ORAL ARGUMENT IS SCHEDULED FOR SEPTEMBER 14, 2004

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IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 03-1153

CHEVRONTEXACO EXPLORATION
& PRODUCTION CO., *et al.*,
PETITIONERS,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.

ON PETITION FOR REVIEW OF ORDERS OF THE
FEDERAL ENERGY REGULATORY COMMISSION

BRIEF OF RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

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APRIL 13, 2004

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CIRCUIT RULE 28(a)(1) CERTIFICATE

A. Parties and Amici

The parties before this Court are identified in the brief of Petitioners.

B. Rulings Under Review

1. *ANR Pipeline Co.*, 101 FERC ¶ 61,123 (2002); and

2. *ANR Pipeline Co.*, 103 FERC ¶ 61,065 (2003).

C. Related Cases

This case has not previously been before this Court or any other court. Counsel is not aware of any other related cases pending before this or any other court.

_____
Lona T. Perry
Attorney

April 13, 2004

TABLE OF CONTENTS

TABLE OF AUTHORITIES

PAGE

COURT CASES:

_____

* Cases chiefly relied upon are marked with an asterisk.

TABLE OF AUTHORITIES

PAGE

COURT CASES: (con't)

ADMINISTRATIVE CASES:

TABLE OF AUTHORITIES

PAGE

GLOSSARY

ANR	ANR Pipeline Co.
Dth	dekatherm
FERC	Federal Energy Regulatory Commission
FRP	fuel reimbursement percentage rate
Hearing Order	*ANR Pipeline Co.*, 101 FERC ¶ 61,123 (2002)
NGA	Natural Gas Act
PTR shippers	plant thermal reduction shippers
Rehearing Order	*ANR Pipeline Co.*, 103 FERC ¶ 61,065 (2003)
Shippers or Petitioners	collectively petitioners ChevronTexaco Exploration & Production Co., BP America Production Co., BP Energy Co., ConocoPhillips Co., Exxon Mobil Corp., and Shell Offshore, Inc.

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STATEMENT OF THE ISSUE

Whether the Commission reasonably permitted ANR Pipeline's NGA § 4 annual cashout surcharge for 2001 -- recovering prudently incurred costs correctly calculated pursuant to an approved tariff provision -- to become effective notwithstanding findings that the underlying surcharge mechanism in the tariff had become unjust and unreasonable and required additional hearings before the just and reasonable rate "to be thereafter observed" under NGA § 5 could be established.

STATUTORY AND REGULATORY PROVISIONS

The pertinent statutes and regulations are contained in the Addendum to this brief.

STATEMENT OF THE CASE

I. Nature of the Case, Course of Proceedings, and Disposition Below

Pursuant to a tariff provision approved in 1993, ANR Pipeline Co. ("ANR") annually calculates the costs of resolving gas imbalances on its system, which costs are recovered through a surcharge applied to future transportation services. The challenged orders, *ANR Pipeline Co.*, 101 FERC ¶ 61,123 (2002) ("Hearing Order"), *on reh'g*, 103 FERC ¶ 61,065 (2003) ("Rehearing Order"), found ANR's proposal to recover its 2001 cashout costs to be calculated consistently with the tariff, and permitted the resulting surcharge to go into effect. The 1993 tariff cashout mechanism appeared to be producing unjust and unreasonable results, however, in that certain shippers lacked adequate opportunity to resolve imbalances and the surcharge varied widely from year to year. As ANR had not proposed to change the mechanism, and the current record was insufficient to devise a replacement mechanism, the Commission set the issue for hearing under Natural Gas Act ("NGA") § 5, 15 U.S.C. § 717d.

Shippers[1] contended that the NGA required the 2001 annual surcharge to be rejected and ANR to continue charging the 2000 surcharge while a just and reasonable tariff cashout mechanism is determined, or, alternatively, the 2001 surcharge to be collected subject to refund. The Commission rejected those contentions, finding that the tariff cashout mechanism could only be modified pursuant to NGA § 5, which precludes

[1] "Shippers" refers to, collectively, petitioners ChevronTexaco Exploration & Production Co., BP America Production Co., BP Energy Co., ConocoPhillips Co., Exxon Mobil Corp., and Shell Offshore, Inc.

retroactive relief, and therefore ANR could recover the 2001 surcharge in accordance with the 1993 mechanism.

II. Statement of Facts

As gas imbalances are a fact of life, pipeline tariffs provide shippers with some degree of operating flexibility. [2] ANR's tariff allows shippers to be out of balance by up to ten percent on a monthly basis after matching their receipts and deliveries. Initial Comments of ANR Pipeline Co., filed August 14, 2002, R. 27 at 2, JA 7. Shippers also may trade offsetting imbalances with other shippers. If a shipper does not eliminate its imbalances by trading, ANR's tariff requires a mandatory monthly close-out (after netting and trading of imbalances during a 15-day grace period) of any remaining imbalances. *Id*. Under close-out, when a shipper's receipts of gas on ANR exceed the shipper's deliveries off the system, ANR buys the excess, but where deliveries exceed a shipper's gas receipts, ANR sells the needed volumes to the shipper. *Id*. at 3, JA 8. The prices paid for the sales and purchases of cashout volumes are set by market-based indicies specified in ANR's tariff. *Id*.

Section 15 of the General Terms and Conditions of ANR's FERC Gas Tariff permits ANR to recover its net costs, or pass on net revenues, from operating its cashout program through an annual cashout calculation mechanism. *ANR Pipeline Co.*, 62 FERC ¶ 61,079, *on reh'g*, 64 FERC ¶ 61,140 (1993), as modified in *ANR Pipeline Co.*, 82 FERC

[2] Although individual shippers may have imbalances at a given time, the pipeline system as a whole must be in balance to maintain operating integrity.

¶ 61,080 (1998). ANR must make annual filings on May 1 to show its cash out activity for the preceding calendar year. *ANR Pipeline Co.*, 91 FERC ¶ 61,195 at 61,683 (2000). Any negative balance (where ANR spent more money than received) is charged to, while any positive balance (less ten percent of gross annual receipts) is returned to, customers through an annual surcharge, based upon actual throughput for the preceding calendar year. *Id*.

On May 1, 2002, ANR made its annual filing for 2001 cashout activity. *ANR Pipeline Co.*, 99 FERC ¶ 61,232 at 61,959 (2002). The cashout surcharge increased substantially from the 2000 level of $0.1508 to a proposed 2001 level of $0.4464, per dekatherm, leading parties to question ANR's practices as well as possible flaws in the underlying cashout mechanism. *Id*. at 61,960. In light of the questions raised, the Commission ordered a technical conference and suspended the 2002 filing. *Id*.

After a July 18, 2002 technical conference, Shippers raised three issues concerning calculation of the current surcharge. Hearing Order ¶ 6, ¶ 15, JA 49, 53. Shippers questioned why ANR paid more in some months for gas than the applicable cashout price (inclusive of the surcharge). *Id*. ¶ 16. ANR explained that the price paid to purchase gas and the cashout price are determined by different methodologies, and the amounts involved were relatively small. *Id*.; Reply Comments of ANR Pipeline Co., filed September 9, 2002, R. 30 at 3, JA 41. The monthly cashout price reflects the weighted average of index prices of both gas bought and sold at the various locations where imbalances occur, in accordance with the tariff mechanism. *Id*. ANR's actual gas

purchases, on the other hand, reflect index prices established by the supply contracts under which ANR purchased the gas. *Id*.

Shippers also questioned why no cashout revenues were shown in connection with two specified imbalance volumes. Hearing Order ¶ 15, JA 53; R. 30 at 3, JA 41. ANR explained that the shipper responsible for these imbalances had filed for bankruptcy protection and therefore ANR did not collect any actual cashout revenues attributable to these imbalances. R. 30 at 3, JA 41. Shippers also questioned an adjustment "zeroing out" a shipper's imbalance, Hearing Order ¶ 15, JA 53; R. 30 at 3, JA 41, which ANR explained was an adjustment to correct a previous erroneous allocation, R. 30 at 3, JA 41. As ANR's responses adequately addressed the issues raised by Shippers, the Commission found the proposed surcharge was calculated consistent with the approved tariff. Hearing Order ¶ 17, JA 54.

The Commission expressed concern, however, about the workings of the tariff cashout mechanism itself, finding that its past operation indicated that it was unjust and unreasonable in two respects. Hearing Order ¶ 18, JA 54. First, the mechanism gave plant thermal reduction ("PTR") shippers an inadequate opportunity to resolve their imbalances. *Id*. PTR shippers' volumes pass through processing plants, which remove certain hydrocarbons from the gas stream, thereby decreasing its thermal content. *Id*. n. 5, JA 49. As transportation on ANR is nominated on a thermal (Dth) basis, PTR shippers cannot determine the resulting amount of their deliveries until they receive actual plant thermal reduction percentages from the processing plant operators. *Id*. ¶ 8, JA 50. Those actual figures are often received too late for the PTR shippers to trade their imbalances

under ANR's tariff, and consequently PTR shippers often lack the ability to avoid imbalances. *Id*. ¶ 9. Second, the carryforward provision in the mechanism resulted in significant accumulated cashout losses being carried forward in some years, but not others, which led to wide swings in the surcharge from year to year. *Id*. ¶¶ 19-20, JA 54.

Although the Commission concluded that the tariff cashout mechanism was producing unjust and unreasonable results, the Commission did not have sufficient facts before it to devise a just and reasonable mechanism pursuant to NGA § 5. *Id*. ¶ 21, JA 55. Consequently, the Commission set the cashout mechanism for a hearing, held in abeyance for settlement discussions. *Id*.

On rehearing, Shippers argued that, once the cashout mechanism was determined to be unjust and unreasonable, the Commission must immediately reject the 2001 surcharge calculated pursuant to that mechanism. Request for Rehearing and Clarification of Indicated Shippers, filed December 2, 2002, R. 42 at 4, JA 60. According to Shippers, in the interim before a new just and reasonable cashout mechanism could be put in place, ANR should continue to charge the 2000 surcharge. *Id*. Shippers contended that failure to reject the 2001 surcharge was inconsistent with Commission precedent. *Id*. at 5, JA 61 (citing *Northwest Pipeline Corp.*, 96 FERC ¶ 61,128 (2001) and *El Paso Natural Gas Co.*, 97 FERC ¶ 61,265 (2001)). Alternatively, Shippers requested that the Commission clarify that the proposed surcharge was being collected subject to refund. *Id*. at 5-6, JA 61-62.

The Commission denied rehearing. Rehearing Order ¶ 7, JA 67. The proposed 2001 surcharge was implemented pursuant to a previously-approved tariff provision, and was calculated properly in accordance with that tariff provision, findings that Shippers did

not dispute on rehearing. *Id*. Because the underlying tariff cashout mechanism had prior FERC approval, it could only be changed prospectively in accordance with NGA § 5. *Id*. In contrast with *Northwest* and *El Paso*, which addressed pipeline proposals under NGA § 4, 15 U.S.C. § 717c, to change existing tariffs, ANR had not proposed a change in its mechanism. *Id*. Without sufficient information to determine a just and reasonable cashout mechanism a further hearing was necessary, a point even the Shippers did not dispute. *Id*. Accordingly, until such time as the Commission could fix the just and reasonable mechanism "to be thereafter observed" in accordance with NGA § 5, ANR could recover the surcharge allowed by its approved tariff. *Id*. Further, under § 5, no refunds are available based on what surcharge for 2001 costs the new just and reasonable mechanism would have produced. *Id*.

SUMMARY OF ARGUMENT

ANR's tariff permits imbalance cost recovery through a surcharge, calculated annually, applied to shippers that are out-of-balance. The challenged orders found that ANR's 2001 annual surcharge filing represented prudent actual costs of operating the imbalance program in that calendar year, calculated properly under the pre-approved tariff calculation mechanism. Therefore, the Commission permitted the surcharge to go into effect.

The Commission's review, however, indicated that the underlying tariff surcharge mechanism may be producing unjust and unreasonable results in that certain shippers lacked a reasonable opportunity to avoid imbalances, and the surcharge fluctuated widely, largely due to its carryforward provision. Because the Commission lacked adequate information to determine a just and reasonable replacement tariff mechanism, the Commission set the matter for hearing.

Shippers contend that, because ANR's 2001 surcharge filing was made under NGA § 4, the Commission was required to reject the proposed surcharge rates upon finding the underlying tariff mechanism unjust and unreasonable, or, alternatively, to order the surcharge subject to refund. As ANR's annual filing did not purport to change the underlying tariff calculation mechanism, the tariff mechanism could only be altered prospectively under NGA § 5. Consequently, ANR was entitled to recover rates in accordance with its approved tariff mechanism until the Commission has acted under § 5 to set the just and reasonable rate "to be thereafter observed."

Shippers alternatively contend that "reparations" can be awarded under NGA § 5 from the time the Commission determines that the existing tariff mechanism is unjust and unreasonable, even though no just and reasonable replacement mechanism has been determined. It is well settled, however, that reparations are not available under § 5 because a new just and reasonable rate determined under that section has prospective effect only. Consequently, the Commission properly denied Shippers' alternative claim for relief.

Fundamentally, Shippers nowhere dispute the basic proposition that ANR should be able to recover its legitimate costs of resolving imbalances on its system. ANR's annual surcharge filing here sought recovery of ANR's 2001 imbalance costs, which the Commission found had been prudently incurred and correctly calculated under ANR's approved tariff mechanism. Until such time as the Commission acts under NGA § 5 to set a new mechanism, ANR was entitled to rely on operation of its existing approved tariff mechanism to recover its costs. Shippers are seeking simply to avoid paying ANR for some or all of its actual costs of resolving imbalances in 2001. No basis exists for denying ANR recovery of those costs.

ARGUMENT

I. STANDARD OF REVIEW

The Court must uphold FERC's orders unless they are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." *Transcontinental Gas Pipe Line Corp. v. FERC*, 54 F.3d 893, 898 (D.C. Cir. 1995). Judicial scrutiny under the NGA is limited to assuring that the Commission's decisionmaking is reasoned, principled, and based upon the record. *Pennsylvania Office of Consumer Advocate v. FERC*, 131 F.3d 182, 185 (D.C. Cir. 1997). Pursuant to NGA 19(b), 15 U.S.C. 717r(b), the finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive.

II. THE COMMISSION ACTED PROPERLY TO REMEDY THE UNJUST AND UNREASONABLE OPERATION OF ANR'S TARIFF SURCHARGE CALCULATION MECHANISM.

ANR's tariff permits cost recovery of resolving imbalances on its system through an annual surcharge paid by shippers with imbalances. *See ANR Pipeline Co.*, 91 FERC at 61,687. On May 1, 2002, ANR filed its annual calculations of the surcharge to recover calendar year 2001 costs. Hearing Order ¶ 2, JA 47. The Commission rejected Shippers' challenges to the prices and volumes used to calculate the surcharge, and found that the surcharge was calculated consistent with the pre-approved tariff mechanism. *Id.* ¶ 17, JA 54. Accordingly, the Commission permitted the surcharge to go into effect. *Id.*

Nonetheless, the underlying tariff calculation mechanism appeared to be producing unjust and unreasonable results in that (1) the mechanism does not give PTR shippers an adequate opportunity to avoid the surcharge by resolving their imbalances through imbalance trading and (2) the mechanism has resulted in wide yearly swings in

the surcharge, largely because the carryforward mechanism is not related to the size of the imbalance and defers collection of significant costs without regard to how that will affect the costs to be recovered or the resulting surcharge level. *Id*. ¶¶ 19-20, JA 54-55. As there was insufficient evidence to devise a just and reasonable replacement mechanism under NGA § 5, the Commission set the matter for hearing. *Id.* ¶ 21, JA 55. Upon completion of the hearing, the Commission will set the just and reasonable tariff calculation mechanism "to be thereafter observed." NGA § 5.

Shippers contend that the finding that the underlying tariff calculation mechanism was unjust and unreasonable invalidates ANR's proposed 2001 imbalance cost recovery. Shippers alternatively assert that the proposed surcharge for 2001 costs can be rejected and refunds provided under NGA § 4, or that "reparations" can be made under NGA § 5 from the time that the tariff cashout mechanism was found unjust and unreasonable, notwithstanding the fact that a just and reasonable replacement rate mechanism has not been determined. Neither argument has merit.

A. Because The Tariff Surcharge Calculation Mechanism Had Been Previously Approved And ANR Did Not Propose to Change It, The Commission Lacked Authority To Alter The Mechanism Or To Order Refunds Under § 4.

Shippers argue ANR's NGA § 4 proposed surcharge to recover 2001 costs could be rejected or made subject to refund based upon the finding that ANR's underlying pre-approved tariff mechanism was unjust and unreasonable. *See* Br. at 8-11, 15-16. However, because ANR proposed only to set the 2001 cost recovery surcharge, and did not propose to modify the underlying tariff mechanism, NGA § 4 limits review to assuring

that the 2001 calculations conformed to the previously approved tariff mechanism. Rehearing Order ¶ 7, JA 67-68. To accomplish this, the Commission examined whether ANR's 2001 cashout program costs were prudently incurred and calculated consistently with the pre-approved tariff. Hearing Order ¶ ¶ 10, 17, JA 50-51, 54; Rehearing Order ¶ 7, JA 67-68.

Finding the costs prudently incurred and appropriately calculated, *id*., the Commission had no basis for rejecting the surcharge for 2001 costs. Although operation of the underlying pre-approved tariff mechanism appeared to result in unjust and unreasonable rates, ANR had not proposed to change that mechanism in its NGA § 4 submission. Accordingly, changes to the approved tariff mechanism itself could only be made in accordance with the strictures of NGA § 5. Rehearing Order ¶ 7, JA 67-68.

It is well settled that, even if a proceeding is initiated under § 4, the Commission must proceed under § 5 when it seeks to impose a rate change not proposed by a § 4 submission. "The Commission's authority under section 4(e) is limited to review of *increases proposed by the natural gas company*. When the Commission seeks to impose its *own* rate determinations – rather than to accept or reject a change proposed by the company – the Commission must act under section 5(a)." *ANR Pipeline Co. v. FERC*, 771 F.2d 507, 513 (D.C. Cir. 1985) (emphasis in original). *See also Western Resources, Inc. v. FERC*, 9 F.3d 1568, 1578 (D.C. Cir. 1993); *Sea Robin Pipeline Co. v. FERC*, 795 F.2d 182, 186-87 (D.C. Cir. 1986). NGA § 4 does not give the Commission "the authority to reject, post hoc, a previously accepted provision or to specify what should replace it." *Sea Robin*, 795 F.2d at 187.

ANR's NGA § 4 filing to set the annual surcharge under its preexisting approved tariff mechanism is analogous to limited NGA § 4 filings to recover specified costs under previously approved tariff flow-through mechanisms. In such circumstances, NGA § 4 limits review to compliance with the preexisting tariff provision; any changes to the tariff mechanism itself must occur under NGA § 5. For example, in *Northwest Pipeline Corp. v. FERC*, 61 F.3d 1479, 1482-84 (10th Cir. 1995), the pipeline's annual filing to recover fuel costs under a fuel reimbursement percentage rate ("FRP") provision had been incorrectly calculated, and so refunds were ordered. There, as here, "the 'rate' in question" in the § 4 filing was the pipeline's "annual adjustment" under an existing tariff mechanism. *Id.* at 1492. With regard to such a filing, the Commission could act under NGA § 4 to the extent it "simply directed that the fuel reimbursement percentage be calculated correctly in compliance with the tariff mechanism." *Id*. at 1490.

In contrast, effecting "a *change* in the mechanism by which the [fuel reimbursement percentage] was calculated" would require compliance with NGA § 5. *Id*. (emphasis in original). Thus, when the pipeline proposed annual changes to the FRP under § 4, *id*., the underlying "FRP calculational mechanism" in the tariff could only be modified under § 5, *id*. at 1493. As the Commission explained in another case:

> Hence, when a pipeline has an approved mechanism in its tariff for the flow-through of a particular type of cost and the pipeline makes a limited section 4 filing to recover newly incurred costs pursuant to that mechanism, the Commission's refund authority is very limited. Since the pipeline's limited section 4 filing would not propose to change the approved flowthrough mechanism, the Commission would have to proceed under section 5 to make any change in that mechanism. For example, if the Commission desired to modify the type of costs currently eligible for recovery under the flowthrough

> mechanism, it would have to proceed under section 5 and the revision to the flowthrough mechanism could only take effect prospectively. The only rate change initiated by the pipeline in such a limited section 4 filing is the inclusion in the approved flowthrough mechanism of newly incurred costs. The Commission could, therefore, order refunds of the resulting proposed rate increase, in the limited circumstance of a finding that the costs were not of the type authorized for recovery under the approved flowthrough mechanism or that the pipeline was imprudent in incurring the new costs.

Dakota Gasification Co., 77 FERC ¶ 61,271 at 62,146 (1996). *See, e.g., Sea Robin*, 795 F.2d at 186-87 (where Sea Robin proposed to increase its rates consistent with existing methodology, FERC could alter existing methodology only under §5). To obtain § 4 approval for proposed rates, pipelines must comply with their approved mechanisms in seeking recovery of prudently incurred costs, and the Commission may order refunds only to the extent they do not. *Dakota*, 77 FERC at 62,149. Once "the Commission moves beyond a finding of failure to comply with the approved recovery mechanism . . . the Commission must proceed under NGA section 5 and cannot order refunds." *Id*.

Although Shippers assert that their prudence challenges to the 2001 costs provide a basis for awarding refunds, *see* Br. at 15, the Commission rejected those challenges. *See* Hearing Order ¶¶ 15-17, JA 53-54. Following the technical conference, Shippers questioned: why ANR paid more for gas in some months than the applicable cashout price; why there were no cashout revenues associated with two imbalance accounts; and why there was an adjustment "zeroing out" a shipper's imbalance. *See* Hearing Order ¶ 15, JA 53. In response, ANR explained that: the price to purchase gas and the cashout price are determined by different methodologies and the amounts involved were relatively

small; the two imbalance accounts from which no revenue was recovered belong to a bankrupt shipper; and the "zeroed" balance corrected a prior erroneous allocation. Hearing Order ¶¶ 15-16, JA 53; Reply Comments of ANR Pipeline Co., filed September 9, 2002, R. 30 at 3, JA 41.

The Commission concluded that ANR's responses adequately answered Shippers' prudence concerns. Hearing Order ¶ 17, JA 54. "Following the technical conference, Indicated Shippers raised questions about a relatively small amount of the gas purchase prices and volumes used to determine the surcharge. The Commission finds that ANR's responses described above adequately address the issues raised by Indicated Shippers." *Id*. (referencing discussion at Hearing Order ¶¶ 15-16).

Shippers did not challenge the Commission's prudence determinations on rehearing. Rehearing Order ¶ 7, JA 67. *See* Request for Rehearing and Clarification of Indicated Shippers, R. 42, JA 57-64. Thus, Shippers cannot pursue those challenges on appeal. NGA § 19(b) ("No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable grounds for failure to do so.") [3] Accordingly, because Shippers' prudence challenges were rejected, and that rejection

[3] *See also City of Orrville, Ohio v. FERC*, 147 F.3d 979, 990 (D.C. Cir. 1998) (court lacks jurisdiction to hear arguments not made on rehearing); *Platte River Whooping Crane Critical Habitat Trust v. FERC*, 876 F.2d 109, 113 (D.C. Cir. 1989) (parties seeking review must themselves raise on rehearing all objections urged on appeal).

went unchallenged, the prudence challenges provide no basis to review whether the Commission could or should have allowed NGA § 4 refunds.

Review of ANR's annual filing under NGA § 4 was limited to prudence and tariff compliance questions. On both issues, the Commission found in favor of ANR's proposal. Hearing Order ¶ ¶ 10, 17, JA 50-51, 54; Rehearing Order ¶ 7, JA 67. Based on these findings, the Commission properly permitted the surcharge to go into effect. On the other hand, the underlying tariff calculation mechanism, which ANR had not proposed to change, could only be modified pursuant to NGA § 5. Rehearing Order ¶ 7, JA 67.

Shippers cite *KN Interstate Gas Transmission Co.*, 87 FERC ¶ 61,267 (1999), as support for the Commission's authority to reject a § 4 rate filing without designing a new rate under § 5. *See* Br. at 11-12. There, the pipeline proposed under NGA § 4 to change from non-rolled-in rates to rolled-in rates, which the Commission rejected because the pipeline failed to meet its § 4 burden to show the resulting rates would be just and reasonable. *Id*. at 62,086-87. The Commission had no need to determine a just and reasonable replacement rate design under NGA § 5 because the pipeline's existing non-rolled-in rate design had been previously approved and had not been found unjust and unreasonable. *Id*. at 62,087. In contrast, here, ANR did not propose to change the existing tariff surcharge mechanism under NGA § 4, and it was the existing tariff mechanism, not a proposed change, that the Commission found unjust and unreasonable. Thus, unlike *KNI*, the Commission here was compelled to act under § 5 to remedy the unjust and unreasonable rate. Similarly, *Northwest Pipeline Corp*., 96 FERC ¶ 61,128

and *El Paso Natural Gas Co*., 97 FERC ¶ 61,265, *see* Br. at 14, rejected tariff changes proposed by the pipeline under NGA § 4, *see* Rehearing Order ¶ 7, JA 67-68.

As there was no basis for rejecting ANR's surcharge to recover 2001 costs, *see* Hearing Order ¶ ¶ 10, 17, JA 50-51, 54; Rehearing Order ¶ 7, JA 67, the Commission did not reach Shippers' arguments that, assuming rejection, the Commission could have required ANR either to continue charging the $0.1508 surcharge applicable to 2000 costs or to submit a new tariff mechanism. *See* Br. at 13. On the latter point, requiring ANR to file a new tariff cashout mechanism would not transform the matter into one under § 4. *See, e.g., Sebring Utilities Commission v. FERC*, 591 F.2d 1003, 1016 (5th Cir. 1979) (requiring pipeline to file a revised plan would not create a § 4 proceeding since the pipeline could "persuasively [] claim that it had filed only under coercion from the Commission and [as] § 5 procedures had not been observed, the filings would be invalid.").

Further, the 2000 surcharge cannot be likened to a pre-existing just and reasonable rate that can provide a "fall-back" position. It was calculated under the same tariff mechanism as the proposed surcharge for 2001, and thus suffers from the same defects. Also, the 2000 surcharge was based on imbalance costs for 2000, calculated from actual volumes and weekly spot prices experienced in the four separate supply receipt areas on ANR's system. *See ANR Pipeline Co.*, 82 FERC at 61,295-96. The volumes and prices used to calculate 2000 costs bear no necessary relationship to the volumes and prices obtaining in 2001, and therefore continuation of the 2000 surcharge could not purport to

reimburse ANR for the costs of resolving imbalances in 2001. [4] No justification exists for continued use of the 2000 surcharge as a reasonable means to recover 2001 costs.

Accordingly, the tariff surcharge mechanism could be changed only pursuant to §5, not § 4, and Shippers' arguments premised upon § 4 must fail.

B. Because § 5 Provides Prospective Relief, No Refunds Or Interim Relief Was Available Pending Determination Of The Just and Reasonable Mechanism "To Be Thereafter Observed."

Shippers contend that the Commission could award "reparations" under § 5 for the time period between the date that the Commission found the tariff mechanism unjust and unreasonable and the date that the just and reasonable rate "to be thereafter observed" is set. *See* Br. at 15 (citing *Amoco Production Co. v. FERC,* 271 F.3d 1119, 1121 (D.C. Cir. 2001)). [5] This does not follow the statutory scheme: "[s]ince any modification in these rates, as a result of this proceeding, would occur pursuant to NGA Section 5, there can be

[4] In fact, ANR explained that the dramatic increase in the surcharge between the filings for year 2000 and 2001 was in significant measure attributable to the fact that ANR was required to purchase a high level of shipper excess quantities during the early part of 2001, when spot prices were very high, while most of the shipper deficient quantifies occurred during the latter part of the year when the applicable spot prices were much lower. *See* Hearing Order ¶ 3, JA 48.

[5] *Amoco* does not support this proposition. When the court stated that "the Commission can award § 5 reparations only prospectively from the date of finding that the rates are not just and reasonable," 271 F.3d at 1121, the court was making the point that, since the § 5 hearing could not be completed prior to the end of the locked-in period for the rates in question, a finding under § 5 that the locked-in rates were not just and reasonable would not lead to any recovery for the locked-in period. That ruling did not endorse Shippers' proposition that "reparations" can be awarded under § 5 for the period between a finding that the current rate is unjust and unreasonable, and the determination of the just and reasonable rate.

no refund." Rehearing Order ¶ 7, JA 67. It is well recognized that, in a § 5 proceeding, "the Commission has no power to make reparations orders," but its power to fix rates "is limited to those 'to be thereafter observed and in force.'" *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 618 (1944) (quoting NGA § 5(a)). *See also Western*, 9 F.3d at 1581; *Sea Robin*, 795 F.2d at 189 n.7. Because under § 5, "the rate found to be just and reasonable becomes effective prospectively only," gas purchasers "have no protection from excessive charges collected during the pendency of a § 5 proceeding." *Atlantic Refining Co. v. Public Service Commission*, 360 U.S. 378, 389 (1959). *See, e.g., FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 643-44 (1972) (under § 5 the Commission must "afford interested parties a full hearing on the reasonableness of the tariff before taking any remedial action," and "a prescribed remedial order can only have prospective application."). The Commission accordingly cannot apply later-determined just and reasonable rates retroactive to the interim period after it found that the existing rates were unjust and unreasonable. *See Electrical District No. 1 v. FERC*, 774 F.2d 490, 492-93 (D.C. Cir. 1985) (Scalia, J.) (interpreting analogous provision, § 206, of the Federal Power Act).

Thus, the Commission correctly concluded that "ANR is entitled to continue recovering the rates provided for in its approved tariff until the Commission acts under NGA Section 5 to fix the just and reasonable rate 'to be thereafter observed.'" Rehearing Order ¶ 7, JA 67 (quoting § 5). Until such time as the Commission can determine a just and reasonable rate "to be thereafter observed," the statute provides no basis for refunds or reparations.

Because § 4(a) states that any rate or charge "that is not just and reasonable is hereby declared illegal," Shippers contend that the Commission was required to take immediate remedial action as soon as it found ANR's tariff mechanism unjust and unreasonable. *See* Br. at 9-10, 12. The Commission rejected that contention because it lacked sufficient information on which to determine a remedy without further hearing. "While the Commission believes that ANR's cashout mechanism is producing unjust and unreasonable results, we do not yet have sufficient information to determine a just and reasonable replacement cashout mechanism. Nor does Indicated Shippers on rehearing suggest we should at this time determine the just and reasonable cashout mechanism. In these circumstances, ANR must be permitted to implement the rates provided for in its existing tariff." Rehearing Order ¶ 7, JA 67.

In *Electrical District*, this Court rejected the contention that an immediate remedy is required upon finding a rate unjust and unreasonable:

> FERC argues that because § 205 (a) of the Federal Power Act provides that: "[a]ll rates and charges. . . shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful," 16 U.S.C. § 824d(a), it follows that a new rate must go into effect as of the date that FERC finds an existing rate to be unjust or unreasonable, because it would be unlawful to allow the unjust or unreasonable rate to continue in effect. It seems to us, however, no more inevitable that the Commission has the obligation to end an unlawful rate from the moment it finds unlawfulness than that an unlawful rate must be regarded as null and void from the moment it becomes unlawful. (A customer cannot, of course, refuse to pay a rate currently in effect on the ground that it has become unlawfully high and therefore void; nor, after payment of such a rate, can the Commission order a refund. [Citations omitted]). Or to use a more remote analogy, it is not the case that once a court has concluded that a particular action challenged before it is unlawful it must immediately issue an injunction, instead of taking time for further deliberations necessary to determine what the precise terms of that injunction should be. The moment

> of required and authorized Commission action in the present case is to be determined not on the basis of an abstract principle such as "once unlawfulness is known agency action must be taken," but rather on the basis of the procedures that the statutes established for adjusting unlawful rates. And those procedures are not at all ambiguous: "Whenever the Commission . . . shall find that any rate . . . collected by any public utility . . . is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate . . . *to be thereafter observed and in force, and shall fix the same by order.*" 16 U.S.C. § 824e(a) (emphasis added).

774 F.2d at 492.

Here, the Commission reasonably declined to impose an immediate remedy because it required further evidence to determine a just and reasonable replacement rate. In *Sebring*, 591 F.2d at 1014, the Court rejected the contention that, upon finding a pipeline's curtailment plan unduly discriminatory under § 5, the Commission was compelled to implement a substitute plan immediately. Rather, because doubt existed concerning the proper plan to employ, the Commission acted reasonably in leaving the discriminatory curtailment plan in place while it obtained sufficient record evidence to devise a new curtailment plan. *Id*. at 1013.

Contrary to Shippers' claim, *see* Br. at 12-14, the Commission's authority to issue interim rate orders does not require immediate relief here. *Sebring*, 591 F.2d at 1013 (discussing *Consolidated Edison Co. v. FPC*, 511 F.2d 372 (D.C. Cir. 1974)). As illustrated by *FPC v. Tennessee Gas Transmission Co*., 371 U.S. 145 (1962) (relied on by Shippers, *see* Br. at 12-13), the Commission may reasonably impose interim relief after it has determined a just and reasonable result for a particular rate issue, even if other rate issues are still being litigated. *See id*. at 146-47 (after rejecting a proposed 7% return on

equity and setting a 6 1/8% return, the pipeline was required to reduce rates for that differential, even though the rate case was not fully resolved). *Id*. The interim relief in *Tennessee* was imposed only after a full hearing, which allowed the Commission to determine the just and reasonable return. Refunds under NGA § 4 were appropriate because the pipeline sought to change its equity return. [6]

Here, in contrast, ANR did not propose to change the surcharge mechanism in its NGA § 4 filing. Further, the record lacked sufficient evidence to determine what a just and reasonable mechanism should be, necessitating further hearing. Thus, the Commission properly exercised its discretion not to grant interim relief in light of the insufficient evidence. *See, e.g., Sebring*, 591 F.2d at 1013-14 (Commission reasonably left unduly discriminatory curtailment plan in place pending hearings where the Commission lacked sufficient evidence to develop a new curtailment plan).

At bottom, it is critical to focus on what is at stake here. Shippers nowhere dispute the basic proposition that ANR is entitled to recover its legitimate costs of resolving imbalances. The Commission's concerns about the tariff mechanism do not draw into question the legitimacy of ANR's 2001 imbalance costs, but rather look to managing imbalance costs better in the future by improving the ability of shippers to avoid

[6] Similarly, *Tennessee Gas Pipeline Co*., 71 FERC ¶ 61,399 at 62,584 (1995), *see* Br. at 12 and n. 20, set differing suspension periods for various aspects of a pipeline's rate proposal. Again, the Commission could provide interim relief because the pipeline had itself proposed changes in all aspects that were suspended. *Id*. at 62,585.

imbalances and addressing the wide swings in the surcharge caused by the carryforward provision.

As the annual surcharge at issue recovered ANR's actual 2001 imbalance costs, which were found prudent and correctly calculated under ANR's approved tariff mechanism, rejecting that surcharge would, contrary to Shippers' assertion, Br. at 13, "deprive ANR of the ability to recover cashout costs." ANR was entitled to rely on operation of its approved tariff provision to recover its costs. *See, e.g.*, *Sea Robin*, 795 F.2d 182, 184 (limitation of § 5 authority to prospective relief allows the pipeline to rely on approved rate until a new rate is set); *Northwest*, 61 F.3d at 1489 ("While § 4's refund provision protects customers from a rate that is unreasonably high when filed (examined as of the filing), § 5's requirement that relief be prospective only assures the utility that rates passing scrutiny under § 4 will not be undone.") (quoting *Associated Gas Distribs. v. FERC*, 898 F.2d 809, 810 (D.C. Cir. 1990) (Williams, J.) (concurring in denial of rehearing and rehearing *en banc*)). Shippers are seeking simply to avoid paying ANR for some or all of its actual costs of resolving imbalances in 2001. No basis exists for denying ANR recovery of those costs.

CONCLUSION

For the reasons stated, the Commission's orders should be affirmed in all respects.

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ChevronTexaco Exploration and Production Co. v. FERC,
D.C. Cir. No. 03-1153

CERTIFICATE OF COMPLIANCE

In accordance with Circuit Rule 28(d)(1), I hereby certify that this brief contains 6276 words, not including the tables of contents and authorities, the certificate of counsel, this certificate and the addendum.

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