

UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;  
Nora Mead Brownell, Joseph T. Kelliher,  
and Suedeen G. Kelly.

Tennessee Gas Pipeline Company

Docket Nos. RP02-114-004  
RP02-114-005  
RP02-114-006

ORDER ON REHEARING AND COMPLIANCE FILING

(Issued August 9, 2004)

1. On December 24, 2003, the Commission issued an order on rehearing, clarification and compliance filing addressing Tennessee Gas Pipeline Company's (Tennessee) 2001 annual cashout refund report.<sup>1</sup> This order addresses requests for rehearing of the December 24, 2003 Order, Tennessee's February 23, 2004 filing of a revised refund proposal to comply with the December 24, 2003 Order, and changes to Tennessee's tariff's cashout provisions it proposes to be effective March 24, 2004. As discussed below, rehearing is denied, the refund plan proposed in its February 23, 2004 filing is found to be in compliance with the December 24, 2003 Order, and Tennessee's proposed tariff revisions are found just and reasonable and accepted effective March 24, 2004.

**Background**

2. As a result of its Cosmic Settlement in Docket No. RP86-119, *et al.*,<sup>2</sup> Tennessee maintained a Volumetric Transition Cost Account (VTCA) to recover certain take-or-pay costs. Under the Cosmic Settlement, Tennessee absorbed 50 percent of the take-or-pay costs while the other 50 percent was allocated to its customers. Of the 50 percent of the take-or-pay costs allocated to Tennessee's customers, 41.78 percent of the costs were classified as demand costs and recovered through a demand transition cost account and 8.22 percent were classified as volumetric costs and recovered through a surcharge. The

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<sup>1</sup> Tennessee Gas Pipeline Company, 105 FERC ¶ 61,367 (2003).

<sup>2</sup> Tennessee Gas Pipeline Company, 52 FERC ¶ 61,045 (1990).

volumetric costs were recorded in the VTCA and are allocated to Market Area Shippers (76.9 percent) and Supply Area Shippers (23.1 percent). The volumetric costs were recovered through surcharges that take effect April 1 of each year. In addition, pursuant to a later cashout settlement, Tennessee's Rate Schedules LMS-MA (Load Management Service-Market Area) and LMS-PA (Load Management Service-Pooling Area) require net cashout gains that Tennessee owes its customers to be credited to the VTCA in the same manner as take-or-pay costs, that is, 76.9 percent to the Market Area VTCA subaccount and 23.1 percent to the Supply Area VTCA subaccount. Section 7(g)(iii) of Tennessee's Rate Schedule LMS-MA provides that if the Market or Supply Area Volumetric Surcharge is terminated, Tennessee must file a plan to refund the net cashout gains attributable to the terminated account. Tennessee is required to file an annual report containing the net cashout balance as of November 30 of each year.

3. In its 2001 annual cashout refund report, Tennessee reported that it had a net total gain from cashouts of \$10,600,893 and a VTCA balance of \$11,038,881. Most of the VTCA balance was attributable to Supply Area Shippers. Pursuant to its tariff, Tennessee would have been required to credit most of the cashout gains to Market Area Shippers. As a result, the Market Area VTCA subaccount would be paid down to zero leaving a negative balance of about \$8 million. Because there was still a substantial balance in the Supply Area VTCA account which Tennessee estimated would take about seven years to extinguish, Tennessee proposed to credit the entire cashout gain to both VTCA accounts, treat the VTCA balance as being reduced to zero, and terminate the take-or-pay provisions of the tariff. On January 17, 2002, the Commission issued an Order rejecting Tennessee's proposal and ordered Tennessee to file a revised refund plan.<sup>3</sup> The Commission found that to apply the entire net cashout gain to reduce the overall take-or-pay balance would result in unjust cost shifting and would unfairly burden Market Area Shippers with take-or-pay costs they were not allocated under the Cosmic Settlement.

4. On December 19, 2002, the Commission issued an order on Tennessee's revised refund report.<sup>4</sup> Among other things, the order rejected Tennessee's and other parties' proposals for refund of the remaining net cashout balance of approximately \$8 million. The Commission found that, after fulfilling the obligation under the Cosmic Settlement, the residual revenues were, by their nature, cashout revenues and should be refunded as such to the source of the cashout revenues, *i.e.*, the point operators on Tennessee's system

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<sup>3</sup> Tennessee Gas pipeline Company, 98 FERC ¶ 61,034 (2002).

<sup>4</sup> Tennessee Gas Pipeline Company, 101 FERC ¶ 61,303 (2002).

pursuant to Operational Balancing Agreements at each point. Therefore, the order directed Tennessee to file a revised refund plan to refund the \$8 million in cashout revenues to OBA point operators.

5. On December 24, 2003, the Commission issued an order on Tennessee's filing to comply with the December 19, 2002 Order and various requests for rehearing and clarification.<sup>5</sup> The December 24, 2003 Order clarified that all balancing parties under the cashout provisions of Rate Schedules LMS-PA and LMS-MA, who are subject to penalties, are eligible for refunds under the refund mechanism, and not just the OBA point operators. The order also clarified that it was equitable and reasonable for the \$8 million balance to be refunded only to Market Area shippers and OBA parties. The Commission found that Supply Area shippers should not receive a refund because over \$2 million in net cashout gains were already allocated to their VTCA account. The Commission determined that to allocate any more of the net cashout gains to Supply Area shippers would constitute an inequitable subsidy by Market Area shippers. The Commission clarified that the refund allocation method must reflect a refund based on total monthly commodity volumes for eligible parties, inclusive of imbalance volumes that are within certain tolerances.

6. Indicated Shippers<sup>6</sup> and National Fuel Gas Distribution Corporation (National Fuel) filed requests for rehearing of the December 24, 2003 Order. On February 23, 2004, Tennessee filed its cashout report and refund plan to comply with the December 24, 2003 Order. Tennessee included in its filing proposed changes to Section 7(g)(iii) of Rate Schedule LMS-MA to prospectively establish a cashout refund allocation methodology for the future that would not reflect the historic take-or-pay allocation percentages of the Cosmic Settlement, to be effective March 1, 2004. The Tennessee Municipal Group<sup>7</sup> filed a protest to the revised refund plan of Tennessee's compliance filing. The requests for rehearing and protests will be addressed below.

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<sup>5</sup> Tennessee Gas Pipeline Company, 105 FERC ¶ 61,367 (2003).

<sup>6</sup> The Indicated Shippers are Amerada Hess Corporation, ConocoPhillips Company, ExxonMobil Gas Marketing Company (A Division of Exxon Mobil Corporation), and Shell Offshore Inc.

<sup>7</sup> The Tennessee Municipal Group consists of the Cities of Clarksville, Springfield, Portland, and Waynesboro, Tennessee; the Corinth Public Utilities Commission, Mississippi; the West Tennessee Public Utility District; the Greater Dickson Gas Authority; and the Humphreys County Utility District.

7. On May 3, 2004, the Director, Division of Tariffs and Market Development-East issued a data request to Tennessee requesting further supporting information and explanations of Tennessee's February 23, 2004 Cashout Report Compliance and Refund Plan Filing. The purpose of the data request was to be able to better evaluate the filing in light of certain issues that were raised in the protests and requests for rehearing. On May 20, 2004, and May 28, 2004, in Docket No. RP02-114-006, Tennessee submitted responses to the data request. Comments and protests to Tennessee's data responses were due June 15, 2004. On June 15, 2004, the Tennessee Municipal Group filed a protest to the data responses, which will also be addressed below.

### **Tennessee's Compliance Filing**

8. In its February 23, 2004 compliance filing, Tennessee submitted a revised refund plan reflecting cashout refunds of \$8,120,479 allocated solely to Market Area shippers and OBA parties based on total commodity volumes. Tennessee states that it will make refunds consistent with its revised plan as listed in Appendix B of its compliance filing by credits to invoices within 60 days of a final order in this proceeding. Tennessee states that the plan includes the appropriate LMS-PA parties in the Market Area and excludes the appropriate LMS-MA parties in the Supply Area. Additionally, Tennessee states that it has reviewed each transportation contract that was cashed out during the cashout period to exclude from the cashout refund plan those transactions that were Supply Area and include those transactions that were Market Area.

9. In addition, Tennessee included in its filing proposed changes to section 7(g)(iii) of Rate Schedule LMS-MA and Article XXV of its GT&C to prospectively establish a specific cashout refund allocation methodology for the future, and to terminate the use of the take-or-pay VTCA as the vehicle to refund net cashout revenues. Tennessee proposes an effective date of March 24, 2004. As noted above, existing section 7(g)(iii) of Tennessee's Rate Schedule LMS-MA provides that if the Market or Supply Area Volumetric Surcharge is terminated, Tennessee must file a plan to refund the net cashout gains attributable to the terminated account. Tennessee's Market Area Volumetric Surcharge previously has been terminated. Tennessee stated that on February 18, 2004, in Docket No. RP04-172-000, it filed to terminate the Supply Area Volumetric Surcharge effective February 1, 2004.<sup>8</sup> Tennessee states that the Supply Area VTCA balance declined to zero in the month of January 2004, and pursuant to its tariff, the surcharge is to be eliminated on the first day of the month after the balance is reduced to zero. Tennessee states that, with this event, both the Market Area and Supply Area surcharges

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<sup>8</sup> Tennessee's tariff sheets in Docket No. RP04-172-000 were accepted on March 12, 2004 by a Director's Letter Order.

have been terminated and the balances in the respective accounts reduced to zero. Tennessee states that, as such, the existing provisions of Tennessee's tariff that credit cashout gains to the take-or-pay VTCA are no longer relevant or appropriate for future refunding of cashout gains. Consequently, Tennessee states that it is submitting revised tariff sheets<sup>9</sup> modifying section 7(g)(iii) of its Rate Schedule LMS-MA to provide for refunds of net cash-out revenues to Non-Offending balancing parties based on commodity volumes without distinction between market area and supply area parties. Tennessee states that it is also filing conforming changes to Article XXV of the General Terms and Conditions to eliminate from the VTCA section any reference to the cashout provisions under Rate Schedules LMS-MA and LMS-PA.<sup>10</sup> Tennessee requests that the Commission grant all necessary waivers of the Commission's regulations to permit such tariff sheets to become effective on March 24, 2004.

## **Discussion**

### **A. Rehearing**

10. On rehearing, Indicated Shippers assert that Tennessee's tariff expressly provides for a reopening of the allocation methodology once either the Market Area or Supply Area VTCA account is extinguished. Indicated Shippers cites to section 7(g)(iii) of Rate Schedule LMS-MA which states the pipeline is required to file a refund plan and "[a]ll Balancing Parties/Shippers will have the right to challenge the refund calculation and allocation methodology." Indicated Shippers states that in the December 24, 2003 Order the Commission held that Tennessee's VTCA tariff provisions make the Cosmic Settlement allocation the most equitable allocation of net cashout revenues. Indicated Shippers argue that the Commission's December 24, 2003 Order renders the parties' opportunity to comment on Tennessee's proposed allocation meaningless.

11. The Commission denies Indicated Shippers' request for rehearing on this issue. Tennessee originally filed a refund plan, parties commented on it and the Commission rejected it because it would result in unjust subsidization of Supply Area take-or-pay costs by Market Area Shippers. Tennessee then filed a revised plan and the Commission held a technical conference. Tennessee, in its technical conference comments, reflected four alternative allocation methods proposed by the parties. Finally, parties had an opportunity to comment on the revised refund plan and cashout report that was the

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<sup>9</sup> Seventh Revised Sheet No. 209A and Seventh Revised Sheet No. 209B to Tennessee's FERC Gas Tariff, Fifth Revised Volume No. 1.

<sup>10</sup> Fourth Revised Sheet No. 393 to Tennessee's FERC Gas Tariff, Fifth Revised Volume No. 1.

subject of the December 24, 2003 Order. Accordingly, the Commission finds that the tariff procedures were followed and parties had an ample opportunity to comment on the proposed refund methodology on several different occasions.

12. Both Indicated Shippers and National Fuel filed requests for rehearing asserting that the December 24, 2003 Order incorrectly excludes certain parties from receiving refunds of the net cashout revenues. Indicated Shippers assert that the balancing parties who cash out their imbalances with Tennessee on a monthly basis, and thus bear the cost of imbalances, may not be transportation shippers on Tennessee's system. Indicated Shippers submit that parties to balancing agreements under Rate Schedule LMS-PA can include producers, pipelines, plant operators, and supply aggregators. Indicated Shippers contend that the December 24, 2003 Order would exclude LMS-PA balancing parties that are not also firm transportation shippers from eligibility for any refunds of net cashout revenues. National Fuel argues that the Commission should ensure that Market Area shippers who are not LMS-MA shippers receive a portion of the refunds.

13. In its responses to the data requests, Tennessee explained which parties were eligible for the cashout refunds and for what volumes. Tennessee stated that, to determine the parties eligible for the cashout refund, Tennessee first identified all balancing parties from September 2000 through August 2001 that were subject to the cashout provisions and were in the Market Area. It stated that those balancing parties included those with contracts under various types of service: LMS-MA, LMS-PA, SA, LMSPL, IT, and NET. Then, it stated, for each balancing contract identified, it determined if the monthly imbalance percentage, either actual or operational, was less than or equal to 5% or if the monthly actual or operational imbalance was less than or equal to 1,000 Dth. Tennessee stated that, if either the actual or operational imbalance percentage was less than or equal to 5% or the actual or operational imbalance was less than or equal to 1,000 Dth, then it included that contract for that particular month in the refund distribution. If the monthly actual and operational imbalance percentage was greater than 5% and the monthly actual and operational imbalance was greater than 1,000 Dth, then Tennessee stated that it excluded that contract for that particular month from the refund distribution.

14. The Commission finds that Tennessee's data request responses fully addresses the questions raised in the requests for rehearing by explaining what entities are eligible for a share of the cashout refunds. Further, the Commission finds that Tennessee's data request responses demonstrate that its revised refund plan is consistent with the Commission's goal in this proceeding of ensuring that the cashout refunds are distributed to the sources of the cashout revenues, that is, the balancing parties, shippers, and any other entities in the Market Area who were subject to Tennessee's cashout mechanism. In light of the

fact that neither Indicated Shippers nor National Fuel filed protests to Tennessee's data request responses and, therefore, appear to be satisfied that their concerns are met by Tennessee's revised plan as clarified by its data request responses, we deny rehearing on these issues as moot.

15. Indicated Shippers states that it is not entirely clear whether the Commission intends by the December 24, 2003 Order to perpetuate the 76.9 percent/23.1 percent division of net cashout gains even after both the Market Area and Supply Area take-or-pay accounts have been extinguished. Indicated Shippers submits that the order appears to suggest at least that the Cosmic Settlement percentage allocations would no longer be appropriate when both VTCA accounts have been terminated. Indicated Shippers states that once the Supply Area VTCA account has been extinguished, the Commission could revisit the allocation of net cashout revenues. Indicated Shippers asserts that the order is unclear as to whether the Commission is actually committing to revisit the allocation once both VTCA accounts are terminated. Indicated Shippers argue that, at a minimum, the Commission should clarify that it does not intend to perpetuate the allocation of net cashout revenues based on allocation of a portion of take-or-pay costs under the Cosmic Settlement.

16. The Commission finds that this issue is moot. In its February 23, 2004 compliance filing, Tennessee observes that both the market area and supply area surcharges are now terminated and that its revised tariff sheet proposal provides a procedure for refunds to Non-Offending balancing parties based on commodity volumes without distinction between market area and supply area parties. There were no protests to the tariff proposal which modifies the tariff to provide that the allocation of cashout revenues will no longer be tied to the allocation methodology related to the recovery of take-or-pay costs under the Cosmic Settlement, consistent with Indicated Shipper's clarification request. Since this order is accepting Tennessee's revised tariff sheets, Indicated Shippers' rehearing is denied as moot.

## **B. Compliance**

17. In its protest to Tennessee's compliance filing, the Tennessee Municipal Group asserts that the Commission must reject the proposed distribution of refunds and require Tennessee to include OBA point operators that have purchased swing storage service under Rate Schedules FT-G and FT-GS. Tennessee Municipal Group states that in informal conversations concerning the February 23, 2004 filing, Tennessee has stated that swing storage customers are not entitled to a share of net cashout refunds because FT-G and FT-GS customers are not balancing parties under Rate Schedules LMS-MA or LMS-PA that are subject to penalties. Tennessee Municipal Group states that, in its Order No. 637 implementation proceeding, Tennessee stressed that swing storage service provided under Rate Schedules FT-G and FT-GS provide limited daily rights and if these

customers exceed their rights and were denied authorized overrun, the cashout penalties under the LMS Rate Schedules would apply.<sup>11</sup> Tennessee Municipal Group argues that, thus, according to Tennessee, swing storage customers are subject to the Rate Schedule LMS penalties. Tennessee Municipal Group submits that swing storage customers have been among the best non-offending customers that have achieved a zero imbalance during the historic period and are obviously entitled to share in cashout refunds. Tennessee Municipal Group also requests that the Commission direct Tennessee to clarify the proposed tariff language to ensure that swing storage customers will receive cashout refunds in the future.

18. Tennessee Municipal Group states that, without explanation, Tennessee has proposed that one of the members of the Tennessee Municipal Group, the City of Clarksville, Tennessee (Clarksville), will not receive a share of cashout refunds. Tennessee Municipal Group states that, unlike other members of the group, Clarksville does purchase firm transportation under Rate Schedule FT-A and would not be excluded from refunds under Tennessee's theory that Clarksville would not be subject to penalties. Tennessee Municipal Group asserts that the Commission should direct Tennessee to explain why Clarksville did not receive refunds and allow the Tennessee Municipal Group to respond to its explanation.

19. In its June 15, 2004 protest to Tennessee's data responses, the Tennessee Municipal Group essentially reiterates its earlier protest. It asserts that Tennessee has not adequately explained in the data response why certain shippers were excluded from refunds. Tennessee Municipal Group argues that the Tennessee theory is an obvious misinterpretation of the December 24, 2003 Order in this proceeding that clearly provided that Delivery Point Operators that stayed within the 0-5 percent imbalance range were eligible for the cash-out refunds. Tennessee Municipal Group also contends that Tennessee's present assertion that the Rate Schedule FT-G and FT-GS swing customers are not subject to the cash-out provisions of the LMS Rate Schedule are wholly undermined by Tennessee's own statements that stressed that these customers were subject to such cash-out provisions.

20. We find no merit in the Tennessee Municipal Group's objections to Tennessee's revised refund plan and will accept the revised plan as in compliance with the Commission's December 24, 2003 Order. In its response to the data request, Tennessee explained that the members of the Tennessee Municipal Group that were not included in

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<sup>11</sup> *Citing*, "Motion for Leave to Answer and Answer of Tennessee Gas Pipeline Company" at p. 9 filed in Tennessee Gas Pipeline Company, Docket No. RP00-477 on November 3, 2000.

the refund are those shippers that elected to use firm storage service in conjunction with their FT-GS transportation service to effect load balancing.<sup>12</sup> Tennessee stated that the LMS-MA Rate Schedule cashout option applies only to those balancing parties that have not elected to use storage to resolve daily variances.<sup>13</sup> Tennessee stated that all shippers that use storage for load balancing were excluded from the cashout refund calculation because they are not subject to the cashout provisions of the LMS-MA Rate Schedule. Tennessee stated that this includes not only the FT-GS shippers that are members of the Tennessee Municipal Group but also FT-A shippers that have elected to swing on storage.

### **C. Proposed Tariff Changes**

21. Although it was not directed to do so, Tennessee included in its filing proposed changes to section 7(g)(iii) of Rate Schedule LMS-MA and Article XXV of its GT&C to prospectively establish a specific cashout refund allocation methodology for the future, and to terminate the use of the take-or-pay VTCA as the vehicle to refund net cashout revenues. Section 154.203(b) of the Commission's regulations states that "compliance filings may not be combined with other rate or tariff change filings." However, since Tennessee's VTCA surcharges have been terminated, it makes sense to eliminate the provisions requiring crediting of cashout gains to the VTCA in this proceeding. Accordingly, for good cause, the Commission will waive section 154.203(b) and permit Tennessee to include the proposed tariff change in the subject compliance filing. The Commission finds that the proposed tariff changes, which are not protested, are just and reasonable because they eliminate out-of-date take-or-pay allocation requirements attributable to the Cosmic Settlement and provide for all net cash-out revenues to be refunded to Non-Offending balancing parties based upon their commodity volumes. Therefore, Tennessee's tariff changes comply with section 284.12(b)(2)(v) of the Commission's regulations, which states that "[p]ipelines may not retain net penalty revenues, but must credit them to shippers in a manner to be prescribed in the pipeline's tariff." Accordingly, the Commission will accept the proposed tariff sheets to be effective March 24, 2004.

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<sup>12</sup> Tennessee referenced Section 7 of its FT-GS Rate Schedule, Sixth Revised Sheet No. 168.

<sup>13</sup> Tennessee referenced Sections 7 and 8 of Rate Schedule LMS-MA, on Sixth Revised Sheet No. 205 and Sixth Revised Sheet No. 209B.

The Commission orders:

(A) The requests for rehearing are denied as discussed above.

(B) Tennessee's revised refund plan in its February 23, 2004 filing in this proceeding is accepted as in compliance with the Commission's December 24, 2003 Order. Tennessee is directed to make refunds consistent with its revised plan within 60 days of a final order in this proceeding.

(C) Seventh Revised Sheet No. 209A, Seventh Revised Sheet No. 209B, and Fourth Revised Sheet No. 393 to Tennessee's FERC Gas Tariff, Fifth Revised Volume No. 1, are accepted to be effective March 24, 2004.

By the Commission.

( S E A L )

Magalie R. Salas,  
Secretary.