

124 FERC ¶ 61,227
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Sudeen G. Kelly, Philip D. Moeller,
and Jon Wellinghoff.

El Paso Natural Gas Company

Docket Nos. RP05-422-011
RP05-422-016
RP05-422-018

ORDER ON REHEARING AND COMPLIANCE

(Issued September 5, 2008)

1. On March 20, 2006, the Commission issued an order¹ in this proceeding addressing the continued applicability of Article 11.2 of El Paso Natural Gas Company's (El Paso) 1996 Settlement. As explained more fully below, Article 11.2 places certain limitations on the rates that El Paso can charge in future rate cases to shippers that were parties to the 1996 Settlement. Timely requests for rehearing of that order were filed by El Paso, the Arizona Corporation Commission (ACC), Arizona Electric Power Cooperative, Inc. (AEP), jointly by Arizona Public Service Company (APS) and Salt River Project Agricultural Improvement and Power District (Salt River) (jointly the Arizona Electrics), El Paso Electric Company, New Harquahala Generating Company, LLC (New Harquahala), jointly by Phelps Dodge Corporation and Apache Nitrogen Products, Inc. (jointly Phelps Dodge), jointly by Public Service Company of New Mexico and the El Paso Municipal Customer Group (jointly Municipal Customers), Southwest Gas Corporation (Southwest Gas), and Texas Gas Service Company (Texas Gas Service). For the reasons discussed below, the requests for rehearing are denied.

2. On April 4, 2006, El Paso submitted revised tariff sheets to comply with the Commission's March 20 Order. On June 30, 2006, the Commission accepted El Paso's compliance filing subject to conditions and directed El Paso to file revised tariff sheets.²

¹ *El Paso Natural Gas Co.*, 114 FERC ¶ 61,290 (2006) (March 20 Order).

² *El Paso Natural Gas Co.*, 115 FERC ¶ 61,395 (2006) (June 30 Order).

El Paso filed a request for rehearing of this order. As discussed below, the Commission will deny El Paso's request for rehearing of the June 30 Order.

3. On July 10, 2006, El Paso filed revised tariff sheets to comply with the June 30 Order. As explained in further detail below, the Commission accepts the compliance filing subject to conditions.

I. Background

4. In 1996, El Paso entered into a settlement with its shippers that established the rates and terms and conditions of service that would apply on its system for a ten-year period, i.e., until January 1, 2006 (1996 Settlement).³ At the time the 1996 Settlement was filed, there was substantial excess capacity on El Paso's system. Following the restructuring of the natural gas industry and the unbundling of sales and transportation services, El Paso's California local distribution company customers (LDC) turned back capacity rights in accordance with their contracts and state policy. These California LDCs notified El Paso that they would be turning back substantial quantities of capacity with the result that approximately 35 percent of El Paso's system capacity was to become unsubscribed.

5. In response to the capacity turnback, El Paso filed a rate case pursuant to section 4 of the Natural Gas Act (NGA) in which it proposed to allocate the costs of the turned-back capacity to its remaining customers. To address this revenue shortfall without a considerable rate increase to the remaining customers, El Paso and its maximum rate shippers entered into the 1996 Settlement in which they agreed to share the fixed costs of the unsubscribed capacity and also to share the revenues when El Paso recontracted that turned-back capacity. Thus, El Paso's maximum rate shippers agreed to bear 35 percent of the costs of the unsubscribed capacity, and El Paso agreed to credit back to these shippers 35 percent of any remarketing revenues above a threshold level for the first eight years of the 1996 Settlement.

6. The 1996 Settlement divided the capacity turned-back by California shippers into three blocks, i.e., the "Block Capacity." Each of the blocks had different receipt points and certain restrictions on their use for the duration of the 1996 Settlement. The restrictions on the Block Capacity terminated at the end of the 1996 Settlement period, and there is no longer any Block Capacity on El Paso's system.

7. The 1996 Settlement also provided for rate certainty for the ten-year period in the form of a rate cap. Article 11.2 of the 1996 Settlement, the provision at issue in this

³ *El Paso Natural Gas Co.*, 79 FERC ¶ 61,028, *reh'g denied*, 80 FERC ¶ 61,084 (1997).

order, capped the base settlement rates and charges for ten years, subject to an annual inflation adjustment. During this time, El Paso served its firm customers under two types of contracts, full requirements (FR) contracts and contract demand (CD) contracts. CD contracts provided specific delivery rights up to specified quantity limitations at delivery points designated in the contracts. FR contracts provided that El Paso must deliver and the customer must take from El Paso, the customer's full gas requirements each day; there was no limit on the amount of gas the FR shippers could require El Paso to transport, other than the capacity of their delivery points. The CD contracts on El Paso were mainly held by California customers, and the FR contracts were mainly held by east of California (EOC) customers.

8. Because El Paso's FR customers did not have fixed contracted quantities, in the 1996 Settlement, the FR customers agreed to a rate cap in the form of fixed annual revenue requirements from which monthly payments and billing determinants were derived. Those billing determinants and revenue requirements did not change throughout the 10 years of the 1996 Settlement, regardless of the actual level of service taken by the full requirements customers. Thus, the charges paid by full requirements shippers were constant throughout the 1996 Settlement, even as their demands grew.

9. In its order accepting the 1996 Settlement, the Commission concluded that the agreement was a reasonable resolution of the excess capacity crisis facing El Paso's system at that time. However, in the first several years of the 1996 Settlement period, circumstances on El Paso's system changed dramatically. El Paso resold the turned-back capacity, and the full requirements shippers' load grew substantially to amounts far in excess of the shippers' billing determinants. As a result, there was no longer sufficient capacity to meet the demands of all firm shippers. Pursuant to section 4.2 of the General Terms and Conditions of El Paso's tariff, if El Paso had insufficient capacity to serve all transportation requests at a nominated receipt pool, firm shipper nominations were subject to pro-rata reductions based upon available capacity. However, as demands grew on El Paso's system, El Paso began routinely reducing firm customers' service requests. Firm service on El Paso's system was no longer reliable.

10. In response to the routine cuts in firm service that were taking place on the El Paso system, three separate shipper groups filed complaints concerning capacity allocation issues.⁴ In addition, the Commission directed El Paso to file a system-wide capacity

⁴ In *KN Marketing, L.P. v. El Paso*, Docket No. RP00-139-000, KN Marketing alleged that El Paso's allocation of firm mainline capacity on the east end of its system was unjust and unreasonable because El Paso sold firm capacity in excess of the available capacity. In *Joint Complainants v. El Paso*, Docket No. RP01-484-000, a group of El Paso's California CD customers alleged that El Paso had oversold its firm capacity and that this, combined with the growth of the demand of the FR customers, had resulted in

(continued)

allocation proposal. On May 31, 2002, the Commission issued an order in the Capacity Allocation Proceeding⁵ that addressed the complaints and established a framework for resolving the capacity allocation problems that had rendered firm service on El Paso unreliable. To restore reliable firm service on El Paso, the May 31 Order, among other things, directed that El Paso convert service under full requirements contracts to service under contracts with specific contract demand limits up to El Paso's available capacity, so that service to one firm shipper would not adversely affect firm service to others. The Commission allocated to the former FR shippers, as part of their new CD levels, a portion of the Block Capacity, as well as capacity related to two expansion projects on the El Paso system, Line 2000 and the Power Up Project.⁶

11. In the Capacity Allocation Proceeding the Commission found that modifying the 1996 Settlement to convert FR service to CD service was in the public interest and necessary to restore reliable firm service on the El Paso system. However, the Commission modified the 1996 Settlement only to the extent needed to restore reliable firm service on El Paso, and stated that the remainder of the 1996 Settlement would remain in place. The Commission's decision in the Capacity Allocation Proceeding was affirmed by the court in *Arizona Corporation Commission v. FERC*.⁷

12. The Commission's actions in the Capacity Allocation Proceeding were narrowly focused on restoring reliability to El Paso's system. The continued applicability of Article 11.2 after the expiration of the remaining terms and conditions of the 1996 Settlement was not at issue in that case. However, several EOC shippers raised the issue

unjust and unreasonable services on the El Paso system. In *Texas, New Mexico, and Arizona Shippers v. El Paso*, Docket No. RP01-486-000, a group of El Paso's full requirements customers alleged that El Paso had violated the NGA by failing to maintain its facilities in a manner that allowed it to provide firm service up to certificated levels.

⁵ *El Paso Natural Gas Co.*, 99 FERC ¶ 61,244 (2002) (May 31 Order), 100 FERC ¶ 61,285 (2002), *reh'g*, 104 FERC ¶ 61,045 (2003) (July 9 Order), *reh'g*, 106 FERC ¶ 61,233 (2004), *aff'd*, *Arizona Corporation Commission v. FERC*, 397 F.3d 952 (D.C. Cir. 2005) (collectively the Capacity Allocation Proceeding).

⁶ Line 2000 and the Power Up Project are two system expansions that El Paso undertook, in part, to help ensure reliable service and to facilitate the conversion of FR contracts to CD contracts required by the Capacity Allocation Proceeding.

⁷ 397 F.2d 952 (D.C. Cir. 2005).

in a request for clarification in a related El Paso proceeding.⁸ In response, the Commission stated that it was premature at that time to address the issue of the continuing applicability of Article 11.2, and that the appropriate forum to address rate issues would be in El Paso's next section 4 rate proceeding.⁹

13. On June 30, 2005, El Paso filed a general system-wide rate case (June 30 Filing), as required by Article 12 of the 1996 Settlement. With regard to Article 11.2 of the 1996 Settlement, El Paso took the position that because of the Commission's actions in the Capacity Allocation Proceeding, Article 11.2 should no longer apply to limit the rates El Paso may charge its eligible shippers. On July 29, 2005, the Commission issued an order accepting and suspending El Paso's primary tariff sheets,¹⁰ subject to refund and conditions, and establishing hearing procedures and a technical conference.¹¹ In the July 29 Suspension Order, the Commission stated that the continued applicability of Article 11.2 would be addressed after the technical conference.

14. The Commission held technical conferences on El Paso's tariff filing on September 20-21, 2005 and October 19-20, 2005. At the technical conferences the Commission established procedures granting parties an opportunity to brief the issues related to the continued applicability of Article 11.2. After the conclusion of the technical conferences and review of the post-technical conference pleadings, the Commission issued two orders. The first is the March 20 Order, which addressed post-settlement issues, including Article 11.2, and is the subject of the requests for rehearing addressed in this order. The details of the March 20 Order are summarized in section

⁸ On August 13, 2004, in El Paso's Docket No. RP04-110-000, the Arizona Electric filed a motion for clarification that the conversion to CD service should not change the calculation of the rate cap.

⁹ *El Paso Natural Gas Co.*, 109 FERC ¶ 61,359, at PP 23-24 (2005).

¹⁰ In the June 30 Filing, El Paso proposed three sets of tariff sheets, i.e., primary tariff sheets and first and second alternate tariff sheets. Each set of tariff sheets proposed a different treatment of Article 11.2 of the 1996 Settlement. El Paso's primary tariff sheets provided for the termination of Article 11.2, the first alternate tariff sheets provided for the continued application of Article 11.2 for the eligible contract demand shippers, and the second alternate sheets provided for the continued application of Article 11.2 for all eligible shippers.

¹¹ *El Paso Natural Gas Co.*, 112 FERC ¶ 61,150 (2005) (July 29 Suspension Order).

III.A below. The second order was issued on March 23, 2006¹² and addressed issues related to the implementation of the new services on El Paso's system.

15. On December 6, 2006, while requests for rehearing of these two orders were pending, El Paso filed a contested settlement (Rate Case Settlement) that resolved all of the issues set for hearing or technical conference, with the exception of issues related to Article 11.2 and issues related to maximum delivery obligations. The Rate Case Settlement established settlement rates to remain in effect on El Paso for a three-year period ending December 31, 2008, and resolved various issues related to penalties, cost of service, and accounting. On August 31, 2007, the Commission issued an order approving the Rate Case Settlement with a modification.¹³

16. With the submission of the Rate Case Settlement, the hearing procedures in this proceeding were terminated. However, because the parties were unable to resolve issues related to Article 11.2, the Rate Case Settlement provided that the requests for rehearing of the March 20 Order would remain pending, and that any resolution of those issues would not take effect until the end of the Rate Case Settlement period. The Commission will address the requests for rehearing of the March 20 Order below.

II. Relevant Settlement Provisions

17. As previously explained, the discussion herein concerns the applicability of Article 11.2 of the 1996 Settlement to El Paso's rates in this and future El Paso rate proceedings. Article 11.2 of the 1996 Settlement contains provisions governing the rates to be paid by certain eligible shippers in the post-1996 Settlement period, i.e., after December 31, 2005. Specifically, Article 11.2 provides:

11.2 Firm TSAs [transportation service agreements] In Effect on December 31, 1995, That Remain in Effect Beyond January 1, 2006. This paragraph 11.2 applies to any firm Shipper with a TSA 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 TSA. El Paso agrees with respect to such Shippers that, in all rate proceedings following the term of this Stipulation and Agreement:

¹² *El Paso Natural Gas Co.*, 114 FERC ¶ 61,305 (2006) (March 23 Order).

¹³ *El Paso Natural Gas Co.*, 120 FERC ¶ 61,208 (2007).

(a) Base Settlement Rate Escalated. El Paso will not propose to charge a rate applicable to service under such TSA during the remainder of the term thereof that exceeds the base settlement rate established under paragraph 3.2(a) applicable to such Shipper, as adjusted pursuant to paragraphs 3.2(b) and 3.5 through the term of this Stipulation and Agreement, as escalated annually thereafter through the remainder of the term of such TSA using the procedure specified by paragraph 3.2(b) unless and until such TSA is terminated by the Shipper.

(b) Unsubscribed Capacity Costs. 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 CD/billing determinants related to the capacity described in this subparagraph (b).

(c) Following the term of this Stipulation and Agreement, any Shipper to which this paragraph 11.2 applies may, at the end of the primary or rollover term of its TSA, reduce its billing determinants or CD without losing the protection of this paragraph 11.2. At the request of any Shipper, El Paso will amend the Shipper's TSA to include the provisions of this paragraph 11.2.

(d) Termination by El Paso of the TSA of a Shipper subject to this paragraph 11.2 shall not terminate such Shipper's rights to the protections afforded by this paragraph 11.2.

18. Thus, under the terms of Article 11.2(a), El Paso agreed to continue the 1996 Settlement rates, as escalated for inflation in accordance with Paragraph 3.2(b), for contracts that were in effect at the time of the 1996 Settlement and that remained in effect on January 1, 2006, unless and until the shipper terminates its TSA. In addition, Article 11.2(b) of the 1996 Settlement provides that the rates for any services to these shippers will not include any charges related to the capacity on El Paso's system on December 31, 1995 that becomes unsubscribed or discounted below the rate cap in the future.

III. Requests for Rehearing of the March 20 Order

A. March 20 Order

19. In the March 20 Order, the Commission found that its actions in the Capacity Allocation Proceeding did not abrogate Article 11.2 of the 1996 Settlement. The Commission thus determined that, in accordance with Article 11.2, the rates El Paso charges to its eligible shippers (i.e., shippers with TSAs that were in effect on December 31, 1995, and that remained in effect on January 1, 2006) may not exceed the base 1996 Settlement rates applicable to service under the shipper's TSA, as adjusted for inflation, through the remainder of the term of the TSA. The Commission stated that the rate cap embodied in Article 11.2 applies to former full requirements shippers as well as contract demand shippers. The Commission further held that because Article 11.2(a) applies only to TSAs in effect on December 31, 1995, the rate cap does not apply to newly executed contracts for new services. In addition, the Commission concluded that the rate cap does not apply to expansion capacity (i.e., the Line 2000 and Power Up Project capacity).

20. With regard to Article 11.2(b), the Commission found that the rates charged to eligible shippers for any service (not limited to service under 1996 TSAs) 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. The Commission stated that in determining whether specific capacity was part of El Paso's 1995 system, the Commission will presume the first 4000 MMcf/d of firm subscribed capacity on El Paso's system is 1995 capacity.

21. The Commission further explained that it was establishing general guidelines for application of Article 11.2 and that the parties would address the details of implementation at the hearing established in the July 29 Suspension Order.¹⁴ The Commission specifically stated that the application of Article 11.2(a) to the rates of eligible shippers, as well as the calculation of such rates, were matters to be addressed at the hearing. Further, the Commission stated that the reasonableness of El Paso's rates would be addressed at the hearing, and that although El Paso would have the burden of establishing the justness and reasonableness of its rates, the 1996 Settlement does not preclude El Paso from proposing rates that recover its cost of service.

22. Several parties filed requests for rehearing of the March 20 Order. The requests for rehearing raise issues concerning the continuing applicability of Article 11.2, as well

¹⁴ The hearing procedures have since been terminated with the submission and acceptance of the Rate Case Settlement.

as its application to the former FR shippers, to the Block Capacity, to expansion capacity, and to new services. These issues are discussed below.

B. Continuing Applicability of Article 11.2

1. March 20 Order

23. In the March 20 Order, the Commission rejected El Paso's argument that Article 11.2 of the 1996 Settlement should no longer apply to any shippers because of changes the Commission made to other aspects of the 1996 Settlement and to El Paso's contracts in the Capacity Allocation Proceeding. The Commission found that nothing in the Capacity Allocation Proceeding resulted in the abrogation of Article 11.2 of the 1996 Settlement at that time or justifies its abrogation in this proceeding.

2. Requests for Rehearing

24. On rehearing, El Paso argues that the Commission erred in the March 20 Order by upholding the continuing applicability of Article 11.2. El Paso argues that by modifying the 1996 Settlement to El Paso's detriment in the Capacity Allocation Proceeding, the Commission frustrated the central purpose of the 1996 Settlement. El Paso therefore asserts it should be excused from complying with Article 11.2 of the 1996 Settlement.

25. According to El Paso, the central purpose of the 1996 Settlement was for the parties to agree upon a mechanism for sharing the risks associated with the capacity turned back by the California shippers, i.e., the Block Capacity. El Paso explains the 1996 Settlement provided that El Paso would bear 65 percent of the costs of the Block Capacity during the first eight years of the 1996 Settlement period and 100 percent during the last two years. In return, El Paso explains, it was entitled to retain 65 percent of all revenues received from the sale of the Block Capacity during the first eight years of the 1996 Settlement period and 100 percent during the last two years.

26. El Paso argues the Commission's requirement in the Capacity Allocation Proceeding that El Paso provide a portion of the Block Capacity to its former FR shippers as part of their new CDs without charge for the remaining term of the 1996 Settlement deprived El Paso of approximately \$175 million in revenues, since it was unable to remarket this portion of the Block Capacity. El Paso argues this frustrated the central purpose of the 1996 Settlement because it changed the expected benefits of the bargain. El Paso argues that this undermining of the 1996 Settlement bargain was not due to shifting market conditions or changes in financial condition, but was caused by an unanticipated modification to the 1996 Settlement by the Commission.

27. El Paso further argues that it should be excused from its Article 11.2 obligations under applicable principles of contract law. El Paso states that in its comments it referred to several treatises and authorities on contract law relating to the doctrine of commercial

frustration and impossibility,¹⁵ and states that under these principles, “a party is excused from performance when a government order frustrates the central purpose of the contract.”¹⁶ El Paso states that it does not dispute the Commission’s authority to modify the 1996 Settlement, but argues it was the Commission’s lawful exercise of its authority that frustrated the purpose of the 1996 Settlement, and consequently, excused El Paso from performance under Article 11.2. In addition, El Paso disagrees with the Commission’s statement in the March 20 Order that regulatory action that merely makes performance more onerous does not excuse performance. El Paso states that the orders in the Capacity Allocation Proceeding disturbed the central purpose of the 1996 Settlement, rather than merely rendering performance more onerous.

3. Commission Determination

28. As El Paso states, the 1996 Settlement addressed the problem of how El Paso was to recover costs associated with the capacity that was turned back to El Paso by its California shippers. This capacity turnback threatened to increase the rates of El Paso’s remaining shippers. However, the 1996 Settlement resolved the capacity turnback problem by means of an agreed-upon sharing of the costs and risks of the unsubscribed capacity. Pursuant to this agreement, El Paso’s existing firm shippers paid to El Paso \$254.8 million as their risk-sharing amount.¹⁷ For the first eight years of the 1996 Settlement period, El Paso was to share with these shippers the revenues from any sales of this turned-back capacity.¹⁸

29. However, in the years following the approval of the 1996 Settlement, the capacity situation on El Paso’s system changed in a way the parties did not anticipate. In a relatively short time, El Paso’s system went from one of excess capacity to one of strained capacity. As a result, El Paso began to routinely reduce nominations for firm service through *pro rata* allocations,¹⁹ making firm service on the system unreliable. Because of these extraordinary circumstances on the El Paso system, the Commission

¹⁵ El Paso cites 30 Williston § 77:95 (4th ed. 2004).

¹⁶ Restatement (Second) of Contracts § 261, 264 (1981).

¹⁷ Article 3.3 of the 1996 Settlement.

¹⁸ Article 3.4 of the 1996 Settlement.

¹⁹ El Paso’s tariff provided for *pro rata* allocations of firm service when El Paso had insufficient capacity to serve all firm customers. However, because of the strained capacity situation, these curtailments were becoming routine, rather than the exception, making firm service unreliable.

determined in the Capacity Allocation Proceeding that the existing allocation methodology on El Paso, with *pro rata* allocations of firm service when El Paso had insufficient capacity to serve all firm customers, was not just and reasonable or in the public interest. Accordingly, the Commission developed a solution which involved, among other things, the conversion of FR contracts to CD contracts.

30. The Commission made clear that it was taking limited action in the Capacity Allocation Proceeding, and modified the 1996 Settlement and FR contracts only to the extent necessary to restore reliable firm service on the El Paso system. In employing this surgical approach to the modification of the 1996 Settlement, the Commission specifically addressed the question of whether, instead of making only these limited changes to the 1996 Settlement, it should abrogate the entire settlement. The Commission concluded that the facts and the law did not support the abrogation of any other parts of the 1996 Settlement, including the Article 11.2 rate cap. In reaching this conclusion, the Commission balanced the interests of all parties and considered the public interest. At the time, El Paso supported the Commission's decision to modify the 1996 Settlement in a limited manner.²⁰ El Paso did not seek rehearing of the Commission's ruling and the Commission's decision was affirmed by the court.²¹

31. Here, El Paso argues that while it does not dispute the Commission's authority to modify the 1996 Settlement,²² the Commission's lawful exercise of its authority in the Capacity Allocation Proceeding frustrated the central purpose of the 1996 Settlement. El Paso specifically contends that by requiring El Paso to provide certain amounts of the Block Capacity to its former FR shippers as part of their new CDs without charge for the remaining term of the 1996 Settlement, the Commission's actions deprived El Paso of lost remarketing revenues. El Paso argues that this frustrated the central purpose of the 1996 Settlement, and pursuant to the applicable principles of contract law, excuses El Paso from performance under Article 11.2. We disagree that El Paso's inability to remarket all of the Block Capacity frustrated the central purpose of the 1996 Settlement.

32. The 1996 Settlement did authorize El Paso to remarket expired capacity contracts and share the revenues from those sales with its firm customers,²³ and early on, the

²⁰ El Paso was not one of the parties in the Capacity Allocation Proceeding that argued for complete, as opposed to partial, abrogation of the 1996 Settlement.

²¹ See *Arizona Corporation Commission v. FERC*, 397 F.3d 952 (D.C. Cir. 2005).

²² Nor could El Paso dispute the Commission's authority to modify the 1996 Settlement since the Commission's actions in the Capacity Allocation Proceeding have been affirmed by the court. See *id.*

²³ See Article 3.4 of the 1996 Settlement.

Commission approved some of these remarketed contracts as consistent with the 1996 Settlement.²⁴ However, the 1996 Settlement did not provide El Paso with an unqualified right to remarket the expired capacity. The option to do so was always tempered by the obligations in section 16.3 of the 1996 Settlement²⁵ and section 284.7(a)(3) of the Commission's regulations,²⁶ which require El Paso to administer its pipeline in a manner that provides reliable firm service to its existing customers. It is for this reason that, as capacity on the El Paso system became scarce and it became apparent that further remarketing of expired capacity contracts would threaten El Paso's ability to meet its obligations under its contracts with its current firm shippers, including the FR shippers, the Commission denied further sales of the expired capacity contracts.²⁷

33. The Commission's decision in the Capacity Allocation Proceeding to require El Paso to use a portion of the Block Capacity to serve its existing firm shippers is similarly justifiable. As discussed further in the next section, El Paso's contracts with its FR customers required it to use all its existing capacity, including the Block Capacity, to serve any increased demand of the FR customers. Thus, El Paso's ability to remarket the Block Capacity to other shippers was always subject to its contractual obligation under the FR customers' TSAs to use the Block Capacity to serve the FR customers. Section 16.3 of the 1996 Settlement reaffirmed this fact. Thus, when the Commission required El Paso, in the Capacity Allocation Proceeding, to use a portion of the Block Capacity to serve the FR shippers, it was simply enforcing El Paso's existing contractual obligation under the FR customers' TSAs and the 1996 Settlement. In making this decision, the Commission did not abrogate the central purpose of the 1996 Settlement. Rather, the Commission held El Paso to its obligation to administer its pipeline consistent with

²⁴ See *El Paso Natural Gas Co.*, 88 FERC ¶ 61,139 (1999); *El Paso Natural Gas Co.*, 90 FERC ¶ 61,050 (2000).

²⁵ Section 16.3 of the 1996 Settlement provides:

Service Obligations. El Paso agrees and affirms that, during the effectiveness of this Stipulation and Agreement, it will maintain and operate facilities sufficient to satisfy and perform the service obligations with respect to both quality and quantity of service imposed upon it by, and subject to the conditions applicable to, the provisions of this Stipulation and Agreement and its firm TSAs in effect on December 31, 1995.

²⁶ See 18 C.F.R. § 284.7(a)(3) (2008).

²⁷ See May 31 Order and the May 1, 2002 Order in Docket No. RP97-287-057.

section 16.3 of the 1996 Settlement and the Commission's regulations, and use its existing capacity to satisfy its contractual obligations under the existing firm customers' TSAs.

34. Granted, prior to the Capacity Allocation Proceeding, El Paso's tariffs, contracts, and settlements did operate to create conflicting requirements regarding how El Paso should deal with the strained capacity situation on the system. However, in the Capacity Allocation Proceeding, the Commission adopted an allocation methodology that resolved this conflict going forward. The Commission also made clear in the Capacity Allocation Proceeding that El Paso continues to be bound by its obligation under section 16.3 of the 1996 Settlement. Thus, the Commission decision to allocate a portion of the Block Capacity to the former FR shippers, and the resulting reduction of the amount of Block Capacity for resale, did not undermine the risk-sharing arrangement of the 1996 Settlement, because that arrangement was always qualified by the requirement in section 16.3 that El Paso maintain and operate its facilities in a manner sufficient to perform and satisfy its service obligations under its contracts with its firm customers.

35. For the same reasons, El Paso should not be excused from performance under Article 11.2 pursuant to the doctrines of frustration of purpose or impossibility. As explained above, the Commission did not frustrate the central purpose of the 1996 Settlement when it determined El Paso must use a portion of the Block Capacity to serve the former FR shippers, it simply enforced an obligation that was in existence at the time the parties entered into the 1996 Settlement. Granted, the strained capacity situation on El Paso's system made it more difficult for El Paso to fulfill its obligation to maintain and operate its facilities in a manner sufficient to perform and satisfy its service obligations. However, the Commission's actions in the Capacity Allocation Proceeding were designed to improve the situation on El Paso's system and make it easier for El Paso to fulfill its obligations, while also maintaining, as much as possible, the benefits of the parties' settlement bargain. The limited changes the Commission made to the 1996 Settlement did not frustrate the purpose or make it impossible for El Paso to perform under the agreement. Further, the Restatement makes clear that regulatory action that merely makes contract performance more onerous does not excuse performance. In addition, as we explained in the March 20 Order, the circumstances here are significantly different from those described in the contract materials cited by El Paso. Section 261 of the Restatement (Second) of Contracts applies to situations where the government frustrates a contract's central purpose by some action outside of the contract. It does not

apply to situations, such as this one, where the government enforces existing contractual obligations.²⁸

36. It is also incorrect for El Paso to assert that the change in expected benefits from the 1996 Settlement was due to the Commission's actions, and not changes in market conditions. By intervening in the Capacity Allocation Proceeding, the Commission was responding to the market conditions that reduced the excess capacity on El Paso's system. Had these market conditions not existed, and there been enough excess capacity on the El Paso system, El Paso could have reliably served its existing firm shippers, while also remarketing the Block Capacity. However, this was not the case and therefore the Commission became involved in the Capacity Allocation Proceeding in an effort to resolve this problem. Thus, when the Commission required El Paso to allocate a portion of the Block Capacity to the former FR shippers in the Capacity Allocation Proceeding, it was simply responding to market conditions.

37. The Commission therefore rejects El Paso's argument that the Commission's actions in the Capacity Allocation Proceeding frustrated the central purpose of the 1996 Settlement. As explained above, El Paso's ability to remarket the Block Capacity under the 1996 Settlement was not unqualified. The Commission made clear in the Capacity Allocation Proceeding and other orders that El Paso could not resell capacity that was needed to serve the needs of its existing shippers. Thus, the Commission's allocation of the Block Capacity to the FR shippers to meet their needs under their contracts did not violate El Paso's rights under the 1996 Settlement, and provides no basis for relieving El Paso of its obligations under Article 11.2. As a result, the Commission denies El Paso's request for rehearing on this issue.

C. Applicability of the *Mobile-Sierra* Doctrine to Article 11.2

1. March 20 Order

38. In the March 20 Order, the Commission explained that any modification of the 1996 Settlement to eliminate Article 11.2 must be evaluated under the public interest

²⁸ The Commission did modify the FR shippers' contracts in the Capacity Allocation Proceeding by shifting those contracts from FR to CD contracts. However, it is not this action that El Paso alleges interferes with its ability to remarket the Block Capacity. Rather, it was the Commission's requirement that El Paso use the Block Capacity to serve the FR customers under the revised CD contracts which allegedly interfered with El Paso's ability to remarket the Block Capacity. However, as explained above, the FR contracts required El Paso to use the Block Capacity to serve the FR customers, and therefore that obligation would have existed regardless of whether the Commission required the FR contracts to be shifted to CD contracts.

standard of the *Mobile-Sierra*²⁹ doctrine. After reviewing El Paso's arguments under this standard, the Commission found that El Paso did not provide a sufficient factual basis for modifying the 1996 Settlement under *Mobile-Sierra*.³⁰

2. Requests for Rehearing

39. On rehearing, El Paso states that it could justify the elimination of its obligations under Article 11.2 pursuant to the *Mobile-Sierra* public interest standard, but argues that this standard is not applicable to Article 11.2. El Paso contends *Mobile-Sierra* does not apply based on the plain language of Article 11.2(a) which permits the Commission to reject the rates produced by Article 11.2(a) if those rates are not just and reasonable.

40. El Paso argues Article 11.2(a) relates only to the rates that El Paso must propose, but does not limit the rates the Commission may approve, or the rates that El Paso can actually charge. El Paso states that the 1996 Settlement does not prohibit El Paso from charging rates higher than the capped rates if the Commission so authorizes. El Paso argues that where a contract or settlement provision, such as Article 11.2(a), merely sets forth what the pipeline will propose, the Commission is not required to approve what the pipeline ultimately proposes.³¹ El Paso states that it is well-established that neither the parties to a settlement nor the Commission itself can bind future Commissions to approve a particular rate.³² Thus, El Paso contends that any interpretation of Article 11.2(a) that would require parties to meet the *Mobile-Sierra* public interest standard in order to defeat the application of Article 11.2(a) would not only conflict with the plain language of Article 11.2(a), but would conflict with the canon of construction that contract interpretations which would render a contract unlawful are disfavored. El Paso asserts that since the 1996 Settlement could not require the Commission to approve Article 11.2(a) rates, it follows that El Paso and the parties who oppose the application of the Article 11.2(a) rate caps are not seeking to change the 1996 Settlement. Therefore, El Paso concludes that by definition, the *Mobile-Sierra* public interest standard does not

²⁹ *United Gas Pipeline Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956); *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Mobile Sierra*).

³⁰ The Commission did state in the March 20 Order that at the hearing pending in that proceeding the parties could address the issue of whether the rates resulting from application of Article 11.2 are in the public interest. However, with the Commission's approval of the Rate Case Settlement, the hearing procedures were terminated.

³¹ El Paso cites *Tennessee Gas Pipeline Co.*, 50 FERC ¶ 61,286, at 61,921 (1990).

³² El Paso cites *Bonneville Power Admin.*, 112 FERC ¶ 61,012, at P 32 (2005); *Columbia Gas Transmission Corp.*, 79 FERC ¶ 61,044, at 61,203-03 (1997).

apply here, and the Commission can reject the Article 11.2(a) rates if they do not meet the lower just and reasonable standard.

3. Commission Determination

41. We agree that if El Paso files for rates in a future proceeding that is set for hearing, any hearing on El Paso's proposed rates will determine just and reasonable rates for all of El Paso's shippers, taking into account the circumstances on El Paso, including El Paso's obligations under Article 11.2 of the 1996 Settlement. This does not mean, however, that the *Mobile-Sierra* public interest standard should not apply to any arguments or evidence that El Paso submits to support its claim that it should be excused from its obligations under that provision. In the Capacity Allocation Proceeding, the Commission found that any changes to the 1996 Settlement must be justified under the *Mobile-Sierra* public interest standard,³³ and the court upheld the Commission's decision.³⁴ Therefore, Commission's decision to apply *Mobile-Sierra* to changes to the 1996 Settlement is final and not subject to review here. Despite El Paso's contention, there is no justifiable reason to make an exception for changes to Article 11.2, while holding the rest of the 1996 Settlement to review under *Mobile-Sierra*. As such, El Paso's request for rehearing is denied.

D. Applicability of Article 11.2 to Former FR Shippers

1. March 20 Order

42. In the March 20 Order, the Commission clarified that in converting FR contracts to CD contracts in the Capacity Allocation Proceeding, it did not cancel, terminate, or abrogate these contracts. The Commission stated that the converted contracts for CD service were a continuation of the same service the shippers received under their former FR contracts with some changes ordered by the Commission. Therefore, the Commission concluded that Article 11.2 still applies to the former FR shippers' contracts.

2. Requests for Rehearing

43. El Paso asserts that the Commission erred in finding that its actions did not abrogate the FR shippers' contracts and that Article 11.2 applies to the FR shippers' new CD contracts. El Paso disagrees with the Commission's statement that it did not abrogate the FR contracts, but rather directed that service under FR contracts be "converted" to service under CD contracts, and that this conversion resulted in an amendment of the

³³ See May 31 Order, 99 FERC at 62,005.

³⁴ See *Arizona Corporation Commission v. FERC*, 397 F.3d 952 (D.C. Cir. 2005).

contracts, not an abrogation. El Paso argues the Commission clearly contemplated that the FR contracts, not merely the service under those contracts, would be converted to and replaced by new CD contracts.³⁵ El Paso asserts that by the express terms of the 1996 Settlement,³⁶ Article 11.2 applies only to contracts that existed in 1995 and that also exist today. Therefore, El Paso argues the Commission-required abrogation of FR contracts in the Capacity Allocation Proceeding terminated any continued applicability of Article 11.2.

44. In addition, El Paso requests clarification that the March 20 Order only addressed the narrow contract issue of whether the former FR contracts had been abrogated for purposes of determining whether Article 11.2(a) applies, and did not address other contracting issues in dispute between El Paso and its former FR shippers, including the issue of the number of contracts that former FR shippers must hold under section 9.1 of El Paso's tariff and the form of those contracts.

3. Commission Determination

45. As we explained in the March 20 Order, the Commission made changes to the FR contracts in the Capacity Allocation Proceeding that were necessary in the public interest. That action did not terminate the service relationship between El Paso and these shippers, and the contracts for CD service are a continuation of the service the FR shippers received under their FR contracts with the changes ordered by the Commission to restore firm service on El Paso. Further, as the Commission pointed out in the March 20 Order, the conversion of FR service to CD service was specifically permitted by the 1996 Settlement without the loss of the Article 11.2 protections.³⁷ In addition, Article 11.2 applies to the rates of El Paso's eligible shippers for the period that the "*Shipper has not*

³⁵ El Paso cites the July 9 Order, 104 FERC ¶ 61,045 at P 93 (stating that the "FR contracts must be converted to CD contracts ..." and that this makes clear that the Commission was not converting service under the FR contracts to service under the CD contracts, but was requiring the FR shippers to enter into new contracts).

³⁶ Article 11 states that its provisions apply to "any firm Shipper with a TSA 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 TSA." El Paso argues that the Commission erroneously relied upon the last phrase to conclude that, since the Shippers did not terminate the TSAs, Article 11 still applies. El Paso contends that that phrase only is operative if the TSA is still in effect on January 1, 2006, which the FR contracts are not.

³⁷ Article 9.2 of the 1996 Settlement provides a shipper the right to convert from FR to CD service after January 1, 2002.

terminated such TSA,” and Article 11.2(a) specifically states that the rate cap applies to these shippers “unless and until such TSA is terminated *by the shipper.*” The amendment of the FR contracts to comply with the Commission’s orders in that proceeding cannot be considered termination of the contract *by the shipper.*³⁸ Thus, the Commission affirms its finding that Article 11.2 applies to the former FR shippers and therefore denies El Paso’s request for rehearing.

46. In response to El Paso’s request for clarification, the Commission clarifies that the March 20 Order addressed the issue of whether Article 11.2 applies to the former FR contracts and did not consider other contracting issues that may be the subject of dispute among the parties.

E. Applicability of Article 11.2 to Block Capacity

47. As explained above, the 1996 Settlement divided the capacity turned back to El Paso by the California shippers into three blocks. Each of the blocks had different receipt points and certain restrictions on their use for the duration of the 1996 Settlement.³⁹ In the Capacity Allocation Proceeding, the Commission allocated some of this Block Capacity to the FR shippers as part of their new CD levels.⁴⁰ The restrictions on the Block Capacity terminated at the end of the 1996 Settlement period. There is no longer any Block Capacity on El Paso’s system.

³⁸ As the Commission explained in the March 20 Order, the Commission did not require El Paso to replace the FR contracts with entirely new contracts or to make any changes to the contracts other than those necessary to implement the conversion of FR to CD service. If El Paso chose to issue new contracts, then that was El Paso’s choice and not termination by the shipper.

³⁹ Block I capacity has alternate receipt point rights unless the capacity is sold for maximum tariff rates and, in that event, it has primary receipt point rights only to the Permian and Anadarko Basins, but not to the San Juan Basin. Block II capacity is a block of 614 MMcf/d of turned back capacity designated for primary point deliveries to Topock for PG&E or other shipper(s) serving a market in PG&E’s service territory (collectively Block II shippers), and has primary access rights to all system receipt points. Block II shippers have recall rights. Block III has primary access rights to all receipt points.

⁴⁰ See *El Paso Natural Gas Co.*, 104 FERC ¶ 61,045 at P 171 (2003).

1. Request for Clarification

48. El Paso asks the Commission to clarify that the Article 11.2 rate cap does not apply to the former Block Capacity that is now included in the CDs of the former FR shippers. El Paso argues that applying the rate cap to the Block Capacity would conflict with the 1996 and 1990 Settlements. With respect to the 1996 Settlement, El Paso argues that because the Block Capacity was turned back to El Paso during the period of January 1, 1995, to January 1, 1998, this capacity was not subject to the rate cap at the beginning of the 1996 Settlement term. El Paso further argues that, when it subsequently remarketed the Block Capacity during the middle of the 1996 Settlement term, the Block Capacity was not subject to the rate cap because the new shippers purchasing the Block Capacity did not hold it continuously during the ten-year term of the 1996 Settlement. It therefore follows, El Paso argues, that the Block Capacity the Commission allocated to the former FR shippers as of September 1, 2003, should also not be subject to the rate cap.

49. El Paso also explains that under the 1996 Settlement, it was required to remarket the Block Capacity to other shippers and share the revenues with its customers. Therefore, El Paso states, the former FR shippers had no right to the Block Capacity under the TSAs that they held on December 31, 1995, and there is no basis to conclude that the rate cap applies to this capacity. El Paso argues this interpretation is supported by the Commission's statement in the March 20 Order that the rate cap was limited to service El Paso could provide the FR customers at the time of the 1996 Settlement with its system as it then existed.⁴¹ El Paso states that at the time of the 1996 Settlement, El Paso could not provide the Block Capacity to FR shippers because that capacity was either under contract to other shippers or had been remarketed to other CD shippers in accordance with the risk sharing provisions of the 1996 Settlement.

50. El Paso further argues that applying the rate cap to the Block Capacity would conflict with the 1990 Settlement⁴² because doing so would effectively require El Paso

⁴¹ March 20 Order, 114 FERC ¶ 61,290 at P 81.

⁴² Section 3.6 of El Paso's 1990 Settlement provides:

El Paso shall not be required to construct any facilities that are not economically justifiable. The provisions of this section 3.6 shall survive the term of this Stipulation and Agreement.

The Commission has held that the “economically justifiable” language means either that any new capacity would bring increased revenues to El Paso, or that the shippers would share the expense with El Paso. *See* July 9 Order at P 103. Therefore,

(continued)

to subsidize FR load growth by providing the former FR shippers with rate-capped capacity in lieu of an expansion. El Paso contends this is contrary to the 1990 Settlement, which requires the shippers to pay for the cost of expansion capacity needed to serve their growth. El Paso argues that if it had no obligation under the 1990 Settlement to build expansion capacity for the FR shippers at its own expense, then it also had no obligation to give the FR shippers a portion of the Block Capacity at its own expense in lieu of building an expansion. El Paso concludes that the Commission has effectively indirectly required El Paso to pay for a portion of the cost of FR growth, even though it was directly prohibited from doing so by the 1990 Settlement. El Paso claims this result violated the well-established principle that the Commission cannot do indirectly what it is barred from doing directly.⁴³ El Paso further asserts that applying the rate cap to the Block Capacity will reward shippers for declining to fulfill their obligation under the 1990 Settlement to fund expansions needed to serve their growth.

51. El Paso also asserts that the fact that FR shippers' demands could grow and change during the term of the 1996 Settlement does not justify applying the rate cap to the Block Capacity. El Paso specifically objects to the Commission's statement in the March 20 Order that "the full requirements clause in each FR customer's 1995 TSAs obligated El Paso to provide those customers any additional service not requiring an expansion."⁴⁴ El Paso contends this incorrectly implies that the FR shippers had an unlimited growth right and that El Paso agreed to serve such a growth at capped rates. El Paso argues the rate cap was only intended to apply to the capacity⁴⁵ that a narrow class of shippers who were parties to the 1996 Settlement held on December 31, 1995 under their existing TSAs, and was never intended to apply to the then-unwanted Block Capacity, regardless of the future level of FR growth. El Paso asserts that capping the rates on the former FR shippers' Block Capacity would effectively re-write the 1996 Settlement to require El Paso to assume the risk that its entire system could eventually become subject to the rate cap, depending on the level of FR growth and the level of future unsubscribed capacity.

pursuant to this section of the 1990 Settlement, El Paso was not obligated under the 1996 Settlement or under the NGA to build capacity at its own expense to meet the growth in the needs of the full requirements shippers.

⁴³ El Paso cites *Richmond Power and Light v. FERC*, 574 F.2d 610, 620 (D.C. Cir. 1978).

⁴⁴ See March 20 Order, 114 FERC ¶ 61,290 at P 85.

⁴⁵ As explained above, the Article 11.2(a) rate caps do not apply to *capacity*, but apply to service under an eligible TSA.

52. Finally, El Paso argues that applying the rate cap to the Block Capacity would conflict with the Commission's stated intent to "maintain the 1996 Settlement's balance of equities between CD and FR shippers."⁴⁶ El Paso states the Commission recognized that if historical CD shippers wanted to purchase Block Capacity, they had to pay an uncapped rate for that capacity. El Paso asserts the same result should also apply to the former FR shippers in order to maintain the "balance of equities" between historical CD shippers and former FR shippers. El Paso thus concludes that the Article 11.2(a) rate cap should not apply to the Block Capacity held by former FR shippers, just as the rate cap does not apply to Block Capacity held by historical CD shippers.

2. Commission Determination

53. The Commission clarifies that the rate cap does apply to the portion of the Block Capacity included in the CDs of the former FR shippers. El Paso's argument that the rate cap should not apply to this Block Capacity is inconsistent with the language of the 1996 Settlement and with the nature of the FR contracts. Article 11.2(a) applies to firm TSAs in effect on December 31, 1995, that remain in effect beyond January 1, 2006, and provides that El Paso will not charge, for the duration of the term of the TSA, a rate that exceeds the rate cap for service under the TSA that was in effect on December 31, 1995 and remains in effect on January 1, 2006. Thus, the focus of this provision is the *service obligation* under the eligible TSA, not the *capacity* used to meet that obligation. As such, the capacity used to provide that service is not determinative of whether the rate cap applies.⁴⁷

54. In the Capacity Allocation Proceeding, the Commission made certain findings about the nature of the FR service and based its remedy in that proceeding on those conclusions.⁴⁸ Specifically, the Commission found that the FR service was not limited to any specific capacity or any specific amount of capacity, but obligated El Paso to serve the full requirements of these shippers. The Commission stated that the shippers' demands under these contracts could change and grow during their duration, and the 1996 Settlement placed no limits on the amount of growth that could occur under the FR contracts.⁴⁹ In other words, there was no limit on the amount of capacity the FR shippers

⁴⁶ March 20 Order, 114 FERC ¶ 61,290 at P 86.

⁴⁷ We recognize that, with regard to the expansion capacity, the Commission has found that the vintage of the capacity is relevant to determining El Paso's service obligation, but as we explain below, the circumstances are not analogous.

⁴⁸ These findings are final and affirmed and not subject to collateral attack.

⁴⁹ July 9 Order, 104 FERC ¶ 61,045 at P 27.

could demand under their contracts, other than the physical capacity of their delivery points.⁵⁰ Therefore, as the FR shippers' demands increased, El Paso's provision of additional capacity to meet the growth in demand under these contracts was part of El Paso's service obligation to these shippers, and was service under the TSAs that were in effect on December 31, 1995.⁵¹

55. El Paso is correct in stating that when the Block Capacity was remarketed to new shippers during the term of the 1996 Settlement, those contracts were not subject to the rate cap. However, it does not follow that the increase in demand of the FR shippers (in accordance with their 1995 contracts) should not be covered by the rate cap simply because El Paso used the Block Capacity to meet this demand growth. As explained above, when El Paso provided service to the FR shippers to meet their increase in demand, it did so under the FR shippers' 1995 TSAs, and thus is subject to the rate cap, regardless of whether the capacity used was Block Capacity.

56. Moreover, if the parties intended the rate cap to apply only to non-Block Capacity, they could have drafted the 1996 Settlement to provide as much. However, there is no language in Article 11.2(a) limiting its application to non-Block Capacity. Article 11.2 distinguishes between capacity in existence on December 31, 1995 and new capacity built afterwards, but Article 11.2 does not indicate that a portion of the pre-December 31, 1995 capacity should be treated differently than the rest. As such, there is no basis in the language of Article 11.2 to hold that the rate cap does not apply to Block Capacity.

57. El Paso contends that if it had no obligation under the 1990 Settlement to build expansion capacity for the FR shippers at its own expense, then it also had no obligation to give the FR shippers a portion of the Block Capacity. El Paso's argument ignores the significant difference between a finding that El Paso is required to meet its firm obligation to its FR shippers with its existing system capacity, and requiring El Paso to construct capacity at its own expense to meet those growing demands. Contrary to El Paso's assertion, expansion capacity is not analogous to the Block Capacity. Unlike the Block Capacity, expansion capacity at issue here (i.e., Power Up Project and Line 2000) was not part of the system at the time of the implementation of the 1996 Settlement. More importantly, the provision in the 1990 Settlement stating that El Paso is not

⁵⁰ *Id.* P 30 (referring to "unrestricted growth" under the FR contracts), P 32 (growth under the FR contracts was "open ended" and "with no limit"), P 61 (no cap on growth), and P 115.

⁵¹ In contrast, if the CD shippers, who had contracts for specific amounts of capacity, required additional system capacity, these shippers would be required to execute new contracts for this capacity and these new contracts executed after December 31, 1995 would not be within the scope of Article 11.2(a).

required to build capacity at its own expense to meet the growth in demands by the FR shippers does not apply to capacity that was already part of El Paso's system, such as the Block Capacity. As explained above, El Paso has an obligation to meet the demands of its current firm shippers with its existing capacity.⁵² While El Paso was under no obligation to expand its system, it did have an obligation to serve its current customers with the capacity existing on its system, regardless of whether the capacity needed for that purpose was part of the former Block Capacity.⁵³

58. In addition, El Paso's suggestion that the FR contracts did not include unlimited growth rights is contrary to the Commission findings in the Capacity Allocation Proceeding and has no basis in the 1996 Settlement provisions. It was the unlimited growth rights under the FR contracts that caused allocation problems on El Paso's system and necessitated the Commission's action in the Capacity Allocation Proceeding. As mentioned above, the orders in that proceeding discussed repeatedly the fact that there were no limits on the amount of growth that could occur under these FR contracts,⁵⁴ and found that this unlimited growth was the most significant cause of the allocation problems on El Paso's system.⁵⁵ It is for this reason that the Commission found it necessary and in the public interest to place limitations on the future growth under the FR contracts, which involved modifying both the 1996 Settlement and the FR shippers' service contracts. El Paso's argument to the contrary, and its suggestion that existing system capacity need not have been used to serve FR shippers' demands, is inconsistent with the record and the Commission's decisions in the Capacity Allocation Proceeding. The Commission's findings regarding the nature of the growth rights under the FR contracts in the Capacity Allocation Proceeding have been upheld by the court upon review and are not subject to collateral attack here.⁵⁶

59. Further, El Paso provides no evidence substantiating its assertion that the FR shippers refused to support an expansion to serve their needs. El Paso also mischaracterizes the Commission's actions in the Capacity Allocation Proceeding by asserting that the Commission gave the FR shippers Block Capacity in lieu of requiring them to pay for additional expansion. As explained above, the FR shippers were entitled to existing capacity on the El Paso system to serve the growth in their demand. Holding

⁵² See section 16.3 of the 1996 Settlement and 18 C.F.R. § 284.7(a)(3) (2008).

⁵³ *Id.*

⁵⁴ See July 9 Order, 104 FERC ¶ 61,045 at PP 27, 30, 32, 61.

⁵⁵ See May 31 Order, 99 FERC at 62,000, 62,003, 62,016.

⁵⁶ See *Arizona Corporation Commission v. FERC*, 397 F.3d 952 (D.C. Cir. 2005).

El Paso to its obligation to serve its firm shippers' needs with existing capacity is different than ordering a pipeline or a shipper to pay for an expansion, which the Commission cannot, and did not, do. As we have explained, El Paso had an obligation to serve its firm customers with the capacity that was unsubscribed on its system, and the rate cap applies to all the capacity that was used to serve the FR shippers under their eligible TSAs. El Paso was providing FR service with existing capacity, including the Block Capacity that had been turned back by the California shippers. Despite El Paso's contention, there is no basis for the Commission to remove the rate cap from Block Capacity that El Paso used to meet its obligations to its former FR shippers, regardless of whether FR shippers refused to pay for an expansion of system capacity.

60. Finally, the Commission finds that the application of the rate cap to the Block Capacity will not disrupt the balance of equities between CD and FR shippers. While the Commission placed the former FR shippers in the same position as the other CD shippers going forward in the Capacity Allocation Proceeding, the Commission also recognized that the 1996 Settlement provided for two types of service – CD and FR – and that these services had very different characteristics. The Commission took these differences into consideration when fashioning its remedy in the Capacity Allocation Proceeding.⁵⁷ As such, the CD customers could nominate volumes up to their fixed contract demand, while the FR shippers could nominate their daily requirements with no limits on the amount they could nominate other than the physical capacity of their delivery points. El Paso cites the Commission's statement in the March 20 Order that "[i]t is just and reasonable and in the public interest and consistent with the Settlement that the former FR customers also pay the uncapped FT rate for the increased service their 1995 TSAs *did not require* El Paso to provide"(emphasis added).⁵⁸ As we discussed above, the 1995 FR contracts did require El Paso to provide service to meet the FR shippers increasing demands and to use the Block Capacity to meet those needs when necessary. Thus, El Paso mistakenly relies on the statement above from the March 20 Order to support its position. Applying the rate cap to the portion of the Block Capacity included in former FR shippers' CDs does not disrupt the balance of equities between CD and FR shippers, and is just and reasonable.

F. Appropriate Rate Cap for Block Capacity

1. Requests for Rehearing or Clarification

61. El Paso states that if the Commission determines that the rate cap applies to the Block Capacity, it seeks clarification, or in the alternative, rehearing, that it is permitted

⁵⁷ See *e.g.*, July 9 Order, 104 FERC ¶ 61,045 at PP 115-117.

⁵⁸ March 20 Order, 114 FERC ¶ 61,290 at P 86 (emphasis added).

to apply the California rate cap to the Block Capacity.⁵⁹ El Paso argues that the capacity turnback which led to the creation of the Block Capacity resulted from a massive capacity turnback by California utilities of capacity traditionally used to serve California end users. El Paso seeks clarification that, in light of the “California-centric” nature of the Block Capacity, any rate cap for the Block Capacity should be based on the California rate level contractually identified with its use. El Paso contends that applying a lower EOC rate cap would be particularly “draconian” since El Paso did not agree to bear the risk that it would be unable to charge up to the California rate cap for the capacity. El Paso contends that it would be highly inequitable, and unjust and unreasonable, to give the former FR shippers the benefit of a rate cap lower than the California rate cap in light of the subsidized capacity that the FR shippers received during the last two years of the 1996 Settlement.

2. Commission Determination

62. The Commission clarifies that El Paso may not apply the California rate cap to the portions of the Block Capacity that do not have California delivery points. The fact that at one time, the former Block Capacity⁶⁰ was under contract to California shippers, has no relevance to the rate that should be charged to other shippers using portions of that capacity. There is no such thing as “California capacity” or “California-centric” capacity.⁶¹ As the Commission explained in the Capacity Allocation Proceeding, when a contract for firm service expires and the shipper does not exercise a right of first refusal, that capacity is available to other shippers. The rate for this capacity will be the rate applicable to the new shipper’s receipt points, not the rate that the former shipper paid. Thus, there is no basis for suggesting that shippers East of California should pay a rate for capacity that they do not use beyond their receipt point. The equities here do not justify a different result, and even if they did, the Commission could not require a shipper

⁵⁹ El Paso notes, however, that even though it is proposing to apply the California rate cap to the Block Capacity, for shippers that redesignated their primary delivery point from California to an EOC point prior to the end of the test period in this case on December 31, 2005, El Paso is not proposing to actually charge anything more for this capacity than the maximum rate authorized by the Commission from time to time in whatever rate zone the former FR shippers hold the capacity on a primary delivery point basis.

⁶⁰ As stated above, the restrictions on this capacity expired at the end of the term of the 1996 Settlement, and therefore this capacity is identical to all the other capacity on the system and there is no longer any Block Capacity on the system.

⁶¹ See July 9 Order, 104 FERC ¶ 61,045 at P 141 (stating that there is no such thing as a “certificated obligation to serve California”).

to pay a rate higher than the applicable rate to offset other alleged benefits the shipper received.

G. Applicability of Article 11.2 to Expansion Capacity

1. Background

63. Section 3.6 of the 1990 Settlement provides that:

El Paso shall not be required to construct any facilities that are not economically justifiable. The provisions of this section 3.6 shall survive the term of this Stipulation and Agreement.⁶²

64. In the Capacity Allocation Proceeding, the Commission interpreted “economically justifiable” to mean that either the new capacity would bring increased revenues to El Paso or that the FR shippers would share the expense of the expansion with El Paso.⁶³ The Commission therefore concluded that El Paso does not have an unqualified obligation, under the 1990 Settlement, the 1996 Settlement, or the NGA, to construct capacity at its own expense to serve the growing needs of the FR shippers.⁶⁴

65. However, during the Capacity Allocation Proceeding, El Paso voluntarily agreed to undertake two expansion projects, the Line 2000 and Power Up Projects,⁶⁵ to help ensure reliable firm service and to facilitate the conversion of FR contracts to CD contracts. Thus, the Commission allocated the capacity related to these two expansion projects to the former FR shippers as part of their new CD levels and El Paso agreed to forgo additional revenues from these projects until its next rate case, i.e. the 2006 Rate Case.

2. March 20 Order

66. In the March 20 Order, the Commission found that the Article 11.2(a) rate cap does not apply to the expansion capacity related to the Line 2000 or the Power Up Projects. The Commission stated that to conclude otherwise would ignore the express language of the 1990 and 1996 Settlements, as well as the Commission’s orders in the

⁶² Section 3.6 of the 1990 Settlement.

⁶³ *See* July 9 Order, 104 FERC ¶ 61,045 at PP 102-103.

⁶⁴ *See id.*

⁶⁵ *See* May 31 Order, 99 FERC at 62,109, 62,011-12.

Capacity Allocation Proceeding and the Power Up Project certificate proceeding.⁶⁶ The Commission reaffirmed its position that the 1990 and 1996 Settlements did not obligate El Paso to build capacity at its own expense to meet the growth in the demands of the FR shippers. The Commission further stated that nothing in the Capacity Allocation Proceeding suggests that El Paso should be unable to recover in its 2006 Rate Case the costs of the expansion projects it voluntarily constructed. The Commission further explained that pursuant to its order in the Power-Up Project certificate proceeding, the costs of the expansion facilities should be allocated to all of El Paso's customers, not just to the East of California customers. With regard to the Line 2000 Project, the Commission stated that the specific method of including the costs in the rates could be addressed at the hearing, but made clear that Article 11.2(a) does not preclude El Paso from including the costs of these expansions in all shippers' rates in this proceeding.

3. Interpretation of the Settlement Agreements

a. Requests for Rehearing

67. AEP, Arizona Electrics, El Paso Electric, Phelps Dodge, Municipal Customers, Southwest Gas, and Texas Gas Service argue that the Commission erroneously relied on the language of the 1990 Settlement to reach the conclusion in the March 20 Order that the rate cap does not apply to service provided with the expansion capacity. These parties argue that this finding is contrary to the plain meaning of Articles 11.2(a) and (b). The parties state that while Article 11.2(b) applies to capacity in existence on December 31, 1995, Article 11.2(a) contains no such limitation, and that the absence of this limitation in Article 11.2(a) reflects the intent of the parties to apply the rate cap to all capacity used to provide services under eligible TSAs, regardless of the date of the construction of the capacity. They assert that the Commission ignored the significant differences in the language of the two subsections and instead erroneously relied on the language of the 1990 Settlement in reaching its decision.

68. Arizona Electrics argue that in interpreting the settlement agreements, the Commission violated several canons of contract construction. Specifically, Arizona Electrics argue that the intent of the parties should be determined from the plain meaning of the language within the four corners of the contract.⁶⁷ Further, they argue, even if it was necessary to consider the 1990 Settlement in interpreting the 1996 Settlement, the

⁶⁶ *El Paso Natural Gas Co.*, 103 FERC ¶ 61,280 (2003); *El Paso Natural Gas Co.*, 105 FERC ¶ 61,202 (2003).

⁶⁷ Arizona Electrics cite *Consolidated Gas Transmission Corp. v. FERC*, 771 F.2d 1536, 1545 (D.C. Cir. 1985) (stating that “[i]n construing tariffs, courts and agencies must look to the four corners of the tariff”).

intent of the parties should be determined in a manner that gives effect to all provisions of contracts between the parties.⁶⁸ Finally, Arizona Electric argue the canons of construction provide that if there is a conflict regarding the meaning of provisions in two successive contracts, the language of the subsequent agreement should control over any conflicting language in a prior agreement.⁶⁹

69. Southwest Gas states that simply because El Paso was not obligated to construct the Line 2000 and Power Up Projects does not mean that the rate cap should not apply to a voluntary expansion. Similarly, Municipal Customers state that though El Paso may not have been required to construct facilities, this does not dictate how costs will be recovered if the facilities are built. AEP states that even if El Paso was not required to expand its system at its own expense, it was free to demand payment from its shippers for any voluntary expansion before it undertook the expansion, but did not do so.

70. In addition, these parties argue that the two expansion projects were intended to serve existing customers' needs under their pre-1995 contracts, rather than to provide additional services, and therefore, the rate cap must apply to services provided with the expansion capacity. Texas Gas Service asserts that the Commission ignored its evidence that El Paso identified the expansion capacity as capacity available to be allocated to the former FR shippers so that El Paso would not be found to have inadequate capacity to meet the needs of those shippers.⁷⁰ Similarly, Phelps Dodge, Municipal Customers, and

⁶⁸ Arizona Electric cite *Consolidated Gas Transmission Corp. v. FERC*, 771 F.2d 1536, 1544-47 (D.C. Cir. 1985).

⁶⁹ Arizona Electric cite *Consolidated Gas Supply Corp. v. FERC*, 745 F.2d 281, 291 (4th Cir. 1984) (stating that when two FERC-approved settlements are placed side-by-side, "the reservation in one and the lack of reservation in the other spring forth and compel . . . [a conclusion that the parties intended not to reserve an issue in the second settlement]").

⁷⁰ Texas Gas Service states that it submitted documents containing El Paso's own statements in the certificate applications that the expansions were necessary to meet its service obligations. Further, Texas Gas Service states that it submitted evidence to demonstrate that El Paso volunteered to construct the expansion capacity in order to meet its obligations under existing TSAs. Further, Texas Gas Service argues, in the expansion capacity proceeding, the Commission was explicit that the expansion capacity would not provide any new or additional service, but would provide existing flexibility for El Paso to meet its existing firm contractual obligations. The Commission stated that the Power Up Project facilities "contribute to the solution of a dysfunctional system that lack sufficient capacity to prevent *pro rata* cuts to all shippers' firm service." 103 FERC ¶ 61,280 at P 14. Texas Gas Service argues that because this capacity was necessary to

(continued)

Southwest Gas argue that the Line 2000 Project was not intended to create incremental capacity, but was necessary for El Paso to meet its existing obligations to its customers and therefore, contracts for this capacity cannot be viewed as expansion capacity contracts, but should be treated as any other preexisting contracts subject to the Article 11.2(a) rate cap.⁷¹

71. El Paso Electric argues that if it had remained an FR shipper, El Paso would have been obligated to provide it with FR service, and the nature of the facilities used to provide that service was immaterial because El Paso's core obligation was to provide FR service as needed on a daily basis. Further, El Paso Electric states that the FR shippers did not ask for conversion of their contracts, and did not request any particular vintage of capacity to be allocated to them.

b. Commission Determination

72. The March 20 Order properly found that the rate cap does not apply to the expansion capacity added by the Line 2000 and Power Up Projects. In reaching this conclusion, the Commission correctly interpreted the relevant provisions of the 1990 and 1996 Settlements. As the Commission explained in the March 20 Order, in interpreting a settlement, it considers the language of the document itself, its purpose, and the circumstances of its execution and performance.⁷² The Commission therefore looks to the language of the agreement and its regulatory context.⁷³ The Commission applied these principals here and determined that with regard to the expansions at issue, the rate cap should not apply to services provided with this new capacity.

73. The parties seeking rehearing would have the Commission ignore the language of the 1990 Settlement and the totality of the agreements among the parties, as well as the regulatory context of the expansions. Section 3.6 of the 1990 Settlement states that El Paso is not obligated to build additional capacity that is not economically justifiable. The parties argue that the Commission erroneously relied on this language in reaching its conclusion in the March 20 Order. However, section 3.6 also specifically provides that the provision will survive the term of the 1990 Settlement. Since neither the 1996

meet El Paso's obligations under its pre-existing contractual obligations under the TSAs, it should be deemed within the scope of the Article 11.2 rate cap protections.

⁷¹ Phelps Dodge cites *El Paso Natural Gas Co.*, 95 FERC ¶ 61,176, at P 9 (2001).

⁷² March 20 Order, 114 FERC ¶ 61,290 at P 74.

⁷³ *Id.*

Settlement, nor any other settlement, has modified section 3.6, the provision, by its terms, continues in effect and is relevant here.

74. In the Capacity Allocation Proceeding,⁷⁴ the Commission interpreted the “economically justifiable” language in section 3.6 to mean either that the new capacity would bring El Paso increased revenues, or that the shippers would share the expense of construction with El Paso.⁷⁵ Since it was not “economically justifiable” for El Paso to expand its system at its own expense to meet the growing needs of the FR shippers, the Commission concluded that El Paso had no obligation to do so. Because El Paso was not obligated to fund new capacity to meet the growing FR demands, the growth that could occur under those FR contracts was limited to the capacity of the system at the time the contracts were executed. In other words, it was not part of El Paso’s service obligation, or part of the FR shippers’ rights under the 1995 contracts, to receive service for their increased demands with expansion capacity at no additional cost.

75. The regulatory context of these expansions is also significant. At the time El Paso proposed these expansion projects, the Commission in the Capacity Allocation Proceeding was addressing the service reliability problems on El Paso that had been caused by the growth in demands under the FR contracts.⁷⁶ The Commission encouraged the parties to resolve these issues by settlement and held a number of technical conferences and a public conference to facilitate this process. At the public conference held on April 16, 2002, El Paso stated that to encourage settlement, it would add the expansion capacity and forgo cost recovery until the next rate case.⁷⁷ While the Commission does not have the authority to order a pipeline to expand its system,⁷⁸ the Commission stated that it would hold El Paso to its agreement to provide additional capacity to assist in the process of converting FR contracts to CD contracts. In offering

⁷⁴ As stated above, that proceeding is final and has been upheld by the court, and these issues are not subject to review in this proceeding.

⁷⁵ July 9 Order, 104 FERC ¶ 61,045 at P 102-04.

⁷⁶ In the Capacity Allocation Proceeding, the Commission stated that while the growth in FR demand may not have been the only cause of the service degradation on El Paso, it was the most significant part of the problem. May 31 Order, 99 FERC at 62,003.

⁷⁷ See transcript of the April 16, 2002 Public Conference at 14.

⁷⁸ As the Commission stated in the July 9 Order, 104 FERC ¶ 61,045 at P 103 n.104, the Commission does not have the authority under the NGA to order a pipeline to construct additional capacity (citing *Panhandle Eastern Pipeline Co. v. FPC*, 204 F.2d 675, 680 (3rd Cir. 1953)).

to build this expansion capacity and forgo revenues until its next rate case, El Paso was compromising in an effort to reach a settlement. This, however, does not mean that the former FR shippers were entitled to the capacity at capped rates.

76. In the Capacity Allocation Proceeding, the Commission exercised its broad remedial authority⁷⁹ and balanced the interests of the parties with the public interest in devising a solution to the complex problems on the El Paso system. In this context, the Commission took a number of actions to address the concerns raised by the former FR shippers over the amount of capacity they would receive and whether they would have sufficient capacity to meet their needs during the transition from FR to CD service.⁸⁰ As part of this remedial action, which, as noted above, was upheld by the court, the Commission adopted a capacity allocation methodology that provided the additional expansion capacity to the FR shippers at no additional charge, consistent with El Paso's proposal, for the remainder of the 1996 Settlement period. This action was part of the Commission's remedy, and it was not based on a finding that El Paso was required to build additional capacity at its own expense to meet the growth in FR demand or that the former FR shippers' contracts entitled them to expansion capacity at a capped rate indefinitely into the future. In fashioning its remedy, the Commission did not provide the FR shippers with any additional rights beyond what they were entitled to in the 1996 Settlement.

77. It is true, as Texas Gas Service, Phelps Dodge, and Southwest Gas point out, that the Commission found that due to the increase in the demands on the system of the FR customers, the additional expansion capacity was needed to serve El Paso's existing customers. It does not follow, however, that the former FR customers should receive a rate preference in the form of the rate cap after the end of the 1996 Settlement period. As we have explained above, it was not part of El Paso's service obligation to build additional capacity to serve the growth in FR demand without cost recovery. El Paso's agreement to build the additional facilities and forgo cost recovery through the end of the 1996 Settlement period in an effort to resolve the capacity allocation issues by settlement did not create a right in the former FR customers to this capacity after the end of the 1996 Settlement period at the capped rate. Without the agreement of El Paso to build the capacity and the remedy adopted by the Commission, the FR shippers' new CDs would have been limited to the 1995 system capacity. The inclusion of this additional capacity

⁷⁹ As the court stated in affirming the Commission's decision in *Arizona Corporation Commission v. FERC*, 397 F.3d 952 at 956 (D.C. Cir. 2005), the Commission wields maximum discretion in selecting a remedy.

⁸⁰ At that time, the FR shippers asserted that they would not have sufficient capacity to meet the needs of their customers if their contracts were changed to CD contracts, and the Commission took action to address their concerns.

in their CDs was outside of, and not required by, the 1996 Settlement and does not give the former FR shippers a rate preference for this capacity in the future.

78. The additional arguments of the parties do not change this conclusion. Arizona Electrics argue it is clear that the parties to the 1996 Settlement contemplated that new construction would be covered by the rate cap because the parties agreed to adjust the entire rate cap, including depreciation and return on investment, by an inflation factor, allowing for an increase in rate base (and corresponding increase to the return) based on inflation. Arizona Electrics assert that if the parties had intended to exclude new construction from application of the rate cap, it would have made no sense to allow all elements of the rate cap (including return on rate base) to increase for inflation.

79. Arizona Electrics' assertion that the parties agreed to adjust the entire rate cap for inflation is incorrect. Article 11.2(a) provides that the 1996 Settlement rates will be adjusted annually after the term of the 1996 Settlement through the remainder of the term of the TSA using the procedure set forth in Article 3.2(b). Article 3.2(b) states that El Paso will be permitted to increase the base 1996 Settlement rates by applying an annual inflation adjustment as provided in the tariff sheets attached to the 1996 Settlement. These tariff sheets provide in section 25.2 of the General Terms and Conditions, Annual Inflation Adjustment, for an increase in the Operations and Maintenance (O&M) and Other Taxes Portion of the base reservation and usage charge based on the increase in the Implicit Price Deflator to the Gross Domestic Product, provided that the annual increase in total Base Rates will not be less than 1 percent or more than 4.5 percent of the prior year's total base rates. Section 25.2 further states that the O&M and Other Taxes Portion of the base rates was equal to 53.7 percent of the base rates as of January 1, 1996. Return on equity and depreciation are not included in O&M and Other Taxes Portion, and thus the 1996 Settlement did not provide for an inflation adjustment to either of these components of the cost of service. Accordingly, there is nothing in the inflation adjustment provisions of the 1996 Settlement that leads to the conclusion that the parties intended to apply the rate cap to major expansion projects added to the system under the circumstances of the Capacity Allocation Proceeding. Thus, the Commission affirms its decision in the March 20 Order that the rate cap does not apply to expansion capacity and denies shippers' requests for rehearing on this issue.

4. Discriminatory Effect

a. Requests for Rehearing

80. Arizona Electrics, Southwest Gas, and Phelps Dodge argue that the March 20 Order fails to address their concerns that not applying the rate cap to expansion capacity results in discrimination against the EOC shippers. They state that because newly constructed capacity was not directly allocated to CD customers, the California shippers (who were largely CD customers) will have rate cap protection for 100 percent of their CDs, while the EOC shippers (who were largely FR customers) are denied rate cap

protection on approximately 60 percent of their contract demands. They argue that this result is arbitrary and capricious and results in unduly discriminatory rates. These parties assert that any exclusion of the expansion capacity from rate cap protection should apply to all eligible CD shippers, not just the former FR shippers, because the expansion capacity was constructed as system capacity to meet system needs, and because the converted CD levels of the former FR shippers under eligible TSAs represent 1995 service rights.

81. Phelps Dodge argues the Commission's conclusion that the Line 2000 Project benefits all shippers is inconsistent with the finding that the Line 2000 Project capacity should be apportioned only to the former FR shippers. Southwest Gas states that as a result of the orders in the Capacity Allocation Proceeding, all firm shippers now have contract demands that should be treated equally if the Commission determines that it would be inequitable to enforce the rate cap in a way that would prevent El Paso from recovering the expansion facilities' construction costs. Arizona Electric's assert the Commission's statement in the March 20 Order that the rates for the new facilities will be rolled-in and allocated to all of El Paso's customers, does not address this issue adequately.

82. Southwest Gas asserts that the allocation of the capacity related to the Line 2000 and Power Up Projects to FR customers as part of the mandatory conversion and allocation of capacity in the Capacity Allocation Proceeding was merely an allocation fiction designed to mathematically assign all system capacity to firm shippers. Southwest Gas acknowledges that under the allocation formula, the Commission mathematically assigned capacity to the CD shippers first, and then assigned the remaining capacity, plus the expansion capacity, to the FR shippers. However, Southwest Gas asserts that this mathematical assignment does not alter the reality that all system capacity, including the expansion capacity, was allocated among all classes of firm shippers, so that El Paso's firm service obligations could be met on a reliable basis.

83. Southwest Gas also states that the Commission's holding is not reasonable in light of the fact that the Line 2000 and the Power Up Project expansions were constructed in part to increase and/or retain physical certificated pipeline facilities with delivery capability to California. In support of its position, Southwest Gas states that El Paso and the California shippers entered into a settlement in *California PUC v. El Paso Natural Gas* (the California Complaint case), wherein El Paso received economic incentives to construct the Line 2000 and Power Up Project expansion facilities, and that the California

shippers effectively waived any rate cap protection applicable to this expansion capacity.⁸¹

b. Commission Determination

84. The Commission's decision that shippers using expansion capacity are not entitled to the rate cap does not result in any undue discrimination. Despite the shippers' contentions, the Commission's decision in the March 20 Order treats FR shippers and CD shippers similarly. After the Capacity Allocation Proceeding, if historical CD shippers needed capacity above the level of their 1995 TSAs, they had to enter into new contracts for additional capacity and pay the uncapped rate for that capacity. Thus, it was just and reasonable for the Commission to find in the March 20 Order that the former FR shippers must also pay the uncapped rate for capacity they want above the level El Paso was required to provide them in their 1995 TSAs. Under the former FR shippers' 1995 TSAs, El Paso was required to serve their needs, including their growth in demand, with the capacity that was a part of the system at that time. Since the expansion capacity at issue here was not a part of El Paso's system when the former FR shippers entered into their 1995 TSAs, El Paso is not obligated to serve the former FR shippers with the expansion capacity at capped rates. The former FR shippers must pay the full rate for this capacity, just as historical CD shippers do for capacity above the level of their 1995 TSAs.

85. The shippers argue that the Commission has been inconsistent in stating that the expansion capacity was specifically allocated to the former FR shippers, while also asserting that the expansion capacity benefits all shippers. The shippers contend that if the expansion capacity benefits all shippers, then any reduction in rate cap protection attributable to the expansion capacity should be spread *pro rata* amongst all firm customers.

86. The Commission's prior statements on this issue are consistent and do not undermine its decision that the rate cap does not apply to the expansion capacity. The creation of the expansion capacity benefitted all shippers by providing additional capacity for the growth in FR demands, which relieved the capacity constraints that were resulting in *pro rata* cuts to firm shippers' nominations, particularly those of CD shippers, rendering them unable to use all of the capacity for which they were paying. However, despite the fact that the expansion projects benefitted all shippers, these projects still only directly provided new capacity for the FR shippers. During this time the CD shippers did not need new capacity because they were consistently taking gas within the limits of their

⁸¹ Southwest cites *California PUC v. El Paso Natural Gas Co.*, 105 FERC ¶ 61,201, at PP 27, 147, 149, 154 (2003), *reh'g denied*, 106 FERC ¶ 61,315 (2004), *petition dismissed, Arizona Corp., Comm'n v. FERC*, 2005 WL 3783024 (D.C. Cir. 2005).

1995 TSAs. Since the FR shippers were not in the same situation and needed expansion capacity that was outside their 1995 TSAs, it is reasonable to require them to pay the uncapped rates for service with this capacity.

87. Southwest Gas suggests the allocation methodology employed by the Commission in the Capacity Allocation Proceeding, including its allocation of the expansion capacity to the FR shippers, was a fiction and should not be used as a basis for declining to apply the rate cap to expansion capacity. We disagree. In the Capacity Allocation Proceeding, the Commission allocated capacity to the CD shippers first because their needs had remained largely unchanged during the course of the 1996 Settlement. The Commission took this approach because it could not determine the amount of capacity that was available for FR shippers, whose demands had changed and grown throughout the course of the 1996 Settlement, until it accounted for the needs of the CD shippers. The Commission also allocated to the FR shippers the new expansion capacity in order to serve the growth in their demands. This allocation methodology was not a fiction, but was a concrete solution to the problems on El Paso's system. Further, this allocation methodology was approved by the court and it is not subject to review or collateral attack here. To the extent the protestors are objecting to the consequences of the allocation methodology established by the Commission in the Capacity Allocation Proceeding, those objections are both untimely and outside the scope of this proceeding.

88. The Commission's decision in the March 20 Order that the rate cap does not apply to expansion capacity is a logical extension of the Capacity Allocation Proceeding's allocation of expansion capacity to FR shippers. In taking the action that it did in the Capacity Allocation Proceeding, the Commission was granting the FR shippers access to capacity that was not part of El Paso's system at the time the parties entered into the 1995 TSAs, and that El Paso could not have originally used to meet the FR shippers' growth in demand. In addition, as explained above, El Paso was not required to build this capacity to meet the FR shippers' demands, but did so voluntarily. Thus, in using the expansion capacity, the FR shippers were using capacity above the levels of the 1995 TSAs. CD shippers are required to enter into new contracts, at uncapped rates, if they want capacity above the level of their 1995 TSAs. It only follows that, in order to treat shippers in a non-discriminatory manner, the Commission must require FR shippers to pay uncapped rates for access to capacity above the level provided for in their 1995 TSAs.

89. Southwest Gas asserts that the expansion projects were constructed in part to increase and/or retain physical certificated pipeline facilities with delivery capability to California. However, the evidence does not support that the expansion facilities were constructed as part of El Paso's settlement with the California Public Utilities Commission (PUC), as Southwest Gas suggests. The applications for both of the

expansion projects were filed⁸² before the June 4, 2003 submission of El Paso's settlement in Docket No. RP00-241-000, *PUC v. El Paso Natural Gas Co.* (California Complaint Case).⁸³ The certificate authorizing El Paso to construct the Line 2000 Project was issued in May 7, 2001,⁸⁴ some two years prior to the filing of the settlement in the California Complaint Case, and the certificate for the Power Up Project was issued on June 4, 2003,⁸⁵ the same date that the settlement in the California Complaint Case was filed. The California Complaint Case settlement was therefore independent of the Commission's authorizations of the expansion projects, and is not relevant to whether the rate cap should apply to the expansion capacity. For the foregoing reasons, the Commission denies the requests for rehearing on this issue and affirms its decision that the rate cap does not apply to expansion capacity.

5. The Presumption Regarding Expansion Capacity

a. March 20 Order

90. In the March 20 Order, the Commission found that pursuant to Article 11.2(b) of the 1996 Settlement, the rates that may be charged to eligible shippers may not include 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. However, the Commission also found that Article 11.2(b) does not apply to expansion capacity added to the system after December 31, 1995, and, therefore, it may be difficult to determine whether specific unsubscribed or discounted capacity is capacity that was on El Paso's system in December 1995. The Commission stated that this could be the case particularly where the capacity has been expanded since 1995, and it is unclear whether the capacity that became unsubscribed or discounted is part of the original or the expanded capacity.

91. In the March 20 Order, the Commission adopted a presumption to assist in resolving these issues. Because the parties agreed that at the time of the 1996 Settlement, the capacity of the El Paso system was slightly more than 4000 MMcf/d, the Commission stated that in determining whether specific capacity was part of El Paso's 1995 system, it

⁸² The Line 2000 Project was filed on July 31, 2000 in Docket No. CP00-422-000, and the Power Up Project was filed on October 3, 2002 in Docket No. CP03-1-000.

⁸³ 105 FERC ¶ 61,201 (2003).

⁸⁴ *El Paso Natural Gas Co.*, 95 FERC ¶ 61,176 (2001).

⁸⁵ *El Paso Natural Gas Co.*, 103 FERC ¶ 61,280 (2003), *reh'g denied*, 105 FERC ¶ 61,202 (2003).

would presume that the first 4000 MMcf/d of firm subscribed capacity is 1995 capacity. Therefore, the Commission held, if El Paso has more than 4000 MMcf/d of firm capacity subscribed at the rate cap or above, there would be a presumption that there is no 1995 stranded or discounted capacity.

b. Requests for Rehearing

92. AEP, Arizona Electrics, El Paso Electric, Phelps Dodge, Municipal Customers, Southwest Gas, and Texas Gas Service argue that the Commission erred in adopting the presumption that the first 4000 MMcf/d of firm subscribed capacity is 1995 capacity. These parties argue that the presumption is factually inaccurate because it is known that a portion of that 1995 capacity is currently unsubscribed or discounted, including the SoCalGas capacity. AEP asserts that the capacity that has been turned back to El Paso since 1995 and either not remarketed or sold at a discount, is virtually all pre-1995 California capacity. In addition, Southwest Gas asserts that capacity under contract to California shippers has declined by approximately 609,824 Dth during the approximately 10 years between the adoption of Article 11 and the rate filing in this case.

93. The parties also argue that the presumption adopted by the Commission is illogical. Arizona Electrics and Municipal Customers argue that it does not make sense for the Commission to allocate all of the Line 2000 and Power Up Project capacity to the EOC shippers at maximum rates, and then presume that this capacity is 1995 capacity for the calculation of capacity subject to 11.2(b). Similarly, Southwest Gas asserts that the implicit assumption that unsubscribed capacity can be attributed to the most recent vintage of capacity first, i.e., the expansion capacity, does not make sense because no logical connection has been established between unsubscribed capacity and the most recent vintage of capacity.

94. Further, these parties argue that the presumption is unnecessary. El Paso Electric states that at the time of the 1996 Settlement, approximately 75-80 percent of the throughput on the system was to California delivery points and approximately 20-25 percent of the throughput was to EOC delivery points. Thus, El Paso Electric argues, if capacity is turned back to El Paso, the vintage of that capacity may be readily ascertained. El Paso Electric states that if a California shipper turns back capacity, that capacity is pre-1996 capacity subject to section 11.2(b), and the March 20 Order does not explain why the identification of the capacity would be difficult. Arizona Electrics assert that the Line 2000 and Power Up Project capacity numbers are readily available. Phelps Dodge asserts that El Paso's filings in its pathing proceeding in Docket No. RP04-251-000 demonstrate that its computers can readily be programmed to track the various vintages of capacity for contracting purposes, and there is no reason for a mathematical presumption that blurs the distinction between old and new capacity when the actual vintage can be tracked.

95. Finally, the parties argue that the presumption improperly shifts the burden of proof to the shippers, while it should be incumbent on El Paso to demonstrate that any stranded or discounted capacity is in fact post-1995 capacity.

c. Commission Determination

96. The Commission affirms its decision to adopt a presumption that the first 4000 MMcf/d of firm subscribed capacity is 1995 capacity for purposes of Article 11.2(b) of the 1996 Settlement. The 1996 Settlement was implemented at a time when El Paso was facing large quantities of turned-back capacity. The 1996 Settlement contained a set of provisions designed to address the consequences of that turned-back capacity in order to avoid an excessive rate increase for the remaining customers. El Paso and its shippers thus agreed to a comprehensive set of provisions to share the costs, risks, and ultimately any rewards associated with the turned-back capacity.⁸⁶ As part of those provisions, Article 11.2(b) provided protection for eligible shippers so that, after sharing the cost of the turned-back capacity during the 1996 Settlement, they would not be required to again pay costs associated with the original turned-back capacity after the 1996 Settlement.

97. Since the 1996 Settlement, the Commission has authorized a number of expansion projects that have added substantial amounts of mainline and lateral capacity to El Paso's system to meet the expanding needs of El Paso's shippers.⁸⁷ In authorizing these projects, the Commission found that these facilities were required by the public convenience and necessity because they either provided a system benefit or enabled a new service without adversely affecting existing shippers. These new facilities have since been incorporated into El Paso's system. El Paso operates its system on an integrated basis, and thus uses all its facilities, both old and new, to serve the demands of all its customers. However, because Article 11.2(b) only protects eligible shippers from an allocation of costs related to unsubscribed or discounted 1995 capacity, implementation of that Article requires a determination of whether any such costs should be attributable to 1995 or expansion capacity.

98. The March 20 Order's presumption that the first 4000 MMcf/d of firm subscribed capacity is 1995 capacity simplifies compliance with Article 11.2(b) while preserving the protections inherent in the Article. The first 4000 MMcf/d presumption ensures that El Paso must have subscribed capacity at maximum rates that is equivalent to the capacity

⁸⁶ As described earlier, those provisions included risk sharing, revenue sharing, capped rates during the settlement, the Article 11.2(a) post-settlement rate cap, and Article 11.2(b).

⁸⁷ *E.g.*, the Line 2000, Power Up, Line 1903, Hobbs Expansion, East Valley Lateral, and Picacho Compressor projects.

that existed on its system in 1995 before it can propose to include the cost of unsubscribed or discounted capacity in the rates of eligible shippers. Similar to our finding that there is no “California capacity” or “California-centric capacity” on El Paso’s system for purposes of applying the Article 11.2(a) cap,⁸⁸ we find no reason to track “1995 capacity” based upon whether it was turned back by California shippers. We recognize that in the Capacity Allocation Proceeding, we allocated a portion of the expansion capacity to the FR shippers. However, that was because at the time of that proceeding, there was insufficient 1995 capacity available to serve the full CDs of the FR shippers’ converted CD contracts. Thus, it was possible to determine the share of the expansion capacity that must be used to award the FR shippers the full amount of CDs given to them in that proceeding. However, when El Paso markets capacity today, it is marketing undifferentiated capacity which cannot be physically attributed to pre-1995 or post-1995 capacity. That is because it operates its system as an integrated whole and uses all its capacity to serve the demands of all its customers. In these circumstances, we believe it reasonable, for purposes of Article 11.2(b), to attribute the first 4000 MMcf/d of firm maximum rate subscribed capacity to 1995 capacity. At the time of the 1996 Settlement, El Paso only had that much capacity on its system, and therefore the parties must have anticipated that, if El Paso marketed that level of capacity at maximum rates, there would be no unsubscribed or discounted capacity left for El Paso either to absorb the costs of or reallocate to other customers. To the extent that anticipation does not hold true today, it is only because El Paso has expanded its system. The Commission finds it unreasonable to interpret Article 11.2(b) to require El Paso to absorb such costs, which only arise because of the expansions. For these reasons, we affirm the presumption that the first 4000 MMcf/d of firm subscribed capacity is 1995 capacity for purposes of Article 11.2(b).

6. Issues for Hearing

99. As stated above, the requests for rehearing in this proceeding were filed prior to the Commission’s approval of El Paso’s 1996 Settlement, when the rate issues were still set for hearing. In its request for rehearing, Phelps Dodge asks the Commission to confirm that all rate issues concerning the Line 2000 Project, including the issue of whether contracts for Line 2000 Project capacity are subject to Article 11.2(a), may be addressed at the hearing.

100. With the approval of the Rate Case Settlement, the hearing in this proceeding was terminated, so Phelps Dodge’s request for rehearing on this issue is moot. The Commission will not prejudge the scope of any hearing in any future rate case, except to clarify that parties may not litigate issues that have been resolved here. Thus, the issue of

⁸⁸ See P 62 of this order.

whether the rate cap applies to expansion capacity has been resolved here and will not be subject to further litigation in any proceeding.

H. Applicability of Article 11.2 to the New Services

1. Article 11.2(a)

101. In its June 30 tariff filing, El Paso proposed a number of new firm services that shippers can purchase in combination with their current FT-1 service to give them greater flexibility to vary their hourly takes.⁸⁹ Issues related to the new services were addressed at the technical conference. In the March 23 Order on the technical conference, the Commission found the new services to be generally just and reasonable, and accepted them subject to certain modifications.⁹⁰ The Commission rejected parties' arguments that the new services resulted in an unlawful degradation of existing services.⁹¹

a. March 20 Order

102. In the March 20 Order, the Commission found that if a shipper elects to use the new services El Paso offered in its June 30 tariff filing, the protections of Article 11.2 will not apply to these services. The Commission rejected shippers' arguments that the new services are the same as the FT-1 service they currently receive, but at an increased price. The Commission explained that the new services give shippers greater flexibility to vary their hourly takes, while service under Rate Schedule FT-1 never gave shippers the firm right to engage in non-ratable hourly swings. Thus, the Commission explained that by offering these new services, El Paso has not changed or degraded the nature of the existing FT-1 service. The Commission stated that shippers are free to keep their existing FT-1 contracts and retain the protections of the Article 11.2 rate cap. However, the Commission found that if shippers elect to sign up for the new services, the contracts for these services will not meet the conditions of Article 11.2 protection because they were not contracts in effect on December 31, 2005 that remain in effect on January 1, 2006. The Commission reasoned that the contracts for new services cannot properly be viewed as a continuation or amendment of shippers' FT-1 contracts because they are for different services not previously offered by El Paso, and therefore the rate cap will not apply.

⁸⁹ See March 23 Order, 114 FERC ¶ 61,305 at P 13-23.

⁹⁰ *Id.* P 11. The requests for rehearing of the March 23 Order were rendered moot by the Rate Case Settlement. See *El Paso Natural Gas Co.*, 121 FERC ¶ 61,266 (2007).

⁹¹ *Id.* P 25-28 (citing *Southwest Gas Corp.*, 111 FERC ¶ 61,511 at P 13, 15 (2005)).

b. Requests for Rehearing

103. The ACC, AEP, Arizona Electrics, El Paso Electric, and Southwest Gas seek rehearing of the Commission's decision that the Article 11.2 rate cap does not apply to new services. The ACC and Southwest Gas specifically object to the so-called "bundled" nature of the new services. The ACC asserts that the new services contain both storage and transmission components, and that El Paso should be required to unbundle these components and apply the rate cap to the transmission portion of the services. The ACC argues that March 20 Order failed to provide an adequate explanation for not applying the rate cap to the transmission portion of the new services, and failed to address the shippers' arguments about how bundling permits El Paso to avoid the rate cap. Southwest Gas argues that the March 20 Order pre-judges the rate issues set for hearing by approving the bundled form of the new services. Southwest Gas asks the Commission to grant rehearing and find that the issue of whether the bundling of FT-1 service with the new Firm Daily Balancing Service (FDBS) is so interrelated with the rate issues set for hearing that the parties should be able to address the issue of the new services design at the hearing.

104. The ACC, AEP, Arizona Electric, and El Paso Electric argue that by bundling its new services and by imposing new restrictions on the FT-1 service that degrade that service, El Paso has forced shippers to purchase the new services in order to retain the hourly flexibility that they previously received under the FT-1 service. These shippers argue that it is El Paso's unilateral actions that have caused shippers to terminate some or all of their FT-1 contracts in order to continue taking non-ratable hourly service under their existing sculpted contracts and that, in these circumstances, the resulting termination of the FT-1 contracts should be treated as termination by El Paso and not the shipper. They assert the Commission should hold that the Article 11.2 rate cap applies to the new services the eligible EOC shippers must purchase simply to preserve the hourly flexibility they previously enjoyed under their FT-1 contracts.

105. The parties also argue that the Commission's finding that the rate cap does not apply to new services is contrary to the plain meaning of Article 11.2. Arizona Electrics argue the parties expressed their agreement that the rate cap would apply to service under the existing FT-1 contracts, and carefully provided that termination by El Paso would not terminate the protections of Article 11.2. They argue the Commission's focus on whether the non-ratable hourly service historically provided by El Paso was firm or interruptible misses the real issue, which is that at all times prior to and after the execution of Article 11.2, El Paso was providing non-ratable service under the existing FT-1 contracts, and it was this service that the shippers intended to protect by Article 11.2.

106. El Paso Electric argues the 1996 Settlement should be interpreted according to the basic rules of contract interpretation, and therefore, the Commission must determine and give effect to the intent of the parties. El Paso Electric states that in 1996 when the contract was made, the parties anticipated that FR service would continue and that the

rate cap would apply to FR service for as long as shippers took that service. El Paso Electric asserts that hourly and daily swings were built into the FR service, and that El Paso assumed the responsibility for having the capacity, the storage, and the line pack to provide FR service as measured by the three-day average non-coincidental peak deliveries of the FR shippers. El Paso Electric states it was the Commission that terminated this service, not the shippers, and therefore the rate cap should apply to CD service under any rate schedule up to the limit of the three-day average non-coincident peak cost allocators filed by El Paso on June 30, 1995 in Docket No. RP95-363-000. El Paso Electric states that this CD service is the operational equivalent of FR service at the time of the 1996 Settlement, and it is immaterial whether the service is provided under Rate Schedule FT-1 or FT-H, or any other firm rate schedule, as long as the shipper continues to take firm service.

107. El Paso Electric further argues that a contract should not be interpreted literally if doing so would produce an absurd result, in the sense of results that the parties, presumed to be rational persons pursuing rational ends, are unlikely to have agreed to seek.⁹² El Paso Electric states that here, the sensible way to give effect to the intent of the parties is to provide Article 11.2 rate cap protection to the level of service purchased in 1996, regardless of the rate schedule.

108. The ACC contends that in deciding El Paso has not changed the nature of FT-1 service, the Commission failed to distinguish its decision from *Portland Natural Gas Transmission System (Portland)*.⁹³ In *Portland*, the Commission rejected the pipeline's proposal to place new limitations on the rights of customers to exceed uniform hourly flows. The ACC states that in *Portland* the Commission explained the proposed limitations were not supported by the factual record, and noted that the pipeline routinely used line pack to deliver gas in excess of uniform hourly rates. The ACC argues that here the shippers similarly argued that El Paso had routinely provided for non-ratable takes, but the Commission did not explain the difference between the instant proceeding and *Portland*.

c. Commission Determination

109. The Commission affirms its findings that Article 11.2 does not apply to new services and that the so-called "bundled" nature of El Paso's new services is just and reasonable. As the Commission has explained in prior orders in this proceeding, El Paso does not have stand-alone storage in its market area and uses system assets, system

⁹² El Paso Electric cites *Beanstalk Group, Inc. v. AM General Corporation*, 283 F.3d 856, 860 (7th Cir. 2002).

⁹³ 106 FERC ¶ 61,289, at P 54 (2004).

management, and line pack to provide the “horizontal” storage component of the new firm services.⁹⁴ This type of horizontal storage is not a stand-alone service and the Commission has not required pipelines to “unbundle” this type of system management because doing so would not be practical. System management and line pack simply cannot practically be sold separately, and the ACC does not cite to any precedent where the Commission has ordered such action. In light of the fact that there are practical and logical reasons for El Paso to bundle its new services, the Commission rejects the shippers’ argument that El Paso did so as a means to avoid the Article 11.2 rate cap.

110. Southwest Gas argues that the unbundling issue is better addressed at hearing. However, as noted above, since the parties filed their requests for rehearing, the Commission has approved the Rate Case Settlement in this proceeding and terminated the hearing. Therefore, Southwest Gas’s argument on this issue is moot.

111. The Commission also rejects the shippers’ argument that not applying the rate cap to the new services is contrary to the plain meaning of Article 11.2. The plain language of that provision states that the rate cap will apply to TSAs in effect on December 31, 1995, which were for service under Rate Schedule FT-1. While the shippers may argue that certain of the new services replace FT-1 service, the new services contracts are not FT-1 contracts, and thus, are not subject to the rate cap.

112. Many of the shippers’ arguments are essentially that they cannot use El Paso’s system as they used it before. This argument is basically the same argument previously discussed and rejected by the Commission in the Capacity Allocation Proceeding that El Paso has degraded its FT-1 service by proposing these new services. As the Commission has explained, the FT-1 service does not give shippers any right to non-uniform hourly takes.⁹⁵ So not permitting shippers to have hourly swings without signing up for the new services to obtain this flexibility is not a degradation of service or a trap to force shippers to forgo their Article 11.2 rate cap protection. Additionally, the issue of service degradation is not before us here. The March 23 Order on the technical conference resolved the degradation issue and, as explained above, the Rate Case Settlement rendered the rehearing of that order moot.⁹⁶ The issue before us here on rehearing of the March 20 Order concerning the interpretation of Article 11.2 is whether to apply the rate cap to the new services, not whether the Commission erred in accepting the new services. Thus, shippers’ arguments regarding their dissatisfaction with the new services are not probative here.

⁹⁴ See March 23 Order, 114 FERC ¶ 61,305 at P 17-19.

⁹⁵ *Id.* at 43-44.

⁹⁶ See n.93 of this order.

113. The ACC argues that the Commission failed to distinguish the situation here from the *Portland* case. In *Portland*, the Commission accepted the pipeline's proposal to implement hourly service, but rejected a proposed amendment to limit shippers' rights to non-uniform hourly flows under Portland's tariff. However, unlike El Paso's tariff, Portland's tariff provided that the deviations from uniform hourly flows were permitted "if mutually agreeable." The Commission found that the elimination of the "mutually agreeable" option degraded current service and therefore rejected the proposed tariff change. In contrast, El Paso's tariff never contained this option.⁹⁷ Further, the Commission noted in *Portland* that there was a large volume of unsubscribed capacity on the system,⁹⁸ while here, the Commission has found that restrictions on hourly flow variations are operationally justified.⁹⁹ Thus, the circumstances in the *Portland* decision are not analogous to those here.

114. The shippers' real complaint here is that they are no longer able to use the El Paso system in the same manner as they did when they were FR shippers. This result, however, is not due to El Paso changing the nature of its FT-1 service, but is the result of the Commission's finding in the Capacity Allocation Proceeding that the continuation of FR service on El Paso was no longer just and reasonable or in the public interest and ordering the conversion of FR service to CD service. The Commission's course of action in the Capacity Allocation Proceeding has been affirmed by the court and is not subject to collateral attack. Therefore, the Commission denies the shippers' requests for rehearing on this issue.

2. Article 11.2(b)

a. March 20 Order

115. In the March 20 Order, the Commission held that Article 11.2(b) is not limited to TSAs that were in effect on December 31, 1995, but applies to rates for all firm forward-haul services provided to eligible shippers. Therefore, the Commission stated that Article 11.2(b) protects eligible shippers from the inclusion in their rates of costs related to 1995 capacity that is unsubscribed or sold at less than the maximum applicable tariff rates for any forward haul service, including the new services.

⁹⁷ Section 20.8 of El Paso's tariff provided that Shipper shall "endeavor to deliver and receive natural gas in uniform hourly quantities during any gas day with operating variations kept to the minimum feasible." The revised version eliminates the words "endeavor to" and added "except when specific hourly services are being provided."

⁹⁸ *Portland*, 106 FERC ¶ 61,289 at P 56.

⁹⁹ March 23 Order, 114 FERC ¶ 61,303 at P 38-44.

116. The Commission also addressed the related issue of El Paso's remarketing of turned-back capacity. Several parties suggested that under Article 11.2(b), El Paso should bear the cost of any unsubscribed or stranded capacity utilized to provide the new services. The Commission rejected this argument and stated that Article 11.2(b) does not prohibit El Paso from reselling that capacity packaged as new services and charging all shippers a reasonable rate for the new services. The Commission stated that capacity is not stranded if it is being used, and all shippers are required to pay reasonable rates for the capacity they purchase from El Paso.

b. Requests for Rehearing

117. On rehearing, the ACC argues that the Commission failed to provide an adequate explanation for not applying the rate cap to new services using the stranded capacity that was part of El Paso's system on December 31, 1995. The ACC states that the Commission failed to explain why Article 11.2(b) does not apply to eligible shippers who require hourly services using turned-back capacity. The ACC contends the argument made by FR shippers is not based on whether turned-back capacity may now be used to provide hourly services, but is based on whether El Paso may seek cost recovery from eligible shippers for capacity that was in existence on December 31, 1995. The ACC states if the turned-back capacity was part of El Paso's system on December 31, 1995, Article 11.2(b) is applicable, and it is irrelevant that El Paso created a new market for the capacity by repackaging it as part of hourly services. The ACC notes that the FR shippers argued that El Paso has structured its new services to shift the costs of turned-back capacity to customers covered by the protections of Article 11.2(b).

c. Commission Determination

118. The ACC's argument confuses Articles 11.2(a) and (b). The rate cap is set forth in Article 11.2(a) of the Settlement and, as discussed above, applies only for service provided under TSAs in effect on December 31, 1995. Article 11.2(b) prohibits El Paso from designing rates for eligible shippers that include costs related to any capacity that was part of El Paso's system in 1995 and which is currently unsubscribed or sold at less than the maximum applicable tariff rates. In the March 20 Order, the Commission held that Article 11.2(b) prohibits El Paso from including the above-described costs in the firm rates of an eligible shipper for "any forward haul services, including the new services proposed by El Paso in this rate case."¹⁰⁰ Thus, the Commission has held that Article 11.2(b) does apply to the rates eligible shippers pay for new services. However, Article 11.2(b) is separate from the rate cap established by 11.2(a) and provides no basis for imposing the Article 11.2(a) rate cap on the rates paid by eligible shippers for new services. Therefore, the Commission denies ACC's request for rehearing.

¹⁰⁰ March 20 Order, 114 FERC ¶ 61,290 at P 58.

I. Discount Adjustment**1. Request for Rehearing & Clarification**

119. Southwest Gas argues that the Commission failed to address the argument that any discount adjustment in connection with Article 11(a) rate caps is subject to the “eligible shipper” protection of Article 11.2(b). Southwest Gas states that the March 20 Order’s finding that “the Settlement does not preclude El Paso from proposing rates that recover its cost of service”¹⁰¹ creates an ambiguity as to El Paso’s ability to propose rates that reallocate costs not recoverable from rate cap protected TSAs. Southwest Gas asks the Commission to clarify that its cost recovery finding does not permit El Paso to propose a discount adjustment that would allow El Paso to recover capacity costs covered by Article 11.2(b) from any “eligible shippers” entitled to Article 11.2(b) rate protection.

2. Commission Determination

120. The Commission grants Southwest Gas’s request for clarification. Any discount adjustment that El Paso could propose to recover the capacity costs covered by Article 11.2(b) may only involve “other shippers” that were “non-parties to the Settlement,” and not the eligible shippers entitled to protection under Article 11.2(b).

IV. Requests for Rehearing and Clarification of the June 30 Order

121. On April 4, 2006, El Paso submitted revised tariff sheets to comply with the Commission’s directives in the March 20 Order (April 4 Filing). In the June 30 Order, the Commission found that El Paso’s April 4 Filing generally complied with the March 20 Order, with a few exceptions.

A. Reservation Charge Adjustment

122. In the June 30 Order, the Commission rejected El Paso’s proposed reservation charge adjustment to the Article 11.2(a) rates. El Paso argued that, because it proposed in its rate case a usage rate decrease in general, and a reservation rate increase in general, a 100 percent load factor rate should be used for comparison instead of rate components. El Paso proposed to charge all customers (11.2(a) and non-11.2(a)) the filed usage rates. El Paso therefore calculated the difference between the filed usage rates and the 1996 Settlement weighted average usage rates, and added the resulting variance to the Article 11.2(a) reservation charge.

¹⁰¹ *Id.* P 92.

123. The June 30 Order found that the reservation charge adjustment exceeded the scope of a compliance filing because it proposed a rate change not directed by the March 20 Order. The Commission explained that in the March 20 Order, the Commission required El Paso to apply the Article 11.2 rate cap to the 1996 Settlement rates for eligible shippers, and this required El Paso to apply the rate cap to basin-specific rates that were in effect pursuant to the 1996 Settlement. The Commission stated that there was no reason to shift charges between the reservation and the usage rate as a result of the March 20 Order. The Commission further stated that the March 20 Order rejected system-wide usage rates for eligible shippers' contracts relating to service in effect as defined in the March 20 Order subject to Article 11.2.

124. El Paso argues that the Commission erred by finding that El Paso's reservation charge adjustment was beyond the scope of the March 20 Order. El Paso argues that in its initial rate filing in this proceeding, it proposed to treat the Article 11.2(a) rates as a single 100 percent load factor rate, and adjust the reservation charge in recognition of the lower usage charges filed in this case. El Paso contends that in the March 20 Order, the Commission did not address this or other adjustments to the Article 11.2(a). El Paso further asserts that the March 20 Order did not reject system-wide usage rates for Article 11.2(a) contracts, as stated in the June 30 Order. El Paso argues that the most reasonable interpretation of the March 20 Order is that the Commission accepted El Paso's proposed adjustments to the Article 11.2(a) rates, including the reservation charge adjustment, subject to further review at the hearing. El Paso therefore contends that the Commission's conclusion that the adjustment went beyond the scope of the March 20 Order is in error and requests clarification that the reservation charge adjustment will be reviewed at the hearing in this matter.

125. El Paso's request for rehearing and clarification on this issue was rendered moot by the Rate Case Settlement, which established settlement rates to remain in effect on El Paso for a three-year period ending December 31, 2008. Since the rate issues have been resolved by Rate Case Settlement, the issue of the reservation charge adjustment is moot and does not need to be addressed here. Any questions regarding the appropriateness of a reservation charge credit going forward (i.e. after the expiration of the Rate Case Settlement period) will be addressed in El Paso's most recent rate case filed on June 30, 2008 in Docket No. RP08-426-000.

B. New Section 37

126. In the June 30 Order the Commission also rejected the new section 37 that El Paso proposed. The new section 37 specified certain rights and obligations for Article 11.2 service and incorporated the inflation adjustment mechanism from the 1996 Settlement. The Commission found that while it was appropriate for El Paso to reinsert Article 11.2 provisions in its tariff, El Paso could not incorporate changes not directed by the March 20 Order. The Commission therefore directed El Paso to remove from section 37 any language that was not already found in another part of El Paso's tariff or in the 1996

Settlement. On rehearing, El Paso contends the Commission erred by rejecting the new section 37 because it eliminated uncertainty related to the implementation of the March 20 Order's directives.

127. El Paso's request for rehearing regarding the new section 37 was rendered moot by the Commission's acceptance of these provisions in a subsequent proceeding. After the Commission's finding in the June 30 Order, El Paso made a filing with the Commission under section 4 of the NGA in Docket No. RP06-442-000 to add the new section 37 to its tariff. The Commission accepted these tariff revisions in an August 18, 2006 letter order.¹⁰² Consequently, El Paso's request for rehearing on this issue is moot.

V. Compliance Filing

128. On July 10, 2006, El Paso filed revised tariff sheets in compliance with the June 30 Order (July 10 Filing). As discussed below, the Commission accepts El Paso's compliance filing subject to conditions.

A. The Filing

129. In its July 10 Filing, El Paso revised its rates to remove the reservation charge adjustment that the Commission rejected in the June 30 Order. El Paso also modified the Article 11.2 rate provision to state basin-specific usage rates for eligible shippers' contracts subject to the 1996 Settlement. El Paso states that the proposed basin-specific usage rates are to be used solely for invoicing of the rate cap in Article 11.2(a) and are derived from the annual escalation of rates provided in the 1996 Settlement, through January 1, 2006.

130. El Paso also modified the Statement of Rates to reflect the reallocation of costs resulting from the modification of the Article 11.2 rates. El Paso states this cost reallocation is consistent with the June 30 Order in that El Paso is recovering its costs from shippers not eligible for the Article 11.2 rates, to the extent such rates would not recover El Paso's cost of service. In its Explanation of Rate Derivation, El Paso states that the California maximum rate will apply to all Block Capacity.

131. El Paso also removed from section 37 of its tariff any proposed language that was not already found in another part of its tariff or in the 1996 Settlement, in compliance

¹⁰² *El Paso Natural Gas, Co.*, 116 FERC ¶ 61,159 (2006).

with the June 30 Order.¹⁰³ Finally, El Paso clarified the termination provision of section 37 and made a minor wording change to the inflation adjustment section.

B. Notice and Protests

132. Notice of El Paso's filing was issued on July 14, 2006. Interventions and protests were due as provided in section 154.210 of the Commission's regulations.¹⁰⁴ Pursuant to Rule 214,¹⁰⁵ all timely filed motions to intervene and any motions to intervene out-of-time filed before the issuance date of this order are granted. Granting late intervention at this stage of the proceeding will not disrupt this proceeding or place additional burdens on existing parties.

133. Protests were filed jointly by El Paso Municipal Customer Group, El Paso Electric Company, Phelps Dodge Corporation, and Public Service Company of New Mexico (EOC Protestors); jointly by the Indicated Shippers, California Public Utilities Commission, Pacific Gas and Electric Company, and Southern California Edison Company (California Protestors); Southwest Gas; and Texas Gas Service and UNS Gas, Inc. (Texas Gas Service/UNS).

134. Salt River filed an answer on July 27, 2006, Texas Gas Service/UNS filed a supplement to its protest on August 4, 2006, and Southwest Gas filed a supplement to its protest on August 30, 2006. El Paso filed an answer to Southwest Gas's supplemented protest on September 26, 2006, and Southwest Gas filed an answer to El Paso's September 26 answer on October 11, 2006. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure¹⁰⁶ prohibits an answer to a protest and answer unless otherwise ordered by the decisional authority. We will accept the answers of APS, El Paso, Southwest Gas, and Salt River because they provided information that assisted us in our decision-making process.

135. The protestors raise issues regarding the appropriate rate cap for Block Capacity with non-California delivery points, El Paso's Btu adjustment, the reallocation of costs to

¹⁰³ El Paso subsequently filed a separate section 4 filing proposing similar tariff provisions to clarify the applicability of out-of-zone charges, capacity release, and scheduling priorities to section 37. *See El Paso Natural Gas Co.*, 116 FERC ¶ 61,159 (2006).

¹⁰⁴ 18 C.F.R. § 385.210 (2008).

¹⁰⁵ 18 C.F.R. § 385.214 (2008).

¹⁰⁶ 18 C.F.R. § 385.213(a)(2) (2008).

non-eligible shippers, the changes to section 37, and Southwest Gas's billing determinants. These protests are discussed below.

C. Discussion

136. Consistent with the Commission's order accepting the Rate Case Settlement, the discussion below will not affect the Rate Case Settlement rates that are currently in effect on El Paso and will not have effect until El Paso's new rate case takes effect after the termination of the Rate Case Settlement period on January 1, 2009.

1. Appropriate Rate Cap for Block Capacity

a. Protests

137. Texas Gas Service/UNS, the EOC Protestors, and Salt River protest El Paso's statement in the compliance filing that the California zone rate applies to all Block Capacity. The EOC Protestors argue that El Paso is proposing to apply the California rate to shippers and TSAs that were not subject to the California rate under Article 11.2. Texas Gas Service/UNS agrees that El Paso has failed to apply the Article 11.2 rates to eligible shippers based on the basin-specific rates that were in effect pursuant to the 1996 Settlement, as escalated.

138. Salt River requests that the Commission confirm that El Paso may not charge more than the maximum Arizona rate for the Block Capacity that is delivered to Arizona delivery points. Salt River notes that El Paso previously stated that, "To remove any ambiguity, El Paso unequivocally reiterates what it believes it has previously made clear: a former FR Arizona shipper that moves an allocated delivery point from California to Arizona prior to the rate case will not be charged more than the maximum just and reasonable rate for Arizona either now or after 2005."¹⁰⁷ Salt River asserts that it redesignated its Block Capacity delivery points from California to Arizona prior to June 30, 2005, and that despite El Paso's "unequivocal" assertions, El Paso began charging Salt River in April 2006 the maximum California rate for Salt River's Block Capacity delivered to primary delivery points in Arizona. Salt River asserts that El Paso has violated both its own commitments to the Commission and its statutory obligations. Salt River requests that the Commission determine that El Paso has no authority to charge more than the maximum rate in effect for the zone in which the Block Capacity is delivered to Salt River's primary delivery points and order El Paso to immediately refund all improperly assessed charges to Salt River.

¹⁰⁷ Salt River cites El Paso's August 30, 2004 Answer to the Motion for Expedited Clarification in Docket No. RP00-336-014.

139. The EOC Protestors argue that having sought rehearing of the Commission's decision regarding the appropriate rate cap for the Block Capacity, El Paso should await a Commission ruling on the merits, and not use the compliance filing as a vehicle to try to obtain what it has not been permitted to obtain directly. The EOC Protestors conclude that El Paso's proposal is beyond the scope of the compliance filing and should be rejected.

b. Commission Determination

140. The Commission denies El Paso's proposal to apply the California maximum rate to all Block Capacity. El Paso's proposal is beyond the scope of this filing, which is to make tariff revisions in compliance with the June 30 Order. In addition, elsewhere in this order the Commission denied El Paso's request for rehearing on this issue and held that El Paso may not charge the California rate cap for all of the former Block Capacity, regardless of delivery zone. As such, El Paso's proposal on this issue is rejected as outside the scope of this filing and in accordance with the Commission's discussion on this issue above. El Paso is directed to file revised tariff sheets eliminating any language that applies the California maximum rate to all Block Capacity within 15 days of the issuance of this order.

2. Southwest Gas's Billing Determinants Subject to Article 11.2

a. March 20 Order

141. The March 20 Order found that the rate cap does not apply to increased service that full requirements customers have obtained as a result of the post-1996 Settlement Power Up Project and Line 2000 expansions.¹⁰⁸ The Commission accordingly held that the billing determinants of each FR customer subject to the rate cap (rate cap billing determinants) should equal the contract demand allocated to each FR customer in the Capacity Allocation Proceeding, minus the Line 2000 and Power Up Project expansion capacity allocated to that FR customer. However, the Commission stated that, if the remaining contract demand is less than the FR customer's 1996 Settlement billing determinants, then the rate cap should nevertheless apply to the entire amount of that customer's 1996 Settlement billing determinants.¹⁰⁹ In other words, each FR customer's rate cap billing determinants would equal the greater of: (1) its remaining contract demand after the expansion capacity allocated to it was subtracted from the total contract demand allocated to it in the Capacity Allocation Proceeding, or (2) the FR customer's 1996 Settlement billing determinants.

¹⁰⁸ March 20 Order, 114 FERC ¶ 61,290 at PP 84-85.

¹⁰⁹ *Id.* at n.68.

b. Compliance Filing

142. El Paso states that it calculated the rate cap billing determinants for each eligible shipper according to the formula set forth in the March 20 Order. In Southwest Gas's case, as with other shippers, the contract demand allocated to it in the Capacity Allocation Proceeding varied by month. El Paso subtracted the expansion capacity allocated to Southwest Gas from each month of Southwest Gas's contract demand. It then determined the average of the remaining contract demands and compared that average monthly figure to Southwest Gas's monthly 1996 Settlement billing determinants.¹¹⁰ Because the average of the remaining monthly contract demands was less than the 1996 Settlement billing determinants it concluded that Southwest Gas's annual rate cap billing determinants should equal its 1996 Settlement billing determinants.

143. El Paso also states that in order to make a proper comparison between the 1996 Settlement billing determinants and the amount of base and Block Capacity in former FR customers' contracts, El Paso adjusted the 1996 Settlement billing determinants in recognition of the updated Btu value.

c. Protests

144. Southwest Gas conditionally protests the rate cap billing determinants shown for Southwest Gas in the July 10 Filing. Southwest Gas states that it discussed the matter with El Paso and believed that it had been resolved informally. However, in Southwest Gas's August 30, 2006 supplement to its protest, Southwest Gas states that it did not reach an agreement with El Paso on this issue. Southwest Gas thus protests El Paso's filing on the basis that El Paso's comparison of billing determinants on an annual average basis underestimates Southwest Gas's rate cap billing determinants because of the varying monthly billing determinants.¹¹¹

¹¹⁰ Southwest Gas's billing determinants eligible for the Article 11.2 rate protection are essentially its Arizona contract demand quantities minus the expansion capacity and the capacity converted to Line 1903 contracts. Using El Paso's data, Southwest Gas's annual average billing determinants subject to the rate cap are 231,302 Mcf compared to its 1996 Settlement billing determinants (after subtracting out the Line 1903 contract from the Arizona billing determinants) of 255,905 Mcf. El Paso calculates the shortfall to be 24,603 Mcf on an annual average basis.

¹¹¹ Southwest Gas states that, on a monthly basis, its rate cap billing determinants (contract demand minus expansion capacity) are less than its 1996 Settlement billing determinants for seven months, while its rate cap billing determinants exceed the 1996 Settlement billing determinants for the remaining five months.

145. Specifically, Southwest Gas argues that El Paso should not compare its current non-expansion billing determinants to its 1996 Settlement billing determinants using an average of its current twelve monthly non-expansion billing determinants, but should look at each month separately. Southwest Gas asserts that, for each month where its non-expansion contract demand is less than its 1996 Settlement billing determinants, its rate cap billing determinants should equal its 1996 Settlement billing determinants, but in each month where its non-expansion contract demand is in excess of the 1996 Settlement billing determinants, its rate cap billing determinants should equal its full non-expansion contract demand for those months. In effect, Southwest Gas argues that each month's rate cap billing determinant should be no less than the 1996 Settlement billing determinant. Thus, Southwest Gas argues that El Paso understates its billing determinants eligible for the Article 11.2 rate protection because averaging the monthly quantities allows El Paso to offset excess quantities in some months with the shortfall in other months.¹¹²

146. In addition, Southwest Gas contends that El Paso's use of the 1.010 system-wide Btu conversion factor, instead of path-specific Btu conversion factors, unreasonably reduces Southwest Gas's rate cap billing determinants. Southwest Gas argues that its average Btu conversion factor should be 1.018. Southwest Gas asserts that the March 23 Order explicitly approves the use of path-specific Btu conversion factors to determine capacity rights and that El Paso used path-specific Btus for other adjustments. Southwest Gas thus requests that the Commission direct El Paso to revise Southwest Gas's rate cap billing determinants to reflect the use of a monthly billing determinant comparison and the Btu conversion factor for the path-specific quantity applicable to the particular shipper.

147. El Paso responds that Southwest Gas's protest of its rate cap billing determinants is untimely and fails to demonstrate good cause for not raising these arguments on a timely basis in response to the April 4 Filing or the July 10 Filing. El Paso further states that the protests are without merit. El Paso states that the March 20 Order did not require El Paso to cap Southwest Gas's 1996 Settlement billing determinants in some months, and add capacity in other months when its 1996 Settlement billing determinants are less than its non-expansion capacity. El Paso argues that Southwest Gas's position would effectively require El Paso to provide Southwest Gas with additional expansion capacity

¹¹² The total shortfall for the seven months that contract demand is less than 1996 Settlement billing determinants is 728,866 Mcf (using El Paso's system-wide Btu adjustment), or 60,739 Mcf on an annual average basis. In the remaining five months, the contract demand exceeds the 1996 Settlement billing determinants by a total of 433,635 Mcf or an annual average of 36,136 Mcf.

at capped rates, contrary to the March 20 Order. El Paso concludes that Southwest Gas's position overreaches and should be rejected.

148. El Paso further states that Southwest Gas fails to demonstrate good cause for not raising on a timely basis its objection to the use of the system-wide Btu conversion factor instead of path-specific conversion factors. El Paso states that Southwest Gas never protested El Paso's Btu adjustment in the April 4 Filing or the July 10 Filing, which proposed no change to the adjustment and which the Commission accepted in its June 30 Order. El Paso contends that Southwest Gas's argument also lacks merit. El Paso states that while Southwest Gas correctly notes that El Paso calculated its current rates on a path-specific basis, El Paso explains that is not how El Paso calculated Southwest Gas's billing determinants under the 1996 Settlement. El Paso states that to maintain consistency, it properly determined Southwest Gas's rate cap billing determinants by using a system-wide Btu conversion factor. El Paso asserts that Southwest Gas fails to address why it would be unreasonable to continue this system-wide approach for purposes of determining the amount of capacity subject to Article 11.2(a) of the 1996 Settlement.

d. Commission Determination

149. We will accept El Paso's proposed billing determinants for Southwest Gas. El Paso complied with our directive in the March 20 Order to calculate the rate cap billing determinants by subtracting the expansion capacity from each shipper's contract demand. For shippers whose resulting rate cap billing determinants were less than their 1996 Settlement billing determinants, the March 20 Order directed El Paso to apply the Article 11.2 rates to the entire amount of the shippers' 1996 Settlement billing determinants. As explained above, in Southwest Gas's case, El Paso subtracted the expansion capacity allocation from each month of Southwest Gas's contract demand and determined that the monthly average of the total annual remaining contract demand was less than Southwest Gas's monthly 1996 Settlement billing determinants. Southwest Gas argues that El Paso should not make the calculation on the basis of an average of twelve months of contract demands, but should look at each month separately, and that El Paso understates its billing determinants eligible for the Article 11.2 rate protection because averaging the monthly quantities allows El Paso to offset the shortfall in some months with excess quantities in other months.

150. We disagree. The March 20 Order found that the Article 11.2 rate protections did not apply to expansion capacity, but noted that if a shipper's non-expansion capacity was less than its 1996 Settlement billing determinants, the rate cap should apply to the entire amount of the 1996 Settlement billing determinants. The Commission did not specify that a shipper was entitled to a minimum of the 1996 Settlement billing determinants for each month, compared to an annual average. El Paso's calculations ensure that the annual volume subject to Article 11.2 rate protection will be no less than its 1996 Settlement billing determinants. Because Southwest Gas's contract demand varies month

to month, there are months where its contract demand subject to Article 11.2 rate protection will be less than its 1996 Settlement billing determinants and months when it will be more, but the total annual service will be no less than its 1996 Settlement billing determinants. In this way, El Paso is required to allocate a portion of the expansion capacity to Article 11.2 rate protection, but only to the extent necessary to ensure that Southwest Gas receives rate cap protection for volumes at least equivalent to its 1996 Settlement billing determinants. We therefore reject Southwest Gas's protest.

151. With regard to the issue of the appropriate Btu conversion factor, we find that Southwest Gas's protest is untimely. El Paso proposed the system-wide Btu conversion factor in its April 4 Filing, which Southwest Gas did not protest. El Paso did not propose any changes to that system-wide Btu conversion factor in its July 10 Filing, and Southwest Gas did not protest the use of the Btu conversion factor in its timely protest of that filing. Only in its supplement to its protest to the July 10 Filing did Southwest Gas raise the issue of path-specific Btu conversion factors. We further note that the billing determinants for the other El Paso shippers were agreed to in the Rate Case Settlement. Accepting El Paso's proposed system-wide Btu conversion factor here is consistent with the Rate Case Settlement. For these reasons, we will reject Southwest Gas's protest.

3. Other Issues

152. The remaining concerns raised by the protestors are now moot. Texas Gas Service/UNS argues that El Paso violated the filed rate doctrine by revising its terms and conditions of service via electronic bulletin board (EBB) postings rather than section 4 filings. Texas Gas Service/UNS explains that, in the July 10 Filing, El Paso removed proposed tariff changes to section 37 relating to Article 11.2 that the Commission had ruled were beyond the scope of the April 4 Filing, but stated that it would post an EBB notice specifying the procedure it will follow if an Article 11.2 shipper releases capacity or schedules to an alternate point. Texas Gas Service/UNS state that, while El Paso states that it will submit a separate section 4 filing proposing tariff provisions specifying those procedures, El Paso should not evade the filed rate doctrine by revising the terms and conditions of service via EBB postings in the interim. The Commission notes that, on July 21, 2006, shortly after the July 10 Filing, El Paso filed such a section 4 filing, which was accepted August 18, 2006. This addresses Texas Gas Service/UNS's concern.

153. The protestors also raise a number of issues regarding the calculation of rates in the July 10 Filing. The EOC Protestors question whether El Paso had double counted the impact of its system Btu measurement change by applying it to both rates and determinants. The California Protestors assert that the Article 11.2 rates are negotiated rates and that El Paso may not reallocate costs from negotiated rates to non-Article 11.2 rates. In addition, the protestors generally contend that acceptance of the compliance filing does not constitute approval of the derivation of the rates, the capacity which is subject to the rate caps or the cost reallocation, all of which remain subject to the outcome of the rate case hearing. With the exception of Southwest Gas's billing

determinants, the Rate Case Settlement resolved the issues regarding the determination of Article 11.2 and non-Article 11.2 rates for the term of the Rate Case Settlement. Thus, the protests regarding how El Paso calculated those rates in the July 10 compliance filing are moot. Any issues regarding how El Paso will calculate those rates in the future, after the Rate Case Settlement terminates, will be addressed in El Paso's pending rate case in Docket No. RP08-426-000, filed June 30, 2008.

The Commission orders:

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

(B) El Paso's July 10 Filing is accepted subject to conditions, as discussed in the body of this order and in the ordering paragraph below.

(C) El Paso is directed to make a compliance filing eliminating any language applying the California maximum rate to all Block Capacity within 15 days of the issuance of this order.

By the Commission. Commissioner Spitzer not participating.

(S E A L)

Kimberly D. Bose,
Secretary.