UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeen G. Kelly.

High Island Offshore System, L.L.C. Docket No. RP04-47-000

ORDER ACCEPTING AND SUSPENDING TARIFF SHEETS SUBJECT TO REFUND AND ESTABLISHING A TECHNICAL CONFERENCE

(Issued December 24, 2003)

1. On November 3, 2003, High Island Offshore System, L.L.C. (HIOS) filed the tariff sheets listed in the appendix, to be effective January 1, 2004, to establish and implement a Natural Gas Liquids Bank (NGL Bank) as part of its tariff. The Commission accepts and suspends the tariff sheets, to become effective June 1, 2004, or on an earlier date specified by subsequent Commission order, subject to refund and the outcome of the technical conference established herein. This order benefits the public by allowing the Commission to investigate issues raised by parties concerning the just and reasonableness of the proposed NGL Bank.

Description of the Filing

2. HIOS states the purpose of the bank is to mitigate inequities in gas processing economics that may occur on HIOS as a result of its commingling of gas streams that contain different liquefiable hydrocarbon compositions, and to provide a new service to meet the needs of producers developing gas supply sources rich in liquefiable hydrocarbons.[1] HIOS proposes to make participation in the NGL Bank mandatory for all shippers using its system.

3. In support of its proposal, HIOS states it currently receives natural gas of varying composition from its shippers at the various receipt points along its system. HIOS states that the economics related to processing of that gas are directly related to the content of

[1] HIOS states that the NGLs referenced are the hydrocarbons that remain in the vapor phase in the pipeline, not the condensate in the liquid phase that may either condense in or be injected into the pipeline. NGLs remain in the gas until extracted at a processing facility.

liquefiable hydrocarbons, or NGLs, in the gas stream, generally expressed in gallons per Mcf, or GPM. HIOS asserts that current gas sources on its system range in gas quality from 0.07 GPM and 1014 Btu/cf to 2.5 GPM and 1130 Btu/cf.

4. HIOS states it receives gas on its three supply legs and the gas is commingled in its forty-two inch mainline and subsequently redelivered as a commingled stream to three downstream pipelines: ANR Pipeline Company (ANR), Tennessee Gas Pipeline Company (Tennessee) and Enbridge Offshore Pipelines (UTOS) L.L.C. (UTOS). HIOS states the quality of its commingled stream typically is analyzed at approximately 1.3 GPM and 1070 Btu/cf. HIOS, which is located entirely offshore, states that there are no processing facilities on its system, and the gas is processed at plants located on downstream pipelines. These plants generally process the average composition of the commingled HIOS stream for each shipper's account, rather than what each shipper injected into the commingled stream. HIOS contends that because the gas is commingled in its facilities, absent a mechanism such as the NGL Bank, when the processing results in crediting shippers, those shippers that deliver gas with relatively low NGL content into HIOS' system are being economically advantaged at the expense of those shipping gas with relatively high NGL content because they receive the same credit as the shippers of the high NGL content gas which is the source of the credit.

5. HIOS contends the NGL Bank will also benefit shippers of drier, lower quality gas. HIOS asserts that during periods when processing margins are negative, downstream pipelines may require the gas to be processed. HIOS notes the processing plants may charge a fee based on conditioning the richer, commingled stream, resulting in an economic disadvantage to shippers of drier gas. HIOS states that under its proposal, in such a situation, shippers of the drier gas would receive a payment from the NGL Bank to offset a portion of the higher charge.

6. Article V of the proposed NGL Bank Agreement describes the procedure for calculating the differing value of each shipper's gas that it injects into the system. Those calculations are intended to approximate the difference between the monthly theoretical gross processing margin for each shipper's gas stream and the processing margin for the HIOS commingled gas stream, and such difference in the monthly theoretical gross processing margin may be either positive or negative. Thus some shippers would receive a credit, while other shippers would be charged. However, the net result between all shippers would be zero, except for the administrative fee.

7. HIOS proposes that a third party be the administrator of the NGL Bank. The administrator would be responsible for the administration and detailed calculations of the NGL Bank adjustments to the calculations and fees, and the distribution of funds to the shippers. The administrator of the NGL Bank would credit or bill all shippers for the

difference in quantities and types of natural gas liquids that are put into the gas stream of the HIOS pipeline by such shippers and then taken out at delivery points by gas processing plants downstream of HIOS. The administrator would charge an administrative fee, which would be billed to all shippers. The administrator would also establish an advisory group to provide a forum to discuss material issues related to the NGL Bank. Initially, the NGL Advisory Group would consist of the top seven shippers, or their respective agents, of the largest volume of gas during the previous six months ending November 30, 2003. Beginning January 1, 2005, and annually thereafter, the administrator would re-determine the advisory group by selecting the top seven shippers for the previous six months ending November 30. The advisory group would meet at least once a year and would review the prices, rates and factors used to perform the settlement calculations under the NGL Bank Agreement, adjusting these items as necessary.

8. HIOS submits that requiring all HIOS shippers to participate in the NGL Bank will mitigate this inequity between producers of high and low NGL content. HIOS portrays the NGL Bank as a service to deepwater gas sources. HIOS contends that deepwater gas generally contains higher volumes of richer quality gas. HIOS states that several shippers have requested that HIOS implement a mechanism that would equitably allocate NGLs to gas sources on the HIOS system.

9. HIOS' tariff filing includes a pro forma NGL Bank Agreement (agreement), which would be entered into by the shipper, HIOS and a third party, Southern Petroleum Laboratory, Inc. (SPL), who will serve as the administrator of the bank. HIOS further proposes to amend its tariff to authorize HIOS to suspend service to a shipper that does not execute an NGL Bank Agreement, consistent with HIOS' proposal to make participation in the NGL Bank mandatory. HIOS submits that its proposal and the accompanying agreement are similar to that previously approved by the Commission for Garden Banks Gas Pipeline, LLC (Garden Banks).[2]

Notice, Interventions and Protests

10. Public notice of this filing was issued on November 5, 2003, with comments, protests or interventions due on or before November 17, 2003, as provided in Section 154.210 of the Commission's regulations. Pursuant to Rule 214 (18 C.F.R. § 385.214), all timely motions to intervene are granted and any motions to intervene out of time filed as of the date of this order are also granted. Granting late interventions at this stage of the proceedings will not disrupt the proceedings or place additional burdens on existing parties.

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[2] See 78 FERC ¶ 61,066 (1997), and 89 FERC ¶ 61,145 (1999).

11. ExxonMobil Gas & Power Marketing Company, A Division of Exxon Mobile Corporation (ExxonMobil) and the Indicated Shippers[3] filed protests. HIOS filed a motion for leave to answer, together with the answer. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure provides that answers to protests are generally not allowed "unless otherwise ordered by the decisional authority." 18 C.F.R. § 325.213(a)(2). We are not persuaded to accept HIOS' answer and will, therefore, reject it.

12. Protestors generally contend that HIOS' proposal could adversely affect HIOS shippers. Although they do not oppose the concept of the NGL Bank, the parties argue the proposal raises many complex issues regarding how the bank would work and whether changes to the agreement are needed. Further, they seek specific modifications and clarifications to the proposal. In addition, as demonstrated below, ExxonMobil requests that the Commission direct that a technical conference be convened to address all the issues raised by the filing. It notes such a conference could prove highly beneficial in developing a proposal that would truly accomplish HIOS' stated objectives. Further, ExxonMobil requests that the Commission suspend the effectiveness of the filing until the earlier of the expiration of a full five-month statutory period or issuance of a Commission order following the technical conference addressing the issues raised by the filing.

Discussion

13. In their protests, the parties raise many concerns and discuss a number of shortcomings with the proposal. They note that HIOS is proposing to require producers to participate in an NGL Bank, which is administered by a non-regulated entity, who then collects an unregulated administrative fee. They note that under the proposal the administrative fees may be adjusted April 1 of each year, but there appears to be no requirement for HIOS to make a tariff filing whenever this fee is adjusted. They argue that any attempt by HIOS to use its regulated tariff to force shippers to pay a non-regulated entity a monthly fee that can be adjusted without regulatory oversight is improper. They propose that a better method would be to make the NGL Bank, without mention of an administrator, a part of HIOS' tariff, and then let HIOS decide whether to contract this service out. Any fee adjustment thus would be subject to HIOS making a tariff filing that would be subject to shipper and Commission review.

14. The protestors have concerns with the settlement calculations under the required processing periods in the agreement. For example, they state the agreement is unclear

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[3] The Indicated Shippers is comprised of BP America Production Company, BP Energy Company and ChevronTexaco Natural Gas, a division of Chevron U.S.A. Inc.

whether the NGL Bank administrator would conduct NGL settlements every month or only when processing economics are negative. ExxonMobil asserts that the Commission should direct HIOS to modify or clarify the agreement to provide that the Administrator will operate the bank continuously and make settlements every month, regardless of whether downstream pipelines are imposing processing requirements.

15. The protestors also have concerns with the data requirements in the agreement. They note the agreement empowers the NGL Bank administrator in some instances to estimate the approximate volume, heat content and NGL component data for gas receipts if the administrator has not received data in a timely manner. However, ExxonMobil states if such estimates depart substantially from the actual data, these estimates will impact the settlements for every shipper. ExxonMobil submits that the agreement should require the NGL Bank administrator to indicate any data that has been estimated and how those data factored into the calculation of the NGL Bank's settlements. Further, it states the NGL Bank administrator should also correct for discrepancies if the actual data differs from the estimate, through an adjustment in a subsequent month.

16. The protestors also have concerns with the billing and payment provision of the agreement. They note this provision appears to require shippers to waive challenges to the NGL Bank administrator's calculations. ExxonMobil asserts the agreement should be revised to permit a shipper to challenge the NGL Bank administrator's calculations.

17. The protestors also argue the Commission should reject HIOS' attempt to avoid liability for the NGL Bank except for cases of gross negligence or willful misconduct. They assert HIOS should be liable for negligence, bad faith, fraud or willful misconduct. They note that HIOS' transportation agreements provide for a negligence standard, not a gross negligence standard, and assert that the same standard should apply to the NGL Bank administrator and HIOS under the NGL Bank. Finally, the protestors have concerns with some of the time limitations included in the audits provision of the agreement that may limit the scope of the audit right, without apparent justification.

Commission Determination

18. HIOS' filing raises substantive concerns regarding its proposal to implement an NGL Bank on its system and presents questions that warrant further review and consideration. The parties have argued that there are numerous specific aspects of the filing that should render the proposal unacceptable in its present form or that should make it subject to modification and clarification, and have requested that the Commission establish a technical conference.

19. The Commission finds it would be beneficial for the parties in this proceeding to be able to address their concerns directly to HIOS and for HIOS to have the opportunity to explain and justify its proposal for the NGL Bank. Therefore, the Commission will establish a technical conference to gather additional information and to provide parties with a forum to discuss relevant issues and concerns raised by the filing.[4]. HIOS should be prepared to address all issues raised by the protests and any concerns others may have with the proposal. In addition, the Commission will accept the tariff sheets listed in the appendix for filing and suspend their effectiveness until the earlier of five months or the date established in a further Commission order following the technical conference.

Suspension

20. Based upon a review of the filing, the Commission finds that the tariff sheets have not been shown to be just and reasonable, and may be unjust, unreasonable, unduly discriminatory, or otherwise unlawful. Accordingly, the Commission will accept the subject tariff sheets for filing, and suspend their effectiveness for the period set forth below, and permit them to become effective, subject to the conditions in this order.

21. The Commission's policy regarding tariff suspensions is that tariff filings generally should be suspended for the maximum period permitted by statute where preliminary study leads the Commission to believe that the filing may be unjust, unreasonable, or that it may be inconsistent with other statutory standards.[5] It is recognized, however, that shorter suspensions may be warranted in circumstances where suspension for the maximum period may lead to harsh and inequitable results.[6] Such circumstances do not exist here. Therefore, the Commission shall exercise its discretion to suspend the rates and permit them to become effective the earlier of June 1, 2004, or on the date specified by subsequent Commission order, subject to the conditions set forth in the body of this order and in the ordering paragraphs below.

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[4] HIOS' reliance on Garden Banks is misplaced since there the Commission accepted an uncontested proposal without any discussion of the type of issues that are raised by protestors in this proceeding.

[5] See Great Lakes Gas Transmission Co., 12 FERC ¶ 61,293 (1980) (five-month suspension).

[6] See Valley Gas Transmission, Inc., 12 FERC ¶ 61,197 (1980) (one-day suspension).

The Commission orders:

(A) HIOS' tariff sheets listed in the appendix are accepted and suspended, to be effective the earlier of June 1, 2004, or on the date the Commission specifies in any future order issued in this proceeding, subject to refund and the outcome of the technical conference.

(B) The Commission staff is directed to convene a technical conference to further explore HIOS' proposal to implement an NGL Bank on its system. Staff must report to the Commission on the technical conference within 120 days of the issuance date of this order.

By the Commission.

(S E A L)

Linda Mitry,
Acting Secretary.

Appendix

High Island Offshore System, L.L.C.
Docket No. RP04-47-000

<u>Revised Tariff Sheets to FERC Gas Tariff, Third Revised Volume No. 1</u>:

Seventh Revised Sheet No. 2
First Revised Sheet No. 14
Second Revised Sheet No. 26
Second Revised Sheet No. 53
Second Revised Sheet No. 64
Original Sheet No. 222
Original Sheet No. 223
Original Sheet No. 224
Original Sheet No. 225
Original Sheet No. 226
Original Sheet No. 227
Original Sheet No. 228
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