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INVESTMENT ADVISORS

The Federal Energy Regulatory Commission (FERC) starts evaluating the Five-Year Index Level for Interstate Oil Pipeline rates; What does that mean to Midstream Investors?

What is this about?

Every five years, FERC will review and set a new rate to calculate annual changes to the interstate oil pipeline rate. Last time FERC set the rate for 2016-2021, and the rate decision was made at the end of 2015 for the rate to be active on July 1, 2016.

The rate FERC used to calculate annual changes to the interstate oil pipeline rate is based on the Producer Price Index for Finished Goods (PPI-FG) with some adjustments to reflect industry cost changes. For July 1, 2016, through mid-2021, the index is based on PPI-FG +1.23%, with a multiplier provided each year based on the annual percent change in the PPI-FG.

In its 2020 review, FERC is expected to evaluate the index based on how costs changed from 2014 through 2019.

FERC is currently seeking comments on their proposed Interstate Oil Pipeline Rates, and the Commission encouraged oil pipelines to file updated to reflect the revised ROE methodology.

What has proposed for 2020?

Last week, FERC proposed a new pipeline index level of PPI-FG +0.09% for the five years beginning July 2021. It is a step down from 1.23% for 2016-2021, but it is reassuring to see a positive adder put forth for comments.

Why is it important?

The AMZ, which consisted of 50% petroleum pipeline transportation companies by weighting, was down 2.2% Thursday and Friday (6/18 and 6/19), compared to a 0.5% decline for the S&P500. The reaction was relatively muted compared to the sell-off in March 2018 policy revision when AMZ Index lost 22% from Jan peak to March low.

What is next?

- **The deadline for comments is September 11, 2020.**
- **Industry expected a finalized index methodology and new index level at the end of 2020**
- **The new rate will become effective July 1, 2021, for an interstate oil pipeline operator. The rate will have no or indirect effect for market-based rates or negotiated rates**

The bottom line: The rate is only applying if a pipeline ultimately determines that the new index level is fair and providing a reasonable return. If not, it could file a rate case with the FERC to petition for a higher rate. It is also important to keep in mind that FERC is ultimately tasked with ensuring that interstate pipeline rates are just and reasonable.

<https://www.ferc.gov/news-events/news/ferc-seeks-comment-five-year-index-level-interstate-oil-pipeline-rates>

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The S&P Index is a market capitalization weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. The Alerian MLP Index (NYSE: AMZ) is a widely recognized, unmanaged index that includes a composite of the 50 most prominent energy MLPs. You cannot directly invest in these indices.

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