

SUBMITTED COMMITTEE REPORTS

Supplemental Report of the Committee on Natural Gas Certificate and Authorization Regulations Implementation of the Access Provisions of Order No. 436

Starting with the issuance of Order No. 436 on October 9, 1985, the Commission has issued a series of orders, substantially altering the conditions under which pipelines may transport natural gas on a self-implementing basis (i.e., may transport natural gas without first obtaining from the Commission a certificate of public convenience and necessity specifically authorizing the transportation).¹ Two key provisions in the regulatory scheme created by these orders are sections 284.8 and 284.9 of the Commission's regulations,² which set out how pipelines are to make self-implementing transportation available. The purpose of this report is to describe how the Commission has construed and implemented these provisions since their promulgation.

Section 284.8 relates to "firm" transportation, defined as transportation not subject to a prior claim by another shipper.³ Section 284.9 deals with "interruptible" transportation, defined as transportation which is subject to prior claims.⁴

The two regulations may be summarized together. These provisions require pipelines choosing to provide self-implementing transportation to do so where capacity is available⁵ without undue discrimination.⁶ In the preamble to Order No. 436, the Commission has explained that new self-implementing transportation must be provided on a "first-come, first-served" basis to the extent capacity is available.⁷ The regulation permits pipelines to impose reasonable operating conditions on shippers for whom they transport⁸ and to

1. Order No. 436, *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, [1982-1985 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 30,665 (1965), *modified*, Order No. 436-A, F.E.R.C. Stats. & Regs. ¶ 30,675 (1985), *modified further*, Order No. 436-B, III F.E.R.C. Stats. & Regs. ¶ 30,688, *reh'g denied*, Order No. 436-C, 34 F.E.R.C. ¶ 61,404, *reh'g denied*, Order No. 436-D, 34 F.E.R.C. ¶ 61,405, *reconsideration denied*, Order No. 436-E, 34 F.E.R.C. ¶ 61,403 (1986), *vacated and remanded sub nom. Associated Gas Distributors v. FERC*, 824 F.2d 981 (D.C. Cir. 1987). In *Associated Gas* the court generally upheld the substance of Order No. 436 and the procedures employed in adopting it, but found problems with certain issues and vacated and remanded the matter for further proceedings. On August 7, 1987, the Commission issued Order No. 500, which promulgated interim regulations in response to the court's remand. III F.E.R.C. Stats. & Regs. ¶ 30,761 (1987). That order was modified in Order No. 500-A, III F.E.R.C. Stats. & Regs. ¶ 30,770 (1987), Order No. 500-B, III F.E.R.C. Stats. & Regs. ¶ 30,772 (1987), and Order No. 500-C, F.E.R.C. Stats. & Regs. ¶ 30,786 (1987). Order No. 500 became effective on September 15, 1987, although, pursuant to Order Nos. 500-B and 500-C, the effective date of some of its provisions is January 1, 1988 and April 1, 1988.

2. 18 C.F.R. § 284.8-9 (1988).

3. *Id.* § 284.8(a)(3).

4. *Id.* § 284.9(a)(3).

5. *Id.* §§ 284.8(a)(e), 284.9(a)(e).

6. *Id.* §§ 284.8(b), 284.9(b).

7. Order No. 436 *supra* note 1, at 31,516.

8. 18 C.F.R. §§ 284.8(c), 284.9(c) (1988).

charge a "reservation fee" for firm transportation.⁹ Such a fee may not be charged for interruptible transportation.¹⁰ Finally, the regulations require sellers of gas to offer "take-or-pay credits" to pipelines in order for the pipelines to transport that gas.¹¹

In implementing these two regulations, the Commission has addressed three basic questions. First, it has determined how pipelines may allocate capacity among different categories of transportation service. Second, it has examined the types of operating conditions which a pipeline may impose on shippers for whom it is transporting. Finally, it has elaborated on what pipelines may require with respect to take-or-pay credits.

I. ALLOCATION OF CAPACITY

A. Priorities of Service

In determining the rules under which pipelines are to allocate capacity, the Commission has looked at two phases in the pipeline's operations: scheduling, which "entails the daily allocation of volumes";¹² and curtailment, defined as "the need to allocate capacity after deliveries have been scheduled, due to some unforeseen circumstance."¹³

1. Self-Implementing Transportation

The Commission has refused to permit pipelines to give other categories of service higher priority than self-implementing transportation when allocating capacity. Transportation which is self-implementing has equal priority to that which is specifically authorized under a certificate.¹⁴ Pipelines must also give self-implementing transportation the same priority as sales when providing service¹⁵ and when curtailing service.¹⁶

Self-implementing transportation of released gas (defined as gas released by the pipeline for which the pipeline receives a benefit) may not be given higher priority than that of other categories of gas in allocating transportation capacity.¹⁷ Transportation of released gas also may not be given a higher curtailment priority than that of other gas.¹⁸

2. Firm Service

Firm service, by definition, takes priority over interruptible service. Pipe-

9. *Id.* § 284.8(d).

10. *Id.* § 284.9(d).

11. This aspect of the regulations is discussed *infra* pt. III.

12. Moraine Pipeline Co., 42 F.E.R.C. ¶ 61,144, at 61,548, *reh'g granted in part*, 43 F.E.R.C. ¶ 61,118 (1988).

13. Consolidated Gas Transm'n Corp., 41 F.E.R.C. ¶ 61,130, at 61,324 (1987).

14. Texas E. Transm'n Corp., 37 F.E.R.C. ¶ 61,260, at 61,694-95 (1986), *reh'g granted in part*, 41 F.E.R.C. ¶ 61,015, *reh'g denied*, 41 F.E.R.C. ¶ 61,304 (1987).

15. MIGC, Inc., 39 FERC ¶ 61,030, at 61,084 (1987); Order No. 436, *supra* note 1, at 31,496.

16. Texas Gas Transm'n Corp., 39 F.E.R.C. ¶ 61,111, at 61,413 (1987).

17. United Gas Pipe Line Co., 39 F.E.R.C. ¶ 61,152, at 61,570-71 (1987), *reh'g granted in part*, 42 F.E.R.C. ¶ 61,247 (1988).

18. Natural Gas Pipeline Co., 41 F.E.R.C. ¶ 61,164, at 61,409 (1987).

lines may reduce available interruptible capacity if they reasonably believe that such capacity is needed for firm service.¹⁹ Interruptible service must be fully curtailed before curtailment of firm service.²⁰

Pipelines may only contract for new firm service if capacity is available.²¹ Capacity that is available is allocated on a first-come, first-served basis.²²

Once the shipper obtains capacity, it has the same entitlement to transportation as other firm customers and is entitled to pro-rata scheduling,²³ and curtailment.²⁴ Section 284.7 of the Commission's regulations²⁵ permits pipelines to offer shippers discounted transportation rates. Firm customers who pay such rates, unlike interruptible customers, do not lose their entitlement to capacity²⁶ or their right to pro-rata curtailment.²⁷

Section 284.10 of the Commission's regulations²⁸ requires pipelines providing self-implementing transportation to permit their firm sales customers to convert all or part of their firm sales entitlements to firm transportation over a five-year period. If there is not available capacity at a receipt point designated by the shipper exercising its conversion rights, the pipeline must offer the shipper capacity at an alternative point.²⁹ It is consistent with section 284.8(b) to give converting customers priority over shippers with pending requests for firm transportation.³⁰

3. Interruptible Service

Unlike firm service, interruptible service may be contracted for regardless of whether capacity is available.³¹ Except for certain instances, interruptible transportation is scheduled on a first-come, first-served basis.³² Under this approach, interruptible service is scheduled and contracted for on the basis of the earliest valid transportation request.³³ Pipelines are required to time-stamp requests received during the day to permit the priorities of shippers

19. Ozark Gas Transm'n Sys., 39 F.E.R.C. ¶ 61,105, at 61,364 (1987).

20. Texas Gas, 39 F.E.R.C., ¶ 61,111 at 61,413; Order No. 436, *supra* note 1, at 31,513.

21. Consolidated Gas Transm'n Corp., 38 F.E.R.C. ¶ 61,150, at 61,410, *reh'g granted in part*, 41 F.E.R.C. ¶ 61,130 (1987).

22. Northern Border Pipeline Co., 39 F.E.R.C. ¶ 61,104, at 61,351, *reh'g denied*, 41 F.E.R.C. ¶ 61,275 (1987).

23. Tennessee Gas Pipeline Co., 41 F.E.R.C. ¶ 61,310, at 61,816 (1987), *reh'g denied*, 42 F.E.R.C. ¶ 61,377 (1988).

24. Order No. 436, *supra* note 1, at 31,517; Moraine Pipeline Co., 42 F.E.R.C. ¶ 61,144, at 61,548 (1988); Transwestern Pipeline Co., 38 F.E.R.C. ¶ 61,061, at 61,171, *reh'g granted in part*, 41 F.E.R.C. ¶ 61,178 (1987).

25. 18 C.F.R. § 284.7 (1988).

26. Order No. 436-A, *supra* note 1, at 31,686; Colorado Interstate Gas Co., 39 F.E.R.C. ¶ 61,227, at 61,800 (1987).

27. Transwestern, 38 F.E.R.C. ¶ 61,061, at 61,170-71.

28. 18 C.F.R. § 284.10 (1988).

29. Northwest Pipeline Corp., 43 F.E.R.C. ¶ 61,342, at 61,956 (1988).

30. Panhandle E. Pipe Line Co., 43 F.E.R.C. ¶ 61,121, at 61,376 (1988).

31. Consolidated Gas Transm'n Co., 38 F.E.R.C. ¶ 61,150 at 61,410, *reh'g granted in part*, 41 F.E.R.C. ¶ 61,130 (1987).

32. Texas E. Transm'n Corp., 41 F.E.R.C. ¶ 61,015, at 61,027 (1987), *reh'g denied*, 41 F.E.R.C. ¶ 61,304 (1988).

33. Order No. 436-A, *supra* note 1, at 31,685.

submitting transportation requests on the same day to be determined.³⁴

Generally, scheduling of interruptible transportation on a pro rata basis is not permitted.³⁵ Such scheduling is inconsistent with the first-come, first-served rule in that such scheduling permits a late-comer to jeopardize the capacity of shippers ahead of it in the queue.³⁶

"Existing" interruptible service takes priority over "new" interruptible service.³⁷ "Existing" service has been defined as that which was in effect prior to either (1) the date on which Order No. 436 was issued (October 9, 1985)³⁸ or (2) the date on which the Commission approves the pipeline's tariff governing transportation under post 284,³⁹ and which qualifies for continuation. The Commission has suggested that existing service might not receive priority if such service was provided in an unduly discriminatory manner.⁴⁰

There are three instances in which interruptible capacity is not scheduled on a first-come, first-served basis. These instances occur where the scheduling of existing service is addressed in service contracts executed before the new service commenced; new service is allocated in an "open season"; or where service is scheduled on the basis of price.⁴¹

If the priority among persons providing existing service has been addressed in the service contracts, the priorities set out therein control; however, if the contracts are silent on this issue, priority should be determined on a first-come, first-served basis.⁴² The Commission has permitted existing interruptible service to be scheduled on a pro rata basis where that was the manner of allocation prior to the pipeline's obtaining a blanket certificate.⁴³

The Commission has permitted pipelines to implement "open seasons" whereby all requests for transportation made in a given time period preceding commencement of new, self-implementing transportation are assigned priorities on a basis other than first-come, first-served.⁴⁴ The shippers making these requests have a higher priority than shippers who submit requests after the close of the open season.⁴⁵ The pipeline must give potential shippers adequate

34. Southern Natural Gas Co., 41 F.E.R.C. ¶ 61,218, at 61,588 (1987), *reh'g granted in part*, 42 F.E.R.C. ¶ 61,261 (1988).

35. Northern Natural Gas Co., 37 F.E.R.C. ¶ 61,272, at 61,818 (1986), *reh'g denied*, 41 F.E.R.C. ¶ 61,275 (1987).

36. Texas E. Transm'n Corp., 37 F.E.R.C. ¶ 61,260, at 61,696 (1986).

37. Texas E., 41 F.E.R.C. ¶ 61,015, at 61,027.

38. Transcontinental Gas Pipe Line Corp., 38 F.E.R.C. ¶ 61,165, at 61,503 (1987).

39. Texas E., 41 F.E.R.C. ¶ 61,015, at 61,027.

40. See Southern Natural, 41 F.E.R.C. ¶ 61,218, at 61,589; Tennessee Gas Pipeline Co., 40 F.E.R.C. ¶ 61,194, at 61,640, *reh'g granted in part*, 41 F.E.R.C. ¶ 61,310, (1987), *reh'g denied*, 42 F.E.R.C. 61,377 (1988).

41. Emergency service may be given priority over the other kinds of interruptible service, regardless of priority in time. See Consolidated, 38 F.E.R.C. ¶ 61,150, at 61,398 (emergency service given a higher priority in curtailment than other interruptible service).

42. Northwest Cent. Pipeline Co., 38 F.E.R.C. ¶ 61,170, at 61,547, *reh'g denied*, Williams Natural Gas Co., 41 F.E.R.C. ¶ 61,141 (1987).

43. Consolidated Gas Transm'n Corp., 42 F.E.R.C. ¶ 61,348, at 61,993 (1988).

44. Tennessee, 40 F.E.R.C. ¶ 61,194, at 61,638; Pacific Gas Transm'n Co., 40 F.E.R.C. ¶ 61,193, at 61,616-19, *reh'g denied*, 41 F.E.R.C. ¶ 61,289 (1987).

45. Tennessee, 40 F.E.R.C. ¶ 61,194, at 61,638-39; Pacific Gas, 40 F.E.R.C., ¶ 61,193, at 61,616-19.

notice of the open season.⁴⁶

In approving open seasons, the Commission has permitted allocation of capacity on a pro rata basis⁴⁷ and on the basis of a lottery.⁴⁸ In approving the lottery, the Commission stated that either method would be appropriate where it was preceded by an open season; it was used only to establish the initial queue; it was conducted fairly; and it did not result in undue discrimination.⁴⁹ With respect to the fairness aspect, the Commission pointed out earlier that the lottery was conducted by an independent accounting firm rather than the pipeline and that the rules were made known to potential shippers prior to its commencement.⁵⁰

Section 284.7 of the Commission's regulations permits pipelines to charge a minimum and maximum rate for self-implementing transportation. The Commission has permitted scheduling of transportation based on the highest rate. The pipeline was permitted to schedule the shippers paying the highest rates first (transportation within this group being allocated on a first-come, first-served basis), prior to those paying lower rates.⁵¹

Specifically, pipelines experiencing anticipated capacity shortages may interrupt on the basis of rate, interrupting the transportation of shippers paying higher rates last.⁵² However, the pipeline must give the latter shipper five days notice and an opportunity to pay the higher rate.⁵³ If the shipper is willing to pay that rate, it maintains its priority; if not, the shipper may not later reclaim its place by offering to pay the higher rate.⁵⁴

In contrast to scheduling, curtailment of interruptible service may be effected under any method that is not unduly discriminatory.⁵⁵ This includes a "last-on, first-off" basis,⁵⁶ a pro rata basis,⁵⁷ or curtailment based on price.

A pipeline curtailing on the basis of price will first interrupt the transportation of those shippers paying the lowest rates.⁵⁸ Such a shipper will only lose its place in the queue during the interruption period.⁵⁹

The shipper should have an opportunity to pay the higher rate before losing its place in the queue;⁶⁰ however, because curtailments respond to unanticipated capacity shortages, the pipeline may not have time to give each shipper an opportunity to match the higher rate with respect to the volumes

46. *Southern Natural*, 41 F.E.R.C. ¶ 61,218, at 61,588.

47. *Tennessee*, 40 F.E.R.C. ¶ 61,194, at 61,639.

48. *Pacific*, 40 F.E.R.C. ¶ 61,193, at 61,617-19.

49. *Pacific Gas Transm'n Co.*, 41 F.E.R.C. ¶ 61,299, at 61,786-87 (1987).

50. *Pacific*, 40 F.E.R.C. ¶ 61,193, at 61,618.

51. *United Gas Pipe Line Co.*, 42 F.E.R.C. ¶ 61,247, at 61,799 (1988); *Natural Gas Pipeline Co.*, 39 F.E.R.C. ¶ 61,153, at 61,595, *reh'g granted in part*, 41 F.E.R.C. ¶ 61,164 (1987).

52. *United*, 42 F.E.R.C. ¶ 61,247, at 61,798; *Natural*, 39 F.E.R.C. ¶ 61,153, at 61,595.

53. *United*, 42 F.E.R.C. ¶ 61,247, at 61,798; *Natural*, 39 F.E.R.C. ¶ 61,153, at 61,595.

54. *United*, 42 F.E.R.C. ¶ 61,247 at 61,798-99; *Natural*, 39 F.E.R.C. ¶ 61,153, at 61,595.

55. *Consolidated Gas Transm'n Co.*, 41 F.E.R.C. ¶ 61,130, at 61,324 (1987).

56. *Southern Natural*, 41 F.E.R.C. ¶ 61,218, at 61,589.

57. *Id.* at 61,590 (prorata curtailment of existing interruptible transportation permitted).

58. *Northwest Pipeline Corp.*, 43 F.E.R.C. ¶ 61,342, at 61,959-60 (1988).

59. *Northwest Pipeline Corp.*, 42 F.E.R.C. ¶ 61,019, at 61,109, *reh'g granted in part*, 43 F.E.R.C. ¶ 61,342 (1988).

60. *Northwest*, 43 F.E.R.C. ¶ 61,342, at 61,959.

subject to curtailment. The Commission has approved an arrangement whereby the pipeline and shippers paying discounted rates provide in the transportation contract whether the shippers will match the higher rate during curtailments.⁶¹

A pipeline may waive its right to allocate capacity on the basis of price with respect to a customer receiving a particular discount.⁶² In that situation the pipeline must waive that right with respect to all customers receiving an equivalent or a lesser discount.⁶³

B. Retention of Priority

1. Extensions of Service

Contracts containing "evergreen" clauses — clauses permitting the shipper to extend the term of the contract — retain their priority to the extent the maximum volumes set out therein do not exceed the volumes set out in the original contract.⁶⁴ Contracts containing these or substantially similar clauses are also referred to as "rollover" contracts.⁶⁵

The Commission has declined to require pipelines to offer shippers evergreen clauses.⁶⁶ However, if the pipeline offers such a clause to one shipper, it must offer it to other shippers on a non-discriminatory basis.⁶⁷ For example, if a pipeline offers rollover contracts to its interruptible customers, it must also offer them to its firm customers.⁶⁸ The pipeline may require that firm transporters with rollover contracts provide reasonable notice regarding whether they wish to extend their contracts.⁶⁹

2. Changes in Service

a. Overrun Service

If a shipper requests a modification of its existing transportation service, the question arises as to whether the shipper retains its priority with respect to the modified portion of the service. Requests for "overrun service" (transportation in excess of the shipper's contractual entitlement) are treated as requests for new service and are subject to prior claims.⁷⁰ This is true even if the shipper's contractual entitlement is firm.⁷¹ Like other kinds of service, overrun service is to be scheduled and contracted for on a first-come, first-served basis,

61. *Id.*

62. *Natural Gas Pipeline Co.*, 41 F.E.R.C. ¶ 61,164, at 61,411 (1987).

63. *Id.*

64. *El Paso Natural Gas Co.*, 35 F.E.R.C. ¶ 61,440, at 62,060-61 (1986).

65. *Tennessee Gas Pipeline Co.*, 40 F.E.R.C. ¶ 61,194, at 61,639; *United Gas Pipeline Co.*, 39 F.E.R.C. ¶ 61,152, at 61,572 (1987).

66. *Columbia Gulf Transm'n Corp.*, 41 F.E.R.C. ¶ 61,281, at 61,731 (1987), *reh'g denied*, 42 F.E.R.C. ¶ 61,369 (1988).

67. *Columbia Gulf*, 41 F.E.R.C. ¶ 61,281, at 61,731.

68. *Tennessee Gas Pipeline Co.*, 41 F.E.R.C. ¶ 61,310, at 61,818 (1987).

69. *South Georgia Natural Gas Co.*, 41 F.E.R.C. ¶ 61,328, at 61,865 (1987).

70. *Texas Gas Transm'n Corp.*, 39 F.E.R.C. ¶ 61,111, at 61,413 (1987); *Transcontinental Gas Pipe Line Corp.*, 38 F.E.R.C. ¶ 61,165, at 61,503 (1987).

71. *Trailblazer Pipeline Co.*, 39 F.E.R.C. ¶ 61,103, at 61,333-34 (1987).

but may be curtailed on any basis that is not unduly discriminatory.⁷²

b. Changes in Receipt Points

Pipelines have discretion as to whether to treat a shipper's request for new receipt points as a request for new transportation or as a routine modification of an existing service. In other words, the pipeline may state in its tariff that the shipper's requests for transportation at the new receipt point will be subject to prior requests at the new point or that the shipper will have the same priority at the new point as it did at the old.⁷³ The latter practice is referred to herein as providing the shipper with "flexible receipt points."

If the pipeline chooses to provide its shippers with flexible receipt points, it must specify the effect of the shipper's request on other shippers receiving or seeking to receive gas at the receipt point at issue.⁷⁴ Such a pipeline need not accept shippers' changes that would impair its ability to meet its obligations to provide firm service or to purchase from suppliers.⁷⁵ The Commission has indicated that a pipeline should not require the shipper to give more than thirty days notice prior to changing receipt points.⁷⁶

The Commission has declined to require pipelines to offer flexible receipt points.⁷⁷ However, a pipeline must offer shippers reasonable flexibility. It may not refuse to provide a new receipt point on the ground that the point will "result in inefficient utilization of the pipeline's system" or for some other similarly vague reason.⁷⁸ Similarly, pipelines may not require that the volumes the shipper is entitled to receive at the individual receipt points total no more than the total volume it is entitled to have transported.⁷⁹

The pipeline must apply its receipt point policy without undue discrimination. The policy should be applied to both existing and new transportation.⁸⁰ If the pipeline allows firm transporters to have flexible receipt points, it must allow interruptible shippers the same flexibility.⁸¹ The reverse is also true.⁸²

3. Changes in Delivery Points

The Commission generally has refused to allow pipelines to permit flexi-

72. Pacific Gas Transm'n Co., 40 F.E.R.C. ¶ 61,193, at 61,624 (1987).

73. See Texas E. Transm'n Corp., 37 F.E.R.C. ¶ 61,260, at 61,691 (1986).

74. Transcontinental, 38 F.E.R.C. ¶ 61,165 at 61,499-500.

75. Transcontinental Gas Pipe Line Corp., 41 F.E.R.C. ¶ 61,085, at 61,218, *reh'g denied*, 42 F.E.R.C. ¶ 61,153 (1987).

76. Panhandle E. Pipe Line Co., 43 F.E.R.C. ¶ 61,530, at 62,318-19 (1988) (pipeline's proposed 60-day notice requirement shortened by Commission to 30 days).

77. Natural Gas Pipeline Co., 41 F.E.R.C. ¶ 61,164, at 61,410 (1987); Texas E. Transm'n Corp., 41 F.E.R.C. ¶ 61,015, at 61,025 (1987).

78. Southern Natural Gas Co., 41 F.E.R.C. ¶ 61,218, at 61,588-89 (1987).

79. Texas E. Transm'n Corp., 43 F.E.R.C. ¶ 61,114, at 61,363 (1988).

80. Kentucky W. Va. Gas Co., 41 F.E.R.C. ¶ 61,155, at 61,389-90 (1987).

81. United Gas Pipe Line Co., 39 F.E.R.C. ¶ 61,152, at 61,570-71 (1987).

82. Tennessee Gas Pipeline Co., 41 F.E.R.C. ¶ 61,310 at 61,818 (1987).

ble delivery points, observing that such a practice would be inconsistent with the requirement, discussed below, that shippers seeking transportation identify the ultimate recipient of the gas.⁸³ If the shipper knows its ultimate recipient, it should be able to identify all of its potential delivery points when it seeks transportation; in that situation, flexible delivery points will be unnecessary.⁸⁴

On the other hand, the Commission has required pipelines to give shippers a degree of flexibility, in that the pipelines must permit shippers to designate at least five delivery points for firm transportation and an unlimited amount of delivery points for interruptible transportation.⁸⁵ The Commission has authorized a pipeline to permit its firm customers to change their delivery points for their system supply gas without losing their entitlements.⁸⁶

It is unclear whether pipelines may permit a shipper to increase its volumes at an individual receipt or delivery point beyond what it was originally designated to receive at that point without making a new transportation request.⁸⁷

C. Allocation of Storage

Sections 284.8 and 284.9 apply to a pipeline's "system" storage but not its "contract" storage. By way of background, a storage facility is an underground reservoir where gas can be injected and stored. Liquefied natural gas tanks are also used for storage and, when used in interstate commerce, are subject to Commission jurisdiction. A pipeline's storage of its own gas in the facility is called system storage; the pipeline's use of its facility to store the gas of another company is called contract storage.⁸⁸ A pipeline uses a storage facility as a second supply area and thereby lessens the need for pipeline capacity between the main production area and the storage facility during periods of peak demand.⁸⁹

The Commission has stated that, to the extent the pipeline uses its storage facilities to effect transportation of gas, they are transportation facilities and are therefore subject to the open-access requirements of Order No. 436.⁹⁰ Specifically, the pipeline must deliver gas into its system storage (to the extent storage capacity is available) in order to make capacity available for requested transportation.⁹¹ This holds true even if storage capacity is unavailable at the

83. *United*, 39 F.E.R.C. ¶ 61,152, at 61,570.

84. *Id.* at 61,570; *El Paso Natural Gas Co.*, 35 F.E.R.C. ¶ 61,440, at 62,066 (1986).

85. *Consolidated Gas Transm'n Corp.*, 42 F.E.R.C. ¶ 61,060, at 61,298 (1988).

86. *Columbia Gulf Transm'n Corp.*, 39 F.E.R.C. ¶ 61,335, at 62,040-41, *reh'g granted in part*, 41 F.E.R.C. ¶ 61,281 (1987).

87. *Compare Colorado Interstate Gas Co.*, 42 F.E.R.C. ¶ 61,380, at 62,124 (1988) (pipeline must treat shipper's requests to increase volumes shipper is authorized to receive at a given receipt point as a new request for transportation) with *Kentucky W. Va. Gas Co.*, 41 F.E.R.C. ¶ 61,155, at 61,390 (1987) (pipeline need not treat such requests as new requests as long as the increased volumes do not exceed the shipper's maximum transportation entitlements under the contract).

88. *Texas E. Transm'n Corp.*, 37 F.E.R.C. ¶ 61,260, at 61,714 (1986).

89. *Id.*

90. *Id.*; Order No. 436, *supra* note 1, at 31,507.

91. *Natural Gas Pipeline Co.*, 41 F.E.R.C. ¶ 61,164, at 61,415 (1987); see *Texas E.*, 37 F.E.R.C. ¶ 61,260, at 61,714.

time the request for storage is made. When capacity becomes available, shippers will be entitled to it on the same terms that they are entitled to available pipeline capacity.⁹² Where a customer changes from firm sales to firm transportation, the pipeline must use its system storage to provide transportation to the same extent that it previously used that storage to provide the customer sales gas.⁹³

Facilities used for contract storage are not subject to Order No. 436, because they are not used by pipelines.⁹⁴ The Commission has declined to require that pipelines provide new firm storage from available system storage, stating that such a requirement would be the equivalent of a requirement that pipelines provide new contract storage.⁹⁵ Pipelines may not use contract storage in a way that limits the pipeline's available firm transportation capacity.⁹⁶

II. REASONABLE OPERATING CONDITIONS

Pipelines must set forth in their tariffs the operating criteria in providing transportation.⁹⁷ The conditions which have received the most attention are discussed below.

A. Obtaining Transportation

If a shipper wishes to obtain self-implementing transportation, the shipper and the pipeline are to follow the following timetable.

Transportation may be requested up to ninety days prior to its commencement, or longer if construction of facilities is required.⁹⁸ The shipper initiates the process by submitting a request for transportation. Transportation requests may be sent by telecopier.⁹⁹

Once the request is received, the pipeline must tender a transportation contract or notify the shipper that its request has been rejected within a reasonable time.¹⁰⁰ If the pipeline tenders a contract, the shipper must execute it within thirty days.¹⁰¹

Shippers who have contracted for interruptible service must tender gas for transportation within fifteen days after the later of the date service is scheduled to start; the date the contract is executed; or the date the facilities to be constructed are ready for service.¹⁰² The shipper will not lose its priority if it fails to tender gas as a result of a force majeure event upstream or down-

92. Transcontinental Gas Pipe Line Corp., 38 F.E.R.C. ¶ 61,165, at 61,511 (1987).

93. Williams Natural Gas Co., 41 F.E.R.C. ¶ 61,141, at 61,358 (1987).

94. *Texas E.*, 37 F.E.R.C. ¶ 61,260 at 61,714.

95. Natural Gas Pipeline Co., 39 F.E.R.C. ¶ 61,153, at 61,610, *reh'g granted in part*, 41 F.E.R.C. ¶ 61,164 (1987).

96. *Williams*, 41 F.E.R.C. ¶ 61,141, at 61,358.

97. Northwest Pipeline Co., 42 F.E.R.C. ¶ 61,019, at 61,106 (1988).

98. Tennessee Gas Pipeline Co., 41 F.E.R.C. ¶ 61,310, at 61,816 (1987).

99. Pacific Gas Transm'n Co., 40 F.E.R.C. ¶ 61,193, at 61,620-21 (1987).

100. United Gas Pipe Line Co., 39 F.E.R.C. ¶ 61,152, at 61,571 (1987).

101. Transwestern Pipeline Co., 38 F.E.R.C. ¶ 61,061, at 61,170 (1987).

102. *Texas E. Transm'n Corp.*, 43 F.E.R.C. ¶ 61,114, at 61,363 (1988).

stream of the pipeline.¹⁰³

B. The Validation Process

The Commission has stated that pipelines must set out procedures to ensure that the shipper's request for transportation is valid and compatible with the pipeline's operation.¹⁰⁴ These procedures are collectively referred to as the "validation process."¹⁰⁵

That process serves three specific purposes: (1) obtaining information sufficient to permit the pipeline to determine whether capacity is available and whether the shipper's arrangements to deliver the gas to and to take the gas off the system meet the pipeline's operating conditions; (2) ensuring that the request for transportation relates to a specific transaction; and (3) obtaining a basis for determining shipper priorities.¹⁰⁶ The pipeline must include its information and documentation requirements in its tariff.¹⁰⁷

1. Mandatory Information Requirements

The pipeline satisfies the Commission's concerns with respect to validation if it requires its shippers to comply with the following procedures.¹⁰⁸

The shipper must include the following information in its request for transportation: (1) the names of the entities delivering and taking the gas to and from the pipeline and of the receipt and delivery points;¹⁰⁹ (2) the dates service is scheduled to commence and terminate;¹¹⁰ (3) certification by the shipper that it has title or a right to acquire title to the gas;¹¹¹ (4) and that it has entered into all necessary arrangements to secure upstream and downstream transportation of the gas.¹¹²

On the date the contract is executed, the shipper must disclose the iden-

103. *United*, 39 F.E.R.C. ¶ 61,152, at 61,571.

104. *See Consolidated Gas Transm'n Corp.*, 38 F.E.R.C. ¶ 61,150, at 61,408-09 (1987).

105. *Texas E. Transm'n Corp.*, 37 F.E.R.C. ¶ 61,260, at 61,678 (1986).

106. *Id.* The Commission's requirement that the request relate to a specific transaction is a part of its general prohibition against "capacity brokering," the practice of reserving capacity without having arranged a specific sale and then permitting other shippers to use it. *See Natural Gas Pipeline Co.*, 39 F.E.R.C. ¶ 61,153, at 61,593 (1987); *Texas E.*, 37 F.E.R.C. ¶ 61,260, at 61,884-85. The Commission's policy in this area is rapidly evolving. *See Notice of Proposed Rulemaking, Brokering of Interstate Gas Pipeline Capacity*, 43 F.E.R.C. ¶ 61,011 (1987), 53 Fed. Reg. 15,061 (1987). Discussion of this policy is outside the scope of this report.

107. *Transwestern Pipeline Co.*, 38 F.E.R.C. ¶ 61,061, at 61,169 (1987).

108. *See Pacific Gas Transm'n Co.*, 40 F.E.R.C. ¶ 61,193, at 61,621-22 (1987); *Consolidated*, 38 F.E.R.C. ¶ 61,150, at 61,408-09.

109. *Consolidated*, 38 F.E.R.C. ¶ 61,150, at 61,408.

110. *Id.*

111. *Pacific*, 40 F.E.R.C. ¶ 61,193, at 61,622; *see Transcontinental Gas Pipeline Corp.*, 41 F.E.R.C. ¶ 61,374, at 62,027-88 (1987), *reh'g denied*, 42 F.E.R.C. ¶ 61,280 (1988).

112. *Pacific*, 40 F.E.R.C. ¶ 61,193, at 61,622. If the pipeline is providing self-implementing transportation pursuant to section 311 of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3371 (1982), and not pursuant to a blanket certificate, the shipper must also certify that the local distribution company (LDC) or intrastate pipeline on whose behalf the gas is being transported is receiving an economic benefit; the requirement of a benefit is satisfied by an agency agreement between the shipper and the LDC or pipeline. *Hadson Gas Systems* (Docket No. GP88-11-000, July 19, 1988).

tity of the ultimate recipient of the gas, unless the gas is being purchased by a pipeline or local distribution company (LDC) for system supply, and provide verification that these ultimate recipients have signed sales contracts to use the transportation provided in the transportation contract.¹¹³ Marketers purchasing for system supply must disclose the end-users of the gas.¹¹⁴

The Commission has recognized that the shipper has a legitimate need to keep the identity of the end-user confidential prior to execution of the contract.¹¹⁵ However, the shipper must disclose the identity of the end-user of the gas at that time to assure all concerned parties that the request for capacity is for a specific transaction.¹¹⁶

Finally, the shipper must disclose, at the time service commences, information necessary to permit the pipeline to determine whether the gas to be transported is subject to take-or-pay crediting.¹¹⁷

2. Discretionary Information Requirements

The pipeline may require the shipper to include additional information in its transportation request. The shipper may be required to provide verification of all necessary government approvals¹¹⁸ and substantiation of the information contained in the request if the pipeline has reason to doubt, based on a reasonable, objective criterion, that the request for transportation has been submitted in good faith.¹¹⁹ If material information supplied by the shipper proves to be inaccurate, the shipper may lose its place in the queue.¹²⁰

C. Processing Fees

The Commission has rejected pipelines' attempts to impose processing fees on shippers seeking interruptible transportation, noting that in those circumstances the processing fee is no more than a prepayment for interruptible transportation, which is, in turn, prohibited under Order No. 436.¹²¹ The Commission has so ruled even when the pipeline has stated that it will not only credit the fee against subsequent transportation but will also refund the fee if no transportation is provided.¹²²

Imposition of processing fees for firm transportation has been allowed, because the fee is equivalent to a reservation fee, which, in turn, is allowed under section 284.8(d).¹²³ This fee is payable at the time the transportation request is forwarded.¹²⁴ The Commission has permitted collection of fees equivalent to two months' transportation; such fee is to be credited in the first

113. United Gas Pipe Line Co., 39 F.E.R.C. ¶ 61,152, at 61,578 (1987).

114. Tennessee Gas Pipeline Co., 41 F.E.R.C. ¶ 61,310, at 61,813-14 (1987).

115. *Texas E.*, 37 F.E.R.C. ¶ 61,260, at 61,681.

116. *Tennessee*, 41 F.E.R.C. ¶ 61,310, at 61,813.

117. These disclosures are discussed *infra* pt. III.

118. Columbia Gulf Transm'n Corp., 39 F.E.R.C. ¶ 61,335, at 62,042 (1987).

119. Trailblazer Pipeline Co., 39 F.E.R.C. ¶ 61,103, at 61,330 (1987).

120. *United*, 39 F.E.R.C. ¶ 61,152, at 61,571.

121. *Id.* at 61,576-77; *Texas E. Transm'n Corp.*, 37 F.E.R.C. ¶ 61,260, at 61,679-80 (1986).

122. *United*, 39 F.E.R.C. ¶ 61,152, at 61,576-77; *Texas E.*, 37 F.E.R.C. ¶ 61,260, at 61,679-80.

123. *United*, 39 F.E.R.C. ¶ 61,152, at 61,577.

124. *Id.*

two months of transportation.¹²⁵ The Commission has declined to permit imposition of a processing fee of more than \$10,000.¹²⁶ A processing fee must be refunded within a reasonable period of time if no transportation contract is executed.¹²⁷

D. Credit Worthiness

1. Financial Stability of Shipper

Pipelines may require prospective shippers to demonstrate their credit worthiness. An objective criterion for credit worthiness must be used.¹²⁸ In this regard, the Commission has rejected a provision requiring the shipper to provide "information sufficient to demonstrate that [it] will be able to meet its financial obligations."¹²⁹ In another order the pipeline has been required to set forth in its tariff standards for determining "minimal credit-worthiness."¹³⁰

Pipelines may require shippers to provide financial data in their transportation requests¹³¹ but may not require that such data be updated subsequently.¹³² The Commission has declined to require a pipeline to permit a shipper to substitute the financial data of a guarantor for its own.¹³³ Pipelines need not require a shipper that has previously demonstrated its credit worthiness to the pipeline to make that demonstration as a precondition to new service.¹³⁴

Shippers demonstrating an inability to pay may obtain transportation but may be required to prepay for as much as three months transportation as a "security deposit."¹³⁵ The Commission has rejected a tariff provision which would have required shippers to make a deposit equal to four months' service.¹³⁶

Pipelines may not terminate service to a shipper that becomes uncreditworthy without first obtaining authorization from the Commission.¹³⁷ The purpose of this requirement is to give the shipper an opportunity to show that the termination is unduly discriminatory.¹³⁸ The pregranted abandonment authority contained in blanket certificates does not provide such author-

125. Consolidated Gas Transm'n Corp., 38 F.E.R.C. ¶ 61,150, at 61,409 (1987).

126. Colorado Interstate Gas Co., 42 F.E.R.C. ¶ 61,380, at 61,124 (1988).

127. See Transcontinental Gas Pipe Line Corp., 41 F.E.R.C. ¶ 61,085, at 61,219 (1987) (pipeline permitted to refund processing fee equal to one month's transportation 120 days after shipper's request becomes void).

128. Texas E. Transm'n Corp., 41 F.E.R.C. ¶ 61,015, at 61,025 (1987).

129. United Gas Pipe Line Co., 39 F.E.R.C. ¶ 61,152, at 61,577-78 (1987).

130. Arkla Energy Resources, 39 F.E.R.C. ¶ 61,358, at 62,122, *reh'g denied*, 41 F.E.R.C. ¶ 61,138 (1987).

131. Tennessee Gas Pipeline Co., 40 F.E.R.C. ¶ 61,194, at 61,635 (1987).

132. *Id.* at 61,636.

133. Tennessee Gas Pipeline Co., 41 F.E.R.C. ¶ 61,310, at 61,814-15 (1987).

134. Trailblazer Pipeline Co., 39 F.E.R.C. ¶ 61,103, at 61,332 (1987).

135. Northern Natural Gas Co., 37 F.E.R.C. ¶ 61,272, at 61,822 (1986).

136. Arkla Energy Resources, 41 F.E.R.C. ¶ 61,138, at 61,348 (1987).

137. Texas E. Transm'n Corp., 37 F.E.R.C. ¶ 61,260, at 61,685-86 (1986).

138. *Id.*

ity because it only permits abandonment at the end of the contract term.¹³⁹

2. Non-Payment of Bills

Pipelines may, without advance authorization from the Commission, curtail service for non-payment of bills as long as they give the shippers notice and an adequate time to correct the situation.¹⁴⁰ An adequate notice procedure includes an initial notice to the shipper that it has twenty days to pay the bill and, after the initial period has run, a second notice that unless payment is made within ten days, service will be suspended.¹⁴¹ The pipeline must state in its tariff the circumstances under which it will "curtail and resume" transportation service for a shipper that has failed to pay its bills.¹⁴²

E. Provisions Relating to Throughput

1. "Use-or-Lose"

"Use-or-lose" provisions provide that a shipper's failure to use reserved interruptible capacity will result in loss of such capacity;¹⁴³ such provisions discourage shippers from reserving more capacity than they need.

Use-or-lose provisions have several interrelated components. The first component is the period of time during which the shipper's use is measured. The second component is the minimum use permitted, measured as a percentage of the shipper's maximum daily transportation entitlements, such as maximum daily transportation quantity (MDTQ). The third component is the amount by which the shipper's entitlements are to be reduced, also measured in terms of the shipper's transportation entitlements, if the shipper fails to tender the minimum quantity of gas during the specified period of time.

The Commission has approved a wide range of use-or-lose provisions, including the following:

- (1) reduction of the allocated capacity of a shipper who has used less than 60% of MDTQ for a three-month period to the average daily quantity that it transported during that period;¹⁴⁴
- (2) reduction of the capacity of a shipper who has tendered gas volumes constituting less than 80% of its MDTQ (or 80% of the capacity made available to it by the pipeline, whichever is less) for a 60-day period to the average daily quantity tendered by the shipper;¹⁴⁵
- (3) reduction of a shipper's maximum receipt volume to 120% of volumes transported in the highest month for the past twelve months if the shipper fails to use 50% of its maximum receipt volume during a given month;¹⁴⁶ and

139. *Id.*

140. Colorado Interstate Gas Co., 42 F.E.R.C. ¶ 61,380, at 62,122 (1988); Natural Gas Pipeline Co., 41 F.E.R.C. ¶ 61,164, at 61,408-09 (1987).

141. Southwest Gas Corp., 43 F.E.R.C. ¶ 61,257, at 61,713 (1988).

142. Tennessee Gas Pipeline Co., 41 F.E.R.C. ¶ 61,310, at 61,815 (1987).

143. El Paso Natural Gas Co., 35 F.E.R.C. ¶ 61,440, at 62,065 (1986).

144. Northwest Pipeline Corp., 39 F.E.R.C. ¶ 61,109, at 61,400 (1987).

145. Transcontinental Gas Pipe Line Corp., 38 F.E.R.C. ¶ 61,165, at 61,492-93 (1987).

146. Colorado Interstate Gas Co., 42 F.E.R.C. ¶ 61,380, at 62,122-23 (1988).

(4) termination of transportation if the shipper fails to use the service for two consecutive months in which capacity is available.¹⁴⁷

A use-or-lose provision may not be implemented where the shipper's failure to use capacity is properly attributable to force majeure.¹⁴⁸ Firm customers, who must pay a reservation charge (the transportation equivalent of a sales demand charge), may not be made subject to such a provision.¹⁴⁹ In reducing a shipper's capacity under a use-or-lose provision, pipelines may not unilaterally specify the shipper's entitlements at each receipt and delivery point.¹⁵⁰

The Commission has declined to require a pipeline to include a use-or-lose provision¹⁵¹ and has permitted a pipeline to delete such a provision retroactively prior to approval of its tariff.¹⁵² However, pipelines choosing to implement use-or-lose provisions must apply them to contracts executed prior to as well as subsequent to issuance of Order No. 436.¹⁵³

Pipelines may implement a "no bump" rule under which a shipper may not increase the volumes it is transporting, regardless of its MDTQ and priority in the queue, if the increase will cause a reduction of quantities being transported by other shippers.¹⁵⁴ This rule may not be implemented to the extent that the shipper seeking the increase has been taking less than its MDTQ as a result of scheduled, routine maintenance,¹⁵⁵ force majeure,¹⁵⁶ or seasonal variations.¹⁵⁷ If capacity becomes available, it must first be offered to shippers, according to their place in the queue, who are currently transporting less than their full contractual entitlements.¹⁵⁸

2. Minimum Throughput

Generally, minimum throughput provisions, which require that shippers tender a specified minimum volume of gas for transportation, are prohibited on the ground that they unduly discriminate against small shippers.¹⁵⁹

Pipelines may include in their tariffs provisions permitting rejection of gas volumes which are too small to be metered; however, the tariff must also state that the pipeline shall notify the shipper that the volumes are too small to be metered, state the quantity of gas that can be metered at the receipt point

147. *Natural Gas Pipeline Co.*, 39 F.E.R.C. ¶ 61,153, at 61,598 (1987). In this proceeding, the pipeline sought a provision which would have permitted it to terminate service after one month of non-use.

148. *Northwest*, 39 F.E.R.C. ¶ 61,109, at 61,400.

149. *Trailblazer Pipeline Co.*, 39 F.E.R.C. ¶ 61,103, at 61,338-39 (1987).

150. *Texas E. Transm'n Corp.*, 43 F.E.R.C. ¶ 61,114, at 61,363 (1988).

151. *El Paso Natural Gas Co.*, 38 F.E.R.C. ¶ 61,008, at 61,034 (1987).

152. *Tennessee Gas Pipeline Co.*, 40 F.E.R.C. ¶ 61,194, at 61,641 (1987).

153. *Northwest Pipeline Corp.*, 42 F.E.R.C. ¶ 61,019, at 61,108-10 (1988).

154. *Tennessee*, 40 F.E.R.C. ¶ 61,194, at 61,641; *Columbia Gulf Transm'n Corp.*, 39 F.E.R.C. ¶ 61,335, at 62,039-40 (1987).

155. *Tennessee*, 40 F.E.R.C. ¶ 61,194, at 61,641; *Columbia Gulf*, 39 F.E.R.C. ¶ 61,335, at 62,039-40.

156. *Columbia Gulf Transm'n Corp.*, 41 F.E.R.C. ¶ 61,281, at 61,731 (1987).

157. *Id.*

158. *Id.*; *Tennessee*, 40 F.E.R.C. ¶ 61,194, at 61,641-42.

159. *E.g.*, *Colorado Interstate Gas Co.*, 39 F.E.R.C. ¶ 61,227, at 61,797 (1987) (provision requiring minimum throughput of 100 Mcfd rejected).

where the gas has been tendered, and identify the receipt points, if any, where the tendered quantities can be measured.¹⁶⁰ The Commission has also required a pipeline to include a list showing the threshold volumes needed for accurate measurements on common types of meters.¹⁶¹ In applying minimum throughput provisions, the pipeline should include all volumes received by the shipper at the receipt point, including sales volumes.¹⁶²

F. Penalties for Imbalances

The Commission has permitted pipelines to assess penalties against a shipper in certain situations where the shipper's deliveries are out of balance with its MDTQ, its nominations, or its deliveries. A pipeline's penalty scheme contains several interrelated elements.

The first element is the period during which the imbalance arises. This may be a day, a month, a season or the term of the contract.¹⁶³

The second element is the type of imbalance. There are two basic types: first, where the shipper delivers a volume of gas higher than its MDTQ or its nominations or less than its nominations; second, where the shipper's deliveries to and subsequent takes from the pipeline are out of balance.¹⁶⁴ Penalties resulting from imbalances between deliveries and MDTQ or nominations are called "scheduling" penalties.¹⁶⁵ Penalties resulting from imbalances between deliveries and takes are sometimes referred to as "balancing" penalties.¹⁶⁶

The foregoing imbalances impede a pipeline's operations in the following ways. Where deliveries exceed MDTQ or nominations or where deliveries and takes are out of balance, the pipeline will have to direct other suppliers to inject more or less gas into the system so that it can maintain throughput; in so doing, the pipeline will have to depart from a "least-cost" strategy of purchasing the least expensive gas available.¹⁶⁷ Where the shipper schedules more gas than it delivers, the pipelines may have to forego providing interruptible transportation and lose business as a result.¹⁶⁸

The third element is the tolerance level, the exceeding of which brings the penalty scheme into play. The Commission has set tolerance levels for daily imbalances at 10% or 50 Dth, whichever is higher;¹⁶⁹ the 50 Dth level is

160. Trailblazer Pipeline Co., 39 F.E.R.C. ¶ 61,103, at 61,335 (1987).

161. *Id.*

162. *Tennessee*, 40 F.E.R.C. ¶ 61,194, at 61,640.

163. *E.g.*, United Gas Pipe Line Co., 39 F.E.R.C. ¶ 61,152, at 61,574-75 (1987) (daily); Natural Gas Pipeline Co., 41 F.E.R.C. ¶ 61,164, at 61,411 (1987) (monthly); Columbia Gulf Transm'n Corp., 41 F.E.R.C. ¶ 61,281, at 61,736 (1987) (seasonal); Northwest Pipeline Corp., 42 F.E.R.C. ¶ 61,019, at 61,110 (1988) (contract term).

164. El Paso Natural Gas Co., 35 F.E.R.C. ¶ 61,440, at 62,066-70 (1986); Northwest Pipeline Corp., 39 F.E.R.C. ¶ 61,109, at 61,402-03 (1987).

165. Natural Gas Pipeline Co., 39 F.E.R.C. ¶ 61,153, at 61,599 (1987); Texas E. Transm'n Corp., 37 F.E.R.C. ¶ 61,260, at 61,690 (1986).

166. Southern Natural Gas Co., 41 F.E.R.C. ¶ 61,218, at 61,586 (1987).

167. Texas Gas Transm'n Corp., 39 F.E.R.C. ¶ 61,111, at 61,414 (1987).

168. *Texas E.*, 37 F.E.R.C. ¶ 61,260, at 61,687; *El Paso*, 35 F.E.R.C. ¶ 61,440, at 62,069-70.

169. *Texas E.*, 37 F.E.R.C. ¶ 61,260, at 61,689; *El Paso*, 35 F.E.R.C. ¶ 61,440 at 62,066-68.

included in all tolerance levels to protect small shippers.¹⁷⁰ The lowest tolerance level the Commission has allowed for imbalances of more than a day is 2%.¹⁷¹

The fourth element is the "notice period," the period, after notice, during which the shipper must take action to stop causing the imbalances or face imposition of penalties. The Commission has permitted a two-day notice period for daily and monthly imbalances. In the case of daily imbalances, the shipper has two days to stop creating imbalances that exceed the tolerance level.¹⁷² The Commission has permitted a pipeline to require shippers to submit, two days after notice, a plan to cure monthly imbalances.¹⁷³

The fifth element is the "make-up period," the period, after notice, during which the shipper must eliminate a past imbalance. The Commission permits a make-up period for all imbalances of at least forty-five days from notice.¹⁷⁴

There are two instances in which the notice discussed in connection with elements four and five need not be required. Where the day's deliveries are less than nominations and the imbalance exceeds the 10%/50 Dth tolerance referred to above, the pipeline may assess penalties without notice.¹⁷⁵ This is because the harm caused by such underdeliveries, lost business, cannot be remedied.¹⁷⁶ Similarly, there is no make-up period for such imbalances.¹⁷⁷ In addition, notice is not required if the shipper controls the metering point and can therefore ascertain whether imbalances have occurred.¹⁷⁸

The sixth element is the penalty itself. Where the shipper's deliveries exceed its MDTQ, nominations or takes, the pipeline may, after appropriate notice, retain the portion of the excess gas which exceeds the established tolerance level, free of cost and adverse claims.¹⁷⁹ Monetary penalties may be imposed in place of retention of the gas, but the sum of the penalties may not exceed the value of the excess gas, which is deemed to have a value no greater than the cost of the transporting pipeline's system supply gas.¹⁸⁰

If the shipper's takes exceed deliveries, the pipeline may, after appropriate notice, collect two times the commodity charge in its firm sales rate schedule for the amount of gas in excess of the tolerance level,¹⁸¹ or substitute its sales gas for the missing transportation gas¹⁸² (i.e., charge its sales rate for the

170. See *Northwest*, 42 F.E.R.C. ¶ 61,109, at 61,110.

171. *Natural*, 41 F.E.R.C. ¶ 61,164, at 61,411; see *Southern Natural*, 41 F.E.R.C. ¶ 61,218, at 61,586.

172. *Northwest Central Pipeline Corp.*, 38 F.E.R.C. ¶ 61,170, at 61,548 (1987).

173. *Tennessee Gas Pipeline Co.*, 40 F.E.R.C. ¶ 61,194, at 61,646 (1987).

174. *Northwest Pipeline Corp.*, 43 F.E.R.C. ¶ 61,342, at 61,961 (1988); compare *Tennessee*, 40 F.E.R.C. ¶ 61,194, at 61,646 (make-up period begins at the time of notice) with *Natural*, 39 F.E.R.C. ¶ 61,153, at 61,597 (make-up period only begins after the two-day notice period during which the shipper must stop creating imbalances).

175. *Natural*, 39 F.E.R.C. ¶ 61,153, at 61,599.

176. *El Paso*, 35 F.E.R.C. ¶ 61,440, at 62,069-70.

177. *Southern Natural*, 41 F.E.R.C. ¶ 61,218, at 61,586 (monthly scheduling penalty).

178. *MIGC, Inc.*, 39 F.E.R.C. ¶ 61,030, at 61,083-84 (1987). In this instance the notice and make-up periods run as if notice has occurred.

179. *United*, 39 F.E.R.C. ¶ 61,152, at 61,576; *Texas E.*, 37 F.E.R.C. ¶ 61,260, at 61,688.

180. *Natural*, 39 F.E.R.C. ¶ 61,153, at 61,598.

181. *South Georgia Natural Gas Co.*, F.E.R.C. ¶ 61,328, at 61,866 (1987).

182. *Natural*, 39 F.E.R.C. at 61,597.

missing gas).

If the shipper's nominations exceed deliveries, the pipeline may, without notice, collect its interruptible transportation rate for the amount of nominated gas exceeding the tolerance level.¹⁸³ The Commission has refused to allow a pipeline to bill on the basis of nominations rather than deliveries.¹⁸⁴

The pipeline may assess both scheduling and balancing penalties at the same time.¹⁸⁵ However, penalties for overdeliveries may not exceed the value of the gas left on the system.¹⁸⁶

The purpose of a penalty provision is to deter practices which will have an adverse effect on the pipeline.¹⁸⁷ The size of the penalty need not be based on the cost of the imbalance to the pipeline because the purpose of the penalty is to deter rather than compensate.¹⁸⁸ Accordingly, the pipeline may impose a penalty even if the imbalance has not caused harm.¹⁸⁹ However, the penalties may not be so onerous that they act as an unwarranted barrier to transportation.¹⁹⁰

Penalties are not supposed to generate revenues for pipelines.¹⁹¹ If penalties do generate such revenues, the appropriate remedy is not to require that the revenues be credited to the pipeline's Account No. 191 but rather to consider this fact in designing its rates in its next rate proceeding.¹⁹²

Pipelines may excuse payment of penalties as long as they do so without undue discrimination.¹⁹³ Payments must be excused if the shipper is unable to deliver or take volumes, after good faith efforts to do so, due to the pipeline's actions or a force majeure event.¹⁹⁴ The availability of penalties does not foreclose a pipeline from taking other action, such as curtailment of transportation, necessary to correct imbalances that threaten the integrity of the system.¹⁹⁵

III. TAKE-OR-PAY CREDITS

Sections 284.8(f) and 284.9(f)¹⁹⁶ require producers to provide an offer of "take-or-pay credits" in order to obtain transportation of their gas. This portion of the report reviews how the Commission has implemented these subsections in its orders.¹⁹⁷

183. *El Paso*, 35 F.E.R.C. ¶ 61,440, at 62,069-70.

184. *Northwest Pipeline Corp.*, 42 F.E.R.C. ¶ 61,019 at 61,110 (1988).

185. *Southern Natural*, 41 F.E.R.C. ¶ 61,218, at 61,586.

186. *Id.*

187. *Northern Natural Gas Co.*, 37 F.E.R.C. ¶ 61,272, at 61,821 (1986).

188. *Id.*

189. *Tennessee Gas Pipeline Co.*, 41 F.E.R.C. ¶ 61,310, at 61,820 (1987).

190. *Northwest*, 39 F.E.R.C. ¶ 61,109, at 61,402.

191. *El Paso*, 35 F.E.R.C. ¶ 61,440, at 62,070.

192. *Id.*

193. *Colorado Interstate Gas Co.*, 42 F.E.R.C. ¶ 61,380, at 62,124 (1988); *El Paso*, 35 F.E.R.C. ¶ 61,440, at 62,070.

194. *United*, 39 F.E.R.C. ¶ 61,152, at 61,575.

195. *El Paso*, 35 F.E.R.C. ¶ 61,440, at 62,067.

196. 18 C.F.R. §§ 284.8(f), 284.9(f) (1988).

197. It is not the intent of this report to discuss the take-or-pay credit mechanisms in detail.

Basically, the sections provide that in order for gas to be eligible for transportation, the producer must submit an offer of credits pursuant to which the pipeline will be allowed to credit, against the pipeline's take-or-pay obligations to the producer, a volume of gas equivalent to the volume of gas being tendered for transportation.¹⁹⁸ Once the offer of credits is made, the pipeline must transport the gas.¹⁹⁹ This requirement applies to system supply gas tendered by pipelines for transportation.²⁰⁰

The foregoing transaction is to be implemented in the following way. The offer of credits must be signed by the producer and persons having 85% of the working interest in the gas and must identify the gas.²⁰¹ The transportation of certain categories of gas will not require producers to provide credits.²⁰² When more than one pipeline is transporting the gas, credits are allocated as follows: if the gas has been released by one of the transporting pipelines, that pipeline gets all of the credits; if the gas has not been released by any of the transporting pipelines, then all of the transporters allocate the credits among themselves.²⁰³ Other persons may guarantee take-or-pay credits if the offer is not made by the working interest owners.²⁰⁴

In practice, it is the shipper who physically submits the offer of credits to the pipeline. The pipeline is not permitted to require the shipper to provide the offer of credits with its transportation request²⁰⁵ but may at that stage require the submission of information, such as the identity of the gas, which will enable the pipeline to determine whether the gas is covered by an offer of credits.²⁰⁶ The pipeline may not at this stage require the shipper to submit information which is not required to be included in the offer of credits itself;²⁰⁷ submit information in the form of an affidavit;²⁰⁸ or warrant the accuracy of the information which the sellers have provided.²⁰⁹ It is the pipeline's responsibility to verify the accuracy of that information.²¹⁰

The offer of credits need not be submitted until the contract is executed.²¹¹ The requirement that the offer be signed by working interest owners having an 85% interest in the gas applies to the entire volume of gas to be transported rather than to each individual well.²¹²

When transportation commences, the shipper must provide each trans-

198. 18 C.F.R. §§ 284.8(f)(1)(ii), (2), 284.9(f)(1)(ii), (f)(2) (1988). The pipeline is permitted to waive its right to an offer of credits. 18 C.F.R. §§ 284.8(f)(1), 284.9(f)(1).

199. 18 C.F.R. §§ 284.8(f)(3), 284.9(f)(3).

200. Northern Natural Gas Co., 43 F.E.R.C. ¶ 61,519, at 62,288-89 (1988).

201. 18 C.F.R. §§ 284.8(f)(1)(ii), 284.9(f)(1)(ii).

202. 18 C.F.R. §§ 284.8(f)(4)(ii), (f)(8)-(10), 284.9(f)(4)(ii), (f)(8)-(10).

203. *Id.* §§ 284.8(f)(5), 284.9(f)(5).

204. *Id.* §§ 284.8(f)(11), 284.9(f)(11).

205. Transcontinental Gas Pipe Line Corp., 41 F.E.R.C. ¶ 61,374, at 62,027 (1987).

206. Natural Gas Pipeline Co., 42 F.E.R.C. ¶ 61,367, at 62,074, *reh'g denied*, 43 F.E.R.C. 61,311 (1988).

207. *See Transcontinental*, 41 F.E.R.C. ¶ 61,374, at 62,027.

208. *Natural*, 42 F.E.R.C. ¶ 61,367, at 62,074.

209. *Id.*

210. *See Natural Gas Pipeline Co.*, 43 F.E.R.C. ¶ 61,311 (1988).

211. *Transcontinental*, 41 F.E.R.C. ¶ 61,374, at 62,027.

212. South Georgia Natural Gas Co., 41 F.E.R.C. ¶ 61,328, at 61,867 (1987).

porting pipeline information regarding the other transporting pipelines that will permit the pipelines to allocate the take-or-pay credits.²¹³ If the gas to be transported has been released by transporting pipeline A, that pipeline receives all of the credits and therefore does not need to know the identities of the other transporting pipelines. If the gas has been released by transporting pipeline B, then that pipeline receives all of the credits, and pipeline A then needs to know that pipeline B has released the gas and is a transporter. If the gas has not been released by any of the transporting pipelines, then all of those pipelines are entitled to share in the credits and each must know the identity of the others.²¹⁴

John W. Ebert, *Chairman**
Robert C. Platt, *Vice Chairman*

John S. Anderson	Sheila S. Hollis
John G. Banner	Marsha L. Hunter
Lee M. Beckett	Robert K. Johnson
Frederic G. Berner, Jr.	Philip M. Knighton
Randolph C. Bruton, Jr.	Edward J. LeDuc
David H. Coffman	Nicholas W. Mattia, Jr.
Stuart W. Conrad	J. Curtis Moffatt
Jeffrey G. DiSciullo	David J. Muchow
Steve H. Finch	Larry Pain
Steven F. Greenwald	Marc Richter
Andrea R. Hilliard	

213. Southern Natural Gas Co., 43 F.E.R.C. ¶ 61,299, at 61,816 (1988). The Commission had previously taken the position that 18 C.F.R. § 284.106 required pipelines to disclose all upstream and downstream transporters upon commencement of transportation; therefore, the shippers needed to disclose the names of these transporters in order to permit the pipeline to make the disclosures required under the regulations. However, upon re-examination, the Commission determined that the only disclosure required under section 284.106 is the names of the parties to the transportation contract.

214. *Southern Natural*, 43 F.E.R.C. ¶ 61,299, at 61,816-17.

* The Chairman acknowledges that this supplemental report was prepared entirely by David H. Coffman, deputy assistant general counsel for enforcement, Federal Energy Regulatory Commission. The interpretation of the cases contained herein are Mr. Coffman's own and not necessarily those of the Commission.

