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# FERC Solicits Feedback on Modernizing Natural Gas Certificate Policy

**April 25, 2018**

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On April 19, 2018, the Federal Energy Regulatory Commission ("**FERC**") initiated a proceeding to evaluate its policies—in place for nearly two decades—governing the review and certification of new interstate natural gas transportation facilities, including pipelines, storage, and liquefaction. FERC's current approach has been in place since the issuance of its 1999 Policy Statement ("**Policy Statement**") setting forth the factors it uses to determine whether a proposed project is required by the public convenience and necessity pursuant to the Natural Gas Act ("**NGA**"). In the nineteen years since, however, the US natural gas market has undergone dramatic transformation as a result of the explosive growth in production from shale formations and fracking advances. At the same time, interests opposed to prolific pipeline development—including affected landowners, environmental advocacy organizations, and state agencies promoting renewable energy and energy efficiency initiatives—have increased the pressure on FERC over the years regarding its approach to determining market need for pipeline development and analyzing adverse impacts under the National Environmental Policy Act of 1969 ("**NEPA**").

The issuance of the Notice of Inquiry ("NOI") on April 19 starts the process to modernize FERC's certificate framework. Starting the overhaul process with an NOI keeps FERC's options open regarding whether to issue an updated policy statement or open a formal rulemaking process to revise FERC's regulations. As evidenced by the questions the NOI poses to the industry, FERC is considering some significant changes that will inevitably cause some stakeholders concern. Comments are due June 25, 2018.

Under the NGA, FERC has exclusive jurisdiction over the interstate transportation and sale of natural gas. Under Section 7 of the NGA, any person seeking to operate or construct an interstate gas pipeline must obtain a certificate of public convenience and necessity from FERC. To grant a certificate, FERC must assess whether the proposed project is in the public interest, which requires balancing the benefits of the proposed project against potential adverse consequences. FERC's current Policy Statement enumerates the factors the Commission considers in evaluating whether a proposed project satisfies the public interest standard. Notably, the Policy

Statement does not purport to address all factors FERC will consider in reviewing a certificate application. Instead, the Commission uses a "sliding scale approach" to holistically account for issues instead of a one-size-fits-all methodology. As such, if a proposed project will have substantial adverse impacts, it must have proportionate public benefits to be approved.

The NOI will evaluate and consider potential changes to the factors FERC considers in this balancing analysis. Comments have been requested in several broad areas: how FERC determines need for a project; landowner interests; FERC's analysis of the environmental impacts of a project; and streamlining the certificate process.

## Need Determination

Since 1999, the natural gas markets in the US have changed dramatically. The Policy Statement was issued at a time when the US markets for natural gas were just beginning the shift toward interstate competition and market-driven pricing. Developers wanted prompt Commission action to approve new projects, whereas local distribution companies ("**LDCs**") raised subsidization concerns over pipeline buildout. The Policy Statement furnished guidance relating to price dynamics now commonplace in the natural gas market. Now, discovery and production of domestic natural gas, bolstered by the economic viability of horizontal drilling and hydraulic fracturing in shale formations, has increased to the extent that the US is now a net exporter of gas. Natural gas demand for electric generation and export as a liquefied commodity soared in the last ten years.

Under the Policy Statement and subsequent precedent, FERC has principally relied on precedent agreements for long-term firm service as key indicia of demand for a greenfield project. FERC has applied equal weight to precedent agreements with third parties and with affiliates of the pipeline developer. This approach of accepting affiliate precedent agreements has facilitated investment in energy infrastructure by enhancing regulatory certainty that the pipeline will be built, which is often a predicate to investment in associated new gas-fired generating facilities or LNG export facilities. In several recent certificate decisions, however, a minority of FERC commissioners have questioned the reliance on affiliated precedent agreements to demonstrate demand.

FERC's insistence that signed precedent agreements be in place to receive a certificate can be a stumbling block for development, too. For example, obtaining signed precedent agreements can be challenging where multiple parties are involved in a series of connected projects (such as pipeline build-out to support an LNG export terminal), and each party is unwilling to take the risk of a firm commitment to the projects before a pipeline certificate is received. This chicken-and-egg problem could be alleviated if FERC relaxed its focus on precedent agreements and considered a broader scope of evidence for demand. In addition, many market participants have changed the way they conceptualize and contract for pipeline capacity. Historically, LDCs and other large end users were the predominant customers of interstate pipeline capacity. Now, natural gas producers are increasingly interested in building out more capacity, which can be achieved by developing pooling points on a pipeline system. This shift prioritizes available capacity to be distributed downstream (by other parties) instead of the traditional destination of a specific end-use customer or clearly defined market. While this trend shows the market adapting to economic interests (of producers, developers, and ratepayers), it also lacks the distinct customer contracted to receive firm capacity that has been the primary means by which FERC has assessed market need for a project. Moving from micro-level (contracted service) to macro-level arrangements (pooling capacity for sale by other entities) illustrates the changing environment of the US natural gas markets under FERC jurisdiction.

The NOI proffers a number of questions aimed at the evaluation of project need, emphasizing a more cohesive strategy for broadening its analytical scope. The NOI asks commenters to explain what types of alternative evidence might be necessary in lieu of the information typically conveyed in a precedent agreement. FERC may also receive comments on various topics, including whether to: use different classifications of public benefit; distinguish between affiliate and non-affiliate precedent agreements; require additional or alternative evidence of need; and change its analysis if multiple pipeline applications are pending in the same geographic area.

If FERC implements new criteria to look beyond precedent agreements, natural gas producers, exporters and pipeline developers could reap benefits from an expanded array of possible bases to demonstrate project need, even where a precedent agreement is not yet in place. On the other hand, walking away from the "bright line" of reliance on affiliated and unaffiliated precedent agreements to demonstrate need may undermine regulatory certainty and thus slow investment.

## Landowner Interests

While FERC's regulations include significant public participation measures, including landowner notification of potential proximate impacts, some community stakeholders find the process inadequate. The NOI explores how to better accommodate the interests of local parties, particularly in the environmental portion of the review. Although incorporated into this component of a certificate proceeding, landowners' rights issues—most frequently right-of-way ("**ROW**") negotiations—are disparate than those under the purview of NEPA. Applicants can only use eminent domain after the certificate for the project has been issued. FERC considers the likelihood of an applicant invoking eminent domain into its appraisal of a project by weighing the impact on landowners relative to the expected benefits. Striking a balance between fruitful ROW negotiations with landowners and outstanding parcels that must be integrated by invoking eminent domain is an imprecise art.

The NOI asks commenters if its current approach to eminent domain should be adjusted, particularly if the overarching priority is to enhance landowner engagement. One question raises the prospect of encouraging alternative routes in order to minimize eminent domain. However, the NOI also seeks comments on how pursuing alternative routes may affect the costs of a project, and to what extent an applicant should be required to take such an action.

## Consideration of Environmental Impacts

An important component of the review process is the appraisal of the potential environmental effects of a proposed project required under NEPA. NEPA allows FERC to consider site-specific environmental factors in addition to cumulative impacts (in terms of both time and geography). Recently, many stakeholders adverse to pipeline development have focused on the amount of greenhouse gas emissions released by natural gas projects. Intervenors in FERC certificate proceedings—such as environmental advocacy groups and federally recognized tribes—have asked FERC to pursue a distinct analysis of climate change impacts. However, as there is no universal standard upon which to measure project-specific impacts, FERC has resisted adopting a significance threshold to determine if a project would exceed reasonable emissions levels. Moving beyond its obligations under NEPA, FERC has provided additional information on production-related greenhouse gas emissions for certain projects. The causal relationship between incremental projects and global climate change impacts remains tenuous.

Intervenors have often asserted that the cumulative impacts of proposed projects have not been adequately measured or reviewed in FERC proceedings to date. The NOI aims to gather information on larger scale approaches, such as regional sizing and boundaries for cumulative impact analyses. Further, if upstream and/or downstream emissions information is made available, FERC is considering how to integrate such criteria into decision-making. Certain stakeholders believe that a Social Cost of Carbon tool is required in the public interest determination for natural gas projects. To this point, FERC has resisted implementing any such model—and there is no established industry standard. The NOI takes up the question of whether to implement a Social Cost of Carbon tool also.

## Application Process

Finally, like any large agency, FERC recognizes existing inefficiencies in its application review process. While it may never be possible to optimize the entire timeline, project proponents have brought forward concerns regarding the long lead time on the FERC process and regulatory uncertainty caused by FERC's limited ability to require cooperating state and federal agencies to toe the line on timely approval of necessary permits. If the project is mired in a protracted review, the overall costs can increase exponentially and therefore negatively affect all parties involved (including eventual customers). To that end, Executive Order 13807, recently issued by President Donald Trump, instructed federal agencies to complete their respective review processes within two years.

If FERC hastens its timetable for review, a shortened application process could yield benefits to applicants. This would be especially true if the applicant had completed the pre-filing process at FERC. Pre-filing can preemptively root out any potential issues prior to filing the full application; notably, the applicant can engage with relevant FERC staff in devising ways to lessen or mitigate environmental impacts. Still, some stakeholders find that pre-filing leads to biased (favorable) outcomes — FERC maintains that applications are more likely be approved following pre-filing because potential obstacles were resolved prior to the application. On the other hand, there may be cause to lengthen certain parts of the process. Extending the deadline for intervening parties to file comments has been raised by affected stakeholders and may have support among some commissioners at FERC.

The NOI is a wide ranging collection of requests for comment that signal FERC is considering changes to nearly every aspect of its Policy Statement. Whether those changes are beneficial for pipeline development will depend on the nature of comments received and how FERC expects to balance encouraging continued investment in energy infrastructure against concerns of overbuild, landowner rights and environmental impacts. At this stage of FERC's review, it is unclear how significant any changes FERC actually decides to make will be to the US natural gas industry.

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