

UNFINISHED BUSINESS: FERC’S EVOLVING STANDARD FOR CAPACITY RIGHTS ON OIL PIPELINES

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Synopsis: Over the past six years, the FERC has gradually fashioned a policy addressing a key issue in regulating oil pipelines: how to apply the 124-year old Interstate Commerce Act and its “common carrier” obligations, in a modern commercial context in which both pipelines and shippers need certainty of access for future pipeline capacity. In a series of orders, the Commission has tried to balance the clear need for assured use of capacity for parties making long-term payment commitments against the statutory admonition that pipelines are common carriers that must provide transportation upon reasonable request. The current policy still presents several significant problems for pipelines and shippers, including apparent limits on prices, scope of contract capacity and its application to new capacity. This article briefly reviews the statutory and case law scope of common carriage under the Interstate Commerce Act and concerning relevant industries, as well as the development of the FERC’s current approach, and suggests that the FERC has ample legal and policy basis for further refinement to the policy.

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I. INTRODUCTION

The Federal Energy Regulatory Commission (FERC or Commission) regulates three complex and distinct systems¹ of liquids pipelines (transporting crude petroleum,² refined petroleum products,³ and natural gas liquids (NGLs)⁴ spanning more than 200,000 miles under the Interstate Commerce Act (ICA).⁵ The physical scope of the interstate oil pipeline network is broadly comparable to the interstate natural gas network. Despite ongoing initiatives to diversify the nation’s energy use away from fossil fuels, the need for investment in the oil and liquids pipeline infrastructure in North America is expected to increase significantly in the next decade.⁶

1. In contrast to the interstate natural gas network, which broadly speaking transports a fungible product (methane) in a vast, potentially integrated network, each type of liquids pipeline exists in a very different business and market context. Even national pipeline maps and atlases are typically designed to show only one of the three types: crude, refined products, and NGL.

2. “Crude petroleum” or “crude oil” broadly includes both petroleum directly extracted as a liquid from underground geological formations and “synthetic” crude petroleum created by the processing of solid mineral resources such as oil sands.

3. “Refined petroleum products” encompasses a wide range of products derived by refineries from crude petroleum, but the principal refined petroleum products transported via pipeline are gasoline, jet fuel, and home heating oil.

4. “NGLs” include a range of hydrocarbons heavier than natural gas (methane), including propane, ethane, normal butane, iso-butane, pentane, and other heavy hydrocarbons. NGLs are produced both from the refining of crude petroleum and from processing natural gas, which emerges from natural gas wells mixed with NGLs that are extracted in gas processing plants.

5. Interstate Commerce Act (ICA), 49 U.S.C. § 1 (1988). The ICA as applied to oil pipelines has a complicated history. Concurrent with the enactment of the ICA in 1887, the Interstate Commerce Commission (ICC) was created to regulate the interstate common carriers subject to the ICA, which were primarily railroads. The ICA was amended in 1906 by the Hepburn Act to include regulation of common carrier oil pipelines. The ICC regulated oil pipelines under the ICA between 1906 and 1977, when jurisdiction over oil pipelines was transferred to the newly-created Federal Energy Regulatory Commission (FERC) by the 1977 DOE Act. *See generally*, 49 U.S.C. § 60502 (2006). In a curious twist of statutory fate, the ICA was heavily amended by reform legislation in 1976, 1980 and 1995, when the ICC itself was terminated and replaced by a successor agency, the Surface Transportation Board (STB). In contrast, the FERC’s regulation of oil pipelines remains subject to the ICA as it existed in 1977. The FERC’s website on statutes for the oil pipeline industry provides a PDF of the ICA scanned from a paper copy at <http://www.ferc.gov/legal/maj-ord-reg/ica.pdf>, because that version of the ICA is no longer available on the federal government’s online statute resources. *See generally* Department of Energy Organization Act, 42 U.S.C. § 7101 (1977).

6. *See generally* KEVIN R. PETAK, DAVID FRITSCH & E. HARRY VIDAS, NORTH AMERICAN MIDSTREAM INFRASTRUCTURE THROUGH 2035: A SECURE ENERGY FUTURE 96-100 (2011), available at <http://www.ingaa.org/File.aspx?id=14900> (projecting an increase in oil and NGL pipeline investment of more than \$36 billion between 2011 and 2020 and more than \$60 billion between 2011 and 2035) (prepared for the

Yet, the FERC has a surprisingly limited role in regulating oil and liquids pipelines, reflected in the tiny percentage of its budget allocated to oil pipeline regulation.⁷ The FERC does not have any regulatory authority regarding the liquids transported by pipeline.⁸ The FERC has never had any role in regulating the production or refining of petroleum.⁹ The FERC has no authority over an interstate oil or liquids pipeline's decision to build a new pipeline, to expand a pipeline, or to abandon service,¹⁰ nor even to interconnect with another pipeline.¹¹ The FERC has no jurisdiction over the decision by a pipeline to reverse the direction of its service,¹² to discontinue offering transportation to particular commodities,¹³ or to lease all or a part of its pipeline system to another pipeline.¹⁴ The limited scope of the FERC's regulation of oil pipelines stands in stark contrast to its pervasive role in pipeline infrastructure under the Natural Gas Act (NGA),¹⁵ which even prohibits a would-be pipeline sponsor from putting a shovel in the ground until a certificate of public convenience and necessity is issued.¹⁶ The developer of a massive new multi-state oil pipeline could (in theory) choose not to inform the FERC of its plan to construct and operate a pipeline until it files an initial tariff thirty to sixty days prior to commencing service. Under the NGA, the FERC recently denied a request by the owners of a natural gas pipeline to abandon service because of the poor economics of continuing service, telling the pipeline to file a rate case or sell the line to shippers but not to cease service.¹⁷ In contrast, an oil or liquids pipeline could simply file a tariff supplement, notifying the FERC that it would be canceling service.¹⁸

The FERC nonetheless plays a vital role in regulating oil and liquids pipelines. The FERC has exclusive jurisdiction to determine whether pipelines' rates and terms of service are just, reasonable, and not unduly discriminatory.¹⁹ A pipeline may be free to build or expand a pipeline without regard to the FERC's views, but ultimately the FERC has the authority to judge and, if

INGAA Foundation). See also *Rocky Mountain Pipeline Sys. LLC*, 126 F.E.R.C. ¶ 61,301 at P 9 (2009) [hereinafter *Rocky Mountain*].

7. See generally FERC, FISCAL YEAR 2012 CONGRESSIONAL PERFORMANCE BUDGET REQUEST (2012), available at <http://www.ferc.gov/about/strat-docs/FY12-budg.pdf> (budgeting approximately 2.5% of its budget for oil pipeline related matters).

8. See generally *Students Corner: Energy We Regulate*, FERC, <http://www.ferc.gov/students/energywe-regulate/oil.htm> (last visited Sept. 21, 2011).

9. *Id.*

10. *Farmers Union Cent. Exch. v. FERC*, 734 F.2d 1486, 1509 n.51 (D.C. Cir. 1984); *Williams Pipe Line Co.*, 21 F.E.R.C. ¶ 61,260, at p. 61,690 n.217 (1982).

11. *Plantation Pipe Line Co. v. Colonial Pipeline Co.*, 104 F.E.R.C. ¶ 61,271 (2003).

12. *Rocky Mountain*, *supra* note 6, at P 14.

13. *Mid-America Pipeline Co., LLC*, 131 F.E.R.C. ¶ 61,012 at P 11 (2010).

14. *Western Ref. Sw., Inc. v. FERC*, 636 F.3d 719, 724 (5th Cir. 2011).

15. Natural Gas Act, 15 U.S.C. § 717 (Supp. 4 1938).

16. 15 U.S.C. § 717f(c) (1988); see generally *Independence Pipeline Co.*, 91 F.E.R.C. ¶ 61,102, at p. 61,347 (2000) (before the construction and operation of a proposed interstate pipeline can take place, the applicant must obtain a certificate of public convenience and necessity from the FERC).

17. *Northern Natural Gas Co.*, 135 F.E.R.C. ¶ 61,048 at P 43 (2011).

18. *Rocky Mountain*, *supra* note 6, at PP 9-19.

19. Conservation of Power and Water Resources, 18 C.F.R. § 342.4 (2011).

required, to prescribe the rates and terms of service of the pipeline.²⁰ Whether a pipeline's rates will provide adequate revenues to investors, and whether its rules and regulations will allow it to attract shippers, are critical threshold issues for pipeline operators. Hence, the FERC's rate and service policies loom large over pipelines' decisions whether or not to build or expand pipelines.

The FERC has faced and addressed several major potential problems relating to certainty for new or expanded pipelines,²¹ and at present, the most contentious rate and service disputes are not issues raising significant uncertainties for the industry, with one major exception: what are the appropriate limits under the ICA to allowing oil and liquids pipelines to grant contract shippers priority (or "firm") capacity rights when requests for service exceed pipeline capacity? The FERC has evolved and clarified its policy since 2006, but that policy appears to be a work in progress. The FERC's orders reflect a central tension between the statutory obligation to enforce pipelines' status as "common carriers," open to current and future non-contract shippers, and the statutory (and marketplace) basis for pipelines to establish not unduly discriminatory contract rights for some shippers based on contract.

The Commission's current policy has developed quickly through a series of declaratory orders as to individual pipeline projects, but the broad contours seem clear. The FERC has thus far allowed pipelines only to apply contract priority rights to new capacity, has not allowed the displacement of existing shippers, appears to have held that priority shippers signing long-term contracts must pay higher rates than uncommitted shippers, and has mandated that pipelines seeking priority contract rights must plan to offer substantial open capacity for new and existing non-contract shippers.²² Yet these constraints run counter to the needs expressed by shippers in the marketplace and may yet hinder the speed and scope of new pipeline projects. The FERC may be asked to further refine and develop its priority capacity policy, as increased oil pipeline capacity is needed for burgeoning new liquids supplies arising from oil sands developments in Canada, from the Bakken and other oil shale plays in the U.S., and from NGL supplies from shale gas development.

This article addresses the origins of the common carrier rules, the Commission's development of its current rules, and the scope of FERC's flexibility in resolving the remaining issues by further refining its policy.

20. In addition to these central responsibilities, the FERC has other regulatory roles, and may determine whether an oil pipeline has complied with its tariff and other obligations under the ICA. Oil pipelines are subject to annual, quarterly, and other reporting and filing obligations, as well as more specific prohibitions under the ICA.

21. See also Christopher J. Barr, *Growing Pains: FERC's Responses to Challenges to the Development of Oil Pipeline Infrastructure*, 28 ENERGY L.J. 43, 43-69 (2007) (four years ago, the author published an article addressing these issues in overview).

22. See *infra* Section IV.

II. BACKGROUND: COMMON CARRIER OBLIGATIONS AND THE RELATIONSHIP OF CONTRACT AND COMMON CARRIER SERVICE

A. Statutory Basis

The FERC's rules regarding oil pipeline capacity rights rest ultimately on the meaning and scope of the "common carrier obligation" of oil pipelines. The text of the ICA provides very little guidance on this topic. The common carrier issue arises in the context of oil pipelines because, by virtue of the ICA, they are declared to be common carriers.²³

The central "common carrier" obligation of oil pipelines is the obligation under ICA section 1(4) "of every common carrier subject to this chapter to provide . . . transportation upon reasonable request therefor."²⁴ The ICA does not elaborate upon the scope of the "duty," nor does it directly address how to address competing requests for service. Section 3(1) prohibits pipelines from granting "any undue or unreasonable preference or advantage" as between persons, geographic areas, or types of transportation, a concept that has been applied in the context of granting requests for service as well.²⁵ Additionally, the ICA imposes less well-defined, common law duties upon the common carriers.²⁶ The FERC has quoted the Supreme Court's evocative, and seemingly archaic, incorporation of older common law principles that would govern a common carrier's rights and obligations "if his coach be full."²⁷ Unfortunately, the Court provided little in the way of concrete guidance under this principle: "[t]he law exacts only what is reasonable from such carriers – but, at the same time, requires that they should be equally reasonable in the treatment of their patrons."²⁸

Pre-1977 precedents construing the scope of the common carrier obligations of oil pipelines when capacity is constrained are quite limited. Traditionally, oil pipelines simply prorated nominations equally, which was more easily done during the early and mid-20th Century when oil pipelines and their shippers were

23. The 1977 Interstate Commerce Act states: "The provisions of this chapter shall apply to common carriers engaged in . . . [t]he transportation of oil . . . by pipe line." 49 U.S.C. § 1(1) (1988). That act goes on to define "common carrier" as including "all pipeline companies." 49 U.S.C. § 1(3) (emphasis added). Finally, the Supreme Court has interpreted similar language to mean that all pipelines, except those that are owned by a company that also owns the well and the refinery that are connected by such pipeline, are considered common carriers. See also *United States v. Ohio Oil Co. (The Pipe Line Cases)*, 234 U.S. 548, 559–60 (1914) (stating that the language was not intended to be a limiting provision). Therefore, it is clear that pipelines are deemed "common carriers" under the ICA and subject to regulation by the FERC. See also *Belle Fourche Pipeline Co.*, 28 F.E.R.C. ¶ 61,150, at p. 61,281 (1984) (citing *The Pipe Line Cases* in stating that oil pipeline companies are common carriers under the statute) [hereinafter *Belle Fourche*]. In contrast to pipelines subject to the ICA, oil pipelines subject to the Outer Continental Shelf Lands Act, as amended, have been treated as being contract carriers. See, e.g., *Enbridge Offshore Facilities, LLC*, 116 FERC ¶ 61,001 at P 19 (2006).

24. 49 U.S.C. § 1(4) (1988).

25. *Suncor Mktg. Inc. v. Platte Pipe Line Co.*, 132 F.E.R.C. ¶ 61,242 at PP 24, 111 (2010) [hereinafter *Platte III*]. In *Platte III*, the FERC also cited as relevant to capacity allocation ICA § 1(6), which prohibits unjust and unreasonable classifications, regulations, and practices. *Id.*

26. *Belle Fourche*, *supra* note 23, at p. 61,281 (summarizing the history of the common carrier obligation) (citing *Illinois Cent. R.R. Co. v. River & Rail Coal & Coke Co.*, 150 S.W. 641 (Ky. 1912)).

27. *Id.* (quoting *Pennsylvania R.R. Co. v. Puritan Coal Co.*, 237 U.S. 121, 133 (1915)).

28. *Id.*

generally closely integrated,²⁹ and more recently, the FERC has approved, without much analysis under the ICA, the practice of allocating capacity primarily on the basis of recent historical volume percentages among shippers.³⁰ Contract rights to capacity were not raised as a potential oil pipeline option until the end of the 20th Century, and in a footnote to a landmark NGA case, the Supreme Court observed (though purely as *dicta*) that gas pipelines fundamentally operated on the basis of contracts between pipeline and customers, in contrast to carriers under the ICA, which operated as common carriers.³¹ Even now, all natural gas customers enter into written contracts for every service with natural gas pipelines, while the relationship between oil pipelines and *most* current shippers does not usually involve any written contract,³² but instead, shipments nominated and tendered are governed by the tariff (and the ICA).

As the FERC continues to frame its policy regarding priority capacity access by contract shippers, it is therefore necessary to have a closer look at what the boundaries of “common carrier obligation” have been under the common law precedents – not just for oil pipelines, but for other common carriers as well. At common law, numerous types of common carriers existed including ferrymen, canal boat owners, stagecoaches, taxicabs, and express companies.³³ However, this analysis will focus on the manner in which, and whether, common carrier obligations for service coexisted with contract obligations with respect to rail carriers, motor carriers, and interstate water carriers, all of which operated subject to the ICA or allied legislation as well as common law common carrier principles.

B. Common Carrier Standards Under the ICC

1. Rail Carriers

A threshold difficulty in assessing the common carrier precedents for rail carriers in this context is that, unlike oil pipelines, railroads do not have quite as readily calculable “capacity” for transportation. An oil pipeline can determine fairly precisely for each type of commodity its capacity in barrels-per-day between various origins and destinations and assess nominations by shippers in light of that limit. In contrast, railroad “capacity” has historically been more difficult to determine, and “pro-rationing” has not been a concept applied to rail shippers. Rail carriers have faced (in particular markets, during particular

29. See generally GEORGE S. WOLBERT, JR., U.S. OIL PIPE LINES: AN EXAMINATION OF HOW OIL PIPE LINES OPERATE AND THE CURRENT PUBLIC POLICY ISSUES CONCERNING THEIR OWNERSHIP 173 (1979) (“[T]he empirical evidence appears to support the opening general principle that, with few exceptions, petroleum pipelines have been conceived, financed, and built by the oil companies who need their services”).

30. See, e.g., *Explorer Pipeline Co.*, 87 F.E.R.C. ¶ 61,374, at p. 62,387 n.14 (1999); *SFPP, L.P.*, 86 F.E.R.C. ¶ 61,022, at p. 61,115 (1999); *Total Petroleum, Inc. v. Citgo Prods. Pipeline*, 76 F.E.R.C. ¶ 61,164, at p. 61,947 (1996); *ConocoPhillips Transp. Ala., Inc.*, 112 F.E.R.C. ¶ 61,213 at P 28 (2005) (stating that “prorating policies based on historical volumes are an acceptable means of allocating capacity on other pipelines”).

31. *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 334 n.1 (1956).

32. Courts deem that a contract of carriage has been created by the carrier’s acceptance of a tender by the shipper, a contract defined by the tariff and pertinent law.

33. 2 ISAAC F. REDFIELD & J. KENDRICK KINNEY, *THE LAW OF RAILWAYS* 93, 26 n.b (6th ed. 1888).

periods) bottlenecks due to congestion,³⁴ although the most common manifestation of “capacity” limitations for rail carriers was shortages of railcars for particular products, often coal or grain, whose demand sometimes showed wide seasonal and yearly swings. However, the ICA has a number of specific provisions addressing both “car service” obligations of rail carriers,³⁵ including special provisions for coal cars.³⁶ Interstate Commerce Commission (ICC) decisions on “capacity” therefore usually addressed car-related issues that turned on provisions specific to railroad instrumentalities and cannot be generalized. There can be little doubt that for most of the 20th century, the ICC was generally not receptive to railroads granting special contract rights in general.³⁷ Late in the ICC’s existence, however, the policies of the ICC evolved to recognize that contracts could be reconciled with the ICA’s non-discrimination and common carrier requirements, and the ICC confirmed that railroads could enter into binding long-term contracts with shippers.³⁸ As the D.C. Circuit found in a seminal case examining the ICC’s evolution towards recognizing contracts:

A logical next step was for the Commission to recognize the economic efficiencies that accrue from private contracting. Although one normally regards contract relationships as highly individualized, contract rates can still be accommodated to the principle of nondiscrimination by requiring a carrier offering such rates to make them available to any shipper willing and able to meet the contract’s terms. If those terms result in lower costs or respond to unique competitive conditions, then shippers who agree to enter into the contract are not similarly situated with other shippers who are unwilling or unable to do so. Under these circumstances, a carrier may properly charge different rates for contract and noncontract carriage without running afoul of the prohibition on discriminatory pricing. Endorsing the logic of this position, the Interstate Commerce Commission acted to approve contract rates for the first time in 1978.³⁹

Consequently, precedents from the first ninety years of the ICC’s existence are of little assistance. However, pre-ICA common law sheds additional light on the nature of the common carrier obligation.

As very general matter, under the common law, railways were required to act as common carriers, at least when they undertook to carry goods for all those who applied.⁴⁰ When acting as common carriers, passengers, their baggage, and other freight were all considered equal in that the railway’s duties as to each were the same and the railway’s liability to each for any damage was the same.⁴¹ That is to say, the general rule was that a railway was “bound to carry for all

34. See generally Don Phillips, *Congestion in the Southwest and California May Affect Asia: U.S. Rail Snags Could Snarl Trade*, N.Y. TIMES, Mar. 30, 2004, http://www.nytimes.com/2004/03/30/business/worldbusiness/30iht-freight_ed3_.html?sep=1&sq=congestion%20in%20the%20southwest%20and%20california&st=cse.

35. ICA, 49 U.S.C. §§ 1(10), (11), (12), (13), (14), (15), (17) (current version at 49 U.S.C. §§ 10102, 11105, 11121-11123, 11126-11128, 11901, 11902, 11907 (2006)).

36. *Id.* § 1(12) (current version at 49 U.S.C. §§ 11902, 11126 (2006)).

37. See, e.g., *Contract Rates on Rugs & Carpeting from Amsterdam, N.Y. to Chicago*, 313 I.C.C. 247 (1961), *aff’d*, New York Cent. R. R. v. United States, 194 F. Supp. 947 (S.D.N.Y. 1961), *aff’d per curiam*, 368 U.S. 349 (1962).

38. See, e.g., *Change of Policy, Railroad Contract Rates*, 45 Fed. Reg. 21,719 (1980); *Iowa Power & Light Co. v. Burlington Northern, Inc.*, 647 F.2d 796 (8th Cir. 1981).

39. *Sea-Land Serv., Inc. v. ICC*, 738 F.2d 1311, 1317 (D.C. Cir. 1984).

40. 2 REDFIELD & KINNEY, *supra* note 33, at 16.

41. *Id.* at 19.

persons who apply, unless they have a reasonable excuse for the refusal to do so.”⁴²

At common law, a common carrier was not required to treat all shippers alike, but any difference in treatment among shippers must be reasonable.⁴³ “[o]nly unjust discrimination by carriers [is] condemned.”⁴⁴ In the railway context, the common law held that the railway and a shipper could enter into an agreement which favors each party,⁴⁵ and “this may consist in a guaranty of large quantities and full train loads at regular intervals” so long as the purpose of the company is to increase profits.⁴⁶ Consequently, it seems as though pre-ICA courts would not object to an agreement that reserved a portion of the railway’s capacity for a shipper so long as the agreement was beneficial to the railway’s business interests.

In 1886, the Supreme Court considered a related issue, holding that a common carrier may simultaneously act as a contract carrier, at least to some extent.⁴⁷ In the *Express Cases*, several railways agreed to reserve a portion of their capacity for exclusive use by the express company.⁴⁸ Although the principal issue presented to the Court was whether the railway *must* carry the goods of an express company,⁴⁹ the Court nonetheless implicitly accepted that a railway could contractually limit use of a portion of its capacity to carry goods and baggage.⁵⁰ The Court noted several reasons why contracts were necessary in the context of an express company using the cars of a railway: (1) speed of transit, (2) reasonable certainty of available capacity, and (3) proper accommodation of both passengers and goods.⁵¹ Finally, the Court also recognized that express companies made substantial capital investments in the expectation of being able to secure the railway facilities needed by these companies.⁵²

2. Motor Carriers

The question of how far a motor common carrier’s obligations could extend as to contract carriage did not arise extensively for motor common carriers because of the deliberate manner in which Congress established motor carrier

42. 2 ISAAC R. REDFIELD, *THE LAW OF RAILWAYS* 87 (5th ed. 1873).

43. 2 DEWITT C. MOORE, *A TREATISE ON THE LAW OF CARRIERS* 702 (2d ed. 1914).

44. *Id.* at 705.

45. 2 REDFIELD & KINNEY, *supra* note 33, at 101 n.15 (citing *Nicholson v. Great W. Ry. Co.*, 5 C.B. (N.S.) 366 (1858)).

46. *Id.*

47. *See, e.g., Memphis & Little Rock R.R. Co. v. Southern Express Co. (Express Cases)*, 117 U.S. 1, 21 (1886) (describing the practice of railways taking express companies on its road by special contract); *accord United States v. Louisville & Nashville R.R. Co.*, 221 F.2d 698, 703 (6th Cir. 1955) (stating as correct that a railway may contract as a private carrier).

48. *Express Cases*, 117 U.S. at 3–4, 8, 13.

49. Because express companies are common carriers themselves, the Court describes the question as whether a railway is a common carrier of common carriers. *Id.* at 21.

50. *Id.* at 20–21. “[N]o railroad company had taken an express company on its road for business except under some special contract, verbal or written, and generally written, in which the rights and duties of the respective parties were carefully fixed and defined.” *Id.* at 21.

51. *Id.* at 23–25.

52. *Id.* at 21.

regulation in the Motor Carrier Act of 1935 (MCA).⁵³ The MCA divided motor carriers subject to extensive regulation into two classes: common carriers⁵⁴ and contract carriers,⁵⁵ and in fact, many trucking companies applied for both types of authority.⁵⁶ In effect, the statute recognized that motor carriers would need to contract and provided for that right expressly in the statute, and its assistance in this inquiry is therefore limited.

3. Water Carriers

Carriers by water were also deemed common carriers at common law,⁵⁷ at least if the ship-owner holds himself out to serve all that apply. Under the general rules of common carriers, a ship-owner would be free to enter a private contract.⁵⁸ At English common law, in *Liver Alkali Co. v. Johnson*,⁵⁹ the court held that one who carried goods by water under a private contract was nevertheless a common carrier⁶⁰ and thus subject to the liabilities of a common carrier.⁶¹

This conclusion drew criticism,⁶² and in contrast, the United States Supreme Court reached a very different conclusion in *Liverpool & Great Western Steam Co. v. Phenix Insurance Co.*⁶³ The Court stated that it was “settled law [that] in the absence of some valid agreement to the contrary, the owner of a general ship . . . is a common carrier,”⁶⁴ contemplating that common carriers by water could enter into private contracts and be exempted as to such contracts from the general rules of common carriers. As to the simultaneous carriage under both a private contract as well as service as a common carrier, most authorities concern themselves with the proper characterization of the vessel: common carrier or private carrier,⁶⁵ but in *The City of Dunkirk*,⁶⁶ the district court was presented with a situation in which the ship-owner carried a large amount of coconut oil –

53. Motor Carrier Act of 1935, Pub. L. No. 74-255, 49 Stat. 543 (1935), *repealed by*, ICC Termination Act of 1995, Pub. L. No. 104-88, 109 Stat. 803, § 204(a) (1995).

54. *Id.* § 203(a)(14).

55. *Id.* § 203(a)(15).

56. *See, e.g.*, Marine Transp. Serv. Sea Barge Grp., Inc. v. Allen Freight Trailer Bridge, Inc., Docket Nos. MC-247354 (C) & MC-247354 (P), 1997 WL 634165 (S.T.B. Oct. 15, 1997).

57. ARMISTEAD M. DOBIE, HANDBOOK ON THE LAW OF BAILMENTS AND CARRIERS 306-307 (1914) (noting “ferryman, bargemen, lightermen, and owners of canal boats, or steamboats” as types of common carriers).

58. *United States v. Louisville & Nashville R.R. Co.*, 221 F.2d 698, 703 (6th Cir. 1955) (“[A] common carrier . . . may contract as a private carrier.”).

59. 2 THOMAS BEVIN, NEGLIGENCE IN LAW 872-74, 1019-21 (3d ed. 1908).

60. *Id.* at 872.

61. *Id.*

62. *Id.* at 1019-22. It has also been said by another that this holding is inconsistent with later decisions. JOSEPH STORY, COMMENTARIES ON THE LAW OF BAILMENTS 530 (5th ed. 1851).

63. *Liverpool & Great W. Steam Co. v. Phenix Ins. Co.*, 129 U.S. 397 (1889).

64. *Id.* at 437 (emphasis added).

65. *See generally* *The Wildenfels*, 161 F. 864, 867 (2d Cir. 1908) (stating that a vessel is a private carrier when it is “hired *exclusively* to convey the goods of one person to a particular place for an agreed compensation”) (emphasis added). This suggests recognition of the possibility that a portion of this ship could be taken by private contract with the remainder open to common carriage. In that case, the vessel would be deemed a common carrier.

66. *City of Dunkirk*, 10 F.2d 609 (S.D.N.Y. 1925).

enough to fill an entire tank on the ship – for one shipper.⁶⁷ The ship then took on goods for shipment by others.⁶⁸ The court was untroubled by this arrangement and held that the ship was nevertheless a common carrier, though simultaneously carrying goods as a contract carrier.⁶⁹ The courts did prevent carriers by water from contracting to carry as a private carriage, and although few cases directly discuss a carrier by water simultaneously carrying under a private contract and as a public carrier, that role was implicit in the courts' statements of the rules of private carriage.⁷⁰

C. Summary: The Scope of Contract and Common Carrier Service at Common Law and Under ICC Regulation

In summary, the precedents under other industries appears to be far from compelling a particular outcome or limitation on the FERC's discretion in applying a standard to govern the allocation of oversubscribed oil pipeline capacity. The common law and even statutory background of several types of common carriers suggests that there has not been a standard or "minimum" common carrier obligation with respect to accommodating common carrier shippers and contract shippers. If a pipeline's "coach be full," in the language of the pre-modern common carrier world⁷¹, obviously it cannot take on more travelers. More significantly for the FERC's current policy concerns, however, the common carrier could allocate space to certain customers that made prior contract arrangements. Indeed, the FERC has gone at least that far in framing its policy, but the question remains: what balance should the FERC strike between the two types of service and what are the ultimate constraints? That question requires an analysis of the FERC's capacity allocation decisions.

III. THE FERC'S DILEMMA: COMMON CARRIER STANDARDS CONFLICT WITH BOTH COMMERCIAL NEEDS AND KEY FERC POLICY GOALS

A. Market and Business Changes in the Liquids Pipeline Business Since the 1990s Regarding Contract Rights

For nearly 20 years after receiving jurisdiction over ICA-regulated pipelines, the FERC did not have much occasion to address the relationship between the rights of contract shippers and non-contract shippers. Indeed, the FERC had relatively little occasion to address any contract issues during that period, in which most oil pipeline litigation focused on the fundamental nature of rate regulation – what type of cost-based regulation, whether to adopt market-

67. *Id.* at 610.

68. *Id.*

69. *Id.* at 611 (finding "no ground whatever for holding, on the evidence, that the vessel was other than a common carrier. The case is very different from a case where the whole vessel is chartered"). The court suggests that there was, in fact, no separate contract between the parties. *Id.* (stating that "[t]he contract sued [up]on [was] the bill of lading, not the charter party"). However, authorities have relied on the case in stating that a vessel that carries both under charter and as a common carrier is treated as a common carrier. HENRY N. LONGLEY, COMMON CARRIAGE OF CARGO § 2.03 n.9 (1967).

70. *Liverpool & Great W. Steam Co. v. Phenix Ins. Co.*, 129 U.S. 397, 440-441 (1889).

71. *See, e.g., Pennsylvania R.R. Co. v. Puritan Coal Mining Co.*, 237 U.S. 121, 133 (1915).

based regulation, and finally implementation of the procedural and ratemaking “streamlining” called for by the Energy Policy Act of 1992.⁷²

The role of contract rights in oil pipeline services and rates rose, however, as the structure of the industry changed. From the late 1800s until the 1980s, the industry was very heavily owned and operated by vertically-integrated companies. Indeed, a high-profile legislative debate occurred in the 1960s regarding whether pipelines should be divested from their integrated oil company owners.⁷³ In the mid-1980s, oil pipelines became more widely held by independent companies not affiliated with production or refining – partly due to the industry’s early embrace of limited partnerships and partly due to changes in the strategies of the integrated oil companies, among other developments.⁷⁴ When pipeline shippers and owners were roughly the same entities, rate issues and capacity issues were unlikely to be contentious in the same way as in an unaffiliated setting.⁷⁵ Shippers commonly entered into unfiled “throughput and deficiency” agreements that committed the shippers to provide commitments of throughput, even though the pipelines never sought to provide tariff guarantees of throughput. Increasingly, the commercial setting, particularly for new pipeline projects or expansions, involved unaffiliated shippers and pipelines, vastly expensive, long-term commitments by shippers, and the need for pipelines to obtain financing support for major projects.

The first FERC order to address these developments directly was in response to a petition for a declaratory order by the proponent of a major new oil pipeline designed to bring Western Canadian crude petroleum from Alberta to the pipeline hub of Casper, Wyoming, with potential further transportation to Rocky Mountain (PADD IV) and Midwest (PADD II) refineries – Express

72. The FERC inherited from the ICC a challenge to the ICC’s longstanding “valuation” methodology, requested remand from the D.C. Circuit to reexamine its approach, and subsequently adopted a ratemaking system that was harshly criticized by the D.C. Circuit in *Farmers Union Cent. Exch. v. FERC*, 734 F.2d 1486 (D.C. Cir. 1984). Although in 1985 the FERC adopted the basic methodology in use today, Opinion No. 154-B, *Williams Pipe Line Co.*, 31 F.E.R.C. ¶ 61,377 (1985), the application of the FERC’s ratemaking methods remained contested until after its implementation of the oil pipeline provisions of the Energy Policy Act of 1992, Pub. L. No. 102-486, § 1801(a), 106 Stat. 3010 (1992); see also Order No. 561, *Revision to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, F.E.R.C. STATS. & REGS. ¶ 30,985, 58 Fed. Reg. 58,753 (1993) (to be codified at 58 C.F.R. pts. 341-345, 347, 360, 361, 375), *order on rehearing*, Order 561-A, F.E.R.C. STATS. & REGS. ¶ 31,000, 59 Fed. Reg. 40,243 (1994) (codified at 58 C.F.R. pts. 341-345, 347, 360, 361, 375), *aff’d sub nom.* Association of Oil Pipe Lines v. FERC, 83 F.3d 1424 (D.C. Cir. 1996). See also Order No. 571, *Cost-of-Service Reporting and Filing Requirements for Oil Pipelines*, F.E.R.C. STATS. & REGS. ¶ 31,006, 59 Fed. Reg. 59,137 (1994) (to be codified at 18 C.F.R. pts. 342, 346-347), *order on reh’g*, Order No. 571-A, *Cost-of-Service Reporting and Filing Requirements for Oil Pipelines*, F.E.R.C. STATS. & REGS. ¶ 31,012 (1994), 60 Fed. Reg. 356 (1995) and related orders.

73. See, e.g., WOLBERT, *supra* note 29, at 392.

74. One factor stemmed from the increasing number of acquisitions, as the FTC allowed integrated oil companies to merge but to divest certain assets, including pipeline operations or segments, to address competitive concerns. See, e.g., *In re Exxon Corp.*, 131 F.T.C. 217 (2001); *In re Chevron Corp.*, No. C-4023, 2001 WL 1022080 (F.T.C. Sept. 7, 2001).

75. Between 1906 and 1978, for example, the ICC issued only a handful of orders on rate or service disputes involving oil pipelines. See generally *Williams Bros. Pipe Line Co.*, 351 I.C.C. 102 (1975) (complaint filed alleging that the pipeline’s rates were and are unjust and unreasonable, unjustly discriminatory, and unduly and unreasonably preferential and prejudicial).

Pipeline Partnership (Express).⁷⁶ Express argued that the FERC should approve in advance the central contract arrangements that its principal shippers had agreed to in a 1995 open season, including tiered, long-term discounted rates for shippers committing to five, ten, and fifteen-year contracts, *inter alia*.⁷⁷ Overruling protests, the FERC approved the requested contract rates, finding that the contract shippers would not be “similarly situated” with shippers that had not made the financial commitment to tender or pay for long-term transportation and, hence, that sharply lower, guaranteed contract rates available only to the contract, “committed shippers,” would not be “unduly discriminatory” under the ICA.⁷⁸ The FERC made this finding, despite the fact that the initial class of contract shippers would be closed to any later shippers willing to sign contracts, because the commitment was needed by the pipeline at the outset to secure financing, and because all interested shippers had an opportunity to become contract shippers in the initial open season.⁷⁹ The FERC relied on *Sea-Land*,⁸⁰ which had found that contract rates could be lawful under the ICA:

Although one normally regards contract relationships as highly individualized, contract rates can still be accommodated to the principle of nondiscrimination by requiring a carrier offering such rates to make them available to any shipper willing and able to meet the contract’s terms. If those terms result in lower costs or respond to unique competitive conditions, then shippers who agree to enter into the contract are not similarly situated with other shippers who are unwilling or unable to do so.⁸¹

Although the *Express* proceeding did not involve a request for special prorationing rights for contract shippers, it established the mechanism for securing advance approval prior to construction as well as the FERC’s interpretation of the ICA as permitting special, closed contract *rate* rights for contract shippers as being not “similarly situated” with others for purposes of section 3(1) of the ICA.⁸² The FERC has subsequently issued numerous orders granting requests for advance approval of contract rates in connection with new pipeline capacity.⁸³

76. *Express Pipeline P’ship*, 75 F.E.R.C. ¶ 61,303 (1996) [hereinafter *Express I*], *order on reh’g*, 76 F.E.R.C. ¶ 61,245 (1996) [hereinafter *Express II*].

77. *Express II* at p. 62,254.

78. *Id.*

79. *Id.*

80. *Id.*

81. *Sea-Land Serv., Inc. v. ICC*, 738 F.2d 1311, 1317 (D.C. Cir. 1984).

82. *Express II*, *supra* note 76, at p. 62,259. Pipelines transporting petroleum from Canada across the international border to the United States are not quite in the same situation as purely domestic pipelines, for purposes of capacity rights. The governing regulatory body in Canada, the National Energy Board, has different policies regarding contract rights to capacity, so the volumes reaching the FERC-regulated pipeline at the U.S. border are already restricted to the capacity rights granted under Canadian regulatory principles. In contrast, U.S. shippers on purely domestic pipelines are less likely to make a long-term commitment to take or pay for transportation without tariff assurances that they will be able to transport those contract volumes.

83. See, e.g., *Enbridge (U.S.) Inc.*, 124 F.E.R.C. ¶ 61,199 (2008); *CCPS Transp., LLC*, 121 F.E.R.C. ¶ 61,253 (2007); *Calnev Pipe Line LLC*, 120 F.E.R.C. ¶ 61,073 (2007).

B. Evolution of FERC's Standards for Pipeline Capacity Rights

1. Prorating Rules Prior to Contract Right Issues

The development of the FERC's policy toward contract rights for *capacity* has followed a very different path. Pipeline tariffs did not traditionally provide for any capacity privileges for contract shippers. Capacity allocation was, tellingly, referred to as "prorating" – a term associated with the most common specific allocation methodology throughout the 20th century, that of "prorating" monthly shipper nominations equally based on the percentage by which nominations exceeded pipeline capacity.

In a 1984 order, the FERC found that pipelines could not simply refuse to accept any further tenders once fully subscribed, citing a 1915 Supreme Court decision, which in turn cited common carrier principles from the common law.⁸⁴ The FERC issued a number of orders assessing the lawfulness of alternatives to prorating nominations, chiefly addressing variations on the other principal method providing shippers with capacity allocations based on an historical period of past volumes, which has become increasingly common over the past two decades.⁸⁵ Even as the FERC has formed a new approach to contract rights in prorating, it has continued to address the limits to traditional prorating among non-contract shippers in a manner that has significance for its contract rationale. Despite, for example, allowing historical volumes to establish shipper rights in capacity allocation, the FERC has long required that pipelines carve out a portion of their capacity (increasingly, at least 10%) to be allocated to new shippers so that access to the pipeline would not be entirely closed to all but incumbent shippers. In 2006, the FERC found, for example, that when a pipeline changes methodologies (*e.g.*, from prorata to historic volume-based), shippers must be given notice and an opportunity to build their "shipment histories" prior to the imposition of the new standard.⁸⁶ Although the FERC has repeatedly stated that pipelines are not constrained to a single method of allocation, the limits on that freedom seem to be increasingly defined by the FERC's rulings on prorating. For example, in 2010, a pipeline proposed a new type of prorating under which the existing primarily historical volume based method would be replaced by one under which capacity would be allocated based not on individual shipment histories to each destination but rather on the collective histories of all shippers to each destination (within the capacity allocated to each destination, shippers nominations would have been prorated equally).⁸⁷ The FERC rejected the pipeline's proposal, strongly criticizing the methodology on factual and legal grounds.⁸⁸ The FERC also restated its fundamental standards for prorating proposals:

84. *Belle Fourche*, *supra* note 23, at p. 61,282 (1984) (citing *Pennsylvania R.R. Co. v. Puritan Mining Co.*, 237 U.S. 121 (1915)).

85. *See, e.g., Explorer Pipeline Co.*, 87 F.E.R.C. ¶ 61,374, at p. 62,387 n.14 (1999); *Mobile Oil Corp. v. SFPP, L.P.*, 86 F.E.R.C. ¶ 61,022, at p. 61,115 (1999); *Total Petroleum, Inc. v. Citgo Prods. Pipeline*, 76 F.E.R.C. ¶ 61,164, at p. 61,947 (1996).

86. *Platte Pipe Line Co.*, 115 F.E.R.C. ¶ 61,215 at P 30 (2006) [hereinafter *Platte I*].

87. *Platte III*, *supra* note 25.

88. *Id.* at P 65. The proposal had been opposed by nearly all shipper interests filing comments.

The purpose of a prorating procedure is to allocate constrained pipeline capacity among shippers in an equitable manner that is consistent with the common carrier obligation established in ICA section 1(4), the section 1(6) prohibition of unjust and unreasonable classifications, regulations, and practices, and the section 3(1) provision forbidding any undue or unreasonable preference or advantage. A prorating procedure may not be structured for the purpose of protecting a pipeline's competitive position, nor may it be structured to favor certain shippers or types of shippers over others if all have made "reasonable requests" for transportation on the pipeline. The Commission does not prescribe a uniform prorating methodology, requiring only that any prorating procedure must be just and reasonable and not unduly discriminatory⁸⁹ in light of factors applicable to each pipeline's provision of service to its shippers.

Although the Commission strongly faulted the pipeline's proposal on various specific factual grounds, it also made it clear that, notwithstanding the pipeline's concern that incumbent historical shippers were dominating and re-selling their allocations, the shipper's own use of their capacity was not relevant,⁹⁰ but further that the Commission sought to protect shippers' (that is, non-contract, non-committed shippers') expectations of pipeline access based on their historical use.⁹¹

The FERC continues to address refinements of the existing methodologies. Indeed, both the pro-rata and historical volume methods are subject to gamesmanship and manipulation, as illustrated in some recent orders.⁹² However, despite the broad apparent range of permitted allocations methods in apportionment, several principles stand out – principles highly relevant to the FERC's consideration of contract rights in apportionment, given that the contract issue is, in FERC's analysis, merely a type of modified prorating method for a type of shipper.

The FERC interprets its obligations regarding prorating as being set essentially by two separate statutory requirements: no undue discrimination between similarly-situated shippers⁹³ and maintenance of the common carrier obligation to accept reasonable tenders.⁹⁴ The resulting specific requirements are significant for purposes of assessing the FERC's contract shipper allocations. First, the FERC requires that all prorating methods must set aside some quantum of capacity to permit new shippers to gain access to capacity – even if

89. *Id.* at P 24 (footnotes omitted).

90. *Id.* at P 104 ("As the intervenors point out, capacity brokering is commonplace within the oil pipeline industry and is not prohibited by the ICA or Commission precedent.").

91. *Id.* at P 119.

92. For example, Enbridge Pipelines (North Dakota) LLC, which has filed a number of tariff changes to refine its prorating policies to deal with chronic pipeline capacity shortfalls for Bakken crude petroleum production, filed a proposal to allocate "new shipper" volumes by lottery when the number of new shippers would result in allocations falling below the minimum tender limit for shippers, as a result of rather dramatic over-nomination by new shippers jockeying for advantage: "To demonstrate the prorating issue on the system, there are currently 211 approved shippers, 196 of which nominated a total of 32,569,512 bpd for transportation in April 2011, while the total system capacity is only 185,000 bpd." Letter from Enbridge Pipelines (North Dakota) LLC to North Dakota Pub. Serv. Comm'n (Apr. 15, 2011) (emphasis added), available at <http://www.psc.nd.gov/database/documents/11-0123/001-010.pdf>. The FERC accepted the filing without issuing an order. Another pipeline serving the Bakken production area implemented a penalty for shippers nominating volumes, but failing to tender them, that escalated from a must-pay obligation (first time), to a penalty (second time), to being disallowed from submitting any nominations for a month (third time).

93. ICA, 49 U.S.C. § 3(1) (1988).

94. *Id.* § 1(4).

for only 10% of capacity. Second, although the FERC has approved and continues to suggest that pure pro-rata allocations can be acceptable, its orders reflect a substantial concern over what can only be termed the expectations of common carrier shippers to continue to receive capacity allocations that they have been receiving in the past, if a change is being contemplated. In *Platte I*, the FERC established an essentially new shipper right to have an opportunity to structure its nominations and tenders to “to build a history of shipments prior to the imposition of historically-based prorationing.”⁹⁵ Moreover, once historic volume-based allocations have been established, the FERC has been protective of those shippers’ continued right and expectation of moving such percentages – even for shippers with no corresponding commitment to tender volumes or to pay the pipeline.

2. Orders Shaping a New and Evolving Policy as to Priority Rights for Contract Shippers

The FERC’s policy regarding the role and scope of priority or “firm” rights for contract shippers reflects a steady evolution from an initial position that appeared to be quite hostile to today’s conditional acceptance of priority rights if certain conditions are present. The FERC’s first order addressing a proposal to grant contract shippers superior rights in prorationing was *Texaco*,⁹⁶ issued in 1995.

a. Early Rejection: *Texaco*

Late in 1995, Texaco Pipeline Inc. filed a tariff proposing to implement discounted volume incentive rates for contract shippers making a commitment to tender or pay for a minimum volume.⁹⁷ Texaco also filed tariff language stating that the contract shipper’s “Contract Throughput capacity will not be subject to proration[ing] as otherwise provided”⁹⁸ in the rules and regulations tariff and further that 60% of the capacity of the system would be available for contract shippers “on a first-come, first-served basis.”⁹⁹ Although no shipper protested the filing, the FERC took the unusual step of *sua sponte* issuing an order rejecting the tariff.¹⁰⁰ The FERC noted that contract rates were not inherently discriminatory under the ICA, if they were generally “available to all similarly situated shippers of like commodities,” but found that it was “less clear . . . whether preferences in access to services may be permitted on a contract basis.”¹⁰¹ In the subject tariff, the FERC found that Texaco had failed to provide “any explanation or justification for the [contract prorationing preferences]” and found that the net effect of the provisions would be “to take 80 percent of the

95. *Platte III*, *supra* note 25, at P 10.

96. *Texaco Pipeline Inc.*, 74 F.E.R.C. ¶ 61,071 (1996) [hereinafter *Texaco*].

97. *Id.*

98. *Id.* at p. 61,201.

99. *Id.* (emphasis omitted). Because of the tariff’s design, including protection for surplus volumes tendered by contract shippers, the FERC concluded that 80% of the capacity was effectively subject to superior protection for contract shippers.

100. *Id.* at p. 61,202.

101. *Id.* at p. 61,201.

pipeline out of common carrier service for non-contract shippers.”¹⁰² This result, the FERC found, both violated the obligation under ICA section 1(4)’s common carrier duty to provide service upon reasonable request and granted an undue preference under ICA section 3(1) by “designating a portion of the pipeline for the exclusive use of a special class of shippers [in] the form of a guarantee of service, which, in effect, denies access to other shippers.”¹⁰³ Despite this strenuous condemnation of limiting access to non-contract shippers, the FERC did, in closing, provide a suggestion of possible future flexibility, stating that the rejection was “[i]n light of Texaco’s failure to demonstrate that its proposed tariff provisions are appropriate and permitted under the ICA.”¹⁰⁴ *Texaco*, therefore, suggested that the FERC had a strong aversion to efforts to provide contract shippers with superior prorationing rights – although the FERC noted that it had not been presented with a compelling rationale for granting such rights.

Shortly and without fanfare, however, the FERC adjusted its policy in response to pipeline demonstrations that distinct service terms for contract shippers could be justified under certain circumstances.

b. Early Contract Priority Filings

In 1999, Mid-America Pipeline Company expanded its Rocky Mountain system and filed a tariff containing a volume-incentive rate applicable to shippers executing contracts for seven year terms applicable to service on the expansion capacity. The tariff provided that for 80% of the expansion capacity, the contract shippers would not be prorated.¹⁰⁵ The filing was not protested, and became effective without a FERC order. Again, no FERC order approved or accepted the proposal, but the presence of expansion capacity and other features appeared to save the filing from the fate of the contract preferences in *Texaco*.

In 2003, Explorer Pipeline Company established a bid program applicable to certain expansion capacity subject to its market-based rate authority, under which it would hold monthly auctions, with the winning bidders granted a priority in prorationing.¹⁰⁶ Explorer explained that the special rights created for the winning bidders were hedged about with protections: the program applied to its market-based rates; the capacity was expansion capacity; only 10% of available capacity would be subject to the bidding; and the bidding would only grant rights for one month at a time, to be succeeded by another bid procedure, thus preventing capacity from being locked-in to the benefit of particular

102. *Id.* In its Transmittal Letter, the pipeline noted the discounts but did not mention prorationing changes. Transmittal Letter, FERC Docket No. IS96-9-000 (Dec. 21, 1995), available at http://elibrary.ferc.gov/idmws/File_list.asp?document_id=74870.

103. *Texaco*, *supra* note 96, at p. 61,201.

104. *Id.* at 61,201-61,202.

105. The circumstances are set out in detail in the Commission’s later order. *Mid-America Pipeline Co., LLC*, 116 F.E.R.C. ¶ 61,040 at P 7 (2006) [hereinafter *MAPL*].

106. See generally Letter from Explorer Pipeline to FERC (Mar. 28, 2003), available at http://elibrary.ferc.gov/idmws/File_list.asp?document_id=4088675. The program provided that bid shippers’ capacity would be prorated only after non-bid capacity was prorated, thus effectively assuring transportation.

shippers over lengthy periods.¹⁰⁷ That filing was not protested, and it became effective without a FERC order. Although this tariff acceptance can be considered at most implicit acceptance of the lawfulness of the bid and prorating procedures, the FERC subsequently issued an order addressing Explorer's program without faulting the basic system of priority prorating. In 2005, Explorer sought to change the nature of the bidding from one in which all shippers paid the market-clearing price to one in which each shipper would pay its own winning bid price. This filing, too, was not protested, but the FERC issued an order rejecting the filing and requiring that the "market-clearing" pricing be restored, on the grounds that allowing multiple winning bidders to pay different rates for the same transportation would violate ICA section 2.¹⁰⁸ Explorer had not sought to change the prorating protection accorded the bid shippers, but when given the opportunity to address the bid program, the FERC did not fault the prorating priority for bid winners. Implicitly, the FERC appears to have accepted that the protections cited by Explorer – use of expansion capacity, use of a small percentage of overall capacity, and the monthly turnover of winning bidders – satisfied its standards for supporting granting higher priority in prorating to certain shippers based on their payment.

c. Scope for Contract Rights: *MAPL*

The Commission directly addressed the lawfulness of priorities in proration rights for contract shippers in its 2006 *MAPL* order. Mid-America submitted a tariff applying the prorating protections for the pre-existing incentive program to apply to a new set of incentive contracts, which were successors to the original seven-year agreements made in 1999. A shipper protested, alleging that the prorating priority accorded to the 1999 expansion capacity incentive contract shippers was not appropriate, in light of the fact that the special rights being accorded to 1999 system expansion capacity applied an extension of the original preferential priority to successor contract shippers. The FERC rejected the protests and found the tariff to be lawful, in light of several factors: all shippers could participate in the new incentive rate contract program; the same, unchanged incentive rates would apply; and no changed tariff provisions were presented.¹⁰⁹ The FERC also noted that the pipeline proposed to enlarge its capacity in 2007 beyond the 1999 expansion volumes, and to make all the old and new expansion capacity available under the tariff provisions granting a prorating priority, and further that the pipeline planned to retain the original 80%/20% split in allocation capacity between contract and non-contract shippers in the combined 1999 and 2007 expansion capacity. Hence, the Commission concluded that the large majority of total capacity would be offered on the traditional prorating basis and that common carrier (non-contract) shippers

107. *Id.* Rather than a straight open bid system, Explorer's program allowed all winning shippers to pay the lowest market-clearing price. Explorer's market-based rate authority was granted in *Explorer Pipeline Co.*, 87 F.E.R.C. ¶ 61,374, at p. 62, 395 (1999).

108. *Explorer Pipeline Co.*, 113 F.E.R.C. ¶ 61,249 (2005).

109. *MAPL*, *supra* note 105, at P 23.

could transport on 75% of total pipeline capacity and thus would not be denied access for failing to join the contract program.¹¹⁰

MAPL represented the FERC's first formal statement that contract shippers could be granted priority prorationing rights and, tellingly, did not reference its earlier order in *Texaco*. Here, in contrast to the *Texaco* case, (as in the *Explorer* filings), the pipeline had justified the disparate treatment for contract and non-contract shippers, and the Commission relied on certain key elements: use of expansion capacity, accessibility of the contract rights to all shippers, and the presence of substantial capacity for non-contract shippers.

d. Confirming the Rule: *Spearhead*

The FERC applied these same principles the following year in granting the petition for declaratory order of a proposed new pipeline project in *CCPS Transportation, LLC (Spearhead)*.¹¹¹ In *Spearhead*, an existing pipeline that transported crude petroleum from the Chicago area to Cushing, Oklahoma proposed to increase its capacity substantially and to commit somewhat less than half the capacity to new committed shippers paying premium rates,¹¹² rates higher than those paid by either uncommitted shippers or a preexisting class of committed shippers that had contract rights to discounted rates though not to priority capacity rights.¹¹³ Under the pre-expansion rules and regulations, the pipeline prorated capacity 90% by historical volumes, setting aside 10% for new shippers.¹¹⁴ The FERC approved the proposal to grant protection from prorationing to the new expansion shippers, who had made long-term commitments in an open season available to any interested shippers.¹¹⁵ The FERC also found that charging premium rates to the expansion shippers was justifiable under the ICA, because of their greater rights in apportionment.¹¹⁶ However, the FERC found that the original rate structure (which did not grant any firm capacity rights but did provide for a 90%/10% allocation according to historical volumes) had included "the premise that neither historical shippers nor new shippers would be denied access to the expansion capacity" in its earlier declaratory order approving the initial contract rates.¹¹⁷ The FERC then concluded that *Spearhead* must set aside "a part" of the expansion capacity for the "new shipper" category under its tariff, noting parenthetically that although it has never mandated a particular percentage for "new shippers" in prorationing cases, it had never approved less than 10%.¹¹⁸

Hence, the FERC reaffirmed its decision in *MAPL* to sanction some degree of heightened prorationing rights for contract shippers in an expansion context, provided that substantial capacity remained available for historic shippers.

110. *Id.* at P 24.

111. *CCPS Transportation, LLC*, 121 F.E.R.C. ¶ 61,253 (2007) [hereinafter *Spearhead*].

112. *Id.* at P 1.

113. *Id.* at P 6.

114. *Id.* at P 17.

115. *Id.* at P 22.

116. *Id.*

117. *Id.* at P 17. See also *Enbridge Energy Co.*, 110 F.E.R.C. ¶ 61,211 (2005). In the prior declaratory order, the FERC did not discuss the prorationing provisions of the proposed pipeline.

118. *Spearhead*, *supra* note 111, at P 17, P 17 n.33.

e. Setting Limits: *Texas Access* and *Keystone*

In 2008, FERC further refined its firm capacity policy by addressing petitions requesting approval of priority in prorationing for contract shippers, posed by the proponents of two major greenfield projects: *Texas Access*¹¹⁹ and *Keystone*.¹²⁰ Both pipelines proposed to establish contract shipper classes paying discounted rates (relative to uncommitted shippers) with long-term commitments made in open seasons, and to file tariff rules granting those contract shippers priority rights during prorationing.¹²¹ Both pipelines planned to grant high percentages of total pipeline capacity to the contract shippers – approximately 90% in *Texas Access* and more than 94% in *Keystone*.¹²² In both orders, the FERC declined to approve the proposed prorationing rights for contract shippers, citing the high percentages granted to sole access by contract shippers during prorationing, denying new or spot shippers access.¹²³ Voicing a new concern, the FERC further objected that the contract shippers would hold superior rights to use of the pipeline while paying rates lower than the uncommitted shippers.¹²⁴ The FERC concluded that with these terms, each project would create unreasonable and unduly preferential arrangements for the contract shippers.¹²⁵ Although the *MAPL* and *Spearhead* orders on priority rights for contract shippers had not cited *Texaco* and its opposition to exclusionary contract rights in prorationing, both *Texas Access* and *Keystone* noted the prior ruling in *Texaco* rejecting a proposal to “lock” uncommitted shippers out of 80% of the capacity of the pipeline.¹²⁶ In *Keystone*, the Commission stated that it “decline[d] to overrule *Texaco*” as requested by the applicant.¹²⁷ The Commission distinguished its earlier *MAPL* and *Spearhead* orders on the grounds that in both, substantial portions of the pipeline remained available to non-contract shippers¹²⁸ and that in *Spearhead*, the contract shippers paid a premium.¹²⁹

The orders therefore identified three flaws in the contract shipper proposals, though it did not suggest which were predominant: (1) granting priority in prorationing to contract shippers paying a discounted rate relative to uncommitted shippers; (2) applying the priority to a very high percentage of the pipeline’s capacity; and (3) barring access to that capacity by non-contract shippers in prorationing “for many years.”¹³⁰

119. *Enbridge (U.S.) Inc.*, 124 F.E.R.C. ¶ 61,199 (2008) [hereinafter *Texas Access*]. This project involved a new, large volume (445,000 b/d) pipeline to transport crude petroleum from the hub of Patoka, Illinois, to Nederland, Texas, with a lateral to Houston.

120. *TransCanada Keystone Pipeline, LP*, 125 F.E.R.C. ¶ 61,025 (2008) [hereinafter *Keystone*]. This project would be a crude petroleum line initially sized at 435,000 b/d to transport crude petroleum from the Canada/U.S. international border to Wood River and Patoka, Illinois (with a corresponding Canadian line originating at Hardisty, Alberta).

121. *Texas Access*, *supra* note 119, at P 1; *Keystone*, *supra* note 120, at P 1.

122. *Texas Access*, *supra* note 119, at P 1; *Keystone*, *supra* note 120, at P 48.

123. *Texas Access*, *supra* note 119, at P 37; *Keystone*, *supra* note 120, at P 51.

124. *Texas Access*, *supra* note 119, at P 34; *Keystone*, *supra* note 120, at P 47.

125. *Texas Access*, *supra* note 119, at P 37; *Keystone*, *supra* note 120, at P 51.

126. *Texas Access*, *supra* note 119, at P 35; *Keystone*, *supra* note 120, at P 48.

127. *Keystone*, *supra* note 120, at P 48.

128. *Texas Access*, *supra* note 119, at P 36; *Keystone*, *supra* note 120, at P 49.

129. *Texas Access*, *supra* note 119, at P 35; *Keystone*, *supra* note 120, at P 48.

130. *Texas Access*, *supra* note 119, at P 36; *Keystone*, *supra* note 120, at P 49.

f. Confirming the Standard: *Enbridge North Dakota 2010*

Following the *Texas Access* and *Keystone* orders, a two-year hiatus followed in which oil pipeline sponsors did not file requests for contract rights in prorationing. Then, in August 2010, the Enbridge companies submitted a request for declaratory order for a somewhat complex project in North Dakota. The Enbridge Pipelines (North Dakota) LLC (Enbridge North Dakota) system had been in prorationing since the mid-1990s, as crude petroleum production from the Bakken formation outpaced Enbridge North Dakota's repeated efforts to expand capacity.¹³¹ In its 2010 petition, the company and its affiliate, Enbridge Pipelines (Bakken), L.P. (Enbridge Bakken), proposed three interrelated projects that together would permit the incremental export of substantial amounts (145,000 b/d) of Bakken production to U.S. markets: (1) building new lines feeding the Enbridge North Dakota mainline; (2) expanding capacity on the mainline to a connection with an idled connecting pipeline (Portal system); and (3) reversing the former Portal system (now owned by Enbridge Bakken) to transport Bakken production to the U.S./Canada international border.¹³² At the border, it would be transported by a Canadian affiliate to the Enbridge mainline and thence transported back across the U.S. border to refining markets served by Enbridge in the U.S. and eastern Canada.¹³³ The petition sought approval for several aspects of the project, including the following capacity arrangements: (1) priority rights for new five and ten year contract shippers on 80% of the newly looped mainline capacity on Enbridge North Dakota; (2) priority rights for 40% of the capacity of the newly constructed lateral supply projects connecting to the mainline; and (3) no capacity rights for the reversed Portal system.¹³⁴ The filing was effectively uncontested, and in November 2010 the FERC issued an order approving the petition, including the requested contract rights in prorationing.¹³⁵ The FERC noted that the proposal met the requirements of its precedents as relevant to capacity:

- “The proposal appropriately distinguishes committed and uncommitted shippers and provides for rates consistent with the obligations of each class of shipper.”

131. *Enbridge Pipelines (North Dakota) LLC*, 132 F.E.R.C. ¶ 61,274 at P 1 (2010).

132. *Id.*

133. *Id.*

134. Contracting shippers on the Enbridge Bakken pipeline would acquire priority capacity access rights on the Canadian counterpart pipeline, under the Canadian National Energy Board's (NEB) rules as to capacity rights, thus rendering formal capacity rights on Enbridge Bakken unnecessary -- only shippers with contract rights to take away volumes at the international border on the Canadian pipeline should be able to support nominations on Enbridge Bakken should prorationing arise. Thus, the FERC approval of capacity rights on Enbridge Bakken was not as essential as for Enbridge North Dakota. In the Canadian pipeline's application for authorization before the NEB it proposed that contract shippers would have priority rights for 79% of the capacity of the new system. See *Application for Bakken Pipeline Project Canada*, Enbridge Bakken Pipeline Company Inc., Vol. 1, at pp. 1-32, 2011 Nat'l Energy Bd. A27927 (Can. Jan. 17, 2011), available at <https://www.neb-one.gc.ca/ll-eng/livelink.exe?func=ll&objId=661440&objAction=browse> (the hearing before the NEB was scheduled to commence in October 2010).

135. *Enbridge Pipelines (North Dakota) L.P.*, 133 F.E.R.C. ¶ 61,167 at P 21 (2010) [hereinafter *Enbridge North Dakota 2010*] (noting that one protest was filed and then withdrawn).

- “Additionally, the Enbridge proposal provides a significant amount of capacity for uncommitted shippers.”
- “It offered all potential shippers the opportunity to become committed shippers.”¹³⁶

The reference to “rates consistent with the obligations of each class of shipper” appears to refer to the fact that the contract shippers’ local rate on Enbridge North Dakota, where they enjoyed priority in prorating, would be higher than the uncommitted shippers.

Enbridge North Dakota 2010 therefore confirms the FERC’s implicit set of requirements for priority contract rights in *Keystone* and *Texas Access*.

IV. ANALYSIS: CURRENT CONTRACT PRIORITY POLICY: PROBLEMS AND SOME SUGGESTED SOLUTIONS

A. *Problems Arising from the Current Policy and Potential Solutions*

The FERC’s policy regarding priority rights for contract shippers has developed dramatically over the past five years – from the pre-*MAPL* precedent of *Texaco*, suggesting that contract shippers could not ‘shut out’ non-contract shippers,¹³⁷ to the rapid and seemingly routine approval of substantial priority rights for contract shippers in *Enbridge North Dakota 2010*.¹³⁸ Major uncertainties remain, however. The relative dearth of declaratory orders since the *Texas Access/Keystone* orders issued in 2008 may suggest serious reservations about current requirements.

The FERC’s restrictions on contract shipper access and rates stem from the tension between recognizing that contract and uncommitted shippers may be granted different rates and terms of services because they may not be “similarly situated” under the ICA and the concern that the common carrier obligations of the ICA mandate some level of continued access. However, should the FERC remain wedded to the current standards, they are likely to pose significant challenges to pipelines and shippers in the current liquids pipeline markets. Commercial and marketplace problems arise from several distinct aspects of the standards applied by the FERC in *Enbridge North Dakota 2010* and its predecessor orders. Some of the chief problems, and possible grounds for addressing them, are discussed below.

1. Pricing

Many oil pipelines have incentive rates and contract commitment rates in their tariffs, and the rates associated with those contract rates have historically been discounts relative to the rates available to uncommitted shippers that do not have any obligation to tender and/or pay for transportation on the pipeline. The

136. *Id.* at P 40 (footnotes omitted).

137. *Texaco*, *supra* note 96, at p. 61,201.

138. The FERC approved this petition in just under three months – a very rapid turnaround time for a petition for declaratory order on a somewhat complex filing.

cost to contracting shippers of shouldering the obligation to supply large volumes of petroleum over many years is enormous.¹³⁹ Moreover, contract shippers making such costly commitments have also insisted on tariffs or other assurances that their rates would not be undercut by uncommitted shippers, for obvious competitive reasons.¹⁴⁰ In its *Texas Access* and *Keystone* orders, the FERC focused on the ‘value of service’ concept: that the quality of service to contract shippers receiving priority rights suggested a need to charge higher rates.¹⁴¹ However, the effective cost to the contract shippers of making the commitments to pay vast sums to the pipeline and risking market changes is not reflected in the tariff price alone. Therefore, the “premium” payment concept is an impediment to building new capacity or greenfield pipelines because it conflicts with the commercial needs of the shippers whose commitments are needed to underpin the pipeline’s financing.

The FERC’s current policy as to pricing contract rates with priority in prorationing should be amenable to a market-responsive approach, consistent with the FERC’s stated goals. Although the decisions in *Texas Access* and *Keystone* faulted the petitioners for not providing “premium” rates for the contract shippers, the FERC has not necessarily required a “premium.” In *Enbridge North Dakota 2010*, the order approved the requested program as “provid[ing] for rates consistent with the obligations of each class of shipper.”¹⁴² Rather than mandating higher filed rates for contract shippers receiving a priority in prorationing, this standard would permit pipeline applicants to demonstrate that even though the tariff *rate* may be lower for contract shippers, the rate is nonetheless consistent with the “obligations of each class of shipper”¹⁴³ because of the demonstrable, and if necessary, quantifiable *costs* to shippers of undertaking commitments.

In its first order approving lower rates for contract shippers – *Express* – the Commission recognized that lower rates for contract shippers were justified in part because of the burden that they undertook by making risky commitments for fixed periods of time in a changeable oil market.¹⁴⁴ Those risks and the other costs to contract shippers should be the basis for not simply justifying lower rates but lower rates in conjunction with tariff assurances of continued access during prorationing. Ultimately, as the Commission has recognized in other regulatory contexts, “anchor” shippers are needed,¹⁴⁵ and the Commission should be able to approve discounted contract rates if the market requirements are that the shippers making large long-term commitments receive both some assurance

139. See, e.g., Joint Petition for Declaratory Order of Enbridge (U.S.) Inc. and ExxonMobil Pipeline Company Regarding Texas Access Pipeline Project at 8 and Exh. A ¶ 22, FERC Docket No. OR08-7-000 (Feb. 7, 2008).

140. *Id.* at p. 22.

141. *Texas Access*, *supra* note 119, at P 34; *Keystone*, *supra* note 120, at P 47.

142. *Enbridge North Dakota 2010*, *supra* note 135, at P 40.

143. *Id.*

144. *Express II*, *supra* note 76, at p. 62,254 (stating that “[t]erm volume shippers committing to longer terms assume greater risks than shippers assuming lesser shipment obligations because 15 and 10 year terms present very long lead times in the oil business”).

145. See e.g., Order No. 2005, *Regulations Governing the Conduct of Open Seasons for Alaska Natural Gas Transportation Projects*, F.E.R.C. STATS. & REGS. ¶ 31,174, 70 Fed. Reg. 8,269 (2005) (to be codified at 18 C.F.R. pt. 157).

of actually being able to transport their committed volumes and receive a lower rate than potential competitors shouldering no risk, either before or after the pipeline is built.

2. “Substantial” Capacity for Non-Contract Shippers

The FERC has been solicitous to ensure that the pipeline’s granting of priority contract rights not displace current shippers and that even if priority rights are granted to some shippers, that substantial capacity must be available for both non-contract shippers and future new shippers.¹⁴⁶ The FERC has accepted expansions granting relatively high percentages (80%) of new expansion capacity to contract shippers, effectively providing large percentages (usually at least 60%) of total pipeline capacity for non-contract shippers, and has rejected outright proposals for contract reservation of 90%-94% on new greenfield pipelines.¹⁴⁷ However, for new pipelines costing hundreds of millions of dollars and more, project sponsors are unlikely to obtain financing easily for pipelines built 60% “on spec,” with a majority of capacity set aside for shippers who may or may not ship once market circumstances shift. New pipelines will likely seek high percentages of pipeline capacity committed to contract shippers – 80%-90% – and those percentages would track the “new shipper” volumes that the FERC has found adequate in the context of other prorationing methods (historical volume).

More broadly, for *new* pipelines the Commission should have broad authority in determining whether the common carrier obligation has been met by the proposed pipeline, *e.g.*, by expanding shipper access to markets and by having held open seasons under which all shippers have had a fair and open opportunity to become contract shippers. For new pipelines, the Commission’s misgivings regarding displacement of current shippers (discussed below) should not arise. The Commission need only address whether new shippers have adequate access to capacity in the future. Balanced against concerns over future access should be a powerful countervailing concern – that the pipeline would not be built without obtaining sufficient contract shipper commitment to support the financing of the project, which in turn would likely require high levels of committed capacity (80%-90%).¹⁴⁸ The interests of potential future new shippers in maximizing new capacity access must be balanced against the likelihood that without adequate contract shipper capacity assurances, the pipeline might not be constructed at all and the potential future shippers would ultimately have no capacity. In these circumstances, the FERC would be fully justified in using the same standard as it has applied in regular prorationing cases, in which a 10% set aside has repeatedly been approved for new shippers.¹⁴⁹ Certainly, nothing in the common carrier precedents discussed

146. See, *e.g.*, *MAPL*, *supra* note 105, at P 24.

147. *Id.*

148. Tellingly, after the two 2008 orders, the *Texas Access* project did not proceed. The *Keystone* project did proceed, but its shippers had contract entitlements to nearly 94% of the capacity on the Canadian pipeline feeding the U.S. Keystone line, thus providing some assurance to those shippers of not being displaced by new shippers in prorationing. See discussion *supra* Part III.B.2.e.

149. Andrew K. Soto, et al., *Report of the Oil Pipeline Committee*, 28 ENERGY L.J. 785, 800-801 (2007).

above in Section II suggests that the Commission cannot reach a contract shipper solution that meets evolving policy needs, consistent with the ICA.

3. Limitation to New Capacity

All of the orders authorizing priority access for contract shippers have involved newly-constructed capacity – either new pipeline segments or expansions of existing pipelines.¹⁵⁰ Although no pipeline has petitioned for a declaratory order regarding a proposal to apply contract rates and priority access to pre-existing capacity without any new construction, the FERC's current prorating policy would appear hostile to such an initiative. *Texaco*, in which the FERC rejected a tariff applying contract priorities to an existing tariff,¹⁵¹ suggests the hurdles faced by an applicant on this issue.

More recently, the FERC rejected a tariff filing by Enbridge North Dakota in 2007 that suggests the legal basis for rejecting requests for priority prorating rights applying to existing capacity.¹⁵² In *Enbridge North Dakota 2007*, the pipeline filed tariff sheets accompanied by an explanation that an expansion of capacity from 80,000 b/d to 110,000 b/d was planned; the tariff provided that post-expansion, 80% of the entire post-expansion capacity of the pipeline would be subject to contracts with priority over non-contract volumes in prorating to be allocated in an open season.¹⁵³ Shippers protested, and the FERC rejected the tariff. The specific ground for rejection was that the filing was premature – the expansion and thus the application of the new prorating procedures were being filed long in advance of the actual expansion, violating the FERC's rule that the tariff be filed when the entire expansion occurred and could be assessed in context.¹⁵⁴ However, in *dicta*, the FERC also addressed the issues raised by shipper protests and strongly suggested that the proposal would also be unlawful because (unlike the tariff addressed in *MAPL*) the pipeline proposed to displace current shippers' capacity arrangements with contract rights of likely different shippers:

In contrast, Enbridge North Dakota's FERC No. 50 completely eliminates its existing historically-based allocation methodology in favor of one that could prevent current shippers from using facilities they have funded through the rates they have paid. While Mid-America's proposal applied the new incentive program to approximately 25 percent of its total capacity, Enbridge North Dakota's proposal would make all of its existing and expansion capacity subject to the Phase 6 expansion. Thus, in Mid-America's case, the Commission found that non-incentive volume shippers would be eligible to ship on 75 percent of the system. Accordingly, the Commission found that neither historical nor new shippers would be denied access even if they did not sign long-term volume dedications.¹⁵⁵

Enbridge North Dakota 2007 therefore suggests a Commission view that applying contract rights to existing capacity, even following an open season, would violate current/historical shippers' rights acquired through long-term

150. See, e.g., *Enbridge North Dakota 2010*, *supra* note 135, at P 9.

151. *Texaco*, *supra* note 96, at p. 61,202.

152. *Enbridge Pipelines (North Dakota) LLC*, 120 F.E.R.C. ¶ 61,025 at P 26 (2007) [hereinafter *Enbridge North Dakota 2007*].

153. *Id.*

154. *Id.* at P 25.

155. *Id.* at P 24 (emphasis added).

payment of rates. This rationale accords with the Commission's stated concern in *Platte III* that shippers had in some way acquired a right or expectation of continuing to hold the allocation rights provided by the tariff.¹⁵⁶ The chief stated rationale thus far for not applying contract rates to existing capacity, as reflected in FERC precedent, therefore appears to be that replacing preexisting allocation methods with contract rights would be harmful to the expectations and even rights to access of pre-existing shippers – in addition to the concern that both preexisting and new shippers could not acquire access to the contract capacity in later years. Reading the various orders approving contract priorities also suggests another, policy-based rationale, even if not fully articulated by the post-*Texaco* orders: allowing contract shippers some degree of priority has the beneficial result of ensuring new construction, particularly in areas in which new capacity is needed (*e.g.*, the Bakken).

Thus, although the FERC has not overtly ruled out applying superior contract shipper access to existing capacity, its prorationing rationales and policy statements would appear to be hostile. Pipelines may, however, have significant market-responsive reasons for seeking to create contract shipper classes with priority prorationing rights for existing capacity. Markets may change in ways that do not require reversing or converting the pipeline to a different use. Shippers may need additional assurances of assured access in order to build new facilities to supply liquids to the pipeline – whether in the form of wells, gas processing plants, or refinery capacity. The FERC should be willing to consider and approve such proposals if they meet demonstrated market needs and provide non-discriminatory opportunities for all shippers to become contract shippers, thus meeting the non-discrimination requirements of the ICA.

Nothing in the court or ICC precedents discussed in Section II suggests that setting aside capacity in existing equipment for contract shippers is prohibited by the ICA or the common law.¹⁵⁷ Instead, those precedents suggest that the FERC has broad latitude to approve different terms of service to classes of customers that are not similarly-situated to allow a greater reliance on open seasons to allocate priority access rights. More broadly, adapting its policies to the special statutory and commercial context of the current oil pipeline industry would be consistent with the greatly varied manner in which agencies have regulated common carriers in different mode. The “common carrier” status of railroads did not prevent contract allocations, nor were water carriers prevented from being both contract and common carriers in the same vessels.

Regarding the concern about shippers having paid for access to the pipeline, the FERC should not adopt a rationale that it has rejected in other contexts. Shippers have never been held to acquire property rights in regulated company facilities solely because of their payment of rates.¹⁵⁸ Nor is there an equitable

156. *Platte III*, *supra* note 25, at P 119 (2010) (“The Commission finds that allocating the pipeline’s capacity first on the basis of historical deliveries to Destinations and then apportioning the Destination’s allocation pro-rata among shippers would adversely affect the shippers’ interests.”).

157. See discussion *supra* Section II.

158. *Duke Power Co.*, 48 F.P.C. 1384 (1972) (citing *Board of Pub. Util. Comm’rs v. New York Tel. Co.*, 271 U.S. 23, 31 (1926)). See also *Consumers Power Co.*, 52 F.E.R.C. ¶ 61,023, at p. 61,142 (1990) (“Properly phrased, the issue appears to be whether Consumers’ ratepayers have any *property rights* in the jurisdictional facilities. It is well established that they do not; ratepayers pay for service, not the property used to render service.”) (emphasis added).

argument that shippers making no commitments, and free to leave the pipeline at any time, have, by virtue of using the pipeline during times of capacity scarcity, created their own right to continued access on the same terms. Instead, the FERC should find, consistent with its policy on rates, that a class of contract shippers can acquire tariff rights without creating undue discrimination so long as a fair and non-discriminatory open season was held. In this respect, the legal basis for the FERC's potentially broader approval of priority rights in prorationing is exactly the same as the FERC's far more permissive policy toward allowing wide disparities in rates based on dissimilar shipper classes. The Commission should therefore remain open to proposals that improve the efficiency of the pipeline system and encourage new resources, while still protecting basic concerns about common carrier access, by allowing pipelines to propose and support contract priority rights in prorationing for existing pipeline capacity.

V. CONCLUSION

The FERC has resolved a number of rate and policy issues facing oil pipelines in the past decade, but its policy on capacity remains somewhat a work in progress. The FERC has, since 2005, begun to develop a robust policy setting out the basis for pipelines to meet shipper needs for assured transportation, as well as meet their need for shipper support. Under the ICA, the FERC does not face any hard-and-fast rules regarding the scope of the "common carrier obligation," but rather should shape a policy that meets the needs of the evolving marketplace as well as the broad access and non-discrimination mandate of the ICA. The FERC should be able to refine its policy to permit broader priority access rights for all types of capacity – greenfield pipelines, expansion capacity and existing capacity.