123 FERC ¶ 61,130
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Enbridge Energy Company, Inc. Docket No. OR08-1-000

Enbridge Energy, Limited Partnership

ORDER ON PETITION FOR DECLARATORY ORDER

(Issued May 7, 2008)

1. On October 18, 2007, Enbridge Energy Company, Inc. (EEC) and Enbridge Energy, Limited Partnership (EELP) (jointly, Enbridge) filed a joint petition for a declaratory order asking the Commission to approve the proposed tariff structure for the Southern Access Extension Pipeline (Extension Pipeline). Flint Hills Resources, LP (Flint Hills) protests the filing because Enbridge proposes a "backstop" mechanism that allows Enbridge to recover from the Lakehead System shippers any deficits resulting from lower than projected throughput over the initial 15 years of the Extension Pipeline's operations and return such amounts (with interest) to the Lakehead shippers if and when the Extension Pipeline achieves surpluses during that period. Flint Hills contends that the backstop mechanism would result in an improper cross-subsidization. As discussed below, the Commission denies the requested declaratory order.

Background

2. According to Enbridge, EEC will construct the Extension Pipeline, which will extend approximately 178 miles south from EELP's Lakehead System at Flanagan, Illinois, to the major oil pipeline hub at Patoka, Illinois. Enbridge explains that the Extension Pipeline, which will cost approximately $434 million, will have an initial annual average capacity of 400,000 barrels per day (bpd), expandable to 800,000 bpd with the addition of more pumping stations.

3. Enbridge states that EELP is constructing a new pipeline (Line 61) from Superior, Wisconsin, to Flanagan, Illinois, that will connect with the Spearhead Pipeline,[1] which extends southwest to Cushing, Oklahoma. Spearhead Pipeline is owned by CCPS Transportation, LLC, another subsidiary of Enbridge Pipelines Inc. (EPI).[2] Enbridge maintains that, by providing an additional outlet for crude oil leaving Line 61 at Flanagan, the Extension Pipeline will enable it to use Spearhead and the entire system more efficiently. Enbridge asserts that the Extension Pipeline also will increase volumes on the Lakehead System and produce quantifiable benefits for upstream shippers, including: (A) reduced batch pigging costs, (B) improved crude oil quality, (C) reduced costs because of faster transit times, (D) increased system security, and (E) rate benefits attributable to reductions in Lakehead surcharges.[3]

4. Enbridge cites the increasing crude oil production in western Canada and the Williston Basin, which it expects to rise to approximately 4.4 million barrels per day (bpd) by 2020. Enbridge adds that it expects much of this increased production to flow into the U.S., where refiners are reconfiguring refinery runs to process larger volumes of crude. However, Enbridge asserts that the increased volumes will saturate traditional markets for Canadian crude in the upper Midwest and Rockies, so western Canadian producers must develop new markets further south.

5. Enbridge explains that the Commission rejected its previous effort to establish a surcharge to recover the costs of the Extension Pipeline from the mainline shippers on EELP's Lakehead System. The Commission found that EELP failed to demonstrate sufficient benefits to the Lakehead mainline shippers to justify charging a rate that subsidizes construction of an affiliate's extension pipeline.[4] Therefore, continues

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[1]Enbridge states that current Spearhead capacity out of Flanagan is 125,000 bpd, but that will increase to 190,000 bpd by the first quarter of 2009, assuming timely commencement of service.

[2] Enbridge states that, on March 16, 2006, the Commission approved the tariff structure for Line 61 (the primary component of the Southern Access Mainline Expansion) as an uncontested Offer of Settlement. Enbridge cites *Enbridge Energy, Limited Partnership*, 114 FERC ¶ 61,264 (2006).

[3] *See* Joint Petition for Declaratory Order of Enbridge Energy Company, Inc. and Enbridge Energy, Limited Partnership, October 18, 2007, at 24-28.

[4] Enbridge cites *Enbridge Energy, Limited Partnership*, 117 FERC ¶ 61,279, at P 28 (2006) (2006 Settlement Order).

Enbridge, it worked with the Canadian Association of Petroleum Producers (CAPP) to develop the instant revised proposal (Tariff Agreement).[5]

Description of the Filing

6. Enbridge seeks approval of the overall tariff structure for the Extension Pipeline, but it does not ask the Commission to approve any specific rates for any year. Enbridge states that the Tariff Agreement provides that EEC will charge a cost-of-service-based, stand-alone tariff rate for transportation from Flanagan to Patoka. Enbridge, however, admits to some uncertainty as to when the Extension Pipeline will attain self-sufficiency.[6] For that reason, continues Enbridge, the Tariff Agreement provides a backstop mechanism if the Extension Pipeline does not attract sufficient volume to recover its cost-of-service in the early years.

7. The proposed rate structure contains the same input elements that Enbridge proposed previously in Docket No. OR06-11-000, but adds the following components:

A. Assumed throughput of 340,000 bpd.

B. At the beginning of each calendar year after commencement of service, EEC will calculate the revenue requirement of the Extension Pipeline using the same inputs and truing-up prior estimates to actual costs.

C. At the beginning of each year following the initial year, EEC will calculate the difference between the revenue actually calculated and the revenue requirement based on the specified parameters. If the actual revenue is less than the revenue requirement, there is deemed to be a deficit, and if the actual revenue exceeds the revenue requirement, there is deemed to be a surplus.

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[5] The Tariff Agreement is attached to the petition as Ex. 1. Enbridge points out that it obtained rate approval for other proposals: *Enbridge Energy, Limited Partnership*, 107 FERC ¶ 61,336 (2004); *Enbridge Energy, Limited Partnership*, 114 FERC ¶ 61,264 (2006) (Southern Access Settlement Order); *Enbridge Energy Co., Inc.*, 110 FERC ¶ 61,211 (2005); *Enbridge Pipelines (North Dakota) LLC*, 117 FERC ¶ 61,131 (2006); *Enbridge Pipelines (Southern Lights) LLC*, 121 FERC ¶ 61,310 (2007), *order on reh'g and clarification*, 122 FERC ¶ 61,170 (2008); *CCPS Transportation, LLC*, 121 FERC ¶ 61,253 (2007), *order on reh'g*, 122 FERC ¶ 61,123 (2008).

[6] Joint Petition for Declaratory Order of Enbridge Energy Company, Inc. and Enbridge Energy, Limited Partnership, October 18, 2007, at 4.

D. If, prior to becoming self-sufficient, EEC incurs a deficit, then EELP will impose a surcharge on all Lakehead shippers to recover that deficit in the subsequent year. If EEC achieves a surplus, it will pay that surplus to EELP, which will apply it as a surcredit to Lakehead shippers until accumulated deficits (with interest) have been repaid in accordance with the terms of the Tariff Agreement. (This is the backstop provision.)

E. To implement the backstop provision, EEC will track the cumulative deficits and surpluses in a balancing account. Deficits recovered through the Lakehead rates (with interest) will be debited to the account. Surpluses are credited to the account until the cumulative deficit is reduced to zero. Once the Extension Pipeline reaches self-sufficiency (defined as three consecutive years of surpluses), no more deficits can be recovered from Lakehead shippers. Thereafter, once the cumulative deficit reaches zero, any subsequent surpluses must be used to reduce the Extension Pipeline rates for the remaining term of the Tariff Agreement.[7]

8. Further, states Enbridge, prior to commencing service, EEC will calculate the initial rate using the Commission's Opinion No. 154-B methodology, estimated capital and operating costs, and the following identical inputs from the Docket No. OR06-11-000 proposal:

A. 55 percent equity and 45 percent debt;

B. Annual depreciation rate of 3.33 percent;

C. Cost of equity – 9 percent real;

D. Cost of debt equal to the weighted long-term average cost of debt of EELP;

E. Inflation rates in accordance with Opinion No. 154-B; and,

F. Tax allowance in accordance with the Commission policy in effect for that year.

9. Enbridge explains that it divided the first 15 years of the Extension Pipeline's operations into three five-year periods. Enbridge states that the first period begins at start-up, when Enbridge will calculate the pipeline's rates as described above. Enbridge further states that the second period, which Enbridge styles as the Self-Sufficiency Period, will begin when the Extension Pipeline experiences three successive years of

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[7] Enbridge acknowledges, however, that in certain narrow circumstances, a portion of the deficit charged to Lakehead shippers will not be debited to the balancing account.

surpluses. Enbridge adds that, once it enters this period, the pipeline can no longer recover any deficits from Lakehead shippers. Therefore, continues Enbridge, when EEC calculates the Extension Pipeline rates during the Self-Sufficiency Period, it will make up for any deficits by adjusting the Extension Pipeline rates, and will credit any surpluses against the cumulative deficit existing in the balancing account. EEC will then return any surpluses to Lakehead shippers in the form of a surcredit. Enbridge also states that, once it eliminates the cumulative deficit in the balancing account, the pipeline will enter the third and final period, the Zero Balance Period, in which the method for calculating the stand-alone rate will change because EEC will not need to repay the Lakehead shippers, and will use any revenue above the revenue requirement to reduce the rates for the following year. Finally, Enbridge states that, at the end of the 15-year term of the Tariff Agreement, EEC will set future rates based on the Commission's ratemaking standards then in effect, subject to carrying forward a credit for any surplus from the final year of the term.

10. Enbridge recognizes that use of the stipulated 340,000 bpd throughput (i.e., 85 percent of the initial annual average capacity of the line) for rate design represents an exception to the Commission's cost-of-service regulations.[8] However, Enbridge maintains that the deficit/surplus provisions of the Tariff Agreement will prevent EEC from over-recovering the agreed cost-of-service.[9] Despite the fact that EEC asks the Lakehead shippers to absorb the deficits temporarily in those early years, Enbridge maintains that this is not a "roll-in" of the Extension Pipeline costs.[10]

11. Enbridge forecasts a volume of 136,792 bpd for the Extension Pipeline during the initial nine months of operation in 2009, although it expects the projected volumes to decrease in the following two years to 91,809 bpd for 2010 and 98,358 bpd for 2011. However, continues Enbridge, increases in crude supply and a planned new pipeline connection to the U.S. Gulf Coast from Patoka will increase the volume to 271,422 bpd by 2012 and will surpass the 340,000 threshold level in 2012, rising to 628,904 bpd. Thereafter, Enbridge anticipates that volumes consistently will average above 340,000 bpd and continue to rise to maximum capacity of 800,000 bpd in 2017 and beyond. Enbridge also emphasizes that its more conservative alternative analysis reaches a similar result, with volumes surpassing 340,000 bpd by 2014.

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[8] Enbridge cites 18 C.F.R. § 346.2 (2007).

[9] Enbridge states that this discussion assumes that the estimated and actual cost-of-service in each year will be the same.

[10] Enbridge cites Joint Petition for Declaratory Order of Enbridge Energy Company, Inc. and Enbridge Energy, Limited Partnership, October 18, 2007, Ex. 4.

Notice, Interventions, Protest, and Answers

12. Notice of Enbridge's filing was issued on October 24, 2007, with comments and interventions due on November 16, 2007. On November 16, 2007, Flint Hills filed a motion to intervene and protest. CAPP intervened in support of the petition and filed an answer to Flint Hills' protest describing the existing transportation constraints and its role in negotiating the Tariff Agreement. On March 14, 2008, a group of land owners, citizens, and other entities (self-styled as Pliura Intervenors) filed a late motion to intervene and a protest. The following energy companies also filed letters in support of the petition: Astra Energy Canada Inc.; Canadian Oil Sands Limited; CANNAT Energy Inc.; Devon Canada Corporation; Nexen Marketing; Plains Marketing, L.P.; and Shell Canada Limited.

13. Enbridge filed a response to Flint Hills' protest, and Flint Hills filed an answer to the response. Enbridge also filed an answer to the motion to intervene and protest of the Pliura Intervenors. While the Commission's regulations generally prohibit answers to protests and answers to answers, in this case, the Commission will accept these responsive pleadings because they have provided additional arguments for the Commission's consideration in its review of the Enbridge petition. Those competing arguments are addressed in the Discussion section below.

14. The Pliura Intervenors state that they intervened in a contested matter before the Illinois Commerce Commission (ICC), Case #07-446, involving the proposed Extension Pipeline. Pliura Intervenors state that an entity known as Enbridge Pipelines (Illinois), L.L.C. (Enbridge Illinois) filed an application with the ICC on August 16, 2007, seeking issuance of a Certificate of Good Standing, authorization to construct, operate, and maintain approximately 170 miles of new 36-inch pipeline between Flanagan and Patoka, and the authority to exercise eminent domain. According to Pliura Intervenors, Enbridge Illinois did not inform the ICC that another entity would own, build, and operate the Extension Pipeline. Further, they state that they sought to identify any filings submitted to this Commission by Enbridge Illinois and only recently identified the instant case as relating to the proposed project between Flanagan and Patoka. Pliura Intervenors contend that there are significant differences between the ICC filing and the filing in the instant case with respect to the Enbridge entities that will construct and operate the facilities.

15. In its answer, Enbridge urges the Commission to deny the motion to intervene and protest of the Pliura Intervenors. Enbridge asserts that: (A) the motion to intervene is untimely and fails to demonstrate good cause for Pliura Intervenors' failure to intervene at an earlier time, (B) the Pliura Intervenors do not state any cognizable interest in this proceeding, and (C) the late intervention is unnecessary because Enbridge provides in its answer the clarification sought by the Pliura Intervenors.

16. The Commission will deny the Pliura Intervenors late intervention in this proceeding. Their principal objective is to obtain an explanation of the seeming inconsistencies in the ICC filing and the instant petition for a declaratory order. Enbridge explains in its answer that Enbridge Illinois is a single-member limited liability company created in 2006 and that EEC is the sole member of Enbridge Illinois. In other words, Enbridge states that the relationship is effectively one of parent company to wholly-owned subsidiary. According to Enbridge, the personnel involved in preparing the instant petition did not focus on the role of Enbridge Illinois because any activities performed by Enbridge Illinois are necessarily performed at the direction of its parent company, EEC. Thus, Enbridge confirms that Enbridge Illinois is the actual entity that will build, own, and operate the Extension Pipeline, and as a wholly-owned subsidiary of EEC, Enbridge Illinois will be bound by the Tariff Agreement and any Commission rulings in this proceeding. As Enbridge also pointed out, the Pliura Intervenors have not shown that their status as landowners gives them an interest in the rate treatment of the transportation of crude oil on the Extension Pipeline. Accordingly, as stated above, the Commission denies the late motion for intervention and protest of the Pliura Intervenors.[11]

17. In its protest, Flint Hills states that it receives heavy Canadian crude oil delivered via the Lakehead system to Clearbrook, Minnesota, and transports it to its refinery at Pine Bend, Minnesota. Flint Hills does not oppose construction of the Extension Pipeline, but argues that the proposed backstop mechanism is a thinly disguised effort to force Lakehead shippers to cross-subsidize the project by bearing all the risk of under-utilization and cost overruns even if they will not ship any crude oil on the Extension Pipeline. Flint Hills maintains that this is contrary to Commission policy and precedent and, further, would afford the Extension Pipeline an unfair advantage in transporting Canadian crude oil to new or expanded U.S. markets.

18. Flint Hills explains that even a small disparity between Enbridge's projections and the Extension Pipeline's actual throughput could mean that Enbridge would not fully repay Lakehead shippers. Flint Hills also explains that the Extension Pipeline could remain at its original capacity (400,000 bpd) if other projects are built, which would create a severe risk for Lakehead shippers, forcing them to subsidize the Extension Pipeline with several hundred million dollars and little, if any, hope of recouping the surcharges. According to Flint Hills, the mere possibility of deficit payback does not change the fact that the deficit surcharges are a subsidy, and in any event, the payback is not guaranteed because Enbridge admits that, after the 15-year term, it will not repay any remaining deficit at all. Flint Hills further points out that Enbridge bases its claim of

[11] However, the Commission expects that Enbridge will make clear the corporate relationships such as the one between EEC and Enbridge Illinois in all future regulatory filings.

repayment of the subsidy on three uncertain assumptions: (A) attaining proven crude oil production levels forecast by CAPP, (B) developing major new pipeline projects to generate additional throughput for the Extension Pipeline, and (C) the failure of other sponsors to complete competing projects that would draw volumes away from the Extension Pipeline.

19. Flint Hills also challenges Enbridge's claim that the subsidy is a "small price to pay" for the claimed benefits because it maintains that Lakehead shippers: (A) can realize these benefits without any throughput going through the Extension Pipeline because other projects are designed to move the Canadian crude oil to U.S. markets using the Enbridge mainline and (B) already have received the benefit of Enbridge's promise to batch pig crude volumes. Flint Hills also contends that, although shippers on other systems, producers, and refiners will not be the direct recipients, certain claimed benefits will inure to them.

20. In its response, Enbridge argues that its petition is ripe for decision and that Flint Hills has not suggested the need for further proceedings to develop the record. According to Enbridge, the parties disagree only with respect to matters of law and policy. Enbridge contends that the proposed surcharge is consistent with applicable Commission regulations and precedent, contrary to Flint Hills' claims. Enbridge also criticizes the analysis performed by a Flint Hills employee, asserting that it is inferior to the analysis performed by Enbridge's expert, which predicts that the surcharge applicable to the Lakehead shippers will be repaid with interest during the term of the Tariff Agreement. Finally, Enbridge seeks to refute Flint Hills' claims that the benefits are insufficient or speculative.

21. In its answer to Enbridge's response, Flint Hills submits that the lack of shipper commitments demonstrates that market conditions do not justify the constuction of the Extension Pipeline at this time and that Enbridge merely seeks an unfair competitive advantage over competing pipelines. According to Flint Hills, the fact that other Lakehead shippers do not oppose the petition does not require the Commission to approve it. Flint Hills further maintains that the "loan" is a subsidy, regardless of whether it is paid back. Finally, Flint Hills refutes certain of Enbridge's assertions that the promised benefits will benefit all Lakehead shippers.

Discussion

22. The crucial facts in this proceeding are Enbridge's admissions that not all Lakehead shippers who would be subject to the surcharge will use the Extension

Pipeline[12] and that there is no guarantee that the Lakehead shippers will be repaid the surcharges collected from them.[13] In fact, as Flint Hills has pointed out, the "loan" is a subsidy regardless of whether it is paid back.[14]

23. Accordingly, as discussed below, the Commission denies the petition for declaratory order. The proposed backstop mechanism would create an improper cross-subsidy that would require the Lakehead mainline shippers to bear the risk of underutilization of the Extension Pipeline over the 15-year term of the Tariff Agreement with no guarantee the mainline shippers would recover all surcharge amounts. In contrast, the backstop would ensure that Enbridge and the Extension Pipeline shippers would face no such risk during the 15-year term. Moreover, the potential benefits to the Lakehead shippers asserted by Enbridge are too speculative and otherwise inadequate to persuade the Commission to allow Enbridge to shift the financial risk of the Extension Pipeline to Lakehead's mainline shippers.

A. <u>The 2006 Settlement Order</u>

24. The 2006 Settlement Order addressed an offer of settlement filed by EELP and claimed to be within the Facilities Surcharge Framework approved by the Commission on

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[12] Response of Enbridge Energy Company, Inc. and Enbridge Energy, Limited Partnership to the Motion to Intervene and Protest of Flint Hills Resources, LP, December 3, 2007, at 2 n.2 ("not all Lakehead shippers will necessarily ship on the Extension. . . .").

[13] *Id.* at 18. (It is "highly likely" that Lakehead shippers will be repaid.)

[14] Flint Hills cites other significant facts relevant to this petition, namely that Enbridge:

A. unsuccessfully attempted to obtain ship-or-pay throughput commitments to support construction of the Extension Pipeline,

B. projects underutilization of the pipeline for four-to-five years,

C. proposes to finance the deficits resulting from such underutilization with a "loan" from Lakehead shippers (i.e., the backstop mechanism) that it may or may not repay with interest, and

D. will not build the Extension Pipeline if it is forced to follow the same rules as all the other competing pipelines (i.e., pipeline absorbs risk of underutilization or shares it with shippers via ship-or-pay contracts).

June 30, 2004.[15] EELP sought to implement a surcharge that would allow it to recover a portion of the costs of the Extension Pipeline from all shippers on the Lakehead System, even though EELP acknowledged that not all shippers would use the Extension Pipeline.[16]

25. In the 2006 Settlement Order, the Commission cited the potential benefits to Lakehead shippers claimed by EELP, including the following: (A) improved ability to bring Canadian crude oil into the U.S.,[17] (B) a system-wide reduction in the tariff rates that otherwise would apply to Lakehead mainline shippers,[18] and (C) increased netback prices to producers.[19] In that order, the Commission examined the manner in which EELP proposed to recover the Extension Pipeline's cost-of-service by means of a joint Lakehead-Extension Pipeline tariff and a surcharge applied to the Lakehead mainline shippers.[20] Specifically, EELP proposed to recover the net unrecovered Extension Pipeline cost-of-service and true-up the surcharge annually, with the surcharge remaining in effect for the projected 30-year depreciable life of the new facilities.[21]

26. The protesting parties, including Flint Hills, supported the proposed additional pipeline capacity, but objected to the surcharge that would apply to all Lakehead mainline shippers, including those that would not use the Extension Pipeline.[22] The Commission concluded in the 2006 Settlement Order that EELP failed to provide sufficient evidence to demonstrate that its proposal would produce just and reasonable rates, largely because the surcharge would apply to all Lakehead shippers, despite the undisputed fact that not all Lakehead shippers would use the Extension Pipeline.[23] Finally, the Commission

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[15] *Enbridge Energy, Limited Partnership*, 107 FERC ¶ 61,336 (2004).

[16] *See Id.* at P 1-2.

[17] *Enbridge Energy, Limited Partnership*, 117 FERC ¶ 61,279, at P 8 (2006).

[18] *Id.* P 9.

[19] *Id.* P 10.

[20] *Id.* P 13.

[21] *Id.* P 13-14.

[22] *Id.* P 15-22.

[23] *Id.* P 25-26.

stated that EELP also failed to quantify its predictions of system-wide benefits, such as improved distribution, improved crude quality, and reduced transit time.[24]

27. Enbridge's petition for a declaratory order in the instant proceeding thus represents its second attempt to require the Lakehead mainline shippers to provide financial support for construction of the Extension Pipeline. However, as stated above, Enbridge again has failed to justify requiring the Lakehead mainline shippers to bear the financial risk of the project.

B. Commission Policy and Precedent

28. Although they differ in their interpretations of Commission policy and precedent, both Flint Hills and Enbridge generally agree that surcharges may be appropriate to fund the construction of new facilities in certain situations. However, they continue to disagree as to whether the Commission should permit Enbridge to impose the instant surcharge on the Lakehead mainline shippers that will not use the Extension Pipeline. Enbridge argues that the benefits to all Lakehead shippers would offset what it characterizes as the minor burden of the surcharge, while Flint Hills contends that the claimed benefits are insufficient to support imposition of the proposed surcharge.

29. Both Flint Hills and Enbridge rely on Order Nos. 561 and 561-A.[25] Flint Hills asserts that the regulations adopted pursuant to these orders prohibit the imposition of such a surcharge on top of the pipeline's indexed rates.[26] Enbridge, on the other hand, argues that the regulations do not preclude this type of surcharge and that the Commission is not limited by the rate methodologies established in the regulations when circumstances warrant a departure from those defined methodologies.[27]

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[24] *Id.* P 28.

[25] *Revisions to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, Order No. 561, FERC Stats. & Regs. ¶ 30,985 (1993), *order on reh'g*, Order No. 561-A, FERC Stats. & Regs. ¶ 31,000 (1994), *aff'd, Association of Oil Pipelines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996).

[26] Flint Hills cites 18 C.F.R. § 342.4 (2007); *Express Pipeline Partnership*, 76 FERC ¶ 61,245, at p. 62,250 (1996).

[27] Enbridge cites *Colonial Pipeline Co.*, 119 FERC ¶ 61,183, at P 23 (2007).

30. Flint Hills and Enbridge also point to the Commission's natural gas pipeline rate design policy.[28] Flint Hills contends that the rationale of prohibiting natural gas pipelines from forcing existing customers to subsidize the construction of an expansion for the sole benefit of new customers applies to oil pipeline expansions as well. Flint Hills acknowledges, however, that the gas policy recognizes limited exceptions for projects designed to improve service to existing customers by replacing existing capacity, improving reliability, or providing additional flexibility.[29] Flint Hills also emphasizes that the cases decided under the gas policy involve new facilities added to integrated systems,[30] and it asserts that the Commission never has allowed a pipeline to force existing customers to pay for a stand-alone, downstream extension, particularly when constructed by an affiliate.[31] In contrast, continues Flint Hills, in the instant case, Enbridge seeks to shift the entire risk of under-recovery to the Lakehead mainline shippers for a lengthy period, so there is no incentive for the pipeline sponsors to control costs or to construct an efficient pipeline system. The arrangement Enbridge seeks also may interfere with market forces by preventing the construction of other, more efficient pipelines.[32]

31. Enbridge disagrees that natural gas pipeline precedent is relevant to this case, citing the common carrier status of oil pipelines.[33] In any event, continues Enbridge, Flint Hills admits that the gas pipeline policy recognizes that there is no subsidy when

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[28] Flint Hills cites *Certification of New Interstate Natural Gas Pipeline Facilities*, 88 FERC ¶ 61,227, at p. 61,746 (1999), *order on clarification*, 90 FERC ¶ 61,128 (2000), *order on clarification*, 92 FERC ¶ 61,094 (2000).

[29] Flint Hills cites *Certification of New Interstate Natural Gas Pipeline Facilities*, 88 FERC ¶ 61,227, at p. 61,746 (1999).

[30] Flint Hills cites, *e.g.*, *Tennessee Gas Pipeline Co.*, 80 FERC ¶ 61,070, at p. 61,214 (1997).

[31] *Id.* at 61,216.

[32] Flint Hills cites *Certification of New Interstate Natural Gas Pipeline Facilities*, *order on clarification*, 90 FERC ¶ 61,128, at p. 61,392 (2000).

[33] Enbridge cites *SFPP, L.P.*, 104 FERC ¶ 61,163, at P 9 (2003). *Colonial Pipeline Co.*, 119 FERC ¶ 61,183, at P 23 (2007); *see also SFPP, L.P.*, 102 FERC ¶ 61,089, at P 18 (2003) (applying Commission policies governing oil pipeline rates rather than natural gas pipeline policies to decide issues regarding rolled-in vs. incremental rates).

there are offsetting benefits,[34] and this principle also is reflected in the Commission's oil pipeline precedents, including the 2006 Settlement Order.[35]

32. The parties further dispute the applicability of several oil pipeline cases addressing expansions of facilities: *SFPP, LP* (*SFPP*),[36] *Colonial Pipeline Co.* (*Colonial*),[37] and *Plantation Pipe Line Co.* (*Plantation*).[38] In general, Flint Hills distinguishes these cases, asserting that they do not support the imposition of a surcharge on another pipeline's shippers that will not use or benefit from the expansion at issue. However, Enbridge argues that these cases support its claim that the Commission has considerable latitude in fashioning methodologies that produce just and reasonable rates and, therefore, should accept the proposed backstop mechanism.

33. Enbridge also relies on *Calnev Pipe Line LLC* (*Calnev*),[39] *Enbridge Pipelines (North Dakota) LLC* (*Enbridge North Dakota*),[40] and *Enbridge Energy, Limited Partnership* (*EELP*).[41] Flint Hills responds that *Calnev* involved the addition of a 16-inch pipeline installed parallel to the existing 24 miles of 8-inch and 14-inch pipelines to alleviate a growing constraint on the existing mainline infrastructure, and all parties agreed that this mainline expansion was necessary to serve growing markets and avoid prorationing of existing customers.[42] Flint Hills further contends that the other two cases cited by Enbridge involved unanimous settlement agreements with no protesting parties; therefore, these cases may not be considered precedent.

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[34] Enbridge cites *Chandeleur Pipe Line Co.*, 108 FERC ¶ 61,181, at P 8 n.5 (2004) ("It is not subsidization for existing customers to pay for facilities from which they will benefit.").

[35] *Enbridge Energy, Limited Partnership*, 117 FERC ¶ 61,279, at P 25 (2006).

[36] 102 FERC ¶ 61,089, *order on reh'g*, 104 FERC ¶ 61,163 (2003).

[37] 116 FERC ¶ 61,078, at P 54 (2006).

[38] 98 FERC ¶ 61,219 (2002).

[39] 120 FERC ¶ 61,073 (2007).

[40] 117 FERC ¶ 61,131 (2006).

[41] 114 FERC ¶ 61,264 (2006).

[42] *Id.* P 18.

34. It is unnecessary to address cases involving the Commission's natural gas rate design policy because the Commission concludes that existing oil pipeline precedent supports its rejection of the proposed backstop agreement. In *SFPP*, the Commission addressed the question of rolled-in versus incremental rates applicable to expanded pipeline capacity. However, the proposal in *SFPP* applied to current and potential new shippers on the same pipeline; there was no issue of the shippers on one line subsidizing the construction of facilities on a separate pipeline that they would not use, as is the case here.[43]

35. Similarly, in *Colonial*, the pipeline proposed to expand existing facilities to alleviate capacity constraints on the portion of its system between Baton Rouge, Louisiana, and Atlanta, Georgia. Colonial sought Commission authorization to recover the expansion costs through its existing grandfathered rates and a uniform rate component (URC) surcharge that would apply to all barrels originating at Gulf Coast origins and delivered beyond Baton Rouge.[44] *Colonial* did not involve a pipeline seeking to impose the costs of its expansion on the shippers on another pipeline.

36. *Plantation* involved the pipeline's mainline extension into a separate market area in Chattanooga, Tennessee. Rather than seeking to charge all Plantation shippers for the extension, Plantation proposed that an affiliate construct the new line as a separate, stand-alone pipeline extension with separate local and joint tariffs to recover the full cost-of-service only from shippers that used the new line. As in *SFPP* and *Colonial*, *Plantation* did not propose to place the financial risk on shippers that would not use the expansion facilities.[45]

37. In *Calnev*, the Commission approved a URC similar to that accepted in *Colonial*. However, it applied equally to all interstate barrels shipped because it would benefit all of Calnev's mainline shippers. The Calnev URC was not intended to require shippers on a different pipeline to subsidize and bear the financial risk of the expansion facilities.[46] Rather, the Calnev URC was paid only by shippers that would benefit from the expanded pipeline facilities. Additionally, as Flint Hills points out, *Enbridge North Dakota* and *EELP* involved uncontested settlements and are not considered Commission precedent.

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[43] *SFPP, LP*, 102 FERC ¶ 61,089, at P 14-18, *order on reh'g*, 104 FERC ¶ 61163, at P 8-12 (2003).

[44] *Colonial Pipeline Co.*, 116 FERC ¶ 61,078, at P 54-57 (2006), *order denying reh'g*, 119 FERC ¶ 61,183, at P 13-19 (2007).

[45] *Plantation Pipe Line Co.*, 98 FERC ¶ 61,219, at p. 61,865-66 (2002).

[46] *Calnev Pipe Line LLC*, 120 FERC ¶ 61,073, at P 13, 30 (2007).

38. Accordingly, the relevant precedent stands for the proposition that shippers expected to benefit from an expansion may share in the financial risk of such an expansion. However, where, as here, shippers who may not benefit from an expansion are required to bear financial risk associated with such expansion, such shippers would be providing a cross-subsidy to the Extension Pipeline shippers, which is inconsistent with Commission policy. Whether the Extension Pipeline provides sufficient benefits to all Lakehead shippers so as to avoid a cross-subsidy is considered further below.

C. Benefits

39. The parties disagree with respect to value and certainty of the benefits that Enbridge claims will flow to the Lakehead shippers as a result of the construction of the Extension Pipeline. Enbridge asserts that these benefits will offset the "minor burden" to the Lakehead mainline shippers, but Flint Hills responds that the benefits Enbridge now predicts largely repeat the claimed benefits associated with the previously-proposed surcharge rejected by the Commission in the 2006 Settlement Order.[47] Flint Hills further argues that there are no changed circumstances that require a reversal of the Commission's order rejecting the previous settlement.

40. As stated above, Flint Hills contends that three of the five claimed benefits (reduced pigging costs, reduced transit time, and reduced surcharges) assume that the Lakehead system will achieve throughput levels made possible by EELP's Southern Expansion Project that increased mainline capacity to 1.2 million bpd and was funded by a surcharge on Lakehead shipper rates approved in Docket No. OR06-3-000. Flint Hills observes that it did not oppose that project, in recognition of the overall system benefits that would inure to all Lakehead mainline shippers, including Flint Hills. Flint Hills also emphasizes that Enbridge quantified essentially all the benefits claimed here, including reduced pigging costs, reduced transit time, improved quality, improved flexibility and security, and the surcharge reduction, in its previous effort to require the Lakehead mainline shippers to finance the Extension Pipeline project, as described in the 2006 Settlement Order. In addition, emphasizes Flint Hills, this proposal would require the Lakehead shippers to subsidize a larger percent of the Extension Pipeline's revenue requirements than did the previous similar proposal.[48]

41. Enbridge responds that, while some of the mechanisms for realizing incremental benefits were established in the context of the Southern Expansion Project cases, it cannot achieve these benefits without the Extension Pipeline. Enbridge admits that

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[47] Flint Hills cites *Enbridge Energy, Limited Partnership*, 117 FERC ¶ 61,279 (2006).

[48] *See* Protest and Motion to Intervene of Flint Hills Resources, LP on Joint Petition for Declaratory Order, November 16, 2007, at 21-22.

shippers on the previously-approved Expansion expressly agreed to bear the incremental operating costs of that line, of which batch pigging is a component. However, Enbridge contends that, by generating incremental volumes on that expanded line, the Extension Pipeline proposed here will reduce the length of time when Enbridge will require batch pigging and thereby relieve the Lakehead mainline shippers of those costs.

42. Enbridge also asserts that reduced transit time on the mainline system will be a direct result of the incremental throughput generated by the Extension Pipeline. Further, continues Enbridge, Flint Hills does not dispute that the existence of the Extension Pipeline will make it possible to improve the quality of crude moving on the Lakehead and Mustang systems. However, Enbridge admits that Flint Hills would not necessarily share in this benefit.[49]

43. Enbridge contends that the Extension Pipeline will provide Lakehead shippers with additional flexibility and reliability by providing alternative routes into and out of Chicago, Illinois, and improved operational security in case of outages on certain other pipelines for U.S. and Ontario refiners. Further, Enbridge asserts that the Extension Pipeline adds the incremental throughput to trigger expansion of Line 61 above 400,000 bpd and potentially up to 1.2 million bpd, and that is what will create the surcharge benefit to Lakehead's mainline shippers.

44. Flint Hills submits that Enbridge is building the Extension Pipeline ahead of the market, so the surcharges will distort the market by allowing Enbridge to obtain a competitive advantage without taking any risks or being tied to minimum throughput commitments. Enbridge responds that it does not seek an unfair advantage, and no other competing pipelines have expressed such a concern. Enbridge asserts that it is merely responding to market demand by creating additional capacity.

45. Flint Hills claims that Enbridge's proposal for treatment of the surcharge revenue as a "cost" rather than as revenue is contrary to the mechanics of a surcharge mechanism. Enbridge responds that its proposed treatment of the surcharge/surcredit amounts for FERC Form No. 6, Page 700 purposes allows the regulatory reporting to reflect the rate treatment and avoid distortion of Page 700's comparison of costs and revenues.

46. Finally, Flint Hills submits that there are other ways that would allow Enbridge to defer cost recovery in the early years without a subsidy. For example, Flint Hills asserts that, in the context of project-financed pipelines, a proposed tariff rate based on 85-percent utilization represents an appropriate sharing of the risk of underutilization

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[49] Response of Enbridge Energy Company, Inc. and Enbridge Energy, Limited Partnership to the Motion to Intervene and Protest of Flint Hills Resources, LP, December 3, 2007, at 27. ("Although Flint Hills would not necessarily share in this benefit, there is no question that some Lakehead shippers would.").

between the pipeline and its shippers rather than shifting the risk to Lakehead mainline shippers. Flint Hills also maintains that the Commission previously allowed pipelines to defer recovery of costs during start-up periods when full throughput is not available.[50] Additionally, Flint Hills suggests that Enbridge could employ a levelized rate to reduce the impact of underutilization during the early years and that it could defer recovery of the depreciation expense until volumes increase. Flint Hills maintains that Enbridge could seek throughput commitments from prospective Extension Pipeline shippers to backstop the risk of underutilization.

47. Enbridge replies that Flint Hills' proposal, to have Enbridge assume all of the risk of the Extension Pipeline is unrealistic because, as a regulated entity, there is no upside potential in later years for Enbridge. Enbridge explains that deferring recovery of costs to later years or levelizing depreciation would require a waiver of the Commission's Opinion No. 154-B cost-of-service approach and would lead to decreased net income for the pipeline for a significant period, which would negatively impact its ability to proceed. Enbridge states that it initially sought shipper volume commitments for the Extension Pipeline, but the shippers were reluctant to provide long-term volume commitments that would lock them into a particular movement when other shippers would retain the flexibility to change volumes and destinations on a month-to-month basis.

48. It is clear from the arguments advanced by the parties that the alleged benefits generally are speculative and appear to some degree dependent on future events over which Enbridge does not have full control, such as the construction or lack thereof of other pipeline facilities, and its ability to attract the volumes it projects. For example, Enbridge admits that it cannot predict when or if the Extension Pipeline will achieve self-sufficiency, i.e., three consecutive years of surpluses. At best, Enbridge can only state that it is "highly likely" that the Lakehead mainline shippers will recover the surcharges they would be required to pay, regardless of whether they actually will utilize the Extension Pipeline. Further, as Flint Hills points out, Enbridge assumes that another pipeline will be built from Patoka to the U.S. Gulf Coast, but there is a risk that any such pipeline project could be delayed or abandoned if a competing pipeline is built. Likewise, Flint Hills points out that several other potentially competing pipelines may be constructed. In any event, the Commission agrees that it is unreasonable to place the risk of potential construction or non-construction on the Lakehead shippers, particularly in light of the fact that not all such Lakehead shippers will utilize the Extension Pipeline. It is telling that Enbridge could not obtain shipper commitments to provide the necessary support for construction of the Extension Pipeline, and it is unwilling to bear the financial risk itself. Enbridge's proposal in this proceeding represents a cross subsidy, despite its claim that various benefits will accrue to the Lakehead shippers.

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[50] Flint Hills cites *Iroquois Gas Transmission System, L.P.*, 52 FERC ¶ 61,091 (1990).

D. Conclusion

49. This filing represents Enbridge's second effort to impose a surcharge on all Lakehead shippers to finance the construction of facilities that it admits will not be used by all such shippers. That flaw in the first filing has not been cured by this new filing. Enbridge focuses on the Commission's statement in the 2006 Settlement Order that EELP had not quantified the benefits it claimed,[51] and Enbridge attempts to provide such evidence in this filing. However, Flint Hills' objections to that evidence have merit, and Enbridge still fails to show that extracting a surcharge from the shippers on another pipeline (at least one of which admittedly would not use the Extension Pipeline) to finance the Extension Pipeline would be just and reasonable.

50. The Commission has ample authority to fashion rates and unique rate structures in appropriate cases; however, the Commission still must determine that those rates and rate structures are just and reasonable. In this case, the Commission cannot conclude that the surcharge Enbridge proposes to impose on all Lakehead shippers is just and reasonable. As discussed above, Commission precedent does not support the ruling that Enbridge seeks. When a pipeline proposes to expand its facilities, it may, in appropriate circumstances, require the shippers that will use the facilities to bear some or all of the financial risk of the facilities. The potential cost/benefit relationship must be clear in such instances. In this case, Enbridge lacks shipper commitments, and it is uncertain when, if ever, the surcharges will be repaid to the Lakehead shippers and whether the "benefits" to the Lakehead mainline shippers expressed by Enbridge will be realized. Accordingly, the Commission denies the requested declaratory order.

The Commission orders:

(A) The petition for a declaratory order is denied, as discussed in the body of this order.

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[51] *Enbridge Energy, Limited Partnership*, 117 FERC ¶ 61,279, at P 28 (2006).

(B) Pliura Intervenors' motion to intervene and protest is denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.