

123 FERC ¶ 61,286
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

18 CFR Part 284

(Docket No. RM08-1-000; Order No. 712)

Promotion of a More Efficient Capacity Release Market

(Issued June 19, 2008)

AGENCY: Federal Energy Regulatory Commission.

ACTION: Final Rule.

SUMMARY: In this Final Rule the Federal Energy Regulatory Commission revises its regulations governing interstate natural gas pipelines to reflect changes in the market for short-term transportation services on pipelines and to improve the efficiency of the Commission's capacity release program. The Commission permits market based pricing for short-term capacity releases and facilitates asset management arrangements by relaxing the Commission's prohibition on tying and on its bidding requirements for certain capacity releases. The Commission further clarifies that its prohibition on tying does not apply to conditions associated with gas inventory held in storage for releases of firm storage capacity. Finally, the Commission waives its prohibition on tying and bidding requirements for capacity releases made as part of state-approved retail open access programs.

EFFECTIVE DATE: This rule will become effective 30 days after publication in the FEDERAL REGISTER.

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SUPPLEMENTARY INFORMATION:

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Docket No. RM08-1-000

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FINAL RULE

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FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeem G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Promotion of a More Efficient Capacity Release
Market

Docket No. RM08-1-000

ORDER NO. 712

FINAL RULE

(Issued June 19, 2008)

1. In this Final Rule, the Commission revises its Part 284 regulations concerning the release of firm capacity by shippers on interstate natural gas pipelines. First, as proposed in its Notice of Proposed Rulemaking,¹ the Commission will remove, on a permanent basis, the rate ceiling on capacity release transactions of one year or less. Second, the Commission will modify its regulations to facilitate the use of asset management arrangements (AMAs), under which a capacity holder releases some or all of its pipeline capacity to an asset manager who agrees to either purchase from, or supply the gas needs of, the capacity holder. Specifically, the Commission will exempt capacity releases made as part of AMAs from the prohibition on tying and from the bidding requirements of section 284.8. Third, the Commission clarifies that its prohibition on tying does not

¹ Promotion of a More Efficient Capacity Release Market, 72 Fed. Reg. 65,916, FERC Stats. and Regs. ¶ 32,625 (November 26, 2007) 121 FERC ¶ 61,170 (2007) (NOPR).

apply to conditions associated with gas inventory held in storage for releases of firm storage capacity. Fourth, the Commission will modify its regulations to facilitate retail open access programs by exempting capacity releases made under state-approved retail access programs from the prohibition on tying and from the bidding requirements of section 284.8. This Final Rule is designed to enhance competition in the secondary capacity release market and to increase shipper gas supply options. This rule will become effective 30 days after publication in the Federal Register.

I. Background

A. The Capacity Release Program

2. The Commission adopted its capacity release program as part of the restructuring of natural gas pipelines required by Order No. 636.² In Order No. 636, the Commission sought to foster two primary goals. The first goal was to ensure that all shippers have meaningful access to the pipeline transportation grid so that willing buyers and sellers can meet in a competitive, national market to transact the most efficient deals possible.

² Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, Order No. 636, 57 Fed. Reg. 13,267 (April 16, 1992), FERC Stats. and Regs., Regulations Preambles January 1991 - June 1996 ¶ 30,939 (April 8, 1992), order on reh'g, Order No. 636-A., 57 Fed. Reg. 36,128 (August 12, 1992), FERC Stats. and Regs., Regulations Preambles January 1991 - June 1996 ¶ 30,950 (August 3, 1992), order on reh'g, Order No. 636-B, 57 Fed. Reg. 57,911 (Dec. 8, 1992), 61 FERC ¶ 61,272 (1992), notice of denial of reh'g, 62 FERC ¶ 61,007 (1993); aff'd in part, 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).

The second goal was to ensure consumers have “access to an adequate supply of gas at a reasonable price.”³

3. To accomplish these goals, the Commission sought to maximize the availability of unbundled firm transportation service to all participants in the gas commodity market.

The linchpin of Order No. 636 was the requirement that pipelines unbundle their transportation and storage services from their sales service, so that gas purchasers could obtain the same high quality firm transportation service whether they purchased from the pipeline or another gas seller. In order to create a transparent program for the reallocation of interstate pipeline capacity to complement the unbundled, open access environment created by Order No. 636, the Commission also adopted a comprehensive capacity release program to increase the availability of unbundled firm transportation capacity by permitting firm shippers to release their capacity to others when they were not using it.⁴

4. The Commission reasoned that the capacity release program would promote efficient load management by the pipeline and its customers and would, therefore, result

³ Order No. 636 at 30,393 (citations omitted).

⁴ In brief, under the Commission’s current capacity release program, a firm shipper (releasing shipper) sells its capacity by returning its capacity to the pipeline for reassignment to the buyer (replacement shipper). The pipeline contracts with, and receives payment from, the replacement shipper and then issues a credit to the releasing shipper. The replacement shipper may pay less than the pipeline’s maximum tariff rate, but not more. 18 CFR 284.8(e) (2007). The results of all releases are posted by the pipeline on its Internet web site and made available through standardized, downloadable files.

in the efficient use of firm pipeline capacity throughout the year. It further concluded that, “because more buyers will be able to reach more sellers through firm transportation capacity, capacity reallocation comports with the goal of improving nondiscriminatory, open access transportation to maximize the benefits of the decontrol of natural gas at the wellhead and in the field.”⁵

5. In Order No. 636, the Commission expressed concerns regarding its ability to ensure that firm shippers would reallocate their capacity in a non-discriminatory manner to those who placed the highest value on the capacity up to the maximum rate. The Commission noted that prior to Order No. 636, it authorized some pipelines to permit their shippers to “broker” their capacity to others. Under such capacity brokering, firm shippers were permitted to assign their capacity directly to a replacement shipper, without any requirement that the brokering shipper post the availability of its capacity or allocate it to the highest bidder.⁶ However, in Order No. 636, the Commission found “there [were] too many potential assignors of capacity and too many different programs for the Commission to oversee capacity brokering.”⁷

⁵ Order No. 636 at 30,418.

⁶ See Algonquin Gas Transmission Corp., 59 FERC ¶ 61,032 (1992).

⁷ Order No. 636 at 30,416.

6. The Commission sought to ensure that the efficiencies of the secondary market were not frustrated by unduly discriminatory access to the market.⁸ Therefore, the Commission replaced capacity brokering with the capacity release program designed to provide greater assurance that transfers of capacity from one shipper to another were transparent and not unduly discriminatory. This assurance took the form of several conditions that the Commission placed on the transfer of capacity under its new program.

7. First, the Commission prohibited private transfers of capacity between shippers and, instead, required that all release transactions be conducted through the pipeline. Therefore, when a releasing shipper releases its capacity, the replacement shipper must enter into a contract directly with the pipeline, and the pipeline must post information regarding the contract, including any special conditions.⁹ In order to enforce the

⁸ Order No. 636-A at 30,554.

⁹ Order No. 636 emphasized:

The main difference between capacity brokering as it now exists and the new capacity release program is that under capacity brokering, the brokering customer could enter into and execute its own deals without involving the pipeline. Under capacity releasing, all offers must be put on the pipeline's electronic bulletin board and contracting is done directly with the pipeline. Order No. 636 at 30,420 (emphasis in original).

prohibition on private transfers of capacity, the Commission required that a shipper must have title to any gas that it ships on the pipeline.¹⁰

8. Second, the Commission determined that the record of the proceeding that led to Order No. 636 did not reflect that the market for released capacity was competitive. The Commission reasoned that the extent of competition in the secondary market may not be sufficient to ensure that the rates for released capacity will be just and reasonable. Therefore, the Commission imposed a ceiling on the rate that the releasing shipper could charge for the released capacity.¹¹ This ceiling was derived from the Commission-approved monthly maximum tariff rates, necessary for the pipeline to recover its annual cost-of-service revenue requirement.¹²

9. Third, the Commission required that capacity offered for release at less than the maximum rate must be posted for bidding, and the pipeline must allocate the capacity “to

¹⁰ As the Commission subsequently explained in Order No. 637, “the capacity release rules were designed with [the shipper-must-have-title] policy as their foundation,” because, without this requirement, “capacity holders could simply transport gas over the pipeline for another entity.” Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services, Order No. 637, FERC Stats. & Regs. ¶ 31,091 at 31,300, clarified, Order No. 637-A, FERC Stats. & Regs. ¶ 31,099, reh’g denied, Order No. 637-B, 92 FERC ¶ 61,062 (2000), aff’d in part and remanded in part sub nom. Interstate Natural Gas Ass’n of America v. FERC, 285 F.3d 18 (D.C. Cir. 2002), order on remand, 101 FERC ¶ 61,127 (2002), order on reh’g, 106 FERC ¶ 61,088 (2004), aff’d sub nom. American Gas Ass’n v. FERC, 428 F.3d 255 (D.C. Cir. 2005).

¹¹ Order No. 636-A at 30,560.

¹² Order No. 637 at 31,270-71.

the person offering the highest rate (not over the maximum rate).”¹³ The Commission permitted the releasing shipper to choose a pre-arranged replacement shipper who can retain the capacity by matching the highest bid rate. The bidding requirement, however, does not apply to releases of 31 days or less or to any release at the maximum rate. But all releases, whether or not subject to bidding, must be posted.¹⁴

10. Finally, the Commission prohibited tying the release of capacity to any extraneous conditions so that the releasing shippers could not attempt to add additional terms or conditions to the release of capacity. The Commission articulated the prohibition against the tying of capacity in Order No. 636-A, where it stated:

The Commission reiterates that all terms and conditions for capacity release must be posted and non-discriminatory and must relate solely to the details of acquiring transportation on the interstate pipelines. Release of capacity cannot be tied to any other conditions. Moreover, the Commission will not tolerate deals undertaken to avoid the notice requirements of the regulations. Order No. 636-A at 30, 559 (emphasis in the original).

11. Subsequent to the Commission’s adoption of its capacity release program in Order No. 636, the Commission conducted two experimental programs to provide more

¹³ 18 CFR 284.8(e) (2007) provides in pertinent part that “[t]he pipeline must allocate released capacity to the person offering the highest rate (not over the maximum rate) and offering to meet any other terms or conditions of the release.”

¹⁴ 18 CFR 284.8(h)(1) provides that a release of capacity for less than 31 days, or for any term at the maximum rate, need not comply with certain notification and bidding requirements, but that such release may not exceed the maximum rate. Notice of the release “must be provided on the pipeline’s electronic bulletin board as soon as possible, but not later than forty-eight hours, after the release transaction commences.”

flexibility in the capacity release market. In 1996, the Commission sought to establish an experimental program inviting individual shipper and pipeline applications to remove price ceilings related to capacity release.¹⁵ The Commission recognized that significant benefits could be realized through removal of the price ceiling in a competitive secondary market. Removal of the ceiling permits more efficient capacity utilization by permitting prices to rise to market clearing levels and by permitting those who place the highest value on the capacity to obtain it.¹⁶

12. In 2000, in Order No. 637, the Commission conducted a broader experiment in which the Commission removed the rate ceiling for short-term (less than one year) capacity release transactions for a two-year period ending September 30, 2002. In contrast to the experiment that it conducted in 1996, in the Order No. 637 experiment the Commission granted blanket authorization in order to permit all firm shippers on all open access pipelines to participate. The Commission stated that it undertook this experiment to improve shipper options and market efficiency during peak periods. The Commission reasoned that during peak periods, the maximum rate cap on capacity release transactions inhibits the creation of an effective transportation market by preventing capacity from going to those that value it the most and therefore the elimination of this rate ceiling

¹⁵ Secondary Market Transactions on Interstate Natural Gas Pipelines, Proposed Experimental Pilot Program to Relax the Price Cap for Secondary Market Transactions, 61 Fed. Reg. 41,401 (Aug. 8, 1996), 76 FERC ¶ 61,120, order on reh'g, 77 FERC ¶ 61,183 (1996).

¹⁶ 77 FERC ¶ 61,183 at 61,699 (1996).

would eliminate this inefficiency and enhance shipper options in the short-term marketplace.¹⁷

13. Upon an examination of pricing data on basis differentials between points,¹⁸ the Commission found that the price ceiling on capacity release transactions limited the capacity options of short-term shippers because firm capacity holders were able to avoid price ceilings on released capacity by substituting bundled sales transactions at market prices (where the market place value of transportation is an implicit component of the delivered price). As a consequence, the Commission determined that the price ceilings did not limit the prices paid by shippers in the short-term market as much as the ceilings limit transportation options for shippers. In short, the Commission found that the rate

¹⁷ Order No. 637 at 31,263. The Commission also explained why it was lifting the price cap on an experimental basis, instead of permanently, stating:

While the removal of the price cap is justified based on the record in this rulemaking, the Commission recognizes that this is a significant regulatory change that should be subject to ongoing review by the Commission and the industry. No matter how good the data suggesting that a regulatory change should be made, there is no substitute for reviewing the actual results of a regulatory action. The two year waiver will provide an opportunity for such a review after sufficient information is obtained to validly assess the results. Due to the variation between years in winter temperatures, the waiver will provide the Commission and the industry with two winter's worth of data with which to examine the effects of this policy change and determine whether changes or modifications may be needed prior to the expiration of the waiver. Order No. 637 at 31,279-80.

¹⁸ Among other things, the data showed that the value of pipeline capacity, as shown by basis differentials, was generally less than the pipelines' maximum interruptible transportation rates, except during the coldest days of the year, and capacity release prices also averaged somewhat less than pipelines' maximum interruptible rates.

ceiling worked against the interests of short-term shippers, because with the rate ceilings in place, a shipper looking for short-term capacity on a peak day who was willing to offer a higher price in order to obtain it, could not legally do so; this reduced its options for procuring short-term transportation at the times that it needed it most.¹⁹ Throughout this experiment, the Commission retained the rate ceiling for firm and interruptible capacity available from the pipeline as well as for long-term capacity release transactions.

14. On April 5, 2002, the United States Court of Appeals for the District of Columbia Circuit, in Interstate Natural Gas Association of America v. FERC,²⁰ upheld the Commission's experimental price ceiling program for short-term capacity release transactions as set forth in Order No. 637.²¹ The court found that the Commission's "light handed" approach to the regulation of capacity release prices was, given the safeguards that the Commission had imposed, consistent with the criteria set forth in Farmers Union

¹⁹ Order No. 637 at 31,280-81.

²⁰ 285 F.3d 18 (D.C. Cir. 2002) (INGAA).

²¹ Specifically, the court found that: "[g]iven the substantial showing that in this context competition has every reasonable prospect of preventing seriously monopolistic pricing, together with the non-cost advantages cited by the Commission and the experimental nature of this particular "light handed" regulation, we find the Commission's decision neither a violation of the NGA, nor arbitrary or capricious." INGAA at 35.

Cent. Exch. v. FERC.²² The court found that the Commission made a substantial record for the proposition that market rates would not materially exceed the “zone of reasonableness” required by Farmers Union. The court also found that the Commission’s inference of competition in the capacity release market was well founded, that the price spikes shown in the Commission’s data were consistent with competition and reflected scarcity of supply rather than monopoly power, and that outside of such price spikes, the rates were well below the estimated regulated price.²³ The Commission’s experiment in lifting the price ceiling for short term capacity releases ended on September 20, 2002.²⁴

B. The NOPR

15. On January 3, 2007, the Commission, in response to petitions from various gas industry participants concerning issues related to capacity releases,²⁵ issued a request for

²² 734 F.2d 1486 (D.C. Cir. 1984) (Farmers Union) (finding that a move from heavy-handed to light-handed regulation can be justified by a showing that under current circumstances, the goals and purposes of the Natural Gas Act (NGA) will be accomplished through substantially less regulatory oversight.

²³ Id. at 33.

²⁴ Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services, FERC Stats. & Regs., Regulations Preambles July 1996 - December 2000, ¶ 31,091 (Feb. 9, 2000), order on rehearing, Order No. 637-A, FERC Stats. & Regs., Regulations Preambles July 1996 - December 2000, ¶ 31,099 (May 19, 2000), order on rehearing, Order No. 637-B, 92 FERC ¶ 61,062 (July 26, 2000), aff’d in part and remanded in part, Interstate Natural Gas Association of America v. FERC, 285 F.3d 18 (D.C. Cir. Apr. 5, 2002).

²⁵ In August 2006, Pacific Gas and Electric Co. (PG&E) and Southwest Gas Corp. (Southwest) filed a petition requesting the Commission to amend sections 284.8(e) and (h)(1) of its regulations to remove the maximum rate cap on capacity releases.

(continued...)

comments on the operation of the capacity release program and whether changes in any of its capacity release policies would improve the efficiency of the natural gas market.²⁶

The Commission also included in its request for comments a series of questions asking whether the Commission should lift the price ceiling, remove its capacity release bidding requirements, modify its prohibition on tying arrangements, and/or remove the shipper-must-have-title requirement.

16. After review of the petitions, comments, responses to its questions, and available data, the Commission issued a Notice of Proposed Rulemaking (NOPR), proposing two major changes to its capacity release regulations and policies. First, the Commission proposed to lift the price ceiling for short-term capacity release transactions of one year or less. The Commission determined that the traditional cost-of-service price ceilings in pipeline tariffs, which are based on annual costs recovered over twelve equal monthly payments, are not well suited to the short-term capacity release market, because they do not reflect short-term variations in the market value of the capacity. Therefore, removing the price ceiling for short-term capacity releases would permit more efficient utilization of capacity by allowing prices to rise to market clearing levels, thereby permitting those who place the highest value on the capacity to obtain it. The Commission determined

Subsequently, in October 2006, a group of large natural gas marketers (Marketer Petitioners) requested clarification of the operation of the Commission's capacity release rules in the context of asset (or portfolio) management services.

²⁶ Pacific Gas & Electric Co., 118 FERC ¶ 61,005 (2007).

that the data obtained by the Commission both during the Order No. 637 experiment and more recently indicated that short-term release prices reflect market value of the capacity as revealed by basis differentials, rather than the exercise of market power. Moreover, the Commission reasoned that shippers purchasing capacity would be adequately protected because the pipeline's firm and interruptible services will provide just and reasonable recourse rates limiting the ability of releasing shippers to exercise market power. Finally, the Commission stated that reporting requirements in Order No. 637 and the Commission's implementation of the Energy Policy Act of 2005, specifically with respect to market manipulation, give the Commission an enhanced ability to monitor the market and detect and deter abuses. The Commission did not propose to remove the price ceiling on either long-term capacity releases or the pipelines' sale of their own primary capacity.

17. Second, the Commission proposed to revise its capacity release policies to give releasing shippers greater flexibility to negotiate and implement AMAs, based on the Commission's findings that AMAs provide significant benefits to participants in the natural gas and electric marketplaces.²⁷ Recognizing that the linking of transportation capacity with gas supply arrangements would violate the Commission's prohibition against "tying" released capacity to any extraneous conditions, the Commission proposed

²⁷ NOPR at P 67-74.

to exempt pre-arranged capacity release transactions that met certain criteria²⁸ from the prohibition against tying.²⁹ This proposal would permit a releasing shipper in a pre-arranged release to require that the replacement shipper agree to supply the releasing shipper's gas requirements and take assignment of the releasing shipper's gas supply contracts, as well as released transportation capacity on one or more pipelines and storage capacity with the gas currently in storage.³⁰

18. The Commission's second proposal to facilitate AMAs was to exempt pre-arranged releases to implement AMAs from competitive bidding.³¹ The Commission stated that, because the asset manager will manage the releasing shipper's gas supply operations on an ongoing basis, it is critical that the releasing shipper be able to release the capacity to its chosen asset manager. Requiring releases made in order to implement an AMA to be posted for bidding would thus interfere with the negotiation of beneficial AMAs by potentially preventing the releasing shipper from releasing the capacity to its

²⁸ The Commission's definition of AMA as proposed in the NOPR is discussed in detail below.

²⁹ NOPR at P 75-82.

³⁰ In addition, the releasing shipper could require that, upon expiration of the AMA, the replacement shipper must return storage capacity included in the release with an appropriate level of inventory, *e.g.*, to promise to replenish storage inventories to a mutually agreed upon level.

³¹ See NOPR at P 83-90. Section 284.8 of the Commission's regulations require capacity release transactions to be posted for competitive bidding unless the transactions are at the maximum tariff rate or are for a term of 31 days or less.

chosen asset manager. The Commission concluded that in the AMA context the bidding requirement creates an unwarranted obstacle to the efficient management of pipeline capacity and supply assets. The Commission emphasized that AMAs would remain subject to all existing posting and reporting requirements.³²

C. Comments

19. Over 60 entities from all segments of the natural gas industry filed comments on the NOPR. The vast majority of those who filed comments regarding the Commission's proposal to permanently remove the price cap for short-term capacity releases of one year or less support the proposal, generally agreeing with the Commission's reasoning in support of removing the cap. Many of the local distribution companies (LDC), marketers, producers, and end-users who support lifting the price cap on short-term capacity releases also support retaining the price cap on long-term capacity releases³³ and/or primary pipeline capacity.³⁴ These parties generally view retention of these price

³² While the NOPR originally required that any comments were due January 10, 2008, a number of entities filed for an extension of that deadline until February 8, 2008. On January 14, the Commission granted an extension of time for filing comments until January 25, 2008.

³³ Those commenters include Direct Energy Services LLC (Direct Energy), New Jersey Natural Gas Company (NJNG), Oklahoma Independent Petroleum Association (OIPA), Reliant Energy Inc. (Reliant), Statoil Natural Gas, LLC (Statoil), and Weyerhaeuser Company (Weyerhaeuser).

³⁴ Such commenters include Edison Electric Institute (EEI), NJNG, NJR Energy Services Company (NJR), Nstar Gas Company (Nstar), OIPA, Piedmont Natural Gas Company, Inc. (Piedmont), Statoil, Weyerhaeuser, and the Wisconsin Distributor Group

(continued...)

caps as providing valuable safeguards in preventing the exercise of market power in the uncapped short-term capacity release market.

20. Two commenters oppose the Commission's proposal to lift the price cap for the short-term capacity release market, arguing that the Commission has not supported its proposed rule and that the proposed rule would fail a cost-benefit test.³⁵ Other commenters express concern over the potential for capacity owners to exercise market power under the proposed rule.³⁶ For example, some end-users of gas express concerns about the concentration of capacity ownership on lateral pipelines and therefore argue that the Commission should either not remove the price cap for laterals or do so on a case-by-case basis.³⁷ Other parties generally urge the Commission to carefully monitor markets to ensure that they are functioning properly. Some suggest a final test period

(WDG). American Gas Association (AGA), American Public Gas Association (APGA), and Independent Petroleum Producers of America (IPAA) oppose lifting the price cap for primary capacity, arguing that doing so would undercut a major premise for lifting the price cap in the short-term secondary market, namely, that the availability of recourse rates from the pipeline will constrain the exercise of market power in the secondary market.

³⁵ Tenaska Marketing Ventures (Tenaska) and National Energy Marketers Association (NEM).

³⁶ See Comments of NEM.

³⁷ Weyerhaeuser, Northwest Industrial Gas Users (NWIGU), and Process Gas Consumers (PGC).

before permanently removing the cap, periodic reassessments of the uncapped market, or a process to revisit the determination if the market becomes dysfunctional.³⁸

21. In general, commenters also overwhelmingly supported the Commission's efforts to facilitate the development of AMAs.³⁹ Those commenters agree with the Commission's assessment that AMAs provide value and benefits to market participants and to natural gas markets overall. Virtually all who commented support the steps proposed by the Commission to facilitate AMAs, though many of those that support the Commission's proposal regarding AMAs request that the Commission modify or clarify

³⁸ Direct Energy, OIPA, Honeywell International, Inc. (Honeywell), Arizona Public Service Company (APS) (arguing that the market currently served by El Paso Natural Gas Pipeline east of California is not competitive). Commerce Energy Group, Inc. (Commerce Energy) suggests including a contingency for replacing the price cap in "exceptional capacity situations."

³⁹ See e.g., Comments of the AGA at 1-2, Comments of APGA at 2-4; Comments of Atmos Energy Corporation (Atmos) at 2-4, Comments of BG Energy Merchants (BGEM) at 1-2, Comments of BP Energy Company (BP) at 2, Comments of Direct Energy at 3-4, Comments of Duke Energy Corporation (Duke Energy) at 3, Comments of the EEI at 6, Comments of the Electric Power Supply Association (EPSA) at 2, Comments of Florida Cities at 2, Comments of the Interstate Natural Gas Association of America (INGAA) at 6, Comments of Marketer Petitioners at 2, Comments of National Grid Delivery Companies (National Grid) at 2, Comments of NJNG at 1, Comments of the Natural Gas Supply Association (NGSA) at 3, Comments of NJR at 1, Comments of NWIGU at 6, Comments of Nstar at 1-2, Comments of the Ohio Gas Marketers Group (OGMG) at 1, Comments of Piedmont at 1, Comments of PPM Energy, Inc., (PPM) at 1-3, Comments of PGC at 5, Comments of the Public Utilities Commission of Ohio (PUCO) at 5-7, Comments of Puget Sound Energy, Inc. (Puget Sound) at 8-9, Comments of Sequent Energy Management, L.P. (Sequent) at 5-6, Comments of the Financial Institutions Energy Group (FEIG) at 6-7, Comments of Turlock Irrigation District (Turlock) at 5, Comments of Ultra Petroleum Corporation (Ultra) at 4, Comments of the WDG at 3, and Comments of the Wyoming Pipeline Authority at 5.

the proposal in various ways in order to permit broader use of AMAs and greater flexibility in the terms of permitted AMAs. They request, for example, that the Commission permit uncapped AMA releases of a year or less to be rolled over without bidding, clarify that profit sharing arrangements in an AMA do not violate any applicable price cap, relax the requirements concerning the replacement shipper's obligation to deliver gas to the releasing shipper, exempt AMAs from the Commission's prohibition against buy/sell arrangements, and allow supply side AMAs. Williston Basin commented that exempting AMAs from the tying prohibition and bidding requirements would encourage discrimination against pipelines and provide preferential treatment to asset managers.

22. The Commission also received favorable comments on whether it should clarify its prohibition against tying agreements to allow a releasing shipper to include conditions in a storage release concerning the sale and/or repurchase of gas in storage inventory outside the AMA context. All comments that addressed this issue supported removing this prohibition for storage services. They assert that a shipper releasing storage capacity should be permitted to require the replacement shipper to take assignment of any gas that remains in the released storage capacity at the time the release takes effect; and/or to return the storage capacity to releasing shipper at end of the release with a specified

amount of gas in storage.⁴⁰ Commenters note that tying storage capacity with storage inventory will enable transactions to be consummated more readily and that the nature of the relationship between storage capacity and storage inventory calls out for a waiver of the tying rule. Others add that the ability of releasing shippers to “tie” storage capacity with storage inventory such that releasing shippers would be permitted to require that replacement shippers take inventory as a condition of release, even in circumstances outside the AMA context, will provide benefits to the marketplace similar to those provided by AMAs.⁴¹

23. The Commission also received numerous comments on its inquiry whether pre-arranged capacity release deals necessary to implement retail access programs should be treated as similar to releases made as part of an AMA, and thus accorded the same exemptions. The majority of comments on this issue advocated affording capacity releases under state retail choice programs the same blanket exemptions from the tying

⁴⁰ Public Service Commission of New York (PSCNY) comments at 20–21.

⁴¹ Comments of Marketer Petitioners.

prohibition⁴² and bidding requirements as those granted to asset managers.⁴³ AGA, for example, recommends that the Commission add an exemption from the bidding requirements for any prearranged, recallable capacity release from an LDC to a natural gas marketer in accordance with the terms of a retail choice program approved by a State commission. AGA also asks that the Commission clarify that LDC releases to retail choice marketers would be entitled to the same partial exemption from the tying prohibition as would be releases under AMAs. The SPSCNY would extend the AMA exemption from the tying prohibition to releases of storage capacity conducted according to state retail access programs.

II. Overview of the Final Rule

24. In this Final Rule, the Commission is modifying its policies and regulations concerning the release of capacity by firm shippers on interstate pipelines in order to enhance the efficiency and effectiveness of the secondary capacity release market. The Commission's capacity release program has created a successful secondary market for

⁴² Those commenters include AGA, Commerce Energy, Duke Energy, Hess Corporation (Hess), Interstate Gas Supply (IGS), NJNG, New York State Electric and Gas Corporation (NYSEG), Rochester Gas & Electric Corporation (RG&E), OGMG, the Public Service Commission of North Carolina (PSNC), South Carolina Electric and Gas Company (SCE&G), SCANA Energy Marketing (SEMI), PSCNY, and Sequent.

⁴³ Those commenters include the AGA, Boardwalk Pipeline Partners (Boardwalk), BP, Commerce Energy, Direct Energy, Duke Energy, FPL Energy, LLC (FPL Energy), Hess, IGS, NJNG, NYSEG, RG&E, Nstar, OGMG, Peoples Gas System, a Division of Tampa Electric Company (Peoples), PG&E, PSCNY, PUCO, SEMI, Sequent, and the WDG.

capacity.⁴⁴ As a result, natural gas markets in general, and the secondary release market in particular, have undergone significant development and change in the sixteen years since Order No. 636 and the inception of the capacity release program. As this market has developed, shippers and potential shippers have sought greater flexibility in the use of capacity. They seek to better integrate capacity with the underlying gas transactions, and are looking for more flexible methods of pricing capacity to better reflect the value of that capacity as revealed by the market price of gas at different trading points. They also seek to implement AMAs, in which capacity holders release their capacity to asset managers (generally marketers) that have greater expertise in maximizing the value of pipeline capacity and negotiating beneficial transactions in the gas commodity markets.

25. In this Final Rule the Commission is taking actions to respond to the industry's request for greater flexibility in the capacity release market and to revise its policies and regulations to reflect the changes and developments in the marketplace. The first major revision is the removal of the price ceiling on short term capacity releases. The permanent elimination of the price ceiling for short term releases will enable shippers to offer competitively-priced alternatives to pipelines' negotiated rate offerings and will permit short-term capacity release prices to rise to market clearing levels, thereby

⁴⁴ As the Commission observed in 2005, the "capacity release program together with the Commission's policies on segmentation, and flexible point rights, has been successful in creating a robust secondary market where pipelines must compete on price." Policy for Selective Discounting by Natural Gas Pipelines, 111 FERC ¶ 61,309, at P 39-41, order on reh'g, 113 FERC ¶ 61,173 (2005).

allocating capacity to those that value it the most. It will also provide more accurate price signals concerning the market value of pipeline capacity.

26. The Commission is also revising its regulations and policies to accommodate and facilitate AMAs, a relatively recent development in the industry. AMAs provide significant benefits to many participants in the natural gas and electric marketplaces and to the secondary marketplace itself. They maximize the utilization and value of capacity by creating a mechanism for capacity holders to use third party experts to both (1) manage their gas supply arrangements and (2) use that capacity to make gas sales or re-releases of the capacity to others when the capacity is not needed to serve the releasing shipper. AMAs result in ultimate savings for end-use customers by providing for lower gas supply costs and more efficient use of the pipeline grid.⁴⁵ The Commission's goal in facilitating AMAs in this rule is to make the capacity release program more efficient by bringing it into line with the realities of today's secondary gas marketplace.

27. To that end, the Commission in this rule is adopting its NOPR proposal to exempt capacity releases made to implement AMAs from the prohibition on tying and the bidding requirements of section 284.8. The Commission is also making several revisions to the definition of AMAs as proposed in the NOPR. The Final Rule modifies the definition of AMAs proposed in the NOPR to relax the delivery obligation of the replacement shipper to the releasing shipper and to permit supply side AMAs. The Final

⁴⁵ See Comments of BGEM at 2, Comments of BP at 5, Comments of Nstar at 8, Comments of Piedmont at 4-5, Comments of PUCO at 7, Comments of WDG at 3.

Rule also clarifies that short term AMAs may be rolled over without bidding. Further, the Final Rule clarifies that the price ceiling does not apply to any consideration provided by an asset manager to the releasing shipper as part of an AMA. These steps, requested by many industry commenters that support the Commission's efforts in the NOPR to facilitate AMA's, will further enhance the efficiency of AMAs by allowing greater flexibility for parties to customize arrangements to meet unique customer needs while at the same time ensuring that capacity releases that qualify for the exemptions from tying and bidding granted in this rule are bona fide AMAs. The rule also extends the benefits of AMAs to sellers of natural gas, creating an even greater diversity of potential suppliers and participants in the secondary market.

28. The Commission is also revising its policies to reflect the realities of today's marketplace by allowing a releasing shipper to include conditions in a release concerning the sale/and repurchase of gas in storage inventory, even outside the AMA context. Allowing such arrangements reflects the fact that in the storage context, storage capacity is inextricably linked to storage inventory. By permitting the tying of releases of storage capacity to conditions on storage inventory, the Commission will enhance the efficient use of storage capacity while at the same time ensuring that releasing shippers will have adequate storage inventories for the winter.

29. The Final Rule also extends the blanket exemptions from the prohibition against tying and from bidding granted to AMAs to capacity releases made to a marketer

participating in a state approved retail access program, finding that such programs provide benefits similar to AMAs.

III. Price Cap Issues

A. Removal of Maximum Rate Ceiling for Short-Term Capacity Releases

30. In this Final Rule, the Commission amends section 284.8 of its regulations to eliminate the price ceiling for short-term capacity release transactions of one year or less. The Commission finds that this action will improve shipper options and market efficiency, particularly during peak periods, by allowing the prices of short-term capacity release transactions to reflect short-term variations in the market value of that capacity. This will enable shippers to better integrate capacity with the underlying gas transactions, and will permit more flexible methods of pricing capacity to better reflect the value of that capacity as revealed by the market price of gas at different trading points. The Commission has previously provided pipelines with the flexibility to enter into negotiated rate transactions which are permitted to exceed the maximum rate ceiling, and this rule will permit releasing shippers similar flexibility in pricing release transactions.

31. At the same time, we are convinced that the rates resulting from removal of the price cap for capacity release will be just and reasonable. The data collected over many years shows that the value of short term capacity only exceeds the price ceiling in times when capacity is scarce. These data are confirmed by the data gathered during the experimental release of the price ceiling which showed that capacity release prices exceed the price ceiling only for brief periods of constraint. Moreover, we are not relying

solely on competition to ensure just and reasonable prices. We are maintaining the rate cap on pipeline services that will provide the same protection for capacity release transactions as it now does for pipeline negotiated rate transactions. Further, we have required informational postings of capacity release transactions that will provide transparency and facilitate the filing of complaints if circumstances warrant. The Commission will also continue to actively monitor the release market.

1. Maximum Rate Ceiling Interferes with Efficient Transactions

32. As we explained in Order No. 637,⁴⁶ the traditional cost-of-service maximum rates in pipeline tariffs are not well suited to the short-term capacity release market.⁴⁷ Under the traditional ratemaking methodology, the Commission develops a maximum annual transportation rate for each pipeline that, when applied to the pipeline's contract demand and throughput levels, will enable the pipeline to recover its annual cost-of-service revenue requirement. Each pipeline's maximum rates for services of less than a year are simply the maximum annual rate prorated over the shorter period.

33. Such prorated annual rates bear no relationship to the competitive rates that would be established in the short-term capacity market, particularly during peak periods. The market value of transportation service from the production area to the downstream market

⁴⁶ Order No. 637 at 31,271-75.

⁴⁷ While the Commission offered pipelines the opportunity to propose other types of rate designs, such as seasonal and term-differentiated rates, only a very few pipelines have sought to make such rate design changes, although many pipelines have taken advantage of negotiated rate authority.

may be inferred by comparing the downstream delivered gas price in bundled sales to the market price at upstream market centers in the production area.⁴⁸ As the D.C. Circuit recognized in INGAA, “if the difference between field prices and city gate prices in a particular pathway is only \$.07, people will not pay more than \$.07 for the unbundled transportation.”⁴⁹ As discussed in more detail below, the data set forth in Order No. 637 and the updated data in Figures 1 through 3 below concerning the implicit value of transportation in the bundled sales market demonstrates the variability of transportation value in the short-term market and the divergence between the transportation value and cost-of-service rates. This data shows that during most of the year, the value of transportation service is significantly less than the pipelines’ annual cost-of-service maximum transportation rates, but during brief, peak demand periods, the value of transportation service is measurably greater than the maximum transportation rates.

34. Because the existing capacity release price ceiling does not reflect short-term variations in the market value of the capacity, the price ceiling inhibits the efficient allocation of capacity and harms, rather than helps, the short-term shippers it is intended to protect. The price ceiling operates to prevent the shipper most valuing short-term

⁴⁸ In Order No. 637, the Commission explained “gas commodity markets now determine the economic value of pipeline services in many parts of the country. Thus, even as FERC has sought to isolate pipeline services from commodity sales, it is within the commodity markets that one can see revealed the true price for gas transportation.” Order No. 637 at 31,274 (quoting M. Barcella, How Commodity Markets Drive Gas Pipeline Values, Public Utilities Fortnightly, February 1, 1998 at 24-25).

⁴⁹ INGAA at 31.

capacity on a peak day from being able to obtain it, because that shipper cannot offer a releasing shipper the full value the shipper places on that capacity. The price ceiling may also reduce the amount of released capacity available during peak periods. As the Commission explained in Order No. 637, “As a result of the maximum rate, firm capacity holders may not find it sufficiently profitable to make their capacity available for release. For instance, a dual fuel industrial customer might determine that it would be more economic not to use gas, and to substitute a different fuel, if it could obtain a sufficiently high price for its released capacity.”⁵⁰ Thus, during a peak day the price ceiling may only serve to limit a purchasing shipper’s capacity options, with the result that it must purchase gas in a bundled transaction in the downstream market at a price reflecting the market-determined value of the transportation.

35. The increased use by pipelines and shippers of negotiated rate transactions based on gas price differentials demonstrates that buyers and sellers value the ability to calibrate the price of transportation to its value in the market. The maximum rate ceiling applied to capacity release transactions denies releasing and replacement shippers the same ability to negotiate transactions that reflect the market value of capacity at all times. As the Commission has found, providing the ability to negotiate capacity release transactions based on price differentials will help in providing short-term capacity to

⁵⁰ Order No. 637 at 31,279.

replacement shippers, such as gas-fired electric generators.⁵¹ With the price ceiling in effect, releasing shippers are unable to effectively use price differentials as a measure of capacity value because they are denied the ability to recover the value of capacity during peak periods when that value exceeds the maximum rate cap.

36. The price ceiling also harms captive customers holding long-term contracts on the pipeline. Those customers pay maximum rates for both peak and off-peak periods. During off-peak periods, they can only recover a small portion of the capacity cost through capacity release because of the low market value of off-peak capacity. However, during peak periods, the price ceiling prevents those customers from releasing their capacity for its full market value.

37. Finally, the price ceiling reduces the dissemination of accurate capacity pricing information. That is because the price ceiling causes transactions to move to the bundled sales market during peak periods, so that there is no separate capacity transaction to be reported.

2. Assurance of Just and Reasonable Rates

38. As the court stated in INGAA, the Commission may depart from cost of service ratemaking upon:

⁵¹ Standards for Business Practices for Interstate Natural Gas Pipelines, Notice of Proposed Rulemaking, 71 FR 64,655 (November 3, 2006), FERC Stats. & Regs. Proposed Regulations ¶ 32,609, P 17 (Oct. 25, 2006), Order No. 698, 72 FR 38,757 (July 16, 2007), FERC Stats. & Regs. Regulations Preambles ¶ 31,251 at P 51 (Jun. 25, 2007).

a showing that ... the goals and purposes of the statute will be accomplished ‘through the proposed changes.’ To satisfy that standard, we demanded that the resulting rates be expected to fall within a ‘zone of reasonableness, where [they] are neither less than compensatory nor excessive.’ [citation omitted]. While the expected rates’ proximity to cost was a starting point for this inquiry into reasonableness, [citation omitted], we were quite explicit that ‘non-cost factors may legitimate a departure from a rigid cost-based approach,’ [citation omitted]. Finally, we said that FERC must retain some general oversight over the system, to see if competition in fact drives rates into the zone of reasonableness ‘or to check rates if it does not.’⁵²

Accordingly, we analyze below (1) the extent to which market conditions and other factors may be expected to keep short-term capacity release prices within a reasonable zone despite the removal of the price ceiling, (2) the non-cost factors supporting a removal of the price ceiling, and (3) our oversight of the short-term capacity release market after removal of the price ceiling.

a. Market Conditions Ensure Just and Reasonable Rates

39. The Commission finds that the short-term capacity release market is generally competitive. Therefore competition, together with our continuing requirement that pipelines must sell short-term firm and interruptible services to any shipper offering the maximum rate, and the Commission’s ongoing monitoring efforts will keep short-term capacity release rates within the “zone of reasonableness” required by INGAA and Farmers Union.

⁵² INGAA at 31.

40. In Order Nos. 636 and 637, the Commission instituted a number of policy revisions which have enhanced competition between releasing shippers as well as between releasing shippers and the pipeline. These revisions provide shippers with enhanced market mechanisms that will help ensure a more competitive market and mitigate the potential for the exercise of market power. The Commission required pipelines to permit releasing shippers to use flexible point rights and to fully segment their pipeline capacity. Flexible point rights enable shippers to use any points within their capacity path on a secondary basis, which enables shippers to compete effectively on release transactions with other shippers. Segmentation further enhances the ability to compete because it enables the releasing shipper to retain the portion of the pipeline capacity it needs while releasing the unneeded portion. Effective segmentation makes more capacity available and enhances competition. As the Commission explained in Order No. 637:

The combination of flexible point rights and segmentation increases the alternatives available to shippers looking for capacity. In the example,⁵³ a shipper in Atlanta looking for capacity has multiple choices. It can purchase available capacity from the pipeline. It can obtain capacity from a shipper with firm delivery rights at Atlanta or from any shipper with delivery point rights downstream of Atlanta. The ability to segment capacity enhances options further.

⁵³ In the example used in Order No. 636, a shipper holding firm capacity from a primary receipt point in the Gulf of Mexico to primary delivery points in New York could release that capacity to a replacement shipper moving gas from the Gulf to Atlanta while the New York releasing shipper could inject gas downstream of Atlanta and use the remainder of the capacity to deliver the gas to New York.

The shipper in New York does not have to forgo deliveries of gas to New York in order to release capacity to the shipper seeking to deliver gas in Atlanta. The New York shipper can both sell capacity to the shipper in Atlanta and retain the right to inject gas downstream of Atlanta to serve its New York market.⁵⁴

41. In addition to enhancing competition through expansion of flexible point rights and segmentation, the Commission in Order No. 637 also required pipelines to provide shippers with scheduling equal to that provided by the pipeline, so that replacement shippers can submit a nomination at the first available opportunity after consummation of the capacity release transaction. The change makes capacity release more competitive with pipeline services and increases competition between capacity releasers by enabling replacement shippers to schedule the use of capacity obtained through release transactions quickly rather than having to wait until the next day.

42. The data accumulated by the Commission during the Order No. 637 experiment, as well as review of more recent data, confirm that capacity release prices reflect competitive conditions in the industry. On May 30, 2002, the Commission issued a notice of staff paper presenting data on capacity release transactions during the experimental period when the capacity release ceiling price was waived.⁵⁵ The staff

⁵⁴ Order No. 637 at 31,301.

⁵⁵ On May 30, 2002, a staff paper was posted on the Commission's web site presenting, and analyzing data on capacity release transactions relating to the experimental period when the rate ceiling on short-term released capacity was waived.

paper provided analysis of capacity release transactions on 34 pipelines during the 22-month period from March 2000 to December 2001.⁵⁶

43. In brief, the data gathered during the 22-month period show that without the price ceiling, prices exceeded the maximum rate only during short time periods and appear to be reflective of competitive conditions in the industry. The following table shows the distribution of above ceiling price releases among the pipelines studied.

Table I
Above Cap Releases by Pipeline
Releases Awarded Between March 26, 2000 and December 31, 2001

Pipeline	Releases Above Max Rate (Number of Transactions)	% of Total Releases	Release Quantity Above Max Rate (MMBtu/day)	% of Total Release Quantity
Algonquin	1	0.1	18,453	0.2
ANR Pipeline	1	0.1	30,000	0.2
CIG	19	6.5	109,984	4.4
Dominion (CNGT)	21	1.0	65,789	0.7
Columbia Gas	101	4.4	374,727	2.7
Columbia Gulf	.	.	.	.
East Tennessee	.	.	.	.
El Paso	135	13.3	631,683	12.5
Florida Gas	25	1.7	43,526	1.4
Great Lakes	3	1.3	15,000	0.6
Iroquois	.	.	.	.
Kern River	2	3.9	55,000	2.5
KMI (KNEnergy)	3	1.0	1,409	0.0
Gulf South (Koch)	.	.	.	.
Midwestern	1	0.6	50,000	2.3
Mississippi River	.	.	.	.
Mojave Pipeline	1	2.6	40,000	4.7

⁵⁶ Many of these release transactions would have occurred prior to completion of the pipeline's Order No. 637 compliance proceedings and the implementation of the changes to flexible point rights, segmentation and scheduling described above.

Table I
Above Cap Releases by Pipeline
Releases Awarded Between March 26, 2000 and December 31, 2001

Pipeline	Releases Above Max Rate (Number of Transactions)	% of Total Releases	Release Quantity Above Max Rate (MMBtu/day)	% of Total Release Quantity
Co.				
Natural Gas Pipeline Co.	16	3.2	270,489	2.3
Reliant (Noram)	.	.	.	.
Northern Border	.	.	.	.
Northern Natural	12	1.6	23,273	0.5
Northwest Pipeline	24	1.8	139,850	4.1
Paiute Pipeline	.	.	.	.
Panhandle Eastern	1	0.4	1,000	0.1
Southern Natural	7	0.3	24,101	0.2
Tennessee Gas	11	0.4	36,421	0.2
TETCO	122	3.8	645,856	3.3
Texas Gas	6	0.5	103,237	1.0
Trailblazer	3	25.0	15,000	10.0
Transco	183	3.3	1,540,885	4.1
Transwestern	11	4.5	64,058	6.5
Trunkline	.	.	.	.
Williams	4	0.4	16,500	0.3
Williston Basin	.	.	.	.
Total	713	2.2	4,316,241	2.1

44. These data show that during periods without capacity constraints, prices remained at or below the maximum rate. The staff paper does identify 713 releases above the ceiling price, representing an average total capacity release contract volume of 4.3 billion cubic feet (Bcf) per day. However, the staff paper reflects that these above-ceiling price releases represented only a small portion of the total releases on these pipelines, comprising approximately two percent of total transactions on the pipelines studied for

the entire period, and two percent of gas volumes. Further, above ceiling releases accounted for no more than six or seven percent of transactions during any given month of the period. As one would expect, the percentages of releases occurring above the ceiling increased during peak periods. However, average release rates were higher by only one cent per MMBtu per day or five and one-half percent higher than they would have been with the price ceiling in place. Of the 34 pipelines in the study, 10 reported no releases above the ceiling price, and 20 pipelines reported fewer than 25 above-ceiling price releases. The data gathered during this 22-month period reflects the Commission's expectations and affirms the Commission's findings in the Order No. 637 proceeding. As the court stated in INGAA:

the data represented in the graph [] do support the Commission's view that the capacity release market enjoys considerable competition. The brief spikes in moments of extreme exigency are completely consistent with competition, reflecting scarcity rather than monopoly. ... [citation omitted] A surge in the price of candles during a power outage is no evidence of monopoly in the candle market.⁵⁷

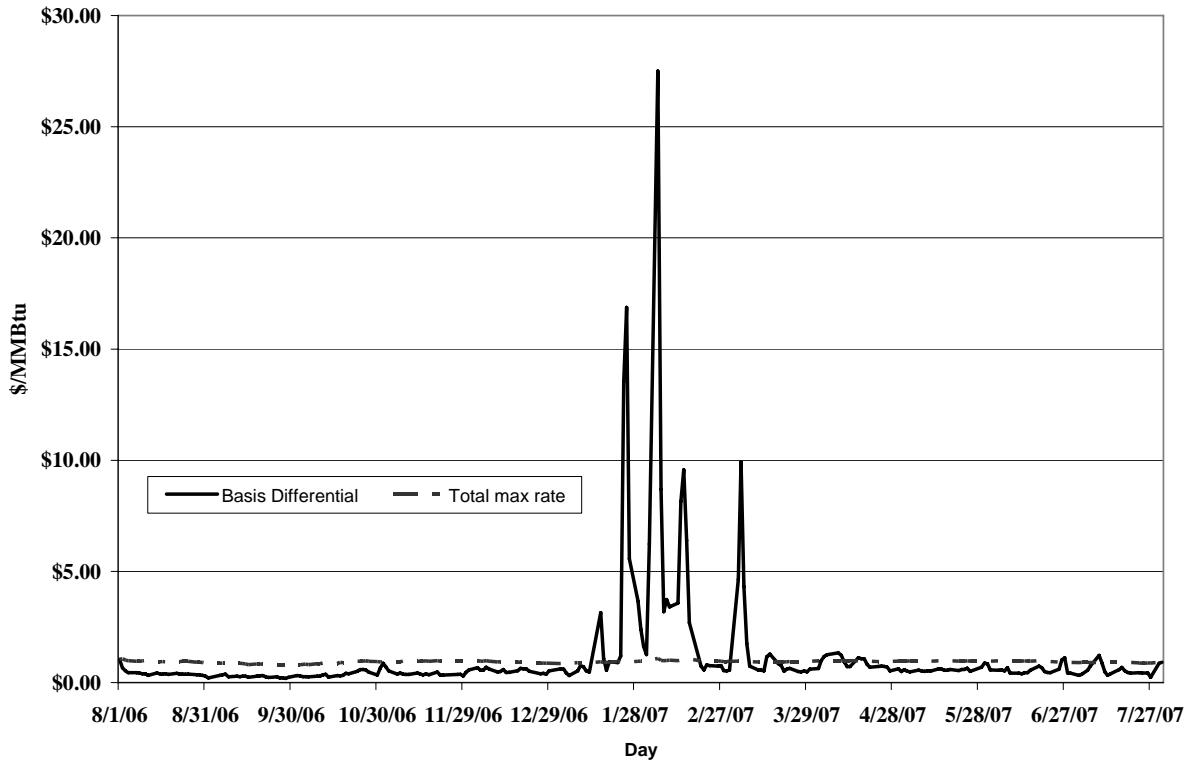
45. The Commission has gathered additional current data and has replicated the evidence presented in Order No. 637. The current data shows that the conditions that existed at the time of Order No. 637 and during the past experimental period continue in today's marketplace.

⁵⁷ INGAA at 32.

46. For example, Figure 1 illustrates the fluctuations in the market value of transportation service, as shown by the basis differentials between Louisiana and New York City. This graph compares the daily difference in gas prices between Louisiana and New York City to Transcontinental Gas Pipe Line Corporation's maximum interruptible transportation rate, including fuel retainage, during the 12 months ending July 31, 2007. This graph shows that for most of the year, the value of transportation service, as indicated by the basis differentials, is less than the maximum transportation rate. However, during brief, peak demand periods, the value of transportation service is measurably greater than the maximum transportation rate. For example, on February 5, 2007, the basis differential between Louisiana and New York City was in excess of \$27.00 per MMBtu, while the maximum tariff rate plus the cost of fuel was approximately \$1.08 per MMBtu.⁵⁸

⁵⁸ In Order No. 637, the Commission presented similar data in figure 6 showing the implicit transportation value between South Louisiana and Chicago. Order No. 637 at 31,274.

Figure 1 -- Daily Gas Price Differentials Louisiana to New York (12 Months Ending July 2007)



47. Figures 2 and 3 below reflect that a similar pattern of transportation value is evident in other areas of the country. Focusing on fluctuations in the market value of transportation service as shown by basis differentials between Louisiana and Chicago and between the Permian Basin and the California border, respectively, these figures show that for most of the year, the value of transportation service is less than the maximum transportation rate of Natural Gas Pipeline Company of America and El Paso Natural Gas Company, respectively. However, similar to figure 1, these figures also reflect that during brief peak-demand periods the value of transportation service is measurably greater than the maximum transportation rate.

Figure 2 -- Gas Price Differentials NGPL La. To Chicago

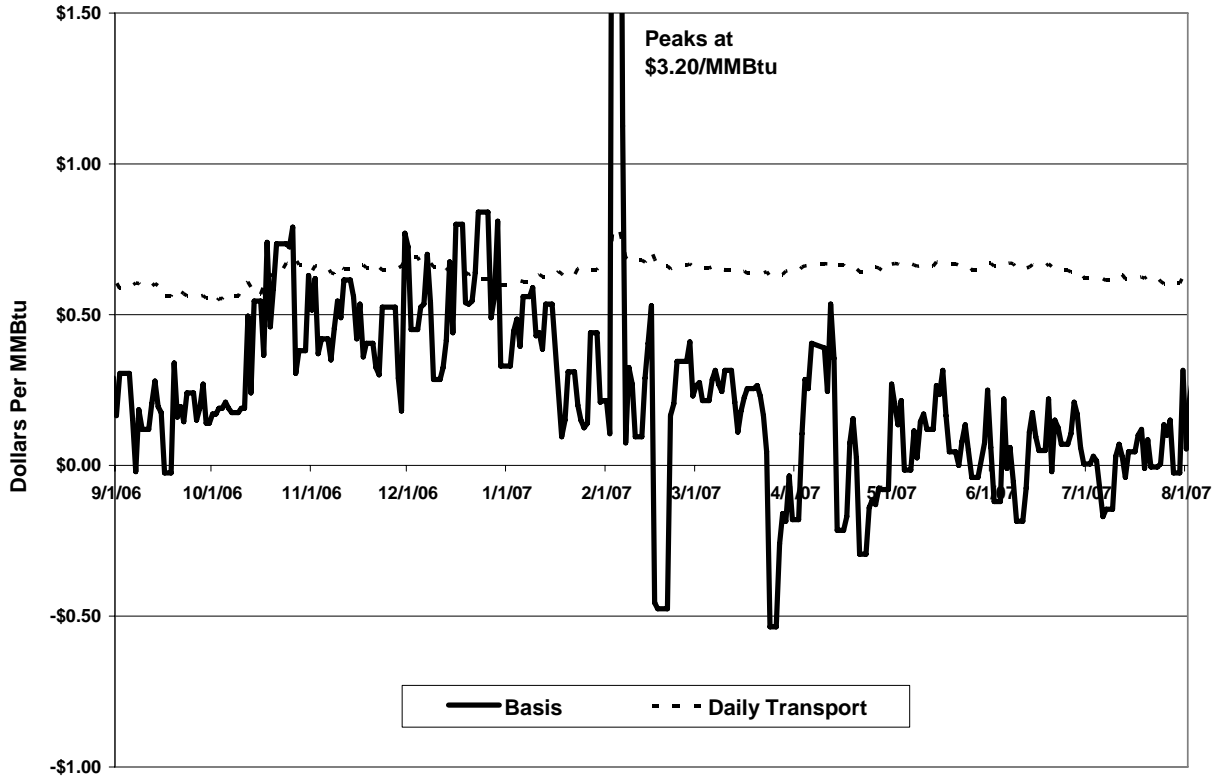
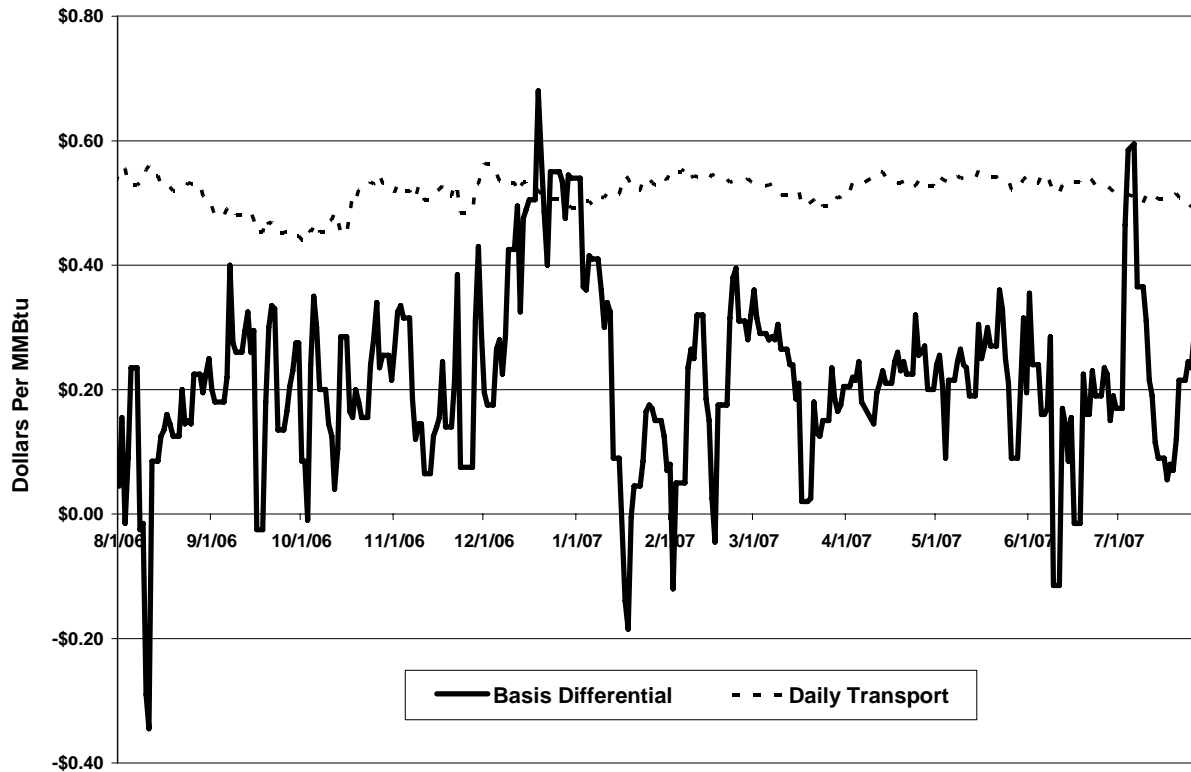


Figure 3 -- Gas Price Differentials for Permian Basin to California Border (SoCal Gas)



The data in all three of the above figures reflect similar market conditions to the data that the Commission relied upon in lifting the price ceiling for short-term capacity releases in Order No. 637, with the market value of capacity generally below the pipeline's maximum rate except for relatively brief price spikes.⁵⁹ In affirming the Commission's actions, the court in INGAA found that the data presented by the Commission constituted a substantial basis for the conclusion that a considerable amount of competition existed in the capacity release market. Further, the INGAA court concluded that the price spikes

⁵⁹ Order No. 637 at 31,273-75.

reflected in the data were consistent with competition and that such spikes reflected scarcity rather than monopoly power.⁶⁰

b. Recourse Rate Protection

48. Moreover, the Commission is not relying only on a competitive market to ensure just and reasonable rates. The pipeline's maximum rates for short-term firm and interruptible services serve as recourse rate protection for negotiated rate transactions,⁶¹ and will provide the same protection to replacement shippers by giving them access to a just and reasonable rate if the releasing shipper seeks to exercise market power.⁶² As the Commission explained in Order No. 637:

the Commission is continuing to protect against the possibility that, in an oligopolistic market structure, the pipeline and firm shipper will have a mutual interest in

⁶⁰ INGAA at 31- 32.

⁶¹ Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines, 74 FERC ¶ 61,076, reh'g denied, 75 FERC ¶ 61,024 (1996), petitions for review denied sub nom., Burlington Resources Oil & Gas Co. v. FERC, 172 F.3d 918 (D.C. Cir. 1998). See also Natural Gas Pipelines Negotiated Rate Policies and Practices; Modification of Negotiated Rate Policy, 104 FERC ¶ 61,134 (2003), order on reh'g and clarification, 114 FERC ¶ 61,042, order dismissing reh'g and denying clarification, 114 FERC ¶ 61,304 (2006). As the Commission explained in its negotiated rate policy statement, "[t]he availability of a recourse service would prevent pipelines from exercising market power by assuring that the customer can fall back to traditional cost-based service if the pipeline unilaterally demands excessive prices or withholds service." 74 FERC ¶ 61,076 at 61,240 (1996).

⁶² The pipeline is obligated to sell capacity at the just and reasonable rate. Tennessee Gas Pipeline Co., 91 FERC ¶ 61,053 (2000), reh'g denied, 94 FERC ¶ 61,097 (2001), petitions for review denied sub nom., Process Gas Consumers Group v. FERC, 292 F.3d 831, 837 (D.C. Cir. 2002).

withholding capacity to raise the price because the Commission is continuing cost based regulation of pipeline transportation transactions. The pipeline will be required to sell both short-term and long-term capacity at just and reasonable rates. In the short-term, a releasing shipper's attempt to withhold capacity in order to raise prices above maximum rates will be undermined because the pipeline will be required to sell that capacity as interruptible capacity to a shipper willing to pay the maximum rate. Shippers also have the option of purchasing long-term firm capacity from the pipelines at just and reasonable rates.⁶³

49. The court in INGAA similarly recognized the value of the pipeline's recourse rate protecting against possible abuses of market power by releasing shippers stating that:

[i]f holders of firm capacity do not use or sell all of their entitlement, the pipelines are required to sell the idle capacity as interruptible service to any taker at no more than the maximum rate – which is still applicable to the pipelines.⁶⁴

c. Short-Term Customers are Not Captive

50. The releasing shippers' ability to exercise market power in the short-term capacity release market also is limited because short-term customers are not captive, even if only connected to one pipeline. Short-term customers, those using interruptible or short-term firm pipeline service or relying on capacity release transactions, are by the very nature of the service for which they are contracting, expressly taking the risk that they may have to forgo the use of gas entirely if short-term capacity is too expensive, or not available,

⁶³ Order 637 at 31,282.

⁶⁴ INGAA at 32.

when they need it.⁶⁵ Thus, short-term shippers always have the option simply not to take service, if the price demanded is above competitive market levels.

d. Non-cost factors

51. Removal of the price ceiling on short-term capacity release transactions provides a number of advantages which “offset whatever harm the occasional high rate might entail.”⁶⁶ Most importantly, removal of the price cap permits more efficient utilization of capacity by permitting prices for short-term capacity releases to rise to market clearing levels, thereby permitting those who place the highest value on the capacity to obtain it. Removal of the price ceiling also will provide potential customers with additional opportunities to acquire capacity. Without the price ceiling, firm capacity holders will have a greater incentive to release capacity during times of scarcity, because they will be able to obtain the full market value of the capacity.⁶⁷ Therefore, a shipper needing gas on a peak day will have a greater opportunity to obtain the capacity it needs from a firm capacity holder, instead of having only the choices of purchasing a bundled sale or taking

⁶⁵ Order No. 637 at 31,285, 31,336-42.

⁶⁶ INGAA at 33.

⁶⁷ For example, an LDC shipper may hold capacity on one or more pipelines and have access to storage and peak shaving facilities. Using these facilities may cost the LDC more to deliver gas than purchasing gas in the upstream markets and using its transportation capacity to transport that gas to the city gate. However, the LDC might be willing to release its transportation capacity and use its peak shaving device instead if it could receive a price above the maximum rate for its transportation capacity so that the price it receives will cover the costs of the peak shaving device. Order No. 637 at 31,277.

gas out of the pipeline and paying the pipeline's scheduling or overrun penalties.⁶⁸ Thus, removal of the price ceiling benefits short-term shippers because the shipper placing a high value on the capacity has a greater assurance of obtaining the capacity it needs than it does under a price cap where that shipper may be unable to obtain any capacity.

52. Second, even if replacement shippers do end up paying higher prices for capacity during peak periods than they did with the regulated rate in effect, it is appropriate for shippers using the system only during peak periods to pay higher prices reflecting the greater demand on the system. Short-term shippers currently receive the benefit of paying reduced capacity release prices during off-peak periods but face a cap on the market price during peak periods. Removal of the price ceiling on short-term capacity releases will ensure that those shippers that receive the benefit of lower market prices during off-peak periods face the higher market prices during peak periods.

53. Third, removing the price ceiling on short-term capacity releases should benefit the "primary intended beneficiaries of the NGA – the 'captive' shippers"⁶⁹ by removing the regulatory bias built into the current rate structure. Those shippers typically have long-term firm contracts with the pipeline. Long-term shippers pay the same rate for capacity during both peak and off-peak periods. During off-peak periods they can recover only a small portion of their capacity cost through capacity release, because the

⁶⁸ Order No. 637 at 31,280; INGAA at 34.

⁶⁹ INGAA at 33.

market value for release capacity is generally quite low due to the reduced demand for capacity and the increased availability of released capacity. But during peak periods, the price cap limits long-term captive customers (who cannot make bundled sales) from receiving the full market value of their capacity. Long-term shippers pay for the largest proportion of the pipeline's fixed costs through their annual reservation charges, and permitting them to receive more revenue from capacity release during peak periods will help them defray those costs. In short, the captive customers will "continue to receive whatever benefits the rate ceilings generally provide," while also "reaping the benefits of [the] new rule, in the form of higher payments for their releases of surplus capacity."⁷⁰

54. Finally, by providing more accurate price signals concerning the market value of pipeline capacity, removal of the price ceiling for short-term capacity releases will promote the efficient construction of new capacity by highlighting the location, frequency, and severity of transportation constraints. Correct capacity pricing information will also provide transparent market values that will better enable pipelines and their lenders to calculate the potential profitability and associated risk of additional construction designed to alleviate transportation constraints.

e. Oversight

55. The reporting requirements in Order No. 637 and the Commission's implementation of the Energy Policy Act of 2005, specifically with respect to market

⁷⁰ Id.

manipulation, provide the Commission with enhanced ability to monitor the market and detect and deter abuses.

56. Order No. 637 improved the Commission's and the industry's ability to monitor capacity release transactions by requiring daily posting of these transactions on pipeline web sites.⁷¹ This has increased the information available to buyers while at the same time making it easier for the Commission to identify situations in which shippers are abusing their market power.⁷² Further, the Commission will entertain complaints and respond to specific allegations of market power on a case-by-case basis if necessary. Furthermore, the Commission directs staff to monitor the capacity release program and, using all available information, issue a report on the general performance of the capacity release program, within six months after two years of experience under the new rules.

3. Comments

57. The vast majority of comments support the removal of the price ceiling for capacity release transactions. But some commenters have raised limited concerns.

a. Lack of Competition in Certain Areas

58. A few commenters have alleged that certain discrete portions of the short term capacity release market may not be competitive at all times. For example, Arizona Public Service states that the transportation markets served by El Paso Natural Gas Company (El

⁷¹ 18 CFR 284.8 (2007).

⁷² Order No. 637 at 31,283; Order No. 637-A at 31,558.

Paso) located east of California are not currently competitive. It asserts that during the 2000-2002 California energy crisis, when the Commission had lifted the price cap on short term capacity releases, prices of releases of El Paso capacity spiked to levels in excess of \$20 per Dth. Honeywell similarly argues that the Commission has failed to address the fact that many geographical areas do not operate as a free market and that areas in the Northeast, East, and Southwest portions of the country faced constrained capacity and difficulties in building new pipeline facilities. Honeywell argues that lifting the price cap on short term capacity release will only exacerbate prices while not addressing the underlying problem of these constrained markets. In addition, some end-users of gas express concerns about the concentration of capacity ownership on lateral pipelines and therefore argue that the Commission should either not remove the price cap for laterals or do so on a case-by-case basis, after a review of market concentration and a demonstration that the releasing shipper does not have market power on the lateral.⁷³

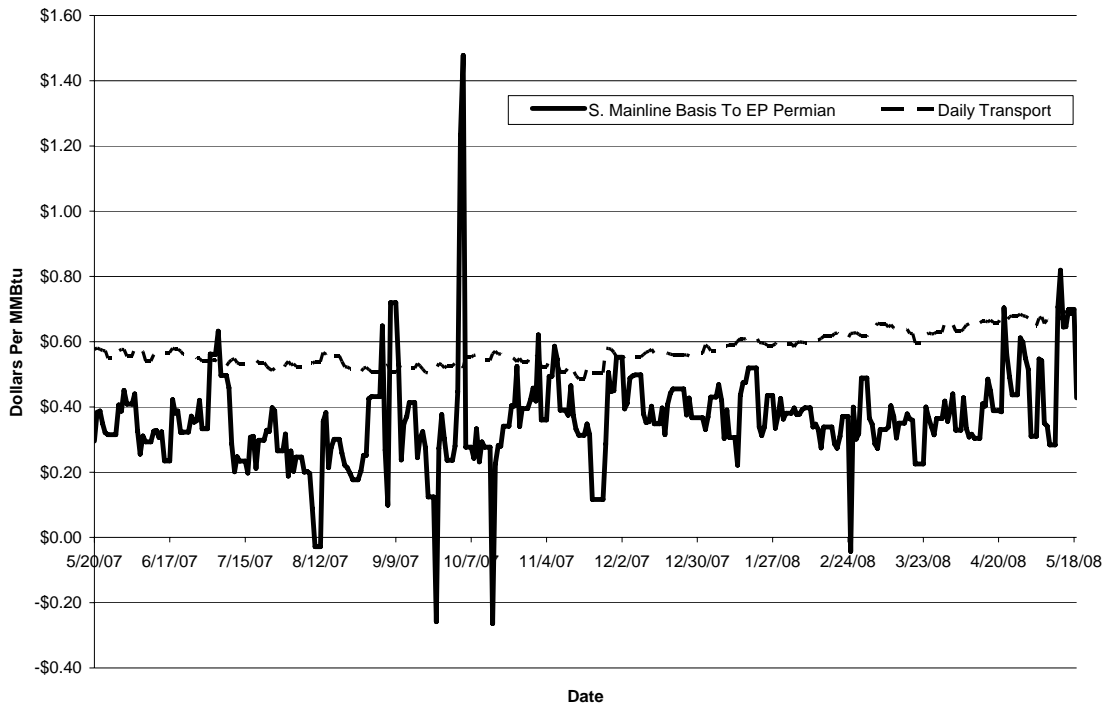
59. While the Commission has not conducted a detailed market analysis for each discrete area of the interstate pipeline grid, the data previously discussed shows that the short-term capacity release market is generally competitive. Indeed, with respect to the El Paso market, the data in Table 1 shows that during the period March 26, 2000 to December 31, 2001, which included the California energy crisis referred to by APS, only 12.5 percent of the total volume of capacity released on El Paso was released at prices

⁷³ Weyerhaeuser, NWIGU, and PGC.

above the maximum rate. Moreover, the updated data in Figure 3 for August 2006 through July 2007 shows that the market value of transportation service from the Permian Basin to the California border was less than El Paso's maximum transportation rate, except during brief, peak-demand periods when the value of transportation service was somewhat greater than the maximum transportation rate. Similar data for deliveries to East of California markets on El Paso's South Mainline reflects the same overall pattern, as shown in the following graph.⁷⁴

⁷⁴ The data for this chart comes from ICE, an on-line electronic trading platform. The El Paso South Mainline area is described on ICE as: El Paso - South Mainline – buyers' choice west of Cornudas.

Figure 4 El Paso Permian-to-South Main Line Basis Differentials vs. Maximum Transport Charge



60. Similarly, while Honeywell suggests that capacity is constrained in areas in the East and Northeast, the data in Figure 1 shows that for most of the year the value of transportation service from Louisiana to New York City is less than the maximum transportation rate on Transco, with only brief spikes above that level during peak demand periods.

61. These data are consistent with the proposition that prices will exceed the maximum rate only during periods of constraint. Moreover, it is precisely for these reasons that the Commission is continuing to insist on the maintenance of the pipeline’s recourse rate as protection against the exercise of market power. Even on laterals or other parts of the pipeline grid where all firm capacity may be held by only a few or one firm shipper, those shippers cannot withhold their capacity in order to charge a price

above competitive levels. The pipeline's cost-based interruptible rate is always available as an alternative when a releasing shipper attempts to withhold its capacity. For example, assume that a releasing shipper with available capacity on a little used lateral seeks to exercise market power by withholding capacity unless a potential replacement shipper pays a higher than justified rate. If market demand for capacity at that rate does not exist,⁷⁵ the replacement shipper has the option of turning down the deal and purchasing the capacity from the pipeline at the just and reasonable interruptible rate.

62. NEM remains concerned that in spite of the Commission's finding that the short term capacity release market is competitive, market power may exist for some market participants resulting in historically high natural gas prices reaching even higher levels. However, the data reflects the competitive nature of the short term capacity release market and the safeguards that the Commission employs in the instant Final Rule to mitigate any residual market power. The Commission accordingly finds that NEM's speculative concerns are unwarranted.⁷⁶

⁷⁵ In other words, the market is not constrained.

⁷⁶ NEM also posits that the lifting of the short term capacity release market price ceiling in states where LDCs are required to release their capacity to marketers as part of a state retail unbundling program will place the marketer in a position where they would no longer be guaranteed the same underlying capacity costs as if the capacity had remained with the utility, and this could increase the costs the marketers must pass on to their state retail customers. To the extent that this feature causes problems in states where capacity release assignments are a mandatory part of a state retail unbundling program, the Commission would expect that the State would consider this in its policies.

b. Benefits from Removing the Price Ceiling

63. Tenaska contests some of the benefits the Commission has cited for removing the price ceiling. It argues there will be no overall increase in allocative efficiency from removal of the short term release price cap. It asserts that capacity that is in excess to the current capacity holder's needs already finds its way to those who value it more by a variety of means, including bundled downstream sales, short and long term capacity releases, and pipeline sales of short-term firm and interruptible service. It also argues that releasing shippers with excess capacity are more likely to release that capacity over a longer term, perhaps multiple years, rather than speculate that it could profit by making very short-term releases during peak period price spikes. It states that releases over relatively long term with few exceptions allow the releasing shipper to realize its full market value without being constrained by maximum pipeline rates.⁷⁷

64. Rather than undercutting the removal of the price cap, Tenaska's argument that releasing shippers can now avoid the price ceiling by making gas sales (in effect bundled sales of gas and transportation) supports our determination. Shippers may well find that releasing transportation alone is far more efficient than making a bundled sales transaction, and therefore, removal of the price ceiling will serve only to promote

⁷⁷ Tenaska explains, "[c]apacity that basis markets show to be worth more than the applicable pipeline maximum rate in the prompt month will almost always drop in value to a level below that maximum rate at some future point. Such capacity can be sold for its full value within the pipeline maximum rate cap simply by extending the term." Tenaska comments at 4-5.

efficiency with negligible effect, if any, on price levels. Similarly, requiring shippers to execute long-term contracts in order to effectuate short-term transactions is inefficient, and would mask more accurate short-term price signals. Moreover, as discussed earlier, releasing and replacement shippers want to contract based on price differentials between markets even when such differentials exceed the maximum rate, and executing long term contracts at some approximate capped rate would not achieve that goal.

65. Tenaska also argues that holders of long term pipeline contracts, that are “net long” compared to their actual capacity needs will be the only shippers to benefit. Market participants that are “net short” hold less capacity than they need and choose to match some portion of their demand with short term services and delivered gas purchases rather than to rely exclusively on long term pipeline contracts. Tenaska argues that the effect of the removal of the short term release rate cap, if there is any effect on reallocation of capacity at all, will be a transfer of value from net short companies to net long companies and states that there will be no net market benefit of the type the Commission must show to justify the proposed removal of the cap.

66. Tenaska ignores the fact that “net short” holders of capacity under its scenario will benefit from the removal of the price cap from short term capacity release because they may be able to gain access to capacity in a constrained market that they could not if the price cap remained. A releasing shipper, subject to a rate ceiling, may well hold onto capacity if the maximum rate is less than its opportunity cost, such as using an alternative

fuel, using expensive storage, or conservation of gas.⁷⁸ Moreover, the fact low load factor “net long” holders of capacity of the type described by Tenaska can profit from above-cap short term releases is one of the benefits of removing the short-term price cap.

c. Promotion of Construction

67. Honeywell argues that the Commission has failed to show that more accurate price signals concerning the value of pipeline capacity will, in fact, promote construction of needed capacity. First, higher prices should serve as price signals indicating where capacity shortages exist and where potentially profitable construction can take place. If prices are “exacerbated” as Honeywell argues, replacement shippers paying such prices have every incentive to go to the pipeline and support economically efficient construction to rectify the shortage. While political and environmental obstacles are also a factor in construction, this factor has not stymied construction. The Commission has processed a large number of certificate applications for new construction of capacity, storage, and liquefied natural gas terminals in every region.⁷⁹ Third, providing incentives for new construction is not the only benefit of removing the price ceiling. As discussed earlier,

⁷⁸ Order No. 637 at 31,554.

⁷⁹In 2007 alone, approximately 34 major pipeline projects were authorized by the Commission which was comprised of approximately 2,782 miles of pipeline, 850 thousand horsepower of compression and the capacity to transport some 23,000 million MMD/t of gas. See the “2007” data at www.ferc.gov/industries/gas/industry-act/pipelines/approved-projects.asp. See similar data for storage at www.ferc.gov/industries.asp and liquefied natural gas terminals at www.ferc.gov/industries/lng.asp.

removal of the price ceiling will benefit the market even in the short term by providing for a more efficient allocation of capacity to those who value that capacity.

d. Changed Circumstances

68. Tenaska and APS argue that even if the Commission's conclusion that all pipeline capacity release markets are competitive is supportable at this time, circumstances could change dramatically in this industry. As a result, they assert that the Commission must include a process for promptly revisiting its determination that the market is competitive if there is evidence that the market is dysfunctional. Honeywell also states that the Commission also proposes to blind itself for almost three years to any problems in the capacity release market by directing its staff to issue a report within six months after gaining two years of experience under the new rules.

69. As set forth above, we are maintaining oversight over the market and can act if market power is being abused in particular circumstances. Order No. 637 improved the Commission's and the industry's ability to monitor capacity release transactions by requiring daily posting of these transactions on pipeline web sites.⁸⁰ This has increased the information available to buyers while at the same time making it easier for the Commission to identify situations in which shippers are abusing their market power.⁸¹ Such information allows the Commission to monitor, with the assistance of all industry

⁸⁰ 18 CFR 284.8 (2007).

⁸¹ Order No. 637 at 31,283; Order No. 637-A at 31,558.

participants, the overall competitiveness of the market including discrete portions of the market that may not be competitive at all times. Moreover, the Commission will entertain complaints and respond to specific allegations of market power on a case-by-case basis if necessary. This action will also guard against the use of market power by any market participant.

70. Further, Honeywell misreads the Commission's directives and intent when it claims the Commission has voluntarily blinded itself to market forces for some three years. While the Commission directs its staff to monitor the capacity release program and issue a report on the general performance of the capacity release program within six months after two years of experience under the new rules, nothing in this directive precludes staff from alerting the Commission to any irregularities in the capacity release market before it issues its general report.

71. Moreover, while Tenaska refers to the Commission lifting of the short term price cap as permanent, and notes that the INGAA court reviewed a proposal by the Commission to lift the price ceiling only on a temporary basis, it is important to note that, although the Commission will remove the price ceiling on short term capacity releases it will monitor the capacity release market and review its staff's report on the effects of the new rule and the overall functioning of the capacity release market.

e. **Exemption from Bidding for Short-Term Releases at the Maximum Rate**

72. The NGSA and others request that the Commission continue to allow market participants to enter into a pre-arranged capacity release transaction without bidding for

releases of capacity with a term of a year or less as long as those releases are made at the pipeline's maximum tariff rate. NGSAs asserts that prearranged releases at the pipeline's maximum rate without the competitive bidding requirement have been proven to provide significant market benefits and should not be eliminated, solely because the Commission removes the rate cap on short-term capacity release transactions.

73. The reason for the prior exemption from bidding for pre-arranged capacity release transactions at the maximum rate was based solely on the fact that with the rate cap in place, no one could submit a higher bid and win the capacity. As discussed earlier, one of the reasons for removing the price ceiling for short-term releases is to ensure that capacity is allocated to the shipper that values it the most. NGSAs has not provided a sufficient justification for permitting shippers to consummate a capacity release at the maximum rate when another potential shipper places a greater value on that capacity.

B. Removal of Price Ceiling for Long-Term Releases

74. Several commenters to the NOPR request that the Commission remove the price ceiling on long-term capacity releases in addition to eliminating the price ceiling on short-term capacity releases.⁸² These commenters assert that the same arguments that support removal of the price cap for short-term capacity releases apply equally to lifting the price cap for long-term capacity releases. For example, commenters argue that lifting the price ceiling on long-term capacity releases would increase liquidity and competition

⁸² See, e.g., Comments of Allegheny Energy Supply Co. (Allegheny), Duke Energy, Dynegy Marketing and Trade (Dynegy), and Southwest .

in the market for capacity release and primary pipeline capacity, thereby promoting the goals of allocative efficiency. Moreover, commentors assert that lifting the price cap on long-term capacity releases will promote the construction of additional pipeline capacity by providing more accurate price signals reflecting the value of such capacity.

75. Commentors also point out that the Commission's concern over replacement shippers being "locked in" to high price long-term contracts is misplaced because such releases of capacity would likely be priced using basis differentials at different price index locations.⁸³ Other commentors such as Duke assert that the Commission's concerns are misplaced because replacement shippers accepting such multi-year deals are sophisticated market participants capable of negotiating fair agreements.

76. Allegheny argues that the pipelines' recourse rates will serve as a check on over-priced long-term capacity releases because replacement shippers would have the ability to negotiate for capacity from a pipeline at the recourse rate if the releasing shippers were seeking excessive prices. Allegheny also points to the Commission's reporting requirements, complaints process, and enhanced civil penalty authority as additional safeguards against the exercise of market power.

77. Several commentors support the retention of the price ceiling on long term capacity releases and argue that it protects customers from being locked into a long term contract without price cap protection, that the price cap provides protection against

⁸³ See e.g., Comments of Southwest at 10; Allegheny at 6-7.

possible abuse of market power and that removal of the price cap for long term capacity releases does not provide the efficiency gains provided by the removal of the price ceiling on short term capacity release.⁸⁴

78. In this instant Final Rule, the Commission will not extend the removal of price ceilings to long term releases as urged by these commentors. The data discussed above indicate only that removal of the price cap for short-term releases is needed to reflect market values. The Commission removed the price ceiling to permit shippers to quickly align their capacity prices with the fluctuating short term market for capacity releases. Such flexibility is not relevant to long-term releases.

79. Limiting this rulemaking to short-term transactions is a reasonable response to the circumstances the Commission is trying to address, i.e., short term price spikes. Only under these conditions do Commission-approved maximum rates prevent the market from rationally allocating scarce capacity to those shippers who value it most. Removing the price cap only for short-term transactions allows a more efficient market-driven allocation of capacity during those brief peak demand periods, and provides more detailed price signals to the market on the value of peak capacity, while retaining valuable consumer protections provided by the price ceiling for longer term transactions. The Commission's policy emphasis in this rule is on short-term transactions, because that is where there is a problem to be solved. No commenter has made a convincing

⁸⁴ See, e.g., Comments of NJNG at 33, OIPA at 3, Statoil at 14, Weyerhaeuser at 11.

argument that price ceilings on longer term transactions create significant allocative inefficiencies or market failures. Accordingly, the Commission concludes that the current record does not warrant removal of the price ceiling on long-term capacity releases.

80. Moreover, as we said in the NOPR,⁸⁵ limiting the release to one year will not prevent the releasing and replacement shipper from continuing an index-based release past one year, because they could repost the release for another year, and the price ceiling would not apply to the release. However, such reposting provides additional assurance to the market that capacity will be allocated to those who value it the most. Any transaction in which the parties want to continue the release past one year would have to be re-posted for bidding to ensure that the capacity is allocated to the highest valued use.⁸⁶ This bidding process could provide an opportunity for re-determining the current market value of the capacity.

C. Removal of Price Ceiling for Pipeline Short-Term Transactions

81. Pipelines request that the Commission remove the price ceiling for short-term primary pipeline capacity whether firm or interruptible. In sum, the Interstate Natural Gas Association of America (INGAA) and the commenting pipelines argue that if the

⁸⁵ NOPR at P 44-45.

⁸⁶As discussed below, however, short term capacity releases made in context of an AMA need not be re-posted for bidding at the end of their term.

Commission lifts the price cap for short-term capacity releases, it should also lift the price cap for primary pipeline capacity.⁸⁷

1. Removal of the Price Ceiling is Not Justified

82. The Commission declines to remove the ceiling from short-term pipeline capacity. In the Alternative Rate Design Policy statement, we offered the pipelines the flexibility to exceed the price cap in one of two ways: either pipelines can make a filing with appropriate information to establish the market is competitive or pipelines can negotiate rates as long as the shipper has the option of purchasing capacity at the recourse (maximum) tariff rate.⁸⁸ These two approaches assured shippers that the pipelines were not exercising market power. The pipelines request for lifting the maximum rate on short-term releases would effectively negate the recourse rate protection we included in the negotiated rate program.

83. Our action here is designed to permit releasing shippers some of the same flexible pricing authority the Commission has already granted pipelines through the negotiated rate program. But, as discussed earlier, the Commission is retaining the maximum rate ceiling on pipeline capacity because it acts as the recourse rate for both pipeline

⁸⁷ See e.g., Comments of Boardwalk, Spectra Energy Transmission, LLC and Spectra Energy Partners, LP (Spectra), and Williston Basin Interstate Pipeline Co. (Williston Basin).

⁸⁸ 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).

transactions as well as release transactions. Removing the rate ceiling for pipeline transactions would therefore remove an important protection both for pipeline customers and for replacement shippers on capacity release transactions.

84. In addition, pipelines are the principal holders of capacity. As the court recognized in INGAA:

there seems every reason to suppose that [releasing shipper] ownership of such capacity (in any given market) is not so concentrated as that of the pipelines themselves--the concentration that prompted Congress to impose rate regulation in the first place.

* * *

Here, the distinction between pipelines and other holders of unused capacity, based on probable likelihood of wielding market power, seems to us to pass muster.⁸⁹

85. Unlike releasing shippers, the pipeline holders of primary capacity have a greater ability to exercise market power by withholding capacity and not constructing facilities. Because pipelines are in the best position to expand their own systems, cost-of-service rate ceilings help to ensure that pipelines have appropriate incentives to construct new facilities when needed. As the Commission found, “the only way a pipeline [can] create scarcity to force shippers to accept longer term contracts would be to refuse to build additional capacity when demand requires it.”⁹⁰ As long as cost-of-service rate ceilings

⁸⁹ INGAA at 35.

⁹⁰ Regulation of Short-Term Natural Gas Transportation Services, 101 FERC ¶ 61,127, at P 12 (2002), aff'd, American Gas Ass'n v. FERC, 428 F.3d 255 (D.C. Cir.

(continued...)

apply, however, “pipelines [will] have a greater incentive to build new capacity to serve all the demand for their service, than to withhold capacity, since the only way the pipeline could increase current revenues and profits would be to invest in additional facilities to serve the increased demand.”⁹¹ Similarly, as long as pipeline short-term services are subject to a cost of service rate, the pipelines will not limit their construction of new capacity to meet demand in order to create scarcity that increases short-term prices. Indeed, releases at prices above the maximum rate will indicate that pipeline capacity is constrained and demonstrate that constructing additional capacity could be profitable.

86. Further, pipelines already have significant pricing discretion. As discussed above, pipelines can enter into negotiated rate transactions above the maximum rate. Pipelines also may seek market-based rates by making a filing with the Commission establishing that they lack market power in the markets they serve.⁹² In addition, pipelines have the ability to propose seasonal rates for their systems, and therefore, recover more of their annual revenue requirement in peak seasons.⁹³ The proposed rule is designed solely to

2005). See also Tennessee Gas Pipeline Co., 91 FERC ¶ 61,053 (2000), reh'g denied, 94 FERC ¶ 61,097 (2001), aff'd, 292 F.3d 831 (D.C. Cir. 2002).

⁹¹ Id.

⁹² 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).

⁹³ See Order No. 637 at 31,574 – 81.

give releasing shippers some of the same flexibility enjoyed by the pipelines, subject to the same recourse rate protection. But removing the ceiling price from the release market does not justify removing all regulatory protections applicable to the primary capacity holder.

2. Response to Specific Comments

a. Evidentiary Record

87. INGAA states that the same evidentiary record relied upon by the Commission to propose lifting the ceiling on capacity releases reflects that the entire market, including short-term pipeline services, is competitive, and therefore contends that the Commission should lift the rate ceilings on the entire short-term market. Spectra adds that the evidence cited by the Commission supports the existence of competition by all participants in the single market for short-term capacity, not just competition in the capacity release sector of the overall market. INGAA asserts that if the market is competitive, the identity of the seller should be irrelevant.

88. As we have explained above, while the data indicates that the short-term secondary market is competitive in general, we have not made a finding that every segment of every pipeline is competitive; we retained the recourse rate as a protection against the potential exercise of market power by both pipelines and releasing shippers in those cases in which the market may not be competitive. While the purpose of capacity release, segmentation, and flexible point rights is to encourage competition between the pipeline's sale of its own capacity and capacity release, and those policies have

successfully created a robust secondary market as demonstrated by the data discussed earlier in this rule, that does not necessarily mean that every pipeline faces competition in the sale of its short-term capacity on all segments of its system. For example, the Commission's selective discounting policy permits pipelines to restrict a shipper's discount to specific points, so that the shipper must pay the pipeline's maximum rate if it releases the capacity to a replacement shipper who uses different points where the pipeline faces less competition.⁹⁴ This may reduce that shipper's incentive to release its capacity to a replacement shipper who will use points on a segment with less competition.⁹⁵ Retaining the recourse rate helps protect against the pipeline's abuse of market power in the sale of capacity on any such segments of its system.

⁹⁴ Williston Basin Interstate Pipeline Co., 110 FERC ¶ 61,210 at P 22, order on reh'g, 112 FERC ¶ 61, 038 (2005). These orders responded to a decision by the United States Court of Appeals for the District of Columbia Circuit in Williston Basin Interstate Pipeline Co. v. FERC, 358 F.3d 45 (D.C. Cir. 2004) (Williston), vacating orders in an Order No. 637 compliance proceeding permitting releasing shippers to retain primary point discounts when their replacement shippers used different points. The D.C. Circuit held that the policy could undermine the benefits of selective discounting, stating that "economic theory tells us price discrimination, of which selective discounting is a species, is least practical where arbitrage is possible-that is, where a low price buyer can resell to a high price buyer . . . yet this is precisely what the Commission's policy would appear not only to allow but to encourage." 358 F.3d at 50 (cite omitted).

⁹⁵ In addition, a particular shipper's incentive to release capacity in competition with the pipeline could be reduced, if its discounted or negotiated rate agreement contains a provision, as permitted by Commission policy, providing that the pipeline will share any revenues the shipper receives from a capacity release in excess of its discounted or negotiated rate. See LSP Cottage Grove, L.P. v. Northern Natural Gas Co., 111 FERC ¶ 61,108 at P58-59 (2005), and cases cited.

89. Further, the repercussions of removing price ceilings for pipeline transactions are more serious than for released capacity, because the exercise of market power by pipelines could reduce the total amount of primary pipeline capacity available to the market. Finally, to the extent pipelines believe their markets are competitive, they have a full opportunity to make a filing with the Commission to obtain market based rates based on a showing of lack of market power.⁹⁶

b. Infrastructure Incentives

90. INGAA alleges that maintaining cost-based recourse rates for pipelines is not required to preserve an incentive for pipelines to construct needed pipeline infrastructure. It asserts this runs counter to the general presumption that market-based rates send the proper signals as to whether new pipeline construction is needed and can be constructed economically. In their comments, INGAA and Spectra argue that pipelines actually compete to build new capacity, and that there is no reason to assume that non-pipeline investment will not fill any void caused by pipelines withholding capacity.⁹⁷

⁹⁶ Pipelines so far have not been successful in demonstrating that their major markets are competitive. See e.g., Gas Transmission Northwest Corp., 119 FERC ¶ 61,288 (2007); Koch Gateway Pipeline Co., 85 FERC ¶ 61,013 (1998), order on reh'g, 89 FERC ¶ 61,046 (1999).

⁹⁷ Spectra also argues that the Commission should remove the price caps for pipeline short-term firm and interruptible capacity, and suggests that to the extent the Commission retains its concerns regarding withholding of capacity, the Commission could retain the price caps for interruptible service. Spectra further argues that this action would provide shippers with a recourse alternative that would be available if the pipeline attempted to withhold short-term firm capacity or the releasing customer tried to withhold short-term release capacity.

91. Neither INGAA nor Spectra have shown that the entry barriers to constructing capacity on existing pipeline rights of way are so low that there is effective competition. Moreover, they have the opportunity to present any such detailed evidence in a proceeding seeking to show that they do not have market power, and other parties would have an opportunity to challenge such evidence. This is not a finding we can make on a generic basis in this proceeding.

c. Competitive Market Structure

92. INGAA asserts that the Commission's concern that pipelines own more pipeline capacity than their firm shippers is based on a pre-restructuring, pre-open access view of the industry, and not based on any empirical study of pipeline market power. Moreover, INGAA and Spectra assert that control of the short-term market is now primarily in the hands of pipelines' firm shippers, which have substantial rights such as capacity release, flexible point rights and segmentation rights. These shipper rights produce a competitive short-term market that cannot reasonably be bifurcated based on the identity of the seller. INGAA and Spectra state that the Commission should focus its concern not on formal ownership, but rather on the entity that controls access to or use of the capacity.

93. Spectra points out that a check on prices is not needed to prevent the exercise of market power because sufficient safeguards - in the form of competition between shippers seeking to release or acquire capacity in the short-term markets, as well as the competition between shippers and pipelines themselves - will protect the market from abuse. Further, Spectra asserts that construction of new capacity, the open access tariff,

reporting and posting requirements, and the Commission's oversight and enforcement authority will also serve as added safeguards.

94. However, as the Court of Appeals found, these arguments are comparing "apples and oranges."⁹⁸ First, the available capacity of the pipeline is on hand and ready to be sold, whereas the capacity held by releasing shippers is not necessarily available, since much of it may be needed to serve its native loads:

The petitioning pipelines assert that pipelines hold only about 7% of pipeline transportation capacity, while shippers hold the remaining 93%. This is classic apples and oranges. The Commission points out that whereas the uncontracted capacity of a pipeline is presumptively available for the short-term market, no such presumption makes sense for the non-pipeline capacity holders: they presumably contracted for the capacity in anticipation of actually using it.⁹⁹

Second, using the market shares for already existing capacity does not reflect the more important relationship of the price ceiling to construction of new capacity infrastructure which is far more critical to ensuring that the pipeline grid is expanded to meet demand. Because the pipelines are the principal parties constructing additional capacity, it is crucial that their incentive to build is not diluted by the ability to earn scarcity rents in the short-term market.

⁹⁸ INGAA at 24.

⁹⁹ Id. In addition, as previously discussed, there may be circumstances in which shippers' discounted or negotiated rate agreements contains provisions that have the effect of reducing competition from capacity release on some segments of the pipeline.

d. **Differences in Flexibility between Pipeline Capacity and Released Capacity**

95. INGAA and the pipelines argue that the pricing flexibility available to the pipelines does not allow pipelines to compete with shippers offering short-term capacity releases without a price ceiling. They argue that market-based pricing for pipelines is subject to a strenuous market-power test that involves lengthy and costly administrative proceedings. They argue that the Commission rarely finds that a pipeline meets this market-power test, and therefore it is impractical for pipelines to engage in competition with capacity releases.¹⁰⁰

96. In regard to negotiated rates, the pipelines argue that their flexibility is limited because the maximum rate is always subject to the shipper's right to elect the recourse rate, and implementation is subject to regulatory delays. INGAA and Williston also argue that the negotiated rate program offers pipelines very little, if any, opportunity to employ market-based pricing to efficiently allocate capacity to those who desire it most.

97. Third, INGAA asserts that seasonal rates do not provide the flexibility necessary to address the pipelines' competitive disadvantage under the Commission's proposal because seasonal rates result in new recourse rates, capped at the pipeline's annual revenues, not the ability to charge rates in excess of recourse rates. Spectra adds that

¹⁰⁰ INGAA at 12 (citing, KN Interstate Gas Transmission Co., 76 FERC ¶ 61,134 (1996); and Rendezvous Gas Services, L.L.C., 112 FERC ¶ 61,141, at 61,792-94 (2005)). Spectra notes that the Commission has never approved market based rates for a major natural gas pipeline. Spectra comments at 24.

seasonal rates do not allow pipelines to award the capacity to the customers who value it most because there is still a maximum rate. In addition, Spectra notes that pipelines are unable to respond to market signals in the short-term market using seasonal recourse rates. Williston asserts that seasonal rates are not a substitute for the removal of a price ceiling because they do not necessarily align prices with what the market will bear.

98. We agree that the flexibility offered to pipelines and releasing shippers is not identical, due to the differences already noted between the primary and secondary markets. The recourse rate, for example, may operate somewhat differently in the two markets by virtue of the design of these markets; but as we have found, the retention of the recourse rate is necessary to provide an effective check on both markets. Thus, we have sought to provide both pipelines and shippers with reasonably comparable flexibility consistent with the differences between these entities and the need to provide protection against market power.

99. For example, the commentors assert that the Commission has rarely granted a pipeline authority to price its capacity upon market based rates. INGAA and the pipelines make this allegation to show that it is administratively difficult to obtain market-based rates from the Commission and that is a difference from the pricing authority the Commission grants capacity releases in this rule. On the other hand, the fact that the pipelines have not been granted market based rates based on their factual showings is strong evidence that the recourse rate is still needed to protect shippers

against the exercise of market power.¹⁰¹ This fact also leaves the Commission reluctant to find that it should remove the ceiling from primary short term pipeline capacity.

100. Spectra argues that the Commission uses a stricter market power analysis to determine whether to grant a pipeline market based rates than it did to conclude that it would remove the price caps for short term capacity releases. Spectra asserts that the Commission, in removing the price ceiling from short term capacity releases, did not define the relevant product market and the relevant geographic market, nor did it calculate a Herfindahl-Hirschman Index to measure market concentration of the releasing shippers and other competing sellers in the market. Spectra argues that the Commission should remove the price caps on short-term pipeline capacity on the same basis it used for removing the caps on short-term capacity releases.

101. The Commission is not using the same analysis to remove the price ceiling from short term capacity releases as it does to determine whether a pipeline lacks market power and should therefore be permitted market based rates. As we have explained, one of the principal reasons for removing the price ceiling on released capacity is the

¹⁰¹ See e.g., Gas Transmission Northwest Corp., 119 FERC ¶ 61,288 (2007); Koch Gateway Pipeline Co., 85 FERC ¶ 61,013 (1998), order on reh'g, 89 FERC ¶ 61, 046 (1999).

existence of the pipeline's service as recourse in the event market power is exercised.¹⁰²

As the court in INGAA observed:

If holders of firm capacity do not use or sell all of their entitlement, the pipelines are required to sell the idle capacity as interruptible service to any taker at no more than the maximum rate--which is still applicable to the pipelines. [footnote omitted] Even though interruptible service may not be as desirable as firm service, the Commission concluded that it would provide an adequate substitute, whose availability would place a meaningful check on whatever anti-competitive tendencies the resellers might have.¹⁰³

102. The analysis we have employed in removing the price ceiling for released capacity is therefore more comparable to that used for pipeline negotiated rates than for the market power analysis under the Alternative Rate Design Policy statement. The continuation of the recourse rate provides sufficient protection to enable us to remove the price ceiling for short term capacity releases without doing a more detailed market power analysis.¹⁰⁴

¹⁰² Tennessee Gas Pipeline Co., 91 FERC ¶ 61,053 (2000), reh'g denied, 94 FERC ¶ 61,097 (2001), petitions for review denied sub nom., Process Gas Consumers Group v. FERC, 292 F.3d 831, 837 (D.C. Cir. 2002).

¹⁰³ INGAA at 22.

¹⁰⁴ Moreover, the Commission's use of stricter standard in reviewing petitions by a pipeline for alternative pricing authority for its primary transportation is not a new concept and is based upon the different risks of abuses of market power. In Koch Gateway Pipeline Co., 89 FERC ¶ 61,046 (1999), the Commission stated:

As reflected in the market power analysis set forth in the Policy Statement, the Commission has taken a conservative and cautious approach concerning the showing a pipeline must make in order to justify a finding that it lacks market power in its primary transportation market, i.e., the pipeline's own sale of its transportation capacity. In fact, many commenters asserted that it

(continued...)

The Commission finds, however, that there are sufficient concerns about the ability of pipelines to exercise market power in short-term transactions on at least some segments of their systems, that a blanket removal of the price cap on all such pipeline transactions in this rulemaking proceeding, without consideration of specific circumstances on individual pipeline systems, would be inappropriate.

e. **Bifurcation of the Markets**

103. The pipelines maintain that continuing the price ceiling on pipeline short term services will create a bifurcated market with higher market prices in the uncapped release market. The premise of this argument is that if shippers that place a lower value on transportation are able to acquire the capped pipeline service, the prices in the uncapped market will be higher than if all capacity were sold without a price ceiling. In the NOPR, the Commission responded to similar arguments.¹⁰⁵ The Commission pointed out that

would be unlikely that the pipeline's primary market would meet the proposed criteria for market-based rates. The Commission recognizes that it has taken a more relaxed and light-handed approach toward market-based rates in other contexts, including for example, the pipeline's sales of storage service and unbundled sales of the gas commodity. Purchasers of such other services are more likely to have good alternatives to purchasing from the pipeline; for example, barriers to entry in the storage and gas commodity markets are likely to be less. The Commission also recognizes that its Short-Term Transportation NOPR proposed a different approach for justifying removal of the price cap on short term (less than one year) transportation services in both the pipeline's primary transportation market and the secondary, capacity release market. That proposal included the establishment of mandatory capacity auctions to control market power. *Id.* at 61,129 (footnote omitted).

¹⁰⁵ NOPR at P 51.

interruptible service has lower priority than firm service so that even if a shipper placing a relatively low value on the capacity has a higher position on the pipeline's queue for price-controlled interruptible transportation, it is not guaranteed that it can acquire that capacity, leading to the supposed higher market clearing price. A firm shipper could always release its unused firm capacity to a replacement shipper who places a higher value on that capacity, thereby displacing the lower-value interruptible shipper.

104. With respect to short-term firm service, the Commission stated that higher market clearing prices would not occur as long as arbitrage exists. Any shipper with a higher queue position that acquires the pipeline capacity at the lower capped rate would have an incentive to resell that capacity to another shipper who places a higher value on the capacity, thus ensuring that the market clearing price will reflect all relevant demand.

105. INGAA asserts that the Commission's observation that pipeline short-term capacity is interruptible and inferior to firm released capacity is a partial answer to its argument that a bifurcated market will produce higher prices in the regulated portion of the market than would otherwise be the case. But INGAA and Spectra assert that short-term pipeline capacity is not always interruptible -- unsubscribed pipeline capacity can be sold on a firm basis during periods of peak demand, and would, if treated on a par with released capacity, compete on a head to head basis. INGAA and Spectra argue that if the rate for that short-term firm pipeline capacity is capped, the pricing inefficiencies will occur because the arbitrage opportunities relied upon by the Commission in the above-quoted text often entail high costs, making reliance on such opportunities inefficient. For

example, Spectra cited articles for the proposition that arbitrage opportunities “often entail high costs, making the reliance on them also inefficient.”¹⁰⁶

106. The only arbitrage costs at issue in this case are the costs of releasing that capacity, which is precisely the same cost releasing shippers must incur and we have sought to reduce the costs of capacity release over the years. In particular, the Commission’s action in Order No. 637, where the Commission instituted a number of policy revisions that were designed to enhance competition and improve efficiency across the pipeline grid should reduce arbitrage costs. There the Commission required pipelines to permit releasing shippers to use flexible point rights in order to compete effectively on release transactions with other shippers and to fully segment their pipeline capacity which permits the releasing shipper to retain the portion of the pipeline capacity it needs while releasing the unneeded portion.¹⁰⁷ This combination of flexible point rights and segmentation increases the alternatives available to shippers looking for capacity. Moreover, the Commission also required that pipelines provide shippers with scheduling equal to that provided by the pipeline, so that replacement shippers can submit a

¹⁰⁶ Spectra comments at 12, citing, Stephen J. Choi and A.C. Pritchard, Behavioral Economics and the SEC, 56 Stan. L. Rev. 1, n. 11 (2003) (discussing that “arbitrage is costly, which may limit its effect”). See also Lynn A. Stout, The Mechanics of Market Inefficiency: An Introduction to the New Finance, 28 J. Corp. L. 635, 655 (2003) (observing that “arbitrage is costly and imperfect”) and Andrei Shleifer & Robert W. Vishny, The Limits of Arbitrage, 52 J. Fin. 35 (1997) (explaining why the capital costs required to engage in arbitrage opportunities can hamper market efficiency).

¹⁰⁷ Order No. 637 at 31,300.

nomination at the first available opportunity after consummation of the capacity release transaction. This action also makes the two types of capacity more interchangeable and should reduce arbitrage costs.

107. On the other hand, we have to recognize that arbitrage can never be perfect. If it were, no interruptible transportation would be sold on fully subscribed pipelines.

Moreover, as previously discussed, in order to preserve at least some of the benefits of selective discounting, the Commission permits pipelines to include provisions in discounted rate agreements which may reduce a shipper's incentive to engage in arbitrage in certain circumstances. It is also important to recognize that the pipelines' argument for removing the price ceiling for pipeline interruptible and short-term firm capacity is predicated on arbitrage. Their essential argument is that as long as long-term prices are regulated, short-term price ceilings can be removed because shippers can purchase firm capacity in the long-term market and arbitrage that capacity by releasing it in the short-term market. If such arbitrage is costly or ineffective, as the pipelines argue here, or if a pipeline uses selective discounting to discourage arbitrage on some parts of its system, the pipelines retain market power over their sales of short-term capacity. Thus, even if arbitrage is not fully effective, that fact does not require removal of the price ceiling because impediments to arbitrage may enhance pipeline market power.¹⁰⁸

¹⁰⁸ Further, even if maintenance of the price ceiling on short-term firm capacity serves to bifurcate the market, we are concerned that lifting the price ceiling on short term firm capacity would create a perverse incentive for pipelines to forgo the sale of
(continued...)

108. In balancing the risks of creating a somewhat bifurcated market against the possibility of the exercise of market power by the pipelines in the short-term market, we have determined to err on the side of enhanced protection against market power. In INGAA, the court recognized the importance of the same trade-off between the possible bifurcation of the market and the need to continue to regulate pipeline short-term capacity. It recognized that while price distortions might occur if arbitrage is not effective,¹⁰⁹ the recourse rate applied to the pipelines provided protection with respect to both pipeline and released capacity:

If holders of firm capacity do not use or sell all of their entitlement, the pipelines are required to sell the idle capacity as interruptible service to any taker at no more than the maximum rate--which is still applicable to the pipelines.¹¹⁰

The Court concluded, and we agree that, the essential differences between pipelines and releasing shippers justified their differential treatment:

firm capacity for periods of more than a year in order to reap the uncapped rates that would be available in the short term.

¹⁰⁹ “The basic proposition asserted by the pipelines (and, as we say, recognized by the Commission) is that where (1) a portion of the supply of a good or service is subject to price controls, and (2) demand exceeds (the price-controlled) supply at the fixed price, the market-clearing price in the uncontrolled segment will be normally higher than if no price controls were imposed on any of the supply.” INGAA at 33.

¹¹⁰ Id.

Here, the distinction between pipelines and other holders of unused capacity, based on probable likelihood of wielding market power, seems to us to pass muster.¹¹¹

IV. Asset Management Arrangements

109. In this Final Rule, the Commission is revising its capacity release policies to give releasing shippers greater flexibility to negotiate and implement AMAs. AMAs are a relatively recent development in the capacity release market, and are beneficial to numerous market participants and to the market in general. However, the Commission's existing regulations and policies concerning capacity release interfere with the ability of releasing shippers to implement the most efficient AMAs. Accordingly, as discussed below, the Commission is adopting its NOPR proposals to grant an exemption from the prohibition against tying and an exemption from bidding for AMAs. The Commission is also revising the definition of AMAs proposed in the NOPR so as to relax the requirements concerning an asset manager's obligation to deliver gas to the releasing shipper and to allow supply side AMAs. In addition, the Final Rule clarifies that uncapped AMA capacity releases of one-year or less may be rolled over without competitive bidding, and that profit sharing arrangements included in an AMA will not violate any applicable price cap. The Commission also exempts certain AMAs from the buy/sell prohibition.

¹¹¹Id at 36.

A. Background

110. In general, AMAs are contractual relationships where a party agrees to manage gas supply and delivery arrangements, including transportation and storage capacity, for another party. Typically a shipper holding firm transportation and/or storage capacity on a pipeline or multiple pipelines temporarily releases all or a portion of that capacity along with associated gas production and gas purchase agreements to an asset manager. The asset manager uses that capacity to serve the gas supply requirements of the releasing shipper, and, when the capacity is not needed for that purpose, uses the capacity to make releases or bundled sales to third parties.

111. While AMAs may be fashioned in a myriad of ways, there are several common components of these arrangements. First, the releasing shipper generally enters into a pre-arranged capacity release to an asset manager ostensibly at the maximum rate in order to avoid the bidding requirement. Second, the releasing shipper makes payments to the asset manager for the gas supply service performed by the asset manager for the releasing shipper. These payments may include the releasing shipper paying the asset manager: (1) the full cost of the released capacity (e.g., maximum rate) on the theory that the asset manager is using the released capacity to transport the releasing shipper's gas supplies, (2) a management fee for transportation-related tasks (e.g. nominations, scheduling, storage injections, etc.) associated with the asset manager's obligation to provide gas supplies to the releasing shipper, and (3) the asset manager's cost of purchasing gas supplies for the releasing shipper. Third, the asset manager generally

shares with the releasing shipper the value it is able to obtain from the releasing shipper's capacity and supply contracts when those assets are not needed to supply the releasing shipper's gas needs. The asset manager obtains such value either by re-releasing the capacity or by using it to make bundled sales to third parties. The asset manager may share that value by: (1) paying a fixed "optimization" fee to the releasing shipper, (2) sharing profits pursuant to an agreed-upon formula, or (3) making its gas sales to the releasing shipper at a price below market levels.

112. In many instances the asset manager is chosen through a request for proposal (RFP) process. The RFP describes the details and terms and conditions of the proposed deal and seeks bids from service providers willing to provide the requested services. The methodology for choosing a winning bidder under an RFP often reflects many different factors, including price, creditworthiness, experience, reliability, and flexibility, and it is clear that price is not always the determining factor. Some RFP procedures are state mandated, and thus, in those situations, the LDC must get approval from the state for the final agreement.

113. As the Commission described in the NOPR, there are several ways in which the Commission's current capacity release regulations may interfere with the ability of shippers to negotiate and implement AMAs. The first relates to the Commission's prohibition against the "tying" of release capacity to any condition. The Commission established this prohibition in Order No. 636-A, using the following language:

[t]he Commission reiterates that all terms and conditions for capacity release must be posted and non-discriminatory and must relate solely to the details of acquiring transportation on the interstate pipelines. Release of capacity cannot be tied to any other conditions. Moreover, the Commission will not tolerate deals undertaken to avoid the notice requirements of the regulations. Order No. 636-A at 30,559.¹¹²

A critical component of many AMAs is that the releasing shipper be able to require the replacement shipper (asset manager) to satisfy the supply needs of the releasing shipper and take assignment of the releasing shipper's gas supply agreements as a condition of obtaining the released capacity. However, such requirements could be considered prohibited tying conditions that go beyond "the details of acquiring transportation on the interstate pipelines," because they relate to the purchase and sale of the gas commodity.¹¹³

¹¹² The Commission stated in Order No. 636-A that releasing shippers may include in their offers to release capacity reasonable and non-discriminatory terms and conditions to accommodate individual release situations, including provisions for evaluating bids. All such terms and conditions applicable to the release must be posted on the pipeline's electronic bulletin board and must be objectively stated, applicable to all potential bidders, and non-discriminatory. For example, the terms and conditions could not favor one set of buyers, such as end users of an LDC, or grant price preferences or credits to certain buyers. The pipeline's tariff also must require that all terms and conditions included in offers to release capacity be objectively stated, applicable to all potential bidders, and non-discriminatory. Order No. 636-A at 30,557.

¹¹³ Since Order No. 636-A, the Commission has granted several waivers of the prohibition against tying, Tennessee Gas Pipeline Co., 113 FERC ¶ 61,106 (2005); Northwest Pipeline Corp. and Duke Energy Trading and Marketing, 109 FERC ¶ 61,044 (2004), but only where an entity sought the waiver to exit the natural gas transportation business. See Louis Dreyfus Energy Services, L.P., 114 FERC ¶ 61,246, at 61,780 (2006), denying a waiver request.

114. AMAs also have implications for the rate cap and bidding regulations. Section 284.8 of the Commission's regulations requires capacity release transactions to be posted for competitive bidding, unless the transactions are at the maximum rate or are for 31 days or less.¹¹⁴ Section 284.8 also allows the releasing shipper to enter into a "pre-arranged" release with a designated replacement shipper before any posting for bidding.¹¹⁵ Prearranged releases are subject to the same bidding requirements as other releases; however, the prearranged replacement shipper will receive the capacity if it matches the highest bid submitted by any other bidder.¹¹⁶

115. As noted, in an AMA, the releasing shipper typically enters into a prearranged deal to release all of its pipeline capacity at the maximum rate to the marketer. It is reasonable to surmise that the main reason for the maximum release rate is so the release will qualify for the exemption from bidding of all maximum rate prearranged capacity releases. By avoiding the requirement to post the release for bidding, the releasing shipper can ensure that the capacity will go to the asset manager whom the releasing shipper has determined will provide the most effective asset management services.

¹¹⁴ 18 CFR 284.8(h).

¹¹⁵ 18 CFR 284.8(b).

¹¹⁶ 18 CFR 284.8(e).

116. As described above, however, the releasing shipper may agree to rebate some or all of the demand charge to the marketer so that the marketer's actual cost of obtaining the capacity is something less than the maximum rate. The Commission has held that such rebates render the release to be at less than the maximum rate, thereby requiring that the prearranged release be posted for bidding.¹¹⁷

117. Moreover, as described above, some AMAs may require the asset manager (replacement shipper) to pay fees to the releasing shipper. The Commission has ruled that if the prearranged release is at the maximum rate, such additional payments violate the maximum rate ceiling on capacity releases.¹¹⁸

¹¹⁷ In Louis Dreyfus Energy Services, L.P., 114 FERC ¶ 61,246 (2006), the Commission stated that:

[t]he Commission has held that any consideration paid by the releasing shipper to a prearranged replacement shipper must be taken into account in determining whether the prearranged release is at the maximum rate. For instance, where the replacement shipper agrees to pay the pipeline the maximum rate for the released capacity, but the releasing shipper agrees to make a payment to the replacement shipper, the release must be treated as a release at less than the maximum rate to which the posting and bidding requirements of sections 284.8(c) through (e) apply. Id. at P 15, citing, Pacific Gas Transmission Co. and Southern California Edison Co., 82 FERC ¶ 61,227 (1998).

¹¹⁸ See Consumers Energy Co., 82 FERC ¶ 61,284, order approving settlement, 84 FERC ¶ 61,240 (1998). See also Order No. 636-A at 30,561, where the Commission stated that capacity cannot be "resold at a rate including the pipeline marketing fee. The marketing fee is not part of the cost of transportation being released and the replacement

(continued...)

B. Discussion

118. In this rule, the Commission is revising its capacity release regulations and policies in order to facilitate the use of AMAs. Based on the industry-wide support for AMAs as shown in the comments, the Commission finds that AMAs are in the public interest because they are beneficial to numerous market participants and to the market in general. Thus, the Commission is modifying the prohibition on tying, the section 284.8 regulations concerning bidding, and making additional policy changes requested by the commenters discussed below in order to eliminate obstacles to the utilization and implementation of AMAs.

119. AMAs are a relatively recent development in the natural gas market, which the Commission did not anticipate when it adopted the capacity release program in Order No. 636. The purpose of that program was to permit shippers to “reallocate unneeded firm capacity” to those who do need it.¹¹⁹ The bidding requirements of section 284.8 and the prohibition against tying the release to extraneous conditions were all part of the Commission’s fundamental goal of ensuring that such unneeded capacity would be reallocated to the person who values it the most. The Commission found that such “capacity reallocation will promote efficient load management by the pipeline and its

shipper should not pay more than the maximum transportation rate for the capacity it is acquiring.”

¹¹⁹ Order No. 636 at 30,418.

customers and, therefore, efficient use of pipeline capacity on a firm basis throughout the year.”¹²⁰

120. The Commission thus developed its capacity release policies and regulations based on the assumption that shippers would handle their own gas purchase and transportation arrangements and release their capacity only when they were not using the capacity to serve their own needs. For example, the Commission envisioned that LDCs with long-term contracts for firm transportation service up to the peak needs of their retail customers would, during off-peak periods, release that portion of capacity not needed to serve the lower off-peak demand of its retail customers but otherwise would retain the capacity to serve their own needs.

121. However, this basic assumption underlying the capacity release program does not hold true in the context of AMAs. As the Commission stated in the NOPR, a distinguishing factor between standard capacity releases and AMAs is that in the AMA context, the releasing shipper is not releasing unneeded capacity, but capacity that it needs to serve its own supply function. Releasing shippers in the AMA context are releasing capacity for the primary purpose of transferring the capacity to entities that they perceive have greater skill and expertise both in purchasing low cost gas supplies, and in maximizing the value of the capacity when it is not needed to meet the releasing shipper’s gas supply needs. In short, AMAs entail the releasing shipper transferring its

¹²⁰ Id.

capacity to a third party expert who will perform the functions the Commission expected releasing shippers would do for themselves – purchase their own gas supplies and release capacity or make bundled sales when the releasing shipper does not need the capacity to satisfy its own needs. The goal of the changes adopted by the Commission herein is to make the capacity release program more efficient by bringing it in line with these developments in today's secondary gas markets.

122. As virtually all the commenters on the NOPR agree, AMAs provide significant benefits to a variety of participants in the natural gas and electric marketplaces and to the secondary natural gas market itself. One of the most important aspects of AMAs is that they provide broad benefits to the marketplace in general. By permitting capacity holders to use third party experts to manage their gas supply arrangements and their pipeline capacity, AMAs provide for lower gas supply costs and more efficient use of the pipeline grid. Asset managers have resources and market knowledge not necessarily available to natural gas capacity holders, such as trading platforms, credit portfolios, hedge fund and risk management experience, cost containment and counterparty credit and contracting expertise, which allow asset managers to better maximize the value of the releasing party's assets and manage the associated risk. AMAs bring diversity to the mix of capacity holders and customers that are served through the capacity release program, thus enhancing liquidity and diversity for natural gas products and services. AMAs result in an overall increase in the use of interstate pipeline capacity, as well as facilitating the use of capacity by different types of customers in addition to LDCs. AMAs benefit the

natural gas market by creating efficiencies as a result of more load responsive gas supply, and an increased utilization of transportation capacity.

123. AMAs are an important mechanism used by LDCs to enhance their participation in the secondary market and allow LDCs to increase the utilization of facilities and lower gas costs. They provide the needed flexibility to customize arrangements to meet unique customer needs. AMAs allow LDCs to use an entity with more expertise to manage their gas supply and thus relieve LDCs of administrative burdens. The ability of LDCs to use AMAs as a means of relieving the burdens of administering their capacity or supply needs on a daily basis also works to the benefit of the entire market because that burden may at times result in LDCs not releasing unused capacity.

124. AMAs also provide LDCs and their customers an increased ability to offset their upstream transportation costs. The profit sharing arrangements in AMAs often allow an LDC to reduce reservation costs that it normally passes on to its customers. They foster market efficiency by allowing the releasing shipper to reduce its costs to the extent that its capacity is used to facilitate a third party sale that also benefits that third party.

125. LDCs are not the only entities that benefit from AMAs. As evidenced by certain comments on the NOPR, many other large gas purchasers, including electric generators

and industrial users, may desire to enter into such arrangements.¹²¹ AMAs increase the ability of wholesale electric generators to provide customer benefits through superior management of fuel supply risk, allow generators to focus their attention on the electric market, and eliminate administrative burdens relating to multiple suppliers, overheads, capital requirements and the risks associated with marketing excess gas and pipeline imbalances.

126. Finally, AMAs bring benefits to consumers, mostly through reductions in consumer costs. AMAs provide in general for lower gas supply costs, resulting in ultimate savings for end use customers. The overall market benefits described above also inure to consumers. These benefits have been recognized by state commissions and the National Regulatory Research Institute.¹²² In light of these substantial benefits provided

¹²¹ See e.g., Comments of the EPSA, Comments of the EEI, Comments of FPL and Comments of the NWIGU. See also Comments of NJNG to the Commission's January 3, 2007 request for comments ("in addition to LDCs, there are many other types of large natural gas purchasers, such as electric generation facilities and large gas process industrial users, who face the same challenges with managing and optimizing their natural gas portfolios. These customers, whose core business lies outside the natural gas industry – are also likely consumers of third party portfolio management services.") at 9, n.9.

¹²² See e.g., Comments of BGEM to the January 3, 2007 request for comments at 8-9, citing to the Indiana Utility Regulatory Commission's order in Case No. 42, 973, approved April 25, 2006. See also Orders of the Massachusetts Department of Telecommunications and Energy, attached to the Marketer Petitioners comments on the January 3, 2007 request for comments, which describe and approve certain asset management arrangements.

by AMAs, the Commission is modifying its capacity release regulations and policies in the specific respects discussed below.

1. Tying

127. First, the Commission adopts its proposal to exempt AMAs from the prohibition against tying in order to permit a releasing shipper in a pre-arranged release to require that the replacement shipper (1) agree to supply the releasing shipper's gas requirements and (2) take assignment of the releasing shipper's gas supply contracts, as well as released transportation capacity on one or more pipelines¹²³ and storage capacity with the gas currently in storage. This exemption will allow firm shippers to pre-arrange releases of capacity to an asset manager (replacement shipper) along with upstream assets and gas purchase agreements in a bundled transaction where the capacity being released will be used to meet that party's gas supply requirements.¹²⁴

128. As discussed above, AMAs provide recognizable benefits to market participants and the marketplace overall in terms of more load-responsive use of gas supply, greater liquidity, increased utilization of transportation capacity and the overall efficiencies these arrangements bring to the marketplace. However, AMAs require that the releasing shipper be able to release both its capacity and its natural gas supply arrangements in a

¹²³ Commission policy already permits a releasing shipper to require a replacement shipper to take a release of aggregated capacity contracts on one or more pipelines, at least in some circumstances. See Order No. 636-A at 30,558 and n.144.

¹²⁴ The exemption is limited to releases to an asset manager to implement an AMA, and does not apply to re-releases to third parties during the term of the AMA.

single package. The very purpose of the transaction would be frustrated if the releasing shipper could not combine the supply and capacity components of the deal. This tying is meant to ensure that the released capacity will continue to be used to support the releasing shipper's acquisition of needed gas supplies. Based on the fact that AMAs provide benefits to the market, and that tying of capacity and supply is necessary to implement beneficial AMAs, it is reasonable to allow the tying conditions discussed above in the AMA context in order to foster and facilitate the use and implementation of such arrangements.

129. All the commenters support this change in Commission policy, except Williston. Williston argues that approval of the proposed changes to exempt AMAs from the prohibition on tying (as well as the bidding requirements discussed in the next section) would encourage discrimination and preferential treatment toward asset managers by allowing participants in the secondary capacity release market to engage in activities prohibited to pipelines.¹²⁵ According to Williston, allowing releasing shippers to tie releases to a requirement that the replacement shipper provide asset management services, and exempting such releases from bidding, will give releasing shippers a strong competitive edge over the pipelines for the sale of similar types of services. Williston asserts the pipelines' reduced sale of similar types of services will result in increased firm transportation rates charged by pipelines. Williston also claims that exempting AMAs

¹²⁵ Comments of Williston Basin at 12-14.

from tying will nullify the goal of awarding capacity to the shipper that values it most and that removing the bidding requirement will inhibit transparency.¹²⁶

130. Williston has failed to show that exempting capacity releases to implement AMAs from the prohibition against tying and bidding will subject pipelines to unfair competition. Pipelines' core business is providing unbundled transportation services. By contrast, a major component of asset management service is the purchase and sale of gas as a commodity. Williston does not assert that it has any interest in either providing or purchasing asset management services. Therefore, Williston has no need or reason to tie the sale of its transportation services to the provision of asset management services. Many shippers, by contrast, have indicated a desire to purchase (or provide) asset management services, and as discussed above, the Commission has found that such services provide substantial benefits to the natural gas and electric markets as a whole. Williston has not identified any tying requirement that it would desire to impose on the sale of its unsubscribed capacity that would provide comparable benefits to the market as a whole.

131. The Commission recognizes that, to the extent asset managers are more skilled at releasing and managing capacity in competition with the pipelines' interruptible services, pipelines may face increased competition from capacity release as a result of this rule.

¹²⁶ The Commission explains in the next section how the benefits AMAs outweigh any disadvantages in exempting such releases from bidding and how the Final Rule will continue to satisfy the goals of disclosure and transparency.

The Commission, however, has always intended that capacity releases would compete with the pipelines' short-term firm and interruptible transportation services.¹²⁷

Accordingly, the fact that this rule may result in greater competition for pipelines' interruptible services is not a compelling reason for the Commission to decline to facilitate AMAs as set forth in this Final Rule.

2. **Bidding**

132. Second, the Commission adopts its proposal to exempt pre-arranged releases to implement AMAs from the bidding requirements of section 284.8 of its regulations. In light of its experience with capacity releases and the comments discussed above, the Commission concludes that, in the AMA context, the bidding requirement creates an unwarranted obstacle to the efficient management of pipeline capacity and supply assets.

133. All capacity releases made to implement AMAs are pre-arranged because it is important that a releasing shipper be able to use the asset manager of its choice to effectuate the components of the agreement. Unlike a normal capacity release where the releasing shipper is often shedding excess capacity and has no intention of an ongoing relationship with the replacement shipper, in the AMA context the identity of the

¹²⁷ See Order No. 636-A at 30,553 and 30,556 (stating “the Commission views the competition between interruptible transportation and capacity releasing as part of a healthy secondary market” and finding “pipeline capacity (firm and interruptible) must compete with released capacity”); see also UDC v. FERC, 88 F.3d 1105, 1149 (D.C. Cir. 1996) (recognizing that capacity release is intended to develop an active secondary market with holders of unutilized firm capacity rights reselling those rights in competition with capacity offered directly by the pipeline).

replacement shipper is often critical because it will manage the releasing shipper's portfolio for some time into the future. During the process of choosing an asset manager (often an RFP process), the releasing shipper considers a number of factors, including experience in managing capacity and gas sales, experience with a particular pipeline or area of the country, flexibility, creditworthiness and price. Because the asset manager will manage the releasing shipper's gas supply operations on an ongoing basis, it is critical that the releasing shipper be able to release the capacity to its chosen asset manager. Requiring releases made in order to implement an AMA to be posted for bidding would thus interfere with the negotiation of beneficial AMAs, by potentially preventing the releasing shipper from releasing the capacity to its chosen asset manager. Moreover, AMAs at their core entail a bundling of commodity sales with capacity release. As a result, it is difficult to have meaningful bidding on the released capacity as a stand-alone component of the arrangement, because the values of the commodity and capacity components of the arrangement are not easily separated. The Commission concludes that the benefits of facilitating AMAs outweigh any disadvantages in exempting such releases from bidding.

134. The exemption from bidding adopted by this rule will apply to all releases to asset managers, made for the purpose of implementing an AMA, regardless of the term of the AMA and whether the release is subject to the price ceiling. As discussed above, in this rule the Commission is removing the price ceiling for all short-term capacity release transactions of one year or less, but is continuing the price ceiling for capacity release

transactions of more than one year. In the NOPR, the Commission stated that, if the parties wanted to continue an uncapped short-term capacity release beyond one year, the release “would have to be re-posted for bidding to ensure the capacity is allocated to the highest valued use.”¹²⁸ Some commenters¹²⁹ request that the Commission clarify that the reposting and bidding requirements for extending uncapped, short-term capacity releases beyond one year do not apply in the context of short-term AMAs. They assert that the proposed exemption from bidding for capacity releases to asset managers should apply in all circumstances, including the circumstance of an expiring short-term release related to an AMA. In essence, they inquire whether the reposting and bidding requirements for extensions of short-term capacity releases would trump the general exemption from bidding requirements proposed by the Commission for AMAs.

135. The Commission clarifies that the exemption from bidding for AMAs adopted in this rule applies to all releases to an asset manager, including those made for the purpose of extending a short-term AMA.¹³⁰ The rationale for exempting releases to an asset

¹²⁸ NOPR at P 44.

¹²⁹ See e.g., comments of Southwest and BGEM.

¹³⁰ Section 284.8(h)(1), as adopted by this rule, provides a blanket exemption from posting and bidding for all releases to an asset manager:

A release of capacity by a firm shipper to a replacement shipper for any period of 31 days or less, a release of capacity for more than one year at the maximum tariff rate, or a release to an asset manager as defined in (h)(3) of this section need not comply with the notification and bidding requirements of paragraphs (c) through (e) of this section. (emphasis added).

(continued...)

manager from bidding applies equally to releases made for the purpose of extending a short-term AMA as to any other release to an asset manager. In all such releases, the identity of the asset manager is critical to the releasing shipper, because the releasing shipper will be relying on the asset manager to obtain its gas supplies. Therefore, as with any other release to an asset manager, requiring releases made for the purpose of extending a short-term AMA to be posted for bidding could interfere with the negotiation of beneficial AMAs by potentially preventing such releases to be made to the releasing shipper's chosen asset manager.

136. While the Commission is exempting releases made to implement AMAs from the capacity release bidding requirements, those releases will remain subject to existing posting and reporting requirements, including the section 284.13(c)(2)(viii) requirement to post the name of any asset manager. In addition, as discussed below, the Commission is adding a requirement to post the asset manager's delivery obligation to the releasing shipper. Therefore, the Commission's goals of disclosure and transparency will still be met. Williston's argument that the exemption from bidding for AMAs will impair

The section 284.8(h)(2) prohibition on extending exempt releases without posting and bidding expressly applies only to the first category of releases included in the section 284.8(h)(1) exemption: releases for a period of 31 days or less.

transparency and allow deals to be consummated without Commission or market participant knowledge thus fails.¹³¹

137. The exemption from bidding adopted by this rule does not extend to releases made outside the AMA context. There has been no showing that non-AMA prearranged releases provide benefits of the type we have found justify exempting AMA releases from bidding. Moreover, in the typical non-AMA pre-arranged release, price is the primary factor, and therefore the releasing shipper should generally be indifferent as to the identity of the replacement shipper so long as it receives the highest possible price. Accordingly, non-maximum rate capacity releases of more than 31 days, made outside the AMA context, will still need to be posted for bidding in order to ensure that the capacity is allocated to the highest valued use.

3. Definition of AMAs

a. NOPR Proposal

138. In the NOPR, the Commission proposed to define AMAs that would qualify for the tying and bidding exemptions, as follows:

¹³¹ Williston Basin is also incorrect in suggesting that the Commission requires pipelines to sell their available capacity in a bidding auction. See Northern Natural Gas Co., 110 FERC ¶ 61,361, at P 10 (2005) ("[T]he Commission has not required pipelines to sell capacity solely through open seasons. Rather, so long as the pipeline posts all available firm capacity, it may sell that capacity on a first-come, first-served basis").

any pre-arranged release that contains a condition that the releasing shipper may, **on any day**, call upon the replacement shipper to deliver to the releasing shipper a volume of gas **equal to** the daily contract demand of the released transportation capacity. If the capacity release is a release of storage capacity, the asset manager's delivery obligation need only equal the daily contract demand under the release for storage withdrawals (emphasis added).

139. The Commission developed this definition in order to address two concerns relating to its facilitation of AMAs. It wanted to limit the exemptions from tying and bidding to bona fide AMAs, that is, arrangements that place a significant delivery obligation on the replacement shipper so as to distinguish AMAs eligible for the exemptions from standard capacity releases. The Commission also sought to avoid a definition that was too narrow and would effectively limit efficient and innovative AMAs. The Commission focused on what it understood to be the fundamental purpose of AMAs, namely that the asset manager would use the released capacity to deliver gas supplies to the releasing shipper. Thus, it included the requirement that the replacement shipper contractually commit itself to deliver to the releasing shipper, on any day, gas supplies equal to the daily contract demand of the released capacity. The Commission reasoned this would achieve the goal of exempting only bona fide AMA transactions from bidding and the prohibition against tying.

140. The Commission also believed that the proposed definition was sufficiently flexible to allow releasing shippers to use AMAs to obtain only a portion of its required gas supplies or to enter into multiple AMAs with different asset managers. In addition, the Commission noted that the proposed definition does not require that the asset

manager make all its deliveries to the releasing shipper over the released capacity, nor did it limit the types of entities that can use AMAs and take advantage of the exemptions.

The Commission recognized that electric generators and industrial end-users may make use of AMAs, and thus the exemption is not limited to LDCs utilizing AMAs.

b. Comments

141. Numerous commenters¹³² requested that the Commission revise or clarify the “on any day” and/or the “equal to” phrases highlighted in the definition above. They claim that “on any day” may be interpreted as requiring the asset manager to stand ready to deliver the contract quantity on “every day” in order for the arrangement to be considered an AMA. Commenters assert that such a requirement would severely inhibit the asset manager’s flexibility and its ability to maximize the value of the capacity. Many commenters also seek to replace “equal to” the daily contract demand of the released capacity with “up to.” Again, commenters cite a lack of flexibility and devaluation of the released capacity because it would inhibit the asset manager from re-releasing the capacity. Commenters note that the beneficial aspects of AMAs are hindered if the asset manager must hold in reserve the entire portfolio of its assets even on days when the releasing shipper does not need the capacity for its supply needs.

¹³² Those commenters include the AGA, BGEM, BP, Canadian Association of Petroleum Producers (CAPP), FPL Hess, the Marketer Petitioners, National Grid, NJNG, NGSAs, Nicor Enerchange (Nicor), NJR, Piedmont, PPM, PSNC, SCE&G, SEMI, Sequent, Statoil and WDG.

142. Commenters suggest several general language changes to remedy these perceived problems. AGA recommends that the Commission clarify the definition by adding “but not necessarily every day” after the phrase “on any day.” It also suggests changing “equal to” to “up to” as noted above.¹³³ BGEM agrees with this latter change, as do FPL, National Grid, PPM, and PSNC. Others take a broader view, suggesting that the delivery obligation should be left to the parties to negotiate. BP, for example, advocates permitting the parties to determine by mutual agreement when the releasing shipper may call upon the replacement shipper to deliver to it a volume of gas equal to the daily contract demand.¹³⁴ Numerous parties agree with the concept that the details of the delivery obligation should be left to the parties and spelled out in the contract. NGSA comments that “may, on any day, call upon” should be revised to “may, as agreed by the parties, require...”¹³⁵ Nicor would add the phrase “pursuant to the terms of its contract” after “any day”. It would also clarify that the replacement shipper should be required to deliver gas to a “location” specified in the agreement.¹³⁶ Piedmont suggests that parties be permitted to negotiate call rights “as necessary and appropriate for the contracting

¹³³ AGA provides a revised definition on page 21 of its comments.

¹³⁴ See BP comments at 2, 5-8.

¹³⁵ NGSA comments at 10.

¹³⁶ Nicor comments at 2-3.

parties.”¹³⁷ SCANA suggests that because the releasing shipper is in the best position to know the appropriate level of delivery obligation it will require, the definition should be revised to clarify that the delivery requirement is limited to specified days set forth in the agreement.¹³⁸ The WDG suggests that parties should be given the flexibility to “tailor” capacity recall rights in AMA transactions to the releasing shipper’s market and supply needs.¹³⁹

143. NJNG also recommends that the definition of AMA be clarified such that a releasing shipper’s recall rights up to the maximum daily quantity of the released capacity is limited to use by the releasing shipper for its “own load” requirements – either its utility retail service obligation or its own system generation or consumption needs.

c. Modified Definition

144. In light of the comments received, the Commission has reconsidered its definition of AMAs and in this rule is modifying the definition to strike a balance between facilitating flexible and innovative AMAs and drawing a clear line between AMAs and

¹³⁷ Piedmont comments at 6.

¹³⁸ Scana comments at 4-7.

¹³⁹ WDG comments at 4-5.

standard capacity releases.¹⁴⁰ The specific modifications to the definition which the Commission is making for this purpose are shown in bold below:

any pre-arranged release that contains a condition that the releasing shipper may, **on any day during a minimum period of five months out of each twelve-month period of the release**, call upon the replacement shipper to deliver to the releasing shipper a volume of gas **up to one-hundred percent** of the daily contract demand of the released transportation capacity. **If the capacity release is for a period of less than one year, the asset manager's delivery obligation described in the previous sentence must apply for the lesser of five months or the term of the release.** If the capacity release is a release of storage capacity, the asset manager's delivery obligation need only **be one-hundred percent** of the daily contract demand under the release for storage withdrawals.¹⁴¹

145. The Commission finds that this definition of AMA will further its goal of delineating AMAs from standard capacity releases. First, it continues to differentiate bona fide AMAs from standard capacity releases by placing a significant delivery obligation, applicable during at least five months out of each 12 month period of the release, on the asset manager, while alleviating the concerns of those commenters that assert the NOPR definition was too restrictive. The Commission has replaced “equal” in

¹⁴⁰ As discussed in detail below, the Commission is also revising the AMA definition to allow for supply AMAs and to extend to retail state unbundling programs the same blanket exemption from bidding granted for AMAs.

¹⁴¹ The annual five month minimum would apply to AMAs with terms of one year or longer. The delivery obligation for any AMA between five months and a year would be for five months of the release. The delivery obligation would apply to the entire term for any AMA of less than five months.

the definition with “up to” in order to clarify that the asset manager does not have to actually make deliveries equal to the daily contract demand on every day the delivery obligation is in effect. However, by using the phrase “up to” in the adopted definition, the Commission does not intend to allow the parties to negotiate a potential delivery obligation of less than one hundred percent of the daily contract demand for the required time period, even though that amount may not actually be delivered to the releasing shipper every day. Before entering into an AMA an asset manager should be able to make reasonable judgments about the releasing shipper’s requirements based upon the releasing shipper’s gas usage in earlier years, and thus make reliable estimations as to when it can use the capacity for bundled sales or re-releases. Thus, under the definition adopted in this rule, the releasing shipper will have the right to call upon the asset manager to deliver the full contract volume on every day of the five month minimum, though it need not actually do so. This delivery obligation for the asset manager will adequately distinguish AMAs from standard capacity releases as well as ensure that AMAs eligible for the exemptions from tying and bidding will fulfill the primary purpose of using the releasing shipper’s capacity to supply its gas needs during peak periods.

146. The definition also furthers the goal of defining AMAs in such a way that they will be flexible enough to allow diverse parties to enter into AMAs and for those parties to be able to maximize the value of pipeline capacity within the context of an AMA. The definition only requires a delivery obligation on behalf of the replacement shipper for a portion of each twelve month period, thus giving the asset manager additional assurance

it can utilize the capacity during non peak periods. The definition adopted in this rule also allows for releasing shippers to only release a portion of their capacity, places no limitations on the asset manager that would require it to use the released capacity to make its deliveries to the releasing shipper, and does not limit the type of party that can enter into an AMA.

147. The Commission considered the comments that the extent of the asset manager's delivery obligation should be left to the parties to negotiate themselves but ultimately determined that approach would not further the primary goal of AMAs that they be used to serve the releasing shipper's supply needs. Absent a specific delivery obligation in the definition, there would be no assurances that capacity releases meant to implement an AMA would actually contain a substantial delivery obligation that would differentiate it from a standard capacity release. Parties would be able to enter into arrangements that may require an asset manager to deliver supply to the releasing shipper on only one day of the year for instance. Such arrangements would technically qualify as AMAs but would not serve the Commission's goal to ensure that AMAs be used to serve the releasing shipper's needs. Accordingly, the Commission does not deem it appropriate to grant the benefits of the exemptions from tying and bidding to such arrangements.

4. Supply AMAs

148. In the NOPR the Commission sought comments on whether it should expand the definition of AMAs and if so, how supply side AMAs should be distinguished from other capacity releases. The Commission in this Final Rule is revising its regulations and the

proposed definition of AMAs to allow for supply side AMAs. Pursuant to the revised definition for AMAs discussed below, a supply AMA will be distinguishable from a standard capacity release, and thus eligible for the tying and bidding exemptions, only if it includes a condition that requires the replacement shipper to purchase a volume from the releasing shipper up to the maximum daily contract demand of the released capacity.

149. In general, gas supply AMAs are arrangements where a production area capacity holder releases capacity to an asset manager that commits to purchase (receive) the releasing shipper's gas and use the capacity to transport and market that gas. The asset manager nets back to the producer a fixed percentage of the price that the asset manager is able to obtain for resale of the gas on a delivered basis. Numerous producer and marketer commenters filed in favor of AMAs for gas sellers.¹⁴² No commenter opposed expanding the AMA definition to include gas supply AMAs.

150. Based on the comments received, the Commission finds that the benefits of AMAs as identified in the NOPR apply with equal weight to producers that want to optimize the value of their capacity and minimize costs. The Commission understands from producer commenters that producers often acquire firm pipeline capacity for flow assurance, that is, to ensure that there will be sufficient capacity to transport the gas they produce to

¹⁴² See e.g., comments of NGSA, BGEM, BP, Dominion Marketers, FPL, Marketer Petitioners, Mewbourne Oil, NEM, Nicor, NJR, Statoil, Ultra, Walter Oil and Gas, and the Wyoming Pipeline Authority.

relevant markets.¹⁴³ Because of the fluctuation in flows related to new wells in particular, producers often purchase capacity in excess of their immediate needs to ensure that there is sufficient capacity for their gas to flow once the production volumes ramp up. The Commission's approval of supply AMAs will allow a producer to release all of its capacity to an asset manager who could maximize the value of that capacity during the start-up period when producers may not need it, resulting in increased and efficient use of capacity.

151. The Commission also finds that the rationale supporting AMAs for end users equally supports supply AMAs. Supply AMAs will help to alleviate a producer's burden of administering capacity on a day to day basis, will maximize the value of pipeline capacity, and will further diversify the mix of capacity holders and customers served through capacity releases. Similar to delivery AMAs, supply AMAs involve an ongoing relationship between the releasing shipper and the asset manager that differentiates the deals from normal capacity releases.¹⁴⁴ Further, supply AMA capacity will be used for its original purpose, that is, to transport the producer's gas to the market place. The Commission finds reasonable comments that the purchase obligation in a supply side

¹⁴³ See e.g., comments of BP.

¹⁴⁴ See e.g., comments of NGSA at 14.

AMA is a mirror image of the delivery obligation required by the Commission for the downstream AMA's facilitated in the NOPR.¹⁴⁵

152. As discussed above, in the Commission's view the most important aspect of a supply AMA is the requirement that the asset manager commit to purchasing the releasing shipper's gas as a part of the agreement. While several commenters suggest definitional language for gas supply AMAs that would require the replacement shipper to "receive" the releasing shipper's gas,¹⁴⁶ the Commission finds that the condition must be to "purchase" the gas in order to avoid running afoul of the shipper must have title rule.¹⁴⁷

¹⁴⁵ Comment of NGSAs at 13, comments of Ultra at 8.

¹⁴⁶ For example, Statoil states that the Commission should extend the exemption to include supply-side AMAs by expanding its proposed section 284.8(h) as follows:

(h)(3) A release to an asset manager exempt from bidding requirements under paragraph (h)(1) of this section is any prearranged capacity release that contains a condition that the releasing shipper may, on any day, call upon the replacement shipper to **(i) deliver to the releasing shipper a volume of gas equal to the daily contract demand of the released transportation capacity or the daily contract demand for storage withdrawals or (ii) receive from the releasing shipper a volume of gas equal to the daily contract demand of the released transportation capacity or the daily contract demand for storage withdrawals.** Statoil comments at 12-13.

¹⁴⁷ As described in the comments, a typical supply AMA could involve a requirement that the replacement shipper accept delivery of the releasing shipper's gas, and use the capacity released to ship and market that gas. Under that scenario, where the replacement shipper would accept the releasing shipper's gas and transport that gas on the released capacity to the releasing shippers' customers, the arrangement would violate the Commission's requirement that the shipper hold title to the gas. The shipper in that
(continued...)

This condition would also help ensure that such arrangements are bona fide AMAs because it imposes a significant purchase obligation on the asset manager.

153. Based on the determination to allow supply AMAs, the Commission will further modify the proposed definition of capacity releases to asset managers to accommodate supply AMAs. Thus, the full definition of the capacity releases that will be eligible for the tying and bidding exemptions adopted by this rule is as follows:

any pre-arranged release that contains a condition that the releasing shipper may, on any day during a minimum period of five months out of each twelve-month period of the release, call upon the replacement shipper to (i) deliver to the releasing shipper a volume of gas up to one-hundred percent of the daily contract demand of the released transportation capacity or (ii) purchase a volume of gas up to the daily contract demand of the released transportation capacity. If the capacity release is for a period of less than one year, the asset manager's delivery or purchase obligation described in the previous sentence must apply for the lesser of five months or the term of the release. If the capacity release is a release of storage capacity, the asset manager's delivery or purchase obligation need only be one-hundred percent of the daily contract demand under the release for storage withdrawals or injections, as applicable.

5. AMA profit sharing arrangements

154. AMAs generally include provisions for the asset manager to share with the releasing shipper the value it is able to obtain from the releasing shipper's capacity and

situation would be the replacement shipper, and it would be transporting gas that was owned by the releasing shipper. Thus, in order for there to be a valid supply AMA, the replacement shipper must purchase and take title to the gas that it will ship for the releasing shipper.

other assigned assets when those assets are not used to serve the releasing shipper. The manager may share that value by: (1) paying a fixed “optimization” fee to the releasing shipper; (2) sharing with the releasing shipper the asset manager’s profits from the use of the released capacity and other assigned assets¹⁴⁸ pursuant to an agreed-upon formula; (3) making gas sales to the releasing shipper at a below-market commodity price; or (4) in some other way mutually agreed to by the contracting parties.¹⁴⁹

155. As discussed above, while this rule removes the price ceiling for all short-term capacity release transactions of one year or less, the Commission is continuing the price ceiling for capacity release transactions of more than one year. Numerous commenters, including marketers, LDCs, and producers are concerned that AMA profit sharing arrangements, such as those described above, may be considered to violate the price ceiling for long-term capacity releases. Accordingly, they contend that the Commission should either (1) exempt long-term capacity releases to asset managers from the price ceiling or (2) determine that the maximum rate does not apply to the asset manager’s payments to the releasing shipper under such profit sharing arrangements.

¹⁴⁸ These uses could include re-releases of the capacity or bundled sales to third parties.

¹⁴⁹ The AMA may also require the releasing shipper to make payments to the manager for the services performed by the manager for the releasing shipper under the AMA. These payments may include the releasing shipper paying the manager: (1) a management fee for transportation related tasks (e.g. nominations, scheduling, storage injections) associated with the manager’s obligation to provide gas supplies to the releasing shipper, and (2) the manager’s cost of purchasing gas supplies for the releasing shipper.

156. AGA, FPL, Integrys,¹⁵⁰ the Marketer Petitioners, NGSa, PGC, NWIGU, Southwest, and others request that the Commission clarify that the various payments made by or to an asset manager under an AMA will not be attributed or imputed to the transportation component of an AMA, and that payments by the parties to one another will not be viewed as causing the maximum rate ceiling to be exceeded for any releases made pursuant to an AMA. Alternatively, they request that the Commission clarify that the price ceiling is removed for all capacity releases associated with an AMA, regardless of their term.

157. These commenters explain that applying the price ceiling to profit sharing arrangements in long-term releases to an asset manager could significantly hinder parties' ability to successfully structure an acceptable AMA. They assert that limiting the compensation the releasing shipper can collect from the asset manager under long-term releases would prevent the releasing shipper from sharing in the full market value the asset manager is able to obtain from the capacity, contrary to the basic purpose of an AMA. This could discourage parties from entering into AMAs with terms of more than a year. These commenters further state that the parties frequently desire to enter into AMAs with terms of two or three years, because longer-term AMAs provide the parties

¹⁵⁰ The Integrys Gas Group (Integrys) consists of the Michigan Gas Utilities Corporation, Minnesota Energy Resources Corporation, North Shore Gas Company, The Peoples Gas Light and Coke Company, and Wisconsin Public Service Corporation.

with a greater ability to plan their business operations for a longer period of time and are administratively more efficient.

158. In response to these comments, the Commission is modifying section 284.8(b) of its regulations to clarify that the price ceiling does not apply to any consideration provided by an asset manager to the releasing shipper as part of an AMA. However, apart from this clarification, capacity releases of more than one year to an asset manager will, like any other long-term capacity release, remain subject to the price ceiling. This modification of the Commission's regulations will provide the parties to an AMA the flexibility to negotiate mutually acceptable arrangements under which the asset manager shares with the releasing shipper the value it obtains from the released capacity, without running afoul of the capacity release price ceiling. However, the price ceiling will continue to apply to the rates the asset manager pays to the pipeline for the released capacity.¹⁵¹

¹⁵¹ As pointed out in the NOPR, in Consumers Energy Co., 82 FERC ¶ 61,284, order approving settlement, 84 FERC ¶ 61,240 (1998), the Commission investigated certain joint marketing agreements whereby replacement shippers agreed either to share with the releasing shipper revenues obtained by the replacement shippers on the sales of the gas transported by means of the released capacity or to pay the releasing shipper prices based on the amount of gas bought and sold. The Commission found in this situation that Consumers had collected money in excess of the pipeline's maximum rate, thereby violating the capacity release price ceiling. Recently, the Commission similarly held in Louis Dreyfus Energy Services, L.P., 114 FERC ¶ 61,246, at 61,779 (2006), that if a pre-arranged release is at the maximum rate, additional payments by the replacement shipper to the releasing shipper are deemed to render the release price above the maximum rate. As a result of the modification to section 284.8(b) adopted in this rule,

(continued...)

159. The Commission finds that this change in its regulations is consistent with the overall goal of this rulemaking of facilitating beneficial AMAs. In the AMA context, unlike in other capacity release situations, the releasing shipper is not releasing unneeded capacity, but capacity that is needed to serve its own supply function and will be so used during the term of the release. Releasing shippers enter into AMAs “for the primary purpose of transferring the[ir] capacity to entities they perceive have greater skill and expertise both in purchasing low cost gas supplies and in maximizing the value of the capacity when it is not needed to meet the releasing shipper’s gas supply needs. In short, AMAs entail the releasing shipper transferring its capacity to another entity that will perform the functions the Commission expected releasing shippers would do for themselves – purchase their own gas supplies and release capacity or make bundled sales when the releasing shipper does not need the capacity to satisfy it owns needs.”¹⁵²

160. Thus, a fundamental purpose of an AMA is for the asset manager to extract as much value from the released capacity and assigned assets as possible and to share that value with the releasing shipper, who has contracted with the asset manager precisely because of the asset manager’s expertise in this area. The asset manager generally obtains revenues related to the released capacity from two basic revenue sources. First, the asset manager may earn money through the re-release of the releasing shipper’s

these precedents will not apply in the context of capacity releases to asset managers. However, these precedents will continue to apply to all other capacity releases.

¹⁵² NOPR at P 66.

capacity for a higher value. For example, the asset manager could enter into short-term re-releases of the capacity that are not subject to the price cap. Second, the asset manager could garner funds through utilizing the released capacity to make bundled sales to third parties. In either situation, the releasing shipper could have attempted to garner these revenues by itself, but instead it utilized the asset manager's skills through the use of an AMA to increase the value of its capacity.¹⁵³

161. Given that the purpose of an AMA is to allow a releasing shipper to maximize the value of its capacity by obtaining the services of an asset manager with greater expertise at accomplishing that goal, it makes little sense to apply the price ceiling on long-term capacity releases in a manner which limits the amount of that value which the asset manager can share with the releasing shipper. As discussed above, permitting the asset manager to maximize the value of released capacity and share that value with the releasing shipper provides numerous benefits, including reducing the releasing shipper's costs of reserving pipeline capacity, and these benefits ultimately serve to reduce consumer costs. Moreover, as some commenters point out, applying the long-term

¹⁵³ There are a number of other potential methods for an asset manager to gain additional revenues from a releasing shipper's transportation, storage, gas supply, and hedging "assets". An asset manager may use the full range of acquired "assets" to enter into a variety of financial, commodity, transportation, or storage-related arrangements which allows the asset manager to generate more revenues from these "assets," when they are not needed to serve the releasing shipper's direct needs, than the releasing shipper would have generated on its own. We do not mean to suggest here any limit to the range of legally-allowed transactions that an asset manager may pursue, but merely provide illustrative examples.

capacity release price ceiling to AMA profit sharing arrangements would likely discourage parties from negotiating AMAs with terms of more than a year in order to avoid the price ceiling. However, longer-term AMAs may provide the parties significant advantages, for example, by enabling the parties to obtain greater certainty concerning their gas supply and sale arrangements for a longer period of time and by minimizing the administrative costs of negotiating multiple AMA arrangements over a relatively short period of time.

162. Thus, the Commission concludes that profit sharing agreements between the releasing shipper and the replacement shipper in the context of an AMA, where the releasing shipper could have earned the monies itself, should not violate the price ceiling just because the releasing shipper utilized the skills of an asset manager. Modifying our regulations to exempt all such profit sharing arrangements from the price ceiling will permit the parties flexibility to craft AMAs in a manner that they perceive as capturing the true value of the release and related assignments of other assets, consistent with our goal of facilitating the use of AMAs.

6. Exemption from Buy/Sell Prohibition

163. Some commenters state that they wish to enter into AMAs whereby they would release their capacity to an asset manager, but would continue to negotiate their own gas purchase contracts. Because such gas supply contracts would be competitively negotiated arrangements containing confidential pricing information, these commenters

do not want to assign such contracts to the asset manager.¹⁵⁴ Instead, they want to sell the gas they purchase from their supplier to their asset manager and then direct the asset manager to transport the gas to their city gate and resell the gas to them. These commenters ask that the Commission exempt such arrangements from the Commission prohibition on buy/sell arrangements.

164. The Commission prohibited buy/sell arrangements in Order No. 636 and companion orders in El Paso Natural Gas Company.¹⁵⁵ Order No. 636 stated that “[u]nder those arrangements, an LDC will purchase gas in the production area from an end-user or a merchant designated by an end-user. The LDC will ship the gas on its own firm capacity and sell the gas to the end-user at the retail delivery point.”¹⁵⁶ The Commission explained that it had adopted a nationally uniform capacity release program in order to provide greater assurance that transfers of capacity from one shipper to another were transparent and not unduly discriminatory. The Commission found that permitting buy/sell arrangements would frustrate this goal, because such arrangements

¹⁵⁴ See e.g., NWIGU comments at 7, PGC comments at 6, Weyerhaeuser comments at 3-11.

¹⁵⁵ 59 FERC ¶ 61,031, reh’g denied, 60 FERC ¶ 61,117 (1992).

¹⁵⁶ Order No. 636 at 30,416. In Order No. 636-B, 61 FERC ¶ 61,272, at 61,997 (1992), the Commission clarified that the buy/sell prohibition applies to all firm capacity holders, not just LDCs. See also, In re BP Energy Co., 121 FERC ¶ 61,088, at P 14 (2007).

“would provide a major loophole, potentially inviting substantial circumvention of the capacity release mechanism.”¹⁵⁷

165. The Commission grants an exemption from the buy/sell prohibition for AMAs that qualify for the exemptions from bidding and tying, but only for volumes of gas delivered to the releasing shipper. In this proceeding, the Commission is modifying its regulations and policies in order to facilitate the development of efficient and beneficial AMAs. Consistent with this objective, the Commission will permit shippers to hire an asset manager solely for the purpose of managing their interstate pipeline capacity, while they continue to purchase their gas supplies from a different marketer under contracts which they do not assign to the asset manager.

166. As the commenters explain, the marketer having the best terms and price for asset management services is not always the marketer who is able to supply the gas commodity at the lowest cost. Moreover, such marketers may be in direct competition with each other, both in the asset management field and in the commodity supply area. Such competition helps the end-user obtain the lowest possible delivered cost for its gas supplies. The commenters state, however, that in such circumstances, the releasing shipper may prefer not to assign its gas purchase contracts to the marketer providing asset management services for their pipeline capacity because this would reveal competitively sensitive information concerning the commodity prices offered by the other marketer.

¹⁵⁷ El Paso, 59 FERC at 61,080.

Rather, the releasing shipper could avoid this result by entering into what is in essence a buy/sell transaction, in which the releasing shipper would purchase the gas commodity from someone other than its asset manager and sell that gas to the asset manager.¹⁵⁸ The asset manager would then use the released capacity to transport the gas to the shipper and resell the gas to the shipper at the delivery point.

167. The Commission finds that exempting such transactions from the buy/sell prohibition is appropriate, in light of the above-described benefits of AMAs in which the asset manager only manages the releasing shipper's pipeline capacity. This exemption will not undercut the Commission's goal in adopting the prohibition on buy/sell arrangements of preventing circumvention of the capacity release program. As we have previously explained, capacity releases to an asset manager differ from other releases, because the releasing shipper is not releasing unneeded capacity, but capacity that will continue to be used to serve its own supply function during the term of the release. The purpose of the buy/sell transactions at issue here is to permit the releasing shipper to negotiate its own gas purchase arrangements with a third party, while having its asset manager transport the gas over the released capacity to the releasing shipper. Thus, the asset manager's purchase from the releasing shipper and resale to that shipper enables the released capacity to be used to meet the releasing shipper's own gas requirements and is a condition of the capacity release. This is unlike the buy/sell transactions prohibited by

¹⁵⁸ The sale to the asset manager is necessary to avoid a violation of the shipper-must-have title requirement.

Order No. 636, where the purchases, transportation, and re-sales were for the purpose of meeting the gas requirements of a third party, and there was no capacity release to any participant in the transactions. While, here, the asset manager would be buying gas from, and reselling it to, the releasing shipper, the capacity release to the asset manager would be done in accordance with the Commission's capacity release regulations and as such, would be transparent to the market. The parties would need to comply with all the notice and posting provisions currently in place. Further, the Commission has found that AMAs are beneficial to the secondary gas markets. By providing a limited exemption from the buy/sell prohibition for AMAs, the Commission is further facilitating the flexibility of AMAs and promoting enhanced competition in the capacity release market.

168. The Commission also clarifies, as requested by several commenters, that an AMA does not necessarily need to involve an assignment of gas supply contracts.¹⁵⁹ Those commenters suggest that while an AMA may involve an assignment of gas supply agreements, an AMA should not be so limited because the asset manager may have different supply sources from which to draw. For example, the releasing shipper may enter into a supply agreement directly with the asset manager, or the asset manager itself may be responsible for acquiring supply for delivery to the releasing shipper. Some commenters seek clarification that an end use customer need not assign actual gas supply

¹⁵⁹ Commenters supportive of this general view include the AGA, BGEM, Direct Energy, NWIGU, Nstar, PPM, PGC, Sequent and Weyerhaeuser.

contracts under which it takes service to an asset manager but that it may avail itself of “any lawful mechanism for transferring title to gas supply.”¹⁶⁰

169. The Commission notes that the definition for AMAs approved in this rule does not include a requirement that the releasing shipper assign gas supply contracts. As discussed above, the releasing shipper may want to negotiate its own gas supply contracts. Alternatively, the releasing shipper may not currently have any of its gas supply contracts to assign, but is hiring an asset manager in part for the purpose of having the asset manager negotiate and enter into gas supply contracts for the purpose of supplying the releasing shippers’ gas supply needs. Consistent with the Commission’s desire to give the parties the flexibility to negotiate the most efficient AMA arrangements to fit their needs, the definition of AMA-related releases adopted in this rule only requires that the replacement shipper enter into a contractual commitment to make the requisite delivery of gas supplies to the releasing shipper. The mechanism by which the replacement shipper will obtain those supplies is left to the parties to negotiate.

7. Other AMA Terms and Conditions

170. Several commenters request that the Commission clarify that parties are free to negotiate all relevant terms and conditions of an AMA, and the Commission does not intend to preclude parties from including in their AMA agreements terms and conditions relating to matters beyond the asset manager’s delivery obligation to the releasing

¹⁶⁰ Weyerhaeuser comments at 2-5.

shipper. For example, Sequent comments that the definition of AMA should not preclude parties from negotiating terms and conditions in addition to capacity release and delivery/receipt requirements, such as form of service and other related agreements, compensation, operating and communication protocols, asset descriptions and risk allocations.¹⁶¹ NJNG likewise seeks clarification that the tying exemption for AMAs applies to all aspects of an AMA, including financial risk management products and services, nominations and scheduling services, asset optimization fees and profit sharing arrangements and other products and services reasonably related to an AMA.

171. The Commission clarifies that its definition of AMAs is not meant to preclude the parties from negotiating the terms and conditions of other agreements necessary to implement AMAs, provided the elements of the AMA definition are satisfied. It is the Commission's intention in this rule to facilitate innovative and efficient AMAs. The Commission recognizes that in order to successfully implement an AMA, the parties will need to negotiate and agree upon certain other practical elements of the transaction aside from the release terms and delivery aspects of the deal. Those items may include communication protocols, risk management arrangements, nominations and scheduling services, asset optimization fees and profit sharing arrangements and other products and services reasonably related to an AMA. It would be counterproductive to the Commission's goal of facilitating AMAs to disallow parties to tie these other necessary

¹⁶¹ Sequent comments at 8-9.

aspects of AMAs to the deal. Thus, the Commission clarifies that if the arrangement meets the essential elements of the definition of AMAs, then the tying exemption applies to all other agreements necessary to implement the AMA. The Commission also clarifies that payments made by or to an asset manager under an AMA that are separate and apart from the cost of the released capacity do not violate the prohibition against tying.

8. Posting and Reporting Requirements

172. In the NOPR, the Commission stated that, while it proposed to exempt capacity releases implementing AMAs from bidding, such releases would remain subject to all existing posting and reporting requirements. Accordingly, the Commission stated, pipelines would still be obligated to provide notice of the release pursuant to 18 CFR section 284.8(d). In addition, the details of the release transaction would have to be posted on the pipeline's Internet web site under 18 CFR section 284.13(b)(1)(viii), which requires the posting of "special terms and conditions applicable to a capacity release transaction." The Commission also stated that sections 284.13(c)(2)(viii) and (ix) require that the pipeline's index of customers include the name of any agent or asset manager managing a shipper's transportation service and whether that agent or asset manager is an affiliate of the releasing shipper.

173. Several parties filed comments regarding the posting and reporting requirements for AMAs.¹⁶² While most support the Commission's goals of transparency and

¹⁶² See e.g., Comments of AGA; Comments of FPL, Comments of Hess; Comments of Integrys, and NGS comments.

disclosure, they seek clarification as to what exactly must be posted. Essentially these comments request clarification that commercially sensitive details of an AMA, such as the structure, assets available for use by the asset manager, and the compensation to be paid, do not need to be posted as “special terms and conditions” of the release pursuant to section 284.13(b)(1)(viii). They assert that only the fact that the release is an AMA needs to be disclosed. FPL requests that the Commission specifically define the facts that must be reported for there to be a valid AMA. Hess makes a similar request, and emphasizes that releasing shippers should not be required to post an RFP or any other details of the AMA because they are proprietary, confidential and commercially sensitive. Hess also requests the Commission confirm that it is not expanding the details that it expects to be disclosed as special terms and conditions. Hess and Integrys assert that posting and reporting on AMAs should be limited to the fact that the release is part of an AMA and describing the terms and conditions of the release associated with the AMA.¹⁶³ NGSA also requests clarification that the posting of a capacity release in the context of an AMA should require only the information normally posted for a typical release of capacity (receipt and delivery points, term), along with a statement that acknowledges that it is part of an AMA.

174. In response to these comments, the Commission clarifies in this rule the posting and reporting requirements that will be applicable to release transactions implementing

¹⁶³ Integrys comments at 6-7.

AMAs. By stating in the NOPR that existing section 284.13(b)(1)(viii) requires that any “special terms and conditions” of such releases must be posted, the Commission did not intend to require that commercially sensitive details of an AMA be disclosed, particularly information concerning the gas commodity aspects of the AMA.¹⁶⁴ The Commission recognizes that in order to promote competition certain details of the AMA are commercially sensitive and thus should remain confidential.

175. However, the Commission finds that any posting under section 284.13(b) that relates to a release to implement an AMA should include (1) the fact that the release is to an asset manager and (2) the delivery or purchase obligation of the AMA, in addition to the information required to be posted for all capacity releases. As discussed in detail above, the requirement that the asset manager deliver or purchase gas to fulfill the releasing shipper’s supply or marketing obligations is the cornerstone for differentiating AMAs from standard capacity releases. In order to ensure that capacity releases posited as AMAs eligible for the exemptions from tying and bidding are bona fide AMAs, the Commission must have a means to monitor this critical component of the arrangement. Other information specifically related to the AMA, however, such as the pricing of any sales of gas commodity and any profit sharing arrangements between the releasing and replacement shipper need not be posted pursuant to section 284.13(b). Consistent with

¹⁶⁴ The Commission retains the right, however, to require a releasing shipper to make all relevant agreements and supporting documents available to the Commission for review if questions arise as to whether a purported AMA satisfies the Commission’s regulations.

this discussion, the Commission is revising section 284.13(b)(1) of its regulations to add a new subsection (x) specifying the information concerning an AMA that must be included in the posting of any capacity release meant to implement an AMA. The required posting concerning the delivery or purchase obligation that qualifies the release as an AMA under the definition discussed above should specify the volumetric level of the replacement shipper's delivery or purchase obligation and the time periods during which that obligation is in effect.

176. INGAA and other pipeline commenters state that as pipelines already have a substantial role in administering the Commission's capacity release program, pipelines should not be overburdened by the proposed changes nor should they be responsible for policing asset managers' compliance therewith. They assert that pipelines' obligations should be limited to posting offers submitted by releasing shippers using the terms and conditions provided to the pipeline.¹⁶⁵

177. The Commission hereby clarifies in this rule that pipelines are responsible for posting offers submitted by releasing shippers that are meant to implement AMAs using the terms and conditions provided by the releasing shipper to the pipeline. It is incumbent upon the releasing shipper to include the details discussed above to qualify the release as an AMA. The Commission further clarifies that the pipeline has no obligation to act on any information other than is provided to it by its customers. The pipeline must

¹⁶⁵ INGAA comments at 21; Spectra comments at 29.

of course, comply with all applicable elements of section 284.13 of the Commission's regulations.

9. **Part 157 Capacity**

178. Several commentors¹⁶⁶ urge the Commission to permit Part 157 individually certificated transportation and storage agreements to be used in the AMA context.¹⁶⁷ The Commission's Part 284 regulations, including the provisions for flexible receipt points and capacity release, do not apply to Part 157 services. This is because pipelines perform Part 157 services pursuant to an individual certificate rather than a Part 284 blanket certificate for open access transportation. Under Part 157, a pipeline negotiates a service with a particular shipper, including the terms and conditions of service. Such an agreement generally would only provide for service between specified receipt and delivery points. Subsequently, the pipeline would apply to the Commission under NGA section 7 for a certificate to perform this individual service.

179. NJNG states that the Commission should permit a capacity holder desiring to enter into an AMA "to release Part 157, as well as Part 284, capacity to the asset manager." However, it qualifies its request to explain that while it believes that a release of Part 157 capacity should be permitted in this context, it does not request all the flexibility of Part

¹⁶⁶ See e.g., comments of AGA, National Grid, NJNG, Nstar, and PPM.

¹⁶⁷ Individually-certificated service agreements are transportation and storage services that have been certificated pursuant to Part 157 of the Commission's regulations and under the authority of Section 7(c) of the NGA. See 18 CFR 157 Subpart A (2007).

284 capacity. NJNG states that a limited expansion of flexibility afforded to Part 157 transactions will facilitate the asset manager's ability to optimize the customer's portfolio of transactions.¹⁶⁸ NGNJ also suggests that inclusion of Part 157 service in AMAs could be achieved "either by making Part 157 services releasable for this limited purpose, or it could be effectuated by affording the asset manager a waiver of the Shipper Must Have Title requirement"¹⁶⁹

180. National Grid also requests that the Commission clarify that "as part of an AMA, a shipper can include all of its pipeline contracts, including individually certificated Part 157 contracts and upstream sales agreements without violating any otherwise applicable Commission rules or policies"¹⁷⁰ AGA recommends that the Commission allow Part 157 capacity to be included in the portfolio of assets that a releasing shipper may assign to an asset manager, but does not advocate that Part 157 capacity be permitted to be released or assigned on a stand-alone basis.¹⁷¹ PPM and Nstar request that the Commission permit customers to include Part 157 service as part of an AMA. They argue that inclusion of Part 157 capacity in AMAs would further advance the Commission's goal of facilitating AMAs and warrants an exception from the rules that

¹⁶⁸ NJNG comments at 3.

¹⁶⁹ Id.

¹⁷⁰ National Grid comments at 5.

¹⁷¹ AGA comments at 22.

otherwise prohibit shippers from releasing their Part 157 capacity, while exclusion of Part 157 capacity, would serve as an obstacle to the maximization of efficient capacity.

181. On February 15, 2008, Spectra filed a reply to these comments. Spectra supports the ability of customers to have asset managers act as their agents in managing Part 157 service agreements, so long as the agreements themselves are not released or otherwise assigned to the asset manager and the customer and asset manager follow all other Commission policies and regulations related to Part 157 service. Spectra opposes requests that the Commission allow Part 157 service to be released or, in any way, be treated in the same manner as Part 284 services and states that such suggestions are inconsistent with Commission policy and are outside the scope of the NOPR.

182. On March 3, 2008, Nstar filed a response to Spectra and clarifies that commentors requesting this treatment for Part 157 capacity are not arguing for flexibility equal to that the Commission provides shippers under Part 284 service. Rather, they simply urge the Commission to clarify that Part 157 rights may be among the assets conveyed under an AMA, and that they seek no additional Part 284 service flexibilities. Nstar argues that the Commission should not require shippers to convert Part 157 service to Part 284 service as a condition of subjecting such capacity to an AMA. Nstar argues that such conversion would be costly and the added flexibilities would not warrant the cost of conversion as they are unnecessary.

183. The Commission did not propose in the NOPR to require pipelines to allow shippers to transfer their Part 157 service agreements to an AMA, because the essence of

an AMA, as defined by Commission, is a pre-arranged capacity release, pursuant to the Part 284 regulations, from the holder of the capacity to the asset manager. The Commission's policies regarding the release of Part 157 capacity are well set:

In Order No. 636-A, the Commission determined that holders of individually certificated transportation under section 7 (c) of the Natural Gas Act and Part 157 of the Commission's regulations (Part157 shippers), i.e. not Part 284 shippers, are not eligible to release capacity under section 284.243 since they are not governed by Part 284 or affected by the provisions of Order No. 636 that amended the Part 284 regulations.¹⁷²

184. In its Order No. 636 proceeding, the Commission recognized that shippers under Part 157 service would not have the same rights and flexibility as Part 284 shippers such as flexible receipt and delivery points and the right to release their capacity to another shipper. However, the Commission stated that shippers with Part 157 service could convert their Part 157 service to Part 284 service if they wanted to release capacity or use flexible receipt and delivery points.¹⁷³ Further, in Order No. 636-B, the Commission

¹⁷² Order No. 636-B, 61 FERC ¶ 61,272 at 61,992 (1992), citing, Order No. 636-A at 30,569.

¹⁷³ Order No. 636-A at 30,569. Moreover, in Order No. 636-B, the Commission stated:

Although the Commission is denying the requests for rehearing, the Commission reemphasizes that it finds conversions from individually certificated transportation to open access transportation to be in the public interest. The Commission anticipates that pipelines and their customers will be able to reach agreement on proposals for implementing such conversions and encourages them to do so. *Id.* at 61,994. (footnote omitted)

recognized that while its open access program under Part 284 granted shippers benefits not enjoyed by Part 157 shippers, it also imposed obligations upon Part 284 shippers that were not imposed on Part 157 shippers, such as requiring non-discriminatory access for all shippers under Part 284 while Part 157 arrangements may include unique terms and conditions.¹⁷⁴ The Commission also pointed out that, because the Part 284 capacity releasing program permits releases at discounted rates but Part 157 capacity cannot be discounted, Part 157 shippers cannot simply be included in the Part 284 capacity release program.¹⁷⁵

185. For the reasons stated above, the Commission is not persuaded to revise its longstanding policy of not permitting Part 157 shippers to participate in the capacity release program without converting their services to service under Part 284 blanket authority. Further, to the extent that Nstar argues that the commentors do not seek capacity release rights such as those enjoyed by Part 284 shippers but, rather the ability to assign a Part 157 individually certificated service agreement to its asset manager, such a request entails a change of the contract between the pipeline and the shipper. That is because such a modification would replace the existing shipper under a contract individually certificated by the Commission with another shipper. If the contract does not include a provision permitting such an assignment, the Commission could only

¹⁷⁴ Order No. 636-B at 61,992.

¹⁷⁵ Order No. 636-B at 61,993.

require the pipeline to permit the assignment by acting under NGA section 5. The Commission finds that such modifications to individually certificated agreements should be addressed on a case by case basis, rather than in this rulemaking proceeding.

V. **Tying of Storage Capacity and Inventory**

186. In its decision in Texas Eastern Transmission, LP,¹⁷⁶ the Commission found that a proposed tariff provision stating that "[i]f the Releasing Customer proposes or requires a transfer of all or a portion of its Storage Inventory in conjunction with its release of storage capacity rights, it shall so specify in its offer to release capacity" constituted a broad authorization for shippers on Texas Eastern's system to tie their release of storage capacity to an extraneous condition (i.e. the taking of gas inventory) in all situations. The Commission held that this proposed tariff provision violated the Commission's current prohibition against tying a release of its capacity to any extraneous conditions. The Commission thus required Texas Eastern to delete the proposed language.

187. Subsequent to the Texas Eastern decision, the Commission in the NOPR requested comment on whether it should clarify its prohibition concerning tying agreements outside of the AMA context to allow a releasing shipper to include conditions in a storage release

¹⁷⁶ Texas Eastern Transmission LP, 120 FERC ¶ 61,199, order on compliance filing, 121 FERC ¶ 61,026 (2007), reh'g denied without prejudice, 122 FERC 61,014 (2008) (Texas Eastern). The Commission stated in its rehearing order that the issues raised in the requests for clarification and/or rehearing in the Texas Eastern case were general policy issues that would be more appropriately addressed in this rulemaking proceeding.

concerning the sale and/or repurchase of gas in storage inventory.¹⁷⁷ All commenters that addressed this issue supported removing the tying prohibition for storage services to allow a shipper that releases storage capacity to condition a release of storage capacity on the sale and/or repurchase of gas in storage inventory. They want to be able to require that a replacement shipper take title to any gas that remains in the storage at the time the release takes effect and/or to require the releasing shipper to return the storage capacity to the releasing shipper at the end of the release with a specified amount of gas in storage.¹⁷⁸ Commenters supporting this change argue that there is nothing extraneous about a releasing shipper addressing gas in storage at the time it releases storage capacity, and thus the requisite “tying” should be permitted.

188. Commenters note that tying storage capacity with storage inventory will allow the releasing shipper greater ease in releasing capacity and will enable transactions to be consummated more readily.¹⁷⁹ Further, because releasing shippers may want to release storage capacity in the summer when they do not need it, they need to get the capacity back with gas in storage or there will not be enough time to re-fill it for the winter season.

189. Commenters also assert that the nature of the relationship between storage capacity and storage inventory calls out for a waiver of the tying rule. They add that the

¹⁷⁷ NOPR at P 82.

¹⁷⁸ See e.g. Comments of the AGA, Duke Energy, Florida Cities, INGAA, the NGSAA, Piedmont, National Grid, NYSEG and RG&E.

¹⁷⁹ See e.g. Comments of Piedmont at 7.

ability of releasing shippers to “tie” storage capacity with storage inventory such that releasing shippers would be permitted to require that replacement shippers take inventory as a condition of release, even outside the AMA context, will provide benefits to the marketplace similar to those provided by AMA.¹⁸⁰ Finally, the NYPSC asserts that the AMA exemption from tying prohibition should be extended to releases of storage capacity performed pursuant to state retail access programs.

190. Based on the substantial support expressed in the comments, the Commission is clarifying in this rule its prohibition on tying to allow a releasing shipper to include conditions in a release concerning the sale and/or repurchase of gas in storage inventory even outside the AMA context. Specifically, this exception to the tying rule is meant to allow a shipper that releases storage capacity to require the replacement shipper to (1) take title to any gas in the released storage capacity at the time the release takes effect and/or (2) return the storage capacity to the releasing shipper at the end of the release with a specified amount of gas in storage. The Commission is persuaded in the storage context, storage capacity is inextricably attached to the gas in storage. By allowing releasing shippers to condition the release of storage capacity on sale and or repurchase of gas in storage inventory and on there being a certain amount of gas left in storage at the end of the release, the Commission will enhance the efficient use of storage capacity while at the same time ensuring that the releasing shipper will have gas in storage for the

¹⁸⁰ Comments of Marketer Petitioners at 15-16.

winter. The Commission also agrees that allowing the tying of storage capacity to storage inventory will provide benefits to the market by enabling more active release of storage capacity into the wholesale market.

VI. Liquefied Natural Gas

191. Statoil seeks clarification that akin to the exemption for AMAs that would allow the tying of released capacity to gas sales agreements, it would be permissible to link throughput agreements and/or sales of gas at the outlet of an NGA Section 3 liquefied natural gas (LNG) terminal with a prearranged capacity release on an interstate pipeline connected to the terminal. Statoil comments that LNG importers often hold firm capacity on interstate pipelines adjacent to the terminals to ensure that re-gasified LNG can exit the terminal efficiently and be transported to the markets on the interstate pipeline grid. Noting that while the contracts governing the use of NGA section 3 capacity are not subject to the Commission's open access or capacity release policies, and that the terms of agreements for the sale of LNG are not governed by the Commission, the NGA section 7 pipelines that connect the terminals to the interstate grid are subject to those regulations. Accordingly, Statoil suggests that the Commission should recognize and permit the natural link between an LNG terminal throughput agreement and an agreement to release downstream pipeline capacity and clarify that such a tie is permissible. Shell LNG filed in support of Statoil's comments.¹⁸¹

¹⁸¹ Chevron also filed late supporting comments on May 27, 2008.

192. The Commission declines to grant the requested clarification in this generic rulemaking proceeding. In this rule, the Commission is providing an exemption from bidding and the prohibition on tying in order to permit gas sellers to use supply AMAs. Statoil and other LNG importers holding firm capacity on interstate pipelines connected to an LNG terminal can use a supply AMA. The comments of Statoil and other LNG importers do not provide adequate detail on the types of transactions for which they seek a tying exemption to explain why a further exemption beyond that provided for supply AMAs is required for LNG facilities. Likewise, it is unclear from the comments how far downstream they seek to have the exemption apply. For example, while some terminals may have direct connection to a dedicated lateral line, others interconnect directly with a major interstate natural gas pipeline. Nor do we have a sufficient record at this time to evaluate the possible benefits of such an exemption or the effect on open access competition that such an exemption might have.

193. While the Commission declines to grant the clarification in this general rulemaking proceeding, the Commission is open to considering this issue on a case-by-case basis if presented to it in a fully justified proposal.

VII. State Mandated Retail Unbundling

194. Section 284.8(h)(1) of the Commission's current capacity release regulations exempts prearranged releases of more than 31 days from bidding only if they are at the "maximum tariff rate applicable to the release." States with retail open access gas programs (in which customers can buy gas from marketers rather than LDCs) have relied

on this “safe harbor” exemption from bidding in structuring their programs. Specifically, a key component of most such programs is a provision for the LDC to make periodic releases, at the maximum rate, of its interstate pipeline capacity to the marketers participating in the program. The marketers then use the released capacity to transport the gas supplies that they sell to their retail customers. The exemption from bidding ensures that the LDC’s capacity is transferred only to the marketers participating in the state retail unbundling program and is not obtained by non-participating third parties.

195. However, the Commission’s removal of the price ceiling for releases of one year or less in this rule eliminates the bidding exemption for releases with terms of between 31 days and one year. That is because there will no longer be a maximum tariff rate applicable to such releases. As a result, absent some additional modification of the regulations concerning bidding, LDCs will have to post for bidding all releases of between 31 days and one year that are made as part of a state retail unbundling program. This would mean that the marketers participating in the program could only obtain the capacity if they matched any third party bid for the capacity.

196. In the NOPR, the Commission proposed to address this issue in a manner generally consistent with its actions in Order No. 637, when a similar issue arose with respect to the experimental lifting of the price ceiling for short-term capacity releases. In Order Nos. 637-A and 637-B,¹⁸² the Commission denied the request by LDCs for a

¹⁸² Order No. 637-A at 31,569; Order No. 637-B, 92 FERC at 61,163.

blanket exemption from bidding of all capacity releases made as part of a state retail unbundling program. The Commission explained that, with the price ceiling removed, posting and bidding was necessary to protect against undue discrimination and ensure that the capacity is properly allocated to the shipper placing the greatest value on the capacity. The Commission nevertheless provided that, if an LDC considered an exemption from bidding essential to further a state retail unbundling program, the LDC could request a waiver of the bidding regulation to allow the LDC to consummate pre-arranged capacity release deals at the maximum rate, subject to certain conditions.¹⁸³

197. In the NOPR, the Commission similarly proposed to permit LDCs to request a waiver of the bidding regulation to allow them to consummate short-term pre-arranged capacity release deals necessary to implement retail access at the maximum rate without bidding. The Commission stated that this limited waiver of the bidding requirement would enable retail access programs to continue to operate with the same exemption from bidding which they now have. While the Commission did not propose a blanket exemption from bidding for releases made by LDCs under state retail choice programs

¹⁸³ On appeal of Order No. 637, the court in INGAA affirmed the Commission's refusal to grant a blanket waiver of the bidding requirement for releases made as part of a state retail unbundling program, finding that the Commission's concern about discrimination was reasonable. However, the court remanded the issue of the reasonableness of the Commission's condition that an LDC seeking a waiver must agree to subject all its releases to the maximum rate. The Commission did not address this issue in its order on remand, because the price ceiling had been re-imposed by the time of the remand order, thus rendering the issue moot.

comparable to the blanket exemption for AMAs, the Commission requested comment on whether such releases should be treated as similar to releases made as part of an AMA and thus accorded the same full exemption from bidding. The Commission recognized that there are similarities between releases made pursuant to a state retail unbundling program and those made as part of an AMA, but requested comment on whether a blanket exemption for state programs would entail greater potential for undue discrimination.

198. The vast majority of comments that addressed this issue supported treating capacity releases under state retail choice programs the same way as AMAs, advocating that those capacity releases be afforded the same blanket exemptions from capacity release bidding requirements as those granted to releases to implement AMAs.¹⁸⁴

Commenters assert that releases made by LDCs for state unbundling programs closely resemble AMAs in that the capacity is committed to be used for its original purpose, to serve the LDC's customers. Commenters also note that the reasons given by the Commission in the NOPR for the bidding and tying exemptions for AMAs apply with equal force to releases to implement state approved retail access programs. Others argue that the Commission's case-by-case exemption analysis creates a greater potential for discrimination than a blanket exemption would. As pointed out by the NYPSC, requiring

¹⁸⁴ Those commenters include the AGA, Boardwalk, BP, Commerce Energy, Direct Energy, Duke Energy, FPL, Hess, IGS, NJNG, NStar, NYSEG, RG&E, Ohio OGMG, PG&E, PSCNY, PUCO, SEMI, Sequent and WDG.

LDCs seeking to participate in state approved unbundling programs will inject a level of uncertainty into the process as well as impose additional expensive burdens on those LDCs. AGA urges the Commission to permit LDCs to make exempt releases at the price the LDC paid for the capacity as opposed to the applicable maximum tariff rate.¹⁸⁵ FPL Energy provides the Commission with an alternative suggestion that would continue to allow a general exemption from bidding for prearranged releases where the replacement shipper agrees to pay the maximum tariff rate.¹⁸⁶

199. The Commission finds that capacity releases by LDCs to implement state approved retail access programs should be granted the same blanket exemptions from the prohibition against tying and the bidding requirements as capacity releases made in the AMA context. As the Commission stated in Georgia Public Service Commission,¹⁸⁷ “state retail unbundling is consistent with the Commission’s overall goals in Order No. 636 of improving the competitive structure of the natural gas industry by promoting access to the interstate pipeline transportation grid and the wellhead market so that willing buyers and sellers can meet in a competitive, national market to transact the most efficient deals possible. Therefore the Commission does not wish to discourage state retail unbundling programs that give retail end-users a greater choice of suppliers from

¹⁸⁵ AGA comments at 7.

¹⁸⁶ FPL Energy comments at 23.

¹⁸⁷ 110 FERC ¶ 61,048 at P 20 (2005).

whom to purchase their gas.” State retail unbundling programs provide benefits similar to AMAs.

200. Accordingly, this rule clarifies that the prohibition against tying does not apply to releases by an LDC to a marketer that agrees to sell gas to the LDC’s retail customers under a state approved retail access program. The final rule also amends section 284.8(h) in order to provide for such an exemption from bidding. The exemption from bidding will apply regardless of the rate at which the LDC makes its releases to the marketers participating in the state retail unbundling program. In order to qualify for the exemption, the capacity release must be used by the replacement shipper to provide the gas supply requirement of retail consumers pursuant to a retail access program approved by the state agency with jurisdiction over the LDC that provides delivery service to such retail consumers. The exemption does not apply to re-releases made by marketers participating in the retail access program.

201. In light of our granting this blanket bidding exemption, the Commission is also modifying section 284.13(b)(1) of its regulations to add a requirement that the pipeline’s posting of a capacity release must state whether the release is to a marketer participating in an eligible state retail access program.

VIII. Implementation Schedule

202. The regulatory changes in this rule will become effective as of the effective date of this rule, at which time parties may act in accordance with the revised regulations adopted by this rule. Pipelines must file within 180 days of the effective date of this rule

to remove any inconsistent tariff provisions and can incorporate this filing into any other tariff filing made by the pipeline within the 180 day period.

IX. Information Collection Statement

203. The Office of Management and Budget (OMB) regulations require that OMB approve certain reporting, recordkeeping, and public disclosure (collections of information) imposed by an agency.¹⁸⁸ 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 1995.¹⁸⁹

204. The Commission identifies the information provided under Part 284.13 as contained in FERC-549B. As mentioned above, natural gas pipelines must also amend their tariffs to remove inconsistent language and to incorporate the provisions from this rule into another tariff filing as covered under FERC-545 and file with the Commission.

205. The Commission did not receive specific comments concerning its burden estimates and uses the same estimates here in the Final Rule, as modified to reflect the addition of what must be included in the posting of any capacity release to implement an asset management agreement or a release made as part of a state retail access program and to make the require tariff filings. The burden estimates for complying with additional filing requirements of this rule pursuant to the procedures in proposed new sections

¹⁸⁸ 5 CFR §1320.11 (2007).

¹⁸⁹ 44 U.S.C. 3507(d) (2000).

284.13(b)(1) are set forth below. For the most part, the burden on respondents to comply with the existing reporting requirements in section 284.13 of the Commission’s regulations will not be changed by this proposed rule. In 1992 in Order No. 636 the Commission established a capacity release mechanism under which shippers could release firm transportation and storage capacity on either a short or long term basis to other shippers wanting to obtain capacity. This Final Rule modifies policies and regulations concerning capacity releases by shippers on interstate pipelines in order to enhance the efficiency and effectiveness of the secondary capacity release market. The Commission is responding to industry’s request for greater flexibility in the capacity release market and to reflect changes and developments in the marketplace. On average, we expect the burden of making the corresponding changes under this Final Rule to be 35 hours. This estimate is based on the modification of websites to account for the posting of the delivery and /or purchase obligation and whether a release is to a marketer serving as an asset manager or a shipper who is participating in a state unbundling program, as well as to make the required tariff changes.

Data Collection	No. of Respondents	No. of Responses Per Respondent	Hours Per Response	Total Annual Hours
FERC-549B	102	1	10	1,020
FERC-545	102	1	25	2,550

Totals	102	1	25	3,570
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Total Annual Hours for Collection: 3570 hours.

206. Information Collection Costs: The Commission sought comments on the cost to comply with these requirements. No comments were received. The Commission has projected the average annualized cost for all respondents to be \$\$145,350. This takes into account IT technical support 5 hours @\$125 an hour, legal review 3 hours @\$250 an hour and administrative support 22 hours @\$25 an hour.

207. Title: Capacity Information (FERC-549B), Gas Pipeline Rates: Rate Change (Non-Formal)(FERC-545)...

208. Action: Proposed Information Collection.

209. OMB Control Nos.: 1902-0169, 1902-0154.

210. 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.

211. Respondents: Business or other for profit.

212. Frequency of Responses: On occasion.

213. Necessity of Information: This Final Rule will permit market based pricing for short-term capacity releases and facilitate AMAs by relaxing the Commission’s prohibition on tying and its bidding requirements for certain capacity releases.

Elimination of the price ceiling for short-term capacity releases will provide more accurate price signals concerning the market value of pipeline capacity. Further,

implementation of AMAs will make the capacity release program more efficient as releasing shippers can transfer their capacity to entities with greater expertise both in purchasing low cost gas supplies, and in maximizing the value of the capacity when it is not needed to meet the releasing shipper's gas supply needs. Such arrangements free up the time, expense and expertise involved with managing gas supply arrangements and serve as a means of relieving the burdens of administering their capacity or supply needs.

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

215. 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, N.W., Washington, D.C. 20503 (Attention: Desk Officer for the Federal Energy Regulatory Commission, 202-395-7345, fax: 202-395-7285).

X. Environmental Analysis

216. 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.¹⁹⁰ The Commission has categorically excluded certain actions from these requirements as not having a significant effect on the human environment.¹⁹¹ The actions proposed to be taken here fall within categorical exclusions in the Commission's regulations for rules that are corrective, clarifying or procedural, for information gathering, analysis, and dissemination, and for sales, exchange, and transportation of natural gas that requires no construction of facilities.¹⁹² Therefore an environmental review is unnecessary and has not been prepared in this rulemaking.

XI. Regulatory Flexibility Act

217. The Regulatory Flexibility Act of 1980 (RFA)¹⁹³ 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 economic impact on a substantial number of small entities. The amendments to our regulations would apply only to natural gas companies, most of which are not small businesses. Under the industry standards used for purposes of the RFA, a natural gas pipeline company qualifies as a "small entity" if it

¹⁹⁰ Order No. 486, Regulations Implementing the National Environmental Policy Act, 52 FR 47,897 (Dec. 17, 1987), FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,783 (1987).

¹⁹¹ 18 CFR 380.4 (2007).

¹⁹² See 18 CFR 380.4(a)(2)(ii), 380.4(a)(5) and 380.4(a)(27)(2007).

¹⁹³ 5 U.S.C. 601-612, citing to Section 3 of the Small Business Act, 15 U.S.C. 623 (2000). Section 3 defines a "small business concern" as a business which is independently owned and operated and which is not dominant in its field of operation.

has annual revenues of \$6.5 million or less. As we stated in both the NOPR and in this Final Rule, removal of the price ceiling will enable releasing shippers to offer competitively-priced alternatives to the pipelines' negotiated rate offerings. Further, removal of the ceiling also permits more efficient utilization of capacity by permitting prices to rise to market clearing levels, allowing those entities that place the highest value on the capacity to obtain it.

218. The RFA directs agencies to consider at a minimum four regulatory alternatives in drafting a rulemaking to lessen the impact on small entities: tiering or establishment of different compliance or reporting requirements for small entities; classification, consolidation, clarification or simplification of compliance and reporting requirements; performance rather than design standards; and exemptions. In this Final Rule, the Commission has revised its regulations to lift the ceiling price from the release market and provided a different compliance regime for shippers making short-term capacity release transactions. This gives releasing shippers some of the same flexibility that is currently enjoyed by jurisdictional pipelines. In addition, the Commission will exempt capacity releases made as part of AMAs from the prohibition of tying and from the bidding requirements of section 284.8. AMAs provide significant benefits to many participants in the natural gas and electric marketplaces particularly by allowing greater flexibility for entities to customize arrangements to meet unique customer needs. Sellers of natural gas by using the benefits of AMAs create a greater diversity of potential suppliers and participants in the secondary markets. AMAs benefits also include better

management of risks to the fuel supply which in turn allows generators to focus on the electric market and not to be consumed with administrative burdens relating to multiplier suppliers, overheads and capital requirements for and the risks associated with marketing excess gas. In addition, capacity releases made under state-approved retail access programs are also exempt from the prohibition on tying and bidding requirements of section 284.8. A small entity that participates in the market will no longer be constrained by a ceiling price for its unused capacity.

219. Accordingly, pursuant to section 605(b) of the RFA, the Commission certifies that the Final Rule would not have a significant economic impact on a substantial number of small entities.

XII. Document Availability

220. 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 5:00 p.m. Eastern time) at 888 First Street, N.E., Room 2A, Washington D.C. 20426.

221. From FERC's Home Page on the Internet, this information is available on 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.

222. User assistance is available for eLibrary and the FERC's website during normal business hours from FERC Online Support at 202-502-6652 (toll free at 1-866-208-3676) or email at ferconlinesupport@ferc.gov, or the Public Reference Room at (202) 502-8371, TTY (202)502-8659. E-mail the Public Reference Room at public.referenceroom@ferc.gov.

XIII. Effective Date and Congressional Notification

223. These regulations are effective insert date 30 days from publication in Federal Register. The Commission has determined, with the concurrence of the Administrator of the Office of Information and Regulatory Affairs of OMB, that this rule is not a "major rule" as defined in section 351 of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of subjects in 18 CFR Part 284

By the Commission. Commissioner Moeller dissenting in part with a separate statement attached.

(S E A L)

Kimberly D. Bose,
Secretary.

In consideration of the foregoing, the Commission proposes to amend part 284, Chapter I, Title 18, Code of Federal Regulations, as follows:

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. Amend § 284.8 as follows:

- a. In paragraph (e), remove the words “(not over the maximum rate)”.
- b. Remove paragraph (i).
- c. Add two sentences to the end of paragraph (b) and revise paragraph (h) to read as follows:

§ 284.8 Release of firm capacity on interstate pipelines.

* * * * *

(b) * * * The rate charged the replacement shipper for a release of capacity for more than one year may not exceed the applicable maximum rate. Payments or other consideration exchanged between the releasing and replacement shippers in a release to an asset manager as defined in (h)(3) of this section are not subject to the maximum rate. No rate limitation applies to the release of capacity for a period of one year or less.

* * * * *

(h)(1) A release of capacity by a firm shipper to a replacement shipper for any period of 31 days or less, a release of capacity for more than one year at the maximum tariff rate, a release to an asset manager as defined in (h)(3) of this section, or a release to a marketer participating in a state-regulated retail access program as defined in (h)(4) of this section need not comply with the notification and bidding requirements of paragraphs (c) through (e) of this section. Notice of a firm release under this paragraph must be provided on the pipeline's electronic bulletin board as soon as possible, but not later than the first nomination, after the release transaction commences.

(2) When a release of capacity for 31 days or less is exempt from bidding requirements under paragraph (h)(1) of this section, a firm shipper may not roll-over, extend, or in any way continue the release without complying with the requirements of paragraphs (c) through (e) of this section, and may not re-release to the same replacement shipper under this paragraph at less than the maximum tariff rate until 28 days after the first release period has ended.

(3) A release to an asset manager exempt from bidding requirements under paragraph (h)(1) of this section is any pre-arranged release that contains a condition that the releasing shipper may, on any day during a minimum period of five months out of each twelve-month period of the release, call upon the replacement shipper to (i) deliver to the releasing shipper a volume of gas up to one-hundred percent of the daily contract demand of the released transportation capacity or (ii) purchase a volume of gas up to the daily

contract demand of the released transportation capacity. If the capacity release is for a period less than one year, the asset manager’s delivery or purchase obligation described in the previous sentence must apply for the lesser of five months or the term of the release. If the capacity release is a release of storage capacity, the asset manager’s delivery or purchase obligation need only be one-hundred percent of the daily contract demand under the release for storage withdrawals or injections, as applicable.

(4) A release to a marketer participating in a state-regulated retail access program exempt from bidding requirements under paragraph (h)(1) of this section is any prearranged capacity release that will be utilized by the replacement shipper to provide the gas supply requirement of retail consumers pursuant to a retail access program approved by the state agency with jurisdiction over the local distribution company that provides delivery service to such retail consumers.

3. Amend § 284.13 as follows:

a. Add sections (x) and (xi) to the end of paragraph (b)(1) to read as follows.

§ 284.13 Reporting requirements for interstate pipelines.

* * * * * *

(b) * * *

(1) * * *

(x) Whether a capacity release is a release to an asset manager as defined in section 284.8(h)(3) and the asset manager’s obligation to deliver gas to, or purchase gas from, the releasing shipper.

(xi) Whether a capacity release is a release to a marketer participating in a state-regulated retail access program as defined in section 284.8(h)(4).

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Promotion of a More Efficient Capacity Release Market Docket No. RM08-1-000

(Issued June 19, 2008)

MOELLER, Commissioner *dissenting, in part*:

Several commenters with interests in the importation of liquefied natural gas (LNG) seek clarification that a prohibited tying arrangement would not occur if an LNG importer combines an LNG throughput agreement (or the sale of regasified LNG at the outlet of the terminal) with a prearranged release of pipeline transportation capacity *on the terminal's directly connected pipeline*. In the alternative, the parties seek a limited exception from the Commission's tying prohibition. Today's final rule declines to grant either the requested clarification or the limited tying exception, but instead provides for adjudication on a case-by-case basis. I cannot support this determination.

While LNG imports admittedly have characteristics that are similar to both natural gas production and storage, LNG imports have important differences that merit a somewhat different policy. LNG cargo owners and terminal operators may have less flexibility as they enter into negotiations and supply arrangements in the global market on the high seas, and the Commission should provide the regulatory certainty to permit the linkage of such agreements without fear of running afoul of the tying prohibition. Providing such an assurance could benefit the public interest by encouraging increased LNG supply deliveries and the efficiencies associated with linking the terminal capacity and pipeline capacity (since the commodity would flow uninterrupted from the terminal to its directly connected pipeline – although separately contracted arrangements on other pipeline(s) may be necessary to deliver the gas to its final destination.) However, separating these arrangements risk stranding capacity at the import terminal or may even result in LNG suppliers serving more flexible markets that do not have such regulatory obstacles. Moreover, due to the limited nature of the exception being sought, I would not expect that either domestic producers or interstate shippers would be placed at a competitive disadvantage.

The need for LNG imports will undoubtedly increase in the coming years and the Commission should take steps to provide regulatory certainty to ensure that LNG tankers can reach our domestic markets without unnecessary risk. Accordingly, I believe that this narrow exception is appropriate in light of the unique position of LNG terminals in the interstate pipeline system.

Philip D. Moeller
Commissioner