

113 FERC 61,183
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. CP05-2-002

ORDER DENYING REQUESTS FOR REHEARING
AND CLARIFICATION

(Issued November 18, 2005)

1. The El Paso Municipal Customer Group and Phelps Dodge Corporation (Municipal Group/Phelps Dodge) filed a timely, joint request for rehearing of the order issued in *El Paso Natural Gas Company*, 111 FERC ¶ 61,408 (June 16, 2005). El Paso Electric Company (El Paso Electric) and Texas Gas Service Company, a Division of ONEOK, Inc. (Texas Gas), also filed timely requests for rehearing of the June 16 Order. The requests for rehearing were filed on July 18, 2005. In addition, on July 18, El Paso Natural Gas Company (El Paso) filed a request for clarification or, in the alternative, a request for rehearing of the June 16 Order.¹
2. The rehearing requests raise rate, engineering, and scheduling and confirmation issues related to El Paso's certificate proposal. We will deny the Municipal Group/Phelps Dodge's joint request for rehearing, as well as El Paso Electric's and Texas Gas' requests for rehearing. We will also deny El Paso's request for clarification or 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

¹ On August 2, the Indicated Shippers filed an answer in response to El Paso's pleading. Rule 385.213(a)(2) of our regulations does not prohibit answers to requests for clarification.

Mojave Pipeline Company (Mojave) and other pipelines. Near Ehrenberg, El Paso's southern system interconnects with North Baja Pipeline, LLC (North Baja) 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. Kern River Gas Transmission Company (Kern River) operates an interstate pipeline extending from various receipt points in Wyoming through Utah and Nevada to the San Joaquin Valley near Bakersfield. Kern River has delivery points located along its system in Utah, Nevada, and California, including a delivery point at Daggett, California with Mojave and another pipeline.

II. The June 16 Order

5. The June 16 Order 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 1903.² 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).

6. As part of its Line 1903 project, El Paso also acquired capacity on Mojave's system.³ El Paso stated that it would use the capacity on Mojave to transport gas 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.⁴ El Paso stated that the proposed project would enable it to transport up to 502,000 Mcf of gas per day through Line 1903 for deliveries to Ehrenberg, North Baja, and east to Phoenix, Arizona markets.

² El Paso did not propose to acquire the remaining 215-mile segment of Line 1903.

³ El Paso did not need certificate authority to acquire capacity on Mojave.

⁴ Mojave and Kern River entered into an agreement to reconfigure the Daggett compressor station to add the capability of bi-directional flow on Mojave. Kern River will modify its compressor station under the terms of its blanket certificate.

7. El Paso entered into precedent agreements 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. These customers are existing Topock customers of El Paso and, according to El Paso, the precedent agreements represent commitments by these shippers to extend their existing contracts because of its Line 1903 proposals.
8. El Paso also entered into precedent agreements 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. These are new, or expansion, agreements.
9. The June 16 Order found that El Paso's proposals met the threshold requirement of the Certificate Policy Statement,⁵ holding that existing customers would not subsidize the proposals since projected revenues exceed expected costs. After making this finding, the June 16 Order determined that El Paso had included the cost of acquiring all 303 miles of Line 1903, rather than the 87.8-mile long segment of Line 1903 that El Paso proposed to acquire in its application. Thus, the June 16 Order found that El Paso could only include the costs of the 87.8-mile long segment. In addition, the order reduced El Paso's costs associated with acquiring capacity on Mojave and assigned 130,438 of the 502,000 Mcf per day of transportation capacity on Line 1903 to system operations. Thus, the June 16 Order increased the amount by which the projected revenues are expected to exceed the cost of the project. With these factors in mind, we made a pre-determination that 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.
10. The June 16 Order also found that the proposed Line 1903 project would provide a west-end connection between El Paso's north and south mainlines, move San Juan Basin supplies for existing customers from Topock through Mojave and Line 1903 to Ehrenberg. It would also enable El Paso to move Rocky Mountain supplies for new customers from Kern River through Mojave and Line 1903 to Ehrenberg, and reduce El Paso's reliance on displacement.

⁵ *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).

11. Finally, the June 16 Order found that “[n]o party provided evidence to suggest the manner in which the Mojave capacity was acquired, or the price paid by El Paso, involved an abuse of our affiliate regulations.” Thus, the June 16 Order denied requests for an evidentiary hearing.

12. On June 30, 2005, in Docket No. RP05-422-000, El Paso filed a general rate case under section 4 of the Natural Gas Act. We accepted El Paso’s proposed tariff sheets and suspended their effectiveness until January 1, 2006, subject to certain conditions.⁶

13. The issues raised in the requests for rehearing of the June 16 Order are discussed below.

III. Discussion

A. Rate Issues

1. Revenues from the Extension Contracts

a. The Requests for Rehearing

14. The Municipal Group/Phelps Dodge and Texas Gas object to the Commission’s inclusion of revenues from the extension contracts with the Phoenix area shippers in the rolled-in rate determination, contending that the inclusion double counts the revenues. Texas Gas asserts that the Commission erred in concluding that it is reasonable for El Paso to include revenues from the extension contracts in its costs/revenue analysis because of the history of capacity allocation on the El Paso system.

15. El Paso Electric and the Municipal Group/Phelps Dodge assert that the Commission’s justification for including the extension contract revenues is flawed because, contrary to the finding that the extension shippers could look elsewhere for gas supplies, the extension shippers are captive customers of El Paso. El Paso Electric points out that there are no other interstate pipelines serving southern Arizona and that there are no pending section 7 certificate applications to serve the area. Thus, El Paso Electric asserts that the extension shippers are captive to El Paso. El Paso Electric also asserts that, because the extension shippers serve native electric and natural gas customers, they cannot simply walk away from their capacity on El Paso.

⁶ *El Paso Natural Gas Co.*, 112 FERC ¶ 61,050 (July 29, 2005).

16. The Municipal Group/Phelps Dodge contends that the Commission overlooked the protestors' assertions that the extension shippers could have acquired additional El Paso capacity without the Topock limitations. They assert that El Paso has plenty of capacity to sell from the Permian Basin that can serve the needs of the Phoenix area shippers.

17. Finally, El Paso Electric contends that the Commission erred by failing to discuss (1) when the existing contracts expire – if the extension shippers are committed to firm service from El Paso for several years, the contractual commitment undermines the contract extension justification; (2) whether the extension shippers would simply choose to release their capacity in lieu of terminating their contracts with El Paso and seeking service from another pipeline; and (3) whether the capacity that might be unsubscribed would be purchased by other shippers. Further, El Paso Electric asserts that the Commission cites no precedent in which revenues from contract extensions justified rolled-in rate treatment.

b. Commission Response

18. We believe that it is reasonable to conclude, as the June 16 Order did, that customers who hold capacity they cannot effectively use will seek alternatives. The extension shippers cannot use the capacity allocated to them on El Paso's north system, with California delivery points, to serve markets east of California on El Paso's south system. While they were once captive customers, the conversion of their service from full requirements to contract demand service in the Capacity Allocation Proceeding⁷ means that they can now seek service from alternate suppliers.⁸ Thus, we find that it is appropriate in this case to consider the revenues from the extension contracts in the rolled-in rate determination.

19. Contrary to the position of the parties requesting rehearing, we believe that the extension shippers could continue to serve their native electric and natural gas customers by "walking away" from their El Paso capacity with California delivery points and instead contracting with El Paso for short-term interruptible or firm service, or both, out

⁷ *El Paso Natural Gas Co.*, 99 FERC ¶ 61,244 (2002), *order on clarification*, 100 FERC ¶ 61,285 (2002), *reh'g denied*, 104 FERC ¶ 61,045 (2003), *aff'd*, *Arizona Corporation Comm. v. FERC*, 397 F.3d 952 (D.C. Cir. 2005) (the Capacity Allocation Proceeding).

⁸ As an example, Transwestern Pipeline Corporation recently held an open season for a project called the "Phoenix Pipeline Project" in southern Arizona that could serve as an alternative to El Paso's service.

of the Permian Basin until other pipeline alternatives are in service. Similarly, the other pipeline alternatives are also available to the protestors who claim that they have not been able to move their primary delivery points to their city gates.

20. El Paso Electric and Texas Gas cite an example to show that El Paso's existing shippers will subsidize the Line 1903 project. In the example, they assume a current total system cost of service to be \$500 million, with the extension shippers paying \$23 million and the remaining shippers paying \$477 million. Assuming the Line 1903 cost of service is \$23 million, El Paso Electric and Texas Gas contend that the system cost of service would increase to \$523 million. El Paso Electric asserts that, even if the extension shippers extend their contracts at a total of \$23 million per year to cover the Line 1903 costs, the remaining shippers will have to pick up the full \$500 million instead of \$477 million. El Paso Electric also asserts that, even if \$8 million of the \$23 million Line 1903 cost of service may be attributed to system benefits, the other existing shippers will be paying \$15 million more in costs and thus will subsidize the project.

21. We disagree with the basic assumption in El Paso Electric's and Texas Gas' calculations. Using the same scenario, it is appropriate to assume that the remaining shippers will end up paying the full \$500 million cost of service even if the Line 1903 project is not constructed, because the extension shippers would no longer be taking service at California delivery points. Further, because the revenues from the Line 1903 project exceed the costs, those net revenues will offset a portion of the \$500 million cost of service, creating a benefit to all shippers. Thus, even after considering this example, we conclude that El Paso's existing shippers will not subsidize the Line 1903 project.

2. Displacement

a. Requests for Rehearing

22. The Municipal Group/Phelps Dodge and Texas Gas contend that the Commission's finding that El Paso would use 130,438 Mcf per day of capacity to reduce El Paso's reliance on displacement is not based on any evidence in the record. To the contrary, they assert that, in *Eastern Shore Natural Gas Co.*, the Commission rejected rolled-in rate treatment for expansion facilities, in part, because the primary benefits of the expansion would accrue to the shippers contracting for the capacity created by the expansion facilities.⁹

⁹ 111 FERC ¶ 61,479 (2005).

23. In this vein, El Paso Electric contends that El Paso's commitment to reduce its reliance on displacement in section 6.6 of its settlement in its Order No. 637 proceeding was unconditional and did not involve a companion commitment by shippers to pay for any system expansion required to reduce displacement capacity.¹⁰ El Paso Electric asserts that absent the Line 1903 project, El Paso would be under a contractual obligation to reduce displacement capacity and would be responsible for meeting that obligation without increasing costs to its firm shippers. El Paso Electric asserts that the June 16 Order is contrary to the orders requiring El Paso to provide firm service or reimburse its customers for failing to do so.

b. Commission Response

24. No party disputes the fact that El Paso currently relies on south-to-north flow capacity to provide north-to-south flow capacity by displacement. As shown in Exhibit N of El Paso's application, Line 1903 will provide new north-to-south flow capacity, by providing a new north-south crossover, which will offset a portion of the north-south shortfall that is currently covered by displacement. The fact that El Paso has not sold the 130,438 Mcf per day of the Line 1903 capacity supports El Paso's assertion that this capacity is available to reduce reliance on displacement. In addition, the facts in *Eastern Shore* are distinguishable from those present here. In *Eastern Shore*, we rejected rolled-in rate treatment because we found that the existing customers would subsidize the project. Here, the revenues for the Line 1903 project exceed the costs of the project, meaning that there is no subsidization. Thus, we find that there is sufficient evidence in the record to support El Paso's claim that 130,438 Mcf per day of the Line 1903 capacity would be used to reduce reliance on displacement.

25. While El Paso Electric is correct that El Paso's commitment to reduce reliance on displacement did not explicitly involve a companion commitment by shippers to pay for any required system expansion, El Paso Electric fails to show that El Paso made a commitment to reduce reliance on displacement without seeking to recover the related costs of system expansion. El Paso is under no contractual commitment to expand its system without seeking cost recovery.

26. The southwestern part of the United States is experiencing significant growth, with a corresponding increase in energy requirements. Additional infrastructure that provides more service to the area, and increases the reliability of service, is a benefit not only to the expansion and extension shippers, but to El Paso's system as a whole. As we noted in the June 16 Order, despite the construction of over 500,000 Mcf per day of capacity by

¹⁰ See *El Paso Natural Gas Co.*, 109 FERC ¶ 61,292 (2004).

El Paso to serve the needs of east of California shippers, El Paso's customers, including El Paso Electric, repeatedly asserted in the Capacity Allocation Proceeding that additional capacity and more reliable service were needed on El Paso's system, particularly to relieve capacity constraints on the north-to-south crossovers. Specifically, El Paso Electric, Phelps Dodge, and the Municipal Group (along with other Texas, New Mexico and Arizona shippers) filed a complaint in Docket No. RP01-486-000 in which they asserted that the Line 1903 capacity was needed to serve the needs of existing customers.¹¹ The June 16 Order found that the Line 1903 project will increase reliability of service on El Paso's system by providing a needed west-end link between El Paso's north and south systems. Consequently, we find that it is reasonable that the cost of such system benefits will be rolled into the system-wide rates of El Paso's shippers.

3. Subsidization

a. Request for Rehearing

27. The Municipal Group/Phelps Dodge contends that the Commission inappropriately used the Line 1903 project to remedy problems associated with the results of the Capacity Allocation Proceeding. They note that many of El Paso's former full requirements customers were left with less than desirable delivery points and transportation paths. The Municipal Group/Phelps Dodge and Texas Gas assert that it is discriminatory to allow only the shippers that signed extension contracts to receive relief from the problems associated with the Capacity Allocation Proceeding, while captive customers with similar problems receive no relief but are required to subsidize the project because there are no "real" incremental dollars to pay for the project. In addition, the Municipal Group/Phelps Dodge notes that the large California shippers are protected from any adverse rate impacts because they have entered into discounted firm contracts. They contend that the result is that the only customers left to bear the cost of the Line 1903 project are the east of California shippers that are captive to the El Paso system and do not have the economic power to negotiate a discount.

¹¹ The complaint in Docket No. RP01-486-000 was addressed in the Capacity Allocation Proceeding.

b. Commission Response

28. As explained in the June 16 Order, we have issued a number of orders designed to facilitate improved reliability on El Paso's system. Specifically, in *Amoco*,¹² we authorized El Paso to replace system-wide delivery rights with specific delivery point rights to eliminate pro-rata capacity allocations at delivery points. In the Capacity Allocation Proceeding, we authorized El Paso to replace system-wide receipt rights with specific receipt point rights and to convert full requirements service to contract demand service to eliminate pro-rata allocations at receipt points. Also, we authorized the Line 2000 project, which converted another portion of the oil pipeline involved in this proceeding to natural gas service and provided 230,000 Mcf per day of capacity for system use.¹³ Subsequently, we authorized construction of the Power-Up project, which added compression to the Line 2000 project, to provide an additional 320,000 Mcf per day of capacity to serve the converting full requirements shippers.¹⁴ El Paso did not seek to recover the costs of those projects through incremental rates, but opted to seek rolled-in rate treatment in its next general rate case proceeding. Thus, El Paso's shippers received additional capacity and improved reliability at no additional cost during the term of the 1996 Settlement (which terminates December 31, 2005).¹⁵ These orders authorized El Paso to take specific action to improve the reliability of its system by defining capacity rights or providing additional capacity to serve the existing contractual demands of the east of California shippers.

29. The Line 1903 project is another step by El Paso to improve system reliability. This project does not solely benefit the extension shippers as the Municipal Group/Phelps Dodge contends. Rather, the Line 1903 project provides enhanced reliability for all shippers through a new north-south interconnect and decreased reliance on displacement, new service to the expansion shippers, and a way for the extension shippers to use their north system capacity to access their markets directly.

¹² *Amoco Energy Trading Corp. v. El Paso Natural Gas Co.*, 93 FERC ¶ 61,060 (2000), *order on clarification*, 93 FERC ¶ 61,222 (2000), *order on reh'g*, 94 FERC ¶ 61,225 (2001), *order on clarification*, 95 FERC ¶ 61,156 (2001).

¹³ 95 FERC ¶ 61,176 (2001).

¹⁴ 103 FERC ¶ 61,280, *reh'g denied*, 105 FERC ¶ 61,202 (2003).

¹⁵ *El Paso Natural Gas Co.*, 79 FERC ¶ 61,028, *reh'g denied*, 80 FERC ¶ 61,084 (1997) (the 1996 Settlement).

30. In regard to the last benefit mentioned above, in the Capacity Allocation Proceeding we directed El Paso to allocate available capacity to the converting full requirements customers. A portion of the capacity allocated to the east of California shippers was north system capacity with San Juan receipt points and California delivery points. The shippers protested that they were unable to use capacity with California delivery points on El Paso's north system to serve their east of California markets on El Paso's south system. For this reason, we directed El Paso to allow those shippers to re-designate their delivery points. Because of capacity constraints on the north-south crossovers, El Paso was not able to accommodate the requested re-designations of delivery points. El Paso was, however, able to allow shippers to re-designate those delivery points if the shippers also re-designated the receipt points to the Permian Basin and used the south system for delivery. Thus, shippers had the option of retaining their north system capacity for future use, including release, or exchanging it for south system capacity to serve their markets directly. We indicated that, while this arrangement may not give these shippers the capacity at the location of their choice, the shippers were receiving more capacity than they otherwise would have, at no additional cost, through the term of the 1996 Settlement. It is this capacity that the extension shippers will use, in conjunction with Line 1903, to serve their markets directly.

31. We do not agree that it is discriminatory to allow only the extension shippers to receive relief from the problems associated with the Capacity Allocation proceeding. As discussed earlier, the east of California shippers had various options available to use their allocated north system capacity. El Paso held an open season for the Line 1903 project that was open to all interested shippers. In addition, as we indicated above, the Line 1903 project will provide system benefits and does not result in subsidization by existing shippers.

4. Burden of Proof

a. Requests for Rehearing

32. The Municipal Group/Phelps Dodge and Texas Gas contend that the Commission inappropriately shifted the burden of proof to show changed circumstances from El Paso to the captive shippers that oppose rolled-in rates.

b. Commission Response

33. In this proceeding, El Paso demonstrated that the projected revenues of the Line 1903 project would exceed the estimated costs. For this reason, the June 16 Order concluded that El Paso's proposed project qualified for a pre-determination of rolled-in rate treatment in its next rate case, absent a material change in circumstances. Consequently, in El Paso's rate filing in Docket No. RP05-422-000, the rates of existing

shippers should not be negatively impacted because the projected revenues of the Line 1903 project exceed the cost of service. However, if the actual project costs exceed the revenues, that fact would constitute a changed circumstance warranting reconsideration of whether rolling in the costs of the Line 1903 project is consistent with the Certificate Policy Statement.

34. When we make a pre-determination that rolled-in rate treatment is appropriate in a certificate proceeding, we base our decision on the facts, estimates, and assumptions at the time the certificate is issued. We cannot foresee whether circumstances will change to such an extent that the project is no longer eligible for rolled-in rate treatment by the time the pipeline files its next rate case. For this reason, we believe that it is appropriate for parties that believe circumstances have changed to have the burden of proof in the rate case. Here, the parties need only show that their proposed rates have increased due to the construction and acquisition of the Line 1903 facilities to show a material change in circumstances.

5. Quantify Actual Costs of the Project

a. Requests for Rehearing

35. The Municipal Group/Phelps Dodge and Texas Gas contend that the Commission failed to quantify the actual costs of the project. They assert that the Commission made three adjustments to El Paso's revenue and expense calculations, but failed to identify the amount of costs that the Commission pre-approved for rolled-in rate treatment. Specifically, the Municipal Group/Phelps Dodge and Texas Gas identified the adjustments as: (1) allowing only \$10.5 million of the oil pipeline costs to be rolled-in; (2) limiting the costs associated with the Mojave capacity to \$16.1 million per year; and (3) allowing the negative crediting of the costs associated with assigning 130,438 Mcf per day to system operations. The Municipal Group/Phelps Dodge contends that El Paso's customers cannot show changed circumstances in the rate proceeding in Docket No. RP05-422-000 in which El Paso seeks to roll in the Line 1903 costs when no party can articulate the precise existing circumstances relied upon by the Commission.

b. Commission Response

36. We do not pre-approve specific costs for rolled-in rate treatment and are not required to quantify the actual costs of the project. The actual costs of the project will not be known until construction is completed. The actual costs of the project will be addressed in El Paso's ongoing rate case in Docket No. RP05-422-000.

37. In the June 16 Order, we determined that the projected revenues of \$31.4 million exceeded the projected cost of service of \$31.1 million. On that calculation alone, we held that a pre-determination of rolled-in treatment was justified. Further, the June 16 Order reduced the projected costs that would be compared to the projected revenues. The specific identification of reduced costs will not change our conclusion here that rolled-in rate treatment is justified. In addition, specifying the actual cost of service is entirely separate from identifying changed circumstances. Our specification of the actual cost of the project is not necessary for a party to assert that changed circumstances exist.

6. Excess Capacity

a. Requests for Rehearing

38. The Municipal Group/Phelps Dodge and Texas Gas contend that the Commission's pre-determination of rolled-in rate treatment failed to take into account that the need for the project has vanished because of the relinquishment of substantial firm rights by Southern California Gas Company (SoCalGas) and other shippers. They also allege that there is a likelihood of overbuilding of capacity and that El Paso faces massive stranded capacity exposure. Given the potential for available capacity on El Paso, they contend that the Commission erred in concluding that a reduction in reliance on displacement would be a system benefit. Texas Gas points out that El Paso, in its rate case in Docket No. RP05-422-000, asserted that it had some 200,000 Dth per day of unsubscribed capacity and was facing a major re-subscription challenge in 2006.

b. Commission Response

39. In the June 16 Order, we approved a pre-determination of rolled-in rate treatment. We also stated that many changes to El Paso's operations and rates, including capacity turnback, will occur in the near future. However, we do not know at this time whether the turned-back capacity will be re-marketed. We will address issues such as capacity turnback in El Paso's general rate case in Docket No. RP05-422-000, which has been set for hearing.¹⁶ Our pre-determination of rolled-in rate treatment was based on the facts at the time the certificate was issued. Changes in those facts can be addressed in the rate case.

¹⁶ 112 FERC ¶ 61,150 (July 29, 2005).

7. Article 11.2 of the 1996 Settlement

a. Requests for Rehearing

40. The Municipal Group/Phelps Dodge and El Paso Electric contend that the Commission failed to acknowledge the significance of Article 11.2 of the 1996 Settlement, which provides that El Paso, not its shippers, is at risk for “capacity that becomes unsubscribed or is subscribed at less than maximum applicable tariff rate as escalated.” These parties maintain that the Commission’s finding in this proceeding protects El Paso at the expense of the captive shippers.

b. Commission Response

41. El Paso raised issues relating to Article 11.2 of the 1996 Settlement in its rate proceeding in Docket No. RP05-422-000. In *El Paso Natural Gas Co.*, we stated that we will address the issue of Article 11.2 in a separate order in El Paso’s ongoing rate case proceeding.¹⁷ Therefore, we need not address the issues here.

8. Pathing Rights

a. Request for Rehearing

42. The Municipal Group/Phelps Dodge contends that the Commission’s reliance upon enhanced pathing rights as a value to be considered under the Certificate Policy Statement was not reasonable. They assert that the Commission wrongly equated pathing rights to primary transportation rights. The Municipal Group/Phelps Dodge contends that the two are distinct and that many shippers, including members of the Municipal Group, have little or no interest in pathing rights. In fact, they point out that Rate Schedule FT-2 shippers do not have paths and may not segment capacity, that these shippers are only interested in their primary rights, and that these shippers have no wish to pay extra for segmentation rights. The Municipal Group/Phelps Dodge asserts that Rate Schedule FT-2 shippers should not be allocated the costs of an incremental project on the basis of system benefits in which they do not share. Finally, the Municipal Group/Phelps Dodge contends that the order implies that reticulated pipeline systems should expand to perfect pathing rights.

¹⁷ *Id.*

b. Commission Response

43. System benefits need not accrue to all shippers for a project to qualify for rolled-in rate treatment. A primary benefit of the Line 1903 project is the increased reliability of service, resulting from a reduced reliance on displacement. Enhanced pathing and segmentation rights are not the sole benefits of the project, but flow from reduced reliance on displacement in this case. Thus, El Paso's shippers, including those who do not have paths or do not segment capacity, will benefit from increased system reliability.

9. The Havasu Project

a. Request for Rehearing

44. El Paso Electric asserts that the June 16 Order is inconsistent with the Commission's order approving incremental rate treatment for the Havasu expansion project.¹⁸ El Paso Electric contends that the Havasu project and the project at issue here are designed to move gas from north-to-south on El Paso's system for a specific set of shippers. Thus, El Paso Electric asserts that the Line 1903 project should be incrementally priced.

b. Commission response

45. The Havasu expansion was authorized during the term of the 1996 Settlement, when El Paso was precluded from filing a rate case to increase rates. Since El Paso did not have the option of seeking rolled-in rate treatment, the cost of any system expansions while the 1996 Settlement was in effect could only be recovered through incremental rates. The 1996 Settlement will terminate on December 31, 2005, and El Paso has submitted a general rate case filing to increase rates effective January 1, 2006. Thus, El Paso now has the option to propose rolled-in rate treatment. Given the different circumstances between the cases, the rate treatment of the Havasu project should not dictate the rate treatment for the Line 1903 project.

10. Discounted Rates

a. Request for Rehearing

46. The Municipal Group/Phelps Dodge asserts that the market does not support the project because El Paso had to discount the transportation agreements with the shippers.

¹⁸ *El Paso Natural Gas Co.*, 77 FERC ¶ 61,129 (1996).

They contend that, in its rate filing, El Paso seeks to recover approximately \$66 million of discounts from its remaining shippers. Of that amount, \$28,950,722 is attributable to the six contracts underlying the Line 1903 project. The Municipal Group/Phelps Dodge contends that system rates would increase if a discount adjustment is granted in the rate case. They assert that the Commission failed to consider this economic impact on captive shippers.

b. Commission Response

47. It is our policy to allow discounts for competitive reasons at specific delivery points. Discounting allows customers, who might otherwise leave the system, to make a contribution to system costs to the benefit of all customers. Further, it is our policy to allow the cost of the lost revenue from discounts to be shared by other system customers through the discount adjustment mechanism in order to allow the pipeline the opportunity to recover its cost of service.

48. We will address issues related to the proposed discount adjustments in El Paso's ongoing rate case in Docket No. RP05-422-000. Whether discount adjustments will be allowed, and to what extent, will be determined in that proceeding. Our pre-determination of rolled-in rate treatment was based on the facts at the time the certificate was issued.

B. Engineering

1. Requests for Rehearing

49. The Municipal Group/Phelps Dodge, El Paso Electric, and Texas Gas contend that El Paso failed to provide a transient model of its system as requested by the Commission. They assert that the Commission erred in authorizing the Line 1903 project without the requested transient analysis, in light of the Commission's finding in the Capacity Allocation Proceeding that El Paso needed to set aside 210,000 Mcf per day of capacity to meet transient operational requirements to ensure reliable firm service on its system after its full requirements conversion.¹⁹ El Paso Electric asserts that the Commission should pre-determine that the Line 1903 project should be accorded incremental rate treatment, or El Paso should be precluded from charging its shippers for reserving capacity to manage transients. The Municipal Group/Phelps Dodge also points out that the Commission held that "El Paso may not contract on the basis of pipeline design capacity and then not allow shippers to schedule a portion of that capacity because of

¹⁹ 104 FERC ¶ 61,045 at P 134 n.133 (2003).

system transient management requirements.” They assert that absent a transient analysis there is no way to determine whether the Line 1903 project will affect system transient management requirements.

2. Commission Response

50. In the Capacity Allocation Proceeding, we sought to ensure that El Paso had sufficient capacity to fully serve its firm service obligations without using the 210,000 Mcf per day of capacity which El Paso needed to manage transients. We made it clear that El Paso could not offer a level of firm service that was equal to its design capacity without first removing the 210,000 Mcf day of firm capacity. Without removing this capacity, we found that El Paso would have to allocate firm capacity on a pro-rata basis in a non-force majeure situation, the exact scenario that the Capacity Allocation Proceeding was attempting to resolve. This is not the case in this proceeding.

51. Under section 157 of the regulations, an applicant is required to provide flow diagrams showing design capacity and maximum capabilities of its pipeline systems operating with and without the proposed facilities. Here, as discussed in the June 16 Order, El Paso met this requirement because it provided flow diagrams and computer models of its pipeline system while operating under steady-state design conditions. The steady-state model provides a snap-shot of the pipeline system operating at design conditions while providing all of the contractual delivery obligations. Although the transient model is another tool that we could use to verify that the existing and proposed facilities are capable of maintaining contractual delivery obligations, in this case, we determined that the historic usage of a steady-state design by El Paso allowed our staff to examine the operations of El Paso’s system to ensure that the integration of Line 1903 would not adversely impact El Paso’s existing shippers while providing the proposed service.

52. We are satisfied with the engineering data supplied by El Paso in this proceeding. El Paso has consistently used the design scenarios from previous applications as the new baseline design scenario for its proposals in each subsequent application. As a result, each of El Paso’s steady-state system models uses the same design criteria that El Paso has used for the last five years. Thus, we find that El Paso has met the engineering requirements contained in our regulations for its certificate application. El Paso is not required to submit a transient model of its system.

C. Scheduling and Confirmation Rules

1. Requests for Rehearing

53. El Paso requests clarification or, in the alternative rehearing, that the June 16 Order does not modify the normal service scheduling and confirmation rules with respect to El Paso's delivery capacity to and through the Topock/Mojave and Ehrenberg/SoCalGas delivery points. El Paso contends that the Commission's requirement that El Paso not sell firm capacity to those delivery points at quantities up to El Paso's capacity to deliver gas to those locations seems to reflect a departure from the Commission's earlier holdings in *Kern River Gas Transmission Co.*²⁰ and *Amoco Energy Trading Corp. v. El Paso Natural Gas Co.*²¹ Under its reading of the June 16 Order, El Paso asserts that a pipeline will be limited to the take-away capacity on the downstream pipeline in determining the capacity that will be available for sale on its system upstream of the interconnection point with the downstream pipeline. El Paso contends that the holding has potential industry-wide implications and departs, without explanation, from long-standing practice, policies, and governing North American Energy Standards Board standards with respect to how much of a pipeline's delivery capacity can be sold on a firm basis, which dictate that the lesser of confirmed quantities between interconnected pipelines should be scheduled.

54. In its answer, the Indicated Shippers assert that the June 16 Order prevents El Paso from overselling delivery point capacity as part of its Line 1903 project and should be retained. The Indicated Shippers assert that if El Paso's request is granted, it would have anti-competitive impacts and return El Paso to the days of chronically unreliable firm transportation service. The Indicated Shippers contend that denying El Paso's request will have no impact on the viability of the Line 1903 project and that El Paso is reading *Amoco* and *Kern River* incorrectly. Thus, the Indicated Shippers request that the Commission deny El Paso's request for clarification or rehearing.

2. Commission Response

55. We clarify that the June 16 Order does not modify the normal service scheduling and confirmation rules with respect to El Paso's delivery capacity to and through the

²⁰ 96 FERC ¶ 61,137, *reh'g denied*, 97 FERC ¶ 61,080 (2001).

²¹ 93 FERC ¶ 61,060, *order on clarification*, 93 FERC ¶ 61,222 (2000), *order on reh'g*, 94 FERC ¶ 61,225, *order on clarification*, 95 FERC ¶ 61,156 (2001).

Topock Mojave and Ehrenberg/SoCalGas delivery points. Our focus is on contracted capacity. The June 16 Order affirms that El Paso may not sell, on a firm basis, capacity that is subject to a prior claim or commitment.

D. Evidentiary Hearing

1. Request for Rehearing

56. The Municipal Group/Phelps Dodge contends that the Commission erred by not holding a hearing on the alleged affiliate abuse issue. Without a hearing and the use of the Commission's investigatory powers to obtain information on the impact of the proposals, the members of the Municipal Group and Phelps Dodge contend that they were denied any opportunity to make a meaningful case regarding affiliate abuse.

2. Commission Response

57. Before we may be required to hold a formal evidentiary hearing, at least three conditions must be met: (1) a party must make allegations of fact material to our determination; (2) the allegations must be supported by an adequate proffer of evidence; and (3) the material facts alleged must be in dispute.²² In its November 4, 2004 protest to El Paso's application, the Municipal Group stated that El Paso's proposals "may be designed to preserve the viability of Mojave as much as any other reason," since El Paso is overpaying for its own capacity on Mojave.²³ In these statements, there was no evidence whatsoever submitted in support of the allegations of affiliate abuse. These assertions standing alone do not constitute a genuine issue of fact that requires the Commission to hold an evidentiary hearing. Our decision in the June 16 Order not to hold a trial-type hearing was a proper exercise of our discretion.

The Commission orders:

(A) The requests for rehearing are denied as indicated in the body of this order.

²² *Cascade Natural Gas Corp. v. FERC*, 955 F.2d 1412, 1425 (D.C. Cir. 1992).

²³ The Municipal Group's November 4, 2004 protest at 10-11.

(B) El Paso's request for clarification or, in the alternative, a request for rehearing is denied.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.