2014 – A Big Year for FERC Orders Addressing LNG Jurisdiction

As domestic supplies of natural gas grow in abundance, United States natural gas markets have sought new markets for natural gas and new methods for moving gas from production to markets, both international and domestic. Technological advances as well as the decrease in commodity prices and desire for lower carbon emission fuel alternatives have spurred growth in non-traditional liquefied natural gas (LNG) markets for fleet vehicle, marine, and locomotive uses. LNG is also displacing diesel as a preferred fuel for non-vehicular end use applications such as drilling rigs and field compression. And the demand for LNG exports from the United States continues to grow.

With new demand and new opportunities for LNG in vehicular and non-vehicular end use markets, as well as continued demand for LNG as a peaking fuel for traditional natural gas local distribution companies, LNG businesses have sought clarity as to the regulatory status of LNG infrastructure and transactions under the Natural Gas Act (NGA).

Illustrative of these trends was a quartet of orders issued by the Federal Energy Regulatory Commission (FERC or Commission) in 2014, ruling on requests for declaratory orders on various LNG jurisdictional issues.

***Gulf Oil Limited Partnership*, 148 FERC ¶ 61,029 (2014) (Docket No. CP14-132-000)**

Request for Declaratory Order

Gulf Oil, a marketer and distributor of motor fuels and other energy products, planned to build a natural gas liquefaction facility (100,000 to 300,000 gallons per day) near Marcellus Shale production in Pennsylvania that would receive Pennsylvania produced and gathered gas, liquefy that gas, and then deliver LNG by truck to various vehicular and non-vehicular end use customers as well as local distribution companies (LDCs) for their use in peak shaving operations. It sought a declaratory order from FERC that the construction and operation of the LNG facility would not be subject to FERC's jurisdiction under the NGA and would not make the owner or operator of the LNG facility a "natural gas company" within the meaning of Section 1(b) of the NGA.

FERC Order

The Commission granted Gulf Oil's request, concluding that Gulf Oil would not be engaging in FERC-jurisdictional transportation of natural gas, nor would its proposed liquefaction and truck loading facility be subject to NGA jurisdiction. Specifically, FERC found:

Determinations about LNG jurisdiction are made on a case-by-case basis.

- FERC has never asserted jurisdiction over liquefaction facilities where the natural gas is not also transported, either upstream or downstream, by a jurisdictional interstate pipeline.
- FERC does not, "as a general rule," have jurisdiction over non-pipeline transportation of gas (i.e., transportation by truck, train, or barge). FERC has asserted jurisdiction over domestic liquefaction/truck loading facilities when those facilities are part of an interstate pipeline transportation "continuum" and where the use of a non-pipeline mode of transportation would serve as a means of "circumventing NGA jurisdiction". It contrasted those scenarios with the Gulf Oil business plan, which appears to be targeting markets that can only be reached by truck.
- FERC also gave Gulf Oil comfort that in the "remote possibility" that some LNG that had passed through its facility was later vaporized and delivered by an LDC customer to an interstate pipeline "or used in a manner that displaces gas being transported on an interstate pipeline," its facility would not become "retroactively" subject to FERC's NGA Section 7 jurisdiction.
- Finally, FERC noted that any wholesale sales of natural gas by Gulf Oil would either be non-jurisdictional "first sales" or would be automatically authorized under FERC's blanket marketer certificate authority provided by regulation (18 C.F.R. § 284.402).

Shell U.S. Gas & Power, LLC, 148 FERC ¶ 61,163 (2014) (Docket No. RP14-52-000)

Request for Declaratory Order

Shell's request for a FERC declaratory order discussed two planned LNG facilities – (1) a liquefaction unit in Sarnia, Ontario, Canada with docking and storage facilities in Michigan, for the liquefaction and import into the U.S by truck, train, or waterborne vessel of natural gas for both vehicular and non-vehicular end use purposes; and (2) a liquefaction unit at an existing Geismar, Louisiana chemical plant (located along the Mississippi River) at which Shell would liquefy domestically produced gas and then load that gas onto waterborne vessels for transportation to marine fuel end users or to on-shore LNG storage facilities (some in other states) for further distribution as vehicular fuel. Shell also acknowledged that although its business purpose is to serve vehicular end use LNG markets, it also would make incidental LNG sales to non-vehicular end use and LDC peak shaving markets.

Shell requested a declaratory order finding that none of its planned LNG activities would be subject to the NGA as they would all fit the "vehicular fuel" exemption from NGA jurisdiction set forth in NGA Section 1(d).

FERC Order

The Commission declared Shell's proposed LNG business activities to be exempt from its NGA jurisdiction, for the most part, but not for the reasons argued by Shell. Specifically, FERC found:

- The NGA Section 1(d) "vehicular fuel" exemption does not trump the NGA's Section 3 import/export jurisdiction. In other words, while NGA Section 1(d) exempts certain eligible entities from being deemed "natural gas companies" under FERC's broad NGA Section 1(b) jurisdiction over interstate sales, transportation, and the entities that perform such activities, NGA Section 3 applies to all "persons" that engage in import or export activities, or that operate LNG terminals and thus applies to entities whether or not they are jurisdictional "natural gas companies."
- Shell's proposed activities would not trigger jurisdiction under NGA Sections 1(b) and 7.
    - FERC interprets its NGA jurisdiction as not extending to non-pipeline modes of gas transportation.
    - If the business purpose of the LNG facility operator is to make LNG for use as an end-use product, its facilities and activities will remain outside FERC's NGA Section 7 jurisdiction, even where the gas received at its facility was previously transported in interstate commerce, so long as
        1. The LNG does not get put back into an interstate pipeline;
        2. If it is delivered to an LDC or other local pipeline in vapor form, such deliveries are limited to boil off or tail gas; and
        3. If liquid is delivered by truck or other non-pipeline means to an LDC system, the transaction does not fall into one of the "circumvention" categories (see the Gulf Oil summary, above). What constitutes "circumvention" remains unclear, and seems to encompass some types of exchange transaction (see also the Pivotal discussion, below).
    - FERC's NGA Section 7 jurisdiction was never intended to apply to sales of gas for resale in interstate commerce where the gas never traveled in an interstate pipeline. Therefore, if the LNG made, stored, or transported by the facility owner/seller never entered an interstate pipeline, then that facility owner/seller, its facilities, and its sales are not subject to NGA Section 7.
- If the gas that was liquefied ever did travel upstream on an interstate pipeline, this does not affect the non-jurisdictional status of Shell's LNG facility, but the wholesale sale of such LNG might be subject to the NGA's sales jurisdiction if Shell could not qualify as a "first seller" – but that is not a problem because it would still qualify for FERC's blanket marketer certificate authority under 18 C.F.R. § 284.402.
- FERC's NGA Sections 3 and 7 jurisdiction has been asserted over pipeline and storage facilities, as well as LNG facilities that are connected (at one end or the other) to pipelines. There is no NGA jurisdiction over an inland LNG facility that does not connect with a pipeline.

- Interpreting its NGA Section 3 domestic LNG terminal jurisdiction for the first time, FERC held that its NGA Section 3 jurisdiction over an LNG terminal that delivers gas to a waterborne vessel for interstate transportation to another US state will trigger if the terminal and waterborne transport are "links in an interstate chain, liquefying and regasifying in order to enable gas to be ferried across a stretch of water interrupting what would otherwise be a continual flow of gas by pipeline from one state to another."
- If the LNG facility is not intended to "serve to bridge pipelines divided by water" but rather "to transform it into a product for sale and delivery in its liquid state to end users, with no intent for any of the LNG to be reintroduced into a pipeline[,]" then the LNG facility is not performing interstate transportation under NGA Section 7, and because the Commission uses the same analysis for NGA Section 3 facilities jurisdiction, neither will it be considered an "LNG Terminal" and the facility will not need NGA Section 3 authority.
- FERC stated that its findings with respect to its lack of jurisdiction over Shell's siting, construction, and operation of facilities to import LNG from Canada did not address the separate issue of whether Shell would need authority under NGA Section 3 to import Canadian LNG – that issue remains within the jurisdiction of the U.S. Department of Energy.

Commissioner Bay's Partial Dissent

The Commission's findings and conclusions were not unanimous. Commissioner Norman Bay (who will assume the Chairmanship of FERC on April 15, 2015) issued a partial dissent, agreeing with the majority's interpretation of the scope of the NGA Section 1(d) vehicular fuel exemption, but disagreeing with its analysis of NGA Section 3, both as to imports/exports and as to "waterborne vessels" transporting gas in interstate commerce. Commissioner Bay argued that Shell's Sarnia project would involve jurisdictional import facilities, and its Geismar facility fit the statutory definition of an "LNG Terminal." He found inconsistent and unpersuasive the majority's attempt to apply its NGA Section 7 jurisdictional analysis to NGA Section 3.

Pivotal LNG, Inc., 148 FERC ¶ 61,164 (2014) (Docket No. RP14-732-000)

Request for Declaratory Order

Pivotal, an LNG marketing company subsidiary of AGL Resources, sought two declaratory rulings from FERC. Both of its requests pertain to (i) an existing LNG facility in Alabama owned and operated by Pivotal that was the subject of a prior FERC dismissal of jurisdiction given Pivotal's end use fuel business purpose and other relevant facts, and (ii) a series of LNG facilities owned and operated by LDC affiliates of Pivotal as part of their local distribution operations, and from which Pivotal sought to make occasional purchases of LNG:

- First, Pivotal asked FERC to determine that none of these LNG facilities would be deemed an "LNG Terminal" subject to FERC's NGA Section 3 jurisdiction by virtue of Pivotal taking LNG from these facilities and transported that LNG in interstate commerce by waterborne vessel. Like Shell, Pivotal argued that the NGA Section 1(d) vehicular fuel exemption should apply to non-vehicular end use applications for LNG, as well, including end use fuel and feedstock uses of LNG.
- Second, Pivotal asked FERC to determine that various sales and purchases of LNG that was liquefied or stored at its or its' LDC affiliates' LNG facilities (referred to as the "LNG Transactions") do not constitute sales or transportation of natural gas in interstate commerce that is subject to FERC's jurisdiction under Sections 1(b) and 7 of the NGA.

FERC Order

FERC granted Pivotal's requests, for the most part, but again diverged in its reasoning from the proposed analysis of its NGA jurisdiction. The Commission stated:

- In reviewing its prior determination that Pivotal's Alabama LNG facility was not subject to NGA Section 7 jurisdiction; FERC confirmed that this result was not based on NGA Section 1(d) and clarified that the 1(d) exemption only applies to gas that will be consumed as vehicular fuel – since Pivotal's business purpose is broader than vehicular gas activities, it could not rely on NGA Section 1(d).

- Regarding the domestic transfer of LNG produced from Pivotal's or one of its affiliate's LNG facilities by waterborne vessel, FERC reiterated its analysis in *Shell* that the interstate commerce component of the LNG Terminal definition was intended to fill a "regulatory gap" with respect to facilities used to transport interstate gas that would be transported by waterborne vessel for delivery into a Hinshaw facility's pipeline system.
- Moreover, FERC reiterated its application of NGA Section 7 precedent in interpreting the scope of NGA Section 3 jurisdiction over import/export facilities, and discussed its "long-standing precedent" finding that NGA Section 7 doesn't extend to facilities used solely to liquefy gas for end product purposes, where there is no intent to have that LNG be reintroduced into a pipeline. Thus, if the LNG facility owner has the same limited business purpose, FERC will find its facility exempt from both NGA Section 7 and NGA Section 3 facilities jurisdiction.
- With respect to the sale of LNG, FERC noted that Pivotal and its LDC affiliates would not be exempt from the Commission's NGA Sections 1(b) or 7 jurisdiction over wholesale sales – but it noted that such sales are authorized by its blanket marketer certificate.

While FERC found Pivotal's end use fuel business purpose supported the conclusion that there would be no NGA Section 3 or 7 jurisdiction over its or its affiliates' facilities, it did caveat that this would not be the result if LNG from one of the LDC affiliates' LNG facilities was delivered by truck to another LDC or end user under a "jurisdictional gas exchange arrangement that would result in displacement of gas being transported on an interstate pipeline." It relied for this conclusion on the "circumvention" analysis discussed in the *Shell* order. Moreover, it issued another warning about the limits of its non-jurisdictional finding in a final footnote:

We note that, as discussed above, if LNG liquefied by Pivotal, one of its Hinshaw affiliates, or another non-jurisdictional company is delivered by a non-pipeline mode of transportation to an LDC or Hinshaw pipeline, rather than directly to the ultimate end user, that would not cause the liquefaction facility to become subject to our section 7 jurisdiction unless the LNG transported to the LDC or Hinshaw pipeline by a non-pipeline mode of transportation would displace gas transported on an interstate pipeline, be part of a jurisdictional gas exchange, or circumvent in some other way the Commission's NGA jurisdiction over the interstate transportation of gas by pipeline, thus making it necessary for the Commission to assert jurisdiction over the liquefaction facility and/or the LDC or Hinshaw pipeline.

Commissioner Bay's Concurrence

Commissioner Bay agreed with the majority's determination that Pivotal's proposed LNG activities should not be regulated by FERC. But he disagreed with the analysis used to support this conclusion with respect to the determination that the subject LNG facilities would not be "LNG Terminals" as defined in the NGA. Rather than applying the same jurisdictional analysis for NGA Sections 3 and 7, Commissioner Bay said that based on the facts presented by Pivotal, it was clear that all those LNG facilities were located well inland (in excess of 150 miles from the nearest coast). As such, they should not be considered within the definition of "LNG Terminal" on that basis, for the NGA definition of "LNG Terminal" is limited to facilities located on or close to water or the coast.

Emera CNG, LLC, 148 FERC ¶ 61,219 (2014) (Docket No. CP14-114-000)

Request for Declaratory Order

Emera proposed to build a small compressed natural gas (CNG) facility (0.025 Bcf/day) at the Port of Palm Beach in Riviera Beach, Florida. That facility would receive interstate gas from an interconnection with a Florida Hinshaw pipeline, compress that gas to fill International Standards Organization (ISO) containers, and transport those containers a distance of approximately a quarter mile to third-party owned and operated commercial ship-loading facilities, where the containers would be loaded onto ships for transportation to the Bahamas. The ultimate destination of the ISO containers was an Emera-affiliated electric utility company operating in Grand Bahama. Emera noted that it had already applied for authority to export gas from the DOE. It sought a declaration that its facility would not be subject to the NGA Section 3 or 7 jurisdiction of FERC.

FERC Order

The Commission found that Emera's construction and operation of the proposed CNG facility would not be subject to its NGA jurisdiction.

- Again, the Commission indicated that it has interpreted and exercised its NGA Section 3 facilities jurisdiction consistent with its interpretation and exercise of jurisdiction over facilities used to transport gas in interstate commerce under NGA Section 7.
- Here, Emera's facilities were not like border-crossing facilities over which FERC has traditionally exercised its jurisdiction = where gas is moving through pipelines or delivered to coastal LNG facilities via pipeline.
- FERC felt that Emera's proposed facility was more analogous to a non-jurisdictional trucking operation where LNG or CNG is trucked across the border. It referenced an existing XNG CNG plant in Maine where it is not regulating that facility under either NGA Section 3 or 7.
- With respect to its NGA Section 7 jurisdiction, the Commission noted the fact that Emera's CNG facility would be receiving gas from a Hinshaw pipeline and stated "[s]ince the gas will have left jurisdictional interstate commerce before reaching Emera and will never re-enter interstate commerce (i.e., will not be transported from Florida to another state), our section 7 jurisdiction will not attach to the Emera facility."
- FERC emphasized that, regardless of how gas is transported, "all imports and exports of natural gas require section 3 authorization from the DOE's Office of Fossil Energy."

Commissioner Bay's Dissent

Once again, Commissioner Bay dissented from FERC's conclusion regarding its NGA Section 3 jurisdiction. He argued that "conflating section 3 with section 7 is not supported by the language of the statute" and noted the very same statutory language distinctions the majority had used in the Shell case to dismiss the argument that NGA's Section 1 jurisdictional exemption could trump NGA Section 3 jurisdiction. In fact, the NGA Section 3 language is broader. Commissioner Bay also dismissed the notion that Emera's facility was too remote from the port location to be deemed an export facility.