

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeem G. Kelly.

Shell Offshore Inc. v. Transcontinental Gas Pipe Line Corporation, Williams Gas Processing – Gulf Coast Company, L.P., Williams Field Services Docket No. RP02-99-009

ORDER ON REMAND

(Issued February 15, 2005)

1. This order addresses the opinion issued on July 13, 2004, by the U.S. Court of Appeals for the District of Columbia Circuit in *Williams Gas Processing – Gulf Coast Co., L.P. v. FERC*.¹ The court vacated Commission orders² that had granted a complaint by Shell Offshore Inc. (Shell), who alleged that Transcontinental Gas Pipe Line Corp. (Transco) and its affiliated gatherer, Williams Field Services (WFS), had engaged in collusive behavior in offering gathering services, had abused their monopoly power and had violated the open access and non-discrimination requirements of the Outer Continental Shelf Lands Act (OCSLA).³ The court remanded the case for further proceedings consistent with its opinion. The court found that the Commission, in granting Shell's complaint, had misapplied Commission precedent under the Natural Gas Act (NGA)⁴ and had erred in finding violations of the OCSLA. Today's order reverses

¹ 373 F.3d 1335 (2004) (*Williams Gas Processing*).

² *Shell Offshore Inc. v. Transcontinental Gas Pipe Line Corp.*, 100 FERC ¶ 61,254 (2002) *reh'g denied* 103 FERC ¶ 61,177 (2003).

³ 43 U.S.C. §§ 1331 – 1356.

⁴ 15 U.S.C. § 717.

the Initial Decision and denies Shell's complaint. The order benefits customers by implementing the Commission's policy as to when the Commission will reassert jurisdiction over a pipeline gathering affiliate.

I. Background

A. Shell's Complaint and the Commission's Orders

2. On November 20, 2000, Transco and its affiliate, WFS, submitted an application and related petition to spin-down roughly 22 miles of Transco's North Padre Island pipeline facilities on the outer continental shelf (OCS), which were originally functionalized as transmission, to WFS. WFS' petition sought a Commission order declaring that the facilities would be gathering upon their acquisition by WFS. Over protests, the Commission approved the abandonment and granted the petition, declaring the facilities to be gathering upon completion of the sale, which occurred on December 1, 2001.⁵

3. Prior to the spin-down, Transco had charged \$0.08/Dth to transport Shell's gas the 230-mile distance from the interconnect with Shell's production facilities to one of Transco's mainline pooling points. After the spin-down, Shell not only paid Transco the \$0.08 transportation rate, WFS also demanded that Shell pay it an additional \$0.08/Dth for transporting Shell's gas 3.08 miles from the connection with Shell's production facilities on what had become WFS' facilities to the interconnection with Transco's transmission facilities. Shell chose to shut-in its production rather than pay double the rate it had been paying Transco alone for the same transportation service.

4. Shell filed a complaint against Transco and its affiliates, and the Commission set the complaint for hearing before an ALJ, who issued an Initial Decision on June 4, 2002.⁶ The Commission subsequently affirmed the Initial Decision and adopted the ALJ's finding that Transco and WFS, in effectuating the spin-down, met the criteria established

⁵ *Transcontinental Gas Pipe Line Corp.*, 96 FERC ¶ 61,115 (2001), *reh'g denied* 103 FERC ¶ 61,177 (2003).

⁶ *Shell Offshore Inc. v. Transcontinental Gas Pipe Line Corp., Williams Gas Processing – Gulf Coast Company, L.P., Williams Field Services Company, and Williams Gulf Coast Gathering Company, L.L.C.*, 99 FERC ¶ 63,034 (2002).

in *Arkla Gathering Services Co.*⁷ for the reassertion of NGA jurisdiction over rates for gathering performed by WFS as if Transco still owned the subject facilities. The Commission's order affirmed the ALJ's finding that: 1) Transco and its affiliate acted in concert with one another in offering gathering services on the North Padre Island system; and 2) concerted action frustrated the Commission's effective regulation of Transco. The Commission's order regarded Transco and WSF as a single entity because of their concerted actions. The Commission found that their behavior frustrated the Commission's regulation of Transco by requiring Shell to execute a gathering agreement that included an exorbitant gathering rate and anticompetitive conditions, such as a life-of-reserves commitment tying Shell's production to the Transco facilities for the life of the reserves. The Commission also found that WFS' actions violated the OCSLA. The Commission then ordered Transco to file a just and reasonable rate of \$0.0169/Dth for gathering services on the spun-down North Padre Island facilities and to maintain a gathering rate schedule for such services.

5. On rehearing, the Commission responded to arguments in requests for rehearing that the Commission had not properly applied the *Arkla* test. The Commission clarified that it viewed the *Arkla* test as being a circumvention test. That is, the Commission stated that it could reassert jurisdiction based on its finding that Transco created the "illusion of a separate gathering entity to evade the Commission's regulations," thus permitting "WFS to extract money that Transco, as a natural gas company, providing both services alone, could not."⁸ The Commission denied requests for rehearing, describing the spin-down as "a sham ... designed to circumvent the Commission's regulation."⁹

B. The D.C. Circuit Court Decision

6. On July 13, 2004, the court vacated the Commission's orders in *Williams Gas Processing – Gulf Coast Company, L.P. v. FERC*¹⁰ and remanded the case. The court rejected both of the Commission's statutory bases for reasserting jurisdiction – the NGA and the OCSLA. With respect to the Commission's NGA jurisdiction, the court

⁷ 67 FERC ¶ 61,871 (1994), *order on reh'g*, 69 FERC ¶ 61,280 (1994), *reh'g denied*, 70 FERC ¶ 61,079 (1995), *reconsideration denied*, 71 FERC ¶ 61,297 (1995) (*Arkla*).

⁸ *Id.* at 61,664, P. 7.

⁹ 103 FERC ¶ 61,177 (2003) at 61,662, P. 7.

¹⁰ *Williams Gas Processing, supra.*

determined that the Commission had misapplied the *Arkla* test. First, the court found that the Commission failed to show that the narrow kinds of abuses that the Commission in *Arkla* stated would trigger a reassertion of jurisdiction had occurred. The court stated that *Arkla* permits a reassertion of jurisdiction in circumstances “limited to” abuses “directly related to the affiliate’s unique relationship with an interstate pipeline,” such as “tying gathering service to the pipeline’s jurisdictional transmission service,” or “cross-subsidization between the affiliate’s gathering rates and the pipeline’s transmission rates.”¹¹ Second, the court found that the Commission, in piercing the corporate veil to treat WFS and Transco as a single entity in a “sham” transaction (the spin-down), analyzed the elements of the *Arkla* test out of sequence: “it adopts as its first premise (WFS is Transco) the *Arkla* [*Gathering*] test’s ultimate conclusion – that corporate form may be set aside.”¹² Under *Arkla*, the rationale for reasserting “in connection with” jurisdiction is that the concerted behavior between the two entities (*i.e.*, the regulated pipeline and the affiliated non-jurisdictional gathering affiliate) has frustrated the Commission’s ability to regulate the *pipeline* (not the gatherer). By treating WFS and Transco as a single entity, the Commission “could thus attribute the gatherer’s alleged malfeasance to the pipeline, and apply the pipeline’s regulatory requirements to the gatherer.”¹³ The court found error, since: “Only when the Commission finds both concerted action between a jurisdictional pipeline and its gathering affiliate and that the concerted action frustrates the Commission’s effective regulation of the pipeline, may it then pierce the corporate veil and treat the legally distinct entities as one.”¹⁴

7. The court also rejected the Commission’s finding that WFS’ actions warranted application of the OCSLA’s open access and nondiscrimination prohibitions to set a just and reasonable gathering rate, finding that its earlier decision in *The Williams Companies v. FERC*,¹⁵ appeared to doom assertion of jurisdiction under the OCSLA. Describing an argument made on appeal that the Commission simply was enforcing the open access and non-discrimination conditions in Transco’s tariff as *post hoc* rationalization, the court observed that the Commission’s assertion of OCSLA jurisdiction over WFS based on the *Arkla* test “is nowhere present in either the Order or the Order on Rehearing.”¹⁶

¹¹ *Id.* at 1342.

¹² *Id.* at 1343.

¹³ *Id.*

¹⁴ *Id.*, citing *Arkla*, 67 FERC at 61,871.

¹⁵ 345 F.3d 910 (D.C. Cir. 2003).

¹⁶ *Id.* at 1345.

II. Discussion

8. Based on the D.C. Circuit Court of Appeal's decision, the Commission will reverse the Initial Decision and deny Shell's complaint. The *Arkla* test involves a determination that, as a result of the concerted action of the pipeline and the gathering affiliate, the Commission's effective regulation of the pipeline is frustrated. The court found that the actions of WFS in increasing its gathering rates and attaching anti-competitive conditions to its gathering services, such as requiring Shell to commit its remaining reserves to WFS' gathering system after the spin-down, did not warrant a reassertion of jurisdiction over WFS under that test. The court stated that, under *Arkla*, the Commission's ability to reassert jurisdiction is limited to abuses directly related to the affiliate's unique relationship with an interstate pipeline, such as tying gathering service to the pipeline's jurisdictional transmission service or cross-subsidization between the affiliate's gathering rates and the pipeline's transmission rates.

9. Under the court's interpretation of the *Arkla* test, "[o]nly those types of activities – where the affiliate is leveraging its relationship with the pipeline to enhance its market power – would 'trigger the Commission's authority to disregard the corporate form and treat the pipeline and its affiliate as a single entity.'"¹⁷ The court found that WFS' actions fell outside this category. It observed that WFS was charging the same rates and imposing the same service conditions that any non-affiliate gatherer could demand in the OCS and, thus, was not "leveraging" its unique relationship with Transco. The Commission in *Arkla* stated that "although an affiliate could undertake other types of anti-competitive activities, the Commission's jurisdiction would be implicated only where the abuse is directly related to the affiliate's unique relationship with the pipeline."¹⁸

¹⁷ *Id.*, citing *Arkla*, 67 FERC at 61,871.

¹⁸ *Id.*

10. Based on the record of these proceedings and the court's interpretation of the *Arkla* test and the OCSLA, the Commission finds that there is not a sufficient basis to reassert NGA jurisdiction or to assert OCSLA jurisdiction over the gathering rates and services of WFS' North Padre Island gathering facilities. Accordingly, the Commission reverses the Initial Decision and denies Shell's complaint. The Commission directs Transco to remove the North Padre Island gathering rate and rate schedule from its tariff.¹⁹

The Commission orders:

(A) The Initial Decision is reversed and the complaint filed by Shell in these proceedings is denied, as discussed in the body of this order.

(B) Transco is directed to refile to remove the North Padre Island gathering rate and rate schedule from its tariff.

By the Commission. Chairman Wood concurring with a separate statement attached.

(S E A L)

Magalie R. Salas,
Secretary.

¹⁹ See *Shell Offshore, Inc. v. Transcontinental Gas Pipe Line Corp., et al.*, 102 FERC ¶ 61,156 (2003).

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WOOD, Chairman, *concurring*:

I remain frustrated with the Commission's statutory inability to prevent monopolistic and discriminatory behavior that disadvantages customers. While I recognize that the Natural Gas Act exempts the gathering of natural gas from the Commission's jurisdiction, I nevertheless believe that Transco's spin-down of facilities to its non-regulated affiliate was designed to circumvent the statutory purpose of the NGA. However, in light of the Court's decision, I unfortunately acknowledge that there is no basis, at this time, by which to assert jurisdiction over the rates charged by Williams for gathering services.

Pat Wood III