

103 FERC ¶ 61,005

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, and Nora Mead Brownell.

Burlington Resources Oil and Gas Co.	Docket Nos. GP99-15-001
Northern Natural Gas Co.	RP98-39-026
Continental Energy	SA98-101-001

ORDER DENYING REHEARING
AND REMOVING PARTY FROM HEARING

(Issued April 1, 2003)

1. This order denies the request for rehearing of Burlington Resources Oil and Gas Co. (Burlington) of the Commission's January 2, 2003 order¹ (the January 2 order) which established a hearing to resolve disputes regarding the proper ad valorem tax refund amounts that are due and payable to Northern Natural Gas Co. (Northern) by producer first sellers of natural gas Burlington and Continental Energy. Both Burlington and Northern² state that Burlington's refund obligation involves only a legal issue so that no hearing is necessary to resolve that issue, and request the Commission to decide the legal issue. This order finds that Burlington is obligated to make the refund, and directs it to make the payment, eliminating the need for a hearing as to Burlington.

Background

2. The Commission has previously ordered that producers must reimburse Northern for Kansas ad valorem taxes collected after October 1983 that resulted in the producer collecting amounts in excess of the Maximum Lawful Price (MLP) established pursuant

¹102 FERC ¶ 61,003 (2003).

²Northern filed an answer to Burlington's request, and Burlington filed a motion to file an answer to Northern's answer together with the answer. The Commission accepts these pleadings since they assist the Commission in consideration of the issues presented.

to the Natural Gas Policy Act (NGPA) of 1978.³ In 1993, the Commission ruled that Kansas' ad valorem tax did not qualify as a reimbursable severance tax under Section 110 of the NGPA,⁴ and ordered producers to refund the excess amount over the MLP that they had collected since 1988, and flowthrough the refunds to their customers. In 1996, the Court of Appeals affirmed the Commission, but held that the producers must also make refunds from 1983, the year the reimbursement was first challenged at the Commission.⁵

3. On September 10, 1997, the Commission issued an order requiring producers to refund amounts, with interest, that unlawfully exceeded the applicable MLP, for the period commencing October 3, 1983, and directed pipelines to submit Statements of Refunds Due to first sellers/producers indicating the refunds claimed by the pipeline, and then file reports reflecting those statements with the Commission.⁶ Northern sent a statement to Southland Royalty Company (Southland), Burlington's predecessor, indicating that Southland owed ad valorem tax refunds to Northern. Burlington, in its responses to Northern, and in a Petition for Resolution in Docket No. GP99-15-001, asserted that it was not responsible for the refunds because of a 1989 agreement between Southland and Northern.

4. A number of other producers also filed various pleadings with the Commission, asserting that the refund amounts claimed by Northern were incorrect, or seeking relief from the refunds for various other reasons. To resolve these disputes the parties participated in extensive settlement discussions which led to the Commission's approval

³Although the 1989 Wellhead Decontrol Act deregulated the price for all first sales of natural gas, in accordance with the intent of Congress, any first sale of natural gas occurring prior to decontrol is subject to the Commission's wellhead pricing regulations as they were in effect at the time of the sale.

⁴Colorado Interstate Gas Co., 65 FERC ¶ 61,292 (1993), reh'g denied, 67 FERC ¶ 61,209 (1994).

⁵Public Service Company v. FERC, 91 F. 3d 1478 (D.C. Cir. 1996), cert. denied, 520 U.S. 1224 (1997).

⁶Public Service Company of Colorado, 80 FERC ¶ 61,264 (1997), reh'g denied, 82 FERC ¶ 61,058 (1998), aff'd in relevant part, Anadarko Petroleum Corporation v. FERC, 196 F.3d 1264 (D.C. Cir. 1999), reh'g, 200 F.3d 867, cert. denied, 120 S.Ct. 2215 (2000), order on remand, 91 FERC ¶ 61,264 (2000) (Public Service).

of a settlement on December 27, 2000.⁷ However, because persons could elect not to be bound by the settlement, and Burlington so elected, Northern's refund report of May 20, 2002, claimed that Burlington still owed \$914,751.42 in ad valorem tax refunds. The January 2 order described some of the contentions producers had raised as to the amount of the ad valorem tax refund claim, and set for hearing the amount Burlington and Continental Energy owed.

Burlington's Request

5. Burlington asserts that there are no disputed issues of fact that necessitate an evidentiary hearing. Rather, it contends, the legal issue is whether the February 28, 1989 Settlement between Northern and Burlington's predecessor, Southland, released and indemnified Burlington for any claims for refund of Kansas ad valorem taxes. Burlington states that under that settlement, which covered 30 gas contracts in three states, including some in Kansas, Southland gave up substantial take-or-pay claims, and agreed to reform the terms of the gas contracts, and the settlement included a mutual agreement to release and indemnify the other for all claims arising from or relating to the gas contracts under which the ad valorem tax reimbursements were paid.

6. Burlington relies on paragraph 5 of the Settlement which provided as follows:

Execution of this Settlement Agreement resolves all disputes between the parties under any and all of said Contracts, and Northern and Seller each hereby fully, completely, and finally releases and discharges the other . . . affiliates, parents or subsidiary corporations, and their respective successors and assigns from any and all liabilities, claims, and causes of action, whether at law or in equity, and whether now known and asserted or hereafter discovered, arising out of, or in conjunction with, or relating to said Contracts for all periods through January 31, 1989

7. Burlington states that it does not claim that it received less than the MLP for gas, nor does it claim that royalty or working interest owners should bear a portion of its ad valorem tax refund obligations. Burlington states that its sole defense is that Northern agreed by the Settlement to indemnify and release Burlington for all claims arising from

⁷Northern Natural Gas Company, 93 FERC ¶ 61,311 (2000).

or relating to Burlington's sale of gas to Northern, and, therefore, Northern is the party responsible for any ad valorem tax liability.

8. Burlington also asserts that prior Commission orders in Williams Natural Gas Co., 67 FERC ¶ 61,153 (1994) (Williams) and Anadarko Petroleum Corp. v. Pan Energy Pipe Line Co., et al., 85 FERC ¶ 61,090 (Anadarko), do not absolve Northern of its contractual obligation to be responsible for any claim relating to the gas contracts covered by the Settlement.

9. Burlington contends that neither of these cases is applicable to the case at hand because Northern and Southland never agreed to have Northern pay more than the MLP for gas. Burlington argues that, to the contrary, without any specific contemplation of Kansas ad valorem taxes or other issues relating to the MLP, Northern agreed to indemnify and release Southland from all claims relating to the gas contracts in return for valuable consideration, including contract reformation and release from significant take-or-pay liability.⁸

10. Burlington argues that giving effect to settlement, and requiring Northern to pay the ad valorem refund amount, will not cause Southland to have violated the NGPA because to the extent Southland might have received in excess of the MLP for gas sold to Northern, Southland already effectively reimbursed Northern well in excess of that amount through the consideration provided to Northern in the form of take-or-pay relief under the Settlement. In addition, Southland agreed to reform the gas contracts to reduce both the contract price and Northern's take obligations in the future. Thus, Northern's customers, who would receive the ad valorem tax refund, have benefitted from Northern's lower gas costs that resulted from the Settlement.

11. Burlington also requests that if the Commission determines that Northern can somehow be relieved of its contractual commitment to indemnify Burlington with respect to the ad valorem tax refunds, such relief should be limited solely to the tax refund principal amount, without interest. If Burlington pays the tax refund principal amount to Northern, it will not have received any amounts in excess of the MLP, but any interest amounts due pursuant to Commission regulations should qualify as liabilities that should be assumed by Northern pursuant to the contractual release set forth in the Settlement.

⁸Burlington contends that under the settlement Southland received only about 10 cents on the dollar that it was entitled to under the gas contracts, and refers to working papers attached to its request to support its contention.

12. Finally, Burlington asserts that if the Commission would find that enforcing the indemnification provision in the Settlement would result in a technical violation of NGPA ceiling prices, the Commission has the authority to grant Burlington an exemption under NGPA Section 502(c), 15 U.S.C. § 3412(c), in order to avoid inequity.

13. Burlington argues that it would be "inequitable" for the Commission to absolve Northern of its contractual commitment under the Settlement to release Burlington from all liabilities associated with certain gas sales contracts, when Northern (and indirectly its sales customers) have already received and enjoyed the benefits of the Settlement in the form of take-or-pay relief and contract reformation. The resulting lower gas costs benefitted Northern's customers to a much greater extent than the ad valorem tax add-on.

Northern's Answer

14. Northern agrees with Burlington that there is no reason to have a hearing to decide Burlington's legal issues. The Commission should resolve this matter without an evidentiary hearing.

15. Northern asserts that Burlington's defense to its liability for the refund based on the 1989 take-or-pay settlement has no merit since the Commission has ruled that such a settlement has no application to the ad valorem tax refund liability of the first seller/producer.

16. Northern cites to Williams, where the Commission stated:

To the extent producers are required to make refunds ... of amounts charged in excess of ceiling prices, they must make such refunds regardless of any agreement by their customers to pay amounts in excess of the ceiling price.⁹

17. Northern argues that again in Anadarko, the Commission reiterated that a release provision between a producer and a pipeline does not relieve the first seller of its liability to refund any NGPA overcharge. The Commission explained:

⁹67 FERC at 61,450.

Anadarko, as the first seller, is responsible for paying the refund. Anadarko's reliance on the release in the 1986 Spin-Off Agreement to refund the overcharge is misplaced. Whatever the parties intended by that release, it cannot relieve the first seller of the obligation to refund an NGPA overcharge, because the buyer and a first seller cannot agree to pay more than the MLP, which would be the effect that Anadarko seeks.¹⁰ (emphasis added)

18. Northern asserts that on rehearing in Anadarko the Commission reaffirmed that ruling because such an agreement by a pipeline to be responsible for a producer's Kansas ad valorem tax refund liability would be illegal and unenforceable, stating:

[A]n agreement by the buyer, here Northern, to be responsible for any refund would be in effect an illegal agreement to pay more than the MLP, and thus unenforceable.¹¹

19. Northern also argues that Burlington mischaracterizes the 1989 settlement in asserting that the settlement released Southland from any refund obligation. Northern asserts that it did not agree in such settlement to allow Southland to keep amounts in excess of the MLP, or to release or indemnify Southland from its Kansas ad valorem tax refund liability for amounts received in excess of the MLP.

Burlington's Answer to Northern's Answer

20. Burlington asserts that there is no merit to any of the arguments Northern raises in support of its position that it is not responsible for the refund of Kansas ad valorem tax reimbursements paid to Burlington's predecessor, Southland. Northern's first argument was that the settlement with Southland did not provide that Northern would allow Southland to keep amounts in excess of the MI or to release or indemnify Southland from its Kansas ad valorem tax refund liability. Burlington contends the indemnity clause covers all claims relating to the gas contract, the ad valorem refund arises from these gas contracts, and there is no basis to exclude the refund claim from the clause's operation.

¹⁰85 FERC at 61,331.

¹¹86 FERC at 61,158.

21. Northern's next argument was that even if it had agreed to release and indemnify Burlington from refund of MLP violations, such as the receipt of Kansas ad valorem tax reimbursements, the provision is unenforceable because Public Service Company of Colorado v. FERC, 91 F.3d 1478 (D.C. Cir. 1996) requires that producers must refund any amount they had received in excess of the MLP. In response Burlington asserts that the Commission approved Northern's settlement with producers¹² under which ad valorem tax refund claims against producers were either entirely eliminated or reduced and the only consideration for the settlement was the agreement by producers to forego further legal challenges against the claims. Accordingly, Burlington contends there is no reason why the indemnity clause in a take-or-pay settlement should not be given effect.

22. Finally, Northern had asserted that Commission precedent provides that any agreement for a pipeline-purchaser to be responsible for a producer-seller's Kansas ad valorem tax refund liability is prohibited under the NGPA, and cited Williams and Anadarko. Burlington maintains that the precedent does not apply here since the Commission has never directly addressed the question whether such provisions are enforceable in the context of an arm's-length, omnibus contract settlement providing for settlement of take-or-pay claims, contract reformation, and mutual releases and indemnification.

23. Burlington states that the quote in Williams was merely dicta, since there was no agreement, and was made in connection with a prudence challenge to the take-or pay settlement, and not to the claim by a producer that it had no ad valorem liability. It also contends that since Anadarko did not involve an arm's-length agreement, and there was no consideration given to the buyer for the indemnity clause as there is here, it is not controlling. Accordingly, neither case requires that the Commission not give effect to the indemnity clause in the settlement.

Discussion

24. Both parties agree that there are no factual issues involving Burlington's ad valorem refund liability, but only whether a 1989 take-or-pay settlement relieves Burlington of that liability. In view of this agreement, the Commission will remove Burlington from the hearing established by the January 2 order and decide the issue in this order.

¹²93 FERC ¶ 61,311 (2000).

25. At the outset, the Commission questions whether the clause Burlington relies upon has the meaning Burlington attributes to it, namely that it indemnifies Burlington for any ad valorem tax refund liability and imposes that liability upon Northern. However, the Commission need not determine that, because even if the clause could be read as having that meaning, Burlington cannot prevail on its request to be relieved of the ad valorem refund liability.

26. The issue presented is whether a purported "indemnity" clause in a 1989 settlement relieves Burlington of the ad valorem refund liability, which it admits is owing. Burlington argues that under the settlement, the pipeline purchaser, not Burlington, must pay the refund. Commission precedent in Williams and Anadarko is clearly contrary to Burlington's position. The Commission stated in Anadarko that the buyer in a first sale cannot agree "to pay more than the MLP," and thus any agreement to do so "is unenforceable."¹³

27. Moreover, in Williams, the Commission expressly addressed the issue of whether a pipeline's settlement with producers resolving take-or-pay liabilities and reforming gas sales contracts, could relieve those producers of the liability for ad valorem tax refunds relating to those contracts. In Williams the pipeline sought to recover the costs of certain take-or-pay settlements with producers. A state commission argued that it could not evaluate the prudence of the settlements because the settlements might have relieved producers of their ad valorem tax refund liability to the detriment of the pipeline's customers who would have received those refunds. The Commission rejected that argument, stating:

To the extent producers are required to make refunds in [the ad valorem tax refund] ... case of amounts charged in excess of ceiling prices, they must make such refunds regardless of any agreement by their customers to pay amounts in excess of the ceiling price. Thus, take-or-pay or GSR settlements between pipelines and their producer/suppliers cannot interfere with refunds required by the Commission to remedy violations of NGPA ceiling prices, or with the flowthrough of such refunds by the pipelines to their customers.¹⁴

¹³86 FERC at 61,158.

¹⁴67 FERC at 61,450.

Consistent with Williams, the Southland settlement at issue here could not relieve Burlington of its obligation to make ad valorem tax refunds to the pipeline.

28. Burlington also argues that the indemnity clause here did not require Northern to pay more than the MLP. However, giving the clause the effect that Burlington seeks, results in that very outcome because the producer will be permitted to retain the excess over the MLP.

29. Burlington claims that there is no statutory prohibition against a pipeline contractually assuming a liability of a producer. It contends that here in enforcing the indemnity clause the pipeline would be required to refund any ad valorem tax amount to the consumer on behalf of the producer, and the legislative intent of the NGPA would be fulfilled because the consumer receives the refund. Further, Burlington points out that the Commission allowed two pipelines to retain the ad valorem tax refunds paid to them, rather than flowing them through to their customers based upon settlements with the customers in which the customers had relinquished their right to any flowthrough by the pipeline of ad valorem tax refunds. Burlington argues that since the Commission has found that consumers, i.e., the intended NGPA statutory beneficiary, are bound by their contractual settlement agreements with pipelines giving up the right to any refund the pipeline recovered, so too the pipeline should similarly be bound by its contractual agreement with the producer regarding that refund.¹⁵

30. There is a bar to the first sale buyer agreeing to pay more than the MLP, since Section 504(a) of the NGPA makes it "unlawful for any person (1) to sell natural gas at a first sale price in excess of any applicable maximum lawful price under this Act..."¹⁶ Clearly, the cases cited by Burlington are irrelevant because the MLP applies only to the first sale, and those cases only involved the pipeline's flowthrough of the refund. The pipeline flowthrough of the refund is governed by the NGA, which does not provide any Congressionally-mandated MLPs. Therefore, whether the consumer can waive the ad valorem tax refund by settlement raises other considerations than those present here. Similarly, that the Commission has approved uncontested settlements between producers and pipelines and their customers, that waived part of the ad valorem tax refund to resolve disputes over the claims, has no application here, since under those settlements producers

¹⁵Burlington cites El Paso Natural Gas Co., 85 FERC ¶ 61,003 (1998); Natural Gas Pipeline Co. of America, 85 FERC ¶ 61,004 (1998); and ANR Pipeline Co., 85 FERC ¶ 61,005 (1998).

¹⁶15 U.S.C. § 3414(a).

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agreed to immediate payment of a substantial part of the refund in dispute. Here Burlington does not dispute the amount of the refund claim, but seeks to be relieved of the entire amount of the refund, and Northern objects to Burlington's request.

31. We also deny Burlington's alternative request that it should be relieved of any obligation to pay interest. This is a collateral attack on the Commission's orders in Public Service, supra, which denied the producers' generic request for a waiver of interest. As the Commission has explained, interest represents the time value of the excess amount received, and we see no reason to deviate from that ruling here.

32. Finally, we deny the request for relief under Section 502(c) since Burlington has not shown that payment of the refund would be a hardship or inequity. It merely reiterates the same argument why it should not be liable for the refund, which argument we have rejected.

The Commission orders:

(A) Burlington's request for rehearing or alternative relief is denied.

(B) Burlington is removed as a party in the hearing established in the January 2, 2003 order.

(C) Burlington must pay Northern the ad valorem tax refund within 30 days of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.