REPORT OF THE JUDICIAL REVIEW COMMITTEE

I. Introduction

The 1995 federal court opinions reviewing the decisions of the Federal Energy Regulatory Commission (FERC or Commission) continue to reflect the problems associated with the transition from a regulated to a competitive market.

Several petitions for review were dismissed on procedural grounds for want of standing or ripeness. In addition, the familiar principles of agency deference, the filed rate doctrine, and the prohibition against retroactive ratemaking all figured prominently in many of the past year's decisions with respect to the gas pipeline industry. In part, this appears to reflect concerns relating to matching recovery of costs, particularly transition costs, to rates in an environment in which some prices are established through competitive means.

By contrast, significant challenges were made to costs imposed by the Public Utility Regulatory Policies Act (PURPA),[1] indicative perhaps of the sea of change which the electric power industry is currently undergoing, as well as the ongoing struggle between federal and state regulators as to primacy in imposing such costs on consumers. Similarly, a notable decision was issued by the First Circuit regarding the proper interpretation of the *Mobile-Sierra* doctrine; the D.C. Circuit issued a decision which presented significant consequences for the retroactivity of civil decisions. Finally, while dismissed for jurisdictional reasons, a district court challenge to the decision by the Michigan Public Service Commission to compel the retail wheeling of electric power may foreshadow a future area of judicial activity.

Each significant energy law decision from 1995 is briefly summarized below. Given the differences between the various industries, the cases are reported according to the various regulatory statutes under which they arose. However, given the cross applicability of many precedents, particularly for cases under the Federal Power Act (FPA) and the Natural Gas Act (NGA), an index organizing each case by issue is provided in Section III as an aid for further review.

II. Summary of Cases

A. *Natural Gas Act*

1. *El Paso Natural Gas Co. v. FERC*[2]

The D.C. Circuit dismissed the petition for review for lack of standing. The FERC had ruled that two LDCs regulated by the California Public

1. 16 U.S.C. §§ 2601-2645 (1994).
2. 50 F.3d 23 (D.C. Cir. 1995).

Utilities Commission (CPUC) under the NGA's[3] Hinshaw exemption would not become subject to the FERC's jurisdiction under sections 4 and 7 of the NGA by extending their pipeline network into Mexico. The court held that a competitor of these two LDCs could not show any necessary "injury in fact" in order to qualify for judicial review. First, although the pipeline competitor supplied gas upstream of the LDCs' facilities, it never suggested that the state regulations for these two LDCs were "currently any less advantageous to [this competitor] than those of the NGA."[4] Second, the court found it "wholly speculative" that this competitor would compete with these LDCs in Mexico.[5]

2. *Transcontinental Gas Pipe Line Corp. v. FERC*[6]

The D.C. Circuit remanded FERC orders which (1) granted Transcontinental Gas Pipe Line Corporation (Transco) certificate authority to provide additional natural gas transportation service to existing customers during peak and shoulder demand months, and (2) ruled that Transco's proposed straight-fixed variable (SFV) methodology should become effective a year after the start of service. Transco originally proposed the SFV rate design methodology, but the FERC rejected it in favor of the Modified Fixed-Variable (MFV) methodology. The rates based on MFV took effect, but on rehearing the FERC reversed itself and accepted the SFV rates to take effect a year after the start of service.

Various parties petitioned for review and the court held that the FERC's "tinkering" with the effective date of SFV, while failing to constitute "retroactive ratemaking," was nonetheless not supported by reasoned decisionmaking. The court found no basis for the FERC's conclusion that SFV rates should become effective a year after the start of service with the MFV rates being effective for only the initial year of service. The court rejected the FERC's rationale that adoption of SFV rates effective on the date of initial service would defeat the expectations of customers concerning their use of service under the MFV rates initially required, and that the pipeline took the risk of the resulting use of its system by providing service before final rate approval. The court remanded to the FERC for it to provide a "legitimate reason" for application of MFV rather than SFV rate design for all or part of the initial year of service or to restore the SFV rate design to the initial year of service.

3. *Transwestern Pipeline Co. v. FERC*[7]

The D.C. Circuit upheld the Commission's order on remand which determined the exact Purchased Gas Adjustment (PGA) amounts that Transwestern Pipeline Company (Transwestern) could collect from its cus-

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3. 15 U.S.C. § 717(c) (1994).
4. *El Paso Natural Gas Co.*, 50 F.3d at 26.
5. *Id.* at 27.
6. 54 F.3d 893 (D.C. Cir. 1995).
7. 59 F.3d 222 (D.C. Cir. 1995).

tomers. In so doing, the court denied petitions for review filed by both the pipeline, as well as its customers, represented by the CPUC.

The Commission approved a certificate application on May 11, 1988 filed by Transwestern which changed the pipeline's method for recovering its gas costs from a PGA charge to a Gas Inventory Charge (GIC). The certificate *inter alia* allowed Transwestern to direct bill its customers from its Account No. 191 if its customers nominated zero purchases under the new GIC regime. In *Transwestern Pipeline Co. v. FERC* (*Transwestern I*),[8] the D.C. Circuit held that this direct bill violated the filed rate doctrine by including gas costs that had been incurred before the GIC certificate was approved in May of 1988. Upon remand, with instructions from the court to develop a precise calculation of the relevant costs which accrued after May 11, 1988, the Commission issued the order to which the petitioners subsequently objected.

Transwestern protested the Commission's removal of $6.4 million (plus interest) from the total PGA costs which accrued before May 11, 1988 for amounts relating to pricing dispute settlement costs, prior period adjustments, and associated interest. Because Transwestern did not pay these amounts until after May 11, the pipeline argued that such costs were improperly excluded as they "accrued" after that date. The court upheld the Commission's rejection of this line of reasoning, noting that the Commission's decision was entirely consistent with the filed rate doctrine. The court's remand in *Transwestern I* "reflected the idea that the task before the Commission was not a mechanical one, and might well require adjustments to the figures produced by the Commission's historic methods for making adjustments to Account No. 191."[9] So long as the Commission remand calculations matched costs with the purchase of gas to which the costs related, the court observed, there was "no error in the Commission's choice."[10]

In contrast to Transwestern, the CPUC objected to the Commission's arithmetic on the grounds that it did not exclude enough from the PGA accounts. The CPUC claimed that the Commission's use of the "first in, first out" (FIFO) accounting methodology, whereby each dollar Transwestern recovered through its PGA after May 11, 1988 would retire the oldest dollar in the account as of that date, violated the *Transwestern I* mandate, the filed rate doctrine and the rule against retroactive ratemaking. The court rebuffed the CPUC's argument that the Commission should have relied upon the pre-existing sub-account system used in PGA accounting which made no distinction between whether PGA rates were recovering past or current cost accruals. While useful under an open-ended PGA accounting regime, this method proved unworkable under *Transwestern I*, which barred the pipeline from recovering costs before notice of its new direct billing GIC procedure. The court noted that the customers represented by the CPUC were put on notice that once the Commission

8. 897 F.2d 570 (D.C. Cir. 1990).
9. *Transwestern Pipeline Co.*, 59 F.3d at 225.
10. *Id.*

approved Transwestern's direct bill as of May 11, 1988, that they could be subject to as much of the direct bill as would ultimately prove lawful. This approval, and the subsequent legal challenges, the court concluded, "undermine[d] any claim that the delay in the unfolding of precise information violated the filed rate doctrine or the rule against retroactive ratemaking."[11]

4. *National Fuel Gas Supply Corp. v. FERC*[12]

The D.C. Circuit denied National Fuel Gas Supply Corporation's (National Fuel) petition for review of a Commission order which retroactively applied the court's vacatur of Order No. 436,[13] effectively nullifying National Fuel's right to reduce its contract demand (CD) obligation to purchase gas from Tennessee Gas Pipeline Company (Tennessee).

While National Fuel did not deny that the court's vacatur of Order No. 436 in *Associated Gas Distributors (AGD)*,[14] and the Commission's subsequent refusal in Order No. 500 to reinstate the CD reduction provision extinguished its claim to such reductions, it nevertheless argued that its reliance upon this aspect of Order No. 436 overcame the legal presumption for retroactivity. After surveying recent Supreme Court decisions concerning judicial retroactivity, the court dismissed the petition.

Judge Ginsburg noted that courts could depart from the well settled rule that judicial decisions must be applied retroactively only in the most compelling circumstances. Citing *Reynoldsville Casket Co. v. Hyde*,[15] he identified four instances where a remedy other than retroactive application of a judicial decision could be properly sought:

> [Where there is] (1) an alternative way of curing the constitutional violation, or (2) a previously existing, independent legal basis (having nothing to do with retroactivity) for denying relief, or (3) as in the law of qualified immunity, a well-established legal rule that trumps the new rule of law, which general rule reflects both reliance interests and other significant policy justifications, or (4) a principle of law . . . that limits the principle of retroactivity itself.[16]

After determining that *Hyde* governed in the context of agency action, the court concluded that National Fuel had not presented any equity arguments, or any claims implicating one of the four above circumstances, which could otherwise justify relief from the retroactive application of *AGD*.

11. *Id.* at 229.
12. 59 F.3d 1281 (D.C. Cir. 1995) (*National Fuel*).
13. Associated Gas Distribs. v. FERC, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988).
14. 824 F.2d at 981.
15. 115 S. Ct. 1745 (1995).
16. *National Fuel*, 59 F.3d at 1288 (quoting *Hyde*, 115 S. Ct. at 1751).

5. *Northwest Pipeline Corp. v. FERC*[17]

In denying a petition filed by Northwest Pipeline Corporation (Northwest), the Tenth Circuit held that a Commission order requiring refunds of overcharges does not violate the rule against retroactive ratemaking.

Northwest objected to a Commission order which, in its view, improperly interpreted the phrase "total annual volumes" contained in the fuel reimbursement percentage (FRP) provision of Northwest's tariff. The FRP provision required each unbundled shipper on Northwest's system to compensate the pipeline for its pro rata share of the system fuel. Customers receiving bundled sales or storage service from Northwest were not required to pay the FRP charge. Nonetheless, the Commission determined that Northwest improperly excluded the volumes which these non-paying bundled customers transported through its system, thereby increasing the pro rata share of the FRP which the unbundled customers were obligated to pay. Language in the FRP tariff provision specifying that each unbundled customer's pro-rata share should be calculated using the "total annual volumes" necessarily included bundled transportation volumes. Pursuant to this rationale, the Commission directed Northwest to refund the FRP overcharges to the affected unbundled customers.

Despite Northwest's position on appeal that since the FRP provision was only contained in its unbundled transportation tariff, "total annual volumes" only referred to unbundled volumes, the court found the Commission's reasoning persuasive. Observing that Commission decisions interpreting contractual language are entitled to judicial deference, the court concluded that the Commission's interpretation was rational.

The court also dismissed Northwest's contention that the Commission's order requiring Northwest to recalculate the FRP was made pursuant to section 5 of the NGA, and therefore could only yield prospective relief. The court noted that since the pipeline's original filing proposing the unbundled tariff containing the FRP provision, as well as its subsequent modifications to the same provision, were all filed pursuant to section 4 of the NGA, the Commission could properly order refunds of the FRP overcharges under section 4(e). Indeed, since the Commission "did not effect a modification to Northwest's rate, or the FRP calculational mechanism," its section 5 authority was not invoked. Thus, the court concluded, "because Northwest was on notice that its filed FRP adjustment may be subject to refund, the Commission's ordering of a refund did not violate the rule against retroactive ratemaking."[18]

6. *Mississippi Valley Gas Co. v. FERC*[19]

The D.C. Circuit dismissed the petition for review without prejudice as unripe. The petitioner, a captive pipeline customer, challenged as unduly discriminatory Commission orders approving settlement agreements in

17. 61 F.3d 1479 (10th Cir. 1995).
18. *Id.* at 1493.
19. 68 F.3d 503 (D.C. Cir. 1995).

which a pipeline reduced the estimated throughput to reflect its selective discounting to meet gas-on-gas (inter-pipeline) competition.

The court deferred ruling on the legality of such discounts, and noted that it had not previously decided that legal issue. The court also declined to reach the issue here, because it found the petition not ripe for review. The court concluded that the customer may still obtain relief from the rate increases in the course of hearings pending at the Commission. Thus the court made clear that the customer may challenge the pipeline's throughput reduction once the Commission had established the pipeline's final rates.

7. *Western Resources, Inc. v. FERC*[20]

The D.C. Circuit denied petitioner's challenge and affirmed the Commission orders approving a direct bill of take-or-pay costs incurred by Transwestern Pipeline Company (Transwestern) over objections by petitioner that (1) it did not have timely notice of potential liability for the direct bill, and (2) imposition of the direct bill violated the filed rate doctrine and the prohibition against retroactive ratemaking.

To implement Order 500, Transwestern filed tariff provisions on October 17, 1988, which resulted in a Commission order of December 16, 1988 allowing Transwestern to recover take-or-pay costs by imposing a direct bill based on purchased gas deficiencies.[21] However, the D.C. Circuit held that the purchased gas deficiency method violated the filed rate doctrine.[22] The Commission then issued Order 528,[23] authorizing pipelines to allocate the take-or-pay burden in accordance with buyers' "current contract demand."[24] Transwestern, therefore, refiled its tariff provisions for the recovery of take-or-pay costs, seeking in effect to have the Commission's December 16, 1988 order replaced with one permitting a direct bill based on its customers' 1988 contract demand. The Commission approved this filing in *Transwestern Pipeline Co.*[25]

The petitioner, a customer of Williams Natural Gas Company (Williams), which was a customer of Transwestern, sought review of these orders. The petitioner was subject to a share of the take-or-pay costs allocated to Williams. The petitioner first argued that the Commission's 1991 approval of the direct bill was unlawful because the 1988 order it replaced failed to give timely notice. The petitioner contended that the 1988 order was conditional on Transwestern withdrawing a judicial appeal of an earlier Commission ruling and that the appeal was not withdrawn until after the petitioner's supplier, Williams, had ceased to be a Transwestern customer.

20. 72 F.3d 147 (D.C. Cir. 1995).

21. *Transwestern Pipeline Co.*, 45 F.E.R.C. ¶ 61,427 (1988).

22. *See* Associated Gas Distribs. v. FERC, 893 F.2d 349, 354-57 (D.C. Cir. 1989).

23. *Mechanisms for Passthrough of Pipeline Take-or-Pay Buyout and Buydown Costs*, 58 F.E.R.C. ¶ 61,163 (1990).

24. *Id.* at 61,547.

25. 54 F.E.R.C. ¶ 61,356 (1991), *reh'g granted in part and denied in part*, 64 F.E.R.C. ¶ 61,145 (1993), *reh'g denied*, 66 F.E.R.C. ¶ 61,287 (1994).

The court, however, held that this argument "does not get past the starting gate," since the petitioner clearly had notice of Transwestern's election to withdraw the appeal, and thereby satisfy the condition of the 1988 order, well before Williams left the Transwestern system.

The petitioner further argued that the method for determining the direct bill in the 1991 order was so different from that approved in 1988 that there was inadequate notice of that direct bill until after Williams had left the Transwestern system. The petitioner contended that the filed rate doctrine precludes Transwestern from allocating costs in a 1991 order on the basis of 1988 contract demand. The court rejected the argument ruling that the presence of the judicial challenge adequately placed petitioner on notice that the rate applicable to its supplier was not final and was subject to change by virtue of correcting the legal error.[26]

Finally, the petitioner argued that, even if the Commission could retroactively impute the contract demand method of allocating take-or-pay costs to the 1983 order as a correction of its legal error, the 1988 order could only apply to take-or-pay liabilities accruing after the 1988 order. The court rejected this argument as well, ruling that the Commission's treatment of take-or-pay costs as "current" as of the date of filing for their recovery was "an acceptable cost-spreading decision requiring those who benefit from the transition to a competitive natural gas market to absorb some of the costs."[27]

B. *Natural Gas Policy Act*

1. *NICOR Exploration Co. v. FERC*[28]

The Fifth Circuit vacated a FERC order granting a gas producer authority to collect incentive-based stripper well rates for gas pursuant to section 108 of the Natural Gas Policy Act (NGPA).[29] The Fifth Circuit held that the order was inconsistent with Oklahoma contract law and that the FERC, by applying Opinion No. 77,[30] improperly relieved the producer of his burden of proving by a preponderance of the evidence that area rate clauses of gas supply contracts authorized such rates. The court also held that it does not generally defer to the FERC's interpretation of gas supply contracts unless it relied on its factual or technical expertise in reaching its conclusions.

2. *Marathon Oil Co. v. FERC*[31]

The D.C. Circuit denied a petition for review on standing grounds. The petitioners challenged the Commission's decision not to accept state

26. *Western Resources*, 72 F.3d at 151 (citing *Public Util. Comm'n of Cal. v. FERC*, 988 F.2d 154 (D.C. Cir. 1993) (*Transwestern III*)). *See also* Natural Gas Clearinghouse v. FERC, 965 F.2d 1066 (D.C. Cir. 1992).

27. *Western Resources*, 72 F.3d at 152 (citing *Transwestern III*, 988 F.2d at 166-69).

28. 50 F.3d 1341 (5th Cir. 1995).

29. 15 U.S.C. § 3318 (1994).

30. *Independent Oil & Gas Ass'n of W. Va.*, 10 F.E.R.C. ¶ 61,214, at 61,397 (1980).

31. 68 F.3d 1376 (D.C. Cir. 1995).

agencies' determinations that their wells produce tight formation gas eligible for higher incentive pricing under the NGPA. They contended that the Commission's actions prejudiced their chances of receiving a tax credit for this gas under section 29 of the Internal Revenue Code.

The court determined that the petitioners lacked the injury-in-fact necessary for standing under Article III. The court found that the Commission's pricing determinations in this case were based on the fact that the wells were "recompletions" not eligible for incentive pricing under the NGPA, not on a factual determination of whether the gas was produced from a tight formation; thus the Commission did not take a position on the state agencies' determination that the wells in question produced tight-formation gas. The court found no reason why the IRS would not accept the state agencies' findings and simply ignore the Commission's decision, because the Commission's decision had no necessary legal significance on the IRS' decision whether to grant the tax credit. Since the tax treatment was the only injury petitioners claimed, the court found that the Commission's decision had not caused them the legally cognizable injury necessary for standing.

3. *Grynberg v. FERC*[32]

The D.C. Circuit vacated and remanded Commission orders interpreting natural gas contracts between a producer and a pipeline. At issue was whether the producer's contract had dedicated certain gas to interstate commerce, in which case the maximum lawful price for certain prior years under the NGPA would be lower than the price provided under a later contract with another pipeline purchaser. The Commission decided that the producer had committed the gas to interstate commerce.

Although noting that the Commission's interpretation of the contract was entitled to deference, the court nonetheless granted the producer's petition for review, because it concluded that the Commission's interpretation of the contract at issue was unreasonable. Because the Commission had not adequately supported its reading of the contract, the court vacated the Commission's orders and remanded for reconsideration.

4. *ANR Pipeline Co. v. FERC*[33]

The D.C. Circuit granted a petition for review of Commission orders allowing an intrastate pipeline to use "blended rates" for the interstate transportation service it provides under section 311 of the NGPA.[34] Section 311 requires such rates to be "fair and equitable" and not exceed an amount "reasonably comparable" to the rates an interstate pipeline would charge for the same service.[35]

32. 71 F.3d 413 (D.C. Cir. 1995).
33. No. 94-1705, 1995 U.S. App. LEXIS 34738 (D.C. Cir. Dec. 12, 1995).
34. 15 U.S.C. § 3371 (1994).
35. *Id.* § 3371(a)(2)(A), (B)(i).

The petitioner, an interstate pipeline subject to regulation under the NGA, is required by Commission regulations adopted in Order No. 636 to use straight fixed-variable (SFV) rate design, which requires all fixed transportation costs to be recovered in the reservation charge. The interstate pipeline alleged that allowing its intrastate competitor to use blended rates for service under section 311 of the NGPA was anticompetitive, because the blended rates allowed its competitor to shift some fixed costs to the usage charge and thus discount its reservation charge.

The court reversed the Commission's orders approving the blended rates because the Commission did not explain why the same policy considerations that led it to adopt SFV rate design in Order No. 636 did not carry over to its approval of rates under section 311 of the NGPA.

C. *Outer Continental Shelf Lands Act*

In *Shell Oil Co. v. FERC*,[36] the D.C. Circuit upheld a FERC order requiring an oil pipeline located entirely on the Outer Continental Shelf (OCS) to provide "open and nondiscriminatory access" under section 5 of the Outer Continental Shelf Lands Act (OCSLA)[37] to a competitor. The court held that original jurisdiction over the pipeline owners' objections to the FERC's order lay in the federal district courts, but a district court could transfer the action to a federal circuit court reviewing a related order. Deferring under the *Chevron*[38] doctrine, the court upheld the FERC's interpretation of the OCSLA.

The court also dismissed for lack of standing the competitor's parallel petition, which challenged the FERC's holding that the Interstate Commerce Act (ICA)[39] did not apply to pipelines located wholly on the OCS. Since the FERC granted the competitor the relief it sought—access to the pipeline—it could not complain about the FERC's disclaimer of ICA jurisdiction over the pipeline.

D. *Interstate Commerce Act*

In *OXY USA, Inc. v. FERC*,[40] the D.C. Circuit upheld the Commission's decision to change the Quality Bank valuation methodology pertaining to petroleum shipments on the Trans Alaska Pipeline System (TAPS); yet, it also remanded the orders on review to the extent that there were some flaws in the Commission's methodology.

The Commission's order was challenged by a host of petroleum shippers that objected to the Commission's use of a new "assay" methodology to value TAPS petroleum shipments for the purpose of making monetary adjustments among shippers to compensate for commingling in the pipeline.

36. 47 F.3d 1186 (D.C. Cir. 1995).
37. 43 U.S.C. § 1334(f) (1988).
38. Chevron U.S.A., Inc. v. NRDC, 467 U.S. 837 (1984).
39. 49 U.S.C. app. §§ 1-2701 (1988).
40. 64 F.3d 679 (D.C. Cir. 1995).

The court rejected several petitioners' claims that the Commission had to show that the changes in circumstances justifying the adoption of the new assay methodology were unforeseeable at the time of the original decision adopting the old gravity methodology. Rather, observed the court, no "finding of unforeseeability is required before the Commission may reach the conclusion that a rate that was previously just and reasonable is no longer so."[41]

The court however agreed with the petitioners' arguments that the Commission's inconsistent treatment of some of the individual components, or "cuts," which went into the TAPS common stream was arbitrary and capricious.

> [I]f the agency chooses to value some cuts of petroleum at the prices they command in the market without the benefit of processing, as it appears to have done, it must attempt to the extent possible, to value all cuts at the price they would command without processing. It cannot, consistent with the requirement of reasoned decisionmaking, value some cuts precisely and others haphazardly.[42]

The court also agreed with the Commission's determination that the prohibition against retroactive ratemaking required that changes in the Quality Bank valuation methodology be prospective only, and thus the parties contesting this issue were not entitled to refunds. A Commission investigation to change an oil pipeline's rates, pursuant to section 13(2) of the ICA,[43] does not give the Commission authority to issue "orders for the payment of money." Although refund authority is granted under section 15(7) of the ICA, this provision is triggered when the filing party requests a change in rates; here, the Commission, not the parties, initially sought a change in the gravity methodology of the Quality Bank. While the parties' original filing at the Commission proposed increases in the Quality Bank adjustments, this filing put no one on notice that there may be a potential change to the assay methodology. Thus, a retroactive change precipitating refunds would have violated the filed rate doctrine. "Because any refund would have constituted impermissible retroactive ratemaking, the Commission quite properly applied the assay methodology prospectively."[44]

E. *Federal Power Act*

1. *Municipal Resale Service Customers v. FERC*[45]

The Sixth Circuit upheld a FERC order rejecting a complaint by various municipal utilities that the seller's wholesale rates, based upon the full cost of coal that it had obtained from its subsidiaries with approval rather than upon the prevailing market price of coal, violated the FERC's "comparable market test" under the FPA.[46] Although the court noted the

41. *Id.* at 690.
42. *Id.* at 694.
43. 49 U.S.C. app. § 13(2) (1988).
44. *OXY USA, Inc.*, 64 F.3d at 700.
45. 43 F.3d 1046 (6th Cir. 1995).
46. 16 U.S.C. §§ 824-824m (1994).

municipalities could raise an issue that they had not raised below where the grounds arose from an appellate decision issued after the FERC denied their rehearing, the petition for review was nonetheless denied. The court agreed that the FERC could not find the seller's costs for this "captive" coal to be excessive because, pursuant to its authority under the Public Utility Holding Company Act (PUHCA),[47] the Securities and Exchange Commission (SEC) had approved the purchase prices.

2. *Thomas Hodgson & Sons v. FERC*[48]

The First Circuit reversed the FERC's order that it had licensing jurisdiction over the petitioner's hydroelectric generating plant on a non-navigable river. The plant was constructed before the "grandfather clause" amendment in 1935 to the FPA's licensing provisions, but was shut down for 12 years between 1969 and 1981, until coterminous with PURPA's enactment, the plant again became profitable to operate. The court refused to give any *Chevron* deference to the FERC as the Commission was purporting to interpret only judicial opinion, rather than a statute, and its holding was wholly contrary to the legislative intent.

3. *Town of Norwood v. FERC*[49]

The D.C. Circuit dismissed a petition for review of a FERC order approving an electric utility's request for a rate increase based in part on the switch from a cash to an accrual basis in accounting for post-retirement benefits other than pensions (PBOP).

In 1990, the Financial Accounting Standards Board (FASB) instructed companies to switch to accrual accounting for PBOPs, requiring companies to currently account for the post-retirement benefits they expect to pay in the future to their current employees. Subsequently, New England Power requested a raise in rates based in part on the switch to accrual accounting for PBOPs. The Town of Norwood challenged the approval of accrual accounting for ratemaking purposes.

The court rejected Norwood's arguments by noting that long-range estimates are an integral feature of ratemaking and financial analysis in general, and that the court has regularly approved reliance on admittedly imperfect future cost estimates. The court also found that the "transition obligation"—the accumulated but unrecognized obligation to current employees—was neither violative of the principle of matching the costs of producing a service with the ratepayers responsible for those costs, nor the prohibition against retroactive ratemaking. The court found that New England Power had not shifted any costs that it failed to collect in the past since it had always planned to collect these costs from future ratepayers; the accrual accounting only shifted the timing for the collection of PBOP costs among future ratepayers.

47. 15 U.S.C. §§ 79-79z-6 (1994).
48. 49 F.3d 822 (1st Cir. 1995).
49. 53 F.3d 377 (D.C. Cir. 1995).

4. *Northeast Utilities Service Co. v. FERC (Northeast II)*[50]

The First Circuit denied a petition for review concerning whether the FERC had complied with the court's mandate in *Northeast I*[51] and applied the "public interest" test in ordering a modification to a wholesale electric power contract. The court found that the FERC gave sufficient thoughtful consideration to the public interest in reviewing its previously ordered contract modification, thus complying with the court's direction in the prior appeal.

In the FERC orders underlying *Northeast I*, the FERC examined the terms and conditions of a wholesale contract for power from a nuclear plant pursuant to section 206(a) of the FPA. The FERC found that the contract might unduly discriminate against entities not parties to it, and there was no genuine arms-length bargaining as the agreement was negotiated at a time when the parties were about to merge and assume identical interests. The Commission therefore ordered three changes in the contract to bring it within the "just and reasonable" standard of section 206(a). In *Northeast I*, the court remanded to the FERC to reconsider its modification of the contract under the "public interest" standard of the *Mobile-Sierra* doctrine, rather than under the "just and reasonable" standard.

In seeking review of the Commission's orders on remand, the utility contended that the Commission did not comply with the mandate, but instead created a new version of the public interest standard which is more flexible and less stringent than the "practically insurmountable" burden imposed on it by the public-interest standard as interpreted by the D.C. Circuit in *Papago Tribal Utility Authority v. FERC*.[52] The First Circuit held, however, that *Papago*, like *Mobile* and *Sierra*, involved a seller utility's attempt to increase a contract rate by claiming that the rate was so low as to be contrary to the public interest; the court accordingly concluded that those cases did not define the public interest considerations applicable in other factual situations. Thus, the court concluded, the public interest standard was not "practically insurmountable" in all circumstances.[53]

The court then concluded that the Commission's orders on remand had articulated sufficient public interest grounds to support the modification of the contract in the distinctly different facts of this case. Here the Commission had modified, as contrary to the public interest, provisions of a wholesale power contract between two utility affiliates that would have automatically adjusted the return on equity in future years (in violation of FERC policy) and would have automatically included in the wholesale formula rate, without an opportunity for FERC review, nuclear decommissioning expenses determined under state law. The FERC deleted the automatic return adjustment mechanisms and required the decommissioning expenses to be filed for its review under section 205 of the FPA. The court

50. 55 F.3d 686 (1st Cir. 1995).

51. Northeast Utils. Serv. Co. v. FERC, 993 F.2d 937 (1st Cir. 1993) (*Northeast I*).

52. 723 F.2d 950 (D.C. Cir. 1983), *cert. denied*, 467 U.S. 1241 (1984).

53. *Northeast II*, 55 F.3d at 692-93.

concluded that these modifications were warranted in order to protect third parties from harm.[54]

5. *Indiana Municipal Power Agency v. FERC*[55]

The D.C. Circuit denied the petition for review of a FERC order determination that the Indiana-Michigan Power Company (Indiana Michigan) did not violate the FPA, FERC regulations, or a FERC-approved settlement, by including certain costs arising from fuel supply contracts in its wholesale electricity rates.

Indiana-Michigan previously had acquired low sulfur coal reserves anticipating that this coal would provide a reliable supply of "clean" fuel necessary to satisfy federal and state air quality standards. Actual demand for the coal fell far below projections, however, resulting in significant losses for Indiana-Michigan over several years. Indiana-Michigan sold the mines and signed contracts with the buyer to purchase coal. Indiana-Michigan sought to pass on to ratepayers the full cost of the coal under those contracts. Certain wholesale ratepayers challenged the costs as inflated, arguing that Indiana-Michigan entered into the contracts to induce the purchase of the mines and that the cost of the coal contained a "premium" or "sweetener."

The D.C. Circuit refused to disturb the Commission finding that Indiana-Michigan's rates were in compliance with section 205 of the FPA, as the utility demonstrated that the prices paid for the coal were not excessive under the comparable market price test.

6. *Cajun Electric Power Cooperative, Inc. v. FERC*[56]

The D.C. Circuit denied a petition for review of a Commission order interpreting a transmission contract between a public utility company and a generation and transmission cooperative. At issue was whether the cooperative could demand delivery at points that are not within a member's system. The Commission ruled against the cooperative, concluding that the contract was intended to provide transmission only for the cooperative's normal load growth, not for sales outside its system.

The Commission originally reached that decision by finding that the contract language was unambiguous, but the D.C. Circuit found the contract was ambiguous and remanded.[57] In that decision, the court reviewed the Commission's contract interpretation by using the same two-step process adopted by the Supreme Court in *Chevron*[58] for judicial review of agency interpretation of statutes. Applying the first step of that process—and thus reviewing the contract language *de novo* without according the FERC's interpretation any deference—the court found that the contract

54. *Id.* at 689-92.
55. 56 F.3d 247 (D.C. Cir. 1995).
56. 66 F.3d 364 (D.C. Cir. 1995) (*Cajun II*).
57. Cajun Elec. Power Coop., Inc. v. FERC, 924 F.2d 1132 (D.C. Cir. 1994) (*Cajun I*).
58. 467 U.S. 837 (1984).

was ambiguous, and it remanded so that the FERC could examine evidence of the bargaining history proffered by the cooperative.

After holding an evidentiary hearing, the ALJ ruled against the cooperative, and the Commission affirmed. This time the court affirmed, stating that the FERC's interpretation of the contract was entitled to deference even if the FERC pointed to no specific public policy supporting its interpretation: "So long as FERC adequately explains why it interprets the contract as it does, we assume that its explanation is drawn from its statutory responsibility and experience."[59] The court upheld the FERC's interpretation of the contract as reasonable.

7. *City of New Orleans v. FERC*[60]

The D.C. Circuit denied petitions for review of Commission orders allowing the spin-off of two electricity generating plants by a public utility company. Both the utility and a municipality challenged the Commission's decision to address the prudence of the spin-off only as to its current effect on rates up until such time as the utility will need to purchase new capacity. Although disagreeing on the merits, both petitioners argued that the Commission must now consider the reasonableness of the ultimate effect on the utility's rates of the additional replacement capacity. In deferring a ruling on this issue, the Commission determined that the ultimate effect of replacement costs on ratepayers will depend on several speculative factual matters.

The court held that the Commission's decision to defer any prudence determination affecting rates based on replacement capacity until such time as that occurs was a matter within the Commission's discretion and was reasonable. The court noted that the Commission was obligated to address the prudence of replacement capacity costs when and if they are actually incurred.

F. Public Utility Regulatory Policies Act

1. *Freehold Cogeneration Associates v. Board of Regulatory Commissioners of New Jersey*[61]

The Third Circuit held that section 210 of PURPA[62] preempted the New Jersey Board of Regulatory Commissioners' orders requiring modification of a previously approved contract between a public utility and a cogenerator. The court also held that a federal district court has federal question jurisdiction over such a preemption claim.

In this case a cogenerator and utility had entered into a long-term power sale contract with the price determined by 1989 estimates of the utility's avoided costs. The state commission approved the contract in 1992. In 1994, however, seeking to encourage buyouts and other remedial

59. *Cajun II*, 66 F.3d at 366.
60. 67 F.3d 947 (D.C. Cir. 1995).
61. 44 F.3d 1178 (3d Cir. 1995).
62. 16 U.S.C. § 824a-3 (1994).

measures of uneconomical power-supply contracts, the state commission directed the parties to renegotiate the purchase price or negotiate a buyout. Failure to do so would result in the commission commencing proceedings to consider other courses of action.

The cogenerator filed suit in federal district court, claiming that section 210 of PURPA preempted the state commission's order. Without reaching the merits, the district court dismissed the action for lack of jurisdiction. The Third Circuit reversed, holding not only that the district court had jurisdiction, but also that section 210 of PURPA preempted the state commission's action.

The court concluded that it had federal question jurisdiction over a claim that a state commission's action is preempted by federal law. The court further concluded that the review provisions of section 210(g) of PURPA did not apply to the claim that the Johnson Act[63] did not deprive the district court of jurisdiction over a statutory preemption claim, and that the forum selection provision of the parties' contract did not govern the preemption claim.[64]

As to the merits, the Third Circuit concluded that the matter was ripe for review. Since the parties had fully briefed the merits and further delay occasioned by a remand would threaten the viability of the cogeneration project, exceptional circumstances warranted the court reaching the merits of the claim even though the district court had not.[65] The court then held that, once the commission had approved the QF contract as consistent with the utility's avoided cost, any commission action pursuant to state law to reconsider that approval or deny the pass-through of those costs to the utility's customers was preempted by federal law.[66]

2. *Industrial Cogenerators v. FERC*[67]

The D.C. Circuit concluded that it lacked jurisdiction to review a FERC order that vacated a prior declaratory order interpreting the Commission's PURPA regulations. Several industrial firms engaged in electric power cogeneration challenged a Florida Public Service Commission order purporting to implement various FERC regulations on the rates electric utilities may charge cogeneration facilities for power. Pointing to the two-part enforcement scheme set forth in section 210 of PURPA, the court held that a complaining party must seek enforcement against the state agency in a separate action in federal district court if the FERC refused to commence enforcement proceedings. Accordingly, the petitioner's efforts to obtain court of appeals review was determined to be contrary to PURPA's enforcement scheme.

63. 28 U.S.C. § 1342 (1994).

64. *Freehold Cogeneration Assocs.*, 44 F.3d at 1183-87.

65. *Id.* at 1187-90.

66. *Id.* at 1192.

67. 47 F.3d 1231 (D.C. Cir. 1995).

3. *New Charleston Power I v. FERC*[68]

The owner of a cow manure-burning small power production facility, that was a QF under PURPA, sought review of FERC orders in which the FERC refused to waive the rule that no more than 25% of a QF's total energy input be fossil fuel. The owner sought a waiver while repairs were made to its facility to enable it to safely burn cow manure. According to the owner, repairs were made necessary because heavy rains caused manure to become contaminated with mud so as to exacerbate facility problems. The FERC found that (1) while the wet manure may have exacerbated the problems, it was not the sole cause, and (2) there was no assurance that, after the waiver period, the QF would begin generating electricity from cow manure with any regularity given previous operational problems. The court held that the FERC acted within its discretion in denying the owner's request to waive the 25% rule.

4. *Independent Energy Producers Ass'n v. California Public Utilities Commission*[69]

Upon reversal and remand by the Ninth Circuit in *Independent Energy Producers Ass'n v. California Public Utilities Commission*,[70] the Northern District Court of California permanently enjoined the CPUC from implementing or enforcing certain aspects of an agency program for the monitoring and enforcement of the FERC's PURPA regulations. It found that the FERC exercises exclusive authority over QF status determinations under section 201 of PURPA for the purpose of conferring on QFs the benefits of section 210 of PURPA. The court further found that federal regulations provide that QFs are entitled to deliver energy to utilities at an avoided cost rate calculated at the time the contract is signed or at the time of energy delivery. The court held that the CPUC program for utility monitoring and enforcement of the FERC standards is preempted by PURPA insofar as it authorized (1) the CPUC to determine that a QF is not in compliance with the FERC's operating and efficiency standards in order to impose a reduced avoided cost rate on that QF below that specified in the QF's purchase power contract; and (2) the CPUC to disconnect from parallel operation a "noncomplying" QF, thereby preventing a determination by the CPUC that a QF is not in compliance with the FERC's operating and efficiency standards.[71]

68. 56 F.3d 1430 (D.C. Cir. 1995).

69. No. C-91-2644 MHP, 1995 U.S. Dist. LEXIS 7349 (N.D. Cal. May 30, 1995).

70. 36 F.3d 848 (9th Cir. 1994).

71. *See* 18 C.F.R. § 292.303(c) (1995) (requiring electric utilities to interconnect with QFs as necessary to accomplish sales and purchases with QFs).

5. *Hopewell Cogeneration Partnership v. State Corporation Commission*[72]

The Virginia Supreme Court addressed the question of whether gross receipts taxes (GRTs) should be included in a utility's "avoided costs" for purposes of its purchases from QFs under PURPA. The court upheld an order disallowing GRT expenses for those contracts that were not specifically ordered or approved by either the FERC or the state commission. While section 292.304 of the PURPA regulations permits avoided cost to be determined based on factors at the time the contract is executed, rather than the time the power is actually delivered, the state commission's authority is not completely emasculated. The court observed that PURPA did not prohibit the state commission from disallowing expenses such as GRTs that it determined to be unreasonable at the time the contracts were executed.

G. *Miscellaneous*

1. *Devils Lake Sioux Indian Tribe v. North Dakota Public Service Commission*[73]

Addressing issues of tribal sovereignty, the court held that an Indian tribe could determine who would supply electric service to tribe-owned businesses located on Indian owned or trust land, without regard to any state public service commission regulations, and that the state agency could not sanction any utility for providing such service, but that the state agency could regulate electric service to tribe-owned businesses located elsewhere.

2. *Alliance for Clean Coal v. Bayh*[74]

The court struck down a portion of Indiana's Environmental Compliance Plans Act as unconstitutional under the Commerce Clause.[75] That statute improperly favors Indiana coal producers by requiring the Indiana Utility Regulatory Commission to impose restrictions on its approval of a utility's compliance plan under the act based on the plan's effects on the Indiana coal industry.

3. *Detroit Edison Co. v. Strand*[76]

The court dismissed for lack of jurisdiction a declaratory judgment action in which Detroit Edison challenged the authority of the Michigan Public Service Commission (MPSC) to compel Detroit Edison to engage in retail wheeling. The court held that the MPSC was immune from suit under the Eleventh Amendment. Further, although the court found that it retained jurisdiction over the individual commissioners named as defendants, certain federal claims were not ripe for adjudication because the

72. 453 S.E.2d 277 (Va. 1995).
73. 896 F. Supp. 955 (D.N.D. 1995).
74. 888 F. Supp. 924 (S.D. Ind. 1995).
75. IND. CODE ANN. §§ 8-1-27-6(b)(6), -8(1)(D), -20 (1991 & Supp. 1994).
76. No. 5:94-CV-123, 1995 U.S. Dist. LEXIS 7262 (W.D. Mich. May 8, 1995).

MPSC had yet to finally determine whether, and under what circumstances, it would exercise its powers to compel retail wheeling.

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