ORAL ARGUMENT HAS NOT BEEN SCHEDULED

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**IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT**

No. 05-1214

**NORTH BAJA PIPELINE, LLC,
PETITIONER,**

v.

**FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.**

**ON PETITION FOR REVIEW OF ORDERS OF THE
FEDERAL ENERGY REGULATORY COMMISSION**

BRIEF OF RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

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FEDERAL ENERGY REGULATORY
COMMISSION
WASHINGTON, D.C. 20426**

FEBRUARY 16, 2006

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CIRCUIT RULE 28(a)(1) CERTIFICATE

A. Parties and Amici

The parties before this Court are identified in the brief of Petitioner.

B. Rulings Under Review

1. *North Baja Pipeline, LLC*, 109 FERC ¶ 61,159 (2004); and

2. *North Baja Pipeline, LLC*, 111 FERC ¶ 61,101 (2005).

C. Related Cases

This case has not previously been before this Court or any other court. Counsel is not aware of any other related cases pending before this or any other court.

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Lona T. Perry
Attorney

February 16, 2006

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GLOSSARY

FERC	Federal Energy Regulatory Commission
North Baja	Petitioner North Baja Pipeline LLC
Opinion No. 406	*Tennessee Gas Pipeline Co*., Opinion No. 406, 76 FERC ¶ 61,022 (1996)
Opinion No. 406-A	*Tennessee Gas Pipeline Co*., Opinion No. 406-A, 80 FERC ¶ 61,070 (1997)
Order No. 636	*Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636, FERC Stats. & Regs. ¶ 30,939, *order on reh'g*, Order No. 636-A, FERC Stats. & Regs. ¶ 30,950, *order on reh'g*, Order No. 636-B, 61 FERC ¶ 61,272 (1992), *reh'g denied*, 62 FERC ¶ 61,007 (1993)
Rehearing Order	*North Baja Pipeline, LLC,* 111 FERC ¶ 61,101 (2005)
Tariff Order	*North Baja Pipeline, LLC*, 109 FERC ¶ 61,159 (2004)

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BRIEF OF RESPONDENT
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STATEMENT OF THE ISSUES

1. Whether the Federal Energy Regulatory Commission ("Commission" or "FERC") appropriately rejected North Baja Pipeline LLC's ("North Baja") proposed *force majeure* credit mechanism because the provision forced shippers to bear an inequitable share of the risk of service interruptions due to no-fault, *force majeure* events.

2. Whether the Commission appropriately determined that service interruptions due to planned maintenance on the North Baja pipeline were not *force majeure* events out of North Baja's control, and therefore it was inequitable to permit North Baja to collect reservation charges, recovering its fixed costs, for firm service not provided to shippers.

STATUTES

The relevant statutes are contained in the Addendum to the Brief for Petitioner.

STATEMENT OF FACTS

I. Commission Policy On Credits for Firm Service Interruptions

A. Adoption of Straight Fixed-Variable Rate Design

Most pipeline customers pay a two-part rate for firm transportation service: a reservation (or demand) charge to reserve pipeline capacity regardless of the volume of gas transported, and a usage (or commodity) charge for the gas actually transported. *See, e.g.*, *Tennessee Gas Pipe Line Co. v. FERC*, 400 F.3d 25, 27 (D.C. Cir. 2005) (explaining pipeline ratemaking).

Prior to Order No. 636,[1] most pipelines used a modified fixed-variable rate design in which the usage charge recovered some of the pipeline's fixed costs – the return on equity and related taxes – as well as variable costs. Order No. 636 at 30,433. Order No. 636 found that the fixed costs in the modified fixed-variable rate usage charge varied between pipelines depending on such factors as the original cost of the pipeline facilities, the amount that had already been depreciated, and the allowed rate of return on equity. *Id*. As a result, competition between gas sellers at the wellhead was not based on the seller's costs, but was influenced by the fixed costs in the pipeline usage charges, thereby inhibiting competition among gas sellers and the development of a national market. *Id*. at 30,433-34. Producers whose gas was transported on pipelines with low usage charge could, under the modified fixed-variable rate design, charge higher prices or sell greater quantities than otherwise equally efficient producers whose gas was transported over pipelines with a higher usage charge. Order No. 636-A at 30,596.

[1] *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636, FERC Stats. & Regs. ¶ 30,939, *on reh'g*, Order No. 636-A, FERC Stats. & Regs. ¶ 30,950, *on reh'g*, Order No. 636-B, 61 FERC ¶ 61,272 (1992), *reh'g denied*, 62 FERC ¶ 61,007 (1993), *aff'd in pertinent part, United Distribution Cos. v. FERC*, 88 F.3d 1105 (D.C. Cir. 1996).

Accordingly, Order No. 636 required that, if a pipeline imposes a reservation charge for firm pipeline service, it must recover all fixed costs of service in the reservation charge, and recover all variable costs of service in the usage charge.[2] This is known as straight fixed-variable rate design. The Commission found that straight fixed-variable rate design would maximize competition at the wellhead by removing the distorting influence of including a pipeline's fixed transportation charges in its usage charges. *Id.* at 30,434.

Under the modified fixed-variable rate design, the risk of a *force majeure* interruption in service was automatically shared between the pipeline and the shippers. *Tennessee Gas Pipeline Co*., Opinion No. 406, 76 FERC ¶ 61,022 (1996) ("Opinion No. 406"), *on reh'g*, Opinion No. 406-A, 80 FERC ¶ 61,070 at 61,199 (1997) ("Opinion No. 406-A"). Because a portion of the pipeline's fixed costs was included in the usage charge, in the event of a *force majeure* interruption shippers were at risk for the payment of the reservation charge, and the pipeline was at risk for the costs included in the usage charge, since the shippers would not have to pay any usage charge. *Id*. However, under the straight fixed-variable method, the

[2] Fixed costs of providing transportation service (such as return on equity) do not change with the amount of gas transported, unlike variable costs (principally the cost of fuel for pipeline compressors).

pipeline shares no risk because all of its fixed costs are included in the reservation charge. *Id*.

B. Opinion No. 406

Opinion No. 406 addressed how to accomplish a sharing of the risk of *force majeure* service interruptions under straight fixed-variable rate design. The Commission continued to find that the risk of *force majeure* service interruptions should be shared by all parties as, by definition, *force majeure* events are unexpected and uncontrollable, and therefore neither the pipelines nor the shippers are at fault. Opinion No. 406 at 61,088. The Commission noted that it had previously implemented a form of risk sharing through limiting the length of time in which a pipeline is excused from providing reservation charge credits during a *force majeure* event. *Id*. at 61,089 (citing *Texas Eastern Transmission Corp*., 62 FERC ¶ 61,015 at 61,089-91, *on reh'g*, 63 FERC ¶ 61,100 at 61,433-35 (1993)). Texas Eastern was permitted to avoid reservation charge adjustments to the earlier of 10 days, or when the pipeline should have resolved the *force majeure* situation through the exercise of due diligence. *Id*. This was found to be a reasonable method of sharing the risk since the customers bore the risk for only a limited period of time, after which the risk shifts to the pipeline. *Id*. This provides an incentive for the pipeline to regain control of its system as soon as possible, and assures customers that they will not bear the risk of an extended *force majeure* interruption. *Id*.

In Opinion No. 406, the Commission considered a proposal providing a partial credit to shippers from day one of the *force majeure* service interruption equal to the pipeline's return on equity and associated income taxes for the undelivered amount. *Id*. The Commission found that, while there may be other methods, such as that employed in *Texas Eastern*, to effectuate sharing of the risks of *force majeure* interruptions, the partial credit proposal was a reasonable implementation of the risk sharing principle. *Id*. In fact, requiring the pipeline to provide reservation charge credits equal to its return on equity and taxes returns the balance of risk back to the status quo under modified fixed-variable rate design before the Commission mandated use of straight fixed-variable rate design -- under modified fixed-variable rate design, the pipeline's recovery of its return on equity and taxes was dependent on its throughput. *Id*.

In contrast, the Commission required full reservation credits for non-*force majeure* interruptions in firm service. *Id*. at 61,086. Because a pipeline is responsible for operating its system so that it can meet its contractual obligations, if the pipeline must curtail firm service due to an event within its control or management, the Commission found it inequitable for the pipeline's customers to bear the risk associated with such mismanagement. *Id*. This reservation charge credit also provides an incentive to the pipeline to manage its system so that it can avoid interruptions that it could have avoided with better management. *Id*. Affording less than full reservation credits to customers does not further the underlying objectives of providing adequate compensation to customers and adequate incentive for the pipeline to avoid interruptions within its control. *Id*.

With regard to maintenance interruptions, the Commission has found that unscheduled maintenance generally results from an operational problem and therefore is a no-fault, *force majeure* event. *El Paso Natural Gas Co*., 105 FERC ¶ 61,262 at P 14 (2003). However, scheduled maintenance is within the control of the pipeline, and therefore full reservation charges must be given for service interruptions due to planned maintenance. *Id*. While the Commission recognized that maintenance is an important and necessary function, the Commission found nevertheless that the pipeline should have an incentive to perform maintenance with minimal service interruptions. *Id*. Full reservation charge credits provide that incentive. *Id*.

As a result, the Commission has rejected arguments that scheduled maintenance should be treated as a *force majeure* event because it is a mandatory function and the pipeline may have limited flexibility to schedule maintenance in a way that minimizes interruptions to customers. *Id*. at PP 6-7, 15. The Commission's policy on scheduled maintenance is dependent on the pipeline's obligation to operate its system in a manner that will provide agreed-upon service and the need to provide incentives to pipelines to minimize service disruptions. *Id*. at P 15; *Natural Gas Pipeline Co.*, 106 FERC ¶ 61,310 at PP 15-16 (2004); *El Paso Natural Gas Co*., 108 FERC ¶ 61,056 at PP 9-10 (2004). The Commission, however, does permit pipelines to design their reservation charge credit proposals in a manner that will allow them to comply with Commission policy and still meet their non-discretionary obligations, such as by approving delivery thresholds over which a pipeline is not obligated to provide a reservation charge credit. *Florida Gas Transmission Co*., 107 FERC ¶ 61,074 at P 32 (2004) (citing *Natural Gas*, 106 FERC ¶ 61,310 at P 17 (approving a 98 percent delivery threshold)).

II. The Challenged Orders

On October 14, 2004, North Baja filed tariff sheets proposing a partial reservation charge credit for service interruptions longer than ten consecutive days occasioned by *force majeure* events. R. 1 at 4-5, JA 4-5. The proposed credit would equal that portion of a shipper's Maximum Daily Quantity that North Baja was unable to deliver, multiplied by the return on equity and related income tax component of North Baja's firm reservation charges. *Id*. at 5.

A. The Tariff Order

On November 12, 2004, the Commission accepted and suspended North Baja's tariff sheets, subject to refund and conditions. The Commission found that North Baja must provide a full reservation charge credit whenever there is a service interruption in a non-*force majeure* event, consistent with the Commission policy set forth in *Natural Gas*, 106 FERC ¶ 61,310. *North Baja Pipeline, LLC*, 109 FERC ¶ 61,159 (2004) ("Tariff Order") at P 11, JA 57.

The Commission further found that North Baja's proposed reservation credit for *force majeure* events did not fully comply with Commission policy. *Id*. at P 12, JA 57. Under North Baja's proposal, no reservation credit would be provided for the first ten consecutive days, and following that, firm shippers would be entitled only to a partial credit. *Id*. at P 13, JA 57-58.

Under Commission policy, *force majeure* events are no-fault occurrences, and therefore all parties, including the pipeline, should share in the burdens of a *force majeure* interruption. *Id*. at P 14, JA 58 (citing *El Paso*, 104 FERC ¶ 61,045 (2003)). Commission precedent provides guidance on appropriate reservation credits. *Id*. *El Paso* allowed the pipeline to provide partial reservation charge credits equal to the return on equity and income tax portion of the reservation charge from day one of *force majeure* service interruptions. *Id*. *Texas Eastern* allowed the pipeline to issue full demand charge credits after the lesser of ten days or when the pipeline should have, in the exercise of due diligence, overcome the *force majeure* event. *Id*. (citing *Texas Eastern*, 62 FERC ¶ 61,015 as well as *Natural Gas*, 106 FERC ¶ 61,310).

Thus, Commission policy had allowed either full reservation credits after ten days or partial credits starting at day one of the *force majeure* service interruption. North Baja's proposal took the pipeline-favorable aspects of both policies and proposed partial credits beginning only after a service interruption of ten days. As this proposal conformed with neither previously-approved approach to sharing the risk of *force majeure* events, nor the policies underlying the two approved approaches, the Commission directed North Baja either to: (1) conform its proposal to the existing policies; or (2) explain why North Baja's proposal would satisfy the sharing of risk requirements pronounced in Opinion No. 406. *Id*. at P 15, JA 58.

On December 13, 2004, North Baja submitted revised tariff sheets providing a full reservation charge credit for non-*force majeure* interruptions, subject to North Baja's contention that service interruptions for planned maintenance should be considered *force majeure* events. R. 7 at 3, JA 80. North Baja left the proposed *force majeure* credit provision unchanged, however, arguing that it was consistent with the Commission's risk-sharing principles because it "combined features of previously-approved partial crediting mechanisms." *Id*. at 4, JA 81.

Also on December 13, 2004, North Baja filed a Request for Clarification and Rehearing of the Tariff Order. R. 8, JA 60. North Baja argued that the Commission erred in requiring it to provide full reservation charge credits for scheduled maintenance without considering whether, on North Baja's fully-subscribed pipeline, certain planned maintenance and resulting service interruptions are unavoidable and therefore should be treated as *force majeure* events. *Id*. at 7-11, JA 66-70. North Baja also asked the Commission to clarify whether the *Texas Eastern* and *Tennessee* partial credits for *force majeure* interruptions in service were the only credit mechanisms permitted. *Id*. at 11-12, JA 70-71. If the Commission found the alternatives limited to those two approaches, North Baja requested rehearing. *Id*. at 12-16, JA 71-75.

B. The Rehearing Order

1. The *Force Majeure* Reservation Charge Credit

North Baja Pipeline, LLC, 111 FERC ¶ 61,101 (2005) ("Rehearing Order") found that pipelines may adopt different approaches to reservation charge crediting for *force majeure* service interruptions as long as the crediting mechanism is "a reasonable implementation of the risk sharing principle." Rehearing Order at P 9 (citing Opinion Nos. 406 and 406-A), JA 103. North Baja contended it met this risk sharing requirement by providing a partial credit after an initial ten-day grace period. *Id*. at P 10, JA 103. The Commission found that North Baja's proposal inequitably placed more risk on the shipper, because shippers received a partial credit only after ten days, thus allowing North Baja to retain the entire reservation charge through the first ten days following a *force majeure* event. *Id*.

North Baja also argued that its proposal retains incentives to resolve the *force majeure* event quickly since it must partially refund reservation charges after the ten-day grace period. *Id*. at P 11, JA 104. The Commission, however, found that shifting the risk to the pipeline after ten days provides additional incentive to the pipeline to regain control of its system as soon as possible, and assures customers that they will not bear the risk of an extended *force majeure* interruption. *Id*. at P 12, JA 104 (citing Opinion Nos. 406 and 406-A).

North Baja also requested clarification of whether *Texas Eastern* and *Tennessee* are the only permissible partial credit approaches for *force majeure* interruptions, or whether the Commission would consider other approaches. *Id*. at P 20, JA 105. While Commission precedent had established two concurrent policies which allow either full reservation credits after ten days or partial credits starting at day one of a *force majeure* service interruption, *id*. (citing *El Paso*, 104 FERC ¶

61,045 (partial reservation charge credits from day one); *Natural Gas*, 106 FERC ¶ 61,310 (full reservation charge credits once the ten-day period ends)), the Commission has not found that these are the only two permissible partial credit approaches. *Id*. Rather, the Commission is open to alternative approaches if fully justified and supported, which is why the Tariff Order allowed North Baja either to modify its proposal to conform to one of the two established policies, or to provide further justification and support of its proposal. *Id*.

2. Planned Maintenance Service Interruptions

North Baja argued that service interruptions for planned maintenance should qualify as *force majeure* events because the foundation of the Commission's policy regarding reservation charge credits has always been control – when the pipeline is not at fault for the interruption and has not mismanaged its pipeline, the Commission has required only partial credits. *Id*. at P 15, JA 104. North Baja contended that certain planned maintenance is unavoidable and cannot be scheduled so as to avoid service interruptions. *Id*. According to North Baja, it has neither a history of operational problems resulting in severe curtailments nor capacity set aside for system maintenance as in *El Paso*, so that precedent on planned maintenance service interruptions is not applicable to North Baja. *Id*. at P 16, JA 104. North Baja urged the Commission to consider the specific circumstances on the pipeline and the extent of control the pipeline has in preventing an interruption in service during planned maintenance. [3]

The Commission rejected North Baja's request for rehearing. *Id*. at P 17, JA 104. Although the pipeline in *El Paso* may have had a history of operational problems resulting in curtailments, *see El Paso*, 105 FERC ¶ 61,262, the Commission has consistently held, at times under circumstances without such a history of operational problems, that interruptions from planned or scheduled maintenance are non-*force majeure* events that require the pipeline to provide full credits. *Id*. (citing *Natural Gas*, 108 FERC ¶ 61,170 at P 7 (2004); *Florida Gas*, 107 FERC ¶ 61,074, at P 27-28 (stating that events such as planned outages "could be read as within its [the pipeline's] control" and disagreeing with the pipeline that "non-discretionary but planned events are appropriately included in its definition of *force majeure*"); *Alliance Pipeline, L.P.*, 84 FERC ¶ 61,239 at p. 62,214 (1998)).

Furthermore, the Commission did not agree that planned maintenance is "uncontrollable". *Id*. at P 18, JA 104. While certain planned maintenance may be necessary and unavoidable to preserve the safety and integrity of the pipeline

[3] North Baja admitted that when a pipeline with unsubscribed capacity curtails service during planned maintenance and such curtailment could have been avoided through better planning, full reservation charge credits may be appropriate. *Id*. n. 11.

facilities, the pipeline has control over how and when it performs such maintenance, unlike acts of God in typical *force majeure* situations. *Id*. Given this control, the pipeline should provide full credits to shippers for all such scheduled gas not delivered. *Id*. Furthermore, since such maintenance is planned, the pipeline should have provided for such maintenance interruptions in its rates. *Id*. Thus, North Baja's lack of a history of operational problems resulting in curtailments should not exempt it from the Commission's *force majeure* policy. *Id*.

Also, although control is an important principle, it is not the Commission's only consideration in such circumstances. *Id*. at P 19, JA 105. The Commission also has an important goal of providing the pipeline, the entity in the best position to cure the non-*force majeure* interruption, in this case planned maintenance, with an incentive to resolve the interruption as quickly as possible. *Id*.

SUMMARY OF ARGUMENT

In the challenged orders, the Commission determined that North Baja's proposed partial reservation charge credits for *force majeure* events, commencing ten days after service interruption, inequitably placed more risk of *force majeure* events on shippers than the pipeline when, under Commission policy, *force majeure* events are "no-fault" events where the risk should be equitably shared. The Commission also determined that service interruptions due to planned maintenance were not *force majeure* events, and that full reservation charge credits were not required, because the pipeline has an obligation to operate its system in a manner that will allow it to provide contracted-for firm service, and it would be inequitable to require shippers to pay for planned service outages.

North Baja contends that the Commission rejected North Baja's *force majeure* reservation charge credit mechanism (partial credits after ten days), based solely on North Baja's failure to duplicate one of two previously-approved credit mechanisms (partial credits from day one or full credits after ten days), when the Commission had promised to consider other alternatives. However, the Commission reasonably rejected North Baja's mechanism as contrary to the policy of risk sharing between pipeline and shippers in *force majeure* situations because -- unlike either of the previously-approved mechanisms -- North Baja's proposal inequitably placed more risk of *force majeure* service interruptions on the shippers than the pipeline. North Baja fails to even acknowledge this express finding of inequity, which provides a plainly reasonable basis upon which to reject its credit proposal.

North Baja does not dispute the general proposition that non-*force majeure* service interruptions should be subject to full reservation charge credits. Nevertheless, North Baja contends that operational circumstances on its pipeline justify treating service outages for planned maintenance as *force majeure* events because certain unavoidable maintenance cannot be scheduled to avoid service interruptions.

The Commission reasonably rejected this argument as inconsistent with the pipeline's obligation to operate its system in manner that will permit it to provide agreed-upon service. The Commission found that it would be inequitable to require shippers to pay for the pipeline's planned service outages when that service is not provided. Further, the pipeline has control over where and when it performs required maintenance, unlike the acts of God typical of *force majeure* events. Full reservation credits also enhance the pipeline's incentive to minimize such service interruptions.

ARGUMENT

I. STANDARD OF REVIEW

The Court must uphold FERC's orders unless they are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." *Transcontinental Gas Pipe Line Corp. v. FERC*, 54 F.3d 893, 898 (D.C. Cir. 1995). Judicial scrutiny under the Natural Gas Act is limited to assuring that the Commission's decisionmaking is reasoned, principled, and based upon the record. *See, e.g.*, *Pennsylvania Office of Consumer Advocate v. FERC*, 131 F.3d 182, 185 (D.C. Cir. 1997). The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. Natural Gas Act § 19(b), 15 U.S.C. § 717r(b).

In this case, North Baja challenges two ratemaking policy determinations by the Commission allocating risk of service interruptions on equitable grounds between the pipeline and shippers. As this Court has recognized, the Court's review of Commission policy in this context is 'highly deferential' because 'the breadth of agency discretion is, if anything, at [its] zenith when the action relates primarily. . . to the fashioning of policies, remedies and sanctions.'" *Tennessee Gas*, 400 F.3d at 25 (quoting *Columbia Gas Transmission Corp. v. FERC*, 750 F.2d 105, 109 (D.C. Cir. 1984)). In *Tennessee*, the challenged Commission orders rejected the pipeline's attempt to collect full reservation charges from suspended shippers, on the ground that it was inequitable to charge suspended shippers for transportation service they were not receiving. The Court deferred to the Commission's policy determination, finding that the fact that the pipeline favored a different balancing of risk was no basis on which to conclude that the Commission policy was undeserving of deference. *Id*. at 27 (noting that the Court "properly defers to policy determinations invoking the Commission's expertise in evaluating complex market conditions.").

Similarly, here, the Commission's equitable determinations regarding the proper allocation of risk of loss between pipeline and shipper of service interruptions due to *force majeure* events or planned maintenance are deserving of deference, and North Baja's contrary views of the proper risk allocation should be rejected.

II. NORTH BAJA'S CHALLENGES TO THE COMMISSION'S EQUITABLE DETERMINATIONS ALLOCATING RISK ARE WITHOUT MERIT.

A. The Commission Properly Rejected North Baja's *Force Majeure* Credit Provision As Inequitably Placing More Risk of *Force Majeure* Events on Shippers.

In its brief, North Baja does not challenge, and indeed embraces, the proposition that the risk of service interruptions due to *force majeure* events is properly shared between the pipeline and the shippers. *See, e.g.*, Brief for Petitioner

("Br.") at 30. North Baja challenges only the Commission's rejection of North Baja's risk-sharing proposal. Br. at 30-37. However, North Baja does not – and cannot – demonstrate any basis upon which the Commission's determination was arbitrary and capricious and not entitled to this Court's deference.

Prior to the challenged orders, the Commission had approved two alternative mechanisms for sharing the risk of *force majeure* service interruptions between the pipeline and shippers: (1) providing full reservation charge credits to shippers after ten days of *force majeure* service interruptions; or (2) providing partial reservation charge credits to shippers from day one of a *force majeure* service interruption. Tariff Order at P 14, JA 58. In its tariff filing, North Baja proposed a "hybrid" of these two mechanisms (adopting only the pipeline-favorable portions), providing partial credit to shippers commencing only after ten days of the *force majeure* service interruption. *Id*. The Commission found this risk-sharing proposal inconsistent with current Commission policy and, as a result, required North Baja to modify the credit mechanism to conform to Commission precedent regarding full and partial credits, or, alternatively, to provide justification and support for its risk sharing mechanism. *Id*. at P 15.

North Baja argued that its proposal was justified because it "combine[d] features of previously-approved partial crediting mechanisms." R. 7 at 4, JA 81.

"Like the *Texas Eastern* approach, North Baja proposes a ten-day grace period in which no reservation charge would be provided." *Id*. at 5, JA 82. After ten days, however, North Baja did not adopt the full reservation credit of *Texas Eastern*, but instead switched to the partial reservation credit in *Tennessee* (which in *Tennessee* was provided from day one of the interruption). *Id*. at 6, JA 83. North Baja argued that "[i]n this way, the pipeline is sharing the risk of the *force majeure* interruption without being required to forego all of its reservation charges." *Id*.

The Rehearing Order rejected North Baja's proposed "hybrid" approach -- adopting only the pipeline-favorable portion of previously-approved risk-sharing mechanisms -- on the ground that it overall placed *more* of the risk of *force majeure* events on the shippers, rather than equitably sharing the risk between the shippers and the pipeline. Rehearing Order at P 10, JA 103. While North Baja's proposal would provide shippers a partial credit, this partial credit would only apply after a ten-day grace period, thus allowing North Baja to retain the full reservation charge through the first ten days following a *force majeure* event. *Id*. Under North Baja's proposal, the shipper bore the *full* risk for the first ten days, and thereafter *shared* the risk with the pipeline, a result the Commission found to be inequitable. *Id*. at P 11, JA 104.

Indeed, the Commission had previously rejected a proposal where the shipper was entitled to partial reservation charge credits (70 percent) once the ten-day period ended, and directed the pipeline to grant the shipper full reservation charge credits after the ten-day period ended. *Id*. at P 13 (citing *Natural Gas*, 106 FERC ¶ 61,310 at P 24). Accordingly, the Commission found that North Baja's *force majeure* reservation charge credit proposal was inequitable and did not satisfy the Commission's risk-sharing requirements pronounced in Opinion No. 406. *Id*. at P 14, JA 104.

Thus, contrary to North Baja's protestations, the Commission did in fact "independently assess[] the merits of [North Baja's] proposal in the context of the risk-sharing principle announced in Opinion No. 406," Br. at 31, and concluded that -- unlike the proposals in *Tennessee* and *Texas Eastern* -- North Baja's proposal failed to equitably share between pipeline and shippers the risk of *force majeure* service interruptions, as required by Commission policy. Rehearing Order at PP 10-11, JA 103-04. North Baja's claim that the Commission rejected its crediting mechanism "simply because it did not match one of the two reservation charge credit mechanisms approved in *Tennessee* or *Texas Eastern*," Br. at 32, is therefore simply false. As North Baja fails to even acknowledge this finding of inequity on brief, North Baja makes no attempt to show that its proposed crediting mechanism is in fact equitable, and therefore the Commission's conclusion of inequity -- and the resulting rejection of North Baja's proposal -- should be affirmed.

Further, the express finding that North Baja's proposal was inequitable refutes North Baja's claim that the Commission would only accept the *Tennessee* and *Texas Eastern* credit mechanisms, even though the Commission professed to be open to alternatives. Br. at 34-35. The Commission has expressly stated that it was and remains fully willing to consider other equitable means of risk sharing. While Commission precedent had approved two concurrent approaches which allowed either full reservation credits after ten days or partial credits starting at day one of a *force majeure* event, Rehearing Order at P 20, JA 105, (citing *El Paso*, 104 FERC ¶ 61,045 (partial reservation charge credits from day one); *Natural Gas*, 106 FERC ¶ 61,310 (full reservation charge credits once the ten-day period ends)), the Commission did not find that these are the only two permissible partial credit approaches. *Id*. Rather, the Commission is open to alternative approaches *if fully justified and supported*, which is why the Tariff Order allowed North Baja either to modify its proposal to conform to one of the two established policies, or to provide further justification and support of its proposal. *Id*.

North Baja complains that the Commission failed to confront the argument that North Baja's *force majeure* credit mechanism provided adequate incentives for the pipeline to cure *force majeure* events. Br. at 33-34. North Baja contends that, during a service interruption, it is unable to provide interruptible service and is at risk for the portion of its fixed costs allocated to interruptible service. *Id*.

To the contrary, the Commission recognized North Baja's argument, see Rehearing Order n. 6, JA 104, and likened that argument to claims made in prior cases that generalized incentives to cure service interruptions (*e.g.*, to provide reliable service in order to get and retain customers), rendered reservation charge refunds associated with *force majeure* events unnecessary. *Id*. at P 11, JA 104. The Commission determined that, notwithstanding the presence of other incentives, reservation charge credits that imposed an equitable share of the risk of the *force majeure* event on the pipeline were nevertheless required to provide pipelines sufficient incentive to cure promptly service interruptions arising from *force majeure* events. *Id*. (citing Opinion No. 406, 76 FERC ¶ 61,022 at 61,088) (rejecting pipeline's argument that no reservation charge credit is required where it already has incentives to restore service). Shifting the risk of a *force majeure* service interruption to the pipeline after ten days provides an incentive to the pipeline to regain control of its system as soon as possible, and assures customers that they will not bear the risk of an extended *force majeure* interruption. *Id*. at P 12, JA 104 (citing Opinion Nos. 406 and 406-A).

B. The Commission Properly Rejected Treating Service Interruptions Due to Planned Maintenance as *Force Majeure* Events.

In the challenged orders, the Commission required North Baja to provide full reservation charge credits whenever there is a service interruption due to scheduled maintenance, consistent with Commission policy set forth in *Natural Gas*, 106 FERC ¶ 61,310. Tariff Order at P 11 & n. 3, JA 57; Rehearing Order at PP 17-19, JA 104-05. North Baja contends it should be exempt from this general policy. Br. at 21-30. It claims that service interruptions due to planned maintenance on its pipeline should be treated as *force majeure* events, because of operational circumstances on its pipeline, *i.e.* it is fully subscribed and purportedly has virtually no ability to avoid some service interruption for maintenance activities. *Id.*

The Commission reasonably found no cause here to depart from its *Natural Gas* policy regarding reservation charge credits for planned maintenance. Rehearing Order at P 17, JA 104. *See El Paso*, 105 FERC ¶ 61,262 at P 15 (cited Rehearing Order at P 17 n. 12, JA 104); *El Paso*, 108 FERC ¶ 61,056 at PP 5, 9. The Commission has, in fact, previously applied this policy to pipelines that argued, like North Baja, that the operational circumstances of their pipelines called for planned maintenance to be given *force majeure* effect. *See* Rehearing Order at P 17 and n. 13, JA 104; *Florida Gas*, 107 FERC 61,074 at P 20 (pipeline argued its diverse demand profile, large geographical market area, and uniformly high capacity usage throughout the year made it difficult for the pipeline to minimize disruptions in service for planned system maintenance); *El Paso*, 105 FERC ¶ 61,262 at PP 6-7 (pipeline argued it had limited flexibility to schedule maintenance in a manner that would limit service interruptions because parts of its system operate at a very high annual load factor, and it also has a bi-modal peak with both a winter heating market demand and a summer electric demand).

Rather, the Commission's *Natural Gas* policy, followed here, is based upon the generally-applicable obligation of pipelines to operate their systems in a manner designed to meet their contractual obligations, which renders it inequitable to require shippers to pay for service interruptions due to a pipeline's failure to meet that obligation:

> Because a pipeline is responsible for operating its system so that it can meet its contractual obligations, if the pipeline must curtail firm service due to an event within its control, or management, the Commission finds it inequitable for the pipeline's customers to bear the risk associated with such mismanagement. Thus, the Commission generally requires a pipeline to provide reservation charge credits to compensate its customers for the interruption in service. The reservation charge credits also provide an incentive for the pipeline to manage its system so that it can avoid interruptions that it could have avoided had it better managed its system.

Natural Gas Pipeline Co., 102 FERC ¶ 61,326 at P 19 (2003), *on reh'g*, 106 FERC ¶ 61,310, *on reh'g*, 108 FERC ¶ 61,170 (2004) (quoting Opinion No. 406, 76 FERC ¶ 61,022 at 61,086). *See also Tennessee Gas Pipeline Co*., 71 FERC ¶ 61,399 at 62,580 (1995) ("Pipelines should be able to provide the service that they have contracted to perform. Thus, in general it is reasonable for pipelines to provide demand charge credits when they interrupt the service they have contracted to provide to customers."); *Florida Gas Transmission Co.*, 105 FERC ¶ 61,171 at P 29 (2004) ("[T]he Commission has held that scheduled maintenance is a necessary non-*force majeure* event within the control of the pipeline, and that because a pipeline is responsible for operating its system so that it can meet its contractual obligations, full reservation charge crediting is an incentive to perform maintenance with minimal service disruptions.") *See also Tennessee Gas*, 400 F.3d at 25 (affirming policy that pipeline may not charge a full reservation charge during shipper's suspension, because during suspension the pipeline is failing to perform its obligation under the contract and therefore should not be permitted to charge the shipper as through the shipper were receiving service.)

In accordance with this rationale, *Natural Gas* required the pipeline to provide full reservation credits for scheduled maintenance and repairs, which are considered to be within the control of the pipeline. *Natural Gas*, 106 FERC ¶

61,310 at P 15 (citing *El Paso*, 105 FERC ¶ 61,262). Here, the Commission simply followed its established policy. *See* Tariff Order at P 11, JA 57; Rehearing Order at P 17 and n.13, JA 104.

Further, the Commission rejected North Baja's argument that service interruptions due to its planned maintenance were outside its control, and therefore properly considered *force majeure* events. Rehearing Order at P 18, JA 104. While certain planned maintenance is necessary and unavoidable, the pipeline nevertheless retains control over how and when such maintenance is performed. *Id*. [4]

North Baja's ability to exercise a degree of control over maintenance differentiates maintenance activities from the "acts of God in typical *force majeure* situations." *Id*. The basic purpose of a *force majeure* clause is to relieve a party from its contractual duties when its performance has been prevented by a force beyond its control or when the contract's purpose has been frustrated. *See, e.g., Phillips Puerto Rico Core, Inc. v. Tradax Petroleum Ltd.*, 782 F.2d 314, 319 (2nd Cir. 1985). *See also Nissho-Iwai Co., Ltd. v. Occidental Crude Sales, Inc.*, 729

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[4] For example, given that pipelines experience periods of peak and off-peak demand, the timing of maintenance can greatly influence the amount of service interruption that results. *See, e.g., El Paso*, 105 FERC ¶ 61,262 at P 11 (shipper charged that pipeline repeatedly performed routine maintenance in peak summer months despite requests that maintenance be performed in the shoulder periods).

F.2d 1530, 1540 (5th Cir. 1984) ("*Force majeure*" has traditionally meant an event which is beyond the control of the contractor."); *Gulf Oil Corp. v. FERC*, 706 F.2d 444, 452 (3rd Cir. 1983) ("[I]t is well settled that a *force majeure* clause in a non-warranty contract defines the area of unforeseeable events that might excuse performance within the contract period.") *Gulf Oil* found maintenance repairs improperly included in a contract definition of *force majeure* events, because such repairs lacked the element of uncertainty that defines unforeseeability. *Gulf Oil*, 706 F.2d at 453-54.

The Commission does, however, permit pipelines to design their non-*force majeure* reservation charge credit proposals in a manner that will allow them to comply with Commission policy and still meet their non-discretionary obligations, such as by approving delivery thresholds over which a pipeline is not obligated to provide a reservation charge credit. *Florida Gas*, 107 FERC ¶ 61,074 at P 32 (citing *Natural Gas*, 106 FERC ¶ 61,310 at P 17, approving a 98 percent delivery threshold). Here, as in *Natural Gas*, North Baja was permitted a 98 percent delivery threshold in its non-*force majeure* reservation charge credit provision. *See* R. 7, Appendix A, First Revised Tariff Sheet No. 116.a, section 7.7, JA 89.

Further, service interruptions due to planned maintenance can be taken into account in the pipeline's rate design. Rehearing Order at P 18, JA 104. *See, e.g.*, 18 C.F.R. § 154.312(a) (operation and maintenance expenses are included in the overall gas utility cost of service). North Baja asserts that the Commission "has cited to no authority in which the Commission has approved a pipeline's proposal to adjust its throughput or billing determinants to reflect service interruptions due to required maintenance." Br. at 28. As the Commission made this point only in the Rehearing Order, the Commission was never asked to provide authority for this proposition.

In any event, such authority does exist. *See, e.g.*, *PG&E Gas Transmission, Northwest Corp.*, 99 FERC ¶ 61,366 at P 21 (2002) (finding pipeline's use of a 95% load factor to design the usage charge reasonable because it takes into account, *inter alia*, "downtime for maintenance and outage.") The Commission has, in fact, rejected arguments that a pipeline's usage rate should be based on a 100 percent throughput level, finding that a "100 percent thoughput level is very unusual and seldom obtained" because, *inter alia*, "a pipeline should be provided a reasonable allowance for downtime and maintenance." *Mojave Pipeline Co.*, 70 FERC ¶ 61,296 at 61,861 (1995), *vacated on other grounds,* 75 FERC ¶ 61,108 (1996) (quoting *Iroquois Gas Transmission System, L.P.*, 53 FERC ¶ 61,194 at 61,710 (1990)).[5]

Thus, the Commission reasonably concluded that requiring firm shippers to pay reservation charges for firm service they do not receive due to maintenance outages is inequitable under its *Natural Gas* policy. *See* Tariff Order at P 11 & n. 3, JA 57; Rehearing Order at PP 17-19, JA 104-05. Therefore, North Baja's proposal to treat planned maintenance as a *force majeure* event cannot constitute a just and reasonable means of recovering the cost of maintenance interruptions. Br. at 29. *See Tennessee Gas*, 400 F.3d at 25 (finding it unjust and unreasonable for pipeline to charge a full reservation charge when it was not providing service). Rather, as discussed, Commission policy reasonably permits the decreased throughput from maintenance downtime to be factored into the usage charges paid by shippers actually using the system.

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[5] When a straight fixed-variable rate is used, the Commission requires the reservation charge to be based on a 100 percent load factor, because the pipeline can enter into contracts for 100 percent of capacity, and thereby collect 100 percent of its fixed costs, regardless of actual throughput. *Mojave*, 70 FERC ¶ 61,296 at 61,862. Thus, if a reduction in throughput for the reservation charge were permitted, the pipeline could overcollect its fixed costs if 100 percent of the pipeline's firm capacity was under contract. *Id*.

Last, although control is an important principle, it is not the Commission's only consideration in these circumstances. Rehearing Order at P 19, JA 105. The Commission also has an important goal of providing the pipeline, the entity in the best position to cure the non-*force majeure* interruption, in this case planning and conducting maintenance in a manner that minimizes service interruptions, with an incentive to resolve the interruption as quickly as possible. *Id*. The Commission reasonably found that North Baja's proposal to treat scheduled maintenance as a *force majeure* event would undermine this goal. *Id*.

CONCLUSION

For the reasons stated, the Commission's orders should be affirmed in all respects.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

In accordance with Fed. R. App. P. 32(a)(7)(C)(i), I certify that the Brief of Respondent Federal Energy Regulatory Commission contains 6825 words, not including the tables of contents and authorities, the glossary, the certificates of counsel and the addendum.

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