106 FERC ¶ 61,088
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeen G. Kelly.

Regulation of Short-Term Natural Gas Transportation Services, and Regulation of Interstate Natural Gas Transportation Services — Docket No. RM98-10-012

ORDER ON REHEARING AND CLARIFICATION

(Issued January 29, 2004)

1. On October 31, 2002, the Commission issued an Order on Remand[1] in this proceeding in which it addressed the remanded issues in Interstate Natural Gas Association of America v. FERC, 285 F.3d 18 (D.C. Cir. 2002) (INGAA) which considered the provisions of Order No. 637.[2] A number of parties requested rehearing or clarification of two issues in the Order on Remand: (1) whether the five-year term matching cap for capacity subject to a right of first refusal (ROFR) should be eliminated and (2) whether shippers in a segmented transaction may transport a quantity up to contract demand in both a backhaul and a forwardhaul to the same delivery point at the same time. For the reasons discussed below, the Commission affirms its decisions eliminating the term matching cap and requiring pipelines to permit segmented transactions consisting of a backhaul and a forwardhaul, both up to contract demand, at the same point at the same time. This order benefits the public by establishing

[1] Order on Remand, 101 FERC & 61,127 (2002).

[2] Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services, FERC Stats. & Regs. Regulations Preambles (July 1996-December 2000) & 31,091 (February 9, 2000); order on reh'g, Order No. 637-A, FERC Stats. & Regs, Regulations Preambles (July 1996-December 2000) & 31,099 (May 19, 2000); order denying reh'g, Order No. 637-B, 92 FERC & 61,062 (2000).

Commission policy regarding pipeline capacity and transportation and thereby creating flexibility and certainty in the transportation of natural gas.

I. Whether the Five-Year Term Matching Cap for Capacity Subject to a Right of First Refusal Should Be Eliminated

2. In the Order on Remand, the Commission eliminated the five-year matching cap for existing capacity subject to a right-of-first refusal (ROFR). By virtue of the cap, a shipper with existing capacity subject to a ROFR could retain its capacity if it matched the highest bid for that capacity up to a term of five years. The local distribution companies (LDCs) argue generally that removing the five-year ROFR term cap will harm natural gas customers and discourage retail choice programs. Industrial end users argue that they will be unable to enter contracts for terms of more than five years and will lose their existing capacity. These shippers assert current regulatory controls are not sufficient to protect consumers if the five-year cap is removed from the ROFR. They assert further that the Commission is failing to perform its statutory duty to protect natural gas customers and is acting contrary to various Court opinions and Commission orders. They ask the Commission to reinstate the five-year cap which, they assert, is supported by the evidence. As discussed below, the Commission rejects the arguments of the LDCs and industrial end users and denies their rehearing requests.

A. Background

3. In Order No. 436, the Commission provided pipelines with pre-granted abandonment authority under Section 7(b) of the NGA for transportation contracts when they expired.[3] In Order Nos. 636 and 636-A, the Commission tempered this grant of authority in order to protect captive customers from the exercise of pipeline monopoly power when their contracts expired or were terminated. The Commission provided existing shippers with the right of first refusal (ROFR). The ROFR provided existing shippers with the opportunity to retain their capacity by matching the highest rate and the longest term offered by other bidders, up to the maximum rate and a term of 20 years. The Court of Appeals approved the ROFR mechanism, but remanded the 20-year term matching cap for further explanation.[4] The Court was concerned that contract term

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[3] American Gas Association v. FERC, 912 F.2d 1496, 1513-14 (D.C. Cir. 1990) (AGA).

[4] United Distribution Companies v. FERC, 88 F.3d 1105, 1140-41 (D.C. Cir. 1996) (UDC).

would be used as a surrogate for price thereby allowing new customers to outbid existing ones by offering longer terms than they would in a truly competitive market.

4. In Order No. 636-C, the Commission reduced the term matching cap to five years and in Order No. 637 it retained this limit. However, on review of Order No. 637, in INGAA, [5] the Court found the evidence supporting the five-year cap, the median for data from January 1, 1995 through October 1, 1996, was incomplete. The Court also stated that the Commission had not affirmatively explained its selection of five years, nor had it answered objections to the five-year limit including those of the pipelines and of the Commission itself. Those concerns were that a five-year cap might result in a bias toward short-term contracts, that a regulation-induced shift toward shorter contracts would increase risks for the pipelines, and that elimination of the cap could help foster efficient competition.[6] Accordingly, the Court of Appeals vacated the five-year limit and remanded this issue to the agency.

5. On remand, the Commission found that a term-matching cap is not necessary to protect a pipeline's existing long-term firm customers from the pipeline's exercise of market power. The Commission adopted the reasoning it had used in Tennessee Gas Pipeline Co., when considering whether a cap is needed in bidding on unsubscribed capacity, where the winning bid is chosen based on which bid has the highest net present value (NPV) to the pipeline.[7] The Commission determined that there was no need for a term cap because the pipeline could not exercise market power in this situation as a result of current regulatory controls. The Commission accordingly eliminated the five-year cap for unsubscribed capacity in the Tennessee orders.

6. Similarly, in the Order on Remand in this proceeding, the Commission stated that market power is exercised through the withholding of capacity to create an artificial scarcity, thereby raising rates. The Commission found that current regulatory controls required the pipeline to limit its rates to maximum just and reasonable rates and to sell all available capacity to shippers willing to pay the maximum rate. Therefore, the

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[5] 285 F.3d at 50-56..

[6] INGAA, 285 F.3d at 52-53.

[7] Tennessee Gas Pipeline Co., 91 FERC & 61,053 (2000), reh'g, 94 FERC & 61,097 (2001) (Tennessee orders); aff'd, Process Gas Consumers Group v. FERC, 292 F.3d 831 (D.C. Cir. 2002) (PGC).

Commission found, the only way a pipeline could create scarcity to force shippers to accept longer term contracts would be to refuse to build additional capacity when demand requires it. However, the Commission found pipelines would have a greater incentive to build new capacity to serve all the demand for their service than to withhold capacity since the only way the pipeline could increase current revenues and profits would be to invest in additional facilities to serve the increased demand. Consequently, the Commission determined pipelines will be unable to induce longer contracts when shippers with existing contracts with a ROFR seek to renew them and that these customers are protected from the exercise of pipeline market power by existing regulatory controls. The Commission also found that the fact shippers may at times bid up contract length likely reflects not an exercise of the pipeline's market power, but rather competition for scarce capacity. Thus, the Commission determined that a term cap is not necessary for bidding on capacity subject to a ROFR.

7. In the Order on Remand, the Commission also addressed the requirements of Section 7(b) of the Natural Gas Act for shippers with existing capacity. As the Commission stated in the Order on Remand, in the ROFR context, unlike the NPV context, the Commission must find under Section 7(b) of the Natural Gas Act that pre-granted abandonment of existing capacity is in the public convenience and necessity.[8] The Commission found that the requirements of Section 7(b) were fulfilled without the need for a term matching cap. The Commission found the requirements of Section 7(b) regarding pre-granted abandonment of existing capacity when an existing shipper's contract expires or is terminated are fulfilled because the existing shipper has a ROFR. The ROFR ensures that if the existing customer is willing to pay the maximum approved rate and match the contract term of a rival bidder, the pipeline may not abandon service to that customer.[9] The Commission concluded that even a captive customer served by a single pipeline can retain its long-term firm transportation service against rival bidders and, therefore, is provided the protection from pipeline market power required for pre-granted abandonment under Section 7(b).

8. The Commission also found in the Order on Remand that eliminating the term matching cap addressed the various objections to the five-year cap. First, it satisfied those of the INGAA court and the pipelines that a cap fosters an imbalance of risks

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[8] PGC, at 838.

[9] United Distribution Companies v. FERC, 88 F.3d 1105, 1140-41 (D.C. Cir. 1996) (UDC).

between pipelines and existing customers and adversely affects the efficient allocation of capacity. Second, it addressed the objections of the INGAA court that the five-year cap provides a disincentive for existing shippers to enter into a contract of more than five years and thus results in a bias toward short-term contracts which, in turn, increases the risk to pipelines that they will be left with stranded capacity. The Commission also found that removing the term cap avoided the difficulty that the Commission has no way of estimating what contract terms a competitive market would produce, since there is no widespread competitive market for primary pipeline capacity.

B. Rehearing Requests

9. A number of local distribution companies (LDCs), associations representing LDCs, state entities, and industrial end users request rehearing on this issue. Individual local distribution companies requesting rehearing are Pacific Gas and Electric Company (PG&E); the Arizona Public Service Company and Pinnacle West Energy Corporation (APS/PWEC); and Bay State Gas Company, Columbia Gas of Kentucky, Inc., Columbia Gas of Maryland, Inc., Columbia Gas of Pennsylvania, Inc., Columbia Gas of Ohio, Inc., Columbia Gas of Virginia, Inc., and Northern Utilities Natural Gas (collectively, "NiSource Distribution Companies).

10. State entities and associations representing LDCs requesting rehearing are the National Association of Regulatory Utility Commissioners (NARUC); the American Gas Association and the American Public Gas Association[10] (collectively AGA); the National Association of State Utility Consumers Advocates (NASUCA); the Missouri Public Service Commission (MoPSC); the Maryland Public Service Commission (MD-PSC);the Public Service Commission of the State of New York (PSCNY); and the Minnesota Department of Commerce.[11]

11. Industrial end users requesting rehearing are Honeywell International, Inc.; the Northwest Industrial Gas Users (NWIGU);[12] and, jointly, the Process Gas Consumers Group, American Forest & Paper Association, American Iron and Steel Institute, Georgia

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[10] The APGA also filed a supplemental request for rehearing.

[11] Formerly, the Minnesota Department of Public Service.

[12] NWIGU is comprised of 31 industrial end users in Oregon, Washington, and Idaho.

Industrial Group, Industrial Gas Users of Florida, Florida Industrial Gas Users, and United States Gypsum (collectively, the "Industrials").

C. Discussion

(1) Summary

12. The Commission adopted pre-granted abandonment under Section 7(b) as part of its adoption of open access transportation in Order Nos. 436 and 636. It has considered at length its policy with respect to the captive customers' rights to retain their capacity when their long-term firm contracts for open access transportation service expire. This is a difficult issue and the Commission has attempted numerous times to formulate a reasonable resolution that balances the interests of the parties. Those interests are varied and, often, conflicting. The existing customers' interest is retaining its capacity at the lowest possible rate and for a term that is consistent with its needs and is not so long as to expose it to undue business risk. The new customers' interests are obtaining the capacity for themselves by outbidding the existing customers at a rate and term consistent with their needs. The pipelines' interests are maximizing the amount of subscribed capacity and obtaining contracts with the longest terms possible because, in that way, the pipeline lowers the financial risks of meeting its long-term debt costs and its business risks of meeting its other costs and making a profit.

13. The Commission initially adopted pregranted abandonment with no protections for captive customers in Order No. 436. On appeal of Order No. 436, the Court remanded this approach for explanation as to how it could be reconciled with the Commission's duty to protect gas customers from the exercise of pipeline monopoly power.[13] In Order No. 636,[14] the Commission tempered the pipeline's pre-granted authority to abandon

[13] American Gas Association v. FERC, 912 F.2d 1496, 1518.(D.C. Cir. 1990).

[14] Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, Order No. 636, 57 Fed. Reg. 13267 (April 16, 1992), FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996 ¶ 30,939 at 30,446-48 (April 8, 1992); order on reh'g, Order No. 636-A, 57 Fed. Reg. 36,128 (August 12, 1992), FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996 ¶ 30,950 (August 3, 1992); order on reh'g, Order No. 636-B, 57 Fed. Reg. 57,911 (December 8, 1992), 61 FERC ¶ 61,272 (1992); reh'g denied, 62 FERC ¶ 61,007 (1993); aff'd in part

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contracts upon their termination with a right of first refusal (ROFR) for firm customers with a contract longer than one year[15] as long as the existing customer matched the term and the rate (up to the maximum rate) offered by the highest competing bidder.[16] In Order No. 636-A, the Commission capped the contract length the existing shipper must match at twenty years.[17]

14. On appeal of Order No. 636, the Court found the twenty-year cap was not justified by the record and remanded it for further explanation.[18] The Court stated that the Commission had not adequately explained how the twenty-year term matching cap protects against the pipelines' preexisting market power, particularly why the twenty-year cap would prevent bidders on capacity constrained pipelines from using long contract duration as a price surrogate to bid beyond the maximum approved rate, to the detriment of captive customers. On remand in Order No. 636-C, the Commission changed its policy and adopted a five-year term matching cap. It relied on the fact most commentors in the Order No. 636 proceeding had supported a term matching cap in the range of five years and more recent evidence showed that five years was about the median length of all contracts of one year or longer between January 1, 1995 and October 1, 1996.[19]

15. On rehearing in Order No. 636-D, the Commission recognized that pipelines had raised legitimate concerns about whether the five-year term matching cap was causing a bias toward short-term contracts, with adverse economic consequences for both pipelines and captive customers. The Commission, however, deferred further consideration of the term cap to the proceeding which became the Order No. 637 proceeding in Docket No. RM98-10-000, where a more current record could be developed. In Order No. 637, the Commission continued the five-year cap policy, finding that none of the parties presented

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and remanded in part, United Distribution Companies v. FERC, 88 F.3d 1105 (D.C. Cir. 1996); order on remand, Order No. 636-C, 78 FERC ¶ 61,186 (1997).

[15] Order No. 636 at 30,446-48.

[16] 18 C.F.R. § 284.221(d)(2)(ii) (2001).

[17] Order No. 636-A, at 30,629-31.

[18] United Distribution Companies v. FERC, 88 F.3d 1105, 1140-41 (D.C. Cir. 1996) (UDC).

[19] Order No. 636-C at 61,774 and 61,792.

evidence to support the conclusion that a five-year contract is atypical in the current market.

16. On appeal of Order No. 637, the Court in INGAA found that the Commission had not supported the five-year cap. It found the Commission had relied on the same evidence that it had used to make its decision in Order No. 636-C, namely the fact that five years was about the median length of all contracts of one year or longer.[20] The Court stated that the Commission had not responded to its own or the pipeline's objections. These were that the five-year cap results in a bias toward short-term contracts. This fosters an imbalance of risks between the pipelines and existing shippers, with shippers obtaining indefinite control over pipelines' capacity, while shorter contracts increase the pipelines' cost of capital and thus the overall cost of pipeline transportation. The Court concluded that the only evidence supporting the Commission's final decision to choose a five-year cap was the original record, which in the Commission's own view was incomplete. Thus, the Court vacated the five-year cap and remanded the issue to the Commission.

17. In the Order on Remand, and in this order, the Commission finds no basis for justifying the distortions to the allocation of capacity created by the matching cap. A matching cap is not necessary to limit the exercise of market power by the pipelines, because the Commission's other regulatory requirements act to prevent pipelines from exercising market power. Since the matching cap is not needed to inhibit the exercise of market power by the pipelines, the Commission finds no justification for distorting the bidding process and not allocating scarce pipeline capacity to the shipper placing the highest value on obtaining that capacity. Removal of the term cap eliminates any bias toward shorter-term contracts, and the resulting imbalance of risks as between the existing customers and the pipelines. Given that the term cap is not needed to prevent pipelines from exercising market power, the Commission finds that the factual data on contract terms provides little factual basis for establishing a cap on contract length different from that established by the competition among buyers for the capacity. These data show a range of contract terms, some even exceeding the 5-year cap when it was in effect, and the Commission cannot find from this data that a specific contract term is what would be produced by a competitive market. In the absence of a concern over the exercise of market power by the pipelines, the Commission finds no basis for establishing an admittedly arbitrary term matching cap.

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[20] INGAA at 53.

18. Moreover, as discussed further below, the Commission's capacity release system helps to mitigate any business harm that might occur to LDCs or other specific customers from elimination of the term matching cap. In any situation in which customers must bid long terms to retain contractual capacity, that capacity is highly valued by the market. The customer has, therefore, obtained a valued asset, which it can release to others in the event that its needs change. Indeed, under Commission policy, the customer could permanently release that capacity to qualified and creditworthy shippers. The Commission, therefore, concludes that authorizing pregranted abandonment subject to a ROFR with no term matching cap strikes the best balance among existing customers, new customers, and the pipelines. Further, as discussed below, the Commission finds that to the extent there may be exercise of pipeline market power, the complaint process will provide adequate protection with regard to existing capacity. Since the matching cap was eliminated in October, 2002,[21] no shipper has alleged that a pipeline has used monopoly power to create an artificial scarcity of capacity and the Commission has looked carefully at other complaints to ensure that the bidding process under the ROFR when capacity is terminated is fair.

19. In addition, the Commission reviews pipeline tariffs and monitors bidding procedures and evaluation methods to ensure that the ROFR process is fair. For example, the Commission has required pipelines that restricted ROFR rights to terminations by the pipeline to provide shippers with ROFR rights when shippers terminate their contracts and the contracts expire.[22] The Commission is also currently considering a complaint alleging that a pipeline improperly required an existing shipper whose capacity was expiring to match a bid that had a different primary receipt point.[23] In addition, to help ensure that any bidding up of contract term actually reflects the value the market places on scarce capacity, where the pipeline uses the Net Present Value (NPV) method to determine the value of a new customer's bid, the Commission has determined that the pipeline must also use the NPV method to determine the value of the existing customer's

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[21] Order on Remand, 101 FERC ¶ 61,127 (2002).

[22] See, for example, orders in Docket Nos. RP00-533-000 and RP00-535-000 including Texas Eastern Transmission, LP, 101 FERC ¶ 61,215 (2002) and Algonquin Gas Transmission Co., 101 FERC ¶ 61,214 (2002).

[23] Fidelity Exploration & Production Co. v. Southern Star Central Gas Pipeline, Inc., Docket No. RP04-130-000 (December 31, 2003).

bid.[24] This will ensure that an existing customer can match the bid of the new customer by bidding any combination of rate and term that has the same NPV as the bid of the new customer. For example, if the new customer's party bid is for a relatively long term, but at a significantly discounted rate, thus indicating that the longer term is valued only if the rate is discounted, the existing shipper could match that bid by bidding for a shorter term at the maximum rate.

(2) Whether current regulatory controls are sufficient to protect consumers

20. The LDCs and Industrials assert that the Commission should not have relied on the Tennessee orders as affirmed by PGC because they apply only to unsubscribed capacity that is not protected by section 7(b) and not to subscribed capacity that is protected by Section 7(b). They also assert that current regulatory controls are not sufficient to protect consumers if the five-year cap is eliminated from the allocation of existing capacity. Specifically, they assert they will be forced to sign contracts in excess of five years regardless of the factthe pipeline is only permitted to charge just and reasonable rates and must make available all of its capacity. They assert that the contract term will act as a surrogate for price.

21. The Commission rejects these arguments. The Commission affirms it was justified in relying on the reasoning in the Tennessee orders concerning the inability of pipelines to exercise market power due to current regulatory controls. The Court in PGC did not prohibit the Commission from considering the effect of regulatory controls on the need for a term cap in the ROFR process for existing capacity. Instead, it distinguished the issue in the Tennessee orders, allocation of unsubscribed capacity, from the allocation of existing capacity at issue here, on the ground that only the latter is subject to Section 7(b).[25] Thus, PGC requires only that the Commission's policy concerning existing

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[24] Transcontinental Gas Pipe Line Corp., 105 FERC ¶ 61,365 P 19-21 (2003).

[25] PGC at 838:

> As INGAA explains, the requirement to protect existing shippers from pipeline market power derives directly from Section 7(b) of the Natural Gas Act, which "generally prohibits 'natural gas companies' from ceasing to provide service to their existing customers unless, after 'due hearing,' FERC finds 'that the present or future public convenience or

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capacity subject to a ROFR meet the requirements of Section 7(b). The Commission may adopt any reasonable policy concerning the ROFR, including the policy in Tennessee, as long as the policy chosen satisfies the requirements of Section 7(b).

22. As required, the Commission addressed the requirements of Section 7(b) in the Order on Remand when it eliminated the term cap. It stated that in the ROFR context, it must find under NGA Section 7(b) that pre-granted abandonment is in the public convenience and necessity.[26] The Commission determined this requirement is fulfilled because there is a ROFR and the ROFR ensures that, if the existing customer is willing to pay the maximum approved rate and match the contract term of a rival bidder, the pipeline may not abandon service to that customer.[27] Thus, even a captive customer served by a single pipeline can retain its long-term firm transportation service against rival bidders, and therefore is provided the protection from pipeline market power required for pre-granted abandonment under Section 7.[28] In addition, the Commission found that other regulatory constraints, like the requirements to sell all available capacity at just and reasonable rates, prohibited pipelines from exercising market power by withholding of capacity. It also found that pipelines would not exercise market power by refusing to build new capacity because they have no incentives to refuse to build.[29]

23. The Commission affirms its determination that current regulatory controls will protect customers if the five-year cap is eliminated from the ROFR for the reasons stated in the Order on Remand.[30] The Commission finds that in cases where customers believe the pipeline is exercising market power in the allocation of capacity when their contracts

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> necessity permit such abandonment.'" 285 F.3d at 51 (quoting 15 U.S.C. ' 717f(b)) . . . . No comparable statutory provision requires FERC to protect new shippers from competition for limited capacity (provided the final rates are just and reasonable).

[26] Order on Remand P 14.

[27] Citing UDC, at 1140-41.

[28] Citing UDC, at 1140-41.

[29] Order on Remand P 9-15.

[30] Order on Remand P 11-18.

have expired or terminated, they may use the complaint process and obtain protection in that way. The Commission notes that since the Order on Remand was issued in October, 2002, it has not received any complaints from customers that pipelines are exercising market power and refusing to renew contracts or insisting on longer terms in order to renew a contract. The closest such complaint is the Fidelity Exploration complaint discussed above in which the pipeline required the shipper to match a bid for twenty years. This case will be resolved by the interpretation and application of the pipeline's ROFR provisions. Thus, the Commission finds that the regulatory controls in place minimize the possibility of the exercise of market power by pipelines. On balance, the Commission finds that the public interest is best served by eliminating the cap, permitting shippers to contract without Commission-imposed term limits, and using the complaint process to address cases in which shippers believe that a pipeline has exercised market power in allocating capacity at the end of a contract. In any event, the Commission will continue to monitor the ROFR process and to evaluate whether additional controls are necessary.

24. The Commission rejects, in addition, the LDCs' other objections. First, the LDCs object that if regulatory controls are sufficient now, they should have been sufficient ten years ago and implies the Commission should have relied on them then instead of adopting a cap. While it is true that the Commission could perhaps have used the same reasoning as it developed in Tennessee, and adopted here, its prior failure to reexamine the extent to which pipelines can exercise market power over the ROFR process does not prevent the Commission from reaching the correct result on remand. The Commission has gone through a lengthy process of determining that existing shippers should have a ROFR and what the ROFR mechanism should include. Over the last ten years, the gas market has evolved and so has the Commission's approach to contracting, both for gas and transportation. The Commission's policy concerning the ROFR has evolved during this period along with its approach to the gas and transportation markets. The elimination of the term cap is most in keeping with the Commission's current views of gas transportation and with the current realities of the market for firm transportation.

25. PSCNY and NARUC assert there is no basis for the Commission's assumption that existing customers' rights to continued service under Section 7(b) of the NGA will be assured because pipelines have a greater incentive to build, rather than withhold, capacity. They assert pipeline construction often takes several years and existing customers cannot afford to have their capacity rights terminated while waiting for new construction to come on line. They argue that the incentive to build new capacity, if it exists, is insufficient to meet the consumer protection mandate under Section 7(b) of the NGA.

26. This argument misses the point. The Commission was not suggesting that construction of new capacity would provide immediate replacement capacity to shippers

that failed to exercise their ROFR and match the highest bid for capacity. The Commission found that because the pipelines had no incentive under its regulatory scheme to withhold capacity and exercise market power, the longer terms required to retain existing capacity were justified by the scarcity of current capacity. Thus, the Commission has no basis to impose artificial caps on bidding, but should permit the allocation of current capacity to the customer valuing it the most.

27. The LDCs also assert that the maximum just and reasonable rates do not protect customers because they were determined a number of years ago, are now too high, and pipelines are no longer filing rate cases so that the rates are not being adjusted. But retention of a cap on bidding does not address this issue. Regardless of whether the matching cap was in place, the same maximum rates would apply. Under the Natural Gas Act, it is generally the pipeline's, not the Commission's, decision whether to file a rate case. Under NGA Section 5, the Commission on its own motion, or on complaint of a gas distributing company or other customer, can institute a proceeding to review a pipeline’s rates if reasonable evidence is presented that a pipeline's rates are unjust and unreasonable.[31] The Commission has not found such action to be generally necessary. If, however, an LDC believes a pipeline's rates are unjust and unreasonable, it may file a complaint.

28. The LDCs assert that pipelines can exercise market power in other ways besides withholding capacity or overpricing it, such as by obtaining special advantages in matters not covered by tariff or requiring customers to forgo challenges to prudence, citing American Gas Association v. FERC, 912 F.2d 1496, 1516 (D.C. Cir. 1990) (AGA). The LDCs here cite to the appeal of Order Nos. 500-H and 500-I.[32]

[31] Section 5(a), Natural Gas Act, 15 U.S.C. ' 717d.

[32] Those orders permitted pre-granted abandonment without any opportunity for existing customers to retain their capacity. FERC Stats. & Regs., Regulations Preambles 1986-1990, **&&** 30,867 (1989) and 30,880 (1990). The LDCS in AGA alleged they would only be able to secure continued service by yielding to monopolistic pipeline demands such as insisting on special advantages in matters not covered by the pipeline's tariff or agreeing to forgo challenges to the prudence of the pipelines' costs. 912 F.2d at 1516. The Court remanded the pre-granted abandonment provisions so that the Commission could reconsider how gas customers could be protected from pipeline monopoly power at the end of a contract period. 912 F.2d at 1518. Subsequently, in Order No. 636, the Commission formulated the ROFR for existing shippers in response to

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29. Under the ROFR rules established by the Commission in Order No. 636, a pipeline cannot require shippers to provide special advantages in order to retain capacity. The shipper can retain its capacity by signing a pro forma service agreement at the maximum tariff rate, which contains no special terms and conditions. In fact, in Order No. 637, the Commission determined that it would not grant pipelines pre-approval to negotiate terms of conditions of service with shippers that were different from those set forth in their tariff.[33] The Commission's regulations require pipelines to file with the Commission any service agreements that contain material deviations from its tariff, and such filings permit review of whether such deviations are unduly discriminatory.[34]

30. Finally, the LDCs assert the complaint process is not applicable to new pipeline capacity, referring to paragraph 12 of the Order on Remand which described the Tennessee orders and stated that a shipper could file a complaint if Tennessee refused to build new capacity. Although the Commission finds that pipelines do not have sufficiently strong incentives to withhold capacity by not constructing when economically justified so as to justify a term cap, the Commission sees no reason why a shipper cannot file a complaint about a pipeline's refusal to construct capacity when economic. While there may be concerns about the Commission's ability, under Section 7 of the NGA, to require a pipeline to construct capacity,[35] the Commission could certainly impose other remedies (such as reimposing a term cap) if it found that a pipeline was attempting to exercise market power.[36]

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the requirements of the Court in AGA. Order No. 636, FERC Stats. & Regs. 1991-1996, **&** 30,939 at 30,448 and see, generally, pages 30,443-452.

[33] Order No. 637 at 31,343.

[34] 18 C.F.R. §154.1(d) (2003).

[35] Panhandle Eastern Pipe Line Co. v. FERC, 204 F.2d 675 (3rd Cir. 1953) (pipeline not obligated to build new facilities for shippers, but not in the context of a remedy).

[36] See Order No. 637, FERC Stats. & Regs. Regulations Preambles ¶ 31,091, at 31,287; Order No. 637-A, FERC Stats. & Regs. Regulations Preambles ¶ 31,099, at 31,570-71 (remedial measures may be needed if pipelines fail to construct in order to benefit affiliates).

(3) Whether LDCs and industrial end users are harmed by elimination of the cap

31. The LDCs assert the Commission has a broad duty under Section 7(b) to protect consumers, and that this duty is not confined merely to protecting consumers from the exercise of monopoly power by the pipeline.[37] The Commission finds that it has properly defined and pursued consumer protection under Section 7(b) of the Natural Gas Act with respect to the ROFR. While Section 7(b) may include broad duties, the primary purpose of the ROFR is and has been to protect captive customers from pipeline market power.[38] "The purpose of the right of first refusal is to protect captive long-term customers from the pipelines' exercise of monopoly power."[39] The exercise of pipeline monopoly power thus remains the appropriate context in which to evaluate the term matching cap.

32. The LDCs allege various forms of harm that will occur if they must meet contract terms that are more than five years. The primary harm alleged by the LDCs is that

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[37] Citing Tennessee Gas Pipeline Co., order on reh'g, 94 FERC & 61,097 at 61,400-401 (2001). In Tennessee the Commission stated it had "provided long-term shippers a ROFR to enable the Commission to make the finding required by NGA Section 7 that abandonment of service following contract expiration is in the public convenience and necessity. That is a broader standard than just controlling market power." The Commission also stated that "Order No. 637 narrowed the ROFR so that it would apply only to maximum rate contracts of 12 or more consecutive months of service in an effort to limit the right only to truly captive customers of the pipeline. Such truly captive customers deserve some added protection for continuity of service, since it is presumed they have ordered their affairs based on receiving services from the pipeline."

[38] Order No. 637, & 31,091 at 31,336; United Distribution Companies v. FERC, 88 F.3d 1105, 1137-39 (UDC). The Court's concern in UDC was that pre-granted abandonment would allow pipelines indirectly to extract monopoly profits from their customers. The Court found that the "basic structure of the right-of-first-refusal mechanism provides the protections from pipeline market power required for pre-granted abandonment under ' 7." 88 F.3d at 1140 (D.C. Cir. 1996), cert. denied, 117 S. Ct. 1723 (1997).

[39] Order No. 637 at 31,336 citing UDC, 88 F.3d 1105, 1140 and Order No. 636-C, 78 FERC & 61,186 at 61,772-773 (1997).

removal of the term cap will increase the costs of natural gas service and discourage retail choice. This, they assert, will happen in several ways. First, the LDCs assert they currently have a public service obligation and, in the 20 states with retail unbundling, they are the supplier of last resort. Consequently, they state, LDCs must match the longest term bid for their expiring contracts, no matter what their needs. But, they assert, states with retail choice may eliminate the LDCs' obligation to be the supplier of last resort.[40] In that case, the LDCs assert, long-term contracts that LDCs have been forced to enter because of the removal of the term cap will result in stranded costs that retail customers will have to pay. For this reason, the LDCs assert that removal of the term cap will have a chilling effect on retail choice programs.

33. Requiring LDCs to match the longest term bid is necessary to ensure that scarce capacity is allocated to the party valuing that capacity the most. The LDCs have not explained why existing shippers are entitled to retain capacity that another shipper values more highly. If the existing shipper has more elastic demand (arising from alternative options) than a competing bidder, then efficiency is enhanced if the capacity is allocated to its most valued use and the existing shipper utilizes its alternative options.

34. Moreover, the harm alleged by the LDCs is that bidding long terms may conflict with their need to shed capacity in the event that a state implements retail unbundling or if other conditions change. But this harm fails to take into account the Commission's capacity release mechanism. If the LDC must bid longer terms to retain capacity through the ROFR process, it will be obtaining a valuable asset that it can then release. For example, if a state implements retail unbundling, that capacity will still be needed by the marketer or other gas provider to serve the same load. The LDC will then be able to release its capacity to the marketer to satisfy the same load, thereby obtaining reimbursement of its reservation charges. Under Commission policy, the LDC can permanently release its capacity to a qualified and creditworthy shipper, thus extinguishing its contractual obligation to the pipeline.

35. Further, the Commission finds that these forms of harm alleged by the LDCs are speculative. It is not certain that states that have retail choice programs will eliminate the obligation of LDCs to be suppliers of last resort, and if they do, it is not certain that LDCs so affected will have made contracts for more than five years that will lead to stranded

[40] BG&E states it is currently unsettled in most retail access states as to whether there will be only limited terms placed on the obligation of local gas distributors to act as the provider of last resort.

costs. The Industrials' study concluded that while the five-year cap was in effect, from 1997 through 2002, it had little or no impact on contracting practices. It found that during the period that the five-year cap was in effect, very few contracts with terms of five years or more were signed each year.[41] If competing customers did not bid up to five years to obtain capacity while there was a five-year cap, there appears little reason why they would bid for a longer period once the cap is removed. Finally, if LDCs find themselves with excess capacity, they may take advantage of capacity release to reduce their costs.

36. The AGA asserts costs will be increased because LDCs will not be able to decrease their capacity within a reasonable time if substantial numbers of their retail customers switch to other suppliers. But the AGA provides only anecdotal evidence of one unnamed LDC that allegedly experienced a large switch in retail customers. This is insufficient evidence on which to base a finding of harm to LDCs in general.

37. Third, the LDCs assert that LDCs with very long contracts will not be able to participate in the development of new supplies or expansion projects. The Commission also finds this claim of harm to be speculative. As indicated above, there is no support for the LDCs' assumption that other shippers will insist on terms of more than five years. In any event, the LDCs have choices. They can exercise their ROFR for a volumetric portion of their existing capacity which would leave them free to contract for transportation on new pipelines. They could also choose not to exercise a ROFR and subscribe to new capacity in the amount they are giving up. Last, one LDC asserts that unregulated shippers could acquire firm transportation service and either exercise market power over retail customers at certain delivery points or re-designate delivery points. But this would occur only if an LDC did not exercise its ROFR, and, again, it is speculative.

38. The harm alleged by the Industrials is somewhat different.[42] The Industrials claim they cannot easily make contracts for more than five years or over a certain dollar amount because such contracts require the approval of their boards of directors or other management officials. They also claim the energy needs of industrial facilities vary dramatically from year to year due to fluctuations in demand for products, plant closures,

[41] Appendix A, Attachment 1 at 2, 3, 7, and Figure 1, Process Gas Consumers' Group Request for Rehearing. Contracts for five years comprised 2.5% to 4.0% of total contracts on a yearly basis.

[42] See, for example, Process Gas Consumers' Group Request for Rehearing at 18-20.

new technology, and changes in the relative prices of different and competing types of energy.[43]

39. The Commission finds the claims of harm raised by the Industrials are unpersuasive. As explained above, Industrials that purchase valuable capacity can release that capacity if their needs change. If internal procedures are an obstacle to making long term contracts, then the remedy is to change those procedures. If fluctuations in their need for gas are so great from one year to the next, then it would not appear that they would find a five-year contract desirable any more than a contract for more than five years. They would experience the same problems with a contract of either length. Finally, it appears that the Industrials, or some of them, have access to alternate sources of fuel and are not wholly dependent on natural gas or on natural gas from one pipeline and so, do not need the protection of a ROFR to the same degree as a customer that is a captive customer, that is, a customer dependent on one pipeline for its supply of energy.

(4) Whether the Commission must adopt a five-year cap

40. The Commission disagrees with the shippers' claims that it failed to respond to the Court's remand of the five-year term matching cap. The Commission is not obligated, as the shippers claim, to consider only reinstituting the five-year cap on remand. Instead, when orders are remanded, an agency generally has discretion to reconsider the whole of its original decision.[44]

41. The shippers support a five-year cap and assert the Commission has ignored the evidence supporting a five-year cap.[45] They assert a cap of five years falls within a zone of reasonableness of 3 to 10 years. The AGA asserts that both the mean and the median

[43] NWIGU Request for Rehearing at 5.

[44] PGC, 292 F.3d at 837 (affirming removal of 20-year term cap for bidding for new capacity); Southeast Michigan Gas Co. v. FERC, 133 F.3d 34 (D.C. Cir. 1998); Tennessee Gas Pipeline Co., 94 FERC & 61,097 at 61,398 (2001).

[45] The AGA cites Table 1 in the Commission's May 31, 2002 Notice, 99 FERC & 61,245 (2002), and Index of Customer data in its Comments of June 30, 2002 at 12-13 in this proceeding. The PGC cites its own data contained in its Comments of July 30, 2002 at 14-19 and Attachment 1, and in its Rehearing Request of November 27, 2002 at 42-49 and Attachment 1 to Appendix A.

of all contracts in the January, 2002 Index of Customer contracts were less than five years.[46] The shippers also assert a five-year cap does not interfere with market forces because more contracts were signed for terms of less than five years than were signed for five years[47] and, also because more contracts were signed for a term of five to ten years than were signed for five years.[48]

42. The Commission is aware of the evidence concerning the length of long term contracts and considered this evidence in its deliberations concerning a ROFR term matching cap.[49] However, the Commission sees nothing in this evidence to suggest that continuation of the term matching cap is necessary or appropriate. Assuming, as the rehearing applicants assert, that this evidence shows a three to ten year zone of reasonableness for contract terms, we see no reason to assure existing shippers that their contract terms will always be at the lower end of the zone of reasonableness, regardless of the willingness of other shippers to bid longer terms that are still within the zone of reasonableness. That the median and average contract terms are less than five years, and thus near the low end of the asserted zone of reasonableness, is consistent with our finding above that current regulatory controls are sufficient to minimize pipelines' incentive to exercise monopoly power to create an artificial scarcity of capacity, so as to force shippers to bid longer contract terms than the market would require. In any event, even if five years is a reasonable cap, the Commission is not obliged to adopt it where there are other reasonable policies. The Commission has adopted a reasonable policy here consisting of removal of the cap.

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[46] Request for Rehearing at 27-28 where the AGA asserts that in 2002, the mean for contracts effective after January 1, 1999 was 4.72 years and the median contract term was 3 years.

[47] The AGPA cites the Commission's Table 1 data which it asserts show that almost 60% of the contracts with terms of five years or less had terms of one to two years, while only about 15% had terms of five years.

[48] The AGA states that according to its Index of Customer study, there were 161 contracts for five years and 301 contracts for five to ten years among the contracts entered after January 1, 1999. See Comments at 12-13.

[49] Order on Remand, Ps 19-20.

43. Finally, as the Commission stated in the Order on Remand, eliminating the term matching cap addressed the various objections to the five-year cap.[50] First, it satisfied those of the INGAA court and the pipelines that a cap fosters an imbalance of risks between pipelines and existing customers and adversely affects the efficient allocation of capacity. Second, it addressed the objections of the INGAA court that the five-year cap provides a disincentive for existing shippers to enter into a contract of more than five years and thus results in a bias toward short-term contracts which, in turn, increases the risk to pipelines that they will be left with stranded capacity. The Commission also found that removing the term cap avoided the difficulty that the Commission has no way of estimating what contract terms a competitive market would produce, since there is no widespread competitive market for primary pipeline capacity.

II. Whether Pipelines Must Allow Segmented Transactions Consisting of Backhauls and Forwardhauls Both Up to Contract Demand to the Same Point

A. Background

44. The Commission established the policy of segmentation and expanded the policy of flexible point rights in Order No. 636.[51] Segmentation refers to the ability of firm capacity holders to subdivide their capacity into segments and to use the segments simultaneously for different capacity transactions.[52] The requirement to permit segmentation was not included in the Commission's regulations, but was implemented through pipeline restructuring filings.

45. Flexible point rights refer to the rights of firm shippers to change receipt or delivery points so they can receive and deliver gas to any point within the firm capacity rights for which they pay.[53] The Commission's flexible point policy distinguishes between primary points and secondary points.[54] Firm contracts between pipelines and

[50] Order on Remand Ps 16-18.

[51] Order No. 636 & 30,939 at 30,420-421 and 30,428-429; Order No. 636-A at 30,559 n.151 and 30,582-586; Order No. 636-B, 61 FERC & 61,272 at 61,997 (1992).

[52] Order No. 637-A at 31,589.

[53] Order No. 637-A at 31,589.

[54] See Transcontinental Gas Pipe Line Corp., 104 FERC ¶ 61,171 P 24-25 (2003).

their shippers typically provide that the pipeline will transport up to a specified contract demand from a primary receipt point or points listed in the contract to a primary delivery point or points listed in the contract. This provision specifies a shipper's guaranteed right to firm service. The Commission requires that pipelines permit shippers to change their primary points, as long as there is sufficient unsubscribed capacity available. However, because the primary points are listed in the contract, this requires a change in the contract.[55] Since Order No. 636, the Commission has also required that firm shippers be permitted to schedule service at all other points in the zones for which they pay reservation charges on a secondary basis. A firm shipper seeking to schedule service at a secondary point has a lower priority than a shipper using that point as a primary point. As explained in the Order on Remand, the Commission has implemented its secondary point policy by acting under NGA Section 5 to change the pipeline's general terms and conditions of service. It has not been necessary to change shipper contracts for this purpose, since those contracts provide for shippers to receive the service set forth in the general terms and conditions of the pipeline's tariff, as those terms may be changed from time to time.

46. In Order No. 637, the Commission again addressed segmentation of capacity and flexible point rights. It found that its segmentation policy was not being uniformly implemented across the pipeline grid. Some pipelines did not permit segmentation at all or only permitted it for release purposes, but not for the shipper's own use. To improve competition, the Commission required pipelines to permit shippers to segment their capacity for their own use and for release to the extent operationally feasible,[56] included this requirement in its regulations,[57] and required pipelines to make a pro forma tariff filing to show how they would comply with the regulation either by revising their tariff, explaining why their existing tariff met the requirements, or explaining why the operational configuration of their system did not permit segmentation.[58] The Commission also adopted the policy in Order No. 637 that shippers in segmented transactions must be able to change and add primary points.[59]

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[55] Tennessee Gas Pipeline Co., 94 FERC ¶ 61,097 at 61,402 (2001).

[56] Order No. 637 & 31,091 at 31,301.

[57] 18 C.F.R. ' 284.7(d) (2003).

[58] Order No. 637 & 31,091 at 31,304; Order No. 637-A & 31,099 at 31,590.

[59] Order No. 637-A & 31,099 at 31, 593-595.

47. In addition, in Order No. 637, the Commission addressed segmented transactions that include backhauls. Shippers may segment their capacity into segments that overlap on the mainline, but may only transport volumes up to the contract demand of the underlying contract in the overlapping segments. In Order No. 637-A, the Commission considered whether a backhaul and a forwardhaul to the same point constituted an overlap. It noted it had previously determined that a forwardhaul and a backhaul to a single point for nomination purposes did not result in a capacity overlap, even though the total amount received by the shipper exceeded contract demand.[60] Thus, the Commission found that in a segmented transaction, a shipper could deliver its full contract demand to a point through a forwardhaul and, at the same time, deliver its full contract demand to the same point through a backhaul because there was no capacity overlap.[61]

48. In Order No. 636-B, the Commission clarified that the general principle that firm shippers should be able to make full use of their pipeline capacity through release transactions applies to backhaul arrangements.[62] In Order No. 637-A, the Commission noted that both the releasing and the replacement shippers would retain the flexibility to use their capacity to make a backhaul as well as a forwardhaul to the same point at the same time.[63]

49. On appeal, INGAA agreed that a segmented transaction consisting of a forwardhaul and a backhaul to the same point does not exceed contracted-for capacity on the mainline, but asserted this transaction does exceed a shipper's contracted-for capacity at the delivery point. In INGAA the Court noted that segmentation had been established in Order No. 636.[64] It affirmed the Commission's generic finding that a pipeline's refusal to permit segmentation where it could operationally do so would be unjust and

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[60] Order No. 637-A & 31,099 at 31,593 citing Transcontinental Gas Pipe Lin Corporation, 91 FERC & 61,031 (2000).

[61] Order No. 637-A & 31,099 at 31,592-593.

[62] Order No. 636-B, 61 FERC & 61,272 at 61,997 (1992).

[63] Order No. 637-A, ¶ 31,099 at 31,592.

[64] INGAA at 36.

unreasonable[65] and the general validity of the Commission's segmentation policy.[66] The Court also found that the new segmentation rule, that is, the segmentation rule as elaborated in Order No. 637 to include a regulation and the mandatory use of additional primary points for segmented transactions, "represents a continuation of past policy rather than a break with it, and no further special showing was required for the continuation of that policy."[67] With regard to the backhaul/forwardhaul policy, the court found the Commission had not adequately addressed whether this policy modified the contracts between the pipeline and its shippers and had not adequately supported the need for any such contract modification.[68] The Court remanded this issue for further explanation, without reversing or vacating the Commission's holdings.

50. In its Order on Remand, the Commission reaffirmed its prior determination that a segmented transaction consisting of a backhaul and a forwardhaul to the same point that exceed a shipper's contract demand at the point is permissible. The Commission found it may require pipelines to permit a forwardhaul and a backhaul, each up to the shipper's mainline contract demand, to the same delivery point by making the necessary findings under Section 5 of the Natural Gas Act and requiring pipelines to incorporate such provisions in their tariffs. The Commission found it need not modify any term in the individual service agreements between pipelines and their shippers to accomplish this, since the service agreements incorporate the terms and conditions in the tariff.

51. The Commission found further in the Order on Remand that the backhaul/forwardhaul policy does not modify the quantity term for delivery at points in the service agreements because that term describes primary point rights, while the backhaul/forwardhaul policy only affects secondary point rights. The Commission stated it was providing an additional right for firm shippers to use delivery points on a secondary basis through the backhaul/forwardhaul policy. The Commission noted it has expanded secondary point rights generally through its segmentation and flexible points policies and that shippers may deliver more than their contract demand in other segmented transactions because of these policies. The Commission stated it has expanded

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[65] INGAA at 37.

[66] INGAA at 37-38.

[67] INGAA at 40.

[68] INGAA at 41.

shippers' ability to use secondary points by requiring pipelines to change their tariffs pursuant to NGA Section 5.

52. The Commission made explicit findings under Section 5 in the Order on Remand with regard to the backhaul/forwardhaul policy. The Commission noted it had found in Order No. 637 that failure to permit segmentation is unjust and unreasonable. The Commission found that the backhaul/forwardhaul transaction is a type of segmented transaction and that failure to permit it is unjust and unreasonable for the same reason that failure to permit other segmented transactions is unjust and unreasonable: it restricts the efficient use of capacity without adequate justification.[69] The Commission found that permitting the backhaul/forwardhaul segmented transaction is just and reasonable because it creates additional supply alternatives for shippers and enhances competition on the pipeline's system. The Commission also found it is just and reasonable because it provides the kind of flexibility that pipelines enjoyed prior to Order No. 636 and because it will assist in creating more competition in the transportation market. The Commission required pipelines that must permit segmentation on their systems to file revised tariff sheets providing that a shipper, or a releasing shipper and a replacement shipper, may segment their capacity by simultaneously transporting their full contract demand in a forwardhaul and their full contract demand in a backhaul to the same point at the same time.

B. Rehearing Requests

53. Requests for rehearing on the backhaul/forward haul issue were filed by pipelines and organizations representing pipelines. The requesters are the Interstate Natural Gas Association of America (INGAA); Kinder Morgan Interstate Gas Transmission L.L.C. (KMIGT); Texas Eastern Transmission, L.P., Algonquin Gas Transmission Co., and East Tennessee Natural Gas Co., subsidiaries of Duke Energy Gas Transmission Corp. (collectively, DEGT); Gulfstream Natural Gas System, L.L.C. (Gulfstream); ANR Pipeline Co. (ANR); and Tennessee Gas Pipeline Co. (Tennessee).

54. In addition, Piedmont Natural Gas Company, Inc. (Piedmont) filed a motion for leave to file an answer and an answer to the requests of DEGT. DEGT then filed a motion for leave to answer and an answer to Piedmont. The Commission grants the motions and accepts the answers as useful in creating a more complete record in this case.

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[69] Citing Order No. 637 at 31,304; Order No. 637-A at 31,591.

C. Discussion

(1) Whether the backhaul/forwardhaul transaction violates pipeline service agreements

55. In this section, the Commission discusses whether the backhaul/forwardhaul policy violates pipelines' service agreements. It finds that the policy does not violate these agreements because it does not affect the primary capacity that is established in the service agreements.

56. INGAA and the pipelines assert that the Commission's backhaul/forwardhaul policy impermissibly expands shippers' contract rights because it permits a shipper to take gas volumes equal to two times its contract demand at a point. INGAA asserts the policy alters shippers' contracts by increasing the contractual quantity of gas to be delivered on a daily basis for the particular customer.[70] The pipelines assert the Commission may not modify the MDQ specified in their contracts which is to be delivered on a primary point basis. DEGT, in particular, indicates the Commission has changed the provisions in Texas Eastern's terms and conditions and its service agreements that limit the amount of gas Texas Eastern will deliver at a point to the customer's maximum daily quantity (MDQ).[71] The pipelines also assert that even if the backhaul service will be provided on a secondary basis, the Commission must support modifying gas contracts to provide for this service in an amount that may exceed a shipper's MDQ at a point.

57. As discussed below, the Commission finds these assertions do not require the Commission to change its backhaul/forwardhaul policy. First, the Commission finds that the backhaul/forwardhaul policy affects secondary point rights, not primary point rights, and that, consequently, it does not modify the contractual amount terms (MDQ) in shippers' contracts. In the pro forma gas service agreements for firm transportation service, the parties specify the maximum amount of gas (maximum daily quantity or MDQ or CD) the pipeline must deliver on a daily basis to the shipper. The parties also specify the maximum amount of gas to be delivered to particular primary delivery points

[70] Request for Rehearing at 9 and 15.

[71] DEGT cites, for example, Texas Eastern's service agreement for FT-1 service, Articles I and IV.

on a daily basis. These amounts are called variously volumes, maximum volumes, Quantity, Maximum Daily Delivery Obligation, and so on. They define a shipper's primary firm delivery rights at a point.[72] The contract quantity provisions, both the MDQ and the point quantities, define the shippers' guaranteed primary firm rights to deliveries.[73] They define the amount of gas a shipper can take at a point on a primary firm basis.

58. The backhaul/forwardhaul policy does not impose on the pipeline any obligation to provide firm primary service beyond that set forth in the pipeline's contracts with its firm shippers or otherwise affect shippers' firm primary rights to deliveries. The Commission has found that when a backhaul is a reversal of the contract flow, which is usually the case, it is an out-of-path, secondary firm transaction. As such, it receives a lower scheduling priority than primary firm service (and within-the-path secondary service).[74] It does not affect the amount of primary firm deliveries the pipeline must make. Thus, the Commission has not increased a shipper's entitlement to take gas at a point on a primary firm basis through the backhaul/forwardhaul policy and has not modified the MDQ terms in pipeline contracts through the backhaul/forwardhaul policy. Consequently, there has been no violation of pipelines' contracts.

59. The pipeline's deliveries in the secondary backhaul transaction do mean that, added together, the deliveries in the primary forwardhaul transaction and the secondary backhaul transaction exceed the contract demand in the shipper's contract. But this result is not significantly different from what occurs in other types of segmentation required under Order Nos. 636 and 637. For example, if a shipper has a contract demand (CD) of 100 Dt from points A to C, with primary delivery point rights of 100 Dt at point C, it could divide its capacity into geographic segments, A to intervening secondary Point B and B to C. It could then take 100% of its CD in each segment, with deliveries at B depending on secondary point rights. The combined deliveries would total 200 Dt, while the shipper's CD is only 100 Dt. Thus, in both sets of transactions, the pipeline has made combined deliveries to a single shipper exceeding that shipper's mainline contract demand, but deliveries made on a primary basis do not exceed contract demand.

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[72] Primary firm has the highest priority. It is superior to all other delivery rights.

[73] <u>Order</u> <u>on</u> <u>Remand</u> P 48, citing Tennessee Gas Pipeline Co., 94 FERC ¶ 61,097 at 61,402 (2001).

[74] Tennessee Gas Pipeline Co., 99 FERC ¶ 61,017 at 61,064-65 (2002).

60. INGAA asserts, however, that the obligation to permit forwardhauls and backhauls to the same point is substantially different from the other types of segmentation required under Order Nos. 636 and 637 because, in INGAA's view, it multiplies a shipper's capacity at a point, while other segmentation transactions, according to INGAA, divide a shipper's capacity at a point. However, we see no substantive difference between the forwardhaul/backhaul to the same point situation and other types of allowed segmented transactions. The key point is that in the forwardhaul/backhaul situation, as in other permitted segmented transactions, any deliveries in excess of contract demand take place on a secondary basis, so that there is no requirement that the pipeline provide greater primary firm service than required in its contract.

61. In fact, it can be argued that the requirement to permit a segmented backhaul to the same point as a segmented forwardhaul is less burdensome on the pipeline than the two segmented forwardhaul transactions example illustrated above. That is because the fowardhaul/backhaul transactions may use less mainline capacity than two segmented forwardhaul transactions. This may be illustrated using the same example given above, where the shipper has a CD of 100 Dt from points A to C, with primary delivery point rights of 100 Dt at point C. To do a forwardhaul and backhaul to the same point, the shipper could schedule a fowardhaul of 100 Dt to flow from A to intervening secondary point B and also schedule a segmented backhaul from C to B of 100 Dt. On the mainline, 100 Dt will flow from A to B and be delivered to the shipper at point B. Another 100 Dt will also be delivered to the shipper at B, but this amount will be taken from gas put on the system by someone else. The shipper will restore the 100 Dt to the system at point C. Thus, as a physical matter, the shipper will use 0 Dt of capacity from B to C, leaving that capacity available for use by the pipeline for interruptible service. This contrasts with the example above of two segmented forwardhaul transactions in which the shipper is actually moving 100 Dt all the way from point A to point C.

62. In its response to Piedmont, DEGT asserts that Texas Eastern's service agreement contains provisions that limit service at a point and that the Commission's backhaul/forwardhaul policy alters these provisions. DEGT cites Articles I and IV of Texas Eastern's FT-1 service agreement.[75] DEGT states that allowing a doubling of the

[75] Article I of Texas Eastern's FT-1 service agreement provides, among other things, that subject to the pipeline's rate schedule FT-1 and the General Terms and Conditions of its tariff, it will provide firm transportation service. It also contains a blank in which to write in the Maximum Daily Quantity (MDQ) of the service. Article IV of
(continued…)

MDQ (maximum daily quantity) is a direct violation of the primary point limitations contained in the Texas Eastern contract[76] and that simply changing the general terms and conditions of the tariff would not change the Commission-approved language in the service agreement.

63. The Commission disagrees with DEGT that the backhaul/forwardhaul policy violates Texas Eastern's service agreements. As with other pipelines, the maximum daily quantity and the receipt and delivery point terms in Texas Eastern’s service agreements define primary point rights, not secondary point rights. The quantity provision of Article I and the receipt and delivery point provisions of Article IV of Texas Eastern’s FT-1 service agreement refer to primary point rights.[77] Thus, the backhaul/forwardhaul policy, which provides secondary point rights, does not change the maximum daily quantity term or the terms describing deliveries at a point in Texas Eastern’s service agreements.

64. In addition, pipeline service agreements, including Texas Eastern's, are subject to the general terms and conditions of pipeline tariffs. With regard to Texas Eastern, Article III of its FT-1 service agreement provides that the service agreement "in all respects shall be and remain subject to the applicable provisions of Rate Schedule FT-1 and of the General Terms and Conditions of [Texas Eastern's] FERC Gas Tariff on file with the Federal Energy Regulatory Commission, all of which are by this reference made a part" of the service agreement.[78] The Commission may and has changed the terms and conditions of pipeline tariffs, including those of Texas Eastern, by making findings under section 5 of the Natural Gas Act, based on substantial evidence, that those provisions are unjust and unreasonable and requiring them to be replaced by just and reasonable

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Texas Eastern's FT-1 service agreement provides, among other things, that the points of receipt and delivery will be specified on Exhibits A and B of the service agreement.

[76] For Texas Eastern's FT-1 service, daily amounts to be delivered at firm receipt and delivery points are designated “Maximum Daily Receipt Obligation” and “Maximum Daily Delivery” on Exhibits A and B to the FT-1 service agreement (Original Sheet Nos. 822 and 823).

[77] 101 FERC ¶ 61,127 P 48.

[78] Article III, Form of Service Agreement for Rate Schedule FT-1, Original Sheet No. 818, Texas Eastern Transmission, L P, FERC Gas Tariff, Seventh Revised Volume No. 1.

provisions. With respect to the backhaul/forwardhaul policy, it has found under section 5 that failure to permit the backhaul/forwardhaul transaction is unjust and unreasonable and that this unjust and unreasonable practice must be replaced by the just and reasonable practice of permitting this segmented transaction. [79] These findings apply to Texas Eastern as well as to other pipelines.

65. The pipelines also assert that even if the backhaul service will be provided on a secondary basis, the Commission must support modifying gas contracts to provide for this service in an amount that may exceed a shipper's MDQ at a point. As explained in the Order on Remand and in this order, the Commission has not modified the MDQ in pipeline contracts or the amounts in those contracts that are to be delivered at points. All of these quantities are primary firm obligations. The backhaul/forwardhaul policy does not modify pipelines' primary firm obligations. The Commission has expanded shippers' secondary point rights through the backhaul/forwardhaul policy. As explained more fully in the Order on Remand and elsewhere in this order, this expansion of secondary rights is justified because the shipper has already paid for service within the zone and because it increases competition on the pipeline.

(2) Whether the backhaul/forwardhaul policy gives shippers more than they pay for

66. INGAA and some pipelines object to an expansion of secondary rights in the backhaul/forwardhaul transaction on the grounds that shippers would be getting more service than they are paying for. INGAA[80] asserts the Commission has given away a service for which a shipper formerly would have paid and that the backhaul/forwardhaul policy gives shippers a free backhaul.

[79] Whether the provisions of Texas Eastern's tariff comply with Order Nos. 636 and 637 with respect to segmentation, flexible point rights, and the backhaul/forwardhaul policy has been reviewed in its Order No. 637 compliance filings in Docket Nos. RP00-468-000, RP01-25-000, and RP03-175-000. In those proceedings, Texas Eastern has implemented provisions to permit backhauls and forwardhauls up to MDQ at the same point. 102 FERC ¶ 61,198 P 144-153 (2003); 103 FERC ¶ 61,278 (2003).

[80] Request for Rehearing at 10.

67. Piedmont argues, to the contrary, that there is no free give-away of capacity[81] because pipeline rates are designed to be fully compensatory based on the recovery of fixed costs through reservation charges associated with primary firm capacity rights and variable cost recovery through volumetric charges. Second, Piedmont argues that the Commission has approved all secondary delivery transactions, including the backhaul/forwardhaul transaction because shippers utilizing such transactions have essentially paid all of the pipeline's fixed costs, including its rate of return, in the zone-wide reservation charges associated with their primary firm capacity and are, therefore, entitled to use the capacity and the facilities they had paid for in as flexible a manner as possible.

68. The Commission agrees with Piedmont and rejects the arguments of INGAA. As the Commission has noted previously, a shipper pays to use all of the capacity, including the points, within a zone. The Commission has permitted the shipper to use the points it has not specified as primary points on a secondary basis because it has already paid for service within the zone. As the Commission stated in the Order on Remand, it is the Commission's policy that a shipper may use all of the points in a zone for which it is paying on a secondary basis precisely because the shipper must pay the costs of the entire zone.[82] The Commission also stated that the general principle that firm shippers should be able to make full use of their pipeline capacity specifically applies to backhaul arrangements in capacity releases[83] and to other segmented transactions. The shipper is getting no more than what it pays for. The pipeline, for its part, has fully allocated its costs and is collecting those costs from its shippers. The Commission also stated in the Order on Remand that if this type of segmented transaction should cause a decrease in IT or short-term firm transportation that the pipeline can sell, then the pipeline is permitted to file a new rate case in which more of its costs would be allocated to firm service.

69. INGAA also objects that a backhaul/forwardhaul transaction in which the backhaul has secondary status will degrade secondary forwardhaul service. INGAA argues that the Commission has adopted a policy against the degradation of secondary

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[81] Piedmont Motion for Leave to File Answer and Answer at 15-16.

[82] 101 FERC ¶ 61,127 P 56.

[83] Citing Order No. 636-B, 61 FERC ¶ 61,272 at 61,997 (1992).

forwardhaul service by providing secondary service for backhauls, citing Tennessee Gas Pipeline Co., 84 FERC ¶ 61,083 (1998).

70. The Commission rejects this argument. First, in Tennessee, the Commission accepted a firm backhaul service subject to the outcome of the Order No. 637 rulemaking proceeding. In that case, the backhaul service was a primary service, it was not a reversal of a forwardhaul service. The issue of the priority of secondary backhaul and forwardhaul services is different.

71. Subsequently, in Tennessee's Order No. 637 proceeding, the Commission settled the priorities of forwardhaul and backhaul services that are both secondary. The Commission held that a transaction that is a reversal of the contract flow has a secondary basis and is also outside the contract path. Thus, a backhaul that is a reversal of the contract flow is a secondary transaction and is also outside the path. As such, it is subordinate to forwardhaul transactions using secondary points within the contract path. Tennessee Gas Pipeline Co., 99 FERC ¶ 61,017 P 90-95 (2002). Thus, there is no degradation of secondary forwardhaul service. When that service is within the path, it takes priority over backhaul service that has a secondary status.

(3) Whether the Commission has met the requirements of Section 5

72. INGAA insists that, with respect to the backhaul/forwardhaul policy, the Commission has not met the requirements of Section 5. First, it insists that the Commission must show that not allowing shippers to backhaul and forwardhaul to the same delivery point an amount which is two times the shipper's contract demand is unjust and unreasonable and, second, that providing shippers this right is just and reasonable. The Commission rejects this argument. The Commission finds it has fulfilled the requirements of Section 5 with regard to its backhaul/forwardhaul policy.

73. As discussed elsewhere in this order and in the Order on Remand,[84] the backhaul/forwardhaul transaction does not permit a shipper to double its primary firm capacity at a point, as INGAA's argument implies. Instead, it permits a shipper to have secondary point rights for a backhaul at the same point at which it delivers its MDQ on a firm primary basis. The Commission must show under Section 5 that failure to permit this expansion of secondary rights is unjust and unreasonable and that permitting it is just and reasonable. The Commission has made these showings.

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[84] 101 FERC ¶ 61,127 P 48.

74. The Commission found generally under Section 5 in Order Nos. 636 and 637 that shippers should have secondary rights to use all points in zones for which they are paying. The Commission found in Order No. 636 that this increased use of the pipeline system was warranted to provide shippers with the same flexibility that pipelines had prior to restructuring and also to promote the maximum efficient usage of the pipeline system, the development of market centers, and the achievement of a meaningful capacity release program.[85] The Commission found in Order No. 637 that failure to permit segmentation is unjust and unreasonable because it restricts efficient use of capacity without adequate justification. These findings in Order Nos. 636 and 637 are applicable to and support the Commission's backhaul/forwardhaul policy, a transaction which arises out of the policies of segmentation and flexible point rights.

75. Thus, the Commission here reiterates and affirms its holdings in the Order on Remand, that failure to permit the segmented backhaul/forwardhaul transaction restricts the efficient use of capacity without adequate justification, and, like the failure to permit other segmented transactions, is unjust and unreasonable.[86] The Commission also reiterates and affirms its prior holding that requiring the backhaul/forwardhaul transaction is just and reasonable for the same reasons that other segmented transactions and transactions using secondary points are just and reasonable, i.e., they create additional supply alternatives for shippers, enhance competition on the pipeline's system, and give shippers the same flexibility the pipeline enjoyed prior to Order No. 636. The Commission has fulfilled the requirements that it make substantial findings concerning its backhaul/forwardhaul policy based on substantial evidence.

76. INGAA also asserts that the Commission has not put forward concrete examples of how pipelines have prevented shippers from accessing backhaul capacity or why the current open access rules bar shippers from full and efficient use of existing pipeline capacity in both directions. INGAA contends the Commission has not provided any support for the backhaul/forwardhaul policy other than the policy justifications of increased efficiency and flexibility that it provided when it issued Order No. 637 and that it has failed to develop an adequate record.

77. The Commission rejects these arguments as well. First, the Commission may make generic findings based on generic evidence when it exercises its authority under

[85] Order No. 636-A at 30,582.

[86] 101 FERC ¶ 61,127 P 54, 55, 58.

Section 5 in a rulemaking proceeding. It is not required to present evidence with regard to specific pipelines.[87] In any event, the Commission is not obligated to create a new record to support the backhaul/forwardhaul transaction because it is simply one type of transaction that can be performed under the Commission's segmentation and flexible point policies. The Commission has already presented evidence regarding segmentation and flexible point rights in the Order No. 636 proceeding,[88] and these policies have already been ruled on and approved by the court.[89] Contrary to INGAA's assertions, there is no need for further evidence concerning segmentation or flexible receipt and delivery points. As discussed in this order, the backhaul/forwardhaul policy is part of and an instance of the Commission's segmentation and secondary point rights policies and is supported by the findings with respect to those policies.

(4) Whether the Commission adequately responded to the Court's remand

78. INGAA and the pipelines contend the Commission has not adequately responded to the Court's remand of the backhaul/forwardhaul policy because it has not explained whether and how the backhaul/forwardhaul policy alters pipelines' contracts and, if there has been a contract modification, the Commission has not justified the modification.

79. The Commission disagrees. The Court remanded the backhaul/forwardhaul issue for the Commission to provide adequate support for modifying shippers' contracts so that they could perform a backhaul and a forwardhaul to the same point at the same time in a segmented transaction, both up to MDQ. In response, the Commission explained its policy had no effect on the primary point capacity terms contained in shippers' service agreements. The Commission explained that, instead, it had modified the terms and

[87] INGAA, 285 F.3d at 37; Transmission Access Policy Study Group v. FERC, 225 F.3d 667, 688 citing Associated Gas Distributors v. FERC, 824 F.2d 981, 1008-09 (D.C. Cir. 1987) and 711 (D.C. Cir. 2000); Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1158 (D.C. Cir. 1985).

[88] Order No. 636 at 30,420-21 and 30,428-429; Order No. 636-A at 30,559 n. 151; Order No. 636-B, 61 FERC & 61,272 at 61,997 (1992).

[89] The policies of segmentation and flexible receipt and delivery points were not challenged in the appeal of Order No. 636 and that order was approved in United Distribution Companies v. FERC, 88 F.3d 1105 (D.C. Cir. 1996).

conditions of pipeline tariffs which are applicable to shippers' contracts and that it was expanding shippers' secondary point rights through these modifications.

80. The Commission believes that the explanations and determinations in the Order on Remand, supplemented by those in this order, adequately respond to the Court's remand. They describe how the backhaul/forwardhaul policy modifies pipeline tariffs and, through the tariffs, apply to pipeline contracts to expand shippers' secondary point rights. They explain that, as part of the Commission's policies on segmentation and flexible point rights, the backhaul/forwardhaul policy is supported by the same findings that support those policies. They explain that the backhaul/forwardhaul policy expands shippers' secondary point rights in a manner similar to other segmented transactions. The Commission thus believes that it has responded adequately to the court's concern that the backhaul/forwardhaul policy was an unjustified modification of pipelines' contracts.

(5) Whether the public interest standard applies

81. INGAA and DEGT assert the Commission may only adopt the backhaul/forwardhaul policy if it can meet the public interest standard established in the Mobile and Sierra cases,[90] which they insist is more stringent than the just and reasonable standard in Section 5, citing, inter alia, Atlantic City Electric Company v. FERC, 295 F.3d a, 14 (D.C. Cir. 2002), Order on Remand, 101 FERC & 61,318 (2002); Exxon Corporation. v. FERC, 206 F.3d 47, 49-50 (D.C. Cir. 2000).

82. The Commission does not agree that the Mobile-Sierra public interest standard is applicable here. The Commission affirms it may proceed under the just and reasonable standard and may use its authority under Section 5 to find that prohibiting backhauls and forwardhauls to the same point is unjust and unreasonable and to adopt the just and reasonable practice of allowing these transactions.

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[90] United Gas Pipe Line Co. v. Mobile Gas Service Corp., 350 U.S. 332 (1956) (this case involves a gas pipeline and determines it could not unilaterally change the price term in a bilateral contract with an agreed upon term by making a filing with the Commission. It mentions, but does not discuss, the Commission changing bilateral contracts with rate terms when it is in the public interest). Federal Power Commission v. Sierra Pacific Power Co., 350 U.S. 348 (1956) (this case involves an electric utility and discusses the public interest standard).

83. The Mobile-Sierra doctrine is not applicable to the contracts at issue here. As discussed below, the Mobile-Sierra doctrine applies to contracts in which the pipeline and the customer agree on a rate and the parties give up the right to change the agreed upon rate unilaterally. The contracts at issue here do not have these characteristics. They are not bilateral agreements that establish a rate and they contain clauses or are subject to provisions that permit the pipeline to change the rate unilaterally.

84. The Mobile-Sierra doctrine holds that "where parties have negotiated a natural gas shipment contract that sets firm prices or dictates a specific method for computing shipping charges and that denies either party the right to change such prices or charges unilaterally, FERC may abrogate or modify the contract only if the public interest so requires." Texaco Inc. v. FERC, 148 F.3d 1091,1095 (D.C. Cir. 1998).[91] Where the utility or natural gas company and its customer have contracted for a particular rate and the agency has accepted the contract for filing and allowed the rate to become effective, the Commission's power to alter the contract under the just and reasonable standard is curtailed. Boston Edison Co. v. FERC, 233 F.3d 60, 65 (1st Cir. 2000). However, the parties can negate the protection afforded by Mobile-Sierra by providing that a contract rate initially fixed by the parties and filed with FERC can be overridden by FERC at any time under the just and reasonable standard. Boston Edison Co. v. FERC, 233 F.3d 60, 66 (1st Cir. 2000) citing United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division, 358 U.S. 103, 112 (1958); Papago Tribal Utility Auth. v. FERC, 723 F.2d 950, 953 (D.C. Cir. 1983), cert. denied, 467 U.S. 1241 (1984); Kansas Cities v. FERC, 723 F.2d 82, 87 (D.C. Cir. 1983).

85. Thus, the Mobile-Sierra doctrine applies if the pipeline and the shippers agree to a specific rate or to a rate changeable in a specific manner and there is no contractual language that the rate may be altered while the contract subsists. Texaco at 1096. Most pipeline contracts do not contain a rate negotiated between the pipeline and the customer

[91] Citing City of Oglesby v. FERC, 197 U.S. App. D.C. 378, 610 F.2d 897, 899-900 (D.C. Cir. 1979); Appalachian Power Co. v. FPC, 174 U.S. App. D.C. 100, 529 F.2d 342, 348 (D.C. Cir. 1976). In Texaco, the court found the Commission had met the public interest standard when it modified negotiated bilateral contracts for capacity constructed under optional expedited certificates by requiring standard fixed variable (SFV) rate design which collects all fixed costs in the reservation charge instead of modified fixed variable (MFV) rate design which collects some fixed costs in the commodity charge. See also Union Pacific Fuels, Inc. v FERC, 129 F.3d 157, 161-62 (D.C. Cir. 1997).

which cannot be changed unilaterally by the pipeline. Instead, most pipeline contracts since 1948 have been made under the tariff and service agreement system in which rates are set for all customers in a rate filing by the pipeline under Section 4 of the Natural Gas Act[92] and pipeline tariffs contain provisions applicable to the standard service agreements that allow the pipelines to change both rates and terms and conditions unilaterally. Thus, most pipeline contracts are not subject to the Mobile-Sierra doctrine and there is no need for the Commission to make a public interest finding when modifying these contracts.

86. Throughout its restructuring of the gas industry, the Commission has relied on its authority under Section 5 and been affirmed by the courts. In Order No. 380 the Commission found under Section 5 that the minimum bill provisions in existing contracts were unjust and unreasonable under Section 5.[93] The court upheld eliminating the minimum bill from the contracts on the ground that "Section 5 gives the Commission

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[92] The United State Supreme Court described the system of natural gas contracting adopted in 1948 as follows:

> When the Natural Gas Act became law in 1938, natural gas companies were permitted to file their existing sales contracts as rate schedules under ' 4 (c). Schedules in this form were extremely lengthy, unwieldy, and otherwise unsatisfactory in that it was most difficult for customers, competitors, and the Commission itself to ascertain whether rates to various customers were unduly discriminatory or otherwise unreasonable. The Commission therefore proposed regulations requiring the conversion of rate contracts into a "tariff-and-service-agreement" system, and these regulations were promulgated in October 1948 as Order No. 144. Under the tariff-and-service-agreement system, the agreement between buyer and seller does not itself contain a price term, but rather refers to rate schedules of general applicability on file with the Commission. It is noteworthy that Order No. 144 expressly contemplates that a seller may reserve the 'privilege' of filing rate changes under ' 4 of the Act. 18 C.F.R. ' 154.38 (d) (3).

United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division, 358 U.S. 103, 115 n.8 (1958).

[93] Order No. 380, Elimination of Variable Costs From Certain Natural Gas Pipeline Minimum Commodity Bill Provisions,

authority to alter terms of any existing contract found to be 'unjust' or 'unreasonable.'"[94] In Order No. 436, the Commission found under Section 5 that the pipelines' refusal to transport gas for third parties was unduly discriminatory and adopted the just and reasonable practice of open access transportation. The court affirmed these findings and the remedy.[95] In Order No. 636, the Commission again made findings under Section 5, this time that pipelines' bundled firm sales service violated Sections 4(b) and 5(a) of the Natural Gas Act.[96] It also concluded under Section 5 that the continued enforcement of customers' gas purchase obligations, which were agreed to before unbundling, were unjust, unreasonable, and unduly discriminatory,[97] so that customers must have the opportunity to reduce or terminate these obligations. The court found the bundled firm sales contracts between pipelines and LDCs were subject to the Commission's Section 5 authority[98] and affirmed the remedy of reduction or termination of gas purchase obligations.[99]

87. In Order No. 637 the Commission continued its efforts under Section 5 to create a more competitive gas market while still protecting captive customers. As discussed above, in INGAA the court affirmed the Commission's policies and regulations in Order No. 637 only remanding the issues of the 5-year term matching cap for the ROFR, the backhaul/forwardhaul issue, and the relation between the ROFR and tariff provisions, for further consideration.[100] In the Order on Remand and in this rehearing order in the Order

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[94] 770 F.2d 1144, 1153 n.9 (D.C. Cir. 1985), cert. denied, 476 U.S. 1114, 106 S.Ct. 1968 (1986).

[95] Associated Gas Distributors v. FERC, 824F.2d 981, 993, 1001 (D.C. Cir. 1987) (these findings were upheld in substance, although the order was vacated for other deficiencies, among them, failure to take action under Section 5 concerning uneconomic producer-pipeline contracts.

[96] Order No. 636, & 30,939 at 30,405.

[97] Order No. 636 at 30,453.

[98] United Distribution Companies v. FERC, 88 F.3d 1105, 1131 (D.C. Cir. 1996).

[99] UDC at 1132-33.

[100] INGAA at 29. A fourth remanded issue, the waiver of the posting requirement for pre-arranged short-term capacity releases and conditions for that waiver, became moot. Order on Remand Ps 60-63.

No 637 proceeding, the Commission is similarly acting under Section 5 of the Natural Gas Act to find that a practice, failure to permit a backhaul and a forwardhaul, both up to MDQ, to the same point in a segmented transaction, is unjust and unreasonable and to provide a just and reasonable remedy under Section 5.

(6) Whether the backhaul/forwardhaul policy affects certificated service levels

88. INGAA characterizes the alleged doubling of the quantity of service as a new service. Based on this characterization, it contends the Commission has no statutory authority to adopt the backhaul/forwardhaul policy because this policy alters pipelines' certificated service levels by changing the quantity provisions of their transportation contracts. INGAA also contends the Commission cannot compel pipelines to provide this alleged new service because the Commission is limited by Section 7(a) of the NGA.

89. The Commission considered and rejected such arguments when it promulgated Order No. 636.[101] In Order No. 636, the Commission found under Section 5 that the entire structure of the gas industry was unjust and unreasonable and mandated many changes including the unbundling of services and no-notice transportation service. The Commission rejects INGAA's arguments concerning Section 7 here for the same reasons it rejected these arguments in Order No. 636. As the Commission stated in that proceeding, the Commission is not compelling service; it is changing the terms of existing services and establishing the terms for future services. Section 7(a) applies only to new service; it does not prevent the Commission from requiring changes in the terms of existing service.

III. Requests for clarification

90. INGAA believes that the backhaul/forwardhaul policy should not apply to complex pipelines and asks for clarification on this issue. If clarification is not granted, it asks for rehearing. The Commission clarifies that it will determine whether the backhaul/forwardhaul policy applies to a pipeline in the pipeline’s individual filing made to comply with the Order on Remand. The Commission finds this is a more appropriate forum for determining the facts and circumstances that apply to an individual pipeline.

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[101] Order No. 636, ¶ 30,939 at 30,422-423; Order No. 636-A ¶ 30,950 at 30,530-533.

91. DEGT asks the Commission to clarify, or in the alternative, grant rehearing, that the Order on Remand does not affect its ruling in Algonquin Gas Transmission Co., 98 FERC ¶ 61,211 at 61,775 (2002). DEGT asserts that in that order, issued February 27, 2002, the Commission held that a shipper may not use a backhaul/forwardhaul transaction to bring gas to a delivery point in an amount that exceeds its contract demand on a lateral. The Commission clarifies that it has ruled on this issue in Algonquin's Order No. 637 proceeding in Docket No. RP00-331-000. The Commission issued an order in this docket on July 23, 2003 in which it addressed both segmentation on laterals and backhaul/forwardhaul provisions.[102]

92. DEGT seeks clarification that the issue of whether the Lowest Unutilized Quantity (LUQ)[103] should determine quantities that can be transported in segmented transactions that are out of the contract path, including backhauls, will be decided in the pipelines' individual Order No. 637 proceedings and not in this proceeding. The Commission clarifies that this issue will be determined in individual Order No. 637 proceedings. With respect to both Texas Eastern and Algonquin, the Commission has rejected the use of the LUQ limit on segmentation within the zones for which shippers are paying.[104]

93. Maritimes and Gulfstream seek clarification that the Commission is not addressing an aspect of segmentation policy consisting of the number of times per day a shipper could require a forwardhaul and a backhaul to the same point. The Commission clarifies that it is not addressing that issue in this proceeding.

The Commission orders:

The requests for clarification and rehearing are granted or denied as expressed in the body of this order.

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[102] Algonquin Gas Transmission Co., 104 FERC ¶ 61,118 P 113, 151-154 (2003).

[103] The LUQ is equal to the difference between the MDTQ specified in the service agreement and the highest quantity of gas scheduled for delivery within the primary path. See, e.g., Algonquin Gas Transmission Company, 98 FERC ¶ 61,211 at 61,769 (2002).

[104] Algonquin Gas Transmission Co., 104 FERC ¶ 61,118 P 17-21, 110-113 (2003); Texas Eastern Transmission, L.P., 98 FERC ¶ 61,215 (2002); 102 FERC ¶ 61,198 (2003).

By the Commission.

(S E A L)

Linda Mitry,
Acting Secretary.