DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Project No. 2197–064]

Notice of Application for Non-Project Use of Project Lands and Soliciting Comments, Motions To Intervene, and Protests

July 29, 2003.

Take notice that the two following application has been filed with the Commission and are available for public inspection:

a. *Application Type:* Non-Project Use of Project Lands.

b. *Project No:* 2197–064.

c. *Date Filed:* June 24, 2003.

d. *Applicant:* Alcoa Power Generating Inc.

e. *Name of Project:* Yadkin Project.

f. *Location:* The project is located on the Yadkin/Pee Dee River in Montgomery, Stanley, Davidson, Rowan, and Davie Counties, North Carolina.

g. Filed Pursuant to: Federal Power Act, 16 U.S.C. 791 (a) 825(r) and 799 and 801.

h. *Applicant Contact:* Mr. David R. Poe, BeBoeuf, Lamb, Greene, & MacRae, LLP, Suite 1200, 1875 Connecticut Avenue, NW., Washington, DC 20009–5728, (202) 986–8039.

i. *FERC Contact:* Any questions on this notice should be addressed to Ms. Shana High at (202) 502–8674, or e-mail address: shana.high@ferc.gov.

j. Deadline for filing comments and or motions: August 29, 2003.

All documents (original and eight copies) should be filed with: Ms. Magalie Roman Salas, Secretary, Federal Energy Regulatory Commission, 888 First Street, NE., Washington DC 20426. Please include the project number (P–2197–064) on any comments or motions filed. Comments, protests, and interventions may be filed electronically via the Internet in lieu of paper. *See* 18 CFR 385.2001(a)(1)(iii) and the instructions on the Commission's Web site under the ''e-Filing'' link. The Commission strongly encourages e-filings.

k. Description of Request:

Alcoa Power Generating Inc. (APGI) is seeking Commission authorization to issue a permit for non-project use of project lands and waters. The permit would be issued to Lake Forest of Badin Lakes, Inc. for the modification and use of an existing marina to accommodate a total of 51 watercraft within the project boundary on Narrows Reservoir, located in Davidson, Stanly, and Montgomery Counties.

l. Location of the Application: This filing is available for review at the Commission or may be viewed on the Commission's Web site at *http://www.ferc.gov*, using the ''FERRIS'' link. Enter the docket number excluding the last three digits in the docket number field to access the document. For assistance, contact FERC Online Support at *FERCOnlineSupport@ferc.gov* or toll-free at (866)208–3676, or for TTY, contact (202)502–8659.

m. Individuals desiring to be included on the Commission's mailing list should so indicate by writing to the Secretary of the Commission.

n. Comments, Protests, or Motions to Intervene—Anyone may submit comments, a protest, or a motion to intervene in accordance with the requirements of Rules of Practice and Procedure, 18 CFR 385.210, .211, .214. In determining the appropriate action to take, the Commission will consider all protests or other comments filed, but only those who file a motion to intervene in accordance with the Commission's Rules may become a party to the proceeding. Any comments, protests, or motions to intervene must be received on or before the specified comment date for the particular application.

o. Filing and Service of Responsive Documents—Any filings must bear in all capital letters the title ''COMMENTS'', ''RECOMMENDATIONS FOR TERMS AND CONDITIONS'', ''PROTEST'', OR ''MOTION TO INTERVENE'', as applicable, and the Project Number of the particular application to which the filing refers. A copy of any motion to intervene must also be served upon each representative of the Applicant specified in the particular application.

p. *Agency Comments:* Federal, state, and local agencies are invited to file comments on the described applications. A copy of the applications may be obtained by agencies directly from the Applicant. If an agency does not file comments within the time specified for filing comments, it will be presumed to have no comments. One copy of an agency's comments must also be sent to the Applicant's representatives.

Magalie R. Salas,

Secretary.

[FR Doc. 03–19834 Filed 8–4–03; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Docket No. PL02–6–000]

Natural Gas Pipeline, Negotiated Rate Policies and Practices; Modification of Negotiated Rate Policy

July 25, 2003.

Before Commissioners: Pat Wood, III, Chairman; William L. Massey, and Nora Mead Brownell.

1. This order addresses the Commission's Negotiated Rate Policy and concludes that several modifications of that policy are necessary in order to continue to permit the flexible, efficient pricing of pipeline capacity in a transparent manner, while ensuring the mitigation of market power.

Background

2. In 1996, the Commission issued its Policy Statement concerning negotiated rates.[1] In summary, this policy, as modified by Order No. 637,[2] permitted interstate pipelines under part 284 of the Commission's regulations to negotiate rates with a shipper that vary from the otherwise applicable cost of service pipeline tariff, subject to certain limitations, such as the Commission's prohibition against pipelines negotiating terms and conditions of service.[3] Moreover, under the Commission's

[1] The Commission's current policies were originally established in, *Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines, Regulation of Negotiated Transportation Services, Statements of Policy and Comments,* 74 FERC ¶ 61,076 (1996), *order on clarification,* 74 FERC ¶ 61,194 (1996), *order on reh'g,* 75 FERC ¶ 61,024 (1996).

[2] 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 at 61,343 (2000) (Order No. 637); *order on rehearing,* Order No. 637–A, FERC Stats. & Regs, Regulations Preambles (July 1996–December 2000) ¶ 31,099 at 31,648 (2000) (Order No. 637–A); and Order No. 637–B, 92 FERC ¶ 61,062 (2000) (Order No. 637–B), *aff'd in part and remanded in part, Interstate Natural Gas Association of America* v. *FERC,* 285 F.3d 18 (DC Cir. Apr. 5, 2002), *Order on Remand,* 101 FERC ¶ 61,127 (2002).

[3] The Commission has determined that negotiated terms and conditions of service include any provisions that result in a customer receiving a different quality of service than that provided other customers under the pipeline's tariff. Dominion Transmission, Inc., 93 FERC ¶ 61,177 (2000). The Commission will, however, permit the implementation of negotiations resulting in deviations from the pipeline's form of service agreement, so long as such changes do not change the conditions under which service is provided and do not present an undue risk of undue discrimination. Columbia Gas Transmission Corp., 97 FERC ¶ 61,221 at 62,001–02 (2001).

policy, pipelines must permit shippers to opt for use of a traditional cost of service ''recourse'' rate instead of requiring them to negotiate for rates for any particular service.[4] The Commission determined that the availability of a recourse rate would prevent pipelines from exercising market power by assuring that the customer can fall back to cost-based, traditional service if the pipeline unilaterally demands excessive prices or withholds service.[5]

3. On July 17, 2002, in Docket No. PL02–6–000, the Commission issued a Notice of Inquiry (NOI) concerning its Negotiated Rate Policy.[6] There, the Commission stated that it was undertaking a review of issues related to its negotiated rate program and requested comments from, and posed questions to, the gas industry regarding the Commission's negotiated rate policies and practices. The Commission has received responses from all segments of the gas industry that raise a variety of issues related to the Commission's negotiated rate policies.[7] As discussed below, upon consideration of its experience with the existing negotiated rate program, and the comments received from the industry in the NOI proceeding, the Commission has determined to modify several aspects of its Negotiated Rate Policy.

Discussion

4. The Commission finds that its negotiated rate program has been generally successful in providing flexible, efficient pricing of pipeline capacity while mitigating pipeline use of market power by means of a recourse rate. This view is supported by the majority of commenters as they support the negotiated rates program and want it to continue. However, certain commenters suggest various changes to increase transparency of the negotiated rates and methodologies for limiting pricing options for negotiated rates. The Commission has reviewed these comments and has determined to revise its filing requirements to increase the transparency of negotiated rates in order to minimize the potential for discrimination. In addition, the Commission has determined to address the pricing mechanisms permitted under negotiated rates in order to ensure adequate mitigation of any pipeline market power. The Commission will begin its discussion with a consideration of the use of natural gas based index prices; in particular, the use of such indices to determine basis differentials, as a pricing methodology for the negotiation of rates.

Gas Index Pricing Mechanisms

5. In its Policy Statement, the Commission set forth a mechanism by which a pipeline that does not attempt to establish a lack of market power to justify market-based rates and does not wish to embark on an incentive rate program, may seek a negotiated rate alternative to traditional cost of service ratemaking and thus achieve flexible, efficient pricing. The Commission determined that, under this policy, the availability of a cost of service based recourse rate would protect shippers from the exercise of any market power by the transporters. As such, in its efforts to permit parties to establish flexible, efficient pricing for transportation service, the Commission did not seek to limit mechanisms used in transportation price negotiations.

6. Since the establishment of this policy, pipelines have availed themselves of the flexibility of the Commission's policies to negotiate many different types of pricing mechanisms. These have included negotiated rates for transportation based upon gas commodity price indices. These gas commodity price indices, when used as a negotiated pricing mechanism, usually reflect gas prices at different points such as at natural gas production basins or certain receipt and delivery points and citygates. This transportation pricing mechanism is based upon the difference between the gas price indices at the two points that is commonly referred to as the basis differential. The foundation for this pricing mechanism is that the difference in price between two points, as shown by the respective price indices, reflects the value of transportation between the two points.

7. Several commenters oppose the use of basis differentials as a pricing mechanism for negotiated transportation rates.[8] Those opposed to the use of such pricing mechanisms argue that the use of such basis differentials in establishing transportation prices leads to rates far in excess of the recourse rate; gives the pipeline an interest in the commodity price of gas; and permits shippers to lock-in a profit margin and mitigate price risk, which provides increased price protection not available to recourse shippers.

8. IPAA states that the fundamental problem with negotiated transportation rates is that they tempt pipeline monopolies with negotiated rate authority to focus more attention on the opportunity to market gas than on their statutory obligation to provide non-discriminatory transportation. On this general note, the Industrials argue that negotiated transportation rate deals based on price differentials give pipelines a stake in the commodity price of gas on a particular day or at a particular location, thus effectively allowing pipelines to re-enter the gas commodity sales business. CPUC adds that transportation rates based upon commodity sales prices allow the pipeline to capture part of the commodity gas price and essentially makes it a partner in a merchant transaction. Mirant also asserts that index-based deals allow pipelines to compete directly with shippers in commodity markets.

9. Oklahoma and NASUCA argue that the use of basis differentials for negotiating transportation rates at best operates as a contractual mechanism to make additional profits, and at worst, operates as an incentive to withhold capacity. BP adds that such contracts provide an incentive for the pipeline to maximize revenue by selling any unutilized firm transportation as interruptible transportation and competing against the shipper's capacity. As such, it argues that this type of arrangement gives the pipeline an incentive to withhold operationally available capacity from the market for the purpose of increasing the commodity basis differential. Mirant states that the shippers and pipelines are not on an equal footing, because of the pipeline's control over capacity, the pivotal component of such trades. In addition, Mirant states that pipelines may have more information regarding the factors leading to differentials between index prices and may actually be able to influence such differentials through the operation of their systems.

10. CPUC opposes the use of negotiated rates in general and index-based rates in particular. CPUC states that evidence indicates that the California energy markets have been manipulated by traders and that spot market published commodity indices are not verifiable. Therefore, CPUC argues that it is unreasonable to continue the use of negotiated rates in

[4] *See* Natural Gas Pipeline Co. of America, 101 FERC ¶ 61,125 (2002) (finding that a pipeline may not restrict the use of recourse rate bids and, thereby, deprive bidders of a cost of service rate alternative, by declaring that only negotiated rate bids would be considered valid for bidding in an open season to determine interest in a pipeline expansion project).

[5] 74 FERC ¶ 61,076 at 61,240.

[6] *Notice of Inquiry Concerning Natural Gas Pipeline Negotiated Rate Policies and Practices,* 100 FERC ¶ 61,061 (2002).

[7] See Appendix for list of commenters.

[8] See generally, comments of Oklahoma, Mirant, CPUC, NASUCA, BP, IPAA, and Calpine.

place of tariff rates to serve markets or to simulate market behavior.

11. Other commenters argue that the Commission should continue to permit the use of basis differentials as a mechanism by which to set negotiated transportation rates. In essence, they maintain that these pricing methodologies represent a reasonable proxy for the value of the transportation and that the indexed rates allow shippers to easily engage in hedging programs and gas supply cost-management.[9] For example, INGAA argues that there is a relationship between the unregulated gas commodity price and the value of a pipeline's transportation, and that to achieve the Commission's goals of price transparency and market efficiency, the Commission should not place unwarranted restrictions on the ability to negotiate rates using basis differentials. INGAA argues that there is nothing inherently wrong about rates that reflect this market reality and that such rates protect shippers because the rate cannot exceed the basis differential.

12. The KM Pipelines and Williams argue that the Commission has recognized, in the context of evaluating the lifting of price caps in the short-term secondary market for released capacity, that basis differentials reflect the value placed by the market on the transportation capacity. Peoples and Duke Trading state that the price differential between points is a commonly accepted proxy for the value of transportation between such points. In the same vein, the KM Pipelines assert that, whether index-based pricing is permitted or not, the expected level of basis differentials will be a fundamental underlying consideration in contracting and, therefore, eliminating this pricing mechanism will not change the basic dynamics of the transaction.

13. Many commenters argue that the Commission should assume that most shippers that negotiate rates are sophisticated market participants, and that the Commission should not get involved in the pricing of such transactions beyond ensuring that the shipper always has the option of taking the recourse rate.[10] The AGA states that flexible and creative negotiations should not be inhibited by proscriptions against certain types of transactions such as those predicated on basis differentials. MidAmerican adds that deals based upon price differentials are no different than fixed price negotiated rate deals, because in either circumstance, the shipper can always revert to a recourse rate. EPSA, Dominion, NGSA and Alliance argue, in essence, that restrictions on the types of rates that can be negotiated may unnecessarily reduce flexibility and the value of the program.

14. Williston Basin, TransColorado and EnCana maintain that it is difficult for pipelines to manipulate hub prices to increase profits. They assert that while the risk of manipulation is low, the potential benefits to shippers and pipelines are high, and shippers are more willing to acquire capacity when they can share the risk with the pipeline.

15. The Canadian Association of Petroleum Producers (CAPP) argues that the Commission should allow indexed-based rates, but that the Commission should ensure that pipelines entering into such arrangements do not withhold capacity from the market in order to affect commodity prices. CAPP asserts that the popularity of indexed rates demonstrates their appeal and that to prohibit them would potentially undermine the purposes of the negotiated rate program. KeySpan asserts that negotiated rate frameworks, such as those based on gas price differentials, respond to the needs of shippers and consumers and that there is no risk associated with these pricing structures that is not outweighed by their potential benefits.

Discussion of Basis Differential Pricing Mechanisms

16. The Commission has determined to modify its negotiated rates policy and will no longer permit the use of gas basis differentials to price negotiated rate transactions. Gas commodity price indices, when used as a negotiated pricing mechanism, usually reflect gas prices at different points, such as at gas basins or certain receipt and delivery points and citygates. The pricing mechanism is based upon the difference between the gas price indices at the two points. As discussed above, the basis differential pricing mechanism uses the difference in gas prices between two points, to reflect the value of transportation between such points. Thus, under this mechanism, the wider the difference between the points, the greater the value of the transportation. In the Commission's view, allowing the use of gas commodity basis differentials by a pipeline as a mechanism for pricing transportation by a pipeline with market power threatens the Commission's regulatory structure for the transportation of gas as well as the Commission's attempts to improve and maintain a competitive natural gas commodity market.[11] This is because such mechanisms provide pipelines with an incentive to withhold capacity in an attempt to manipulate the gas commodity market by widening the differences between the indices.

17. In Order No. 637, the Commission discussed how its policies under traditional cost of service rate regulation limit the pipeline's market power stating:

> The principal reason for limiting pipeline rates to a level that would permit recovery of a pipeline's annual revenue replacement is to limit the ability of the pipelines to exercise market power, so that the pipeline does not charge excessive rates. Without rate regulation, pipelines would have the economic incentive to exercise market power by withholding capacity (including not building new capacity) in order to raise rates and earn greater revenue by creating scarcity. Because pipelines are regulated, however, there is little incentive for a pipeline to withhold capacity, because even if it creates scarcity, it cannot charge rates above those set by its cost of service. Since pipelines cannot increase revenues by withholding capacity, rate regulation has the added benefit of providing pipelines with a financial incentive to build new capacity when demand exists.[12]

18. Subsequently, in *Tennessee,* the Commission examined the pipeline's incentive to withhold capacity in spite of the Commission's part 284 regulations prohibiting such action and determined that its traditional cost of service regulation that does not permit the pipeline to charge more than the maximum cost of service rate provided an adequate check on such incentives.[13]

19. However, the Commission's negotiated rate policy permits pipelines

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[9] *See, e.g.*, Comments of Alliance, ProLiance, Dominion, KM Pipelines, KeySpan, AGA, Peoples, EnCana, APSA, Northern Natural, MidAmerican, El Paso, Williston Basin, TransColorado, INGAA, Peoples, Duke Trading, Williams, EPSA and NGSA.

[10] *See, e.g.*, Comments of NEG, El Paso, Peoples, Encana, WDG, MidAmerican and Alliance.

[11] In Order No. 636, the Commission reviewed the House Committee Report leading to the Natural Gas Wellhead Decontrol Act of 1989, [Pub. L. 101–60, 103 Stat.157 (1989)], which stated that the Commission's competitive open-access pipeline system should be maintained and that:

> The Committee stresses that these new rules, and especially the wide adoption of blanket certificates for nondiscriminatory open access interstate transportation of non-pipeline gas, are essential to its decision to complete the decontrol process. All sellers must be able to reach the highest-bidding buyer in an increasingly national market. All buyers must be free to reach the lowest-selling producer, and to obtain shipment of its gas to them on even terms with other supplies. Order No. 636 at 30,397, H.R. Rep. No. 29 101st Cong.1st Sess., at p 6.

In addition, the Commission noted that the House Committee Report urged the Commission "to retain and *improve* this competitive structure in order to maximize the benefits of decontrol." *Id.* (emphasis in original)

[12] Order No. 637 at 31,270.

[13] Tennessee Gas Pipeline Co., 91 FERC ¶ 61,053 at 61,191 (2000), *order on reh'g,* 94 FERC ¶ 61,097 (2001), *aff'd, Process Gas Consumers Group* v. *FERC,* 292 F.3rd. 831 (DC Cir. 2002). (*Tennessee*)

to charge rates above the maximum cost of service rate thus presenting the possibility that a pipeline could increase revenues by withholding capacity. The Commission has relied on the availability of recourse service to prevent such an exercise of market power ''by assuring that the customer can fall back to cost-based traditional service if the pipeline unilaterally demands excessive rates or withholds service.'' [14] As a general matter, this should be sufficient to prevent the pipeline's exercise of market power, since ordinarily a shipper would be expected to choose the recourse rate in preference to a significantly higher negotiated rate.

20. However, this may not be true where the negotiated transportation rate is tied to the commodity price of gas. Such a negotiated rate may render the shipper indifferent to the actual costs of transportation. For example, a shipper may agree to an index differential-based, negotiated transportation rate with a pipeline. The shipper may then enter into gas sales agreements with its customers based upon the downstream price index that, in effect, lock in this transportation rate and/or a profit on the transaction. As a result, the shipper is indifferent to the price of gas at the downstream point and the pipeline's withholding of capacity to manipulate the downstream commodity gas price (and the effect of such manipulation on the negotiated transportation rate). It has, in effect, shifted the possible risks of the pipeline's abuse of its market power to the gas commodity market as a whole. In other words, negotiated transportation rates that use basis differentials to price transportation give the pipeline an incentive to withhold capacity so as to widen the basis differentials. In addition, the shipper may have little incentive not to agree since it is either held harmless or may, in fact, share in the profits from the increased price differential.[15]

21. In Order No. 636, the Commission stated that its primary goal was to improve the competitive structure of the natural gas industry and, at the same time, maintain adequate and reliable service. The Commission stated that its intent was to further ''facilitate the unimpeded operation of market forces to stimulate the production of natural gas * * * .'' [16] The Commission thus undertook the task of improving the benefits of the decontrol of natural gas prices—chiefly, abundant gas supplies at lower prices—through the maintenance and improvement of its competitive pipeline transportation system. To permit pipelines to utilize pricing mechanisms, such as those based upon natural gas commodity prices, which create powerful incentives for the pipelines to attempt to use their monopoly power to manipulate the prices of the competitive natural gas commodity market, is contrary to the Commission's goal of improving the competitive pipeline transportation system set forth in Order No. 636.[17]

22. Pricing mechanisms that invest pipelines with an incentive to use market power to manipulate the commodity price of gas hinder the Commission's attempt to maintain and improve the competitive natural gas market. To allow pipelines to acquire an interest in commodity prices, or more precisely the difference between the commodity prices at separate points, reverses the regulatory trend which is based upon the competitive transportation structure acting to ensure competitive natural gas markets. This interest in the prices of the natural gas commodity presents pipelines with an incentive to withhold existing capacity in order to manipulate natural gas prices and may also create a disincentive to invest in the expansion of capacity.[18]

23. While such pricing mechanisms may be useful in permitting parties to the negotiated agreement to engage in various hedging programs and gas supply cost-management programs, in the Commission's view this flexibility cannot justify the increased risk of market manipulation faced by market participants. This slight limitation of transportation pricing flexibility is offset by the fact that negotiated rates may be based upon a virtually unlimited number of non-gas indices or other financial mechanisms that have no relationship with the commodity price of gas and are therefore not subject to manipulation through the withholding of pipeline capacity.

24. Accordingly, the Commission will no longer permit the pricing of negotiated rates based upon natural gas commodity price indices. Negotiated rates based upon such indices may continue until the end of the contract period for which such rates were negotiated, but such rates will not be prospectively approved by the Commission.

Filing Requirements

25. As the Commission's negotiated rate program has evolved, the Commission has clarified the filing requirements necessary for implementing such rates. In its original Policy Statement, the Commission stated that pipelines would need to file a tariff sheet indicating that the negotiated rate for a service would be either the rate stated on its existing rate schedule or a rate mutually agreed to by the pipeline and its customer. The Commission stated that when a rate is negotiated, the pipeline would need to file a numbered tariff sheet stating the exact legal name of the customer and the negotiated rate for the service.[19]

26. The Commission then modified this filing requirement to require that the pipeline file either the negotiated contract itself or a tariff sheet reflecting the essential elements of the negotiated rate agreement necessary to permit shippers that believe they are similarly situated to the shipper receiving the negotiated rate to make such a determination.[20] The Commission determined that if the pipeline chose to file a tariff sheet, the tariff sheet must contain the essential details of the transaction.[21] In addition, the Commission required that the tariff sheet must include a statement affirming that the negotiated rate contract does not deviate in any material aspect from the form of service agreement in the pipeline's tariff.[22] The

[14] 74 FERC ¶ 61,076 at 61,240.

[15] *See, e.g.*, Transwestern Pipeline Co., 100 FERC ¶ 61,058 (2002), in which a shipper agreed to a negotiated transportation rate based upon a basis price differential that led to prices many times the pipeline's maximum rate.

[16] Order No. 636 at 30,393, *citing*, S.Rep. No. 39, 101 Cong., 1st Sess., at p. 2 (1989).

[17] In Order No. 636, the Commission determined that because of firm transportation available under the rules promulgated by Order No. 636, and because of the abundance of uncommitted gas supplies available to replace pipeline sales of gas throughout North America, it would not be profitable for a pipeline to attempt to exercise market power over the sale of natural gas. Order No. 636 at 30,440.

[18] *See* Tennessee Gas Pipeline Co., 91 FERC ¶ 61,053 (2000), *order on reh'g*, 94 FERC ¶ 61,097 (2001).

[19] 74 FERC ¶ 61,076 at 61,241.

[20] NorAm Gas Transmission Co., 75 FERC ¶ 61,091 (1996), *order on reh'g*, 77 FERC ¶ 61,011 at 61,037 (1996). 18 CFR § 154.1(b) (2003) provides that pipelines must file all contracts related to their services. An exception to this general requirement is permitted by 18 CFR 154.1(d) (2003) which states that although any contract which ''deviates in any material aspect from the form of service agreement in the tariff'' must be filed, it also states that any contract that conforms to the pipeline's form of service agreement set forth in the pipeline's tariff need not be filed.

[21] The Commission stated that the tariff sheet ''must state the name of the shipper, the negotiated rate, the type of service, the receipt and delivery points applicable to the service and the volume of gas to be transported.'' 77 FERC ¶ 61,011 at 61,037 (1996).

[22] The Commission's regulations provide that the *pro forma* service agreement must refer to the service to be rendered and the applicable rate schedule of the tariff; and, provide spaces for insertion of the name of the customer, effective date, expiration date, and term. Blank spaces may be provided for the insertion of receipt and delivery

Commission found that this information was necessary so that the Commission could evaluate whether the transaction was unduly discriminatory.[23]

27. Subsequently, the Commission defined a material deviation as any provision of a service agreement that goes beyond the filling-in of the spaces in the form of service agreement with the appropriate information provided for in the tariff and that affects the substantive rights of the parties.[24] Therefore, if a negotiated rate agreement contains any such deviation from the form of service agreement, the pipeline must file the agreement for the Commission's review. The Commission will only accept negotiated rate agreements with such material deviations from the pipeline's form of service agreement if such deviations do not change the conditions under which service is provided and do not present a risk of undue discrimination.[25]

28. Many commenters assert that the Commission's filing requirements for negotiated rates provide sufficient information for the necessary transparency of negotiated transactions.[26] Duke Trading, WDG and NEG state that the current filing requirements permit the Commission and other interested parties to monitor the contracting activity of the pipelines for undue discrimination, and to allow market participants to undertake a full commercial analysis of each negotiated rate deal. El Paso asserts that there is no evidence to justify a change in the filing requirements, or that additional requirements are necessary for transparency. The KM Pipelines add that additional information may actually obscure the important terms of the agreement.

29. On the other hand, Calpine states that the filing requirements do not provide sufficient transparency of information for negotiated rate transactions and joins BP and EPSA in asserting that the lack of a consistent format complicates any assessment of the options available to a shipper when reviewing multiple pipeline filings and comparing the negotiated rates granted to other shippers. Mirant states that the current filing requirements are insufficient to ensure transparency and states that the Commission should not permit the pipelines to file a mere contract summary because the summaries may fail to disclose all meaningful and negotiated contract terms. NGSA joins Mirant and requests that the Commission require pipelines to file both the negotiated rate contract and a tariff sheet describing the contract. NGSA states that there is too much risk that the pipeline could omit details of a transaction that shippers *see* as important, and without full disclosure of the contract, the Commission and shippers have only limited ability to monitor negotiated transactions.

30. NASUCA and BP state that negotiated rate transactions lack transparency because of their bilateral nature, despite the posting and filing requirements. NASUCA states that recourse shippers and regulatory agencies often lack access to essential information. BP states that, even when the contracts are filed, it is sometimes hard to determine what elements are negotiated.

Discussion of Negotiated Rate Filing Requirements

31. The Commission's experience with negotiated rate filings has shown that the filings on occasion lack the information necessary for the Commission's Staff and the pipelines' shippers to analyze the negotiated agreement. First, even where the agreement contains no deviation from the form of service agreement, the tariff sheet summary may not describe the primary rate formula or the other essential elements of the transaction in sufficient detail. Second, pipelines have sometimes failed to file a service agreement even though it contained a material deviation. Finally, and most importantly, where pipelines have filed service agreements with material deviations, the deviations have often not been clearly identified, requiring the Commission to carefully compare the negotiated rate agreement with the form of service agreement in order to determine how the two may differ. Indeed, on some occasions, parties have drafted the entire service agreement independently of the form of service agreement in the tariff. As a result, provisions may be worded differently from similar provisions in the form of service agreement, but it is not immediately apparent whether the parties intended the provisions to be substantively different. These circumstances hinder the Commission's ability to assess whether the transaction is unduly discriminatory as well as the assessment of the transaction by shippers attempting to determine if they are similarly situated to the shipper in the negotiated transaction.[27]

32. The Commission will permit a pipeline filing a negotiated rate transaction that does not deviate from its *pro forma* service agreement to file a tariff sheet reflecting the terms of the agreement, together with a statement that the agreement conforms in all material respects with its *pro forma* service agreement.[28] However, pipelines are reminded that the tariff sheet summaries must fully describe the essential elements of the transaction, including the name of the shipper, the negotiated rate, the type of service, the receipt and delivery points applicable to the service and the volume of gas to be transported. Also, where the price term of the negotiated rate agreement is a formula, the formula should be fully set forth in the tariff sheet.[29] Pipelines are also reminded that, in order to file a tariff sheet summary, they must certify that the agreement contains no deviation from the form of service agreement that goes beyond filling in the blank spaces or that affects the substantive rights of the parties in any way. Since there would appear to be no reason for the parties to use language different from that in the form of service agreement other than to affect the substantive right of the parties, this effectively means that all language that is different from the form of service agreement should be filed with the Commission.

33. In addition, in order to provide greater transparency and to assist the Commission and interested parties in analyzing negotiated rate transactions, the Commission has determined that the form of service agreement must be used as a starting point in drafting any negotiated rate contract. Therefore, the Commission will henceforward require that a pipeline filing a contract proposing material changes from its form of service agreement must clearly

points, contract quantity and other specifics of each transaction as appropriate. 18 CFR § 154.110 (2003).

[23] 77 FERC ¶ 61,011 at 61,037 (1996).

[24] Columbia Gas Transmission Corp., 97 FERC ¶ 61,221 at 62,002 (2001).

[25] *Id.* at 62,001–02.

[26] See Comments of Northern Natural, Peoples, MidAmerican, Alliance, The Industrials, ProLiance, El Paso, EnCana, INGAA, Vector, CAPP, Williston Basin, Dominion, Williams, and Duke Transmission.

[27] *See, e. g.,* Gulfstream Natural Gas System, L.L.C., 103 FERC ¶61,312 (2003); CenterPoint Energy Gas Transmission Co., 102 FERC ¶61,094 (2003) and CenterPoint Energy Gas Transmission Co., 102 FERC ¶61,059, *order on reh'g,* 103 FERC ¶61,228 (2003).

[28] This action merely emphasizes the Commission's current regulations which require that if the pipeline contends that its filing implements a negotiated contract that conforms to its form of service agreement in all material aspects, and therefore, it is not necessary to file the contract, such a filing will contain a statement that the pipeline's filing complies with the requirements of 18 CFR 154.1(d) (2003). Violation of this regulation may result in the rejection of the filing or suspension of the pipeline's negotiated rate authority.

[29] In the case of complicated formula, the pipeline may, as an alternative, simply file the agreement.

delineate differences between its negotiated contractual terms and that of its form of service agreement in redline and strikeout. In addition, the pipeline shall provide a detailed narrative outlining the terms of its negotiated contract, the manner in which such terms differ from its form of service agreement, the effect of such terms on the rights of the parties, and why such deviation does not present a risk of undue discrimination.

34. Information presented in such a manner, in conjunction with the tariff sheets, will permit the Commission and the parties to efficiently ascertain whether the proposed negotiated transaction entails such a risk of undue discrimination that it cannot be permitted or whether other similarly situated shippers may be able to obtain such service.

By the Commission. Commissioner Brownell dissenting with a separate statement attached.

Linda Mitry,

Acting Secretary.

Appendix

Commenters

Alliance Pipeline L.P. (Alliance)
American Gas Association (AGA)
American Public Gas Association (APGA)
BP Energy Company (BP) Calpine Energy Services, L.P. (Calpine)
Canadian Association of Petroleum Producers (CAPP)
Connecticut Department of Public Utility Control (Connecticut)
Consolidated Edison Company of New York, Inc. and Orange and Rockland Utilities, Inc. (ConEd and Orange and Rockland)
Dominion Resources, Inc. (Dominion)
Duke Energy Gas Transmission Corp. (Duke Transmission)
Duke Energy Trading and Marketing, L.L.C. (Duke Trading)
Dynegy Marketing and Trade (Dynegy)
Electric Power Supply Association (EPSA)
El Paso Corporation's Pipeline Group (El Paso)
EnCana Gas Storage Inc., EnCana Marketing (USA) Inc., and EnCana Energy Services Inc. (EnCana)
Gulf South Pipeline Company, LP (Gulf South)
Illinois Municipal Gas Agency (IMGA)
Independent Petroleum Association of America (IPAA)
Interstate Natural Gas Association of America (INGAA)
KeySpan Delivery Companies (KeySpan)
Louisville Gas and Electric Company (Louisville)
Maritimes & Northeast Pipeline, LLC (Maritimes)
Michigan Public Service Commission (Michigan PSC)
MidAmerican Energy Co. (MidAmerican)
Mirant Americas Energy Marketing, LP (Mirant)
National Association of State Utility Consumer Advocates (NASUCA)
Natural Gas Pipeline Company of America and Kinder Morgan Interstate Gas Transmission, LLC (jointly ''KM Pipelines'')
Natural Gas Supply Association(NGSA)
NEG Shippers (NEG)
NiSource Pipelines (NiSource)
Northern Natural Gas Company (Northern Natural)
Northwest Industrial Gas Users (NWIGU)
Oklahoma Corporation Commission (Oklahoma)
Peoples Gas Light and Coke Co., North Shore Gas Co., and Peoples Energy Resources Corp. (Peoples)
Process Gas Consumers Group, American Forest & Paper Association, American Iron and Steel Institute, Georgia Industrial Group, Industrial Gas Users of Florida, Florida Industrial Gas Users United States Gypsum Company (collectively, the ''Industrials'')
ProLiance Energy, LLC (ProLiance)
Public Service Commission of the state of New York (New York)
Public Utilities Commission of California (CPUC)
Sempra Energy Trading Corp. (Sempra)
TransColorado Gas Transmission Company (TransColorado)
Vector Pipeline L.P. (Vector)
The Williams Companies, Inc. (Williams)
Williston Basin Interstate Pipeline Company (Williston Basin)
Wisconsin Distributor Group (WDG)

Brownell, Commissioner, dissenting

1. In this order, the majority prohibits on a prospective basis the use of gas basis differentials to price negotiated rate transactions. The majority bases its determinations on the theory that such mechanisms provide pipelines with an incentive to withhold capacity in an attempt to widen the gas basis differential.

2. Gas basis differential pricing is a widely used tool for structuring competitive flexible transportation arrangements, demonstrating the appeal to both shippers and transporters alike. Many commenters argue that the Commission should assume that most shippers that negotiate rates are sophisticated market participants, and that gas basis differential pricing responds to the needs of shippers and consumers. These commenters conclude that the risk of manipulation is low while the potential benefits to shippers and pipelines are high and, therefore, the Commission should not preclude such transactions.

3. Gas basis differential pricing does not blur the role of the pipeline as a transporter with no direct interest in the commodity price because pipelines already use the gas basis differentials to value transportation. Whether or not a pipeline uses gas basis differential pricing in its negotiated rate transactions, pipelines determine the level of the discount that is necessary to maintain throughput on their systems by reference to the gas basis differentials. The Commission itself has recognized that the implicit price for transportation represents the most any shipper purchasing delivered gas at a downstream market would pay to move gas from the lower priced market to the higher priced market. Order No. 637 at 31,271.

4. The majority opinion ignores the Commission's existing regulations which prevent pipelines from withholding capacity. The order cites to no evidence that pipelines have the ability to withhold capacity or, in fact, have withheld capacity to increase the gas basis differentials. In Docket No. PL02–4–000, the Commission Staff presented data it had collected concerning capacity release transactions over a 22 month period. The data reflected that rates shippers received for their released transactions (above and below the recourse rate) tracked the applicable basis differentials. This finding further validates the Commission's determination in Order No. 637 that the ''fact that prices for transportation rise during peak periods is not evidence of the exercise of market power but may be the appropriate market response to an increase in demand for capacity''. Order No. 637 at 31,281.

5. The majority opinion seems to rely on *Transwestern Pipeline Co.,* 100 FERC ¶ 61,058 as a reason for prohibiting the use of gas basis differential pricing. In the *Transwestern case,* the pipeline was found to have violated its tariff by improperly giving prior notice of the capacity posting to two shippers that were awarded the capacity. Not complying with the open access tariff provisions is not a concern directed solely at negotiated rate transactions, but is a concern regardless of how the capacity is priced. I would further note that capacity was not being withheld in that proceeding, but unfairly directed.

6. Finally, the blanket prohibition of negotiated rate transactions that use gas basis differentials is overly prescriptive and an unnecessary intrusion in the marketplace, particularly when shippers have other choices. Most gas basis differential priced transactions are below the recourse rate. More importantly, shippers are protected because each negotiated rate transaction is noticed for comment and ultimately approved (or disapproved) by the Commission. The Commission has access to information about available pipeline capacity and daily gas basis differentials to monitor these types of transactions to determine if a pipeline is withholding capacity to increase the gas basis differential. With pipelines obligated to offer all available capacity, a viable recourse rate alternative, and our capability to monitor these transactions, the prohibition of gas basis differential pricing unnecessarily reduces flexibility and the value of the negotiated rate program.

7. For these reasons, I respectfully dissent.

Nora Mead Brownell,

Commissioner.

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