

134 FERC ¶ 61,117  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Marc Spitzer, Philip D. Moeller,  
John R. Norris, and Cheryl A. LaFleur.

Magellan Pipeline Company, L.P.

Docket No. OR10-6-000

ORDER ON INTERLOCUTORY APPEAL

(Issued February 16, 2011)

1. On February 1, 2011, the Presiding Administrative Law Judge (ALJ) in this proceeding issued an order granting Frontier Oil and Refining Company's (Frontier) motion for interlocutory appeal of an order denying its motion to compel Magellan Pipeline Company, L.P. (Magellan) to produce certain information in response to a data request in the hearing addressing Magellan's market-based rate application.<sup>1</sup> The issue on appeal is whether Magellan should be compelled, in the context of a market-based rate proceeding, to produce five years of aggregate cost-of-service information. For the reasons discussed below, the Commission denies Frontier's interlocutory appeal.

**Background**

2. On January 15, 2010, Magellan filed an application for authority to charge market-based rates for the transportation of refined petroleum products on its Mountain System from its origins at McPherson and El Dorado, Kansas (McPherson-El Dorado) to its destination at Aurora, Colorado (Denver). Frontier and Sinclair Oil Corporation protested. In its July 7, 2010 order on Magellan's application, the Commission found that Magellan lacked significant market power in the Aurora, Colorado destination market and permitted Magellan to charge market-based rates on this segment of its system.<sup>2</sup> The Commission found, however, that there were material issues of fact concerning, among other things (1) the construction of the origin market area as a single market and not two individual markets; (2) the appropriate netback analyses for ascertaining the level of competition in the origin market or markets; and (3) the viability of alternative options available to shippers and local refineries in the origin market for

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<sup>1</sup> *Magellan Pipeline Company, L.P.*, 134 FERC ¶ 63,009 (2011).

<sup>2</sup> *Magellan Pipeline Company, L.P.*, 132 FERC ¶ 61,016 (2010).

distribution of petroleum products. Accordingly, the Commission set for hearing the issue of whether Magellan lacks significant market power in its origin market(s).

3. As part of the discovery procedures in this hearing, Frontier sent a data request to Magellan on October 8, 2010. The request was as follows:

Please refer to Magellan's January 15, 2010 Application, Statement I, the Prepared Direct Testimony of Stanley P. Rogers, page 7, lines 1-12. Please provide any workpapers or other documents supporting the figures reported on page 700 of Magellan's Form 6 for the years 2005 through 2010.

4. Magellan objected to the data request on October 22, 2010, on the grounds that the request was overly broad, unduly burdensome, and not likely to lead to the discovery of admissible evidence. On December 22, 2010, Frontier filed a motion to compel Magellan to respond to the data request. Frontier argued that the data request seeks information that is relevant to determining whether Magellan possesses market power and, in turn, whether market-based rates on Magellan's Mountain system would be just and reasonable. Frontier asserted that the disputed discovery request submitted to Magellan seeks information directly relevant to the issues the Commission has set for hearing in this proceeding and is reasonably calculated to lead to the discovery of admissible evidence.

5. On January 5, 2011, Magellan filed an answer in opposition to Frontier's motion. Magellan argued that the Commission's regulatory framework for oil pipeline market-based rate proceedings, Commission and the United States Court of Appeals precedent, and the Commission's hearing order in this case make clear that cost-of-service information is not relevant to the issue set for hearing in this case.

6. The Presiding ALJ conducted an oral argument on the matter on January 10, 2011, and denied Frontier's motion to compel in an order issued on January 13, 2011. The ALJ determined that the Commission's regulations only require cost-of-service data where an oil pipeline has filed a cost-of-service rate increase and not where the pipeline is seeking market-based rate authority. The ALJ found that cost-of-service information would not lead to any relevant information germane to the ultimate issue of market power in the origin market. As Magellan explained, and the ALJ recognized, production of such information would significantly and inappropriately expand the scope of this market-based rate proceeding, in which no Magellan rate, much less Magellan's cost-of-service, is at issue.

7. On January 18, 2011, Frontier filed a motion to permit an interlocutory appeal of the January 13, 2011 Order denying its motion to compel. Frontier argues that the cost, revenue, profitability, and return information it seeks are relevant to determine whether Magellan is earning above-average returns, which, it asserts, is evidence of market power.

8. On January 28, 2011, Magellan filed an answer to Frontier's motion. Magellan reiterated its prior objections to Frontier's request. Magellan also added that it does not have a cost-of-service for the Mountain System, and accordingly, Frontier would use the requested information to perform wholly arbitrary adjustments and allocations in an attempt to derive a purported Mountain System "cost-of-service." Magellan argued that this would result in an extravagant expansion of the scope of these proceedings and is directly contrary to the Commission's regulations.

9. In light of Frontier and Magellan's sharply contrasting views regarding the scope of the issues relevant to a determination of market power under Commission precedent, and the scope of discovery regarding those issues that Frontier is requesting, the ALJ determined that Frontier should be permitted to seek an interlocutory appeal of the ruling denying its motion to compel.<sup>3</sup> The ALJ stated that the issue of whether Magellan should be compelled, in the context of a market-based rate proceeding, to produce five years of aggregate cost-of-service information will have a direct and immediate impact on the scope of issues to be adjudicated in this docket. The ALJ held that guidance from the Commission at an earlier stage in the proceedings, rather than later, would appear to serve the best interests of the parties as well as to conserve Commission resources should the Commission have a different view of the matter.<sup>4</sup>

### **Discussion**

10. The issue presented on appeal is whether Magellan should be compelled, in the context of a market-based rate proceeding, to produce five years of aggregate cost-of-service information. Frontier argues that in a competitive environment, one would expect a profitable pipeline to realize revenue that covers its costs and provides the pipeline with a reasonable return. Frontier contends that in such a competitive market, if the pipeline attempted to charge a rate that would provide an excessive return, shippers would turn to alternative options. Frontier submits that the competitive pressure would ensure that the pipeline earned no more than this reasonable return. Frontier asserts that evidence that a pipeline is earning a supranormal return, therefore, is evidence that the pipeline is not operating in a competitive environment, and that it has the ability to exercise market power.

11. In the data request at issue here, Frontier seeks information regarding the cost, revenue, profitability, and return Magellan is earning on shipments originating in the El Dorado market. Frontier contends that because evidence of above-average returns is evidence that a pipeline can exercise market power, this information is relevant to the

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<sup>3</sup> *Magellan Pipeline Company, L.P.*, 134 FERC ¶ 63,009, at P 14 (2011).

<sup>4</sup> *Id.*

determination of whether Magellan can exercise market power in the El Dorado origin market. Frontier argues that its request is therefore reasonably calculated to lead to admissible evidence, and Magellan should be compelled to answer it.

12. The Commission agrees with the Presiding ALJ's decision to deny Frontier's motion to compel. The ALJ correctly found that "cost-of-service information is beyond the scope of and irrelevant to the issues set for hearing in this case because the justness and reasonableness of a market-based rate is to be determined on the basis of the Commission's established market power inquiry, not an inquiry into costs."<sup>5</sup>

13. Frontier cites to Order No. 572,<sup>6</sup> which states that profitability can be considered in a market-based rate application. However, Frontier makes an unsupported leap of logic to suggest that the reference to profitability means it can seek information on costs, revenue and rate of return.

14. Specifically, Order No. 572 states:

In Statement H, the oil pipeline would describe any other factors that bear on the issue of whether it lacks significant market power in the relevant markets. The oil pipeline must explain why those other factors are pertinent. Possible other factors are: Exchanges, Excess Capacity, Competition with vertically integrated companies, buyer power, and profitability. The Commission is not excluding any factor and is not limiting the factors to those listed in the NOI. For example, an oil pipeline might want to show that it has been losing markets over a period of years or that the relevant market is expanding. The burden is on the oil pipeline to show the relevance of any factor to showing its lack of significant market power.<sup>7</sup>

Thus, under Order No. 572, to the extent that profitability is a factor to be considered, it is something that is to be raised by the pipeline in its application. Magellan has not raised the issue of profitability in its application and Frontier has not pointed to anything to suggest otherwise. As the description of Statement H shows, the burden is on the pipeline to show the relevance of the additional

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<sup>5</sup> January 13, 2011 Order Denying Motion to Compel at P 8.

<sup>6</sup> *Market-Based Ratemaking for Oil Pipelines*, FERC Stats. & Regs., Regulations Preambles January 1991- June 1996 ¶ 31,007 (1994), *order on reh'g*, Order No. 572-A, 69 FERC ¶ 61,412 (1994), *pet. for rev. denied*, *AOPL v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996).

<sup>7</sup> *Id.* at 31,193.

factors. Further, the pipeline is required to show that it lacks market power. The burden of proof is on the pipeline to support its application and not on the opponents of the application.

15. As the ALJ correctly held, an inquiry into costs has nothing to do with the issue of whether a pipeline can establish a lack of market power for the purposes of charging market-based rates instead of cost-of-service rates. Market-based rates are a substitute for cost-of-service rates because a showing of a lack of market power would mean that sufficient competition exists to ensure a just and reasonable rate.<sup>8</sup> In fact, the underpinning of the approval of market-based rates is that sufficient competition exists such that shippers can find alternatives to the pipeline if the pipeline attempts to raise rates above a certain threshold. Frontier seems to have conflated market-based rate concepts and cost-of-service concepts when it argues that above-average returns are evidence of market-power.

16. Further, as Magellan points out, it does not even have a cost-of-service for the Mountain System. Magellan states that when it acquired the Mountain System from Shell Pipeline Company in 2004, it adopted the existing rates and, since that time, Magellan has simply adjusted those rates annually pursuant to the Commission's indexing methodology. Magellan states that its page 700 information includes all of Magellan's pipeline systems and is not Mountain System specific. Magellan states that Frontier would use the requested information to perform wholly arbitrary adjustments and allocations in a misguided attempt to derive a purported Mountain System "cost-of-service." Magellan asserts it would then be required to engage a cost-of-service expert, develop its own Mountain System "cost-of-service" for this proceeding, and submit responsive testimony. The Commission finds that such an expansion of the scope of these proceedings is contrary to the Commission's regulations governing market power determinations for oil pipelines and, as the ALJ correctly found, would not provide the Commission with any relevant information that would assist it in determining whether Magellan possesses market power in its origin market, the issue set for hearing in this case.

17. Accordingly, for the reasons cited by the ALJ in her order and the additional reasons given here, Frontier's interlocutory appeal is denied.

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<sup>8</sup> See also sections §35.36 and 36.37 of the Commission's regulations, 18 C.F.R. §§ 35.36 and 35.37 (2010), where the market power analysis for sellers seeking market-based rates also does not include an examination of cost-based issues.

The Commission orders:

Frontier's interlocutory appeal is denied.

By the Commission.

( S E A L )

Kimberly D. Bose,  
Secretary.