Capacity Release & Related Rules for Using Pipeline Services

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Topics Covered

- Capacity Release
- Tying prohibition
- Shipper Must Have Title rule
- Buy-Sell prohibition
- Bidding in open seasons
- Application of Capacity Release rules in specific circumstances
- Waivers
Underlying Policies

- **Transparency**
  - in the reallocation of interstate capacity

- **Efficiency**
  - in the allocation of interstate capacity to ensure that capacity goes to the user willing to pay the highest price
The Basic Rules (18 CFR § 284.8)

- Firm shippers can release their firm transportation and storage rights permanently or on a short-term basis
  - Hinshaws/LDCs are not required to offer capacity release mechanisms because not required to provide firm transportation
  - FERC proposed expansion to Hinshaws/LDCs but panned in comments; proposal not yet withdrawn
- Releases must comply with the posting and bidding procedures in the pipeline’s tariff
- Releases can be conditioned on certain terms, such as the right to recall the capacity
The Basic Rules (cont’d)

- Both the releasing shipper and the replacement shipper contract with the pipeline
  - The releasing shipper remains liable for the reservation charges; receives a credit for the replacement shipper’s payments
  - Usage charges are not subject to the capacity release mechanism
- Pre-arranged releases are permitted, subject to the posting and bidding requirements
The Basic Rules (Rates)

- Rate cap on releases greater than one year: the max. rate in the pipeline’s tariff
- No rate cap on releases of one year or less
  - Release must take effect within 1 year of date pipeline is notified
- All consideration between the releasing and replacement shipper counts towards release rate
  - Could constitute a discount or a premium exceeding the max. rate
  - Exception: release is to an Asset Manager (as defined in the regulations)
The Basic Rules (Process)

- All capacity releases are posted
- Releases must be competitively bid, except:
  - Release of 31 days or less
    - But cannot be rolled-over to same replacement shipper without bidding
  - Pre-arranged release for more than one year at the max. rate
  - Release to an Asset Manager
  - Release to a marketer as part of a state-regulated retail access program
- If a pre-arranged release, the replacement shipper has a right to match any bids
The Basic Rules (AMAs)

- Releases to Asset Managers under an Asset Management Agreement (AMA)
  - A pre-arranged release exempt from bidding and tying prohibition, and some buy-sell prohibitions
  - AMA must be structured correctly under the rules
The Basic Rules (AMAs cont’d)

- AMA requirements: Releasing shipper call right
  - Releasing shipper must have right to call on delivery or purchase up to 100% of daily CD of released capacity any day during minimum of 5 months out of each 12 month period; 5/12 rule thereafter
  - If the release is less than one year, the call applies to the lesser of 5 months or the term of the release;
  - If the release is for storage capacity, the call is 100% of the daily CD for withdrawals or injections.
  - Call rights apply to each segment of a multi-segment release.
The Basic Rules (AMAs cont’d)

- Only AMAs that meet the definition qualify for the exemption from bidding and tying prohibitions, and some buy-sell prohibitions

- Information to be posted: whether the release is to an asset manager and the obligation to deliver gas to, or purchase from, the replacement shipper
The Basic Rules
(state retail access exception)

- Releases to marketers as part of a state retail access program
  - Pre-arranged release exempt from bidding
  - Consecutive short-term releases to the same marketer won’t be considered equivalent to a long-term release
  - Capacity must be used to provide gas supply to retail consumers under a state approved retail access program
  - Marketer can re-release the capacity to an asset manager
  - Marketer or asset manager can use excess released capacity to serve other, non-retail access customers
Related Rules
(most are policies announced in orders)
“Tying” prohibition

All terms and conditions for capacity release must be posted and non-discriminatory; and relate solely to the details of acquiring transportation on interstate pipelines (i.e., not “tied” to any other conditions). (source – Order No. 636-A)

Prohibited:

- Requiring the replacement shipper to take a particular source of supply
- Requiring the replacement shipper to use the capacity for deliveries to a particular state or LDC system

Permitted:

- Requiring the replacement shipper to take two different segments of interstate capacity
- Release of storage capacity tied to a sale of the gas in storage
- Release under an AMA tied to the sale or purchase of gas
Shipper Must Have Title ("SMHT") rule

The shipper on an interstate pipeline must hold title to the gas shipped.

• Prevents circumvention of the capacity release rules with capacity brokering
  • Capacity brokering is the subletting or re-release of capacity without notice to the pipeline or the Commission

• A firm capacity holder can authorize an agent to schedule transportation, but title to the gas must be held by the capacity holder and not the agent.
Buy-Sell prohibition

“A prohibited buy/sell transaction is a commercial arrangement where a shipper holding interstate pipeline capacity buys gas at the direction of, on behalf of, or directly from another entity (e.g., an end-user), ships that gas through its interstate pipeline capacity, and then resells an equivalent quantity of gas to the [same] entity at the delivery point.”

**Prohibited Buy-Sell Transactions**

Examples:

- LDC (Shipper) buys gas from AB Industrial Co. at the pipeline receipt point, transports it and sells the same quantity to AB Industrial Co. at the citygate.

- LDC (Shipper) buys gas from seller designated by AB Industrial Co., transports the gas and sells it to AB Industrial Co. at the citygate.

These transactions circumvent the capacity release rules.
Prohibited Buy-Sell Transactions (cont’d)

Comply with the SMHT rule but --

Do not conform to the transparency and efficiency policy objectives

Difficult to distinguish from commodity exchanges, or trading transactions that are netted, which are permitted

- AMAs are a permitted form of buy-sell
Rule of thumb for distinguishing commodity exchanges from prohibited buy-sell:

- Can the transaction be structured as a capacity release? If so, it may circumvent the capacity release rules.

- Are the two points liquid trading hubs? Would the transactions be netted at the end of the day?
Summary

Prohibited: Transactions that circumvent the rules

Capacity brokering

Buy-sell transactions

Exceeding rate cap & rebates

- Replacement shipper pays more consideration than the max. rate (if a rate cap applies)
- or receives payments from the releasing shipper that were not subject to bidding (rebates)
  - Exception: AMA agreements

Tying interstate capacity to particular sources of supply, to particular LDC systems, or limiting capacity for deliveries to one state
Summary

Examples of what may be permissible:

Commodity exchanges (or netting)

Releases tied to the release of other open access interstate capacity (with posting & bidding)

Releases tied to (bundled with) the sale of gas as long as it is not tied to one source of production and the capacity can be used for other shipments
  - AMAs that are consistent with the shipper call requirements
  - Storage release tied to purchase of the gas in storage
Bidding in Open Seasons

- 18 C.F.R. § 284.15 – Bidding by affiliates in open seasons for pipeline capacity
  
  - Multiple affiliates cannot bid in the open season for a pro rata share unless each has an independent business reason for bidding.
  
  - Coordinated bidding by affiliates could be considered market manipulation.
Applying the Capacity Release rules in specific circumstances
Short-term releases (no cap)

- One year or less & starts within one year of notifying pipeline
- Must be posted for bidding
  - Can be pre-arranged
  - Releasing shipper can notify a select few of posting
- Less than 31 days – no bidding required
  - Flipping prohibited – can not be extended or re-released to the same replacement shipper within 28 days without bidding

Negotiated Rate Agreements

- Releases capped at the max. rate for a long term release and requires posting and bidding for a short-term release
- A permanent release of a negotiated rate above the max. rate requires a waiver
- Negotiated usage charges are not subject to release
Storage releases

- Capacity may be tied to a sale of gas in storage or requirement to return storage capacity full
- Capacity release is separate from commodity transaction (pricing)
- Any conditions on the release must be disclosed in posting
When pipeline maximum rates change

- Pipeline refunds
  - Short term release – replacement shipper does not get refunds unless releasing shipper voluntarily agrees to flow-through or state commission requires

- Fixed rate vs max rate prearranged deal
  - Prearranged deals and/or bids should be clear whether they are for a fixed rate or the max rate (which can change)

Usage charges

- Not subject to the Capacity Release rules – pipeline and replacement shipper must negotiate this separately under selective discounting and negotiated rate policies
Commonly Granted Waivers

- From prohibitions on tying, SMHT, buy-sell, or rules for posting and bidding and max. rates (attribution of consideration)

- Circumstances:
  - Exiting the business – corporate restructuring, mergers, sales of business units or assets
  - Production tied to transportation

- These are temporary waivers (up to 180 days)

- For petition requirements see 127 FERC ¶ 61,106 P10 (2009)
Recent Issues

- Posting of offers to acquire capacity
  - Tariff compliance by pipelines
- Master FT agreements in lieu of capacity release
  - An issue in the Northeast
- Whether buy-sell prohibition applies to supply-side AMAs
  - Petition of Rice Energy
The decline in enforcement settlements in this area does not mean companies can relax compliance efforts!
Questions?

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FERC Regulations

Capacity Release, 18 CFR § 284.8

Affiliate Bidding in Open Seasons,
18 CFR § 284.15

Supplementary Materials for Presentation on Capacity Release and Related Rules for Using Pipeline Services by Andrea Wolfman, Alston & Bird, LLP

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§ 284.8 Release of firm capacity on interstate pipelines.

(a) An interstate pipeline that offers transportation service on a firm basis under subpart B or G of this part must include in its tariff a mechanism for firm shippers to release firm capacity to the pipeline for resale by the pipeline on a firm basis under this section.

(b)(1) Firm shippers must be permitted to release their capacity, in whole or in part, on a permanent or short-term basis, without restriction on the terms or conditions of the release. A firm shipper may arrange for a replacement shipper to obtain its released capacity from the pipeline. A replacement shipper is any shipper that obtains released capacity.

(2) The rate charged the replacement shipper for a release of capacity may not exceed the applicable maximum rate, except that no rate limitation applies to the release of capacity for a period of one year or less if the release is to take effect on or before one year from the date on which the pipeline is notified of the release. Payments or other consideration exchanged between the releasing and replacement shippers in a release to an asset manager as defined in paragraph (h)(3) of this section are not subject to the maximum rate.

(c) Except as provided in paragraph (h) of this section, a firm shipper that wants to release any or all of its firm capacity must notify the pipeline of the terms and conditions under which the shipper will release its capacity. The firm shipper must also notify the pipeline of any replacement shipper designated to obtain the released capacity. The pipeline must provide notice of offers to release or to purchase capacity, the terms and conditions of the release, and the name of any replacement shipper designated in paragraph (b) of this section, on an Internet web site, for a reasonable period.

(d) The pipeline must provide notice of offers to release or to purchase capacity, the terms and conditions of such offers, and the name of any replacement shipper designated in paragraph (b) of this section, on an Internet web site, for a reasonable period.

(e) The pipeline must allocate released capacity to the person offering the highest rate and offering to meet any other terms and conditions of the release. If more than one person offers the highest rate and meets the terms and conditions of the release, the released capacity may be allocated on a

§ 284.7 not include in its tariff any provision that inhibits the development of market centers.

(c) Reasonable operational conditions. Consistent with paragraph (b) of this section, a pipeline may impose reasonable operational conditions on any service provided under this part. Such conditions must be filed by the pipeline as part of its transportation tariff.

(d) Segmentation. An interstate pipeline that offers transportation service under subpart B or G of this part must permit a shipper to make use of the firm capacity for which it has contracted by segmenting that capacity into separate parts for its own use or for the purpose of releasing that capacity to replacement shippers to the extent such segmentation is operationally feasible.

(e) Reservation fee. Where the customer purchases firm service, a pipeline may impose a reservation fee or charge on a shipper as a condition for providing such service. Except for pipelines subject to subpart C of this part, if a reservation fee is charged, it must recover all fixed costs attributable to the firm transportation service, unless the Commission permits the pipeline to recover some of the fixed costs in the volumetric portion of a two-part rate. A reservation fee may not recover any variable costs or fixed costs not attributable to the firm transportation service. Except as provided in this paragraph, the pipeline may not include in a rate for any transportation provided under subpart B, C or G of this part any minimum bill or minimum take provision, or any other provision that has the effect of guaranteeing revenue.

(f) Limitation. A person providing service under Subpart B, C or G of this part is not required to provide any requested transportation service for which capacity is not available or that would require the construction or acquisition of any new facilities.

[Order 436, 50 FR 42493, Oct. 18, 1985]

Editorial Note: For Federal Register citations affecting §284.7, see the List of CFR Sections Affected, which appears in the Finding Aids section of the printed volume and at www.fdsys.gov.
basis provided in the pipeline’s tariff, provided however, if the replacement shipper designated in paragraph (b) of this section offers the highest rate, the capacity must be allocated to the designated replacement shipper.

(f) Unless otherwise agreed by the pipeline, the contract of the shipper releasing capacity will remain in full force and effect, with the net proceeds from any resale to a replacement shipper credited to the releasing shipper’s reservation charge.

g) To the extent necessary, a firm shipper on an interstate pipeline that offers transportation service on a firm basis under subpart B or G of this part is granted a limited-jurisdiction blanket certificate of public convenience and necessity pursuant to section 7 of the Natural Gas Act solely for the purpose of releasing firm capacity pursuant to this section.

(h)(1) The following releases need not comply with the bidding requirements of paragraphs (c) through (e) of this section:

(i) A release of capacity to an asset manager as defined in paragraph (h)(3) of this section;

(ii) A release of capacity to a marketer participating in a state-regulated retail access program as defined in paragraph (h)(4) of this section;

(iii) A release for more than one year at the maximum tariff rate; and

(iv) A release for any period of 31 days or less.

(v) If a release is exempt from bidding requirements under paragraph (h)(1) of this section, notice of the release must be provided on the pipeline’s Internet Web site as soon as possible, but not later than the first nomination, after the release transaction commences.

(2) When a release of capacity is exempt from bidding under paragraph (h)(1)(iv) of this section, a firm shipper may not roll over, extend or in any way continue the release to the same replacement shipper using the 31 days or less bidding exemption until 28 days after the first release period has ended. The 28-day hiatus does not apply to any re-release to the same replacement shipper that is posted for bidding or that qualifies for any of the other exemptions from bidding in paragraph (h)(1) of this section.

(3) A release to an asset manager exempt from bidding requirements under paragraph (h)(1)(i) of this section is any pre-arranged release that contains a condition that the releasing shipper may call upon the replacement shipper to deliver to, or purchase from, the releasing shipper a volume of gas up to 100 percent of the daily contract demand of the released transportation or storage capacity, as provided in paragraphs (h)(3)(i) through (h)(3)(iii) of this paragraph.

(i) If the capacity release is for a period of one year or less, the asset manager’s delivery or purchase obligation must apply on any day during a minimum period of the lesser of five months (or 155 days) or the term of the release.

(ii) If the capacity release is for a period of more than one year, the asset manager’s delivery or purchase obligation must apply on any day during a minimum period of five months (or 155 days) of each twelve-month period of the release, and on five-twenths of the days of any additional period of the release not equal to twelve months.

(iii) If the capacity release is a release of storage capacity, the asset manager’s delivery or purchase obligation need only be up to 100 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)(ii) 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.
§ 284.15 Bidding by affiliates in open seasons for pipeline capacity.

(a) Multiple affiliates of the same entity may not participate in an open season for pipeline capacity conducted by any interstate pipeline providing service under subparts B and G of this part, in which the pipeline may allocate capacity on a pro rata basis, unless each affiliate has an independent business reason for submitting a bid.

(b) For purposes of this section, an affiliate is any person that satisfies the definition of affiliate in §358.3(a)(1) and (3) of this chapter with respect to another entity participating in an open season subject to paragraph (a) of this section.

[Order 894, 76 FR 72306, Nov. 23, 2011]

Subpart B—Certain Transportation by Interstate Pipelines

§ 284.101 Applicability.

This subpart implements section 311(a)(1) of the NGPA and applies to the transportation of natural gas by any interstate pipeline on behalf of:

(a) Any intrastate pipeline; or

(b) Any local distribution company.

§ 284.102 Transportation by interstate pipelines.

(a) Subject to paragraphs (d) and (e) of this section, other provisions of this subpart, and the conditions of subpart A of this part, any interstate pipeline is authorized without prior Commission approval, to transport natural gas on behalf of:

(1) Those that are located upstream of a processing, treatment or dehydration plant;

(2) Those that deliver more than ninety-five percent (95%) of the natural gas volumes they flow directly to end-users or on-system storage as measured in average deliveries for the previous three calendar years;

(3) Storage providers;

(4) Those that deliver the entirety of their transported natural gas directly to an end-user that owns or operates the major non-interstate pipeline.


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(a) Multiple affiliates of the same entity may not participate in an open season for pipeline capacity conducted by any interstate pipeline providing service under subparts B and G of this part, in which the pipeline may allocate capacity on a pro rata basis, unless each affiliate has an independent business reason for submitting a bid.

(b) For purposes of this section, an affiliate is any person that satisfies the definition of affiliate in §358.3(a)(1) and (3) of this chapter with respect to another entity participating in an open season subject to paragraph (a) of this section.

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