

REPORT OF THE OIL & LIQUIDS PIPELINE REGULATION COMMITTEE

This report summarizes policy developments and legal decisions that have occurred at the Federal Energy Regulatory Commission (FERC or Commission) and the U.S. Courts of Appeals in the area of oil and liquids pipeline regulation. The time frame covered by this report is the period between July 1, 2009, and June 30, 2010.*

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I. SIGNIFICANT ADMINISTRATIVE ORDERS

A. *Jurisdictional Issues*

1. Mid-America Pipeline Co., 131 F.E.R.C. ¶ 61,012 (2010)

On March 11, 2010, Mid-America Pipeline Company, L.L.C. (Mid-America) filed a tariff cancelling naphtha and refinery grade butane (RGB) transportation service on one of its batched natural gas liquids lines.¹ Prior to the cancellation, the line moved five products (normal butane, isobutane, RGB,

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1. *Mid-America Pipeline Co.*, 131 F.E.R.C. ¶ 61,012 (2010).

natural gasoline, and naphtha). After the cancellation, the line moved only normal butane, isobutane, and natural gasoline. Mid-America stated that the level of naphtha and RGB volumes did not justify the expense in continuing to move them.

Flint Hills Resources, L.P. (Flint Hills) filed a protest, claiming that the naphtha and RGB were essential to its refining operations and that it had no other means of obtaining the products. Flint Hills contended that all of the products transported by Mid-America were natural gas liquids which, Flint Hills claimed, represented a single service. Since Mid-America was not proposing to cancel transportation for all natural gas liquids, Flint Hills argued, the Commission had authority to review the proposed cancellation. For support, Flint Hills relied on *Amoco Pipeline Co.*, in which the Commission exercised jurisdiction over a crude oil pipeline's proposal to cancel certain origin points while continuing to provide service from other origins.²

On April 9, 2010, the Commission allowed the tariff to take effect without suspension or investigation. The FERC held that it "lack[ed] jurisdiction to require a pipeline to hold itself out to provide service that the pipeline proposes to abandon completely."³ The FERC found that each product transported by Mid-America represented "a distinct service."⁴ The Commission relied on an affidavit provided by Mid-America showing that the different natural gas liquids products were "distinct commodities [with] 'different chemical and physical properties, different uses, different prices, different markets and different transportation characteristics.'"⁵ The Commission explained that in *Amoco*, by contrast, the pipeline's "proposal did not constitute the complete abandonment of a distinct service because Amoco would continue crude oil service over the remainder of the line."⁶

On May 10, 2010, Flint Hills filed a request for clarification or, in the alternative, request for rehearing. On July 9, 2010, Flint Hills withdrew its protest and request for clarification, noting a settlement with Mid-America.

2. TE Products Pipeline Co., L.L.C., 130 F.E.R.C. ¶ 61,257 (2010)

On March 1, 2010, TE Products Pipeline Co., L.L.C. (TEPPCO) removed from its tariff charges for truck loading and odorization services provided at its destination terminals.⁷ Two groups of shippers protested, arguing that the terminal facilities were FERC-jurisdictional, and that the services provided at the terminals should be included in the tariff.

2. *Amoco Pipeline Co.*, 83 F.E.R.C. ¶ 61,156, 61,672-73 (1998).

3. 131 F.E.R.C. ¶ 61,012 at P 23 (2010).

4. *Id.* at P 25.

5. *Id.* at P 24. (quoting Response of Mid-America Pipeline Company, L.L.C. to Protest of Flint Hills Resources, L.P., Mar. 31, 2010, at 6 (citing Collingsworth Aff. at ¶¶6-7, 11)).

6. *Id.* at P 26.

7. The TEPPCO line in question moves propane and butane from the Gulf Coast through the Midwest to New York. The odorization service consists of adding a chemical to propane to give it a distinctive smell to alert end users to possible leaks.

On March 30, 2010, the Commission rejected the protest and allowed the tariff to take effect without suspension or investigation.⁸ The FERC explained that “[a] service is subject to the [Interstate Commerce Act] and the Commission’s jurisdiction only if it is ‘integral’ or ‘necessary’ to the pipeline transportation function.”⁹

The FERC found that, under that test, the terminal services were not jurisdictional for three reasons. First, the services occurred “at the destination point after transportation of propane and butane products ha[d] been completed.”¹⁰ Second, neither service was necessary for pipeline transportation, in contrast to the breakout storage tanks in Lakehead that were found to be “the functional equivalent of missing pipe.”¹¹ Third, many of the terminals connected to the TEPPCO system were operated by non-affiliated companies that did not file FERC tariffs.¹² The Commission concluded that, while TEPPCO may have provided the services as a convenience to shippers, the Commission had “no authority to prevent TEPPCO from removing these non-jurisdictional services from its tariff.”¹³

Shippers filed a request for rehearing on April 29, 2010. On June 28, 2010, the Commission denied the request.¹⁴ The Commission stated that it “continues to find that the terminalling facilities and services that were removed from TEPPCO’s tariff are non-jurisdictional.”¹⁵ The FERC reiterated its prior holding “that jurisdictional transportation is completed when the product enters the terminal facilities and [the] facilities are not integral or necessary to the transportation function.”¹⁶ The Commission explained that “the terminal facilities are not on TEPPCO’s mainline system and consist of smaller pipes, metering facilities, and storage tanks, in addition to the truck unloading facilities.”¹⁷ The FERC noted that “[t]he fact that storage tanks are . . . found at the terminal facilities shows that something other than jurisdictional transportation is occurring at these facilities.”¹⁸ In addition, the FERC stated that “[i]t is also important to note that throughout the industry and on TEPPCO’s system, other entities provide the same or similar terminalling services as TEPPCO and they do not have FERC tariffs on file.”¹⁹ The Commission concluded that “the physical nature of the terminalling facilities . . . and the fact that these services are provided by non-jurisdictional entities supports the

8. *TE Prods. Pipeline Co.*, 130 F.E.R.C. ¶ 61,257 (2010).

9. *Id.* at P13 (citing *Lakehead Pipe Line Co.*, 71 F.E.R.C. ¶ 61,338, at p. 62,325 (1995), *order on reh’g*, 75 F.E.R.C. ¶ 61, 181, at p. 61,601 (1996)).

10. *Id.* at P 14.

11. *Id.*

12. *Id.* at P 15.

13. *Id.* at P 14.

14. *TE Prods. Pipeline Co.*, 131 F.E.R.C. ¶ 61,277 (2010).

15. *Id.* at P 10.

16. *Id.* at P 12.

17. *Id.*

18. *Id.*

19. *Id.*

conclusion that they are not integral or necessary for jurisdictional transportation.²⁰

3. *Western Refining Southwest, Inc. v. TEPPCO Crude Pipeline, L.L.C.*, 127 F.E.R.C. ¶ 61,288 (2009)

On February 9, 2009, Western Refining Southwest, Inc. and Western Refining Pipeline Company (collectively Western Parties) filed a complaint against TEPPCO Crude Pipeline, L.L.C. (TEPPCO Pipeline), alleging that TEPPCO Pipeline violated its statutory, regulatory, and contractual obligations to the Western Parties by reversing the flow of its pipeline, illegally retaining crude oil belonging to the Western Parties, and continuing to demand lease payments.²¹

Western Parties amended their complaint on March 4, 2009, “alleging that TEPPCO Pipeline was illegally retaining additional crude oil owned by the Western Parties.”²² The Western Parties asked the FERC to “order TEPPCO Pipeline to pay damages resulting from the lease payments allegedly retained illegally by TEPPCO Pipeline and the lost value of the crude oil allegedly seized illegally by TEPPCO Pipeline.”²³

On June 22, 2009, the Commission dismissed the complaint for lack of jurisdiction.²⁴ The FERC determined that the foundation of the parties’ dispute – a Capacity Lease Agreement – “created property and contractual rights allowing Western Pipeline to operate its own pipeline within the TEPPCO Pipeline facilities,” rather than a common carrier relationship.²⁵ Accordingly, the allegations in the complaint did not “involve the Commission’s jurisdiction over oil pipeline transportation,” but rather arose from “a private contract governing property rights that is solely within the jurisdiction of the appropriate state court to resolve.”²⁶

The Commission order noted that submission of required notices by Western Refining to TEPPCO Pipeline and the receipt of bills did not establish a common carrier/shipper relationship.²⁷ The billing invoices demonstrated that “the various charges being paid by Western Pipeline were incurred pursuant to the lease agreement,” and that “no transportation charges were assessed as would occur if either of the Western Parties received common carrier service pursuant to FERC Tariffs.”²⁸ Because the Commission dismissed the complaint for lack of jurisdiction, the Commission also denied the interventions and request for consolidation of Resolute Natural Resources Company and Resolute Aneth, L.L.C. (collectively Resolute).²⁹

20. *Id.*

21. *W. Refining Sw., Inc. v. TEPPCO Crude Pipeline, L.L.C.*, 127 F.E.R.C. ¶ 61,288 (2009).

22. *Id.*

23. *Id.*

24. *Id.*

25. *Id.* at P 27.

26. *Id.* at P 25.

27. *Id.*

28. *Id.*

29. *Id.* at P 31.

On July 20, 2009, the Western Parties filed for rehearing of the Commission's June 22 Order, and argued that the Commission was required by statute to investigate and set for hearing their complaint, which alleged that the common carrier was acting in an unjust, unreasonable, or discriminatory manner, regardless of any private contractual arrangement.³⁰ On July 21, 2009, Resolute filed for rehearing of the Commission's denial of its intervention in the proceeding.³¹

On October 22, 2009, the Commission denied rehearing and affirmed that the Commission does not have jurisdiction over this private contractual dispute. The Commission found that the Western Parties attempted "to artificially create common carrier/shipper relationships where none exist[ed] in an effort to create jurisdiction over a private contractual dispute."³² In addition, the Commission denied Resolute's request for rehearing as Resolute was not a party to the contract at issue and had not claimed that it had any third-party beneficiary interest affected by the lease agreement.³³

4. West Texas LPG Pipeline Limited Partnership, 128 F.E.R.C. ¶ 61,066 (2009)

"On June 18, 2009, West Texas LPG Pipeline Limited Partnership (WTP) filed Supplement No. 1 to [its] FERC Tariff No. 49 to be effective June 18, 2009."³⁴ The Supplement would cancel the Denton, New Mexico plant as a transportation origin point. WTP's Tatum Lateral connected to the Denton Plant had "recently sustained third-party damage, and... no requests for transportation from this point [had been made] since November 2007."³⁵

Davis Gas Processing, Inc. (Davis), owner and operator of the Denton Plant, and WTG Gas Marketing, Inc. (WTG), a marketer who had arranged to purchase and sell natural gas liquids from the Denton Plant, filed a timely motion to intervene and protest.³⁶ While acknowledging that the Commission lacked jurisdiction over oil pipeline abandonments, the protestants asserted that the immediate cancellation of service from the Denton Plant is unsupported and improper, and that the proposed Supplement No. 1 is unjust and unreasonable.³⁷ WTP responded that continued service would require costly inspection work and hydrostatic testing, and, in addition, the Commission lacked jurisdiction citing the Commission's recent decision in *Rocky Mountain Pipeline System, L.L.C.*³⁸

The Commission accepted the filing on July 17, 2009, and agreed that, in light of the Commission's uncontested lack of jurisdiction over complete abandonments of service, "it was unnecessary... to address other issues presented by the protesting parties."³⁹

30. *W. Refining Sw., Inc. v. TEPPCO Crude Pipeline, L.L.C.*, 129 F.E.R.C. ¶ 61,053 at P 5-6 (2009).

31. *Id.*

32. *Id.* at P 11.

33. *Id.* at P 19.

34. *West Texas LPG Pipeline Ltd. P'ship*, 128 F.E.R.C. ¶ 61,066 at P 1 (2009).

35. *Id.*

36. *Id.* at P 4.

37. *Id.* at P 7.

38. *Id.* at P 8.

39. *Id.* at P 9 (footnote omitted).

WTP subsequently filed on June 29, 2009, in Docket No. IS09-410-000, Supplement No. 1 to FERC Tariff No. 52 to cancel the Denton, New Mexico plant as a transportation origin point, in light of the FERC's actions in Docket No. IS09-401. Davis and WTG raised objections similar to those raised in the earlier proceeding. In light of the July 17 order, which relied on the Rocky Mountain decision, the Commission rejected the protests and accepted WTP's filing in a July 29, 2009, order.⁴⁰

B. *Ratemaking Issues*

1. BP Pipelines (Alaska) Inc., 127 F.E.R.C. ¶ 61,317 (2009)

This is the third in a series of orders regarding the FERC's requirement that the Trans Alaska Pipeline System (TAPS) Carriers adopt a uniform rate and a revenue pooling mechanism. In the first order, the Commission held that the TAPS Carriers' practice of charging different rates for their respective transportation services on TAPS was unjust and unreasonable, and ordered the Carriers to file a uniform rate.⁴¹ In the second order, the Commission denied rehearing of the uniform rate requirement, and also ordered the Carriers to implement a revenue pooling mechanism.⁴² In its third order, the Commission denied a request for rehearing of the second order, in which three of the TAPS Carriers - ConocoPhillips, ExxonMobil, and Unocal (Indicated TAPS Carriers) - had challenged the Commission's authority under section 5(1) of the Interstate Commerce Act (ICA) to impose a pooling mechanism absent the assent of all Carriers involved.⁴³

In denying the Indicated TAPS Carriers' request for rehearing, the Commission explained that it did not act under ICA section 5(1) when it ordered pooling. Rather, it acted pursuant to its ancillary authority under the ICA to establish a pooling mechanism as "a necessary incident to [its statutory obligation to] establish[] . . . just and reasonable rate[s]" for TAPS.⁴⁴ The Commission explained that it had determined, "that the practice of each TAPS Carrier charging an individual rate resulted in unjust and unreasonable rates because . . . differences in the carriers' rates were not based on differences in [their] costs of providing service."⁴⁵ Further, "because of TAPS' unique cost/revenue allocation methodology" (in which a Carrier's costs are based on its percentage ownership of TAPS, while its revenues are based on its throughput share), "a uniform rate would lead to under- or over-recovery when a [C]arrier's throughput differed from its ownership share."⁴⁶ For this reason, a pooling mechanism was necessary to ensure that the Carriers do not over- or under-recover their costs.⁴⁷ However, the Commission allowed the Carriers to include the pooling mechanism in their tariffs rather than via a modification to the TAPS

40. *West Texas LPG Pipeline Ltd. P'ship*, 128 F.E.R.C. ¶ 61,098 (2009).

41. *BP Pipelines (Alaska) Inc.*, 123 F.E.R.C. ¶ 61,287 (2008) (Opinion No. 502).

42. *BP Pipelines (Alaska) Inc.*, 125 F.E.R.C. ¶ 61,215 (2008).

43. *BP Pipelines (Alaska) Inc.*, 127 F.E.R.C. ¶ 61,317 at P 26 (2009).

44. *Id.* at P 27 (internal quotation marks omitted).

45. *Id.* at P 30.

46. *Id.*

47. *Id.*

Operating Agreement, as it had previously required in the second order described above.⁴⁸

2. BP West Coast Products, L.L.C. v. Calnev Pipe Line, L.L.C., 129 F.E.R.C. ¶ 61,109 (2009)

On November 5, 2009, the Commission issued its “Order on Audit Complaints,” in *BP West Coast Products, L.L.C. v. Calnev Pipe Line, L.L.C.*, in which it addressed four related complaints filed by shippers, BP West Coast Products, L.L.C. (BP West Coast) and Tesoro Refining and Marketing Company (Tesoro), against the affiliated pipelines, SFPP, L.P. and Calnev Pipeline, L.L.C.⁴⁹

The complaints requested that the Commission commence an audit of the pipelines’ Form No. 6 for two recent years, to allow for the investigation of the underlying workpapers and basis for the pipelines’ Page 700 calculations. The complainants raised differing arguments in support of the relief sought, but generally contended that under the Commission’s standards for challenging annual index increases, shippers needed to produce a “look behind” the Page 700 earnings data in order to support a complaint.⁵⁰ BP West Coast argued that, following an audit and a staff analysis of the underlying data, the resulting data would allow the shippers to meet their burden to show that the pipelines’ indexed rate increases were “substantially in excess of the actual cost increases.”⁵¹ Tesoro argued that there were excessive earnings by the respondent pipelines, relying in part on evidence submitted in another complaint proceeding, but urged that it needed “underlying documentation” to pursue some claims of unsupported costs, such as excessive overhead allocations.⁵² The respondent pipelines answered and denied the complainants’ claims, arguing that they had failed to make an adequate showing to support a complaint or to require an audit, and in addition defended the data in the Form No. 6 reports, among other defenses.⁵³

The Commission dismissed the complaints, finding that they did not meet the standard enunciated in its earlier orders that had prompted the complaints, i.e., that the complaint did not provide “reasonable grounds to conclude that the pipeline did not properly apply its existing cost-of-service methodology to develop the underlying cost inputs used to develop the Page 700 in its annual FERC Form No. 6, or the inputs were improperly entered into its accounts or the calculations.”⁵⁴

The Commission concluded instead that the complaints appeared to be “a discovery attempt that is [far] beyond the purpose of an audit complaint” as required by the earlier precedent.⁵⁵ The Commission also found that Tesoro

48. *Id.* at P 41.

49. *BP W. Coast Prods., L.L.C. v. Calnev Pipe Line, L.L.C.*, 129 F.E.R.C. ¶ 61,109 (2009) (Audit Order).

50. *Id.* at P 2.

51. *Id.* at P 3.

52. *Id.* at P 5-6.

53. *Id.* at P 7-13.

54. *Id.* at 14. (citing *BP W. Coast Prods., L.L.C. v. SFPP, L.P.*, 121 F.E.R.C. ¶ 61,243 at P 9 (2007)).

55. 129 F.E.R.C. ¶ 61,109 at P 15.

failed to provide an analysis showing that the pipelines' Page 700 was incorrect, or that the underlying accounting data was not correctly captured. Instead, the Commission found that the complainants' assertions "all address whether the respondent pipelines had a correct cost of service methodology embedded in their rates, not whether they properly applied their existing methodologies to a year of pipeline operations and reported the results correctly."⁵⁶ Tesoro's criticism of the pipelines' rate design, the Commission concluded, was misplaced, and belonged in a complaint against the base rates, not an audit request. Consequently, the Commission found that the complainants did not meet their burden of proof, by presenting evidence that was not actually linked to the errors or activities or omissions that were the subject of the complaint, and because they were too general and failed to provide reasonable grounds for concluding that the threshold had been met.⁵⁷

3. *Calnev Pipe Line, L.L.C.*, 127 F.E.R.C. ¶ 61,304 (2009), order on reh'g., 130 F.E.R.C. ¶ 61,082 (2010)

In two related orders, the Commission further addressed its standards for challenging pipeline rate increases filed pursuant to the index regulations.

On June 26, 2009, the Commission issued its "Order on Tariff Filing," in *Calnev Pipe Line, L.L.C.*, in which it addressed protests filed by shippers to a rate increase filed by Calnev based on the Commission's index for oil pipeline rates effective on July 1, 2009.⁵⁸ Calnev rates were subject to ongoing complaint litigation regarding the base rates, but it filed to increase rates by a percentage higher than the yearly index because the prior rates were below the index ceiling level. Certain shippers filed protests, arguing that the filing should be made subject to refund because the base rates were subject to a complaint and investigation; that the pipeline was over-recovering its costs, which would be exacerbated by the filing; that the cost increase was not supported if the increase in return were eliminated; that the rates included improper costs and methodologies; that the current regulations failed to provide adequate information or rights to shippers to challenge the filings; and other arguments.⁵⁹ Calnev filed an answer addressing and denying these assertions.

The Commission accepted the filing, finding that the protests failed to demonstrate that the rate increase violated the index regulations. Rather, the Commission concluded that the pipeline had shown that the pipeline's actual cost increases exceeded the index increase. The Commission stated that the accuracy of the costs and accounting underlying the pipeline's cost showing are not reviewed in the context of a protest to an index filing, but rather in a complaint against the increased rates. Further, the Commission found that the indexed increase would not be subject to refund obligations simply because the underlying rates were subject to a complaint. The Commission found other criticisms to be unsupported or to constitute collateral attacks on its policies.⁶⁰

56. *Id.* at P 17 (emphasis omitted).

57. *Id.* at P 18.

58. *Calnev Pipe Line, L.L.C.*, 127 F.E.R.C. ¶ 61,304 (June 26, 2009) (*Calnev I*).

59. *Id.* at P 3.

60. *Id.* at P 5.

On rehearing, the protesting shippers argued that the Commission had failed to adequately address their argument that the pipeline's "2009 index increase substantially exacerbates Calnev's existing over recovery of its cost of service."⁶¹ After dismissing one rehearing request as being procedurally deficient,⁶² the Commission denied rehearing and further explained its rationale for rejecting the shippers' argument: that protests to index filings were intended in the indexing system to be a simplified, "preliminary screening tool" comparing year-to-year changes in costs and revenues under the "percentage comparison test" based on Page 700 data.⁶³ Other arguments are not considered in such protests, although the Commission stated that a wider range of factors would be considered in a complaint proceeding against an index-based rate increase – including the "substantially exacerbates standard," which had been found to warrant investigation in a complaint context.⁶⁴ Here, in contrast, the Commission found that the protesters had failed to meet the "percentage comparison test" appropriate to a protest to index-based increases.⁶⁵

4. Enbridge Pipelines (Toledo), Inc., 130 F.E.R.C. ¶ 61,270 (2010)

Enbridge Energy, Limited Partnership (Enbridge Energy) made four tariff filings related to its Alberta Clipper Project (Project). Each tariff filing established surcharges to recover costs incurred to complete the Project. Enbridge Energy and the Canadian Association of Petroleum Producers (CAPP), which represents almost all of the producers that ship crude on the pipeline, agreed to establish the surcharges in a settlement. In a separate petition for declaratory order filing, Suncor Energy Marketing Inc. (Suncor) sought a determination that, due to dramatically changed circumstances, the Commission-approved long-term rate methodology for the U.S. portion of the Project would not result in just and reasonable rates in the near term, and therefore urged the Commission to deny Enbridge Energy's filings to effectuate the surcharges.⁶⁶ On March 31, 2010, the Commission accepted the tariffs, as proposed, and dismissed Suncor's request as moot.⁶⁷

In considering Suncor's petition for declaratory order, the FERC stated that providing declaratory relief is discretionary. "While a declaratory order may have been appropriate in the absence of an actual tariff filing by Enbridge Energy,"⁶⁸ such was not the case here because Enbridge Energy did make tariff filings. Thus, any issues concerning the recovery of costs of the Project would be properly addressed in the tariff filing proceeding. Because Suncor raised the same issues in its protest of Enbridge Energy's tariff filings as it did in its petition for declaratory order, and had the additional benefit of commenting on the actual Project costs in the tariff filing proceeding, the FERC concluded that

61. *Calnev Pipe Line, L.L.C.*, 130 F.E.R.C. ¶ 61,082 at P 5 (2010) (*Calnev II*).

62. *Id.* at P 7 (the party failed to include a separate "Statement of Issues" section in the rehearing request).

63. *Id.* at P 9-10.

64. *Id.* at P 11.

65. *Id.* at P 12.

66. *Enbridge Pipelines (Toledo), Inc.*, 130 F.E.R.C. ¶ 61,270 at P 26 (2010).

67. *Id.* at P 26.

68. *Id.*

Suncor would not be prejudiced by the decision to dismiss the petition for declaratory order as moot.⁶⁹

After reviewing the various protests to Enbridge Energy's tariff filing, the Commission accepted the tariff filings as proposed.⁷⁰ The protestors argued that the Project costs may not have been calculated in accordance with the approved methodology, and that Enbridge Energy should be required to address those issues. The Commission rejected the protestors' arguments.

Specifically, the protestors argued that "Enbridge Energy improperly applied its capital structure for each surcharge, because it allegedly failed to use the capital structure of 55% equity and 45% debt included in the settlements."⁷¹ Enbridge Energy stated that its previous settlement adopted a stipulated capital structure to avoid the need to re-determine the actual capital structure on an annual basis. For purposes of implementing the Opinion No. 154-B methodology, Enbridge Energy argued that it was necessary to adjust the weighted average cost of capital to assure that the pipeline's deferred earnings receive an equity rate of return. Thus, "Enbridge Energy . . . appropriately made that adjustment in all of its cost-of-service surcharge calculations."⁷²

The protestors also asserted that Enbridge Energy improperly calculated the return on equity for one of the surcharges. Enbridge Energy explained that the protestors had failed to consider that the nominal equity rate of return must be adjusted for inflation in the prior years as had been done consistently since 1998. Thus, Enbridge Energy made a corresponding adjustment to reduce deferred earnings by the same negative inflation percentage, so the net effect over time was a wash.⁷³

In addition, the protestors argued that Enbridge Energy incorrectly claimed a return for pipeline integrity work. Enbridge Energy stated that since it had been incorporating such costs in the same way since 1996, and CAPP had approved these integrity cost charges for years, it was unclear why the protestors were only now challenging this practice. Finally, the protestors asserted that the tariff filings indicated that there was a drop in throughput of approximately 18% from 2009 to 2010, and this decrease accounted for significant rate increases. Enbridge Energy explained that the Project would not be in service for the full year. Thus, both the throughput and costs were reduced accordingly.⁷⁴

The Commission found that Enbridge Energy adequately responded to the protests and demonstrated that the tariff filings conformed to the methodology contained in the previous settlement.⁷⁵ Thus, no further review was necessary. The protestors also requested cost support for other cost elements. The Commission rejected such requests because Enbridge Energy was not required to include such justifications or additional data in its tariff filings. Therefore, the

69. *Id.*

70. *Id.* at P 27.

71. *Id.* at P 28.

72. *Id.*

73. *Id.* at P 29.

74. *Id.* at P 31.

75. *Id.* at P 32.

FERC concluded that the generalized assertions by the protestors were not enough to require further cost support, let alone any formal discovery.⁷⁶

5. MarkWest Michigan Pipeline Company, L.L.C., 130 F.E.R.C. ¶ 61,084 (2010)

In January 2006, MarkWest Michigan Pipeline Co., L.L.C. (MarkWest) filed a settlement in Docket No. IS06-41-000 under which MarkWest established initial tariff rates. The settlement established a three-year moratorium prohibiting MarkWest from adjusting its rates with limited exceptions. An exception to the moratorium permitted MarkWest to increase its rates annually up to a defined Annual Inflation Cap. The Annual Inflation Cap was below the ceiling level established by the Commission's indexing regulations, 18 C.F.R. § 342.3(a). The moratorium was in effect from January 2006 through January 2009. During this moratorium, MarkWest increased its rates three times, applying the 2006 settlement's Annual Inflation Cap. As a result of this cap, upon expiration of the moratorium, MarkWest's rates were below what the rates would have been had MarkWest taken the full annual index adjustment pursuant to the Commission's indexing regulations.

On February 24, 2009, MarkWest Michigan filed a tariff case seeking to increase its rates pursuant to the FERC's indexing methodology. Specifically, MarkWest proposed to increase its rates to the ceiling levels that would have applied on February 1, 2009, under the indexing methodology absent the 2006 settlement agreement. On March 31, 2009, the Commission rejected MarkWest's filing as inconsistent with the Commission's regulations.⁷⁷ The Commission also clarified that MarkWest's ceiling rates for the index year ending June 30, 2009, were the rates established by MarkWest's July 1, 2008, rate filing, not the ceiling rates that would have existing on February 1, 2009, absent the 2006 settlement.

MarkWest requested rehearing of the Commission's March 31 order. On February 2, 2010, the Commission denied rehearing.⁷⁸ The Commission confirmed its previous finding that the rate increases MarkWest received on July 1, 2008, pursuant to the terms of the 2006 settlement, became MarkWest's ceiling level for that index year (July 1, 2008, through June 30, 2009).

Pursuant to section 342.3(d)(5) of the Commission's regulations, "[w]hen an initial rate, or rate changed by a method other than indexing, takes effect during the index year, such rate will constitute the applicable ceiling level for that index year."⁷⁹ MarkWest changed its rates during the 2006/2007 index year by a method other than indexing. Thus, pursuant to the terms of section 342.3(d)(5) of the Commission's regulations, MarkWest's July 27, 2006, filed rate became its ceiling level for the remainder of the 2006/2007 index year. This process was repeated for the 2007-2008 index year and the 2008-2009 index

76. *Id.* at P 27.

77. *MarkWest Michigan Pipeline Co.*, 126 F.E.R.C. ¶ 61,300 (2009).

78. *MarkWest Michigan Pipeline Co.*, 130 F.E.R.C. ¶ 61,084 (2010).

79. 18 C.F.R. § 342.3(d)(5) (2010).

year. Thus, the rate increases filed by MarkWest pursuant to the 2006 settlement for the 2008-2009 index year became the ceiling level for that year.

The Commission clarified, however, that upon expiration of the moratorium period, MarkWest was free to file a petition to change its rates pursuant to any other rate methodology available to it under the applicable Commission regulations for the 2008-2009 index year.⁸⁰ For example, MarkWest could have filed for cost-of-service rates, market-based rates, or new settlement rates. The Commission's regulations only barred MarkWest from seeking to increase its rates pursuant to the FERC's indexing methodology for the 2008-2009 index year.

6. SFPP, L.P., 127 F.E.R.C. ¶ 61,312 (2009), order on reh'g, 130 F.E.R.C. ¶ 61,081 (2010)

Numerous protests were filed against SFPP, L.P.'s application of the index to its rates to be effective on July 1, 2009, including the argument that under the rule in MarkWest,⁸¹ certain rates could not be indexed because they had been charged as "settlement rates" during the year prior to July 1, 2009; that the rates should be made subject to refund because of a pending complaint against the underlying rates; that faulty accounting and other factors resulted in excessively high pre-existing rates; that the pipeline's cost increases were disproportionately due to investment in one segment whose rates alone should qualify for the index increase; that the indexed increase would exacerbate already excessive rates; and other concerns.⁸² The Commission accepted the rates subject to one modification. The Commission concluded that one tariff rate was the result of a settlement rate filed within a year of July 1, 2009, and thus was subject to the principle announced in MarkWest that such a settlement rate becomes a new ceiling rate for the index year in which it becomes effective.⁸³

The Commission rejected the other protesting parties' arguments, finding that because the pipeline had shown that the actual level of its cost increases exceeded the increase in revenues from the indexed increase, the protesting shippers could not show that the increase in rates would be so in excess of the pipeline's actual cost increases as to render the rates unreasonable; indeed, the Commission stated that it was "impossible to meet this standard if the dollar increase resulting from the application of the index is less than the actual dollar increase in the pipeline's costs in the previous year."⁸⁴ Further, the Commission found that a review of the dollar amounts occurs only in the context of a complaint, and that as found in prior cases, "the appropriateness of the individual cost factors embedded in . . . [the] cost of service," would not be reviewed in an index protest context, but only in complaint, and that the same rule applied to claims of over-recovery of costs.⁸⁵ Similarly the Commission found that it would not address in a narrowly-focused, simplified protest proceeding a protesting party's concern that an investment in one segment was being applied

80. 130 F.E.R.C. ¶ 61,084 at P 18.

81. 126 F.E.R.C. ¶61,300 at P 3.

82. SFPP, L.P., 127 F.E.R.C. ¶ 61,312 at P 3-8 (2009).

83. *Id.* at P 19.

84. *Id.* at P 20.

85. *Id.* at P 21.

to the costs of the entire system.⁸⁶ The Commission also dismissed an “estoppel” argument relating to a differing inflation rate applied in the rate litigation, and rejected other criticisms as collateral attacks on the indexing methodology.⁸⁷

On rehearing, certain protesters argued principally that the Commission erred in relying on Form 6 cost of service data which was allegedly flawed, and that the Commission failed to adequately explain why the indexed increase would not “substantially exacerbate” the pipeline’s alleged over recovery of costs.⁸⁸ In an order, closely resembling the order in *Calnev II*⁸⁹ issued the same day (*See* discussion of *Calnev II supra*), the Commission dismissed one of the rehearing requests on procedural grounds, and rejected the argument against use of the Form 6 data and the failure to use the “substantially exacerbates” standard as both being inconsistent with the limited scope of an indexed rate proceeding.⁹⁰

II. SIGNIFICANT COURT DECISIONS

A. *ExxonMobil Oil Corp. v. FERC*, No. 07-1163, 2010 U.S. App. LEXIS 2620 (2010)

BP West Coast Products, L.L.C. (BP) and ExxonMobil Oil Corporation (Exxon) (collectively, the Shippers) petitioned for review of two FERC orders dismissing challenges to 2005 and 2007 index-based rate increases filed by SFPP. The D.C. Circuit dismissed both petitions in a per curiam opinion.⁹¹ The court decided: (1) “[t]he FERC did not abuse its [broad] discretion in holding that the shippers’ challenges to the pipeline’s rates and reported costs and revenue were outside the scope of a . . . proceeding,” to challenge an index-based rate filing under 18 C.F.R. § 343.2(c)(1); and (2) “the FERC [did not] abdicate[] its statutory obligation to ensure rates are just and reasonable . . . by limiting the scope of [BP’s and Exxon’s] complaints against index-based rate increases.”⁹²

The Shippers challenged the FERC’s decision regarding a 2005 index-based rate increase for SFPP’s North Line on the ground that the FERC departed from precedent without reasoned explanation.⁹³ BP and Exxon argued before the FERC that the index-based rate increase “was unnecessary because SFPP had recently increased its North Line rate under [18 C.F.R. § 342.4(a), which] permits rate adjustments for pipelines substantially under-recovering their cost of service.”⁹⁴ The Shippers claimed the recent North Line rate increase “fully compensated [SFPP] for its annual costs increases,” and that the additional index-based increase would result in unjust and unreasonable rates.⁹⁵ The FERC

86. *Id.*

87. *Id.* at P 20-23.

88. *SFPP, L.P.*, 130 F.E.R.C. ¶ 61,081 (2010).

89. 130 F.E.R.C. ¶ 61,082.

90. 130 F.E.R.C. ¶ 61,081 at P 5.

91. *ExxonMobil Oil Corp. v. FERC*, No. 07-1163, 2010 U.S. App. LEXIS 2620, at *6 (D.C. Cir. Feb. 5, 2010) (per curiam).

92. *Id.* at *5.

93. *BP W. Coast Prods., L.L.C. v. SFPP, L.P.*, 121 F.E.R.C. ¶ 61,195 (2007).

94. *ExxonMobil Oil Corp.*, 2010 U.S. App. LEXIS 2620, at *3.

95. *Id.*

acknowledged it recently denied SFPP an index-based rate increase for its East Line on similar grounds, but distinguished that case by noting that SFPP would continue to under-recover its cost of service on the North Line despite both rate increases.⁹⁶ The court denied review, stating that “[b]ecause the FERC adequately discussed why the shippers’ reliance on the East Line orders was misplaced, it did not depart from precedent without reasoned explanation.”⁹⁷ The court also denied Shippers’ request to “require the FERC to hold in abeyance their complaint against the 2005 North Line index-based rate increase” because the FERC’s order assured Shippers that all relief sought in the complaint could be recovered, if appropriate, in a separate, pending proceeding.⁹⁸

BP also petitioned for a review of a FERC order denying BP’s challenge to a 2007 index-based rate increase filed by SFPP.⁹⁹ BP West Coast claimed the FERC misconstrued 18 C.F.R. § 343.2(c)(1) in dismissing its complaint.¹⁰⁰ The FERC denied BP challenge to the 2007 rate increase on the ground that SFPP’s existing rate was already unjust and unreasonable, and that the increase would only add to an existing over-recovery.¹⁰¹ The FERC dismissed BP’s complaint, noting that BP could not meet its burden of showing the index-based rate increase was “substantially in excess of the actual cost increases incurred” as required by 18 C.F.R. § 343.2(c)(1).¹⁰² The FERC found the actual cost increases incurred by SFPP during the relevant year were greater than the revenue increase permitted by indexing.¹⁰³ The court dismissed the petition, finding the FERC’s interpretation of the regulation “to require dismissal of BP’s complaint was not ‘plainly erroneous or inconsistent with the regulation,’ . . . [and therefore] not arbitrary or capricious.”¹⁰⁴

B. *SFPP, L.P. v. FERC*, 592 F.3d 189 (2010)

In Opinion Nos. 435 and 435-A,¹⁰⁵ the FERC resolved complaints by shippers who used SFPP, L.P.’s (SFPP) Watson Station drain-dry facilities. Opinion Nos. 435 and 435-A stated that under section 1803 of the Energy Policy Act of 1992, rates for the drain-dry facilities (Watson Contract rates) were deemed reasonable and, although SFPP should have filed the Watson Contract rates, it would not be ordered to pay reparations.¹⁰⁶ In 2004, the D.C. Circuit remanded to the FERC for consideration of whether the rates were grandfathered.¹⁰⁷ On remand, the FERC ruled that the Watson Contract rates

96. *BP W. Coast Prods., L.L.C. v. SFPP, L.P.*, 121 F.E.R.C. ¶ 61,195 at P 7 (2007) (citing *SFPP, L.P.*, 117 F.E.R.C. ¶ 61,271 (2006)).

97. *ExxonMobil Oil Corp.*, 2010 U.S. App. LEXIS 2620, at *4.

98. *Id.* at *6.

99. *BP W. Coast Prods, L.L.C. v. SFPP, L.P.*, 123 F.E.R.C. ¶ 61,121 at P 1 (2008).

100. *Id.* at P 5.

101. *Id.* at P 4.

102. *Id.* at P 6.

103. *Id.* at P 2, 8.

104. *ExxonMobil Oil Corp.*, 2010 U.S. App. LEXIS 2620, at *4-*5 (quoting *Bluestone Energy Design, Inc. v. FERC*, 74 F.3d 1288, 1292, 316 U.S. App. D.C. 27 (D.C. Cir. 1996)).

105. *BP W. Coast Prods., L.L.C. v. FERC*, 374 F.3d 1263, 1270-71 (D.C. Cir. 2004).

106. *SFPP, L.P.*, 86 F.E.R.C. ¶ 61,022 (1999); *SFPP, L.P.*, 91 F.E.R.C. ¶ 61,135 (2000).

107. *BP W. Coast Prods, L.L.C.*, 374 F. 3d at 1270-71.

could not be grandfathered under section 1803 because, regardless of whether they were filed, the rates became effective after the cutoff date for grandfathered rates.¹⁰⁸ SFPP and the complaining shippers then settled all outstanding issues except two: (1) whether the Watson Contract rates established the rate level or limited reparations for drain-dry services provided prior to April 1, 1999; and (2) the calculation of the period for which any reparations payments would be due. These two legal issues were referred to an Administrative Law Judge, who ruled that the Watson Contract rates did not establish the rate for service because they had not been filed, and that the reparation period for each shipper would be limited to two years before the complaint was filed. Reparations were then awarded in the amounts stipulated in the settlement agreement.¹⁰⁹

On exceptions, the FERC affirmed the Initial Decision that SFPP's failure to file the Watson Contract rates violated sections 6(1) and 6(7) of the ICA.¹¹⁰ The FERC interpreted *Maislin Industries, U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116 (1990), as requiring ICA rate filings in order to prevent unreasonable or discriminatory rates. The FERC also concluded it properly exercised its remedial discretion to order reparations, and relied on *City of Piqua, Ohio v. FERC*, 610 F.2d 950 (D.C. Cir. 1979) to find that mutual agreement between SFPP and its shippers with respect to the Watson Contract rates did not relieve SFPP of the obligation to file the rates with the FERC.¹¹¹ The FERC also concluded that shippers were not required to establish damages because the settlement agreement established the value of any reparations due.¹¹²

SFPP petitioned for review of the Commission's determination that the Watson Contract rates did not establish the rate level applicable to drain-dry service provided prior to April 1, 1999, and the court denied the petition.¹¹³ The court explained that the "FERC premised its reasoning on its initial conclusion that SFPP had not violated its rate filing obligation,"¹¹⁴ and that once it was determined the Watson Contract rates were not grandfathered, an entirely different question was presented regarding whether the contracts otherwise established the rate level, or if reparations were due.¹¹⁵ The court upheld the FERC's determination that the ICA required SFPP to file the Watson Contract rates in order to collect those rates from shippers, even though shippers and SFPP agreed to the rates by contract. SFPP also argued that voiding the contracts was not the appropriate remedy for the ICA violation. The court clarified that the FERC did not void the contracts, but rather awarded SFPP the quantum meruit value of its performance under the contracts.¹¹⁶

SFPP also argued that the FERC unreasonably disregarded SFPP's argument that the failure to file the Watson Contract rates was a good faith error, and thus that the rates should be enforced despite not being filed. The court

108. *Id.* at 1272.

109. *SFPP, L.P.*, 118 F.E.R.C. ¶ 63,033 at P 52-64 (2007).

110. *SFPP, L.P.*, 122 F.E.R.C. ¶ 61,126 at P 4-10 (2008).

111. *Id.* at P 6-10.

112. *Id.* at P 10-15.

113. *SFPP, L.P. v. FERC*, 592 F.3d 189, 195 (D.C. Cir. 2010).

114. *Id.* at 192.

115. *Id.* at 192-93.

116. *Id.* at 193.

responded that the claim of good faith error was not supported by the joint stipulation of facts, that the ICA filing requirement does not depend on the FERC's interpretation of a party's good faith effort to comply with that requirement, and that because the obligation to file rates is on the carrier, SFPP had an opportunity to protect itself against the risk of reparations.¹¹⁷ The court also affirmed the FERC's dismissal of SFPP's argument that shippers needed to show not only that SFPP failed to file the rates, but also that they had suffered damage from the negotiated rates. The FERC ruled, and the court affirmed, that the settlement agreement established the level of reparations and "the only question was whether reparations were due, not the amount due."¹¹⁸

Finally, SFPP argued that "FERC erroneously denied that it had equitable discretion to fashion a remedy,"¹¹⁹ and that FERC had discretion under section 6(3) of the ICA to accept the rates without compliance with sections 6(1) and 6(7). Despite the FERC's statement that "the obligation to file the charges is absolute,"¹²⁰ the court found that the FERC acknowledged its "equitable discretion to fashion a remedy" when awarding reparations.¹²¹ The court dismissed the section 6(3) argument because SFPP did not raise it before the FERC. The court noted that, "even were this argument timely,"¹²² the FERC rejected SFPP's arguments that there is good cause to exercise such discretionary authority, and in fact exercised such authority by explaining that reparations were appropriate because the record suggested SFPP exercised market power by extracting economic rent via the Watson Contract rates.¹²³

117. *Id.* at 194.

118. *Id.*

119. *Id.*

120. *SFPP, L.P.*, 122 F.E.R.C. ¶ 61,126 at P 13.

121. *SFPP, L.P. v. FERC*, 592 F.3d 189, 195 (D.C. Cir. 2010).

122. *Id.* at 195.

123. *Id.*

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