

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

El Paso Natural Gas Company

Docket No. CP05-2-003

ORDER DENYING REQUEST FOR REHEARING

(Issued April 21, 2006)

1. On December 19, 2005, Phelps Dodge Corporation (Phelps Dodge) filed a timely request for rehearing of the order issued in *El Paso Natural Gas Company*, 113 FERC ¶ 61,183 (November 18, 2005). The November 18 order denied requests for rehearing and clarification of an order issued in *El Paso Natural Gas Company*, 111 FERC ¶ 61,408 (June 16, 2005).
2. For the reasons discussed below, we will deny Phelps Dodge's request for rehearing.

I. Background

3. El Paso operates an interstate pipeline system extending from production areas in the southwestern United States through Texas, New Mexico, Colorado, and Arizona to two points of termination at the boundary between Arizona and California near Topock and Ehrenberg, Arizona. At Topock, El Paso's northern system interconnects with Mojave Pipeline Company (Mojave) and other pipelines.
4. Mojave, an affiliate of El Paso, operates an interstate pipeline extending from interconnects with El Paso's northern system and other pipelines near Topock to a point near Bakersfield, California. Mojave interconnects with Kern River Gas Transmission Company (Kern River) near Daggett, California.
5. In 1996, El Paso entered into an offer of settlement with its customers to resolve all of the issues in El Paso's Natural Gas Act section 4 rate case in Docket No. RP95-363-000. Article 11 of the settlement contained provisions that would continue beyond the termination of the 10-year settlement, *i.e.*, December 31, 2005. One of those

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continuing provisions, Article 11.2(b) of the settlement, provided that El Paso, not its shippers, would be at risk for 1995 capacity that becomes unsubscribed, or is subscribed at less than the maximum applicable tariff rate.¹ We approved the settlement in *El Paso Natural Gas Company*, 79 FERC ¶ 61,028, *reh'g denied*, 80 FERC ¶ 61,084 (1997).

6. On June 30, 2005, in Docket No. RP05-422-000, El Paso filed a general rate case under section 4. We accepted El Paso's proposed tariff sheets and suspended their effectiveness until January 1, 2006, subject to certain conditions.² In its rate case filing, El Paso requested, among other things, that the Commission find that the provisions of Article 11.2(b) no longer apply.

7. In a March 20, 2006 Order,³ we found that the rate protections of Article 11.2 still apply for the eligible shippers (hereafter referred to as Article 11.2 rate shippers).⁴ We found that, pursuant to Article 11.2(b) of the 1996 Settlement, the rates charged to Article 11.2 rate shippers for any service may not include any costs related to (1) unsubscribed capacity that was part of El Paso's system on December 31, 1995 or (2) any such capacity sold at a rate less than the rate cap.

¹ Article 11.2(b) states that:

El Paso agrees that the firm rates applicable to service to any Shipper to which this paragraph 11.2 applies will exclude any cost, charge, surcharge, component, or add-on in any way related to the capacity of its system on December 31, 1995, to deliver gas on a forward haul basis to the Shippers listed on Pro Forma Tariff Sheet Nos. 33-35, that becomes unsubscribed or is subscribed at less than the maximum applicable tariff rate as escalated pursuant to paragraph 3.2(b). El Paso assumes full cost responsibility for any and all existing and future step-downs or terminations and the associated [contract demand]/billing determinants related to the capacity described in this subparagraph (b).

² *El Paso Natural Gas Co.*, 112 FERC ¶ 61,050 (2005).

³ *El Paso Natural Gas Co.*, 114 FERC ¶ 61,290 (2006) (March 20 order).

⁴ Article 11.2 applies to “any firm Shipper with a [transportation service agreement] that was in effect on December 31, 1995, and that remains in effect, in its present form or as amended, on January 1, 2006, but only for the period that such Shipper has not terminated such [transportation service agreement].”

II. The June 16 and November 18 Orders

8. In the June 16 Order, we authorized El Paso to acquire, convert, and operate an 87.8-mile long, 30-inch diameter segment of an existing crude oil pipeline known as Line 1903. The pipeline segment to be acquired and operated as a natural gas transmission line extends from the termination point of El Paso's southern system near Ehrenberg, Arizona northwest to Cadiz, California. The June 16 Order also authorized El Paso to construct and operate 6.4 miles of 30-inch diameter line and associated metering facilities to connect the 87.8-mile long segment of Line 1903 to Mojave's system near Cadiz (the Cadiz Crossover).⁵

9. As part of its proposals, El Paso entered into six precedent agreements for firm transportation capacity. Three of the precedent agreements are with existing Topock customers of El Paso (extension contracts).⁶ El Paso states that these precedent agreements represent commitments by the three shippers to extend their existing contracts because of El Paso's Line 1903 proposals. El Paso also entered into three precedent agreements with new customers.⁷

10. The June 16 Order found that El Paso's proposals met the threshold requirement of the Certificate Policy Statement,⁸ holding that existing customers would not subsidize the proposals since projected revenues exceeded expected costs. We pre-determined that

⁵ As part of its Line 1903 project, El Paso acquired capacity on Mojave's system in order to transport gas on Mojave west from Topock to the Cadiz Crossover and to transport gas east from Mojave's connection with Kern River at Daggett to the Cadiz Crossover.

⁶ These precedent agreements are with the Arizona Public Service Company and Pinnacle West Energy Corporation, Salt River Project Agricultural Improvement and Power District (Salt River), and Southwest Gas Corporation for 182,106 Mcf per day of firm transportation.

⁷ These precedent agreements are with the California Department of Water Resources, Coral Energy Resources, L.P., and Salt River for 189,438 Mcf per day of firm transportation from Daggett.

⁸ *Certification of New Interstate Natural Gas Pipeline Facilities* (Certificate Policy Statement), 88 FERC ¶ 61,227 (1999), *order clarifying statement of policy*, 90 FERC ¶ 61,128, *order further clarifying statement of policy*, 92 FERC ¶ 61,094 (2000).

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the costs associated with the Line 1903 project qualify for rolled-in rate treatment in El Paso's next general section 4 rate filing, absent a material change in circumstances.

11. Several parties filed for rehearing of the June 16 Order. In their rehearing requests, three parties, including Phelps Dodge,⁹ contended that under Article 11.2(b) of the 1996 Settlement, El Paso was precluded from including any costs in its rates associated with the stranding of 1995 capacity on El Paso's system. Because Article 11.2(b) insulated the shippers from bearing stranded capacity costs, these parties asserted that if there were no extension contracts and the capacity associated with the contracts were stranded, there would be no impact on future rates for virtually all of the remaining firm shippers on El Paso's system. Thus, the parties concluded that the extension contracts cannot be a system benefit under the Certificate Policy Statement.

12. In the November 18 Rehearing Order, we stated that the Article 11.2(b) issue need not be addressed, because it would be addressed in a separate order in El Paso's ongoing rate proceeding in Docket No. RP05-422-000.

III. Phelps Dodge's Request for Rehearing of the November 18 Order

13. In its request for rehearing of the November 18 Order, Phelps Dodge requests that the Commission reverse its pre-determination of rolled-in rate treatment, contending that the Commission erred in finding that the extension contracts created a system benefit. Phelps Dodge asserts that, by deferring the Article 11.2(b) issue to the rate case in the November 18 Order and continuing to include the extension revenues in its rolled-in rate determination, the Commission irrevocably prejudiced the rights of the shippers in the pending rate proceeding. If the Commission denies El Paso's request in the rate case to disregard Article 11.2(b), Phelps Dodge contends that the Commission should also modify its finding that the extension contracts provide an economic benefit. However, Phelps Dodge points out that the Commission will not be able to grant that relief, because the pre-determination of system benefits for the Line 1903 project is not at issue in El Paso's rate case. Thus, Phelps Dodge requests that the Commission must now find that the extension contracts did not create a system benefit or, in the alternative, clarify that its pre-determination finding in this case is conditioned on the outcome of the rate proceeding.

IV. Discussion

14. In the June 16 order, we found that existing customers would not subsidize the project because the proposed revenues for the project, \$31.4 million, exceed the cost of

⁹ The parties that raised the issue of Article 11.2(b) are Phelps Dodge, the El Paso Municipal Group, and El Paso Electric Company.

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the project, \$23.4 million.¹⁰ We also found that the Line 1903 project would provide direct benefits to El Paso's system by ameliorating the historical service reliability problems engendered, in part, by use of displacement. Finally, we found that the project would provide access to new supply sources that were previously unavailable to the interstate gas market due to a lack of infrastructure.

15. Phelps Dodge contends that the revenues from the extension contracts cannot be included in the comparison of revenues and costs from the project, because Article 11.2(b) precludes El Paso from shifting the cost of unsubscribed capacity to most of El Paso's customers. Phelps Dodge asserts that the extension contracts do not provide a system benefit by forestalling decontracting, because if the extension shippers terminated their contracts, the cost of the resulting unsubscribed capacity could not be included in the rates of the shippers covered by Article 11.2(b). Phelps Dodge states that El Paso's customers are already fully insulated from bearing any stranded capacity costs should the three extension shippers have chosen to terminate their contracts.

16. In the March 20 Order, we found that the rate protections of Article 11.2 continue to be in effect for the Article 11.2 rate shippers. Even though Article 11.2(b) continues to be in effect, however, we find, for the reasons discussed below, that the holding on Article 11.2(b) in the March 20 Order does not change the pre-determination of rolled-in rate treatment in this case.

17. As Phelps Dodge acknowledges, not all of El Paso's current customers are covered by the protections of Article 11.2(b). The provisions of Article 11.2 apply to any shipper with a transportation service agreement that was in effect on December 31, 1995 and that remains in effect on January 1, 2006. Any shipper that entered into a transportation service agreement after December 31, 1995 would not be covered by Article 11.2. While Phelps Dodge characterizes the shippers who do not have Article 11.2(b) protection as a "handful of new firm shippers who . . . represent only a small part of the system," in fact, there are over 20 shippers in this category. Those shippers would not be protected from the costs of unsubscribed capacity and would benefit from the extension contracts. We have previously ruled that a project need not benefit each and every customer on the system to be considered as providing a system

¹⁰ The cost could be further reduced depending on the outcome of the pending rate case with regard to whether the full acquisition cost of the crude oil pipeline is included in the Line 1903 project. In the June 16 order, we limited the pre-determination of rolled-in treatment to the costs associated with the 87.8-mile portion of the crude oil pipeline proposed in the Line 1903 project and deferred the issue of the treatment of the cost of the remaining 215-mile portion to El Paso's next general section 4 rate filing.

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benefit.¹¹ The fact that El Paso agreed not to charge certain shippers rates that include the cost of discounted or unsubscribed 1995 capacity does not alter the fact that extension contracts will provide additional revenue to the system. Thus, we find that shippers not covered by Article 11.2(b) will directly benefit from the lower maximum rates.

18. Next, it is likely that the Article 11.2(b) rate protections would not apply if the extension shippers terminated their contracts. The March 20 Order described how we would determine whether specific capacity was part of El Paso's 1995 system and covered by the Article 11.2(b) rate protections¹² stating that, if El Paso has 4,000 MMcf per day of firm capacity subscribed at the rate cap level or above,¹³ there will be a presumption that there is no 1995 stranded or discounted capacity. Thus, since El Paso's current system capacity is over 5.3 Bcf per day and is currently fully or nearly fully contracted, Article 11.2(b) might not apply even if the 186,295 Dth per day of extension contracts were terminated, unless substantial quantities of additional capacity were also unsubscribed or discounted below the rate cap level. We find that it is not only likely, but probable, that the Article 11.2 rate shippers will also benefit from the extension of these contracts to the extent that they opt to purchase additional services from El Paso that are not covered by Article 11.2. Thus, we conclude that the extension contract revenues were properly included in the analysis to determine that existing customers would not subsidize the Line 1903 project. For these reasons, Phelps Dodge's request for rehearing is denied.

19. Also, the orders issued in this proceeding and the related orders in El Paso's pending rate case were issued on a timely basis. The hearing in El Paso's rate case proceeding has been held in abeyance pending the issuance of the orders on the Article 11.2 issue and the technical conference issues. Thus, any assertion by Phelps Dodge that it, or the shippers in El Paso's rate proceeding, may have been irrevocably prejudiced is misplaced.

¹¹ See *Tennessee Gas Pipeline Co.*, Opinion No. 406, 76 FERC ¶ 61,022 at 61,101 (1996).

¹² 114 FERC at P 60 (2006).

¹³ In the 1996 Settlement, the parties agreed that the capacity of the El Paso system was slightly more than 4,000 MMcf per day. Thus, we will presume that the first 4,000 MMcf per day of firm subscribed capacity on El Paso's system is 1995 capacity.

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The Commission orders:

Phelps Dodge's request for rehearing is denied.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.