UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Cost Recovery Mechanisms for Modernization Of Natural Gas Facilities	))	Docket No. PL15-1-000

COMMENTS OF THE
AMERICAN GAS ASSOCIATION

Pursuant to the Proposed Policy Statement issued in this proceeding,[1] by the Federal Energy Regulatory Commission ("Commission"), the American Gas Association ("AGA") respectfully submits these comments. AGA's members are committed to providing safe and reliable natural gas service to their customers, and thus share the Commission's overall goal of its proposed policy statement of enhancing the efficient and safe operation of the interstate natural gas pipeline grid. AGA believes that pipeline cost recovery mechanisms must be tailored to the individual circumstances of the pipeline, and be designed so as not to impose unreasonable cost burdens or risks on natural gas customers.

I. COMMUNICATIONS

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[1] *Cost Recovery Mechanisms for Modernization of Natural Gas Facilities*, 79 Fed. Reg. 70517 (Nov. 26, 2014), 149 FERC ¶ 61,147 (2014).

II. IDENTITY AND INTERESTS

The AGA, founded in 1918, represents more than 200 local energy companies that deliver clean natural gas throughout the United States. There are more than 71 million residential, commercial and industrial natural gas customers in the U.S., of which 94 percent — more than 68 million customers — receive their gas from AGA members. AGA is an advocate for local natural gas utility companies and provides a broad range of programs and services for member natural gas pipelines, marketers, gatherers, international gas companies and industry associates.[2]

AGA's member local distribution companies take service from virtually every interstate natural gas pipeline regulated by the Commission under the Natural Gas Act. As customers of jurisdictional pipelines, AGA members are directly affected by the rates, terms and conditions of the services provided by jurisdictional pipelines, including any mechanisms for recovering the costs associated with system upgrades to enhance the efficient and safe operation of pipeline systems. Accordingly, AGA's members have a direct interest in the issues raised in this proceeding.

III. BACKGROUND

The Commission stated that it is issuing the Proposed Policy Statement in an effort to establish an analytical framework for evaluating proposed cost recovery mechanisms to recoup infrastructure modernization costs necessary for the efficient and safe operation of the pipeline's system and compliance with new regulations.[3] The Commission noted that recent regulatory initiatives as well as increased safety regulations may require interstate natural gas pipelines to

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[2] For more information, please visit www.aga.org.

[3] *See Proposed Policy Statement* at P 20.

undertake significant investments to upgrade their facilities in order to meet these revised safety and reliability standards. In particular, the Commission noted that the Pipeline and Hazardous Materials Safety Administration ("PHMSA") is in the process of implementing a multi-year pipeline safety reform initiative to comply with a mandate to enhance the agency's ability to reduce the risk of future pipeline failures.[4] The Commission also noted that the Environmental Protection Agency ("EPA") issued a series of white papers which offer mitigation options for limiting the leaking of natural gas from compressors.[5] In addition, the EPA issued a rule for mandatory reporting, effective January 1, 2015, which will impose new requirements on the industry to monitor and report methane emissions.[6] The Commission, therefore, acknowledged that pipelines may face greater environmental monitoring and compliance costs, as well as potentially having to upgrade existing natural gas facilities.[7]

The Commission stated that it has historically required interstate natural gas pipelines to design their transportation rates to recover their costs based on projected units of service.[8] The Commission explained that such a requirement provides pipelines incentives to both minimize costs in order to provide services at the lowest reasonable costs consistent with reliable long-term service, and provide the maximum amount of service to the public.[9] The Commission has previously maintained the view that recovering costs associated with regulatory requirements in a tracking mechanism was contrary to the requirement to design rates based on estimated units of

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[4] *Id.* at P 3.
[5] *Id.* at P 6.
[6] *Id.* at P 7.
[7] *Id.* at P 8.
[8] *Id.* at P 10.
[9] *Id.*

service because the use of cost-trackers undercuts the referenced incentives by guaranteeing the pipeline a set revenue recovery.[10]

The Commission noted, however, that it had recently approved a contested settlement involving Columbia Gas Transmission, LLC, which included a tracking mechanism to recover substantial pipeline modernization costs that were shown to be necessary to ensure the safety and reliability of the pipeline's system.[11] In that case, the Commission determined that the tracking mechanism included certain characteristics that allowed the pipeline to make substantial capital investments while maintaining the necessary incentives for innovation and efficiency.[12] Based on *Columbia Gas*, the Commission proposed to allow pipelines to recover costs to modernize their systems through a tracking mechanism based on five criteria: (1) the pipeline's base rates must have been recently reviewed; (2) eligible costs must be limited to one-time capital costs to comply with safety or environmental regulations or be shown to be necessary for the safe or efficient operation of the pipeline; (3) the surcharge must protect captive customers from cost shifts; (4) the tracker must include a method to allow for periodic review; and (5) the pipeline must work collaboratively with shippers to obtain support for the surcharge.[13]

AGA and its members are committed to providing safe and reliable natural gas service to customers. Many AGA members, working in cooperation with their own state regulatory authorities, have developed and implemented pipeline modernization programs to ensure the safety and reliability of their systems. AGA, therefore, supports the efforts of the Commission to enhance the safe and reliable service provided by jurisdictional pipelines through appropriate

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[10] *Id.* at P 12.
[11] *Id.*, citing *Columbia Gas Transmission, LLC*, 142 FERC ¶ 61,062 (2013).
[12] *Id.* at PP 13-17.
[13] *Id.* at P 20.

cost recovery mechanisms. While AGA agrees with the overall goal of the Commission's proposal to provide interstate pipelines the option of employing a tracking mechanism to recover the costs of modernizing their facilities and infrastructure to enhance the efficient and safe operation of their systems, AGA believes that the Commission should ensure such tracking mechanisms are carefully crafted so as not to impose unreasonable cost burdens or risks on customers. Accordingly, AGA offers the following comments and recommendations regarding the criteria for approving such cost recovery trackers to allow for investments in enhancing safe and reliable operations while providing service at just and reasonable rates.

IV. COMMENTS

Review of Existing Rates

The Commission's proposal provides that a pipeline's base rates must have been recently reviewed through a general rate proceeding under Section 4 of the Natural Gas Act ("NGA") or through a collaborative effort between a pipeline and its customers.[14] AGA supports the consumer protection nature of this criterion and believes that collaboration between a pipeline and its customers will facilitate mutual understanding of the expected safety, reliability and compliance benefits resulting from any modernization investments which the pipeline would seek to recover through a tracking mechanism.[15] This collaborative effort will also provide an

[14] *Id.*

[15] In *Columbia Gas*, the mechanism provided for a revenue stream to support eligible facility capital costs, namely, return, taxes and depreciation on a rate base calculated at original cost less depreciation and associated deferred taxes. As a result, shippers received the benefit of a declining rate base and the full benefits of accelerated depreciation which significantly reduced carrying costs.

opportunity for shippers to consider a pipeline's current base rates in the context of the pipeline's proposed incremental investments and their overall benefits.[16]

Eligible Costs

The Commission proposed that costs eligible for recovery through a modernization tracking mechanism must be limited to one-time capital costs incurred to modify the pipeline's existing system to comply with safety or environmental regulations issued by PHMSA, EPA, or other federal or state government agencies, and other capital costs shown to be necessary for the safe or efficient operation of the pipeline.[17] The Commission also proposed that pipelines must specifically identify each capital investment to be recovered by the surcharge as well as an upper limit on the capital costs related to each project.[18]

AGA believes that pipelines should work collaboratively with their shippers to evaluate and identify up front what initial modernization investments may be recovered through a tracking mechanism as eligible costs. Pipelines should be required to clearly specify the investments which will be recovered through the tracking mechanism, and shippers should have the ability to challenge the inclusion of projects or costs as part of the collaborative process.[19] Fundamentally, projects should benefit customers through improved safety and reliability of the

[16] It may be the case that settlement of a rate investigation under Section 5 of the NGA may not necessarily be sufficient to establish that a pipeline's base rates and rate structure are reflective of current costs.
[17] *Proposed Policy Statement* at P 20.
[18] *Id.* at PP 20, 25.
[19] For example, in *Columbia Gas*, the costs of fines or remedial actions ordered by safety regulators were excluded from recovery through the tracker in order to give the pipeline an incentive not to ignore safety problems. In addition, costs should be limited to properly classified jurisdictional transmission and storage facilities. Also, it may be the case that projects are not cost-effective compared to alternative methods of addressing safety or reliability problems in which case it may be more appropriate to abandon certain facilities rather than replace them.

pipeline system in order for their costs to be included as eligible for recovery through a tracking mechanism.

AGA believes that expansion projects should not generally be considered as eligible projects unless the pipeline can demonstrate that existing shippers will receive an appropriate benefit.[20] Expansion project costs should only be eligible for recovery through a tracking mechanism if the project meets the standards specified in the Commission's policy statement regarding the certification of new interstate natural gas facilities.[21] Existing shippers should be able to choose, as part of the collaborative process, to support the inclusion of some modernization investments that would otherwise have been incurred as part of an expansion project in the tracking mechanism to the extent such investments benefit all shippers.

AGA would not oppose the inclusion of incremental non-capital maintenance costs of an eligible project if inclusion of such costs received widespread shipper support as part of the collaborative process. Similarly, AGA would not oppose the inclusion of incremental costs to comply with advisories, industry guidelines or local mandates that do not meet the definition of safety or environmental regulations issued by PHMSA, EPA, or other federal or state government agencies, if such costs received widespread shipper support as part of the collaborative process. The important criterion here is that a pipeline should work collaboratively with its shippers to identify and provide recovery for only those modernization costs that are in excess of a representative level of operation and maintenance costs already included in the cost of service underlying the pipeline's existing base rates.

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[20] For example, where an expansion project would benefit from a modernization investment or where there is a joint modernization and expansion project, the pipeline and its customers may determine the appropriate rate and tracking treatment as part of the collaborative process.

[21] *See Certification of New Interstate Natural Gas Pipeline Facilities*, 88 FERC ¶ 61,227 (1999), *clarified* 90 FERC ¶ 61,128, *further clarified* 92 FERC ¶ 61,094 (2000).

In its proposal, the Commission sought comment on whether costs incurred to minimize emissions should be considered for inclusion as eligible costs even if such costs are not expressly required to comply with safety or environmental regulations.[22] While AGA supports the goal of improving system efficiency and reducing emissions, AGA is concerned that allowing pipelines to define eligibility too broadly may lead to customers having to pay for investments that are not cost-effective. In other words, shippers should be permitted to challenge as part of the collaborative process the eligibility of projects undertaken for the purpose of emissions reduction that may not be cost-effective relative to alternative means of reducing emissions or to the reasonable expected costs of not undertaking the emissions reduction.[23]

In a similar vein, AGA recognizes that limiting cost recovery to only those projects identified on a pre-approved list at the outset of the process may be too restrictive. Priorities, needs, rule changes and project scopes will undoubtedly change as projects are completed, system conditions are assessed, and project engineering techniques advance. The Commission's proposal should recognize that the list of eligible projects will necessarily be dynamic and allow pipelines, working with their shippers on an ongoing basis, to create appropriate mechanisms to review and modify the list of eligible projects over time with a view toward ensuring that such modifications provide value to customers and are supported by the pipeline's shippers.

Avoidance of Cost Shifting

The Commission's proposal included a provision that requires pipelines to design the cost recovery mechanism in a manner that will protect the pipeline's captive customers from cost

[22] *Proposed Policy Statement* at P 26.
[23] As noted, it may be the case that significant emissions problems arise on economically marginal facilities such that abandonment or other actions such as purchasing emission credits, rather than replacement, are more cost-effective options.

shifts if the pipeline loses shippers or must offer increased discounts to retain business.[24] The Commission noted that the cost recovery mechanism in *Columbia Gas* provides rate stability and safeguards shippers against cost shifts by including a floor on the billing determinants that would be used to design the surcharge.[25] AGA supports the need to ensure that existing shippers are protected from substantial cost shifts, and believes that pipelines should be required, in consultation with their shippers, to develop appropriate measures to protect customers from cost shifts. AGA believes that the Commission should be open to various methods for protecting customers from potential cost shifts that have been developed through the collaborative process and have the widespread support of customers.

Periodic Review of the Surcharge

The Commission's proposal includes a provision that would require pipelines to include some method to allow a periodic review of whether the surcharge and the pipeline's base rates remain just and reasonable.[26] AGA supports the requirement and believes, as above, that there are a variety of methods that could be used to address the need to ensure that rates remain just and reasonable. Again, AGA believes that the Commission should be open to various, alternative methods for protecting customers through periodic reviews of rates or other means that have been developed through the collaborative process and have the wide-spread support of customers.

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[24] *Proposed Policy Statement* at P 20.
[25] *Id.*
[26] *Id.*

Shipper Support

The Commission specified that while it expects pipelines to work collaboratively with their shippers to seek support for the pipeline's proposed infrastructure modernization cost recovery mechanism, support from all shippers is not a prerequisite to approval of a cost recovery charge.[27] While AGA agrees that 100 percent shipper support should not be a necessary prerequisite for the establishment of a modernization cost recovery mechanism, any approved tracking mechanism for the recovery of costs to modernize a pipeline's system should be established through a robust, ongoing, collaborative process between the pipeline and its shippers that has widespread shipper support.

AGA contends that shipper support is needed to ensure that customers benefit from the investments that are made for which a tracker is used to recover the costs. Pipelines can always seek to obtain recovery of their costs, including modernization costs, through a rate change filing under NGA section 4, regardless of whether shippers support such a rate change. But, in order to obtain recovery of modernization costs through a tracking mechanism that is in addition to existing base rates, pipelines should be required to demonstrate that customers will benefit and that customers broadly support the pipeline's proposal.

[27] *Id.* at P 31.

V. CONCLUSION

Wherefore, the American Gas Association respectfully requests that the Commission consider the above comments in this proceeding.

Respectfully submitted,

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