DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Docket No. PL15-1-000]

Cost Recovery Mechanisms for Modernization of Natural Gas Facilities

AGENCY: Federal Energy Regulatory Commission.

ACTION: Proposed policy statement.

SUMMARY: In this proposed Policy Statement, the Commission seeks to provide greater certainty concerning the ability of interstate natural gas pipelines to recover the costs of modernizing their facilities and infrastructure to enhance the efficient and safe operation of their systems. The proposed Policy Statement explains the standards the Commission would require interstate natural gas pipelines to satisfy in order to establish simplified mechanisms, such as trackers or surcharges, to recover costs associated with replacing old and inefficient compressors and leak-prone pipes and performing other infrastructure improvements and upgrades to enhance the efficient and safe operation of their pipelines.

DATES: Initial Comments are due **[INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**, and Reply Comments are due **[INSERT DATE 50 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

ADDRESSES: Comments, identified by docket number, may be filed in the following ways:

- Electronic Filing through http://www.ferc.gov. Documents created electronically using word processing software should be filed in native applications or print-to-PDF format and not in a scanned format.
- Mail/Hand Delivery: Those unable to file electronically may mail or hand-deliver comments to: Federal Energy Regulatory Commission, Secretary of the Commission, 888 First Street, NE, Washington, DC 20426.

Instructions: For detailed instructions on submitting comments and additional information on the rulemaking process, see the Comment Procedures Section of this document.

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SUPPLEMENTARY INFORMATION:

PROPOSED POLICY STATEMENT

1. In this proposed Policy Statement, the Commission seeks to provide greater certainty concerning the ability of interstate natural gas pipelines to recover the costs of modernizing their facilities and infrastructure to enhance the efficient and safe operation of their systems. The proposed Policy Statement explains the standards the Commission would require interstate natural gas pipelines to satisfy in order to establish simplified mechanisms, such as trackers or surcharges, to recover costs associated with replacing old and inefficient compressors and leak-prone pipes and performing other infrastructure improvements and upgrades to enhance the efficient and safe operation of their pipelines. The Commission requests comments on this Proposed Policy Statement. Initial Comments are due 30 days after publication of this order in the Federal Register, with reply comments due 50 days after publication in the Federal Register.

I. Background

2. There have been several recent legislative actions, and resulting regulatory initiatives, to address natural gas pipeline infrastructure safety and reliability. In 2012, Congress passed the Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011.[1] That act includes requirements for the Department of Transportation to take various actions to reduce the risk of future pipeline failures. Among other things, the

[1] Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011, 49 U.S.C.S. 60101 (2012) (Pipeline Safety Act).

Pipeline Safety Act requires the Department of Transportation to (1) consider expansion and strengthening of its integrity management regulations, (2) consider requiring automatic shut-off valves on new pipeline construction, (3) require pipelines to reconfirm their Maximum Allowable Operating Pressures (MAOP), and (4) conduct surveys to measure progress in plans for safe management and replacement of cast iron pipelines.

3. The Pipeline and Hazardous Materials Safety Administration (PHMSA) is in the process of implementing a multi-year Pipeline Safety Reform Initiative to comply with the Pipeline Safety Act's mandate to enhance the agency's ability to reduce the risk of future pipeline failures.[2] Prior to the Pipeline Safety Act's enactment, on August 25, 2011, PHMSA published an Advance Notice of Proposed Rulemaking (ANOPR) titled "Pipeline Safety: Safety of Gas Transmission Pipelines," which asked all stakeholders whether PHMSA should modify its existing integrity management and other pipeline safety regulations for interstate natural gas pipelines.[3] The ANOPR requested public comment on a range of topics related to current industry practices, the effects of enhanced regulations on safety and cost, and the best method to implement proposed

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[2] Written Statement of Cynthia Quarterman, Administrator, PHSMA, before the U.S. House of Representatives, Committee on Transportation and Infrastructure, Subcommittee on Railroads, Pipelines, and Hazardous Materials (May 20, 2014), http://transportation.house.gov/uploadedfiles/2014-05-20-quarterman.pdf (Quarterman Testimony) at 3.

[3] *Pipeline Safety: Safety of Gas Transmission Pipelines*, (RIN: 2137-AE72), 76 Fed. Reg. 53086 (August 25, 2011).

regulations. For example, PHMSA sought comments on shut-off valves and remote controlled shut-off valves. In addition, PHMSA held a public leak detection and valve workshop on March 28, 2012.

4. Also as part of the ANOPR process, PHSMA is considering expanding the definition of a High Consequence Area (HCA) so that more miles of pipeline may become subject to integrity management requirements.[4] PHMSA is also considering potential new rules related to repair criteria, including applying the integrity management repair criteria to non-HCAs; reassessing the repair criteria in areas where the population has grown since the pipeline was constructed; requiring methods to validate in-line inspection tool performance and qualifications of personnel; and implementing risk tiering such that repairs in an HCA have priority over repairs in a non-HCA. PHMSA held a Class Location Methodology workshop on April 16, 2014. Based on the comments from the ANOPR and the workshop, PHMSA "has started drafting a report to Congress on this issue."[5]

5. PHMSA is also considering changes to its requirements that pipelines perform baseline and periodic assessments of pipeline segments in an HCA through one or a combination of in-line inspection, pressure testing, direct assessment of external and

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[4] An HCA is a location which is defined in the pipeline safety regulations as an area where pipeline releases have greater consequences to the safety, health and environment. Basically, these are areas with greater population density.

[5] Quarterman Testimony at 10.

internal corrosion, or other technology demonstrated to accurately assess the condition of a pipe. In June 2013, as updated in September 2013, PHMSA issued a flow chart reflecting its draft Integrity Verification Process for natural gas pipelines.[6] To this end, PHMSA seeks information as to what anomalies have been detected using the various assessment methods, and proposes to include criteria in the regulations that would require more rigorous corrosion control.

6. In addition to pipeline safety issues, there have been growing concerns about the emissions of greenhouse gases (GHG) in the production and transportation of natural gas. On April 15, 2014, EPA issued a series of technical white papers, for which they have requested input from peer reviewers and the public, to determine how to best pursue reductions of emissions from, inter alia, natural gas compressors.[7] The EPA Compressor White Paper discusses the most prevalent types of compressors (reciprocating and centrifugal) and compressor emission data. As relevant to this proposed policy statement, the EPA lays out several "mitigation options for reciprocating compressors involve[ing] techniques that limit the leaking of natural gas past the piston rod packing, including replacement of the compressor rod packing, replacement of the piston rod, and the refitting or realignment of the piston rod."[8] The EPA also describes several mitigation

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[6] 78 FR 56268 (Sept. 12, 2013).

[7] See http://www.epa.gov/airquality/oilandgas/whitepapers.html.

[8] EPA Compressor White Paper at 29.

options for centrifugal compressors to limit the leaking of natural gas "across the rotating shaft using a mechanical dry seal, or capture the gas and route it to a useful process or to a combustion device."[9] If the EPA's white papers result in the agency imposing mitigation requirements on natural gas pipelines, such controls could be significant.[10]

7. We also note that in 2009, the EPA published a rule for mandatory reporting of greenhouse gas emissions (GHG) from sources that, in general, emit 25,000 metric tons or more of carbon dioxide equivalent per year in the United States.[11] This initiative, commonly referred to as the Greenhouse Gas Reporting Program (GHGRP), collects greenhouse gas data from facilities that conduct Petroleum and Natural Gas Systems activities, including production, processing, transportation and distribution of natural gas. Moreover, on November 14, 2014, the EPA issued a prepublication version of a final rule revising the Petroleum and Natural Gas Systems source category (Subpart W) and the General Provisions (Subpart A) of the GHGRP.[12] The final rule, which is effective

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[9] *Id.* at 29-42.

[10] For example, the Interstate Natural Gas Association of America (INGAA) comments that one of its member companies "reported capital costs of $865,000 for replacement of a wet seal" on a centrifugal compressor. *See* INGAA Comments on EPA Compressor White Paper at 13 (filed June 16, 2014). INGAA also commented on the EPA's Leaks White Paper and noted that many factors could affect leak repair costs and that "the cost of the repair may far exceed the benefit of eliminating a small leak." *See* INGAA Comments on EPA Leaks White Paper at 12-13 (filed June 16, 2014).

[11] Mandatory Reporting of Greenhouse Gases Rule, 74 Fed. Reg. 56260 (Oct. 30, 2009). *See also* 40 CFR Pt. 98 (2014).

[12] Greenhouse Gas Reporting Rule: 2014 Revisions and Confidentiality

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January 1, 2015, imposes new requirements for the natural gas industry to monitor methane emissions and report them annually. Lastly, we note that on that same day, the EPA issued a prepublication version of a proposed rule to add calculation methods and reporting requirements for greenhouse gas emissions, as relevant here, from blowdowns of natural gas transmission pipelines between compressor stations. The EPA also proposes confidentiality determinations for new data elements contained in the proposed amendments.[13]

8. One likely result of the Pipeline Safety Act and PHMSA's rulemaking proceedings is that interstate natural gas pipelines will soon face new safety standards requiring significant capital cost expenditures to enhance the safety and reliability of their systems.[14] Moreover, pursuant to EPA's initiatives, pipelines may in the future face increased environmental monitoring and compliance costs, as well as potentially having to replace or repair existing natural gas compressors or other facilities.

Determinations for Petroleum and Natural Gas Systems, Docket Nos. EPA-HQ-OAR-2011-0512 and FR:-9918-95-OAR (Nov. 14, 2014).

[13] *See* Greenhouse Gas Reporting Rule: 2015 Revisions and Confidentiality Determination for Petroleum and Natural Gas Systems, Docket ID No. EPA-HQ-OAR-2014-0831 (issued Nov. 14. 2014).

[14] On July 29, 2014, the Department of Energy (DOE) announced steps to help modernize natural gas infrastructure. Moreover, on July 31, 2014, Secretary of Energy Ernest Moniz sent a letter to the Chairman of the Commission recommending the Commission explore efforts to provide greater certainty for cost recovery for new investments in modernization of natural gas transmission infrastructure as part of the FERC's work to ensure just and reasonable natural gas pipeline transportation rates.

9. Against this background, the Commission is proposing the instant Policy Statement in an effort to ensure that existing Commission ratemaking policies do not unnecessarily inhibit interstate natural gas pipelines' ability to expedite needed or required upgrades and improvements. The proposed Policy Statement would allow interstate natural gas pipelines to recover certain capital expenditures made to modernize pipeline system infrastructure in a manner that enhances system reliability, safety and regulatory compliance through a surcharge mechanism, subject to conditions intended to ensure that the resulting rates are just and reasonable and protect natural gas consumers from excessive costs. Further, under the proposed Policy Statement, the Commission may consider capital costs to replace compressor facilities or make other improvements in response to increased federal or state environmental regulations as eligible for inclusion in a modernization cost recovery mechanism, to the extent a pipeline shows such costs to be beyond ordinary capital investments in a pipeline's existing system for maintenance purposes.

10. The Commission generally requires that interstate natural gas pipelines design their open access natural gas transportation rates to recover their costs based on projected units of service.[15] This requirement means that the pipeline is at risk for under-recovery of its costs between rate cases but may retain any over-recovery. As the Commission explained in Order No. 436, this requirement gives the pipeline an incentive both to (1)

[15] 18 CFR 284.10(c)(2) (2014).

"minimize costs in order to provide services at the lowest reasonable costs consistent with reliable long-term service"[16] and (2) "provide the maximum amount of service to the public."[17]

11. Before the Pipeline Safety Act, the Commission held that capital costs incurred to comply with the requirements of pipeline safety legislation or with environmental regulations should not be included in surcharges,[18] except in the context of an uncontested settlement.[19] Noting that pipelines commonly incur capital costs in response to regulatory requirements intended to benefit the public interest, the Commission stated that recovering those costs in a tracking mechanism was contrary to the requirement to design rates based on estimated units of service because the use of cost-trackers undercuts the referenced incentives by guaranteeing the pipeline a set revenue recovery.

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[16] *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 436, FERC Stats. & Regs., Regulations Preambles 1982-1985 ¶ 30,665, at 31,534 (1985).

[17] *Id*. at 31,537.

[18] *See Granite State Gas Transmission, Inc.*, 132 FERC ¶ 61,089, at P 11 (2010) (*Granite State*); *Florida Gas Transmission Co.*, 105 FERC ¶ 61,171, at PP 47-48 (2003) (*Florida Gas*).

[19] *See e.g., Granite State Gas Transmission, Inc.*, 136 FERC ¶ 61,153 (2011); *Florida Gas Transmission Co.*, 109 FERC ¶ 61,320 (2004). In 2012, the Commission again rejected a protested proposal that would allow the pipeline to recover regulatory safety costs through a tracker, but noted that PHSMA was in the early stages of developing regulations to implement the Pipeline Safety Act, and that the Commission would consider the need for further action as PHMSA's implementation process moved forward. *CenterPoint Energy – Mississippi River Transmission, LLC*, 140 FERC ¶ 61,253, at P 65 (2012).

12. More recently, however, the Commission approved a contested settlement which included a tracker to recover substantial pipeline modernization costs that were shown to be necessary to ensure the safety and reliability of Columbia Gas Transmission LLC's (Columbia Gas) pipeline system.[20] The Columbia Gas settlement outlined significant operational and safety issues resulting from the age of its system and the corresponding inability to monitor and maintain the system using efficient modern techniques.[21] The Commission found that approving the settlement would facilitate Columbia Gas' ability to make substantial capital investments necessary to correct significant infrastructure problems, and thus provide more reliable service while minimizing public safety concerns.

13. The Commission's determination in *Columbia Gas* thus established general parameters for pipelines to consider when seeking recovery of pipeline investments for modernization costs related to improving system safety and reliability. The tracker approved in that case was designed to recover pipeline modernization capital costs of up to $300 million annually over a five year period. The Commission found that Columbia Gas' settlement included numerous positive characteristics that distinguished its cost

[20] *Columbia Gas Transmission, LLC*, 142 FERC ¶ 61,062 (2013) (*Columbia Gas*).

[21] Columbia Gas stated in that proceeding that over fifty percent of its regulated pipeline system was over 50 years old, that a significant portion of its system contained dangerous bare steel pipeline, that many of its compressors were also dated, that many of its control systems were running on obsolete platforms, and that it was only able to inspect a small percentage of its system using modern in-line inspection tools.

tracking mechanism from those the Commission had previously rejected and that work to maintain the pipeline's incentives for innovation and efficiency. The key aspects of the settlement upon which the Commission relied to approve the tracker included the following.

14. First, Columbia Gas worked collaboratively with its customers to ensure that its existing base rates, to which the tracker would be added, were updated to be just and reasonable. This included a reduction in Columbia Gas' base rates and a refund to its customers.

15. Second, the settlement specifically delineated and limited the amount of capital costs and expenses that may go into the cost recovery mechanism. Moreover, the eligible facilities for which costs would be recovered through that mechanism were specified by pipeline segment and compressor station. Further, the pipeline agreed to spend $100 million for normal system maintenance annually during the initial term of the tracker, which would not be recovered through the tracker. The Commission found that these provisions should assure that the projects whose costs are recovered through the tracker go beyond the regular capital maintenance expenditures the pipeline would make in the ordinary course of business and are critical to assuring the safe and reliable operation of Columbia Gas' system.

16. Third, the Commission found that a critically important factor to its approval of the settlement was the pipeline's agreement to a billing determinant floor for calculating the cost recovery mechanism, together with an agreement to impute the revenue it would achieve by charging the maximum rate for service at the level of the billing determinant

floor before it trues up any cost underrecoveries. The Commission found these provisions should alleviate its historic concern that surcharges which guarantee cost recovery diminish a pipeline's incentive to be efficient and to maximize the service provided to the public. The Commission also found that these provisions protect the pipeline's shippers from significant cost shifts if the pipeline loses shippers or must provide increased discounts to retain business.

17. Fourth, the surcharge was temporary and would terminate automatically on a date certain unless the parties agreed to extend it and the Commission approved the extension. Finally, the tracker was broadly supported by the pipeline's customers.

II. Discussion

18. The ultimate implementation of the recent initiatives described above, to improve natural gas infrastructure safety and reliability and to address environmental issues related to the operation of natural gas pipelines, appear likely to lead to the need for interstate natural gas pipelines to make significant capital investments to modernize their systems. In light of these developments, the Commission has a duty to ensure that interstate natural gas pipelines are able to recover the costs of these system upgrades in a just and reasonable manner that does not undercut their incentives to provide service in an efficient manner and protects ratepayers from unreasonable cost shifts.

19. As noted, the Pipeline Safety Act and EPA's proposed revisions to the Petroleum and Natural Gas Systems source category address serious concerns that directly affect the public interest. Although historically the Commission has generally disfavored pipelines' use of trackers to recover costs, the high probability that the initiatives discussed will lead

to imposition of significant compliance costs on pipelines justifies the consideration of such mechanisms, subject to specified conditions, as a way for pipelines to recover those costs in a timely manner, while also maintaining safe and efficient operation of pipeline systems and providing the maximum amount of service at a just and reasonable cost consistent with safe operations. Establishing a framework for pipelines to accelerate the recovery of one-time capital costs necessary to make system improvements to comply with new safety and environmental requirements should maintain pipelines' incentives for innovation and efficiency and prompt them to make such necessary system modifications in an expeditious manner, in advancement of the public interest.

20. Accordingly, the Commission proposes to establish a policy outlining the 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. The Commission proposes to base the policy on the guiding principles established in *Columbia Gas.* Pursuant to the proposed policy, a pipeline proposal for a cost recovery tracker to recover pipeline modernization costs would need to satisfy five standards:

(1) **Review of Existing Rates -** the pipeline's base rates must have been recently reviewed, either by means of an NGA general section 4 rate proceeding or through a collaborative effort between the pipeline and its customers; (2) **Eligible Costs** – the eligible costs 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, and the pipeline must specifically identify each capital investment to be recovered by the surcharge; (3) **Avoidance of Cost Shifting –** the pipeline must design the proposed surcharge in a manner that will protect the pipeline's captive customers from costs shifts if the pipeline loses shippers or must offer increased discounts to retain business; (4) **Periodic Review of the Surcharge** – the pipeline must include some method to allow a periodic review of whether the surcharge and the pipeline's base rates remain just and reasonable; and (5) **Shipper Support** – the pipeline must work collaboratively with shippers to seek shipper support for any surcharge proposal.

21. We discuss these five proposed standards, and potential issues for comment, below.

1. <u>Review of Existing Rates</u>.

22. Pursuant to this standard, the Commission proposes to require a pipeline proposing a tracker mechanism to establish that the base rates to which any surcharges would be added are just and reasonable and reflect the pipeline's current costs and revenues as of the date of the initial approval of the tracker mechanism. While in *Columbia Gas* the pipeline did this through a negotiated settlement with its shippers in which it agreed to reduce its base rates and establish a revenue sharing mechanism for base rate revenues above a certain level, the Commission will consider methods other than a pre-negotiated base rate settlement by which the pipeline could establish that its current base rates are just and reasonable. For example, concurrently with the pipeline's filing to establish the

tracker, the pipeline could make a new NGA general section 4 rate filing, or the pipeline could file a cost and revenue study in the form specified in section 154.313 of the Commission's regulations showing that its existing rates are just and reasonable. The Commission seeks input on these or other acceptable approaches for pipelines to demonstrate that existing base rates are just and reasonable.

2. Eligible Facilities.

23. The Commission intends that any tracking mechanism authorized under this policy be used by pipelines to recover only capital costs incurred to modify their existing systems to address the safety and other concerns discussed above. Accordingly, the Commission proposes that the capital costs eligible for recovery through the tracking mechanism authorized under the proposed policy be limited to one-time capital costs to modify the pipeline's existing system to comply with safety and environmental regulations, such as those being considered by PHMSA and by the EPA, as well as other capital costs shown to be necessary for the safe or efficient operation of the pipeline.

24. As we have recognized previously, interstate natural gas pipelines routinely make capital investments related to system maintenance in the ordinary course of business. It will continue to be the Commission's policy that such ordinary capital maintenance costs should not be included in a tracker mechanism. Permitting normal system capital maintenance costs to be recovered through a surcharge mechanism would inhibit a pipeline's incentives to minimize costs and maximize service because it would guarantee a certain level of cost recovery. Thus, the Commission proposes to establish a policy that, in order for a pipeline to recover costs through a proposed modernization surcharge

mechanism, it would need to demonstrate that the costs to be included are not normal capital maintenance expenditures but are costs necessary to address system safety, efficiency, or other similar concerns, such as in *Columbia Gas*, or to comply with federal or state regulations.

25. The Commission also proposes to require that, when the pipeline files to establish a tracker mechanism, it should specifically identify in its proposal the projects eligible for recovery, the facilities to be upgraded or installed by those projects, and an upper limit on the capital costs related to each project to be included in the surcharge. This will allow an upfront determination that the costs are eligible for recovery through the tracker and avoid later disputes about which costs or facilities qualify for such recovery. These requirements will also help ensure that normal capital expenditures to maintain the pipeline's system will not be eligible for recovery through a surcharge mechanism.[22] Allowing pipelines to only recover costs incurred to address critical system efficiency, safety, and environmental concerns and requirements through a tracker will provide the pipeline with an inducement to make the necessary modifications on an expedited basis without inhibiting the pipeline's incentive to provide the maximum level of service. Allowing such recovery will also advance the public's interest in the safe, efficient and environmentally sound operation of the nation's natural gas pipeline system.

[22] For example, the costs allowed to be recovered through Columbia Gas' modernization program are limited to capital costs to modify the pipeline's existing system that go beyond its normal capital investments to modify its system, and costs of expansions are expressly excluded from that surcharge.

26. In relation to this standard, the Commission also seeks comments on the following questions:

- Should the costs of modifications to compressors for the purpose of waste heat recovery be eligible for recovery under a modernization surcharge?
- This proposed policy statement would limit the capital costs eligible for recovery through the surcharge to costs incurred to modify the pipeline's existing system. However, the Commission requests comment on whether there are any capital costs associated with the expansion of the pipeline's existing capacity or its extension to serve new markets that may reasonably be included in the surcharge as necessary one-time capital expenditures to comply with safety and environmental regulations.
- Should capital costs incurred to minimize pipeline facility emissions be considered for inclusion in the surcharge, even if those costs are not expressly required to comply with environmental regulations?
- Should non-capital maintenance costs associated with environmentally sound operation of a compressor be considered for inclusion in the surcharge?
- Under what circumstances should the Commission permit a pipeline to include in the tracking mechanism the costs of additional projects not identified in the pipeline's original filing to establish the tracking mechanism?

3. Avoid Cost Shifts.

27. As noted above, the Commission's general open access interstate natural gas transportation rate regulations require that a pipeline's costs be recovered based on projected units of service. 18 C.F.R. § 284.10(c)(2) (2014). This requirement results in pipelines being placed at risk for any cost underrecovery between rate cases but also allows pipelines to retain any over recovery during that period, thereby providing pipelines with an incentive to minimize costs and to provide the maximum amount of service to the public.

28. The recovery of certain costs through a tracker mechanism, however, reduces those incentives because it guarantees the pipeline recovery of those costs. Moreover, a tracker mechanism can shift costs to the pipeline's captive customers. If a pipeline recovering costs through a tracker or surcharge loses shippers or must offer increased discounts to retain business, a tracker mechanism may shift the amounts previously paid by those shippers directly and automatically to the pipeline's remaining shippers. This direct cost shifting is one of the reasons the Commission has generally disfavored trackers, namely that the cost shifting described would occur without consideration of any offsetting items that would generally be considered in a section 4 rate proceeding, and which the pipeline would normally need to justify to recover.[23]

[23] For example, in order to recover costs associated with discounted rates the pipeline may have offered to certain shippers, the pipeline must demonstrate that the discount was required to meet competition. *Policy for Selective Discounting by Natural Gas Pipelines*, 113 FERC ¶ 61,173 (2005). In the case of a tracker, no such showing is

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29. Accordingly, as a prerequisite to the Commission approving a modernization cost tracker, and thereby effectively granting an exemption from the requirement that a pipeline recover costs based on projected units of service, the Commission proposes to establish a policy that the pipeline is required to design the surcharge in a manner that will protect the pipeline's shippers from significant cost shifts. One way to accomplish this goal may be that approved in *Columbia Gas*, where the pipeline sought to provide rate stability and safeguard shippers against cost shifts resulting from losses in billing determinants by agreeing to a floor on the billing determinants that could be used to design the surcharge. The provisions of the *Columbia Gas* tracker require the pipeline to design the surcharge based on the greater of actual annual billing determinants or the agreed upon floor, and to impute the revenue it would achieve by charging the maximum rate for service at the level of the billing determinant floor before trueing up any cost under-recoveries. The Commission found that these provisions alleviated the historical concern that allowing the recovery of capital costs through a surcharge will diminish the pipeline's incentive to operate efficiently and maximize service to the public, as well as provided protections from cost shifts if the pipeline lost customers or had to offer increased discounts to retain business.[24] While the Commission found this to be a just

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required by the pipeline to recover the covered costs from its remaining customers.

[24] *Columbia Gas*, 142 FERC ¶ 61,062 at P 25.

and reasonable way to ensure the prevention of cost shifts, we are open to considering other methods that may similarly protect a pipeline's customers.

4. Periodic Review of Surcharge.

30. Under this standard, the Commission proposes to require pipelines seeking approval of a modernization surcharge to include some method to allow a periodic review of whether the surcharge and the pipeline's base rates remain just and reasonable. For example, in *Columbia* Gas, the pipeline agreed to make the surcharge a temporary part of its rates (the surcharge expires automatically after five years), and included a requirement that the pipeline make a new NGA section 4 filing if it wants to continue the surcharge. The settlement also requires Columbia Gas to file a new NGA general section 4 rate case at that time. While the Commission intends to require that surcharge proposals must include a mechanism for periodic review, we remain open to, and seek comments on, reasonable methods of accomplishing this goal aside from that approved in *Columbia Gas*.

5. Shipper Support.

31. The Commission expects any pipeline seeking approval of a pipeline modernization surcharge to work collaboratively with its shippers to seek support for the pipeline's proposal.[25] We note, however, that while we strongly encourage the pipeline

[25] As we noted in *Columbia Gas*, the proposed surcharge had the support of a broad spectrum of the pipeline's shippers.

to attempt to garner support for its proposal among all interested parties, the Commission may nonetheless approve any proposal the pipeline demonstrates to be just and reasonable without one-hundred percent shipper agreement. Thus, the Commission does not intend to require support from all shippers as a prerequisite to approval of a cost recovery surcharge.

32. In addition to the considerations outlined above, the Commission also seeks comment on the following related issues:

- **Accelerated Amortization**

33. The capital costs included in the *Columbia Gas* surcharge are treated as rate base items, and thus Columbia Gas is allowed to recover a return on equity on the portion of those costs financed by equity. Consistent with the rate base treatment of those costs, they are to be depreciated over the life of Columbia Gas' system.[26] The Commission requests comments on whether pipelines should also be allowed to use accelerated amortization methodologies, akin to that approved by the Commission for hurricane repair cost trackers,[27] to recover the costs of any facilities installed pursuant to a modernization cost recovery mechanism. Under such a methodology the costs would not

[26] *Columbia Gas*, 142 FERC ¶ 61,062 at P 9.

[27] *See, e.g.*, *Sea Robin Pipeline Co., LLC*, 144 FERC ¶ 61,008 (2013) (*Sea Robin*).

be included in the pipeline's rate base, and the pipeline would not recover any return on equity with respect to the costs financed by equity. Instead, the pipeline would only be allowed to recover the interest necessary to compensate it for the time value of money. The Commission has approved amortization periods for hurricane or storm surcharges ranging from one year to four years at the Commission's interest rate for refunds.[28] Thus, the Commission seeks comments on whether pipelines should be permitted to use accelerated amortization methodologies, such as those approved for hurricane trackers, to recover the costs of any facilities installed pursuant to the modernization cost recovery mechanism, or whether the Commission should require pipelines to depreciate facilities subject to a modernization cost tracker over the life of the facilities.

- **Reservation Charge Credits**

34. The Commission requests comments on whether it should make any adjustments to its current reservation charge crediting policy in light of the proposed Policy

[28] *See, e.g., Sea Robin Pipeline Co.*, 137 FERC ¶ 61,201, at P 51 (2011) (approving 4-year recovery period for hurricane surcharge and finding surcharge to be just and reasonable); *High Island Offshore System, L.L.C.*, 135 FERC ¶ 61,105, (2011); *Stingray Pipeline Co., L.L.C.*, 127 FERC ¶ 61,308 (2009) (approving tariff provisions that allowed up to 36 months to amortize hurricane-related costs); *Discovery Transmission LLC*, 122 FERC ¶ 61,099, at P 8 (2008) (approving a 12-month recovery period for a hurricane surcharge subject to a cap with any uncollected amounts due to the cap to be recovered in a subsequent period); *Chandeleur Pipe Line Co.*, 117 FERC ¶ 61,250 (2006) (approving 12-month hurricane surcharge recovery period that was subsequently extended to 24 months).

Statement. As noted, given recent legislative and other actions to address pipeline efficiency, safety, and environmental concerns, it is likely that pipelines will be required to meet additional requirements that may include performing facility upgrades and replacements. This work, particularly the replacement of existing compressors or pipelines, may result in disruption of primary firm service. Pursuant to the Commission's existing reservation charge crediting policies, such one-time outages, if necessary to comply with government orders, may be treated as *force majeure* outages, for which only partial reservation charge credits are required.[29] Thus, the Commission seeks comment on whether it should modify its existing reservation crediting policy to require pipelines with modernization cost trackers to provide full reservation charge credits during periods that the pipeline must interrupt primary firm service to replace or install eligible facilities under the provisions of the modernization tracker.

- **Other Considerations**

35. The Commission welcomes comments on any other issues or factors the Commission should consider for inclusion in the Policy Statement as a prerequisite for approving a modernization cost recovery mechanism.[30]

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[29] *See e.g.*, *TransColorado Gas Transmission Co., LLC*, 144 FERC ¶ 61,175 (2013); *Gulf South Pipeline Co., LP*, 144 FERC ¶ 61,215 (2013).

[30] Because the proposed policy statement would address issues pertaining to the Commission's review of natural gas rate filings, the statement is categorically excluded from the requirements of the National Environmental Policy Act (NEPA), thus neither an environmental assessment nor an environmental impact statement is required. *See* 18 CFR 380.4(a)(25) (2014).

III. Procedure for Comments

36. The Commission invites interested persons to submit written comments on the Commission's proposed policy to establish guidelines for pipelines to implement trackers or surcharges to recover infrastructure modernization costs as discussed above. **Comments are due 30 days from the date of publication in the Federal Register** and **reply comments are due 50 days from the date of publication in the Federal Register**. Comments must refer to Docket No. PL15-1-000, and must include the commentor's name, the organization it represents, if applicable, and its address. To facilitate the Commission's review of the comments, commentors are requested to provide an executive summary of their position. Additional issues the commentors wish to raise should be identified separately. The commentors should double space their comments.

37. The Commission encourages comments to be filed electronically via the eFiling link on the Commission's web site at http://www.ferc.gov. The Commission accepts most standard word processing formats. Documents created electronically using word processing software should be filed in native applications or print-to-PDF format and not in a scanned format. Commenters filing electronically do not need to make a paper filing.

38. Commenters that are not able to file comments electronically must send an original of their comments to: Federal Energy Regulatory Commission, Secretary of the Commission, 888 First Street NE, Washington, DC 20426.

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

IV. Document Availability

40. 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 the Commission's Home Page (http://www.ferc.gov) and in the Commission's Public Reference Room during normal business hours (8:30 a.m. to 5:00 p.m. Eastern time) at 888 First Street, NE, Room 2A, Washington DC 20426.

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

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

By the Commission.

Kimberly D. Bose,
Secretary.

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