



Open Access To Natural Gas Transportation

Session 2

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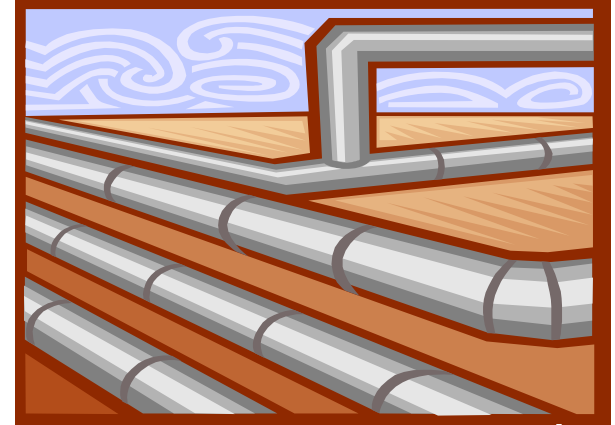
*Participants: NARUC, USAID, DC Public Service Commission,
Public Utility Commission of Ohio, West African Gas Pipeline Authority (WAGPA)*

Physical Flow of Natural Gas before Deregulation

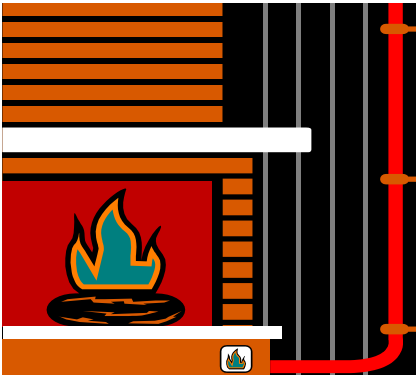
[Producers]



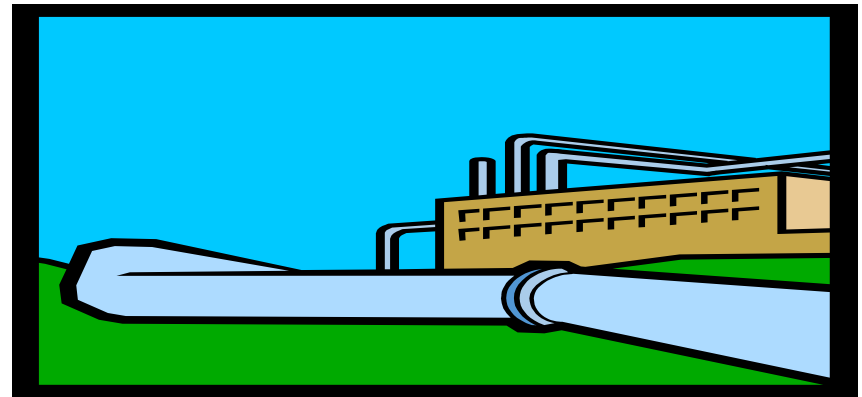
[4 Pipelines]



[Homes & Businesses]



[Washington Gas]



Four (4) Pipelines Supply District Consumers with Natural Gas

- Columbia Transmission and Gulf
- Dominion Transmission
- Williams Transco Pipeline
- Dominion Cove Point Pipeline

History of Pipeline Regulations in U.S.

- Between 1911 and 1928, several states attempted to assert regulatory oversight of these interstate pipelines
- In 1935, the Federal Trade Commission issued a report outlining its concern over the market power that may be exerted by merged electric and gas utilities.
- 1935 Congress passed the Public Utility Holding Company Act to limit the ability of holding companies to gain undue influence over a public utility market.
- In 1938, the federal government became involved directly in the regulation of interstate natural gas with the passage of the Natural Gas Act (NGA).
- In 1954, however, this all changed with the Supreme Court's decision in *Phillips Petroleum Co. v. Wisconsin* (347 U.S. 672 (1954)). In this decision, the Supreme Court ruled that natural gas producers that sold natural gas into interstate pipelines fell under the classification of 'natural gas companies' in the NGA, and were subject to regulatory oversight by the FPC. (**The Phillips Decision - Wellhead Price Regulation**)

FERC Order No. 436 changed how interstate pipelines were regulated

- **FERC Order No. 436:** In 1985, FERC issued Order No. 436, which changed how interstate pipelines were regulated. This order established a voluntary framework under which interstate pipelines could act solely as transporters of natural gas, rather than filling the role of a natural gas merchant. The interstate pipelines were barred from discriminating against transportation requests based on protecting their own merchant services

Effects of FERC Order No. 436

FERC Order No. 436 had a number of immediate effects, including:

- Pipelines began offering transportation service to all customers
 - Pipeline customers realized cost savings, in that the spot market prices of natural gas were much lower than the prices offered for natural gas by the pipelines (due to the long term 'take-or-pay' contracts that the pipelines were bound under)
 - The payments necessary under these 'take-or-pay' contracts increased for pipelines, as few customers were willing to purchase higher priced gas from the pipelines
 - Pipelines and producers were often forced into litigation to resolve issues surrounding 'take-or-pay' contracts
- FERC Order No. 436 also had a number of longer term effects, including:
 - The transportation function became the primary function of pipelines, as opposed to offering the bundled merchant service
 - A wide variety of natural gas purchasing and transportation patterns and practices emerged due to the availability of choices to the end user
 - New pricing patterns emerged, known as 'netback' pricing, in which a reasonable price was set at the point of consumption, and that minus the cost of distribution, minus the cost of transportation, gave the 'netback' price to the producer at the wellhead

The Natural Gas Wellhead Decontrol Act of 1989

- As mentioned, under the NGPA, the deregulation of natural gas producers sale prices at the wellhead had begun. However, it wasn't until Congress passed the Natural Gas Wellhead Decontrol Act (NGWDA) in 1989 that complete deregulation of wellhead prices was carried forth. Under the NGWDA, the NGPA was amended and all remaining regulated prices on wellhead sales were repealed. As of January 1, 1993, all remaining NGPA price regulations were to be eliminated, allowing the market to completely determine the price of natural gas at the wellhead.
- The NGWDA stated that 'first sales' of natural gas were to be free of any federal price regulations. The Act defined 'first sales' as the sale of gas:
 - To a pipeline
 - To a local distribution company
 - To an end user
 - Preceding the sale to any of the above
 - Determined by FERC to be a first sale
- Excluded from falling under the definition of a first sale were any sales of gas by pipelines and local distribution companies, including interstate pipelines.

FERC Order No. 636

OPEN ACCESS TO TRANSPORTATION

- Order 636 is often referred to as the Final Restructuring Rule:
- FERC Order 636 involves the restructuring of interstate pipeline services. The main objectives of this order include:
- Requiring interstate pipelines to 'unbundle' their service, essentially separating the sale of natural gas from the transportation. Under FERC Order 436, pipeline unbundling was voluntary; Order 636 made it mandatory
- Allows FERC to issue blanket certificates which allow pipelines to offer unbundled services for firm or interruptible service at market-based rates
- Allows for abandonment options for interruptible and short term firm transportation, and in certain instances longer term firm transportation services
- Sets a generic capacity brokering program for pipelines to release excess capacity (which includes setting rate ceilings for the sale of released capacity)

Open Access and Wholesale Competition

[Producers]



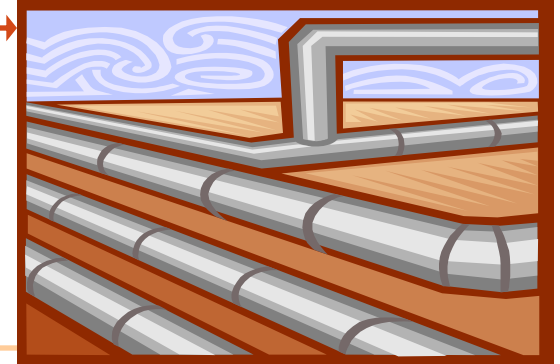
(Well Head Prices)

[Commodity]

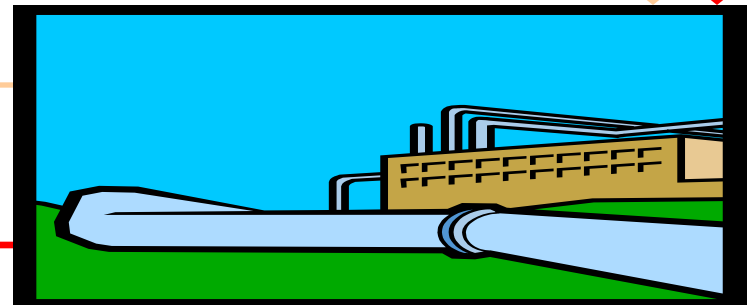
[Wholesale Market]



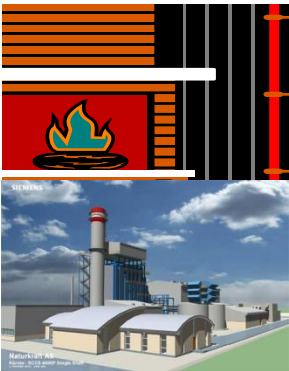
[Pipeline Companies]



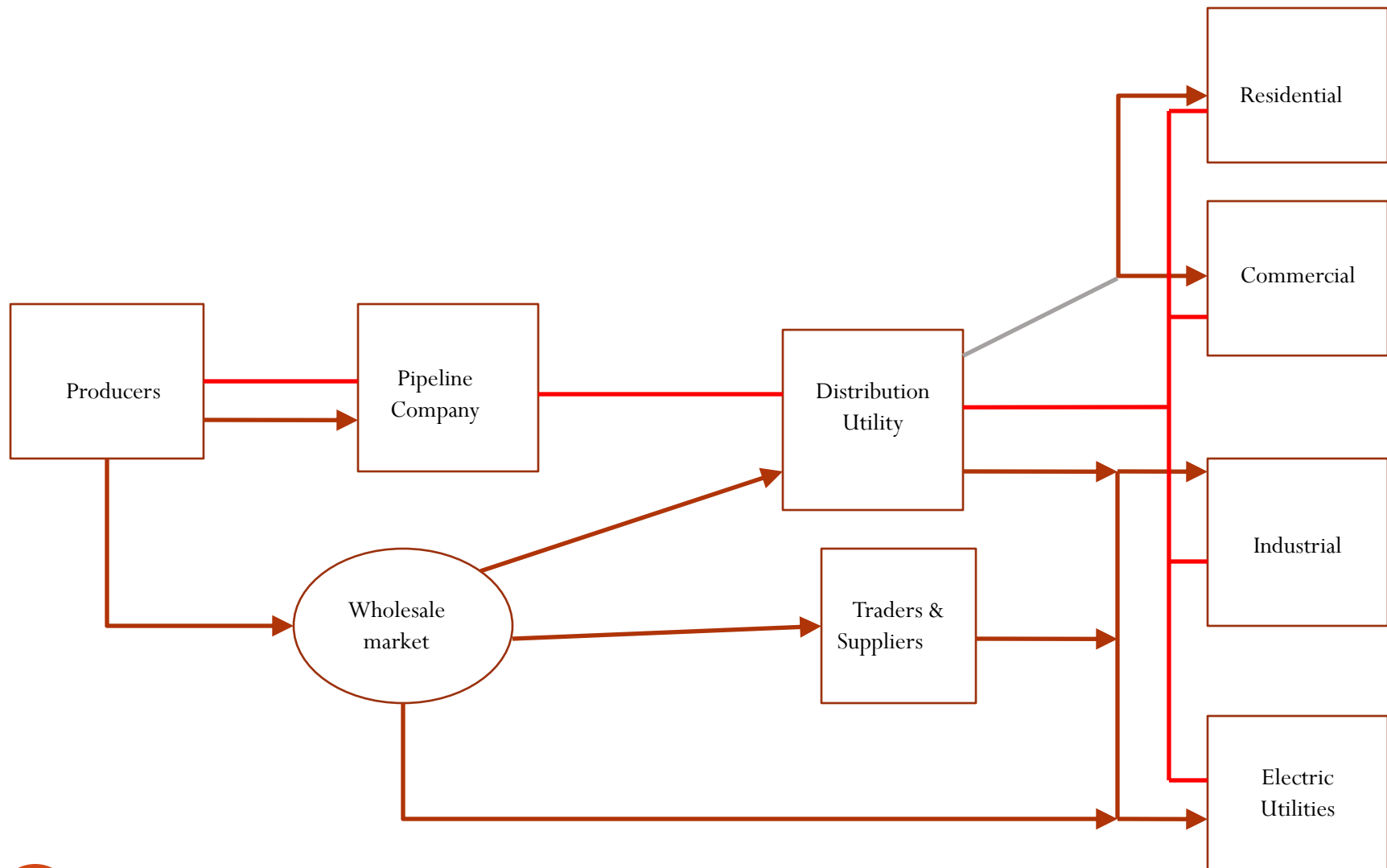
[Distribution Companies]



End users (homes/businesses)



Open Access and Wholesale Competition



What Does Ensuring Open Access Mean?

- ❑ Open Access purpose is to allocate available interstate pipeline capacity to shippers up to a maximum rate.
- ❑ Pipelines conduct open season to alert shippers to the availability of capacity on pipelines and allows shippers to bid for available capacity.
- ❑ Open season process is open and transparent and is set out in pipelines' tariff.
- ❑ Pipeline notifies shippers of available capacity by posting notice on its Electric Bulletin Board (EBB) and/or website for available capacity.
- ❑ During open season, FERC requires pipeline to sell all available capacity to shippers willing to pay pipeline's maximum rate.
- ❑ Pipeline evaluates bids using primarily one of two methods "NPV" – net present value.

or

What Does Ensuring Open Access Mean? (Cont'd)

- ❑ “First come – first serve” where the first shipper to submit qualifying bid receives capacity.
 - ❑ If not sufficient capacity to meet all equal maximum bids the capacity is shared by pro rate allocation.
- or
- ❑ Allocated to the earliest applicant who submitted maximum bid.
 - ❑ All shipping bidders have equal opportunity to secure capacity.

Ensuring Open Access

Case Study – Apache, Enogex, Midcontinent Open Access Quarrel for Pipeline Capacity

- ❑ Apache is a natural gas producer.
- ❑ Enogex is an intrastate gas pipeline.
- ❑ Midcontinent is an interstate gas pipeline.
- ❑ In 2006, Midcontinent and Enogex agreed to a lease for capacity to allow Midcontinent (larger entity) to transport natural gas over Enogex (smaller entity) intrastate pipeline to get to Midcontinent's interstate pipeline.
- ❑ Lease had to be approved by FERC.
- ❑ Apache, customer of Enogex's pipeline, objected claiming it was discriminatory and would harm Apache and other Enogex customers because lease equivalent to firm transportation service that Enogex did not offer to Apache.
- ❑ Apache's contract with Enogex for interruptible service.

Ensuring Open Access

Case Study – Apache, Enogex, Midcontinent Open Access Quarrel for Pipeline Capacity (Cont'd)

- ❑ Midcontinent's contract with Enogex was for capacity.
- ❑ Interruptible service ensures transportation on a “when available basis”.
- ❑ Enogex offers transportation on interruptible basis.
- ❑ Midcontinent lease allows it to use Enogex's capacity to provide firm and interruptible service over its pipeline.
- ❑ Firm Service ensures transportation on an “obligated” basis for specific volumes of gas.
- ❑ Firm service customers have higher priority for transportation over pipeline interruptible service customers.
- ❑ FERC approval of lease was upheld by Federal courts because interruptible service has less priority.

THE END
THANK YOU!