**UNITEDSTATESOFAMERICA**
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**FEDERALENERGYREGULATORYCOMMISSION**

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| **StandardsofConductforTransmission Providers** | ) ) | **DocketNo.RM01 -10-000** |

# COMMENTSOF SHELLOFFSHOREINC.

Pursuanttothe Notice of Proposed Rulemaking ("NOPR") issuedon September27, 2001,inthecaptionedproceeding, [1] ShellOffshoreInc.("SOI")herebysubmitsthefollowing comments.

## COMMUNICATIONSANDCORRESPONDENCE

Communications and correspondence concerning these comments should be directed tothefollowing:


CharlesJ.McClees,Jr.
ShellOilCompany
P.O.Box576
Houston,Texas77001
(281)544 -4516

StewartJ.Kepper
ShellOilCompany
P.O.Box576
Houston,Texas77001
(281)544 -3235

and

KevinM.Sweeney
John&Hengerer
120017thS treet,N.W.
Suite600
Washington,D.C. 20036
(202)429 -8802


[1] *StandardsofConductforTransmissionProviders* ,DocketNo.RM01 -10-000,IVFERC¶ 32,555(2001).

## SUMMARY OF POSITION

SOI vigorously opposes the proposal to eliminate the exemption from the Standards of Conduct ("Standards") that has applied to interstate pipelines' activities involving sellers that sell gas solely from their own production under Section 161.2(c)(1) of the Commission's Regulations ("the Producer Exemption").[2] The Producer Exemption has applied since the original adoption of the marketing affiliate regulations in 1988. The Commission has repeatedly revisited and reaffirmed the Producer Exemption, and it should do so again in this proceeding.

None of the reasons cited in the NOPR for expanding the definition of marketing affiliate to include "all energy affiliates" applies to the Producer Exemption. Indeed, the NOPR does not suggest *any* reason for eliminating the exemption. It simply states the Commission's intent to do so. There is no record support for elimination of this exemption. The calls for expansion of the applicability of the Standards, and the Commission's discussions of its concerns, relate to new types of affiliated entities such as generators, financial affiliates and risk managers. Producer affiliates, in contrast, are not a new phenomenon, as evidenced by the adoption of the Producer Exemption in the original marketing affiliate regulations 13 years ago.

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[2] References in these comments to the "Producer Exemption" are intended to mean the exemption in the current marketing affiliate rules for transportation of an affiliated producer's own production as set forth in Section 161.2(c)(1) and described in more detail below. The current Standards apply to pipelines only if they conduct transportation transactions with marketing or brokering affiliates. In contrast, the NOPR would evidently apply the revised Standards of Conduct to pipelines with Energy Affiliates, including affiliated producers, even if the pipeline does not transport gas for the affiliate in question. Thus, for purposes of these comments, the "Producer Exemption" that SOI seeks to preserve would also apply if the pipeline does not conduct any transportation transactions with its producer affiliate.

Particularly for producers on the deepwater Outer Continental Shelf ("OCS") affiliated with OCS pipelines, the Producer Exemption permits producers to engage in essential communications with affiliated pipelines that reflect the challenges posed by exploring for, developing and producing gas reserves on the OCS, and by day-to-day operation on the OCS. Contemporaneous disclosure of these communications would impose significant burdens on both the pipeline and the producer affiliate. Affiliated producers would be hindered in their ability to engage in essential communications with their affiliated pipelines, with no corresponding benefit. This is especially true when the affiliated producer is the point operator at an offshore receipt point on the affiliated pipeline's system. Extending the affiliate rules to hinder communications in such situations would tend to reduce the competition that has already been fostered by existing affiliated pipelines on the OCS. In addition, applying the Standards to OCS pipelines' dealings with affiliated producers would not advance any of the pro-competitive purposes of the Standards. The proposed rule would penalize those offshore exploration and production companies that have invested in necessary transportation systems. The proposed rule would place these producers at a competitive disadvantage relative to exploration and production companies that did *not* undertake these investments but now use these transportation systems.

The Commission absolutely must not place a percentage or quantity limit on the amount of capacity a producer can hold on an affiliated pipeline. In particular, deepwater OCS producers that rely upon affiliated pipelines to transport their production from

production areas should not be hamstrung by arbitrary rules limiting their capacity rights on those pipelines simply due to the affiliate relationship.[3]

Similarly, the Commission should not require disclosure of communications between a producer and an affiliated pipeline regarding capacity expansions or new greenfield pipeline projects. Such a requirement would require disclosure of proprietary and competitively sensitive information, and be cumbersome, disadvantaging the affiliated producer relative to competing producers and other parties whose communications would not be subject to similar disclosure rules.

In addition, the Commission must not prohibit pipeline and affiliated producer employees from communications in connection with the safe and reliable operation of connecting facilities consistent with common industry practice, and also must not burden these parties with cumbersome disclosure requirements related to such communications.

The interests of the marketplace and gas consumers are best served by regulatory policies that encourage exploration, development and production of gas from promising areas such as the deepwater OCS. SOI respectfully submits that the regulations proposed in the NOPR would hinder OCS exploration and development, contrary to the interests of consumers in obtaining adequate supplies of natural gas at reasonable prices, and contrary to the national interest in achieving greater energy security.

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[3] These comments focus on the particular hardships the NOPR would pose for OCS *deepwater* producers affiliated with pipelines that transport those producers' deepwater gas on the OCS to shore, including pipelines in shallower, closer-in offshore areas that were nonetheless constructed to provide transportation for deepwater gas making its way to onshore areas. However, *all* OCS producers would be faced with the same problems if the Commission were to adopt the NOPR as proposed. Therefore, the Producer Exemption

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shouldcontinueapplyataminimumtoallOCSproductionbyproducersaffiliatedwithOCS pipelines.

## INTRODUCTION

SOI's principal business is exploration, development and production of oil and natural gas. SOI's goal is to maximize oil and gas production and ultimate recovery of hydrocarbon reserves in a safe and commercially viable manner. SOI's activities include exploration and development of subsurface reservoirs underlying the Gulf of Mexico on the OCS, production of oil and gas from those formations, and other related activities necessary for delivery of natural gas and oil to interstate pipelines for transportation to markets.

SOI's exploration and production business is distinct from the pipeline business of its affiliated pipeline Shell Gas Transmission, LLC ("SGT"). SGT provides natural gas gathering and transportation service for shippers, both affiliated and non-affiliated.

Producers have spent billions of "at risk" dollars developing OCS properties, particularly in deepwater areas. Producers have explored for oil and gas in the deeper waters of the Gulf since the late 1970s. For many years, deepwater development was largely considered uneconomic. The costs of a fixed production platform increased exponentially with water depth. As those costs became prohibitive, new technology (*e.g.*, tension leg platforms) was developed to make deepwater production economically viable.

In 1989, less than three percent of the oil produced in the Gulf of Mexico was from deepwater projects. Since the early 1990s, however, a combination of significant new discoveries, legislated deepwater royalty relief, and advances in deepwater production systems have transformed the deepwater region of the Gulf into one of the nation's most

prolific and competitive areas for exploration and development.[4] Production of deepwater gas reserves has required new production technology.[5] For some time SOI has been, and remains today, at the forefront of cutting-edge deepwater tension leg platform ("TLP") and subsea production technology. Moreover, SGT has been and remains today at the vanguard of pioneering technological advancements in deepwater transportation technology.

The NOPR proposes new standards of conduct regulations that would apply uniformly to natural gas pipelines and transmitting public utilities ("transmission providers") currently subject to the gas pipeline Standards of Conduct (Part 161 of the Commission's Regulations) and the electric utility Standards (Part 37).[6] In place of the current separate Standards, the Commission would adopt a single set of Standards (new Part 358). The Commission also proposes to expand the scope of applicability to include transactions between regulated transmission providers and all of their energy affiliates, thus broadening the definition of an affiliate covered by the standards of conduct, from the more narrow definitions in the existing regulations.

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[4] According to the Mineral Management Service, in 1989 approximately 58.4 Bcf of gas was produced from deepwater areas in the Gulf of Mexico in 1989 (defined as water depths greater than 1,000 feet). By 1999, annual Gulf of Mexico deepwater gas production had increased to 845.5 Bcf.

[5] Because the prohibitive costs of installing a fixed platform in deepwater areas, for Shell's Auger project, which commenced production in 1994 Shell used a TLP to extract the oil and gas. Unlike a fixed platform, a TLP is a floating structure that is held in place by tensioned tendons connected to the sea floor. The Auger project and other TLP development projects also employed another new important production technology, the subsea well. This technology extends the areal reach of a project by enabling the operator to place a satellite well on the seafloor and pipe the oil and gas back to the TLP or to other facilities.

[6] These comments focus on the impact of the NOPR on gas pipelines and affiliated deepwater OCS producers.

Currently, the gas Standards exempt pipeline transportation transactions with producers that sell from their own production, gatherers that sell from their own gathering facilities and local distribution companies that make on-system sales. The NOPR would propose a new defined term, "energy affiliates," that would eliminate these exemptions.[7]

In merging the separate gas pipeline and electric utilities Standards, the Commission stated its intent that the Standards should continue to carry out the two basic principles underlying the current gas affiliate regulations. The central principles of the regulations are that: (1) the transmission providers' employees engaged in transmission system operations must function independently from the transmission providers' sales or marketing employees and from any employees of their energy affiliates; and (2) the transmission providers must treat all transmission customers, affiliated and non-affiliated, on a non-discriminatory basis, and cannot operate their transmission systems to benefit preferentially an energy affiliate. The NOPR would modify and expand upon the current gas pipeline Standards in several respects discussed below.

## COMMENTS

### I. THE INDUSTRY CHANGES CITED BY THE COMMISSION IN EXTENDING THE STANDARDS OF CONDUCT TO ALL ENERGY AFFILIATES DO NOT SUPPORT OR JUSTIFY ELIMINATION OF THE PRODUCER EXEMPTION.

#### A. The Reasons the Commission Established and Repeatedly Reaffirmed the Producer Exemption Continue to Apply Today.

##### 1. Background

[7] NOPR, IV FERC at p. 34,085. Although the NOPR does not refer to the exemption for "intrastate pipelines," presumably the Commission meant to eliminate that exemption as well.

The Commission's current gas marketing affiliate regulations generally do not apply to transactions and communications between a pipeline and a non-marketing affiliate. Of particular relevance to these comments, Section 161.2(c) of the regulations exempts the pipeline from the regulations in its dealings with entities that sell solely their own gas production (*i.e.*, the "Producer Exemption").

Order Nos. 497, *et seq*.,[8] and 566, *et seq*.,[9] promulgated regulations "intended to prevent interstate natural gas pipelines from providing preferential treatment to their marketing or brokering affiliates." The Commission adopted the marketing affiliate regulations for several reasons. Those reasons included: (1) the fact that pipelines have economic incentives to show undue preferences toward their marketing affiliates; (2) a lack of consensus within the industry about what pipeline marketing affiliate practices were improper; (3) several specific instances of abuse brought before the Commission for adjudication; and (4) many allegations of unlawful behavior received by the Commission in response to a prior Notice of Inquiry and the establishment of an Enforcement Task Force.[10]

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[8] *Inquiry Into Alleged Anticompetitive Practices Related to Marketing Affiliates of Interstate Pipelines*, FERC Stats.& Regs. [Regs. Preambles 1986-1990] ¶ 30,820 (1988)(Order No. 497), *on reh'g*, FERC Stats. & Regs. [Regs. Preambles 1986-1990] ¶ 30,868 (1989)(Order No. 497-A), *affirmed in part and remanded in part, Tenneco Gas v. FERC*, 969 F.2d 1187 (D.C. Cir. 1992), *on remand*, FERC Stats. & Regs. [Regs. Preambles 1991-1996] (Order No. 497-D)(1992), *on reh'g*., 65 FERC ¶ 61,381 (Order No. 497-E)(1993), *order den'g. reh'g. and granting clarification*, 66 FERC ¶ 61,347 (Order No. 497-F).

[9] *Standards of Conduct and Reporting Requirements for Transportation and Affiliate Transactions*, FERC Stats. & Regs. [Regs. Preambles 1991-1996] ¶ 30,997 (Order No. 566), *order on reh'g.*, FERC Stats. & Regs. [Regs. Preambles 1991-1996] ¶ 31,002 (1994)(Order No. 566-A), *order on reh'g*., 69 FERC ¶ 61,334 (1994)(Order No. 566-B).

[10] Order No. 497, FERC Stats. and Regs. ¶ 30,820 at pp. 31,129–31,130.

The current gas marketing affiliate regulations consist primarily of the Standards of Conduct[11] and reporting requirements.[12] In Order No. 599,[13] the FERC amended its Standards of conduct to require interstate pipelines to identify the names and addresses of their marketing affiliates on their Internet web sites, and to update the information within three business days of changes.

**2. The Producer Exemption**

The current gas marketing affiliate regulations apply to "any interstate natural gas pipeline that transports gas for others pursuant to subpart A of part 157, and subparts B or G of part 284, an disaffiliated in any way with a natural gas *marketing or brokering* entity and conducts transportation transactions with its *marketing or brokering* affiliate." These regulations also apply to "pipeline sales operating units." 18 C.F.R. § 161.1 (emphasis added). The regulations define "marketing or brokering" to mean "a sale of natural gas to any person or entity by a seller that is not an interstate pipeline, *except when: (1) the seller is selling gas solely from its own production* ...." 18 C.F.R. § 161.2 (emphasis added). The regulations also exclude from the definition of "marketing or brokering" sellers making sales "solely" from their own gathering or processing facilities, or if the seller is an intrastate natural gas pipeline or a local distribution company making an on-system sale. *Id.*

The definitions set forth above reflect the Commission's intent that the current gas marketing affiliate regulations "apply only to pipeline affiliates that are engaging in gas sales activities that would compete with independent marketers." The Commission created the

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[11] 18 C.F.R. § 161.3.
[12] 18 C.F.R. § 250.16.

Producer Exemption at the inception of the pipeline marketing affiliate rules in 1988-1989. On rehearing of Order No. 497, the Commission clarified the types of activity that constituted "marketing" for purposes of the current gas marketing affiliate regulations to *exclude* "[p]roducers, gatherers or processors, acting in their traditional roles, that sell gas solely from their own production, gathering or processing facilities."[14] The Commission found that "[i]n making these sales, such entities are acting in the roles that their names imply."

The Commission has maintained the exemption in effect ever since, having revisited the regulations repeatedly over that time. Prior to issuance of Order No. 566 in 1994, the regulations required annual review and reaffirmation of the reporting requirements. The Commission extended the reporting requirements several times. However, the Commission did not disturb the Producer Exemption, finding that

> The definition [of "marketing or brokering"] does not apply to *producers*, gatherers or processors, acting in their traditional roles of selling gas from *their own production*, gathering or processing facilities, or to intrastate pipelines and local distribution companies acting in their traditional roles of making on system sales of gas. These entities will be included as marketers only to the extent that their activities go beyond their traditional roles and they make sales for which an independent marketer could compete.

Order No. 566-A, FERC Stats. and Regs. at 31,130 (emphasis added).

In Order No. 566-A, the Commission revised the wording but not the substance of Section 161.2(c). The revisions were intended to reflect the elimination of producer regulation under Part 270 as a result of enactment of the Natural Gas Wellhead Decontrol

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[13] *Reporting Interstate Natural Gas Pipeline Marketing Affiliates on the Internet*, III FERC Stats. & Regs. [Regulations Preambles] ¶ 31,064 (1998).

Act.[15] In making these revisions, the Commission stressed that it was *not* modifying the existing exemptions under Section 161.2(c). The Commission continued to preserve the Producer Exemption throughout its continuing re-examination of the marketing affiliate rules and the industry changes described in the NOPR.

The Commission also did not raise any question specifically regarding the Producer Exemption in Order No. 637.[16] The Commission raised general issues concerning its regulatory policy with respect to pipeline affiliates and non-affiliates, and asked in general whether "there need to be revisions to regulations relating to pipeline affiliates."[17] Moreover, the record in the Order No. 637 rulemaking proceeding did not reflect any expressed desire on the part of any participant to eliminate the affiliated Producer Exemption, or any expression of concern that the exemption interfered with the Commission's flexibility and efficiency goals.

**B. The Industry Changes Cited By The NOPR As Supporting An Expansion Of The Rule Do Not Pertain to the Producer Exemption.**

As discussed above, throughout the 14 years since the Commission adopted the initial marketing affiliate rules the Commission has maintained the Producer Exemption. The Commission has consistently recognized that pipeline transportation of an affiliated producer's own production does not pose the market power and competition concerns that

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[14] Order No. 497-A, FERC Stats. and Regs. [1986-1990 Regs. Preambles] ¶ 30,868 at p. 31,591 (footnotes omitted).
[15] Order No. 566-A at p. 31,129, *citing* Pub. L. No. 101-60; 103 Stat. 157.
[16] *Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services*, FERC Stats. & Regs. [Regulations Preambles July 1996-December 2000] ¶ 31,091 (2000); *order on rehearing*, FERC Stats. & Regs. [Regulations Preambles July 1996-December 2000] ¶ 31,099 (Order No. 637-A) (2000) and 92 FERC ¶ 61,062 (Order No. 637-B) (2000).

originally prompted the Commission to adopt the regulations. That is the Commission's current practice. SOI respectfully submits that the Commission should maintain its current practice in this regard by continuing the Producer Exemption.

The NOPR does not cite any evidence whatsoever that the Producer Exemption has resulted in circumvention of the Standards. There is no basis for a finding that producers engaged in sales of their own production are using affiliated pipelines to exercise market power. Producers using an affiliated pipeline to transport gas are simply engaging in a traditional transaction that does not raise the same competitive issues as a non-producer affiliate using an affiliated pipeline for transportation service.

The NOPR cites a number of "significant changes" in the gas industry that have occurred since the Commission first adopted the pipeline Standards of Conduct.[18] None of these changes indicate a need for changing the current rule to eliminate the Producer Exemption. Indeed, the Commission acknowledged the same changes in earlier rulemaking orders in which it reaffirmed the exemption.

The NOPR identifies "unbundling, capacity release, and e-commerce" as reasons for eliminating the Producer Exemption. However, the Commission had recited several of these developments in Order No. 566, which made significant changes in the Standards of Conduct and reporting requirements but *retained* the Producer Exemption.[19] The NOPR also states that today, due to mergers and consolidations, gas pipeline companies "have a much wider

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[17] Order No. 637, III FERC Stats. and Regs. ¶ 31,091 at 31,268-31,269.
[18] NOPR, IV FERC at p. 34,081.
[19] Order No. 566, FERC Stats. and Regs. [Regs. Preambles 1991-1996] ¶ 30,997 at 31,059 (noting that in Order No. 636 the Commission had created a new operating environment for pipelines and shippers through the unbundling and capacity release provisions of that rule).

array of affiliates in all sectors of the energy business."[20] The Commission also took note of the "sophisticated, lightning-speed transactions" -- both physical and financial – engaged in by marketing and non-marketing gas pipeline affiliates.[21]

None of these changes has altered the basis for the Producer Exemption discussed in Order Nos. 497-A and 566-A, discussed above. The NOPR does not attempt to connect the industry changes to a need to eliminate the exemption. To the extent that a producer seeks service on an affiliated pipeline solely for the purpose of selling gas that it produces, none of the concerns expressed by the Commission has any relevance.

While several of the commenters at the March 15, 2001 technical conference in Docket No. PL00-1-000 called in general for expansion of the coverage of the Standards to "all affiliates" of interstate pipelines, none of those commenters specifically called for elimination of the Producer Exemption. None of the commenters even asserted that the Producer Exemption raised any new concerns. And none of the commenters provided evidence, anecdotal or otherwise, establishing that the exemption has led to circumvention of the affiliate regulations.

## II. IMPOSITION OF THE AFFILIATE RULES ON OCS PRODUCERS' TRANSACTIONS WITH AFFILIATED PIPELINES WILL NEEDLESSLY BURDEN DEEPWATER PRODUCTION.

The rationale for not disturbing the Producer Exemption is particularly compelling in the case of pipelines that transport affiliated producers' own gas production from the OCS.

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[20] NOPR, IV FERC at p. 34,081 (citing as examples the mergers of El Paso Energy Corporation, Sonat Inc. and the Coastal Corporation and the acquisitions by the Enron Corporation).

[21] *Ibid.* The Commission noted the same industry trends in Order No. 637. III FERC *Stats. and Regs.* ¶31,091 at pp. 31,249-31,257 (Order No. 637),

These pipelines were created for the purpose of transporting OCS production for affiliated and non-affiliated producers to onshore or offshore delivery point interconnects with one or more long-line interstate pipelines. From that onshore or offshore point, a non-affiliated interstate pipeline generally transports the gas to a market area.

The offshore pipeline affiliated with the producer almost universally does not have direct control over access to market areas. These affiliated pipelines were built only after OCS producers had explored the possibility of having an existing non-affiliated interstate pipeline construct the offshore extension to the producer's deepwater production. Non-affiliated pipelines were unwilling to construct the necessary facilities and provide flexible/firm services in a manner that would satisfy the special needs of producers operating in deepwater areas. The pipelines affiliated with SOI generally perform an aggregation function, *i.e.*, aggregation of production in the offshore production area for delivery to one or more non-affiliated interstate pipelines, more likely than not long-line pipelines, for downstream transportation to an end-use market. SOI's affiliated offshore pipelines generally have very limited direct access to any end-use market.

### A. The Elimination of the Producer Exemption Would Hinder Development of the OCS.

The orderly development of the OCS is furthered by the construction of pipeline facilities to deepwater production locations by pipeline affiliates of deepwater producers. Elimination of the Producer Exemption, and extension of the marketing affiliate standards of conduct and reporting requirements to such affiliated pipelines, particularly when combined with some of the proposed changes set forth in the NOPR, will impede further deepwater development. For example, the push into deepwater projects caused producers to invest in

research and development projects that created new technologies. Those technologies enabled installation of pipeline facilities in conditions not encountered on the Shelf. Future deepwater and ultra-deepwater[22] projects will require extensive communication between deepwater producers and deepwater pipelines.

In view of the unique technical challenges encountered in deepwater exploration, development and production, it is absolutely essential that a producer be able to have a complete and confidential dialogue with the pipeline regarding these complex operations. Because of the intensely proprietary nature of the information being discussed, however, a requirement that an affiliated pipeline contemporaneously disclose to the public any information it shares with an affiliated producer during the course of such discussion would make it literally impossible to have this meaningful dialogue.

The proposed disclosure requirements therefore would almost certainly result in the pipeline revealing highly confidential proprietary information provided to the pipeline by the affiliated producer. Disclosure of pipeline discussions with the affiliated producer regarding, among other things, projected pipeline size, capacity and the proposed route, would permit competing producers, by analyzing that information, to deduce the location of the exploration activities, reserve estimates and projected production levels. A requirement that in effect compels disclosure of this information to the producer's competitors would be so detrimental to the producer's exploration, development and production activities that it would effectively prohibit such discussions altogether.

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[22] Ultra-deepwater projects occur in waters deeper than 5,000 feet.

These unprecedented disclosure requirements would severely handicap affiliated producers, but would not apply to comparable discussions between a pipeline and non-affiliated producers. Indeed, a pipeline affiliated with one producer would be required to disclose communications with that affiliated producer that it would not be required to disclose as to non-affiliated producers for which it transported gas. Imposing such burdens solely on pipelines' communications with affiliated producers would serve none of the objectives set forth in the NOPR, but would be discriminatory and impede offshore exploration and development to the detriment of robust competition that the NOPR seeks to promote. The information provided by an OCS production company to a pipeline in connection with possible production development projects is so sensitive and proprietary that the producer would not provide the information to anyone outside the company absent a confidentiality agreement. However, under the proposed rule, even if an affiliated pipeline executes a confidentiality agreement with an affiliated producer, it would be useless since any information the pipeline provides about its transmission system in the course of a dialogue with the producer would nonetheless have to be disclosed. Disclosure of any of this proprietary information by an affiliated pipeline to the affiliated producer's competitors as a result of the proposed rule would place the affiliated producer at a severe disadvantage in the very competitive OCS exploration, development and production industry.

The interests of the marketplace and gas consumers are best served by regulatory policies that encourage, or at least do not inhibit exploration, development and production of gas from promising areas such as deepwater and ultra-deepwater locations. Policies that hinder these activities would be contrary to the interests of consumers in obtaining adequate

supplies of natural gas at reasonable prices, and contrary to the national interest in achieving greater energy security.

OCS pipelines affiliated with producers, especially deepwater pipelines, do not present the market power issues addressed in the NOPR. The construction of pipelines affiliated with deepwater producers did not evolve out of any effort to exert market power. Pipelines affiliated with producers were established to move deepwater gas out of necessity -- there were no viable alternatives. In short, affiliated pipelines were created to transport deepwater gas to onshore pipeline interconnects because at key stages of development, existing interstate pipelines were unwilling to accept the risks inherent in deepwater production or to provide the flexibility necessary to create an incentive for development of such reserves.

SOI initially held discussions with established non-affiliated interstate pipelines to transport their deepwater gas from the point of production. SOI initially perceived existing pipelines with already-developed infrastructure to be well positioned to transport deepwater gas. However, the pipelines approached by SOI declined to construct deepwater facilities on terms, such as the flexible/firm tariff model, that would permit the development of the deepwater reserves on terms that satisfied the practical needs of producers.

There were numerous stumbling block issues that made existing pipelines non-viable as transporters of deepwater reserves. First, many existing pipelines were neither technically capable of nor commercially willing to build facilities to the deepwater areas. Thus, the producer would have been compelled to build a pipeline to connect to the interstate pipeline's facilities somewhere closer to shore. Significantly, deepwater exploration and production projects have tended to drive investment in offshore technology.

Moreover, existing pipelines typically would propose to connect the deepwater production to their own systems to the exclusion of other pipelines. OCS Producers did not wish to limit their ability to gain access to multiple pipeline markets.

In addition, as a general matter, existing pipelines failed to grasp the unique needs of producers operating in deepwater production areas. A key early concern of producers was oil production. Without the pipeline facilities in place to transport both gas and oil production, deepwater producers faced the prospect of shut-in or curtailment of their oil production. The Commission has recognized that "OCS gas is often produced in conjunction with oil and that there must be an assured gas transportation outlet to prevent curtailment of oil production, [and has] praised what was deemed an alternative form of transportation with features designed to meet the needs of OCS shippers, as well as guaranteeing a revenue stream which would make the project viable for its owners [*i.e.,* the flexible firm "FT-2" service structure described above]." [23] The Commission has also recognized that the regulations of the Minerals Management Service, which govern the production of oil and gas from the federal domain offshore, prohibit the flaring of significant quantities of natural gas, except for well testing and emergency situations, and that flaring of casinghead gas due to pipeline unavailability would not qualify for this exception. [24]

Moreover, production in deepwater areas poses some unique operating requirements. Pipelines in deepwater areas must operate differently than conventional onshore or shallow-water pipelines. For example, deepwater production is characterized by an initial sporadic

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[23] *Mississippi Canyon Gas Pipeline, LLC*, 89 FERC ¶61,318 at p. 61,982 at n. 5 (1999), citing *Shell Gas Pipeline Company*, 76 FERC ¶61,126, at p. 61,687 (1996).
[24] *See, Nautilus Pipeline Company, L.L.C.,* 78 FERC ¶61,325 at p. 62,380 n. 11 (1997).

production rate during the ramp-up of production. Additionally, periodic well shut-downs in deepwater fields create higher levels of uncertainty and correspondingly greater risk to producers than shut-downs in other areas. Returning deepwater wells to production following shut-down is a lengthy process; the inflexible nature of standard reservation charges during such a shut-down fails to recognize this reality. Thus, the traditional interstate pipeline reservation charge approach did not offer the flexibilities essential for the development of deepwater projects, as explained earlier. Historically, in its experience, SOI found existing pipelines unwilling to accept the need for a flexible approach.

To address these concerns, pipelines affiliated with deepwater producers developed and implemented alternative firm rate schedules with features that met the needs of offshore producers while at the same time making the project economically viable for the owners. Thus, affiliated pipelines used rate structures in which the offshore producers obtained firm service but at volumetric rates, subject to minimum throughput commitments and life-of-reserve commitments.[25] Non-affiliated pipelines were not willing to offer satisfactory services with this level of flexibility.

Moreover, it is important to note that the creation of these producer-affiliated deepwater pipeline systems was generally if not universally preceded by an open season during which any interested party could seek capacity on the same flexible terms available to the affiliate. These open seasons significantly limited any opportunity a deepwater pipeline might have to favor an affiliated producer. Further, producer-affiliated pipelines have

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[25] *See, Nautilus,* 78 FERC at p. 62,382; *Shell Gas Pipeline Company*, 76 FERC ¶ 61,126, *on reh'g.*, 78 FERC ¶ 61,192 (1997); *Garden Banks Pipeline, LLC*, 78 FERC ¶ 61,066 (1997); *Discovery Producers Services LLC*, 78 FERC ¶ 61,194 (1997).

continued to hold open seasons when expansion of capacity is justified by further development.

Burdening a deepwater pipeline with needless filing and reporting requirements concerning arrangements involving the pipeline's production affiliate would only hinder deepwater production activities. Before undertaking the risk and cost associated with deepwater exploration and production, the producer needs to know that there will be a pipeline in-place and ready to provide service when production begins, and that the pipeline will transport the producer's gas from the production area to shore in the most efficient, flexible manner possible. As the Commission has recognized, the success of deepwater ventures tends to stimulate the exploration and development of additional deepwater areas. The Commission has recognized the increasing importance of deepwater production as a source of domestic energy reserves. Over 25% of the natural gas production in the lower 48 states originates in the Gulf of Mexico, with a growing percentage coming from deepwater fields.

The Commission should not extend its marketing affiliate regulations in a manner that will hinder the development of deepwater oil and gas resources. As discussed above, producer-affiliated OCS pipelines enhance competition for both producers and pipelines. Exploration for and development of additional gas reserves, and production of increased quantities of natural gas, enhances competition. Without pipeline affiliates to move gas from the deepwater OCS, it is doubtful that the development to date would have occurred as rapidly as it has, simply because in the past traditional pipelines have been unwilling, or slow to consider offering, terms that producers required and only affiliated pipelines were willing to offer. If the Commission effectively precludes OCS producers from using transportation

services provided by affiliated pipelines to move their deepwater OCS production, a very real possibility if the Commission adopts the NOPR, the competitive landscape would be severely limited. This is an unintended result of the proposed rule that would likely delay the development of deepwater reserves. It is therefore doubtful that regulation of such entities now through the proposed Standards, as well as other possible regulations on which the Commission sought comment in the NOPR (*e.g.*, capacity limits, divestiture and divorcement) would allow continued efficient development of deepwater reserves at the pace possible otherwise.

**B. The Elimination of the Producer Exemption Would Not Advance The Stated Purposes of the NOPR.**

Extending the marketing affiliate regulations to pipelines providing transportation service to affiliated producers' own production will not further the Commission's regulatory objectives. Indeed, elimination of the exemption would impede those objectives. The Commission seeks to promote competition and efficient markets, while mitigating market power and preventing undue discrimination. [26] Encouraging the construction of pipeline facilities to deepwater production areas by entities other than existing interstate pipelines promotes competition and efficiency.

Existing pipelines with onshore interstate systems have an obvious incentive to promote the use of their onshore pipeline systems by inhibiting the movement of the offshore gas to other pipelines once the gas has been transported to the onshore area. Conversely, OCS pipelines affiliated with OCS producers have an equally obvious incentive to offer interconnects with different onshore pipelines, to increase the likelihood that the offshore gas

will find a competitive onshore market. Thus, producer-affiliated OCS pipelines promote competition.

Imposition of the marketing affiliate regulations on transactions between pipelines and affiliated OCS producers involving the affiliated producers' own production is not necessary to achieve the objectives of the NOPR. The concerns that prompted adoption of the standards of conduct and reporting requirements required under the marketing affiliate rules are inapplicable to a pipeline providing service on behalf of an affiliated producer seeking to ship its own production. In these circumstances, the affiliate relationship is a result of the need for deepwater producers to move gas production to existing transporters closer to or onshore.

The costs that would be imposed on pipelines transporting affiliated producers' gas by the proposed affiliate rules would exceed the benefits of such rules. Whether there are *any* benefits is questionable. As the Commission has consistently recognized for the entire 13-year history of the current gas marketing affiliate rules, there is no basis for extending those rules by eliminating the Producer Exemption.

Deepwater pipelines typically do not control access to any markets; they deliver gas to unaffiliated downstream pipelines or groups of pipelines for transportation to markets. Due to the characteristics of deepwater production, in particular higher rates of production per well, and significantly greater fluctuations in volumes than would be typical of onshore wells, it is in the economic interest of a deepwater pipeline to size its facilities in order to attach future production, either by an affiliated producer or non-affiliated producer. Such deepwater

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[26] Order No. 637, III FERC Stats. and Regs. ¶ 31,091 at p. 31,262.

pipelines have no incentive to restrict access to other producers; indeed, they have every reason to seek additional reserve commitments from other deepwater producers.

Indeed, for these reasons, non-affiliated OCS producers who develop reserves after the pipeline has been constructed and is in service may receive greater service and rate flexibility than the producer-affiliate or anchor shipper under the current regulatory structure. Moreover, the producer-affiliated pipeline offered service of a higher quality than a non-affiliated pipeline. As discussed above, the producer-affiliated pipelines were constructed in lieu of non-affiliated pipelines in part because the producer-affiliated pipelines were prepared to adopt greater flexibility to OCS producers, in recognition that OCS producers face different production challenges than are found onshore or in shallower waters. The producers who developed these projects took the risks that caused the pipeline to be constructed in the first place. Producers that subsequently undertook production on the OCS only after these additional lines were built benefited from these pioneering activities.

The construction of the deepwater facilities by pipelines affiliated with some of the producers developing those reserves enhanced the ability of producers generally to gain access to pipeline services. Because the affiliated producer is selling its own production,[27] its primary motivation is in assuring continuous flow from its wells, not gaining market power or excluding competitors. Deepwater pipelines will have an obvious incentive to acquire additional throughput, through discounting if necessary.

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[27] The producer may operate the wells and own a working interest, or it may be a non-operating working interest owner or an overriding royalty owner. Regardless, that producer is acting in a traditional role.

For all of these reasons, *preserving* the Producer Exemption will *promote* the Commission's competitive goals. Eliminating the exemption, in contrast, would likely *reduce* the level of competition both off- and onshore.

## III. THE COMMISSION MUST NOT LIMIT THE ABILITY OF OCS PRODUCERS TO DISCUSS THE NEED FOR CAPACITY EXPANSION OR NEW CAPACITY WITH AFFILIATED OCS PIPELINES.

As discussed above, prior to undertaking a deepwater or ultra-deepwater project, it is critical that the producer and pipeline confer extensively regarding, among other things, the technical requirements for the pipeline. This is true whether the project is an entirely new greenfield project or an extension/expansion of existing pipeline facilities. It is extremely important for SOI as it moves forward with deepwater and ultra-deepwater development that it be able to engage in a full dialogue with an affiliated pipeline as it plans its exploration and production activities. By requiring disclosure of information regarding projected pipeline size, capacity and route that would provide competing producers with proprietary and competitively sensitive information regarding the affiliated producer's exploration and development activities, the proposed regulations, as applied to an offshore producer's communications with an affiliated offshore pipeline company, would severely hinder these necessary communications.

Proposed Sections 358.5(a)(1) and (a)(2) are intended to prevent an "energy affiliate" from having access to "information about Transmission Provider's system" that is not available on OASIS or the Internet, as applicable. Among the categories of "information" included in the prohibition are information concerning available transmission capability, maintenance activity, capacity expansion plans, or similar information. Proposed Section

358.5(b)(1) similarly prohibits a pipeline employee from disclosing such information unless it is posted. Section 358.5(b)(1) also expands the prohibition to include "other pipelines."

SOI is deeply concerned that these prohibitions will hinder OCS producers' ability to make inquiries to affiliated pipelines regarding available capacity or to discuss new capacity solutions for transportation of gas from reserves yet to be discovered or developed. Prohibiting pipeline employees from disclosing, or affiliate employees from receiving, capacity information without posting the information on the pipeline's web site would result in an enormous and unwarranted commercial disadvantage to the affiliated producer, as contrasted with non-affiliated producers. If a producer is in the process of developing reserves in a deepwater location, the producer will need to arrange for transportation of the gas. That may require expansion of an existing pipeline or construction of a new pipeline. Both will require in-depth engineering and other discussions to reach an informed decision as to whether the production project is commercially feasible or even technologically possible.

Under the rule as proposed, if an OCS producer contacts an affiliated pipeline regarding the need for expansion or extension of existing pipeline facilities or a new greenfield pipeline system, the pipeline will be obligated to post any information provided to the producer affiliate regarding its intentions or ability to expand its capacity in the future. As the proposed regulations are drafted, the pipeline would appear obligated to disclose, among other things, the quantity of gas for which the affiliated producer requested service from the reserves. As discussed above in Section II.A. of these comments, such information is highly proprietary and confidential. For that matter, all information regarding an exploration project is competitively sensitive and proprietary in the exploration industry, including the very fact that the discussion has taken place. Public disclosure of such

information could cause serious economic harm to the affiliated producer. It is important to note that as drafted, the regulations would *not* require the pipeline to disclose such information received from a *non*-affiliated producer.

When a producer is considering a new exploration and production project, it will need to involve the pipeline that would transport the gas from the earliest stage of the project. It is fairly common to have exploratory sessions between the producer and the pipeline, followed by numerous meetings at which planning issues are reviewed in detail, concerning common technological hurdles, among other things. These discussions generally would precede a decision to pursue the project. Such discussions will be increasingly important as producers such as SOI explore for gas in ever-deeper offshore frontier areas. Compelled disclosure of information regarding projected pipeline size, capacity and route that could allow competing producers to deduce proprietary and competitively sensitive information regarding the affiliated producer's exploration and development activities would restrict the producer's ability to share information necessary for both the producer and the pipeline to plan for the project. The inability to share such information without required contemporaneous disclosure could contribute to the decision to abandon a project.

The proposed prohibitions against disclosure by employees of the pipeline under Section 358.5(b) reach absurd heights by including, as one of the prohibited categories of information, information concerning the transmission system of another. If, for example, an OCS producer contemplating the development of new offshore reserves meets with an affiliated pipeline to discuss a possible expansion or extension of that pipeline's system, logical topics for discussion will be the potential for interconnections with and the availability of capacity on onshore pipelines downstream of the affiliated pipeline. As

explained above, producer-affiliated OCS pipelines typically offer only limited direct access to end-use markets. Therefore, the new production project's economic viability will ultimately depend upon whether the gas that would be produced can access onshore take-away capacity that will reach desirable markets.

During exploratory sessions between the producer and its affiliated pipeline, the pipeline's employees may discuss a number of topics related to the availability of capacity on one or more non-affiliated pipelines' systems. As discussed above, OCS producers generally seek access to multiple downstream pipelines to provide additional opportunities to reach different markets and to provide flow reliability options when downstream outages occur. The discussions between the producer and the affiliated pipeline would logically involve discussion of information regarding unaffiliated downstream pipelines. Some of this "information" may be speculative, such as the perceived willingness of a downstream pipeline to expand its own system to accommodate additional volumes.

Under the proposed prohibition, following the meeting, the affiliated pipeline's employees would be required to visit the web sites of every pipeline discussed to determine whether any information they shared was not posted on that pipeline's web site. If in that investigation it turned out that some piece of information was not available on the non-affiliated pipeline's web site, the affiliated pipeline would have to contemporaneously disclose that information on its own web site. Imposing such an absurd burden would accomplish nothing meaningful.

These circumstances provide a further illustration of the harm that could result from elimination of the Producer Exemption in the current regulations. The result of the application of the proposed rule to producer affiliates is a patently unfair and unbalanced

handicap for the producing affiliate. The producing affiliate would be virtually unable to discuss customary and routine matters with an affiliated pipeline without risking disclosure of proprietary exploration and production information, while competing producers could freely engage in the same type of discussions with that pipeline without disclosure concerns since they are not energy affiliates. As indicated above, the best solution would be to preserve the exemption, at least for pipelines transporting affiliated producers' OCS gas. If the Commission is unwilling to preserve the exemption, then the Commission must design an exclusion to the requirements of Sections 358.5(a)(1), (a)(2) and (b)(1) to ensure that producer affiliates of OCS pipelines are not placed at a competitive disadvantage by disclosure rules that will hinder their ability to communicate in a timely manner with their affiliated pipelines regarding their anticipated future capacity needs.

Finally, as proposed, the wording of Sections 358.5(a)(1) and (a)(2) and (b)(1) appears redundant. Section 358.5(a)(1) contains a broad requirement that the pipeline ensure against any pipeline employee providing an affiliate with "any information" concerning the pipeline's system not available to non-affiliates, without limitation. Section 358.5(a)(2) requires the pipeline to prohibit affiliate employees from receiving such information, with some examples of the types of information not to be disclosed. Section 358.5(b)(1) prohibits pipeline employees from disclosing this information to an affiliate. If these provisions are each intended to set forth a distinct requirement, it is not evident from the wording. In the Final Rule, the Commission should clarify the distinctions, if any, between these sections, and eliminate any redundant sections.

## IV. THE COMMISSION MUST NOT ESTABLISH RULES THAT WOULD LIMIT THE AMOUNT OF CAPACITY THAT A PRODUCER CAN HOLD ON AN AFFILIATED PIPELINE.

If the Commission decides to eliminate the current Producer Exemption despite the compelling reasons to retain the exemption discussed above, the Commission must not "limit[] the amount of capacity (by volume or by percentage of capacity)" a producing affiliate can hold on an affiliated pipeline.[28]

Any requirement that an OCS producer would be limited by volume or percentage in its use of an affiliated OCS deepwater pipeline, leave aside divorcement or divestiture, would discourage *future* deepwater development. Moreover, it would undermine *existing* development absent a grandfather provision exempting existing services for producers on existing offshore systems from the quantity limitation. As discussed above, deepwater producers face numerous challenges, only one of which is getting the gas transported from the production area. Placing percentage or quantity limits on an affiliated deepwater producer would be highly problematic, because it could curtail or shut-in its offshore production.

Indeed, establishment of maximum quantity or percentage limits would imply the power to lower the maximum quantity and/or percentage at some point in the future. Thus, even if the initial quantity/percentage limits could be complied with, OCS producers would have no assurance that the Commission would not establish lower, unacceptable levels in the future.

Exploration and development in the OCS requires an extended timeline and much advance planning. Introducing a substantial element of uncertainty regarding the producer's ability to produce gas, once discovered and developed, will discourage or delay such

production and thereby potentially reduce supplies and competition. Moreover, any quantity or percentage limitation on a deepwater producer's capacity rights on an affiliated pipeline would also potentially jeopardize associated oil production.

Imposition of a quantity limitation also raises jurisdictional issues, in that the limitation would in effect regulate the producer affiliate's production of gas. A quantity limitation could obviously diminish a producer's transportation rights on an affiliated pipeline to a level below its production capability. The OCS producer's ability to have its production transported from the platform is an obvious and basic precondition to exploration and development. If the producer has to worry that it will see its capacity rights arbitrarily reduced by a regulation somewhere down the road, the producer will not invest as readily in such production as it might have otherwise.

Finally, such a limitation as applied to producers affiliated with OCS pipelines would be at odds with the reasoning underlying Commission's regulations under OCSLA, as promulgated in Order Nos. 639 and 639-A. In those orders, the Commission explicitly endorsed "the idea of sizing facilities to match anticipated transportation needs:"

> Particularly offshore, where developing a producing field may entail extensive time and expense, we recognize the practicality of coordination, whereby a producer incrementally bringing additional volumes on line can be assured that when the field's extraction reaches its zenith, pipeline facilities will be in place with the capacity to take away and transport all gas volumes.

Order No. 639-A, at 31,688. For this very reason, placing an arbitrary quantity or percentage limit on the amount of capacity an offshore producer can hold on an affiliated pipeline would undermine the producer's ability to develop the offshore field effectively.

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[28] NOPR, IV FERC at 34,088.

Similarly, limiting an offshore producer's capacity on an affiliated pipeline by "revising allocation policies," purportedly to "minimize an affiliate's ability to exercise market power by allocating firm capacity to as many shippers as possible,"[29] would effectively prorate an offshore producer's production. Such limits would conflict with the Commission's open-access policies, which are based on contract carriage, not common-carriage.

All of these concerns apply with greater force to even the possibility of divorcement or divestiture, which would impede development of OCS reserves that required new or additional pipeline facilities. As discussed above, OCS producers have found historically that they cannot rely on traditional interstate pipeline companies to extend their facilities to remote areas of the OCS in a manner that offers producers the flexibility they need to explore for and develop natural gas. A producer could be discouraged from development of newly discovered OCS reserves if it faces a significant risk the affiliated pipeline it is relying on for flexible transportation could be divested or divorced from the producer.

The difficulties and harms posed by this possible regulation are yet another example of why the proposed rules should not apply to producers affiliated with OCS pipelines. As SOI has demonstrated through the discussion above, failure to preserve the Producer Exemption on the OCS would be a grave error. If the Commission were to nonetheless eliminate the Producer Exemption, the Commission must at a minimum exempt OCS producers affiliated with OCS pipelines from any quantity limitation on the capacity the OCS producer can contract for on an affiliated pipeline.

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[29] NOPR, IV FERC at p. 34,088.

## V. THE COMMISSION MUST NOT PROHIBIT PRODUCERS AFFILIATED WITH OCS PIPELINES FROM OPERATING THEIR INTERCONNECTING FACILITIES IN A SAFE AND EFFICIENT MANNER.

Proposed Section 358.4(a)(3) also appears potentially problematic for an OCS pipeline and its producer-affiliate. This proposed standard would prohibit the "transmission provider" from permitting employees of its affiliate to (1) "conduct[] transmission system operations or reliability functions" or (2) "[have] access to the system control center or similar facilities used for transmission operations or reliability functions that differs in any way from the access available to other transmission customers."

The terms "system operations and reliability functions" and "system control center" used in this proposed standard are electric utility terms taken from current Part 37 (Section 37.4(b)(1). How the Standard would be applied to gas pipelines is unclear. Thus, it is not clear whether this Standard would prohibit pipelines from permitting affiliated producer employees to participate in routine operations and maintenance functions at the point of interconnect with the pipeline.

Presumably the pipeline affiliate would "conduct" operations and reliability functions, but the pipeline would presumably call upon the producer affiliate (as it would any platform operator) to "conduct" related operations that may involve interconnecting facilities owned and operated by the pipeline. Moreover, offshore platforms typically contain a room or rooms in which technicians employed by the producer monitor the flow of gas from the well or wells feeding the platform and the flow of gas into the pipeline. These facilities and operations exist on platforms as part of a platform operator's function, regardless of whether the operator is affiliated with the pipeline in question. It does not appear that the Commission would have intended to include such operations in the definition of a "system

control center," but due to the ambiguity of the term as applied to the natural gas industry, SOI requests that the Commission clarify that such facilities and operations do not fall within the definition of "system control center" as that term is used in the NOPR.

In addition, it is common for pipeline company employees to have access to producing platforms attached to their systems, and for production company affiliates to have access to pipeline equipment located at producing facilities. Offshore platforms commonly include some equipment owned and operated by the producer, and other equipment owned and operated by the pipeline, regardless of whether the producer and pipeline are affiliated. For purposes of safety and efficiency, production company employees examine and supervise the installation of pipeline equipment, including, for example, separation and metering equipment located on a platform. This is true whether or not the production company is affiliated with the pipeline. Prohibition of these routine forms of cooperation would be extremely disruptive and would serve no purpose related to the intent of the affiliate rules.

Producer and pipeline personnel frequently engage in operational activities on behalf of each other, in order to operate the production and pipeline facilities in the most reliable, efficient and safe manner possible. For example, producer personnel may:

1) launch a pipeline pig from the production platform;
2) inject or monitor chemicals into the pipeline to preserve or improve flow levels; and
3) change orifice plates in meters.

In some instances, a producer, a non-jurisdictional offshore gatherer and a pipeline may have facilities in a single location, such as a platform or group of connected platforms. Producers typically allow pipeline company employees access to their platforms, and production

company employees typically perform pipeline functions on the platform. Although these activities are routine, they afford the platform operator access that "differs . . . from the access available to other transmission customers" that are *not* operators. Thus, the activities appear to be prohibited under the proposed rule.

Other types of activities may be prohibited under proposed Section 358.4(a)(3)(ii)'s prohibition against a pipeline permitting Energy Affiliates to have "access to the system control center or similar facilities used for transmission operations or reliability functions that differs in any way from the access available to other transmission customers." For example, would an offshore producer that operates facilities at a subsea tie-in using a remote control valve be operating facilities "similar" to the "system control center?"

SOI cannot describe in these comments every conceivable scenario in which affiliated producer employees could have access to facilities that would be involved with "transmission operations or reliability functions." Suffice it to say that these types of activities are commonly encountered in offshore operations, regardless of whether the producer and pipeline are affiliates. Again, the Commission can avoid these needless complexities that are irrelevant to the purposes of the NOPR by preserving the Producer Exemption. Failing that, however, the Commission must define "transmission operations and reliability functions," and "system control center or similar facilities" to narrow those terms to the activities and conduct the Commission seeks to prevent – i.e., affiliate access to the facilities in which the pipeline schedules its system gas. Moreover, "access" must be clarified to mean that an employee is physically present, and not merely interacting with the pipeline's bulletin board (e.g., nominating or confirming a nomination) as all shippers do.

The problems discussed above appear to stem at least in part from the attempt in the NOPR to consolidate the current Part 37 and Part 161 Standards into a common set of Standards to apply to both gas pipelines and electric utilities. Despite the industry trend toward convergence of the gas and electric industries ( discussed in the NOPR at p. 7), for obvious reasons, the physical activities surrounding the production and transportation of natural gas differ considerably from the activities involved in the transmission of electricity. While in some respects a common set of affiliate Standards may be desirable, in the particular context of OCS operational issues, a common set of Standards may be needlessly confusing and difficult to comply with, resulting in numerous clarification requests.

Section 358.4(a)(1) and (2) would apparently constitute a partial exception from the prohibition in case of "emergencies." However, this partial exemption is insufficient, particularly in view of the Commission's warning in the NOPR that "if a pattern of activities indicates that 'emergencies' are not authentic, the Commission will take strong action against the offending transmission provider." [30] Producers and pipelines will not be able to react appropriately to an emergency if they must worry that the Commission or a competitor will second-guess their actions at some future point, and accuse them of violating the affiliate standards.

More fundamentally, producers currently have access to a pipeline's facilities at the point of interconnect precisely to *avoid* emergency conditions from developing in the first place. This access is routine among producers and pipelines, whether affiliated or not. The Commission must not prohibit activities of this type. Thus, if the Commission does not

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[30] NOPR, IV FERC at p. 34,085.

retain the Producer Exemption, it must at a minimum clarify the prohibition in proposed Section 358.4(a)(3) to exclude producer and pipeline affiliates who have joint access to interconnected facilities for purposes of ensuring reliability and safety.

## VI. THE COMMISSION MUST CLARIFY WHAT CONSTITUTES AN OFFER FOR PURPOSES OF THE DISCOUNT DISCLOSURE REQUIREMENT.

Section 358.5(d) of the Proposed Rule would require that "[a]ny offer of a discount for any transmission service made by the transmission provider must be posted on the OASIS or Internet web site contemporaneously with the offer." The information posting would be required to include the information required under current Standard H of the pipeline Standards of Conduct.[31]

The NOPR states that the discount disclosure requirement for pipelines at Section 161.3(h)(1) of the current regulations provides that if a pipeline *offers* a discount to its marketing affiliate, the pipeline must make a comparable discount contemporaneously available to all similarly situated non-affiliated shippers. However, under current Section 161.3(h)(2), the pipeline is required to post relevant information (name of affiliate, maximum rate, discounted rate, delivery points, quantity of gas and conditions) on its website within 24 hours of the time at which gas first flows under a discounted transaction. The NOPR would henceforth require contemporaneous disclosure of a discount offer.

[31] 18 C.F.R. § 161.3(h)(2). This information includes: the name of the customer involved in the discount and whether it is an affiliate or whether an affiliate is involved in the transaction, the rate offered; the maximum rate; the time period for which the discount would apply; the quantity of power or gas scheduled to be moved; the delivery points under the transaction; and any conditions or requirements applicable to the discount. The posting must remain on the OASIS or Internet website for 60 days from the date of posting.

However, the NOPR does not define "offer" for purposes of the disclosure requirement. Determining whether or not a pipeline has made an "offer" of a discount to an energy affiliate could turn on complex facts, and thus embroil the Commission and the parties in numerous disputes over whether or not a discussion of a possible discount between a pipeline and an affiliated shipper constituted an "offer." In any Final Rule, if the Commission retains this requirement, it must define "offer" and provide guidance in the regulatory text as to characteristics of an "offer."

## VII. THE COMMISSION MUST CLARIFY THE POSTING REQUIREMENTS APPLICABLE TO POTENTIAL MERGER PARTNERS.

SOI further requests clarification of the Commission's proposal with respect to the electronic posting of merger partners. As SOI interprets the NOPR, the Commission has asked for comment solely on whether the proposed rules should require the posting of the identities of potential merger partners on the Internet *after* the merger has been announced.[32] Requiring offshore producers (or other entities) to post the identities of entities that are possible merger partners would be extremely burdensome, would serve no useful purpose, and would probably result in considerable misunderstanding. SOI seeks confirmation that the Commission's use of the term "*potential* merger partners" means only "announced" merger partners.

[32] IV FERC at p. 34,046.

WHEREFORE, for the foregoing reasons, SOI submits that in any Final Rule promulgated in this proceeding, the Commission should retain the affiliated Producer Exemption currently contained in the natural gas pipeline marketing affiliate regulations. If, however, the Commission eliminates the Producer Exemption, the Commission must limit and clarify the requirements of the proposed Standards so that at a minimum, they do not apply to OCS pipelines' dealings with affiliated OCS producers as discussed above.

Respectfully submitted,

Charles J. McClees, Jr.
Shell Oil Company
200 North Dairy Ashford
Houston, Texas 77079
(281) 544-4516

Kevin M. Sweeney
John & Hengerer
1200 17th Street, N.W.
Suite 600
Washington, D.C. 20036
(202) 429-8802

**Attorneys for Shell Offshore Inc.**

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