

**DEPARTMENT OF ENERGY****Federal Energy Regulatory Commission****18 CFR Part 284**

[Docket Nos. RM05–23–000 and AD04–11–000]

**Rate Regulation of Certain Underground Storage Facilities**

December 22, 2005.

**AGENCY:** Federal Energy Regulatory Commission, DOE.**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** The Federal Energy Regulatory Commission (Commission) is proposing to amend its regulations to establish criteria for obtaining market-based rates for storage services offered under part 284. First, the Commission is proposing to modify its market-power analysis to better reflect the competitive alternatives to storage. Second, pursuant to Title III, Subtitle B, section 312 of the Energy Policy Act of 2005, the Commission is proposing rules to implement new section 4(f) of the Natural Gas Act, to permit underground natural gas storage service providers that are unable to show that they lack market power to negotiate market-based rates in circumstances where market-based rates are in the public interest and necessary to encourage the construction of the storage capacity in the area needing storage services, and that customers are adequately protected. These revisions are intended to facilitate the development of new natural gas storage capacity while protecting customers.

**DATES:** Comments are due February 27, 2006.

**ADDRESSES:** Comments may be filed electronically via the eFiling link on the Commission's Web site at <http://www.ferc.gov>. Commenters unable to file comments electronically must send an original and 14 copies of their comments to: Federal Energy Regulatory Commission, Office of the Secretary, 888 First Street, NE., Washington, DC, 20426. Refer to the Comment Procedures section of the preamble for additional information on how to file comments.

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**SUPPLEMENTARY INFORMATION:****I. Introduction**

1. On August 8, 2005, the Energy Policy Act of 2005 (EPAAct 2005 or the Act)<sup>1</sup> was signed into law. Section 312 of EPAAct 2005, adding a new section 4(f) to the Natural Gas Act (NGA),<sup>2</sup> permits the Commission to allow a natural gas storage service provider placing new facilities in service to negotiate market-based rates even if it is unable to show that it lacks market power if the Commission determines that market-based rates are in the public interest and necessary to encourage the construction of the storage capacity in the area needing storage services, and that customers are adequately protected.<sup>3</sup>

2. The enactment of EPAAct 2005 adds momentum to efforts already underway at the Commission to adopt policy reforms that would encourage the development of new natural gas storage facilities while continuing to protect consumers from the exercise of market power. On September 30, 2004, the Commission issued a staff report that examined underground natural gas storage.<sup>4</sup> On October 21, 2004, the Commission held a public conference with representatives of the industry to discuss the Staff Storage Report and issues relevant to underground storage.<sup>5</sup> The Commission received oral and written comments in connection with the Staff Storage Report and conference.

3. After considering the conference comments, the current characteristics of the storage market, the nation's existing

<sup>1</sup> Energy Policy Act of 2005, Pub. L. No. 109–58, 119 Stat. 594 (2005).

<sup>2</sup> 15 U.S.C. 717, *et seq.* (2000).

<sup>3</sup> Energy Policy Act of 2005, Pub. L. 109–58, § 312, 119 Stat. 594, 688 (2005).

<sup>4</sup> *Current State of and Issues Concerning Underground Natural Gas Storage*, FERC Staff Report, Docket No. AD04–11–000 (Sept. 30, 2004) (Staff Storage Report).

<sup>5</sup> *State of the Natural Gas Industry Conference*, Docket No. PL04–17–000, October 21, 2004; *see* State of Natural Gas Industry Conference; Staff Report on Natural Gas Storage; Notice of Public Conference, 69 FR 59917 (Oct. 6, 2004) (summarizing the issues to be discussed at the conference).

and projected storage capacity needs, and the new legislation, the Commission concludes that reform of its current pricing policies may be appropriate. The purpose of this reform is to ensure access to storage services on a nondiscriminatory basis at just and reasonable rates and ensure that sufficient storage capacity will be available to meet anticipated increases in market demand. To achieve these goals, the Commission is adopting a two-prong approach. First, this notice of proposed rulemaking (NOPR) proposes modifications to the Commission's market power analysis to permit the consideration of close substitutes to storage in defining the relevant product market. This will ensure that market-based rates are not denied because of an overly narrow definition of the relevant market. Second, the Commission is proposing regulations to implement section 312 of EPAAct 2005, which permits qualifying storage providers to charge market-based rates for a new facility even when they cannot (or do not) demonstrate that they lack market power. The Commission seeks comment, among other things, on whether there are certain generic safeguards that will provide adequate customer protections for entities applying for market-based rates under new NGA section 4(f). It should be noted, however, that these two policy reforms do not require a "sequential" approach for a potential storage developer. Instead, where a prospective applicant believes that it can make a showing sufficient to satisfy the requirements of new NGA section 4(f), it need not submit a traditional market power analysis in support of its request for market rates. In reviewing the applicant's request for market-based rates under section 4(f), the Commission will presume that the applicant has market power for the purposes of ensuring that customers are adequately protected. Taken together, the intent of these reforms is to facilitate the expansion of gas storage capacity to, among other things, mitigate natural gas price volatility, while continuing to protect consumers from the exercise of market power.

**II. Background***A. Changing Nature of Storage Services*

4. In Order No. 636, the Commission found that pipelines held a competitive advantage over other gas sellers, in part

because of the lack of access to storage services.<sup>6</sup> Therefore, the Commission amended § 284.1(a) of its regulations to define transportation to include storage. This required pipelines to offer their customers firm and interruptible storage on an open-access, contract basis. Since the 1992 issuance of Order No. 636, much has changed. Storage is now being used to support new services made possible by the unbundling of storage from transportation and by new market conditions arising from the Commission's restructuring efforts. In addition, traditional interstate natural gas pipelines are experiencing competition for contract storage customers from independent storage providers. Many new entities provide myriad service options, and natural gas customers are able to choose among competing sellers, often as supplements or alternatives to "backstop" long-term, firm transportation and storage services contracted at Commission-regulated rates.

5. The nature of the gas storage marketplace also has changed significantly over the last decade. Traditionally, local distribution companies (LDCs) contracted for firm storage service on a long-term basis, principally to meet peak winter heating needs. Thus, underground storage fields were typically designed to inject gas during the spring, summer, and fall, and then draw on the accumulated underground inventory to meet winter heating demands. This model is changing. Instead of relying primarily on firm, long-term gas supply or transportation service contracts, wholesale customers are increasingly relying on a portfolio of both long-term and short-term contracts to purchase, store and transport natural gas.<sup>7</sup> There

is a growing use of storage volumes not only to meet traditional winter heating demand, but also to supply gas to meet daily, or even hourly, demand for gas-fired electric generation plants. Storage is also being used to ensure liquidity at market centers to help market participants capture short-term changes in the value of natural gas.

6. This fundamental shift in contract terms and load profile challenges longstanding operational and financial presumptions regarding storage service. Whereas a storage facility designed for one annual injection-withdrawal cycle is well suited to supply gas to meet winter heating demands, such a facility may be less than ideal in meeting the intermittent summer demand spikes associated with supplying gas to fuel electric generation plants. A storage facility capable of cycling working gas repeatedly throughout the year, using high deliverability and injection to fulfill daily, even hourly, swings in demand, such as salt cavern storage, is able to satisfy such load profiles.<sup>8</sup> However, electric generators are much less likely to sign traditional long-term firm contracts, but may be more interested in the type of flexible pricing proposals offered uniquely under market-based rates.<sup>9</sup>

#### B. Storage Capacity and Natural Gas Prices

7. Regardless of whether a storage facility is operated on a traditional, annual injection-withdrawal cycle, or completes multiple cycles throughout a year, the fact that gas can be injected into a storage facility and then held in repose, to be called upon during periods of high demand, has a moderating influence on gas prices. As a physical hedge, customers can build up underground inventories during times of lower demand, and then rely on these supply stores to avoid paying high spot market gas prices. Among the key

*Natural Gas Association of America v. FERC*, 285 F.3d 18 (D.C. Cir. 2002). In that proceeding, the Commission considered the consequences of the restructuring of the gas industry following Order No. 636, and found "a short-term gas market that is robust, functioning, efficient, and effective." FERC Stats. & Regs. Regulations Preambles (July 1996–December 2000) ¶ 31.091 at 31.255 (Feb. 9, 2000) (quoting comments submitted by the New York Mercantile Exchange).

<sup>8</sup> The Commission has authorized a number of salt cavern storage facilities that have these operational characteristics. See, e.g., *Pine Prairie Energy Center, LLC*, 109 FERC ¶ 61,215 (2004) (authorizing the construction and operation of a high deliverability salt-cavern storage facility capable of as many as 30 injection-withdrawal cycles a year at maximum injection and withdrawal rates).

<sup>9</sup> See, e.g., Energy Information Administration, *The Challenge of Electric Power Restructuring for Fuel Suppliers*, at 54–56 (September 1998).

findings highlighted by the Staff Storage Report is that the "continued commodity price volatility indicates that more storage may be appropriate" and that storage "may be the best way of managing gas commodity price, so the long-term adequacy of storage investment depends on how much price volatility customers consider 'acceptable.'" <sup>10</sup> The last several years have seen a marked rise in the overall commodity cost of natural gas and sharp swings in gas prices. In view of the resulting adverse economic impacts, Commission policy should not discourage the development of additional storage capacity through overly narrow definitions of the relevant market. Furthermore, we should consider a range of customer protections in implementing our new authority under NGA section 4(f).

#### C. The Need for Additional Storage

8. Currently, there are approximately 200 storage facilities subject to the Commission's jurisdiction, with an aggregate working gas capacity of approximately 2.5 Tcf. Estimates of total domestic working gas capacity (both subject to and exempt from NGA jurisdiction) range up to 4.7 Tcf.<sup>11</sup> Considering future storage needs of the United States and Canada together, the National Petroleum Council (NPC) estimates an additional 700 Bcf will be required by 2025.<sup>12</sup> Although current and projected storage development is keeping pace with aggregate national storage demands, underground storage development in some market areas, such as New England<sup>13</sup> and the Southwest, is not.<sup>14</sup>

9. In large part, a storage facility's utility is a function of its location. Gas-fired electric generation is anticipated to

<sup>10</sup> Staff Storage Report, at 1 (Sept. 30, 2004).

<sup>11</sup> The Department of Energy's Energy Information Administration (EIA) reports that in 2002 working gas storage capacity varied between 4.4 and 4.7 Tcf, whereas the Department of Energy's Office of Fossil Energy reports that in 2003 there were 415 underground storage facilities with a working gas capacity of 3.9 Tcf. The Staff Storage Report considered the range of estimated aggregate existing working gas and concluded that the present working gas capacity is 3.5 Tcf, of which 2.5 Tcf is subject to NGA jurisdiction, and that by improving existing storage reservoirs (*i.e.*, by reengineering existing facilities to enhance efficiency, rather than by expanding cavern capacity), there is the potential to obtain another 200 to 500 Bcf. See Staff Storage Report at 7–10.

<sup>12</sup> *Balancing Natural Gas Policy—Fueling the Demands of a Growing Economy*, NPC, Volume II at 261 (2003).

<sup>13</sup> New England appears to have little geologic potential for the development of underground storage facilities.

<sup>14</sup> See, e.g., Southwestern Gas Storage Technical Conference, Docket No. AD03–11–000, Transcript at 23, lines 10–14 (Aug. 26, 2003).

<sup>6</sup> *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, 57 FR 13267 (Apr. 16, 1992), III FERC Stats. & Regs. ¶ 30,939 at 30,425–427 (Apr. 8, 1992), *order on reh'g*, Order No. 636–A, 57 FR 36128 (Aug. 12, 1992), III FERC Stats. & Regs. ¶ 30,950 (Aug. 3, 1992), *order on reh'g*, Order No. 636–B, 57 FR 57911 (Dec. 8, 1992), 61 FERC ¶ 61,272 (1992), *notice of denial of reh'g*, 62 FERC ¶ 61,007 (1993), *aff'd in part and vacated and remanded in part, United Dist. Companies v. FERC*, 88 F.3d 1105 (D.C. Cir. 1996), *order on remand*, Order No. 636–C, 78 FERC ¶ 61,186 (1997).

<sup>7</sup> The development of a short-term market for gas services was addressed by the Commission in 2000, in its *Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services*, Order No. 637, FERC Stats. & Regs. Regulations Preambles (July 1996–December 2000) ¶ 31.091 (Feb. 9, 2000), *order on reh'g*, Order No. 637–A, FERC Stats. & Regs. Regulations Preambles (July 1996–December 2000) ¶ 31.099 (May 19, 2000), *reh'g denied*, Order No. 637–B, 92 FERC ¶ 61,062 (2000), *aff'd in part and denied in part, Interstate*

drive a significant portion of the growth in gas consumption. Electric demand is expected to grow along with population, and one region of recent and forecasted population growth is the desert Southwest.<sup>15</sup> Since electric generation requirements are more transient than steady-state demand, base-load infrastructure facilities may not be an ideal means to meet future electric needs. Storage projects, especially high-deliverability salt cavern facilities, may prove more adaptable than pipelines in supplying gas on an as-needed basis to match the fluctuations in the demand profile of electric generation facilities.

10. Over the last several years, there has been a revival of interest in expanding existing and building new marine terminal facilities to import liquefied natural gas (LNG). New storage projects are being developed to absorb the additional revaporized LNG imports. To date, most such activity has been in the states along the arc of the Gulf of Mexico. The natural gas production, gathering, processing, transportation, and storage infrastructure in this region is extensive. Storage project sponsors have been able to demonstrate that the competitive nature of the gas market in this region ensures that new storage entrants are unlikely to be able to exercise market power, and hence merit market-based rates for new storage services.<sup>16</sup> In contrast, in the Southwest there is no equivalent infrastructure in place. This is noteworthy because several new LNG terminals are planned for the Mexican states of Baja California, Sonora, and Sinaloa, and a significant portion of the LNG received in Mexico is expected to flow north for consumption in the United States, with the Southwest as a targeted market. Additional storage in the Southwest could facilitate the receipt and distribution of these new natural gas supplies.

11. The development of underground storage facilities is dictated (1) by geology, which determines the physical properties of prospective reservoirs, such as size and cushion gas requirements; (2) by access to supply; (3) by access to consuming markets; and (4) by access to pipelines capable of transporting additional volumes of stored gas. Once a suitable site is identified, whether new storage capacity

will be built turns on matters of construction and operating costs, market demand and the environment. Severe, adverse and unavoidable environmental impacts may preclude construction in certain locations. Investors also may be reluctant to fund a new project because of unattractive risk/reward prospects due to regulatory pricing constraints. This NOPR seeks to ensure that the Commission's regulatory approach does not unnecessarily impede the development of needed storage projects.

12. For storage services used on a short-term or spot basis, cost-of-service rates designed on the basis of an annual working gas cycle may not match up with the market value of storage service during transient periods of peak demand. Cost-of-service rates are based on projections of annual revenue requirements and relatively constant levels of demand. However, in today's markets, wholesale customers are not always willing to enter into long-term storage contracts sufficient to assure the storage investors that their annual revenue requirements will be met. Storage services used on a short-term or spot basis often do not exhibit the level of demand assumed by cost-of-service rate design. Permitting storage operators to earn higher revenues from short-term services during peak demand periods or through other pricing mechanisms may make an investment in the project economically feasible. Therefore, the NOPR seeks to lead to increased storage capacity that could benefit customers while continuing to protect them from the exercise of market power.

### III. Discussion

13. This NOPR is proposing changes to our regulations to permit storage providers to secure market-based rates under certain circumstances, while at the same time seeking to protect customers against potential exercises of market power. First, we are proposing regulations permitting all companies with storage facilities to seek market-based rates through a showing that their storage operations do not have significant market power. We have re-examined our approach to analyzing market power so that our analysis of whether to permit market-based rates for storage services better reflects the current competitive realities of the storage market. Second, for new storage capacity related to a specific facility placed into service after August 8, 2005, we are proposing regulations under new NGA section 4(f) that will authorize market-based rates under certain circumstances. Under these regulations, storage operators will be required to propose measures to protect customers

from the potential exercise of market power, and we solicit comment on various approaches that could be used as generic safeguards in providing such protection. A storage service provider may apply for market-based rates under either method by filing appropriate supporting data when it files its certificate application, or as part of its request for NGA section 311 rate authorization, or in a request for declaratory order for authority to charge market-based rates, but in any case it cannot charge market-based rates until the Commission concludes that the storage applicant has established that it lacks significant market power<sup>17</sup> or that it will adopt adequate customer protections pursuant to new NGA section 4(f).

14. The Commission recognizes that the measures proposed herein will not guarantee the proliferation of new storage projects. For example, despite a perceived need for new storage in the Southwest, there have been proposals for new storage projects that have failed to go forward for reasons unrelated to rate treatment.<sup>18</sup> Nevertheless, the flexibility proposed herein may induce the development of new storage capacity that would otherwise not be built.

#### A. Market Power Analysis for Market-Based Rates

15. The Commission evaluates requests to charge market-based rates for storage services under the analytical framework of its 1996 Alternative Rate Policy Statement (Policy Statement).<sup>19</sup> The Policy Statement establishes procedures for service providers to demonstrate that they lack significant market power, using criteria recognized by the courts and similar to those used

<sup>17</sup> See *Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines*, 74 FERC ¶ 61,076 at 61,236 (1996), *reh'g and clarification denied*, 75 FERC ¶ 61,024 (1996), *petitions denied and dismissed*, *Burlington Resources Oil & Gas Co. v. FERC*, 172 F.3d 918 (D.C. Cir. 1998); see also *Association of Oil Pipe Lines v. FERC*, 83 F.3d 1424, 1442-43 (D.C. Cir. 1996).

<sup>18</sup> See, for example, *Desert Crossing Gas Storage and Transportation System LLC*, 98 FERC ¶ 61,277 (2002), a proposal that has stalled, apparently due to shortfalls in contractual commitments and environmental concerns, and *Copper Eagle Gas Storage L.L.C.*, 97 FERC ¶ 62,193 (2001) and 99 FERC ¶ 61,270 (2002), a proposal delayed due to expressions of concern by the State of Arizona legislature raised as a result of security and safety issues associated with the project's planned location near Luke Air Force Base.

<sup>19</sup> *Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines and Regulation of Negotiated Transportation Services of Natural Gas Pipelines*, 74 FERC ¶ 61,076 (1996), *reh'g and clarification denied*, 75 FERC ¶ 61,024 (1996), *petitions denied and dismissed*, *Burlington Resources Oil & Gas Co. v. FERC*, 172 F.3d 918 (D.C. Cir. 1998).

<sup>15</sup> For example, Arizona's population is expected to increase by 5.6 million by 2030. U.S. Census Bureau, Population Division, Interim Projections (April 2005).

<sup>16</sup> See, e.g., *Caledonia Energy Partners, L.L.C.*, 111 FERC ¶ 61,095 (2005) and *Freebird Gas Storage, LLC*, 111 FERC ¶ 61,054 (2005) (approving new storage projects in the Gulf of Mexico area that qualified for market-based rates).

by the Department of Justice and the Federal Trade Commission. Under the Policy Statement, an applicant seeking authority to charge market-based rates must demonstrate that it lacks significant market power, or has adopted conditions that sufficiently mitigate its market power.<sup>20</sup>

16. The first step in analyzing whether an applicant has significant market power involves defining the relevant market in terms of both product market and geographic market. Such markets are defined by identifying the specific products or services and the suppliers of those products or services that provide good alternatives to the applicant's products and services. A good alternative is one that is available soon enough, has a price that is low enough, and has a quality high enough to permit customers to substitute the alternative for the applicant's services.

17. The Commission's initial screening tool for significant market power is the Herfindahl-Hirschman Index (HHI), a formula that focuses on the relevant market's concentration as an indicator of the potential of an applicant to act together with other sellers to raise prices. In general, an HHI below 1,800 suggests limited market concentration with less potential for any participant to exercise significant market power. However, an HHI above 1,800 suggests a higher level of concentration, and will cause the Commission to increase its scrutiny of other factors such as the applicant's market share, ease of entry into the market, the relative size of the applicant's capacity, and/or the sustainability of a potential attempt by the applicant to exercise market power.<sup>21</sup>

18. Since 1996, over 40 storage service providers have sought market-based rates pursuant to the criteria in the Policy Statement. In the majority of these cases, the Commission found that the applicant lacked significant market power and approved market-based rates. In applying its market concentration and market share screens in these cases to date, the Commission has looked only to the availability of other storage alternatives (in the relevant geographic market), in assessing whether a storage provider can exercise significant market

power. Using this analysis, the Commission has approved all requests for market-based rates where the applicant was located in the production area. Due to extensive storage infrastructure in these regions, the Commission has been able to find a lack of significant market power based on findings that HHIs in that geographic region are well below 1,800, and without intense scrutiny of other factors.<sup>22</sup>

19. On the other hand, storage markets in consuming regions, such as the Northeast portion of the United States, have fewer storage providers, and have certain providers with large market shares, resulting in HHI values sufficient to require a higher level of Commission scrutiny of factors beyond market concentration. Nevertheless, the Commission has approved requests in consuming areas of the Northeast by considering factors other than market concentration. For example, in *Avoca Natural Gas Storage*,<sup>23</sup> the Commission approved market-based rates despite an HHI for deliverability of 4,100 in the relevant New York/Pennsylvania market, specifically noting the small size of Avoca's market share and the apparent ease of entry into the market as factors mitigating the market concentration reflected in the HHI.<sup>24</sup>

20. However, in areas where there are truly only a limited number of storage service providers, the Commission's traditional analysis will likely result in a storage provider having high HHI values as well as relatively large market shares. For example, in 2002, Red Lake Gas Storage, L.P. (Red Lake) proposed to construct a new underground storage facility in Arizona, an area not currently served by underground gas storage, and sought approval to charge market-based rates. The Commission denied Red Lake's market-based rate request based on its determination that, if built, the market Red Lake would operate in would be extremely concentrated and it would have substantial market power.<sup>25</sup>

21. The Commission is concerned that its current approach to analyzing market power may be too limiting in some

circumstances because it does not consider the fact that non-storage products and services in a properly defined geographic market may be good alternatives to storage services, and thus mitigate a storage provider's ability to exercise market power. For example, in today's natural gas markets, pipeline capacity that is unaffiliated with the storage provider may be a good alternative to the storage service being offered. A new entrant proposing to offer its storage services in an area already fully served by existing pipelines would offer customers in that market area new service options, which to some extent would compete with existing service providers. Any new independent storage capacity would be expected to lower the market concentration and increase available alternatives in such a market.

22. The Commission therefore believes that it is not appropriate to limit the relevant product market to services offered by competing storage facilities. Such a narrow definition may incorrectly indicate that the storage applicant can exercise significant market power when, in fact, such ability could be constrained by sufficient pipeline alternatives. The denial of market-based rate authority in these circumstances could harm customers by providing a disincentive to storage development, particularly in underserved areas, in situations where significant market power does not exist.

#### 1. Modifications to Market-Based Rate Test

23. The Commission proposes to reform its market-power test for natural gas storage operators to more accurately reflect the competitive conditions in the market for gas storage services. The Commission believes it is appropriate to adopt a more expansive definition of the relevant product market for storage to explicitly include close substitutes for gas storage services. We will evaluate potential substitutes, such as available pipeline capacity, and local gas production or LNG terminals, on a case-by-case basis in the context of individual applications for market-based rates<sup>26</sup>

24. In order to show that a non-storage product or service such as

<sup>26</sup> Historically, market area storage was often developed to provide an economic alternative to more expensive pipeline expansions. By design, market area storage service used available off-peak pipeline capacity to inject gas into storage and expanded pipeline capacity from the storage fields to markets to deliver incremental supplies during market peaks. Thus, storage plus limited pipeline expansions provided a good economical alternative to more expensive production-area-to-market-area pipeline expansions.

<sup>22</sup> See, e.g., *Caledonia Energy Partners, L.L.C.*, 111 FERC ¶ 61,095 (2005); *Egan Hub Partners, L.P.*, 99 FERC ¶ 61,269 (2002); *Egan Hub Partners, L.P.*, 95 FERC ¶ 61,395 (2001).

<sup>23</sup> 68 FERC ¶ 61,045 (1994).

<sup>24</sup> The Commission reached a similar result analyzing storage services in *Steuben Gas Storage Co.*, 72 FERC ¶ 61,102 (1994); *New York State Electric and Gas Corp.*, 81 FERC ¶ 61,020 (1997); *N.E. Hub Partners, L.P.*, 83 FERC ¶ 61,043 (1998); *Seneca Lake Storage, Inc.*, 98 FERC ¶ 61,163 (2002); and *Wyckoff Gas Storage Co., LLC*, 105 FERC ¶ 61,027 (2003).

<sup>25</sup> *Red Lake Gas Storage, L.P.*, 102 FERC ¶ 61,077, *reg'h denied*, 103 FERC ¶ 61,277 (2003).

<sup>20</sup> The Policy Statement describes significant market power as the ability to withhold services in a relevant market in order to produce a significant price increase for a significant period of time. The Commission adopted 10 percent as its standard price change threshold but did not preclude parties from arguing for the adoption of a higher or lower threshold in individual cases. 74 FERC ¶ 61,076 at 61,232.

<sup>21</sup> *Id.*

transportation is a good alternative, the storage applicant would need to meet the criteria set forth in the Commission's Policy Statement,<sup>27</sup> including a showing that the service is available. In addition, consistent with the Commission's current practice, capacity on pipeline systems owned or controlled by the applicant's affiliates should not be considered among the customers' alternatives. Rather, affiliated capacity will be included in the market share calculated for the applicant.<sup>28</sup>

25. We provide the following guidance regarding the types of products that may be close substitutes depending on the facts of a given case. As a general matter, competition to a storage provider can come from entities that have the ability to deliver gas in the same market as the storage facility. In producing areas, storage may compete with production or LNG supply, in addition to other storage facilities. In market areas, there may also be local production or LNG available. In addition, available pipeline capacity can function as a close substitute by delivering gas at peak times to compete with a storage provider. For these reasons, we will permit applicants to present evidence that both available pipeline capacity and local production/LNG supply in the geographic market area can reasonably be considered as alternative products to storage services.

26. In addition, firm capacity available through capacity release can be a good alternative in appropriate circumstances. Under the Commission's capacity release regulations, holders of firm capacity are free to release the capacity to other shippers, as well as to make bundled sales at alternate delivery points. Because of this flexibility, some portion of firm, contracted-for capacity may have a sufficiently elastic demand (a willingness to re-sell firm capacity when price rises) to serve as a good alternative to an applicant's storage service.

27. A determination of whether capacity release provides a close substitute will depend on the facts of a particular case. For example, to the extent an LDC or similar entity holds pipeline capacity that is needed to meet state-mandated service obligations for captive retail customers, the capacity holder may have a relatively inelastic demand that makes it unlikely that the

LDC will release that capacity and therefore that increment of transportation capacity may not be considered a good alternative during peak periods. However, LDCs and marketers also serve industrial and other customers under interruptible contracts which might make that portion of the LDC's capacity a reasonable alternative.

28. Moreover, in some circumstances, an applicant may be able to show that even when firm capacity on a pipeline is reserved for captive customers, *e.g.*, residential and small commercial customers, potential product or service substitution in downstream markets can result in capacity becoming available to compete in upstream markets while still serving captive customers. Under the Commission's open-access program, competition in a downstream market may create competition in upstream markets, particularly due to Order No. 636's requirement that pipelines provide flexible receipt and delivery points and segmentation including backhaul. Thus, an LDC's ability to buy capacity from another pipeline or storage facility or to purchase gas in the downstream market may free it to release upstream capacity, to compete with storage in the upstream market. This ability to buy capacity from another pipeline or storage facility or buy gas in the market area is present in the large downstream markets in the United States including California, Chicago and the Northeast.

29. Take, for example, the California downstream market. Capacity held on Transwestern Pipeline Company, LLC (Transwestern) and El Paso Natural Gas Company (El Paso) could compete with a storage project located in a market upstream of California if California customers of these pipelines can buy gas from other sources in the downstream markets. This could free upstream capacity to compete with the upstream storage project. For example, Pacific Gas & Electric Company (PG&E) could buy gas from PG&E Gas Transmission, Northwest Corporation (PGT), Kern River Gas Transmission Company, an electricity generator in the California market, withdraw from its own storage, or purchase local production or regasified LNG to serve its captive or core customers. As a result, PG&E would be able to either release a portion of its firm capacity on El Paso, or nominate a secondary delivery at an upstream point to sell gas in the upstream market. As indicated above, whether capacity release in a given market would qualify as a close substitute under the Policy Statement

would be determined on the facts of a given case.

30. Thus, based upon a proper showing, the Commission believes it would be appropriate for a storage applicant to include pipeline capacity that is used to serve captive customers if it is demonstrated that there are reasonable substitutes in the downstream market for serving load that would free up capacity in the upstream market that would compete with the storage project.

31. In summary, the Commission proposes to modify its current approach to analyzing market power to explicitly permit a storage applicant to propose to include other storage services, as well as non-storage products and services, including pipeline capacity and local production/LNG supply as described above, in its calculation of market concentration using the HHI and in its analysis of market share. The Commission believes that consideration of these alternative products will ensure that the Commission's market power analysis accurately reflects whether a storage applicant is able to exercise significant market power. The Commission requests comments on this approach as well as suggestions regarding other approaches for quantifying the amount of pipeline capacity that would compete with an applicant's storage services.

## 2. Filing Procedures and Periodic Review

32. Because most of the applications requesting market-based rates have been filed by storage providers, the Commission believes it would be beneficial to adopt specific procedures and filing requirements. Therefore, the Commission proposes to add a new subpart M to part 284 that requires, among other things, that applications by storage providers requesting market-based rates contain certain information. The Commission will continue its practice of approving market-based rate proposals on a prospective basis only.

33. Approval of blanket certificate authority to provide open access storage services at market-based rates will subject the storage service provider to the existing reporting requirements applicable to open-access service providers under § 284.13 of the Commission's regulations. The public disclosure of this information will enable the Commission and the industry to monitor the market-based storage transactions.

34. In a recent case, the Commission also required an applicant to file an updated market-power analysis within five years of the date of the Commission

<sup>27</sup> A good alternative is one that is available soon enough, has a price that is low enough, and has a quality high enough to permit customers to substitute the alternative for the applicant's services.

<sup>28</sup> See Policy Statement, 74 FERC ¶ 61,076 at 61,234 (1996).

order granting authority to charge market-based rates, and every five years thereafter.<sup>29</sup> The Commission believes that imposition of a periodic review is necessary to ensure that our grant of market-based rates to an applicant remains just and reasonable. Accordingly, the Commission proposes to add § 284.504 to the regulations to require storage applicants receiving market-based rates on the basis of a market power analysis to file updated market-power analyses within five years of the date of the Commission order granting authority to charge market-based rates, and every five years thereafter.

### B. Energy Policy Act of 2005

35. Section 312 of EPAct 2005 adds new NGA section 4(f), which permits the Commission to authorize new natural gas storage projects (*i.e.*, projects placed in service after the passage of the Act) to provide service at market-based rates notwithstanding the fact that the applicant is unable to demonstrate that it lacks market power. New NGA section 4(f) requires that, to authorize market-based rates, the Commission must find that “market-based rates are in the public interest and necessary to encourage the construction of the storage capacity in the area needing storage services” and “customers are adequately protected.” The Act further requires that the Commission “ensure that reasonable terms and conditions are in place to protect consumers” and that the Commission “review periodically whether the market-based rate is just, reasonable, and not unduly discriminatory or preferential.” Intrastate pipelines also provide storage services, and new NGA section 4(f)(1) extends the market-based rate authority to intrastate pipelines subject to Commission authority under the Natural Gas Policy Act of 1978.<sup>30</sup> We discuss below the relevant aspects of new NGA section 4(f).

#### 1. Storage Capacity Eligible for Market-Based Rates

36. Under the new NGA section 4(f), the Commission may authorize market-based rates “for new storage capacity related to a specific facility placed in service after the date of enactment.”

<sup>29</sup> *Liberty Gas Storage LLC*, 113 FERC ¶ 61,247 (2005).

<sup>30</sup> 15 U.S.C. 3301–3432 (2000). We note that the Commission has authorized Hinshaw pipelines to be treated the same as LDCs and we intend the same here. See *Certain Transportation, Sales and Assignments by Pipeline Companies not Subject to Commission Jurisdiction Under Section 1(c) of the Natural Gas Act*, Order No. 63, FERC Stats. & Regs. Regulations Preambles (1997–1981) ¶ 30,118 (Jan. 9, 1980).

Interstate natural gas pipelines asked the Commission at the October 12, 2005 Conference on State of Natural Gas Infrastructure to allow post-EPAct 2005 storage expansions of existing storage facilities to qualify under this provision.<sup>31</sup>

37. We believe that the phrase “placed in service after the date of enactment” modifies the term “facility,” not the term “capacity,” such that it is the facility which must be placed into service after August 8, 2005, rather than the storage capacity. While the statute does not define the term “specific facility,” the Commission proposes to interpret that term to consider a new cavern, reservoir or aquifer that is developed after August 8, 2005, as a facility qualifying for market-based rates under the Act. We believe that this interpretation is most consistent with the wording of new NGA section 4(f). We invite comments on alternative constructions of the Act. We also invite comments on how, if we construe the Act differently, the Commission may adequately protect other customers already receiving service under cost-based authorizations that pre-date the Commission’s new NGA section 4(f) authority.

#### 2. Market-Based Rates Are in the Public Interest and Necessary To Encourage the Construction of Storage Capacity in the Area Needing Storage Services

38. Before authorizing market-based rates under new NGA section 4(f), the Commission is required to determine that such rates are in the public interest and are necessary to encourage the construction of storage capacity in the area needing storage services. As discussed in the section below, applicants for authorization under section 4(f) will be required to demonstrate that customers will be adequately protected from any abuses of market power by the storage provider. Those customer protections will serve to ensure that the market-based rates charged are in the public interest.

39. The Commission proposes to require that the applicant bear the burden of showing that in its specific circumstances, market-based rates are necessary to encourage the construction of storage capacity and that storage services are needed in the area. The Commission invites comment on how a project applicant might make these showings. One possible way would be for the applicant to present evidence

<sup>31</sup> Comments of Scott Parker, President, Kinder Morgan Pipeline Group, State of the Natural Gas Infrastructure Conference, Docket No. AD05–14–000, Transcript at 120, lines 6–11 (Oct. 12, 2005).

that it offered its capacity at cost-based rates through an open season and was unable to obtain sufficient long-term commitments at those cost-based rates.

#### 3. Customer Protection

40. New NGA section 4(f) also requires that the Commission, as a prerequisite for granting market-based rate authority, determine that customers are adequately protected, and requires the Commission to ensure that reasonable terms and conditions are in place to protect them. The Commission proposes to allow the applicant to propose a relevant method of protecting customers.

41. In general, the Commission believes that customers will be better off if more storage infrastructure is built. Additional storage will benefit customers by increasing customer alternatives in a market and by mitigating price volatility.<sup>32</sup> Therefore, just as the Commission balances the benefits of proposed new construction against residual adverse impacts in determining need under the Certificate Policy Statement, the Commission proposes, in considering requests for market-based rate authority under new NGA section 4(f), to balance the obvious benefits of additional storage capacity in areas needing storage services against any adverse impacts which might arise from the potential exercise of market power by the storage provider. The Commission is concerned that to the extent unnecessary conditions are imposed, the additional storage infrastructure and the additional service options they create would be lost to the detriment of potential customers. Accordingly, the Commission seeks comment on methods of customer protection which will allow it to achieve the desired balance.

42. The appropriate method of customer protection may well vary depending on the facts and circumstances of individual project proposals. Thus, the Commission proposes to allow each applicant to propose a method of protecting customers best suited to its project. However, the Commission seeks comments on whether it would be beneficial to identify in this rulemaking certain acceptable approaches. Establishment of generic safeguards would facilitate the application process for NGA section 4(f) market-based rate authority. Each applicant, however, would retain the right to propose another method of protecting customers that might better fit the circumstances of

<sup>32</sup> See *Pine Prairie Energy Center, LLC*, 109 FERC ¶ 61,215 at P 21 (2004).

its project. The Commission seeks suggestions of possible generic safeguards, as well as comments on the methods described below.

43. Entities with market power can exercise that power in two general areas: (1) The withholding of capacity; and (2) the extraction of monopoly rents. Thus, there are two approaches to protecting customers against the exercise of market power: (i) Conditions that limit the withholding of capacity and (ii) rate protections. We seek comment on whether there are generic safeguards in either method that would fairly balance the interests of consumers with the economic considerations relevant to financing new storage projects. As a general matter, we favor customer protections that are clear, easy to implement and oversee, and provide certainty to an applicant that is sufficient to support financing of a storage project.

44. One approach to customer protection is restrictions on withholding capacity. Market power can be exercised in those circumstances where a storage operator can withhold capacity from the market and raise prices. As long as storage capacity has not been withheld, "the fact that shippers may at times bid up contract length likely reflects not an exercise of [the pipeline's] market power, but rather competition for scarce capacity."<sup>33</sup> We seek comment whether by ensuring that the storage operator has sold or made available to the market all of its capacity (and thus it is not withholding capacity), customers can be assured that market power is not being exercised by the storage service provider and that any increase in price is due to customers' demand for storage relative to the available supply.<sup>34</sup>

45. A difficulty in applying this standard is in defining when withholding should be found to be indicative of the exercise of market power. The Commission requests comment on how to apply a prohibition against withholding which balances the competing needs of the project sponsor to secure revenues adequate to attract necessary investment in new infrastructure and of the needs of customers to be protected from the abuse of market power. For example, would allowing the storage operator to set a reserve price provide an appropriate balance? Should the withholding prohibition apply all the time, or only during periods of peak

demand for storage services? If the Commission were to allow such conditions, how should terms such as "reserve price" (a minimum price below which the storage operator is not required to sell capacity) and "period of peak demand" be defined?<sup>35</sup> Should a formal auction process under which the applicant is obligated to sell all capacity above a reserve price be considered?

46. Market power can be exercised in those circumstances where a storage operator can extract monopoly rents. Rate protections could take several forms. For example, rate caps could be designed to provide adequate customer protection while also supporting the financing of new storage projects. We seek comment on whether there are certain approaches to rate caps that could be adopted as a generic safeguard. As another example, the Commission could allow an applicant to establish a long-term (e.g., 5–10 years) recourse rate that was cost-based and allow the applicant to negotiate contracts under market-based rates for shorter-term transactions. Would this approach be sufficient to protect customers without imposing an undue burden on the financing of new storage projects? Are there other cost-based rate designs or price cap methodologies that the Commission should consider to be generally acceptable if proposed by an applicant under this program?

#### 4. Periodic Review

47. New NGA section 4(f) also requires that, for those entities granted market-based rates under this authority, the Commission "review periodically whether the market-based rate is just, reasonable, and not unduly discriminatory or preferential."

48. The Commission believes that to encourage the construction of new storage infrastructure, it must balance the benefits of the additional options new storage will bring to wholesale customers against the burdens of various forms of periodic review. Certain forms of periodic reviews may deter applicants from pursuing projects by introducing an unnecessary element of regulatory uncertainty. Should this happen, additional storage infrastructure and the additional service options it creates would be lost to the detriment of wholesale customers.

49. For market-based rates approved under NGA section 4(f), the Commission believes that the periodic review requirement should focus on the consumer protection safeguards adopted and ensure that these safeguards are working as intended and effectively preventing the storage provider from exercising significant market power. In the Commission's view, an effective approach of complying with the periodic review requirement is through regular monitoring and taking appropriate action under section 5 of the NGA either sua sponte or in response to a complaint. In cases where the consumer protection requirements imposed prohibit withholding, the Commission believes the existing § 284.13 posting requirements and storage reports combined with publicly available information regularly reviewed by Staff are sufficient for this purpose. These require that interstate storage operators post information about transactions and available capacity, and require the submission of quarterly index of customers' reports, and submission of semi-annual storage reports to the Commission. Those storage operators providing service only under NGPA section 311 are subject to fewer reporting requirements set forth in § 284.126, which requires an annual transaction report, and a semi-annual storage report.

50. Therefore, existing posting requirements on contractual obligations, including prices charged, and levels of available capacity should provide the information for monitoring whether storage operators have been exercising market power by withholding. This information is currently required of all open-access transporters and storage operators. Should concerns be raised about the practices of any storage provider charging market-based rates authorized by this Commission, this information along with more specific information required during the course of any necessary inquiry in a specific case will provide the Commission with the information needed to ensure that rates conform to the statutory requirement. Similarly, the Commission believes that the lesser burden imposed on NGPA section 311 storage providers, which are primarily regulated by state authorities, is also adequate for this purpose. The Commission believes this monitoring approach adequately complies with the periodic review requirement in NGA section 4(f).

51. The Commission requests comment on this approach and whether this type of periodic review should be enhanced by other reporting or transparency requirements. Comments

<sup>33</sup> *Process Gas Consumers Group v. FERC*, 292 F.3d 831, 837 (D.C. Cir. 2002).

<sup>34</sup> *Id.* (affirming Commission determination that prices determined through an uncapped bidding process were the product of competitive forces, not the exercise of market power.)

<sup>35</sup> The Commission has long recognized that open access pipelines are not required to sell capacity at rates below the maximum cost-based rate. This form of withholding balances the pipeline's right to compensatory rates against the customer protections required by the Natural Gas Act. However, under market-based rates there is no clear point at which these conflicting interests may be easily balanced.



should discuss with specificity how other requirements might be imposed without unduly deterring needed new storage infrastructure investment. Moreover, the Commission seeks comment on whether the applicant should be required to demonstrate the continued adequacy of its existing customer protections every five years. Additionally, in cases where the Commission adopts customer protection safeguards other than withholding, the Commission intends to consider whether additional reporting is necessary to effectively monitor and review whether the market-based rate is just and reasonable.

52. The Commission, therefore, proposes to revise its part 284 regulations as follows. New subpart M will be added, which addresses applications for market-based rates for storage. Within new subpart M, § 284.501, Applicability, explains which pipelines or storage service providers are eligible to apply for market-based rates under subpart M, § 284.502, Procedures for applying for market-based rates, explains what procedures must be followed for submitting an application. Section 284.503, Market-power determination, explains what must be submitted as part of an application for market-based rates, including what information must be submitted related to an applicant's market power. Section 284.504, Periodic review for market power determinations, requires the filing of updated market-power analyses by storage providers granted the authority to charge market-based rates every five years. Section 284.505, Market-based rates for storage providers without a market-power determination, explains what a storage service provider that does not seek a market-power determination must submit to the

Commission in an application for market-based rates.

**IV. Information Collection Statement**

53. The Office of Management and Budget (OMB) regulations require that OMB approve certain reporting, record keeping, and public disclosure (collections of information) imposed by an agency.<sup>36</sup> Accordingly, pursuant to OMB regulations, the Commission is providing notice of its proposed information collections to OMB for review under section 3507(d) of the Paperwork Reduction Act of 1995.<sup>37</sup>

54. The Commission identifies the information provided under Part 284 subpart M as contained in FERC-545, FERC-546 and FERC-549.

55. Comments are solicited on the Commission's need for this information, whether the information will have practical utility, the accuracy of the provided burden estimates, ways to enhance the quality, utility, and clarity of the information to be collected, and any suggested methods for minimizing respondent's burden, including the use of automated information techniques.

56. The burden estimates for complying with additional filing requirements of this rule pursuant to the procedures in proposed new sections 284.503 and 284.505 are set forth below. For the most part, the burden on applicants seeking market-based rates for open-access storage services will not be changed by this proposed rule. Since 1996, applications for authority to charge market-based rates have been filed under the Commission's procedures applicable to NGA section 7 initial rate determinations, NGA section 4 rate changes, or NGPA section 311 rate determinations under the Commission's existing data collection authorities. This rule codifies application procedures and filing requirements which are little

changed from the process followed since 1996. Codification of filing requirements will allow applicants to know what information must be filed with such an application and should reduce the need for staff to send out follow-up data requests and respondents to file data responses. To the extent respondents seek market-based rate authority under the new NGA section 4(f) authorization process, also codified in these regulations, the burdens may be lower than if they had filed to seek authorization under the Commission's 1996 Policy Statement. On average, we expect the burden of making an application for authority to charge market-based rates under this proposed rule to be 350 hours.

57. Applicants granted market-based rate approval after the effective date of a final rule will also be required pursuant to proposed new § 284.504 to file an updated market power analysis once every five years. The burden of this requirement will be imposed on all who operate under market-based rate authorizations granted on the basis of a market power determination. On average, we expect the burden of filing an updated market power analysis under this proposed rule to be 350 hours, imposed once every five years.

58. Over the past several years the Commission has approved market-based rates for storage services at an average pace of about 4.5 per year. The Commission is issuing this proposed rule in hopes that more storage will be constructed and operated, especially in underserved areas. In reflection of this policy goal, the Commission estimates that up to 10 filings may be made in a typical year. While this estimate may be high, in light of recent experience, at worst the Commission is overestimating the burden.

Data collection	Number of respondents	Number of responses per respondent	Hours per response	Total annual hours
FERC-545, FERC-546, or FERC-549 .....	10	1	350	3,500

*Total Annual Hours for Collection:* 3,500 hours.

59. *Information Collection Costs:* The Commission seeks comments on the cost to comply with these requirements. It has projected the average annualized cost for all respondents to be \$280,000 (3,500 hours x \$80.00 per hour).

60. *Title:* Gas Pipeline Rates: Rate Change (FERC-545); Certificated Rate Filings: Gas Pipeline Rates (FERC-546);

and Gas Pipeline Rates: NGPA Title III Transactions (FERC-549).

61. *Action:* Proposed Information Collection.

62. *OMB Control Nos.:* 1902-0154, 1902-0155 and 1902-0086

63. The applicant shall not be penalized for failure to respond to these collections of information unless the collections of information display valid OMB control numbers.

64. *Respondents:* Business or other for profit.

65. *Frequency of Responses:* On occasion.

66. *Necessity of Information:* On August 8, 2005, Congress enacted EPA Act 2005. Section 312 of EPA Act 2005 amends the NGA to insert a new section, 4(f), which allows the Commission to permit natural gas storage service providers authority to

<sup>36</sup> 5 CFR 1320.11 (2005).

<sup>37</sup> 44 U.S.C. 3507(d) (2000).



charge market-based rates, subject to conditions and requirements set forth in the statute. The Commission considers the issuance of these regulations necessary to implement this Congressional mandate and to encourage the development of new natural gas storage facilities. The proposed rule updates the Commission's market power analysis to better reflect the competitive alternatives to storage available in today's wholesale natural gas marketplace. These changes should ease the applicant's burden in showing that a Commission grant of market-based rate authority is appropriate, thus encouraging the construction and operation of needed new storage infrastructure. While the new requirement for respondents to file an update of its market power analysis imposes a modest new burden, this will allow the Commission to ensure that customers will be protected from abuse of market power. In addition, the proposed rule in implementing EPA Act 2005 creates regulations that allow qualifying storage providers to seek authority to charge market-based rates when the providers cannot or do not demonstrate they lack market power. The proposed rule revises the requirements contained in 18 CFR Part 284 to add a new subpart M to require that applications by storage providers requesting market-based rates contain certain information including a method for protecting customers and a showing of why market-based rates are necessary to encourage storage services.

67. *Internal Review:* The Commission has assured itself, by means of internal review, that there is specific, objective support for the burden estimates associated with the information requirements. The Commission staff will review the data included in the application to determine whether the proposed rates are in the public interest as well as for general industry oversight. Evidence establishing that market-based rates are necessary to encourage the construction of storage capacity is sufficient to also demonstrate that market-based rates are in the public interest. The Commission staff will review periodically the transactional and operational information provided by those granted authority to charge market-based rates pursuant to NGA section 4(f) to determine "whether the market-based rate is just, reasonable, and not unduly discriminatory or preferential." These requirements conform to the Commission's plan for efficient information collection,

communication and management within the natural gas industry.

68. Interested persons may obtain information on the reporting requirements by contacting the following: Federal Energy Regulatory Commission, 888 First Street, NE, Washington, DC 20426 (Attention: Michael Miller, Office of the Executive Director, 202-502-8415, fax: 202-273-0873, e-mail: [michael.miller@ferc.gov](mailto:michael.miller@ferc.gov)).

69. For submitting comments concerning the collection of information and the associated burden estimate(s) including suggestions for reducing this burden, please send your comments to the contact listed above and to the Office of Management and Budget, Room 10202 NEOB, 725 17th Street, NW., Washington, DC 20503 (Attention: Desk Officer for the Federal Energy Regulatory Commission, 202-395-4650, fax: 202-395-7285).

#### V. Environmental Analysis

70. The Commission is required to prepare an Environmental Assessment or an Environmental Impact Statement for any action that may have a significant adverse effect on the human environment.<sup>38</sup> The Commission has categorically excluded certain actions from these requirements as not having a significant effect on the human environment.<sup>39</sup> The actions proposed to be taken here fall within categorical exclusions in the Commission's regulations for rules that are clarifying, corrective, or procedural, for information gathering, analysis, and dissemination, and for sales, exchange, and transportation of natural gas that requires no construction of facilities.<sup>40</sup> Therefore, an environmental review is unnecessary and has not been prepared in this rulemaking. We note that environmental review will be prepared in each proceeding in which an applicant requests authority to construct facilities that might become subject to the rate-setting requirements of this rule.

#### VI. Regulatory Flexibility Act Certification

71. The Regulatory Flexibility Act of 1980 (RFA)<sup>41</sup> generally requires a description and analysis of the impact the proposed rule will have on small entities or a certification that the proposed rule will not have significant

<sup>38</sup> Order No. 486, Regulations Implementing the National Environmental Policy Act, 52 FR 47897 (Dec. 17, 1987), FERC Stats. & Regs. Preambles 1986-1990 ¶ 30,783 (1987).

<sup>39</sup> 18 CFR 380.4 (2005).

<sup>40</sup> See 18 CFR 380.4(a)(2)(ii), 380.4(a)(5), 380.4(a)(27) (2005).

<sup>41</sup> 5 U.S.C. 601-612.

economic impact on a substantial number of small entities. However, the RFA does not define "significant" or "substantial" instead leaving it up to an agency to determine the impacts of its regulations on small entities. In determining the impacts, the RFA proposes that agencies consider alternatives that are less burdensome to small entities and an explanation of why an alternative was rejected. The RFA provides four examples of alternatives including tiering, classification and simplification, performance rather than design standards, and exemptions or waivers. The Small Business size classification standard for natural gas storage operators is that their revenues are not in excess of \$6 million per year.<sup>42</sup> In the Commission's experience, it has found that the smallest entity applying for a market-based storage application had projected revenues that exceeded the SBA standard. Agencies are not required to make such an analysis if a rule would not have a significant adverse impact on a substantial number of small entities. The Commission does not believe that this proposed rule would have such an effect on small business entities, since the proposed amendments to our regulations would apply only to natural gas companies, most of which are not small businesses. However, should a small entity believe that this rule will have a significant impact on them, they may apply to the Commission for a waiver. Accordingly, pursuant to section 605(b) of the RFA, the Commission proposes to certify that the regulations proposed herein will not have a significant adverse impact on a substantial number of small entities.

#### VII. Comment Procedures

72. The Commission invites interested persons to submit comments on the matters and issues proposed in this notice to be adopted, including any related matters or alternative proposals that commenters may wish to discuss. Comments are due February 27, 2006. Comments must refer to Docket Nos. RM05-23-000 and AD04-11-000, and must include the commenter's name, the organization they represent, if applicable, and their address in their comments. Comments may be filed either in electronic or paper format.

73. Comments may be filed electronically via the eFiling link on the Commission's Web site at <http://www.ferc.gov>. The Commission accepts most standard word processing formats and commenters may attach additional files with supporting information in

<sup>42</sup> <http://www.sba.gov/size/sizetable2002.html>.

certain other file formats. Commenters filing electronically do not need to make a paper filing. Commenters that are not able to file comments electronically must send an original and 14 copies of their comments to: Federal Energy Regulatory Commission, Office of the Secretary, 888 First Street, NE., Washington, DC 20426.

74. All comments will be placed in the Commission's public files and may be viewed, printed, or downloaded remotely as described in the Document Availability section below. Commenters on this proposal are not required to serve copies of their comments on other commenters.

### VIII. Document Availability

75. In addition to publishing the full text of this document in the **Federal Register**, the Commission provides all interested persons an opportunity to view and/or print the contents of this document via the Internet through FERC's Home Page (<http://www.ferc.gov>) and in FERC's Public Reference Room during normal business hours (8:30 a.m. to 5 p.m. Eastern time) at 888 First Street, NE., Room 2A, Washington DC 20426.

76. From FERC's Home Page on the Internet, this information is available in the Commission's document management system, eLibrary. The full text of this document is available on eLibrary in PDF and Microsoft Word format for viewing, printing, and/or downloading. To access this document in eLibrary, type the docket number excluding the last three digits of this document in the docket number field.

77. User assistance is available for eLibrary and the FERC's website during normal business hours. For assistance, please contact FERC Online Support at 1-866-208-3676 (toll free) or 202-502-6652 (e-mail at [FERCOnlineSupport@ferc.gov](mailto:FERCOnlineSupport@ferc.gov)), or the Public Reference Room at 202-502-8371, TTY 202-502-8659 (e-mail at [public.referenceroom@ferc.gov](mailto:public.referenceroom@ferc.gov)).

### List of Subjects in 18 CFR Part 284

Continental shelf, Incorporation by reference, Natural gas, Reporting and recordkeeping requirements.

By direction of the Commission.

**Magalie R. Salas,**  
Secretary.

In consideration of the foregoing, the Commission proposes to amend part 284, Chapter I, Title 18, Code of Federal Regulations, as set forth below.

### PART 284—CERTAIN SALES AND TRANSPORTATION OF NATURAL GAS UNDER THE NATURAL GAS POLICY ACT OF 1978 AND RELATED AUTHORITIES

1. The authority citation for part 284 continues to read as follows:

**Authority:** 15 U.S.C. 717-717w, 3301-3432; 42 U.S.C. 7101-7352; 43 U.S.C 1331-1356.

2. New subpart M is added to read as follows:

#### Subpart M—Applications for Market-Based Rates for Storage

Sec.

284.501 Applicability.

284.502 Procedures for applying for market-based rates.

284.503 Market power determination.

284.504 Periodic review requirement for market power determinations.

284.505 Market-based rates for storage providers without a market-power determination.

#### § 284.501 Applicability.

Any pipeline or storage service provider that provides or will provide service under subparts B, C, and G of this part, and that wishes to provide storage and storage-related services at market-based rates must conform to the requirements in subpart M.

#### § 284.502 Procedures for applying for market-based rates.

(a) Applications for market-based rates may be filed with certificate applications. Service, notice, intervention, and protest procedures for such filings will conform with those applicable to the certificate application.

(b) With respect to applications not filed as part of certificate applications,

(1) Applicants providing service under subpart B or subpart G of this part must file a request for declaratory order and comply with the service and filing requirements of part 154 of this chapter. Interventions and protest to applications for market-based rates must be filed within 30 days of the application unless the notice issued by the Commission provides otherwise.

(2) Applicants providing service under subpart C of this part must file in accordance with the requirements of that subpart.

(c) An applicant cannot charge market-based rates under this subpart of this part until its application has been accepted by the Commission. Once accepted, the applicant can make the appropriate filing necessary to set its market-based rates into effect.

#### § 284.503 Market power determination.

An applicant may apply for market-based rates by filing a request for a market power determination that complies with the following:

(a) The applicant must set forth its specific request and adequately demonstrate that it lacks market power in the market to be served, and must include an executive summary of its statement of position and a statement of material facts in addition to its complete statement of position. The statement of material facts must include citation to the supporting statements, exhibits, affidavits, and prepared testimony.

(b) The applicant must include with its application the following information:

(1) *Statement A—geographic market.* This statement must describe the geographic markets for storage services in which the applicant seeks to establish that it lacks significant market power. It must include the market related to the service for which it proposes to charge market-based rates. The statement must explain why the applicant's method for selecting the geographic markets is appropriate.

(2) *Statement B—product market.* This statement must identify the product market or markets for which the applicant seeks to establish that it lacks significant market power. The statement must explain why the particular product definition is appropriate.

(3) *Statement C—the applicant's facilities and services.* This statement must describe the applicant's own facilities and services, and those of all parent, subsidiary, or affiliated companies, in the relevant markets identified in Statements A and B in paragraphs (b) (1) and (2) of this section. The statement must include all pertinent data about the storage facilities and services.

(4) *Statement D—competitive alternatives.* This statement must describe available alternatives in competition with the applicant in the relevant markets and other competition constraining the applicant's rates in those markets. Such proposed alternatives may include other storage, local gas supply, LNG, and pipeline capacity. These alternatives must be shown to be reasonably available as a substitute in the area to be served soon enough, at a price low enough, and with a quality high enough to be a reasonable alternative to the applicant's services. Available capacity (transportation, storage, LNG, or production) owned or controlled by affiliates of the applicant in the relevant market shall be clearly and fully identified and may not be considered as alternatives competing

with the applicant. Rather, the capacity of an applicant's affiliates is to be included in the market share calculated for the applicant. To the extent available, the statement must include all pertinent data about storage or other alternatives and other constraining competition.

(5) *Statement E—potential competition.* This statement must describe potential competition in the relevant markets. To the extent available, the statement must include data about the potential competitors, including their costs, and their distance in miles from the applicant's facilities and major consuming markets. This statement must also describe any relevant barriers to entry and the applicant's assessment of whether ease of entry is an effective counter to attempts to exercise market power in the relevant markets.

(6) *Statement F—maps.* This statement must consist of maps showing the applicant's principal facilities, pipelines to which the applicant intends to interconnect and other pipelines within the area to be served, the direction of flow of each line, the location of the alternatives to the applicant's service offerings, including their distance in miles from the applicant's facility. The statement must include a general system map and maps by geographic markets. The information required by this statement may be on separate pages.

(7) *Statement G—market power measures.* This statement must set forth the calculation of the market concentration of the relevant markets using the Herfindahl-Hirschman Index. The statement must also set forth the applicant's market share, inclusive of affiliated service offerings, in the markets to be served. The statement must also set forth the calculation of other market power measures relied on by the applicant. The statement must include complete particulars about the applicant's calculations.

(8) *Statement H—other factors.* This statement must describe any other factors that bear on the issue of whether the applicant lacks significant market power in the relevant markets. The description must explain why those other factors are pertinent.

(9) *Statement I—prepared testimony.* This statement must include the proposed testimony in support of the application and will serve as the applicant's case-in-chief, if the Commission sets the application for hearing. The proposed witness must subscribe to the testimony and swear that all statements of fact contained in the proposed testimony are true and

correct to the best of his or her knowledge, information, and belief.

**§ 284.504 Periodic review requirement for market power determinations.**

Applicants granted the authority to charge market-based rates under § 284.503 are required to file an updated market-power analysis within five years of the date of the Commission order granting authority to charge market-based rates, and every five years thereafter.

**§ 284.505 Market-based rates for storage providers without a market-power determination.**

(a) Any storage service provider seeking market-based rates for storage capacity, pursuant to the authority of Section 4(f) of the Natural Gas Act, related to a specific facility put into service after August 8, 2005, may apply for market-based rates by complying with the following requirements:

(1) The storage service provider must demonstrate that market-based rates are necessary to encourage the construction of the storage capacity in the area needing storage services; and

(2) The storage service provider must provide a means of protecting customers from the potential exercise of market power.

(b) Any storage service provider seeking market-based rates for storage capacity pursuant to this section will be presumed by the Commission to have market power.

[FR Doc. E5-8031 Filed 12-28-05; 8:45 am]

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**DEPARTMENT OF THE INTERIOR**

**National Park Service**

**36 CFR Part 7**

**RIN 1024-AD44**

**Cape Lookout National Seashore, Personal Watercraft Use**

**AGENCY:** National Park Service, Interior.  
**ACTION:** Proposed rule.

**SUMMARY:** The National Park Service (NPS) is proposing to designate areas where personal watercraft (PWC) may be used in Cape Lookout National Seashore, North Carolina. This proposed rule implements the provisions of the NPS general regulations authorizing park areas to allow the use of PWC by promulgating a special regulation. The NPS Management Policies 2001 directs individual parks to determine whether PWC use is appropriate for a specific park area based on an evaluation of that

area's enabling legislation, resources and values, other visitor uses, and overall management objectives.

**DATES:** Comments must be received by February 27, 2006.

**ADDRESSES:** You may submit comments, identified by the number RIN 1024-AD44, by any of the following methods:

- Federal rulemaking portal: <http://www.regulations.gov> Follow the instructions for submitting comments.
- Mail or hand delivery to:

Superintendent, Cape Lookout National Seashore, 131 Charles Street, Harkers Island, NC 28531.

• For additional information see "Public Participation" under **SUPPLEMENTARY INFORMATION** below.

**FOR FURTHER INFORMATION CONTACT:** Jerry Case, Regulations Program Manager, National Park Service, 1849 C Street, NW., Room 7241, Washington, DC 20240. Phone: (202) 208-4206. E-mail: [jerry\\_case@nps.gov](mailto:jerry_case@nps.gov).

**SUPPLEMENTARY INFORMATION:**

**Background**

*Additional Alternatives*

The information contained in this proposed rule supports implementation of portions of the preferred alternative in the Environmental Assessment (EA) published January 2005. The public should be aware that two other alternatives were presented in the EA, including a no-PWC alternative, and those alternatives should also be reviewed and considered when making comments on this proposed rule.

*Personal Watercraft Regulation*

On March 21, 2000, the NPS published a regulation (36 CFR 3.24) on the management of PWC use within all units of the national park system (65 FR 15077). This regulation prohibits PWC use in all national park units unless the NPS determines that this type of water-based recreational activity is appropriate for the specific park unit based on the legislation establishing that park, the park's resources and values, other visitor uses of the area, and overall management objectives. The regulation banned PWC use in all park units effective April 20, 2000, except for 21 parks, lakeshores, seashores, and recreation areas. The regulation established a 2-year grace period following the final rule publication to provide these 21 park units time to consider whether PWC use should be permitted to continue.

*Description of Cape Lookout National Seashore*

Cape Lookout National Seashore was established by Congress in 1966 to