

# NOTES AND COMMENTS

## STRICT SCRUTINY OF FERC DECISIONS BY THE UNITED STATES COURTS OF APPEALS

### I. INTRODUCTION

The possibility exists that many Federal Energy Regulatory Commission (FERC or the Commission) decisions under review by courts of appeals trigger a form of strict judicial scrutiny which the courts do not identify as such. The purpose of this note is to discuss application of administrative law principles concerning standards of review of FERC decisions, but not the substantive law of those decisions.

Since January, 1988, the FERC has suffered more remands by the United States Circuit Courts of Appeals of its orders, in whole or part, than it has been affirmed.<sup>1</sup> Of sixty surveyed cases, the results are as follows: twenty-nine affirmed, twenty-five remanded, and six remanded in part/affirmed in part. Denials of petitions for review were treated as affirmed orders. The majority of petitions for review of FERC orders have been in the District of Columbia Circuit and the Fifth Circuit. The remand/affirmed ratio in the former is nearly 2 to 1. Only ten cases were affirmed or petitions for review denied; while nineteen cases have been remanded. In the Fifth Circuit, the FERC is just ahead of the .500 mark with nine cases affirmed and eight remanded. Collectively, the remaining courts of appeals have treated the FERC more favorably with ten orders affirmed and four remanded.

The standards of review of decisions of administrative agencies are the guideposts by which the courts begin their analyses of the agencies' decision. Whether the standard articulated by the reviewing court will actually be exercised will depend on the degree of deference the court has historically accorded the particular agency before it, and whether the agency has satisfied that enigma of administrative law: "reasonableness."

For the most part, the courts of appeals have applied the standards of review to orders of the FERC mandated by the Administrative Procedure Act<sup>2</sup> (APA), The Natural Gas Act,<sup>3</sup> The Natural Gas Policy Act of 1978<sup>4</sup> and precedent of the United States Supreme Court.<sup>5</sup> However, some cases decided

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1. *But see* INSIDE F.E.R.C., Oct. 15, 1990, at 2 (comment of FERC General Counsel William Scherman that FERC policy decisions have been upheld in 75% to 80% of recent court cases).

2. Administration Procedure Act § 5, 5 U.S.C. §§ 501-1305 (1988).

3. Natural Gas Act § 15b, 15 U.S.C. § 717r (1988) states in part that the Commission's findings of fact shall be conclusive if supported by substantial evidence.

4. Natural Gas Policy Act § 60, 15 U.S.C. § 3416(a)(4) (1988) states in part that the findings of fact of the Commission shall be conclusive if supported by substantial evidence.

5. *In re Permian Basin Area Rate Cases*, 390 U.S. 747 (1968) (reviewing court's responsibility is to assure itself that the Commission has given reasoned consideration); *NRLB v. Bell Aerospace Co. Div. of Textron, Inc.*, 416 U.S. 267 (1974) (agency decision whether to promulgate rule by adjudication or

in the Fifth Circuit and D.C. Circuit appear to hold the FERC to a higher standard of reasonableness without directly stating so in court opinions.

## II. OVERVIEW OF STANDARDS OF JUDICIAL REVIEW OF ADMINISTRATIVE AGENCIES

Standards of review of administrative agency decisions have their genesis in specific statutes such as the Natural Gas Act,<sup>6</sup> the Natural Gas Policy Act<sup>7</sup> and the APA.<sup>8</sup> In addition, United States Supreme Court decisions have clarified standards of review in such cases as *Chevron USA, Inc. v. NRDC*,<sup>9</sup> and *NLRB v. Bell Aerospace*.<sup>10</sup>

Findings of fact by the FERC are reviewed under the substantial evidence test,<sup>11</sup> which is evidence that a reasonable mind might accept as adequate to support a conclusion.<sup>12</sup> While the substantial evidence test is deferential to agency findings of fact, questions of law are freely reviewable.<sup>13</sup>

However, courts will generally defer to the informed judgment of an agency in matters specific to its expertise.<sup>14</sup> Matters that are committed to agency discretion are reviewed under the standard of abuse of discretion.<sup>15</sup> So-called "mixed" questions of law and fact are generally reviewed under a reasonableness standard because of a reviewing court's deference to the agency's expertise in the factual and legal matters it frequently deals with.<sup>16</sup> The standard for an agency's decision-making process (its reasoning) is subject to the highly deferential arbitrary and capricious standard.<sup>17</sup> Section 706 of the APA incorporates the standards of review set out above.<sup>18</sup>

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rulemaking is up to its informed discretion); *Chevron USA, Inc. v. NRDC*, 467 U.S. 837 (1984) (court may not substitute its own construction of statutory provision for reasonable interpretation made by agency where legislative delegation on the question is not explicit).

6. 15 U.S.C. §§ 717-717z (1988).

7. 15 U.S.C. §§ 3301-3432 (1988).

8. 5 U.S.C. §§ 501-1305 (1988).

9. 467 U.S. 837 (1984).

10. 416 U.S. 267 (1974).

11. 15 U.S.C. § 717r (1988); 15 U.S.C. § 3416(a)(4) (1988); 5 U.S.C. § 706(2)(E) (1988).

12. *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 477 (1951).

13. *Walker Operating Corp. v. FERC*, 874 F.2d 1320, 1332 (10th Cir. 1989).

14. *Id.* at 1332.

15. *South Carolina Pipeline Corp. v. FERC*, 868 F.2d 650 (3rd Cir. 1989) (FERC decision not to hold a discretionary hearing held not an abuse of discretion).

16. *Washington Urban League v. FERC*, 886 F.2d 1381, 1387 (3rd Cir. 1989).

17. *Id.* at 1388.

18. 5 U.S.C. § 706 (1988) provides that:

To the extent necessary to decision and when presented, the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of an agency action. The reviewing court shall—

- (1) compel agency action unlawfully withheld or unreasonably delayed; and
- (2) hold unlawful and set aside agency action, findings, and conclusions found to be—
  - (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law;
  - (B) contrary to constitutional right, power, privilege, or immunity;
  - (C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right;

### A. *Factual Determinations*

Factual determinations subject to the substantial evidence test<sup>19</sup> are seldom the sole basis for petition for review of FERC orders. Although the FERC's factual determinations are often challenged, they will be upheld if they are rational and supported by substantial evidence.<sup>20</sup> In the absence of a clear, reviewable record the courts of appeals likely will remand the decision for development of a complete record that explains the FERC's decisionmaking<sup>21</sup> process.

### B. *Jurisdictional Decisions*

Under the NGA, the FERC has jurisdiction over gas sold in interstate commerce.<sup>22</sup> The standard of review for a FERC jurisdictional decision is whether it had an adequate basis in law.<sup>23</sup> Essentially, this means that the FERC must reasonably interpret and apply congressional intent of statutory language and interpretations by the United States Supreme Court in making its jurisdictional conclusion.<sup>24</sup> Where the jurisdictional decision is unreasonable, it is arbitrary or capricious and the FERC will be reversed.

### C. *Discretionary Acts*

The standard of review of discretionary acts is substantial deference, otherwise known as abuse of discretion.<sup>25</sup> Because discretion denotes the

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- (D) without observance of procedure required by law;
  - (E) unsupported by substantial evidence in a case subject to section 556 and 557 of this title or otherwise reviewed on the record of an agency hearing provided by statute; or
  - (F) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court.

In making the foregoing determinations, the court shall review the whole record or those parts of it cited by a party, and due account shall be taken of the rule of prejudicial error.

*Id.*

19. Substantial evidence means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion. It must be enough to justify if the trial were to a jury, a refusal to direct a verdict when the conclusion sought to be drawn from it is one of fact for the jury. *Walker Operating Corp.*, 874 F.2d at 1331.

20. *Boston Edison Co. v. FERC*, 885 F.2d 962, 970 (1st Cir. 1989); *South Carolina Pipeline Corp. v. FERC*, 868 F.2d 650 (3rd Cir. 1989); *but see Mobil Oil Corp. v. FERC*, 886 F.2d 1023, 1033 (8th Cir. 1989) (in new regulatory scheme the primary considerations are of policy and law, not substantial evidence, referencing Order No. 436 that undertakes to restructure the natural gas transportation system to foster competition).

21. *Panhandle E. Pipeline Co. v. FERC*, 890 F.2d 435 (D.C. Cir. 1989) (remanded because the FERC failed to give explanation in the record for implementation of transportation-conversion entitlements; no reason given by the FERC for rejection of tariff).

22. § 2 of the NGA defines a natural gas company as "a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale." 15 U.S.C. § 717(a)(b) (1988).

23. *Walker Operating Corp.*, 874 F.2d at 1328.

24. *E P Operating Co. v. FERC*, 876 F.2d 46, 50 (5th Cir. 1988) (the FERC did not reasonably explain its classification of one pipeline as a jurisdictional transmission line and another as a nonjurisdictional gathering system when the two lines were markedly similar in operational characteristics).

25. *Union Tex. Prod. Corp. v. FERC*, 898 F.2d 432 (5th Cir. 1990) (filing requirements of the FERC);

capability to choose from among two or more courses of action, it is abused when that choice is unreasonable. For example, the FERC's refusal to explore or consider the need for environmental protections in licensing and relicensing procedures under the Federal Power Act<sup>26</sup> was held an abuse of discretion. Many years of governmental and private concern over the environment and legislative history endorsed that the FERC should consider environmental issues when granting annual licenses.<sup>27</sup> The FERC was free to decide that new license conditions are not called for, but failure to undertake any environmental assessment in connection with the issuance of a license was an abuse of its discretion. A discretionary choice will be upheld where the record reflects that the FERC gave reasoned consideration in its choice.<sup>28</sup>

#### *D. Statutory Interpretation and Contract Construction*

The FERC is involved in two related areas because of its regulatory function: the interpretation of statutes and construction of contracts. As an administrative agency, the FERC must interpret the statutes that control its congressionally delegated authority; as a regulatory body, it must interpret the regulations by which it exercises its authority. Under the FERC's regulatory power it must interpret contracts between private parties, and settlement agreements between itself and a regulated entity.

##### 1. Statutory Interpretation

An agency's interpretation of its organic statute and regulations is owed substantial deference.<sup>29</sup> The interpretation must rationally flow from the language of the regulation.<sup>30</sup> In *Acadian Gas Pipeline System v. FERC*,<sup>31</sup> the FERC required Acadian Gas Pipeline System to file a petition for rate approval for initial reports on NGPA section 311 transportation service after the FERC had already approved a three-year system-wide rate. The FERC contended that a change in the rate filing fee requirement justified its order because prior to the filing fee requirement it made no difference how many initial reports were received, but after the filing fee requirement there was a "strong regulatory purpose" to be served by this requirement.<sup>32</sup>

The Fifth Circuit found that the only strong regulatory purpose to be served was collecting more fees to spread the exorbitant cost of the filing fee for rate approval over a number of filings for the same service. This purpose

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*Gulf S. Pipeline Co. v. FERC*, 876 F.2d 431 (5th Cir. 1989) (delegation of authority to the Director of the Office of Pipeline and Producer Regulation); *Mobil Exploration & Prod., NA v. FERC*, 881 F.2d 193 (5th Cir. 1989) (the FERC's decision to promulgate policy by rule making or adjudication); *Williams Natural Gas v. FERC*, 872 F.2d 438, 451 (D.C. Cir. 1989) (agency discretion at its height when choosing not to act).

26. Federal Power Act § 12, 16 U.S.C. §§ 791a-828c (1988).

27. *Platte River Whooping Crane v. FERC*, 876 F.2d 109, 117, 118 (D.C. Cir. 1989).

28. *Borden Inc. v. FERC*, 855 F.2d 254, 264 (5th Cir. 1988) (the FERC's departure from a line of precedent held not an abuse of discretion where record indicated the FERC would not agree with older cases not requiring payback of money from grant of extraordinary relief).

29. *Acadian Gas Pipeline Sys. v. FERC*, 878 F.2d 865, 868 (5th Cir. 1989).

30. *Id.*

31. *Id.*

32. *Id.* at 869.

was stated in the FERC's brief before the court and was seen as insufficient to justify the FERC's change in procedure. Such a self-serving conclusion does not persuade a court to defer to the FERC's decision.

## 2. Contract Construction

FERC construction of settlement agreements between parties subject to its jurisdiction is based in general contract law and, historically, is a question of law subject to de novo review.<sup>33</sup> However, if the interpretation of the FERC is based on its technical expertise and findings of fact, then the courts will review the FERC's conclusions with deference; without the expertise factor, the courts may not defer to the FERC.<sup>34</sup> The deference accorded by the courts is based on a reasonable interpretation of the contract language by the FERC. In this context, reasonableness is a "satisfactory explanation for its action including a rational connection between the facts found and the choice made."<sup>35</sup> Once again, this is a different label for the "core" standard of review of the agencies: reasonableness.

### E. Policy Implementation

"The power of an administrative agency to administer a congressionally created . . . program necessarily requires the formulation of policy [,] . . . and such legislative regulations should be given controlling weight unless they are arbitrary or capricious."<sup>36</sup> In *Mobil Oil Corp. v. FERC*,<sup>37</sup> the FERC's decision to set an interruptible transportation rate was not arbitrary and capricious because the decision was based on relevant factors articulated in a reasoned fashion.

Conversely, if the FERC did not substantiate the application of a policy it promulgated through the development of facts or by a reasoned explanation, the order implementing the policy was remanded for further consideration. *Florida Gas Transmission Co. v. FERC*.<sup>38</sup> In *Florida Gas*, the FERC justified its actions on policy grounds alone. It did not hear evidence nor consider it necessary to rely on particular facts and circumstances, claiming its policy grounds were "prophylactic" in nature.<sup>39</sup> In remanding the order of the FERC, the Fifth Circuit stated that due process required that the FERC be able to substantiate its rule. In light of the increased filings and costs of those filings, the FERC's considerations were unreasonable, thus arbitrary and capricious.<sup>40</sup>

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33. *Dayton Power & Light Co. v. FERC*, 843 F.2d 947, 953 (6th Cir. 1988).

34. *Associated Gas Distrib. v. FERC*, 893 F.2d 349 (D.C. Cir. 1989); *City of Seattle v. FERC*, 883 F.2d 1084 (D.C. Cir. 1989).

35. *Associated Gas Distrib.*, 893 F.2d at 361.

36. *Chevron*, 467 U.S. at 844.

37. 886 F.2d 1023, 1030 (8th Cir. 1989) (petition for review of FERC order implementing new policy of open access).

38. 876 F.2d 42 (5th Cir. 1989).

39. *Id.* at 44.

40. *Id.* at 45.

### F. Decisionmaking

Decisionmaking is the FERC's reasoning that caused it to fashion, as it did, the order under review. Of course, decisionmaking is involved in factual determination, jurisdictional decisions, conclusions of law and the like. But, even though these preliminary decisions may be reasonable, their use in the rationalization process that leads to the ultimate order comes under separate scrutiny under the arbitrary and capricious standard.<sup>41</sup>

Part of the arbitrary and capricious standard is the requirement of a "reasoned explanation."<sup>42</sup> This is simply the FERC's articulation of a rational connection between the facts and the decision.<sup>43</sup> In *Gulf States Utilities Co. v. FERC*,<sup>44</sup> the D.C. Circuit remanded the FERC's decision to require Gulf States Utilities to provide back-up power to a Union Carbide plant that was located 1.7 miles from a co-generation facility<sup>45</sup> and was jointly owned by Union Carbide and Fina Oil and Chemical Company. On review of the FERC's order, the D.C. Circuit stated that "unfortunately, in this case we are unable to find in the Commission's orders, or in its brief, a coherent explanation for its determination . . ."<sup>46</sup> The FERC had supported its conclusion with two subordinate conclusions which the court thought had no reasoned basis. The first that multiple ownership posed no obstacle to certification; the second that the FERC would not draw on artificial distinction between the consumption and production of cogeneration energy where the two were a unitary and reciprocal process.<sup>47</sup>

The court reacted to these reasons by saying that "we . . . merely point out that it is not enough, in support of a conclusion, to cite another conclusion."<sup>48</sup> Where the FERC gives the reviewing courts a "reasoned explanation," its decisions will generally be affirmed.<sup>49</sup>

### III. THE STRICT SCRUTINY STANDARD OF REVIEW: FAILURE OF REASONED DECISIONMAKING

The courts of appeals have created a partnership with administrative agencies in effectuating the role assigned to the latter by Congress and the

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41. *Walker Operating Co. v. FERC*, 874 F.2d 1320, 1337, (10th Cir. 1989) (citing *Citizens to Preserve Overton Park, Inc. v. Volpe*, "The Supreme Court has declared that the generally applicable standards of [5 U.S.C.] § 706 require the reviewing court to determine that the agency's actual choice was not "arbitrary [and] capricious").

42. *Id.*

43. *Id.*

44. 872 F.2d 487 (D.C. Cir. 1989).

45. *Id.* at 438. Under the Public Utility Regulatory Policies Act of 1978 the FERC is to prescribe rules under which electric utilities would be required to provide back-up power to and purchase surplus power from, "qualifying cogeneration facilities." *Id.*

46. *Id.* at 490.

47. *Id.*

48. *Id.* at 491.

49. *Michigan Consol. Gas Co. v. FERC*, 883 F.2d 117 (D.C. Cir. 1989); *Hadson Gas Systems, Inc. v. FERC*, 877 F.2d 66 (D.C. Cir. 1989); *Kansas Power and Light Co.*, 891 F.2d 939 (D.C. Cir. 1989); *Borden, Inc. v. FERC*, 855 F.2d 254 (5th Cir. 1988); *Boston Edison Co. v. FERC*, 885 F.2d 962 (1st Cir. 1989).

Executive Branch.<sup>50</sup> As one court of appeals judge has observed, however, "There is little doubt who is considered to be the senior partner."<sup>51</sup>

Nearly twenty years ago, the D.C. Circuit began flexing its partnership muscle. In *Environmental Defense Fund, Inc. v. Ruckelshaus*,<sup>52</sup> Chief Judge Bazelon stated:

We stand on the threshold of a new era in the history of the long and fruitful collaboration of administrative agencies and reviewing courts . . . . On matters of substance, the courts regularly upheld agency action, with a nod in the direction of the substantial evidence test, and a bow to the mysteries of administrative expertise . . . . Courts occasionally asserted, but less often exercised, the power to set aside agency action on the grounds that an impermissible factor had entered into the decision, or a crucial factor had not been considered.<sup>53</sup>

Judge Bazelon was discussing this judicial evolution of scope of review in the context of administrative action that touched fundamental personal interests in life, health and liberty.<sup>54</sup> To protect these interests (but not economic interests which are at stake in ratemaking or licensing proceedings) Judge Bazelon said "It is necessary, but not sufficient, to insist on strict judicial scrutiny of administrative action."<sup>55</sup>

About the same time as Judge Bazelon was raising the standard of "reasoned decisionmaking" to a level of strict scrutiny, his brother on the bench, Judge Leventhal, was evolving the D.C. Circuit's "hard look" doctrine.<sup>56</sup> Judge Leventhal suggested that a reviewing court should study the record even as to the evidence on technical and specialized matters that underlie the agency's decisionmaking to "satisfy itself" that the agency has exercised a "reasoned discretion."<sup>57</sup> The court must be satisfied that the agency has taken a "hard look" at the issues with the use of reasons and standards.<sup>58</sup> If the agency's path can "reasonably be discerned"<sup>59</sup> after the hard look, then the agency's decision will be affirmed.

#### A. Failure of Reasoned Decisionmaking

The D.C. Circuit uses the standard of reasoned decisionmaking most often when remanding or vacating the FERC.<sup>60</sup> More often than not, how-

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50. See *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 851-852 (D.C. Cir. 1970).

51. Friendly, *Some Kind of Hearing*, 123 U. PA. L. REV. 1267, 1311 n.221 (1975).

52. 439 F.2d 584 (D.C. Cir. 1971).

53. *Id.* at 597.

54. *Id.* at 598.

55. *Id.*

56. *Greater Boston*, 444 F.2d at 851.

57. *Id.* at 850.

58. *Id.* at 851.

59. *Id.*

60. See *ANR Pipeline Co. v. FERC*, 863 F.2d 959 (D.C. Cir. 1988); *Colorado Interstate Gas Co. v. FERC*, 850 F.2d 769 (D.C. Cir. 1988); *Associated Gas Distrib. v. FERC*, 899 F.2d 1250 (D.C. Cir. 1990); *Panhandle E. Pipeline Co. v. FERC*, 890 F.2d 435 (D.C. Cir. 1989); *Associated Gas Distrib. v. FERC*, 893 F.2d 349 (D.C. Cir. 1989); *American Gas Assoc. v. FERC*, 888 F.2d 136 (D.C. Cir. 1989); *Gulf States Util. Co. v. FERC*, 872 F.2d 487 (D.C. Cir. 1989); *Williams Natural Gas Co. v. FERC*, 872 F.2d 438 (D.C. Cir. 1989); *Tennessee Gas Pipeline Co. v. FERC*, 871 F.2d 1099 (D.C. Cir. 1989); *Laclede Gas Co. v. FERC*, 873 F.2d 1494 (D.C. Cir. 1989); *Raton Gas Co. v. FERC*, 852 F.2d 612 (D.C. Cir. 1988); *Public Util. of*

ever, when the D.C. Circuit decides to affirm the FERC, it invokes one of the familiar APA standards of review like the arbitrary and capricious standard, or the substantial evidence test.<sup>61</sup>

Recent developments suggest that the standards of review of the APA have been merged into one standard of reasonableness. In *Michigan Consolidated Gas Co. v. FERC*,<sup>62</sup> the D.C. Circuit reduced the substantial evidence test of the Natural Gas Act<sup>63</sup> to an application of the arbitrary and capricious standard to factual findings.<sup>64</sup> But, the "highly deferential" arbitrary and capricious standard requires the reviewing court to satisfy itself that the agency examined the relevant data and articulated a satisfactory explanation for its action, including a rational connection between the facts found and choice made.<sup>65</sup> The terms of art in the APA are used to indicate the point on the spectrum of reasonableness where the reviewing court accepted or rejected the FERC's reasoning are merely descriptive of the degree of deference given by the court.

The D.C. Circuit's sometimes departure from the familiar standards of review begs the question of whether it has crossed the line between economic interests and "fundamental" personal interests that Judge Bazelon drew in *Environmental Defense Fund, Inc. v. Ruckelshaus*.<sup>66</sup> That court's use of its failure of reasoned decisionmaking standard closely resembles a strict scrutiny standard applied to orders of the FERC that touch economic interests.

The phrase "economic interest" must be grounded in the policy underlying the statute through which the FERC is exercising its authority. The Natural Gas Act was enacted to accomplish the overall purpose of protecting the consumers' interest in an adequate supply of natural gas at reasonable rates.<sup>67</sup> The Natural Gas Policy Act was passed to eliminate jurisdictional limitations of the NGA and alleviate natural gas shortages caused by inadequate supplies in interstate pipeline systems.<sup>68</sup> The NGPA encouraged the production and exploration of natural gas sources, as well as the maintenance of adequate supplies of natural gas in the interstate market.<sup>69</sup>

Because a FERC order can touch interests or producers, interstate and intrastate pipelines, distributors, local distribution companies, consumers and others, the phrase "economic interest" has a broad sweep. The following cases

*Cal. v. FERC*, 894 F.2d 372 (D.C. Cir. 1990); *Panhandle E. Pipeline Co. v. FERC*, 881 F.2d 1101 (D.C. Cir. 1989); *American Mun. Power v. FERC*, 863 F.2d 70 (D.C. Cir. 1988).

61. *National Fuels Supply Corp. v. FERC*, 899 F.2d 1244 (D.C. Cir. 1990); *Tennessee Gas Pipeline Co. v. FERC*, 898 F.2d 801 (D.C. Cir. 1990); *ANR Pipeline Co. v. FERC*, 876 F.2d 124 (D.C. Cir. 1989); *Michigan Consol. Gas Co. v. FERC*, 883 F.2d 117 (D.C. Cir. 1989); *Pennsylvania Pub. Util. Comm'n v. FERC*, 881 F.2d 1123 (D.C. Cir. 1989).

62. 883 F.2d 117, 124 (D.C. Cir. 1989).

63. 15 U.S.C. § 717r(b) (1988).

64. 883 F.2d at 124.

65. *Walker Operating Co. v. FERC*, 874 F.2d 1320, 1337, (10th Cir. 1989).

66. 439 F.2d 584, 598 (1971).

67. *Florida Power & Light v. FERC*, 598 F.2d 370 (5th Cir. 1979).

68. *Associated Gas Distrib. v. FERC*, 824 F.2d 981, 1001 (D.C. Cir. 1987).

69. H. REP. NO. 95-436, 95th CONG., 2nd Sess. 10, reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 7855, 7858-59; H. REP. NO. 95-496 pt. IV, 95th CONG. 2nd Sess. 96-97, reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 7659, 8540-41.69.

illustrate some, but obviously not all, economic interests which can be affected by the FERC.

### 1. Decisions Which Failed to Trigger the Higher Standard

In *Kansas Power and Light Co. v. FERC*,<sup>70</sup> Kansas Power and Light (KPL) petitioned for review of a FERC order amending the certificates of Williams Natural Gas (Williams) to allow it to sell gas directly to Atlas Power Company, bypassing KPL. The court found that KPL offered no service to Atlas Power Co. that might be injured by the amended certificate.<sup>71</sup> It stated that KPL transported the gas a trivial distance,<sup>72</sup> and that the loss to KPL of \$100,000 per year in net profit versus its \$90,000,000 per year revenues was not a material issue of fact.<sup>73</sup> In the view of the *Kansas Power and Light Co.* court, the FERC order in question furthered economic interests overall rather than being injurious: "Thus, without jeopardizing any potential countervailing values, the Commission was able to secure the benefits of competition, giving others access to market-priced gas and KPL a spur to efficiency and competitive pricing."<sup>74</sup>

The court's holding reflected one of the policies of the Natural Gas Act, forcing competition to allow end users competitive priced gas. In affirming the FERC, it is notable that the D.C. Circuit did not state the standard of review it was using.

In *Hadson Gas Systems, Inc. v. FERC*,<sup>75</sup> the D.C. Circuit affirmed a FERC order where the petitioner was unable to convince the court that its economic interest in avoiding unfair competition outweighed the economic benefit of increased competition. The FERC approved a tariff filed by a gas merchant, Tennessee Gas Pipeline Co., that required shippers of natural gas to disclose to Tennessee Gas the names of the end-users of the gas to be transported. Hadson Gas Systems, Inc. alleged the disclosure requirement was anticompetitive because Tennessee could essentially steal its customers. The court found that Tennessee was not sharing end-user information with its marketing affiliate, and the practice was prohibited by FERC regulation.<sup>76</sup> The court stated that "The mere suggestion that Tennessee may be tempted in the future to violate that regulation and pass the information to its marketing affiliate is insufficient to justify a determination that the Commission disregarded its duty to promote competition."<sup>77</sup> Using a reasonableness standard the D.C. Circuit affirmed the order that promoted the policy of competition embodied in the Natural Gas Act.

Where a FERC order protects a distinctly articulated economic interest,

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70. 819 F.2d 939 (D.C. Cir. 1989).

71. *Id.* at 942.

72. *Id.*

73. *Id.*

74. 891 F.2d at 943.

75. 877 F.2d 66 (D.C. Cir. 1989).

76. *Id.* at 71.

77. *Id.*

the D.C. Circuit appears likely to uphold it. In *ANR Pipeline Co. v. FERC*,<sup>78</sup> the FERC issued individual certificates of public convenience and necessity to ANR and Great Lakes Transmission Company (Great Lakes). The certificates were to expire at the earlier of one year from issuance or the date on which the pipeline accepted a blanket certificate. The court affirmed the order as "reasonable" because of the FERC's concern over discriminatory access to transportation pipelines and specific allegations of such relating to Great Lakes.<sup>79</sup> Apparently, natural gas purchasers had submitted to the FERC specific allegations of such discrimination by Great Lakes.<sup>80</sup> To allow discriminatory access to gas transportation lines would undoubtedly restrict competition. The acceptance of the blanket certificates would induce the pipelines to buy from a wider range of producers and sell to a wider range of buyers, thereby promoting competition.<sup>81</sup>

In *Michigan Consolidated Gas Co. v. FERC*,<sup>82</sup> the D.C. Circuit denied review of a FERC order allowing Panhandle Eastern Pipeline Co. to bypass Michigan Consolidated Gas Co. (MichCon), a local distribution company (LDC), to supply gas to National Steel Corp. The FERC has a "preference" policy favoring LDC service to industrial customers, but it is rebuttable if economic considerations preclude the preference. Factors the court considered important in the FERC's "reasoned explanation" of its decision to bypass MichCon were that National would eventually be forced to reduce its energy costs, causing it to avail itself of cheaper gas than MichCon could supply.

The harm to MichCon was inevitable. National employed 12,000 people company-wide, while MichCon only 5,500.<sup>83</sup> All of National's employees' jobs would be affected unless National could reduce its costs, which it could do by using Panhandle Eastern's lower priced gas. The Commission decided that insistence on the use of MichCon would cause significant economic harm to National and the local economy supported by National.<sup>84</sup> Thus, the economic interests of the public in cheaper gas took priority over the economic interest of MichCon in a small segment of its market.

## 2. The Higher Standard in Application

Where the petitioner demonstrates that an economic interest has been or will be impaired, the D.C. Circuit generally applies its version of strict scrutiny: failure of reasoned decisionmaking. Williams Natural Gas Co. (Williams) petitioned for review of an order of the FERC terminating an ongoing rule making proceeding in *Williams Natural Gas Co. v. FERC*.<sup>85</sup> The Notice of Proposed Rulemaking (NOPR) proffered substantial changes in the incentive price for tight formation gas. The FERC suspected its own decisions were

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78. 876 F.2d 124 (D.C. Cir. 1989).

79. *Id.* at 133.

80. *Id.* at 130.

81. *Id.* at 127.

82. 883 F.2d 117 (D.C. Cir. 1989).

83. *Id.* at 123.

84. *Id.*

85. 872 F.2d 438 (D.C. Cir. 1989).

exacerbating the current gas pricing problems. The proposed change would have affected all new tight formation gas for which surface drilling had commenced after the date of the publication of the notice of proposed order. The FERC was also considering expanding the new pricing to gas from wells already drilled. Four years after the notice, the FERC terminated the rule making.

Using its failure of reasoned decisionmaking standard, the D.C. Circuit remanded the order because of potential harm to the petitioners. The court observed that:

If the agency had promulgated the rule as set forth in the NOPR, the retroactive application of that rule would have resulted in substantial refunds to the pipelines.<sup>86</sup> It nevertheless seems clear to us that this additional category of gas—tight formation gas already bought and paid for which was produced from wells drilled after February 22, 1983—was at least *potentially* affected by FERC's termination of the docket.<sup>87</sup>

The FERC's major justifications for terminating the rule making were that changes in the natural gas industry and competition had caused the proposed rule to become obsolete.<sup>88</sup> In refusing to defer to the FERC's expertise in this area, the court rejected these findings of fact and appeared to put the burden on the FERC to deal with the take-or-pay problem.<sup>89</sup>

In an era where the FERC has been attempting to restructure the natural gas industry, the D.C. Circuit refused to allow the FERC to do so in arguable contravention of Supreme Court precedent in *Chevron USA, v. NRDC*,<sup>90</sup> and *SEC v. Chenery Corp.*<sup>91</sup> The court stated that it would give less deference to the promulgation of a new rule that changed the status quo than the decision to terminate a rule making.<sup>92</sup> Yet, in *Williams Natural Gas* above, the termination of the rule making did not change the status quo; it only threatened such a change. Logically, the *Williams Natural Gas* court should have been more deferential to the FERC decision.

*Associated Gas Distributors v. FERC*<sup>93</sup> reaffirms the D.C. Circuit's higher standard of review of orders causing economic harm where the result violates a provision of the NGA. The D.C. Circuit remanded a FERC order promulgating a "purchase deficiency" allocation mechanism under which the pipeline operators costs, with respect to take-or-pay contracts with producers, were allocated among customers based in part upon deficiencies between customers' levels of purchases in a "deficiency period" and those in a "base period."

The court found that the FERC's orders forced past customers who no longer purchased any gas from one of the petitioners, to pay their share of the take-or-pay liability.<sup>94</sup> Further, downstream purchasers would be expected to

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86. *Id.* at 444.

87. *Id.*

88. *Id.* at 446, 447.

89. *Id.* at 447.

90. *Chevron USA, Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984).

91. *SEC v. Chenery Corp.*, 332 U.S. 194 (1947).

92. 872 F.2d at 443.

93. 893 F.2d 349 (D.C. Cir. 1989).

94. *Id.* at 355.

pay a surcharge, over and above the rates on file at the time of sale, for gas they had already purchased.<sup>95</sup> The FERC also violated the filed rate doctrine<sup>96</sup> by allowing a pipeline company to charge its customers a retroactive rate different from the rate on file.

In *Laclede Gas Co. v. FERC*,<sup>97</sup> the petitioners sought review of a FERC order rejecting a settlement agreement of certain contested issues among United Gas Pipeline Company and its customers, including Laclede Gas. The effect of the order was to suspend refunds to customers, delay the filing of new rates and delay collecting the difference between old rates and new filed rates.<sup>98</sup> The court remanded the order because the FERC had not considered reasonable alternatives nor had it given reasons for not considering them.

The key to the case may be the court's statement that "Many millions of dollars of ratepayers money may be at stake. When so much depends upon the agency having a sure footing, it is not too much for us to demand that it look first, and then leap if it likes."<sup>99</sup> This quote suggests that the D.C. Circuit's primary concern is to protect persons and entities from economic harm caused by orders of the FERC.

In *American Municipal Power-Ohio, Inc. v. FERC*,<sup>100</sup> the economic harm suffered by American Municipal Power-Ohio, Inc. (AMP) was that a FERC order forced it to buy power at a higher rate.<sup>101</sup> The court was dissatisfied with the FERC's attempt to distinguish prior precedent: "Counsel for FERC has eloquently argued to us apparently meaningful distinctions between this case and *Wisconsin Power* and *Commonwealth Edison*. Unfortunately, FERC did not set those out below."<sup>102</sup> The FERC had failed to supply "adequate reasoning"<sup>103</sup> for its conclusion so the D.C. Circuit remanded the order for a more complete development of the record.

Being forced to provide back-up power for a "cogeneration facility"<sup>104</sup> could be an economic injury to the utility providing the back-up power. *Gulf States Utilities Co. v. FERC*<sup>105</sup> involved this scenario. The D.C. Circuit remanded the order because the FERC had "failed to explain the basis for its decision."<sup>106</sup>

Apparently, when the D.C. Circuit disagrees with the FERC's balancing of interests in the latter's decisions, this triggers a higher, less deferential, standard of review from the court. Because of that court's role as the primary or

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95. *Id.*

96. 15 U.S.C. § 717 c(d) (1988) (requires that no regulated seller may collect a rate other than the one filed with the Commission).

97. 873 F.2d 1494 (D.C. Cir. 1989).

98. *Id.* at 1496.

99. *Id.* at 1499.

100. 863 F.2d 70 (D.C. Cir. 1988).

101. *Id.* at 72.

102. *Id.* (citing *Commonwealth Edison Co.*, 35 F.E.R.C. ¶ 61,352 (1986) and *Wisconsin Power & Light Co.*, 40 F.E.R.C. ¶ 61,316 (1987)).

103. *American Municipal*, 863 F.2d at 73.

104. See 16 U.S.C. §§ 824(a)-3(a) (1988).

105. 872 F.2d 487 (D.C. Cir. 1989).

106. *Id.* at 491.

alternate court of review in many federal statutory schemes, knowledge of this higher standard of review is critical to a petitioner in framing allegations of error made by the FERC.

### III. THE FIFTH CIRCUIT AND ORDER 451

Because of the number of decisions in the D.C. Circuit, the higher standard of review is more easily seen. It is less obvious in the other circuit courts. *Mobil Oil Exploration and Producing Southeast, Inc. v. FERC*,<sup>107</sup> demonstrates that the Fifth Circuit may be employing a similar higher standard.

In *Mobil Oil*, the Fifth Circuit vacated in its entirety, Order 451.<sup>108</sup> Briefly, Order 451 allowed first sellers of old gas to engage in Good Faith Negotiations with pipeline purchasers for a higher price up to newly created ceilings; allowed sellers to terminate existing contracts in the absence of agreement from the negotiations; and allowed existing sellers to terminate and abandon existing contracts where agreement is reached with a new user/purchaser after notice of first refusal.

Order 451 collapsed the previous vintage price system and set a single higher-than-market ceiling on old gas. The Congressional intent of the NGPA was to protect consumers from high prices of old inexpensive gas.<sup>109</sup> The court saw this as an act in excess of the FERC's authority because of Congressional remarks showing that Congress believed that deregulation of old gas could never be feasible.<sup>110</sup> In the expert opinion of the FERC, market forces would keep the price of old gas low by allowing more of it to enter the market.<sup>111</sup> Addressing this point, the court simply stated that the FERC had exceeded its statutory authority, without giving any deference whatsoever to the FERC's expertise with the natural gas market.<sup>112</sup>

Order 451 authorized "pre-granted" abandonment.<sup>113</sup> The FERC supported this feature of Order 451 by stating that it was FERC policy that the propriety of abandonment was governed by a balancing of the needs of current gas consumers being served by the gas reserves with the benefits that would be conferred on the natural gas market as a whole if these reserves were released from dedication. However, the court refused to accept this reasoning because in its judgment, the abandonment procedure would be in the producer's control and thus only serve the producer's interest but not the consumer and market as a whole.<sup>114</sup>

The FERC stated in Order 451 that the market would resolve the take-

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107. 885 F.2d 209 (5th Cir. 1989).

108. Order 451, *Ceiling Prices: Old Pricing Structures*, III F.E.R.C. Stats. & Regs. ¶ 30,701, 51 Fed. Reg. 22, 168 (1986) (to be codified at 18 C.F.R. pts. 154, 157, 270, 271 284); *vacated*, 885 F.2d 209 (5th Cir. 1989); *cert. granted*, 110 S. Ct. 2585 (1990); [hereinafter Order 451].

109. 885 F.2d at 218, 219 (5th Cir. 1989).

110. *Id.*

111. *Id.* at 219, 220.

112. *Id.* at 226.

113. § 7(b) of the NGA requires that a jurisdictional facility get permission from the FERC prior to abandonment of facilities.

114. *Mobil Oil*, 885 F.2d at 222, 223.

or-pay problem created during the 1970's.<sup>115</sup> The Fifth Circuit, however, stated that "[a]s we view the operation of Order No. 451, it would not, as the Commission asserts, alleviate the take or pay problem."<sup>116</sup> If in the informed expert judgment of the FERC, market forces would deal with the take or pay problem, it seems that the Fifth Circuit should have granted the FERC's policy conclusion the deference required by *Chevron*.<sup>117</sup> In *Mobil Oil*, the Fifth Circuit was protecting the economic interests of consumers of natural gas and the players in that marketplace. In doing so it substituted its judgment for that of the FERC.

## V. REVEALING DISSENTERS

It is noteworthy that when the courts of appeals cross this line, which the Supreme Court has admonished them in the past for doing,<sup>118</sup> one of their brethren writes a dissenting opinion reminding the court of its proper role in reviewing agency action. Circuit Judge Brown vigorously dissented in *Mobil Oil*.<sup>119</sup> He argued that the court substituted its judgment for that of the FERC, failed to defer to agency expertise, imposed a legislative mandate on the FERC to resolve the take or pay problem, and, said "this Court's own action in nullifying the 451 Order is an unauthorized intrusion into a field which neither Article III nor legislation commands."<sup>120</sup>

Judge Starr in the D.C. Circuit felt compelled to similarly speak out in his dissent in *Laclede Gas Co. v. FERC*.<sup>121</sup> Judge Starr thought that the FERC had struck a reasonable balance between private interests in a particular settlement and the broader public interest in reasonable rates.<sup>122</sup> Citing *Permian Basin Area Rate Cases*,<sup>123</sup> Judge Starr reminded the court that the standard of review in rulemaking cases in the natural gas industry was limited to whether the rates were just and reasonable. Congress had entrusted the regulation of the natural gas industry to the informed judgment of the Commission, and not to the preferences of reviewing courts. In closing, Judge Starr said "the court has allowed petitioners to shoot down FERC's orders by sending up a few trial balloons. That approach, with all respect, fails to comport with out limited scope of review."<sup>124</sup>

When Chief Judge Bazelon set out his strict judicial scrutiny of adminis-

115. During a time of gas shortage, pipelines entered into take or pay contracts which typically required the pipeline to take a specified volume of gas from the producer or, in the event the gas was not taken, pay for the specified volume anyway.

116. *Mobil Oil*, 885 F.2d 224 (emphasis supplied).

117. 467 U.S. 886 (1984).

118. The Supreme Court reminded the courts of appeals that where Congress has left policy decisions to the agencies, federal judges who have no constituency and no expertise, have a duty to respect the legitimate policy choices made by those who do—Congress and the Executive Branch. *Chevron*, 467 U.S. 837 (1984).

119. *Mobil Oil*, 885 F.2d at 226-235.

120. *Id.* at 235.

121. 873 F.2d 1494, 1499 (D.C. Cir. 1989).

122. *Id.* at 1500.

123. 390 U.S. 747 (1968).

124. *Laclede Gas*, 873 F.2d at 1505.

trative action in *Environmental Defense Fund, Inc. v. Ruckelshaus*,<sup>125</sup> Judge Robb in a brief, but targeted dissent, stated “[in] my view the majority opinion substitutes the judgment of this court for the judgment of the Secretary in a matter committed to his discretion by law . . . In effect, the court is undertaking to manage the Department of Agriculture. Finding nothing in the statutes that gives us such authority I respectfully dissent.”<sup>126</sup>

## VI. CONCLUSION

The D.C. Circuit, and perhaps other courts of appeals as well, seem to be operating under a dual approach to standards of review of orders of the FERC. On one side are orders with little or no adverse economic impact on those affected, such as licensing and issuance of certificates of public convenience, which are reviewed under the deferential standards of review—arbitrary and capricious, substantial evidence, etc. Indeed, such orders usually promote economic interests embodied in statutory policies such as competition and between regulated parties or reasonably priced gas to consumers.

However, when the order appears to have the potential to cause economic injury to an industry, individual industry petitioners or consumers without offering a countervailing benefit, the D.C. Circuit uses its minimally deferential standard of review: strict judicial scrutiny, otherwise known as failure of reasoned decisionmaking. Application of the stricter standard undoubtedly expands the courts of appeals’ power beyond the limits of Article III and leads them into regions of policy making more properly reserved for Congress and its agencies. Although there is support for the argument that the FERC has at times been remiss in its administrative and procedural duties,<sup>127</sup> these instances are not as numerous as those in which the D.C. Circuit flatly disagrees with the decisions of the FERC.

In the late 1970’s the D.C. Circuit was reversing policy decisions of the Environmental Protection Agency (EPA) in its use of “bubbling”<sup>128</sup> in portions of the Clean Air Act.<sup>129</sup> In *Alabama Power Co. v. Costle*,<sup>130</sup> *Asarco, Inc. v. EPA*,<sup>131</sup> and *Natural Resources Defense Council, Inc. v. Gorsuch*,<sup>132</sup> the D.C. Circuit decided that the EPA had incorrectly defined “source” in the EPA’s clean air attainment programs. The Supreme Court decided that the D.C.

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125. 439 F.2d 584 (1971).

126. *Id.* at 598.

127. *City of Fredricksburg v. FERC*, 876 F.2d 1109 (4th Cir. 1989) (acting director of FERC’s Hydropower Licensing Office violated the FERC’s own regulations by issuing licensing without compliance with state water quality certification.); *Mobil Prod. Tex.-N.M., Inc. v. FERC*, 886 F.2d 745 (5th Cir. 1989) (the FERC abused its discretion in not holding an evidentiary hearing when the evidence was readily available); *Panhandle E. Pipeline Co. v. FERC*, 890 F.2d 435 (D.C. Cir. 1989) (the FERC changed its policy on capacity brokering but failed to inform the court until oral argument).

128. EPA had conceived a bubble concept whereby a measuring area over an entire plant was considered a bubble to measure the emissions from stationary sources within the plant instead of measuring each individual stationary source, i.e. piece of emitting equipment.

129. 42 U.S.C. §§ 7401-7642 (1988).

130. 636 F.2d 323 (D.C. Cir. 1979).

131. 578 F.2d 319 (D.C. Cir. 1978).

132. 685 F.2d 718, *rev’d*, 467 U.S. 837 (1984).

Circuit had exceeded its authority under Article III in those cases by substituting its judgment in policy areas which Congress had entrusted to the EPA.<sup>133</sup> In the words of Mr. Justice Stevens, "The responsibilities for assessing the wisdom of such policy choices and resolving the struggle between competing views of the public interest are not judicial ones: Our Constitution vests such responsibilities in the political branches."<sup>134</sup>

Because the Supreme Court has granted *certiorari*<sup>135</sup> to review Order 451, the Court may once again be asked to cast an authoritative eye on the reviewing activities in administrative contexts, of its brethren on the courts of appeals.

*Richard E. Warzynski*

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133. *Chevron, USA, Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984).

134. *Id.* at 866.

135. Order 451, *supra* note 108.