

132 FERC ¶ 61,155  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
John R. Norris, and Cheryl A. LaFleur.

El Paso Natural Gas Company

Docket No. RP05-422-031

ORDER ON REHEARING

(Issued August 24, 2010)

1. On September 5, 2008, the Commission issued an order on rehearing and compliance filing in this proceeding that addressed the continuing applicability of Article 11.2 of the 1996 Settlement between El Paso Natural Gas Company (El Paso) and its shippers.<sup>1</sup> As explained more fully below, Article 11.2 places limitations on the rates that El Paso can charge in future rate cases to certain shippers who were parties to the 1996 Settlement. On October 6, 2008, El Paso, and Gila River Power, L.P. (Gila River) and New Harquahala Generating Company, LLC (New Harquahala), filed requests for rehearing of the September 5 Order. As discussed in detail below, the Commission denies the requests for rehearing.

**I. Background**

2. In support of its rehearing request, El Paso raises several arguments that have been resolved previously in other El Paso proceedings. To aid in demonstrating that these issues have already been addressed, the Commission provides an extensive background of the relevant prior proceedings below.

**A. 1996 Settlement**

3. 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).<sup>2</sup> At the time the 1996 Settlement

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<sup>1</sup> *El Paso Natural Gas Co.*, 124 FERC ¶ 61,227 (2008) (September 5 Order).

<sup>2</sup> *El Paso Natural Gas Co.*, 79 FERC ¶ 61,028, *reh'g denied*, 80 FERC ¶ 61,084 (1997).

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 turned back their rights to capacity on the El Paso system,<sup>3</sup> resulting in approximately 35 percent of the capacity on El Paso becoming unsubscribed.

4. The excess unsubscribed capacity on the El Paso system threatened to impose a substantial cost burden on El Paso and its remaining customers. The 1996 Settlement resolved this issue through an agreed-upon sharing of the risk that the turnback capacity would not be subscribed by new shippers, and of the revenues from any resales of the unsubscribed capacity. Specifically, for the first eight years of the 1996 Settlement, El Paso's maximum rate shippers agreed to bear 35 percent of the fixed costs related to the unsubscribed capacity, while El Paso was responsible for 65 percent of such costs. In addition, El Paso agreed to credit back to these shippers 35 percent of the revenue from remarketing the unsubscribed capacity, while El Paso would retain 65 percent of any such revenue. For the last two years of the 1996 Settlement, El Paso was responsible for all of the costs of the unsubscribed capacity and was entitled to keep all revenue from the sales of the unsubscribed capacity.

5. In addition to establishing the risk-sharing arrangement, the 1996 Settlement provided rate certainty for shippers in the form of a rate cap that would extend beyond the term of the 1996 Settlement.<sup>4</sup> Article 11.2 of the 1996 Settlement provided that rates for

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<sup>3</sup> The capacity turned back by El Paso's California shippers is often referred to as turnback capacity, unsubscribed capacity, or Block Capacity. The term "Block Capacity" originated because the 1996 Settlement divided the turnback capacity into three blocks. Each of the blocks had different receipt points and certain restrictions on 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 the El Paso system.

<sup>4</sup> Article 11.2 of the 1996 Settlement states:

11.1 Applicability. The provisions set forth in this Article XI shall apply to all periods subsequent to the term of this Stipulation and Agreement.

11.2 Firm TSAs 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

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capacity then under contract by eligible shippers<sup>5</sup> will be capped, subject to inflation, and that the rate cap will continue to apply until the termination of the shippers' transportation service agreements (TSA). Article 11.2(b) provided that the rates applicable to any shipper with an Article 11.2(a) rate-capped contract will never include costs related to system capacity in existence on the El Paso system at the time of the 1996 Settlement that becomes unsubscribed or is subscribed at less than the maximum applicable rate (i.e., 1995 Capacity).

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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:

(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).

<sup>5</sup> For the purposes of Article 11.2 of the 1996 Settlement, eligible shippers are firm shippers with TSAs that were in effect on December 31, 1995 and remain in effect.

6. The Commission approved the 1996 Settlement and concluded that it provided a reasonable resolution of the excess capacity situation on El Paso's system at that time.<sup>6</sup>

**B. Capacity Allocation Proceeding**

7. During the first few years of the 1996 Settlement period, circumstances on El Paso's system changed dramatically. Available capacity on El Paso went from an excess to a constrained condition. Several factors contributed to this change.

8. At the 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 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. El Paso's CD contracts were mainly held by California customers, while the FR contracts were mainly held by customers located east of California (EOC).

9. In addition, during this time, section 4.2 of the General Terms and Conditions (GT&C) of El Paso's tariff stated that if El Paso had insufficient capacity to serve all transportation requests at a nominated receipt pool, firm shipper nominations would be subject to *pro-rata* reductions based upon available capacity. Section 4.2 of El Paso's tariff implemented a *pro rata* curtailment provision agreed to by all of El Paso's shippers in a 1990 Settlement.<sup>7</sup>

10. During the first few years of the 1996 Settlement period, the FR shippers' load grew substantially. The El Paso system went from one of excess capacity to one of strained capacity. In 2000 and 2001, El Paso experienced capacity allocation problems and began to rely on the *pro rata* curtailment provision in its tariff. As shipper demands continued to grow, *pro rata* curtailments on the El Paso system became routine and firm service became unreliable.

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<sup>6</sup> *El Paso Natural Gas Co.*, 79 FERC ¶ 61,028 (1997).

<sup>7</sup> In 1990, El Paso entered into a settlement with its customers that implemented contract conversions from bundled sales service to transportation service (1990 Settlement). The 1990 Settlement specifically provided for the continuation of FR service and included procedures for *pro rata* service curtailments.

11. In response to the routine cuts in firm service that were taking place on the El Paso system, shippers filed complaints against El Paso.<sup>8</sup> The Commission issued a series of orders in the Capacity Allocation Proceeding that addressed the complaints and established a framework for resolving the capacity allocation problems that had rendered firm service on El Paso unreliable.<sup>9</sup>

### 1. May 31 Order

12. The first order in the Capacity Allocation Proceeding was the May 31 Order. In that order, the Commission found that El Paso's existing capacity allocation methodology was no longer just and reasonable and was adversely affecting the public interest because parties with firm transportation contracts were not receiving the firm service for which they paid.<sup>10</sup> The Commission stated that capacity allocation procedures that result in regular cuts in firm service are not just and reasonable. The Commission explained that *pro rata* allocation is an appropriate way to deal with emergency circumstances, but it cannot be a regular part of the daily scheduling process. The Commission stated that section 284.7 of the Commission's regulations provides that firm service is service that is not subject to a prior claim by another customer.<sup>11</sup> The Commission stated it is inconsistent with this regulation for firm shippers to be charged for firm service and have

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<sup>8</sup> 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 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 Natural Gas Act (NGA) by failing to maintain its facilities in a manner that allowed it to provide firm service up to certificated levels.

<sup>9</sup> *El Paso Natural Gas Co.*, 99 FERC ¶ 61,244 (2002) (May 31 Order); 100 FERC ¶ 61,285 (2002) (September 20 Order), *reh'g*, 104 FERC ¶ 61,045 (2003) (July 9 Order), *reh'g*, 106 FERC ¶ 61,233 (2004) (March 8 Order), *aff'd*, *Arizona Corporation Comm. v. FERC*, 397 F.3d 952 (D.C. Cir. 2005) (collectively the Capacity Allocation Proceeding).

<sup>10</sup> May 31 Order at 62,000-62,001.

<sup>11</sup> 18 C.F.R. § 284.7 (2009).

service reduced through *pro rata* allocations on a non-emergency basis so that the pipeline can provide service to another shipper.

13. In addition, the May 31 Order found that FR contracts on El Paso were no longer just and reasonable or in the public interest.<sup>12</sup> The Commission stated that there was not a single cause of the capacity crisis on the El Paso system. The Commission stated that El Paso continued to remarket firm service capacity as contracts expired irrespective of capacity availability on the system and the impacts its actions may have had on all other shippers. However, the Commission found that the growth in FR demand was the most significant part of the service degradation problem. As a result, the Commission determined it was necessary to convert the FR contracts to CD 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 stated that its decision to modify the FR contracts was not premised on the fact that the FR shippers' load growth was unreasonable. But the Commission declined to state whether that growth was foreseeable and instead focused on providing a remedy for the future.<sup>13</sup>

14. The Commission explained that there were extraordinary circumstances on El Paso's system that required modification of the FR contracts under the *Mobile-Sierra* public interest doctrine.<sup>14</sup> The Commission stated its determination that the public interest required modification of the FR contracts was not based merely on generalized statements of policy goals, but was based on a detailed analysis of how the FR contracts on the El Paso system harmed the public interest and how the conversion of those contracts would further the public interest. The Commission stated that all customers would benefit from reliable firm service on El Paso as a result of the conversion of the FR contracts to CD contracts.

15. The Commission also found that modification of El Paso's 1990 and 1996 Settlements to the extent necessary to convert the FR contracts to CD contracts was just and reasonable and in the public interest.<sup>15</sup> The Commission explained that its policy is to encourage settlements and that it was extremely reluctant to alter a settlement during its term. However, the Commission stated that the circumstances on El Paso have

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<sup>12</sup> May 31 Order at 62,002-62,003.

<sup>13</sup> *Id.* at 62,004.

<sup>14</sup> *Id.* at 62,005-62,006 (citing *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956); *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956)).

<sup>15</sup> *Id.* at 62,007-62,008.

changed dramatically since the 1990 and 1996 Settlements were executed. The Commission stated that while the 1996 Settlement was a reasonable resolution of the issues facing El Paso and its customers at that time, the circumstances that made the 1996 Settlement reasonable no longer existed. The Commission stated that unless it made some adjustment to the terms of the 1996 Settlement to reform the FR contracts, the problems of unreliability on El Paso would continue and worsen. The Commission stated that while it rarely alters an approved settlement, it has not only the authority, but also the responsibility under section 5 of the NGA to make an adjustment to a settlement if the terms of the settlement have become unjust and unreasonable and the settlement operates in a way that is contrary to the public interest. The Commission stated that it was attempting to minimize the changes to the 1996 Settlement while taking action to alleviate the reliability problems.<sup>16</sup> The Commission explained that it modified the 1996 Settlement only to the extent necessary to restore reliable firm service on El Paso, and stated that the remainder of the 1996 Settlement would remain in place.<sup>17</sup>

16. In establishing a methodology for converting the FR contracts to CD contracts, the Commission stated that El Paso should allocate to the FR shippers all system capacity not under contract by the CD shippers.<sup>18</sup> In addition, the Commission noted that El Paso dedicated the capacity related to its Line 2000 and Power Up expansion projects for system use.<sup>19</sup> The Commission explained that the full existing system capacity, plus the expansion capacity, minus the full CD shippers' contract levels and a reasonable amount to serve FT-2 shippers, was the amount available to be allocated to the FR shippers at no additional charge above their current demand charge responsibility.

17. The May 31 Order also found that El Paso may not enter into new firm service contracts unless it can demonstrate that it has available capacity to provide the service.<sup>20</sup> The Commission explained that pursuant to section 16.3 of the 1996 Settlement<sup>21</sup> and

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<sup>16</sup> *Id.* at 62,008.

<sup>17</sup> *Id.* at 62,018.

<sup>18</sup> *Id.* at 62,009.

<sup>19</sup> The 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.

<sup>20</sup> *Id.* at 62,012.

<sup>21</sup> Section 16.3 of the 1996 Settlement provides:

section 284.7(a)(3) of the Commission's regulations, El Paso has an obligation to provide firm shippers with the firm service for which they contracted. The Commission stated that El Paso must reasonably insure the quality of this service and that its actions do not degrade the quality of such service. The Commission stated that during the pendency of the 1996 Settlement, El Paso must first offer firm capacity that becomes available to its existing shippers.

## 2. July 9 Order

18. In the July 9 Order, the Commission affirmed its decisions in the May 31 Order. The Commission found that the decision to convert the FR contracts to CD contracts and to modify El Paso's tariffs and settlements was consistent with *Mobile-Sierra* and the NGA.

19. The Commission rejected shippers' arguments that it should have abrogated the entire 1996 Settlement, rather than partially modifying it.<sup>22</sup> The Commission explained that in resolving the capacity allocation problems on El Paso, the Commission attempted to retain the bargains in the 1996 Settlement to the greatest extent possible and modified only those portions that clearly became unjust and unreasonable.<sup>23</sup> The Commission stated that it already fully explained why the FR contracts must be converted to CD contracts to restore reliable firm service on El Paso.<sup>24</sup> The Commission stated that it does not necessarily follow that once the Commission modified the 1996 Settlement to reflect those changes, the other elements of the 1996 Settlement should be abrogated. The Commission explained that there is no evidence that provisions of the 1996 Settlement unrelated to the provision of firm service have contributed to the service

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*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.

<sup>22</sup> July 9 Order at P 93.

<sup>23</sup> *Id.* P 173.

<sup>24</sup> *Id.* P 93.

disruptions on El Paso. The Commission thus concluded that there was no factual or legal basis for abrogating the entire 1996 Settlement.

20. The Commission also responded to shipper allegations that El Paso was at fault for the capacity shortfall problem because it oversold its system.<sup>25</sup> The Commission stated that El Paso had an obligation to administer its pipeline system in a manner that provides reliable firm service to its customers as set forth in section 16.3 of the 1996 Settlement, and that El Paso remarketed expired capacity when it could not meet all of its firm service obligations. However, the Commission stated that because the terms of El Paso's tariffs, contracts, and settlements operated to create conflicting requirements, the net result of these settlements, tariffs, and contracts was unjust and unreasonable and not in the public interest. The Commission explained that the remedy it adopted going forward will end the routine *pro rata* allocations on the system. The Commission stated that in these circumstances, it would not be reasonable for the Commission to penalize El Paso for implementing the terms of its settlements agreed to by its shippers and approved by the Commission.<sup>26</sup>

21. The Commission also affirmed the decision in the May 31 Order to allocate the full available system capacity to the converting FR shippers.<sup>27</sup> The Commission stated that allocating the full amount of available capacity to FR shippers is appropriate to ensure El Paso can meet the peak firm requirements of its customers and is necessary to restore reliable firm service on El Paso. The Commission also clarified that Block Capacity should be included in the initial allocation to FR shippers.<sup>28</sup> The Commission explained that there is a finite amount of capacity on El Paso to be allocated to the FR customers and that providing the converting shippers with new CDs that include the Block Capacity provides these shippers with a higher CD level than they would otherwise have been able to receive.

22. In addition, the Commission clarified that the May 31 did not prohibit El Paso from reselling capacity, but required that El Paso demonstrate that resales of existing capacity will not degrade service to its existing firm customers.<sup>29</sup> The Commission

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<sup>25</sup> *Id.* P 112.

<sup>26</sup> *Id.* P 126.

<sup>27</sup> *Id.* P 133.

<sup>28</sup> *Id.* P 171.

<sup>29</sup> *Id.* P 161.

explained that El Paso cannot sell as firm service capacity for which there is a prior commitment. The Commission stated that the sale, on a firm basis, of capacity that is required to serve firm shippers under their current contracts would violate the Commission's regulations<sup>30</sup> and El Paso's current contracts. The Commission clarified that El Paso may remarket its turnback capacity if that capacity is not needed to serve current firm service obligations.

23. The Commission's decisions in the Capacity Allocation Proceeding were affirmed by the United States Court of Appeals for the District of Columbia Circuit (Court).<sup>31</sup>

24. The Commission's actions in the Capacity Allocation Proceeding were narrowly focused on restoring reliability to El Paso's system. The continued applicability of the Article 11.2 rate caps after the expiration of the 1996 Settlement was not raised as an issue in that case. However, several EOC shippers later raised the issue in a related El Paso proceeding.<sup>32</sup> In response, the Commission stated that it was premature to address the issue of the continuing applicability of Article 11.2 and that the appropriate forum to address future rate issues would be in El Paso's next rate proceeding.<sup>33</sup>

### C. 2005 Rate Case Proceeding

25. On June 30, 2005, El Paso filed a general system-wide rate case (2005 Rate Case), as required by 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,<sup>34</sup> subject to refund and conditions, and

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<sup>30</sup> 18 C.F.R § 284.7(a)(3) (2009).

<sup>31</sup> *Arizona Corporation Commission v. FERC*, 397 F.3d 952 (D.C. Cir. 2005).

<sup>32</sup> On August 13, 2004, in El Paso's Docket No. RP04-110-000, Arizona Public Service Company, Pinnacle West Energy Corporation, and Salt River Project Agricultural Improvement and Power District (collectively, Arizona Electrics) filed a request for clarification that the conversion from FR to CD service did not change the calculation of rates under Article 11.2 of the 1996 Settlement.

<sup>33</sup> *El Paso Natural Gas Co.*, 109 FERC ¶ 61,359, at P 23 (2005).

<sup>34</sup> In the 2005 Rate Case, 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

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establishing hearing procedures and a technical conference.<sup>35</sup> In the July 29 Suspension Order, the Commission stated that any issues related to Article 11.2 of the 1996 Settlement would be addressed at the technical conference.

26. The Commission held technical conferences on El Paso's Rate Case Filing in September and October 2005. After the conclusion of the technical conferences, the Commission issued two orders (collectively, Technical Conference Orders). The March 23 Order addressed issues related to the implementation of new services,<sup>36</sup> while the March 20 Order dealt with post-1996 Settlement issues, including Article 11.2.<sup>37</sup>

27. 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 stated that the Article 11.2 rate cap applies to former FR shippers as well as CD shippers. The Commission further held that because the Article 11.2(a) rate cap applies only to shippers with TSAs in effect on December 31, 1995, the rate cap does not apply to any newly executed contracts. In addition, the Commission concluded that the rate cap does not apply to Expansion Capacity.

28. With regard to Article 11.2(b), the March 20 Order 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 capacity that was part of El Paso's system on December 31, 1995 that (1) becomes unsubscribed, or (2) is 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 4,000 MMcf/d of firm subscribed capacity on El Paso's system is 1995 Capacity.

29. On December 6, 2006, while requests for rehearing of the March 20 Order were pending, El Paso filed a settlement (2006 Settlement) that resolved all of the issues in the Rate Case Filing set for hearing or technical conference, with limited exceptions. The

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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 CD shippers, and the second alternate sheets provided for the continued application of Article 11.2 for all eligible shippers.

<sup>35</sup> *El Paso Natural Gas Co.*, 112 FERC ¶ 61,150 (2005) (July 29 Suspension Order).

<sup>36</sup> *El Paso Natural Gas Co.*, 114 FERC ¶ 61,305 (2006) (March 23 Order).

<sup>37</sup> *El Paso Natural Gas Co.*, 114 FERC ¶ 61,290 (2006) (March 20 Order).

2006 Settlement established “black box” rates to remain in effect on El Paso for a three-year period, ending December 31, 2008. The 2006 Settlement was agreed to by all parties except one.

30. The 2006 Settlement left unresolved a few discrete issues, including those related to Article 11.2 of the 1996 Settlement. Although the March 20 Order addressed Article 11.2 issues, the requests for rehearing of the March 20 Order were pending when the 2006 Settlement was filed. In addition the March 20 Order set certain Article 11.2 implementation issues for hearing. As such, the 2006 Settlement provided that any outstanding issues related to Article 11.2 would be resolved by the Commission when it addressed the requests for rehearing of the Technical Conference Orders and that the Commission’s resolution of those rehearing requests would not take effect until the end of the three-year settlement period.

31. On August 31, 2007, the Commission issued an order approving the 2006 Settlement for all parties, including the one contesting party, with a modification to the standard of review.<sup>38</sup>

#### **D. September 5 Order**

32. In the September 5 Order, the Commission addressed the requests for rehearing of the March 20 Order. The requests for rehearing raised issues concerning the continued applicability of Article 11.2 of the 1996 Settlement, as well as Article 11.2’s application to the former Block Capacity and whether El Paso could propose a discount adjustment to shift costs related to the 1995 Capacity to its shippers.

33. As an initial matter, the Commission affirmed its decision in the March 20 Order that the Capacity Allocation Proceeding did not abrogate El Paso’s obligations under Article 11.2 of the 1996 Settlement.<sup>39</sup> In addition, the Commission found that the Article 11.2(a) rate cap applies to the former Block Capacity.<sup>40</sup> The Commission also stated that any discount adjustment 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 1996 Settlement.<sup>41</sup>

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<sup>38</sup> *El Paso Natural Gas Co.*, 120 FERC ¶ 61,208 (2007).

<sup>39</sup> September 5 Order at P 28-37.

<sup>40</sup> *Id.* P 53-60.

<sup>41</sup> *Id.* P 120.

## II. Requests for Rehearing

34. On October 6, 2008, Gila River and New Harquahala (jointly) and El Paso filed requests for rehearing of the September 5 Order.

35. Gila River and New Harquahala argue that the September 5 Order erred by allowing El Paso to propose a discount adjustment which would allow El Paso to shift costs related to the 1995 Capacity to its shippers. Gila River and New Harquahala further assert that even if it were permissible for El Paso to shift these costs to shippers, it was improper for the Commission to allow El Paso to impose those costs on only those shippers who were not a party to the 1996 Settlement. Gila River and New Harquahala argue these rulings ignore El Paso's obligation under Article 11.2(b) of the 1996 Settlement to assume full responsibility for costs related to 1995 Capacity.

36. El Paso argues the September 5 Order improperly asserts a different rationale for refusing to terminate Article 11.2 than the rationale asserted in the March 20 order. El Paso contends this new rationale is erroneous and, on rehearing, the Commission should reverse its decision and find that its actions in the Capacity Allocation Proceeding frustrated the central purpose of the 1996 Settlement, releasing El Paso from its obligations under Article 11.2.

37. In addition, El Paso argues that even if Article 11.2 continues to apply, the Commission should reverse its decision in the September 5 Order that Article 11.2 applies to the former Block Capacity. El Paso contends that if the Commission finds that Article 11.2 applies to the former Block Capacity, the California rate cap is the appropriate rate cap for the Block Capacity.

38. On October 23, 2008, the Joint Movants<sup>42</sup> filed an answer to El Paso's request for rehearing. The Joint Movants contend El Paso is incorrect in arguing that the Commission changed its rationale in the September 5 Order. The Joint Movants assert that the September 5 Order is consistent with the Commission's prior orders regarding El Paso's service obligations under the FR contracts.<sup>43</sup> The Joint Movants argue

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<sup>42</sup> The Joint Movants are: El Paso Municipal Customer Group; Freeport-McMoRan Copper & Gold Inc.; Public Service Company of New Mexico; Southwest Gas Corporation; Texas Gas Service Company, a division of ONEOK, Inc.; UNS Gas, Inc.; and Arizona Public Service Company.

<sup>43</sup> Joint Movants' October 23, 2008 Answer at 3-4 (citing September 5 Order at P 33; July 9 Order at 61,133, 61,151).

El Paso's rehearing request is an improper collateral attack on the orders in the Capacity Allocation Proceeding and should be rejected.

39. On November 7, 2008, El Paso filed an answer arguing that the Joint Movants mischaracterize and ignore relevant prior Commission orders and that the Commission should reject their answer.

### **III. Discussion**

40. As discussed below, the Commission denies El Paso's request for rehearing and clarifies the September 5 Order's holdings regarding Article 11.2(b), as requested by Gila River and New Harquahala.

#### **A. Continuing Applicability of Article 11.2 of the 1996 Settlement**

##### **1. September 5 Order**

41. In its request for rehearing of the March 20 Order, El Paso argued that the remedial action taken in the Capacity Allocation Proceeding frustrated what El Paso views as the central purpose of the 1996 Settlement, and consequently El Paso should be relieved of its obligations under Article 11.2. El Paso argued that in the 1996 Settlement parties agreed upon a mechanism for sharing the risks associated with the Block Capacity. El Paso asserted that by requiring El Paso to provide certain amounts of 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 deprived El Paso of revenue from remarketing the Block Capacity. El Paso argued this frustrated the central purpose of the 1996 Settlement, and therefore El Paso should be excused from performance under Article 11.2 of the 1996 Settlement.

42. In the September 5 Order, the Commission denied rehearing and affirmed that the Capacity Allocation Proceeding did not abrogate Article 11.2 of the 1996 Settlement. The Commission rejected the notion that its actions in the Capacity Allocation Proceeding frustrated the central purpose of the 1996 Settlement. The Commission explained that although the 1996 Settlement authorized El Paso to remarket the Block Capacity, this right was not unqualified. The option to remarket the Block Capacity was always tempered by El Paso's obligations in section 16.3 of the 1996 Settlement<sup>44</sup> and

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<sup>44</sup> 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

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section 284.7(a)(3) of the Commission's regulations,<sup>45</sup> which require El Paso to administer its pipeline in a manner that provides reliable firm service to its existing customers. Moreover, El Paso's contracts with its FR customers, by requiring El Paso to serve their full requirements, obligated El Paso to use all existing unsubscribed capacity, including the Block Capacity, to serve the demand of the FR customers. The September 5 Order held that when the Commission required El Paso to use a portion of the Block Capacity to serve FR shippers, it was simply enforcing El Paso's existing contractual obligation under the FR customers' TSAs and the 1996 Settlement. By making El Paso fulfill this obligation, the Commission did not abrogate the central purpose of the 1996 Settlement. Rather, the Commission found it required El Paso to fulfill its obligation to administer its pipeline consistent with section 16.3 of the 1996 Settlement and the Commission's regulations, and to use its existing capacity to satisfy its contractual obligations under the existing firm customers' TSAs.

## **2. El Paso's Request for Rehearing of the September 5 Order**

43. El Paso argues that the September 5 Order adopted a new justification for rejecting El Paso's claim that the Capacity Allocation Proceeding frustrated the central purpose of the 1996 Settlement and that its obligations under Article 11.2 of the 1996 Settlement should thus be terminated. El Paso contends the Commission has offered a new justification for continuing to enforce Article 11.2, which should be reversed.

44. El Paso states that in the March 20 Order, the Commission offered several reasons for rejecting El Paso's position. El Paso states that the Commission's principal reason was that the changes made to the 1996 Settlement in the Capacity Allocation Proceeding were limited in scope and made for the limited purpose of restoring reliable firm service on El Paso's system. El Paso states that the March 20 Order also rejected its argument on the grounds that El Paso should have raised any objections it had regarding modifications to the 1996 Settlement in the Capacity Allocation Proceeding. Furthermore, El Paso states that the March 20 Order rejected its position based on the rationale that parties are not permitted to withdraw from settlements simply because they turn out to be less beneficial than expected, and because El Paso was not the only party whose expectations under the 1996 Settlement were altered. El Paso argues that the March 20 Order accepted

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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.

<sup>45</sup> See 18 C.F.R. § 284.7(a)(3) (2009).

the premise that the Commission's remedy in the Capacity Allocation Proceeding required significant changes to the 1996 Settlement and the FR contracts.

45. El Paso argues that in contrast, the September 5 Order states that the changes to the 1996 Settlement and the FR contracts simply enforced the parties' own understandings, rather than constituting a material modification to those agreements. El Paso states that the Commission now interprets the 1996 Settlement and the FR shippers' contracts as preserving for the FR customers a right to claim the Block Capacity if, during the term of the 1996 Settlement, their needs grew beyond the service levels assumed in the 1996 Settlement.

46. El Paso states that this rationale appears for the first time in the September 5 Order and as a result, El Paso has not had an opportunity to address it. El Paso argues this interpretation of the 1996 Settlement and FR contracts is unsupported and conflicts with the clear intent and purpose of those agreements. El Paso contends the parties to the 1996 Settlement expected El Paso to try to sell every Mcf of the Block Capacity and they had no expectation that some quantity of this capacity would be held back for use by the FR customers. El Paso asserts that the intent and effect of the 1996 Settlement was to impose on El Paso a continuing obligation to attempt to sell all of its unsubscribed capacity, and not simply an option to do so. El Paso states that the 1996 Settlement contained no provision dedicating even part of the Block Capacity to, or reserving it for, the FR shippers. El Paso thus contends that the 1996 Settlement represented a conscious decision by El Paso's existing shippers to accept the risk that they would not need any portion of the Block Capacity to serve their needs.

47. In addition, El Paso disagrees with the Commission's broad view of El Paso's capacity obligation to the FR shippers. El Paso acknowledges that the FR shippers' TSAs did not embody a stated limit on firm service and permitted an unspecified amount of growth. However, El Paso argues that, under established principles of contract law, El Paso's obligation to serve an increase in requirements is limited to quantities reasonably foreseeable when the contract was made. El Paso states that the controlling legal standard is whether the growth is "unreasonably disproportionate to the expectation of the parties."<sup>46</sup> El Paso argues that growth that occurred in FR shippers' loads was disproportionate to the reasonable expectations of the parties and could not have been embodied in the parties' contracts or settlement agreements.

48. El Paso further argues it had no obligation to pursue its legal claims regarding the continuing applicability of Article 11.2 in the Capacity Allocation Proceeding. El Paso

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<sup>46</sup> El Paso's October 6, 2008 Request for Rehearing at 16 (citing Tx. Bus. & Comm. Code Ann. § 2.306(a) (Vernon 1994)).

states the Commission found in the Capacity Allocation Proceeding that because it was modifying the FR shippers' contracts to specify a definite CD quantity, it was not necessary to determine whether El Paso's obligations under those contracts were limited by the principles of foreseeability and reasonableness.<sup>47</sup> El Paso contends that because the Commission found that it was not necessary to determine whether a limit existed under the FR shippers' TSAs, El Paso considered the Commission's characterization of the FR shippers' rights as "unlimited" to be essentially harmless. El Paso claims that it was not apparent that the Commission would rely on this characterization to enforce a provision of the 1996 Settlement that was not at issue in that case. El Paso further contends that it did not contest the issue of whether the FR shippers' rights were unlimited because El Paso did not object to the Commission's remedy in the Capacity Allocation Proceeding, and El Paso was not impacted by this characterization until the subject rate proceeding. In support of its position, El Paso asserts that the Commission held that it was premature to address Article 11.2 issues until the next rate case.<sup>48</sup>

49. El Paso argues that, even if the FR shippers had unlimited growth rights, they either relinquished them, or at least put them at the mercy of El Paso's remarketing efforts, when they agreed to the 1996 Settlement. El Paso argues that by imposing on El Paso the obligation to dispose of the Block Capacity in the 1996 Settlement, the FR customers made the choice to rely on one of the following contingencies if their future needs increased: (1) the possibility that El Paso would have enough unsubscribed capacity to meet their needs; (2) a system expansion; or (3) *pro rata* curtailment. El Paso asserts that *pro rata* curtailment was the short-term solution parties agreed to in the 1996 Settlement for any capacity shortfall. El Paso states that if the FR shippers' needs increased for the long term, and all other capacity was subscribed, the parties agreed in the 1996 Settlement to solve the problem through a system expansion with an appropriate rate adjustment to reflect increased costs. El Paso states that a system expansion should have been used to meet the FR shippers' growth, rather than appropriating existing capacity used to serve other customers.

50. El Paso contends that the Commission appears to conclude that section 16.3 of the 1996 Settlement required El Paso to cease making sales of Block Capacity to other shippers if necessary to assure sufficient capacity for its FR shippers and avoid curtailments. El Paso argues that section 16.3 has nothing to do with El Paso's capacity sales and only requires that El Paso retain sufficient facilities to meet its service obligations. El Paso further contends section 16.3 must be read in concert with the other

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<sup>47</sup> *Id.* at n.16 (citing May 31 Order at 62,003-04).

<sup>48</sup> *Id.* (citing *El Paso Natural Gas Co.*, 109 FERC ¶ 61,359, at P 23 (2004); July 9 Order at P 93; September 5 Order at P 12).

provisions of the 1996 Settlement, such as the provisions granting El Paso the right to remarket the Block Capacity and to make *pro rata* curtailments in the event of a capacity shortfall.

51. In addition, El Paso disagrees with the Commission's finding that its *pro rata* curtailment procedures violated section 284.7(a)(3) of the Commission's regulations, which defines firm service obligations. El Paso argues that the *pro rata* curtailment procedures, which were initially approved by the Commission, have remained in effect for more than ten years, and have been confirmed as appropriate in several settlements.<sup>49</sup> Moreover, El Paso contends the Commission expressly rejected allegations in the Capacity Allocation Proceeding that El Paso violated the Commission's firm service regulations by curtailing firm shippers on a *pro rata* basis in accordance with its settlements.

52. El Paso argues the September 5 Order's conclusion that El Paso's right to remarket the Block Capacity was a qualified right conflicts with findings in the Capacity Allocation Proceeding. El Paso asserts that if the Commission's purpose in the Capacity Allocation Proceeding was to enforce existing rights, it would have had no need to modify El Paso's settlements, contracts, and tariff. El Paso argues that in the Capacity Allocation Proceeding, the Commission expressly addressed and rejected the argument that El Paso had breached an obligation to use Block Capacity for FR shipper growth when it sold the Block Capacity to other shippers. El Paso argues it is improper for the Commission to now conclude that El Paso always had a service obligation to serve the FR shippers with Block Capacity.

53. El Paso argues the September 5 Order fails to acknowledge that the Capacity Allocation Proceeding fundamentally changed the elements of the parties' deal in the 1996 Settlement package, from which the Commission does not have the right to pick and choose which provisions to enforce.

54. El Paso contends that Article 11.2 embodied a voluntarily-assumed limitation on El Paso's NGA section 4 rights to change its rates based on the benefits provided by the other provisions of the 1996 Settlement. El Paso argues that in the Capacity Allocation Proceeding, a substantial number of the benefits of the 1996 Settlement, including El Paso's right to remarket Block Capacity, were stripped out of the agreement. El Paso states that once the 1996 Settlement was changed in a material way, unless a settling party consents, the Commission is required to find authority for its decision not in

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<sup>49</sup> El Paso states that its 1990 Settlement, its Order No. 636 Settlement, and its 1996 Settlement all provide for *pro rata* curtailments.

the terms of the settlement, but in the provisions of the NGA.<sup>50</sup> Thus, El Paso argues that, absent its agreement to abide by Article 11.2, which El Paso no longer agrees to do, the Commission has no authority to impose rate caps or other requirements stemming from Article 11.2 on El Paso's rate filings.

### 3. Joint Movants' Answer

55. The Joint Movants filed an answer to El Paso's request for rehearing.<sup>51</sup> The Joint Movants argue that the September 5 Order is not inconsistent with the Commission's prior orders regarding El Paso's service obligations under the FR shippers' contracts. The Joint Movants claim that El Paso's request is a collateral attack on the final orders in the Capacity Allocation Proceeding. The Joint Movants state that El Paso failed to seek rehearing of such orders and cannot use its current rehearing request to revitalize rights that have been waived.

56. The Joint Movants acknowledge that the extent to which FR contracts permitted growth in overall demand was debated in the Capacity Allocation Proceeding. However, the Joint Movants contend that the issue is irrelevant considering the Commission ultimately determined that it was reasonable to expect El Paso to use all available capacity, including the Block Capacity, to provide the former FR shippers with new CD entitlements that corresponded to their peak usage under their former FR contracts (i.e., sculpted contracts).<sup>52</sup> Moreover, the Joint Movants state that the various settlement provisions qualifying El Paso's obligation to construct new facilities to accommodate such growth do not detract from the Commission's conclusion that it was incumbent on El Paso to dedicate all available capacity to the former FR shippers to meet their historical needs. The Joint Movants state that the September 5 Order correctly observed

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<sup>50</sup> El Paso's October 6, 2008 Request for Rehearing at 29 (citing *Texas Eastern Transmission Corp v. FPC*, 306 F.2d 356, 357 (5th Cir. 1962), *cert. denied*, *Manufacturer's Light & Heat Co. v. Texas Eastern Transmission Corp.*, 375 U.S. 941 (1963)).

<sup>51</sup> Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2009), prohibits an answer to a request for rehearing unless otherwise ordered by the decisional authority. We will accept the Joint Movants' answer because it has provided information that assisted us in our decision-making process.

<sup>52</sup> When the Commission prescribed new CD contracts for the former FR shippers in the Capacity Allocation Proceeding, it set the capacity entitlements under these new "sculpted" CD contracts at the level historically required by each former FR shipper for each month of the year.

that the Block Capacity was existing capacity that had become available and was not new capacity requiring a new investment from El Paso.

57. The Joint Movants assert that there is no provision in the 1996 Settlement to support El Paso's claim that the FR shippers relinquished their rights to service growth commensurate with their needs, or placed such rights at the mercy of El Paso's remarketing efforts when entering the 1996 Settlement. The Joint Movants point out that the Commission already rejected this claim when it was raised by a shipper in the Capacity Allocation Proceeding that was disappointed it would not benefit from revenue credits resulting from El Paso's sales of the unsubscribed capacity.<sup>53</sup>

58. The Joint Movants state that El Paso never argued to the Commission that it should not be required to use the Block Capacity to support its contractual obligations to the converting FR shippers, nor did El Paso seek rehearing of the Commission's determinations rejecting such arguments made by others. The Joint Movants assert that El Paso's use of the Block Capacity to meet the converting FR shippers' needs was consistent with its certificate and contractual agreements.

59. In addition, the Joint Movants argue that it is a mischaracterization for El Paso to state that it was exonerated from claims that it oversold its system during the capacity shortfall. The Joint Movants point out that the Court rejected El Paso's position that it was not at fault for curtailing its firm shippers and preserved for firm shippers the right to raise the issue of El Paso's culpability for curtailments in a later proceeding.<sup>54</sup>

#### **4. El Paso's Answer**

60. El Paso argues that the Joint Movants mischaracterize and ignore prior Commission decisions relevant to the issues at hand. El Paso argues that the Commission should reject the Joint Movants' answer.<sup>55</sup>

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<sup>53</sup> Joint Movants' October 23, 2008 Answer at 4 (citing July 9 Order at P 142-43).

<sup>54</sup> *Id.* at 5 (citing *Arizona Corp. Comm'n v. El Paso Natural Gas Co.*, No. 04-1123, 2005 U.S. App. LEXIS 22751 (D.C. Cir. Oct. 20, 2005)).

<sup>55</sup> Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2009), prohibits an answer to an answer unless otherwise ordered by the decisional authority. We will accept El Paso's answer because it has provided information that assisted us in our decision-making process.

## 5. Commission Determination

61. The September 5 Order was a final order on the issues discussed therein. The Commission did not change its rationale or reverse any of its holdings in the September 5 Order. Thus, El Paso's request for rehearing of the September 5 Order on this issue is an improper request for rehearing of a final order, which is not permitted. Accordingly, the Commission could reject the El Paso rehearing petition on that basis alone. Nonetheless, for purposes of clarity and administrative transparency, the Commission will address the arguments in El Paso's request for rehearing.

62. The Commission affirms its finding in the September 5 Order that the Capacity Allocation Proceeding did not abrogate Article 11.2 of the 1996 Settlement. El Paso contends it should be excused from its obligations under Article 11.2 because the Commission's actions in the Capacity Allocation Proceeding frustrated the central purpose of the 1996 Settlement. Many of the arguments El Paso uses to support its position have already been resolved in the Capacity Allocation Proceeding and it is improper for El Paso to attempt to reargue them here. For these reasons, as discussed in greater detail below, the Commission denies El Paso's request for rehearing.

63. El Paso argues the September 5 Order asserted a new rationale for refusing to terminate Article 11.2. However, in rejecting El Paso's request for rehearing of the March 20 Order, the September 5 Order did not rely on a new justification for its decision, but instead, expanded on the reasoning underlying the March 20 Order.

64. In the March 20 Order, the Commission explained that its actions in the Capacity Allocation Proceeding were limited and that it only modified the 1996 Settlement and the FR contracts to the extent necessary to restore reliable firm service on the El Paso system and to eliminate the *pro rata* curtailments that had made firm service unreliable.<sup>56</sup> The March 20 Order explained that in adopting a surgical approach to modifying the 1996 Settlement in the Capacity Allocation Proceeding, the Commission specifically considered and rejected the argument that the entire 1996 Settlement should be abrogated because the facts and the law did not support such an outcome.<sup>57</sup> As a result, the Commission found that the Capacity Allocation Proceeding provided no basis for finding that Article 11 no longer applies.<sup>58</sup>

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<sup>56</sup> March 20 Order at P 25, 27.

<sup>57</sup> *Id.* P 27.

<sup>58</sup> *Id.* P 26.

65. The September 5 Order expanded upon this rationale. Specifically, the September 5 Order explained, in response to El Paso's request for rehearing, why its limited modification of the 1996 Settlement did not frustrate the agreement's central purpose or excuse El Paso from any of the remaining provisions, including Article 11.2. The Commission explained that El Paso's right to remarket the Block Capacity was always subject to its contractual obligation under the FR shippers' TSAs to use its existing capacity to serve their needs, as well as the obligations under section 16.3 of the 1996 Settlement and section 284.7(a)(3) to operate its pipeline in a manner that provides reliable firm service to its existing customers. Because El Paso's right to remarket the Block Capacity was never unqualified, the decision in the Capacity Allocation Proceeding to limit these sales while capacity was constrained and allocate a portion of the Block Capacity to the former FR shippers was fully consistent with El Paso's existing obligations and did not eliminate El Paso's bargain or frustrate the central purpose of the 1996 Settlement.<sup>59</sup>

66. El Paso argues that in the September 5 Order, the Commission erred in asserting that it was simply enforcing an existing obligation on the part of El Paso to serve the FR shippers' needs. El Paso states that this interpretation conflicts with the intent and purpose of the 1996 Settlement, which El Paso interprets as imposing on El Paso a continuing obligation to attempt to sell all of the unsubscribed Block Capacity, whatever the consequences for system reliability.

67. El Paso's attempt to raise issues regarding the Commission's decision to allocate a portion of the Block Capacity to the former FR shippers, and whether this decision was consistent with the intent and purpose of the 1996 Settlement, amounts to a collateral attack on the Capacity Allocation Proceeding orders. The capacity allocation methodology developed in those orders, which includes the Commission's decision to allocate the Block Capacity to FR shippers, was affirmed by the Court and cannot be questioned here.

68. Moreover, the Commission is not persuaded that the intent and purpose of the 1996 Settlement was to obligate El Paso to remarket all of the Block Capacity, regardless of the impact on El Paso's ability to provide reliable firm service. As the Commission already determined in the Capacity Allocation Proceeding, the risk-sharing arrangement in the 1996 Settlement did not insulate El Paso from its statutory and contractual obligation to take capacity constraints into consideration before selling the Block Capacity.<sup>60</sup>

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<sup>59</sup> September 5 Order at P 28-37.

<sup>60</sup> May 31 Order at 62,012; July 9 Order at P 161.

69. Nothing in the 1996 Settlement expressly requires that El Paso sell all of the Block Capacity. Sections 3.3 and 3.4 of the 1996 Settlement set forth the risk-sharing arrangement between El Paso and its shippers to address the excess unsubscribed capacity on the system. Section 3.3 provides that over the first eight years of the 1996 Settlement, shippers will pay El Paso approximately 35 percent of the fixed costs allocable to the unsubscribed Block Capacity. Section 3.4 states that El Paso must credit against this amount 35 percent of the revenues that El Paso obtains for reselling the Block Capacity. Nowhere in either of those sections does the 1996 Settlement state that El Paso *must* sell all of the unsubscribed capacity. Moreover, nowhere in the 1996 Settlement is there a requirement that El Paso remarket all of the unsubscribed Block Capacity regardless of whether it can meet the needs of its existing firm shippers.

70. As the Commission held in the Capacity Allocation Proceeding, El Paso had an ongoing obligation to serve the needs of its existing shippers.<sup>61</sup> Thus, the decision in the September 5 Order affirming this obligation is consistent with the findings in the Capacity Allocation Proceeding and does not contradict the terms or the intent of the 1996 Settlement. El Paso's attempt to raise this issue again here amounts to an impermissible collateral attack on the Capacity Allocation Proceeding orders.

71. El Paso argues it could not have had an obligation to serve the FR shippers with the Block Capacity, because if it did, the Commission would have found El Paso at fault for not fulfilling that obligation in the Capacity Allocation Proceeding. Moreover, El Paso argues that if it had such an existing obligation, there would not have been a need for the Commission to modify the 1996 Settlement. However, this argument oversimplifies the situation. Throughout the Capacity Allocation Proceeding, as well as in the September 5 Order, the Commission emphasized that when capacity became constrained on the El Paso system, El Paso's tariffs, contracts, and settlements operated to create conflicting rights and obligations,<sup>62</sup> making it almost impossible for El Paso to fulfill them all. On the one hand, El Paso's FR contracts obligated El Paso to deliver the customer's full gas requirements each day, with no stated limit. On the other hand, El Paso's CD contracts, the Commission's regulations, and section 16.3 of the 1996 Settlement, required El Paso to provide reliable firm service. In addition, the 1996 Settlement not only permitted El Paso to remarket the Block Capacity, but gave El Paso an incentive to do so by providing that El Paso would retain the majority of the remarketing revenues.

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<sup>61</sup> *Id.*

<sup>62</sup> July 9 Order at P 112; September 5 Order at P 34.

72. The rights and obligations under these various agreements worked reasonably when El Paso's system was undersubscribed. El Paso could provide the FR shippers with unlimited service, sell the Block Capacity, and guarantee its CD shippers firm service because there was sufficient capacity to meet all of these needs. However, as capacity on the system became scarce, it became apparent that El Paso's rights and obligations under these agreements conflicted. El Paso could not reasonably meet the growing demands of its FR shippers, provide reliable firm service to the CD shippers, and remarket the Block Capacity without firm service suffering grievously as a result of routine *pro rata* curtailments.

73. In the Capacity Allocation Proceeding, the Commission had to decide which of the rights and obligations in El Paso's conflicting agreements should remain and which needed to be changed. With reliable firm service as the ultimate goal in mind, the Commission adopted a remedy that required compromises by all parties. The Commission limited El Paso's ability to resell the Block Capacity when capacity was constrained, modified the FR contracts to incorporate demand limits, and allocated a portion of the Block Capacity and Expansion Capacity to the former FR shippers as part of their new CD amounts, among other things. The Commission had no choice but to modify certain of El Paso's conflicting agreements in order to protect the public interest and restore just and reasonable firm service on the system. In fashioning this remedy, the Commission helped El Paso respond to a situation that its tariff, settlements, and contracts left it unequipped to deal with.

74. Thus, in limiting El Paso's ability to remarket the Block Capacity, the Commission was enforcing an existing obligation on the part of El Paso to provide reliable firm service and meet the needs of its FR shippers. However, the Commission recognized that this obligation conflicted with El Paso's other rights and obligations, making it difficult for El Paso to respond appropriately.<sup>63</sup> Because of these conflicting agreements, the Commission chose not to fault any party for the capacity shortfall on the El Paso system, and instead focused on restoring firm service and making parties' rights and obligations clear for the future.<sup>64</sup> However, this does not mean that, during that time, El Paso was successfully fulfilling all of its obligations, including its obligation to serve the needs of its existing shippers.

75. As the Commission stated in the Capacity Allocation Proceeding, and reiterated in the September 5 Order, El Paso's contracts with its firm shippers, the Commission's

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<sup>63</sup> July 9 Order at P 112.

<sup>64</sup> May 31 Order at 62,004; July 9 Order at P 112, 126.

regulations,<sup>65</sup> and section 16.3 of the 1996 Settlement, all required El Paso to administer its pipeline in a manner that provides reliable firm service to its existing customers.<sup>66</sup> El Paso argues the September 5 Order erred in relying on section 16.3 of the 1996 Settlement because section 16.3 requires El Paso to retain sufficient facilities to meet its service obligations and has nothing to do with El Paso's capacity sales. The Commission disagrees with El Paso's narrow reading of that section. Section 16.3, which is titled "Service Obligations," requires El Paso to "maintain and operate facilities sufficient to satisfy and perform the service obligations with respect to both quality and quantity of service imposed on it" by the 1996 Settlement. The requirement that El Paso operate its facilities in a manner sufficient to satisfy and perform its service obligations under the 1996 Settlement certainly includes the requirement that El Paso use its existing facilities to meet the needs of its existing customers. This is why the Commission relied on section 16.3 in the Capacity Allocation Proceeding orders to find that El Paso could not enter into new service contracts unless it could demonstrate that it has available capacity to provide the service. The Court affirmed this decision, including the Commission's reliance on section 16.3 in making this finding, and it is improper for El Paso to raise the issue of the section 16.3 again here.

76. The same is true for El Paso's argument regarding the inapplicability of section 284.7(a)(3) of the Commission's regulations. El Paso argues it was not required under section 284.7(a)(3) to refrain from remarketing its unsubscribed capacity to avoid *pro rata* curtailments, and asserts that its *pro rata* curtailment procedures could not have violated this regulation because they were approved by the Commission earlier and remained in effect. El Paso also argues that in the 1996 Settlement the FR shippers agreed that if system capacity became constrained, a short-term solution would be *pro rata* curtailments.

77. The Commission already explained in the Capacity Allocation Proceeding orders that the routine *pro rata* curtailments on El Paso were unjust and unreasonable and not permitted under section 284.7(a)(3) of the Commission's regulations.<sup>67</sup> Regardless of

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<sup>65</sup> See 18 C.F.R. § 284.7(a)(3) (2009).

<sup>66</sup> See July 9 Order at P 112 ("El Paso has an obligation to administer its pipeline system in a manner that provides reliable firm service to its customers as set forth in Section 16.3..."); May 31 Order at 62,012 ("El Paso, with respect to its obligation to provide firm shippers with the firm service for which they have contracted, must reasonably insure the quality of firm service, and that its actions do not degrade the quality of such service.").

<sup>67</sup> May 31 Order at 62,000-62,001.

whether the FR shippers agreed to some *pro rata* curtailments and the Commission originally approved the *pro rata* curtailment procedure in El Paso's tariff, the *pro rata* curtailments that were occurring on the El Paso system at the time of the Capacity Allocation Proceeding were extreme and impairing service reliability.<sup>68</sup> As a result, the Capacity Allocation Proceeding determined that *pro rata* curtailments, as implemented on the constrained El Paso system, were unjust and unreasonable and needed to be modified.<sup>69</sup> The Commission was not persuaded that the FR shippers agreed to submit to unjust and unreasonable impairment of their firm services arising from excess use of *pro rata* curtailments. Thus, El Paso's argument that the Commission approved *pro rata* curtailments that could be applied on a routine basis without limitation is inconsistent with the Commission's findings in the Capacity Allocation Proceeding. Because the Commission already addressed this issue in the Capacity Allocation Proceeding, El Paso may not raise it again here.

78. El Paso argues that rather than allocating the Block Capacity to the former FR shippers to fulfill their new CD levels, there should have been a system expansion funded by the FR shippers. Once again, this is a collateral attack on the remedy developed in the Capacity Allocation Proceeding and approved by the Court. In the Capacity Allocation Proceeding, the Commission stated that the proper price signals for the expansion of infrastructure did not exist.<sup>70</sup> While El Paso had no incentive, or obligation,<sup>71</sup> to expand

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<sup>68</sup> *Id.*

<sup>69</sup> In the Capacity Allocation Proceeding, the Commission stated with respect to the *pro rata* curtailments occurring on El Paso:

The Commission finds... that El Paso does not have sufficient firm capacity to meet growing demand for firm service on its system, and firm service has been curtailed through *pro rata* allocations of service nominations on a routine basis.

Capacity allocation procedures that result in regular cuts in firm service are not just and reasonable. *Pro rata* allocation is an appropriate way to deal with emergency circumstances, but it cannot be a regular part of the daily scheduling process. For El Paso's capacity allocation methodology to be just and reasonable, a firm shipper must be able to reliably schedule its firm contractual entitlements without service reductions....

May 31 Order at 62,001.

<sup>70</sup> *Id.* at 61,998, 62,000.

its system to provide additional capacity for FR shippers who were not subject to an increased reservation charge, the FR shippers had no incentive to fund an expansion because El Paso was already required to meet their full service needs. Thus, while a system expansion may have prevented the capacity shortfall, the situation was one where neither El Paso nor its shippers were obligated, or had the incentive, to expand the system. Given the situation, the Capacity Allocation Proceeding required both parties to compromise, by requiring the FR shippers to limit their contracts and requiring El Paso to allocate the available Block Capacity to the former FR shippers.

79. Nor does the Commission agree that the FR shippers relinquished their rights to unlimited capacity when they entered into the 1996 Settlement. There is no provision in the 1996 Settlement supporting El Paso's claims that the FR shippers gave up any such rights, or placed them at the mercy of El Paso's remarketing efforts. On the contrary, the 1996 Settlement specifically protects the FR shippers' rights.<sup>72</sup> Moreover, this was an issue addressed in the Capacity Allocation Proceeding. Had the Commission believed the FR shippers relinquished their rights to unlimited capacity when entering the 1996 Settlement, the Commission would have found the growth in the FR shippers' needs leading up to the Capacity Allocation Proceeding to be unreasonable, which it declined to do.<sup>73</sup>

80. El Paso argues it had no obligation to serve the growing needs of the FR shippers with the Block Capacity because FR shippers' capacity rights were not unlimited. El Paso asserts its obligation to the FR shippers was limited to a quantity that was reasonably foreseeable and the growth that actually occurred could not have been foreseen. In the Capacity Allocation Proceeding, the Commission declined to state whether the growth that occurred under the FR contracts was foreseeable and instead focused on providing a remedy for the future.<sup>74</sup> However, the Commission did state that

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<sup>71</sup> *Id.* at 62,003.

<sup>72</sup> *See, e.g.*, section 9.2 of the 1996 Settlement, which states that "the rights as provided in the TSA of the Shippers to which this paragraph applies [defined as "full-requirements Shippers in El Paso's EOC market area" who have TSAs that will be terminated and converted to CD service] shall not be affected or modified by the Stipulation and Agreement unless the Shipper and El Paso mutually agree otherwise."

<sup>73</sup> July 9 Order at P 61.

<sup>74</sup> May 31 Order at 62,004 (stating that "establishing a reasonable limit on the capacity the FR customers can take in the future" is "preferable to the Commission setting a limit on the FR contracts based on its determination of what level of growth in those contracts was foreseeable and proportionate to the expectations of the parties").

the FR shippers' load growth was not unreasonable.<sup>75</sup> Moreover, El Paso itself acknowledges that the FR shippers' TSAs did not embody a stated limit on firm service and permitted some unspecified amount of growth.<sup>76</sup> Thus, the Commission is not persuaded that El Paso had no obligation to serve the FR shippers' load growth because it was unforeseeable.

81. El Paso argues that the Commission's decision in the Capacity Allocation Proceeding allocating the Block Capacity to the FR shippers and limiting El Paso's ability to remarket the Block Capacity undermined the benefits of El Paso's bargain in the 1996 Settlement. Once again, this argument raises an issue that was already resolved in the Capacity Allocation Proceeding. As the Commission made clear in the Capacity Allocation Proceeding, El Paso received substantial benefits from the 1996 Settlement.<sup>77</sup> At the outset, El Paso benefitted from the risk-sharing payments it received from shippers to cover 35 percent of the costs related to the unsubscribed capacity. El Paso also benefitted from the numerous sales of the Block Capacity it made prior to the Capacity Allocation Proceeding and continued to collect revenue from well into the future. Even after the changes imposed in the Capacity Allocation Proceeding, El Paso continued to benefit from the 1996 Settlement. El Paso retained its ability to resell the Block Capacity, so long as the sales would not degrade service to its existing customers.<sup>78</sup> El Paso also benefitted from the Commission's decision to terminate the FR contracts. After this change, El Paso was no longer subject to the FR shippers' unlimited demands for service, which it was apparent the El Paso system could not handle. Moreover, as the Commission stated in the Capacity Allocation Proceeding, all parties benefitted from reliable firm service on El Paso and from the establishment of proper market incentives for expansion of the infrastructure that resulted from the conversion of FR contracts to CD contracts.<sup>79</sup> Thus, El Paso has enjoyed and retained many benefits of the 1996 Settlement and cannot now decide that it should be excused from its ongoing obligations under Article 11.2.

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<sup>75</sup> July 9 Order at P 61.

<sup>76</sup> El Paso's October 6, 2008 Request for Rehearing at n.16.

<sup>77</sup> May 31 Order at 62,008.

<sup>78</sup> In the Capacity Allocation Proceeding, the Commission did not summarily restrict sales of Block Capacity, but determined that before making resales of existing capacity, El Paso must show that such sales will not degrade service to its existing customers. *See* July 9 Order at P 161.

<sup>79</sup> May 31 Order at 62,006.

82. Moreover, the Capacity Allocation Proceeding did not change the bargain for El Paso any more than for any other party. While El Paso's right to remarket the Block Capacity was no longer unlimited, the FR shippers lost their entitlement to unlimited service. These changes did not abrogate the entire 1996 Settlement. As the Commission explained in the Capacity Allocation Proceeding, there was no evidence that provisions of the 1996 Settlement unrelated to the provision of firm service contributed to the service disruptions on El Paso, and therefore, these other provisions remained unchanged.<sup>80</sup> The Court affirmed this decision.<sup>81</sup>

83. All parties to the Capacity Allocation Proceeding had interests to be balanced in restoring reliable firm service, and the Commission was determined to fairly hold all parties to the consequences of the bargain made in the 1996 Settlement, insofar as possible.<sup>82</sup> Thus, while the changes it made in the Capacity Allocation Proceeding were significant, they did not favor any one group or party, and the Commission finds no basis to excuse El Paso from its obligations under Article 11.2.

84. The Capacity Allocation Proceeding specifically addressed the question whether the 1996 Settlement should be terminated in its entirety. At that time, El Paso never argued to the Commission that Article 11, or any other provisions of the 1996 Settlement, should be abrogated. Rather, El Paso's position was that the bargains of the 1996 Settlement should be retained to the greatest extent possible. The Commission agreed with this position and decided to modify the 1996 Settlement in a limited manner, with any modifications focused on restoring reliable firm service on the El Paso system. The Capacity Allocation Proceeding orders did not modify Article 11.2 of the 1996 Settlement and the Court upheld the Commission's decision.<sup>83</sup> El Paso did not seek rehearing or appeal the Commission's decision on this issue.

85. Yet, now that the Capacity Allocation Proceeding remedy is implemented and the 10-year term of the 1996 Settlement has ended, El Paso maintains the Commission's actions in the Capacity Allocation Proceeding effectively excuse El Paso from its obligations under the remaining terms of the 1996 Settlement. The Commission has repeatedly rejected this argument as untimely.<sup>84</sup> El Paso argues it was not required to

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<sup>80</sup> *Id.* at 62,008.

<sup>81</sup> *Arizona Corporation Commission v. FERC*, 397 F.3d 952 (D.C. Cir. 2005).

<sup>82</sup> July 9 Order at P 180.

<sup>83</sup> *Arizona Corporation Commission v. FERC*, 397 F.3d 952 (D.C. Cir. 2005).

<sup>84</sup> March 20 Order at P 32; September 5 Order at P 30.

assert its arguments regarding the continuing applicability of Article 11.2 in the Capacity Allocation Proceeding. El Paso suggests it did not raise the issue earlier because it did not realize the matter was important at the time.<sup>85</sup> By its terms, Article 11.2 continues past the term of the 1996 Settlement.<sup>86</sup> Thus, El Paso should have known or realized the Commission's decision to modify the 1996 Settlement in a limited manner and to keep the remaining provisions, including Article 11.2, would impact El Paso in future rate proceedings. Despite this, El Paso chose not to challenge the continuing applicability of Article 11.2 in the Capacity Allocation Proceeding.

86. El Paso argues that it would have been improper to do so because Article 11.2 was not at issue in the Capacity Allocation Proceeding. However, as we have explained, the *entire* 1996 Settlement, including Article 11.2, was under Commission review in the Capacity Allocation Proceeding. The Commission ultimately decided to modify only those portions of the 1996 Settlement necessary to restore reliable firm service, but this was not a foregone conclusion. The issue of whether the 1996 Settlement as a whole should be abrogated as a result of any surgical modifications was clearly at issue, considering several parties raised this argument on rehearing of the Capacity Allocation Proceeding orders.<sup>87</sup> The bottom line is that El Paso failed to seek rehearing of the decision in the Capacity Allocation Proceeding to modify only certain portions of the 1996 Settlement, and El Paso cannot use this proceeding to revitalize rights it waived and contest its obligations under Article 11.2.

87. For these reasons, the Commission denies El Paso's request for rehearing on this issue.

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<sup>85</sup> See El Paso's October 6, 2008 Request for Rehearing at n.16 (explaining that El Paso did not raise its objections to Article 11.2 earlier because the Commission's characterization of the FR contracts as "unlimited" in the Capacity Allocation Proceeding seemed to be essentially "harmless" and because El Paso was not impacted by the Commission's decision not to modify Article 11.2 until a future rate proceeding).

<sup>86</sup> Article 11.2 states that the rate cap protections embodied in that provision will apply "in all rate proceedings following the term of [the 1996 Settlement]." Moreover, Article 2.3 of the 1996 Settlement, titled "Survival of Certain Provisions," states that "Article XI...shall remain in effect in accordance with the terms thereof following the term of this Stipulation and Agreement."

<sup>87</sup> In the Capacity Allocation Proceeding, certain parties argued that the Commission erred in not terminating the entire 1996 Settlement, but El Paso was not one of them. See May 31 Order at 62,007-08; July 9 Order at P 91-92.

**B. Application of Article 11.2(a) Rate Cap to the Block Capacity****1. September 5 Order**

88. In the September 5 Order, the Commission clarified that the Article 11.2 rate cap applies to Block Capacity, which the Commission allocated to the former FR shippers in the Capacity Allocation Proceeding. The Commission stated that the focus of the rate cap in Article 11.2(a) of the 1996 Settlement was the *service obligation*, and not the *capacity* used to meet that obligation and, therefore, the type of capacity is not determinative of whether the Article 11.2 rate cap applies. The Commission explained that when El Paso provided service to meet the FR shippers' unlimited demands, it did so under their 1995 TSAs, which were covered by the Article 11.2 rate cap, regardless of what type of capacity was used.

89. Moreover, the Commission stated that if the parties intended the Article 11.2 rate cap to apply only to non-Block Capacity, they could have drafted the 1996 Settlement to provide as much. The Commission explained that the 1996 Settlement distinguishes between capacity in existence on December 31, 1995 and new capacity built afterwards, but does not indicate that any portion of the pre-December 31, 1995 capacity should be treated differently than the rest with regard to FR service. Thus, the Commission concluded that the Expansion Capacity, which is not covered by the Article 11.2 rate cap, is not analogous to Block Capacity. The Commission stated that while El Paso was under no obligation to expand its system to meet the demands of the FR shippers, it did have an obligation to serve its current customers with the capacity on its existing system, regardless of whether the capacity needed for that purpose was a part of the former Block Capacity.

90. The Commission also rejected El Paso's argument that in the Capacity Allocation Proceeding, the Commission gave the FR shippers Block Capacity in lieu of requiring them to pay for a system expansion. The Commission reiterated its Capacity Allocation Proceeding holding that the FR shippers were entitled to existing capacity on the El Paso system to serve their growth in demand. The Commission stated that holding El Paso to its obligation to serve its firm shippers' needs with existing capacity is different from ordering a pipeline or a shipper to pay for an expansion, which the Commission could not and did not do.

**2. El Paso's Request for Rehearing**

91. El Paso argues that the Commission erred by ruling that the Article 11.2(a) rate caps apply to Block Capacity. El Paso states that the Commission addressed this issue for the first time in the September 5 Order. El Paso asserts that, by applying the Article 11.2 rate cap to Block Capacity, the Commission gave the former FR shippers an undeserved free ride by allowing them to meet load growth with Article 11.2 rate-capped capacity rather than uncapped Expansion Capacity. El Paso states that, while the

Commission claims that El Paso had an obligation to use its unsubscribed Block Capacity to serve FR growth and has found that the Article 11.2 rate cap applies when the Block Capacity is used for that purpose, the Commission overlooks the fact that the Block Capacity was used for the FR shippers only because the Commission ordered El Paso to cease making sales of the Block Capacity to others. El Paso contends that it was the Commission's directive, and not El Paso settlements and contracts, that required El Paso to use the Block Capacity for the FR shippers. El Paso states that the Block Capacity was only available due to the coincident bankruptcy of Enron Corporation, which resulted in the return of a significant quantity of capacity to El Paso at just the moment the Commission was addressing the issue of the FR shippers' capacity needs.

92. El Paso contends (as discussed *supra*) that the Commission's present view that El Paso was required, when confronted with continuing *pro rata* curtailments, to refrain from reselling the Block Capacity to other shippers and allocate it instead to the FR shippers, is inconsistent with prior Commission orders. El Paso states that in those prior orders, the Commission recognized that *pro rata* curtailments were a permissible aspect of FR service.<sup>88</sup> Moreover, El Paso contends that in the Capacity Allocation Proceeding, the Commission rejected the FR shippers' claim that El Paso had an obligation to expand its system at its own expense and additionally held that El Paso was not required to reserve Block Capacity to meet the FR shippers' needs.

93. El Paso further states that the Commission erred by finding that El Paso failed to provide evidence that the former FR shippers refused to support a system expansion to serve their needs. El Paso states that the Commission previously found in the Capacity Allocation Proceeding that the FR shippers refused to pay for an expansion to serve their growth.<sup>89</sup> El Paso argues that the Commission's decision to allocate Block Capacity to the FR shippers saved them from the full consequences of refusing to support an expansion. El Paso contends that the Commission's remedial action of allocating the Block Capacity to the former FR shippers does not, however, justify the further relief of applying the Article 11.2 rate cap to that capacity. El Paso asserts that it has already contributed approximately \$300 million of Block and Expansion Capacity to help restore reliability on its system, even though the Commission correctly found that it had not violated its service obligations. El Paso concludes it is unjust and unreasonable to give the FR shippers a further windfall by applying the Article 11.2 rate cap to the Block

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<sup>88</sup> El Paso's October 6, 2008 Request for Rehearing at 33-36 (citing *El Paso Natural Gas Co.*, 54 FERC ¶ 61,316, at 61,923-24 (1991); July 9 Order at P 103, 126-127).

<sup>89</sup> *Id.* at 36-37 (citing July 9 Order at n.103 ("The FR shippers have declined to contribute to expansions to serve their needs.")).

Capacity, which El Paso argues they were not entitled to under the terms of the 1990 and 1996 Settlements.

94. In addition, El Paso argues that the substitution of sculpted CD contracts for FR contracts in the Capacity Allocation Proceeding fundamentally altered those agreements so that they were no longer eligible for Article 11.2(a) rate cap treatment. El Paso argues that the focus of Article 11.2 is the *TSA*, not the *service obligation* under that TSA, as the September 5 Order held. El Paso argues that because the Commission changed the form of the FR shippers' TSAs by converting them to CD contracts in the Capacity Allocation Proceeding, the former FR shippers should be disqualified from benefiting from the rate cap under Article 11.2. El Paso states that Article 11.2 provides that the rate cap will continue to apply to TSAs that have been amended, but only if the amendment is one to which the contracting parties have consented. El Paso asserts that changes ordered by the Commission are not the sort of bilateral change that was contemplated.

95. El Paso further argues that, because the sculpted CD contracts awarded capacity to the former FR shippers in high-value months, leaving El Paso to remarket the capacity in low-value months, the consequence was a general devaluation of El Paso's remaining unsubscribed capacity and an increase in the likelihood that the capacity would remain unsubscribed. El Paso argues that given these changes, the Commission's finding in the September 5 Order that the changes it made in the Capacity Allocation Proceeding have no effect on El Paso's obligation to apply the Article 11.2 rate cap is erroneous and must be reversed.

96. El Paso also argues the Commission misunderstood El Paso's proposal to apply the California rate cap to the Block Capacity and erred in rejecting the proposal. El Paso states that the September 5 Order characterized El Paso's proposal as an attempt to apply the California maximum rate to the Block Capacity. El Paso clarifies that it is proposing to apply the California *rate cap*, not the California *rate*, to the Block Capacity, if it is otherwise lower than the applicable EOC zone rate. El Paso states that if the applicable non-Article 11.2 EOC zone rate is lower than the California rate cap, then El Paso would charge EOC shippers holding the Block Capacity the applicable EOC zone rate, depending on each shipper's zone of delivery. However, if the applicable non-Article 11.2 EOC zone rate is higher than the California rate cap, then El Paso states that it will only charge up to the California rate cap.

97. El Paso argues that if any rate cap is to apply to the Block Capacity, the only cap that makes sense is the California rate cap. El Paso states that although it agreed in the 1996 Settlement to bear most of the risk of remarketing the Block Capacity, it did not agree to assume the risk that a lower EOC rate cap would ever apply to the Block Capacity. El Paso asserts that applying a lower EOC rate cap to the Block Capacity imposes far greater risks on El Paso than it agreed to under the 1996 Settlement.

98. El Paso argues the Commission's statement that "there is no 'California capacity' on El Paso's system" misstates the issue. El Paso contends that the question is not whether the capacity is being used in a particular zone, but what rate cap most nearly achieves the intent of the 1996 Settlement now that the capacity has been awarded to EOC shippers. El Paso asserts that the Block Capacity allocated to the FR shippers in the Capacity Allocation Proceeding was associated with the California rate zone and, thus, if a rate cap applies, it must be the California rate cap.<sup>90</sup> El Paso contends that, as long as the EOC rates remain lower than the California rate, applying an EOC rate cap to the Block Capacity would permanently relegate the capacity to a rate that reflects less than the allocated costs of the capacity, in direct conflict with the 1996 Settlement.

99. El Paso further argues that the FR shippers already received greatly subsidized capacity during the last two years of the 1996 Settlement due to the fact that El Paso was required to give them 1 Bcf/day of Block and Expansion Capacity. Thus, El Paso argues that from September 1, 2003 (the implementation date of the Capacity Allocation Proceeding remedy), through December 31, 2005 (the expiration of the 1996 Settlement), the former FR shippers paid effective unit rates far below even the EOC maximum tariff rates. El Paso argues that it is arbitrary to require El Paso to provide them with a further windfall by applying a lower EOC zone rate cap to Block Capacity, which they agreed to treat as California capacity in the 1996 Settlement. El Paso concludes that the September 5 Order erroneously rejects El Paso's arguments on this point based on its misconception that El Paso was attempting to charge the California rate for service to the former FR shippers' EOC delivery points. El Paso thus requests that the Commission grant rehearing on this issue.

### **3. Joint Movants' Answer**

100. The Joint Movants contend the Commission did not force El Paso to use sculpted CD contracts for the former FR shippers. The Joint Movants state that the new CD contracts were developed by shippers and El Paso working cooperatively. The Joint Movants argue that the use of Block Capacity and sculpted CD contracts to serve FR shippers was a plan developed during the Capacity Allocation Proceeding through a give and take negotiation between shippers and El Paso.<sup>91</sup> The Joint Movants conclude that it is inaccurate for El Paso to portray these remedies as mandated by the Commission.

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<sup>90</sup> El Paso states that the rate caps are simply the 1996 Settlement rates (escalated for inflation) determined for each rate zone.

<sup>91</sup> Joint Movants' October 23, 2008 Answer at 6 (citing May 31 Order at 62,010).

#### 4. Commission Determination

101. The Commission affirms its decision that the Article 11.2 rate cap applies to Block Capacity and that the appropriate rate cap is the delivery zone rate cap. In the September 5 Order, the Commission clarified the March 20 Order and rejected El Paso's arguments that the Article 11.2 rate cap should not apply to the Block Capacity. El Paso's request for rehearing raises the same basic argument the Commission rejected in the September 5 Order. However, for purposes of clarity, we will address El Paso's arguments.

102. El Paso asserts that by applying the Article 11.2 rate cap to Block Capacity, the Commission gave the former FR shippers an undeserved free ride by allowing them to meet load growth with rate-capped capacity rather than uncapped Expansion Capacity. The Commission disagrees. In the Capacity Allocation Proceeding, the Commission found that El Paso did not have sufficient capacity to meet the firm service demands of its shippers and that additional capacity was needed to provide reliable firm service to El Paso's CD shippers, as well as the former FR shippers.<sup>92</sup> El Paso offered to use its Expansion Capacity to provide firm service for the former FR shippers at no cost through the term of the 1996 Settlement.<sup>93</sup> Because not all of the Expansion Capacity was in service at the time and because the Expansion Capacity was not enough to entirely resolve the capacity shortage, additional capacity was needed. Fortunately, a certain amount of Block Capacity was turned back to El Paso during that time and the Commission directed El Paso to use that capacity to meet the current firm service needs of its former FR shippers. Thus, both the Expansion Capacity and the turned-back Block Capacity were needed to meet existing firm service obligations.

103. El Paso argues that the Block Capacity was used for the FR shippers only because the Commission ordered El Paso to cease making sales of Block Capacity to others. Whether it was appropriate for the Commission to allocate a portion of the Block Capacity to the FR shippers in the Capacity Allocation Proceeding is not at issue here because that decision has been affirmed by the Court. Moreover, in making this argument, El Paso seems to be asserting that, if the Commission had not stepped in, El Paso would have resold the turnback capacity, despite having insufficient capacity to serve its existing firm shippers, thereby exacerbating a capacity crisis on El Paso's system. It is precisely for this reason that it was in the public interest for the Commission in the Capacity Allocation Proceeding to relieve El Paso from its perceived obligation to remarket the Block Capacity without consideration of the other needs on the system.

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<sup>92</sup> May 31 Order at 61,998, 62,011-62,012.

<sup>93</sup> *See id.* at 62,011-12.

104. As explained above, El Paso's tariff, contracts, and settlements operated in conflict with one another when the system was constrained. Thus, to restore reliable service, the Commission stepped in to clarify certain rights and obligations (e.g., El Paso's obligation to provide firm service to meet the full daily demand of the FR shippers) and to modify others (e.g., El Paso's ability to remarket Block Capacity). When the Block Capacity became unsubscribed, the Commission acted to ensure that this capacity would be used to restore reliable firm service. In doing so, the Commission did not order El Paso to cease remarketing the Block Capacity unconditionally. To the contrary, the Commission directed El Paso not to remarket Block Capacity unless it could demonstrate that it had available capacity to provide service.<sup>94</sup> The turned-back Block Capacity was clearly needed to provide existing service to the FR shippers and thus was not available to be resold. In other words, the Commission found in the Capacity Allocation Proceeding that El Paso's service obligation under its FR contracts prevented the remarketing of the capacity. Having allocated the Block Capacity to the former FR shippers in the Capacity Allocation Proceeding, it was reasonable for the Commission to find that when El Paso serves those former FR shippers with the Block Capacity, the Article 11.2(a) rate cap applies. The Block Capacity was existing system capacity that the Commission allocated to the former FR shippers as part of their existing contract service in the Capacity Allocation Proceeding.<sup>95</sup> As such, it became part of the service provided under their converted FR contracts and was no different than service provided over other segments of existing capacity.<sup>96</sup> When the 1996 Settlement terminated on December 31, 2005, Block Capacity as a separately-identified class of capacity ceased to exist and the turned-back Block Capacity became indistinguishable from the other segments of capacity that comprised El Paso's system at the time of the Capacity Allocation Proceeding. Therefore, the Commission's finding that the Article 11.2 rate cap applies to Block Capacity is consistent with the Commission's findings in the Capacity Allocation Proceeding.

105. In the Capacity Allocation Proceeding, the Commission accepted El Paso's offer to provide the Expansion Capacity to the FR shippers at no cost through the term of the 1996 Settlement and additionally directed El Paso to use the turned-back Block Capacity

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<sup>94</sup> See *id.* at 60,012; July 9 Order at P 161.

<sup>95</sup> July 9 Order at P 171.

<sup>96</sup> See March 20 Order (stating that "it is consistent with the language of the [1996] Settlement, its purpose, and its regulatory context to interpret the section 11.2(a) rate cap as being limited to service El Paso could provide FR customers at the time of the 1996 Settlement with its system as it then existed").

for the former FR shippers.<sup>97</sup> The Commission made clear in the Capacity Allocation Proceeding, as well as in the certificate proceedings for the Expansion Capacity, that while it was accepting El Paso's commitment to offer the Expansion Capacity at no charge through the term of the 1996 Settlement, the former FR shippers would be required to bear the cost of the Expansion Capacity after the term of the 1996 Settlement.<sup>98</sup> The Commission did not make a similar statement regarding the Block Capacity because, once the Block Capacity was allocated to the FR shippers, it was no different than capacity provided by other segments of El Paso's existing non-Expansion Capacity.

106. El Paso argues the Commission's finding that El Paso was required to refrain from reselling the Block Capacity when confronted with *pro rata* curtailments is inconsistent with prior orders wherein the Commission recognized that *pro rata* curtailments were sometimes needed. This is an issue that was already resolved in the Capacity Allocation Proceeding and cannot be reargued here. The Commission held in the Capacity Allocation Proceeding orders that *pro rata* curtailments were permissible on an occasional basis, but when such curtailments became a regular part of the daily scheduling process, they resulted in unreliable firm service and were no longer just and reasonable.<sup>99</sup> The Capacity Allocation Proceeding also found that *pro rata* curtailments in capacity constrained conditions were antithetical to other provisions of El Paso's tariff, contracts, and settlements.<sup>100</sup> Thus, simply because El Paso's *pro rata* curtailment procedures were originally accepted by the Commission and were implemented on occasion without problem for a period, does not mean that El Paso's quotidian implementation of these procedures once capacity became constrained was acceptable. Because this issue was already decided in the Capacity Allocation Proceeding, the Commission rejects El Paso's argument concerning its *pro rata* curtailment provisions.

107. El Paso further argues that the holdings in the September 5 Order are inconsistent with the Commission's findings in the Capacity Allocation Proceeding that El Paso was not required to reserve Block Capacity to meet the FR shippers' needs. However, the Commission never stated in the September 5 Order that El Paso was required to *reserve* Block Capacity for the FR shippers. Rather, the Commission reiterated the finding in the Capacity Allocation Proceeding that, if unsubscribed Block Capacity was needed to serve

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<sup>97</sup> May 31 Order at 62,009, 62,012.

<sup>98</sup> July 9 Order at P 109.

<sup>99</sup> See May 31 Order at 62,001.

<sup>100</sup> See July 9 Order at P 112.

existing firm shippers, it could not be resold. Thus, the Commission has never imposed on El Paso an obligation to hold Block Capacity for future FR service, but the Commission has required El Paso to ensure that its existing capacity needs were satisfied before remarketing any remaining available capacity.

108. The Commission does not consider the application of the rate cap to the Block Capacity allocated to the FR shippers to be a “windfall” or an “undeserved free ride.” As was fully addressed in the Capacity Allocation Proceeding, and affirmed by the Court, the Commission’s actions in the Capacity Allocation Proceeding (including allocating Block Capacity to FR shippers to meet their existing firm service needs) were necessary to restore reliable service on El Paso’s system. In crafting its remedy, the Commission balanced the interests of all the parties and preserved the benefits of the 1996 Settlement to the fullest extent possible. There may have been other ways to balance these interests, but the Commission’s approach was just, reasonable, and has been affirmed on judicial review. As a result of the Capacity Allocation Proceeding, El Paso benefitted from the restoration of reliable service on its system, the elimination of the unlimited growth of the rate-capped FR demand by the conversion of those contracts to CD contracts, and the ability to continue to reap the benefits of the already remarketed Block Capacity under the 1996 Settlement. El Paso voluntarily offered the Expansion Capacity at no cost to the FR shippers during the 1996 Settlement. The orders adopting that remedy and balancing of interests in the Capacity Allocation Proceeding are now final, having already been appealed and affirmed by the Court. El Paso’s attempt to resurrect arguments about the costs it bore as a result of that remedy is therefore rejected.

109. As the Commission has previously stated, Article 11.2(a) applies to non-Expansion Capacity service under the former FR contracts.<sup>101</sup> Article 11.2 makes clear that the rate caps in that provision apply to firm TSAs in effect on December 31, 1995, that remain in effect beyond January 1, 2006. The Commission found that the Article 11.2 rate caps apply to the converted FR contracts that were in effect on December 31, 1995 and remained in effect beyond January 1, 2006, with the exception of the Expansion Capacity, which was provided at a special zero-rate during the remainder of the 1996 Settlement.<sup>102</sup> Service under those converted FR contracts included the Block Capacity as well as service provided over other existing facilities (i.e., the 1995 Capacity). Because the applicability of Article 11.2 rate caps is tied to an eligible TSA, and not to a type of capacity, it is irrelevant whether the service flows through former Block Capacity or other 1995 Capacity. As the Commission stated in the September 5 Order, “the

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<sup>101</sup> March 20 Order at P 68-69; September 5 Order at P 72-79.

<sup>102</sup> September 5 Order at P 45.

capacity used to provide that service is not determinative of whether the rate cap applies.”<sup>103</sup>

110. El Paso argues that because the Commission changed the form of the FR shippers’ TSAs by converting them to CD contracts in the Capacity Allocation Proceeding, the former FR shippers should be disqualified from benefiting from the rate cap under Article 11.2. We disagree that the changes the Commission made to the FR contracts in the Capacity Allocation Proceeding revoke those shippers’ eligibility for the Article 11.2 rate cap. The Commission addressed and rejected this same basic argument by El Paso in the March 20 Order.<sup>104</sup> The Commission explained that in the Capacity Allocation Proceeding, it converted the FR contracts to CD contracts, but did not cancel, terminate, or abrogate those contracts.<sup>105</sup> The converted CD contracts allow a continuation of the same firm service that the shippers received under their FR contracts notwithstanding the change to a CD basis ordered by the Commission.<sup>106</sup> The Commission therefore found that the converted contracts are “amended” contracts within the meaning of the 1996 Settlement.<sup>107</sup> El Paso did not seek rehearing of the March 20 Order on this issue, and so cannot raise the issue here.

111. The Commission also finds unpersuasive El Paso’s argument that El Paso and its shippers must mutually agree to a contract amendment for Article 11.2 to apply to an amended contract. Article 11.2 states:

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 (emphasis added).

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<sup>103</sup> *Id.* P 53 (footnote omitted).

<sup>104</sup> March 20 Order at P 38-41. El Paso argued that the Commission abrogated the FR contracts by converting them to CD contracts and that Article 11.2 no longer applied to these “new” contracts.

<sup>105</sup> *Id.* P 39.

<sup>106</sup> *Id.* See also July 9 Order at P 119 (stating that after the contract conversion, the FR customers will receive service that is comparable to the service they have been receiving under the FR contracts in terms of the quantity of service they receive).

<sup>107</sup> March 20 Order at P 39.

112. There is no requirement in Article 11.2 that El Paso and its shippers must agree to amend the FR contracts into CD contracts in order for the Article 11.2 rate cap to continue to apply to the contract “as amended.” The Commission effectively amended the FR shippers’ TSAs in the Capacity Allocation Proceeding, and the Commission finds that the Article 11.2 rate cap continues to apply to these TSAs, as amended. Moreover, as stated in the March 20 Order, conversion of the FR contracts to CD contracts was specifically contemplated by the 1996 Settlement.<sup>108</sup> Article 9.2 of the 1996 Settlement gave the FR shippers the option of converting to CD service. Thus, the conversion of FR service was not unforeseen by the 1996 Settlement and such conversion did not eliminate those shippers’ protections under Article 11.2.<sup>109</sup>

113. Similarly, the Commission finds that its conversion of FR contracts to sculpted CD contracts did not eliminate the Article 11.2 protections for these shippers. Because of the limited availability of system capacity to meet El Paso’s firm shippers’ needs, it was necessary to allocate capacity to the former FR shippers on a varying monthly basis. Without sculpting, El Paso would not have had sufficient capacity to meet the needs of all its firm shippers. Thus, the Commission effectively amended the FR contracts in the Capacity Allocation Proceeding, not only to convert them to CD contracts, but to modify the monthly CDs under those contracts. The Article 11.2 rate cap continues to apply to those TSAs, as amended. Thus, the Commission finds unpersuasive El Paso’s argument that its rights and obligations under the 1996 Settlement were materially and unreasonably altered by sculpting of CD contracts in the Capacity Allocation Proceeding.

114. The idea of sculpted CD contracts was developed in discussions between El Paso and the shippers in the Capacity Allocation Proceeding. When the parties were unable to agree to a capacity allocation methodology, the Commission developed a capacity allocation methodology that incorporated the ideas and suggestions of the parties, such as the sculpted CD contracts. Thus, while El Paso may not have supported the specific sculpting methodology ultimately ordered by the Commission, it did offer to provide sculpting to its shippers during the Capacity Allocation Proceeding.<sup>110</sup> Moreover, at the time of the Capacity Allocation Proceeding, the impact of sculpted contracts on El Paso’s ability to remarket the Block Capacity in the future was speculative. That potential

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<sup>108</sup> *Id.* P 40.

<sup>109</sup> *Id.* n.24 (stating that in light of Article 9.2, nothing assured El Paso that the FR shippers would remain FR shippers through the term of the 1996 Settlement).

<sup>110</sup> *See* May 31 Order, 99 FERC ¶ 61,244 at 62,010 (stating that El Paso “offered, at the April 16 conference, to work with its shippers to ‘sculpt’ (incorporate seasonal variations into) the FR entitlement allocations”).

impact was but one compromise of many in the Capacity Allocation Proceeding and was necessary to restore firm reliable service to El Paso's system. The Commission's remedy, including the sculpted contracts, was affirmed by the Court. Given this context, El Paso overstates matters when it argues that the sculpted CD contracts eliminated the essential bargain of the 1996 Settlement, excusing it from Article 11.2, especially since El Paso never raised such an argument or took such a position in the Capacity Allocation Proceeding when the Commission was implementing these changes.

115. El Paso argues that if the Commission applies any rate cap to the Block Capacity, it should be the California rate cap. El Paso asserts the Commission misunderstood El Paso's proposal to apply the California rate cap to the Block Capacity in the September 5 Order and erred in rejecting the proposal. El Paso further argues that the question is not whether the capacity is being used in a particular zone, but what rate cap most nearly achieves the intent of the 1996 Settlement now that the capacity has been awarded to non-California shippers. El Paso contends that applying an EOC rate cap to the Block Capacity would permanently relegate the capacity to a rate that reflects less than the allocated costs of the capacity, contrary to the intent of the 1996 Settlement.

116. The Commission understands El Paso sought to charge California-related rates, but disagrees. Whatever California rate El Paso may have proposed to charge for the former Block Capacity is irrelevant for portions of the Block Capacity that do not have California delivery points. The Commission explained both in the September 5 Order, as well as in the Capacity Allocation Proceeding, that there is no "California capacity,"<sup>111</sup> and the rate for the Block Capacity will be the rate applicable to the shipper's receipt points, not the rate that a former shipper paid. The Commission's clarification in the September 5 Order regarding Block Capacity is consistent with the findings in the March 20 Order and prior Commission orders, and we deny rehearing. Any other issues raised here related to El Paso's ability to recover its cost of service through its rates are properly addressed in the current rate case proceeding in Docket No. RP08-426-000.

**C. Discount Adjustment and Article 11.2(b)**

**1. Background**

117. In its pleadings on the technical conference, El Paso argued that if the Commission determined that Article 11.2 continues to apply, El Paso has the right to reallocate costs it cannot recover from the Article 11.2-protected shippers to other shippers, or to contracts that are not covered by Article 11.2, through a discount adjustment.

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<sup>111</sup> July 9 Order at P 141 (stating that "nothing in the NGA or in El Paso's contracts with its shippers establishes a 'certificated obligation to serve California'").

118. Several parties responded that El Paso should be at risk for the Article 11.2 rates and should not be permitted to recover from other shippers the costs it cannot recover under Article 11.2(a). They argued that pursuant to Article 11.2(b), El Paso agreed to relinquish its right to a reasonable opportunity to recover its costs, to the extent that costs exceed the revenue garnered by the capped rates under Article 11.2(a). Parties further argued that Article 11.2(a) capped rates are not discounted rates, but negotiated rates for which no discount is available.

119. In the March 20 Order, the Commission stated that nothing in the 1996 Settlement precludes El Paso from proposing to price its services so that it could recover its costs from other shippers to the extent that Article 11.2 rates would not recover its cost of service.<sup>112</sup> The Commission stated that it does not read Article 11.2(b) as providing any guarantees to non-parties to the 1996 Settlement. The Commission stated that to the extent El Paso proposes to include a discount adjustment in its rates, that proposal will be evaluated at the hearing pursuant to the Commission's selective discount policy.<sup>113</sup>

## 2. September 5 Order

120. In response to the March 20 Order, Southwest Gas requested the Commission to clarify that El Paso may not 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.

121. The September 5 Order clarified that any discount adjustment 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).<sup>114</sup>

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<sup>112</sup> March 20 Order at P 92.

<sup>113</sup> *Id.* P 93 (citing *Policy for Selective Discounting for Natural Gas Pipelines*, 111 FERC ¶ 61,173 (2005), *reh'g denied*, 113 FERC ¶ 61,173 (2005)). Under the Commission's discount policy, the pipeline has the ultimate burden of showing that any discount for which it seeks an adjustment is necessary to meet competition. *See* 111 FERC ¶ 61,173 at P 59-661; 113 FERC ¶ 61,173 at P 104-105.

<sup>114</sup> September 5 Order at P 120.

### 3. Gila River and New Harquahala's Request

122. Gila River and New Harquahala argue that the September 5 Order erred by allowing El Paso to propose shifting costs related to the 1995 Capacity to shippers. Gila River and New Harquahala assert that given the plain meaning of the language in Article 11.2(b), El Paso may not shift, or propose to shift, any of the cost responsibility associated with its 1995 system to any of its shippers through a discount adjustment. Gila River and New Harquahala argue that Article 11.2(b) requires El Paso to assume full cost responsibility for any 1995 Capacity if underutilized by virtue of any step-downs or contract terminations related to the 1995 Capacity.<sup>115</sup>

123. Gila River and New Harquahala state that if the Commission finds it did not err in holding that El Paso may shift costs associated with the 1995 Capacity to its shippers, the Commission should find that it erred in stating that El Paso could shift those costs only to shippers who were not parties to the 1996 Settlement. Gila River and New Harquahala argue this decision is contrary to the March 20 Order, the remainder of the September 5 Order, and the plain language of Article 11.2.<sup>116</sup> Gila River and New Harquahala state that Article 11.2(b) unequivocally provides rate cap protection to only those customers that have Article 11.2(a) contracts which remain in effect, not to signatories of the 1996 Settlement if they no longer have any such contracts. Gila River and New Harquahala explain that several shippers who were parties to the 1996 Settlement no longer have rate cap contracts and thus are no longer “eligible shippers” under Article 11. Gila River and New Harquahala argue that any discount adjustment should apply to them as well.

124. Gila River and New Harquahala assert that applying a discount adjustment only to non-parties to the 1996 Settlement is unduly discriminatory. Gila River and New Harquahala argue the Commission must ensure that non-parties to the 1996 Settlement (i.e., those who were not around at the time it was entered into and, therefore, had no opportunity to protect themselves from Article 11.2) do not bear the brunt of the burden of the 1996 Settlement.

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<sup>115</sup> Article 11.2(b) states, in relevant part:

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).

<sup>116</sup> Gila River and New Harquahala's October 6, 2008 Request for Rehearing at 8-9 (citing March 20 Order at P 58; September 5 Order at P 118).

125. Gila River and New Harquahala state that a number of issues pending in El Paso's most recent rate case in Docket No. RP08-426 may moot the need to address this issue. The parties explain that in Docket No. RP08-426, El Paso demonstrated that it has subscribed enough firm capacity at the appropriate rates to satisfy the 4,000 MMcf/d threshold the Commission established in the March 20 Order and affirmed in the September 5 Order.<sup>117</sup> Gila River and New Harquahala state that if El Paso has satisfied the 4,000 MMcf/d threshold, then there will be no costs to shift under Article 11.2(b), and the issue of whether, and to whom, El Paso may shift 1995 system costs is moot. In addition, Gila River and New Harquahala state that a favorable ruling on either of the following issues that are also pending in Docket No. RP08-426 would also moot the need to resolve the discount adjustment issue: (1) whether El Paso has failed to satisfy its burden of proving that Article 11.2 satisfies the discount adjustment policy; and (2) whether Article 11.2(b) is unjust, unreasonable, unduly discriminatory, anti-competitive, and against the public interest.

#### **4. Commission Determination**

126. The Commission will provide clarification on this issue. Parties have raised concerns about two types of costs that El Paso may propose to shift to its shippers through a discount adjustment. The first category includes the costs El Paso is unable to recover from Article 11.2(a) shippers as a result of their capped rates. The second category includes costs related to any unsubscribed or discounted 1995 Capacity.

127. The Commission addressed whether El Paso could propose a discount adjustment to recover the first category of costs in the March 20 Order.<sup>118</sup> As we stated there, nothing in Article 11 prevents El Paso from proposing a discount adjustment to recover costs it cannot recover from the Article 11.2(a) shippers as a result of their capped rates.<sup>119</sup> Necessarily, any such discount adjustment may not shift costs to shippers with Article 11.2(a) capped rates. However, signatories to the 1996 Settlement who no longer have an Article 11.2(a) contract remaining in effect would share the cost of any such discount adjustment with non-signatories to the 1996 Settlement (i.e., shippers with post-1995 TSAs).

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<sup>117</sup> In the March 20 Order, the Commission stated that in determining whether specific capacity was part of El Paso's 1995 system for the purposes of Article 11.2(b), the Commission will presume the first 4,000 MMcf/d of firm subscribed capacity on El Paso's system is 1995 Capacity. *See* March 20 Order at 56-63.

<sup>118</sup> March 20 Order at P 92-93.

<sup>119</sup> *Id.* P 92.

128. This is not to say a discount adjustment to recover the costs El Paso cannot recover from the Article 11.2(a) shippers will necessarily be accepted. Any discount adjustment El Paso proposes will be evaluated at the hearing in El Paso's current rate case in Docket No. RP08-426 pursuant to the Commission's discount policy.<sup>120</sup>

129. With respect to the second category of costs, which is the subject of Gila River and New Harquahala's request, Article 11.2(b) prohibits El Paso from shifting costs related to any unsubscribed or discounted 1995 Capacity to any shippers to which Article 11.2 applies (i.e., firm shippers with at least one TSA that was in effect on December 31, 1995 and remains in effect).<sup>121</sup> Thus, as we made clear in the March 20 Order, El Paso cannot propose a discount adjustment shifting costs related to any unsubscribed or discounted 1995 Capacity to shippers who still have at least one effective Article 11.2(a) rate-capped contract.<sup>122</sup>

130. Gila River and New Harquahala argue El Paso should not be permitted to propose a discount adjustment shifting 1995 Capacity costs to any of its shippers (non-Article 11.2 or otherwise). The Commission finds this issue is not ripe for review. In the March 20 Order, the Commission addressed the issue of whether El Paso could propose a discount adjustment to recover the first category of costs (i.e., costs it could not recover from the Article 11.2(a) shippers) because El Paso proposed such a discount adjustment there. However, El Paso has not proposed in this proceeding a discount adjustment shifting costs related to the 1995 Capacity to its shippers. Should El Paso propose such a discount adjustment in its current rate case in Docket No. RP08-426-000, the Commission will address the issue there.

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<sup>120</sup> See *Policy for Selective Discounting for Natural Gas Pipelines*, 111 FERC ¶ 61,173 (2005), *reh'g denied*, 113 FERC ¶ 61,173 (2005).

<sup>121</sup> Article 11.2(b) states, in relevant part:

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... that becomes unsubscribed or is subscribed at less than the maximum applicable tariff rate...

<sup>122</sup> March 20 Order at P 58.

The Commission orders:

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

By the Commission. Commissioners Spitzer and Moeller are not participating.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.