ORAL ARGUMENT HAS NOT BEEN SCHEDULED

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

Nos. 05-1299, 05-1300, & 05-1301
(consolidated)

EXXON MOBIL CORPORATION, *ET AL*.
PETITIONERS,
v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.

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

BRIEF FOR RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

JOHN S. MOOT
GENERAL COUNSEL

ROBERT H. SOLOMON
SOLICITOR

JUDITH A. ALBERT
SENIOR ATTORNEY

FOR RESPONDENT
FEDERAL ENERGY REGULATORY
COMMISSION
WASHINGTON, D.C. 20426

AUGUST 4, 2006
FINAL BRIEF: SEPTEMBER 26, 2006

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CIRCUIT RULE 28(a)(1) CERTIFICATE

A. Parties

The parties are as stated in the Petitioners' brief.

B. Rulings Under Review:

The rulings under review are as follows:

1. *Regulations Governing the Conduct of Open Seasons for Alaska Natural Gas Transportation Projects*, "Order No. 2005," FERC Stats. & Regs., Regs. Preambles ¶ 31,174 (February 9, 2005), and 70 Fed. Reg. 8,269 (February 18, 2005); and

2. *Regulations Governing the Conduct of Open Seasons for Alaska Natural Gas Transportation Projects*, "Order No. 2005-A," FERC Stats. & Regs., Regs. Preambles ¶ 31,187 (June 16, 2005), and 70 Fed. Reg. 35,011 (June 16, 2005).

C. Related Cases:

Counsel is aware of no other related cases pending in this or any other court. On April 8, 2005, petitions for review of Order No. 2005 were filed in this Court. *ChevronTexaco Natural Gas v. FERC*, No. 05-1111 (D.C. Cir. April 8, 2005) (consolidated with 05-1113, 05-1114, and 05-1115). On November 1, 2005, the Court dismissed the consolidated actions as premature because of a pending administrative rehearing request. The rehearing request was later resolved by issuance of Order No. 2005-A.

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Judith A. Albert
Senior Attorney

September 26, 2006

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GLOSSARY

1976 Act	Alaska Natural Gas Transportation Act of 1976
Bcf	Billion cubic feet
Commission	Federal Energy Regulatory Commission
FERC	Federal Energy Regulatory Commission
NGA	Natural Gas Act
North Slope Producers or Petitioners	Petitioners Exxon Mobil Corporation, et al.
Pipeline Act	Alaska Natural Gas Pipeline Act, 15 U.S.C. § 720a et seq.
Tcf	Trillion cubic feet

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STATEMENT OF THE ISSUES

1. Whether the Federal Energy Regulatory Commission ("Commission" or "FERC"), when reviewing an application for a certificate to construct an Alaska natural gas transportation project, has authority to require, as a condition of the certificate, design changes that advance the Alaska Natural Gas Pipeline Act ("Pipeline Act") objectives of providing access to alternative supplies of natural gas.

2. Assuming that the Commission has such statutory authority, whether the regulations it issued pursuant to this authority were reasonable.

STATUTES AND REGULATIONS

The applicable 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

The orders under review are *Regulations Governing the Conduct of Open Seasons for Alaska Natural Gas Transportation Projects*, FERC Stats. & Regs., Regs. Preambles ¶ 31,174 (Feb. 9, 2005); 70 Fed. Reg. 8,269 (February 18, 2005) ("Order No. 2005") (R 52, JA 1);[1] and *Regulations Governing the Conduct of Open Seasons for Alaska Natural Gas Transportation Projects*, FERC Stats. & Regs., Regs. Preambles ¶ 31,187 (June 1, 2005); 70 Fed. Reg. 35,011 (June 16, 2005) ("Order No. 2005-A") (R 69, JA 60). The orders issued pursuant to the Pipeline Act,[2] codified at 15 U.S.C. §§ 720-720n, which directed the Commission to issue regulations governing the conduct of open seasons for Alaska natural gas transportation projects, including procedures for allocation of capacity. The

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[1] "R" refers to a record item. "JA" refers to the Joint Appendix page number. "P" refers to the internal paragraph number within a FERC order.

[2] P.L. 108-324, 118 Stat. 1220 (2004).

regulations, codified at 18 C.F.R. §§ 157.30-157.39, sought to balance the Pipeline Act's dual objectives: (1) facilitating the timely development of an Alaska natural gas transportation project; and (2) encouraging the exploration for new gas reserves by assuring competitive access to the pipeline.

On appeal, Petitioners (consisting entirely of North Slope Producers) challenge only a small portion of the Commission's Alaska natural gas transportation regulations. Specifically, Petitioners challenge regulations adopted at 18 C.F.R. §§ 157.36 and 157.37, announcing that the Commission would condition its granting of a pipeline certificate by requiring project design changes if necessary to advance the Pipeline Act competition and access goals.

II. Statement of Facts

A. Regulatory Background

Section 1(b) of the Natural Gas Act ("NGA"), 15 U.S.C. § 717(b), confers upon the Commission comprehensive regulatory authority over the transportation and sale for resale of natural gas in interstate commerce. NGA § 7(c)(1)(A) prohibits any "natural-gas company or person" from constructing or operating pipeline facilities prior to obtaining a "certificate of public convenience and necessity" from FERC. 15 U.S.C. § 717f(c)(1)(A). NGA § 7(e) mandates the issuance of such certificates to qualified applicants once the Commission determines that the proposed service "is or will be required by the present or future

public convenience or necessity[.]" 15 U.S.C. § 717f(e). NGA § 7(e) further authorizes FERC to attach to certificates "such reasonable terms and conditions as the public convenience and necessity may require." *Id*. NGA § 7(a) permits the Commission to order the extension or improvement, but not the enlargement, of existing pipeline facilities under certain conditions. 15 U.S.C. § 717f(a).

In 1976, Congress enacted the Alaska Natural Gas Transportation Act ("1976 Act"), 15 U.S.C. §§ 719 – 719o, to encourage "the expeditious construction of a viable natural gas transportation system for delivery of Alaska natural gas to United States markets" by transferring the project selection process to the President, with Congressional concurrence. *See* 15 U.S.C. § 719, 719a. Although a project has been approved under this statute, and efforts to move the project forward are ongoing, so far no pipeline has been constructed.[3]

On October 13, 2004, Congress, in light of increasing North American demand for natural gas, enacted the Pipeline Act. Pipeline Act § 114(1), 15 U.S.C. § 720*l*. It encourages construction by offering loan guarantees up to $18,000,000,000 for pipeline projects proceeding under either statute, mandates

[3] *See* the Commission's February 1, 2006 Report to Congress on Progress Made in Licensing and Constructing the Alaska Natural Gas Pipeline at pp. 2-4 (published on the FERC web site at http://www.ferc.gov/legal/staff-reports/alaska-report.pdf). The Commission's recent July 10, 2006 Report to Congress (http://www.ferc.gov/legal/staff-reports/angta-second.pdf) provides a comprehensive update of Alaska transportation developments.

expedited processing by the Commission of certificate applications for Alaska natural gas transportation projects,[4] and directed the Commission, within 120 days of enactment, to issue regulations governing the conduct of "open seasons" for proposals to construct such projects (including procedures for the allocation of capacity).[5] Pipeline Act §§ 116, 103(c) and (e)(1), 15 U.S.C. §§ 720n, 720a(c) and (e)(1). The Pipeline Act also specifies that the regulations governing Alaska open seasons must "include the criteria for and timing of any open seasons," "promote competition in the exploration, development, and production of Alaska natural gas" and, "for any open season for capacity exceeding the initial capacity, provide the opportunity for the transportation of natural gas other than from the Prudhoe Bay and Point Thomason units." Pipeline Act § 103(e)(2), 15 U.S.C. § 720a(e)(2).

B. The Notice of Proposed Rulemaking

The Commission received comments from several parties even before the notice of proposed rulemaking issued. *Regulations Governing the Conduct of*

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[4] More specifically, the Act requires expedited processing of any natural gas pipeline that carries natural gas derived from that portion of Alaska lying north of 64 degrees north latitude to the border between Alaska and Canada.

[5] An open season is a process through which potential shippers on a proposed pipeline may obtain firm capacity rights on a non-discriminatory basis and pipeline sponsors can ensure that proposed projects are sized properly for the quantity of gas available for shipment. *See Midcoast Interstate Transmision, Inc. v. FERC*, 198 F.3d 960, 966 (D.C. Cir. 2000).

Open Seasons for Alaska Natural Gas Transportation Projects, "Notice of Proposed Rulemaking," FERC Stats. and Regs. ¶ 32,577 (Nov. 15, 2004); 69 Fed. Reg. 68,106 (Nov. 23, 2004) ("Notice") (R 6, JA 110). These parties included Petitioners BP Exploration (Alaska) Inc., ConocoPhilips Company, and Exxon Mobil Corporation (collectively, "Petitioners" or "North Slope Producers"); other gas producers; potential project sponsors; and members of the Alaska legislature. Order No. 2005 at P 6 (JA 4). The Notice issued on November 15, 2004.

Proposed § 157.34 set the criteria and timing for any open season for an Alaska natural gas transportation project. Proposed § 157.34(a) provided for public notice of an open season of at least 30 days prior to commencement of the open season, proposed § 157.34(b) detailed the information that any notice of an open season must contain, and proposed § 157.34(c) provided that an open season must remain open for a period of at least 90 days. Proposed § 157.35 required that capacity allocated as a result of any open season be awarded without undue discrimination or preference. Proposed § 157.36, one of the regulations at issue here, provided that:

> Any open season for capacity exceeding the initial capacity of an Alaska natural gas transportation project must provide the opportunity for the transportation of gas other than Prudhoe Bay or Point Thomson production.

The proposed regulations did not include § 157.37, the other regulation now challenged.

In addition to seeking comments on the proposed rules, the Commission also sought comments on, *inter alia*, whether existing Commission policies regarding open seasons accorded with the Congressional mandate to promote natural gas exploration in Alaska:

> Congress has made expressly clear that the open season rules must promote competition in the exploration, development, and production of Alaska natural gas. Commenters are invited to discuss whether, and to what extent, any tension may exist between this mandated purpose and the application of existing Commission policies to the open season rules due to circumstances unique to access to capacity on any Alaska natural gas transportation project.

Notice at P 15, part (4) (JA 117).

On December 3, 2004, FERC held a public technical conference in Anchorage, Alaska and the transcript of the conference was incorporated into the record. About 25 parties subsequently submitted comments in response to the Notice. *Id*. at PP 5-6 (JA 3-4).

C. The Comments

Several commenters, including Petitioners, supported the proposed regulations as providing the flexibility needed to help a project sponsor to properly size the pipeline and satisfy the demands of financers. Order No. 2005 at P 7 (JA 4-5). Others, however, expressed "concern that the North Slope Producers, either as project sponsors or as producers whose reserves will support the initial development of the project, will use that flexibility to develop open season rules to

accommodate their own interests, to the exclusion and detriment of other explorers, developers and producers of Alaska natural gas. . . ." *Id*. at P 8 (JA 5).

These commenters emphasized that approximately 35 trillion cubic feet ("Tcf") of proven gas reserves exist within 100 miles of the existing Trans Alaska oil pipeline corridor, 32 Tcf of it within the Prudhoe Bay and Point Thomson units.[6] These gas fields alone could support a 4.3 billion cubic feet ("Bcf")/day pipeline throughput for 15-20 years.[7] Petitioners own 90 to 95 percent of these proven reserves,[8] are likely sponsors of the pipeline, and could fill the pipeline with their own reserves possibly for as long as 15 years.[9]

The proven reserves, however, are only the tip of the iceberg. It has been estimated that 250 Tcf of gas reserves may be recoverable by conventional means from the North Slope and offshore.[10] North Slope gas hydrate potential exceeds

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[6] State of Alaska comments at 1-2 (R 36, JA 294-95); Calpine Corporation comments at 2 (R 35, JA 290A); United States Department of the Interior comments at 1-2 (R 29, JA 211-11A); Doyon, Limited comments at 4 (R 41, JA 517D). Doyon, one of the thirteen Native regional corporations established by Congress, is the largest private landowner in Alaska. Doyon comments at 1 (JA 517A).

[7] State of Alaska comments at 2 (JA 295).

[8] Anadarko Petroleum Corporation comments at 5 (R 37, JA 336); State of Alaska comments at 22 (stating three companies control 98 percent of the gas reserves at Prudhoe and 82 percent of the reserves at Point Thomson) (JA 315).

[9] State of Alaska comments at 11 (JA 304).

[10] Calpine Corporation comments at 2, citing United States Geological Survey estimates (JA 290A); State of Alaska comments at 2 (JA 295); United

100 Tcf, and Alaska's interior basins, now mostly unexplored, may also have significant reserves.[11] Exploration of these reserves is largely in the hands of companies other than Petitioners, and two of the Petitioners have publicly stated that they are not interested in exploring for additional Alaska gas reserves at this time.[12] The commenters contended further that unless the Commission's regulations provide assurance to companies of pipeline access, the exploration and competition that Congress intended to encourage will not occur.[13]

D. Order No. 2005

In response to the unique competitive conditions in Alaska, the Pipeline Act mandate to promote competition, and the concerns expressed in the comments, FERC revised proposed § 157.36 and added § 157.37, to "make clear that the Commission will examine proposed pipeline designs, as well as expansion proposals, to ensure that all interested shippers are given a fair opportunity to obtain capacity both on an initial project and on any voluntary expansion." Order No. 2005 at P 102 (JA 37). FERC reiterated that:

States Department of the Interior comments at 1 (JA 211); Anadarko Petroleum Corporation comments at 4-5 (JA 335-36).

[11] *Id*.

[12] United States Department of the Interior comments at 6 (JA 213).

[13] United States Department of Interior comments at 8 (JA 214A); State of Alaska comments at 10-11 (JA 303-04); Anadarko Petroleum Corporation comments at 9-11 (JA 340-42); Doyon Limited comments at 10 (JA 517F); Shell Exploration and Production Company comments at 2 (R 40, JA 512).

> [I]t is in both the sponsor's and shippers' best interests to build the pipeline to accommodate all qualified shippers who are ready to sign firm agreements. We will carefully review project design and . . . allocation of capacity, with the goal of promoting our open access and pro-competition policies.

Order No. 2005 at P 102 (JA 37).

Revised § 157.36, 18 C.F.R. § 157.36, announces that in considering a proposed voluntary expansion of an Alaska pipeline, the Commission may require design changes to meet the Pipeline Act objectives:

> § 157.36 Open seasons for expansions.
>
> Any open season for capacity exceeding the initial capacity of an Alaska natural gas transportation project must provide the opportunity for the transportation of gas other than Prudhoe Bay or Point Thomson production. In considering a proposed voluntary expansion of an Alaska natural gas pipeline project, the Commission will consider the extent to which the expansion will be utilized by shippers other than those who are the initial shippers on the project and, in order to promote competition and open access to the project, may require design changes to ensure that some portion of the expansion capacity be allocated to new shippers willing to sign long-term firm transportation contracts, including shippers seeking to transport natural gas from areas other than Prudhoe Bay and Point Thomson.

New § 157.37, 18 C.F.R. § 157.37, sets forth similar considerations for proposed projects:

> § 157.37 Project design.
>
> In reviewing any application for an Alaska natural gas pipeline project, the Commission will consider the extent to which a proposed project has been designed to accommodate the needs of shippers who have made conforming bids during an open season, as well as the extent to which the project can accommodate low-cost expansion, and may require changes in project design necessary to promote

> competition and offer a reasonable opportunity for access to the project.

E. Order No. 2005-A.

Several issues were raised on rehearing by various parties. As relevant here, the North Slope Producers objected to §§ 157.36 and 157.37 to the extent they announced the Commission might require design changes in proposed Alaska natural gas transportation projects. Order No. 2005-A at P 16 (JA 68). The Commission rejected the North Slope Producers' arguments that design changes would constitute an unlawful or unreasonable mandatory expansion requirement, and denied rehearing. *Id*. at PP 31-36 (JA 74-77).

This appeal followed.

SUMMARY OF ARGUMENT

A design change that might be required under either § 157.36 or 157.37 would not constitute an unlawful mandatory expansion of the project. Design changes can include changes in such things as routing, cost allocations, and the design of initial rates, and are routinely required by FERC to allow a finding that a proposed project satisfies the public convenience or necessity requirement.

NGA § 7(a) bars FERC from mandating enlargement of facilities already subject to existing certificates on which the pipeline company has relied in expending resources on construction. In contrast, §§ 157.36 and 157.37 pertain to proposed projects, and the purpose of any design changes that might be imposed

would be to support the finding of public convenience or necessity required for a certificate to issue. If the applicant does not want to change its proposed project design, it is not required to accept the certificate.

Regulations allowing for design changes are entirely consistent with the Pipeline Act, which explicitly references the Commission's existing certificate authority under NGA §§ 7(c) and 7(e) . In particular, NGA § 7(e) obliges FERC to consider all factors bearing on the public interest, and, if necessary, to attach conditions to the certificates it issues. The Pipeline Act's mandate to promote competition and provide the opportunity for the transportation of natural gas from regions other than Prudhoe Bay and Point Thomson are clearly such factors.

The North Slope Producers' claim that the regulations are unreasonable lacks merit. The unusual competitive conditions in Alaska, the fact that only one pipeline likely will be built, and the Pipeline Act mandate to promote exploration and development of gas reserves fully support the reasonableness of the regulations. Moreover, contrary to Petitioners' arguments, the regulations do not mandate a pipeline sized to serve all potential shippers, regardless of efficiency or other business considerations.

ARGUMENT

I. The Commission Has Authority To Require Design Changes As A Condition For Issuance Of A Certificate Of Public Convenience And Necessity For An Alaska Natural Gas Transportation Project.

A. Standard of Review.

Where a court is called upon to review an agency's construction of the statute it administers, well-settled principles apply. If Congress has directly spoken to the precise question at issue, "that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." *Chevron U.S.A., Inc. v. Natural Resources Defense Council*, 467 U.S.C. 837, 842-43 (1984). *See also*, *e.g.*, *Whitman v. American Trucking Assn's*, 531 U.S. 457, 481 (2001). If the statute is silent or ambiguous as to the question at issue, then the Court "must defer to a reasonable interpretation made by the . . . agency." *Whitman*, 531 U.S. at 481; *Chevron*, 467 U.S. at 843.

B. The Commission Has Jurisdiction under the NGA and the Pipeline Act to Impose Conditions to Support a Finding of Public Convenience and Necessity.

Petitioners argue throughout their brief that the Commission lacks jurisdiction to require a "mandatory expansion" of a proposed pipeline. The regulations, however, describe the conditions that may be imposed as "design changes." Design changes, as FERC explained, are routinely imposed to support a public convenience and necessity finding. Order No. 2005-A at P 33 (JA 75)

(stating that "Sections 157.36 and 157.37 merely codify our existing authority and practice").

In the past, design changes have involved such things as routing, cost allocations, and the design of initial service rates. *See* Order No. 2005-A at PP 31, 33 (JA 74, 75) citing *Transcontinental Gas Pipe Line Corp. v. FERC*, 589 F.2d 186, 191 (5th Cir. 1979) (FERC has responsibility to consider whether a proposed pipeline is either inadequate or oversized); *Vector Pipeline, L.P.*, 87 FERC ¶ 61,225 at 61,892-93 (1999) (discussing possible route and design changes to satisfy environmental requirements); *NE Hub Partners, L.P.*, 83 FERC ¶ 61,043 at 61,170-71 (1998) (construction of underground gas storage facilities extensively conditioned to prevent injection of salt brine into ground water); and *Maritimes & Northeast Pipelines, L.L.C.*, 80 FERC ¶ 61,345 at 62,146 (1997) (addressing rate design changes for proposed pipeline project).[14]

As the challenged orders demonstrate, *see* Order No. 2005-A at PP 32-33 (JA 74-75), the Commission has authority to impose design changes as certificate

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[14] *See also Fuel Safe Washington v. FERC*, 389 F.3d 1313, 1324 (10th Cir. 2004) (discussing FERC consideration of various route and system alternatives to a proposed natural gas pipeline); *Georgia Strait Crossing Pipeline LP*, 102 FERC ¶ 61,051 at P 12 (2003) (denying request that Commission order proposed gas pipeline project to replace gas-fueled generators with electric-driven unit at compressor station); *Northwest Pipeline Company*, 56 FERC ¶ 61,006 at 61,043 (1991) (ordering project downsized because of insufficient downstream capacity commitments to assure the continued flow of gas).

conditions for an Alaska natural gas pipeline. The Pipeline Act directs the Commission, "in accordance with section [7(c)] of the Natural Gas Act," 15 U.S.C. § 717f(c), to "consider and act on an application for the issuance of a certificate of public convenience and necessity authorizing the construction and operation of an Alaska natural gas transportation project. . . ." Pipeline Act § 103(a), 15 U.S.C. § 720a(a). The Pipeline Act continues that the Commission "shall issue a certificate of public convenience and necessity authorizing the construction and operation of an Alaska natural gas transportation project" only if "the applicant has satisfied the requirements of section 7(e) of the Natural Gas Act (15 U.S.C. § 717f(e))." Pipeline Act § 103(b)(1), 15 U.S.C. § 720a(b)(1).

NGA § 7(c) requires, generally, a certificate of public convenience and necessity before a natural gas company can construct pipeline facilities or engage in the transportation of natural gas. 15 U.S.C. § 717f(c). *See B&J Oil and Gas v. FERC*, 353 F.3d 71, 73 (D.C. Cir. 2004). NGA § 7(e) provides, with greater specificity, that the Commission cannot provide such a certificate unless it finds that the applicant "is able and willing" to perform the certificated services in a manner consistent with the statute and the Commission's implementing regulations. 15 U.S.C. § 717f(e). NGA § 7(e) requires FERC "to evaluate *all* factors bearing on the public interest." *FPC v. Transcontinental Gas Pipe Line Corp*., 365 U.S. 1, 7-8 (1961) (emphasis in original) (citation omitted). FERC

"certainly has the right to consider a congressional expression of fundamental national policy as bearing upon the question whether a particular certificate is required by the public convenience and necessity." Order No. 2005-A at P 32 (JA 75), quoting *City of Pittsburgh v. FPC*, 237 F.2d 741, 754 (D.C. Cir. 1965) (finding that Commission must consider antitrust implications of the particular pipeline certification at issue).

Moreover, under NGA § 7(e), the Commission has broad conditioning authority to support findings of public convenience and necessity: "The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require." 15 U.S.C. § 717f(e). *See FPC v. Hunt*, 376 U.S. 515, 525-527 (1964) (Commission was clearly given the power to lay down conditions precedent to entry); *Tennessee Gas Pipeline Co. v. FERC*, 689 F.2d 212, 214 (D.C. Cir. 1982), citing *Transcontinental Gas Pipe Line Corp. v. FERC*, 589 F.2d at 190-91 (reiterating "the well established principle that generally the Commission has extremely broad authority to condition certificates of public convenience and necessity").

The scope of this broad authority is defined by the purposes for which the statutes at issue were adopted. *See NAACP v. FPC*, 425 U.S. 662, 669 (1976). The principal purpose of the NGA "was to encourage the orderly development of

plentiful supplies of . . . natural gas at reasonable prices." *Id*. at 669-70;[15] *Public Utilities Comm'n of California v. FERC*, 900 F.2d 269, 281 (D.C. Cir. 1990) (same). More on point, Pipeline Act § 103(e)(2) requires regulations that "promote competition in the exploration, development, and production of Alaska natural gas," and, "for any open season for capacity exceeding the initial capacity, provide the opportunity for the transportation of natural gas other than from the Prudhoe Bay and Point Thomson units." 15 U.S.C. § 720a(e)(2)(B)-(C). The Commission has not only the authority, but the obligation to consider these factors in determining whether an application satisfies the public convenience and necessity. *FPC v. Transcontinental Gas Pipe Line Corp*., 365 U.S. at 7-8.

As the regulations here respond directly to statutory mandates, the Commission acted within its jurisdiction in promulgating them. *See*, 18 C.F.R. § 157.36 (an open season for a pipeline expansion "must provide the opportunity for the transportation of gas other than Prudhoe Bay or Point Thomson production," and in order to promote competition and open access to the project, the Commission "may require design changes to ensure that some portion of the expansion capacity be allocated to new shippers . . ."); 18 C.F.R. § 157.37 (the Commission will consider the needs of shippers and the extent to which the project

[15] Quoting, *inter alia*, *FPC v. Hope Gas Co*., 320 U.S. 591, 610 (1944) (The "primary aim" of the NGA is "to protect consumers against exploitation at the hands of natural gas companies").

can accommodate low-cost expansions, and may require design changes "to promote competition and offer a reasonable opportunity for access to the project").

C. A Design Change Required Pursuant to § 157.36 or 157.37 Would Not Constitute a Mandatory Expansion of the Project.

Petitioners, characterizing design changes as "mandatory expansions," contend that NGA § 7(e) does not authorize FERC to impose them. Pet. Br. at 20-21. Petitioners rely on NGA § 7(a) to support this contention. NGA § 7(a) states that the Commission "may by order direct a natural gas company to extend or improve its transportation facilities," provided that "the Commission shall have no authority to compel the enlargement of transportation facilities for such purposes . . . ." 15 U.S.C. § 717f(a).

FERC considered this argument in Order No. 2005-A, and found that a design change that might be required under either § 157.36 or § 157.37 would not constitute a mandatory expansion barred by NGA § 7(a). As Order No. 2005-A explains:

> First, in every case in which the Section 7(a) limitation has been addressed, the facilities involved were existing facilities subject to existing certificate authorization. The reasoning behind this limitation is clear. Once a natural gas company accepts a certificate and in reliance thereof expends resources to construct the facilities authorized therein, the pipeline and its customers should have the right to rely on the authorization contained in that certificate. It is quite another thing where the Commission tells a certificate applicant that unless it agrees to certain changes (including cost allocations and the design of initial service rates), its proposal will not be found in the public convenience and necessity. In such a case, if the applicant does

> not want to change its proposed project design, it is not required to accept the certificate.

Order No. 2005-A at P 31 (JA 74).

The Commission's construction of NGA § 7 is reasonable. NGA § 7(a) authorizes FERC, on its own initiative, to order a natural gas company to improve existing, certificated facilities, but bars FERC from ordering the company to enlarge them. Under NGA § 7(e), a natural gas company voluntarily proposes a project, but the Commission is obligated to consider whether the proposal is in the public interest and if it is not, to deny the application. As an alternative to denying an application, FERC may attach conditions that would bring the application into conformity with the public interest. The applicant, however, remains free to decline the certificate and the construction of the pipeline facilities.

The Pipeline Act, as explained above, explicitly references the Commission's authority under NGA § 7(e), including its authority to condition any certificate of public convenience and necessity it issues, but it does not reference NGA § 7(a). Instead, the Pipeline Act refers to pipeline expansion in § 105(a), 15 U.S.C. § 720c(a), which provides that "the Commission may order the expansion of the Alaska natural gas project" only under certain conditions enumerated in § 105(b), 15 U.S.C. § 720c(b).

There is no reason to presume, as do Petitioners (*see* Pet. Br. 20-21), that the Commission's limited expansion authority applies at the time of an initial application for a certificate of public convenience and necessity. In contrast to Pipeline Act § 103(a), which instructs the Commission to consider and act upon "an application for the issuance of a certificate," 15 U.S.C. § 720a(a), Pipeline Act § 105(a) instructs the Commission to act "on a request by 1 or more persons and after giving notice and an opportunity for a hearing." 15 U.S.C. § 720c(a). It is, at the very least, reasonable for the Commission to interpret this latter authority, using language that contemplates complaint-like proceedings, as applying only to situations in which a complainant is challenging the limited scope of an already-certificated project. *See* Order No. 2005-A at P 31 (JA 74) (finding that "the statutory requirements of [Pipeline Act] Section 105 have no application" to voluntary applications for certificates of public convenience and necessity).

D. Petitioners' Arguments Otherwise Are Not Persuasive.

Petitioners contend (Br. at 21-23) that the Commission's analysis is inconsistent with precedent, including two old Third Circuit cases, *Panhandle Eastern Pipe Line Co. v. FPC*, 204 F.2d 675 (3d Cir. 1953) and *Central West Util. Co. v. FPC*, 247 F.2d 306 (3d Cir. 1957). Both cases involved essentially the same ongoing dispute. In *Panhandle*, the Commission sought to eliminate discrimination by requiring the pipeline company to deliver a certain amount of natural gas to

specified customers. *Panhandle*, 204 F.2d at 678. The amount of gas was substantially more than the existing system could carry. *Id.* The court found that the Commission's remedial authority must be construed as "subject to the proviso in section 7(a) that the Commission may not compel the enlargement of" transportation facilities, *id*. at 679, and concluded that "Congress meant to leave the question whether to employ additional capital in the enlargement of its pipeline facilities to the unfettered judgment of the stockholders and directors . . .," *id*. at 680.

In *Central West*, the pipeline company filed an NGA § 7(c) application to enlarge laterals serving some of its customers, but not the lateral serving another customer. Claiming discrimination, that customer contended that the Commission should condition the certificate to require the pipeline company to deliver increased volumes to it as well. *Central West*, 247 F.2d at 308. The Commission declined on grounds, *inter alia*, that the condition would coerce the pipeline company to enlarge its facilities, contrary to *Panhandle*, and the court affirmed. *Central West*, 247 F.2d at 311.

Neither *Panhandle* nor *Central West* requires a finding that §§ 157.36 and 157.37 are unlawful. As explained *supra* at 13-14, the design changes contemplated by these provisions are not necessarily expansions at all, much less mandatory expansions. Moreover, *Panhandle* addressed the relationship between

the Commission's NGA §§ 4 and 5 remedial authority and its NGA § 7 certificate authority, not the Commission's authority to determine the public convenience and necessity of a proposed project in the first instance.

Central West involved remedies as well. The petitioner there sought, as a remedy for discrimination, a condition requiring enlargement of laterals other than those for which the NGA § 7 application had been filed. In an Alaska pipeline certificate proceeding, design changes would apply to the facilities for which the certificate had been sought and would be intended to advance the Pipeline Act objectives, thereby allowing the proposed project to satisfy the public convenience and necessity requirement. *Compare, Central West*, 247 F.2d at 312 (the discrimination to be thus considered must be shown to have some reasonable connection or relationship to the particular certificate authorization proposed).[16]

Petitioners' argument (Br. at 21-22) that the Commission "cannot force companies to expend capital or take on significant business risk" greatly overstates their case. FERC undoubtedly has authority to impose conditions which require pipeline companies to expend capital. *See* discussion *supra* at 13-18. Under Petitioners' theory, FERC would be in the anomalous position of having authority

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[16] *Panhandle Eastern Pipe Line Co. v. FERC*, 613 F.2d 1120, 1128-29 (D.C. Cir. 1979), cited by Petitioners (Br. at 26, 30), also addressed the relationship between the NGA remedial provisions and NGA § 7, and is distinguishable on similar grounds.

to impose expensive design changes to, for example, protect the environment, but not to protect the public against an exercise of monopoly power. The Commission, moreover, is not contending that NGA § 7(e) authorizes it to "force" pipeline companies to spend money or take risks, only that § 7(e) obliges the agency to determine whether a proposed project is in the public interest, and to deny the application if it is not.

Petitioners' various arguments (Br. at 22-29) that Pipeline Act § 105 and NGA § 7(a) impliedly limit the Commission's conditioning authority under NGA § 7(e) lack merit for similar reasons. Those provisions cabin the Commission's authority to require enlargement of facilities on its own initiative, not its NGA § 7(e) obligation to determine whether a pipeline company's own proposal meets the public convenience and necessity standard.

Petitioners also contend (Br. at 28-30) that the regulations "claim the power" to "impose undue economic risk" on project sponsors and initial shippers by forcing them to pay for capacity and expandability that will go unused initially and maybe for the life of the project. As is true for much of Petitioners' argument, this contention goes more towards application of the regulations than the regulations themselves. If the Commission imposes a design change the pipeline sponsor deems to "impose undue risk," the sponsor may, of course, seek judicial review of

that particular application of the regulations. The challenged regulations themselves are neither arbitrary nor capricious, as discussed *infra* at 24-29.

Iroquois Gas Transmission Sys., L.P. v. FERC, 172 F.3d 84, 85 (D.C. Cir. 1999), is cited by Petitioners (Br. at 30-31) for the proposition that "conditions are mandatory even when the applicant has no reliance interest in an existing certificate." In fact, *Iroquois Gas* addressed aggrievement, not the scope of FERC's conditioning authority, finding that a petitioner is aggrieved for jurisdictional purposes and may seek review of certificate conditions even though it could have avoided the conditions by declining the certificate. *Iroquois Gas*, 172 F.3d at 85.

Finally, Petitioners argue (Br. at 32) that the authority to issue open season regulations "does not expand" FERC's authority to condition certificates. However, the Commission must evaluate all factors bearing on the public interest when considering applications for certificates; Pipeline Act objectives are such factors. *See* discussion, *supra* at 15-17; Order No. 2005-A at P 32 (JA 74-75). The regulations, moreover, indicate that the Commission may take certain actions, based on the results of an Alaska natural gas pipeline open season, to try to ensure that the open season objectives are attained.

II. The Challenged Regulations Are Neither Arbitrary Nor Capricious.

A. Standard of Review

FERC orders are reviewed under the arbitrary and capricious standard of the Administrative Procedure Act, 5 U.S.C. § 706(2)(A); *see, e.g.*, *Sithe/Independence Power Partners v. FERC*, 165 F.3d 944, 948 (D.C. Cir. 1999). This standard requires the Commission to "examine the relevant data and articulate a . . . rational connection between the facts found and the choice made." *Motor Vehicle Mfrs. Ass'n v. State Farm Mutual Automobile Ins. Co*., 463 U.S. 29, 43 (1983) (quoting *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168 (1962)); *see also*, *e.g.*, *Midwest ISO Transmission Owners v. FERC*, 373 F.3d 1361, 1368 (D.C. Cir. 2004). The Commission's factual findings, if supported by substantial evidence, are conclusive. *See* 15 U.S.C. § 717r(b).

B. The Regulations Are a Reasonable Response to the Pipeline Act Mandate to Promote Competition in the Development of Alaska Natural Gas Reserves.

The challenged regulations respond directly to the Pipeline Act mandate to promote competition in the exploration, development, and production of Alaska natural gas, to the unique competitive circumstances in Alaska, and to the comments filed in response to the Notice. *See* Order No. 2005 at PP 9-11 (JA 5-6). The project is unique in its size, scope and cost; if it were not, the country might not still be awaiting construction of a 1976 Act pipeline. The comments

demonstrated, moreover, that "there are complex, competitive conditions surrounding an Alaska natural gas transportation project, which are intensified by the generally agreed upon fact that there will be only one such pipeline for the foreseeable future." Order No. 2005 at P 10 (JA 6). The North Slope Producers hold the proven reserves that may support construction of the pipeline, but assurance of future access to a pipeline is needed to encourage exploration and development of other reserves. *Id*.; *see also* discussion of the comments, *supra* at 7-9.

The open season rules sought "to balance the need to allow project sponsors the flexibility to develop and bring to market Alaska natural gas with the equally competing needs to ensure fair competition in the transportation and sale of natural gas, promote the development of natural gas resources in addition to those in the North Slope, and consider Alaskan in-state requirements." Order No. 2005 at 11 (JA 6). Thus, the Commission gave prospective applicants the flexibility to decide when open seasons should occur and to develop the methodologies for determining the value of bids and for allocating capacity, but announced that changes in a project's design could be required if necessary to promote competition and offer a reasonable opportunity for access to the project.

For their part, the North Slope Producers contend (Br. at 36-37) that the regulations are arbitrary and capricious because design changes could interfere

with the "top priority" of getting a pipeline built. This ignores the fact that if Congress had wanted to elevate rapid construction of a pipeline above all else, it could have done so by barring FERC from considering any other factor. *Cf.*, Pipeline Act § 103(b)(2), 15 C.F.R. § 720a(b)(2) (Commission to "presume" that an Alaska project is supported by both a "public need" and "sufficient downstream capacity" within the United States). Instead, the Pipeline Act not only mandates that the Commission consider whether the applicant has satisfied the requirements of NGA § 7(e), but adds as factors to be considered, the promotion of competition and transportation of gas from areas other than Prudhoe Bay and Point Thomson. Pipeline Act §§103(b)(1) and (e)(2), 15 U.S.C. §§ 720a(b)(1) and (e)(1).

Petitioners' argument that design changes could scuttle or delay a pipeline is speculative. The North Slope Producers have maintained that an Alaska gas pipeline could be designed and built with sufficient capacity to accommodate the needs of every shipper. Order No. 2005-A at P 34 (JA 75-76); *see* Petitioners' reh'g request at 11 (R 61, JA 561). The open season, of course, should also provide the pipeline sponsor with information about prospective shippers. If the pipeline sponsor believes that a properly sized pipeline cannot accommodate all bidders, it can expedite the certificate process by explaining in the application why a pipeline that could serve everyone is not appropriate. *See* Order No. 2005-A at P

34 (JA 76) (explaining that the Commission has not ruled out a pipeline that will be oversubscribed).

Petitioners' argument (Br. at 37) that the Commission has erroneously assumed that a pipeline can be precisely sized to accommodate all qualifying bids lacks merit as well. The Commission explicitly recognized that it might certify a pipeline that was oversubscribed, rather than require one sized to service all bidders:

> We noted in Order No. 2005 that both the North Slope Producers and Enbridge maintained that an Alaska pipeline could be designed and built with sufficient capacity to accommodate the needs of every qualified shipper. Our expectation is that an Alaska natural gas transportation project will be designed and built, to the extent possible, to accommodate all qualified shippers who are ready to sign firm transportation agreements. Nonetheless, in Order No. 2005, we certainly did not rule out the possibility that a project . . . might be oversubscribed.

Order No. 2005-A at P 34 (JA 75-76).

Petitioners also contend (Br. 37-38) that a design change that increases capacity or expandability would force sponsors to pay for costs to transport gas that may never be developed. However, the open seasons will be for the purpose of "making binding commitments for the acquisition of initial or voluntary expansion capacity." 18 C.F.R. § 157.30; Order No. 2005 at P 19 (JA 9). Section 157.36 refers to design changes to ensure that some capacity is allotted to "new shippers willing to sign long-term firm transportation contracts," and § 157.37

similarly refers to the "needs of shippers who have made conforming bids during an open season." Since the design changes would be primarily for the benefit of shippers who have made binding commitments for capacity, Petitioners' argument is wide of the mark.

Petitioners also argue (Br. at 38-40) that the regulations are inconsistent with prior agency policy. As Order No. 2005-A points out, competitive conditions in Alaska and the lower 48 states are different, and policies for the latter are ill-suited for the former, particularly in view of the Pipeline Act directives:

> As we stated in Order No. 2005, a successful Alaska natural gas transportation project will have to overcome a variety of significant obstacles, including unique and complex competitive conditions. Those competitive conditions, we said, are intensified by the generally-agreed upon fact that there will be only one such Alaska pipeline for the foreseeable future. Against that backdrop, we affirm the conclusions of Order No. 2005, which serve as the underpinnings of the Final Rule's regulations, including the need in certain instances to accommodate existing Commission policy to the unique circumstances surrounding the exploration, production, development, and transportation to market of Alaska natural gas.

Order No. 2005-A at P 36 (JA 76-77); *see Motor Vehicles Mfrs. Ass'n*, 463 U.S. at 57 (agency may change view of the public interest, but must supply reasoned analysis).

Petitioners' argument (Br. at 40-41) that § 157.36 grants an unlawful *per se* advantage to new shippers "discounts, if not ignores," the Congressional mandate of Pipeline Act § 103(e)(2)(C) that requires the open season regulations to ensure

that any open season for expansion capacity provides the opportunity for the transportation of natural gas from areas other than Prudhoe Bay or Point Thomson. Order No. 2005-A at P 35 (JA 76). Section 157.36 does so in a reasonable manner and, moreover:

> [the] regulations do not require that an expansion proposal must, regardless of economic and technical considerations, provide transportation of gas of other than Prudhoe Bay/Point Thomson volumes. The regulations simply require that an opportunity for such transportation be provided.

Id.

Finally, Petitioners' arguments concerning both the lawfulness and reasonableness of the regulations focus on conditions Petitioners fear could be imposed. However, the Commission routinely imposes design changes to support findings of public convenience and necessity. Here, no application has been filed, no certificate has issued, and no conditions have been imposed. Should all of these events occur and an aggrieved party believe that specific conditions imposed are arbitrary and capricious, it may seek judicial review at that time.

CONCLUSION

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

Respectfully submitted,

John S. Moot
General Counsel

Robert H. Solomon
Solicitor

Judith A. Albert
Senior Attorney

Federal Energy Regulatory
Commission
888 First Street, N.E.
Washington, D.C. 20426
Phone: 202-502-6046
Fax: 202-273-0901
judith.albert@ferc.gov
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Exxon Mobil Corporation, et al. v. FERC **Docket No. RM05-1**
D.C. Cir. Nos. 05-1299*, et al.*

CERTIFICATE OF COMPLIANCE

In accordance with Fed. R. App. P. 32(a)(7)(C)(i), I certify that the Brief of Respondent Federal Energy Regulatory Commission contains 7,011 words, not including the tables of contents and authorities, the certificates of counsel and the addendum.

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Judith A. Albert
Senior Attorney

Federal Energy Regulatory
Commission
Washington, D.C. 20426
TEL: (202) 502-6046
FAX: (202) 273-0901

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