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Administrative Law: Primary Jurisdiction...F.P.C.

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ADMINISTRATIVE LAW: PRIMARY JURISDICTION . . . F.P.C.

As a result of two cases decided the same day in the United States Court of Appeals, 5th Circuit,[1] the Federal Power Commission has been called upon for the first time[2] to decide whether or not it has jurisdiction, under the Natural Gas Act,[3] over payments of gas royalty under an oil and gas lease. The court held that the question is one for the Commission's primary jurisdiction.

J. M. Huber Corporation v. Denham[4] was an action by natural gas lessors for damages on the ground that the corporate lessee had breached and was continuing to breach contractual obligations under royalty clauses of three leases. The trial court found for the plaintiffs. On appeal, it was held that the evidence sustained the finding that the terms "market price" and "market value" in the leases were intended in their ordinary sense and not as synonymous with or identical to proceeds received by the lessee-producer under its contract with its pipeline purchaser and that it was appropriate for the Federal Power Commission rather than the Court of Appeals to initially determine jurisdiction of the Commission over royalty payments. The case was affirmed in part and remanded in part.

Unlike *Huber, Weymouth v. Colorado Interstate Gas Company*[5] involved an action between a landowner-lessor and a lessee-producer who was also the purchaser of the gas for resale in interstate commerce. Grounds for the action were that royalty payments for gas taken did not come up to "market value" which the lessors were to be paid under their lease and that the lessee under-produced the lease by failing to exercise diligence in marketing gas available from the lease. After a verdict for the lessors on the underproduction question and for the lessee-producer on

[1] J. M. Huber Corp. v. Denman, 367 F.2d 104 (5th Cir. 1966); Weymouth v. Colorado Interstate Gas Co., 367 F. 2d 84 (5th Cir. 1966).

[2] *See* two isolated exceptions: *In re* Northern Natural Gas Producing Co. (unreported) 6 Oil and Gas Reporter 538 (1956); *In re* Elk River Coal & Lumber Co. (unreported) 6 Oil and Gas Reporter 538 (1956).

[3] The Natural Gas Act, 15 U.S.C. § 717 (1952).

[4] J. M. Huber Corp. v. Denman, *supra* note 1.

[5] Weymouth v. Colorado Interstate Gas. Co., *supra* note 1.

the "market value" question, a partial new trial was granted for evidentiary reasons. There the jury returned a verdict which increased the amount of the lessor's judgment. The lower court decision was affirmed on the question of market value but reversed on the question of underproduction for lack of evidence. The court, holding that a sale of gas for resale in interstate commerce must be examined in the light of the practical realities of the gas industry, ruled that, as in *Huber*, the question as to whether the F.P.C. has jurisdiction over payments of royalty must first be ruled on by the Commission.

"Primary Jurisdiction" applies where a claim is originally cognizable in the courts, and comes into play whenever enforcement of the claim requires the resolution of issues which, under a regulatory scheme, have been placed within the special competence of an administrative body for its views.[6] It has effectively been used to secure a prior determination by an agency, acting under a regulatory authority, of the scope and meaning of the statute so that a court can better apply the statute to the circumstances of a particular case.[7]

The doctrine of primary jurisdiction has developed to a great extent in transportation cases, antitrust cases, and N.L.R.B. cases and has grown significantly with the development of administrative law. The 5th Circuit has ordered primary jurisdiction reference with respect to the legal validity of tariffs,[8] questions involving the interplay of the Interstate Commerce Act and the Agricultural Marketing Act,[9] and the question of whether the validity of a tariff is justification for action claimed to violate the antitrust laws.[10]

Factors involved in determining that an agency should exercise primary jurisdiction are securing uniformity and consistency

[6] U.S. v. Western Pac. R.R., 352 U.S. 59, at 63-64 (1956).

[7] Federal Maritime Bd. v. Isbrandsten Co., 356 U.S. 481 (1958).

[8] Southwestern Sugar & Molasses Co. v. River Terminals Corp., 360 U.S. 411 (1958).

[9] Agricultural Trans. Ass'n. v. King, 349 F.2d 873 (5th Cir. 1965); Louisville & Nashville R.R. v. Knox Homes Corp., 343 F.2d 887 (5th Cir. 1965).

[10] Carter v. Am. Tel. & Tel. Co., 365 F.2d 486 (5th Cir. 1966).

in the regulation of business entrusted to a particular agency and more rationally exercising the limited functions of review by the judiciary.[11] The purpose of the doctrine is not to divide powers between courts and agencies but only to determine which tribunal should take initial action.[12]

Where the real question is the scope of the agency's authority, it is well established that an agency has jurisdiction to make the determination.[13] N.L.R.B. cases have held that if a labor dispute is "arguably" subject to the jurisdiction of the N.L.R.B. then the courts are not free, without a prior board determination, to determine the question of whether the dispute is beyond the power of the Board.[14]

The Federal Power Commission for sixteen years did not extend its jurisdiction to producers of natural gas, but in *Phillips Petroleum Co. v. Wisconsin,*[15] extended its jurisdiction to cover the rates received by producers who sold their gas for resale in interstate commerce. The *Phillips* case in broad terms recognized F.P.C. jurisdiction "over the rates of all wholesales of natural gas in interstate commerce, whether by a pipeline company or not and whether occurring before, during or after transmission by an interstate pipeline company."[16]

Since the producers of natural gas, who sell their gas to inter-

[11] *See* Far East Conference v. U.S., 342 U.S. 570 (1952); U.S. Navigation Co. v. Cunard S.S. Co., 284 U.S. 474 (1932); Keogh v. Chicago & N.W. Ry., 260 U.S. 156 (1922). *Contra,* Georgia v. Pennsylvania R.R., 324 U.S. 439 (1945).

[12] Best v. Humboldt Placer Mining Co., 371 U.S. 334 (1963); General Am. Tank Car Corp. v. ElDorado Terminal Co., 308 U.S. 422 (1940).

[13] FPC v. Ark. Power and Light Co., 330 U.S. 802 (1947); Sunshine Anthracite Coal Co. v. Adkins, 310 U.S. 381 (1940); Texas & Pac. Ry. v. Abilene Cotton Oil Co., 204 U.S. 426 (1907); U.S. v. Sing Tuck, 194 U.S. 161 (1904).

[14] Local 438 Constr. Union v. Curry, 371 U.S. 542 (1963); Incres S.S. Co. v. Int'l Maritime Workers Union, 372 U.S. 24 (1963); Marine Engineers Beneficial Ass'n v. Interlake S.S. Co., 370 U.S. 173 (1962); San Diego Building Trades Council v. Garmon, 359 U.S. 236 (1959); Myers v. Bethlehem Shipbuilding Corp., 303 U.S. 41 (1938).

[15] Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954).

[16] *Id.* at 682.

state pipeline companies, by far outnumber their purchasers, one result of the *Phillips* case was to add heavily to the case load of the Commission. The Commission amended its rules to specifically include an "independent producer."[17] Now each operator of a producing unit is required to file a rate schedule and an application for a certificate of public convenience and necessity on its own behalf, on behalf of all non-operators who are signatory parties to a gas sales contract but do not wish to file their own rate schedule, and on behalf of all non-operators who are not signatory parties to a gas sales contract covering their interest in the gas, before one cubic foot of gas is allowed to be delivered from that unit into interstate commerce.

It has been held that Congress "meant to create a comprehensive and effective regulatory scheme" in enacting the Natural Gas Act,[18] and that when Congress enacted the Natural Gas Act, it was motivated by a desire "to protect consumers against exploitation at the hands of natural gas companies."[19] The Supreme Court has upheld the Commission's extension of jurisdiction to cover not only direct sales of natural gas for resale in interstate commerce, but also sales of gas which is commingled with gas sold for resale in interstate commerce.[20]

The lessors in *Huber* made a strong argument based on the contention that there can be no "sale of gas by royalty owners since they have no gas to sell."[21] They argued that as the gas leaves the wellhead, the entire ownership of the gas is in the lessee and that at this point a simple debtor-creditor relationship exists between a lessee-producer and the lessors.[22]

[17] 18 C.F.R. § 154.91 (1956, Supp. 1966) Regulations Under the Natural Gas Act.

[18] *See* United Gas Improvement Co. v. Continental Oil Co., 381 U.S. 392, at 400 (1965); Federal Power Comm'n v. Texaco Inc., 377 U.S. 33 (1964); and Sunray Mid-Continent Oil Co. v. FPC, 364 U.S. 137 (1960).

[19] Panhandle Eastern Pipe Line Co. v. Public Service Comm'n, 332 U.S. 507, at 520 (1947).

[20] California v. Lo-Vaca Gathering Co., 379 U.S. 366 (1965); FPC v. Amerada Petroleum Corp., 379 U.S. 687 (1965).

[21] J. M. Huber Corp. v. Denman, *supra* note 1, at 113.

[22] Theisen v. Robison, 117 Tex. 489, 8 S.W.2d 646 (1928). *See also*

However, since the decision in *United Gas Improvement Co. v. Continental Oil Co.,*[23] the Supreme Court has made it clear that neither the form of the transaction nor the peculiarities of state law are controlling in determining whether there is a jurisdictional sale under the Natural Gas Act. Even though the sale was consummated before the gas left the ground and consideration for the sale was a lump sum price, the Supreme Court held that it was a "sale" under the Act. This result was necessary to prohibit an apparent means of circumventing regulation.

Royalty has been treated by the Commission as a significant cost in its Area Rate Proceedings.[24] *Huber* and *Weymouth* both leave open the possibility of a distinction between royalty paid on the basis of the proceeds the producer receives for his gas and the "market price" or "market value" of the gas. If the producer were required to pay royalty on a basis other than the proceeds he received for gas sold in interstate commerce, his costs of producing gas would be significantly increased and either would have to be absorbed by the producer or permitted by the Federal Power Commission to be passed along to the pipeline purchaser and, eventually to the consumer. A very pertinent example is a producer selling what the Commission has termed "old gas" by reason of its being contracted before a designated cut-off date in an area where the Commission permits gas committed to contract more recently to be sold at a price six cents per thousand cubic feet higher. Such an area is the Oklahoma panhandle. The producer, limited to selling his gas at a rate of eleven cents per thousand cubic feet, but required to pay royalty on the basis of a seventeen cents per thousand cubic feet "new gas" rate as the "market value" would be under a definite economic burden.

If the Commission took this cost factor into consideration and permitted a higher rate for the gas, the probable result would be

Phillips Petroleum Co. v. Bynum, 155 F.2d 196 (5th Cir. 1946); Phillips Petroleum Co. v. Johnson, 155 F. 2d 185 (5th Cir. 1946); Elliff v. Texon Drilling Co., 146 Tex. 575, 210 S.W.2d 558 (1948).

[23] United Gas Improvement Co. v. Continental Oil Co., 381 U.S. 392 (1965).

[24] Area Rate Proceeding (Permian Basin), 34 F.P.C. 159 (1965). *See also In re* Phillips Petroleum Co., 24 F.P.C. 537 (1960); *cf.* Wisconsin v. FPC, 373 U.S. 294 (1963).

higher gas prices to the consumer. Due to the potential impact on the consumer it is not unforeseeable that the Commission could extend its holding in the *Phillips* and *Rayne* cases to hold jurisdictional the amount of royalty payments by lessee-producers selling their gas for resale in interstate commerce. Such a holding would be consistent with the regulatory purpose of protecting the consumer.

Should the Commission decline to assert jurisdiction over royalty payments, the cost impact on the lessee-producer may be even heavier. Royalties based on "market value" in the *Huber* case would net the lessor an amount in excess of 95% of the total proceeds received by the F.P.C.-regulated lessee-producer.[25] Costs of this magnitude would reduce the incentive to search for new gas reserves and the development of known reserves. A lack of gas reserves might defeat the Commission's purpose of protecting the consumer. Although in negotiating future leases the lessee-producers will undoubtedly attempt to avoid use of the "market value" provision for payment of royalty, that precaution cannot be of help to the immediate problem where millions of productive acres are covered by leases providing for payment of royalty at "market value" or "market price."

The holdings in *Huber* and *Weymouth* are not inconsistent with the trend in the development of the doctrine of primary jurisdiction, but are significant as they extend the application of the doctrine into the area of natural gas regulation. They open the possibility for an expansion of the Federal Power Commission's exercise of jurisdiction which may be of greater impact than even the *Phillips* decision because just as producers outnumber pipeline companies, royalty owners greatly outnumber producers. The result would be to place an unprecedented case load on the Commission and may in itself be a reason for the Commission's denying jurisdiction. The added case load would undoubtedly further delay the granting of producer and pipeline certificates, again adding to the costs to the producer in selling its gas and to the pipeline in purchasing gas to fulfill consumer demands.

In view of the complex nature of the problems raised in *Huber* and *Weymouth*, the 5th Circuit's decision to refer the

[25] J. M. Huber Corp. v. Denman, *supra* note 1, at 110.

cases to the Commission's expertise is a particularly sound extension of the application of the doctrine of primary jurisdiction. As stated by the court, both cases involve both public and private interests. The impact of the decision will affect a large cross-section of the economy and, by its nature, necessitates an experience in dealing with the natural gas industry and a flexibility of procedure well suited to the nature of the Commission.

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