

**IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT**

Nos. 04-73650 & 04-75240

CALIFORNIANS FOR RENEWABLE ENERGY, INC.

&

CALIFORNIA PUBLIC UTILITIES COMMISSION

Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION

Respondent.

On Petition for Review of an Order of the Federal Energy Regulatory Commission
FERC Docket Nos. CP04-58-000 and CP04-58-001

**REVISED* REPLY BRIEF OF PETITIONER
CALIFORNIA PUBLIC UTILITIES COMMISSION**

Dated: May 3, 2005

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(dated April 13, 2005) pursuant to
this Court's April 20, 2005 Order

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INTRODUCTION

This case is not about the need for liquefied natural gas (“LNG”) facilities. The California Public Utilities Commission (“CPUC”) agrees that new LNG terminals are needed, and has an ongoing rulemaking which is addressing many issues in order to ensure access onto the CPUC-regulated intrastate pipelines for the natural gas from LNG facilities. ER 054. There are numerous proposed LNG projects which could provide natural gas to California (ER 054 n.3), and, as discussed below, there are considerably more proposals to serve California and all of North America than the market could ever support.

The regulatory mission of the CPUC in the energy area is to ensure:

- (1) reliable utility service, which requires sufficient supplies of natural gas;
- (2) reasonable prices for that service, which is affected positively by increasing supplies but also negatively by withholding them (as California’s energy crisis so harshly demonstrated just four years ago); and (3) the safety of the utility’s operations, which is significantly affected by the siting of the utility’s facilities.

The Federal Energy Regulatory Commission’s (“FERC”) orders challenged herein seek to divest the CPUC of the ability to achieve this balance.

What is before this Court and what this case is about is the law. It centers on the Natural Gas Act (“NGA”), 15 U.S.C. §§ 717-717z, in which Congress’ primary purpose was to “protect consumers against exploitation by natural gas companies”

by supplementing state regulation with federal regulation over the market served by interstate pipelines. *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 609-10 (1944). The NGA “was designed to take ‘no authority from State commissions.’” *Id.* at 610.

FERC, whose authority is derived from statutes, must follow them.¹ In the present case, FERC seeks to take away the CPUC’s authority in order to prevent the CPUC from protecting California citizens from the potential hazards of Sound Energy Solutions’ (“SES”) proposed LNG facilities at the Port of Long Beach and from SES’s potential exercise of market power.

The other briefs, supporting FERC and challenging the role of the CPUC and all other states in LNG safety and market power matters, are filed by SES and other intervenors (collectively “SES”), and by *Amici Curiae* Interstate Natural Gas Association of America (“INGAA”) and Natural Gas Supply Association (“NGSA”) (collectively “INGAA”). These are the very companies from whom state laws and the NGA were enacted to protect consumers. Although FERC, SES and INGAA (collectively “FERC, *et al.*”) may prefer FERC’s authority to occupy the full field of the Commerce Clause, the language in the NGA was “meticulous” to occupy only a limited territory involving sales and transportation in interstate

¹ References to “FERC” herein are to the Federal Energy Regulatory Commission, its predecessor, the Federal Power Commission, and/or the term “Commission” as it is used in the NGA, unless otherwise specified.

commerce, as reflected in section 1(b), 15 U.S.C. § 717(b), the “coverage section” of the NGA. *Panhandle E. Pipeline Co. v. Pub. Serv. Comm'n of Indiana*, 332 U.S. 507, 516-24 (1947).

In the siting and enforcement of safety requirements for intrastate LNG facilities, state commissions, such as the CPUC, are also provided a major role under certain sections of the Natural Gas Pipeline Safety Act, as amended (“NGPSA”). *See* 49 U.S.C. §§ 60103, 60104(c), 60105, 60117(h)(3).

In complete defiance of the NGA and NGPSA’s respect for and preservation of the states’ role on the safety and economic issues, FERC, *et al.* base their arguments upon implying words in the NGA and silence in its legislative history in order to construe the NGA in derogation of its actual language. As the Supreme Court stated in *Panhandle E. Pipeline Co.*, 332 U.S. at 519:

It would be an exceedingly incongruous result if a statute [the NGA] so motivated, designed and shaped to bring about more effective . . . state regulation, were construed in the teeth of those objects, and the import of its wording as well, to cut down regulatory power . . . making the states less capable of regulation than before the statute’s adoption.

ARGUMENT

At issue here is FERC’s interpretation of the NGA, 15 U.S.C. §§ 717-717z, and FERC’s conclusion that section 3 of that NGA, 15 U.S.C. § 717b, gives FERC exclusive jurisdiction to determine the siting and operation of the LNG facility that SES wants to construct. This Court must reject an agency’s interpretation of a

statute if “the statute unambiguously forbids the Agency's interpretation, and, if not, (2) whether the interpretation, for other reasons, exceeds the bounds of the permissible.” *Barnhart v. Walton*, 535 U.S. 212, 218 (2002); *see generally Chevron U.S.A., Inc. v. NRDC*, 467 U.S. 837, 842-43 (1986). Such is the case here.

- Section 1(b) of the NGA expressly prohibits FERC from regulating facilities, such as those here, that do not involve interstate commerce.
- Section 3(c) expressly prohibits FERC from using its conditioning authority – the sole basis in the NGA that putatively supports FERC’s position – to regulate LNG import facilities.
- And even if these two provisions did not put an end to the question, as they must under *Chevron*, none of FERC’s many attempts, to show that its assertion of authority over LNG import facilities somehow is reasonable is, in fact, itself reasonable.

At best FERC, *et al.*’s answering briefs amount to an extended argument that the statute should be construed, no matter how strained the construction, to conform to what FERC contends is a desirable policy. As detailed below, not only are FERC, *et al.*’s policy arguments predicated upon conjecture and lacking in any factual basis, but an agency’s view of what constitutes a desirable policy cannot trump the language and purposes of a statute itself. As the Supreme Court stated in

Barnhart v. Sigmon Coal Co., Inc., 534 U.S. 438, 461-62 (2002), the court’s “role is to interpret the language in the statute enacted by Congress. . . . We will not alter the text to satisfy the policy preferences of [an agency].”

I. Section 1(b) of the NGA Forbids FERC to Regulate Facilities That, as Here, Are Not Involved in Interstate Commerce

FERC looks to section 3 of the NGA as the exclusive source of its authority over the siting and operation of natural gas facilities used involved in foreign commerce. *See* FERC Br. 24-32. Fatal to that position is FERC’s failure to address the effect of section 1(b), the coverage section of the NGA, on the scope of section 3.

FERC concedes that the facilities at issue here do not involve the transportation or sale of natural gas in interstate commerce. FERC Br. 23. In light of the fact that the proposed facilities would be wholly intrastate, however, and regardless of the authority that section 3 might otherwise give FERC, section 1(b), in the words of *Barnhart*, “unambiguously forbids” FERC’s position. Specifically, section 1(b) makes clear that the provisions of the NGA, including section 3, apply *only* to the transportation and sale of natural gas in interstate commerce, and – to make sure there is no room for ambiguity – explicitly prohibits FERC from exercising jurisdiction over facilities that do *not* involve the transportation and sale of natural gas in interstate commerce:

The provisions of this chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas ... and to natural-gas companies engaged in such transportation or sale, ***but shall not apply to any other transportation or sale of natural gas***

15 U.S.C. § 717(b) (emphasis added). This language is unambiguous. As the Supreme Court explained in reference to section 1(b), “Congress made sure its intent could not be mistaken.” *Panhandle E. Pipeline Co.*, 332 U.S. at 516; *see also United Gas Pipe Line Co. v. FPC*, 385 U.S. 83, 86-87 (1966) (facilities subject to FERC’s jurisdiction require transportation and sales in interstate commerce).

Nothing in FERC’s brief addresses, or otherwise calls into question this conclusion. For example, *Distrigas Corporation v. FPC*, 495 F.2d 1057 (D.C. Cir. 1974), FERC’s and SES’s main source of authority for arguing that section 3 authorizes FERC regulation of facilities used for transportation in foreign commerce, involved *interstate* and intrastate transportation of gas. *See id.* at 1058. Thus, *Distrigas* never addressed the effect of section 1(b), which prohibits FERC jurisdiction where there is no interstate commerce, on whatever authority FERC might derive from section 3. Moreover, no authority cited by FERC or SES overrules or call into question *United Gas*, where the Supreme Court made clear that FERC’s authority does not extend to facilities, like the SES facility at issue here, that do not involve interstate commerce. *See United Gas*, 385 U.S. at 86-87.

SES argues in a footnote that section 1(b) merely governs FERC jurisdiction over facilities used in interstate commerce, and section 3 governs FERC regulation over foreign commerce, as if section 1(b) has no relationship to section 3. SES Br. 20-21, n.22. SES's argument is contrary to the language in these sections. Section 1(b) starts out with the words, "The provisions of this chapter shall apply to," 15 U.S.C. § 717(b), showing much broader applicability (*i.e.*, it governs the whole NGA) than SES claims. In contrast, section 3 only discusses exportation or importation, and does not generally discuss foreign commerce, indicating a much narrower applicability than SES claims.²

Significantly, FERC, SES, and INGAA completely ignore the holdings in the two controlling Supreme Court cases regarding how section 1(b) determines the NGA's coverage. *See Panhandle E. Pipeline Co.*, 332 U.S. at 516-19; *United Gas*, 385 U.S. at 86-87; *see generally* CPUC Op. Br. 32-34. FERC is not entitled to any deference on this issue, because under the doctrine of *stare decisis*, these cases represent settled law. *See Neal v. U.S.*, 516 U.S. 284, 295 (1996).

II. Section 3 Does Not Authorize FERC to Regulate LNG Import Facilities

Even if section 1(b) did not foreclose FERC's interpretation, FERC's position still would be foreclosed by the language of section 3, itself.

² In circumstances, such as here, where no interstate commerce is involved, section 1(b) can be harmonized with section 3 by limiting authorization under section 3 to the fact of importation or exportation (which are not prohibited by section 1(b)).

A. Section 3, as Amended by EPAct, Prohibits FERC from Using the Conditioning Clause to Regulate LNG Import Facilities

Relying on *Distrigas*, FERC contends that the conditioning clause in section 3(a), 15 U.S.C. § 717b(a) (formerly the entirety of section 3), gives it authority over facilities involved in the importation of natural gas in foreign commerce. In *Distrigas*, 495 F.2d at 1064, the D.C. Circuit stated that under the former section 3, in addition to simply denying or granting an import application, FERC may grant an import application conditionally, “subjecting it to ‘terms and conditions’ that it finds ‘necessary or appropriate’ to the public interest.” The D.C. Circuit subsequently explained that its decision in *Distrigas* was based upon FERC’s “broad authorization under section 3 to *modify* import authorization as required by the *public interest*,” to regulate construction of LNG import facilities. *West Virginia PSC v. U.S. Dept. of Energy*, 681 F.2d 847, 857 (D.C. Cir. 1982) (emphasis added). FERC has acknowledged that this conditioning/modification authority is the sole basis in the statute for its assertion of jurisdiction over natural gas facilities under section 3. March 24 Order at PP 15, 19, ER 84, 87.

As noted in the CPUC’s opening brief, however, *Distrigas* was decided before Congress enacted the Energy Policy Act of 1992, Pub. L. 102-486, tit. II, § 201, 106 Stat. 2866 (codified as amended 15 U.S.C. § 717b(a)-(c)) (“EPAct”), which amended section 3. In a nutshell, after EPAct, *Distrigas* no longer is good law as to LNG imports, because sections 3(b) and 3(c), added by EPAct,

unambiguously forbid the interpretation of section 3 on which *Distrigas* is based, and on which FERC relies. EAct's amendments explicitly divest FERC of discretion to condition imports of LNG on "modifications" that FERC thinks are in the "public interest":

For purposes of subsection (a), the importation of the natural gas referred to in subsection (b) [which includes liquefied natural gas] ... *shall be deemed to be consistent with the public interest, and applications for such importation or exportation shall be granted without modification or delay.*

15 U.S.C. § 717b(c) (emphasis added). It was precisely, and exclusively, this authority to condition LNG import approvals on such modifications that formed the basis for FERC's assertion of jurisdiction over import facilities that *Distrigas* affirmed.

1. That the EAct amendments do not expressly refer to "facilities" does not create an ambiguity

In an effort to create an ambiguity in the statute where none exists, FERC first contends that the EAct amendments are ambiguous, because they do not expressly enumerate regulation of facilities as one thing over which the EAct amendments withdraw FERC's conditioning authority. It argues that this alleged omission indicates that Congress intended FERC to continue to be able to use its conditioning authority to regulate such facilities. FERC Br. 29. This argument is baseless. The plain language of the amendments prohibits *all* exercise of FERC's conditioning authority with respect to applications to import LNG. Given that

broad and unequivocal ban, there would have been no reason for Congress to have enumerated any specific examples of how that authority may no longer be used. FERC's inference from the lack of any reference in the EPAct's amendments to removing FERC's purported authority in section 3 over the "siting, construction, and operation of LNG import facilities" (FERC Br. 29), is similarly flawed: it is not reasonable to expect that Congress necessarily would even think to include in its amendment to section 3 an express statement that it was eliminating language that did not exist in the statute in the first place.

2. That DOE has some authority over imports does not alter the conclusion that FERC lacks conditioning authority to regulate facilities

FERC next attempts to create a non-existent ambiguity by arguing that the EPAct amendments, restricting conditioning authority, apply only to the Department of Energy ("DOE"), and not to FERC itself. FERC Br. 27-28. Nothing in the language of the statute supports that strained reading, however.

The CPUC does not dispute that the DOE has delegated to FERC authority to impose conditions on imports, pursuant to section 3(a), while retaining for itself other section 3 authority. But the DOE's delegation orders are irrelevant to interpreting the language in subsection 3(a). The DOE's authority over LNG imports is derived from section 3 of the NGA, which was transferred to DOE in 1977 (*see* 42 U.S.C. § 7172(f)), and any delegation of that authority by DOE to any

other federal agency, including FERC, is derived from section 3. The DOE cannot delegate authority that the statute does not confer upon it in the first place. That the DOE may have chosen to delegate to FERC part of what section 3 authorizes “the Commission” to do, does not, and cannot, alter the scope of the authority granted to “the Commission” in section 3(a), and limited by sections 3(b) and 3(c).

FERC contends those parts of section 3 that forbid “the Commission” from using its conditioning authority to modify permit applications somehow pertain only to the DOE’s retained authority to issue import permits, and do not apply to the extent that DOE has delegated other section 3 authority to FERC. Simply reciting this argument demonstrates its unreasonableness. Nothing in section 3 distinguishes between DOE’s authority to impose import conditions and FERC’s authority to do so. Section 3 is a unitary statement of the sole and limited authority that “the Commission” – and by extension, any delegatee of that authority – has. *See CPUC Op. Br. 19-21.*

3. The legislative history of the EAct amendments does not dictate a different conclusion

Lacking any support in the text of the statute for its position, FERC resorts to the legislative history of EAct in an attempt to create an ambiguity. Neither FERC nor this Court, however, may resort to the legislative history to create an ambiguity in the statute when, as here, it is clear on its face. *See Ratzlaf v. U.S.*,

510 U.S. 135, 147-48 (1994); *Patenaude v. Equitable Life Assurance Society of U.S.*, 290 F.3d 1020, 1025 (9th Cir. 2002).

In any event, even if the Court were to look to the legislative history, it does not lend support to FERC's interpretation.

(a) The legislative history's silence regarding FERC's jurisdiction over siting and facilities does not change the plain meaning of the statute

FERC argues that because the legislative history of the EAct amendments does not specifically discuss FERC's alleged jurisdiction over siting and facilities, that silence reflects a congressional intent to acquiesce in and to affirm FERC's pre-EAct practices of regulating siting and facilities. That argument, like the rest, fails as both a matter of fact and a matter of law.

Courts may not assume acquiescence simply from silence in legislative history. *See Schism v. U.S.*, 316 F.3d 1259, 1294-97 (Fed. Cir. 2002). Rather, courts may recognize congressional acquiescence to administrative agencies' practices only with "extreme care," and when there is "overwhelming evidence" of acquiescence. *Solid Waste Agency of Northern Cook County v. U.S. Army Corps of Engineers*, 531 U.S. 159, 169-70 & n.5 (2001). Particularly when, as here, a statute has been changed, silence in legislative history about an administrative agency's purported practice is irrelevant. The agency must follow the new law. *See Ford Motor Co. v. EPA*, 606 F.2d 1293, 1299-1300 (9th Cir. 1979). FERC's

brief does not even address these principles, nor does it cite any evidence, much less overwhelming evidence, of Congress' intent to acquiesce regarding FERC's past exercises of jurisdiction over siting and facilities.

Lorillard v. Pons, 434 U.S. 575 (1978), on which FERC relies, does not dictate a different conclusion. That decision addressed cases where Congress "re-enacts a statute without change." *Id.* at 579-81. Here, EAct did not simply re-enact section 3 without change. It added two new subsections that expressly modified the only pre-existing part of section 3. That EAct did not directly alter the language in subsection 3(a) itself, but instead altered it by via two new subsections that refer to 3(a) (*see* FERC Br. 29) is beside the point.

In any event, even if the Court were to look to FERC's past practice to interpret the statute, it would find no support for FERC's position. At the time of EAct's enactment in 1992, FERC's past practice had not been, as FERC suggests, to use section 3 authority to regulate LNG import facilities. FERC's regular practice had been to authorize all LNG import facilities under section 7 of the NGA, 15 U.S.C. § 717f, even for the LNG import terminal after the remand from *Distrigas*. ER 229-30.³ Indeed, it was not until 2002 that FERC decided to stop relying upon section 7 for this purpose, and instead invoke section 3. ER 230. At

³ *See, e.g., Distrigas Corp.*, 58 FPC 2589, 2592 (1977); *Trunkline LNG Company*, 58 FPC 726, 744 (1977).

the time in 1992 when Congress voted on EAct's amendments to section 3, Congress could not have acquiesced to FERC's purported practice to exercise jurisdiction under section 3 to regulate LNG import facilities, because that was not FERC's past practice.⁴ As noted in the *Amici Curiae* Brief of the Indicated Members of Congress ("Indicated Members of Cong. Br.") at 14, Congress cannot be expected to be constantly aware of agencies' practices.

(b) Congress' concern over environmental protection and safety does not support FERC's interpretation of the statute

FERC next speculates that because the legislative history of the EAct shows that Congress cared about safety and the environment with regard to section 7 certificate proceedings to construct facilities, it is "unlikely" that Congress would want to eliminate section 3 conditioning authority. FERC Br. 32. As previously stated, there is no evidence to support FERC's contentions regarding either

⁴ FERC, *et al.* refer to 18 years of administrative practice prior to EAct (FERC Br. 29) or 30 years of administrative practice (since *Distrigas*) concerning LNG import facilities (SES Br. 4; INGAA Br. 4). However, the only LNG import facilities FERC approved, which were constructed or expanded prior to the EAct's amendments, were based upon section 7, not section 3. ER 229-30. In a few unique cases prior to 1992, such as at an international border crossing, FERC at various times exercised authority over pipeline facilities either under section 3 or section 7 of the NGA and/or pursuant to a Presidential Permit, which is independent of the NGA. *See, e.g. Inter-City Minnesota Pipelines Ltd.*, 29 FERC ¶ 61,105 at 61,208-09 (1984); *Inter-City Minnesota Pipelines Ltd.*, 44 FPC 262 (1970).

Congress' awareness or FERC's practice of exercising authority under section 3 over LNG import facilities.

The EPAct amendments left intact FERC's authority under section 7 to regulate LNG facilities involved in the interstate transportation and sale of natural gas, including ensuring safety and environmental protection. All they did was eliminate FERC's conditioning authority under section 3. And for those LNG facilities – which involve intrastate sales or transportation and pose no interstate threats – EPAct left intact the states' abilities to protect themselves from intrastate environmental and safety effects.

B. FERC's Authority to Permit/Deny Imports Does Not Implicitly Entail Authority over Import Facilities

In an effort to demonstrate that FERC's interpretation of the statute is reasonable, FERC and SES suggest that separate from the conditioning authority (*i.e.*, *Distrigas*' basis for indirect regulation), section 3 authority to approve or disapprove import applications necessarily entails authority to regulate LNG facilities themselves, because imports cannot be accomplished without facilities, and thus imports and facilities are “two sides of the same coin.” FERC Br. 24; SES Br. 9-12 This argument is without merit, for two reasons.

1. FERC's theory conflicts with *Border Pipe Line*

First, this “implied authority” theory is foreclosed by the D.C. Circuit's decision in *Border Pipe Line Co. v. FPC*, 171 F.2d 149, 151 (D.C. Cir. 1948). In

that case, the court recognized that the NGA limits FERC's jurisdiction under section 3 to only the fact of exportation or importation when there is no interstate commerce involved. *See id.* at 150-51. *Border Pipe Line* holds that section 3, the one section of the NGA applicable to foreign commerce, does not include "regulatory measures," which the court identifies as "rates, practices, accounting, facilities and financing." *Id.* Because these regulatory measures are in the other sections applicable only to interstate commerce by virtue of their reference to a "natural-gas company," FERC did not have jurisdiction over *Border Pipe Line's* facilities (*see id.*), and, likewise, does not have jurisdiction over SES's facilities. CPUC Op. Br. 27-28, 38-39.

Distrigas is not to the contrary. In *Distrigas*, 495 F.2d at 1063-64, the court did not find authorization over facilities implied in section 3, and it refused to overrule *Border Pipe Line* (in part because FERC had been unsuccessful on 14 occasions in trying to get Congress to overrule it, *see id.*). Instead the court found that FERC could regulate import facilities only by using its section 3 conditioning authority, as detailed above. In fact, during the 66 years since the NGA was enacted, no court has ever held that FERC's section 3 authority over imports necessarily implies authority over import facilities, or that FERC has any authority over facilities apart from whatever indirect authority it could exercise via section 3's conditioning clause.

FERC cannot simply ignore *Border Pipe Line* without explanation or an attempt to explain why it might be wrongly decided. And that would be difficult to do, not only because *Border Pipe Line's* rationale is so reasonable in terms of the regulatory measures in the NGA all being tied to interstate commerce, but also because its conclusion has been confirmed by this Court. *See Wentz v. U.S.*, 244 F.2d 172, 176 (9th Cir. 1957).

2. FERC's theory conflicts with the structure of the NGA

The basis for FERC's implied authority theory is that LNG importation cannot be accomplished without facilities. FERC Br. 24. It is true that importation cannot be accomplished without facilities. But it does not follow, as FERC suggests, that because FERC has authority to regulate imports, it necessarily must have jurisdiction over facilities utilized to transport the imported LNG or natural gas, as well.⁵

This fundamental flaw in FERC's reasoning is highlighted by other provisions of the NGA. Where Congress intended to give FERC jurisdiction over facilities involved in the interstate sale and transportation of gas, it did so expressly. *See, e.g.*, NGA section 7(c)(1)(a), 15 U.S.C. § 717f(c)(1)(a). Just as natural gas cannot be imported without facilities, so too can it not be transported or

⁵ For example, importation cannot be accomplished without facilities in other countries exporting the LNG, transportation in ships, and, as here, transportation via intrastate pipelines or distribution facilities. FERC has not claimed jurisdiction over these other facilities.

sold in interstate commerce without facilities. Yet Congress did not just assume that FERC's jurisdiction over the interstate transportation and sale of gas necessarily implied jurisdiction over facilities used for those purposes. Congress made that jurisdiction explicit. It is unreasonable to assume Congress would not have been equally explicit in section 3 if Congress had intended section 3 to govern facilities. *See Perdomo-Padilla v. Ashcroft*, 333 F.3d 964, 970 (9th Cir. 2003).

The exclusion does not cause a regulatory gap, because if the imported natural gas will be transported to customers in more than one state, FERC has explicit authorization over the necessary facilities under section 7 of the NGA, 15 U.S.C. § 717f.⁶ If the transportation will occur in only one state, certificate provisions of state law (*e.g.*, Cal. Pub. Util. Code §§ 1001-1005.5) can fill that function.⁷ The NGA was intended to supplement, not supplant, state law. *See Panhandle E. Pipeline Co.*, 332 U.S. at 517.

⁶ In *Border Pipe Line*, 171 F.2d at 151, the court recognized that when a company engages in both interstate and foreign commerce, the regulatory burdens of the Natural Gas Act would apply. Therefore, section 7 can be the basis for FERC's authorization for facilities needed to transport natural gas that is in both foreign and interstate commerce.

⁷ For wholly local facilities necessary to transport the natural gas, the state involved can regulate the intrastate facilities. *See, e.g., Border Pipe Line Co.*, 3 FPC 827, 828 (1942) (FERC authorized export pursuant to section 3 and border crossing pursuant to Presidential Permit, without prejudice to state commission authority over Border Pipe Line).

III. FERC's Interpretation of the NGA Is Unreasonable Because There Is No Regulatory Gap Requiring FERC Jurisdiction

A. The LNG Processed and Regasified in LNG Import Facilities, Such as SES's Proposed Facilities, Is Not in Foreign Commerce

FERC argues that its section 3 authority necessarily includes jurisdiction over import facilities in order to fill a regulatory gap, because those facilities will be transporting LNG or natural gas in foreign commerce, an area over which FERC alleges states have no jurisdiction. FERC Br. 8, 41. This argument is inconsistent with FERC's precedent and court precedent concerning when foreign commerce ends.

1. FERC's conclusion is inconsistent with FERC's own precedent

In *Distrigas Corp.*, 58 FPC 2589, 2592-93 (1977) (the "Remand Order"), FERC held that the foreign commerce involving LNG ended by the time LNG was unloaded from the flange of the ship. This holding was consistent with a previous order, which held that the LNG storage and regasification operations were "separate and separable" from the act of importation. *See Distrigas*, 495 F.2d at 1060. Pursuant to this precedent, the LNG facilities at issue here would only involve LNG in intrastate commerce, because the LNG would leave foreign commerce when it is offloaded from ships in the Port of Long Beach. CPUC Br. 41-43. Although FERC may deviate from its own precedent, its failure to give a

reasoned explanation justifying the deviation requires reversal. *See City of Morgan v. FERC*, 181 F.3d 1155, 1163 (10th Cir. 1999).

FERC's only explanation for its deviation from precedent here is the statement that the LNG import facilities in the present case "would have no other function than to receive LNG and deliver imported gas from the terminal directly into local facilities." FERC Br. 36. FERC never explains, however, why that fact makes a difference to the foreign commerce analysis.

In the present case, SES's storage and vaporization facilities will perform storage and regasification functions after the LNG is unloaded from the ship, just as in *Distrigas*. *See* March 24 Order at P 5, ER 081. The fundamental difference between the facilities at issue there and those at issue here is that in *Distrigas* the LNG facilities were used to serve both interstate and intrastate customers. *See Distrigas Corp.*, 58 FPC at 2592-93. This difference explains why the LNG facilities here – in contrast to those in *Distrigas* – involve only intrastate commerce (and thus why section 1(b) prohibits FERC jurisdiction over them). It does nothing to establish that the natural gas in the facilities remain in foreign commerce.

2. Foreign commerce ends when LNG arrives at facilities which, as here, process and alter the LNG

SES labels its proposed LNG facilities as "instrumentalities of foreign commerce." Then, relying on *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S.

434, 436-37 (1978), it asserts that subjected to this label, the LNG facilities must be in foreign commerce. SES Br. 13-14.

Japan Line, however, is not relevant to the issue before this Court. In contrast to the containers in *Japan Line*, which stayed completely intact throughout their international voyage, SES's proposed intrastate LNG facilities would fundamentally transform all of the LNG into three different types of commodities after substantial processing. Most of the LNG would be converted into natural gas after SES alters the LNG in two ways: (1) by processing the LNG to remove certain natural gas liquids (e.g., ethane, propane, butane), so that it can become pipeline quality (ER 218); and (2) by regasifying it in the vaporizers. ER 007. Some of the LNG will not be vaporized, and will be distributed as liquid fuel in or near the Port. ER 007. Even this LNG would first have to be processed to remove some liquids and then recondensed for vehicle grade fuel. ER 010. In addition, some of the extracted liquids (e.g., ethane) would be separately sold. ER 218. These functions are not import functions, anymore than refining imported crude oil into gasoline at a refinery makes the refinery's functions import functions.

Analogous cases to the present case involve the Robinson-Patman Price Discrimination Act ("RPPDA"), 15 U.S.C. § 13(a), which, like the NGA, does not broadly occupy the Commerce Clause by applying to matters just "affecting"

interstate commerce. Both Acts require the commodities to be transported in interstate commerce (i.e., across state lines). Under the RPPDA, “[c]ourts have generally held that where goods are processed in some substantial way, the flow of commerce ends when they arrive at the place of alteration.” *Zoslaw v. MCA Distributing Corp.*, 693 F.2d 870, 878, n.11 (9th Cir. 1982); *see also Chawla v. Shell Oil Co.*, 75 F. Supp. 2d 626, 647-48 (S.D. Tex. 1999).

Because the LNG would be altered at SES’s proposed LNG facilities and thereafter sold as three different products, the foreign commerce will end at the point the ship has arrived at SES’s facilities. FERC and SES ignore the facts, because they lead to the conclusion that the intrastate LNG facilities will therefore be transporting the LNG and natural gas in intrastate commerce subject to the CPUC’s jurisdiction.

B. Even If the LNG in SES’s Facilities Were in Foreign Commerce, the State of California Would Have Authority to Regulate the LNG Facilities

1. A state’s even-handed regulation of local effects of commerce does not violate the Commerce Clause

Citing *Japan Line*, 441 U.S. at 438, SES claims that regulation of foreign commerce requires uniform national rules, and that states therefore cannot regulate in that area. SES Br.14. This argument, however, is undermined by numerous decisions that hold that states do not impermissibly interfere with foreign commerce when they impose regulations that address the local effects of such

commerce, and that do not discriminate against foreign commerce. *See* CPUC Op. Br. 44-47; *see also* Brief of California Earth Corps 4-5.⁸ SES never addresses the effect of these decisions on its position.

Although FERC and SES assume that states cannot regulate import facilities in their harbors, in reality, this is the classic example of Commerce Clause cases where courts have upheld state regulation on the ground that the use of those facilities produce local effects. *See, e.g., South Carolina State Highway Dept. v. Barnwell Bros.*, 303 U.S. 177, 187-88 & n.5 (1938) (state regulation of harbors, piers and docks have been upheld since beginning of the nation for safety of local area and other reasons); *Duckworth v. Arkansas*, 314 U.S. 390, 394-95 (1941) (“a state may insure the safe and convenient use of its harbors . . . by controlling the movement of vessels in interstate and foreign commerce”); *Huron Portland Cement Co. v. City of Detroit*, 362 U.S. 440, 442-44 (1960) (local effects on environment caused by interstate or foreign commerce are primarily matters of local concern); *Dept. of Revenue of Washington v. Ass’n of Washington Stevedoring Cos.*, 435 U.S. 734, 749 (1978) (state tax on stevedoring, the business of loading and unloading cargo from ships in interstate and foreign commerce but involving local services, upheld); *Barber v. State of Hawaii*, 42 F.3d 1185, 1193-

⁸ On such constitutional matters, there is no deference to FERC under *Chevron*. *See Solid Waste Agency of Northern Cook County*, 531 U.S. at 174.

94 (9th Cir. 1994) (anchorage and mooring rules not “federally sensitive in nature”).

In the present case, the CPUC is concerned with local issues: the siting and safety of the facilities in the close proximity of neighborhoods of two of California’s largest cities, the seismic issues due to the site being proposed on landfill, and the potential market power that SES, a California corporation, could exercise in the Southern California region. ER 108-111. These are local effects occurring only in California and only incidental to the foreign commerce relating to the SES facility. Nothing in the record indicates that the CPUC is less than even-handed in addressing these issues in certificate proceedings. ER 148-49.

It would not be contrary to the Commerce Clause for the CPUC to impose additional safety requirements if the evidentiary record supports such requirements. *See Erie Railroad Co. v. Board of Public Utility Commissioners*, 254 U.S. 394, 410-11 (1921) (state commissions could require safety-related improvements at grade crossings for railroads). If the evidence in the record were to establish that the particular conditions at that site would cause too much of a risk to the health and safety of the nearby businesses and residents, and the CPUC were to reject a certificate at the proposed site without prejudice to a project at an alternative, more remote site, it would not be impermissibly blocking or

prohibiting commerce. *See Bradley v. Public Utilities Commissioners of Ohio*, 289 U.S. 92, 94-96 (1933).

2. Section 1(c) further restricted FERC’s jurisdiction, not the states’ jurisdiction

Because section 1(c) of the Natural Gas Act, 15 U.S.C. § 717(c), which was added in 1954, only exempted from federal regulations certain intrastate transactions, which were in interstate commerce but not in foreign commerce, FERC asserts that FERC still has jurisdiction over the transactions in foreign commerce, and the state does not have such jurisdiction. FERC Br. 8, 41. This argument has no merit.

Section 1(b) has never granted FERC jurisdiction over transactions in foreign or intrastate commerce in the first place. Thus, there would be no reason for a savings clause in section 1(c) to even mention foreign commerce or intrastate commerce.

The purpose of section 1(c) was to further define the limits of FERC's jurisdiction prescribed in section 1(b), consistent with the original intent of the Congress to supplement, and not supplant, state regulation. *See S. Rep. No. 83-817*, at 1-2 (1954), *reprinted in 1954 U.S.C.C.A.N. 2101, 2102*. Congress relied, in part, upon FERC's comments on the bill, which had stated: “No good purpose is seen for the imposition of Federal regulation in addition to that provided under State laws where only one state is affected” *Id.* This restriction on FERC’s

jurisdiction cannot possibly be read to support FERC's claim that it has exclusive jurisdiction over transportation and sales of natural gas in foreign commerce (as distinct from the fact of importation).

C. The NGPSA Supports States' Authority Over LNG Import Terminals

Although FERC's orders never relied upon the NGPSA's definition of LNG facilities, SES argues that the NGPSA definition of an LNG facility as a pipeline facility for transporting or storing LNG "in interstate or foreign commerce," 49 U.S.C. § 60101(a)(14)(A), supports federal jurisdiction over LNG safety, because it allegedly supports that it is an instrumentality of foreign commerce. SES Br. 11-12, n.15. SES is wrong. The definition of "interstate or foreign commerce" in the NGPSA includes commerce that "affects" commerce that crosses a state line. *See* 49 U.S.C. § 60101(a)(8)(A)(ii). Therefore, even if foreign commerce or interstate commerce ended by the time the LNG was unloaded from the ship and intrastate commerce began, the Department of Transportation's ("DOT") safety standards still would apply, because they "affect" the foreign or interstate commerce.

The federal agency issuing the standards is the DOT, not FERC. *See* 49 U.S.C. § 60103. Notwithstanding the breadth of the applicability of the DOT's safety standards under the NGPSA's definition (*i.e.*, "affecting" commerce crossing state lines), the *jurisdictional* provision that defines state authority under the NGPSA, 49 U.S.C. § 60104(c), does not preclude the states from regulating

LNG facilities, even if it is an LNG import terminal that affects foreign commerce. Instead, the NGPSA ultimately categorizes all pipeline facilities, including LNG facilities, as either “intrastate,” which is within a state, or “interstate,” which means facilities subject to FERC’s jurisdiction under the NGA. *See* 49 U.S.C. § 60101(a)(6)(A) & (9)(A). What is significant is this deliberate choice of Congress in the jurisdictional section of the NGPSA, 49 U.S.C. § 60104(c), to cross-reference the NGA’s limited occupation of the Commerce Clause (*e.g.*, natural-gas companies engaged in interstate commerce). In 1979, Congress intended to retain a major role for the states with regard to the LNG safety standards. *See Amici Curiae* Indicated Members of Congress Br. 15-19 (citing legislative history).

In key sections of the NGPSA, as amended in 1979, 49 U.S.C. §§ 60103, 60104(c), 60105, 60117(h)(3), there is no question that Congress intended that the CPUC could regulate the siting and safety of the proposed intrastate LNG import facilities. *See* CPUC Op. Br. 48-51. Indeed, in the legislative history of section 60117(h)(3), the example given of a state proceeding involving the siting of LNG facilities, in which the Secretary of Transportation could intervene to provide expertise, was the CPUC's pending proceeding at that time involving the proposed LNG import terminal at Point Conception, California. ER 164. *See* H.R. Rep. No. 96-201, pt. 1, at 23 (1979).

Quite clearly, there could be state jurisdiction over an LNG import terminal, at least when it does not involve interstate commerce, as here. There was no regulatory gap for FERC to fill.

IV. Even if FERC’s Interpretation of the Statute Were Correct, Its Order Must be Vacated for Lack of Adequate Findings

Even if FERC were correct that section 3 gives it authority to regulate import facilities, FERC’s decision in this case still must be vacated, because the decision lacks the requisite findings. To rely on section 3, FERC must make “more than unadorned assertions that it has exercised its expertise on a particular issue. The findings of fact necessary to the agency’s analysis in decisions must be supported on the record.” *West Virginia PSC*, 681 F.2d at 859. FERC’s determination of the public interest under section 3 must also be consistent with the primary purpose of the NGA, which was to protect consumers against exploitation. *Id.* at 855.

A. FERC’s Findings Are Contrary to the Purpose of the NGA

Despite FERC’s assertion that it must be permitted to regulate import facilities in order to avoid a regulatory gap, FERC’s orders have done nothing in terms of economic regulation to regulate the facilities and close the alleged gap. FERC’s orders merely state it will rely instead upon other federal agencies or, perhaps, it may revisit this in the future, which would first require hearings under section 3. ER 091 at PP 29-30; ER 255-56 at PP 81-82.

FERC has therefore done nothing to protect consumers by regulating SES's facilities. To the contrary, FERC is deregulating them.² Instead, FERC is attempting to regulate the states. ER 090 at P 27 (states should not have to use their resources to regulate LNG facilities); ER 249-50 at PP 68-69 (federal oversight to protect against hypothetical unreasonable barriers by the states.)

Indeed, SES faults the CPUC for asserting jurisdiction over SES, as a California public utility, in order for the CPUC to address potential emergencies, prevent market abuses by SES and prevent mergers where SES would increase its market power. SES Br. 17. FERC rejected the CPUC's authority, because FERC claims to have exclusive jurisdiction, but then it just chose not to use it. FERC Br. 40; SES Br. 17. FERC and SES also contradictorily state that these issues are not ripe, but that FERC is nevertheless correct to preempt the CPUC. *Id.* Because FERC purports to preempt the CPUC's regulatory authority over SES, these issues are ripe even though SES has not yet attempted to exercise market power.

Significantly, SES is not a "natural-gas company" under the NGA. SES Br. 20-21. Neither FERC nor SES has ever pointed to a provision of the NGA that would give FERC jurisdiction over SES as a company or over merger applications, in order to provide a basis for FERC to preempt the CPUC's authority over SES as

² See Indicated Members of Congr. Br. 10-11 (FERC cannot avoid section 7 requirements).

a public utility under California law.¹⁰ Because FERC has no statutory basis to regulate SES as a company, FERC cannot preempt the CPUC's authority over SES's conduct to the extent it attempts to exercise market power or merge to enhance its market power. CPUC Br. 51-55.

FERC is therefore creating a gap by trying to prevent the CPUC from protecting California consumers. FERC's orders are not in accordance with the law, because they are contrary to primary purpose of the NGA, which was to "protect consumers against exploitation by natural gas companies." *FPC v. Hope Natural Gas Co.*, 320 U.S. at 609-10. The NGA "was designed to take 'no authority from State commissions.'" *Id.* at 610.

FERC's view that it can choose to forego economic regulation and attempt to preempt the CPUC from doing any type of regulation is not filling a regulatory gap; it is creating one. *Arkansas Electric Cooperative v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 384 (1983). Nothing in the language, history or purpose of the NGA supports FERC's interpretation in this regard. *Id.* at 378-84.

B. FERC's Conclusory Statements Are Legally Inadequate to Support Its Decision

FERC states that it is choosing to use its section 3 conditioning authority here based upon a "public policy goal . . . served by a uniform national policy

¹⁰ All of SES's extensive intrastate operations would make the company a California public utility. ER 053-57.

applicable to LNG imports.” FERC Br. 36 (quoting March 24 Order at P 27, ER 090). This assertion lacks any evidentiary support or rationale. As such, it is inadequate to support FERC’s invocation of section 3 conditioning authority, even if FERC has such authority.

FERC's other assertions referenced on this point are not based upon any evidence in the record, let alone substantial evidence in the record. FERC refers to its Rehearing Order at PP 68-69, ER 249-250, which alleges that long-term capital needs for LNG projects require uniformity and that states may erect unreasonable hurdles. FERC Br. 36. There is no evidence in the record whatsoever that such uniformity is required for investors or that the CPUC has proposed unreasonable hurdles. Such speculation by FERC cannot substitute for substantial evidence in the record. *See Ding v. Ashcroft*, 387 F.3d 1131, 1138 (9th Cir. 2004); *Office of Consumers’ Counsel v. FERC*, 914 F.2d 290, 296 (D.C. Cir. 1990).

SES mischaracterizes the CPUC’s position as attempting to block or prohibit LNG importation, but SES cites to no evidence in the record below to support its accusations. SES Br. 14-17. Similarly, INGAA speculates that if section 3 were interpreted to allow states to regulate siting and facilities, all coastal states would reject LNG terminals, again with no evidence. INGAA Br. 18-21. What *is* in the record is that the CPUC has not tried to delay anything and informed SES in October 2003 that it should apply to the CPUC for a certificate, but SES refused to

do so. ER 053. The CPUC has agreed that there is a need for LNG. ER 102. Indeed, the CPUC has an ongoing rulemaking proceeding addressing issues to *facilitate* LNG-supplied natural gas access into California’s existing intrastate pipelines. ER 054. In the past, the CPUC has, in fact, approved LNG facilities sited at Point Conception. ER 164.

C. FERC’s, SES’s and INGAA’s Claims About the Need for Uniformity Are Inconsistent with the NGA and Other Federal Statutes

FERC’s orders and the briefs of FERC, SES and INGAA stress a vague and general policy argument that there is a need for uniformity in the regulation of LNG importation and importation facilities. They do not tie this argument to the NGA, which is understandable because they could not do so. As discussed above, the NGA and NGPSA were designed to preserve state authority, not take it away. In addition, in the Deepwater Port Act, 33 U.S.C. §§ 1502(9) & (13), 1507(d), 1508(b), applicants for authority to construct LNG facilities in federal waters need the approval of adjacent states. And the existence of state regulation necessarily entails a lack of national uniformity.

In addition, the specific safety concerns for siting LNG terminals will vary based upon local conditions of which the states have much more knowledge than the FERC. Under the NGPSA, the six different factors to be included in “minimum” LNG siting safety standards belie any notion that siting should be

done on a uniform basis. *See* 49 U.S.C. § 60103(a)(1)-(6). In its brief, FERC has contradicted its position that there needs to be uniformity, and has agreed that the safety concerns involving the siting of LNG terminals require consideration of various local conditions. Therefore, even FERC did not adopt a uniform-one-size-fits-all approach. FERC Br. 38-39.

D. Allegations in an *Amici Curiae* Brief Do Not Provide FERC with an Evidentiary Record

INGAA argues that this case could determine the future availability of oversea gas supplies to the United States. None of INGAA's arguments constitutes evidence, let alone evidence in the record below. This Court must review FERC's orders based upon the record before FERC. *See National Ass'n of Home Builders v. Norton*, 340 F.3d 835, 841 (9th Cir. 2003).

INGAA mischaracterizes the CPUC's argument as stating FERC has no jurisdiction over LNG projects under any section of the NGA and anywhere in the United States. INGAA Br. 18. This is obviously not true, and INGAA is creating the uncertainty for which it complains. The CPUC does not deny FERC's jurisdiction over LNG projects involving interstate commerce, and the CPUC has referred in numerous places in this brief and the CPUC's opening brief to section 7 of the NGA for FERC jurisdiction over LNG facilities that involve interstate commerce. In the present case, however, all parties agree there would be no interstate commerce involved. Moreover, because there are no interstate pipelines

in California near the ocean, the LNG terminals will necessarily have to interconnect with CPUC-regulated intrastate pipelines. ER 088. This is different in other parts of United States where interstate pipelines may or may not transport natural gas from LNG facilities. That is one of the reasons, among many other reasons, why there is not a basis for uniform regulation.

INGAA's fear that LNG terminals will not be built or investors will go elsewhere, if states have any decisionmaking authority, ignores the reality of how many proposals there actually are for LNG projects around North America at this time. One of the excerpts cited by INGAA refers to a long-range forecast of a need for nine additional LNG terminals (in addition to the four existing ones) and seven expansions of existing or future terminals *by 2025*. INGAA Br. 8, n.6. What INGAA omits mentioning is that there already are 55 proposed and potential Northern American LNG projects (not including the five existing ones) as of March 25, 2005, which FERC has posted on its website.¹¹

The CPUC's point is that INGAA's brief omits key facts, and this Court should not rely upon INGAA's allegations. The CPUC was not given any opportunity below to respond to these allegations or to any evidence that would support FERC's findings, because there was none. Therefore, FERC's findings

¹¹ See CPUC's Request for Judicial Notice ("RJN"), Exhibit A, filed April 13, 2005. These include projects in federal waters, which are filed with MARAD/Coast Guard, and projects in Mexico and Canada.

cannot be upheld. It is “not a matter of *weight* of the evidence; there was simply *no* evidence to weigh.” *West Virginia PSC*, 681 F.2d at 864-65.

INGAA may prefer FERC’s lack of economic regulation of LNG terminals and FERC’s refusal to have hearings on safety issues. However, the CPUC’s petition for review is based upon the NGA and NGPSA, which preserved state authority and were founded upon protecting consumers from exploitation and protecting communities from potential hazards.

CONCLUSION

For the foregoing reasons, the CPUC respectfully requests that this Court reverse the FERC’s orders.

May 3, 2005

Respectfully submitted,

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**CERTIFICATION OF COMPLIANCE WITH FED. R. APP. P. 32(a)(7)(C)
AND NINTH CIRCUIT RULE 32-1**

I certify that pursuant to Federal Rule of Appellate Procedure 32(a)(7)(C), Ninth Circuit Rule 32-1, and this Court's April 20, 2005 Order, the attached revised reply brief is proportionately spaced, has a typeface of 14 points or more and contains 8,353 words.

Dated: May 3, 2005

Harvey Y. Morris

CERTIFICATE OF SERVICE

I hereby certify that I have this day caused copies of the foregoing “REVISED* REPLY BRIEF OF PETITIONER CALIFORNIA PUBLIC UTILITIES COMMISSION” to be served upon the parties to these proceedings before this Court by sending to each party two copies thereof in the U.S. mail, postage prepaid, addressed as follows:

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