

103 FERC ¶ 61,237
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, and Nora Mead Brownell.

East Tennessee Natural Gas Company	Docket Nos.	RP00-469-002
		RP00-469-003
		RP01-22-004
		RP01-22-005
		RP03-177-000

ORDER ON REHEARING AND COMPLIANCE FILINGS

(Issued May 23, 2003)

1. This order addresses East Tennessee Natural Gas Company's (East Tennessee) request for rehearing and clarification of the Commission's January 30, 2002 Order in this proceeding (January 30 Order).¹ That order approved subject to conditions a Settlement of East Tennessee's proceedings to comply with Order Nos. 637, 587-G, and 587-L (Settlement). This order also addresses East Tennessee's March 27, 2002 filing to comply with the directives of the January 30 Order. In addition, this order addresses East Tennessee's December 2, 2002 filing in Docket No. RP03-177-000 that was required by the Commission's October 31, 2002 Order On Remand (Remand Order)² in response to the decision by the United States Court of Appeals in Interstate Natural Gas Association of America v. FERC (INGAA).³ The request for rehearing and clarification will be granted and denied, as discussed below. As more fully explained in the order, we will accept certain tariff sheets, subject to the conditions of this order, reject other tariff sheets as moot, and direct East Tennessee to make certain modifications in other tariff sheets and to file revised tariff sheets to reflect the modifications within 30 days of the date of this order. East Tennessee will be required to comply with Order No. 637 on the first day of the month four months from the date of this order. This order benefits customers by enhancing pipeline transportation services consistent with the Commission's policies in Order No. 637.

¹East Tennessee Natural Gas Co., 98 FERC ¶ 61,060 (2002).

²101 FERC ¶ 61,127 (2002), reh'g pending.

³Interstate Natural Gas Ass'n of America v. FERC, 285 F.3d 18 (D.C. Cir. 2002).

BACKGROUND

2. On August 15, 2000, in Docket No. RP00-469-000, East Tennessee filed pro forma tariff sheets to comply with Order No. 637. On July 18, 2001, in Docket No. RP00-469-001, East Tennessee filed a Settlement to resolve the issues in its Order No. 637 proceeding.

3. On January 30, 2002, the Commission conditionally approved East Tennessee's Settlement subject to certain modifications. East Tennessee filed a request for rehearing or clarification of the January 30 Order. On March 27, 2002, East Tennessee filed revised tariff sheets to comply with the Commission's January 30 Order.⁴ East Tennessee also filed revised tariff sheets on December 2, 2002, to comply with the Remand Order.⁵

4. Public notices of East Tennessee's March 27, 2002 and December 2, 2002 compliance filings were issued. No comments or protests to the March 27, 2002 compliance filing were filed. East Tennessee Group (ETG) filed comments on the December 2, 2002 compliance filing. Pursuant to Rule 214 (18 C.F.R. § 385.214 (2002)), all motions to intervene are granted.

DISCUSSION

A. Modifications to the Settlement

1. January 30 Order

5. As modified in this order, the Commission, in the January 30 Order, accepted the Settlement subject to conditions. East Tennessee argues that the Commission has failed to accord the Settlement the weight that FERC and the appellate court precedents require. East Tennessee contends that the Commission and the courts have made clear that universal or near universal agreement of all parties to the terms of the Settlement while not determinative, is highly probative of the justness and reasonableness of the Settlement, citing, e.g., Tejas Power Corp. v. FERC, 908 F.2d 998 at 1003 (D.C. Cir. 1990). East Tennessee further contends that the Courts have "consistently required the Commission to give weight to the contracts and settlements before it," quoting a portion of Midcoast Interstate Transmission v. FERC, 198 F. 3d 960 at 968 (D.C. Cir. 2000). East Tennessee asserts that the parties intended that the Settlement would resolve all issues related to

⁴See the Appendix to this order.

⁵See the Appendix to this order.

Order No. 637, et seq., and the components of the settlement operate as an integrated whole. East Tennessee argues that by modifying the Settlement in material ways, the Commission may be imposing protracted litigation, expense and a lengthy period of uncertainty, all of which settlements are designed to overcome. East Tennessee further argues that the Settlement contains a nullification provision at Paragraph III.2 and that the changes ordered by the Commission threaten to upset the Settlement process entirely. East Tennessee contends that there is no acknowledgment by the Commission of these potential effects nor any attempt to balance the Commission's desire to alter the terms and conditions of the Settlement against the resulting harm of forcing the parties into a litigated resolution.

6. East Tennessee argues that the Commission generally forgoes a full on-the-merits analysis of the individual aspects of agreements when they are in the context of a settlement and when no party specifically objects to those agreements. East Tennessee asserts that certain of the changes are based on policy but that the Commission has never vetted this policy in the context of a rulemaking or shown the justness and reasonableness of applying that policy to a particular pipeline.

7. East Tennessee asserts that the Commission is obligated to explain how the Settlement or East Tennessee's existing tariff fails to serve the public interest and how the contesting parties or other segments of the public will be harmed if the changes are not made, citing, e.g., Wyoming Interstate Co., Ltd, 91 FERC ¶ 63,014 (2000). East Tennessee further asserts that explanation is particularly called for in this case since the changes requested by the January 30 Order were not requested by any party, including the few parties that did not join in the Settlement. East Tennessee argues that the Commission has a strong policy favoring settlement and the forced alteration of the Settlement contradicts this policy and constitutes error.

8. East Tennessee further argues that the Commission has failed to meet the NGA Section 5 requirements to modify the Settlement terms and existing contracts and tariff provisions. East Tennessee asserts that the required showing of the justness of the replacement terms or the unjustness of the existing tariff provision is not found in the January 30 Order.

9. East Tennessee asserts that where the Commission imposes rates, terms, and conditions of its own creation or at the behest of a third party, it is per force operating under NGA Section 5 and bears the burden of proof in showing that the current rate or term is unjust and unreasonable and also bears the burden of proof to show that any replacement rate or term is just and reasonable. East Tennessee argues that the Commission can not claim that its NGA Section 5 obligations to demonstrate unjustness and unreasonableness were satisfied in the Order No. 637 rulemaking. East Tennessee asserts that the

Commission recently held in Granite State⁶ that while it has the lawful authority to impose new policies in an adjudicatory proceeding, it can not uncritically apply policy developed in one case to a second case without taking into account the factual distinctions between the two situations, citing 98 FERC ¶ 61,019 at 61,054-5.

2. Commission Decision

10. In this proceeding, East Tennessee sought to settle a Commission NGA Section 5 proceeding with its shippers. But even then, East Tennessee did not achieve a complete Settlement and many of its proposals were protested. East Tennessee also failed to address in its Settlement all of the issues set for consideration in Order No. 637.

11. But more important, because this is a proceeding under Section 5 of the Natural Gas Act, the Commission must review the proposals (regardless of whether protests were received) to ensure that these proposals meet the procompetitive requirements of Order No. 637. While the Commission often accepts settlements of rate issues, which only affect the financial interests of the parties, it gives greater scrutiny to settlements of filings to comply with rulemakings to ensure that those settlements satisfy the important requirements of the rulemaking.⁷ As the Commission stated in Trailblazer,⁸ "when settlements have involved fundamental issues concerning the competitive effect of the terms and conditions under which pipelines perform open access, unbundled transportation service, the Commission has modified such settlements to be consistent with commission policy, even though the parties had settled on a somewhat different result." Thus, in Florida Gas, the Commission rejected a settlement provision when it conflicted with a competitive goal of Order No. 637: "the fact that FGT has reached a settlement agreement with its shippers does not compel the Commission to permit a feature with the effect on competition as important as the manner in which capacity is allocated on a pipeline's system to be substantially different on FGT's system than on the rest of the pipeline grid."⁹

⁶Granite State Gas Transmission, Inc., 96 FERC ¶ 61,273 (2001)(Granite State).

⁷The Commission's regulations require that the Commission must find that an uncontested settlement is fair and reasonable and in the public interest. 18 C.F.R. § 385.602(g)(3) (2002). Contested settlement provisions must be found to be just and reasonable. Here, the Commission reviewed the Settlement to determine if the Settlement provisions met the goals of Order No. 637.

⁸Trailblazer Pipeline Company, 85 FERC ¶ 61,345 at 62,341 (1998) (Trailblazer).

⁹Florida Gas Transmission Company, 102 FERC ¶61,217, at P 24 (2003) (Florida

On the other hand, in Reliant, the pipeline and the customers agreed on a distribution of penalty revenues in a way different from the general Commission policy, but the Commission accepted this aspect of the Settlement because "this uncontested aspect of the Settlement will not have any significant adverse effect on competition."¹⁰

12. With respect to East Tennessee's arguments concerning NGA Section 5, this entire proceeding was under NGA Section 5, and the Commission set forth in the January 30 Order and in this order its justifications for finding East Tennessee's existing tariff unjust and unreasonable and for concluding that its requirements are just and reasonable.

13. In ruling on East Tennessee's Settlement, the Commission applied the principles discussed above in determining whether the Settlement provisions served the competitive goals of Order No. 637, and as discussed below, modified only those provisions that it found were unjust and unreasonable and conflicted with these competitive requirements. Thus, the Commission finds that it has not improperly modified East Tennessee's Settlement and denies its rehearing request.

B. Segmentation – Future Expansions

1. January 30 Order

14. In the January 30 Order, the Commission noted that, while East Tennessee has several future system expansions planned, its current system configuration lacks significant interconnection points that could present segmentation opportunities downstream of the Dixon Springs and Lewisburg compressor stations. However, the Commission further noted that it may become operationally feasible for East Tennessee to offer segmentation in the future because of the various system expansion projects being contemplated. Therefore, the Commission, in light of the future expansion of East Tennessee's system, required East Tennessee to file tariff language indicating that it will permit additional segmentation opportunities on its system as a result of any system expansion to the extent operationally feasible. The Commission further stated in footnote number 12 of the January 30 Order that, if East Tennessee does not include this language in its tariff, it must address in every NGA Section 7 application to construct and operate that it files with the Commission, why the proposal will not provide the operational capability necessary to provide segmentation.

⁹(...continued)
Gas).

¹⁰Reliant Energy Gas Transmission Company, 98 FERC ¶ 61,362, at 62,552 (2002) (Reliant).

2. Rehearing Request

15. East Tennessee argues that these requirements related to future expansions are in error. East Tennessee states that if the Commission rejects its request for rehearing it will adopt the option of addressing segmentation in each NGA Section 7 certificate application subject to its requested clarifications being granted. East Tennessee argues that the Commission failed to give proper weight to the Settlement. East Tennessee contends that the segmentation condition is fundamentally inconsistent with the regulation promulgated in Order No. 637 since segmentation is limited to capacity for which the customer has contracted.¹¹ East Tennessee asserts that its existing service agreements do not provide for any segmentation and, in its Order No. 637 filing, East Tennessee demonstrated that it could not offer system-wide segmentation, subject to customer MDQ and transportation quantity rights set forth in the Order No. 637 regulations. East Tennessee further asserts that the Commission accepted this segmentation proposal in the January 30 Order, including the maximum daily quantity limitation in any segment of the system except forwardhaul/backhaul point capacity. East Tennessee contends that the Commission has failed to consider the limitations in the parties' contracts. East Tennessee further contends that there is nothing in Order No. 637 stating that the pipeline must take on an impermissibly vague constantly changing, and perpetual obligation to make changes in its Order No. 637 tariff provisions and customer contracts. East Tennessee argues that the Commission has failed to acknowledge or support its heavy burden in changing contracts.

16. East Tennessee asserts that its service agreements incorporate the Rate Schedules and General Terms and Conditions (GT&C) which will contain the Settlement segmentation provisions. East Tennessee further asserts that, under the January 30 Order, its existing customers are contractually not permitted to segment except in the western portion of the system. East Tennessee argues that, under the law, the Commission can not alter the terms and conditions of a pipeline's tariff that have become final pursuant to proceedings under Sections 4 or 5 in a Section 7 certificate proceeding. East Tennessee asserts that the Commission can not act indirectly to accomplish what it cannot do directly through tariff language or the alternative approach in the January 30 Order. East Tennessee further argues that once tariff provisions have been approved in a NGA Section 4 or 5 proceeding and the order is final, the Commission and other parties have the burden to show that the existing provisions are no longer just and reasonable and the new provisions are just and reasonable. East Tennessee asserts that, in acting under NGA Section 5, there is the burden of going forward and the burden of proof and supporting the replacement provisions as just and

¹¹Citing Order No. 637 at 31,303 and INGAA , Brief of Respondent at 104-108, filed June 5, 2001.

reasonable. East Tennessee argues that the Commission's condition regarding future expansions is a blatant attempt to avoid the requirements of NGA Section 5 and shift the burden of proof. East Tennessee contends that it is not an answer to say that the provision would relate to future expansions since East Tennessee adhered to the Commission's Order No. 637 directives in its original Order No. 637 filing and in its Settlement proposal.

17. East Tennessee asserts that any change or proposed change related to the challenged segmentation condition would implicate a myriad of other interrelated provisions proposed to comply with Order No. 637 and supported by its customers and existing tariff provisions, such as Rate Schedules LMS-MA and LMS-PA, that it has sought to preserve for the customers' benefit. East Tennessee further asserts that this would be true not only of contracts implemented pursuant to a future expansion but also contracts prior to and not directly related to the expansion. East Tennessee contends that it would be bad policy and contrary to seamless, easily administered service to vintage Order No. 637 provisions in the manner implied by the segmentation condition. East Tennessee further contends that this condition is particularly pernicious since it raises uncertainty regarding not only what contracts say in terms of day to day operations and the rights and obligations of parties, but also the agreed upon rate, if it is other than the maximum rate. East Tennessee argues that the Commission has not imposed such a requirement in the context of other Order No. 637 settlements, citing, e.g., ANR Pipeline Co., 97 FERC ¶ 61,323 (2001) (ANR) and has not stated a reason to apply such a requirement here. East Tennessee further argues that there is no rationale stated for this requirement.

18. East Tennessee argues that, at a minimum, if the Commission requires it to address segmentation in each of its future Section 7 proceedings, the Commission must acknowledge that it bears the burden of proof, including interrelated tariff provisions, and that East Tennessee is entitled to reopen all related provisions of its tariff, including existing LMS-PA and LMS-MA agreements, to address the effects of further segmentation. East Tennessee asserts that the operational flexibility East Tennessee's customers use in balancing their volumes is predicated on a one MDQ delivery regime, whether transportation is forwardhaul or backhaul. East Tennessee further asserts that expanded segmentation and forward/backhaul rights directed in the January 30 Order would require modifications to the operator level LMS-PA and LMS-MA agreements.¹²

¹²East Tennessee also repeats its argument that the Commission must recognize that shippers can not exceed contract demands on East Tennessee's laterals and that a shipper is not permitted to use a forwardhaul and a backhaul to bring gas to a delivery point in an amount that exceeds its contract demand on a lateral. Those arguments will be addressed later in this order.

19. Finally, East Tennessee asserts that, if existing shippers are afforded segmentation rights on incremental projects, particularly those that allow backhaul and forwardhaul to a single point in excess of MDQ, it will need to consider rolling in the cost of the expansion project in conflict with current Commission policy favoring incremental pricing. East Tennessee argues that the Commission has stated no reason why an incremental project that creates new contract rights for existing shippers should be priced on an incremental basis.

3. Commission Decision

20. The Commission will grant rehearing in part and modify the tariff requirement imposed in the January 30 Order. The requirement for a pipeline to permit segmentation when operationally feasible is contained in Section 284.7(d) of the Commission's regulations. This requirement is not fixed in time, but is an ongoing requirement and applies whenever segmentation becomes operationally feasible and also applies to expansions and to greenfield pipelines.

21. In the January 30 Order, the Commission agreed with East Tennessee that segmentation downstream of the Dixon Springs and Lewisberg compressor stations are not currently feasible, because it lacks interconnection points on that portion of its system. However, the Commission also recognized that East Tennessee has planned expansion projects, including having obtained a certificate for a project, that adds capacity to that portion of the pipeline in which segmentation is not currently practicable. If, and when these system expansions are built, segmentation may be possible on these portions of East Tennessee's system. At that time, East Tennessee is under a regulatory obligation to provide segmentation on those portions of its system when operationally feasible.

22. Under its NGA Section 5, and its NGA Sections 10 and 14 authority, the Commission can require East Tennessee to make filings with the Commission explaining whether such expansions will make segmentation feasible, and, if segmentation is feasible, proposing tariff provisions providing for segmentation.¹³ In other cases, where segmentation is not currently feasible, the Commission has required the pipeline to file a comprehensive segmentation proposal at least 60 days before segmentation is operationally feasible.¹⁴

¹³See Order No. 637-B, 92 FERC ¶ 61,062, at 61,165 (2000), aff'd, INGAA, 285 F.3d at 38 ("the Commission has authority under § 5 to order hearings to determine whether a given pipeline is in compliance with FERC's rules [citation omitted] and under § 10 and § 14 to require pipelines to submit needed information for making its § 5 decisions.")

¹⁴See, e.g., Paiute Pipeline Co., 96 FERC ¶ 61,167 (2001).

23. Accordingly, the Commission will modify the January 30 Order to remove the requirement for East Tennessee to place in its tariff a requirement to provide segmentation when operationally feasible. As it has done on other pipelines, the Commission will require East Tennessee to file a comprehensive segmentation proposal at least 60 days before segmentation is operationally feasible on its system. This is nothing more than a procedural, filing requirement to ensure that the pipeline complies with Section 284.7(d) of the Commission's regulations. The Commission agrees with East Tennessee that in acting on these filings, the Commission will be proceeding under Section 5 of the Natural Gas Act.

24. However, unlike other pipelines in which this condition has been applied, East Tennessee has already applied for, and accepted, a certificate for the Patriot Project expansion in Docket No. CP01-415-000. The Patriot Project, among other things, will extend East Tennessee's system approximately 93 miles from Wytheville, Virginia, through several counties in Virginia, to an interconnect with the facilities of Transcontinental Gas Pipe Line Corporation at Eden, North Carolina. The new 24-inch diameter extension will ultimately provide up to 510,000 dekatherms (Dth) a day of firm natural gas service. Further, the Patriot Project will create a major point of interconnection downstream of East Tennessee's Dixon Springs and Lewisburg compressor stations. The addition of this interconnection would seem to make segmentation feasible on the portion of East Tennessee's system downstream of the Dixon Springs and Lewisburg compressor stations. Accordingly, pursuant to NGA Section 5, the Commission will require East Tennessee to file 120 days prior to the proposed in-service date of these facilities an explanation of whether the expansion will make segmentation feasible, and, if so, proposing pro forma tariff provisions providing for segmentation. This will provide the Commission with sufficient time to act on these filings prior to the in-service date.

25. East Tennessee argues that imposing a condition regarding future expansions is inconsistent with its Settlement, which did not address this issue. In the first place, East Tennessee does not contend that the parties expressly reached agreement that segmentation would not apply to expansion projects. Further, as explained earlier, segmentation was an integral part of a pipeline's Order No. 637 obligation, and the pipeline cannot through a settlement eliminate its obligation to comply with the procompetitive requirements of Order No. 637.

26. East Tennessee also raises a number of arguments about interference with contractual rights, but it is not clear what these arguments have to do with the limited issue for which East Tennessee is seeking rehearing: whether the Commission should require East Tennessee to include in its tariff a provision requiring it to permit segmentation whenever operationally feasible. Since the Commission has granted rehearing on this issue for the reasons discussed above, and clarified that it is only imposing a procedural filing

requirement, it would appear that there is no further need to address these arguments. In any event, these contractual arguments are collateral attacks on the Commission's finding, in Order No. 637, that pipeline tariffs and contracts that prohibit segmentation where operationally feasible are unjust and unreasonable.¹⁵

C. Segmentation – Backhauls and Forwardhauls to the Same Point

1. January 30 Order and Remand Order

27. In the January 30 Order, the Commission noted that East Tennessee's proposed Rate Schedule FT-A, Section 9.1, provided "that the combined scheduled volumes of the two or more nominated segments do not exceed the Shipper's original contract MDQ ... at any point where the nomination paths overlap." The Commission further noted that East Tennessee had not explained what would happen in the event of a shipper requesting backhaul service overlapping with another segment's nomination at a point and that, in Order No. 637-A, it had stated that a forwardhaul and backhaul to a single point did not result in a capacity overlap even though the total amount received by the shipper exceeded contract demand.¹⁶ The Commission required East Tennessee to clarify its tariff to permit this result.

28. After the January 30 Order, the United States Court of Appeals for the District of Columbia Circuit issued its decision in INGAA, remanding certain issues to the Commission regarding Order No. 637, including the issue of forwardhauls and backhauls to the same point. On October 31, 2002, the Commission issued the Remand Order. Ordering Paragraph B of the Remand Order required the following: "pipelines that the Commission has found must permit segmentation on their systems must file [by December 2, 2002] revised tariff sheets to expressly permit segmented transactions consisting of forwardhauls up to contract demand and backhauls up to contract demand to the same point at the same time."

2. Rehearing Request

29. East Tennessee argues that the Commission erred by ordering it to modify its tariff to permit forwardhauls and backhauls to a single point that are not limited to a customer's MDQ. East Tennessee contends that rather than a clarification the Commission is ordering a major and material modification to East Tennessee's tariff not contemplated in the

¹⁵INGAA, 285 F.3d at 37-38.

¹⁶Order No. 637-A at 31,593, citing Transcontinental Gas Pipe Line Corp., 91 FERC ¶ 61,031 (2000).

Settlement or required by Order No. 637 and not justified by the Commission. East Tennessee asserts that the Commission has not articulated why it should override the Settlement, particularly in the face of the Commission's clear policy of encouraging parties to resolve their disagreements by settlement. East Tennessee contends that permitting customers to multiply their MDQ is directly contrary to the Order No. 637 requirement which limits segmentation to capacity for which a customer has contracted.¹⁷ East Tennessee further contends that this requirement is also contrary to the Commission's obligations under NGA Section 5 to meet the burden of justness and reasonableness to any change in East Tennessee's tariff, since that showing was not made as part of Order No. 637.

30. East Tennessee argues that as a policy matter disruptions of contracts and settlements, along with related uncertainty, undermines relationships among parties, destroys incentives to enter into new contracts, and harms the pipeline's and customers' ability to market unsubscribed capacity, East Tennessee asserts that the Commission has made clear in numerous cases that customers are not entitled to capacity for which they have not contracted.¹⁸ East Tennessee contends that its proposed limitation of point rights for backhaul service was established as part of the Settlement negotiation process, and as such, East Tennessee and the settling parties should not have been held to a higher standard of demonstrating why such a limitation is warranted. East Tennessee further contends that this is particularly so given the Commission's acknowledged burden of demonstrating that changes to East Tennessee's tariff imposed by the Commission must be just and reasonable and that any replacement must also be just and reasonable.

31. East Tennessee also requests the Commission to clarify that the requirement to permit forwardhauls and backhauls to the same point does not apply to the portion of East Tennessee's system not operationally available for segmentation. In addition, East Tennessee contends that the Commission should clarify that a shipper cannot exceed its contract demand on any lateral upstream of Dixon Springs on the 3100 Line or upstream of Lewisburg on the 3200 Line where segmentation is permitted. East Tennessee asserts that consistent with Commission precedent, a shipper is not permitted to use a forwardhaul and a backhaul to bring gas to a delivery point in an amount that exceeds its contract demand on a lateral, citing Algonquin Gas Transmission Co., 98 FERC ¶ 61,211 (2002)(Algonquin).

¹⁷Citing Order No. 637 at 31,303.

¹⁸Citing, e.g., Tennessee Gas Pipeline Co. 95 FERC ¶ 61,096 (2001); Natural Gas Pipeline Co. of America, 92 FERC ¶ 61,221 (2000); Texas Eastern Transmission Corp., 91 FERC ¶ 61,105 (2000); and Transcontinental Gas Pipe Line Corp., 78 FERC ¶ 61,264 (1997).

3. Compliance with Remand Order

32. East Tennessee filed tariff revisions consistent with the directive in the Remand Order in Docket No. RP03-177-000. East Tennessee's proposed tariff language satisfactorily complies with the Remand Order, with exceptions noted below. Therefore, the proposed tariff sheets, as indicated in the Appendix to this order, will be accepted to be effective four months from the date of issuance of this order, subject to the conditions of this order.

33. In its comments, ETG asserts that, in view of the uncertainty currently surrounding segmenting on the East Tennessee system, it is troubled by East Tennessee's reservation of the right to surcharge customers retroactively for transportation performed consistent with the proposed tariff sheets. ETG questions what additional charges would East Tennessee have in mind. ETG asserts that shippers certainly could not exercise their forward/backhaul rights under the threat that East Tennessee might retroactively deem them to have violated their maximum contract demand and penalize them accordingly. ETG argues that, because the status of segmenting on East Tennessee is so unsettled, the proposed tariff sheets need to be scrutinized closely to see whether they fulfill the Commission's requirements and that any sheets adopted now must be subject to revisiting when and if East Tennessee implements wider segmenting on its system to see whether they continue to achieve the Commission's objectives.

4. Commission Decision

a. Rehearing Request

34. Contrary to East Tennessee's assertions, the Commission properly found that East Tennessee must permit a shipper to use a forwardhaul and backhaul to the same delivery point even if that amount exceeds its mainline contract demand.

35. In the Remand Order, issued after East Tennessee filed the instant rehearing request, the Commission found that 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 NGA Section 5 to modify the pipeline's terms and conditions of service. The Commission determined that it need not modify any term in the individual service agreements between pipelines and shippers to accomplish this since the related service agreements incorporate the terms and conditions set forth in the tariff. The Commission further determined that it is not requiring pipelines to permit the shipper to use the primary point rights defined by its contract demand beyond those set forth in its contract. Rather, the Commission is providing an additional right to firm shippers on a secondary basis. The Commission made the necessary related findings pursuant to NGA

Section 5. The Commission, inter alia, found that permitting segmented transactions consisting of a backhaul and a forwardhaul to the same point that exceed contract demand is just and reasonable. Therefore, consistent with its Remand Order, the Commission is requiring East Tennessee to comply with the requirement to permit backhauls and forwardhauls to the same point.

36. The Commission agrees with East Tennessee that the requirement to permit forwardhauls and backhauls to the same point only applies to segmented transactions and therefore will not apply to transactions on the portion of East Tennessee's system where segmentation is not required.

37. East Tennessee also is not required to permit transactions that result in shippers exceeding their contract demand on laterals. In Algonquin, the Commission rejected a request to permit overlapping of segmented capacity on a pipeline's lateral facilities to the extent necessary for shippers to make forwardhaul and backhaul deliveries to a point located on the lateral.¹⁹ The Commission found that this would be inconsistent with Order No. 637 which states that segmentation cannot exceed shipper's contract demand in any segment. However, where there is no overlap on the lateral or mainline but the transactions only use the same point, the two transactions must be permitted.

b. Compliance Filing

38. The Commission accepts East Tennessee's compliance filing in Docket No. RP03-177-000, subject to the changes discussed below.

39. East Tennessee's proposed revision to Section 15.3 of its GT&C includes the following proposed language:

In addition, for any movement of gas that traverses a segment(s) in which the total nominated quantity for that gas exceeds the firm contractual entitlement, the quantity in excess of the contractual entitlement shall be deemed to be outside of the Shipper's Contract Path.

40. East Tennessee provides no explanation of why this tariff language is required by the Remand Order and is necessary in order to implement the requirement regarding forwardhauls and backhauls to the same point, and the purpose or intent of this provision is not clear. Therefore, the Commission rejects this proposed tariff language.

¹⁹Algonquin Gas Transmission Co., 98 FERC ¶ 61,211 at 61,774-5 (2002).

41. East Tennessee proposes to add the following tariff language in Section 9.6 to Rate Schedule FT-A.

For the purpose of determining, for that portion of Transporter's system which is subject to segmentation as provided in Section 9.1 of this Rate Schedule FT-A, whether any overlapping transactions exceed, in the aggregate (based on all relevant Shipper utilization) the contract entitlements of the original firm contract in any segment or at any point (including, without limitation, the TQ or segment entitlements), a transaction that involves movement of gas in the same direction as that contemplated by the Primary Receipt Point(s) and the Primary Delivery Point(s) on the firm service agreement and a transaction that involves movement of gas that is counter to the direction contemplated by the Primary Receipt Point(s) and the Primary Delivery Point(s) on the firm service agreement that are nominated to the same delivery point for the same gas flow date and time shall not be deemed to be an overlap at that delivery point; provided, however, in no event shall Transporter be obligated to deliver on a primary firm basis at that delivery point a quantity in excess of the MDQ applicable to that delivery point. For the purpose of determining whether any overlapping nominations in a segment exceed, in the aggregate (based on all relevant Shipper utilization) the contract entitlements of the original firm contract in any segment or at any point (including, without limitation, the TQ or segment entitlements), a transaction that involves movement of gas in the same direction as that contemplated by the Primary Receipt Point(s) and the Primary Delivery Point(s) on the firm service agreement and a transaction that involves movement of gas that is counter to the direction contemplated by the Primary Receipt Point(s) and the Primary Delivery Point(s) on the firm service agreement that are nominated on the same segment for the same gas flow date and time shall be deemed to be an overlap on that segment.

42. While the first part of Section 9.6 of Rate Schedule FT-A appears to take away the right to do a forwardhaul/backhaul to the same point, Section 9.6 later provides that right. The first sentence of Section 9.6 states that customers cannot exceed "in the aggregate (based on all relevant Shipper utilization) the contract entitlements of the original firm contract in any segment or at any point." (emphasis added). However, the second sentence of Section 9.6 provides that: "For the purpose of determining whether any overlapping nominations in a segment exceed, in the aggregate (based on all relevant Shipper utilization) the contract entitlements, a [forwardhaul/backhaul] transaction ... shall not be deemed to be an overlap at that Point of Delivery." (emphasis added)²⁰ Thus, East

²⁰In effect, what East Tennessee taketh away in the first sentence of Section 9.6 of

Tennessee's tariff allows a shipper to segment its capacity utilizing multiple receipt and delivery points and does not restrict shippers from making simultaneous forwardhaul and backhaul deliveries to points within its transportation path. The tariff further provides that a shipper is permitted, to receive or deliver gas outside its primary capacity path, but the transaction will be assigned a lower priority than transactions within the shipper's primary path.²¹

43. Nonetheless, the prohibition against exceeding contract entitlements "at any point" in Section 9.6 of Rate Schedule FT-A of East Tennessee's tariff could mislead shippers as to their rights to conduct forwardhauls and backhauls to the same point. The Commission can discern no reason for East Tennessee to provide in Section 9.6 of Rate Schedule FT-A that shippers cannot exceed the aggregate at any point, and, therefore, the Commission will require East Tennessee to remove this language from Section 9.6.

44. ETG protests the following language in East Tennessee's compliance filing:

East Tennessee submits these revised tariff sheets subject to the outcome of its rehearing requests in Docket No. RM98-10-011 and in its Order No. 637 proceeding in Docket Nos. RP00-469-000, et al., and any related appeal. Furthermore, to the extent that any of the changes in the tariff sheets subject to rehearing become effective and are later revised on rehearing or appeal, East Tennessee reserves its right to assess surcharges or refunds retroactively to the implementation date of the relevant provision to make East Tennessee whole for the losses incurred by the erroneous ruling.

45. ETG's comments with regard to possible future refunds related to rehearings or appeals are rejected as premature and speculative, since these provisions have not gone into effect. Should the Court require changes in these proceedings on appeal, the Commission will consider whether refunds or surcharges are owed.

D. Discount Requirement

1. January 30 Order

²⁰(...continued)
Rate Schedule FT-A, it giveth back to the shipper later in the same section.

²¹Proposed Section 9.7 of Rate Schedule FT-A.

46. In the January 30 Order, the Commission stated that in order to assure uniform implementation of its discounting policy on all pipelines, it has adopted a standardized process for pipelines to act on requests to retain discounts while balancing the need to provide the pipeline with sufficient time to process requests to retain discounts and providing shippers with notice of pipeline determinations in sufficient time for shippers and replacement shippers to submit nominations at the four standard nomination cycles. The Commission further stated that in seeking to achieve this balance, it has found that two hours is a reasonable outside time limit for pipelines to evaluate requests to retain discounts and, therefore, requires pipelines to include in their tariffs a process under which the pipeline must process shipper requests to retain discounts in no longer than two hours from the time the request is submitted. Therefore, East Tennessee was directed to file tariff sheets implementing a procedure for processing requests to retain discounts within two hours of submission of a request.

2. Request for Rehearing

47. East Tennessee argues that the Commission has erroneously applied the CIG²² discount policy requiring East Tennessee to rebut a presumption that discounts may be retained in transactions involving segmentation or alternative points and that it must make decisions about the applicability of discounts to others within two hours of any request. East Tennessee contends that the Commission has not shown that this policy is just and reasonable either on an industry-wide basis or as applied to East Tennessee. East Tennessee further contends that the Commission has not explained, for example, how the CIG policy is consistent with a just and reasonable standard when the end result of its application is certain to be the curtailment of discounts. East Tennessee argues that the policy is vague and unexplained and does not articulate the meaning of key concepts such as similarly situated. East Tennessee asserts that the Commission has not met its burden of showing that the Settlement inappropriately balances the parties rights as regards the transfer of discounts. East Tennessee further asserts that given its lack of precedential impact there is no likelihood that approval would compromise the Commission's ability to apply policy in other litigated contexts. East Tennessee contends that the Commission's decision to reject the parties' extensive, good faith efforts to overcome their disagreements is in itself bad policy that is not justified or even acknowledged.

3. Commission Decision

48. The Commission rejects East Tennessee's rehearing request. In Order No. 637-A, the Commission found that the interaction of its segmentation policies and its current

²²Colorado Interstate Gas Co., 95 FERC ¶ 61,321 (2001)(CIG).

policy of permitting pipelines to limit discounts to particular points needed to be re-examined. The Commission determined that placing restrictions on discounted transactions could interfere with competition created through released capacity.²³

49. In Colorado Interstate Gas Company,²⁴ the Commission examined the effects of its existing discount policy on competition and found that if shippers with a discount would lose the discount and be subject to the maximum rate if they utilized their flexible point rights to move to a secondary point or segmented capacity which would use different points than the primary points contained in the contract, this would have the effect of restricting competition. The Commission, however, also recognized that if the discount were to be automatically applied at secondary points, discounts may be given for other than competitive reasons contrary to the discount policy. Therefore, the Commission found that these interests could best be balanced by permitting the shipper to retain its discount when moving to secondary or segmented points, if the pipeline has granted a discount to a similarly situated shipper at the alternate point. This allows a shipper to better compete with primary capacity offered by the pipeline and with other shippers at the alternate points. This policy was an application of the general requirement that pipelines must not engage in undue discrimination by ensuring that a shipper with a discounted contract can continue to receive a discount at points where it is similarly situated to other shippers receiving a discount. Therefore, the Commission has fully explained the reasoning behind the discount policy it has applied in the instant proceeding. Because the discount policy is designed to enhance competition between releasing shippers and the pipeline, East Tennessee cannot through a settlement eliminate its obligation to comply with the pro-competitive requirements of Order No. 637.

50. East Tennessee further requests that the Commission permit additional time until 8:30 a.m. CCT the next business day for it to process segmented capacity discount requests received after 4:00 p.m. CCT and require the shipper seeking to retain its discount on a non-business day to submit its request by 4:00 p.m. CCT on the business day prior to the non-business day. East Tennessee argues that the Commission contends the Commission has approved such requirements in other cases, citing, e.g., Transcontinental Pipe Line Corp., 96 FERC ¶ 61,352 (2001); National Fuel Gas Supply Corp., 98 FERC ¶ 61,123 (2002)(National Fuel); ANR; and Questar Pipeline Co., 98 FERC ¶ 61,159 (2002).

51. The Commission has recognized that pipelines may not have sufficient staff to process discount requests overnight. Therefore, pipelines must act on overnight requests to retain discounts received by 4 p.m. no later than 8:30 a.m. CCT the next business day and

²³Order No. 637-A at 61,595.

²⁴Colorado Interstate Gas Co., 95 FERC ¶ 61,321 at 62,120-21 (2001).

need not process requests on weekends. See National Fuel. Consistent with National Fuel, the Commission will grant East Tennessee additional time to process discount requests as requested.

E. Imbalance Trading Transportation Charge

1. January 30 Order

52. In the January 30 Order, the Commission rejected East Tennessee's proposal to assess a transportation charge on imbalance trades. The Commission stated that it was not satisfied with East Tennessee's answer with respect to its proposal to charge a transportation fee for imbalance trading. The Commission stated that East Tennessee had not documented how transportation revenue will be lost given that East Tennessee's system is based on a postage stamp rate design and is not divided into separate rates zones. The Commission further stated that East Tennessee has not demonstrated that its billing practices and rate design would lead to a revenue under recovery if a transportation charge is not assessed.

2. Rehearing Request

53. In its request for rehearing, East Tennessee argues that examples contained in Mr. McBride's testimony show its loss of revenue and new forms of gaming if the charge is not imposed. East Tennessee asserts that the LMS-MA and LMS-PA rate schedules are not transportation rate schedules but rather are load management, pooling types of arrangements at specific points, and, therefore, for the trade to occur transportation must be involved. East Tennessee further asserts that Mr. McBride's testimony demonstrates with specific examples how and when transportation occurs. Mr. McBride gives the example of a shipper which schedules 1000 Dth at an LMS-MA delivery point but actually takes 1500 Dth at that point and therefore, is 500 Dth "due pipe" and wishes to trade this imbalance with an LMS-PA customer who is 500 Dth "due shipper." Mr. McBride states that, since the LMS-MA Rate Schedule provides that the shipper will remain whole, the shipper only paid for the 1000 Dth scheduled. Mr. McBride further states that the LMS-MA customer must transport the 500 Dth "due shipper" imbalance to the LMS-PA customer's delivery point thereby incurring a transportation charge. East Tennessee argues that without a transportation charge it would lose transportation revenue, when real physical transaction takes place for the trade to be effectuated.²⁵

²⁵ Exhibit No. GEM-2 also claims that there is a loss of transportation revenue under Rate Schedule LMS if imbalances are tracked at the transportation contract level.

54. East Tennessee also provides an example which it asserts demonstrates when certain trades are revenue neutral. Mr. McBride states that although all imbalance trades involve transportation not all imbalance trades will incur a transportation charge. Mr. McBride gives the example of a shipper which schedules 1,000 Dth at an LMS-MA delivery point, but actually delivers 500 Dth and, therefore, the LMS-MA customer is 500 Dth "due shipper". Mr. McBride contends that the LMS-MA customer trades this imbalance with a LMS-PA customer that is 500 Dth "due pipeline" and there is no loss of transportation revenue for the trade.

55. As explained in East Tennessee's Order No. 637 compliance filing, East Tennessee currently provides a form of imbalance management service through OBAs at all of its receipt and delivery points under its Rate Schedule LMS-PA (receipt point OBAs) and Rate Schedule LMS-MA (delivery point OBAs). East Tennessee and the Balancing Party (any party that has executed an OBA) assume the responsibility for imbalance resolution. The shipper is deemed to have received its scheduled receipts and deliveries. Therefore, all receipt and delivery point imbalances on East Tennessee are resolved by the Balancing Parties rather than by shippers. Under the Settlement, LMS-MA and LMS-PA Balancing Parties are permitted to trade imbalances within the same Operational Impact Area (OIA) during the month and after the end of the month through the 17th business day of the following month, provided that the Balancing Party with the due pipeline imbalance reimburse East Tennessee for any differences in transportation revenues that may result from such trading and, as discussed below, the trade does not result in a transportation path that crosses a Posted Point of Restriction.

3. Commission Decision

56. Upon review of East Tennessee's explanation set forth in its request for rehearing, the Commission determines that East Tennessee has provided a sufficient explanation of how transportation revenue will be lost in certain trading transactions if there is no transportation charge for the transaction. Therefore, on rehearing, East Tennessee's trading transportation charge is acceptable subject to the conditions set forth below. East

²⁵(...continued)

However, under East Tennessee's tariff, imbalances are determined at the receipt and delivery point level under Rate Schedule LMS, not on a transportation service and shipper basis. Further, such revenue impact is inherent in East Tennessee's existing Rate Schedule LMS, as all transportation and shippers' imbalances behind every point are netted without reference to the origin of the imbalance. The Rate Schedule LMS netted imbalances have no direct correlation to any East Tennessee transportation service.

Tennessee has adequately explained that, because shippers pay transportation charges based solely on scheduled amounts, not on actual flows, netting and trading of excess receipts and deliveries could lead to a loss of transportation revenue.²⁶

a. Transportation Rate for Traded Imbalances

57. East Tennessee proposes to charge the "difference in transportation revenues that may result from such trading."²⁷ This proposed rate is ambiguous, as it leaves to East Tennessee's discretion what the difference in transportation revenues may have been. Under Rate Schedules LMS-MA and LMS-PA, imbalances are calculated monthly on a point-by-point basis. These imbalances are the net imbalance of all transportation services from or to the point. When these netted imbalances are traded with other point's imbalances, there may or may not be an comparable set of transportation service agreements behind the point. For East Tennessee, these imbalance volumes have lost all attribution to any specific transportation service.²⁸ Therefore, it is not clear what transportation rate East Tennessee will apply, and East Tennessee cannot simply choose any transportation rate. Accordingly, East Tennessee is directed to file revised tariff language, with adequate support, expressly stating the proposed transportation charges and how they would be calculated.²⁹

b. Transportation Overpayments:

58. East Tennessee did not fully address the reimbursement by the pipeline to the shipper should an overpayment to East Tennessee result from a netting and trading transaction. This could occur where a receipt point operator trades an underage below scheduled receipts to a delivery point operator with an underage below scheduled deliveries, such as in East Tennessee's example, discussed above, which East Tennessee incorrectly describes as revenue neutral. East Tennessee is directed to modify its tariff to

²⁶See Midwestern Gas Transmission Co., 101 FERC ¶ 61,310 (2002).

²⁷Proposed Section 8.4 to Rate Schedule LMS-MA, Second Revised Sheet No. 50C.

²⁸Under Rate Schedules LMS-MA and LMS-PA, how point imbalances and resulting any fees or penalties are allocated among transportation shippers behind the point are matters between the point operator and the transportation shippers.

²⁹The Commission notes that it accepted Tennessee's proposed traded imbalance transportation rate. That rate is the higher of the transportation rate provided in the Balancing Parties' transportation agreement or the firm transportation usage charge. Tennessee Natural Gas Company, 99 FERC ¶ 61,017 at P 144.

include language crediting or refunding revenue should a netting and/or trading transaction result in an overpayment to East Tennessee.

F. Posted Point of Restriction

1. January 30 Order

59. In the January 30 Order, the Commission noted that, in Order No. 587, the Commission permitted pipelines to designate Operational Impact Areas (OIA) in order to permit shippers to net and trade imbalances over the largest area possible without causing operational problems or threatening the pipeline's system integrity. The Commission further noted that Section 8.4 of Rate Schedule LMS-MA³⁰ provides, in part, that:

An LMS-MA Balancing Party may trade any imbalance with another LMS-MA Balancing Party, provided that the trade shall not result in a transportation path which crosses a Posted Point of Restriction, as defined in Section 1.44 of the GT&Cs, for that month.

60. The Commission found that East Tennessee had not adequately supported limiting trades that would cross a Posted Point of Restriction. The Commission required East Tennessee to address the following concerns and provide examples where appropriate. The Commission directed East Tennessee should include any operational reasons why such restrictions are necessary. Specifically, the Commission noted that it is unclear which "month" East Tennessee is referring to. The Commission questioned whether the restriction is in the month the imbalance occurred or in the following month when shippers are trying to trade imbalances and whether there are points of restriction issued for a specific day, a whole month, or some other standard of time.

61. The Commission stated that East Tennessee proposes to limit trading through a Posted Point of Restriction, to apparently prevent gaming, where it believes a customer could achieve a transportation service via a trade that it could not have nominated and scheduled on the day the restriction was in effect. The Commission further stated that preventing a trade to occur after the day of the restriction, or by subsequently permitting a trade to occur across the point of restriction if it is in the opposite direction of the system imbalance, will not alleviate the restriction nor aid in maintaining the integrity of the

³⁰Proposed East Tennessee FERC Gas Tariff, Second Revised Volume No. 1, Sheet No. 52C. Proposed Section 6 of Rate Schedule LMS-PA, Sheet No. 61 contains similar tariff language with respect to trades across the posted point of restriction.

system. The Commission noted that this is so since the trade will take place after the fact and the trade represents a financial transaction, not a physical transportation. The physical transportation has already taken place for the shipper that takes deliveries in excess of receipts downstream of the Posted Point of Restriction. If that shipper subsequently decides to trade with a shipper upstream of the point of restriction, there is no physical transportation, as that transportation has already occurred.

2. Rehearing Request

62. East Tennessee argues that the Commission's decision to question its support for limiting trades that cross a Posted Point of Restriction is in error. East Tennessee asserts that since its OIA was broadly drawn it needed a mechanism to ensure it would have the flexibility to address operational issues as they arose on the system. East Tennessee argues that in the face of near unanimous customer support and the fact that no customer or other party challenged this portion of the Settlement, there is no valid reason that this change is required. East Tennessee contends that, as detailed in the attached testimony of Mr. Gregg McBride, any other approach would be a means to game the system and avoid other imbalance service options. Mr. McBride states that the restriction occurs in the month and on the day or days in which the factors set forth in the definition of Posted Point of Restriction actually occur. Mr. McBride further states that posting of the Point of Restriction will be made prior to or during the day of the restriction and that the duration depends on the duration of the specific operating conditions.

63. East Tennessee further contends that there is physical transportation occurring at the time the Posted Point of Restriction is in place. East Tennessee asserts that trades between Rate Schedules LMS-MA and LMS-PA require physical transportation to occur. East Tennessee further asserts that if a customer wanted to circumvent the restriction it would go "due shipper" on the upstream side of the Posted Point of Restriction and get another customer to go "due pipe" on the downstream side during the time the restriction is in place. East Tennessee states that the trading may still occur on each side of the Posted Point of Restriction while the restriction is in place. East Tennessee contends that without the proposed limitations, netting and trading could be used to game the system or the restriction would be ignored, possibly bringing about further operational difficulties. East Tennessee further contends that permitting trades up to 17 business days after the month is a surrogate for transportation that could not occur in the prior month due to a Posted Point of Restriction and may impinge on the rights of other customers in their routine daily scheduling and nominating activities.

3. Commission Decision

64. East Tennessee has provided sufficient justification for its Posted Point of Restriction, and its request for rehearing is granted. The Commission has recognized that trading of OBA imbalances raises different issues than trading of shipper imbalances and has allowed pipelines to impose additional limitations on OBA trading, such as not permitting OBA operators to trade imbalances across operational impact areas (OIA).³¹ Here, although East Tennessee has proposed only one OIA, it has identified operational limitations that, at least in some circumstances, would justify having two OIAs for imbalance trading purposes. By permitting imbalance trading across its system unless a posted point of restriction is in effect, East Tennessee permits OBA operators greater flexibility than two OIAs would allow.³² Therefore, the Commission will grant rehearing and permit East Tennessee to implement imbalance trading for OBA imbalances with the posted point of restriction.

G. Nominations and Notifications for Pre-arranged, Non-Biddable Capacity Release Transactions

65. East Tennessee's tariff at Section 17.6(a) provides for the awarding of a contract within one hour of the posting of a pre-arranged release. In the January 30 Order, the Commission determined that the tariff is inconsistent with Section 284.12(c)(1)(ii) as it limits the nomination until the next day gas flow. The Commission noted that, as stated in CIG, pre-arranged replacement shippers should be able to nominate coincident with notification to the pipeline of the release at each of the four nomination opportunities.

66. East Tennessee argues that the Commission should clarify that East Tennessee may, within the meaning of coincident, have up to 15 minutes from the time the replacement shipper confirms the bid to finalize the contractual details. East Tennessee contends that it does process prearranged, non-biddable releases at the earliest available opportunity but cannot physically process those requests instantaneously.

³¹See Transcontinental Gas Pipe Line Corporation, 96 FERC ¶ 61,352, at 62,332 (2001); 98 FERC ¶ 61,365, at 62,575-76 (2002).

³²In addition, East Tennessee imposes no scheduling penalty for OBA operators who inject or delivery more than their scheduled quantity, and thus has no other protection in its tariff against potential "gaming."

67. The Commission, in Order No. 587-O,³³ has adopted Version 1.5 of the NAESB standards. Version 1.5 of Standard 5.3.2 establishes a revised capacity release timeline, which the Commission found satisfies the scheduling equality provisions of Section 284.12(c)(1)(ii). Under this standard, biddable releases would be posted by 3:00 p.m (rather than at 5:00 p.m. under the existing timeline), contracts would be issued within one hour of posting, and shippers would be able to nominate at the 5:00 p.m. Intra-day 2 nomination cycle or any following nomination cycle. Pipelines must be notified of non-biddable prearranged deals one hour prior to the nomination deadline for each of the four NAESB nomination cycles.

68. On August 12, 2002, East Tennessee made its filing in Docket No. RP02-493-000 to comply with Order No. 567-O.³⁴ Therefore, East Tennessee's request for rehearing regarding nominations and notifications for pre-arranged, non-biddable capacity release transactions is moot.

H. Penalty Provisions

1. January 30 Order

69. In the January 30 Order, the Commission considered Cumulative Imbalance Penalty provisions proposed by East Tennessee to correct imbalances on its system. The Municipals opposed this proposal as an unsupported increase in penalties. The Commission noted that, East Tennessee's then-current tariff provided that customers could resolve monthly imbalances through the existing cash-out mechanism at month's end and that East Tennessee was not proposing to replace the current monthly cash-out mechanism with a daily cash-out mechanism herein, but proposed to introduce a Cumulative Imbalance Penalty. The Commission found that, with the certain modifications, East Tennessee's proposed Cumulative Imbalance Penalty is a reasonable approach to dealing with adverse operational conditions on its system.

70. The Commission noted that East Tennessee's proposed tariff provided that it may prospectively invoke the Cumulative Imbalance Penalty on a customer-specific basis or on a system-wide basis after 24 hours notice if certain situations exist on its system. Specifically, the proposed penalty might be invoked if any of the following situations exist: (I) Transporter becomes aware of adverse operational or imbalance conditions on an

³³Standards for Business Practices Of Interstate Natural Gas Pipelines, Order No. 587-O, 99 FERC ¶ 61,146 (2002).

³⁴See September 30, 2002 Letter Order in Docket No. RP02-493-000, unpublished letter order, order on reh'g, 102 FERC ¶ 61,132 (2003).

upstream pipeline on which Transporter has swing capability; (ii) Transporter's system-wide imbalance is greater than 5 percent for any Day; (iii) Any Balancing Party's customer imbalance for any rolling twelve day period is greater than 8 percent; (iv) Maintenance or unexpected outages which result in the occurrence of operational or imbalance issues; or (v) Transporter deems it necessary in order to protect firm obligations.

71. The Commission stated that, for the most part, East Tennessee's proposal generally includes situations that allow East Tennessee to invoke the Cumulative Imbalance Penalty because the operational integrity of its system is threatened. However, the Commission further stated that conditions (ii) and (iii) appear to allow East Tennessee to invoke the penalty even if its system integrity is not threatened, but the system is merely out of balance by more than 5 percent, or if a customer is out of balance by more than 8 percent. The Commission recognized that its policy requires pipelines to narrowly design penalties to deter only conduct that is actually harmful to the system. Therefore, the Commission required East Tennessee to remove these two conditions under when it may invoke a Cumulative Imbalance Penalty or to justify why proposed tariff conditions (ii) and (iii) are necessary in order to protect system integrity.

72. In a contested element of the Settlement, East Tennessee also proposed to increase the amount of penalties assessed during a critical period for a violation of an Action Alert OFO³⁵ and unauthorized delivery imbalance charge³⁶ by adding the Henry Hub spot price to those penalties. East Tennessee proposed to assess these penalties only during critical periods. The Municipals opposed the increase in these penalties during critical periods. However, the Commission approved the proposal.

2. Rehearing Request

73. East Tennessee argues that the Commission's decision to require explanation and/or removal of two of the conditions under which East Tennessee may invoke its proposed Cumulative Imbalance Penalty is arbitrary, capricious, and an abuse of discretion. East Tennessee asserts that based on negotiations with its customers, it did not propose to replace the current monthly cash-out mechanism with a daily cash-out mechanism, but rather proposed the Cumulative Imbalance Penalty.

³⁵Pro Forma Tariff, GT&C ' 14.9, Sheet No. 126, provided that an Action Alert penalty is equal to an index price based on the Henry Hub Spot Price plus \$0.98 per dth for any volume of gas which deviates from the requirements of the Action Alert.

³⁶Pro Forma Tariff, GT&C ' 15.8, Sheet No. 132, provided that the Unauthorized Delivery Imbalance charge is equal to three times the daily demand rate pursuant to Rate Schedule FT-A plus an index price based on the Henry Hub Spot Price per dth for any unauthorized deliveries.

74. On March 15, 2002, the Municipals filed an answer to the request for rehearing.³⁷ The Municipals assert that East Tennessee has avoided discussion of Commission decisions involving two of its affiliates, Algonquin and Texas Eastern Transmission Corp., 98 FERC ¶ 61,215 (2002)(Texas Eastern). The Municipals further assert that in these orders the Commission rejected new penalties and tighter balancing requirements since such provisions were outside the scope of an Order No. 637 implementation proceeding.

3. Commission Decision

75. On further consideration of this issue, the Commission will require East Tennessee to revise its penalty provisions because in these provisions, East Tennessee increased its penalties and such increases go beyond pure compliance with Order No. 637.³⁸ This action is without prejudice to East Tennessee's refiling these provisions under NGA Section 4.

76. Order No. 637 established an NGA Section 5 proceeding to examine whether existing penalties remain just and reasonable since they are necessary to prevent the impairment of reliable service. Pipelines were neither required nor permitted to expand those existing penalties as part of their Order No. 637 compliance filings. Compliance with Order No. 637 should not be utilized as an opportunity for pipelines to propose new penalty provisions or increase their penalties either in a compliance filing or a related proposed settlement as in the instant proceeding. East Tennessee's proposal to increase penalties is contrary to Order No. 637.

77. In recent orders addressing other Order No. 637 compliance filings, the Commission has consistently reiterated its shift to a service-oriented policy that gives shippers other options to obtain flexibility, rejecting new penalty proposals or existing

³⁷Although our rules prohibit answers to requests for rehearing (18 C.F.R. § 213(a)(2) (2002)), we may, for good cause, waive this provision. We find good cause and will do so here to insure a complete record in this proceeding.

³⁸Although the Commission recognizes that these issues were not raised by any party on rehearing, the provisions were protested, and the Commission is requiring changes to these provisions to ensure consistency in its processing of Order No. 637 filings. This proceeding is not final, and the Commission has the authority, sua sponte, to modify its original order. See Valero Interstate Transmission Co. v. FERC, 903 F.2d 364 (5th Cir. 1990); Tennessee Gas Pipeline Company v. FERC, 871 F.2d 1099, 1107-09 (D.C. Cir. 1989); North Baja, 102 FERC. ¶ 61,239, at P 12, n.14 (2003).

penalties found to lack a relationship to the operational harm caused by shipper behavior.³⁹ Consistent with our rulings in other Order No. 637 orders including Texas Eastern, we deny East Tennessee's proposed Cumulative Imbalance Penalty and its proposed increase in its penalties by adding an index price component to the Action Alert OFO and authorized delivery imbalance charge. Therefore, East Tennessee must remove the proposed Cumulative Imbalance Penalty provisions and the proposed increase for a violation of an Action Alert OFO and unauthorized delivery imbalance charge from its proposed tariff sheets.

78. The Commission finds that East Tennessee's existing penalties are just and reasonable and consistent with Order No. 637. Therefore, East Tennessee can accept its proposal, in this docket, without the increase in penalties or continue its existing tariff provisions.⁴⁰

79. East Tennessee also challenged the Commission's determination that East Tennessee should not subject shippers to dual penalties for the same conduct by charging the Cumulative Imbalance Penalty as well as a monthly cash-out penalty. Since the Commission is requiring East Tennessee in this filing to eliminate the proposed Cumulative Imbalance Penalty provisions, there is no longer an issue of whether the pipeline is charging shippers twice for the same conduct. Should East Tennessee refile these provisions under NGA Section 4, it should address whether a double penalty is created.⁴¹

I. Crediting of Cash-out Mechanism Revenues

³⁹See Colorado Interstate Gas Co., 95 FERC ¶ 61,321 at 62,124-5 (2001); Canyon Creek Compression, 96 FERC ¶ 61,006 at 61,020-1 (2001); Steuben Gas Storage Co., 96 FERC ¶ 61,004 at 61,013 (2001); Gulf States Transmission Corp., 96 FERC ¶ 61,150 at 61,696 (2001); ANR Storage Co., 96 FERC ¶ 61,162 at 61,709 (2001); Iroquois Gas Transmission System, Inc. 97 FERC ¶ 61,164 at 61,746 (2001); Texas Eastern Transmission, L.P., 98 FERC ¶ 61,215 at 61,842-3 (2002); Southern Natural Gas Company, 99 FERC ¶ 61,042 at 61,163 (2002); and Cove Point LNG Limited Partnership, 99 FERC ¶ 61,142 (2002).

⁴⁰See Texas Eastern Transmission, L.P., 102 FERC ¶ 61,198 at 61,572 (2003).

⁴¹Pursuant to Section 154.203(b) of the Commission's regulations, East Tennessee should not mix its compliance obligation in this Docket with a NGA Section 4 filing.

80. In the January 30 Order, the Commission found that East Tennessee's proposal to keep separate accounts for all penalty revenue collected and then to credit each net penalty revenue back to non-offending shippers is in compliance with Order No. 637. However, the Commission noted that it believed that East Tennessee's tariff may be incomplete with respect to crediting the revenues East Tennessee receives from its monthly cash-out mechanism.⁴² Therefore, East Tennessee was required to credit back to all firm and interruptible non-offending shippers the net revenues its receives from its monthly cash-out mechanism.

81. In its rehearing, East Tennessee argues that the cash-out mechanism is not a penalty. East Tennessee further argues that the crediting required by the Commission already takes place under East Tennessee's tariff which has an existing cash-out refund mechanism.⁴³ East Tennessee contends that the Commission has not presented any evidence regarding the inadequacy of this refund mechanism. East Tennessee further contends that NGA Section 5 requires that the existing tariff provision be shown to be unjust and unreasonable and the replacement provision must be just and reasonable. East Tennessee asserts that the Commission failed to accord the Settlement its proper weight and to balance the benefits, if any, of overriding the parties' intentions.

82. East Tennessee does have an existing cash-out refund mechanism which requires the crediting of net revenues on an annual basis as it asserts. If the net cash-out activity for the annual period results in charges collected by East Tennessee in excess of payments by East Tennessee, East Tennessee credits the excess revenues to non-offending parties. East Tennessee's existing cash-out revenue crediting provisions are in accordance with Order No. 637. Therefore, the Commission grants the request for rehearing on this issue.

J. Compliance Filing

83. In the January 30 Order, the Commission found that East Tennessee had generally complied with Order No. 637 subject to certain modifications. The Commission ordered East Tennessee to file actual tariff sheets reflecting modifications related to scheduling equality, flexible point rights, discount provisions, park and loan service, penalty provisions, and penalty revenue crediting mechanism.

⁴²East Tennessee FERC Gas Tariff, Second Revised Volume No. 1, Rate Schedule LMS-MA Section 8.5, Sheet Nos. 53-55; Rate Schedule LMS-PA, Sheet Nos. 62-64.

⁴³Citing East Tennessee FERC Gas Tariff, Second Revised Volume No. 1, Rate Schedule LMS-MA Section 8.5(f) on Fourth Revised Sheet No. 55 and Rate Schedule LMS-PA Section 8 on Second Revised Sheet No. 64.

84. East Tennessee states that it has submitted tariff sheets reflecting the following modifications: (1) refinements to the capacity release provisions to conform to the Commission's policies on scheduling equality; (2) modifications to Rate Schedules FT-A and FT-GS relating to the submission of requests for primary point capacity; (3) the addition of new tariff provisions to reflect the Commission's policy on discounting as articulated in CIG, as modified by Granite State; (4) modification of the minimum time frame specified in Rate Schedule PAL within which a PAL shipper upon notification from East Tennessee, must take delivery of parked quantities or return loaned quantities to East Tennessee; (5) the addition of a mechanism to credit the value of imbalances upon the termination of a PAL service agreement to non-offending shippers; (6) consolidation of all penalty provisions under one section of the tariff; (7) crediting any revenues received from contract balances remaining after the contract termination to non-offending LNGS shippers; and (8) conforming changes to accurately reflect the provisions of the Settlement.

85. East Tennessee further states that it has filed alternative tariff sheets reflecting directives in the January 30 Order that the subject of its rehearing request as follows: (1) the requirement that upstream of Lewisberg and Dixon Springs, East Tennessee allow forwardhauls and backhauls to a single point without reference to a customers MDQ; (2) removal of provisions relating to trades across a posted point of restriction and Transportation Charges on traded quantities; and (3) removal of two conditions under which East Tennessee may invoke a Cumulative Imbalance penalty.

86. East Tennessee's proposed tariff language satisfactorily complies with the January 30 Order. The Appendix lists the tariff sheets that will be accepted, subject to the conditions of this order, and also lists other tariff sheets, including some of the alternative tariff sheets that are rejected.

87. The Commission is rejecting tariff language relating to partial day releases because this issue is being addressed in the proceeding relating to East Tennessee's Order No. 597-O compliance. On August 12, 2002, East Tennessee made a filing in Docket No. RP02-493-000, to comply with Order No. 587-O, and included tariff sheets incorporating time lines found in Version 1.5 of NAESB standard 5.3.2, and also included provisions relating to partial day recall. On September 30, 2002, the Commission, by letter order, conditionally accepted East Tennessee's August 12, 2002 filing on the NAESB time line standard. However, the September 30 order required East Tennessee to eliminate certain restrictions on the quantity of gas that can be released on a partial day basis, to which East Tennessee filed for rehearing of that issue. On February 5, 2003, the Commission denied East Tennessee's request for rehearing related to the determination of partial day release

quantities and required further modifications.⁴⁴ On February 19, 2003, East Tennessee submitted its compliance filing to the Commission's February 5, 2003 order, which is pending before the Commission.

88. Since the Commission is acting on East Tennessee's proposed tariff sheets relating to partial day releases in Docket No. RP02-493, et al., that issue is moot in this proceeding. Therefore, we reject the tariff language filed in this proceeding relating to partial day releases.

K. Implementation Schedule

89. East Tennessee states that Article III of the Settlement, inter alia, provides that the effective date of the Settlement is four months following the date upon which the Commission order approving the Settlement is no longer subject to rehearing or appeal and, therefore, the earliest possible effective date is six months from the date of the order on its rehearing request in these proceedings. The Commission will not accept a settlement provision that allows a pipeline to put off compliance with Order No. 637 simply by filing an appeal, because such a provision could potentially deny shippers the benefits of Order No. 637 until an indeterminate and potentially far off date. Therefore, the Commission rejects this aspect of the Settlement. Since the Commission is ruling on East Tennessee's rehearing request in this proceeding, the Commission will require East Tennessee to comply with the requirements of Order No. 637 on the first day of the month four months from the date of this order. East Tennessee is required to file revised tariff sheets reflecting the discussion in this order within 30 days of the date of the order.

The Commission orders:

(A) Revised tariff sheets filed on March 27, 2002, and December 2, 2002, in these proceedings, as indicated in the Appendix to this order, except those rejected in the Ordering Paragraph (B) below, are accepted subject to the conditions in this order and the Ordering Paragraphs below, as discussed in the body of this order, to become effective on the first day of the month four months from the date of this order.

(B) The requests for clarification and rehearing are hereby granted, and denied, as discussed in the body of this order

(C) The Commission finds that subject to the modifications discussed above, East Tennessee has complied with the January 30 Order and the Remand Order in these

⁴⁴102 FERC ¶ 61,132 (2003).

proceedings.

(D) East Tennessee is directed to file actual tariff sheets consistent with the directives set forth in this order within thirty days of the date of issuance of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.

Appendix

East Tennessee Natural Gas Company
Docket Nos. RP00-469-003 and RP01-22-005

FERC Gas Tariff
Second Revised Volume No. 1

Sixth Revised Sheet No. 1	Seventh Revised Sheet No. 101 */
First Revised Sheet No. 2	Sixth Revised Sheet No. 103
Third Revised Sheet No. 4A	Eighth Revised Sheet No. 105 */
First Revised Sheet No. 8	First Revised Sheet No. 105A */
Seventh Revised Sheet No. 9	First Revised Sheet No. 112
Fifth Revised Sheet No. 10	Third Revised Sheet No. 113
Original Sheet No. 13	Fifth Revised Sheet No. 123
Sheet Nos. 14 - 16	Fifth Revised Sheet No. 124
First Revised Sheet No. 19	Second Revised Sheet No. 125
Fifth Revised Sheet No. 20	Third Revised Sheet No. 126
Fourth Revised Sheet No. 33	Eighth Revised Sheet No. 127 */
Seventh Revised Sheet No. 52	Fifth Revised Sheet No. 129A */
Eighth Revised Sheet No. 52A	Third Revised Sheet No. 129B
Second Revised Sheet No. 52B	Third Revised Sheet No. 130
Fifth Revised Sheet No. 52C	Fifth Revised Sheet No. 131 */
Seventh Revised Sheet No. 54	Fifth Revised Sheet No. 132
Second Revised Sheet No. 54B */	Fourth Revised Sheet No. 134 */
Fifth Revised Sheet No. 55	Sixth Revised Sheet No. 139 */
First Revised Sheet No. 55A	Original Sheet No. 139A */
Eighth Revised Sheet No. 61	Fifth Revised Sheet No. 140 */
First Revised Sheet No. 62A	Third Revised Sheet No. 144 */
Eighth Revised Sheet No. 63 */	Fourth Revised Sheet No. 147
Third Revised Sheet No. 64	Original Sheet No. 147A
Original Sheet No. 68	Fourth Revised Sheet No. 167
Original Sheet No. 69	Fifth Revised Sheet No. 168
Original Sheet No. 70	Ninth Revised Sheet No. 176 */
Original Sheet No. 71	Original Sheet No. 177A
Original Sheet No. 72	Original Sheet No. 177B
Original Sheet No. 73	Original Sheet No. 177C
Original Sheet No. 74	Original Sheet No. 177D
Original Sheet No. 75	Original Sheet No. 177E
Sheet Nos. 76 - 99	Original Sheet No. 177F
	Original Sheet No. 177G

Second Revised Sheet No. 205
First Revised Sheet No. 207
Second Revised Sheet No. 208
First Revised Sheet No. 214
Third Revised Sheet No. 216
Third Revised Sheet No. 217
Second Revised Sheet No. 223
Third Revised Sheet No. 224
Second Revised Sheet No. 225
Second Revised Sheet No. 230
Second Revised Sheet No. 231
Third Revised Sheet No. 232
First Revised Sheet No. 233
First Revised Sheet No. 234

Second Revised Sheet No. 235
Sheet Nos. 236 - 237
Second Revised Sheet No. 273

Alt Original Sheet No. 13 */
Alt Fifth Revised Sheet No. 52C */
Alt Eighth Revised Sheet No. 61 */
Alt First Revised Sheet No. 105A */
Alt Original Sheet No. 177A */

*/ Rejected as moot

East Tennessee Natural Gas Company
Docket No. RP03-177-000

FERC Gas Tariff
Second Revised Volume No. 1

Eighth Revised Sheet No. 9
Original Sheet No. 9A
Original Sheet No. 13A
Fourth Revised Sheet No. 129B
Fourth Revised Sheet No. 130