

expressed concern about affiliated pipelines that cross the U.S. and Canadian borders. These companies argued that under the exception proposed by the Major Issues Analysis, affiliated pipelines that cross or interconnect at the U.S. and Canadian borders would fall within the definition of Energy Affiliate. The commenters argued that they should be treated as affiliated pipelines because their operations are closely coordinated and transmission services are shared even though they cross the international border. The Commission agrees and will permit these companies to share their transmission function activities and coordinate along both sides of the border as long as neither of the Transmission Providers shares employees or information with any of its Marketing or Energy Affiliates.

6. Affiliates Buying Power for Themselves

63. Several commenters, including Dominion, Calpine and KM, argued that the Commission needs to clarify the definition of Energy Affiliates because including the terms "buy," "sell," or "administer" could be construed to include an affiliated entity that is purchasing power for its own consumption, such as a communications affiliate that is purchasing power to heat its office building. They argued that under the NOPR, if an affiliate is simply "buying" power for its own energy consumption and not using the affiliated Transmission Provider for transmission, the Transmission Provider would be required to post the organizational charts and job descriptions for the Energy Affiliates, which the commenters argue would be burdensome.

64. In response to these comments, the Major Issues Analysis recommended that the Commission exclude an affiliate of a Transmission Provider that is purchasing electricity or natural gas for its own consumption and is not using an affiliated Transmission Provider for transmission.

65. Although these purchases can have an impact on the energy markets, nonetheless, there is little potential for competitive harm if the definition of Energy Affiliates is clarified to exclude any affiliate of the Transmission Provider that is solely purchasing power or natural gas for its own consumption and is not using an affiliated Transmission Provider for transmission. Therefore, the Commission will adopt this recommendation in the Final Rule. However, this exception is not intended to create a loophole that circumvents

the intent of rule, and does not apply to Energy Affiliates that use natural gas or power to produce another source of energy, e.g., generation affiliates.

7. Producers, Gatherers, and Processors

66. The NOPR defined Energy Affiliate to include producers, gatherers and processors. The NOPR states that whether a producer or gatherer is making an on-system sale or an off-system sale, it is still competing for access to the interstate transmission system. NGA stated that upstream services and transportation services are frequently offered as a single package by pipelines or their affiliates, which allows a pipeline to leverage its market power in the transportation market to gain an advantage in the upstream market. The comments regarding affiliated producers, gatherers, and processors were mostly included in the comments about affiliated LDCs. Commenters, including El Paso Energy Partners, Shell Offshore and Shell Gas, argued that: (1) The Commission does not have jurisdiction over producers, gatherers or intrastate pipelines; (2) there is no evidence to support eliminating the exemption granted under Order No. 497; (3) to require separation would cause unnecessary duplication of employees and gas control facilities, resulting in additional costs to customers;³² and (4) restrictions on communication would impair reliability.

67. The Commission is adopting the proposed regulation. The Commission is not asserting jurisdiction over the producers, gatherers or processors. The Commission has ample authority to ensure that the interstate pipeline treats all customers, affiliated and unaffiliated, on a non-discriminatory basis by regulating the behavior of the Transmission Provider. Staff's review of the October 2003 Index of Customers indicates that 14 interstate natural gas pipelines transport gas for their production and gathering affiliates, which hold an average of 46% of the affiliated pipelines' capacity. But, unlike LDCs, producers, gatherers and processors are not generally subject to state regulation.

68. Several commenters argue that Section 1 of the NGA makes production and gathering subject to regulation by the states and not the Commission. The Commission is not asserting jurisdiction over producers, gatherers or processors. The Commission has ample authority to ensure that the Transmission Provider

treats all customers, affiliated and non-affiliated, on a non-discriminatory basis by regulating the conduct of the transmission provider's interactions with affiliated producers, gatherers or processors.

69. The commenters voiced practical concerns about how the proposed standards of conduct would impact communications between a Transmission Provider and affiliated producers, gatherers, and processors. During the May 21 Conference there was much discussion about the possibility that expanding the standards of conduct would harm deepwater operations and future off-shore development efforts. Several participants stated that competing producers had worked cooperatively on affiliated pipelines to develop deepwater gas reserves. On the other hand, BP argued that Transmission Providers should not be permitted to share any information regarding a shipper's use of the pipeline or information regarding the operations or customers of non-affiliated gatherers that compete with the affiliate. BP argued that the definition of Energy Affiliate should not include affiliate gas processing plants. However, as discussed in more detail below, the Commission is permitting transmission providers to share crucial operational information with certain of its Energy Affiliates.

70. Commenters also argued that there was no evidence that pipelines had unduly favored their producers, gatherers or processing affiliates. However, in a recent example, Transcontinental Gas Pipe Line Corporation and its gathering affiliate, Williams Field Services Company, acted as one entity for purposes of gathering and transporting natural gas in interstate commerce in a monopolistic fashion and abused their market power.³³

71. The Commission's focus is to ensure comparability of service. To retain a loophole that permits the transmission provider to share employees or give its affiliated producers, gatherers or processors preferential information is inconsistent with the Commission's goal of non-discriminatory interstate transmission service. Producers that are selling energy are competing with other non-affiliated shippers for access to the pipelines' transmission systems. Whether a producer is selling gas from its own production or from the production of another, it is competing

³² A discussion of the commenters' concerns regarding additional costs is included in the Independent Functioning discussion, below.

³³ *Shell Offshore Inc. v. Transcontinental Gas Pipe Line Corp., et al.*, 100 FERC ¶ 61,254 (2002), order on reh'g, 103 FERC ¶ 61,177 (2003), appeal filed June 27, 2003 (D.C. Cir. No. 03-1179).