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Assessment of Section 311 of the Natural Gas Policy Act of 1978

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ASSESSMENT OF SECTION 311 OF THE NATURAL GAS POLICY ACT OF 1978

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I. INTRODUCTION

> Only those who lived before the Revolution can know how sweet it can be. Talleyrand[1]

Although section 311 of the Natural Gas Policy Act of 1978 (NGPA)[2] was one of the least controversial sections when the NGPA was enacted by Congress, it may prove to be an important element in solving this country's energy problems[3] and a significant

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1. M. GUIZOT, MEMOIRES POUR SERVIR A L'HISTORIE DE MON TEMPES I, 6 (n.p. 1858) (translated from original French version).

2. 15 U.S.C. §§ 3301-3432 (Supp. III 1979). In Oklahoma v. Federal Energy Regulatory Comm'n, 661 F.2d 832 (10th Cir. 1981), *cert. denied*, 102 S. Ct. 2902 (1982); 102 S. Ct. 2903 (1982), the court upheld the constitutionality of the Natural Gas Policy Act of 1978 (NGPA) against charges that the imposition of price controls on intrastate gas exceeded Congress' powers under the commerce clause, and that the NGPA provisions invaded state sovereignty and intergovernmental immunity.

3. The energy problems were judicially recognized in Federal Power Comm'n v. Louisiana Power & Light Co., 406 U.S. 621 (1972).

step toward the decontrol of natural gas. Section 311 was designed to allow the interstate natural gas market greater access to intrastate sources of natural gas without needless duplication or construction of pipeline facilities. During the years the NGPA has been in effect, the implementation of section 311 by the Federal Energy Regulatory Commission (Commission)[4] appears to have fostered the congressional goals expressed in section 311.

Section 311(a) of the NGPA provides that the Commission may "by rule or order"[5] authorize certain transportation of natural gas by interstate and intrastate natural gas pipelines. Specifically, under section 311(a)(1) the Commission is empowered to authorize an interstate pipeline to transport natural gas on behalf of any intrastate pipeline and any local distribution company.[6] Under section 311(a)(2) the Commission is empowered to authorize an intrastate pipeline to transport natural gas on behalf of any interstate pipeline and any local distribution company served by an interstate pipeline.[7] In addition, under section 311(b) the

4. The Federal Energy Regulatory Commission (Commission), a five-member independent regulatory agency within the Department of Energy, succeeded to the functions of the Federal Power Commission (FPC). *See* 42 U.S.C. §§ 7171-7177 (Supp. III 1979); Exec. Order No. 12,009, 3 C.F.R. 142 (1978), *reprinted in* 42 U.S.C. § 7341 app. at 854-55 (Supp. III 1979).

5. 15 U.S.C. § 3371(a).

6. 15 U.S.C. § 3371(a)(1). Section 3371(a)(1) provides as follows:

> (a) Commission approval of transportation
> (1) Interstate pipelines
> (A) In general
> The Commission may, by rule or order, authorize any interstate pipeline to transport natural gas on behalf of—
> (i) any intrastate pipeline; and
> (ii) any local distribution company.
> (B) Just and reasonable rates
> The rates and charges of any interstate pipeline with respect to any transportation authorized under subparagraph (A) shall be just and reasonable (within the meaning of the Natural Gas Act [15 U.S.C. 717 et seq.]).

Id.

7. 15 U.S.C. § 3371(a)(2). Section 3371(a)(2) provides that:

> (2) Intrastate pipelines
> (A) In general
> The Commission may, by rule or order, authorize any intrastate pipeline to transport natural gas on behalf of—
> (i) any interstate pipeline; and
> (ii) any local distribution company served by any interstate pipeline.
> (B) Rates and charges
> (i) Maximum fair and equitable price
> The rates and charges of any intrastate pipeline with respect to any transportation authorized under subparagraph (A), including any amount computed in accordance with the rule prescribed under clause (ii), shall be fair and equitable and may not exceed an amount which is reasonably comparable to the rates and charges which interstate pipelines would be permitted to charge for providing similar transportation service.
> (ii) Commission rule
> The Commission shall, by rule, establish the method for calculating an amount necessary to—
> (I) reasonably compensate any intrastate pipeline for expenses incurred by the pipeline and associated with the providing of any

Commission may "by rule or order" authorize an intrastate pipeline to sell natural gas to any interstate pipeline or local distribution company served by an interstate pipeline.[8]

The significance of section 311 is that in connection with the acquisition and transportation of certain volumes of natural gas, it eliminates the need for an interstate natural gas pipeline, in a potentially time consuming administrative proceeding, to obtain a certificate of public convenience and necessity under section 7(c) of the Natural Gas Act.[9] Moreover, pursuant to sections 601(a)(1)(C)(i), 601(a)(2)(A)(ii) and 601(a)(2)(B) of the NGPA participation by an intrastate pipeline in a section 311 transaction does not subject the pipeline to the Commission's jurisdiction under the Natural Gas Act.[10]

This Article will assess section 311, its legislative history, recent Commission actions pursuant to section 311, and the role of section 311 in connection with the nation's natural gas supply and demand balance.

II. TRANSPORTATION AND SALES OF NATURAL GAS PRIOR TO PASSAGE OF THE NGPA

Regulation of the transportation and sale of natural gas prior to passage of the NGPA was shaped predominantly by three

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> gathering, treatment, processing, transportation, delivery, or similar service provided by such pipeline in connection with any transportation of natural gas authorized under subparagraph (A); and
>
> (II) provide an opportunity for such pipeline to earn a reasonable profit on such services.

Id.

8. 15 U.S.C. § 3371(b). Section 3371(b)(1) states that "[t]he Commission may, by rule or order, authorize any intrastate pipeline to sell natural gas to (A) any interstate pipeline; and (B) any local distribution company served by any interstate pipeline." *Id.*

9. 15 U.S.C. § 717f(c) (Supp. III 1979). *See infra* notes 92-97 and accompanying text.

10. 15 U.S.C. §§ 3431(a)(1)(C)(i); 3431(a)(2)(A)(ii); 3431(a)(2)(B). Section 3431(a)(1)(C)(i) states that "[f]or purposes of Section 1(b) of the Natural Gas Act [15 U.S.C. 717(b)], the provisions of the Natural Gas Act [15 U.S.C. 717 et. seq.] and the jurisdiction of the Commission under such Act shall not apply by reason of any sale of natural gas—(i) authorized under Section 3362(a) or 3371(b) of this title." 15 U.S.C. § 3431(a)(1)(C)(i). Section 3431(a)(2)(A) provides that "[f]or purposes of Section 1(b) of the Natural Gas Act [15 U.S.C. 717(b)] the provisions of such Act [15 U.S.C. 717 et. seq.] and the jurisdiction of the Commission under such Act shall not apply to any transportation in interstate commerce of natural gas if such transportation is— . . . (ii) authorized by the Commission under Section 311(a) of this title." 15 U.S.C. § 3431(a)(2)(A). Section 3431(a)(2)(B) provides as follows:

> For purposes of the Natural Gas Act [15 U.S.C. 717 et. seq.], the term "natural gas company" (as defined in Section 2(6) of such Act [15 U.S.C. 717 et. seq.]) shall not include any person by reason of, or with respect to, any transportation of natural gas if the provisions of the Natural Gas Act and the jurisdiction of the Commission under the Natural Gas Act do not apply to such transportation by reason of subparagraph (A) of this paragraph.

15 U.S.C. § 3431(a)(2)(B).

factors. First, jurisdiction over the sale and transportation of natural gas was provided by section 1(b) of the Natural Gas Act.[11] Under section 1(b), the Federal Power Commission (FPC) had jurisdiction over interstate transportation of natural gas, interstate sales of natural gas for resale, and natural gas companies which engage in such transportation or sale.[12] The FPC, however, did not have jurisdiction to regulate the local distribution of natural gas or the facilities used for local distribution.[13] Direct sales of natural gas in interstate commerce that were not for resale also were not subject to the jurisdiction of the FPC, although the interstate transportation of direct sale gas was subject to the certificate requirements of section 7 of the Natural Gas Act.[14] Further, the Natural Gas Act exempted from the FPC's jurisdiction the facilities used for producing and gathering natural gas.[15] Before engaging in jurisdictional natural gas activity, companies were required to obtain a certificate of public convenience and necessity under section 7 of the Natural Gas Act.[16]

The two other factors which shaped the regulation of natural gas sales and transportation were the Supreme Court's decisions in *Phillips Petroleum Co. v. Wisconsin*[17] and *California v. Lo-Vaca Gathering Co.*[18] The prices for natural gas sales by producers under interstate contracts were first regulated by the FPC after the landmark decision in *Phillips* in 1954.[19] Thereafter, the FPC engaged in a series of area rate cases. These were followed in 1974 by Opinion No. 699[20] in which the FPC first established a national rate for natural gas sold in interstate commerce. In 1976 the establishment of a second biennial national rate followed.[21] As noted by one

11. 15 U.S.C. § 717(b) (1976).

12. *Id.* Section 717(b) provides:

> The provisions of this chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

Id.

13. *See* Federal Power Comm'n v. East Ohio Gas Co., 338 U.S. 464 (1950).

14. *See* Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n, 332 U.S. 507 (1947).

15. 15 U.S.C. § 717(b) (1976); *see* United Gas Improvement Co. v. Continental Oil Co., 381 U.S. 392 (1965).

16. 15 U.S.C. § 717f(c) (Supp. III 1979).

17. 347 U.S. 672 (1954).

18. 379 U.S. 366 (1965).

19. *See generally* MacAvoy, *The Natural Gas Policy Act of 1978,* 19 NAT. RESOURCES J. 811 (1979); Nordhaus, *Producer Regulation and the Natural Gas Policy Act of 1978,* 19 NAT. RESOURCES J. 829 (1979).

20. 51 F.P.C. 2212 (1974), *aff'd,* Shell Oil Co. v. Federal Power Comm'n, 520 F.2d 1061 (5th Cir. 1975), *cert. denied,* 426 U.S. 941 (1976).

21. *See* Opinion No. 770, 56 F.P.C. 509 (1976); Opinion No. 770-A, 56 F.P.C. 2698 (1976),

commentator, however, the FPC's "response to *Phillips* had been excruciatingly slow."[22] The result of this pricing policy was the severe decline in dedications of gas to the interstate market.[23]

The pricing problem was compounded by the Supreme Court's opinion in *Lo-Vaca*.[24] In *Lo-Vaca* the Lo-Vaca Gathering Company had contracted to sell gas in Texas to be used by an interstate pipeline company in its own facilities outside Texas. The interstate pipeline also delivered other gas from other producers at the Arizona-California border to California distributors. Such gas was commingled with the gas sold by Lo-Vaca to the interstate pipeline. In adopting a commingling doctrine, the Supreme Court stated that "[t]he fact that a substantial part of the gas will be resold, in our view, invokes federal jurisdiction at the outset over the entire transaction."[25]

The decision in *Lo-Vaca* upholding the application of the commingling doctrine had a significant impact on the structure of the interstate and intrastate pipeline systems. For example, in *Louisiana Power & Light Co. v. Federal Power Commission*[26] the Fifth Circuit confronted the issue of the jurisdictional status of a gas pipeline, the Green System-East, which was located entirely within Louisiana and which only carried gas produced within Louisiana. The Green System-East, however, was connected to an interstate gas pipeline. The FPC, in determining the Green System-East was jurisdictional under the Natural Gas Act, found that gas flowing in the Green System-East had once been transported in a pipeline carrying interstate gas.[27] Although the FPC had determined that the injection of interstate gas into the Green System-East was not minimal, the FPC contended that even a single molecule of interstate gas introduced into the Green System-East would provide jurisdiction.[28] The Fifth Circuit upheld the jurisdictional status of the Green System-East, but specifically refused to consider

aff'd, American Pub. Gas Ass'n v. Federal Power Comm'n, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978).

22. Nordhaus, *supra* note 19, at 836.

23. Nordhaus, *supra* note 19, at 836-40.

24. California v. Lo-Vaca Gathering Co., 379 U.S. 366 (1965).

25. *Id.* at 369.

26. 483 F.2d 623 (5th Cir. 1973), *cert. denied*, 416 U.S. 974 (1974) (the "Green System" case). In *Louisiana Power & Light* the Fifth Circuit found that substantial volumes of interstate gas had been injected into an intrastate system and had been commingled with the intrastate gas. As a result of the commingling, the court upheld the FPC's ruling establishing the jurisdictional status of the intrastate pipeline. Louisiana Power & Light Co. v. Federal Power Comm'n, 483 F.2d 623, 631-32 (5th Cir. 1973).

27. 483 F.2d at 628-29. Additionally, some gas in the Green System-East eventually was introduced into another interstate pipeline, although "in all probability this gas does not physically leave Louisiana." *Id.* n.2.

28. *Id.* at 631-32.

whether "one molecule would be sufficient to automatically confer federal control."[29]

The *Lo-Vaca* commingling doctrine has been muted somewhat by court and FPC decisions.[30] Nevertheless, the commingling doctrine made intrastate pipelines reluctant to make connections with other pipelines which could lead to the reception of interstate gas and result in the intrastate pipeline becoming jurisdictional under the Natural Gas Act.[31]

The effect of these factors was a disparity in prices between the interstate and intrastate market and shortages of gas in the interstate market.[32] In 1978 a House committee report noted that "it is apparent that the present dual market system of natural gas pricing, including cost-based regulation of the interstate market is no longer tenable."[33] The dual market structure of the Natural Gas Act and the resultant shortages were recognized by the Fifth Circuit in *Mid-Louisiana Gas Co. v. Federal Energy Regulatory Commission.*[34] In *Mid-Louisiana* the court stated:

> The fuel shortages of the 1970s revealed two flaws in

29. *Id.* at 632.

30. *See* Colorado Interstate Gas Co., 56 F.P.C. 1916 (1976); United Gas Pipe Line Co., No. CP76-238, 10 F.E.R.C. (CCH) ¶ 61,057 (1980). In these administrative decisions the FPC and the Commission, respectively, held that the commingled stream additionally must cross a state line after the producer's gas enters the jurisdictional pipeline to satisfy the sale for resale in interstate commerce test. More recently, in Sebring Utilities Comm'n v. Federal Energy Regulatory Comm'n, 591 F.2d. 1003 (5th Cir. 1979), *cert. denied*, 444 U.S. 183 (1979), the Fifth Circuit held that direct sale gas which is transported in interstate commerce and which is commingled with interstate gas, but which is not owned by the pipeline, could not be curtailed because the pipeline merely stood in a bailee relationship to the purchasers. 591 F.2d at 1018-19. The court also concluded that the direct sale gas was not subject to the Commission's jurisdiction. *Id.* A careful distinction must be drawn between the *gas* and the *transportation*. Under *Sebring*, the gas does not become jurisdictional, although the interstate transportation of such gas clearly is jurisdictional. Columbia Gas Transmission Corp. & Nat'l Fuel Gas Supply Corp., No. CP77-316, 10 F.E.R.C. (CCH) ¶ 61,111 (1980).

31. In Louisiana Power & Light v. Federal Power Comm'n, 483 F.2d 623, the court observed that the interstate pipeline had resisted FPC jurisdiction, fearing that in the then current gas shortage they would become subject to the curtailment plan of interstate pipelines. *Id.* at 626.

32. *See* MacAvoy, *supra* note 19, at 815-19; Nordhaus, *supra* note 19, at 835-40. The following was noted in a comparative analysis of natural gas pricing proposals prepared prior to passage of the NGPA:

> At present, natural gas is sold in the United States under two different market systems. Gas that is in interstate commerce is sold under prices regulated by the Federal Power Commission; gas sold in the state in which it was produced is not regulated. Slightly less than half the net marketed production of gas is consumed in intrastate markets. . . . Intrastate prices have been increasing fairly steadily for several years while interstate prices have moved sporadically in response to new regulatory actions. As a consequence of the price disparity between the intrastate and interstate markets, about 90 percent of new production in recent years has been dedicated to the intrastate markets.

COMMITTEE ON ENERGY AND NATURAL RESOURCES, 95TH CONG., 1ST SESS., NATURAL GAS PRICING PROPOSALS: A COMPARATIVE ANALYSIS 1 (Comm. Print 1977).

33. STAFF OF SUBCOMM. ON ENERGY AND POWER, COMM. ON INTERSTATE AND FOREIGN COMMERCE, 95TH CONG., 2D SESS., ECONOMIC ANALYSIS OF H.R. 5289, NATURAL GAS POLICY ACT OF 1978 1-2 (Comm. Print 1978).

34. 664 F.2d 530 (5th Cir. 1981).

> the regulation of gas production. The first appeared when the area and national rates established by the Commission for gas sold on the interstate market fell markedly below the price available for gas sold on the intrastate market, which was not regulated by the Commission. The price disparity between the two markets skewed the distribution of gas and resulted in shortages of gas available for interstate sale.[35]

Before enactment of the NGPA the FPC attempted to deal with the emerging dual market in several ways, but had little success.[36] In Order No. 402[37] and Order No. 402-A[38] the FPC announced a policy to encourage sixty-day emergency sales and transportation by Hinshaw pipelines, distributors, and intrastate pipelines without prior authorization.[39] This statement of policy was designed to assure that participation in emergency transactions would not result in jurisdictional consequences. In 1975 the FPC moved to alleviate the shortages of natural gas facing interstate pipelines by instituting the Order No. 533 program that involved a statement of policy on the certification of transportation by interstate pipelines of direct sale gas to high priority users.[40] One of

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35. Mid-Louisiana Gas Co. v. Federal Energy Regulatory Comm'n, 664 F.2d 530 (5th Cir. 1981).

36. *See generally* Nordhaus, *supra* note 19, at 839-40.

37. 35 Fed. Reg. 8927 (1970), *reprinted in* 43 F.P.C. 707 (1970).

38. 18 C.F.R. § 2.68 (1981), *reprinted in* 43 F.P.C. 822 (1970).

39. 18 C.F.R. §§ 2.68, 157.22, 157.29 (1981). Even earlier, the FPC had promulgated regulations acknowledging that in emergencies involving imminent danger to life and property, natural gas producers could enter into 60-day sales and transportation of natural gas without prior authorization. *See* Order No. 193, 16 F.P.C. 497 (1956), *amended by* Order No. 418, 35 Fed. Reg. 19,173 (1970); Opinion No. 699-B, 52 F.P.C. 700 (1974) (clarified in Opinion No. 699-C, 52 F.P.C. 851 (1974)). Such regulations were coupled with the FPC's action under § 7(f) of the Natural Gas Act, 15 U.S.C. § 717f(c) (Supp. III 1979), exempting from prior FPC approval the construction and operation of facilities to make 60-day emergency sales. Order No. 192, 21 Fed. Reg. 9165 (1956), *amended by* Order No. 280, 29 Fed. Reg. 4879 (1964); Order No. 391, 34 Fed. Reg. 17,331 (1969); Order No. 418, 35 Fed. Reg. 19,174 (1970); Order No. 280(a), 40 Fed. Reg. 3981 (1975); Order No. 565, 42 Fed. Reg. 29,002 (1977); 43 Fed. Reg. 56,536 (1978).

40. *See* Order No. 533, 18 C.F.R. § 2.79 (1981), *enforced sub nom.* American Pub. Gas Ass'n v. Federal Power Comm'n, 587 F.2d 1089 (D.C. Cir. 1978). In implementing Order No. 533, the FPC stated:

> Several persons have stated that despite the advantages that might result from the implementation of this policy, it will by no means solve the natural gas shortage in this country. Only deregulation of the wellhead price or regulation of the intrastate market, we are told, could possibly lead to a solution of the gas shortage. As these same persons recognize, however, deregulation of wellhead prices or regulation of the intrastate market are matters for the Congress to decide upon. . . . [I]mplementation of the policy statement should, by making intrastate gas available to the interstate market, help mitigate the serious effects that will follow from curtailment of customers who are peculiarly dependent upon natural gas. . . . Overall implementation of our policy statement will ration gas more efficiently between intrastate and interstate users.

Order No. 533, 54 F.P.C. 821, 833 (1975). In Order No. 27 the Commission extended the Order No. 533 program to certain eligible high priority users which formerly might have been unable to take advantage of § 2.79. 18 C.F.R. §§ 157.100-.105 (1981).

the FPC's stated goals was to make gas otherwise sold in the intrastate market available to the interstate market.[41]

The FPC limited the Order No. 533 program to direct sales of natural gas to existing high priority commercial and industrial customers of interstate pipelines when deliveries to the users were curtailed or in imminent curtailment danger. The interstate pipeline was required to obtain a certificate of public convenience and necessity. Only an interstate pipeline with declining deliveries and unused capacity was eligible under the program.[42] Significantly, the FPC noted it could not impose ceilings on the price of the direct sale gas. It did, however, observe that consistent with the holding in *Federal Power Commission v. Transcontinental Gas Pipe Line Corp.*,[43] the price of the direct sale gas would be considered in determining whether to grant the transportation certificate.[44] The term of the Order No. 533 program certificate was initially limited to two years.

The Commission extended the Order No. 533 program in its Order No. 2.[45] It stated that the program was an important way to avoid plant curtailments and that it had found no evidence that the program resulted in higher prices in the intrastate market or limited dedications in the interstate market.[46] The Commission stated:

> While a bifurcated pricing system exists (intrastate versus interstate), gas will continue to be sold intrastate for prices in excess of the Commission's national rate. . . . [H]owever, we have found no evidence that the 533 program has resulted in either an increase in intrastate prices or a deterrent to interstate dedications. So long as the intrastate market demand is greater than the supply, the prices unregulated, and the uses unrestricted, parity of access will not be restricted by Commission action; but it will be restricted instead by the dynamics of the marketplace.[47]

In Order No. 2 the Commission extended the Order No. 533

41. Order No. 533, 54 F.P.C. at 834.

42. *See, e.g.*, Cerro Wire & Cable, No. CP80-153, 12 F.E.R.C. (CCH) ¶ 61,158, *reh'g denied*, 13 F.E.R.C. (CCH) ¶ 61,036 (1980), *aff'd*, 677 F.2d 124 (D.C. Cir. 1982). The Order No. 533 program did not include transportation of direct sales gas to distributors for resale and did not apply to offshore federal domain gas.

43. 365 U.S. 1 (1961).

44. Order No. 533, 40 Fed. Reg. 41,760 (1975); *see also* General Policy and Interpretations, 43 Fed. Reg. 5362, 5365 n.13 (1978).

45. General Policy and Interpretations, 43 Fed. Reg. 5362 (1978).

46. *Id.* at 5363-65.

47. *Id.* at 5365.

program to cover transportation by intrastate pipelines. The Commission stated:

> Participation by an intrastate pipeline in a 533 transaction involves it in interstate transportation which is a jurisdictional activity. In order to encourage intrastate pipelines to participate in 533 arrangements, the Commission will assert only a limited claim of jurisdiction over participating intrastate pipelines. commission [sic] jurisdiction will be restricted to the 533 service performed and will not serve as a basis for the assertion of authority over other activities of the intrastate pipeline nor its facilities.[48]

As part of the certification procedure, the Commission required intrastate pipelines to submit data showing that their proposed transportation rates were just and reasonable.[49]

The FPC's policy regarding the pricing of producer sales in interstate commerce resulted in market distortions, prompting many producers to sell their production in the intrastate market, resulting in shortages of natural gas in nonproducing states and in the intrastate market's securing of the majority of new production.[50] Further, the FPC's ability to deal with the dual market was hampered seriously by its inability to insulate intrastate pipelines from the Natural Gas Act's jurisdiction and certification requirements.

III. LEGISLATIVE HISTORY

> Courts in the past have been able to rely on legislative history for important insights into congressional intent. Without implying that this is no longer the case, we note that interest groups who fail to persuade a majority of the Congress to accept particular statutory language often are able to have inserted in the legislative history of the statute statements favorable to their position, in the hope that they can persuade a court to construe the statutory language in light of these statements.[51]

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48. *Id.* at 5368-69.

49. *Id.* at 5369. The Commission noted that approval of rates by state regulatory agencies would be given evidentiary weight. *Id.*

50. *See* Oklahoma v. Federal Energy Regulatory Comm'n, 661 F.2d at 834.

51. National Small Shipments Traffic Conference, Inc. v. Civil Aeronautics Bd., 618 F.2d 819, 828 (D.C. Cir. 1980).

The legislative history of section 311 of the NGPA indicates that its provisions regarding transportation of gas by interstate and intrastate pipelines and sales by intrastate pipelines to interstate pipelines were viewed as "noncontroversial."[52] The NGPA, however, was enacted into law on November 9, 1978,[53] only after an immense legislative struggle. Throughout the struggle the provisions embodied in section 311 were regarded as being "generally acceptable."[54] It is the uncontroversial nature of the section 311 provisions that underscores their importance to this country's natural gas supply system.

The genesis of the NGPA came on July 27, 1976, when the House Ad Hoc Committee on Energy issued report no. 95-543 on House Bill 8444.[55] The Ad Hoc Committee on Energy specifically amended House Bill 8444 to include proposed section 414(b)(1) which specified that:

> The Commission may, by rule or order, authorize any intrastate pipeline to sell natural gas to, or transport natural gas on behalf of, any interstate pipeline upon such terms and conditions, including provisions respecting fair and equitable prices, as the Commission determines appropriate. No person shall be subject to regulation under the Natural Gas Act or as a common carrier under any provisions of Federal or State law by reason of making any sale, or engaging in any transportation, of natural gas authorized by the Commission under this subsection.[56]

This amendment was known as Ad Hoc Committee Amendment No. 7.[57] It appears that the predominant motivation

52. 124 CONG. REC. S15,019 (daily ed. Sept. 13, 1978) (statement of Sen. Hansen).

53. 15 U.S.C. §§ 3301-3432 (Supp. III 1979).

54. 124 CONG. REC. S14,898 (daily ed. Sept. 11, 1978) (statement of Sen. Tower).

55. H.R. 8444, 95th Cong., 1st Sess. (1976) (introduced by Rep. Ashley on July 20, 1976). The legislative genesis of the NGPA actually commenced earlier with the introduction of President Carter's bill, the National Energy Act, on May 2, 1976. H.R. 6831, 95th Cong., 1st Sess. (1976). One of the National Energy Act's stated purposes was "to deal with short-term supply shortages of natural gas through extension of the allocation provisions of the Emergency Natural Gas Act of 1977." *Id.* Specifically, § 416 of House Bill 6831 would have slightly modified the Emergency Natural Gas Act of 1977 (ENGA) and extended that Act into 1979. 15 U.S.C. § 717 (1976). Under ENGA the President was empowered to declare a natural gas emergency if he found a gas shortage existed or was imminent and endangered the gas supply of high priority users. During the declared emergency the President was empowered to require that interstate pipelines deliver emergency supplies or transport interstate gas to other interstate pipelines or local distribution companies served by interstate pipelines. The President also could require intrastate pipelines to transport emergency supplies. There were no jurisdictional consequences for any sale authorized by the President under ENGA or for any intrastate pipeline transportation connected with such a sale. *Id.* § 717(b). House Bill 6831, however, did not contain provisions analogous to § 311 of the NGPA.

56. H.R. 8444 at 209.

57. *See* H.R. REP. NO. 543, 95th Cong., 1st Sess. 44 (1978).

for the sales authority in amendment no. 7 was to facilitate emergency sales of intrastate gas to needy interstate pipelines.[58] The committee report stated:

> This type of authority has, in the past, been limited to periods of severe emergency, in part to avoid its becoming a means of circumventing FPC wellhead price controls and becoming *de facto* deregulation. The extension of Federal price controls to previously unregulated intrastate markets by this legislation assures that this authority will not become a vehicle for interstate pipelines to pay unregulated intrastate prices.[59]

The committee report also revealed, however, that the transportation authority contained in amendment no. 7 was motivated by a different reason.[60] The committee report stated:

> A second aspect of the authority added to the bill by Amendment No. 7 relates to FPC approval of transportation of natural gas on behalf of an interstate pipeline. This authority may save interstate pipelines great expense by avoiding the need to duplicate intrastate pipeline routes in order to obtain natural gas from producing areas presently served only by intrastate pipeline systems.
>
> The amendment facilitates development of a national natural gas transportation network without subjecting intrastate pipelines, already regulated by State agencies, to FPC regulation over the entirety of their operations. Instead, the intrastate pipelines are immunized from State or Federal regulation as common carriers and from FPC regulation under the Natural Gas Act. The intrastate pipelines are only subjected to FPC regulation under this legislation to the extent the intrastate pipeline is involved in an authorized sale of natural gas to interstate pipelines or an authorized transportation of natural gas on behalf of interstate pipelines. Other operations of an intrastate pipeline are not intended to be subject to FPC regulation by reason of this amendment.[61]

58. *Id.* at 44-45.
59. *Id.* at 44 (emphasis added).
60. *Id.* at 45.
61. *Id.*

The amendment was approved by the House on August 3, 1977.[62] Amendment no. 7, embodied in section 414(b)(1) of House Bill 8444, was unchanged when received in the Senate on September 7, 1977.[63] Thus, amendment no. 7 contained the basic features of section 311, with the exception of the provision allowing transportation by interstate pipelines on behalf of intrastate pipelines and local distribution companies.

On September 15, 1977, Senator Jackson submitted report no. 95-436 on Senate Bill 2104 (entitled the Natural Gas Policy Act) on behalf of the Committee on Energy and Natural Resources.[64] On September 16, 1977, Senator Jackson introduced amendment no. 868 to Senate Bill 2104,[65] which proposed allowing the Commission by rule or order, to authorize any intrastate pipeline "to sell natural gas to, or transport natural gas on behalf of, any interstate pipeline or local distribution company served by any interstate pipeline."[66] In introducing this amendment Senator Jackson stated:

> The bill is amended to allow the Federal Energy Commission to authorize use of intrastate pipelines for interstate transportation of gas if they believe it is in the public interest to do so. . . . The determination of whether to allow the use of the pipeline would be made on a case-by-case basis.[67]

Notably, there was an ambiguity between this language and that of the proposed amendment concerning whether decisions on intrastate pipeline transportation would be made under a Commission policy or on a case by case basis.

On September 26, 1977, Senators Pearson and Bentsen offered an amendment to Senate Bill 2104 that would have allowed the Commission to authorize transportation by intrastate

62. 123 CONG. REC. H8382 (daily ed. Aug. 3, 1977).
63. H.R. 8444 (as received in Senate on Sept. 7, 1977).
64. S. REP. NO. 436, 95th Cong., 1st Sess. (1977).
65. 123 CONG. REC. S15,099 (daily ed. Sept. 16, 1977).
66. 123 CONG. REC. S15,102 (daily ed. Sept. 16, 1977).
67. 123 CONG. REC. S15,099 (daily ed. Sept. 16, 1977) (statement of Sen. Jackson). The summary of amendment no. 868 stated in regard to the proposed amendment that:

> This subsection will also facilitate use of existing intrastate pipelines for transportation of gas in the interstate market as existing boiler fuel and other industrial uses of natural gas are phased out. It will also enable use of existing intrastate pipelines for delivery of natural gas from Mexico to the interstate market. The decision to allow use of an interstate pipeline for such purposes will be made by the Commission on a case-by-case basis.

123 CONG. REC. S15,103 (daily ed. Sept. 16, 1977).

pipelines.[68] On October 13, 1977, the Senate and House appointed conferees to resolve any differences.[69] The Senate was insisting that the Commission be empowered to authorize any intrastate or interstate pipeline to transport natural gas on behalf of any interstate or intrastate pipeline. In contrast, the House version would have given the Commission authority to authorize any intrastate pipeline to sell natural gas to an interstate pipeline and to transport natural gas on behalf of any interstate pipeline.[70]

On May 3, 1978, the Joint Conference Committee staff issued a memorandum to the House and Senate members of the Natural Gas Conference Committee.[71] This document represented a compromise natural gas pricing proposal and contained the following provision regarding assignments by intrastate pipelines to interstate pipelines and local distribution companies:

> [The Commission is authorized] to allow intrastate pipelines to assign to interstate pipelines and distribution companies the right to receive surplus (as determined by an appropriate State agency) natural gas that is subject to a price ceiling under this Act without affecting the exempt status, under the Natural Gas Act, of any party to the transaction.[72]

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68. The amendment provided as follows:

> [The Commission may] by rule or order, authorize any interstate or intrastate pipeline to transport natural gas on behalf of any interstate or intrastate pipeline or local distribution company served by any interstate or intrastate pipeline, upon such terms and conditions, including provisions respecting fair and equitable prices, as the Commission deems appropriate. No person shall be subject to regulation under the Natural Gas Act, or as common carrier under any provision of Federal or State law, by reason of the transportation of any natural gas authorized by the Commission under this subsection.

123 CONG. REC. S15,695 (daily ed. Sept. 27, 1977). Amendment no. 1039, offered by Pearson and Bentsen, amended amendment no. 1022, which itself amended amendment no. 862. 123 CONG. REC. S15,697 (daily ed. Sept. 27, 1977). Amendment no. 1039 was approved on October 4, 1977, by a vote of 50 to 46. 123 CONG. REC. S16,323 (daily ed. Oct. 4, 1977).

69. 123 CONG. REC. H10,966; S17,165 (daily ed. Oct. 13, 1977).

70. S. REP. NO. 1126, 95th Cong., 2d Sess. 106-09 (1978). House Bill 5289 was utilized as the House vehicle. House Bill 5289 was amended to include the text of Senate Bill 2104, as amended, and the pertinent text of House Bill 8444. 123 CONG. REC. H10,966 (daily ed. Oct. 13, 1977).

71. Memorandum from Joint Conference Committee staff to House and Senate members of the Natural Gas Conference Committee (May 3, 1978) (discussing subject of Natural Gas Pricing Proposal).

Several internal congressional documents reveal the conferees' thinking in regard to the legislative predecessors to § 311. For example, on February 2, 1978, two staff members of the Senate Committee on Energy and Natural Resources wrote a memorandum to Senator Jackson containing a synopsis of a proposed compromise. Memorandum from Betsy Moler and Mike Harvey to Senator Henry M. Jackson (Feb. 2, 1978). Under the February 2, 1978, proposal the Commission would have been authorized to allow intrastate pipelines to assign to interstate pipelines the right to receive gas subject to a price ceiling under the Act. *Id.* at 2-3. The memorandum also stated: "There are also a number of subjects addressed in both bills (e.g., agriculture priority, authority for intrastate pipelines to transport interstate gas without becoming subject to Federal jurisdiction) that would also be retained in a compromise form." *Id.* at 5.

72. Memorandum from Joint Conference Committee staff to House and Senate members of

The provision for assignments was developed to make it possible for intrastate pipelines to assign surplus gas. The staff memorandum explained that some of the conferees wanted to broaden the assignment provision to authorize transportation and sales by intrastate pipelines for interstate pipelines and transportation by interstate pipelines on behalf of intrastate pipelines without subjecting the intrastate pipelines to the Commission's jurisdiction.[73]

On May 25, 1978, Congressman Eckhardt addressed a letter to Congressman Dingell proposing language to reconcile the differences between the Senate and House conferees before the Joint Conference Committee reconvened on June 6, 1978. Representative Eckhardt stated specifically that he did not address the subject of interstate transportation authority contained in the Senate bill and did "not intend to recommend for or against such authority at this time."[74] However, Eckhardt's "proposed language" contained terms which are remarkably similar to the final version of section 311.[75] The agenda for the Conference Committee meeting on June 7, 1978, reflected the persuasiveness of Eckhardt's proposal.[76]

On August 18, 1978, the conference report was issued as Senate Report No. 95-1126.[77] The House issued an identical report

Natural Gas Conference Committee 22 (May 3, 1978) (discussing subject of Natural Gas Pricing Proposal).

73. *Id.* The memorandum contained the following footnote:

> This provision was originally developed to make it possible for intrastate pipelines to assign their contracts for gas supplies that are surplus to demand due to seasonal market fluctuations. Some would like to broaden the provision to authorize intrastate pipelines to make sales to interstate pipelines or to transport gas for interstate pipelines without becoming subject to [the Commission's] jurisdiction. A new provision is contemplated for the second purpose. It would authorize [the Commission] to allow intrastate pipelines to transport natural gas on behelf [sic] of, or sell natural gas to, interstate pipelines and to make a fair and equitable return on such transactions, with no jurisdictional consequences under the Natural Gas Act to the intrastate pipeline.

Id.

74. Letter from Bob Eckhardt to John Dingell (May 25, 1978). Eckhardt's letter stated he was the author of § 414(b) of House Bill 8444 "dealing with intrastate pipeline transportation and sales authority." *Id.*

75. *Id.* Eckhardt's letter began his description of a compromise as follows:

> 1. In General—Vest discretionary authority in [the Commission] to authorize, by rule or order, intrastate pipelines to transport natural gas on behalf of, or sell natural gas to, interstate pipelines or local distribution companies served by such interstate pipelines with no jurisdictional consequence under the Natural Gas Act to the intrastate pipeline.

Id.

Eckhardt also explained duration of sales, the Commission's general authority to impose conditions regarding the interruption of sales, a definition of fair and equitable transportation fees, protection of existing customers, protection against circumvention of the act, and procedural provisions with respect to sales. *Id.*

76. *See* Agenda of the Natural Gas Conference Committee (June 7, 1978).

77. S. REP. NO. 1126, 95th Cong., 2d Sess. (1978).

as House Report No. 95-1752 on October 10, 1978.[78] The House acceded to the Senate provision regarding interstate pipeline transportation authority and the Senate acceded to the House provision regarding sales by intrastate pipelines, with the proviso that those sales be interruptible.

The Senate and House debates on the conference bill reveal that the section 311 provisions were generally viewed as being meritorious and uncontroversial. On August 25, 1978, Senator Russell Long spoke against the conference bill, but added the following comments on the section 311 provisions:

> One of the key provisions that passed both the Senate and the House of Representatives on other occasions, passed twice, and has been signed by the President twice is the idea that you could buy gas from the intrastate pipelines and put it in the interstate pipelines if you need it. If you take care of that and take care of the movement of gas within the States, then anyone who has some gas can sell it and will sell it. He will have an incentive to go ahead and produce more. While that will not solve all the problems, it will not create any additional problems which unfortunately would be the case with the so-called compromise that will be laid before us sometime soon.[79]

On September 11, 1978, the Senate undertook consideration of House Bill 5289.[80] Senator Jackson stated that House Bill 5289 proposed a policy of opening the interstate market to producers and allowing gas backed up in the intrastate market to flow into the interstate market.[81]

On September 11 Senator Hatch supported a motion to recommit the conference report and to report a bill with the provisions already agreed to by the conferees, which would facilitate transfer of surplus and emergency gas to the interstate market under conditions preventing brokerage of gas by intrastate pipelines.[82] Senator Tower described the motion to recommit as an attempt to strip the unacceptable portions and to report those

78. H.R. REP. No. 1752, 95th Cong., 2d Sess. (1978).
79. 124 CONG. REC. S14,594-95 (daily ed. Aug. 25, 1978) (statement of Sen. Long).
80. 124 CONG. REC. S14,868 (daily ed. Sept. 11, 1978).
81. 124 CONG. REC. S14,869 (daily ed. Sept. 11, 1978) (statement of Sen. Jackson).
82. 124 CONG. REC. S14,892 (daily ed. Sept. 11, 1978) (statement of Sen. Hatch). *See* Natural Gas Pipeline Co. of Am., No. CP80-520-003, 20 F.E.R.C. (CCH) ¶ 61,324 (1982); Pacific Interstate Trans. Co., No. CP81-124, 17 F.E.R.C. (CCH) ¶ 63,069 (1981) (Commission approved brokerage type arrangement where interstate pipeline bought and sold gas to affiliate Hinshaw pipeline where direct sale was not possible).

portions "which are pretty generally acceptable."[83]

Senator Bartlett also supported recommittal, but he would have supported the conference provision that gave "general authorization for [the Commission] to allow sales of natural gas by intrastate to interstate pipelines under specific price guidelines, protecting both the consumer in the consuming State and the consumer in the producing State."[84] The motion to recommit was defeated on September 19, 1978.[85]

On September 27, 1978, the Senate agreed to the conference report on House Bill 5289.[86] Just before passage, Senator Glenn predicted that passage would encourage both a single market system and sales into the interstate system.[87] President Carter signed into law the NGPA, including section 311, on November 9, 1978.[88]

IV. COMMISSION'S IMPLEMENTATION OF SECTION 311

> [R]egulators will have to come to grips with the realities of the marketplace.[89]

Charged with the plain meaning and legislative history of section 311, the Commission "by rule or order"[90] was to facilitate the movement of gas to the interstate market via the existing national network of natural gas pipelines. Unfortunately, the Commission was without specific guidance as to how such a goal could be accomplished. The Commission, however, possessed broad powers under section 311 which were supplemented by its general rulemaking powers under section 501 of the NGPA.[91]

In implementing section 311, the Commission was required to act consistently with the provisions of the Natural Gas Act.[92] Under section 1(b) of the Natural Gas Act the Commission has jurisdiction

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83. 124 CONG. REC. S14,898 (daily ed. Sept. 11, 1978) (statement of Sen. Tower).

84. 124 CONG. REC. S15,093 (daily ed. Sept. 14, 1978) (statement of Sen. Bartlett).

85. 124 CONG. REC. S15,421 (daily ed. Sept. 19, 1978). Senator Dole made another motion to recommit with report back of these same provisions. 124 CONG. REC. S16,128-31 (daily ed. Sept. 26, 1978). This second motion was defeated on September 26, 1978. 124 CONG. REC. S16,139 (daily ed. Sept. 26, 1978).

86. 124 CONG. REC. S16,265 (daily ed. Sept. 27, 1978).

87. 124 CONG. REC. S16,263 (daily ed. Sept. 27, 1978) (statement of Sen. Glenn).

88. 1978 U.S. CODE CONG. & ADM. NEWS 3411 (codified at 15 U.S.C. §§ 3301-3432).

89. Muchow, *The Future of Gas Energy*, 2 ENERGY L.J. 241, 269 (1981).

90. 15 U.S.C. §§ 3371(a)(1)(A), 3371(a)(2)(A) (Supp. III 1979).

91. 15 U.S.C. § 3411 (Supp. III 1979). Representative Dingell observed that the Commission had "substantial discretion with respect to implementation of Section 311 in particular cases." 124 CONG. REC. H13,118-19 (daily ed. Oct. 14, 1978).

92. Order No. 46, 44 Fed. Reg. 52,179, 52,180 (1979)

over interstate transportation and interstate sales for resale of natural gas.[93] Before engaging in such activity a natural gas company[94] must obtain a certificate of public convenience and necessity from the Commission.[95] An applicant for a certificate is required to comply with the Commission's regulations governing certificate applications.[96] This process can be both complex and time consuming.[97]

The Commission implemented section 311(a) in its Interim Regulations,[98] and its Order No. 46.[99] In its Interim Regulations the Commission established a "mechanism" under which transportations by interstate pipelines under section 311(a)(1) could be "self-executed" without prior Commission approval for periods up to two years.[100] The Commission also established a "mechanism" for permitting transportation for fixed periods longer than two years.[101] The basic difference between these types of authorizations permitted by the Interim Regulations was that arrangements in excess of two years required prior approval from the Commission.[102] The Commission explained this distinction as follows:

> [T]he Commission is well aware that the NGPA seeks to strike down the jurisdictional barriers which have precluded interstate and intrastate pipelines from taking advantage of the most economic and efficient means of transporting natural gas. Sections 311(a)(1) and 311(a)(2) provide the Commission with important new authorities designed to achieve a national transportation system with its attendant economies and efficiencies. On the other hand, transportation arrangements for fixed periods greater than two years contemplate service periods which may so significantly affect a pipeline's system operation as to require prior Commission scrutiny and approval.[103]

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93. 15 U.S.C. § 717(b) (Supp. III 1979).

94. A "natural gas company" is defined in the Natural Gas Act as "a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale." *Id.* § 717(a)(6).

95. *Id.* § 717f(c).

96. 18 C.F.R. §§ 157.5-.22 (1981).

97. *See* Kansas Pipe Line & Gas Co., 2 F.P.C. 29, 55-58 (1939) (discussing the minimum showing required to establish public convenience and necessity).

98. Interim Regulations Implementing the Natural Gas Policy Act of 1978, 43 Fed. Reg. 56,448 (1978) [hereinafter cited as Interim Regulations].

99. Order No. 46, 44 Fed. Reg. 52,179 (1979). The Commission subsequently amended Order No. 46. Order on Rehearing of Order No. 46, 44 Fed. Reg. 66,789 (1979).

100. Interim Regulations, *supra* note 98, at 56,521.

101. *Id.*

102. *Id.*

103. *Id.* at 56,522. The Commission further explained that transportation arrangements for

Under the Interim Regulations, the rates charged by the interstate pipeline for the self-executing transportation arrangements were its applicable transportation rates on file with the Commission.[104] Otherwise, the interstate pipeline could elect to use the rates in a filed rate schedule covering comparable service[105] or base its rates on the methodology used to design rates covering transportation and storage costs in one of its own effective sales rate schedules. For transactions of longer than two years, the Commission stated that it would specify the rates and charges, duration, and conditions of the service.[106] Generally, all transportation revenues in excess of a one cent per Mcf allowance to cover out-of-pocket expenses were required to be credited to the interstate pipeline's purchased gas account and flowed back to its jurisdictional customers.[107] An interstate pipeline, however, was not required to credit any demonstrated actual out-of-pocket expenses in excess of one cent per Mcf.[108]

The Commission adopted similar Interim Regulations for intrastate pipelines under section 311(a)(2), but indicated that it was having difficulty with the term "fair and equitable in determining a practical method for applying the statutory limitation on rates contained in section 311(a)(2)" to rates for transportation.[109] The Commission attempted to resolve the problem by "presuming" that an intrastate pipeline regulated on a cost of service basis by a state agency would not be permitted to charge a rate greater than an interstate pipeline providing similar service.[110] Accordingly, the Commission provided that the intrastate pipeline could elect to base its rates on the methodology and cost used to design rates to recover the costs of transportation or on the methodology and cost used to determine the allowance authorized by a state agency for city-gate service by the pipeline.[111]

fixed terms over two years could involve significant investments such as construction and operation facilities. *Id.*

104. *Id.* at 56,623-34.

105. The Interim Regulations did not specify whether the filed schedule covering comparable service was required to be a schedule of the interstate pipeline undertaking the § 311 service.

106. Interim Regulations, *supra* note 98, at 56,623.

107. *Id.* at 56,624. In regard to the one cent figure, the Commission stated:

> The Commission notes, parenthetically, that the 1 cent per Mcf allowance for out-of-pocket costs derives from the Commission's experience in a number of individual cases under the Natural Gas Act which evidenced that the 1.0 cent per Mcf reasonably represented the level of out-of-pocket costs normally incurred by interstate pipelines in rendering transportation service.

Id. at 56,523.

108. *Id.* at 56,624.

109. *Id.* at 56,525.

110. *Id.*

111. *Id.* at 56,524-25. The costs of transportation include processing, gathering, treatment, delivery, or other similar service. *See* 18 C.F.R. § 284.123(b)(1)(i)(A) (1981).

Alternatively, the intrastate pipeline could elect to use a transportation rate on file with the state agency covering comparable service.[112] Rates computed under either part of this election were presumed to be "fair and equitable and not in excess of [the rates] an interstate pipeline would be permitted to charge for providing similar service."[113] If the foregoing election was not made, the intrastate pipeline was permitted to file proposed rates and charges with the Commission and commence service at the proposed rates subject to refund.[114]

The Commission's implementation of section 311(a) continued in Order No. 46.[115] In Order No. 46 the Commission defined the term "transportation" in a broad manner to maximize the amount of gas moving in interstate commerce.[116] Because an exchange of natural gas had elements of both a transportation and a sale the Commission included exchanges within the definition of transportation, although an exchange was defined as a sale under the NGPA. The effect of this definition is that an interstate pipeline may exchange gas without a certificate with an intrastate pipeline under section 311.[117] In addition, the Commission limited the definition of "appropriate state regulatory agency"[118] to those state agencies regulating rates on a cost of service basis. The Commission stated that under such a definition "it is assured that all section 311(a)(2) rates will be cost based."[119] The Commission also explained the term "on behalf of" in sections 311(a)(1) and 311(a)(2) by stating that a "nexus" must be present, such as an agency relationship or "having title to the transported gas reside, during the transaction, in the party on whose behalf the transportation is conducted."[120] The Commission clarified the definition of "intrastate pipeline" for purposes of section 311 by

112. 18 C.F.R. § 284.123(b)(1)(ii) (1981). The Commission did not specify that the comparable tariff had to have been filed by the intrastate pipeline contemplating the § 311 service.

113. Interim Regulations, *supra* note 98, at 56,524. The Commission stated that it "presumes that all revenues associated with those transportation transactions engaged in by regulated intrastate pipelines have been, or will be, considered by the appropriate state regulatory authority in establishing rates to be charged. This treatment would be consistent with treatment of interstate pipelines by this Commission." *Id.*

114. *Id.* at 56,524-25. In the Interim Regulations the Commission established procedures under § 311(a)(1) and § 311(a)(2) for extending self-implementing transactions and for filing reports of transactions with the Commission. *See* 18 C.F.R. §§ 284.106, .107, .125, .126 (1981). The Commission reserved issuance of regulations applicable to sales by intrastate pipelines under § 311(b). Interim Regulations, *supra* note 98, at 56,521.

115. Order No. 46, *supra* note 99.

116. The Commission stated that limiting the term "transportation" to actual movements of gas "would minimize the impact of section 311(a)." Order No. 46, *supra* note 99, at 52,183. Accordingly, the Commission defined transportation to cover exchanges, backhauls, displacement, and other methods of transportation. *Id.* at 52,184.

117. Panhandle Eastern Pipe Line Co., No. CP80-231, 12 F.E.R.C. (CCH) ¶ 61,159 (1980).

118. Order No. 46, *supra* note 99, at 52,184.

119. *Id.* at 52,183.

120. *Id.* at 52,180.

stating that section 2(16) of the NGPA seemingly requires a pipeline to be engaged in transportation.[121] However, a pipeline which has not commenced service could establish its status as an intrastate pipeline by obtaining a declaratory order from the Commission.[122] In this matter, a new pipeline could be assured that by undertaking a particular transaction it would not be subjecting itself to the Commission's jurisdiction under the Natural Gas Act.

In Order No. 46 the Commission limited self-executing transportations under sections 311(a)(1) and 311(a)(2) to "those arrangements in which the final recipient of the natural gas has acquired the natural gas for its system supply and will resell the gas in accordance with its applicable curtailment plan."[123] Order No. 46 did not "authorize transportation directly to end-users unless the transportation is specifically approved by the Commission."[124] This limitation meant that the self-executing arrangements allowed under section 311 were unavailable to a large end user, such as a petrochemical plant which intended to buy the gas solely for its own use.

Order No. 46 also addressed the jurisdictional consequences to the participants of an arrangement providing transportation service under section 311(a). The Commission stated that by operation of section 601(a) of the NGPA[125] transportations and sales authorized under section 311 were "clearly exempted from the Commission's Natural Gas Act . . . jurisdiction."[126] The Commission stated that

121. 15 U.S.C. § 3301(16) (Supp. III 1979). Basically, an intrastate pipeline is any person, other than a pipeline exempt from jurisdiction under § 1(c) of the Natural Gas Act, engaged in the transportation of natural gas not subject to the Commission's jurisdiction under the Natural Gas Act. *Id.*

122. Order No. 46, *supra* note 99, at 52,180. The Commission cited its declaratory order in Texas Sea Rim Pipeline, Inc., No. CP79-117 (Federal Energy Regulatory Comm'n Feb. 16, 1979), in which the Commission declared that for § 311 purposes an offshore pipeline which had not commenced service was an intrastate pipeline. In *Texas Sea Rim* the Commission stated that to qualify as an intrastate pipeline the pipeline must be engaged in transportation rather than gathering. *Id.* at 3. The Commission also considered certain factors indicative of the intentional use of the facilities for intrastate transportation, including the contract between an intrastate seller and intrastate purchaser and the pending application for a certificate to contract a separate line for interstate transportation. *Id.* at 6.

123. Order No. 46, *supra* note 99, at 52,180. The Commission excluded the transportation of gas sold directly to end users from the self-implementing transactions. Such transportations require prior Commission approval. *Id.*

As in the Interim Regulations, the Commission limited self-executing transactions to renewable two-year terms. 18 C.F.R. §§ 284.102(b)(1)(i), 284.122(b)(1)(i) (1981). The two-year limitation was predicated on the need to examine the available capacity of the transporting pipeline. In its proposed rulemaking issued April 27, 1981, the Commission proposes to amend its regulations to permit unlimited two-year extensions of self-implementing transportation transactions. Sales and Transportation by Interstate Pipelines and Distributors, 46 Fed. Reg. 24,585 (1981).

124. Order No. 46, *supra* note 99, at 52,180.

125. 15 U.S.C. § 3431(b) (Supp. III 1979).

126. Order No. 46, *supra* note 99, at 52,179. The Commission indicated in Order No. 46 that § 601 only removes those arrangements authorized by the Commission from the Commission's Natural Gas Act jurisdiction. It indicated that if transportation authority under § 311(a) was found not to exist, then § 601 did not remove Natural Gas Act jurisdiction, despite the good faith of the parties in entering into the transaction. *Id.*

a pipeline used only for section 311(a) transportation would not be subject to Natural Gas Act jurisdiction.[127] The Commission, however, stated:

> Section 601 removes the Commission's [Natural Gas Act] jurisdiction from a transaction otherwise subject to [Natural Gas Act] jurisdiction only if the transaction is "authorized" by a Commission rule or order. Section 601 does not remove the Commission's [Natural Gas Act] jurisdiction from a transaction otherwise subject to [Natural Gas Act] jurisdiction if the parties erroneously, in good faith, believed they had section 311(a) authorization, when in fact such authorization did not exist.[128]

The significance of this statement is that parties erroneously believing a transaction was authorized under section 311 could be in violation of the Natural Gas Act by participating in a jurisdictional activity under the Natural Gas Act without a certificate of public convenience and necessity.[129]

In Order No. 46 the Commission indicated a preference for using section 311(a) over section 7(c) of the Natural Gas Act as a means of authorizing transportation of natural gas. The Commission specifically indicated that it "will not issue [section 7(c)] certificates unless the reasons for not transporting pursuant to section 311(a)(1) are extraordinary."[130] The Commission rejected suggestions that certain transportations of gas by an interstate pipeline on behalf of another interstate pipeline be made self-executing.[131] The Commission stated that certificates were necessary to implement transportation services between interstate pipelines, and that the NGPA did not supersede the section 7 requirements of the Natural Gas Act.[132]

The Commission considered section 311(a)(1) rates and charges for interstate pipelines and reiterated the one cent per Mcf allowance and required flowthrough of excess revenues to

127. *Id.* The Commission explained that if the facility also transported gas in interstate commerce outside the provisions of § 311(a), Natural Gas Act jurisdiction would attach. *Id.* n.3.

128. *Id.* at 52,179.

129. 15 U.S.C. § 717t (1976) (contains criminal penalties). *See* Valero Transmission Co., No. ST80-330-000, 19 F.E.R.C. (CCH) ¶ 61,279 (1982) (civil penalty imposed under NGPA for engaging in § 311 transaction without meeting reporting requirements).

130. Order No. 46, *supra* note 99, at 52,180. The Commission stated that it shall be its policy "that authorization under section 311(a)(1) of the NGPA should be utilized wherever possible, without resort to certification under section 7 of the [Natural Gas Act]." *Id.*

131. *Id.*

132. *Id.*

customers.[133] The Commission stated that the one cent limit is subject to change if pipelines can show such an allowance is insufficient.[134] However, the Commission clarified its regulations to indicate that the one cent allowance was "optional."[135] The Commission stated that "if the interstate pipeline chooses, it may forego the allowance and demonstrate its out-of-pocket expenses to the Commission. The Commission will not require a flow back of any amount the interstate pipeline has established as representative of out-of-pocket expenses."[136] The Commission also amended its regulations to clarify that an interstate pipeline could only elect to use its own filed rates for comparable service and could not use filed rates for comparable service by another interstate pipeline.[137]

In Order No. 46 the Commission rejected two suggestions concerning rates for intrastate pipelines under section 311(a)(2). First, the Commission stated it would be unreasonable to let an intrastate pipeline base its rates on comparable tariffs of an interstate pipeline.[138] The Commission indicated that the "costs of operation of intrastate and interstate pipelines are simply not comparable."[139] Second, the Commission rejected the suggestion that an intrastate pipeline be allowed to file a tariff with the state regulatory agency if it did not have one on file. The Commission indicated that "[i]t would be unwise for the Commission to delegate to a state regulatory agency the power to set the rate to be charged to an interstate pipeline for section 311(a)(2) transportation."[140] The Commission, however, did accept one suggestion. It stated that Commission action regarding a specific transportation service took precedence over a rate derived by a formula under the regulations.[141]

In Order No. 46 the Commission also addressed several comments regarding the two-year term of the self-executing transactions, including suggestions that extensions beyond two years also be self-executing, that the two-year review by the Commission be replaced by a program limiting transportation on a priority basis, and that "best efforts" section 311(a) transportation

133. *Id.* at 52,181.
134. *Id.*
135. *Id.*
136. *Id.*
137. *Id.*
138. *Id.* at 52,182.
139. *Id.* The Commission stated that "[t]he final rule in § 284.123(b)(1)(ii) has been amended to make clear that only a 'then effective' tariff filed by the transporting intrastate pipeline may be used for comparison." *Id. See* Oasis Pipeline Co., No. SA80-107, 12 F.E.R.C. (CCH) ¶ 62,186 (1980) (comparable service means rate schedule for city-gate service).
140. *Id.*
141. *Id.*

be used to alleviate the need to review the pipeline's capacity to engage in the section 311 transportation.[142] The Commission agreed that extensions of two years are self-executing unless the extension is not in the public interest.[143] The Commission rejected the other suggestions because it believed "that it is appropriate to review long-term transportation arrangements in order to allow an evaluation of the impact of such arrangements on the capacity of interstate pipelines to meet the needs of its customers."[144]

The Commission later modified the regulations issued in Order No. 46 and clarified the term "cost of service" by stating that the appropriate standard encompassed rates set by reference to costs rather than by reference to the rate the service could demand.[145] The Commission also clarified its requirement of excess revenue crediting for transportation under section 311(a)(1). It stated that its regulations required an interstate pipeline to credit only that portion of the excess revenues above one cent per MMBtu which are allocable to jurisdictional customers.[146]

The Commission's regulations under section 311(b) were promulgated before the issuance of Order No. 46.[147] Under the section 311(b) regulations intrastate pipelines may sell gas to interstate pipelines or local distribution companies served by interstate pipelines without prior Commission approval for up to two years.[148] The sales can be extended for periods of up to two years if the Commission does not disapprove after opportunity for comment.[149] However, the sale is subject to interruption at the seller's discretion or by the Commission to the extent the gas is needed by the intrastate pipeline to provide adequate service to its customers.[150] After a hearing a sale may be terminated by the Commission if adequate service cannot be maintained or if the intrastate pipeline acquired the gas solely or primarily for the purpose of resale under section 311(b).[151] The Commission also specified the rates and charges for such sales and related services.[152] An intrastate pipeline was authorized to sell gas without prior

142. *Id.* at 52,181.
143. *Id.*
144. *Id.* Self-executing transactions under § 311(a)(1) are conditioned on sufficient capacity on the interstate pipeline to provide service without "detriment or disadvantage to . . . existing customers." 18 C.F.R. § 284.104(a) (1981).
145. Order on Rehearing No. 46, *supra* note 99, at 66,790. The Commission explained that a state agency could qualify as an "appropriate" agency for some rates but not for others. *Id.* at 66,789-90.
146. *Id.* at 66,791.
147. 18 C.F.R. §§ 284.141-.148 (1981).
148. *Id.* § 284.145.
149. *Id.* § 284.146.
150. *Id.* § 284.145(b).
151. *Id.* § 284.145(e).
152. *Id.* § 284.144.

Commission approval for a two year period at the "weighted average acquisition cost of natural gas."[153]

In sum, the Commission established an elaborate program under which significant amounts of gas could be sold and transported under section 311 without prior authorization and without fear of jurisdictional consequences for intrastate pipelines. The Commission, however, did not act to the full extent of its authority in promulgating its section 311 regulations.

V. DECISIONS UNDER SECTION 311

> Much of the apparently ridiculous action of the courts is calculated to contain bureaucratic self-dealing to manageable proportions.[154]

A. SECTION 7 OF THE NATURAL GAS ACT VS. SECTION 311 OF THE NATURAL GAS POLICY ACT

The Commission announced a policy that no certificates of public convenience and necessity would be issued to interstate pipelines under section 7 of the Natural Gas Act "unless the reasons for not transporting pursuant to section 311(a)(1) are extraordinary."[155] It also stated that section 311(a)(1) should be utilized wherever possible without resort to section 7 of the Natural Gas Act.[156] The Commission's reason for announcing this policy was easy to discern. Transactions for certain types of

153. Under § 311(b)(2) the sale is made at the intrastate pipeline's "weighted acquisition cost." 18 C.F.R. § 284.145 (1981). Under § 311(b)(2)(B) the Commission is required to establish by rule an amount necessary to compensate the intrastate pipeline for the costs of gathering, treating, transporting, processing, and delivering the gas, including the opportunity to earn a reasonable profit. If the "weighted acquisition cost" is raised by purchases by an intrastate pipeline to satisfy a § 311(b) sale, the Commission can permit recovery above the weighted acquisition cost. The determination of the weighted acquisition cost is required to reflect the contemporaneous costs associated with § 311(b) sales. S. REP. No. 1126, 94th Cong., 2d Sess. 108 (1978). The final rule provided that the weighted acquisition cost would be based on the "most recent calendar month data for which data was available prior to the first day of the billing period in which deliveries pursuant to the sale occur and for which deliveries the weighted acquisition cost is to be charged." Certain Sales of Natural Gas by Intrastate Pipelines, 3 F.E.R.C. (CCH) ¶ 30,035, at 30,278 (1979).

154. R. NEELY, HOW COURTS GOVERN AMERICA ____ (1981).

155. Order No. 46, *supra* note 99, at 52,180.

156. *Id.* Earlier the Commission had utilized the same policy in denying ONG Western, Inc., an Oklahoma natural gas gatherer, § 7(c) certificate authority to sell approximately 100,000 Mcf of gas per day over a period of eight years on a best efforts basis to Natural Gas Pipeline Company of America, an interstate pipeline. ONG Western, Inc., No. CP79-133 (Federal Energy Regulatory Comm'n Aug. 1, 1979). The Commission denied the application on the ground that ONG Western had not satisfied the criteria established for approval of limited term emergency sales of natural gas; no showing had been made that the interstate pipeline needed the gas. The Commission also observed that ONG could have utilized the § 311 regulations to consummate the sale without fear of inducing Commission regulation under the Natural Gas Act and without the need for requesting pregranted abandonment, two factors for which ONG had requested approval in applying for the § 7 certificate.

transportations and sales of natural gas could be commenced under the section 311 regulations without the need for prior regulatory approval. In *ONG Western, Inc.*,[157] the Commission noted that sections 311(b) provided "freedom from the burden of regulation and a limitation on the commitment of the gas beyond the term of the sale."[158]

In several orders subsequent to Order No. 46 the Commission adhered to its policy of favoring section 311 over section 7 in treating several applications.[159] However, the Commission soon confronted a situation which required a more detailed explanation of its policy of preference for section 311 over section 7.[160] In the spring of 1979 Algonquin Gas Transmission Company, Texas Eastern Transmission Corporation, and Transcontinental Gas Pipe Line Corporation filed applications seeking authorization under section 7 for various transportation and exchange services for liquefied natural gas (LNG) imported from Algeria. The applicants had negotiated long-term arrangements pursuant to encouragement from the Commission after the services had been authorized under a series of single year certificates. Additionally, on the expiration of those certificates the various transportation services had been commenced by the applicants on a self-implementing basis under section 311(a)(1).[161] The Commission indicated that while its decision did not signal a change in its preference for section 311(a)(1), the greater certainty available under the Natural Gas Act was appropriate in order to minimize the risks inherent in the LNG trade. The Commission stated:

> If anything, this decision and the detailed discussion above should be read as a reaffirmation of the superiority of NGPA Section 311(a)(1) as a vehicle for authorizing

157. ONG Western, Inc., No. CP79-133 (Federal Energy Regulatory Comm'n Aug. 1, 1979).

158. *Id.* at 3.

159. In one instance the Commission noted the absence of compelling reasons for acting under § 7 of the Natural Gas Act and granted authority under § 311(a)(1) to Transcontinental Gas Pipe Line Corporation to transport 9900 dekatherms of gas per day on behalf of United Cities Gas Company. The Commission took this action despite the fact that Transcontinental had requested § 7 authorization. Transcontinental Gas Pipe Line Corp., No. CP70-391, 10 F.E.R.C. (CCH) ¶ 61,040 (1980). On rehearing the Commission discussed Transcontinental's requested clarification that the parties to the § 311 transaction had the same rights and remedies as if authority had been granted under § 7. Transcontinental Gas Pipe Line Corp., No. CP79-391, 10 F.E.R.C. (CCH) ¶ 61,209. Transcontinental sought assurance that it could seek a rate increase and that it could rely on the finality of the order authorizing service under § 311. *Id.* The Commission observed that Transcontinental could rely on the finality of the earlier order, and that the § 311 regulations provided a mechanism under which an amendment to the conditions and terms of service could be sought. More importantly, however, the Commission stated, "[t]he transportation service is authorized herein under the NGPA and the rights and remedies of parties to the service are determined by reference to that statute." *Id.* at 61,384.

160. Algonquin Gas Transmission Co., No. CP79-234, 11 F.E.R.C. (CCH) ¶ 61,212 (1980).

161. *Id.* at 61,426.

> these services. There are a great many factors which support the Commission's preference for NGPA Section 311(a)(1); precious few considerations would support the exercise of our authority under the [Natural Gas] Act. Section 311(a)(1) provides a simple, straightforward statutory mechanism which essentially incorporates the core protections and provisions of the Act and, if Algonquin's transportation arrangement can be regarded as typical, the framework within which interstate pipelines normally undertake transportation services.[162]

In *Algonquin* the Commission stated that an interstate pipeline was not free to select whether it would receive authorization under section 7 or section 311. To allow such a choice would undermine the discretion "which Congress intended for the Commission to have" to determine when the grant of authority under each section would best serve the public interest.[163] The Commission also stated that it could exercise its authority to impose conditions on section 311(a)(1) transportation requiring continuity of service and nondiscrimination. In this way, the applicant would receive the same protection under section 311 as it would have under the antidiscrimination provision of the Natural Gas Act and the provision of the Natural Gas Act requiring abandonment authorization before cessation of service. The Commission further stated that its enforcement provisions were more comprehensive under the NGPA and that authorizing transportation under section 7(c) would create the potential for discriminatory impact with respect to other section 311 transactions.[164]

Recently the Commission reversed its position in *Algonquin*.[165] In an order issued on August 20, 1980, the Commission authorized Tennessee Gas Pipeline to transport natural gas on a best efforts interruptible basis for Southern Connecticut Gas Company under section 311(a)(1) of the NGPA, although Tennessee sought section 7 certificate authorization.[166] Tennessee sought rehearing,[167] and

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162. *Id.*
163. *Id.* at 61,425.
164. *Id.*
165. Tennessee Gas Pipeline Co., No. CP79-352, 16 F.E.R.C. (CCH) ¶ 61,016 (1981).
166. Tennessee Gas Pipeline Co., No. CP79-352, 12 F.E.R.C. (CCH) ¶ 61,178 (1980).
167. 16 F.E.R.C. (CCH) ¶ 61,016. Tennessee argued that a pipeline has the ability to elect between § 311 and § 7(c) and that if a § 7(c) certificate application is filed the Commission must act on the application without changing it into a request for § 311 authorization. *Id.* at 61,025. Tennessee also contended that the language of § 7 of the Natural Gas Act is mandatory. *Id.* Tennessee contended that § 7 is to be contrasted with § 5 which states that the Commission may issue temporary certificates. Tennessee also claimed that, even assuming the Commission did have discretion to proceed under either § 311 or § 7, the circumstances of Tennessee's arrangement

after oral argument, the Commission concluded that pipelines have the ability to choose whether to utilize section 7(c) or section 311.[168]

The Commission's conclusion in *Tennessee* is significant because it allows interstate pipelines greater latitude in structuring natural gas transportation arrangements. Interstate pipelines can engage in short-term transportation on a self-executing basis or can commence such activity while awaiting a certificate authorizing transportation for an extended term. These self-implementing transactions also can be commenced with a degree of confidence regarding the rates to be charged. An interstate pipeline can also elect to seek Commission approval under section 311(a)(1) on a longer term basis.

B. RATES AND CHARGES

The Commission has shown flexibility in implementing its regulations regarding rates under section 311. For example, under section 311(a)(2) several intrastate pipelines without city-gate rates on file with the state regulatory agency have been granted waivers of the city-gate requirement and have been allowed to file cost of service information with the state regulatory agency.[169] In a case of first impression involving the comparability of service standard of section 311(a)(2)(B)(i), the Commission approved use of a rate proposed by Black Warrior Pipeline, an intrastate pipeline, for service rendered to Southern Natural Gas Company, an interstate pipeline.[170] The Commission used Southern Natural's current rate of return to calculate the rate which Southern Natural would have been permitted to charge if it had constructed and operated the pipeline extension, instead of Black Warrior.[171] The Commission

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required that § 7 authority be granted. *Id.* at 61,026. Finally, Tennessee claimed the legislative history surrounding § 311 indicated there was no intent to amend or abolish § 7 of the Natural Gas Act. *Id.* at 61,025.

168. *Id.* at 61,026.

169. *E.g.*, Hydrocarbon Transfer, Inc., No. SA80-70, 10 F.E.R.C. (CCH) ¶ 62,232 (1980) (Hydrocarbon permitted to base rate on transportation component of § 311(b) sales rate for noncity-gate service; rate to be subjected to cost of service analysis by Texas Railroad Commission); Delhi Gas Pipeline Corp., No. SA80-73, 11 F.E.R.C. (CCH) ¶ 62,028 (1980); Dow Pipeline Co., No. SA80-77, 11 F.E.R.C. (CCH) ¶ 62,205 (1980); Southwestern Gas Pipeline, Inc., No. SA80-128, 13 F.E.R.C. (CCH) ¶ 62,055 (1980) (intrastate pipeline permitted to use industrial tariff on file with Texas Railroad Commission otherwise pipeline would be subjected to dual agency review); GHR Transmission Corp., No. SA81-35-000, 16 F.E.R.C. (CCH) ¶ 62,617 (1981). In each instance the applicant was granted an "adjustment" under § 502(c) of the NGPA. An adjustment may be granted if application of an NGPA rule will result in special hardships, inequity, or an unfair distribution of burdens. 15 U.S.C. § 3412(c) (Supp. III 1979). The Commission has not granted waivers in all instances. IMC Pipeline Co., No. SA80-133, 13 F.E.R.C. (CCH) ¶ 62,215 (1980).

170. Black Warrior Pipeline, Inc., No. CP79-295 (Federal Energy Regulatory Comm'n Aug. 31, 1979).

171. *Id.* The Commission looked to Black Warrior's cost of service for facilities proposed to be constructed to implement the transportation and the rate of return approved by the Commission in

concluded that the rates proposed by Black Warrior were very close to those Southern Natural would have been permitted to charge. Therefore, the Commission approved the proposed rates. In another instance the Commission, while noting that the standards were different for approving rates under section 7 and section 311, delayed a determination on a proposed intrastate section 311 rate pending investigation of the rate in a section 7(c) certificate application sought by the intrastate pipeline so it could undertake the service for an extended term.[172]

In *Panhandle Eastern Pipe Line Co. v. Federal Energy Regulatory Commission* the court rejected the Commission's argument that not allowing the flowthrough of uncontemplated revenues would constitute a windfall to Panhandle, whose rates already were designed to cover its cost of service.[173] In Order No. 46 the Commission had upheld the one cent allowance and ensuing flowthrough on the ground that a greater incentive might have an adverse effect on other short-term transactions and purchases for system supply.[174] The court noted the similarity of the certificate condition in *Panhandle* with the crediting requirements for section

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Southern Natural's most recent pipeline rate case. The Commission specifically noted that, as a case of first impression, the course followed would not be the exclusive method for determining fair and equitable rates. *Id.*

172. Big Sandy Gas Corp., No. ST80-94, 12 F.E.R.C. (CCH) ¶ 61,031 (1980). The Commission, however, made the following statement:

> The Commission . . . must consider the appropriate initial rates for the same interstate service. Although there is a commonality of inquiry between the section 7 and section 311 proceedings, the standard for the respective proceedings is different, as is the service in question. Consequently, our determination in the section 7 proceeding will not, of necessity, determine the fair and equitable rate.

Id. at 61,055.

173. 613 F.2d 1120 (D.C. Cir. 1979). The *Panhandle* case involved three petitions for review. Two of the petitions challenged the Commission's actions requiring Panhandle to flowthrough transportation revenues via the unrecovered purchased gas account, account 191, while prohibiting the flowthrough of new transportation costs. Panhandle was transporting gas for an end user, Libby-Owens-Ford. The Commission required Panhandle to credit transportation revenues received from Libby-Owens, but denied Panhandle the flowthrough of the costs of gas transportation for Libby-Owens, a portion of which was performed by Trunkline. Panhandle claimed that under Commission regulations account 489 was the proper location for the transportation revenues. The Commission, however, said account 489 was inappropriate because account 489 defers revenues until a rate proceeding under § 4 of the Natural Gas Act and because it has no provision for flowing excess revenues to customers. Panhandle Eastern Pipeline Co. v. Federal Regulatory Energy Comm'n, 613 F.2d at 1135.

The court also held that the Commission erred in requiring the crediting of revenues as a certificate condition. The court stated that requiring the crediting of revenues without an offset for expenses was unreasonable. The court concluded that the Commission had no power under § 7(e) of the Natural Gas Act to attach certificate conditions concerning rate changes because they should be implemented under § 5 of the Natural Gas Act. Additionally, the court stated that the Commission could consider rates in issuing certificates, but could not adjust previously approved rates in the process. The court suggested that the Commission might use tracker provisions to solve the problem of costs of transportation performed by other pipelines. The court also stated that the Commission had violated its own regulations by requiring flowthrough under account 191 when account 489 provided the appropriate mechanism. *Id.*

174. Order No. 46, *supra* note 99, at 52,181.

311(a)(1) transportation revenues, but declined comment.[175]

In light of the *Panhandle* decision, the Commission has considered its revenue crediting requirement in several section 7(c) certificate cases.[176] In at least one instance, the Commission has dealt with the issue of revenue crediting in the context of section 311(a)(1) service, when it required the interstate pipeline to treat section 311(a)(1) revenues in the manner provided in the pipeline's most recent rate case.[177] The Commission, however, has not altered its basic revenue crediting requirements under its section 311(a)(1) regulations. But, the validity of the revenue crediting requirements is subject to serious question in light of *Panhandle.* If the one cent allowance does not serve as an incentive for interstate pipelines to engage in section 311(a)(1) transportation services, the congressional purpose of creating a national natural gas pipeline network is not fostered.[178]

The Commission has considered at least one challenge to the transportation rates of an intrastate pipeline selling gas to an interstate pipeline under section 311(b).[179] The Nueces Company, an intrastate pipeline, had filed an application with the Commission seeking approval of rates charged for the sale and transportation of gas to Colorado Interstate Gas Company, an interstate pipeline.[180] The Public Service Company of Colorado and others filed a complaint challenging the transportation rate charged by Nueces. The Commission dismissed the complaint because the complaint contested the transportation rate rather than

175. 613 F.2d at 1136 n.86. The court concluded that "[s]ince the enactment of the statute [NGPA] and promulgation of the regulations occurred after entry of the instant order, they provide no support for the Commission's decision here. The validity of the new regulations is not an issue in this case, and consequently we leave that question undecided." *Id.*

176. Northwest Pipeline Corp., No. CP77-457, 14 F.E.R.C. (CCH) ¶ 61,205 (1981) (Commission deleted certificate condition that interstate pipeline credit all but one cent per Mcf transportation revenues to purchased gas adjustment (PGA) account). However, the results have not been consistent. *See* Natural Gas Pipeline Co., No. CP81-302, 16 F.E.R.C. (CCH) ¶ 61,130 (1981) (Commission deferred resolution of treatment of costs and revenues associated with sales and transportation in an off-system sale for consideration in interstate pipeline's pending rate proceedings); Michigan Wisconsin Pipe Line Co., No. CP80-176, 12 F.E.R.C. (CCH) ¶ 61,272 (1980) (treatment of interstate pipeline's rates and revenues for sale of gas to electric utility to displace fuel oil set for hearing); Texas Eastern Transmission Corp., No. CP78-129, 15 F.E.R.C. (CCH) ¶ 61,238 (1981) (Commission amended a certificate order that implemented Texas Eastern's settlement agreement in its pipeline rate case to credit all revenues to its account 191 less one cent per dekatherm or such higher incremental costs to perform the transportation as Texas Eastern could demonstrate).

177. Transcontinental Gas Pipe Line Corp., No. CP79-391, 10 F.E.R.C. (CCH) ¶ 61,209 (1980). The effect is to require the refund of all revenues above those utilized in calculating the cost of service for the test period to sales and firm transportation customers.

178. *See* Holtzinger, *Transportation Under Section 311 of the NGPA,* OIL & GAS REGULATION ANALYST, April 1981, at 6.

179. Nueces Co., No. ST79-6, 12 F.E.R.C. (CCH) ¶ 61,031 (1980).

180. *Id.* at 61,054. Nueces also had applied for a certificate under the Natural Gas Act, which would authorize the transportation of the gas on a long-term basis. *Id.* Under the Commission's regulations, the sale under § 311(b) was self-implementing. However, Nueces sought approval of the transportation rate. *Id.*

termination of the sale.[181] The Commission postponed action on Nueces' proposed transportation rate until it considered the rates in the section 7(c) certificate application.[182] Thus, the Commission indicated that the provisions of section 311(b)(6) under which section 311 sales may be terminated by the Commission in certain instances are not available as a means of contesting section 311 transportation rates.

C. DEFINITION OF THE TERM TRANSPORTATION

In Order No. 46 the Commission defined the term "transportation" to include exchanges, backhauls, displacement, and other methods of transportation.[183] A recent interpretation rendered by the Commission's General Counsel pursuant to section 1.42 of the Commission's regulations indicates that storage is included within the term "transportation."[184] This interpretation should give added flexibility to pipelines when they structure transactions. In at least one proceeding, however, the Commission has indicated that an intrastate pipeline cannot reserve pipeline capacity without making at least some deliveries as part of an arrangement to provide section 311 transportation service for an interstate pipeline.[185] The Commission indicated that

181. *Id.* at 61,055. Pursuant to the provisions of § 311(b)(6) of the NGPA, 15 U.S.C. § 3371(b)(6), the Commission on its own motion or on complaint of an interested person may terminate a § 311(b) sale if the Commission determines that: Termination is required to enable the intrastate pipeline to provide adequate service to its customers at the time of the sale, the sale involves natural gas acquired by the intrastate pipeline solely or primarily for the purpose of resale, the sale violates any term or condition established by rule or order of the Commission applicable to the sale, or the sale circumvents or violates any provision of the NGPA. 18 C.F.R. § 284.147(c)(1)-(4) (1981). The Commission's regulations regarding transportation rates under § 311(a)(2) do not provide a mechanism for challenging the transportation charges of an intrastate pipeline. When an intrastate pipeline seeks the Commission's approval of a rate under 18 C.F.R. § 284.123(b)(2)(i), the rate is deemed approved unless the Commission disapproves the proposed rate within 150 days or extends the time for action. 18 C.F.R. § 284.123(b)(2)(ii) (1981).

182. Nueces Co., *supra* note 179, at 61,055.

183. Order No. 46, *supra* note 99, at 52,184. In Panhandle Eastern Pipe Line Co., No. CP80-231, 12 F.E.R.C. (CCH) ¶ 61,159 (1980), the Commission approved a 20 year gas exchange between Panhandle and Stauffer Chemical Company under the transportation provisions of § 311.

184. Letter Opinion, Consumers Power Company (July 1, 1981), *reprinted in* FED. PROGRAMS ADVISORY SERVICE ¶ 4543 (Aug. 8, 1981). Consumers Power Company, a Hinshaw pipeline exempt from regulation under § 1(c) of the Natural Gas Act, requested an interpretation of whether a proposal to render storage service to West Lake Arthur Distribution Company during the 1981-82 winter months would constitute "transportation" under § 311. The General Counsel answered the question in the affirmative, observing that under the Natural Gas Act storage has consistently been viewed as an integral part of sales and transportation service. *Id.* at 2. Because the storage service would have been subject to § 7(c) of the Natural Gas Act in the absence of § 311, the General Counsel concluded that storage could also be authorized under § 311. *Id.* In specifying the rates and charges for transportations under § 311 the Commission refers to "storage costs" in the case of both interstate and intrastate pipelines. *See* 18 C.F.R. § 284.103(c) (1981); 18 C.F.R. § 284.123(b) (1981).

185. Producer Gas Co., No. ST79-8, 12 F.E.R.C. (CCH) ¶ 61,032 (1980). In connection with a § 311(b) sale by Producer Gas Company to Panhandle Eastern Pipe Line Company, Transok Pipe Line Company, an intrastate pipeline, sought approval from the Commission under 18 C.F.R. § 284.123(b)(2) of rates to be charged to an interstate pipeline for transporting natural gas under § 311. Transok had reserved pipeline capacity to perform the service, but the interstate pipeline had

its regulations require gas deliveries, and that reservation of capacity without more does not constitute transportation.

D. PARTIES WHO CAN TRANSPORT GAS UNDER SECTION 311

The meaning of the definition of the term "intrastate pipeline" has arisen in several instances. The Commission stated in one case that an intrastate pipeline is defined as a person and not in terms of facilities.[186] In another instance the Commission confirmed the intrastate status of a pipeline that had transferred its Hinshaw pipeline facilities to an affiliate.[187] The Commission's decision in yet another instance indicates it may be inclined to a broad definition of the term "intrastate pipeline."[188] Although it rejected a section 7 certificate application, the Commission suggested that a company that had defined itself as a "gatherer" in an application for a certificate to make a sale to an interstate pipeline might attempt a section 311(b) sale.[189] The Commission's willingness to construe the term "intrastate pipeline" in a broad manner further increases the utility of section 311.

Recently, the Commission issued three orders delineating the consequences of participation in various section 311 transactions involving the sale of gas across state lines. In the first case[190] two intrastate pipelines requested a declaratory order regarding the proposal by the Oklahoma pipeline to sell surplus gas to the Texas pipeline with transportation provided by an interstate pipeline under section 311(a)(1). The pipelines contended that by virtue of sections 601(a)(2)(A) and 601(a)(2)(B) of the NGPA, the sale and transportation of the gas were nonjurisdictional. The Commission concluded that although section 601(a)(2)(B) insulated the transporter from jurisdiction, the sale was clearly a sale for resale in interstate commerce.[191]

The second proceeding involved a section 311(a)(1)

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not requested commencement of service. The Commission's order states that transportation requires deliveries of gas and that reservation of capacity "without more" is not transportation. *Id.* at 61,057.

186. Seagull Pipeline Corp., No. CP79-240, 11 F.E.R.C. (CCH) ¶61,267 (1980).

187. Delhi Gas Pipeline Corp., No. CP68-139 (Federal Energy Regulatory Comm'n Nov. 19, 1979).

188. ONG Western, Inc., No. CP79-133 (Federal Energy Regulatory Comm'n Aug. 1, 1979). In *ONG Western* the Commission was confronted with a certificate application by ONG to sell gas to Natural Gas Pipeline Company of America. The Commission's order reveals that ONG was asserting it was a gas gatherer for its parent company. *Id.* No certificate was issued because ONG indicated it would accept a certificate only under certain conditions. *Id.* at 2. The Commission suggested ONG attempt a § 311(b) sale. *Id.* at 3. This statement suggests the possibility that the Commission might construe the definition of "intrastate pipeline" broadly.

189. *Id. See also* Panhandle Eastern Pipe Line Co., No. CP80-231, 12 F.E.R.C. (CCH) 61,159 (1980) (end user with significant transmission system classified as intrastate pipeline).

190. Delhi Gas Pipeline Corp., No. CP81-496-000, 19 F.E.R.C. (CCH) ¶61,189 (1982).

191. *Id.*

application by an interstate pipeline to transport gas from Texas to Louisiana to implement a direct sale of gas by a Texas intrastate pipeline to a high priority Louisiana end user.[192] The Commission granted the transportation authority noting that the direct sale was nonjurisdictional in contrast to a sale for resale in interstate commerce. Thus, the intrastate pipeline did not jeopardize its status by participation in the sale.[193]

The third proceeding involved the section 311(a)(1) application by an interstate pipeline to transport gas by exchange from New Mexico to Texas for delivery to a Texas intrastate pipeline which had purchased the gas in New Mexico.[194] The gas was not subject to the certificate requirements of the Natural Gas Act because the gas was not "committed or dedicated to interstate commerce" within the meaning of section 2(18) of the NGPA.[195] In this circumstance, the Commission declared that the Texas intrastate pipeline would not be subject to Natural Gas Act jurisdiction.

VI. STATISTICAL ASSESSMENT OF SECTION 311 TRANSACTIONS

> Valid form derives only from function understood and served.[196]

The statistics compiled by the Commission on the self-implementing transactions commenced under the section 311 regulations indicate that the Commission's program has been successful.[197] Under section 311(a)(1) interstate pipelines have commenced a total of 169 self-implementing transportations for intrastate pipelines and local distribution companies involving an estimated total movement of over 769 million MMBtu of natural gas from December 1, 1968, through October 31, 1981.[198] The monthly quantity of gas moving under the self-implementing transactions rose nearly tenfold since December 1, 1978, to the

192. United Gas Pipe Line Co., No. CP81-52-000, 19 F.E.R.C. (CCH) ¶ 61,190 (1982).

193. *Id.*

194. Transwestern Pipeline Co., No. CP81-99-000, 19 F.E.R.C. (CCH) ¶ 61,191 (1982). The Commission issued a declaratory order to clarify the jurisdictional consequences, although the application was withdrawn.

195. *Id.*; 15 U.S.C. § 3301(18) (Supp. III 1979).

196. J. FITCH, AMERICAN BUILDING 270 (2d ed. 1966).

197. *See* Federal Energy Regulatory Commission, Office of Pipeline and Producer Regulation, Staff Report on Part 157 and Part 284 Self-Implementing Transactions Which Commenced From December 1, 1978, Through September 30, 1981 (n.d.) (available through Public Information Division, Federal Energy Regulatory Commission, Washington, D.C.).

198. *Id.*, Appendix A, at 1.

estimated monthly level of approximately forty-five million MMBtu during the months of June 1981 through September 1981 and to fifty-three MMBtu in October 1981.[199] The maximum number of section 311(a)(2) self-implementing transactions commenced in any month has been twelve, in October 1980.[200] In September 1981 only two such transactions were commenced.[201]

In contrast, intrastate pipelines have transported an even greater quantity of gas for interstate pipelines and local distribution companies under the self-implementing regulations of section 311(a)(2). During the period of February 1979 through October 1981 intrastate pipelines commenced 127 transportations involving an estimated total movement of over one billion MMBtu.[202] The estimated monthly movement under the self-implementing provisions of section 311(a)(2) averaged approximately fifty-five million MMBtu during the months of June 1981 through October 1981.[203]

Under the self-implementing regulations of section 311(b) a total of fifty-four sales by intrastate pipelines were commenced from March 1979 through October 1981.[204] Through October 1981 an estimated total of over one billion MMBtu of gas has been sold under these self-implementing provisions.[205] The peak month of such sales occurred in January 1980. In that month almost forty-seven million MMBtu of gas was sold by intrastate pipelines under the self-implementing provisions of section 311(b).[206] The prices for these sales has ranged from $.89 per MMBtu to $3.30 per MMBtu.[207]

While the foregoing statistics are by themselves impressive, they do not include the other self-implementing transactions which were modeled after the section 311 provisions.[208] In the period from December 1978 through October 1981 an estimated total of over

199. *Id.*
200. *Id.*
201. *Id.*
202. *Id.*
203. *Id.*
204. *Id.*, Appendix A, at 5.
205. *Id.*
206. *Id.*
207. *Id.*
208. During the period from February 1980 through October 1981 interstate pipelines with blanket certificates under § 311(a)(2) commenced 274 transportations involving an estimated total movement of over one and a half billion MMBtu. The monthly figure has risen steadily to over 148 million MMBtu in October 1981. Hinshaw pipelines have transported an additional four million MMBtu under the self-implementing provisions of part 284(g) during the period October 1980 through October 1981. Hinshaw pipelines have sold over 238 million MMBtu under the self-implementing provisions of 18 C.F.R. Part 284(g) from July 1980 through October 1981. From June 1979 through October 1981 over 140 million MMBtu of natural gas has been transported under the self-implementing transportations of fuel oil displacement gas. *Id.*

5,191 million MMBtu of natural gas was either sold, transported, exchanged, or assigned in self-executing transactions.[209] This performance was achieved without the necessity of the participants engaging in a possibly extended certification procedure and without subjecting the nonjurisdictional participants to the Commission's jurisdiction under the Natural Gas Act.

In addition to reviewing statistics, however, any assessment of section 311 must be made in light of the current supply and demand posture of the interstate and intrastate markets. In November 1981, the Senate Committee on Energy and Natural Resources heard testimony that the most serious development caused by Title I pricing has been the emergence of a dual market structure favoring interstate over intrastate pipelines. The committee also heard testimony that as a result of Title I the "gas bubble" has shifted from the intrastate to the interstate markets, and that intrastate market, such as the Texas market, are in a bad position in terms of gas availability.[210] Although the Commission has moved to correct the dilemma to some extent by authorizing a significant number of "off-system" sales by interstate pipelines to intrastate pipelines and end users in the intrastate market,[211] certain of those commenting at the Senate hearings on the current dual market structure advocated creation of a free market structure through the phased deregulation of all natural gas by 1985. In recent testimony before the House Subcommittee on Fossil and Synthetic Fuels, a number of witnesses again stated that the intrastate markets, such as Texas and Louisiana, are severely disadvantaged under the NGPA in terms of access to reasonably priced gas supplies.[212]

In this regard it should be noted that several natural gas "deregulation" bills have been introduced in Congress.[213] In

209. *Id.* at 5.

210. *Implementation of Title I of the Natural Gas Policy Act of 1978: Hearings Before the Senate Committee on Natural Resources,* 97th Cong., 1st Sess. 5 (1981) (testimony of C. M. Butler, III, Chairman of the Commission); *id.* at 53 (testimony of James E. Nugent, Chairman, Texas Railroad Commission); *id.* at 69 (testimony of Mr. Ed Vetter, Energy Advisor to the Governor of Texas).

211. *E.g.,* Natural Gas Pipeline Co., No. CP81-302, 16 F.E.R.C. (CCH) ¶61,130 (1981).

212. *Review of Current Federal Policy on Natural Gas: Hearings Before the House Subcommittee on Fossil and Synthetic Fuels,* 97th Cong., 2d Sess. (1982) (testimony of James E. Nugent, Chairman, Texas Railroad Commission, and Frank P. Simoneaux, Secretary of Natural Resources, State of Louisiana).

213. H.R. 4885, 97th Cong., 1st Sess. (introduced Nov. 4, 1981, by Rep. Collins); H.R. 4390, 97th Cong., 1st Sess. (introduced Aug. 4, 1981, by Rep. Gramm). Two additional bills have been introduced which are aimed, in part, at eliminating certain restrictions on the transmission of natural gas. On February 8, 1982, Senators Johnston and Long introduced Senate Bill 2074. S. 2074, 97th Cong., 2d Sess., 128 CONG. REC. S491-96 (daily ed. Feb. 8, 1982). Under Senate Bill 2074, Title III of the NGPA would be amended to allow any pipeline to sell gas to any other pipeline or local distribution company. Under a new § 311(b)(3) the rates and charges for interstate pipelines would have to be "just and reasonable" within the meaning of the Natural Gas Act. Sales by an interstate pipeline under § 311(b)(3) would be interruptible to the extent necessary to render service

addition to dealing with natural gas pricing, these bills contain provisions designed to broaden the scope of section 311 in the movement of natural gas. These provisions include allowing any pipeline to sell gas to any other pipeline or local distribution company in any state without jurisdictional consequences as long as transportation between the states is performed by an interstate pipeline under section 7 of the Natural Gas Act or section 311(a)(1) of the NGPA. Passage of these provisions would foster the goal of facilitating the movement of natural gas, particularly to the currently disadvantaged intrastate market.

VII. CONCLUSION

[T]he glut will grow larger.[214]

This observation made by the Director of Energy Studies of the Hudson Institute in connection with oil may be equally applicable, for almost the same reasons, to natural gas. For example, he concluded that an oil glut will exist because of energy conservation, alternate fuels, slowed economic growth, inventory reduction, and falling prices.[215] A regulatory mechanism such as section 311 of the NGPA operating in a market in which supply exceeds demand, becomes effective in making gas supplies available in markets where there is a demand. In effect, section 311 allows intrastate pipeline sellers and certain buyers to approach a free market for a limited term.

The importance of section 311 could become enhanced upon passage of natural gas decontrol legislation. On January 7, 1982, the Department of Energy made available for comment a draft outline of proposed amendments to the NGPA.[216] The thrust of the

to its own customers. The Senate Bill also would add a new § 311(a)(3) providing that no amounts paid for transportation services under § 311(a) would be taken into account in setting the rates of the transporting pipeline.

Section 1(b) of the Natural Gas Act would be amended to provide that jurisdiction would not attach to transportation or sales (including sales for resale) by intrastate pipelines where all transportation between states or between the Outer Continental Shelf (OCS) and any state is performed by interstate pipelines under § 302, § 303 (President's emergency authorities), § 311(a)(1) of the NGPA, or § 7 of the Natural Gas Act.

Senate Bill 2074 also would amend § 601(a)(1)(B) of the NGPA so that the Natural Gas Act's jurisdiction would not attach to sales of gas produced in the OCS to an intrastate pipeline, local distribution company, or end user in any state. The Natural Gas Act's jurisdiction also would not attach as a consequence of any transportation used to make the foregoing sale.

On March 17, 1982, Representative Gramm introduced House Bill 5866 containing provisions similar to those outlined above. H.R. 5866, 97th Cong., 2d Sess. (1982).

214. Brown, *Can OPEC Survive the Glut?*, FORTUNE, Nov. 30, 1981, at 89.

215. *Id.* at 89-90. According to the American Petroleum Institute during the last week in January 1982, United States imports of crude oil averaged 3.08 million barrels a day, the lowest level in almost seven years. Houston Post, Feb. 4, 1982, at 2C, col. 1.

216. *DOE Circulates Draft of Latest Proposal for Phased Decontrol of Natural Gas Price,* FOSTER'S NATURAL GAS REPORT, Jan. 14, 1982, at 1.

draft proposal was not much different from the positions taken during the summer of 1981 by the Reagan Administration and by the two bills on gas deregulation introduced in Congress during August and October of 1981.[217] The pertinent features of the draft outline included the immediate descontrol of new gas supplies and the phased decontrol by 1985 of old gas prices. In the event of passage of such legislation, section 311 could prove instrumental in allowing the movement of natural gas to satisfy demand.

In the absence of further legislation, however, the Commission possesses the administrative authority to make section 311 even more useful. For example, eliminating the requirement that interstate pipelines credit excess revenues from section 311 transportation to their cost of service would encourage additional participation. Also, the Commission could delete the requirement that section 311 transactions be self-executing only when the gas is acquired by the pipeline for its own system supply. However, section 311 already has been instrumental in achieving its congressional objective of increasing access to the interstate markets for sources of natural gas supply traditionally in the intrastate market.

217. Memorandum from Danny J. Boggs, Executive Secretary, to Cabinet Council on Natural Resources and Environment (July 28, 1981) (discussing natural gas strategy). On August 4, 1981, Representative Gramm introduced House Bill 4390 providing for the immediate price deregulation of gas produced from wells drilled after January 1, 1985, and the phased price deregulation of all gas by 1985 to a price equal to the average wholesale price for no. 2 fuel oil. H.R. 4390, 97th Cong., 1st Sess. (1981). On November 4, 1981, Representative Collins introduced House Bill 4885 proposing a similar scheme for the decontrol of gas prices. H.R. 4885, 97th Cong., 1st Sess. (1981).