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FERC Denies Market-Based Rate Application

Failure to provide detailed cost data relating to the provision of oil transportation service causes FERC to deny a pipeline's request to charge market-based initial rates.

On May 7, the Federal Energy Regulatory Commission (FERC or Commission) issued an order denying a request to charge market-based rates as initial rates for transportation service to be provided on the Seaway Crude Pipeline Company (Seaway) system.[1] The Commission's order clarifies for oil pipelines seeking market-based authority in the future that detailed cost data is a necessary prerequisite in conducting a market-power analysis in the context of market-based rate applications filed under the Interstate Commerce Act.

Background

On December 2, 2011, Enterprise Products Partners L.P. and Enbridge Inc. (together, Applicants) filed an Application for Authorization to Charge Market-Based Rates with the Commission in connection with a proposed reversal of the Seaway system. Applicants requested authority to charge market-based rates for the interstate transportation of crude oil on the Reversed Seaway Pipeline at its Cushing, Oklahoma, origin and its proposed destinations on the U.S. Gulf Coast.

Currently, the Seaway system provides south-to-north transportation of crude oil from origins on the U.S. Gulf Coast to its destination at Cushing. However, Enbridge recently purchased a 50% interest in Seaway. After the purchase, the Applicants intended to reverse the flow of crude oil on the system in order to provide north-to-south service from Cushing to an initial delivery point in Houston, Texas, and (following construction of additional pipeline facilities) an additional delivery point in the Beaumont/Port Arthur, Texas, area. Currently, the Applicants anticipate that the Reversed Seaway Pipeline will begin operating in north-to-south service during the second quarter of 2012, with an initial capacity of approximately 150,000 barrels per day depending upon the specific mix of crude oil transported. Following pump additions and modifications anticipated to be completed by early 2013, the capacity of the Reversed Seaway Pipeline is expected to be approximately 375,000 barrels per day, again depending upon the specific mix of crude oil transported.

In their request, the Applicants argued that operating under the Commission's indexing procedures and cost-of-service ratemaking alternatives would constrain the Reversed Seaway Pipeline's ability to respond appropriately to the market forces in those locations. In support of their request, the Applicants argued that statistical analysis demonstrates that there are very low levels of market concentration in both the applicable origin and destination markets. In addition, the Applicants argued that in both its origin and destination markets, the Reversed Seaway Pipeline will have a low market share and there is significant excess capacity. However, the Applicants did not provide any price data, such as a netback analysis, to demonstrate that the Applicants would be competing cost-effectively. Instead, the Applicants stated that it is not possible to provide such data and perform such an analysis since the Reversed Seaway Pipeline has not yet begun providing service and does not have rates on file.

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1. *See Enterprise Products Partners L.P.*, 139 FERC ¶ 61,099 (2012) (MBR Order).

Commission Determination

The Commission determined that the information filed by the Applicants in their request was “insufficient to permit a determination that the proposed Reversed Seaway Pipeline lacks market power in its contested origin and destination markets.”[2] In reaching its determination, the Commission first explained that price data is an “indispensible” component of a market-power analysis. In that regard, the Commission noted that a recent decision issued by the U.S. Court of Appeals for the D.C. Circuit, *Mobil Pipe Line Company v. FERC*,[3] did not take issue with the Commission’s consideration of price data when conducting a market-power analysis. Instead, the *Mobil* court determined only that the pipeline at issue in that case could not possess market share sufficient to constitute market power and, therefore, remanded the Commission’s denial of that pipeline’s market-based rate request. Notwithstanding the court’s action, the Commission stated that in *Mobil* the court did find that the pipeline could not raise its rates above the competitive level for a significant period of time. In light of this finding, the Commission did not interpret *Mobil* from precluding price data in the market-power analysis.

Having distinguished *Mobil*, the Commission explained that in order to conduct a market-power analysis, alternative competitors for supply must be considered to determine whether a market-based rate applicant would be competing cost-effectively. In that respect, “[f]or an alternative to be included in a geographic market, it must be a ‘good’ alternative. A good alternative must be a good alternative in terms of price.”[4] For that reason, any market-power analysis requires a proxy for a competitive price because “[t]he necessity of identifying an appropriate proxy for the competitive price is central to the entire market power analysis.”[5] The proxy need not be a regulated tariff rate, but *something* must be presented as a proxy to be used in an analysis. The Commission stated that even though parties may dispute whether the proxy used by a pipeline adequately reflects the competitive price level, the pipeline must still present such price data in order to determine good alternatives for inclusion into the market-power analysis.

Turning to the Applicants’ request, the Commission found that the Applicants’ failure to provide a proxy for a competitive price was fatal. The Commission noted the Applicants’ recognition that such information could not be provided; therefore, the Commission declined to set the request for hearing and denied the request. In doing so, the Commission determined that “[a] hearing would not be productive where, as even the applicant acknowledges, a fundamental element required to demonstrate a lack of market power cannot be provided.”[6]

The Commission distinguished several cases on which the Applicants’ relied for the proposition that the Commission may approve market-based rate requests without detailed cost analyses. The Commission found that in one instance, it reviewed detailed cost analyses provided by a protestor and determined that the pipeline would be unable to exercise market power even if the protestor’s data was accurate. In other instances, the Commission explained that the cost analyses were not required because market-based rate authorization was sought for economic areas (BEAs) defined by the Bureau of Economic Analysis as relevant regional markets surrounding metropolitan or micropolitan statistical areas. The Commission implied that in instances where market-based rate authorization is requested within BEAs, price analyses are not required because BEAs appropriately define geographic markets, including good competitors. As such, the cases on which the Applicants’ relied were distinguishable from their application because they did not request market-based rate authority within a BEA.

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2. *Id.* at P 33.
3. Case No. 11-1021 (D.C. Cir. Apr. 17, 2012).
4. MBR Order at 32.
5. *Id.* at P 40.
6. *Id.* at P 41.

Morgan Lewis

Contacts

If you have any questions or would like more information on the issues discussed in this LawFlash, please contact any of the following Morgan Lewis attorneys:

Washington, D.C.		
Mark R. Haskell	202.739.5766	mhaskell@morganlewis.com
Levi McAllister	202.739.5837	lmcallister@morganlewis.com
Houston		
Charles A. Moore	713.890.5730	cmoore@morganlewis.com
Christina M. Vitale	713.890.5764	christina.vitale@morganlewis.com

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