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110 FERC ¶ 61,198
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Southern Natural Gas Company — Docket Nos. RP04-523-000, RP04-523-001

ORDER ON TECHNICAL CONFERENCE AND REHEARING

(Issued February 28, 2005)

1. On December 9, 2004, the parties to this proceeding participated in a technical conference established by the Commission in its September 30, 2004 Order Accepting and Suspending Tariff Sheets, Subject to Refund and Conditions, and Establishing Technical Conference and Hearing Procedures (September 30, 2004 Order).[1]

2. The technical conference addressed the following issues raised by Southern Natural Gas Company's (Southern) August 31, 2004 filing pursuant to section 4(e) of the Natural Gas Act (NGA): (1) Southern's proposal to extend the notice period in section 39 of the General Terms and Conditions (GT&C) of its tariff from 90 days to 24 months for transportation demand reductions pursuant to an order of a state regulatory commission, (2) Southern's proposal to revise section 2.1(e) of the GT&C to provide that primary receipt points may be added to or deleted from Exhibit A to a service agreement only if they are in the same zones for which the shipper has contracted for firm service, and to allow shippers to add or delete primary delivery points from Exhibit B to a service agreement only if the additional delivery points are in the same zone as the shipper's current delivery points, (3) Southern's proposal to change its cashout price calculation to apply the high/low index to the zero-to-two-percent tolerance level, and (4) Southern's *pro forma* proposal to revise section 14.2 of the GT&C to apply the Storage Cost Reconciliation Mechanism (SCRM) to supply poolers.

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[1] *Southern Natural Gas Co.*, 108 FERC ¶ 61,328 (2004).

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3. The Alabama Municipal Distributors Group, Austell Gas System, Southeast Alabama Gas District, Municipal Gas Authority of Georgia, and Alabama Gas Corporation (jointly Southern LDCs) filed a limited request for rehearing of the September 30, 2004 Order. Southern LDCs seek rehearing of the Commission's decision not to accept unconditionally the revisions proposed by Southern to its cashout pricing formula applicable to the zero-to-two percent monthly imbalance level for majority shippers.

4. Duke Energy Trading and Marketing, L.L.C. and Duke Energy Marketing America, L.L.C (Duke) filed a request for clarification of the September 30, 2004 Order. Duke states that the Commission set for the technical conference the "fifth week" and "high/low" proposals and directed the parties to explore the propriety of applying the high/low pricing to the zero-to-two percent imbalance band. However, Duke contends that the Commission did not explicitly mention Southern's refund obligation should the Commission ultimately find that Southern must provide a true, "no-penalty" imbalance tolerance band. Duke asks the Commission to clarify that Southern is obligated to provide full refunds with interest to the extent that the Commission ultimately rejects or modifies the index pricing mechanism applicable to shipper imbalances.

5. As discussed below, the Commission (1) with the exception of Third Revised Sheet No. 3, removes the conditions applicable to the revised tariff sheets set for the technical conference and permits them to become effective October 1, 2004, and March 1, 2005, as reflected in the Appendix to this order without condition, (2) refers Third Revised Sheet No. 103, which includes the proposal regarding the addition or deletion of primary receipt points, to the hearing already established in this proceeding, (3) directs Southern to file as actual tariff sheets *pro forma* Sheet Nos. 144A and 240, (4) denies as moot the request for rehearing filed by Southern LDCs, and (5) denies as moot the clarification requested by Duke. This order benefits customers by ensuring that Southern's tariff proposals are just and reasonable and not unduly discriminatory.

I. **Background**

6. On August 31, 2004, Southern filed an NGA general section 4 rate case proposing an increase in its jurisdictional rates of approximately 10 percent or $35 million annually to be effective October 1, 2004. Southern also proposed changes to the rate schedules and GT&C of its tariff. Additionally, Southern filed *pro forma* tariff sheets to be effective prospectively from the date of a

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Commission order approving the changes. The background and a description of Southern's section 4 filing is set forth in detail in the September 30, 2004 Order and will not be repeated here.[2]

7. In the September 30, 2004 Order, the Commission accepted and suspended certain of the revised tariff sheets for the maximum five months statutory period to be effective on March 1, 2005, subject to refund and subject to the outcome of a hearing or pending the outcome of the technical conference and further Commission orders. The Commission also made disposition of the *pro forma* tariff sheets subject to the outcome of the technical conference and further Commission orders. Finally, the Commission accepted certain tariff sheets to become effective on October 1, 2004, subject to conditions.

II. Discussion

A. Notice Period for CD Reductions Pursuant to State Commission Orders (PSC-out Provision)

1. Background

8. Section 39 of Southern's GT&C provides that a local distribution company (LDC) or Hinshaw pipeline may reduce its firm transportation quantities on Southern's system as a result of a final order from a state regulatory commission requiring the shipper to make such a reduction. The currently effective section 39 provides that the reduction will become effective 90 days after the date of written notice to Southern. Southern seeks to change the effective date of any such reduction to 24 months, arguing that the existing notice period does not allow it enough time to respond to the action in order to mitigate the effects of the turned-back capacity. Southern asserts that it and the other customers on the system should not have to bear the risk of the early turnback, and by changing the effective date to 24 months, Southern will have time to hold an open season, which could allow it to either remarket the capacity or use it in conjunction with a system expansion.

2. Southern's Comments

9. Southern emphasizes that it is not required to maintain in its tariff the section at issue. However, Southern contends that its proposed change provides an efficient balance of the rights of the parties regulated by state commissions to

[2] *Id*. at P 3-18.

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reduce their transportation demand, Southern's need to remarket the capacity, and the interests of other customers on Southern's system who may be required to absorb the revenue loss from the reductions if the capacity cannot be remarketed.

10. Southern reiterates that 90 days does not allow it enough time to remarket the capacity. While a shipper could attempt to mitigate its losses during this period, Southern contends that, if the capacity cannot be remarketed, the only alternative would be for Southern to expand its facilities to a new market, which could require 24 months or longer. Southern cites *Florida Gas Transmission Company* (*Florida Gas*),[3] contending that the Commission there accepted a three-year notice period for exercising a reduction based on state commission action.

11. Southern states that the current provision applies only to an LDC or a Hinshaw pipeline subject to the jurisdiction of a state commission, and it does not propose to extend the applicability of the provision to other types of customers. Moreover, contends Southern, no party has met the burden of proof required by NGA section 5 to force Southern to make that change. In fact, continues Southern, the Commission has found that it is not unduly discriminatory to offer transportation reduction rights only to shippers that are subject to state commission regulation and that these shippers are not similarly situated with shippers that are not regulated by state commissions.[4] Southern distinguishes municipal shippers from state-regulated utilities, contending that the former are operated in a manner more analogous to a business that acts in its own interests, while the latter are supervised by a state commission with no direct economic interest in the business decisions of the regulated entities.

12. Southern emphasizes that section 39 was intended to address regulatory risk, not to assist customers in mitigating market risks. Southern also points to the requirement that a shipper seeking to exercise this right must have opposed the reduction at the state commission and also must give Southern adequate notice to permit Southern to participate in the state proceeding. In Southern's view, the involvement of a neutral third-party regulatory body and the likelihood of a hearing distinguish these reductions from those made by other shippers and arising out of the ordinary business decision-making process.

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[3] 101 FERC ¶ 61,401 (2002).

[4] Southern cites *Columbia Gulf Transmission Co.*, 105 FERC ¶ 61,351 at P 11, 13-14 (2003) (*Columbia Gulf).*

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3. **Comments of Intervenors**

13. The parties opposing Southern's proposal generally contend that section 39 is anti-competitive and discriminatory and that this relief should be available to all of Southern's customers. Some intervenors also express concern that the proposed revision may inappropriately shift costs to other customers. Further, certain intervenors maintain that the proposed increase in the notice period is excessive and unsupported.

14. A threshold issue is whether the Commission set the alleged discrimination issue for the technical conference. Municipals[5] contend that a reasonable interpretation of the September 30, 2004 Order is that the Commission did not intend to limit the discussion solely to the notice period. Given the procedural posture of the case, Municipals argue that it makes sense to resolve this issue at this stage rather than deferring it to the hearing. However, Dalton Utilities (Dalton) argues that the Commission should defer a decision on the PSC-out Provision until a full record is developed in the public evidentiary hearing.

15. Dalton and Calpine Corporation (Calpine) review the history of the current provision in Southern's tariff, which they emphasize has never been used by any of Southern's shippers. They point out that the provision arose as part of a 1995 settlement and that the Commission found at that time that the provision was essentially a negotiated contract termination clause that was consistent with the Commission's policy of allowing pipelines and their open-access transportation customers maximum flexibility to structure their own contractual transportation agreements.[6] According to Dalton, the Commission also found in that proceeding that the provision allowing only LDCs regulated by state commissions to reduce their transportation demands was not unduly discriminatory because of a risk undertaken by such LDCs that state commissions would deny passthrough of costs incurred as a result of increased contract demands.[7]

16. Dalton also contends that the real issue here is whether the provision has become so unduly discriminatory that it should be eliminated because the basis on which the Commission originally accepted it no longer exists, *i.e.*, commitments

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[5] Municipals include The Alabama Municipal Distributors Group, The Austell Gas System, The Southeast Alabama Gas District, and The Municipal Gas Authority of Georgia.

[6] Dalton and Calpine cite *Southern Natural Gas Co*., 72 FERC ¶ 62,347 (1995).

[7] Dalton and Calpine cite *Southern Natural Gas Co*., 75 FERC ¶ 61,046 (1996).

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by three major LDCs to increase their demand determinants and to extend their existing contract terms during the period the PSC-out Provision would be in effect. According to Dalton, the Commission found that the result was "to the benefit of all of Southern's customers."

17. Municipals and other intervenors claim that the provision must be revised to include municipal LDCs, or in the alternative, the right must be eliminated for all customers. Municipals cite *ANR Pipeline Co. (ANR)*,[8] claiming that the Commission held there that transportation reduction rights must be established in a pipeline's tariff on a non-discriminatory basis. Southern Cities contend that other pipelines voluntarily offering transportation reduction rights have restructured their tariffs to eliminate the discrimination in favor of state-regulated LDCs.[9]

18. Municipals assert that Southern has failed to demonstrate that they are not similarly situated and thus not entitled to this right. For example, state Municipals, Southern claimed that the issue already had been resolved by Commission precedent, particularly in *Columbia Gulf*, [10] but that Southern acknowledged at the technical conference that *Columbia Gulf* did not resolve the issue of whether investor-owned and municipal LDCs were similarly situated and should be provided the same transportation reduction rights.

19. Municipals further contend that the *Columbia Gulf* case concerned a transportation reduction right that was triggered only as a result of retail unbundling. In contrast, state Municipals, section 39 is not limited to retail unbundling, but provides transportation reduction rights, subject to certain procedural requirements, in any situation where the LDC's transportation demands exceed its requirements. Municipals assert that excessive transportation demands occur in a variety of circumstances, but typically are a result of inaccurate estimates by the LDC or an actual reduction in customer demand because of bypass or, in the case of an industrial customer, plant closings, all of which can apply equally to investor-owned and municipal LDCs and can result in the costs associated with the excess demand being absorbed by the LDC or passed through

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[8] 99 FERC ¶ 61,310 (2002), *order on reh'g*, 101 FERC ¶ 61,246 (2002), *order on reh'g*, 106 FERC ¶ 61,210 (2004).

[9] Southern Cities cite *Panhandle Eastern Pipeline Company, LLC*, 108 FERC ¶ 61,225 (2004) and *Trunkline Gas Company, LLC*, 108 FERC ¶ 61224 (2004).

[10] 105 FERC ¶ 61,351 (2003).

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to its customers. Municipals cite *Midwestern Gas Transmission Company* (*Midwestern*),[11] in which the Commission approved a contract reduction provision applicable to retail unbundling that would give contract reduction rights to both investor-owned and municipal LDCs if they are subject to "unbundling risks." Municipals argue that existing section 39 is anti-competitive because it allows an investor-owned LDC to shed costs of excess transportation demands -- even if the demands were imprudently contracted -- while denying municipal LDCs that same right.

20. Calpine and Calhoun Power Company I, LLC (Calhoun) point out that, in *Columbia Gulf*, the Commission ruled that "[i]n its next rate case, Columbia Gulf will bear the burden to prove that any rate effect resulting from Columbia Gulf extending a Reduction Option to any of its customers is just and reasonable, providing of course that Columbia Gulf and any of its customers even avail themselves of this option."[12] Calpine and Calhoun ask the Commission to impose this requirement on Southern as well.

21. PCS Nitrogen Fertilizer, L.P. (PCS) argues that commensurate transportation demand reduction rights must be provided to Southern's firm industrial shippers, in the event of a plant outage or a scale-down of operations, to satisfy the standards of NGA sections 4 and 5.[13] In this case, contends PCS, it is only asking the Commission for a continuation of the comparable contract demand (CD) reduction rights to which Southern's firm industrial shippers have been entitled for the last four years under the settlement in Docket Nos. RP99-496-000 and RP99-496-001.[14]

22. Southern Cities argue that in *Florida Gas,*[15] the Commission permitted Florida Gas to include in its tariff a contract reduction provision relating to retail choice that drew no distinction between investor-owned (PSC-regulated) and municipally-owned (and regulated) electric utilities in the State of Florida.

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[11] 103 FERC ¶ 61,259 (2003).

[12] Calhoun cites *Columbia Gulf Transmission* Co., 103 FERC ¶ 61,389 at 62,530 (2003), *order on reh'g*, 105 FERC ¶ 61,351 at P 19 (2003).

[13] PCS cites *Southern Natural Gas Co*., 91 FERC ¶ 61,206 (2000); *ANR Pipeline Co*., 99 FERC ¶ 61,310 (2002), *reh'g denied*, 101 FERC ¶ 61,246 (2002), *reh'g denied*, 106 FERC ¶ 61,210 (2004).

[14] *Southern Natural Gas Co*., 91 FERC ¶ 61,206 (2000).

[15] 101 FERC ¶ 61,401 (2002).

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23. On the other hand, Alabama Gas Corporation (Alabama Gas) argues against extending the applicability of section 39, contending that the provision protects against the unique risk of governmental action, not from other types of load loss. Alabama Gas and SCANA Energy Marketing, Inc. (SCANA) also contend that the proposed extension of the notice period is excessive.

24. Atlanta Gas Light Company and Chattanooga Gas Company (Atlanta and Chattanooga) argue that Southern has not supported the proposed 24-month notice requirement. According to Atlanta and Chattanooga, the 24-month notice period would shift the risk to the shipper exercising the PSC-out Provision.

25. Peoples Gas System, a Division of Tampa Electric Company (Peoples) challenges the proposed increase in the notice period, contending that the time intervals associated with expansion have more to do with construction lead times than with open season procedures. In any event, even if an extension of the notice period is necessary, Peoples argues that a far less extreme adjustment -- perhaps six months -- would be adequate.

26. In their reply comments, Municipals emphasize that *Columbia Gulf* establishes that a pipeline can tailor its tariff to provide for transportation demand reductions in terms of a single event -- retail unbundling -- while Southern's section 39 is not so limited and provides for transportation demand reduction whenever the LDC has excess capacity. Municipals also cite *CenterPoint Energy Gas Transmission Company* (*CenterPoint*),[16] contending that the tariff provision approved by the Commission in that case (relying on *Columbia Gulf*) addressed unbundling ordered by "a governing authority having jurisdiction." Municipals argue that this must include a municipal's board.

27. In their reply comments, Southern Cities submit that municipal utilities are indeed subject to governance review in which the public, including Southern, can participate. They emphasize that the reviewing body, whether a PSC or a city commission, will be seeking to balance the long-term supply security of the utility against the risk of stranded costs to the utility and its customers.

4. Commission Analysis

28. The Commission will accept Southern's proposal to extend the notice period in section 39 from 90 days to 24 months. Additionally, the Commission rejects the proposal of certain intervenors to extend the scope of eligibility under section 39 to cover shippers that are not state regulated. Further, the Commission rejects the request that this issue be addressed in the evidentiary hearing. The

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[16] 109 FERC ¶ 61,387 (2004).

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parties discussed it at length at the technical conference, and the Commission finds that the post-technical conference comments have provided a sufficient basis to allow the Commission to resolve in this order both issues relating to section 39.

a. Length of Notice Period

29. The Commission will accept Southern's proposed 24-month notice period for section 39 of the GT&C. It is reasonable to assume that 90 days does not allow Southern enough time to remarket capacity if it must construct additional facilities to do so, and the intervenors have failed to provide support for a specific, alternative, shorter period that would afford Southern adequate time to construct any necessary facilities.

30. Southern's transportation demand reduction provision grew out of a negotiated settlement, and Southern voluntarily retains it in the tariff. Because the Commission does not require Southern to maintain this provision, the Commission cannot require Southern to establish a particular period of time for advance notice of CD reductions. Nothing about the proposed extension of time has an effect that is unduly discriminatory, and as stated above, the longer period proposed by Southern appears to be a reasonable estimate of the time that could be required to extend Southern's facilities so that it can remarket the relinquished capacity. As Southern has pointed out, the Commission accepted a three-year notice period in *Florida Gas*.[17] Further, the Commission is unpersuaded that extending the notice period shifts the risk to the shippers exercising the transportation demand reduction option. Southern has the ability to remove this provision from its tariff, which would place the LDCs at greater risk of having to absorb or pass through costs attributable to capacity they are required to relinquish. The Commission also finds it significant that no shipper has exercised this right since it was added to the tariff. Viewed in that light, the arguments advanced by the intervenors concerning the length of the notice period are speculative and carry even less weight.

b. Scope of Eligibility

31. The more significant question concerning section 39 is whether Southern can or should be required to extend applicability of that section to shippers other than state-regulated pipelines. Southern points out that it has not proposed a change in the eligibility requirements of section 39 and that no party has met the burden of proof required under NGA section 5 to force Southern change the eligibility requirements. The parties dispute at length whether industrial end-users, municipal utilities, and state-regulated LDCs are similarly situated and whether section 39 unduly discriminates in favor of the state-regulated entities. The Commission concludes that these classes of shippers on Southern's system are

[17] *Florida Gas Transmission Co.*, 101 FERC ¶ 61,401 at P 4 (2002).

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not similarly situated, and it is not undue discrimination to limit section 39 to a clearly defined set of requirements applicable only to state-regulated entities.

32. As Southern has pointed out, it did not propose a change to the applicability of section 39. Thus, the parties proposing such a change bear the burden of proof to demonstrate that section 39 is unjust, unreasonable, and unduly discriminatory. They also bear the burden of proving that their suggested changes would be just, reasonable, and not unduly discriminatory. The intervenors in this case have failed to carry that dual burden. It is not Southern's responsibility to demonstrate that an existing tariff provision has not become unduly discriminatory. Further, there is no merit to the argument that other pipelines may have voluntarily offered contract demand reduction rights to a broader group of their shippers. A pipeline's voluntary offer to a broader group of customers does not require a Commission finding that different categories of shippers are similarly situated in the instant case.

33. In *Columbia Gulf*, the Commission accepted a voluntary proposal by that company to allow it to include contract demand reduction rights in its service agreements with customers subject to regulatory unbundling or restructuring. The Commission specifically rejected a request that the pipeline extend the right to industrial end-users, distinguishing regulatory risk from business risk. The Commission emphasized that it does not require pipelines to permit customers to terminate or reduce their contractual obligations before the end of the contract terms.[18]

34. While that case resolves the question of whether industrial end-users and LDCs are similarly situated, it does not address whether municipal utilities and state-regulated LDCs are similarly situated and entitled to equal treatment in a voluntary transportation reduction provision. However, the Commission's analysis in that case is persuasive here. In *Columbia Gulf*, the Commission stated, "It is reasonable for Columbia Gulf to grant the right only to LDCs adversely affected by regulatory unbundling. The Commission has specifically stated that it may be reasonable for a pipeline to tie contract demand reductions to certain events, one of which is retail unbundling."[19] Municipal governing boards or agencies do not order retail unbundling; state regulatory agencies do. Further, even though various classes of customers may find themselves with excess capacity, that fact alone does not cause them to be similarly situated. The provision at issue in Southern's tariff has specific requirements that the state

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[18] *Columbia Gulf Transmission Co.*, 105 FERC ¶ 61,351 at P 11-14 (2003).

[19] *Id*. at P 12 (footnotes omitted).

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regulatory agency must find that pipeline has excess capacity and direct it to reduce its firm transportation quantities. Further, the provision in Southern's tariff requires that the pipeline must defend against the reduction and advise Southern of the state proceeding so that Southern will have an opportunity to participate in the state proceeding. All of these requirements are specific to state-regulated pipelines, and in this case, it is not undue discrimination for Southern to limit the applicability of its PSC-out Provision to these customers.

35. The Commission finds that Southern's section 39 is intended to address a situation specific to state-regulated LDCs and contains procedural requirements that assume public participation and a decision by an independent body that has no direct interest in the outcome. On the contrary, by definition, a city commission or other municipal governing entity has a much narrower focus and a much more direct interest in the rates and services provided by the utilities it regulates.[20]

36. The other pipeline proceedings cited by the intervenors do not support the outcome the intervenors seek. In those cases, the other pipelines voluntarily offered CD reduction rights to classes of customers as they deemed appropriate. The Commission made it clear in those cases that pipelines are not required to offer such provisions, but if they do so, they must offer the rights on a non-discriminatory basis. Yet the Commission also made it clear that not all classes of customers are similarly situated for purposes of CD reduction rights. The Commission affords pipelines considerable latitude in determining those customers to which they will offer CD reduction rights, as long as the provisions are made available on a non-discriminatory basis to individual customers within the specified classes.

37. Finally, the Commission will not grant here the requested ruling that there is no presumption that Southern can pass through to its other customers the risk of transportation reductions. It is a basic ratemaking principle that, in any general section 4 rate proceeding, the applicant bears the burden of proof with respect to any costs for which it seeks recovery. Further, the Commission will not require Southern to expand or continue shipper rights that arose out of the settlement of a prior proceeding.

38. Accordingly, the Commission will not require Southern to expand the applicability of section 39 to other classes of customers, nor will the Commission require Southern to eliminate the provision from its tariff merely because similar rights are not provided for other classes of customers.

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[20] *Cf. CenterPoint Energy Gas Transmission Co.*, 109 FERC ¶ 61,387 at P 4-6 (2004) ("LDCs have a regulatory obligation to serve high priority captive customers and its [sic] customer base is much wider.").

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B. Proposed Limitation on Adding or Deleting Receipt Points

1. Background

39. Section 2.1(e) of the GT&C describes the rights of firm shippers to add or delete their firm receipt and delivery points. According to Southern, it recently revised its tariff to replace its current mechanism of awarding primary receipt point capacity from a first-come, first-served methodology to a net present value (NPV) allocation mechanism, consistent with the manner in which Southern awards pipeline capacity and delivery point capacity. To further the consistency between the award of delivery point and receipt point capacity, Southern proposes to revise section 2.1(e) on Third Revised Sheet No. 103 to specify that primary receipt points may be added or deleted from Exhibit A to the service agreement if they are in the same zones for which the shipper has contracted for firm service. Similarly, continues Southern, shippers are already permitted to add or delete primary delivery points from Exhibit B to a service agreement only if the additional delivery points are in the same zone as the shipper's current delivery points. Southern states that this new provision does not specify a shipper's rights to deliver or receive gas from secondary delivery or receipt points, and it is not intended to define when a replacement shipper may select primary point rights.

2. Southern's Comments

40. Southern states section 2.1(e) of the GT&C already addresses firm delivery points. Thus, states Southern, it's proposal here merely seeks to clarify the rule with respect to firm receipt point amendments. Southern maintains that it does not seek to limit shippers' rights to nominate to any non-firm receipt points on a secondary basis. According to Southern, this right was thoroughly discussed in the Commission's order of May 6, 2003, in Docket No. RP03-76-000,[21] where the Commission found that shippers should have secondary rights to nominate from any receipt point on Southern's system under Southern's zone-of-delivery reservation rate design.

41. Southern contends that, given its zone-of-delivery rate design, it is not clear whether shippers who originally contracted for firm west to east (Zone 0 to Zones 1 or 2) service should be allowed to turn around their firm rights east to west (Zone 3 to Zones 2, 1, or 0) service where the shipper has not contracted for Zone 3 capacity. Southern emphasizes that it does not propose to prohibit shippers from executing new contracts for east to west (Zone 3 to Zone 2, 1, or 0) service, and indeed, it recently initiated an open season requesting bids for such service.

[21] Southern cites *Southern Natural Gas Co.*, 103 FERC ¶ 61,131 (2003).

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However, Southern argues that it does not seem fair to allow shippers that previously did not have any firm capacity in Zone 3 to use the receipt point amendment process to gain access to Zone 3 and essentially reverse the flow of their firm capacity.

42. Southern also clarifies that, under its zone of delivery reservation rate design, if a shipper's reservation rate is established based on the delivery zone and given that such rate is a derivation of the cumulative total costs of the upstream zones (west to east), then Southern did not intend to limit a shipper's right to amend its firm receipt points to points in upstream zones. Southern reiterates that the limited situation it intends to address here is the situation where a shipper wants to amend or shift its firm receipt point rights to a downstream zone.

43. On January 27, 2005, Southern filed a letter with the Commission stating that it is willing to have this issue resolved at the hearing. Southern states that, if the Commission defers a ruling on this issue pending the outcome of the hearing, Southern will not move to put this tariff change into effect on March 1, 2005, at the expiration of the suspension period, but will wait until the Commission addresses it in an order or the parties act on the provision through the settlement process.

3. Comments of Intervenors

44. Most intervenors oppose Southern's proposal. They generally assert that it would produce arbitrary and unreasonable results, that it is contrary to Commission policy,[22] and that it is merely a repackaging of arguments rejected by the Commission in earlier proceedings.[23] They connect this proposal with the reactivation of the Elba Island LNG terminal and state that it would preclude many shippers from accessing this new source of supply. The intervenors further contend that the proposal is inconsistent with Southern's zone-of-delivery rate

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[22] The intervenors cite Order No. 636-A, FERC Stats. & Regs., [Regulations Preambles 1991-1996] ¶ 30,950 (1992); *ANR Pipeline* Co., 97 FERC ¶ 61,323 at 64,480 (2001); *Great Lakes Gas Transmission Limited Partnership*, 101 FERC ¶ 61,206, *clarifying* 100 FERC ¶ 61,083 (2002) ("The Commission will require Great Lakes to permit shippers to permanently add, or change, primary points to those outside the transportation paths stated in their firm contracts, but within zones for which they are paying. This policy applies to segmented transactions as well.")

[23] The intervenors cite *Southern Natural Gas Co.*, 103 FERC ¶ 61,131 (2003).

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design under which firm shippers pay a reservation charge based solely on the primary point of delivery, so they cannot be precluded from switching to new receipt points in any zone except for operational reasons. The intervenors point out that the zone-of-delivery rate design is among the issues set for hearing.

45. The intervenors dispute whether the Commission should rule on this proposal at this juncture, including whether the proposed revision should be allowed to go into effect, subject to refund, while the hearing addresses Southern's zone-of-delivery rate design. Dalton argues that reactivation of the Elba Island facility undermines a major premise underlying Southern's zone-of-delivery rate design, which assumes that all of the gas on Southern's system flows from supply sources in the west to markets in the east. In contrast, states Dalton, Elba Island volumes would flow in the opposite direction. Dalton observes that at different times in the past, zone differentials were eliminated and reinstated on Southern's system, depending on whether the Elba Island facility was operational.[24] Dalton also points to Southern's recent open season relating to transportation of gas from Elba Island.

4. <u>Commission Analysis</u>

46. As stated above, Southern filed a letter with the Commission indicating its willingness to defer moving into effect the proposed tariff sheet at issue here. Several parties have emphasized the interrelationship of this proposal and Southern's existing zone-of-delivery rate design, which is at issue in the hearing. Because no party will be harmed if the tariff provisions relating to this proposal are not moved into effect, the Commission will accept Southern's offer to delay the effectiveness, and the Commission will direct the Presiding Administrative Law Judge in this proceeding to include this issue in the ongoing evidentiary

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[24] Dalton cites *Southern Natural Gas Co*., 10 FERC ¶ 61,287 (1980), *reh'g denied,* 11 FERC ¶ 61,506 (1980) ("Our decision to eliminate zones on Southern's system was based on the changes in pipeline use and benefits that resulted from the introduction of substantial volumes of LNG in the terminal zone.") Dalton further states that zone of delivery rates were reinstated effective January 1, 1982, due to the termination of LNG shipments from Algeria to Elba Island. Dalton cites *Southern Natural Gas Co*., 27 FERC ¶ 61,476 at 61,915 (1984). According to Dalton, although under the zone-of-delivery rate design "the rate for the zone of delivery applies regardless of the zone of receipt," *Southern Natural Gas Co*., 67 FERC ¶ 61,262 at 61,903, n.6 (1994), the Commission did recognize after the termination of deliveries from Elba Island that the resultant zoned rates reflected distance in that customers in the zone closest to the wellhead sources of gas on the western end of the system paid the lowest reservation rate. Dalton cites *Southern Natural Gas Co*., 62 FERC ¶ 61,136 at 61,942 (1993).

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hearing for development of a more extensive record on this issue and its relationship to any changes that may be required in Southern's rate design.

C. Cashout Price Calculation and Applicability to the Zero-to-Two Percent Tolerance Level

1. Background

47. Southern proposed three changes to its cashout pricing mechanism associated with the zero-to-two percent tolerance level, including (1) adding to the calculation of the monthly index price two new prices, incorporating the first published weekly and monthly index prices for the month succeeding the transportation month, (2) utilizing a high or low price as the cashout price for majority imbalances in the first tier, zero-to-two percent imbalance level instead of the simple average, and (3) cashing out 100 percent of minority shippers' imbalances (the opposite direction of the majority of imbalances on the system) at the average monthly index price. In the September 30, 2004 Order, the Commission accepted Southern's proposals effective October 1, 2004, but included the application of the high/low price to the zero-to-two percent tolerance level in the issues to be addressed at the technical conference to develop a more complete record.

2. Southern's Comments

48. Southern states that Indicated Shippers argued that, because Southern's measurement correction threshold established in its tariff is two percent, shippers accrue imbalances that are cashed out at the high/low price even when their percentages are less than Southern's meter error. Southern asserts that it presented evidence at the technical conference showing that the two percent meter correction tolerance is not relevant to the first tier imbalance tolerance. According to Southern all of its meters have electronic measurement,[25] and that of all the measurement transactions on its system, only 0.3 percent of the calculated volumes have been adjusted for measurement error. Southern maintains that, if an error is discovered after the end of the month, where actual flow adjustments

[25] Southern points out that its shippers have ready access to their electronic data through Southern's SoNet Premier service so that they have the ability to correct any imbalances that result from a measurement discrepancy.

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cannot be made, any correction is considered to be a prior period adjustment and is cashed out at the average index price rather than the high or low cash out price for the month.[26]

49. Southern states that the two-percent measurement error provision only establishes the threshold for when measurement adjustments must be made, but it does not relate to the actual accuracy of Southern's measurement. Southern asserts that all of its custody transfer meters have electronic measurement that is accurate to within 0.6 percent.

50. Southern contends that, although the Commission approved the high/low cashout price in the September 30, 2004 Order, many of the parties at the technical conference wanted to discuss whether such high/low pricing is equitable. Southern suggests that the parties should give it time to test the effectiveness of the pricing mechanism's effectiveness in mitigating arbitrage. Southern explains that its filed testimony showed that 88 percent of imbalances on Southern's system occur in the zero-to-two percent tier,[27] and further, that Southern's technical conference presentation showed that net cashout imbalances can be larger than the net system imbalance at the end of the month due to the incentives provided by an average index price being applied to cash out imbalances. Southern claims that it is trying to eliminate the environment in which cashing out is the imbalance resolution mechanism of choice because of the economic incentives associated with it.

51. Southern asserts that the Commission has allowed pipelines to change their cashout pricing methodologies to prevent arbitrage.[28] Further, states Southern, the Commission has indicated that one way to do so is to eliminate the incentives for shippers to borrow gas from the pipeline because the cash out price is less (or more) than the market price for gas.[29] Southern contends that the high/low pricing

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[26] Southern cites Second Revised Sheet No.143, section 14.1(g) of the GT&C.

[27] Southern cites Ex. JHP-2 at 1-2.

[28] Southern cites *Transcontinental Gas Pipe Line Corp.*, 98 FERC ¶ 61,213 at 61,813 (2002); *Texas Gas Transmission Corp.*, 96 FERC ¶ 61,318 at 62,218 (2001), *order on reh'g,* 97 FERC ¶ 61,349 (2001); *Northern Natural Gas Co.*, 105 FERC ¶ 61,172 at 61,889, *order on reh'g*, 107 FERC ¶ 61,252 at P 17 (2004); *ANR Pipeline Co.*, 109 FERC ¶ 61,138 at 61,541 (2004).

[29] Southern cites Order No. 637, FERC Stats. & Regs., [Regulations Preambles 1996-2000] ¶ 31,091 at 31,414-15.

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methodology does two things to mitigate arbitrage. First, states Southern, it creates uncertainty, and second, it reduces the economic incentive to resolve imbalances through the cashout mechanism. Southern maintains that the Commission approved the use of the high/low pricing in *Northern Natural Gas Company*.[30] Southern also states that, in *ANR Pipeline Company,*[31] the Commission stated that it was particularly appropriate to apply high/low pricing to the first tier of imbalance resolution because that is where shippers have the greatest incentive to engage in arbitrage. Southern emphasizes that its cash out price mechanism does not constitute a penalty.

52. Specifically, continues Southern, shippers control the direction of their imbalances and the mechanisms they use to resolve their imbalances. Southern asserts that, for October 2004, the first month in which the high/low price could be the cashout price, the shippers met the net system imbalance tolerance test, and the cashout price was the average index price. Further, states Southern, in November 2004, the first month in which the high/low price was used for cash out, 54 percent of the majority shippers elected to use storage over cash out to resolve imbalances. According to Southern, majority shippers leave their imbalances to be cashed out more frequently than minority shippers. Southern states the data show that, with the exception of a few months when the end of the month pricing was erratic, the arbitrage opportunity created by the cashout price differential determined the direction of the majority imbalance. According to Southern, October 2004 was the first time the system met the system-wide imbalance test since July 2001, and if imbalances in the zero-to-two percent tolerance range are incidental, then the net system imbalance test should be met more frequently. Southern argues that, while a shipper on an individual contract may not be able to achieve a zero imbalance for operational reasons, by allowing free netting across contracts and rate zones and through imbalance agents, Southern's tariff allows shippers the opportunity to have their monthly imbalances netted out to zero through aggregation of imbalances.

53. Southern claims that the high/low pricing mechanism is not a penalty; rather it is a weekly or monthly average price. Further, argues Southern, average index pricing is not analogous to charging the highest or lowest daily spot price during the month, and it does not use the same pricing strategy as the highest tiers, which adjust the actual price by a percentage to create an inherent penalty in the price of gas being bought or sold. Southern claims that the average index price has been found not to be the most equitable price because it has not matched the

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[30] 107 FERC ¶ 61,252 (2004).

[31] 109 FERC ¶ 61,138 at P 36 (2004).

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market price, and the system has had to pay for the mismatch. Moreover, Southern contends that the average index price does not correspond to the actual market price of the gas when it is bought or sold the next month.

3. Comments of Intervenors

54. Indicated Shippers argue that measurement accuracy to 0.6 percent does not justify a zero-percent tolerance, claiming instead that this is evidence that balancing cannot be 100 percent accurate. Further, contend Indicated Shippers, because actual meter error is less than two percent, actual imbalances that are less than two percent do not justify a zero-percent tolerance. Indicated Shippers ask the Commission to provide some minimum level of flexibility with regard to transportation imbalances in recognition of the fact that it is operationally impossible to manage imbalances to zero each month, and gas imbalances cannot be measured with that degree of accuracy.

55. Indicated Shippers acknowledge that the majority of imbalances are in the first tier, but argue that this fact does not demonstrate the existence of arbitrage. Indicated Shippers state that the record evidence is inconclusive and does not support Southern's case. For example, Indicated Shippers dispute Southern's claim that the more days arbitrage is possible after the index price is known, the greater the imbalance. Indicated Shippers further claim that Southern has not demonstrated conclusively that there is a linkage between the amount of cashout imbalance and the arbitrage price differential. Additionally, contend Indicated Shippers, there is no discernible pattern in the imbalances on an individual level that would suggest price arbitrage is occurring. Indicated Shippers assert that that Southern's imbalance mitigation tools (*e.g.*, storage, no-notice service, park and loan, make up during the month, and imbalance trading) are either more costly and unreliable or unavailable.

56. Georgia Industrial Group (GIG) argues that Southern's proposal would penalize a shipper that runs even a slight imbalance and further, that shippers can run imbalances due to the vagaries of running an industrial facility. GIG maintains that minor imbalances in the zero-to-two percent range are not affecting system reliability and that shippers are not intentionally gaming the system. GIG claims that it is premature to assess the impact of the new cashout mechanism because only two months of data were available to review. GIG further asserts that Southern's proposal is contrary to Order No. 637, where the Commission determined that pipelines can only impose penalties when needed to protect system integrity and that penalties must be limited to those situations that are necessary and appropriate to protect against system reliability problems. GIG asserts there should not be tightened cashouts or increased penalty levels absent a demonstration of operational harm.

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57. Calhoun states that there appears to be no adequate justification for the entire elimination of the zero-to-two percent tolerance band because, while the overall system is more in balance, individual shippers have created higher imbalances after the end of the month when they utilized storage. SCANA does not support the change at this time, and argues that the Commission should allow the system to operate with the addition of the extra week of the cashout price determination and review it at a later time.

58. Duke argues that there is no evidence that arbitrage is actually occurring, much less that it is having an operational impact on Southern's system. Further, states Duke, it is not possible to manage imbalances to zero, given that Southern's meters are not 100 percent accurate, and especially because Southern's imbalance resolution tools are practically unavailable. Duke asserts that the Commission should gain some operational experience, but in the meantime, should reject Southern's proposal.

59. Alabama Gas, Southern Cities, and Municipals argue that Southern has demonstrated that the two-percent meter error correction is not relevant to the first tier and is simply the point at which Southern is required to go back and rebill the shipper unless the meter error is greater than that amount. They contend that the actual meter error is inconsequential, claiming that virtually all pipelines have the same provisions relating to meter error and the same types of meters.

4. Commission Analysis

60. The Commission accepts Southern's proposal to apply the high/low cashout pricing to its zero-to-two percent imbalance tier. As explained below, Southern has shown that this change to its cashout mechanism is reasonable in order to minimize arbitrage, which can result in increased SCRM surcharges. This determination also is consistent with Commission precedent.

61. Southern presented evidence that (1) the vast majority of imbalances that are cashed out on its system occur in the zero-to-two percent tier when the average index price is applied, (2) under the cashout mechanism with an average index price, shippers typically are able to determine the average index price with certainty before the end of the month, and (3) the direction of the net imbalances on the system typically tracks the direction of the market price changes during the month, as compared to the average index price.[32] Additionally, Southern has consistently had an underrecovery in its SCRM account. The Commission finds that this evidence clearly shows that the use of the average monthly index price gives shippers an opportunity to engage in arbitrage on Southern's system.

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[32] *See* Prepared Direct Testimony of Ms. Janice H. Parker.

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62. The Commission also finds that adoption of the high/low cashout pricing for the zero-to-two percent imbalance tier is an appropriate response that will mitigate the opportunity for arbitrage. During the last week of the month, the shippers should not have any degree of certainty that the cashout price will be higher or lower than the market price on the day in question. This finding is consistent with the Commission's approval of similar proposals finding that using a weekly high/low index price to resolve all majority imbalances is just and reasonable.[33] As the Commission found in *Northern Natural Gas Company*,[34] shippers may incur imbalances in the initial tier cashed out at 100 percent of the applicable monthly average cash out index price for the purpose of arbitrage, just as they can incur greater imbalances for that purpose. Indeed, it is in this tier that shippers would have the greatest incentive to engage in arbitrage. That is because in the higher tiers, the percentage adjustment to the index price would tend to reduce any price differential between the cashout price and the index price.

63. The intervenors' argument that this remedy should be rejected because of meter error is not persuasive. Southern has shown that there is no correlation between the two-percent measurement provision in its tariff and the zero-to-two percent cashout tolerance level. As Southern has explained, the two-percent measurement provision establishes the threshold when measurement adjustments must be made, and it does not relate to the accuracy of Southern's measurements. Rather, Southern states that its meters have electronic measurement that is accurate to within 0.6 percent. Further, Southern provides procedures by which shippers' concerns over inaccurate metering can be addressed. Southern has shown that shippers have access on SoNet Premier to electronic data that permits them to monitor the meter measurement and to make adjustments to control imbalances. The intervenors have not established that Southern's meter error percentage is excessive or atypical in the industry. Additionally, meter error applies to all imbalances, not just those in the zero-to-two percent tier, as well as billing for the underlying transportation services. Hence, unless shown to be inaccurate, shippers must assume that the metered volumes are accurate for all purposes, including for the purpose of determining imbalances. Thus, the Commission concludes that the existence of meter error alone is not sufficient to restrict the application of the high/low cashout pricing to the zero-to-two percent imbalance tier.

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[33] *See ANR Pipeline Co.,* 109 FERC ¶ 61,138 at P 32 (2004), *reh'g pending* (*ANR*); *Texas Gas Transmission Corp*., 97 FERC ¶ 61,349 at 62,632 (2001) (*Texas Gas*).

[34] 107 FERC ¶ 61,252 at P 23-24 (2004) (*Northern Natural*).

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64. The Commission also rejects the argument that Southern's proposed weekly high/low index price is an inappropriate penalty under the standards of Order No. 637. The Commission has stated that the goal of minimizing arbitrage supports the use of the high/low pricing method for all imbalances, not just those in excess of a tolerance level, despite the possibility that using the high/low pricing for cashing out first tier imbalances might be considered a penalty in some sense.[35] Moreover, it is not reasonable to require a showing of operational harm before adopting the high/low pricing, nor does Order No. 637 require it. In Order No. 637-A, the Commission held that:

> the fact that arbitrage is occurring … within pipeline systems demands that pipelines revise the level and structure of their penalty provisions to minimize the opportunity for arbitrage. For example, as the Commission stated in Order No. 637, pipelines may be able to change their imbalance cashout procedures or methods to eliminate incentives for shippers to borrow gas from the pipeline because the cashout price is less than the market price for gas.[36]

65. When price arbitrage occurs, the pipeline is, in essence, required to sell gas to its customers at below-market levels and buy gas from them at above-market levels. This can lead to the pipeline incurring a substantial underrecovery of costs. As the Commission held in *Texas Gas*, there is no reason to make the correction of such a problem contingent on a showing that the imbalances are causing operational problems.[37] It is not just and reasonable to require pipelines to underrecover their costs, and, as the quoted language above indicates, the Commission did not require it in Order No. 637.

66. Finally, any impact of the Commission's adoption of high/low pricing is mitigated because Southern offers a number of imbalance management services to its customers as alternatives to resolving the imbalances by cashout both during the month and after the month. While these services may not always be available and may only be available at a cost, the Commission finds that they offer reasonable alternatives to shippers to manage their imbalances and make choices that are in their best economic interests.

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[35] *ANR Pipeline Co*., 109 FERC ¶ 61,138 (2004), *reh'g pending*.

[36] Order No. 637-A, FERC Stats. & Regs. [Regulations Preambles July 1996 – December 2000] ¶ 31,099 at 31,607 (2000).

[37] *Texas Gas Transmission Corp*., 97 FERC ¶ 61,349 at 62,634 (2001).

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67. Accordingly, the Commission accepts Southern's proposal to revise its cashout price calculation to apply the high/low index to the zero-to-two percent tolerance level.

D. Proposal to Apply SCRM to Supply Poolers

1. Background

68. Section 14.2 of the GT&C of Southern's tariff provides for an annual reconciliation of Southern's storage costs to reflect differences between the cost to Southern of its storage gas inventory and the amount Southern receives for such gas arising out of: (1) the purchase and sale of such gas in order to resolve shipper imbalances pursuant to the cashout mechanism in section 14.1 of the GT&C; and (2) the purchase and sale of gas as necessary to maintain an appropriate level of storage gas inventory for system management purposes. Under the existing mechanism, the SCRM surcharge (or credit) is calculated by dividing costs by transportation delivery volumes under Southern's FT, FTNN, and IT rate schedules and assessed on these transportation deliveries.

69. In this proceeding, Southern proposes to apply the SCRM surcharge to volumes of gas pooled on its system under Supply Pool Balancing Agreements for receipt volumes that are nominated into pools from sources other than Rate Schedule CSS or ISS contracts, other Supply Pool Balancing Agreements, and Rate Schedule PALS. In addition, Southern proposes to include volumes associated with pooling on its system in the calculation of the SCRM surcharge. Southern filed the tariff changes to the SCRM surcharge on *pro forma* tariff sheets, requesting that it be allowed to place these sheets into effect on a prospective basis once an order on the merits or settlement of this proceeding has been issued.

2. Southern's Comments

70. Southern explains that shippers pool their gas on its system through the use of Supply Pooling Balancing Agreements. The poolers nominate their gas into the pooling agreements from physical receipt points, and then the pool can nominate directly into a transportation agreement or another pooling agreement. Southern explains that, while purchasing gas from a pool insulates the shipper from supply imbalances (because nominated deliveries equal scheduled deliveries), it is the responsibility of the pooler to resolve its receipt imbalance into the pool.

71. Southern maintains that imbalances caused by pools affect the system in the same manner as any other imbalances. Southern states it must use its system assets to cover or store imbalances caused by insufficient or excess supply. Similarly, continues Southern, once a pooling imbalance is cashed out, the system

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bears the costs associated with resolving the imbalance by buying or selling gas to offset the imbalance. Southern asserts that the pre-filed testimony of its Witness Parker shows that the imbalances from pools represent 47 percent of the total imbalance activity on the system during the 12 months ending April 30, 2004. In addition, Southern submitted data that showed in the nine out of 12 months pool imbalances represents a significant percentage of the net system imbalance and that this percentage was enough to drive the direction of the system imbalance (short or long). Additionally, Southern notes that the pool imbalances followed the direction of the arbitrage opportunities during the same nine months.

72. Southern contends that inclusion of pooling volumes and application of the SCRM surcharge to poolers will increase the number of shippers that incur the SCRM, but it will also spread the cost of the SCRM more equitably by: (1) applying it to a larger group of shippers, thereby minimizing the cost to each shipper; and (2) ensuring that it applies to all groups of shippers that incur imbalances and create the costs that are passed through the SCRM.

3. Comments of Intervenors

73. Southern Cities state that there is a compelling case for including supply poolers in the SCRM calculation and surcharge assessment. Southern Cities explain that (1) roughly two-thirds of Southern's throughput enters the system via a supply pool, (2) the supply pooler (rather than the shipper) is properly deemed to have control of the activities at the receipt points, (3) supply poolers have access to imbalance tools similarly to those afforded shippers, (4) supply pool imbalances constitute a substantial percentage of total system imbalances, and (5) under Southern's proposal, there would be no double charging of sequential pools and no charging of storage withdrawals. Southern Cities state that Southern's proposal more equitably allocates costs associated with system imbalances and should be approved. Southern Cities argue that Southern should continue to consider deliveries out of the supply pools into transportation agreements for redelivery to be the confirmed receipt quantity under those agreements, but they should not be charged with imbalances between volumes confirmed for delivery into the pool and the actual volumes delivered under the agreements between supply poolers and their suppliers.

74. GIG argues that supply poolers should pay equitable charges and that the SCRM should be assessed on all pool receipts, but that the SCRM should not apply to receipts from other pools or storage contracts. Alabama Gas notes that supply poolers are responsible for 47 percent of the cashed out imbalances, but on a gross basis supply poolers are 202 percent of net majority imbalances. Atlanta and Chattanooga also support Southern's tariff proposal because they claim it will result in a more equitable distribution of SCRM costs.

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75. Dalton states that by taking into account the pooling receipts, Southern's proposed change in calculating the SCRM appears to reflect actual operations better than the calculation currently in use. Municipals state that the imposition of the SCRM surcharge on poolers is necessary to ensure that all entities that create imbalances are accountable for the costs they impose on the system.[38] Calhoun states that poolers should share in the burden of paying the SCRM surcharge, and applying the SCRM surcharge to only the first movement into the pool should not inhibit flexibility to make pool to pool transfers. SCANA also supports Southern's proposal to amend section 14.2 of the GT&C to include pooling receipts in the calculation of Transportation Volumes.

76. Indicated Shippers assert that Southern should not be permitted to apply the SCRM surcharge to poolers because Southern has mismanaged the SCRM account by failing to take available steps to reduce the balance in the SCRM account. Indicated Shippers maintain that Southern has discounted the SCRM surcharge and does not absorb the costs related to the discount, thereby unfairly shifting costs to other shippers. Indicated Shippers also state that Southern paid $1 per MMBtu more for gas it bought than for gas it sold in the same month of September 2004, and therefore, Southern has no incentive to minimize the SCRM balance. Indicated Shippers also argue that Southern has purchased gas adding additional costs to the SCRM account when it did not need to purchase gas because it had overrecovered fuel. Indicated Shippers state that the effect of charging a SCRM surcharge to poolers will act as a disincentive to pool gas. Moreover, Indicated Shippers claim that it will result in unreasonable double charges on the same transportation transaction, indirectly where the pooler and shipper are different entities, and directly where the pooler and shipper are the same entity, and that is not reasonable. Finally, Indicated Shippers claim that no correlation exists between the amount of pool imbalances and the level of the price differential. If the Commission approves the application of the SCRM surcharge to poolers, Indicated Shippers argue that the Commission should require Southern to absorb any discount to the SCRM surcharge and implement procedures to minimize the costs in the SCRM account.

77. Duke requests that the Commission reject Southern's attempt to apply the SCRM to pooling transactions because it claims Southern has not explained how the pooling process creates physical imbalances that require Southern to deploy its operational storage and other balancing assets, and that there is no cost causation basis for imposing the SCRM surcharge on pooling transactions. Duke also

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[38] Municipals cite *Texas Gas Transmission Corp.*, 96 FERC ¶ 61,318 at 62,219 (2001), *reh'g denied*, 97 FERC ¶ 61,349 (2001).

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asserts that it is unduly discriminatory to impose SCRM charges twice, *i.e.*, on volumes that are pooled and then transported.

4. **Commission Analysis**

78. The Commission accepts Southern's proposal to assess the SCRM surcharge on volumes that are nominated into supply pools from all sources, excluding receipts from CSS or ISS contracts, other supply pools, and receipts from Rate Schedule PALS transactions. Southern has demonstrated that imbalances caused by pools affect the system in the same manner as any other imbalances that are includable in its cash imbalance mechanism because supply pool imbalances have the same effect on Southern's gas storage inventory.Thus, application of the SCRM surcharge to poolers will ensure that all parties that create imbalances are accountable for the costs they impose on the system.

79. Indicated Shippers do not contest the fact that pool imbalances cause the system to incur costs to correct the imbalances. Rather, they argue the SCRM should not be applied to pool volumes because Southern has mismanaged the SCRM account. However, this issue is not relevant to whether pool volumes should be assessed the SCRM surcharge and only is relevant to the appropriate level of the surcharge to be assessed on all volumes subject to the surcharge. This issue is not properly addressed here, but instead should be addressed in Southern's annual filings to adjust the SCRM.

80. Similarly, the Commission rejects Indicated Shippers' argument that the SCRM should not be extended to poolers because Southern discounts the SCRM surcharge and does not absorb the costs related to the discount. The fact that the SCRM is discounted has nothing to do with whether it is appropriate to include poolers in the set of customers subject to the SCRM surcharge. Moreover, as Southern explains in its reply comments, Southern does not discount the SCRM, rather it discounts the total rate, and the SCRM is deemed to be discounted first. This is consistent with Commission policy on discounting and with the order of discounting in section 32 of the GT&C of Southern's tariff. The Commission also rejects Indicated Shippers' request that Southern be required to use fuel overrecoveries to offset gas imbalances in the SCRM. The SCRM mechanism does not provide for a fuel offset, and Indicated Shippers has not met its burden of demonstrating that the SCRM mechanism is unjust and unreasonable because it does not contain such an offset. Indicated Shippers has not shown any relationship between the fuel charge and the SCRM.

81. Finally, Indicated Shippers' claim that applying the SCRM surcharge to poolers will result in double charges on the same transportation transaction and will act as a disincentive to pool gas is not persuasive. Poolers create imbalances under Supply Pool Balancing Agreements that are separate from imbalances

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created under transportation contracts. Applying the SCRM surcharge to pool imbalances will ensure that poolers are responsible for the costs that are incurred to resolve imbalances created under their pooling agreements in the same manner as shippers are responsible for the costs associated with imbalances created under transportation contracts. Even if this does provide a disincentive to pool, it is justified to ensure that poolers are responsible for the costs that are incurred on their behalf. Moreover, any disincentive is minimized because under Southern's proposal there is no charging of sequential pools.

82. In sum, the Commission finds that Southern has demonstrated that imbalances are created by pooling arrangements on Southern's system and that supply poolers should be responsible for costs imposed on the system associated with those imbalances. Within 15 days of the date of issuance of this order, Southern must file actual tariff sheets implementing its SCRM proposal, as reflected on its *pro forma* Sheet Nos. 144A and 240, to be effective on March 1, 2005.

E. Requests for Rehearing and Clarification

83. As stated above, Southern LDCs filed a limited request for rehearing of the September 30, 2004 Order insofar as the Commission declined to accept unconditionally the proposed revisions to Southern's cashout pricing formula applicable to the zero-to-two percent monthly imbalance level for majority shippers. In light of the Commission's ruling above, the request for rehearing is denied as moot.

84. Duke filed a request for clarification of the September 30, 2004 Order asking the Commission to clarify that Southern is obligated to provide full refunds with interest to the extent that the Commission ultimately rejects or modifies the index pricing mechanism applicable to shipper imbalances. Because the Commission has resolved the imbalance issue, as discussed above, the requested clarification is moot and is also denied.

The Commission orders:

(A) Except as specifically ordered below, the tariff sheets listed in the Appendix to this order that were set for consideration at the technical conference are approved and accepted without condition.

(B) Within 15 days of the date of issuance of this order, Southern must file actual tariff sheets to be effective March 1, 2005, implementing its SCRM proposal, as reflected on its *pro forma* tariff sheets.

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(C) The issues raised by Third Revised Sheet No. 103, which includes Southern's proposal to revise section 2.1(e) of its GT&C, are referred to the Presiding Administrative Law Judge for consideration in the hearing established in this proceeding.

(D) Rehearing and clarification are denied as moot, as discussed in the body of this order.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.

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Appendix

Seventh Revised Volume No. 1

Tariff Sheets Effective October 1, 2004, Without Condition
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Fourth Revised Sheet No. 140A
Fifth Revised Sheet No. 141
First Revised Sheet No. 141A
Ninth Revised Sheet No. 142
Second Revised Sheet No. 143
Fourth Revised Sheet No. 144
Fourth Revised Sheet No. 144A
Fourth Revised Sheet No. 212G

Tariff Sheet Effective March 1, 2005, Without Condition
Fourth Revised Sheet No. 212G