ENERGY BAR ASSOCIATION | 2019 MID-YEAR ENERGY FORUM

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Session B: *Drafting and Negotiating Precedent and Firm Transportation Agreement - A Skills Session*

Pipeline projects get built on the strength and stability of Precedent and Firm Transportation Agreements. These agreements have shifted over time as deals have evolved and FERC policies adjusted. Federal, state and local activities also have created additional risks and extended timelines for certain projects that parties often seek to mitigate contractually. What are the current best practices for these agreements? Join the panel as they explore this questions and more.

Speaker:
Patty Francis, *Vice President and Managing General Counsel*, Kinder Morgan

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Natural Gas Pipeline

Precedent Agreements

The Basic Terms

- Rate
- Volume
- Term
- Receipt Point
- Delivery Point

Types of Reservation Charges

<u>Type</u>	**<u>Policy</u>** *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) (Policy Statement).
• Tariff Rate	Aka “Recourse Rate,” “Maximum Rate”
• Rolled-In Rate Treatment (RIRT)	Request presumption for RIRT must meet system benefit test
• Neutral	Leave ambiguous for rate case w/o presumption
• Incremental	Cannot be lower than tariff rate FERC favorite, no subsidies Special accounting treatment
• Negotiated Rate	The Commission’s policies 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).

Types of Reservation Charges (cont'd)

Type

- Discounted Rate

- Lateral, Backhaul or facility specific

Policy

Policy for Selective Discounting By Natural Gas Pipelines, 111 FERC ¶ 61,309 (2005), *Order Denying Rehearing,* 113 FERC ¶ 61,173 (2005).

- More difficult with mainline facilities
- Can align with a new service
- Can be add-on or stand alone rate
- Allocation issues are rate case concern

Discounted Rate

- Must be below max tariff rate
  - Northern Natural Gas Co., 111 FERC ¶ 61,223 (2005).

- Discount terms specified in tariff, Natural Gas Pipeline Co., 84 FERC ¶ 61,099 (1998).
  - May apply to specified quantities
  - May apply only if certain quantities achieved
  - May apply during specified periods i.e., summer only
  - May apply to specified receipt/delivery points or other geographical areas
  - May adjust to provide overall effective rate
- Special rate case treatment (billing determinant adjustment) but only if show discount was given to meet competition
  - No change in facts and circumstances
    - TGP, 89 FERC ¶ 61,129 (1999).

Negotiated Rate

- Most common form of contract rate
- May be more or less than max tariff rate
  - Shipper paying more than max rate, is treated as paying max rate for open season/scheduling/allocation purposes
- Benefit to shipper is rate certainty
- Can use gas index basis differentials for pricing, 104 FERC ¶61,134 (2003)
- Must file contract or detailed terms in tariff
- Must give shipper right to pay recourse rate
- Must establish sub-account for revenues received, <u>NorAm Gas Transmission Co.</u> 75 FERC ¶ 61,091 (1996).

Other Charges

- Commodity

- Fuel
  - Can only forego if show no fuel is used in provider's service
    - ANR Pipeline Company, 86 FERC ¶ 61,316 at 62,135 (1999).
  - No subsidy rule is strictly applied and evaluated

- Surcharges

Volume

- Anchor shippers may be allowed to choose volume prior to a certain threshold date in PA as long as that date is clear in open season
- Anchor shippers may be allowed to ramp up or ramp down their volume but the open season must specify this opportunity
- Special rights to increase or decrease the volume after service has commenced are not generally permitted unless tariff allows
  - Commission perceives that changes in the contract demand are valuable and substantive rights that should be afforded to all other similarly situated firm shippers.
    - Columbia Gas Transmission LLC, 153 ¶61,008 (2015).
    - ANR, 97 FERC ¶61,224 (2001).

Term

- Primary Term
- Rights to Extend
  - Automatic (Evergreen) or affirmative extension
  - Shipper or Pipeline Choice to extend or terminate
  - Notice Period
  - ROFR rights
  - Period of extension
  - Rate after Primary Term
- At minimum, term should be long enough to allow pipeline to recover cost of facilities and a reasonable rate of return

Other PA Terms

- Credit Requirements
- Conditions Precedent (prior to service/prior to construction)
  - Termination Rights under PA
- Upstream/Downstream Facilities (jurisdictional and nonjurisdictional)
- In-Service definition (Start Date)
- Right to adjust rates (if capped or negotiated)
- Open Season Status/Timing
  - Obligation to solicit turnback
- Reps and Warranties
- Miscellaneous
  - Choice of Law
  - Notices
  - No Modification
  - Assignment
  - Waiver
- Cooperation
  - Right to contest/protest/complain about deal

Credit

- "Policy Statement on Creditworthiness,"111 FERC ¶ 61,412 (2005).
  - Result of Pipelines reacting to Enron crisis
  - Commission withdrew Proposed Rulemaking
- Forms of Security
  - Cash deposits
  - Letters of credit
  - Surety bonds
  - Parental guarantees

Credit (cont'd)

Base Tariff Rule

- 3 mos. Collateral of Reservation Charges North Baja Pipeline, LLC, 102 FERC ¶ 61,239 (2003).
- 3 mos. = amount of time pipeline can terminate shipper in default and be needy to remarket capacity
- Pipelines allowed to take into account credit risk into ROE, Williston Basin, 67 FERC ¶ 61,137 (1994).

Construction Projects (where capital is employed)

- Determined in Precedent Agreements (otherwise tariff rules apply)
- Offers opportunity to explicitly state what happens in bankruptcy
- Applies only to initial shippers (but continues after in-service)
- No predetermined amount but must reasonably reflect risk of remarketing project, Calpine Energy Services vs. SNG, 103 FERC ¶ 61,273 (2003) (30 mos. found reasonable).
- Must reduce credit obligation collateral over time

Negotiated Terms and Conditions of Service (everything else)

- Must start with proforma service agreement in Tariff
  - Elba Express, 130 FERC ¶ 61,144 (2010).
- If outside proforma service agreement then considered to be non-conforming
  - 18 CFR Section 154.1(d), Section 154.110.
- Tariff is intended to provide guidelines for service
- Generally must rely on GT&C in Tariff
- Intent is to ensure not unduly discriminatory service
  - Columbia Gas, 97 FERC ¶ 61,221 (2001).

Negotiated Terms and Conditions of Service (everything else) (cont'd)

- Some nonconforming NTCS may be permissible deviations
  - Is it a NAESB standard being waived or changed? Material
  - Does it harm other shippers or give Expansion Shipper a priority? Material
  - Does it give Expansion Shipper a benefit others don't have? Material
  - Does it restrict Expansion Shipper or Pipeline? Permissible
  - Is it likely only applicable to Expansion Shipper? Permissible

How to Cure A Material Deviation

- Put it in Tariff/Be Creative
  - Make it a “fill in the blank” provision
    - Seasonal terms
    - Choice of Law
    - Contract pressure
    - Evergreen rights
    - Days notice to terminate
  - Narrow the applicability of tariff provision to specific shipper’s circumstance or circumstances affecting expansion project
- Create new service or rate schedule
- Make restrictive provision part of Negotiated Rate
  - Revenue crediting adjustments
  - IT crediting
  - Flex firm
  - Banking
  - Minimum Bill
  - Exit Fee

Anchor/Foundation Shippers

- Allowed to give Anchor Shippers benefits (rate, term, capacity)
- Must give all potential shippers right to be an Anchor Shipper by meeting specified criteria
- Must be explicit in Open Season about rights giving Anchor Shippers and Criteria, Columbia Gas, 153 FERC ¶ 61,098 (2015).
- Must relate to parameters of project, Bison Pipeline LLC, 131 FERC ¶ 61,013 (2010). (May have different classes of customers to address unique circumstances of infrastructure.)
- Shippers that are anchor shippers may want more explicit terms in the PA to protect their rights.

Other Related Agreements

- Generally not permissible outside of Service Agreement and Tariff

- Generally viewed as nonconforming NTCS if deal with transportation or storage service

- May enter into separate Construction and Operating Agreements

- Must enter into OBA's at pipeline interconnections 18 CFR §284.12b(2)(i) (2019).

Most Favored Nations

- Generally not advisable because of long-term obligation
  - Not only does it restrict future business with other shippers it is a headache to administer
  - Consider limiting term and scope (narrower the better)
  - Acceptable in the context of a Negotiated Rate
- Defining comparable terms is important
  - Rate vs. rate + term vs. rate + volume
  - Level of volumes qualify
  - Long term vs. short term
  - Max rate deals exempted
  - Does it apply to capacity release
  - Capacity path or zone restrictions
    - Rockies Express, 145 FERC ¶61,179 (2013).
- Define process
  - Obligation to match?
  - Timeframe to accept?

Conditions Precedent

- Common provisions where PA will terminate if certain event does not occur by a specified date.
  - FERC approval
  - Receipt of other permits, consents, authorizations (e.g., air, USACE, DOE, Coastal Zone, SHPO, State DEQ)
  - Company Board approval
  - Final Investment Decision on upstream or downstream project
  - PSC approval or other regulatory permits for upstream or downstream project
  - Pipeline does not file application or place the project in-service
- Development cost obligations if CP's not met
  - Shipper pays prorata share of 100%
  - Shipper and pipeline pay 50%
  - Pipeline pays 100%

Rate Adjustments

- Under what circumstances may either party be allowed to renegotiate the rate or the deal?
  - Prior to start date and in negotiated rate provision
  - Could also pertain to renegotiation of CP dates
- Examples of circumstances may be:
  - Capital cost increases above a certain threshold
    - Threshold could be a percentage of estimated capital or dollar amount
    - Increases could be caused by expansion of scope or delays
  - Unforeseen permitting or construction issues
  - Changes in governmental regulations or changes in the applicability of governmental regulations (federal, state or local)
  - Conditions in the FERC Order that are material or deviations from the base application
  - Stays or injunctions threatened or issued in opposition to the project

Summary

- Precedent Agreement should generally track Service Agreement and Tariff terms and conditions.
- Exceptions (negotiated terms and conditions) outside of negotiated rate terms need careful examination. Facts will matter.
- If special credit terms apply (outside of 3 months rule) then they must be spelled out in the Precedent Agreement.
- Pay attention to timing and interaction with conditions precedent and other terms.
- Permitting and FERC timelines should be generously defined.