123 FERC ¶ 61,151
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Burlington Resources Oil & Gas Company Docket No. GP99-15-005

Panhandle Eastern Pipe Line Company Docket No. RP98-40-041

ORDER ON REMAND

(Issued May 15, 2008)

1. In this order the Commission addresses the remand by the United States Court of Appeals for the District of Columbia Circuit, *Burlington Resources Oil & Gas Company v. FERC (Burlington II)*.[1] At issue is who is responsible for payment of the *ad valorem* tax refund obligation arising from certain sales of natural gas by Burlington Resources Oil and Gas Co. (Burlington). Consistent with *Burlington II*, this order directs two pipelines to refund to Burlington the refunds that Burlington paid to them under protest claiming that its earlier settlements with those pipelines, which included an indemnity clause, relieved it of that obligation.

2. The extensive background is set forth in the prior Commission orders and court decisions and will be repeated here only to the extent necessary to understand the issue. In 1993, the Commission held that Kansas *ad valorem* taxes did not qualify as a reimbursable severance tax under section 110 of the Natural Gas Policy Act (NGPA), and thus producer/first sellers could not recover such taxes as an add-on to the maximum lawful price (MLP) under the NGPA.[2] The court affirmed that decision, but held that the Commission had improperly waived refunds for the period October 1983 through June

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[1] 513 F.3d 242 (D.C. Cir. 2008).

[2] *Colorado Interstate Gas Co.*, 65 FERC ¶61,292 (1993), *reh'g denied*, 67 FERC ¶ 61,209 (1994).

1988.[3] The Commission accordingly ordered first sellers/producers to make refunds of *ad valorem* taxes they had collected in excess of the MLP during the October 1983 to June 1988 period.[4] To implement the Commission's order, pipelines that had first paid the *ad valorem* taxes as an add-on to the MLP were directed to send statements of refunds due to producers. The refunds the pipelines received from the producers would be flowed back to customers that had paid the excess amount.

3. Panhandle Eastern Pipe Line Co. (Panhandle) and Northern Natural Gas Co. (Northern) sent a statement of refunds due to Burlington which had collected the add-on in its sales to those pipelines. Burlington denied any liability for these *ad valorem* tax refund claims. Burlington contended that it was not liable for any *ad valorem* tax refund because it had entered into earlier settlements with Panhandle and Northern which settlements included an indemnity clause which Burlington contended covered the pipelines' *ad valorem* tax refund claims (the Burlington Settlements). Burlington asserted that although the amount of the *ad valorem* refund claims against it were correct, the indemnity clause relieved it of any *ad valorem* refund liability, and required each pipeline, not Burlington, to pay the refund to its customers.

4. The Commission rejected Burlington's defense, holding that the NGPA prohibited a producer from receiving more than the MLP and that the "indemnity" clause Burlington relied upon cannot relieve the producer from paying the refund when it receives more than the MLP in a first sale.[5] Burlington paid the refund claims to Northern and Panhandle under protest, and sought review in the court.[6] Northern and Panhandle flowed those refunds through to their customers.

5. The clauses relied upon by Burlington were in settlements whose main purpose the court acknowledged was to exchange immediate payments for a reduction in the pipeline's future "take-or-pay obligations." The language in the two clauses were not

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[3] *Public Service Company of Colorado v. FERC*, 91 F.3d 1478 (D.C. Cir 1996).

[4] *Public Service Company of Colorado*, 80 FERC ¶ 61,264 (1997), *reh'g denied*, 82 FERC ¶ 61,058 (1998).

[5] *Burlington Resources Oil and Gas Co.*, 103 FERC & 61,005, *reh'g denied*, 104 FERC & 61,317 (2003), and *Panhandle Eastern Pipe Line Co.*, 103 FERC & 61,007, *reh'g denied*, 105 FERC & 61,141 (2003).

[6] Burlington stated that on May 1, 2003, it paid Northern $950,767.74 and Panhandle $633,953.94, which amounts represented principle and interest.

identical. Paragraph 5 of the Panhandle settlement provided that under the settlement each party agreed to "release, discharge, waive and indemnify" the other party from all claims relating to the contracts covered by the settlement. Paragraph 7 of the Northern settlement stated that the settlement "resolves all disputes between the parties under any and all contracts" under the settlement, and "releases and discharges the other … from any and all liabilities [and] claims arising out of … or relating to said Contracts."

6. In *Burlington I*[7] the Court considered both clauses as "release and indemnity clauses," and held that the *ad valorem* tax refund claims were covered by them. The court held that "the Commission reads too much into the language limiting the release and indemnification to claims between the parties relating to the contracts; the contract language does not reasonably permit exclusion of any claim that relates to payments made under the contracts," including "Northern's and Panhandle's refund claims against Burlington."[8] The Court stated it was troubled with the apparent inconsistency it found between the Commission's rejection of Burlington's indemnification clause to relieve it of its *ad valorem* tax refund liability, and the Commission's approval of Panhandle and Northern's "Omnibus Settlements." Those settlements involved the pipelines' *ad valorem* refund claims against hundreds of other producers, and the settlements reduced or eliminated the pipelines' refund claims against some of the producers. Thus those settlements permitted some producers to retain some amount they had collected in excess of the MLP. The Court remanded for a more adequate explanation of the Commission's different treatment of the Omnibus and Burlington Settlements.

7. On remand, the Commission reaffirmed its orders, relying on a number of distinctions between the Burlington Settlements and the Omnibus Settlements.[9] In the remand order, the Commission accepted the Court's interpretation of the Burlington "indemnity clause" as encompassing the *ad valorem* refund claims asserted against Burlington arising from first sales that were made under the gas purchase contract covered by the Burlington settlement. However, the Commission held that the NGPA established a federally regulated price covering Burlington's sale of the gas in question to the pipelines. Therefore, the Commission held that the release and indemnity clauses in the Burlington Settlements were unenforceable. The Commission explained that

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[7] *Burlington Resources Oil & Gas Company v. FERC* 396 F.3d 405 (D.C. Cir. 2005).

[8] 396 F.3d at 411.

[9] *Burlington Resource Oil and Gas Co.*, 112 FERC ¶ 61,053, *reh'g denied*, 113 FERC ¶ 61,257 (2005).

"requiring Northern and Panhandle, the purchasers in Burlington's first sales, to make refunds of *ad valorem* tax reimbursements that would otherwise be owed by Burlington, while Burlington is allowed to retain those amounts, is the equivalent of requiring the purchasers to pay the first seller in excess of the applicable maximum lawful price."[10] The remand order explained that the Commission approved the Omnibus Settlements, which permitted certain producers to possibly also retain an excess over the regulated price, as an exercise of its prosecutorial discretion given the substantial benefits that flowed from those settlements. Those settlements covered hundreds if not thousands of *ad valorem* refund claims, many of which producers disputed. Since none of these benefits flowed from the Burlington Settlements, the Commission did not see any basis to exercise its prosecutorial discretion with respect to those settlements and required Burlington, and not the pipelines, to pay the *ad valorem* refund. Accordingly, the Commission concluded that Burlington was responsible for payment of the *ad valorem* refund claims and was not entitled to the return of the refunds it had paid to the pipelines.

8. In *Burlington II*, the Court vacated the Commission's orders responding to *Burlington I* and remanded the case to the Commission. The Court first made clear that its interpretation of the indemnity clause as stated in *Burlington I* governed this proceeding, stating "Whether or not the *ad valorem* liabilities were within the main purpose of the [Burlington] settlements, they were within their language, written at a time when, as the background described above makes clear, the law was deeply unsettled and the parties would have had reason to seek accord."[11] The Court rejected the contention by intervenor Northern that the Court's interpretation of the indemnity clause in *Burlington I*, was dictum, and that the Commission with the benefit of extrinsic evidence, should be allowed to construe the Burlington settlement language first. The Court stated "*Burlington I's* construction has thus become law of the case, which … cannot [be] challenge[d] here. *See LaShawn A. v. Barry*, 87 F.3d 1389, 1393, (D.C. Cir. 1996) (*en banc*)."[12]

9. The Court found the Commission's explanation of the differences between the "ostensibly similar" settlements unpersuasive and that the Commission's reliance on "prosecutorial discretion" to enforce the Omnibus Settlement but to not enforce the Burlington Settlement was misplaced since "the factors on which the Commission justified its approval of the Omnibus Settlement are equally applicable to the Burlington

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[10] 112 FERC ¶ 61,053 at P 47.

[11] 513 F.3d at 246.

[12] *Id.* at 246.

Settlements."[13] The Court recognized that the NGPA "in a general sense invalidated any private agreement to pay more than the maximum lawful price."[14] However, the Court held that this did not necessarily prohibit good faith settlements at arm's length over past gas sales, like the Burlington settlements where consideration was furnished in exchange for permitting the party to retain such excess, and "with no apparent detriments to third parties."[15]

10. The Court stated that the precedent on which the Commission relied to conclude that such settlements were unenforceable does not support that conclusion. The Court held that, where there was a regulated gas sale above the MLP, the law does not prevent the purchaser with an *ad valorem* refund claim from exchanging those accrued rights for other valuable consideration. Turning to the Burlington Settlements, the Court held that while the "pipeline would have indeed have done better by preserving their claims … the law does not prevent them from exchanging the entitlement for other goods."[16] The Court concluded that there was no basis to disregard the otherwise lawful Burlington settlements. The Court vacated the Commission's orders under review, and "remand[ed] the case to the Commission for it to proceed with the adjudication in accordance with this opinion."[17]

11. Consistent with the Court's opinion in *Burlington II*, the Commission orders Northern and Panhandle to return to Burlington, with interest, the amount of *ad valorem* tax refunds Burlington paid to them under protest. In addition, the two pipelines may not seek to recover from their customers the amounts of those refunds.

12. The Court has held that the Burlington Settlements are fully enforceable and do not violate the NGPA. As interpreted by the Court, under the release and indemnity clauses, Burlington is released from any obligation to make refunds to the pipelines, and the pipelines must pay their customers any *ad valorem* tax refunds which would otherwise be due from Burlington. There is no need for further proceedings in this case to adjudicate the amount of the relevant refunds, because Northern and Panhandle have

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[13] *Id*. at 250.

[14] *Id*. at 248.

[15] *Id*. at 250.

[16] *Id*. at 250.

[17] *Id*. at 251.

already stated the amount of the refunds they believe are due, and Burlington has not contested the pipelines' calculations of the refund amounts. Northern and Panhandle have already flowed through the amount of the refunds to their customers, and thus have complied with the Settlements' requirement that they pay the amount of the refunds to their customers. In these circumstances, the only further action required for full implementation of the Burlington Settlements is for the two pipelines to return the amounts of the refunds to Burlington, with interest.

The Commission orders:

Northern and Panhandle must, within 30 days of this order, refund to Burlington, with interest, the *ad valorem* tax refunds paid by Burlington to them under protest.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.