). No such circumstances are present here. Accordingly, the Commission will suspend Iroquois' rates for five months and permit them to take effect on July 1, 2004, subject to refund and subject to the conditions set forth in the body of this order and in the ordering paragraphs below.

The Commission orders:

(A) The tariff sheet listed in Footnote No. 1 is accepted and suspended for five months, to be effective July 1, 2004, subject to refund, conditions, and the outcome of a hearing established in this proceeding, as described in the body of this order.

(B) Iroquois is required to file within 20 days of the date of this order, an explanation and support for the proposed secondary access service, including the priority of service between firm, interruptible, and secondary access rate service, cost justification, impact on capacity release market, projected revenues, volumes, supporting testimony, and tariff sheets in sufficient detail to permit the Commission to evaluate the proposed service, as required by 18 C.F.R. § 154.202 (2003).

(C) Iroquois is required to file within 5 days of the date of this order, a revised tariff sheet reflecting the initial rate for service on the Eastchester project as the currently effective Part 284 rate of $0.4234 per day, effective as of the in-service date of the project. Such rate will remain in effect during the suspension period of this filing.

(D) Pursuant to the authority of the Natural Gas Act, particularly Sections 4, 5, and 15 thereof, and the Commission's rules and regulations, a public hearing shall be held concerning the lawfulness of Iroquois' proposed rates.

(E) A presiding administrative law judge, to be designated by the Chief Administrative Law Judge for that purpose pursuant to 18 C.F.R. ' 375.304, shall convene a prehearing conference in this proceeding, within 20 days of the date of this order, in a hearing or conference room of the Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. 20426. The prehearing conference shall be held for the purpose of clarification of the positions of the participants and establishment by the presiding judge of any procedural dates necessary for the hearing. The presiding administrative law judge is authorized to conduct further proceedings in accordance with this order and the rules of practice and procedure.

By the Commission. Chairman Wood and Commissioner Kelly concurring with a joint separate statement attached.

( S E A L )

Magalie R. Salas,
Secretary.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Iroquois Gas Transmission System, L.P. Docket No. RP04-136-000

(Issued January 30, 2004)

WOOD, Chairman, concurring
KELLY, Commissioner, concurring:

We support suspending the proposed rate increase for the full five-month period, but write separately to express my own concerns about allowing such a dramatic rate increase (more than double the existing Part 284 rates) due to substantial cost overruns ($124 million) to go into effect even subject to refund. The level of cost overrun and the resultant rate increase stretch far beyond the expectations of the parties that signed up for the expansion capacity and may also adversely impact existing shippers' use of the expansion delivery points through the secondary access service charge. Moreover, we look forward to the parties' developing an adequate record on the appropriate ROE to be reflected in the rates. In our view, a pipeline that has experienced such a large cost overrun should not necessarily be "rewarded" with a 14.9% return on equity as a result of the increased risks brought about by the overrun. For these reasons, we concur.

Pat Wood, III
Chairman

Suedeen G. Kelly
Commissioner