

136 FERC ¶ 61,222
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Midcontinent Express Pipeline LLC

Docket No. CP08-6-007

Enogex Inc.

Docket No. CP08-9-003

ORDER DENYING REHEARING OF ORDER ON REMAND

(Issued September 29, 2011)

1. In response to the decision of the United States Court of Appeals for the District of Columbia Circuit in *Apache Corporation v. FERC* (*Apache Corp. v. FERC*),¹ the Commission issued an order on remand on March 3, 2011 (Order on Remand)² clarifying and reaffirming the prior Commission orders in this proceeding. A timely request for rehearing of the Order on Remand was filed by Apache Corporation (Apache). As discussed below, we will deny rehearing.

I. Background

A. The Certificate Order (July 25, 2008 Order)

2. On July 25, 2008, the Commission issued an order that granted Midcontinent Express Pipeline LLC (Midcontinent) a certificate to construct a new 506-mile long interstate pipeline from southeastern Oklahoma to western Alabama. The July 25, 2008 Order also granted certificate authorization for Enogex Inc. (Enogex) to lease 272,000 Dth/d of capacity in its intrastate pipeline system to Midcontinent.³ Enogex operates an extensive, web-like configuration of pipeline facilities that access Oklahoma

¹ 627 F.3d 1220 (D.C. Cir. 2010).

² *Midcontinent Express Pipeline LLC*, 134 FERC ¶ 61,155 (2011).

³ *Midcontinent Express Pipeline LLC*, 124 FERC ¶ 61,089 (2008).

gas production from numerous wells and gathering facilities. Enogex's certificate conditions require it to operate the leased capacity in a manner that ensures Midcontinent's ability to provide its shippers with NGA-jurisdictional interstate transportation services on an open-access basis. Thus, the lease agreement enables Midcontinent to assure its shippers of firm deliveries of Oklahoma gas production from receipt points on Enogex's system (Waynoka, West Pool, and East Pool) as specified in the lease.

3. In the July 25, 2008 Order, the Commission addressed Apache's protest that the lease of capacity from Enogex to Midcontinent, in concert with Enogex's lease of capacity to Gulf Crossing Pipeline Company, LLC (Gulf Crossing),⁴ would impair Apache's rights as a shipper with an existing service agreement with Enogex for interruptible transportation service under section 311 of the Natural Gas Policy Act (NGPA)⁵ by reducing the amount of capacity that Enogex would be able to make available to Apache for its interruptible NGPA section 311 service. Applying the *Islander East* test,⁶ the Commission concluded that the proposed lease was required by the public convenience and necessity because the lease payments were satisfactory, the

⁴ See *Gulf Crossing Pipeline Company LLC (Gulf Crossing)*, 123 FERC ¶ 61,100 (2008), in which the Commission approved, *inter alia*, Gulf Crossing's lease of 90,000 Dth/d of capacity on Enogex's system.

⁵ 15 U.S.C. § 3371 (2006). The NGPA was passed in 1978 to reduce then-existing restraints on the flow of gas between interstate and intrastate markets in order to remedy supply and demand imbalances. NGPA section 311 enabled intrastate pipelines to transport gas destined for the interstate market without becoming subject to NGA jurisdiction over the entirety of their operations and spared interstate pipelines from having to construct duplicative facilities. See, e.g., *Egan Hub Partners, L.P.*, 73 FERC ¶ 61,334, at 61,930-31 (1995). While intrastate pipelines' services under NGPA section 311 are shielded from the Commission's NGA jurisdiction, section 311 of the NGPA provides that interstate gas services under that authority are subject to the Commission's implementing regulations. The Commission's regulations governing section 311 interstate services are set forth in Part 284, subpart C of the regulations, 18 C.F.R. § 284.121 *et seq.* (2011), and require that intrastate pipelines satisfy certain rate and reporting requirements.

⁶ Under the *Islander East* test, the Commission will approve a pipeline lease if: "(1) there are benefits for using a lease arrangement; (2) the rate under the lease is less than comparable transportation service; and (3) the lease arrangement does not adversely affect existing customers." *Islander East Pipeline Co.*, 100 FERC ¶ 61,276, at P 69 (2002).

lease provided significant benefits, and those benefits outweighed any potential harm to Enogex's existing customers.⁷ In response to Apache's claim that it would be adversely affected, the Commission concluded that "[w]hile the amount of capacity Enogex can provide as interruptible section 311 transportation service could change at some point in the future, those transactions are, by definition, interruptible and subject to change."⁸

B. The Rehearing Order (May 2009 Rehearing Order)

4. Apache sought rehearing of the July 25, 2008 Order, arguing, among other things: (1) the Enogex-Midcontinent lease is unduly discriminatory, anti-competitive, and in violation of the Commission's open-access regulations; (2) the Commission should require Enogex to offer firm NGPA section 311 transportation service to its own existing shippers as a condition of the Commission's approval of the capacity lease arrangement; and (3) the Commission's finding that Apache would not be harmed by the Enogex-Midcontinent lease was not based on substantial evidence.

5. On May 21, 2009, the Commission issued an order denying rehearing (May 2009 Rehearing Order).⁹ In the May 2009 Rehearing Order, the Commission rejected Apache's discrimination-based arguments. The Commission noted that Apache's rehearing arguments claiming undue discrimination were not based on the differences or similarities between the lessee -- Midcontinent -- and Enogex's shippers, but rather on those between Midcontinent's shippers whose services utilize the leased Enogex capacity and Enogex's own shippers. For reasons explained in the May 2009 Rehearing Order, the Commission found that Enogex's existing shippers (with service agreements for interruptible service by Enogex under NGPA section 311) were not similarly situated to Midcontinent's shippers (for whom Midcontinent would provide NGA section 7(c) firm service using leased capacity on Enogex's system).¹⁰

6. The May 2009 Rehearing Order also rejected Apache's insistence that the Commission should require that Enogex offer firm section 311 transportation service as a condition of the lease approval. The Commission observed that the adverse effects Apache might experience as a result of the Enogex-Midcontinent lease are inherent to the nature of Apache's interruptible service agreement with Enogex and therefore did not

⁷ See July 25, 2008 Order, 124 FERC ¶ 61,089 at P 32.

⁸ *Id.* P 43, citing *Gulf Crossing*, 123 FERC ¶ 61,100 at P 121.

⁹ *Midcontinent Express Pipeline LLC*, 127 FERC ¶ 61,164 (2009).

¹⁰ *Id.* P 12.

warrant the Commission's rejection of the Enogex-Midcontinent lease or a condition on its lease approval to require that Enogex offer firm section 311 transportation service.¹¹

7. The Commission rejected Apache's assertions regarding the sufficiency of record evidence to support the Commission's conclusion that Apache would not be harmed by the Enogex-Midcontinent lease. The Commission and Enogex both acknowledged that the lease could result in a reduction in the amount of capacity available at certain receipt points for Enogex's own interruptible shippers. However, Apache did not provide evidence to convince the Commission that shut-ins of Oklahoma gas production were likely to result from Enogex's lease of capacity to Midcontinent. Rather than being the result of the lease arrangement, the Commission concluded that capacity constraints on Enogex's system would be primarily due to increased gas production in the supply areas accessed by Enogex's system, thus leading to increased demand for its capacity.

8. The July 25, 2008 Order and May 2009 Rehearing Order both observed that Midcontinent is required to offer firm and interruptible transportation on a non-discriminatory basis, and any of Enogex's interruptible section 311 shippers could have participated in Midcontinent's open season for firm transportation service utilizing the leased capacity. The Commission recognized that there might have been valid business reasons militating against that option for some of Enogex's shippers. However, the fact that certain of Enogex's shippers did not see bidding for firm service on Midcontinent to be an attractive business choice did not alter the fact that capacity for firm service on Enogex's facilities was available to all shippers on a nondiscriminatory basis through Midcontinent. Thus, the Commission found that Midcontinent's lease of Enogex capacity was not anticompetitive or in violation of the Commission's open-access regulations, as Midcontinent's open season offered all shippers access to service at Commission-approved rates without preference.¹²

9. In essence, the Commission found that Apache's claimed lease-resultant adverse effects were speculative and not consistent with the best reading of the record. The Commission also explained that, "because interruptible shippers have no claim of right to system capacity, the limited potential reduction in the capacity available for section 311 interruptible transportation service of the result of the lease cannot be viewed as an undue adverse effect."¹³ In light of this analysis, the Commission affirmed that the benefits of

¹¹ *Id.* P 19.

¹² *Id.* P 13.

¹³ *Id.* P 26; *see also id.* P 18-19.

the lease outweighed possible changes in the service to Enogex's existing interruptible customers.¹⁴

C. The Court's December 28, 2010 Remand to the Commission

10. On judicial review, the court held that the Commission had not found, as required by the third prong of the Commission's own *Islander East* test, that the Enogex-Midcontinent lease would not adversely affect existing customers. Rather, the court explained, the Commission had stated that the lease would not have an *unduly* adverse impact on Enogex's existing services, and that the lease's benefits outweighed any potential harm to Enogex's customers. The court noted that the Commission: (1) could have explained that diminished interruptible service does not constitute an "adverse effect" for purposes of its pipeline lease analysis because interruptible service is inherently subject to disruption and therefore cannot be "adversely affected" by a lease; and/or (2) could have modified its *Islander East* test to preclude only "undue" adverse effects and to expressly include a balancing of benefits against burdens. Because the Commission's analysis of the Enogex-Midcontinent lease did not specifically find that the arrangement would not have *any* adverse effects on existing customers, only that there would be no *undue* adverse effects, the court found that the Commission's holding was not consistent with the *Islander East* test as previously articulated by the Commission, and the court remanded the case to the Commission for further explanation.

D. Apache's January 21, 2011 Motion for Expedited Remand Procedures

11. On January 21, 2011, Apache filed a motion urging the Commission to not adopt either approach suggested by the court, but instead to hold to a standard requiring that a pipeline seeking to lease capacity to another pipeline demonstrate either: (1) that "the lease arrangement does not adversely affect existing customers" of the lessor pipeline; or (2) that the lessor pipeline has taken all feasible steps to mitigate that harm and the benefits of the lease arrangement outweigh any remaining harm. In its motion, Apache argued: (1) the Commission could not reasonably deny that a reduction in availability of capacity for interruptible section 311 service resulting from the Enogex-Midcontinent lease is an adverse effect; (2) the Commission should not change the standard in the third prong of the *Islander East* lease analysis test standard from no adverse effect to no "undue" adverse effect; and (3) the Commission should require Enogex to offer firm section 311 transportation service to its existing customers in order to mitigate the lease's adverse impacts on Enogex's customers.

12. Apache requested in its January 21, 2011 Motion that before issuing an order denying its requested relief, the Commission should establish either an expedited briefing

¹⁴ *Id.*

schedule or evidentiary hearing to address the issue of the appropriate legal standard to be applied.

E. The Order on Remand

13. On March 3, 2011, the Commission issued its Order on Remand in which it clarified its decisions in the July 25, 2008 Order and May 2009 Rehearing Order. In the Order on Remand, the Commission acknowledged that, while it had previously *indicated*, it had never expressly *stated* that the third “no impact” prong of the *Islander East* test to protect the interests of pipelines’ existing customers is a relative, rather than absolute, standard. The Commission clarified that in applying the test, it will consider whether a proposed lease arrangement would have an *undue* adverse affect on a pipeline’s existing customers, such that the adverse impacts on the existing customers would outweigh the positive benefits identified under the first prong of the test.¹⁵ The Commission emphasized in its Order on Remand that it will not consider any of the prongs of the test in isolation, but rather will balance them on a case-by-case basis.¹⁶ The Commission emphasized that reading “undue” into “adverse impact” is necessary to allow the Commission to engage in reasoned decision making, as it would make no sense for it to reject a proposed lease that would have very minimal or insignificant impacts on existing customers if the lease would circumvent the need for a lengthy new pipeline that would traverse environmentally sensitive areas and result in higher rates and decreased supply to many other customers.¹⁷

14. After clarifying that application of the *Islander East* test may result in the Commission finding that a proposed capacity lease arrangement will have sufficient benefits to justify its approval even when it is also clear that the lease will have some adverse effects on existing customers, the Commission reiterated that like any other interruptible shipper on any pipeline system, Apache has no claim of right to any specific amount of capacity on Enogex, and that any reduction in the amount of capacity on Enogex available for interruptible section 311 transportation service is “a consequence

¹⁵ Order on Remand, 134 FERC ¶ 61,155 at P 13. The Commission noted its finding in *Gulf Crossing* that the benefits from the Enogex lease at issue in that proceeding “outweigh any possible changes that may result to shippers receiving interruptible 311 service.” 123 FERC ¶ 61,100 at P 121 (2008).

¹⁶ Order on Remand, 134 FERC ¶ 61,155 at P 13.

¹⁷ *Id.* P 14.

inherent to the nature of interruptible service.”¹⁸ Thus, the Commission found that Apache’s insistence on continuing to receive its historical levels of service was baseless in light of “the intermittent quality of [interruptible] service ... which all purchasers of such service must accept.”¹⁹

15. In any event, Enogex’s engineering information showed that, while in combination the Enogex-Midcontinent and Enogex-Gulf Crossing leases may result in a reduction in the amount of capacity available for interruptible service at certain receipt points on Enogex’s system, the record did not support Apache’s speculation that Enogex’s lease commitments would result in Enogex having to reduce its levels of interruptible service to the extent that some of its producer-shippers might have to shut in gas wells.²⁰ Since Enogex provided no evidence to make this a convincing argument, it provided no justification for rejection of the lease or imposition of lease conditions to ensure that Enogex would be able to continue making its historical levels of capacity available for “transactions [which] are, by definition, interruptible and subject to change.”²¹ Consequently, the Commission’s Order on Remand did not need to reach the question of whether interruptible shippers’ rights to use capacity, a contingent right that can only be exercised when capacity is available, can be a decisive consideration when weighing the benefits and adverse impacts of a proposed lease. Based on the record in this proceeding, the Commission found in its Order on Remand that potential reduction in available capacity for interruptible service for Apache and Enogex’s other interruptible shippers as a result of the lease would not be an unduly adverse effect of the type that the *Islander East* test is designed to consider and, where possible, avoid.²² On the other hand, the Order on Remand affirmed the Commission’s conclusion that the lease will have many

¹⁸ Order on Remand, 134 FERC ¶ 61,155 at P 15, *citing* May 2009 Rehearing Order, 127 FERC ¶ 61,164 at P 18.

¹⁹ *Id.* P 15, *quoting* *Columbia Gas Transmission Corp.*, 55 FERC ¶ 61,366, at 62,144 (1991).

²⁰ Based on the record, the Commission found that increased demand for service due to increased production, not Enogex’s lease of capacity to Midcontinent, was the only reasonably-likely cause in the foreseeable future of a large reduction in the amount of Enogex’s capacity available for interruptible service. *See* May 2009 Rehearing Order, 127 FERC ¶ 61,164 at P 25.

²¹ *Id.*, *citing* *Gulf Crossing*, 123 FERC ¶ 61,100 at P 121.

²² Order on Remand, 134 FERC ¶ 61,155 at P 15.

significant benefits, which were not challenged by Apache and are thus no longer subject to debate, which benefits were found to outweigh those potential adverse effects.²³

II. Apache's Request for Rehearing of the Order on Remand

16. The issues raised in Apache's rehearing request include: (1) the Commission's alleged failure to engage in reasoned decision making by failing to address the claims asserted in Apache's January 21, 2011 Motion and March 1, 2011 Answer; (2) whether the Commission's modification of the *Islander East* lease-approval test, without requiring mitigation of the lease's adverse impacts, is unduly discriminatory and inconsistent with Commission precedent and sound policy; (3) whether the Commission's determination that interruptible shippers cannot be adversely impacted by a diminution in service as a result of a lease is unjust and unreasonable, unduly discriminatory, and inconsistent with open-access requirements and related precedent; (4) whether the Commission's failure to require Enogex to offer firm section 311 transportation as a condition of lease approval was unjust and unreasonable, arbitrary and capricious, and inconsistent with open-access requirements and related precedent; (5) whether the Commission's finding that the lease is unlikely to adversely affect Enogex's existing shippers is supported by substantial evidence; and (6) whether the Commission should have conducted a paper or evidentiary hearing prior to acting on the court's remand.

A. Failure to Address January 21, 2011 Motion and March 1, 2011 Answer and to Conduct a Paper or Evidentiary Hearing; Sufficiency of Record to Support Finding that Lease Is Unlikely to Adversely Affect Existing Shippers

17. At the crux of Apache's January 21, 2011 Motion and its request for rehearing of the Commission's Order on Remand is its claim that "a Section 311 pipeline unlawfully discriminates against existing shippers if it leases firm capacity to another pipeline, while

²³ As referenced by the Order on Remand, 134 FERC ¶ 61,155 at P 7, the Commission's July 25, 2008 Order authorizing Enogex's and Midcontinent's capacity lease arrangement found that its benefits would include: avoiding the need for Midcontinent to construct duplicative facilities that would essentially parallel the Enogex system; minimizing impacts on the environment and landowners; allowing for the efficient use of Enogex's system; reducing the cost of constructing the Midcontinent system and allowing it to be placed in service earlier; and allowing Midcontinent's shippers seamless access, under a single contract, from Oklahoma production areas to multiple pipelines serving the southern and eastern United States. 124 FERC ¶ 61,089 at P 35.

refusing to allow those shippers to purchase comparable firm capacity in order to maintain their existing levels of service.”²⁴

18. Apache has doggedly assailed the Enogex-Midcontinent lease as unduly discriminatory and contrary to the Commission’s open-access policies. In its petition for rehearing of the July 25, 2008 Order that approved the lease, Apache’s argument to the Commission was that the lease would result in discrimination against Apache in favor of Midcontinent’s customers. However, in its petition for judicial review, Apache argued the lease resulted in discrimination against producers like Apache in favor of Midcontinent itself.²⁵ The court, noting this shift in Apache’s undue discrimination argument, declined to consider Apache’s new discrimination argument since it had not been urged before the Commission in its rehearing request.²⁶

19. Undaunted, and disagreeing with the court’s basis in its December 28, 2010 decision for declining to address its undue discrimination argument, Apache filed its January 21, 2011 Motion with the Commission in an attempt to resuscitate its claim of

²⁴ January 21, 2011 Motion at 11-12. *See also* Apache’s April 4, 2011 Request for Rehearing of the Order on Remand at 8, wherein Apache contends that the Commission failed to “address the fundamental issue in this case - that it is unduly discriminatory and contrary to the Commission’s open-access regime for a pipeline to lease capacity to another pipeline without allowing other shippers to compete for that capacity on equal terms.”

²⁵ *Apache Corp. v. FERC*, 627 F.3d at 1222, *citing* Apache’s August 25, 2008 Request for Rehearing of the Commission’s July 25, 2008 Order at 9.

²⁶ The court explained:

Apache did not raise this claim in its petition for rehearing to the Commission, and we therefore do not reach the issue here. The Natural Gas Act provides that “[n]o objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do.” 15 U.S.C. § 717r(b).

In fact, as the court noted, Apache expressly disavowed in its August 25, 2008 Request for Rehearing of the July 25, 2008 Order the argument it subsequently presented to the court. *Id.*

undue discrimination,²⁷ and to otherwise retool arguments heretofore raised in this proceeding, either to the Commission or to the court. However, the Commission does not believe that the court's intention in remanding this case to the Commission was to give Apache the opportunity to renew or reshape arguments against the approval of the Enogex-Midcontinent lease which had already been rejected by the Commission and the court. The court simply directed the Commission to explain a rationale not clearly expressed in its previous orders, and that is precisely what the Commission did in its Order on Remand.

20. The court made clear its instructions to the Commission, stating that “the Commission did not adequately explain one aspect of its decision to approve the lease, and we therefore remand for further explanation.”²⁸ The court explained that the Commission never concluded in the May 2009 Rehearing Order that the lease would not adversely affect existing customers, but instead found that the lease would “not have an unduly adverse impact on Enogex’s existing services”²⁹ and that “the lease’s benefits outweigh any potential harm to Enogex’s customers.”³⁰ Because there is a difference between the pre-existing *Islander East* lease-approval test’s stated “any adverse effects” criterion and the “undue adverse effects” criterion that the Commission employed in the May 2009 Rehearing Order’s lease analysis, the court directed the Commission to clarify only this aspect of its ruling. However, that was the court’s only direction to the Commission; in all other respects, the court denied Apache’s petition for review, including Apache’s contention “that the Enogex-Midcontinent lease is discriminatory and that [the Commission’s] approval subverts the ‘open access’ regulatory scheme for natural gas regulation.”³¹ Furthermore, the court directed the Commission “to provide the necessary clarification without unreasonable delay.”³²

²⁷ Apache went so far as to attach its briefs to the court as an exhibit to both its January 21, 2011 Motion and April 4, 2011 Request for Rehearing of the Commission’s Order on Remand.

²⁸ *Apache v. FERC*, 627 F.3d 1220 at 1221.

²⁹ *Id.* at 1222, citing *Midcontinent Express Pipeline, LLC*, 124 FERC ¶ 61,089 at P 43.

³⁰ *Id.*, citing *Midcontinent Express Pipeline, LLC*, 124 FERC ¶ 61,089 at P 37.

³¹ *Id.*

³² *Id.* at 1223.

21. Nevertheless, Apache still asserts in its request for rehearing of the Commission's Order on Remand that in order to comply with the court's instructions in its remand, the Commission should establish either a paper or evidentiary hearing in order to develop a record on what legal standard the Commission should apply and how that standard would be applied in this case.³³ The Commission disagrees. As discussed above, the court gave no indication that it was requiring or expected the Commission to consider any new theory of discrimination that Apache might put forward or conduct further proceedings. As directed by the court, the Commission provided the necessary clarification by explaining in its Order on Remand a rationale that it had not explained with sufficient clarity in prior orders. In doing so, as discussed below, the Commission did not, in the Order on Remand (or in the previous orders, for that matter), establish a new standard to be used in the lease-approval context.

22. However, the Order on Remand acknowledged that the court's remand was the first time the issue of adverse effects (other than rates) on existing shippers in lease cases had been so squarely posed, making it necessary for the Commission to consider the interplay among the three prongs of its *Islander East* test. Thus, the Commission explained in the Order on Remand that reasoned decision making requires that the third—"no impact"—prong of the *Islander East* test be viewed as a relative, rather than absolute, standard. That is, it is implicit that the Commission's application of the test will consider whether a proposed lease arrangement would result in *undue* adverse impacts on existing customers, i.e., adverse impacts on the existing customers that would not be clearly outweighed by the lease's positive benefits identified under the first prong of the test.³⁴ The Order on Remand also emphasized that the Commission will not consider any of the prongs of the test in isolation, but rather will balance them, on a case-by-case basis. Given the facts of individual lease cases, the Commission will determine whether a proposal meets all of the three established criteria, and, if it does not, weigh the significance of the lease's failure to satisfy any criterion against the benefits it would provide with respect to other criteria.³⁵ The Commission concluded in its Order on

³³ See Apache's January 21, 2011 Motion at 9, where Apache states that "[t]he D.C. Circuit instructed the Commission to conduct further proceedings."

³⁴ Order on Remand, 134 FERC ¶ 61,155 at P 13.

³⁵ *Id.* While the Order on Remand was the first time the Commission expressed its view that reasoned decision making necessitates that it apply its *Islander East* lease test so that it precludes only *undue* adverse effects on existing shippers, the Order on Remand noted that the Commission had indicated in *Gulf Crossing* that it does not view its lease test's third criterion as an absolute standard precluding approval of a proposed leased lease with substantial benefits that clearly outweigh some adverse impacts on existing shippers. The Commission found that the benefits of the lease at issue in that case, which

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Remand that the benefits of the Enogex-Midcontinent lease arrangement will clearly outweigh the adverse impacts on Enogex's existing customers that could be attributed to the lease.³⁶

23. Apache asserts in its request for rehearing of the Order on Remand that the Commission should go beyond the court's instructions and reopen the record in this proceeding because the Order on Remand perpetuates the same errors the Commission made in its factual analysis in its earlier orders. However, Apache's assertion that the Commission's findings regarding the potential adverse effects of the Enogex-Midcontinent lease on existing shippers were not based on substantial evidence was addressed by the Commission in its May 2009 Rehearing Order.³⁷ During the more than a year and a half between the Commission's issuance of its notices of Enogex's and Midcontinent's applications³⁸ and the May 2009 Rehearing Order, Apache had the opportunity to raise its arguments as to how the Commission's approval of the lease might adversely impact it. The record developed during that period supported a finding that the Enogex-Midcontinent lease might contribute to a reduction in capacity being available at certain receipt points on Enogex's system for interruptible shippers. The

also was a lease of capacity by Enogex, would "outweigh any possible changes that may result to shippers receiving interruptible 311 service." 123 FERC ¶ 61,100 at P 121.

³⁶ As discussed above, engineering information provided by Enogex supported its assertion that, while available capacity at certain individual receipt points might decrease, planned reconfigurations on its system before the in-service dates of the Midcontinent and Gulf Crossing leases would result in an overall increase in system capacity so that Enogex would be able to accommodate its capacity commitments under both leases and its own service obligations. July 25, 2008 Order, 124 FERC ¶ 61,089 at P 43. In addition, as discussed in both the July 25, 2008 Order and May 2009 Rehearing Order, if an Enogex shipper had concerns that it might at some point not be able to get as much capacity at the receipt points specified in the lease as it had historically been able to obtain, it could have participated in Midcontinent's open season for firm transportation service using the leased capacity. Regardless whether Apache or other Enogex shippers viewed paying Midcontinent's rates for firm service an attractive option, the opportunity for firm service by Midcontinent nevertheless was a mitigating factor. See May 2009 Rehearing Order, 127 FERC ¶ 61,164 at P 13.

³⁷ *Id.* P 21-29.

³⁸ Notice of Enogex's application was published in the *Federal Register* on October 24, 2007 (72 Fed. Reg. 60,332). Notice of Midcontinent's application was published in the *Federal Register* on October 26, 2007 (72 Fed. Reg. 60,932).

Commission also acknowledged that there might be a reduction in the capacity available for interruptible service on Enogex's system at some point in the future, and concluded the likely cause of such a reduction would be increased production leading to increased demand for pipeline capacity. However, Apache did not convince the Commission that approval of the lease would significantly increase the likelihood of well shut-ins in the foreseeable future due to insufficient capacity on Enogex's system for interruptible service.

24. Whether the potential reduction in available interruptible capacity at certain receipt points was a sufficiently adverse effect on existing shippers to warrant rejection of the lease with its substantial benefits was not a factual issue. Rather, it was a policy decision for the Commission to make. While Apache also argued in its petition for judicial review that the Commission's factual analysis was deficient, the court remanded this case only for the Commission to clarify its reasoning on the one aspect discussed above, observing that there was a "serious possibility that the Commission will be able to substantiate its decision on remand," the court did not vacate the Commission's orders approving the Enogex-Midcontinent lease.

B. Whether the Commission's Determination that Interruptible Shippers cannot be Adversely Impacted by a Diminution of Service is Unjust, Unreasonable, Unduly Discriminatory, and Inconsistent with Open-Access Requirements

25. The Commission did not, contrary to Apache's assertion, take the view that a reduction in the amount of capacity available for interruptible section 311 transportation service would not be an adverse effect on Enogex's shippers. Rather, the Commission took into account the fact that interruptible shippers have no claim of right to any specific amount of capacity on a pipeline; hence, the Order on Remand reflected the Commission's conclusion that, as a general rule, the potential for a lease to diminish the amount of interruptible service that the lessor pipeline is able to provide should not be a disqualifying adverse effect under the *Islander East* test when that effect will be clearly outweighed by the benefits of the lease.³⁹ As the Commission explained, any other result

³⁹ Order on Remand, 134 FERC ¶ 61,155 at P 15. Because Enogex's shippers have never been able to count on any set amount of capacity being available at any given time, the Commission did not agree with Apache's assertion that the Commission's priority should be to protect a producer-shipper against the possibility of having to shut in its production as the result of a lease causing diminished capacity for interruptible service. Therefore, the Commission also did not agree that its approval of the lease amounted to an abdication of any duty on its part to protect interruptible shippers. In any

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would empower interruptible shippers on any pipeline's system to prevent that pipeline from ever leasing any of its capacity to another pipeline, since any capacity committed to a lease would no longer be available to those interruptible shippers under the lessor pipeline's own tariff.⁴⁰

26. The Commission has already addressed Apache's assertions that the lease results in undue discrimination against Enogex's own shippers and is inconsistent with the Commission's open-access requirements because the Commission did not condition its approval of the capacity lease arrangement to require that Enogex begin offering firm service to its shippers with service agreements for interruptible interstate service under section 311 of the NGPA. As explained in the July 25, 2008 Order that approved the Enogex-Midcontinent lease, an intrastate pipeline's decision whether to offer firm section 311 service lies within the intrastate pipeline's discretion, and Enogex has thus far declined to offer firm interstate service.⁴¹ The July 25, 2008 Order also addressed and rejected the discrimination theory that Apache raised before the Commission in its protest. At that time, Apache's argument was that the agreement by Enogex, which only provides interruptible interstate service, to lease capacity to Midcontinent, which would offer the same capacity on a firm basis to its shippers, would result in discrimination against Enogex's shippers in favor of Midcontinent. The July 25, 2008 Order explained that the lease does not result in Enogex providing firm service to Midcontinent. Rather, Midcontinent has a property interest in a portion of Enogex's capacity and uses the capacity to offer its own services, which are fully subject to the Commission's NGA jurisdiction and, therefore, the full panoply of the Commission's open-access requirements, including a requirement to offer firm service.⁴² In its request for rehearing of the July 25, 2008 Order, Apache focused not on the differences or similarities between the lessee, Midcontinent, and Enogex's shippers, but rather on those between Midcontinent's shippers on Enogex and Enogex's shippers on Enogex. For reasons explained in the May 2009 Rehearing Order, the Commission found that Apache suffered no undue discrimination because Enogex's shippers using Enogex's capacity for NGPA section 311 interruptible service were not similarly situated to Midcontinent's shippers,

event, as the Commission noted in its Order on Remand, the record in this proceeding does not indicate that a shut-in of production is likely to result simply from Enogex's lease operations. 134 FERC ¶ 61,155 at n.27.

⁴⁰ *Id.* P 16.

⁴¹ *See* July 25, 2008 Order, 124 FERC ¶ 61,089 at P 52.

⁴² *Id.* P 51.

for whom Midcontinent provides NGA section 7(c) firm service using leased capacity on Enogex.

27. In its petition for review of the May 2009 Rehearing Order, Apache's discrimination arguments again centered on the theory that the lease discriminates in favor of Midcontinent itself against Apache and other producers. The court did not consider Apache's undue discrimination claim because Apache did not raise it in its request for rehearing. In fact, the court noted, Apache expressly disavowed this theory in its rehearing request.⁴³

28. Based on the above, the Commission will not address Apache's discrimination theory arguments. These issues have been thoroughly considered by the Commission and the court, and are outside the scope of the court's remand mandate.

C. **Whether the Order on Remand's Modification of the *Islander East* Lease-Approval Test, Without Requiring Mitigation of the Lease's Adverse Impacts, Is Unduly Discriminatory and Inconsistent with Commission Precedent and Sound Policy; Whether the Commission's Failure to Require Enogex to Offer Firm Section 311 Transportation as a Condition of Lease Approval was Unjust and Unreasonable, Arbitrary and Capricious, and Inconsistent with Open-Access Requirements and Related Precedent**

29. Apache asserts that it was unduly discriminatory and inconsistent with Commission precedent and policy for the Commission to modify the *Islander East* test without requiring that the lessor pipeline mitigate the adverse impacts of the lease on its customers. That is to say, according to Apache, either Enogex should have voluntarily offered firm section 311 transportation service to its existing customers, or the Commission should have required it as a condition of the lease approval.⁴⁴ This claim was previously raised, rejected by the Commission, and again raised by Apache in its petition for judicial review. The Commission did nothing in the Order on Remand that

⁴³ See *Apache Corp. v. FERC*, 627 F.3d at 1222, citing Apache's August 25, 2008 Request for Rehearing of the Commission's July 25, 2008 Order at 9.

⁴⁴ Apache has never suggested that there was any other way in which to mitigate the impact of the lease on section 311 interruptible shippers. However, as discussed above, there was a significant mitigating factor because any interruptible section 311 shipper on Enogex's system willing to pay Midcontinent's rates for firm service could have participated in its open season to ensure that it would continue to have access to as much capacity as it needed on Enogex's system. See May 2009 Rehearing Order, 127 FERC ¶ 61,164 at P 13.

would justify or require reconsideration of that claim. As discussed above, the Commission simply clarified that the *Islander East* test's third "no adverse effect" requirement is a relative, rather than absolute standard, and further, that in general, the possible diminution of capacity available for interruptible section 311 service as a result of a lease is not a disqualifying adverse effect due to the nature of interruptible service. Also, as stated above, Apache's discrimination theory arguments have been thoroughly considered by the Commission and the court, and are outside the scope of the court's remand mandate.

30. Apache adds, in its renewed request, that Enogex should be required to offer firm section 311 transportation service to its interruptible section 311 customers because it is necessary to ensure consistency with the criterion of the Commission's Certificate Policy Statement⁴⁵ which looks to the efforts made by an applicant for a certificate authorizing new pipeline construction to minimize the proposed project's adverse effects on existing customers. However, the only mitigation step Apache urged was that Enogex be required to offer existing shippers firm section 311 transportation service. The Commission declined to impose such a condition on its approval of the Enogex-Midcontinent lease because the Commission's regulations governing section 311 services by intrastate pipelines exempt them from having to offer firm interstate transportation service and, as discussed above, there is no justification here for a departure from the policy considerations underlying that exemption.

31. Following the court's lead, the Commission's Order on Remand clarified that under the *Islander East* test, the Commission would balance benefits against burdens, precluding only "undue" adverse effects, i.e., adverse effects that outweighed the lease's potential benefits. Additionally, the Commission explained that it generally does not view diminished interruptible service as constituting an "adverse effect" for purposes of its pipeline lease analysis because interruptible transactions are, by definition, subject to change. Thus, the Order on Remand's clarifications fully addressed the question remanded by the court. It was not a "perfunctory order" that blindly followed the court's suggested course, as characterized by Apache in its request for rehearing.⁴⁶ Further, while the Commission acknowledged in the Order on Remand that the rationale described therein had not been thoroughly explained in prior orders, the clarifications provided by the Order on Remand's were entirely consistent with a prior order in which the

⁴⁵ *Certification of New Interstate Natural Gas Pipeline Facilities*, 88 FERC ¶ 61,227 (1999), *clarified*, 90 FERC ¶ 61,128, *further clarified*, 92 FERC ¶ 61,094 (2000) (Certificate Policy Statement).

⁴⁶ *See* Apache's April 4, 2011 Request for Rehearing of the Order on Remand at 12.

Commission considered whether diminished interruptible section 311 capacity was an adverse effect requiring rejection of a capacity lease and found that the capacity lease arrangement proposed by Enogex in that proceeding satisfied the Commission's *Islander East* test, implicitly indicating that "adverse affect" is less than an absolute standard to be at least to some extent balanced against the potential benefits of a lease.⁴⁷

32. Specifically, in *Gulf Crossing*, the Commission approved Enogex's lease of some of its system's capacity to another interstate pipeline, Gulf Crossing Pipeline Company, LLC, over the protest by Unimark LLC, another interruptible NGPA section 311 shipper on Enogex's system. The protestors also argued in that proceeding that approval of the lease at issue would result in diminished availability of capacity for Enogex's interruptible section 311 services. The Commission stated in *Gulf Crossing* that "[w]hile the amount of capacity Enogex can provide as interruptible section 311 transportation service could change at some point in the future, those transactions are, by definition, interruptible and subject to change." The Commission found that since Enogex would continue to provide section 311 interruptible service after implementation of the lease, with the same rights, existing interruptible NGPA section 311 shippers on Enogex would not be adversely affected.⁴⁸ Moreover, the Commission in *Gulf Crossing* also found that the benefits from the Enogex lease outweighed any possible changes that might result to shippers receiving interruptible section 311 service.⁴⁹

33. In summary, certain notions preexisted all the prior orders in this proceeding: (1) the Commission generally will not find that diminished interruptible service constitutes an adverse effect on existing customers for purposes of pipeline lease analysis under the *Islander East* test; (2) that the test involves a balancing of benefits against burdens; and (3) the test precludes approval of a lease only if it will have "undue" adverse effects, i.e., its adverse effects outweigh the lease's benefits.

⁴⁷ Order on Remand, 134 FERC ¶ 61,155 at P 4.

⁴⁸ *Gulf Crossing*, 123 FERC ¶ 61,100 at P 121.

⁴⁹ *Id.*

The Commission orders:

Apache's request for rehearing of the March 3, 2011 Order on Remand is denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.