UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Columbia Gas Transmission Corporation	Docket No. RP05-21-002
Columbia Gulf Transmission Company	Docket No. RP05-20-002

ORDER DENYING REHEARING

(Issued June 2, 2005)

1. On December 6, 2004, Columbia Gas Transmission Corporation and Columbia Gas Transmission Company (collectively Columbia) filed a joint request for rehearing of the Commission's November 5, 2004 Order[1] in this proceeding. The Commission denies rehearing with one modification to its prior findings. This order benefits the public by assuring that pipelines will not require unduly discriminatory or overly broad waivers of a shipper's rights under section 5 of the Natural Gas Act (NGA) as a condition of discounted or negotiated rate agreements.

I. Background

2. This proceeding began when Columbia filed agreements providing rate discounts to certain of their respective customers. In Columbia Gulf's Docket No. RP05-20-000 these were Mountaineer Gas Company (Mountaineer),[2] Cincinnati Gas and Electric Company (CG&E), and Union Light, Heat, and Power Company (ULH&P). In Columbia Gas's Docket No. RP05-21-000 the customers were the three companies just named, plus two additional companies, Baltimore Gas and Electric Company (BG&E) and Columbia Gas of Kentucky (CKY). The agreements with BG&E and CKY were based on previously existing non-conforming agreements and certain modifications thereto which were being submitted for approval by the Commission. In both dockets the

[1] *Columbia Gulf Transmission Company and Columbia Gas Transmission Corporation*, 109 FERC ¶ 61,152 (2004) (prior order).

[2] Mountaineer is a wholly-owned subsidiary of the Monongahela Power Company, which collectively with The Potomac Edison Company and West Penn Power Company do business as Allegheny Power, a wholly-owned subsidiary of Allegheny Energy Inc.

agreements between Columbia and Mountaineer, CG&E, and ULH&P contained clauses providing that they would lose the discounts granted in these contracts if they filed challenges under section 5 of the NGA to "the base rate or the rate structure of either" Columbia Gulf or Columbia Gas, or participated in such challenges with one exception. That exception would permit intervention to prevent the reallocation of costs from other customers to those three specific customers in the context of a section 5 challenge to Columbia's rates. The limits on the customers seeking changes under NGA section 5 would generally remain in place until April 1, 2013. There is no commitment on the part of Columbia not to file a section 4 rate case in the intervening period.

3. Columbia asserted that the agreements with Mountaineer, CG&E, and ULH&P were discount agreements that need not be filed with the Commission.[3] The Commission rejected this contention. The Commission found that Columbia may not include in a discount agreement any provision limiting the right of shippers to seek Commission action under NGA section 5 to modify the pipeline's recourse rates. The Commission stated that, in the negotiated rate context, the Commission has approved a provision that the customer not seek to change the agreed-upon rate for the service to be provided under the negotiated rates. It held that this assures that there will be rate certainty for the duration of the agreement and that both parties will receive the benefits of their bargain. The Commission observed that, in the negotiated rate situation, the shipper has the alternative option of obtaining service at the just and reasonable recourse rate, without having to give up its rights under NGA section 5. The Commission further held that all the cases cited by Columbia to support its position involved negotiated rate agreements.

4. The Commission concluded that the section 5 waiver provision in the discount agreements was overly broad and beyond the scope of any such agreement previously approved by the Commission. The Commission concluded that the waiver went far beyond the discounted rates agreed to for the service to be provided under the service agreements at issue, and would apply to the pipelines' recourse rates for all their services, including service not covered by the subject service agreements but which the shippers could conceivably contract for in the future. The Commission noted it has rejected efforts to include such broad waivers of section 5 rights in negotiated rate agreements not subject to the pipeline's recourse rates, and therefore found that they would be even more unreasonable in discounted rate agreements that are subject to the pipeline's recourse rates.

5. Thus, the Commission concluded that its concern with such provisions was even greater in the context of discounted rate transactions because discounted rates must fall within the pipeline's maximum and minimum recourse rates. Thus, a shipper who agrees

[3] The different agreements involved discounts from Rate Schedules FTS, FST-1, FST-2, SST, and FSS contained in Columbia's FERC Gas Tariffs.

to a discounted rate is assured that, at no time during the term of its service agreement, will it ever be required to pay more than a just and reasonable maximum recourse rate and that the relative allocations of costs among different categories of shippers will remain the same. The Commission therefore concluded in the prior order that discounted rate shippers should not be deprived of the right to complain under NGA section 5 that the recourse rate has become unjust and unreasonable and should be lowered. The Commission stated that if a pipeline and a shipper want to obtain rate certainty by agreeing to a rate that will remain in effect through the term of the service agreement, the Commission provides them the opportunity to do so by entering into a negotiated rate agreement which provides the shipper with the alternative of relying on the pipeline's recourse rate.

6. The Commission therefore directed Columbia to either remove the limitations on section 5 rights from the discounted agreements at issue here, or to refile the agreements as negotiated rate agreements containing clauses that were consistent with its prior order. On November 22, 2004, Columbia refiled the discount agreements with Mountaineer, CG&E, and ULH&P without the limitations on section 5 rights that the Commission had rejected. The revised agreements were unprotested and were accepted in an unpublished order on January 19, 2005.[4] Columbia filed its rehearing request on November 22, 2004.

II. The Request for Rehearing

7. On rehearing, Columbia contends that the Commission erred in rejecting the section 5 waiver provision. It first argues that the Commission incorrectly stated that the section 5 waiver provision in the discount agreement deprived the shippers of their statutory right under NGA section 5 to challenge Columbia's rates. Columbia states that the provision permits the shippers to exercise their section 5 rights at any time. The provision only states that, if the shipper institutes a section 5 challenge, it will lose its discount. Thus, the shippers are free at any time to file a section 5 complaint against Columbia's recourse rates, so long as they agree to pay Columbia's maximum rate.

8. Columbia also argues that the Commission erred in concluding that a waiver of section 5 rights is more troubling in the discounted rate context than the negotiated rate context, because, unlike the case with negotiated rate agreements, discounted rate shippers do not have an alternative rate option. Columbia contends that the discounted rate shippers here had the same alternative option as negotiated rate shippers when they requested service – taking service at the maximum just and reasonable rate. In fact, the discounted rate shippers not only had that alternative when they originally requested service, but continue to have it during the terms of their agreements.

[4] *See* Docket Nos. RP05-20-001 and RP05-21-001.

9. Columbia further argues that the Commission failed to adhere to its own stated distinction between discounted rate and negotiated rate arrangements, when it held that the section 5 waiver would only be acceptable if Columbia converts the transaction into a negotiated rate deal. Columbia points out that, in response to the court's decision in *Northern Natural Gas Company v. FERC*,[5] the Commission has defined a discounted rate as a rate that stays within the maximum and minimum rates in the pipeline's tariff and is based on the same rate design as the pipeline's recourse rates.[6] Columbia states that the rates in the subject agreements satisfy these requirements. Columbia contends that the non-conforming section 5 waiver provision does not have anything to do with the nature of the rate and thus that provision cannot convert a discounted rate into a negotiated rate. Columbia also argues that the Commission incorrectly cited *CenterPoint Energy Gas Transmission Company*[7] because it was clear in that case that the shippers would lose the protection of the recourse rate under the agreements involved. Finally, it asserts that its proposal is no different than a volumetric discount, a published price index discount, or discounts contained in a most favored nation clause.

III. Discussion

10. The Commission denies rehearing. Upon review, the Commission recognizes that the section 5 waiver provision does not require Mountaineer, CG&E, and ULH&P to completely waive their rights to file a section 5 complaint against Columbia's recourse rate. Rather, they may file such a complaint, subject to loss of their discounts while the complaint is pending. The Commission also recognizes that the agreements at issue are discounted rate agreements and not negotiated rate agreements as they are (1) within the range of the maximum and minimum recourse rate, and (2) do not depart from the standard SFV rate design.[8] However, the central issue here is the fact that the waiver of the section 5 rights provision at issue is a non-conforming clause that is a material

[5] *Northern Natural Gas Company v. FERC,* 335 F.3d 1089 (2003) (*Northern Natural*).

[6] *Northern Natural Gas Company,* 105 FERC ¶ 61,299 (2003) (*Northern Natural* remand order*).*

[7] *CenterPoint Energy Gas Transmission Company,* 104 FERC ¶ 61,281 (2004) (*CenterPoint*).

[8] *Northern Natural* remand order at P 3, 12, and 20.

deviation from the pipeline's form of service agreement,[9] and as such must be reviewed to determine whether it is a permissible deviation regardless of whether the rate at issue would be characterized as a discount or a negotiated rate.

11. The Commission has held that material deviations fall into two general categories: (1) material deviations that must be prohibited because they present a significant potential for undue discrimination among shippers,[10] and (2) material deviations that can be permitted without undue risk of discrimination. One type of material deviation that is not generally permitted is negotiated terms and conditions of service different from those provided to other customers. The Commission generally finds that such provisions would be permissible only if the pipeline modifies its tariff to make the provision available to its other customers.[11] Other clauses are deemed to present such a danger of discrimination or contrary to Commission policy that they are rejected with finality.[12]

12. Columbia's request for rehearing therefore raises the issue of the extent to which a pipeline may negotiate with its customers to limit their statutory rights under NGA section 5 to challenge the justness and reasonableness of the pipeline's recourse rates, and

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[9] Such clauses can occur in either a discounted rate agreement or a negotiated rate agreement and are designed to facilitate the goals of the transaction. It is equally true that both a discounted rate agreement and a negotiated rate agreement can include a rate that is numerically less than the maximum recourse rate, but this is not necessarily true in the case of a negotiated rate agreement. S*ee Viking Natural Gas Pipeline Company*, 105 FERC ¶ 61,303 (2003). The Commission has approved agreements where the negotiated rate was initially more than the recourse rate, but was less than the recourse rate once the recourse rate was increased pursuant to a section 4 settlement.

[10] *CenterPoint* at 61,954-55, *citing Noram Gas Transmission Company*, 75 FERC ¶ 61,091 (1996), *order on reh'g*, 77 FERC ¶ 61,011 (1996) at footnotes 2, 11, and 12; *Columbia Gas Transmission Corp.*, 97 FERC ¶ 61,221 at 62,001-02 and 62,004 (2001); *ANR Pipeline Company*, 97 FERC ¶ 61,222 at 62,012-13 (2001).

[11] For example, the Commission required that all agreements having an early termination provision be placed in the pipeline's general terms and conditions authorizing such a clause because of the danger of discrimination. *See ANR Pipeline Company*, 97 FERC ¶ 61,222 at 62,012-13 (2001); *ANR Pipeline Company*, 97 FERC ¶ 61,223 at 62,017 (2001); *Columbian Gas Transmission Corp.*, 97 FERC ¶ 61,221 (2001)., involving an issue of modifications of minimum pressure requirements.

[12] *CenterPoint*, 104 FERC ¶ 61,281 at PP 22, 31, 42-52; *see also CenterPoint Gas Transmission Company*, 102 FERC 61,059 (2003), *order on reh'g*, 103 FERC ¶ 61,228 (2003) (rejecting a provision for sharing capacity release or marketing revenues).

the appropriate procedural vehicle for including such limits. The basic reason that Congress authorized the Commission to regulate pipeline rates under NGA sections 4 and 5 is that interstate gas pipelines have market power over many of the markets and shippers that they serve. Given that gas pipelines have market power, the Commission has been reluctant to allow pipelines to include in service agreements with individual shippers any limits on the shipper's statutory rights under NGA section 5 to challenge the justness and reasonableness of the pipeline's rates, or condition benefits of lower rates on shippers giving up rights under NGA section 5.[13]

13. For this reason departures from the recourse rate are normally market and transaction specific because they reflect situations where the pipeline is unable to charge the maximum recourse rate and must respond to some competitive pressure in the market or otherwise address the needs of the shipper in the transaction at issue.[14] The Commission allows two vehicles for the pipeline to negotiate rates different from the maximum recourse rate with individual customers in response to such pressures. As previously stated, these are (1) discounted rates and (2) negotiated rates. Discounted rates must use the same rate design as the recourse rates and are bound by the maximum and minimum recourse rates. Negotiated rates provide greater flexibility, may use a different rate design, and give the pipeline flexibility to obtain additional customers it could not otherwise obtain by meeting their economic needs in particular transactions. Each vehicle is intended to help captive customers by enabling the pipeline to obtain additional throughput over which to spread fixed cost recovery. However, since the purpose of a negotiated or discounted rate is generally to make the particular transaction in question economic, there is normally no reason for the agreement to address the pipeline's recourse rates in relation to other transactions unless the agreements provide for the same type of general applicability as a section 4 filing or a related settlement.

14. As such, the Commission has been reluctant to sanction a section 5 waiver in a service agreement for a particular transaction, where the customer waives its section 5 rights not only as to the rate for its particular transaction at issue, but as to the pipeline's rates for all services. This reluctance stems from two concerns. While shippers may have some leverage in negotiating specific rates and services in some markets, this leverage does not necessarily extend to the broader range of services contained in the pipeline's

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[13] *Columbia Gas Transmission Corporation*, 79 FERC ¶ 61,044 at 61,200 (1997) (*1997 Settlement Order)* at 61,203-04.

[14] Basic economic theory holds that a business will charge the maximum possible price in any given market based on the level of competition present. Thus, a pipeline would discount from its maximum rate only if it must do so to attract the business. Otherwise it would charge the maximum recourse rate authorized by the tariff.

tariffs at recourse rates.[15] The Commission does not believe that the pipeline should be permitted to condition the offering of a discount for one service for which a shipper may have competitive alternatives on limiting the shipper's section 5 rights to challenge the pipeline rates for other services over which the pipeline does have market power.

15. A second and more fundamental concern raised by this proceeding is that a pipeline may offer favorable rates solely to its larger customers with greater resources to litigate the justness and reasonableness of the pipeline's recourse rates, in return for their agreement not to challenge the pipeline's recourse rates and rate structure. The larger customers may be willing to accept such an offer, since they obtain the benefit of reduced rates for the services of interest to them. However, smaller customers with fewer resources may not receive the benefit of the deal offered the large customers. In short, the Commission is concerned that such broad waiver provisions may increase the risk of undue discrimination among customer classes unless the terms of the agreement are offered to all similarly situated customers.

16. It is because of the broad range of customers that are served, and the wide range of markets served by many pipelines, that pipelines establish their generally applicable recourse rates through rate filings under NGA section 4. This assures the maximum opportunity for all shippers to examine the inter-relationships between the various types of service and the geographic markets in which they are provided. Since section 4 proceedings are used to allocate the pipeline's costs among the different types of services and different geographic markets, section 4 proceedings provide the best opportunity for a thorough review to fairly allocate the pipeline's costs among the competing interests.[16] As Columbia points out, the Commission has approved section 5 rate moratoriums provisions as part of settlements of general section 4 rate cases**.** Typically, however, those provisions not only limit the shippers' rights to challenge the pipeline's rate under section 5, but also limit the pipeline's right to file rate increases under NGA section 4, which Columbia has not agreed to do here. Moreover, the recourse rates established in a section 5 proceeding are available to all the pipeline's shippers, both its captive shippers as well as those with competitive alternatives. Thus, all the pipeline's customers have an opportunity to benefit from the rates being established under the settlement.

17. For these reasons the instant case presents a materially different set of facts than those of the recently decided *Algonquin Gas Transmission, LLC.*[17] In that case Algonquin entered into a large number of negotiated rate agreements designed to

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[15] *Northern Natural* remand order at P 3.

[16] *Id.* at P 4.

[17] *Algonquin Gas Transmission, LLC*, 111 FERC ¶ 61,003 (2005) (*Algonquin).*

discount the rates to its customers below the recourse rates without the expense of litigation and the review of numerous controversial issues. Algonquin's agreements provided not only that the customers would not challenge any of the pipeline's recourse rates under NGA section 5, but also that the pipeline would not file to increase its recourse rates under NGA section 4. To assure that there was no undue discrimination among customers Algonquin offered to execute such agreements with all of its similarly situated customers if the customer so desired, and in fact has done so.[18] Moreover, to further guard against discrimination, the Commission required Algonquin to offer the discounts to all similarly situated existing and new shippers that later receive service under the same rate schedules. In short, the negotiated rate agreements in *Algonquin* accomplished much the same purpose as a section 4 settlement.

18. By contrast, in the instant case the discounts involve the lowering of certain rates for a limited number of relatively large customers without offering comparable rate reductions to other shippers. Moreover, Columbia has not agreed to not file a rate increase under NGA section 4. The instant case therefore falls within the Commission's particular concern that agreements that effectively reduce the recourse rates for a selected set of the pipeline's shippers may have an undue risk of discrimination when coupled with a waiver of the shippers' section 5 rights and no corresponding agreement by the pipeline not to file a generally applicable rate increase under NGA section 4.

19. The Commission recognizes that it has allowed pipelines to include in negotiated rate agreements provisions that the shipper will not challenge the negotiated rate for a particular transaction under NGA section 5. However, for the following reasons the Commission concludes that the broad waiver of section 5 rates at issue in these dockets presents a sufficient risk of discrimination that further argues against their approval. In this proceeding the Cities of Charlottesville and Richmond, Virginia (the Cities) protested the discounted rate agreements at issue here on the ground that prior to October 31, 2004, Mountaineer, CG&E, ULH&P were beneficiaries of a settlement clause in a November 22, 1996 Settlement that provided them with a reduced rate through that date. Some 95 percent of the discount was to be recovered through a Settlement Component in the reservation charges of Columbia's other customers.[19] As the 1996 Settlement neared the end of its term, Columbia removed the Settlement Component in a filing dated

[18] *See* Algonquin's April 12, 2005 Filing in Docket No. RP00-70-012 and its April 29, 2005 Filing in Docket No. RP00-70-013.

[19] The relevant settlement terms are summarized in an Order on Uncontested Settlement issued on April 17, 1997 in the *1997 Settlement Order*. Mountaineer's estimate benefit was estimated at $7.1 million and CG&E, including ULH&P at $6.9 million. Other beneficiaries included Dayton Power and Light Company, $3.8 million, and West Ohio Gas Company, $0.15 million.

September 30, 2004, effective November 1, 2004. In their protest, the Cities argued that Columbia was continuing the settlement discounts in the discount rate agreements and also seeking to shift the potential rate impact of those discounts to other customers in a future section 4 rate proceeding through the use of the Commission's discount adjustment methodology.[20]

20. While the Commission has concluded on rehearing that the agreements at issue are discount rate agreements, Columbia's efforts to continue the selected discounts for three large shippers through agreements including a broad section 5 waiver clause in the context of a selective discount is inconsistent with the Commission's general policy of restricting the use of such clauses to relatively narrow situations.[21] The Commission's past and present caution regarding the use of broad section 5 waiver clauses in agreements with discounted rates is appropriate here given the apparent ability of certain of Columbia's customers to extract rate concessions that are the equivalent to a broad rate reduction, but which is not available to smaller parties with less leverage. By providing several of its large shippers a rate reduction, Columbia reduced the risk that the balance of its revenue would be subject to challenge by those customers that provide substantial revenue collectively, but individually are less likely to have the means to contest the rates, as suggested by the Commission's order in *Algonquin*. Similarly, if Columbia were to file a section 4 rate case, it would have resolved in advance certain disputes it had in the past with its large customers involved in this proceeding while reserving the right to seek a discount adjustment for the discounted rates.[22]

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[20] In order to obtain a discount adjustment in a future section 4 rate case in connection with these transactions, Columbia will have to prove that the discounts at issue here were necessary to meet competition or to attract additional business to its system, and not for some other purpose. *See Trunkline Gas Co.* 90 FERC ¶ 61,017 at 61,093-95 (2000) (rejecting a discount adjustment with respect to a discount given in the middle of a long-term contract).

[21] The November 22, 1996 Settlement contained a broad clause prohibiting the exercise of section 5 rights by any party to the settlement through April 1, 2002. Even in the context of the uncontested settlement, the Commission concluded that the bar to section 5 complaints would not apply either to shippers who were not parties to the settlement or to the Commission. The Commission also stated that it had more general reservations about a breadth of the section 5 clause in that case. *1997 Settlement Order* at 61,203-04.

[22] *Id.* at 61,200 and 61,203, particularly footnote 7, which sought to preclude the Commission's trial staff from taking a position that would place Columbia at risk for the annual cost savings discussed in footnote 19.

21. In light of this concern, the Commission concludes that, in contrast to more limited restrictions on section 5 rights agreed to in the context of narrower, more limited negotiated rate agreements,[23] the discounts to the pipeline's recourse rates that were proposed here, conditioned broad waivers of the customers right to challenge the pipeline's recourse rates under section 5 clauses, are more appropriately addressed through settlement discussions in which all of the pipeline's shippers could participate, or as in *Algonquin*, a negotiated rate transaction in which all shippers can participate on equal terms.[24] For the reasons stated, the prior order properly required the deletion of the section 5 waivers at issue here. Columbia's request that it be permitted to retain the broad section 5 waiver provision in the agreements at issue is denied.[25]

The Commission orders:

Columbia's request for rehearing in the caption dockets is denied.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.

[23] *See* footnote 16, *supra.*

[24] Columbia must establish at its next section 4 rate hearing that these agreements were required by competition and thus not unduly discriminatory. *See Transcontinental Gas Pipe Line Corporation*, 107 FERC ¶ 61,058 (2004), and *Iroquois Gas Transmission System*, 84 FERC ¶ 61,086 (1998), *reh'g denied*, 86 FERC 61,266 (1999).

[25] Columbia cites *Vector Pipeline L.P*, 85 FERC ¶ 61,083 (1998), *reh'g denied*, 87 FERC ¶ 61,255 (1999) and *Alliance Pipeline, L.P.*, 80 FERC ¶ 61,169 (1997), *modified in part*, 84 FERC ¶ 61,239 (1998), *reh'g denied*, 85 FERC ¶ 61,331 (1998) for the proposition that the Commission has approved broad section 5 waivers. Neither case is apposite as both are certificate cases in which there is no significant discussion of the wavier issue. Furthermore, both involved negotiated rates available to all shippers desiring the rates during the subscription phase of the project. Neither case addresses the market and discrimination issues analyzed in this order involving the settlement recourse rates for an existing service.