

FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, D.C. 20426

September 11, 2003

In Reply Refer To:
Docket Nos. RP98-53-000 and
GP98-29-000

Kinder Morgan Interstate Gas Transmission LLC
Attn: Bentley Breland
Attorney for Kinder Morgan Interstate Gas Transmission LLC
370 Van Gordon Street
Lakewood, CO 80228

Dear Mr. Breland:

1. On June 23, 2003, Kinder Morgan Interstate Gas Transmission LLC (KMIGT) filed with the Presiding Administrative Law Judge a Settlement Agreement (Phase II Settlement) between KMIGT and Aquila Networks (successor to Peoples Natural Gas), CenterPoint Energy Minnegasco, George Kravis II Trust, Raymond and Bessie Kravis Foundation (as successor to the Raymond Kravis Trust), J. T. Oil Company, Kansas Natural Gas, Inc. (representative of the Ross Beach Trust), Kinder Morgan, Inc. (successor to KN Energy, Inc.), Marden Producing Company, Midwest Energy, Inc., NorthWestern Energy, a division of NorthWestern Corporation, ONEOK Energy Resources Company (formerly ONEOK Resources Company) (ONEOK), Par Petroleum Company, Patina Oklahoma Corp. (successor to Halliburton Oil Producing Company), and Public Service Company of Colorado (hereinafter collectively referred to as the Signatory Parties). Commission Trial Staff supports the Settlement. Initial comments were filed in support of the Phase II Settlement by KMIGT, Kinder Morgan, Inc. and the Staff. Reply Comments in support of the Settlement were filed by KMIGT. No party has filed comments opposing the Phase II Settlement. On August 4, 2003, the Presiding Administrative Law Judge certified the settlement to the Commission as uncontested.

2. The Phase II Settlement addresses the unextinguished Kansas ad valorem tax liabilities of twelve producers¹ and associated working interest owners (Phase II Producers) who did not participate in an earlier settlement (2002 Settlement) in these proceedings that was approved by the Commission on March 18, 2002.² Specifically, the Phase II Settlement resolves the unextinguished Kansas ad valorem tax liability of eight Phase II Producers and determines that the Commission should cease refund collection efforts for the remaining four non-participating producers. The Phase II Settlement in conjunction with the settlement in GP98-29-000 also resolves the issue of the liability, if any, of ONEOK.

3. The Phase II Settlement is binding on all parties with a continuing interest in these proceedings that do not affirmatively opt-out of the process (Settling Parties). The Phase II Settlement provides two means of opting-out of the Phase II Settlement. They are: (1) the filing with the Commission of initial comments opposing the Phase II Settlement, or (2) the failure to pay by the due date any positive Settlement Payment applicable to the first seller reflected on Appendix A, with additional interest accruals as provided in the Phase II Settlement. All Phase II Producers who make payment to KMIGT by the due date in accordance with the terms of the Phase II Settlement are bound by the Settlement as if they were Signatory Parties thereto. All Phase II Producers shown on Appendix A, that are not also Signatory Parties thereto, will be deemed to have accepted this Phase II Settlement unless such Phase II Producer affirmatively opts out of participation in the Phase II Settlement. The refund liability of royalty owners to working interest owners accepting the Phase II Settlement is completely and fully released.

4. The Phase II Settlement specifies a Settlement Payment applicable to each Phase II Producer as set forth in Appendix A to the Phase II Settlement. Settlement Payments include interest through April 30, 2003, and will be adjusted only for additional interest that accrues, as specified in the Phase II Settlement, until the first day of the month following the date of a final Commission order approving the Phase II Settlement without

¹ In addition to the Phase II Settlement that KMIGT filed in Docket No. RP98-53-000, the Signatory Parties agreed to a separate negotiated settlement with ONEOK, as of April 30, 2003, in the amount of \$5,403.99. This amount constitutes the final settled obligation of ONEOK as of April 30, 2003 and is not subject to further negotiation or change for any reason, but may be subject to additional interest accruals calculated as explained in Article II of the Phase II Settlement.

² Kinder Morgan Interstate Gas Transmission LLC, 98 FERC ¶ 61,303 (2002).

modification. The Phase II Settlement also specifies the Settlement Payment applicable to ONEOK.

5. Each Phase II Producer's ad valorem tax refund amount is based on the aggregated liability associated with its working interests, and reflects appropriate adjustments for headroom³ where shown. The Phase II Settlement then resolves the refund liability of five of the Phase II producers by reducing this refund liability by the greater of \$80,000 or 25%, but in no event can the settlement reduction reduce the producer's aggregate refund liability below zero. The effect of this negotiated resolution is that any of the five Phase II Producers with an aggregate refund liability, as of April 30, 2003, of \$80,000 or less is released from liability under the Phase II Settlement. The liability of any of the five Phase II Producers with an aggregate liability, as of April 30, 2003, of greater than \$80,000, but less than \$320,000, is reduced by \$80,000. The liability of any of the five Phase II Producers with an aggregate refund liability, as of April 30, 2003, of greater than \$320,000 is reduced by 25%.

6. The Phase II Settlement resolves the refund liability of the Ross Beach Trust, a Kansas trust, upon payment of a negotiated dollar refund payment of \$50,000 as of April 30, 2003. Interest will accrue on this amount as set forth in the Phase II Settlement. This payment reflects the settlement of the significant legal and factual issues involved. The Phase II Settlement also resolves the liability, if any, of ONEOK on a negotiated payment of \$5,493.99, as of April 30, 2003. Interest will accrue on this amount as set forth in the Phase II Settlement. The payment resolves difficult disputed factual and legal issues concerning ONEOK's liability, if any, for refunds of Kansas ad valorem tax reimbursements. The Phase II Settlement extinguishes the refund liability of Goodland Gas Company based upon a headroom analysis which determined that all of the specific Goodland wells associated with Kansas ad valorem tax payments made by KMIGT had been deregulated under the NGPA during the 1983-1988 refund period. The Phase II Settlement also resolves the liability of Imperial Oil and Gas, Inc., Robert L. Williams, and Imperial Oil Company, its predecessors and affiliated entities and individuals, on a negotiated basis following a "headroom analysis," an adjustment under the terms of the Settlement, and an evaluation of the expenditures of resources that would otherwise be

³ Under our decisions and those of the D.C. Circuit Court of Appeals regarding Kansas ad valorem taxes, a producer's obligation to refund Kansas ad valorem tax reimbursements is limited in any specific first sale transaction only to that portion of the reimbursement that caused the total proceeds in the transaction to exceed the applicable maximum lawful price established by the NGPA. "Headroom" refers to the factual determination as to whether the ad valorem tax reimbursements caused the price received by the producer to exceed the applicable MLP, and by how much.

required to achieve a refund. The impact of these agreed-upon reductions is reflected in the “Settlement Balance” column on Appendix A.

7. Each Phase II Producer is responsible for refunding to applicable royalty interest owners amounts previously paid-in, directly or indirectly, to the Phase II Producer applicable to the royalty interest owner’s liability for Kansas ad valorem tax liability on the KMIGT system.

8. Under the terms of the Phase II Settlement, once a Phase II Producer with a positive Settlement Payment makes payment to KMIGT of the sum calculated in accordance with the Phase II Settlement, the Phase II Producer will be released from any further liability for refunds and any interest on refunds that is owed to KMIGT and its customers under the NGPA for the subject period. ONEOK also will be released from any liability upon payment of the amount negotiated in the Docket No. GP98-29-000 agreement, plus interest calculated in accordance with the Phase II Settlement. All other Phase II Producers are released from any further liability for refunds and any interest on refunds that is owed to KMIGT and its customers under the NGPA for the subject period unless they opt-out of the Phase II Settlement. KMIGT is released from any claims for refunds or other liability with respect to all Phase II producers and any interest on refunds that is owed to KMIGT and its customers under the NGPA for the subject period. Finally, under the Phase II Settlement, each royalty interest owner is released from all liability to KMIGT and its customers, and to the relevant working interest owner, for refunds of Kansas ad valorem tax refunds on the KMIGT system.

9. Settling Parties agree that regardless of any legislative or regulatory initiatives, they will pay their respective Settlement Payments under the terms and conditions of the Settlement and that they will not support legislation or regulation that would alter the terms of the Settlement.

10. ONEOK and each Phase II Producer with a positive Settlement Payment shall have 15 days from the first day of the month after the Commission’s order approving the Phase II Settlement without modification becomes final and non-appealable to make refunds to KMIGT of the Settlement Payment and additional interest calculated in accordance with the Phase II Settlement, accompanied by sufficient documentation to show the interest accrued, if any, on escrowed refund amounts to the effective date of the Settlement.

11. Within 30 days of the receipt of refunds from Phase II Producers with positive Settlement Payments, KMIGT will distribute the net refunds received from them, plus additional interest calculated in accordance with the Phase II Settlement, to the parties

specified in Appendix B to the Settlement, calculated using the annual factors listed in that appendix. Pursuant to the Phase II Settlement, KMIGT is entitled to reduce the net refunds by \$30,000 to reflect incremental expenses incurred by KMIGT since the effective date of the 2002 Settlement for outside legal and temporary services related to the proceedings culminating in the Phase II Settlement.

12. The Phase II Settlement recommends that the Commission cease collection efforts with respect to four Phase II Producers – The Maurice Brown Company, Petroleum Production Management (which KMIGT determined after the 2002 Settlement to be the successor by name change to The Maurice L. Brown Company), Brock Resources/Argonant Energy, and Leland E. Brock. These Phase II Producers did not participate in the 2002 Settlement, did not respond to repeated attempts to contact them following that settlement, and did not participate in the negotiations that resulted in the Phase II Settlement. Continued collection efforts are no longer warranted and place unnecessary burdens on Commission staff and KMIGT.

13. The Phase II Settlement will become effective on the first day of the month following the day that the Commission's order approving the Phase II Settlement without modification or condition is final and non-appealable. The Phase II Settlement is void if the Commission modifies or imposes conditions upon the Phase II Settlement and rehearing is sought by a Signatory Party, unless the Signatory Parties agree otherwise in writing within 15 days after such petition for rehearing is filed. The effectiveness of the Phase II Settlement also is contingent on approval or non-opposition by all applicable state regulatory agencies.

14. The Settling Parties intend the Phase II Settlement to be a full and complete resolution of any and all issues on KMIGT's system relating to the obligation Phase II Producers (including ONEOK) to pay refunds with interest of Kansas ad valorem tax reimbursement to KMIGT and the entitlement of KMIGT and its customers to receive refunds with interest of such tax reimbursements for all periods through June 28, 1988. The Phase II Settlement resolves all outstanding NGPA Section 502(c) adjustment relief proceedings as well as all proceedings for legal or equitable relief from the obligation to pay refunds of and interest on refunds of Kansas ad valorem tax reimbursements as they may relate to KMIGT brought by any Appendix A Phase II Producer that does not affirmatively opt-out of the Phase II Settlement. Such proceedings are moot as to refunds relating to KMIGT. Phase II Producers are required to make any filings in such proceedings necessary to effectuate the Phase II Settlement.

15. Settling Parties and their affiliates are prohibited from commencing, or causing to be commenced, any new Commission proceedings, court cases, appeals, or other proceedings related to Kansas ad valorem taxes or rates on KMIGT's system associated

with the refund period ending in June 1988.⁴ If a Settling Party pursues any legal action of any type or description in any forum relating either to generic Kansas ad valorem tax issues or to the refund claims of any other pipeline, any resulting decision shall have no effect whatsoever on the Phase II Settlement approved by the Commission. The Phase II Settlement also resolves any collection proceedings brought by KMIGT relating to refunds and interest on refunds of Kansas ad valorem tax reimbursements to KMIGT as to each Appendix A working interest owner that is a Settling Party. Regardless of the outcome of any such proceeding, Settling Parties agree to pay their Settlement Payments without recourse and to abide by the terms of the Phase II Settlement.

16. The Settling Parties intend the Phase II Settlement to be a full and complete resolution of any and all issues related to Kansas ad valorem tax refunds on KMIGT's system. Should any decisions in cases currently pending in federal and state courts related to the legal rights and obligations of the parties with respect to the payment and distribution of Kansas ad valorem tax refunds conflict with the Phase II Settlement, and apply to KMIGT and its customers, the terms of the Phase II Settlement shall apply in lieu of any such decisions, to the extent allowed by law, with respect to the claims of the Settling Parties.

17. The Settling Parties that have been actively involved in any legislative or regulatory proposal related to these refunds, agree that they will actively oppose any actions taken by any entity that would alter the terms and provisions agreed to in the Phase II Settlement while all other Settling Parties will not support such proposals. The Settling Parties further agree that, regardless of any such action, each Settling Party will pay its Settlement Amount in accordance with the terms of the Phase II Settlement. Regardless of any legislative enactment, whether presently pending or subsequently introduced or enacted, the Phase II Settlement shall govern the rights and obligations of the Settling Parties, to the extent allowed by law.

18. No party has filed comments opposing the Phase II Settlement. The Commission finds that the uncontested Settlement is fair, reasonable and in the public interest, and accordingly the Commission approves the settlement. The Commission's approval of the

⁴ This provision does not apply to the Kansas Corporation Commission (KCC)/Kansas appeal pending in Case No. 99-1156 in the U.S. Court of Appeals for the D.C. Circuit, or to the KCC proceeding in Docket No. 99-GIMG-068-GIG, or to the appeal pending before the Kansas Supreme Court in Case No. 01-86614, except insofar as any decision in Case No. 99-1156 conflicts with the Settlement and applies to KMIGT and its customers. In that case, the terms of the Settlement will apply in lieu of any such decision.

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Settlement does not constitute approval of, or precedent regarding, any principle or issue in this proceeding.

19. The Commission ceases collection efforts with respect to The Maurice Brown Company, Petroleum Production Management, Brock Resources/Argonant Energy, and Leland E. Brock.

20. This letter terminates Docket Nos. RP98-53-000 and GP98-29-000.

By direction of the Commission.

Linda Mitry,
Acting Secretary.

cc: All parties