

133 FERC ¶ 61,129
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
John R. Norris, and Cheryl A. LaFleur.

El Paso Natural Gas Company

Docket No. RP08-426-002

ORDER ON REHEARING

(Issued November 10, 2010)

1. On June 30, 2008, El Paso Natural Gas Company (El Paso) filed a rate case pursuant to section 4 of the Natural Gas Act (NGA) in the above-captioned proceeding (2008 Rate Case). On August 5, 2008, the Commission issued an order accepting and suspending the tariff sheets El Paso filed in the 2008 Rate Case, subject to refund and conditions, and establishing a hearing and a technical conference.¹ Several parties filed requests for rehearing of the August 5 Order. For the reasons discussed below, the Commission denies the requests for rehearing.

I. The Instant Proceeding

2. In an effort to encourage long-term firm contracting, El Paso proposed to implement in the 2008 Rate Case rates for short-term services (for terms less than one year, but not equal to a five-month winter contract or a seven-month summer contract) capped at 250 percent of the related recourse rate. El Paso further proposed a revenue crediting mechanism whereby El Paso would credit 75 percent of the portion of the revenue it collects from short-term rates that exceeds the related long-term rates to the extent that its total revenues exceed the annual cost of service established in the 2008 Rate Case.

3. In the August 5 Order, the Commission accepted and suspended El Paso's primary tariff sheets, subject to conditions and the outcome of a hearing and technical conference and the outcome of certain pending requests for rehearing in Docket No. RP05-422-011. With respect to El Paso's short-term rate proposal, the August 5 Order denied requests for summary disposition of the issue and instead set the matter for hearing.

¹ *El Paso Natural Gas Co.*, 124 FERC ¶ 61,124 (2008) (August 5 Order).

II. Requests for Rehearing

4. Requests for rehearing of the August 5 Order were filed by El Paso, Arizona Public Service Company (APS), the Electric Generator Coalition (Generator Coalition),² and Gila River Power, L.P. (Gila River) and New Harquahala Generating Company, LLC (New Harquahala) (jointly). The Commission addresses the issues raised on rehearing in the discussion below.

A. Short-Term Rate Proposal

1. August 5 Order

5. In the August 5 Order, the Commission denied parties' requests for summary rejection of El Paso's short-term rate proposal.³ The Generator Coalition and others argued that El Paso's proposal was contrary to Commission precedent and that there were no genuine issues of material fact requiring a hearing.

6. The Commission disagreed, stating that the costs and benefits of the short-term rate proposal should be addressed in light of the other cost-of-service issues at the hearing.⁴ The Commission explained that El Paso's short-term rate proposal was similar to the short-term rates proposed by other pipelines.⁵ The Commission stated that in those cases, it found that the proposals might not be inconsistent with Order No. 637, which provides that a pipeline may propose a cost-based seasonal rate or term-differentiated

² The Electric Generator Coalition members include Blythe Energy, LLC; Dynegy Arlington Valley, LLC; Gila River Power, L.P.; Golden Spread Electric Cooperative, Inc.; GS Electric Generating Cooperative, Inc.; and New Harquahala Generating Company, LLC.

³ August 5 Order, 124 FERC ¶ 61,124 at P 25-26.

⁴ *Id.* P 27.

⁵ *Id.* P 26 (citing *Gas Transmission Northwest Corp.*, 117 FERC ¶ 61,315 (2006) (*GTN*); *Northern Border Pipeline Co.*, 113 FERC ¶ 61,230 (2005) (*Northern Border*)). The August 5 Order at n.20 incorrectly cited to a different Northern Border case in n.20. The correct Northern Border case was cited in n.6 of the August 5 Order.

rates,⁶ and therefore, did not warrant summary rejection.⁷ The Commission stated that in the *GTN* case, the Commission found that GTN's rate proposal did not raise a rate design issue, but a cost allocation issue, and that the proposal, along with the related revenue-sharing mechanism, warranted a full investigation through the hearing process, along with other cost-of-service issues.⁸ The August 5 Order also cited the *Northern Border* case, where the Commission set Northern Border's short-term rates for hearing.⁹ Consistent with these cases, the August 5 Order denied the parties' requests for summary disposition of this issue and set the short-term rate proposal for hearing.

2. Requests for Rehearing

7. The Generator Coalition argues that it was inappropriate for the Commission to rely on prior decisions that accepted peak/off-peak rate proposals subject to hearing as justification for denying the Generator Coalition's request for summary rejection of El Paso's short-term rate proposal. The Generator Coalition argues that the orders cited by the August 5 Order were issued prior to the issuance of Order No. 712, which constitutes a material changed circumstance.¹⁰

8. The Generator Coalition explains that Order No. 712 lifted the rate cap on the capacity release market conditioned on pipelines having cost-based recourse rates in place in order to guard against the exercise of market power by the releasing shippers and pipelines in negotiated rate transactions. The Generator Coalition argues that when

⁶ *Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services*, Order No. 637, FERC Stats. & Regs. ¶ 31,091, *clarified*, Order No. 637-A, FERC Stats. & Regs. ¶ 31,099, *reh'g denied*, Order No. 637-B, 92 FERC ¶ 61,062 (2000), *aff'd in part and remanded in part sub nom. Interstate Natural Gas Ass'n of America v. FERC*, 285 F.3d 18 (D.C. Cir. 2002), *order on remand*, 101 FERC ¶ 61,127 (2002), *order on reh'g*, 106 FERC ¶ 61,088 (2004), *aff'd sub nom. American Gas Ass'n v. FERC*, 428 F.3d 255 (D.C. Cir. 2005).

⁷ August 5 Order, 124 FERC ¶ 61,124 at P 26.

⁸ *Id.* (citing *GTN*, 117 FERC ¶ 61,315 at P 75).

⁹ *Id.* (citing *Northern Border*, 113 FERC ¶ 61,230 at P 22-23).

¹⁰ Generator Coalition's September 4, 2008 Request for Rehearing at 4 (citing *Promotion of a More Efficient Capacity Release Market*, Order No. 712, FERC Stats. & Regs. ¶ 31,271 (2008), *order on reh'g*, Order No. 712-A, FERC Stats. & Regs. ¶ 31,284 (2008), *order on reh'g*, Order No. 712-B, 127 FERC ¶ 61,051 (2009)).

El Paso's rates go into effect on January 1, 2009, there will no longer be any capped cost-based rates for interruptible and short-term firm services to act as recourse rates to guard against the exercise of market power in the uncapped secondary market. The Generator Coalition contends that both markets will suffer because releasing shippers and El Paso will be better able to exert market power to charge monopoly rents for short-term services. The Generator Coalition further argues that this is the result the Commission sought to avoid in Order No. 712.

9. The Generator Coalition notes that in Order No. 712, the Commission specifically referenced the El Paso system as one that is susceptible to the exercise of market power by releasing shippers in an uncapped market because El Paso has numerous captive customers, including most of the members of the Generator Coalition, who generally pay maximum rates for the services El Paso provides. The Generator Coalition concludes that the Commission acted in an arbitrary and capricious manner by failing to take into account these market consequences following the issuance of Order No. 712.

10. The Generator Coalition and APS argue that the Commission erred in relying on the *GTN* and *Northern Border* cases when accepting El Paso's short-term rates. APS states that *GTN* involved a settlement and, as such, lacks precedential value. Furthermore, APS states that *Northern Border* dealt exclusively with the pipeline's proposed revisions to its permanent firm transportation capacity release program and did not apply to short-term firm and/or interruptible services. The Generator Coalition further states that these cases were proposed only for prospective application following a hearing or settlement. Thus, the Generator Coalition states that there were no immediate consequences for shippers as there are here, where the Commission allowed the rates to go into effect subject to refund, and set El Paso's rate proposal for hearing.

11. The Generator Coalition argues that, contrary to the rate proposals in *GTN* and *Northern Border*, the Commission's decision to permit El Paso's rates to go into effect January 1, 2009 will have severe market consequences for electric generators. The Generator Coalition explains that electric generators served by El Paso will be forced to submit bids to sell their power to the electric market based on the higher dispatch costs and that refunds will not compensate a generator who was not dispatched and loses a power sales opportunity because its bid reflected the higher 250 percent rates. The Generator Coalition contends that the Commission recognizes that refunds as a form of retroactive relief may be an inadequate remedy for electric generators because they cannot undo bids and dispatch decisions in the power market.¹¹ In addition, the

¹¹ *Id.* at 10 (citing *Maryland Public Service Comm'n v. PJM Interconnection, L.L.C.*, 123 FERC ¶ 61,169, at P 49 (2008); *El Paso Natural Gas Co.*, 34 FERC ¶ 61,316, at 61,576 (1986)).

Generator Coalition asserts that shippers will be forced to make contracting decisions for longer-term contracts prior to resolution of the final rates in this proceeding.

12. The Generator Coalition further contends that the Commission erred in failing to recognize the unique service features on El Paso's system that distinguish it from the prior cases cited by the Commission setting peak/off-peak rate proposals for hearing. The Generator Coalition states that, unlike GTN and Northern Border, El Paso has a complex array of hourly firm service options that are often unique to individual delivery points, and the hourly variation component of the service cannot always be transferred to other delivery points. As a result, the Generator Coalition argues that it is very difficult for marketers and other shippers holding longer-term hourly services to supply end users who need hourly flexibility on an alternate-point basis by moving their longer-term hourly firm contracts to an alternate delivery point. The Generator Coalition states that these shippers have less ability to manage the higher charges for short-term services by purchasing spot gas than they would on other pipelines like GTN and Northern Border.

13. The Generator Coalition additionally argues that the Commission erred by determining that El Paso's short-term rate proposal may be consistent with Order No. 637 and Commission policy and precedent. The Generator Coalition states that Order No. 637 allows a pipeline to propose a term-differentiated or seasonal rate with the limitation that the rates in the aggregate produce the pipeline's annual revenue requirement.¹² Thus, the Generator Coalition explains that higher rates for peak seasonal or shorter-term services would be offset with lower rates for non-peak or long-term services. The Generator Coalition argues that El Paso's proposal to use a rate multiplier for short-term services is in clear contravention of Order No. 637 because it has made no effort to link its short-term rate to actual cost responsibility. The Generator Coalition further states that Order No. 637 envisioned pipelines providing an incentive for shippers to contract for longer-term service, rather than a disincentive for shorter-term service.

14. The Generator Coalition asserts that consistent with Commission policy and precedent favoring a 100 percent load factor rate for interruptible service, El Paso should have been required to show a need to ration capacity, or that the proposal will increase throughput, in order to move away from a 100 percent load factor rate design. In addition, the Generator Coalition argues that El Paso's proposal violates the Commission's policy prohibiting a higher rate for interruptible services that are inferior to firm services. The Generator Coalition states that the Commission already rejected El Paso's proposal to institute a 60 percent load factor interruptible rate in El Paso's last rate case.¹³ The Generator Coalition states that the Commission found in that case that

¹² *Id.* at 15 (citing Order No. 637, FERC Stats. & Regs. at 31,293).

¹³ *Id.* at 18 (citing *El Paso Natural Gas Co.*, 112 FERC ¶ 61,150 at 61,830-32 (2005)).

El Paso had not demonstrated the need to ration capacity on its system because it was not fully subscribed, that El Paso should have the goal of designing its rates to maximize throughput, and that the proposed 60 percent load factor rate would not maximize throughput.¹⁴ The Generator Coalition states that El Paso cannot show that there is a need to ration capacity in this case because El Paso's system is not fully subscribed. Furthermore, the Generator Coalition argues that increasing the short-term rates will create a disincentive to move short-term volumes and will thus lower throughput.

15. Finally, the Generator Coalition states that El Paso's short-term services are all the same quality of service and should be priced accordingly. The Generator Coalition objects to El Paso's proposal to price short-term services that have terms of five or seven months at long-term firm rates, while pricing short-term services that are for a two-month or eleven-month term at the 250 percent rate.

16. APS argues that the Commission erred by accepting El Paso's short-term rate proposal without addressing APS's arguments that the rate increase constituted a request for market-based rates and an exercise of market power in the highly concentrated Arizona market. APS states that the August 5 Order failed to address the issue of whether a rate that is two and a half times higher than a cost-based rate is the functional equivalent of a market-based rate.

17. APS further contends that the Commission erred by failing to follow its policy governing the processing of applications for market-based rates without providing a reasoned explanation. APS argues that allowing the 250 percent rate increase to go into effect, subject to refund, on January 1, 2009, is in direct contravention of the Commission's market-based rate policy, which provides that market-based rates will only be authorized after the Commission finds that the pipeline lacks market power, and only on a prospective basis.

18. APS also asserts that the refund protection afforded by the August 5 Order does not address the potential harm that could flow from the decision in that order. APS contends that the economic dispatch of its generation units may be altered by El Paso's short-term service rate increase, with the result that APS may need to run a generation unit with a different fuel source or purchase electricity in the wholesale market. APS argues that refunds will not protect APS from the higher electricity prices it may incur as a result.

¹⁴ *Id.*

3. Commission Determination

19. The Commission denies the parties' requests for rehearing. El Paso has not proposed market-based rates and therefore its proposal was not processed as a market-based rate application. APS argues that the proposal to charge short-term rates up to 250 percent of the recourse rate is the equivalent of market-based rates. We disagree.

20. El Paso's proposed rates are tied to the cost-based recourse rate and are capped at 250 percent of the relevant recourse rate, unlike market-based rates which have no cap. In addition, El Paso proposed a revenue credit to assure that after revenues are applied to the cost of service, El Paso will credit the majority of the excess revenues to shippers. Market-based rates are not tied to a pipeline's revenue requirement and do not provide revenue credits to shippers.

21. However, while we find that El Paso's short-term rates are not the equivalent of market-based rates, we have not found that they are just and reasonable. Because the Commission found that the proposed rates may be unjust, unreasonable, unduly discriminatory, or otherwise unlawful, the August 5 Order suspended the rates, subject to refund and the outcome of a hearing. The Commission declined to summarily reject the short-term rates, and other portions of El Paso's proposal, because these issues involve questions of fact that the Commission could not resolve based on the information in the pleadings.¹⁵ Thus, the Commission's decision to set the short-term rate proposal for hearing was justified.

22. The Generator Coalition argues that the Commission's refusal to summarily reject El Paso's short-term rate proposal is contrary to Order No. 712. We disagree. Order No. 712 removed the rate cap on the capacity release market based on a finding that competition in the capacity release market, combined with the continuing requirement that pipelines must sell short-term firm and interruptible services to any shipper offering the maximum rate, and the Commission's ongoing monitoring efforts, will keep short-term capacity rates within the "zone of reasonableness."¹⁶ Order No. 712 stated that the pipeline's maximum rates for short-term firm and interruptible services serve as recourse rate protection for negotiated rate transactions and will provide the same protection to replacement shippers by giving them access to short-term firm and interruptible services purchased directly from El Paso at a just and reasonable rate if the releasing shipper seeks to exercise market power.¹⁷

¹⁵ August 5 Order, 124 FERC ¶ 61,124 at P 27.

¹⁶ Order No. 712, FERC Stats. & Regs ¶ 31,271 at P 39.

¹⁷ *Id.* P 48.

23. Here, El Paso proposes a maximum rate for short-term firm and interruptible services that is capped at 250 percent of the recourse rate. Because the proposed rate may act as a recourse rate to the uncapped capacity release rate, the Commission did not find the proposal was necessarily inconsistent with Order No. 712 or warranted summary rejection. Instead, the Commission appropriately set for hearing the issue of whether El Paso's short-term rate proposal and crediting mechanism is a just and reasonable cost-based rate. Based on the hearing record, the Commission will determine such a just and reasonable rate for El Paso's short-term firm and interruptible services, consistent with Order No. 712.

24. The Generator Coalition asserts that Order No. 712 specifically references El Paso as a system that is susceptible to releasing shippers being able to exercise market power in an uncapped market.¹⁸ We find that the Generator Coalition misrepresents the Commission's statements in Order No. 712. In Order No. 712, the Commission reviewed data on capacity release transactions during an experimental period when the capacity release ceiling price was waived. The Commission found that El Paso did have more releases above the maximum rate than most other pipelines in the survey, but that above-maximum-rate releases on El Paso's system during that period amounted to only 13.3 percent of total releases on El Paso's system.¹⁹ In fact, the Commission concluded that the data shows that the short-term capacity release market is generally competitive and that with respect to the El Paso market, the data shows that during the period March 26, 2000 to December 31, 2001, only 12.5 percent of the total volume of capacity released by El Paso was released at prices above the maximum rate. Order No. 712 further noted that data from August 2006 through July 2007 shows that the market value of transportation service from the Permian Basin to the California border was less than El Paso's maximum transportation rate, except during brief, peak-demand periods when the value of transportation service was somewhat greater than the maximum transportation rate. Order No. 712 found similar data for deliveries to East of California markets on El Paso's South Mainline.²⁰ Thus, contrary to the Generator Coalition's assertions, Order No. 712 did not reference El Paso as a system that is susceptible to market power and does not bar the Commission from setting El Paso's proposal for hearing.

25. The Commission finds that the August 5 Order is also not inconsistent with the prior orders in *GTN* and *Northern Border*, contrary to the Generator Coalition's assertions. In *GTN*, the Commission declined to summarily reject a flexible services

¹⁸ Generator Coalition's September 4, 2008 Request for Rehearing at 8.

¹⁹ Order No. 712, FERC Stats. & Regs. ¶ 31,271 at P 43, Table 1.

²⁰ *Id.* P 59.

proposal very similar to El Paso's proposal.²¹ GTN had proposed to set the maximum rate for new contracts for non-full-haul interruptible, short-term firm, variable MDQ long-term firm, and seasonal long-term firm transportation equal to 2.5 times the maximum reservation component of the recourse rate applicable to long-term firm, uniform MDQ shippers. In addition, GTN proposed that revenues above a specified threshold would be shared among GTN and its shippers on a 25/75 percent basis. GTN further proposed to charge market-based rates for long-haul interruptible transportation, and provided a market power analysis to support its position. The Commission accepted and suspended the tariff sheets subject to refund and, after a technical conference, set the flexible services proposal for hearing, stating that the proposal raised cost allocation issues that warranted a full investigation through the hearing process where the potential costs and benefits could be addressed in light of the other cost-of-service issues.²² The parties ultimately settled the case and the Commission approved the settlement, which did not include the flexible services proposal.²³ In *Northern Border*, the Commission set for hearing *pro forma* tariff sheets that set forth a proposal to set the maximum reservation rate for short-term service (less than a year) at 2.5 times the maximum reservation rate for long-term firm service, with a 50/50 revenue sharing provision.²⁴

26. The procedural steps taken by the Commission in *GTN* and *Northern Border* are similar to those taken in this proceeding. While *Northern Border*'s proposal was presented in the form of *pro forma* tariff sheets, and thus was prospective in nature, GTN's rates were suspended, subject to refund, just as El Paso's were, and went into effect at the end of the suspension period. In both *GTN* and *Northern Border*, the Commission set the rates for hearing to allow the parties to litigate the issue along with all other cost-of-service issues, rather than summarily rejecting the proposal. The fact that the *GTN* case ultimately was settled has no bearing on whether the Commission may follow the same procedural steps taken to set the short-term rate proposal for hearing and allow the rates to go into effect subject to refund.

27. In support of their plea for summary rejection, the Generator Coalition further argues that the Commission has recognized that refunds as a form of retroactive relief may be an inadequate remedy for electric generators because they cannot undo bids and dispatch decisions in the power market. In this case, as we have discussed above, this is not a sufficient basis for summary rejection because the filing has not been found to be in

²¹ *GTN*, 117 FERC ¶ 61,315 at P 75.

²² *Id.*

²³ *GTN*, 122 FERC ¶ 61,012.

²⁴ *Northern Border*, 113 FERC ¶ 61,230 at P 22-23.

patent violation of applicable statutes, regulations, or Commission policy. Because there are material issues of fact regarding the short-term rate proposal, the Commission set the issue to be fully examined through the hearing process. The August 5 Order suspended the rates for the maximum five-month period to provide the maximum refund protection allowed. In these circumstances, this was the appropriate action for the Commission to take. All shippers, including electric generators, are protected by the Commission's refund authority.

28. The Generator Coalition further argues that the Commission failed to consider El Paso's complex array of hourly firm service options that cannot always be transferred to other delivery points, making El Paso's system distinguishable from *GTN* and *Northern Border*. We disagree. While the ability of El Paso's shippers to release hourly firm service may be more limited than that of shippers on other pipelines, El Paso does have a variety of rate schedules and services available to electric generators with varying rate and service options. El Paso's unique service features do not so distinguish it from the circumstances in *GTN* and *Northern Border* that summary rejection of the short-term rate proposal is warranted.

29. Further, we are not persuaded by the Generator Coalition's argument that El Paso's proposal is so clearly inconsistent with Order No. 637 that summary rejection of the proposal is warranted. The Generator Coalition argues that El Paso's proposal contravenes Order No. 637 because it has made no effort to link its short-term rate to actual cost responsibility. However, El Paso's revenue crediting provision is triggered when the revenues exceed the cost of service.²⁵ Thus, the Commission appropriately determined that these issues should be examined more fully through the hearing process, and not summarily decided.

30. Finally, the parties will have the opportunity at the hearing to address the issues regarding whether El Paso has demonstrated a need to deviate from the Commission's 100 percent load factor rate policy. Because El Paso's short-term rate proposal raises material issues of fact, a hearing is the appropriate forum to determine whether the proposed rates are needed to increase throughput and whether El Paso has supported charging a different rate for five-month and seven-month rates compared with other short-term rates.

²⁵ See Order No. 637, FERC Stats. & Regs. at 31,293 (stating that "a shorter term contract is riskier for the pipeline, and a higher rate would compensate the pipeline for this additional risk," and that, "like peak/off peak rates, term-differentiated rates would be cost-based, just and reasonable rates because the Commission will limit the rates in the aggregate to produce the pipeline's annual revenue requirement").

B. Article 11.2 of the 1996 Settlement

1. Background

31. In 1996, El Paso entered into a settlement with its shippers to resolve an NGA section 4 rate case it had filed in Docket No. RP95-363-000, *et al.* (1996 Settlement). The 1996 Settlement established the rates and terms and conditions of service that would apply on the El Paso system for a ten-year period, i.e., until January 1, 2006 (1996 Settlement).²⁶ Article 11.2 of the 1996 Settlement provided that rates for capacity then under contract by eligible shippers would be capped, subject to annual inflation adjustment, until the termination of the shippers' transportation service agreements (TSAs).²⁷

32. Pursuant to the terms of the 1996 Settlement, on June 30, 2005, El Paso filed a general NGA section 4 rate case in Docket No. RP05-422-000 (2006 Rate Case). On December 6, 2006, El Paso submitted a settlement agreement which resolved most issues in the 2006 Rate Case (2006 Rate Case Settlement). Among other things, the 2006 Rate Case Settlement provided for the continuation of Article 11.2 rate caps during the settlement term, but provided that any outstanding issues related to Article 11.2 would be resolved by the Commission and would not take effect until the end of the three-year settlement period, i.e., December 31, 2008. The Commission approved the 2006 Rate Case Settlement on August 31, 2007.²⁸

2. The August 5 Order

33. In the 2008 Rate Case, El Paso proposed two sets of tariff sheets providing for different treatment of Article 11.2 of the 1996 Settlement. El Paso's primary tariff sheets assumed the continued applicability of Article 11.2, while the alternate tariff sheets reflect the elimination of Article 11.2.

34. The August 5 Order accepted and suspended El Paso's primary tariff sheets, subject to conditions, including the outcome of El Paso's pending request for rehearing of

²⁶ *El Paso Natural Gas Co.*, 79 FERC ¶ 61,028, *reh'g denied*, 80 FERC ¶ 61,084 (1997).

²⁷ Article 11.2 contains provisions applicable to the rates to be paid by eligible shippers in the post-settlement period, i.e., after December 31, 2005. Eligible shippers are firm shippers with TSAs that were in effect on December 31, 1995, and that remained in effect on January 1, 2006.

²⁸ *El Paso Natural Gas Co.*, 120 FERC ¶ 61,208 (2007).

the March 20, 2006 order in Docket No. RP05-422-000.²⁹ The March 20 Order had determined that the Article 11.2 rate caps and other rate provisions continue to apply to certain eligible shippers beyond the termination of the 1996 Settlement.³⁰ The August 5 Order also set various issues for hearing, including the issue of cost shifting to non-Article 11.2 shippers and whether Article 11.2 rates are no longer in the public interest.

3. Requests for Rehearing

35. El Paso asserts that the Commission erred in accepting the primary tariff sheets and rejecting the alternate tariff sheets because the decision was premised on the provisional validity of the rulings in March 20 Order. El Paso further argues that, because it has contended on rehearing, and continues to maintain, that the March 20 Order was in error, it is reasserting in this case the arguments made in its request for rehearing in Docket No. RP05-422-000, in order to ensure that its position with respect to the issues decided in the March 20 Order is fully protected.

36. Specifically, El Paso argues that the Commission's decision to reject El Paso's proposed alternate tariff sheets is in error because the March 20 Order was arbitrary, unreasonable, and in excess of the Commission's statutory authority. El Paso states that because the August 5 Order relies on the March 20 Order's rulings, it (1) erroneously holds that Article 11.2 remains in effect and is contrary to applicable precedent; (2) misconstrues Article 11.2(a) as permitting the "converted" CD contracts of El Paso's former full-requirements customers to become subject to the Article 11.2(a) rate caps; and (4) misconstrues Article 11.2(b) as applying to all contracts held by a shipper covered by Article 11.2, rather than to the shipper's contract in effect on December 31, 1995, as intended. El Paso further argues that the Commission's failure to interpret Article 11.2 as incorporating the just and reasonable standard under NGA sections 4 and 5, and not the "public interest" standard that applies to fixed rate contracts, is contrary to controlling precedent.

37. Gila River and New Harquahala argue that if the Commission permits Article 11.2 to continue, either El Paso or shippers not protected by Article 11.2 must absorb the resulting cost shift, which could amount to as much as \$43.3 million per year.³¹ Gila

²⁹ See *El Paso Natural Gas Co.*, 114 FERC ¶ 61,290 (2006) (March 20 Order).

³⁰ The Commission issued an order denying the requests for rehearing of the March 20 Order on September 5, 2008. See *El Paso Natural Gas Co.*, 124 FERC ¶ 61,227 (2008) (September 5 Order).

³¹ Gila River and New Harquahala state that El Paso's primary tariff sheets reallocate \$16.3 million, but that some Article 11.2 shippers advocate alternate applications of Article 11.2 that would increase the cost shift to over \$43 million.

River and New Harquahala assert that, as a result of this cost shift, they would have to pay approximately \$9.5 million more per year than Article 11.2-protected shippers who are their competitors. Gila River and New Harquahala argue that this cost shift will result in increased dispatch costs which will then be reflected in higher electricity bid prices which will decrease the likelihood that non-Article 11.2 shippers will be dispatched. Gila River and New Harquahala assert that the Commission cannot remedy the competitive harms which will result, for there is no remedy for lost sales. Gila River and New Harquahala conclude that the continuing effectiveness of Article 11.2 will precipitate a cost shift that may threaten the financial health of the companies.

38. Gila River and New Harquahala argue that it was error for the Commission to reject the alternate tariff sheets and that the Commission should have rejected the primary tariff sheets as unduly discriminatory, unjust, unreasonable, anticompetitive, and against the public interest. Gila River and New Harquahala argue that once the suspended rates go into effect on January 1, 2009, the non-Article 11.2 shippers would shoulder the cost shift from January 1, 2009 until issuance of a merits order but possibly without redress back to January 1, 2009. Thus, Gila River and New Harquahala contend that the Commission should grant rehearing of its decision to reject the alternate tariff sheets.

39. Gila River and New Harquahala argue that continued application of Article 11.2 results in undue discrimination because one class of shippers will bear the cost of Article 11.2 so that another class of customers may enjoy lower rates for the same services. Gila River and New Harquahala assert competition in the power generation market will be distorted as a result. Gila River and New Harquahala contend that, under court precedent, the record must exhibit factual differences which justify distinct customer classes and differences in treatment.³² The parties contend that a rate disparity predicated on a settlement agreement, as in this case, is only lawful “provided that there is no evidence of actual competitive harm or undue burden to a customer group” and the disparity is temporary.³³ Because Article 11.2 continues in perpetuity, Gila River and New Harquahala argue that shippers without Article 11.2 TSAs will continue to subsidize the Article 11.2 shippers, some of which are direct competitors in the power generation market. In addition, Gila River and New Harquahala argue that the cost shift does not follow the well-accepted policy that cost allocation should follow cost causation.

³² Gila River and New Harquahala’s September 4, 2008 Request for Rehearing at 11 (citing *St. Michaels Utilities Commission v. FPC*, 377 F.2d 912, 915 (4th Cir. 1967); *Consolidated Edison Co. of New York, Inc. v. FERC*, 165 F.3d 992, 1012 (D.C. Cir. 1999)).

³³ *Id.* (citing *Cities of Bethany v. FERC*, 727 F.2d 1131, 1138-1139 (1984) (rate disparity due to settlement lawful because rate difference was temporary and Commission found no evidence of anti-competitive harm.))

40. Gila River and New Harquahala further argue that the application of Article 11.2 will distort competition in the power generation market. Gila River and New Harquahala state that they run newer, more efficient and cleaner generating units than many of the units operated by Article 11.2 shippers. They contend that they will be forced to reflect their increased delivered gas costs in electricity bid prices which will result in a perverse competitive advantage for the Article 11.2 shippers: newer, more efficient generating units will run less often because they will subsidize the gas transportation costs of the older, less efficient units run by the Article 11.2 shippers. Gila River and New Harquahala assert that the increased charges will cause them irreparable harm because they do not have captive customers and, thus, will be completely at risk for these increased costs which have no relationship to actual cost responsibility.

41. Gila River and New Harquahala argue that, under certain circumstances, Article 11.2 fully separates cost responsibility from cost causation. Gila River and New Harquahala contend that because Article 11.2(b) protects all the quantities held by shippers with Article 11.2(a) TSAs, irrespective of the amount of Article 11.2(a) quantities a shipper holds, a shipper could reduce its Article 11.2(a) TSAs to just 1 dth and still receive the full protection of Article 11.2(b). Gila River and New Harquahala argue that the ability of shippers to avoid paying for certain costs in perpetuity, by maintaining a *de minimis* amount of Article 11.2(a) quantities, is not just and reasonable.

42. Gila River and New Harquahala also argue that the Commission should grant rehearing of its decision to reject the answer of the Competitive Power Suppliers (Blythe Energy, LLC, Gila River, and New Harquahala).³⁴ Gila River and New Harquahala argue that the answer addressed arguments raised for the first time in the July 15, 2008 pleadings of other parties that the amount of the Article 11.2 cost shift must be increased and allocated to a smaller class of shippers. Gila River and New Harquahala argue that they could not have filed the answer any earlier and that the answer is relevant to whether the Commission erred in rejecting the alternate tariff sheets and in failing to summarily reject continued application of Article 11.2 and the primary tariff sheets.

43. Finally, Gila River and New Harquahala argue that the August 5 Order is not the result of reasoned decision-making because it failed to give a reasoned justification for rejecting the alternate tariff sheets. Gila River and New Harquahala contend that the August 5 Order neither engaged the arguments raised by the Competitive Power Suppliers regarding the negative impacts of continued application of Article 11.2 nor addressed the evidence adduced by the Generator Coalition and the Competitive Power Suppliers on this point. Gila River and New Harquahala conclude that the Commission must grant rehearing of the rejection of the alternate tariff sheets and the answer.

³⁴ Gila River and New Harquahala's September 4, 2008 Request for Rehearing (citing Competitive Power Supplier's July 21, 2008 Answer).

4. Commission Determination

44. The Commission denies El Paso's request for rehearing. El Paso requests rehearing of the August 5 Order on the grounds that it relied on the decision in the March 20 Order that Article 11.2 continues to apply, which El Paso argues was arbitrary and capricious. Moreover, El Paso states that its request reasserts the arguments made in its request for rehearing of the March 20 Order to assure that its position with respect to the March 20 Order is fully protected.

45. However, in the time since El Paso filed the instant rehearing, the Commission has addressed all requests for rehearing of the March 20 Order.³⁵ In the September 5 Order, the Commission affirmed its decision that Article 11.2 continues to apply and addressed all arguments raised by El Paso. Therefore, the Commission finds El Paso's request for rehearing in this case is moot.

46. The Commission will also deny Gila River and New Harquahala's request for rehearing. In the August 5 Order, the Commission accepted and suspended the primary tariff sheets subject to refund and the outcome of the technical conference and hearing in this proceeding. The Commission rejected the alternate tariff sheets because they were inconsistent with the Commission's prior orders concerning the continued applicability of Article 11.2.³⁶ The primary tariff sheets provided for the continued applicability of Article 11.2, consistent with Commission precedent, and so were properly accepted.

47. The Commission's acceptance of the primary tariff sheets does not constitute a finding that those rates are just and reasonable. To the contrary, the Commission determined that El Paso's proposed rates have not been found to be just and reasonable and may be unjust and unreasonable, and for this reason, suspended the primary tariff sheets subject to refund and conditions, including the outcome of hearing procedures.³⁷ All issues regarding the justness and reasonableness of El Paso's proposed rates, including whether Article 11.2 continues to be just and reasonable and/or in the public interest, and whether the proposed cost shift because of Article 11.2 results in discriminatory and/or anti-competitive rates, are appropriately addressed in the hearing. In setting El Paso's proposed rates for hearing, the Commission acted to ensure that the parties had ample opportunity to address the Article 11.2 issues in the context of a hearing, where all rate issues could be addressed together.

³⁵ September 5 Order, 124 FERC ¶ 61,227.

³⁶ See March 20 Order, 114 FERC ¶ 61,290.

³⁷ See August 5 Order, 124 FERC ¶ 61,124 at P 30-31.

48. While the Commission has determined that Article 11.2 continues to apply, the Commission has not yet had the opportunity to rule on whether the application of Article 11.2 results in just and reasonable rates. In the last rate case, in Docket No. RP05-422-000, the parties settled before litigating the case, and in that settlement, agreed to continue Article 11.2 rates for the term of the settlement. In the current rate case, the parties filed a partial settlement but reserved this issue, among others, for hearing. At the hearing, all parties will have the opportunity to present evidence and arguments regarding whether the proposed rates are just and reasonable. There Gila River and New Harquahala can present the arguments contained in this rehearing request including issues of competitive harm, financial impact, rate disparity for similar service, and cost causation. The Commission will then have a hearing record on which to base a decision on whether Article 11.2 results in just and reasonable rates that are in the public interest.

49. Because there are issues of material fact regarding the proposed rates, including the application of Article 11.2, the Commission could not summarily reject the issue of the impact of the Article 11.2 cost shift. For this reason, the Commission set the issue for hearing and rejected the answers filed by the Competitive Power Suppliers and other parties. As noted in the August 5 Order, the parties will have a full opportunity to discuss issues raised by El Paso's filing in the hearing.³⁸ We therefore deny the request for rehearing of the Commission's decision to reject the Competitive Power Suppliers' answer.

The Commission orders:

The requests for rehearing are denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

³⁸ *Id.* P 24.