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FERC Rejects Marketing Affiliate Petition

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Can a marketing affiliate of an oil pipeline purchase transportation at the filed tariff rate and then re-sell this capacity at a lower, non-public rate without running afoul of the Interstate Commerce Act's prohibition on rebates? On November 22, 2017, the Federal Energy Regulatory Commission ("FERC") issued an order that addressed this very issue.

One year ago, Magellan Midstream Partners, L.P. ("Magellan") filed a petition for declaratory order at FERC seeking FERC's opinion on several structures involving a to-be-created marketing affiliate. This marketing affiliate would facilitate movements on Magellan's system by purchasing capacity on Magellan's system and transporting product (including third party product) at price differentials between origin and destination markets that may be different from Magellan's filed tariff rates. Magellan suggested that a marketing affiliate could increase utilization of the system, provide flexibility for producers and markets, and increase access to the pipeline, while improving the revenues of the pipeline's integrated corporate system. Such benefits could accrue even though the marketing affiliate would lose money on a given transaction by paying Magellan the filed tariff rate, but charging the marketing affiliate's counterparty a lesser rate. Magellan's petition drew significant industry attention.

FERC generally denied the petition, but at the outset it confirmed that an oil pipeline may create a marketing affiliate without FERC authorization, that a marketing affiliate may ship on the affiliated pipeline, and that FERC's ICA jurisdiction does not extend to the sales of petroleum products. *Magellan Midstream Partners, L.P.*, 161 FERC ¶ 61,219 at PP 12-13 (2017). However, FERC found that Magellan's proposed transactions would run afoul of the ICA's prohibition on giving special rates or rebates to any particular shipper. FERC explained that it has not been previously faced with the contemplated structure as described by Magellan. It concluded that such transactions would violate the prohibition on rebates where the pipeline would subsidize its marketing affiliate's losses in the transactions because the ICA prohibits any and all means or devices that result directly or indirectly in a rebate from the filed tariff rate. FERC stated that as proposed by Magellan, the marketing affiliate is essentially offering capacity below cost, equating the below-cost offering with an unlawful rebate. FERC also clarified, however, that the ICA does not prevent a marketing affiliate from shipping "where the price differential equals or exceeds the filed tariff rate."

Besides illegal rebates, FERC offered several additional explanations of how the proposal would violate the ICA:

- First, FERC stated that Magellan's proposed transaction could constitute circumvention of the ICA requirement that all rates must be subject to FERC's review under the just and reasonable standard. FERC noted that the proposal would preclude FERC from being able to review the reasonableness of the actual rates for transportation being offered by the pipeline.

- Second, FERC suggested that the proposal could violate the ICA's anti-discrimination provisions by offering pipeline transportation pursuant to customized terms, conditions, and rates unavailable to shippers who ship directly with the pipeline.

- Finally, FERC indicated that the proposal appeared to seek permission to refrain from publishing the arrangements between the pipeline and the affiliate, suggesting that the proposal would circumvent the ICA obligation to publish all rates for transportation.

FERC stated that the ICA's prohibition on rebates is not a blanket restriction on integrated company financing, which FERC said was an issue for ratemaking and accounting. FERC did not rule on the propriety of dividends being paid to an affiliated shipper of a common carrier, as this issue was simply not raised in the petition.

While FERC's order rejected Magellan's specific proposal, the broader implications of the order are less clear, and the industry should be cautious of overly broad interpretations. FERC's pronouncements in the order must be considered within the particulars of a given transaction or structure.

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