

REPORT OF THE JUDICIAL REVIEW COMMITTEE

I. INTRODUCTION

This Report summarizes the major energy cases decided by judicial review in 1999, with a focus on cases at the appellate level.

II. ADMINISTRATIVE LAW

A. Requirement to Explain Departure from Prior Policy

In *Panhandle Eastern Pipe Line Co. v. FERC*,¹ the D.C. Circuit remanded the Federal Energy Regulatory Commission's (FERC or Commission) orders on the grounds that the agency did not provide a reasoned explanation for departing from its prior policy. The court found that the FERC's rejection of an interstate pipeline's proposed tariff provision relating to its construction of pipeline interconnections, and subsequent requirement that it adopt language reflecting new criteria, reflected a change in policy. Instead of adhering to its prior policy of requiring pipelines to construct interconnects on a case-by-case basis only if the pipeline had previously done so for similarly situated parties, the FERC instead required the pipeline to do so "for any party willing to pay the reasonable costs and expenses of the construction and who meets the other conditions of Panhandle's interconnect policy as modified by the Commission."²

Although the FERC did not acknowledge that it had departed from its prior policies, the court concluded that it had. The court noted that if the FERC's orders were upheld, the pipeline "would be bound to construct an interconnect for any requester falling within its FERC-modified tariff, even if the requester were not similarly situated to any party for whom [the pipeline] had previously built an interconnect."³ Because the FERC failed to explain the reason for deviating from its prior policy, the court remanded for a better explanation.

B. Rehearing Requirement

The D.C. Circuit reaffirmed the statutory rehearing requirement of the FERC orders in *Granholm v. FERC*.⁴ The court held that section 313(a) of the Federal Power Act (FPA) barred the petitioner, a state attorney general on behalf of the state's Department of Natural Resources, from seeking review of the FERC orders involving the issuance of a hydroelectric power license. The petitioner failed to apply for rehearing of a FERC order on remand from the D.C. Circuit, which did not change the FERC's prior ruling. The court determined the fact that the proceeding was on remand, as opposed to an initial proceeding, was of no consequence: "Nothing in § 313(a) exempts Commission orders issued on remand from the rehearing requirement."⁵

The Ninth Circuit, in *American Rivers v. FERC*,⁶ ruled that it did not have jurisdiction over a petition for review of a FERC refusal to initiate consultation procedures under the Endangered Species Act. Rather than seeking rehearing of

1. *Panhandle E. Pipe Line Co. v. FERC*, 196 F.3d 1273 (D.C. Cir. 1999).

2. *Panhandle*, 196 F.3d at 1274.

3. *Id.* at 1275.

4. *Granholm v. FERC*, 180 F.3d 278 (D.C. Cir. 1999).

5. *Id.* at 281.

6. *American Rivers v. FERC*, 170 F.3d 896 (9th Cir. 1999).

an actual FERC order, the petitioners sought rehearing of an agency refusal to respond to a petition to initiate consultation. The court concluded that "[b]ecause appellate jurisdiction is dependent on the issuance of an order by FERC, we lack jurisdiction of the petition."⁷

C. Ripeness

In *New York State Electric & Gas Corp. v. FERC*,⁸ the D.C. Circuit dismissed a pipeline customer's petition for review of the FERC orders approving the pipeline's expansion as unripe. The orders being challenged found that, absent changed circumstances, the pipeline would be permitted to roll the costs of its expansion into its systemwide rates in its next rate case. On appeal, the petitioner contended that the FERC's presumption in favor of rolled-in rates would control the pipeline's next rate case, and the FERC therefore should have proceeded under section 4 of the Natural Gas Act (NGA). The court concluded that since the petitioner would have the opportunity to challenge rolled-in rates in the pipeline's next rate proceeding, the petition should be dismissed.

III. ANTITRUST LAW

A. *Indeck Energy Services, Inc. v. Consumers Energy Co.*⁹

Indeck alleged Consumers Energy violated sections 1 and 2 of the Sherman Act and section 3 of the Clayton Act, by executing long-term exclusive discount contracts to provide electricity to General Motor's (GM) Flint, Michigan plant and seventeen other large electricity consumers. The court granted summary judgment for Consumers Energy, finding that the Michigan Public Service Commission's (MPSC) regulation of these contracts qualified them for state action immunity under the two-prong test established in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*¹⁰ The court further ruled that, as to the other seventeen contracts, Indeck lacked standing to sue because it did not suffer antitrust injury as defined in *Brunswick Corp. v. Pueblo Bowl-O-Mat*.¹¹

In 1994, Indeck and GM entered into a cogeneration contract premised on Indeck's understanding that GM would run its Flint plant with power from Indeck's facility. GM subsequently entered into an exclusive dealing contract with Consumers Power providing discount electricity to the Flint plant and eighteen other GM plants for terms ranging from five to ten years. Indeck alleged that through its contract with GM, and through similar contracts with seventeen other consumers, Consumers Energy monopolized the market for electric service to large-scale industrial and commercial customers in Michigan.

Consumers Energy successfully argued that its activities met both prongs of the Midcal test for state action immunity. Examining the first prong, the pres-

7. *Id.* at 897.

8. *New York State Elec. & Gas Corp. v. FERC*, 177 F.3d 1037 (D.C. Cir. 1999).

9. *Indeck Energy Servs., Inc. v. Consumers Energy Co.*, No. 97-CV-10366-BC, 1999 U.S. Dist LEXIS 7251 (E.D.Mich. Mar. 31, 1999).

10. *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980).

11. *Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. 477 (1977).

ence of a clearly articulated state policy displacing competition, the court agreed that Michigan had articulated a permissive policy under which regulated utilities may execute long-term, exclusive discount contracts as part of the state's gradual transition to increased retail competition. As to the second prong of active supervision of the state policy as applied to the allegedly anticompetitive activity, the court found that active supervision was satisfied by the MPSC's review and approval of the Consumers-GM contract.

The court further ruled that, as to the seventeen other exclusive discount contracts, Indeck did not suffer a legally recognizable antitrust injury, and therefore lacked standing to sue. Central to the court's decision was the fact that Indeck itself was not attempting to offer electricity to any of the other seventeen customers.

*B. North Star Steel Co. v. MidAmerica Energy Holdings Co.*¹²

North Star alleged MidAmerica violated federal antitrust laws by refusing to provide retail wheeling service to North Star's Wilton, Iowa, plant. Affirming the district court's grant of summary judgment, the Eighth Circuit ruled that the refusal by MidAmerica was entitled to state action immunity given Iowa's statutorily created system of exclusive electric service territories.

North Star unsuccessfully argued that Iowa's system of exclusive service territories afforded state action immunity to electric distribution and transmission service, but not to electricity generation and sales. In support of its position, North Star emphasized that MidAmerica did not generate all of the electricity it provided, but instead bought power from others for distribution within its "exclusive" service territory. North Star also pointed to a program established by the Iowa Utilities Board in 1998 which allowed MidAmerica to resell limited amounts of third-party generation to end users.

The court ruled that North Star was collaterally estopped from arguing that Iowa's exclusive territories statute did not preclude competition in electricity generation and retail sales. During the pendency of the federal action, the Iowa Board issued a declaratory order (at MidAmerica's request) that electricity generation and retail sales were subject to the exclusive territory restrictions. The Iowa Board's order, which was subsequently upheld in state court, was deemed conclusive on the federal action.

Noting the distinction between wholesale and retail electricity markets, the court held that MidAmerica's purchase of third party generation for distribution within its service territory did not detract from state action immunity. To a similar effect, the inauguration of a limited retail wheeling pilot program did not undermine state action immunity, but served to illustrate that the overarching state policy favored exclusive service territories in lieu of retail competition.

12. *North Star Steel Co. v. MidAmerica Energy Holdings Co.*, 184 F.3d 732 (8th Cir. 1999).

IV. ENERGY TAXES

A. *Duke Energy Natural Gas Corp. v. Commissioner of Internal Revenue*¹³

In *Duke Energy*, the court reversed the Tax Court, finding that natural gas gathering systems could be depreciated over seven years rather than fifteen years because the assets were used in the exploration for and production of petroleum and natural gas. The Court stated that, even though Duke Energy was not a producer, the assets were "used by" producers through contractual arrangements for production of natural gas and were, therefore, qualified for the seven-year depreciation period provided under the Modified Accelerated Cost Recovery System (MACRS). The primary use of the assets placed them under MACRS, rather than under the fifteen-year depreciation period required for transmission lines.

B. *Amerada Hess Corp. v. Department of Interior*¹⁴

In *Amerada Hess*, the court affirmed the district court's finding that reimbursements for production-related costs that a federal natural gas lessee received from its gas purchasers under FERC Order No. 94 were royalty bearing under the Outer Continental Shelf Lands Act, absent a showing that the lessee's gas was in marketable condition and could be sold directly from the wellhead or that the reimbursements were for transportation.

C. *Anadarko Petroleum Corp. v. FERC*¹⁵

In *Anadarko*, the court affirmed the FERC's denial of a generic waiver of interest with respect to producers' refunds of overcollections from the Kansas *ad valorem* tax. In addition, the court affirmed the FERC's denial of a reduction in the refund liability by the amount of the "tax-on-tax" effect arising under the Kansas tax assessment methodology. However, the court set aside the FERC's decision regarding the starting date for refunds and remanded the case for entry of an order prescribing a date consistent with the court's finding that the relevant transaction is the sales transaction. It is the overcharges paid in those individual sales transactions which must be refunded, plus interest.

D. *Exxon Corp. v. Commissioner of Internal Revenue*¹⁶

The Tax Court held that the petroleum revenue tax Exxon paid to the United Kingdom constitutes an excess profit or income tax creditable under section 901 of the Internal Revenue Code against Exxon's United States federal income tax liability.

13. *Duke Energy Natural Gas Corp. v. Commissioner of Internal Revenue*, 172 F.3d 1255 (10th Cir. 1999).

14. *Amerada Hess Corp. v. Department of Interior*, 170 F.3d 1032 (10th Cir. 1999).

15. *Anadarko Petroleum Corp. v. FERC*, 196 F.3d 1264 (D.C. Cir. 1999).

16. *Exxon Corp. v. Commissioner of Internal Revenue*, 113 T.C. 24 (1999).

V. FEDERAL POWER ACT-HYDROELECTRIC LICENSING AND RELATED ENVIRONMENTAL ISSUES

A. *FERC v. Seneca Falls Power Corp.*¹⁷

In *Seneca Falls*, the FERC asked the district court to issue an injunction ordering the defendant to comply with section 10(c) of the Federal Power Act (FPA),¹⁸ which requires hydroelectric licensees to take action deemed necessary by the FERC. The defendant licensee had repeatedly failed to submit plans and adhere to proposed schedules for the repair of a Waterloo Dam canal wall located within the Waterloo and Seneca Falls Development (Development). The FERC is empowered under the FPA to monitor and investigate operations under hydroelectric licenses, and to issue orders necessary to insure compliance with the terms of those licenses. In this case, Seneca had been issued a license in 1997 to continue operations at the Development (previously licensed to New York State Electric & Gas). Part of the license required Seneca to repair a severely deteriorated canal wall. Throughout the balance of 1997 and into the next year, Seneca repeatedly failed to submit reports and plans when due and to adhere to schedules for the needed repairs. Finally, the FERC filed this action seeking injunctive relief under section 314(a) of the FPA.

The decision turned on the showing required for injunctive relief. The FERC argued that, in accord with a line of Second Circuit cases, the court could issue an injunction on grounds other than the traditional basis of immediate irreparable harm, specifically, upon a showing of the reasonable likelihood of future violations, i.e., the statutory violations test.¹⁹ The court agreed. First, it found that Seneca had clearly violated the statutory mandate in the FPA. Second, it followed the Second Circuit in *Commodities Futures* and found that a court may infer future violations from past conduct. Based on Seneca's protracted history of ignoring orders, it found a likelihood of future violation. The "proper showing" for relief having been established, the court issued an injunction requiring the repairs be performed by a date certain in accordance with submitted plans or face stiff civil penalties.

B. *Wisconsin v. FERC*²⁰

In *Wisconsin v. FERC*, the State of Wisconsin challenged provisions of hydroelectric licenses granted to companies for operations on the Flambeau River. In 1991, Fraser Papers, Inc. and Northern States Power Company sought licenses for six hydroelectric projects in the river basin. They conducted fish entrainment and mortality studies and consulted with State representatives.

Wisconsin disputed the studies because they underestimated mortality and used improper methodology. In 1996, the FERC issued its Final Environmental

17. *FERC v. Seneca Falls Power Corp.*, No. 98-CV-1716, 1999 U.S. Dist. LEXIS 577 (N.D.N.Y. Jan 14, 1999).

18. 16 U.S.C. § 803(c) (1994); 18 C.F.R. § 12.4(b)(2)(iv) (1999).

19. See, e.g., *Commodities Futures Trading Comm'n v. American Bd. of Trade*, 803 F.2d 1242, 1250-51 (2d Cir. 1986).

20. *Wisconsin v. FERC*, 192 F.3d 642 (7th Cir. 1999).

Impact Statement. In it, the FERC adopted the position of Fraser and Northern, finding that the "specific effect of entrainment" could not be ascertained from such a short study period. It issued the requested licenses, but required the companies to work with the State to formulate alternative fish protection devices or compensatory measures, and to conduct further entrainment studies. The licenses also included traditional reopener clauses, whereby the FERC retained authority to revisit the issue if necessary.

The licensees challenged the licenses, arguing that requiring further studies or compensatory mitigation was not supported by the record and would be unduly burdensome. Upon review, the FERC revised the licenses, removing the objectionable requirements. Wisconsin's request for reconsideration was denied.

The State appealed, asserting that deletion of these requirements was error as a matter of law. The court found that Wisconsin was not a party "aggrieved" by the order, as that term is used in FPA Section 313(b), and had no standing to pursue the appeal. A party is aggrieved under that section if it satisfies both constitutional and prudential standing requirements. Article III standing requires: (1) an actual or imminent injury in fact; (2) causal connection between the conduct and the injury; and (3) likelihood that the injury will be redressed by a favorable decision.²¹ Looking at the final requirement, the court held it would be merely speculative to find that a favorable ruling would redress the harm, due to the fact that only a short-term study was conducted. The court noted that the reopener clause could be utilized if the facts should justify a reexamination in the future.

VI. FEDERAL POWER ACT: ELECTRIC REGULATORY LAW

A. *Western Massachusetts Electric Co. v. FERC*²²

In *Western Massachusetts*, the court of appeals denied petitions for review of the FERC orders holding that the cost of upgrades to the transmission grid associated with the interconnection of cogeneration facilities must be rolled into the public utility's transmission rate base rather than assigned exclusively to the interconnecting facilities.

A threshold issue in the case was whether the FERC properly asserted jurisdiction over the interconnection agreements pursuant to the FPA. The court upheld the FERC's ruling that its regulations under the Public Utility Regulatory Policies Act (PURPA) did not assign jurisdiction over the interconnection agreements to the states.²³ The court further upheld the FERC's finding that these interconnection agreements related to interstate transmission service and thus must be filed with the FERC under section 205(c) of the FPA.²⁴

On the rate issue, the court held that the FERC properly required the utility to roll into its transmission rates the cost of the grid upgrades necessary to interconnect these facilities. The court held that the FERC's finding that the grid up-

21. *Bennett v. Spear*, 520 U.S. 154, 167 (1997).

22. *Western Mass. Elec. Co. v. FERC*, 165 F.3d 922 (D.C. Cir. 1999).

23. *See infra* Part XI.A.

24. 16 U.S.C. § 824d(c) (1994).

grades will be used by and will benefit all users of the transmission grid was based on substantial evidence. The court also upheld the FERC's determination that rolling in the upgrade costs did not unfairly shift costs from the interconnecting facility to all grid customers. Finally, the court accepted the FERC's finding that the utility would over-collect its costs if it assigned the grid upgrade costs to the interconnecting facility while also charging grid customers an increased rate for receiving energy from the facility.

*B. Sithe/Independence Power Partners, L.P. v. FERC*²⁵

In *Sithe/Independence Power*, the court remanded FERC orders summarily dismissing a complaint that had challenged the method of computing losses under a contract for transmission service. The customer argued that FERC policy required consistent (or "matching") methods of computing the charges for base transmission service and losses. Here, the base transmission rate was computed on a rolled-in basis while the loss charge was computed on an incremental basis. The transmission provider contended that the base transmission charge was a "hybrid," not a pure rolled-in charge based on average system costs, and thus the "matching" principle allowed for an incremental loss charge.

The court remanded the FERC's orders dismissing the complaint, holding that the FERC had not clearly explained its rationale or revealed the data and assumptions underlying its findings. The court found that the transmission and loss charges were not computed with "matching" methodologies, but the FERC had not explained why the matching rule was not followed in this instance. The FERC also concluded that the total charges for transmission and losses were discounted from the fully allocated rolled-in rates that presumably could have been charged. The court found that the FERC had not adequately explained its "independent analysis" of the rates or disclosed the calculations that led it to this conclusion. Furthermore, the court directed the FERC on remand to clarify its ruling on the customer's allegation that it was unduly discriminatory to compute higher incremental loss charges for customers with later contracts.

*C. Louisiana Public Service Commission v. FERC*²⁶

The FERC found that the operating companies of a public utility holding company had violated the terms of the intercompany system agreement they used to equalize capacity costs among them, which had been previously filed with and approved by the FERC. They violated the agreement by including in their capacity calculations generating units they removed from active status (because they were unnecessary for present capacity needs) and placed in extended reserve shutdown (ERS) status (which lowered the costs associated with these units). The FERC found that the system agreement did not allow the companies to include ERS generating units in their capacity equalization; but the FERC did not order the operating companies to pay refunds among themselves to remedy the resulting overcharges and undercharges. The FERC also approved tariff amendments allowing the ERS units to be included in the system agreement's

25. *Sithe/Independence Power Partners, L.P. v. FERC*, 165 F.3d 944 (D.C. Cir. 1999).

26. *Louisiana Pub. Serv. Comm'n v. FERC*, 174 F.3d 218 (D.C. Cir. 1999).

capacity-equalization calculations.

The court of appeals denied petitions for review brought by two state commissions. As to the FERC's failure to order refunds, the court noted that the scope of its review was especially narrow. It concluded that there was substantial evidence to support the FERC's finding that including the ERS units in the system agreement calculations, while a violation of the agreement's terms, had nonetheless conferred a benefit on the system in the form of greater efficiencies and lower costs.²⁷ The court also accepted the FERC's rationale that the ERS units should be treated like other generating reserves, because they were planned and built for the benefit of the system and could be brought back into active status to serve the system's needs.²⁸ The court did not find as convincing, but nonetheless accepted, two other rationales also cited by the FERC: (1) that the tariff violation did not result in unjust enrichment of the holding company system; and (2) the estoppel argument that no party had objected to the tariff violation from 1986 until 1993.²⁹

Finally, the court upheld the FERC's acceptance of an amendment to the system agreement to permit ERS units to be included in capacity equalization determinations. The petitioners alleged that the amended agreement granted unfettered discretion to the holding company to include ERS units under the agreement. But the court deferred to the FERC's judgment that the agreement specified the parameters of the holding company's discretion, and that any discriminatory implementation of the agreement could be remedied upon complaint to the FERC.³⁰

*D. Louisiana Public Service Commission v. FERC*³¹

The Louisiana Public Service Commission (LPSC) filed a complaint alleging that it was unjust and unreasonable for a public utility holding company to count interruptible loads when allocating capacity costs pro rata among its several operating companies. The FERC dismissed the complaint without a hearing. It ruled that interruptible loads were properly assessed responsibility for capacity costs, and further, that the state commission had not shown that changed circumstances had upset the existing "rough equalization" of costs among the operating companies.

The court of appeals vacated and remanded the orders, concluding that the FERC's action was arbitrary and capricious. The FERC had not explained why it was failing to follow its long-standing precedent that does not assign responsibility for capacity costs to interruptible loads. The court further held that the FERC had not adequately explained the rough equalization standard it used to deny a hearing on the complaint.

27. LPSC, 174 F.3d at 225-27.

28. *Id.* at 228-29.

29. LPSC, 174 F.3d at 229-230.

30. *Id.* at 230-31.

31. Louisiana Pub. Serv. Comm'n v. FERC, 184 F.3d 892 (D.C. Cir. 1999). This case is also discussed *infra* Part XI.C.

*E. Northern States Power Co. v. FERC*³²

The Eighth Circuit held that the FERC did not have jurisdiction under the FPA to require a public utility to curtail its use of its transmission facilities to provide retail sales service on a pro rata basis with its curtailments of unbundled transmission service provided under its open access transmission tariff. The case arose on the utility's petition for review of the FERC orders requiring the utility to amend its open access transmission tariff to provide for pro rata curtailments of the utility's own uses of its transmission system to serve its bundled retail and native load customers when the utility curtails transmission service under the tariff. The court held that the FPA did not give the FERC authority over curtailments of retail service, but expressly reserved this authority to the states. It rejected the argument that the FERC was only taking account of non-jurisdictional matters, and indirectly affecting them, in exercising its jurisdictional duties. The court also noted that if the utility made pro rata curtailments it might violate its obligations to serve under state law.

The court of appeals denied rehearing and rehearing en banc. The FERC did not seek further review. After a further order by the FERC on remand, the utility withdrew the tariff provisions that did not conform with the FERC's *pro forma* open access tariff. A petition for a writ of certiorari filed by other parties remains pending, as of the end of 1999. In light of the utility's withdrawal of the tariff provisions, the petition asks that the court of appeals' decision be vacated as moot.

VII. NATURAL GAS ACT: PIPELINE RATE REGULATION

A. General Rate Adjudication

In "*Complex*" *Consolidated Edison Co. v. FERC*,³³ the D.C. Circuit denied petitions to review the FERC's orders in Tennessee Gas Pipeline Company's (Tennessee Gas) general rate case.³⁴ JMC Power Projects and New England Power Company (JMC/NE) protested Tennessee Gas's continuing to incrementally price its NET/T-180 expansion, and the FERC found that they had not submitted evidence upon which the FERC could impose rolled-in pricing under section 5 of the Natural Gas Act (NGA). Equitable Gas Company (Equitable) protested Tennessee Gas's proposal to change the pricing of the FSST/T-149 and Boundary expansion from incremental to rolled-in, which the FERC approved under section 4 of the NGA. Consolidated Edison, Brooklyn Union, and Long Island Lighting (collectively ConEd Group) claimed that Tennessee Gas engaged in undue discrimination by charging the same rate for services subject to different operating conditions, but the FERC refused to impose different rates. The D.C. Circuit reviewed and upheld the FERC's decisions on all three issues.

The FERC held JMC/NE to the two-part NGA section 5 burden because

32. *Northern States Power Co. v. FERC*, 176 F.3d 1090 (8th Cir. 1999), *petition for cert. pending*. See also *infra* Part XIII for further discussion of this case.

33. "*Complex*" *Consol. Edison Co. of N.Y. v. FERC*, 165 F.3d 992 (D.C. Cir. 1999).

34. *Tennessee Gas Pipeline Co.*, 76 F.E.R.C. ¶ 61,022 (1996), *reh'g denied*, 80 F.E.R.C. ¶ 61,389 (1997).

Tennessee Gas had not proposed to change the pricing of the NET/T-180 expansion. The D.C. Circuit affirmed the doctrine that "there is no single just and reasonable rate"—no "single magic point" exists where incremental pricing becomes unjust and unreasonable and rolled-in pricing becomes just and reasonable. The difference between section 4 and section 5 of the NGA becomes critical, because a party other than the pipeline that proposes a change must prove that both: (1) the current pricing has become unjust and unreasonable; and (2) incremental pricing has become just and reasonable. Relying on the FERC's old test, which the D.C. Circuit had previously remanded for blurring the difference between sections 4 and 5, JMC/NE had submitted evidence showing, at most, only that rolled-in pricing might be just and reasonable. The D.C. Circuit denied their petition, holding that: (1) the FERC's new test (the refined *Battle Creek* test³⁵) respected the difference between section 4 and section 5; (2) the FERC may, but need not, rely on quantitative as well as qualitative analysis of the costs and benefits of expansion facilities; and (3) JMC/NE had no equitable right to application of the FERC's old test, because they had neither (a) reasonable expectation that Tennessee Gas would propose to change the pricing nor (b) suffered manifest injustice from application of the FERC's new test.

The FERC held Tennessee Gas to only the section 4 burden of proving that rolled-in pricing for the FSST/T-149 expansion was just and reasonable. Equitable argued on appeal that Tennessee Gas, as the proponent of change, carried the heavier, two-prong section 5 burden. The D.C. Circuit denied the petition and held that: (1) section 5 applies only to changes in rates proposed by a party other than the pipeline; (2) the pipeline may satisfy section 4 with evidence submitted by any other party; (3) the FERC has broad discretion to decide whether a filing substantially complies with the minimum filing regulations; and (4) courts should defer to the FERC's decision to reach the merits without further hearings.

Finally, the FERC found that Tennessee Gas had not unduly discriminated against the ConEd Group. Tennessee Gas charged the same rate to the ConEd Group and New England shippers who, the ConEd Group argued, had greater flexibility to take deliveries beyond the uniform hourly quantities. The ConEd Group requested that the FERC impose a lower rate for their "lower quality" service. The FERC declined. The D.C. Circuit affirmed that the facts did not evidence a "substantive difference in treatment" essential to a discrimination claim, finding that: (1) Tennessee Gas applied the same tariff standard evenhandedly to both the ConEd Group and the New England shippers; (2) operating conditions caused differences between the hourly quantities the two groups could take, rendering them dissimilarly situated; (3) the ConEd Group failed to submit cost allocation studies that would show a disparity in the cost of service that would require different rates for the two groups of shippers; and (4) the New England shippers who took hourly volumes other than uniformly did so only on an interruptible basis, and therefore, the ConEd Group's firm service was not "necessarily inferior."

35. Under the so-called *Battle Creek* test, the costs associated with expansion facilities can be properly rolled into the general system rates whenever such facilities are integrated with the pipeline system and provide system-wide benefits. *"Complex" Consol. Edison*, 165 F.3d at 995 n.3. See also *Battle Creek Co. v. FPC*, 281 F.2d 42 (D.C. Cir. 1960).

In *Northern Municipal Distributors Group v. FERC*,³⁶ the D.C. Circuit denied petitions for review of FERC orders modifying and approving a settlement of "highly contentious" rate issues.³⁷ The contested Carlton settlement among Northern Natural Gas Company (Northern) and its shippers solved an operational problem by requiring some shippers to take a portion of receipts at Carlton and other shippers to pay a surcharge. Northern would collect the surcharge from the latter shippers to reimburse the former for the higher price of gas at Carlton.

The FERC approved the settlement with one modification. If Northern opted to discount, then the discount would apply first to the base rate, then to the Carlton surcharge, and last to any transition surcharges. Northern would therefore bear the Carlton cost if it deeply discounted its rates. Northern argued on appeal that the Carlton surcharge, as a non-transition cost, could be discounted as Northern saw fit. The D.C. Circuit upheld the FERC, even though the FERC conceded that the only cited precedent did not apply, other precedent supported Northern's proposal, and Northern raised legitimate concerns. Because the FERC had to create a new policy for a new and highly contentious situation, the result deserved the court's deference.

The FERC also held that an earlier settlement among Northern and its shippers did not exempt small shippers from the Carlton régime of receipt allocations and cost surcharges. The D.C. Circuit agreed. Although it could be interpreted to exempt small shippers, the settlement did not encompass situations unknown and unforeseen when the parties reached agreement. The FERC was not bound in perpetuity to its terms if new situations arose.

In *Williston Basin Interstate Pipeline Co. v. FERC*,³⁸ the D.C. Circuit remanded the FERC's orders setting rates under section 4 of the NGA.³⁹ Williston Basin petitioned for review of three FERC determinations: (1) calculating a return on common equity using a two-stage discounted cash flow (DCF) methodology that averages (a) short-term growth data from the Institutional Brokers Estimate System (IBES), and (b) long-term growth data from gross domestic product (GDP) projections by Data Resources Inc./McGraw Hill (DRI) and the Energy Information Administration (EIA); (2) using actual *ad valorem* taxes for the test period as the most representative level of taxes for the effective period of the rates, rather than Williston Basin's proposal to increase taxes by applying the current tax rate to actual, plant additions at the end of the test period; and (3) using the actual throughput for the test period, rather than Williston Basin's proposal to decrease throughput to account for two major bypasses of its system, which Williston Basin estimated to occur within the test period but which actually occurred shortly after.

The D.C. Circuit upheld the FERC's use of a two-stage DCF methodology and the inclusion of GDP data as the long-term growth factor. However, while

36. *Northern Mun. Distrib. Group v. FERC*, 165 F.3d 935 (1999).

37. *Northern Natural Gas Co.*, 79 F.E.R.C. ¶ 61,348, *reh'g denied*, 80 F.E.R.C. ¶ 61,148 (1997).

38. *Williston Basin Interstate Pipeline Co. v. FERC*, 165 F.3d 54 (D.C. Cir. 1999).

39. *Williston Basin Interstate Pipeline Co.*, 79 F.E.R.C. ¶ 61,311, *reh'g denied*, 81 F.E.R.C. ¶ 61,033 (1997).

Williston Basin's appeal remained pending, the FERC revised its DCF methodology by giving long-term growth only one-third, rather than average (*i.e.*, one-half), weight. The FERC also surprised Williston Basin with the use of GDP projections by DRI and EIA, which the parties had not explored during the hearing. Therefore, the D.C. Circuit remanded these two issues to the FERC.

Williston Basin succeeded in persuading the D.C. Circuit that the FERC departed from precedent—or failed to explain the applicability of the precedent—in disallowing increased *ad valorem* taxes to account for plant additions during the test period. While suggesting distinguishing facts that would make Williston Basin's proposal too speculative, the D.C. Circuit remanded to the FERC for an opportunity to explain its findings.

The legal authorities on post-test period adjustments also required further explanation. By refusing to allow Williston Basin to decrease throughput to account for bypasses occurring shortly after the test period, the FERC's order conformed to its rate filing regulations, which use updated actuals to the exclusion of filed estimates. But by disregarding Williston Basin's filed rates to exclude the bypasses, the order contradicted FERC and court precedent by upholding pipeline estimates: (1) that were reasonably made at the time of filing; and (2) that did not produce unreasonable results. The D.C. Circuit therefore remanded to give the FERC an opportunity to justify its findings in light of conflicting precedent.

B. Settlements

In *Panhandle Eastern Pipe Line Co. v. FERC*,⁴⁰ the D.C. Circuit denied Panhandle's petition to review the FERC's denial of a motion to vacate two opinions in Panhandle's section 4 rate cases. The FERC had issued Opinion No. 395 in Panhandle's first section 4 filing and Opinion No. 404 in Panhandle's second Section 4 filing.⁴¹ In both cases, several parties filed requests for rehearing. Before the FERC issued orders on rehearing of Opinion Nos. 395 and 404, Panhandle and its customers settled the two underlying rate cases. The FERC approved the settlement, and Panhandle subsequently moved to vacate Opinion Nos. 395 and 404 as moot. The FERC denied Panhandle's motion and denied rehearing.⁴² The D.C. Circuit never reviewed the merits of the FERC's refusal to vacate the opinions, holding instead that Panhandle lacked standing to seek judicial review under Section 19(b) of the Natural Gas Act and Article III of the U.S. Constitution. The FERC conceded that the settlement mooted Opinion Nos. 395 and 404, which were pending rehearing when the FERC approved the settlement. The opinions that Panhandle moved to vacate never became final, binding orders with precedential weight, but remained only the functional equivalent of general policy statements. Because the mere existence of these "policy statements" could not cause an injury that satisfied section 19(b) or Article III, the D.C. Circuit lacked jurisdiction to review the FERC's refusal to va-

40. *Panhandle E. Pipe Line Co. v. FERC*, 198 F.3d 266 (D.C. Cir. 1999).

41. *Panhandle E. Pipe Line Co.*, 71 F.E.R.C. ¶ 61,228 (1995) (Opinion No. 395); *Panhandle E. Pipe Line Co.*, 74 F.E.R.C. ¶ 61,109 (1996) (Opinion No. 404).

42. *Panhandle E. Pipe Line Co.*, 83 F.E.R.C. ¶ 61,008, *reh'g denied*, 83 F.E.R.C. ¶ 61,353 (1998).

cate.

In *Williams Field Services Group, Inc. v. FERC*,⁴³ the D.C. Circuit vacated and remanded the FERC's order to refunctionalize fuel costs from transmission to gathering. El Paso Natural Gas Company had received approval to abandon gathering facilities by sale to a nonjurisdictional affiliate.⁴⁴ El Paso retained the Chaco compressor station as a transmission facility. In response to Williams's protest that the Chaco station served a nonjurisdictional gathering function, the FERC ordered El Paso to show cause why it should not be required to abandon this facility as well. Before the FERC issued an order, however, El Paso submitted a settlement resolving a pending section 4 rate case, and the settlement functionalized the Chaco station as transmission plant, included in El Paso's jurisdictional rates. The FERC approved the settlement⁴⁵ and subsequently issued an order in the show cause proceeding that found that the Chaco station served a transmission function.⁴⁶ The FERC subsequently reversed itself, relying on additional evidence that the Chaco station served a gathering function.⁴⁷ Williams urged the FERC also to remove the Chaco station from El Paso's jurisdictional rates established in the approved settlement. Citing the settlement, other parties urged the FERC to reinstate its finding that the Chaco station served a transmission function and to clarify that the settled rates would not be modified. On rehearing, the FERC interpreted the settlement to allow a refunctionalization of only the fuel costs associated with Chaco station.⁴⁸

The D.C. Circuit granted petitions to review filed both by parties believing the FERC's rate decision went too far and by parties believing the decision did not go far enough. The FERC's order rested on an interpretation of the El Paso settlement that the D.C. Circuit had previously remanded on other grounds.⁴⁹ Therefore, the D.C. Circuit vacated and remanded the refunctionalization decision to allow reconsideration within the context of the evolving settlement proceeding.

C. Initial Rates

In *Trunkline LNG Co. v. FERC*,⁵⁰ the D.C. Circuit denied Trunkline LNG's petition to review the FERC's certificate conditions excluding unrecovered depreciation from initial rates and requiring a cost-and-revenue study after three years of operating experience. Trunkline LNG owns a terminal in Lake Charles, Louisiana, where liquefied natural gas is imported by cryogenic tankers and stored before being vaporized and delivered into the pipeline network. Import prices had previously caused Trunkline LNG to suspend its sales service, provided under a merchant tariff that pre-dated the FERC's open-access transporta-

43. *Williams Field Servs. Group, Inc. v. FERC*, 194 F.3d 110 (D.C. Cir. 1999).

44. *El Paso Natural Gas Co.*, 72 F.E.R.C. ¶ 61,220 (1995).

45. *El Paso Natural Gas Co.*, 79 F.E.R.C. ¶ 61,028 (1997).

46. *El Paso Natural Gas Co.*, 79 F.E.R.C. ¶ 61,079 (1997).

47. *El Paso Natural Gas Co.*, 81 F.E.R.C. ¶ 61,209 (1997).

48. *El Paso Natural Gas Co.*, 82 F.E.R.C. ¶ 61,337, *reh'g denied*, 84 F.E.R.C. ¶ 61,048 (1998).

49. *Report of the Judicial Review Committee*, 20 ENERGY L.J. 167, 178-79 (1999).

50. *Trunkline LNG Co. v. FERC*, 194 F.3d 68 (D.C. Cir. 1999).

tion regime. The merchant tariff included a minimum bill through which customers would in times of suspended sales pay Trunkline LNG's fixed costs other than return on and return of equity in the facilities. Trunkline LNG accumulated \$106.9 million in unrecovered depreciation during suspended service.

Following suspended service, Trunkline LNG filed an application to provide service under the FERC's open-access regime. The application contained a new tariff with initial rates calculated on a rate base that included the unrecovered depreciation. The FERC authorized the new service under section 7 of the NGA but used its conditioning power to require Trunkline LNG to: (1) file a cost-and-revenue study after three years' operating experience; and (2) exclude the unrecovered depreciation from its initial rates. The FERC denied Trunkline LNG's request for rehearing.⁵¹

The D.C. Circuit upheld the FERC's orders. First, the orders did not deny Trunkline LNG an opportunity to recover its investment in the Lake Charles terminal. Trunkline LNG had an opportunity during its sales service, and the possibility of suspended service was specifically contemplated in the minimum bill. No changes had occurred that would justify overturning the result (i.e., unrecovered depreciation) of the minimum bill. Second, the orders did not blur the distinction between sections 4 and 5 of the NGA. The D.C. Circuit agreed that the FERC cannot use section 7 to avoid its burden of proof under section 5, by conditioning Trunkline LNG's open-access certificate on a section 4 filing requirement. But section 10 of the NGA grants the FERC authority—separate and apart from sections 4 and 7—to require Trunkline LNG to file a cost-and-revenue study. The FERC will then bear a section 5 burden if the study suggests that Trunkline LNG's initial rates have become unjust and unreasonable.

In *New York State Electric & Gas Corp. v. FERC*,⁵² the D.C. Circuit dismissed a petition to review the FERC's orders pricing an expansion by Columbia Gas Transmission Company's (Columbia) system. The FERC granted Columbia a presumption of rolled-in pricing for the project, because the cost would not increase rates more than 5%, and the project would benefit Columbia's system.⁵³ New York State Electric and Gas Corporation (NYSEG) protested that the FERC's findings rested on a flawed cost study, illusory systemwide benefits, and an inadequate hearing. The FERC denied NYSEG's protest and request for rehearing.⁵⁴

The D.C. Circuit concluded that the dispute had not yet become ripe for judicial review. The rate increases that NYSEG cited as injury sufficient to establish jurisdiction actually resulted from prior FERC orders approving Columbia's last rate settlement, and that settlement contained a refund provision that mitigated any hardship NYSEG would suffer from postponing judicial review. Be-

51. *Trunkline LNG Co.*, 82 F.E.R.C. ¶ 61,198 (1998).

52. *New York State Elec. & Gas Corp. v. FERC*, 177 F.3d 1037 (D.C. Cir. 1999).

53. *Pricing Policy for New and Existing Facilities Constructed by Interstate Natural Gas Pipelines*, 71 F.E.R.C. ¶ 61,241 (1995), *reh'g denied*, 75 F.E.R.C. ¶ 61,105 (1996). The Commission revised its pricing policy on September 15, 1999. *Certification of New Interstate Natural Gas Pipeline Facilities*, 88 F.E.R.C. ¶ 61,227 (1999).

54. *Columbia Gas Transmission Corp.*, 78 F.E.R.C. ¶ 61,030, *reh'g denied*, 79 F.E.R.C. ¶ 61,160 (1997).

cause Columbia's next rate case offered an opportunity to challenge rolled-in pricing for the expansion, and NYSEG suffered no hardship from the certificate orders on review, the D.C. Circuit dismissed the petition.

In *The Brooklyn Union Gas Co. v. FERC*,⁵⁵ the Fifth Circuit dismissed petitions to review the FERC's orders pricing Transcontinental Gas Pipe Line Corporation's (Transco) extension from Mobile Bay into the Gulf of Mexico. Transco's marketing affiliate purchased all the new capacity and benefitted from the FERC's orders: (1) allowing Transco to charge WESCO an initial rate equal only to the systemwide rate; and (2) granting the project a presumption of rolled-in pricing that shifted costs to Transco's unaffiliated customers, several of whom competed with Transco's marketing affiliate.⁵⁶

Two commissioners filed separate opinions, one dissenting. The FERC majority denied a number of protests by Transco's customers and competitors, who argued that the project: (1) served primarily a nonjurisdictional, gathering function; (2) constituted part of a larger project that Transco segmented to circumvent the FERC's test for rolled-in pricing; (3) caused anticompetitive effects; and (4) failed to provide systemwide benefits that justified unaffiliated customers' subsidizing WESCO's rolled-in rates.

Transco intervened in the appeal and moved to dismiss for lack of subject matter jurisdiction. The FERC supported Transco's motion. The Fifth Circuit boiled all the issues down to rolled-in versus incremental rates. The petitioners had standing—both constitutional and statutory—because a presumption of rolled-in rates in the certificate orders gives Transco and WESCO a competitive advantage. Rather than reach the merits, however, the Fifth Circuit directed that the FERC—which on appeal had undermined the importance of the presumption—allow petitioners a full opportunity to challenge rolled-in pricing in Transco's next general rate case. The issue of rolled-in versus incremental pricing for the project remained open for contest, without regard for the presumption or its corollary “changed circumstances” test. Having accepted the FERC's and Transco's invitations to litigate these issues in the future, the Fifth Circuit dismissed the petitions as unripe.

In *Iroquois Gas Transmission System, L.P. v. FERC*,⁵⁷ the D.C. Circuit remanded the FERC's certificate orders prohibiting discounted rates to expansion shippers. Iroquois had applied to expand its system by adding compression. Following a capacity auction, two shippers contracted for the expansion capacity below Iroquois's maximum rate. The FERC issued a certificate to Iroquois but ordered that the expansion shippers must pay no less than the rate Iroquois charged existing shippers.⁵⁸

In a separate proceeding, Iroquois's maximum rate was reduced below the discounted rates the FERC had rejected for expansion shippers in the certificate

55. *Brooklyn Union Gas Co. v. FERC*, 190 F.3d 369 (5th Cir. 1999).

56. *Transcontinental Gas Pipe Line Corp.*, 81 F.E.R.C. ¶ 61,104 (1997), *reh'g denied*, 82 F.E.R.C. ¶ 61,084 (1998).

57. *Iroquois Gas Transmission Sys., L.P. v. FERC*, 172 F.3d 84 (D.C. Cir. 1999).

58. *Iroquois Gas Transmission Sys., L.P.*, 79 F.E.R.C. ¶ 61,394 (1997), *reh'g denied*, 82 F.E.R.C. ¶ 61,086 (1998).

orders. On appeal of the certificate orders, the FERC moved to have Iroquois's petition for review dismissed for lack of subject matter jurisdiction. The subsequent rate order rendered the discounting issue moot because Iroquois now charged the expansion shippers the lower, undiscounted rate. The D.C. Circuit held that Iroquois continued to satisfy both constitutional and statutory standing because the prohibition on discounting deprived Iroquois of an extremely valuable tool to exploit the business opportunities that the cheap expansibility of its system offered.

The D.C. Circuit started its merits determination by reciting the FERC's policy in favor of competitive discounting and found that the FERC failed to explain why that policy did not apply to Iroquois's application. First, the discounting in this case would not have a different impact in end-use markets than the discounting approved in prior cases. The increased competition that Iroquois's existing shippers faced in the end-use market did not warrant a departure from the FERC's precedent. Second, the fact that existing shippers paid for the cheap expansibility of the system did not justify a departure from precedent. The shippers who had subscribed to the pre-expansion capacity could have anticipated increased competition with new marketers and protected themselves contractually with Iroquois. Because the distinctions the FERC offered would have held true in prior cases that supported Iroquois's discount proposal, the D.C. Circuit remanded the certificate orders to the FERC.

D. Capacity Release Rates

In *Southern California Edison Co. v. FERC*,⁵⁹ the D.C. Circuit remanded the FERC's order dismissing a complaint seeking relief under section 5 of the NGA. Southern California Gas Company (SoCal) subscribed for a large portion of the interstate pipeline capacity that entered California. Southern California Edison Company (Edison) filed a complaint against SoCal's practice of releasing a portion of that interstate capacity to an affiliate at below-market rates while offering remaining portions to nonaffiliates only at above-market prices. The above-market capacity went unused and caused Edison competitive injury in the market for gas-fired electric generation in California.⁶⁰

The FERC dismissed the complaint. SoCal had not violated the FERC's regulations, which prohibited the release of capacity at rates above the just and reasonable rate established by the FERC for the interstate pipeline whose capacity was being released. The FERC presumed that interstate pipelines and some holders of interstate capacity (e.g., local distribution companies (LDCs)) possessed market power and established maximum rates to prevent abuse. Even presuming that it possessed market power, SoCal had not abused that power because it offered nonaffiliates the capacity at or below the just and reasonable

59. *Southern Cal. Edison Co. v. FERC*, 172 F.3d 74 (D.C. Cir. 1999). See also *infra* Part XII.C for further discussion of this case.

60. The court noted that several circumstances had changed that may have mooted Edison's concerns and deprived the court of subject matter jurisdiction. The court directed the FERC to develop a record on Edison's standing to challenge SoCal Gas's practice and on the continuing existence of facts distinguishing this case from Commission precedent.

rate.⁶¹

The D.C. Circuit held that the FERC had too narrowly defined unlawful practices under section 5 of the NGA. Just and reasonable rates did not exhaust the scope of that section, which also encompassed unjust practices and preferential and unduly discriminatory rates. Nor did the FERC's presumption that pipelines and some LDC's possess market power address Edison's complaint. SoCal was allowed to collect a state-authorized surcharge that distinguished this case from FERC precedent holding the maximum rate dispositive. The surcharge was for the purpose of recovering the difference between the cost of holding the interstate capacity and the revenues that releasing the capacity generated. Because this surcharge freed SoCal from the incentive to maximize revenues by releasing capacity at market prices, the court directed the FERC to consider this distinction on remand.

VIII. NATURAL GAS ACT: NON-PIPELINE REGULATIONS

A. *Federal-State Jurisdiction*

The FERC authorized KN Wattenberg Limited Liability Company (KNW) to construct a new natural gas line and related facilities in the state of Colorado to receive gas from Colorado Interstate Gas Company. These new facilities were physically separate from the remainder of KNW's system and all gas received by the new line was to be consumed within Colorado. The City of Fort Morgan, Colorado (Fort Morgan), had argued that the facilities were exempt from FERC jurisdiction as Hinshaw amendment facilities under section 1(c) of the NGA. Rejecting this contention, the FERC found that a jurisdictional interstate pipeline can never own discrete facilities that would be exempt from FERC jurisdiction under the Hinshaw amendment. The FERC held that the Hinshaw exemption applies to entire companies and not to discrete facilities. In *City of Fort Morgan v. FERC*,⁶² however, the Tenth Circuit determined that the FERC's position was inconsistent with the language of the Hinshaw amendment itself, with previous FERC rulings, and with federal case law. Further, the court stated that prior FERC and appellate decisions have acknowledged that the same company can engage in both Hinshaw-exempt activities and FERC-regulated activities, as long as the activities and/or facilities do not constitute a single integrated system. Finding that KNW's new and existing facilities do not appear to be integrated, the court reversed the FERC's orders and remanded the case for further proceedings.

B. *Capacity Allocation; Twenty-Year Cap on Bids*

The FERC authorized Tennessee Gas to allocate generally available capacity on the basis of net present value (NPV) with a twenty-year cap on bids. In addition, the FERC approved the use of NPV to evaluate requests from shippers to change the primary receipt or delivery points under their contracts (meter

61. *Southern Cal. Edison Co. v. Southern Cal. Gas Co.*, 79 F.E.R.C. ¶ 61,157, *reh'g denied*, 80 F.E.R.C. ¶ 61,390 (1997).

62. *City of Fort Morgan v. FERC*, 181 F.3d 1155 (10th Cir. 1999).

amendments). In *Process Gas Consumers Group v. FERC*,⁶³ the D.C. Circuit held that the FERC had failed to engage in reasoned decisionmaking and remanded the case. The court stated that the FERC did not explain why the existence of ten and fifteen year precedent agreements in the gas industry supported a twenty-year cap. The court also noted that in Order No. 636-C, the FERC conceded that it could not justify a twenty-year cap on bids in the right of first refusal context and, instead, reduced the cap to five years.⁶⁴ For purposes of a cap, the court could not perceive any material difference between the right of first refusal process and the awarding of generally available capacity. Consequently, the court found that the FERC had failed to show justification as to why its Order No. 636-C policy was not relevant here. In similar fashion, the court ruled that the FERC's explanation for utilizing NPV for meter amendments was inadequate. The court held that the FERC failed to seriously address the impact of NPV on existing shippers. The court observed that NPV's focus on incremental revenue to the pipeline was a disadvantage to existing shippers in competing with new shippers for receipt or delivery points. The case was remanded to the FERC either to better explain or to modify its decision.

C. Eminent Domain

1. Southern Natural Gas Company v. Land, Cullman County⁶⁵

The FERC granted Southern Natural Gas Company (Southern) an NGA section 7(c) certificate to extend its pipeline over 100 miles in order to provide transportation service to the cities of Huntsville and Decatur, Alabama. The extension required the use of fifty-foot wide easements crossing approximately 500 tracts of land in seven Alabama counties. Although a majority of the landowners signed right-of-way agreements with Southern, it became necessary to condemn almost 200 tracts of land. Pursuant to its NGA section 7(h) power of eminent domain conferred by the certificate, Southern filed condemnation actions in the United States District Court for the Northern District of Alabama to determine the "just compensation" due the landowners for the taking of the easements. Concluding that jury trials would take years to resolve the issue of just compensation, the district court judge appointed a federal land commission under Rule 71A of the Federal Rules of Civil Procedure to hear the cases. If either party in a particular case objected to the commission's report regarding the amount of just compensation due the landowner, the district court would hear such objections before deciding whether to accept, modify or reject the report. On appeal, certain landowners claimed that they were entitled to a jury trial under section 7(h). In *Southern Natural Gas Co. v. Land, Cullman County*, however, the Eleventh Circuit agreed with the district court that Rule 71A superseded the NGA's provisions for the condemnation of property. Finding that Rule 71A was promulgated

63. *Process Gas Consumers Group v. FERC*, 177 F.3d 995 (D.C. Cir. 1999).

64. Order No. 636-C, *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation Under Part 284 of the Commission's Regulations, Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, 78 F.E.R.C. ¶ 61,186, 61,773-74 (1997).

65. *Southern Natural Gas Co. v. Land, Cullman County*, No. 99-6008, 1999 U.S. Dist. LEXIS 32598 (11th Cir. Dec. 16, 1999).

in 1951 to provide a uniform set of procedures to be utilized in deciding federal eminent domain actions, the court of appeals affirmed the district court's appointment of a commission. In addition, the court of appeals affirmed, with one exception, the district court's just compensation findings and remanded the case for more specific findings as to that one item.

2. *Humphries v. Williams Natural Gas Co.*⁶⁶

After receiving a certificate under section 7(c) of the NGA, Williams Natural Gas Company (Williams) commenced construction of a pipeline on the property of Jack Humphries. Humphries filed a lawsuit in Kansas state court seeking damages against Williams for trespass, unlawful taking and damage to property. Williams removed the case to federal district court and filed a motion for summary judgment, arguing that Humphries' claims were preempted by federal law. Williams contended that, subsequent to Humphries' lawsuit, it filed a condemnation proceeding under section 7(h) of the NGA and that such proceeding was the only proper forum for determining compensation owed to Humphries. The district court denied Williams' motion for summary judgment. Noting that Williams had entered Humphries' property prior to filing its condemnation action and prior to seeking permission or attempting to negotiate an agreement with him, the district court found that Williams had not abided by the terms of section 7(h). The court ruled that Williams' condemnation action under section 7(h) did not preempt any claim that existed prior to the date that Williams filed the condemnation action.

D. *Migration of Storage Gas: Unjust Enrichment*

In *Beck v. Northern Natural Gas Co.*,⁶⁷ the Tenth Circuit affirmed a jury verdict in favor of certain landowners on trespass and unjust enrichment claims. The court ruled that there was sufficient evidence to support the findings that Northern's storage gas had migrated onto the landowners' properties and that Northern had been unjustly enriched by such migration. The jury's award of the fair rental value of the properties for the period in question was therefore upheld by the court. In addition, the court affirmed the district court's assessment of attorney fees against Northern.

IX. OIL PIPELINE REGULATION

In *Exxon Co. v. FERC*,⁶⁸ certain shippers petitioned for judicial review of a FERC order approving a contested settlement revising the methodology for valuation of specified grades of petroleum products shipped on the Trans Alaska Pipeline System (TAPS).

The court granted the petition for review in part and vacated and remanded those parts of the FERC's order which: (1) approved the use of proxies for the market valuation of residual fuel oil; and (2) applied the settlement prospectively

66. *Humphries v. Williams Natural Gas Co.*, 48 F. Supp.2d 1276 (D. Kan. 1999).

67. *Beck v. Northern Natural Gas Co.*, 170 F.3d 1018 (10th Cir. 1999).

68. *Exxon Co. v. FERC*, 182 F.3d 30 (D.C. Cir. 1999), *reh'g and reh'g en banc denied* (Sept. 15, 1999).

only. With respect to Petitioners' other claims the court held that: (1) the FERC's failure to account for intragrade differences in quality among heavy distillate before commingling in TAPS was not arbitrary and capricious; (2) reference price alterations for heavy distillate were supported by evidence; (3) the FERC was not required to employ marginal use of residual fuel oil as a blending agent in establishing its valuation methodology; (4) the FERC could consider processing cost in valuation of distillate; (5) the calculation of the cost of sulfur removal was not improper; (6) the FERC could value light residual oil as vacuum gas oil; and (7) the procedures employed by the FERC satisfied due process requirements despite not allowing live testimony and cross-examination.

X. PUBLIC UTILITY HOLDING COMPANY ACT

In *Madison Gas & Electric Co. v. SEC*,⁶⁹ petitioners Madison Gas and Electric Company and the Wisconsin Citizens Utilities Board (collectively Madison) brought this action challenging a decision of the U.S. Securities and Exchange Commission (SEC) approving the merger of three utilities located in Wisconsin and Illinois under the PUHCA.⁷⁰ Stating that it must treat the SEC's findings as "conclusive. . . [if] supported by the substantial evidence," the court denied the petition for review.

Madison's first claim was that in approving the merger, the SEC violated PUHCA section 10(c)(2),⁷¹ which prohibited the SEC from approving the acquisition of a public utility or a holding company unless it finds that the resulting company will serve the public interest by leading towards the economic development of an integrated public utility system. Madison claimed that this provision requires that a permanent physical connection be in place at the time of the acquisition. However, Interstate's "east" and "west" portions were not physically interconnected with one another. The SEC found, and the court affirmed, that a long-term contract with non-related parties that provided a transmission link between the two portions, combined with a commitment to construct two tie lines, was sufficient. Madison also argued the cost of the future integration showed that the merger would not result in economic efficiencies. The court found that the overall economic benefits of the merger greatly outweighed the costs, and rejected this claim.

Madison then claimed that the merger tended to increase the concentration of public utility ownership to the detriment of the public interest, in violation of PUHCA section 10(b)(1).⁷² The SEC had relied on similar findings made by the FERC and other agencies that examined the merger in finding a lack of impermissible concentration. Stating that the SEC was entitled "watchfully" to defer to findings of other agencies, the court affirmed the SEC's findings.

Finally, Madison claimed the SEC's approval of the merger violated

69. *Madison Gas & Elec. Co. v. SEC*, 168 F.3d 1337 (D.C. Cir. 1999).

70. Specifically, the SEC approved the merger application of WPL Holdings, Inc. (WPL), IES Industries, Inc. (IES), and Interstate Power Company (IPC) into Interstate Energy Company (Interstate), a newly formed holding company. IES and WPL were holding companies under PUHCA prior to the acquisition.

71. 15 U.S.C. § 79(j)(c)(1) (1994).

72. 15 U.S.C. § 79(b)(1) (1994).

PUHCA section 10(c)(1),⁷³ which prohibited any merger detrimental to PUHCA's purpose of limiting holding company acquisitions to a single utility system. PUHCA allowed an exemption to this limitation when substantial economies resulted from the merger that would not otherwise be obtained.⁷⁴ Finding that the merger would enhance the individual utility systems' ability to compete in the emerging energy markets, and that customers would benefit from the merger, the court found this condition satisfied.

XI. PUBLIC UTILITY REGULATORY POLICIES ACT

A. *Western Massachusetts Electric Co. v. FERC*⁷⁵

The court in this case upheld the FERC's assertion of FPA jurisdiction over interconnection agreements for certain qualifying facilities. A public utility that transmitted the output of the facilities for sale to another utility had argued that the FERC's Public Utilities Regulatory Policies Act (PURPA) regulations assigned jurisdiction over the interconnection agreements to the state commissions.⁷⁶ But the FERC concluded that its PURPA regulation requiring an electric utility to interconnect with a qualifying facility⁷⁷ did not apply when the electric utility was not purchasing the output of the facility but was instead transmitting the output for sale to another electric utility. Because its PURPA regulation did not require the electric utility to interconnect with the facility, the FERC held that its regulations did not assign the states jurisdiction over the interconnection agreements. The court upheld the FERC's interpretation of its PURPA regulation because it was not plainly erroneous.

B. *Southern California Edison Co. v. FERC*⁷⁸

The court granted a petition for review of orders in which the FERC interpreted the "small power production facility" provision of section 3(17) of the FPA, which was added in 1978 by PURPA.⁷⁹ This provision requires such a facility to use alternative fuels as its "primary energy source." The FERC issued a declaratory order that a landfill gas-to-energy facility would remain a qualifying facility under PURPA and the FERC's regulations if it burned natural gas, in amounts up to 25% of its annual energy input, to "levelize" its power output, as well as to provide input energy during forced outages and landfill maintenance. On appeal, the FERC contended that the statute was ambiguous and that its interpretation should be upheld as reasonable. The court rejected that notion, however, concluding that the FERC's interpretation was inconsistent with the plain language of section 3(17), the structure of PURPA, and the context in which the

73. 15 U.S.C. § 79(c)(1) (1994).

74. PUHCA § 11(b)(1). This section also contained two other requirements that were not at issue here.

75. *Western Mass. Elec. Co.*, 165 F.3d 922.

76. 18 C.F.R. § 292.306(a) (1999).

77. 18 C.F.R. § 292.303(c) (1999).

78. *Southern Cal. Edison Co. v. FERC*, 195 F.3d 17 (D.C. Cir. 1999).

79. 16 U.S.C. § 796(17) (1994).

statute was enacted.⁸⁰ The court held that section 3(17) allows a qualifying facility to use fossil fuels only for designated purposes—"ignition, startup, testing, flame stabilization, and control uses, and . . . to alleviate or prevent . . . unanticipated equipment outages, and . . . emergencies, directly affecting the public health, safety, or welfare, which would result from electric power outages"⁸¹—and did not delegate to the FERC the authority to expand upon the list of permissible uses. Furthermore, the court concluded that the FERC's order was contradicted by the plain terms of its own regulation,⁸² which expressly identifies the permissible uses for fossil fuels in conformance with the statute.⁸³

C. *Louisiana Public Service Commission v. FERC*⁸⁴

The FERC summarily denied a complaint by the LPSC alleging that a public utility holding company's system operating agreement may not count interruptible loads when allocating capacity costs pro rata among the system's operating companies. Although granting the petition for review on other grounds,⁸⁵ the court rejected the LPSC's claim that the FERC's orders conflicted with the state's adoption of interruptible retail rates pursuant to PURPA.⁸⁶ The court held that PURPA specifically provides that it does not restrict the FERC's authority to regulate wholesale rates.⁸⁷

XII. SIGNIFICANT APPELLATE DECISIONS INVOLVING STATE REGULATION

A. *Northern States Power Co. v. FERC*⁸⁸

In *Northern States*, the United States Court of Appeals for the Eighth Circuit held that the FERC may not require a public utility to curtail its native load/retail customers on a comparable basis with its wholesale customers when it experiences transmission constraints. The dispute arose when Northern States Power Company (NSP) filed proposed revisions of its Open Access Transmission Tariff with the FERC. NSP requested that it be allowed to curtail firm point-to-point transactions at times of congestion without making similar curtailments for its native load/retail customers. The FERC rejected NSP's proposal, requiring NSP to modify its tariffs so that native load customers would be curtailed in the same proportion as wholesale customers. The FERC stated that NSP could not give preferential treatment to its native load when curtailing transmission because Order No. 888 requires that transmission providers treat themselves no differently than other wholesale transmission users.⁸⁹

80. *Edison*, 195 F.3d at 22-27.

81. *Id.* at 20.

82. 18 C.F.R. § 292.204(b)(2) (1999).

83. *Edison*, 195 F.3d at 27-28.

84. *LPSC*, 184 F.3d 892.

85. *See supra* Part V.D.

86. 16 U.S.C. § 2621(d)(5) (1994).

87. *LPSC*, 184 F.3d at 899-900 (citing 16 U.S.C. § 2612(b) (1994)).

88. *Northern States*, 176 F.3d 1090. *See also supra* Part VI.E, for further discussion of this case.

89. Order No. 888, *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities*, F.E.R.C. STATS. &

After the FERC's rejection of its revisions, NSP filed its appeal with the Eighth Circuit. NSP argued that to comply with the FERC's mandate would violate state regulatory law prohibiting a public utility from shedding its retail load absent an emergency. NSP maintained that if it were required to provide comparable transmission to both its retail and wholesale customers, its native load customers could face blackouts. Wholesale customers, NSP contended, are in a position to obtain alternative supplies from other utilities whereas native load customers are not.

The Eighth Circuit held that the FERC could not disturb the manner in which NSP curtailed its native load customers. The court stated that the FERC's orders were an attempt to regulate matters outside of its FPA authority to oversee wholesale transmission. The court noted that Congress had limited the FERC's jurisdiction to interstate transactions and that any attempt to regulate the curtailment of electrical transmission for native load customers is unlawful. The FERC had placed NSP "between the proverbial rock and hard place"⁹⁰ by requiring the utility to violate either state regulatory laws or Order No. 888.

The Eighth Circuit denied the FERC's request to reconsider the court's decision.⁹¹ Although the FERC has decided not to seek Supreme Court review of the decision, other litigants in the proceeding filed a petition for certiorari review with the Supreme Court. The Supreme Court has yet to act on this petition.

*B. Connecticut Valley Electric Co. v. Patch*⁹²

The United States Supreme Court refused to hear an appeal challenging a state's handling of stranded costs. In the underlying case, *Public Service Co. of New Hampshire v. Patch*,⁹³ the U.S. Court of Appeals for the First Circuit upheld a New Hampshire Public Utilities Commission (NHPUC) order stating that Connecticut Valley Electric Service Company (Connecticut Valley) had acted imprudently by continuing to purchase power from its parent company, Central Vermont Public Service Company (Central Vermont), when cheaper power was available on the market. The NHPUC argued that the sales agreement between Connecticut Valley and Central Vermont contained a termination provision that should have been exercised by Connecticut Valley in order to obtain cheaper power. The NHPUC's order would preclude Connecticut Valley from including the costs of such power in a stranded cost recovery plan. The First Circuit rejected the argument of Connecticut Valley that the NHPUC's order was preempted by federal jurisdiction, stating that when a state finds a utility's actions to be imprudent, it is not necessarily trespassing on the FERC's authority to determine whether rates are just and reasonable.

REGS. ¶ 31, 036, *clarified*, 76 F.E.R.C. ¶ 61,009 and 76 F.E.R.C. ¶ 61,347 (1996).

90. *Northern States*, 176 F.3d at 1095.

91. *Northern States Power Co. v. F.E.R.C.*, No. 98-3000, 1999 U.S. App. LEXIS 23494 (8th Cir. Sept. 1, 1999).

92. *Connecticut Valley Elec. Co. v. Patch*, 119 S. Ct. 1458 (1999).

93. *Public Service Co. of New Hampshire v. Patch*, 167 F.3d 29 (1st Cir. 1998).

C. *Southern California Edison Co. v. FERC*⁹⁴

The U.S. Court of Appeals for the D.C. Circuit issued a ruling addressing the propriety of a state-imposed interstate gas transportation surcharge that would allow a pipeline to recover the cost difference between what it pays for capacity and what it receives for releasing that capacity. The surcharge essentially allowed Southern California Gas Company (SoCal) to release capacity for a cheaper price than what SoCal paid for it without sustaining any loss. Southern California Edison Company (Edison) filed a complaint with the FERC, stating that SoCal could abuse its market power by giving its own affiliates lower prices for released capacity than it gives anyone else without losing transportation revenue. The FERC dismissed Edison's complaint, stating that the rates being charged were just and reasonable and that the released capacity prices did not exceed the maximum tariff rate.⁹⁵

The D.C. Circuit remanded the case back to the FERC, requiring it to consider Edison's complaint. The court instructed the FERC not only to consider whether rates are unjust or unreasonable, but also whether the lower rates constitute unjust and unreasonable practices or unduly discriminatory or preferential rates or practices.⁹⁶ The court noted that the surcharge created "perverse incentives" for SoCal which the FERC should have considered.⁹⁷ The court stated that the surcharge would allow SoCal to sell to its own affiliates at lower prices, while selling to others at unacceptable prices, and without having to reduce its transportation revenue.

D. *California Independent System Operators v. FERC*⁹⁸

On January 8, 1999, the D.C. Circuit rejected a request to stay a FERC order⁹⁹ requiring the removal of certain provisions in the California Independent System Operators (ISO) and the California Power Exchange Corporation (PX) bylaws. This dispute between the California Oversight Board (Oversight Board) and the FERC originated in November 1996, when the FERC rejected requirements that board members of the ISO and the PX be California residents and that the Oversight Board play a permanent role in the governance and operations of the ISO. The FERC maintained that the residency requirement would discourage out-of-state participation in the new market and that Oversight Board governance would impair the independence of the ISO.¹⁰⁰ The FERC rejected requests to stay and reconsider its decision.¹⁰¹

By November 1998, the Oversight Board had not complied with the FERC's order to remove the requirements from the ISO and the PX bylaws.

94. *Edison*, 172 F.3d 74. See also *infra* Part VII.D, for further discussion of this case.

95. *Southern Cal. Edison Co. v. Southern Cal. Gas Co.*, 79 F.E.R.C. ¶ 61,157, *reh'g denied*, 80 F.E.R.C. ¶ 61,390 (1997).

96. *Edison*, 172 F.3d at 75.

97. *Id.* at 76.

98. *California Indep. Sys. Operators v. FERC*, *appeal docketed*, Nos. 98-1225 *et al.* (D.C. Cir.).

99. *California Power Exch. Corp.*, 85 F.E.R.C. ¶ 61,263 (1998).

100. *Pacific Gas and Elec. Co.*, 77 F.E.R.C. ¶ 61,204 (1996).

101. *California Indep. Sys. Operator*, 82 F.E.R.C. ¶ 61,223 (1998).

Therefore, the FERC threatened legal action against the ISO and the PX unless they removed: (1) provisions allowing the Oversight Board to appoint governing board members; (2) the California residency requirement for board members; (3) the requirement that the Oversight Board approve changes to the ISO or the PX bylaws; and (4) the Oversight Board's role in hearing appeals of the ISO governing board decisions, except for state jurisdictional matters.¹⁰²

The Oversight Board has maintained that it is required to comply with a state law mandating that the Oversight Board play a role in the ISO's and the PX's governance and that board members be residents of California. The Oversight Board contends it is in the position of being required to serve "several masters," specifically the state legislature and the FERC. According to the Oversight Board, the ISO, and the PX are neutral parties trying to avoid being caught in the middle of a jurisdictional dispute.

Nonetheless, the D.C. Circuit Court denied the request for a stay of the FERC's order. Upon this denial, the ISO and the PX filed the revisions requested by the FERC. In filing the revisions, the ISO and the PX stated that they hope the FERC will discuss the jurisdictional issues with the State of California. The ISO and the PX also informed the FERC that a California state senator had already introduced legislation removing the ISO and the PX from the FERC's jurisdiction.¹⁰³

Despite the denial of the stay, the Oversight Board still has a pending appeal of the FERC's initial order on this matter. The appeal was filed with the D.C. Circuit in the Spring of 1998, but has not been scheduled for argument.¹⁰⁴

*E. Columbia Gas Transmission Corporation v. Drain*¹⁰⁵

In this case the U.S. Court of Appeals for the Fourth Circuit ruled that a dispute over an interstate pipeline easement is a state, not a federal issue. The case originated when Columbia Gas Transmission Corporation (Columbia) and a landowner disputed the extent to which the pipeline had an easement across the landowner's property.

In 1950, Columbia's predecessor had obtained a right-of-way for an eight inch diameter line across the landowner's property, but the applicable agreement did not specify the width of the right-of-way. Columbia did not object when the landowner built structures near the line, including a home which was built within 7.5 feet of the line. Subsequently, several years after the structures near the line were built, Columbia told the landowner that its easement extended for twenty-five feet on either side of the right-of-way and that she had to move her home. In 1994, Columbia went to U.S. District Court for a ruling on the easement.

The court held that eminent domain actions are properly brought under the NGA in Federal Court. In this case, however, Columbia did not bring an eminent domain proceeding - it was asking the court to declare that it already owned the fifty foot right-of-way. The action was determined to be a common law

102. 85 F.E.R.C. ¶ 61,263, at 62,063-66.

103. *California Elec. Oversight Bd.*, 88 F.E.R.C. ¶ 61,172 (1999).

104. *California Indep. Sys. Operators v. FERC*, appeal docketed, Nos. 98-1225 *et al.* (D.C. Cir.).

105. *Columbia Gas Transmission Corp. v. Drain*, 191 F.3d 552 (4th Cir. 1999)

property dispute. The court stated that "[t]he allocation of property rights among contracting parties is a paradigmatic question of state law."¹⁰⁶ Therefore, neither the Natural Gas Pipeline Safety Act nor the NGA created jurisdiction over this action.

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106. *Id.* at 556.

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