Morgan Lewis

OIL AND GAS:
REGULATORY ROUNDUP

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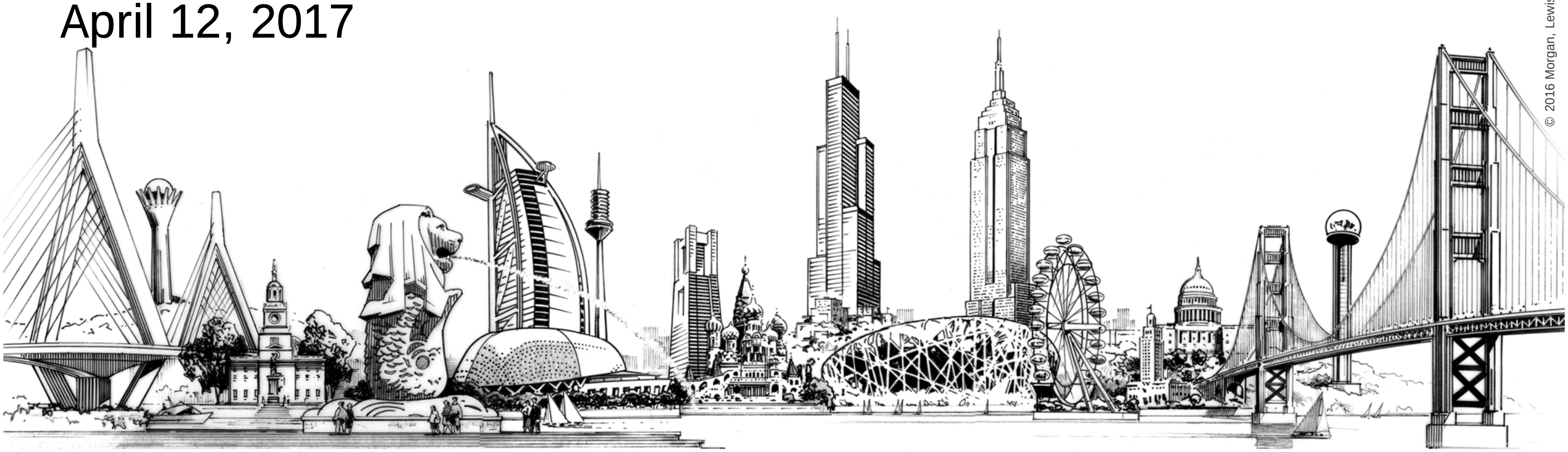

Composition of FERC

- The priorities and initiatives in 2017 will depend, in large part, on the composition of the Commission itself.
  - FERC is an independent agency, which means that its policy directives are set through the interests of its Commissioners rather than any direction from the White House or Congress.
- January 26, 2017 – President Trump naming of Commissioner LaFleur as Acting Chairman sets off a chain reaction that results in the absence of a quorum at FERC.
  - FERC's ability to act without a quorum is severely impacted.
  - On the last day on which FERC had a quorum (February 3), FERC attempts to minimize the impact by delegating the authority to act in certain instances to its Staff.

Composition of FERC

- What can FERC do without a quorum?
  - Accept and suspend rate and other filings made pursuant to Section 4 of the Natural Gas Act (NGA) and Section 205 of the Federal Power Act (FPA) and:
    - (a) make them effective, subject to refund and further order of the Commission or
    - (b) make them effective, subject to refund, and set the proceeding for hearing and settlement judge procedures.
  - Extend the time for action on matters where an extension is permitted by statute.
  - Act on uncontested filings made pursuant to NGA Section 4, FPA Section 205 and Section 6(3) of the Interstate Commerce Act.
  - Accept uncontested settlements.

Composition of FERC

- FERC cannot act on:
  - Contested rate filings or related settlements under the FPA or NGA
  - Applications for certificates of public convenience and necessity for new natural gas pipelines
  - Contested settlements
  - Complaint proceedings or rehearing requests
  - Petitions for declaratory orders

Composition of FERC

- The new administration has only floated names of potential nominees:
  - Kevin McIntyre
  - Neil Chatterjee
  - Robert Powelson

- Once nominated, the individuals must be confirmed first by the Senate Committee on Energy & Natural Resources and then by the full Senate.

Pipeline Infrastructure Projects

<u>Tennessee Gas Pipeline Company's Susquehanna West Project</u>

- Environmental groups filed a request for stay of construction and other land disturbance pending resolution of the rehearing request.
  - Construction and operation of the project will harm its members' environmental interests in their own property and the public lands they visit.
  - Project will degrade the scenic quality of trails in the Tioga State Forest.
  - Construction and operational activities will add to preexisting noise impacts.
  - The project may lead to future gas drilling in the Tioga State Forest and shale gas development near a member's home.

Pipeline Infrastructure Projects (cont.)

Tennessee Gas Pipeline Company's Susquehanna West Project

- FERC denied the request for stay.
  - Pipeline facilities are located within or adjacent to the pipeline's existing right-of-way.
  - Project will cause temporary disruptions to certain trails in the Tioga State Forest.
  - Project will temporarily increase ambient sound levels but will not affect nighttime noise levels. The pipeline is required to file noise surveys.
  - Alleged harm to support a stay must be certain and actual and not theoretical.
  - FERC has not ruled on the rehearing requests and noted that, to the extent the pipeline proceeds with construction, the pipeline bears the risk that FERC will revise or reverse its initial decision or that its orders will be overturned on appeal.

Pipeline Infrastructure Projects (cont.)

Equitrans' Prior Notice Request for Uprate Project

- Homeowners protested the prior notice request and raised the following concerns:
  - Noise from existing compressor station and future compressor station
  - Future emissions
  - Safety concerns
  - Devaluation of homeowner's property

Pipeline Infrastructure Projects (cont.)

Equitrans' Prior Notice Request for Uprate Project

- FERC denied the protests and authorized construction.
  - Reviewed as a case-specific certificate application under NGA Section 7 because the protests were not withdrawn during the 30-day reconciliation period.
  - Homeowners raised concerns that are not related to the uprate project.
  - EA concluded the project will not result in an increase in operational noise; the uprate falls within the existing operating pressure envelope of the stations and does not require any new aboveground, noise generating facilities.
  - Project will be operated and maintained in accordance with the Department of Transportation's pipeline safety regulations.

Pipeline Application Review

- Former Commissioner Bay's statement encourages FERC to reexamine its pipeline application review process.
  - Statement was attached to the February 3 order approving the Northern Access Project.
- (1) FERC should examine whether other evidence can help evaluate a project's need.
  - Focusing on precedent agreements may not account for other considerations.
  - Is the capacity needed to ensure deliverability to new or existing natural gas-fired generators?
  - Is there a significant reliability or resiliency benefit?
  - Does the additional capacity promote competitive markets?
  - Is there is any concern that anticipated markets may fail to materialize?

Pipeline Application Review (cont.)

- (2) FERC should reexamine how it conducts environmental reviews of pipeline projects and should analyze the environmental effects of increased regional gas production from the Marcellus and Utica.
  – FERC has never conducted a comprehensive study of the environmental consequences of increased production from the Marcellus and Utica.
  – FERC has never performed a programmatic review of gas production in the different shale formations.
  – FERC should be open to analyzing the downstream impacts of the use of natural gas and to performing a life-cycle greenhouse gas emissions study.

Update on FERC Income Tax Policy Notice of Inquiry

- FERC sought comments on methods to allow regulated entities to earn an adequate return, consistent with *Hope*, that do not result in a double recovery of investor-level taxes for partnerships or similar pass-through entities.
- FERC also sought comments on the practical implications for the proposed remedy.
- Initial comments were due on March 8, and reply comments were due by April 7.

Update on FERC Income Tax Policy Notice of Inquiry (cont.)

- Comments included:
  - Eliminate the income tax allowance in the cost of service for interstate natural gas pipelines owned by a Master Limited Partnership.
  - Stagger the elimination of the income tax allowance, starting with the pipelines with the most egregious over-earnings.
  - Retain the income tax allowance, which was created to provide an incentive for investment in infrastructure to provide oil and natural gas transportation.
  - Any changes to tax or ROE policies should not apply to electric utilities as the inclusion of a tax allowance and adequate ROE are necessary for electric utilities to ensure just and reasonable rates.
  - Any changes to the ROE to address double recovery should be carefully scrutinized and should be done through a technical conference.

FERC Oil Pipeline Indexing Policies and Form No. 6 ANOPR

- FERC sought comments on potential modifications to its policies for evaluating pipeline index rate changes and data reporting requirements.
  - Should FERC deny index increases for pipelines whose Form No. 6, page 700 revenues exceed costs by 15% for both of the prior two years?
  - Should FERC deny index increases that exceed by 5% the cost changes reported on page 700?
  - Should FERC apply the new criteria to costs more closely associated with the pipeline's proposed rates than with total company-wide costs and revenues now reported on page 700?
- Initial comments were due on January 19, 2017, and reply comments were due March 17, 2017.

FERC Oil Pipeline Indexing Policies and Form No. 6 ANOPR (cont.)

- Pipelines Strongly Oppose Proposed Changes:
  - Proposed changes increase the regulatory burdens and introduces regulatory risk on interstate common carrier liquids pipelines.
  - Proposed changes to indexing undermine the goals of indexing by (1) ensuring that pipeline rates will not keep pace with inflation, (2) eliminating efficiency-enhancing incentives that encourage pipelines to manage their costs, and (3) reducing oil pipeline pricing flexibility.
  - ANOPR rejects the concept of "segmentation" and requires pipelines to identify and file supplemental page 700 reports for "major pipeline systems" and "non-contiguous pipeline systems," which are difficult to identify.
    - "Systems" are not static.
    - Pipelines and their subsidiaries do not maintain their books on a "system" basis.
  - Proposed changes to Page 700 place heavy burdens on the liquids pipeline industry and unreasonably favor shippers.
  - ANOPR fails to demonstrate any changed circumstance that warrants the proposed changes.

FERC Oil Pipeline Indexing Policies and Form No. 6 ANOPR (cont.)

- Shippers Generally Support the Proposed Changes
  - FERC should adopt a new “substantially exacerbate” test but adjust the over-recovery to threshold to 5% (instead of 15%).
  - Shippers support proposal that requires oil pipelines to file their annual indexing ceiling rates, even if they do not propose to increase rates to the ceiling level.
  - Shippers support improvements to the transparency of FERC Form No. 6 page 700 reporting, as proposed.
    - Pipelines should be required to file supplemental Page 700s and report information on how costs were allocated between or among the supplemental Page 700s.
    - Pipelines should be required to disaggregate Page 700 revenue, barrel, barrel-mile data associated with cost-based rates, non-cost based rates, and other jurisdictional revenues.
    - Pipelines should be required to make their Page 700 workpapers available to shippers or interested persons upon request, and not just to FERC and its staff.

PHMSA Pipeline Safety Rule

- Pipeline Safety: Operator Qualification, Cost Recovery, Accident and Incident Notification, and Other Pipeline Safety Change.
- Purpose: provide safety benefit to the public, environment, and limit property damage.
- New requirements:
  - Requires pipeline operators to report any accident or incident within one hour of confirmed discovery of the event electronically or by telephone.
  - Requires revision or confirmation of initial notification within 48 hours of confirmed discovery of the accident or incident.
- Effective March 24, 2017

PHMSA Pipeline Safety Rule

- Other requirements include:
  - Sets up cost recovery fee structure for design review of new gas and hazardous liquid pipelines with either overall design and construction costs totaling at least $2.5 billion or that contain new and novel technologies.
  - Excludes farm taps from the Distribution Integrity Management Program requirements and proposes safety requirements for the farm taps.
  - Requires pipeline operators to report to PHMSA a change in product or permanent reversal of flow that lasts more than 30 days.
  - Provides methods for assessment tool selection by incorporating consensus standards by reference in Part 195 for stress corrosion cracking direct assessment (SCCDA) that were not developed when the Integrity Management regulations were issued.
  - Requires electronic reporting of drug and alcohol testing results.

CFTC's Regulation of Energy Derivatives

- Chairman Timothy Massad on Tuesday tendered his resignation to President Obama, effective Jan. 20.
  - Massad's resignation left only two Commissioners at CFTC – J. Christopher Giancarlo (R) and Sharon Bowen (D).
  - The White House nominated Giancarlo to serve as Chairman in March.
- Giancarlo has publicly stated that under his oversight, it is time for the CFTC to "reinterpret its regulatory mission" by focusing on fostering economic growth, enhancing U.S. markets, and "right-sizing" its regulatory footprint.

CFTC’s Regulation of Energy Derivatives

- Giancarlo has stated that the CFTC will continue aggressive enforcement action under the Trump administration.

  > But, as I mention the CFTC’s Division of Enforcement, let me take this moment to warn those who may seek to cheat or manipulate our markets: you will face aggressive and assertive enforcement action by the CFTC under the Trump Administration. There will be no pause, let up or reduction in our duty to enforce the law and punish wrongdoing in our derivatives markets. The American people are counting on us.

- Spoofing statute survives constitutional challenge.
- Rule 180.1 survives constitutional challenge.
- Dismissal of gas manipulation class action arising from CFTC allegations.

Questions?

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