NOTES AND COMMENTS

CONSTITUTIONAL LAW

STATE REGULATION OF INTERSTATE PIPELINES NATURAL GAS ACT

The Panhandle Eastern Pipeline Company delivers natural gas from its interstate pipeline to distributing utilities and to industrial consumers in Indiana. The Public Service Commission of Indiana ordered that it file with the Commission its tariffs covering rates, rules, and regulations in regard to industrial sales and to make annual reports "in connection with the regulation of rates and service . . . " The Pipeline Company thereupon brought a statutory action[1] for review of the order praying that it be vacated and its enforcement enjoined. The judgment of Randolph County Circuit Court finding the industrial sales to be interstate commerce exempt from state regulation was reversed by the Indiana Supreme Court. It was held that even considered as interstate commerce the industrial sales may be regulated by the state since they are without the field occupied by the Natural Gas Act[2] and of a local nature not burdening interstate commerce. *Public Service Commission v. Panhandle Eastern Pipeline Co.*, 71 N. E. 2d 117 (Ind.1947), probable jurisdiction noted, 67 S.Ct. 1352 (1947).

I

The first question is the determination of whether Congress acted in regard to direct industrial sales in its enactment of the Natural Gas Act. Before the passage of that Act it had been held by the Supreme Court that the several states might regulate the price of burner-tip sales of natural gas from local distributing companies to domestic consumers.[3] If the transporting pipeline company also operated the local distribution facilities and sold directly to local consumers, the state public service commissions had jurisdiction

1. Ind. Stat. Ann. (Burns, 1933) § 54-429.
2. 52 Stat. 821 (1938), 15 U.S.C. § 717 (1939).
3. Public Utilities Comm. v. Landon, 249 U.S. 236 (1919).

over the consumer sales.[4] But where the sale was by the pipeline company to a local distributing company, *i.e.*, a wholesale sale, the states were held to be constitutionally powerless to regulate on the ground that it was interstate commerce national in character.[5] The motivating purpose of the enactment of the Natural Gas Act was to subject these sales for resale to federal regulation.[6] The Act applies to: (1) transportation of natural gas in interstate commerce, (2) the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, or industrial use, (3) natural gas companies so engaged.[7]

Congressman Halleck of Indiana discussed on the floor of the House the status of a manufacturer who buys directly from a pipeline company. He concluded that "this bill seeks only to reach those sales when the sale is for resale to the ultimate consumer. So a purchaser for industrial use, who bought the gas, not for resale, but for consumption in his own plant, would not be reached by the measure."[8] The rate regulatory power of the Federal Power Commission being over sales "for resale" only, the Commission has recognized it does not have jurisdiction over sales direct to industrial consumers.[9] And the Supreme Court has termed industrial sales "unregulated business," saying that "The Commission, while it lacks authority to fix rates for direct industrial sales, may

4. Pennsylvania Gas Co. v. Public Service Comm., 252 U.S. 23 (1920); accord, East Ohio Gas Co. v. Tax Comm. of Ohio, 283 U.S. 465 (1931). Where the distributing company was affiliated with the selling company the state commission could demand that the wholesale rate be a fair and reasonable one. Western Distributing Co. v. Public Service Comm. of Kansas, 285 U.S. 119 (1932).

5. Missouri v. Kansas Gas Co., 265 U.S. 298 (1924); Public Service Comm. v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927). See State Corporation Comm. v. Wichita Gas Co., 290 U.S. 561, 563 (1934); Peoples Natural Gas Co. v. Public Service Comm., 270 U.S. 550, 554 (1926).

6. The charge of a what-the-traffic-will-bear rate at the "city-gate," a sale over which the state commission had no authority, handicapped their regulation of burner-tip rates, since the wholesale rate is the most potent factor in the determination of the retail rate. This fact was illustrated by House debate on the Natural Gas Act. It appeared that at that time domestic rates averaged 74.6 cents per 1000 cubic feet, while rates to industrial consumers, where a competitive situation with other fuels, notably coal, exists, the price was 16.9 cents per 1000 cubic feet. 81 Cong. Rec. 6721 (1937).

7. 52 Stat. 821 § 201(b) (1938), 15 U.S.C. § 717(b) (1939).

8. 81 Cong. Rec. 6723 (1937).

9. Re Cities Service Gas Co., 50 P.U.R. (N.S.) 65, 89 (1943).

take those rates into consideration when it fixes the rates for interstate wholesale sales which are subject to its jurisdiction."[10] The Natural Gas Act, then, was specific legislation for a specific need (regulation of sale for resale of natural gas in interstate commerce) and direct sales to industrial consumers are beyond its language and purpose.

In the principal case the Indiana Court was able to infer from the legislative history of the Act and Supreme Court pronouncements as to the legislative purpose that "those transactions over which jurisdiction was not given to the Federal Power Commission may be considered as local matters and left to state regulatory bodies."[11] Doubtless the meaning here is that no regulatory power was taken away from the states by the Natural Gas Act. In this connection it is to be noted that the states were not regulating industrial sales at the time the Act was passed and have not been able to do so prior to the present decision.[12]

If it could be said that Congress added to the states' authority by delegating to them a portion of its supreme power under the commerce clause in passing the Act, there would be no necessity to inquire whether this would be a permissible activity under the Constitution.[13] The Act does provide, after its positive grants, that it "shall not apply to . . .

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10. Panhandle Eastern Pipeline Co. v. Federal Power Comm., 324 U.S. 635, 646 (1945).
11. 71 N.E.2d 117, 124 (Ind. 1947).
12. The holding has been that where the pipeline company, as in the instant case, transports gas from out of the state and delivers it to industrial consumers without storing in compliance with a contract, it is engaged in interstate commerce and is not subject to the jurisdiction of the state commission. Cities Service Gas Co. v. Public Service Comm., 337 Mo. 809, 85 S.W.2d 890 (1935), cert. denied, 296 U.S. 657 (1936); accord, Sioux City, Iowa v. Missouri Valley Pipe Line Co., 46 F.2d 819 (D.C. Iowa 1931); Re Colorado Interstate Gas Co., P.U.R. 1933E 349 (1933). See Columbia Gas & Electric Corp. v. U.S., 151 F.2d 461, 463-4 (C.C.A. 6th 1945); Interstate Natural Gas Co. v. Louisiana Public Service Comm., 34 F.Supp. 980 (D.C. La. 1940). In the industry the present decision is considered to be a "test case." Crosby, "Which Way Does FPC Gas Probe Point?" 38 P.U. Fort. 464, 467 (1946).
13. Limitations, if any, on Congressional authorization of state taxation and regulation of interstate commerce, are beyond the scope of this note. The rule has been stated that "Where the federal legislation authorizes state action, such state action is permissible even as to matters which could otherwise be regulated only by uniform national enactments." Black, J., in Cloverleaf Butter Co. v. Patterson, 315 U.S. 148, 155 n. 4 (1942). See So. Pac. Co. v. Ariz., 325 U.S. 761, 769 (1945); Note, "Congressional Consent to Discriminatory State Legislation," 45 Col. L. Rev. 927 (1945).

the local distribution of natural gas or to the facilities used for such distribution . . . "[14] However, this negative command should not operate as an affirmative authorization to the states to regulate beyond their constitutional power by imposing what would otherwise be an undue burden on interstate commerce in the manner of the legislation upheld in *Prudential Insurance Co. v. Benjamin.*[15] What may be said with assurance in this case is only that there was a Congressional intent at the time of passing the Act not to deprive the states of any jurisdiction they were then exercising, but rather to supplement their regulatory scheme in a field in which the states were constitutionally unable to act.[16] Congress has therefore not acted in respect to industrial sales either by conferring jurisdiction over them upon the Federal Power Commission, or by authorizing the states to assert such authority.

II

We now reach the question of whether the commerce clause "of its own force" prohibits state regulation of direct industrial sales.

Whether sales to industrial consumers by the pipeline company are in interstate commerce or are in intrastate commerce should not be a conclusive determination of state regulatory power. In either case the sales may be subject to state authority. However, in past cases arising under the regulation of this industry the Court has reached the result that where intrastate commerce was involved the states could regulate;[17] but with the exception of the decision in *Pennsylvania Gas Co. v. Public Service Comm.*,[18] where interstate commerce was at issue, it was held that the states could not exercise this power.[19] This approach is not in accord with the climate of the present Court. Nevertheless, those cases are part of the history of the principal case and it should be considered whether the court, under them, could appropriately

14. See n. 7 supra.
15. 328 U.S. 408 (1946), 46 Col. L. Rev. 882, 32 Va. L. Rev. 1197.
16. See Public Utilities Comm. v. United Fuel Gas Co., 317 U.S. 456, 467 (1943).
17. Public Utilities Comm. v. Landon, 249 U.S. 236 (1919).
18. 252 U.S. 23 (1920).
19. Missouri v. Kansas Gas Co., 265 U.S. 236 (1924).

term the industrial sales "intrastate commerce" and thus never arrive at the commerce clause question.

The first in a series of tests distinguishing interstate commerce from intrastate commerce in distribution of natural gas came in *Public Utilities Comm. v. Landon.*[20] It was there held that the movement in interstate commerce ended when the gas passed into the "local mains" of the distributing company. But in the *Pennsylvania Gas Co.* case where the local mains were owned by the pipeline company which sold the gas directly to the local consumer the entire transaction was stated to be interstate commerce. The inconsistency of these holdings was noted in *East Ohio Gas Co. v. Tax Comm. of Ohio.*[21] There the *Pennsylvania Gas Co.* case was criticized by the Court[22] and a second test laid down: The step-down in pressure when the gas passes from the pipeline into the local distribution lines was compared by the court to the breaking of an "original package"[23] after shipment in interstate commerce, and therefore the movement of gas in interstate commerce was declared at an end at the step-down.[24] But that test is of doubtful contemporary utility, as it was argued in vain in *Illinois Natural Gas Co. v. Public Service Co.*[25] The Supreme Court there applied a third test, finding that the company was "engaged in interstate commerce in the purchase and sale of the natural gas which moves in a continuous stream from points without the state into appellant's pipes within the

20. 249 U.S. 236 (1919).

21. 283 U.S. 465 (1931).

22. Id. at 471: "The theory on which that conclusion was reached [that the gas continued in interestate commerce to burner-tips] is not wholly consistent with the views expressed in Public Utilities Comm. v. Landon and in Missouri v. Kansas Gas Co., . . . It does not appear that there were presented, in Pennsylvania Gas Co. v. Public Serv. Comm., to the state court or here the considerations on which it is held that interstate commerce ends and intrastate business begins when gas flowing through pipe lines from outside the state passes into local distribution systems for delivery to consumers in the municipalities served. But, however that may be, the opinion in that case must be disapproved to the extent that it is in conflict with our decision here."

23. Southern Natural Gas Corp. v. Ala., 301 U.S. 148 (1938); Hoover & Allison Co. v. Evatt, 324 U.S. 652 (1945); Leisy v. Hardin, 135 U.S. 100 (1890); Brown v. Maryland, 12 Wheat. 419 (U.S. 1827). See Gavit, "Commerce Clause" 125-30, § 72 (1932).

24. For a criticism of the view that the issue is one of "physics" see Powell, Note, 58 Harv. L. Rev. 1072 (1945).

25. 314 U.S. 498 (1942).

State . . . "[26] That this "continuous stream" test alone is an inadequate criterion admits itself to easy demonstration. Thus, in the *Illinois Natural Gas Co.* case the continuous movement of the gas progressed not only through the first step-down in pressure from the interstate pipeline to the Gas Company but also through the second reduction of pressure when the gas passed from the wholesaler's facilities into the service mains of local distributors. The consequence is that the gas on arrival at burner-tips of individual consumers is moving in interstate commerce. Yet the Court has uniformly held that sales by the distributor to local consumers are intrastate commerce.[27] It is probable that the test was not meant to be applied through the second delivery and reduction of pressure.

In applying these tests to the fact situation here presented we find that the pressure of the gas is reduced from 200 pounds per square inch to 80 or 100 pounds per square inch upon leaving the main line. The gas then flows through a lateral to a meter house where the pressure is further reduced, and then deliveries are made to the industrial consumer at a pressure of from 40 pounds to 10 pounds per square inch. Deliveries are made to the local distribution company at 9 to 25 pounds pressure per square inch. Whatever vitality remains to the "original package" doctrine after the *Illinois Natural Gas Co.* case would therefore mechanically determine the interstate movement on the reduction of pressure, and the sale to industrial consumers would be intrastate commerce. The Indiana Supreme Court in the principal case, while not passing on the point, was impressed with the manifest absurdity of this result. It is clear under previous cases that the delivery of gas to distributing utilities, which was made at substantitally identical pressure and conditions as that to the industrial consumer, is interstate commerce.[28] It would be vulnerable reasoning which would hold the distributor fork of the pipeline interstate commerce and the industrial fork intrastate commerce, because of a possible analogy to the breaking of an "original package." There remain the "local

26. Id. at 513. See Macey, Note, 27 Corn L. Q. 399 (1942).
27. East Ohio Gas Co. v. Tax Comm., 283 U.S. 465 (1931); Public Utilities Comm. v. Landon, 249 U.S. 236 (1919).
28. See n. 5 supra.

mains"[29] and the "continuous stream"[30] mechanical tests; and if the Court uses either the principal case presents a transaction constituting interstate commerce.

The Court cannot, consequently, avoid now deciding whether the commerce clause prohibits the state regulation of the price paid for gas by industrials. The Court has not previously passed on the point.[31] It is to be expected that in doing so it will follow the approach indicated by Mr. Chief Justice Stone in the *Illinois Natural Gas Co.* case, *supra.* On this supposition they will be "less concerned to find a point in time and space where the interstate commerce in gas ends and intrastate commerce begins" but rather will confront the question he posed as to "whether the interest of the state in the present regulation of the sale and distribution of gas

29. Public Utilities Comm. v. Landon, 249 U.S. 236 (1919).

30. Ill. Natural Gas Co. v. Public Service Co., 314 U.S. 498 (1942).

31. The case nearest in point is Arkansas-Louisiana Gas Co. v. Dept. of Public Utilities, 304 U.S. 61 (1937). There the Gas Company transported gas from Texas and Louisiana to Arkansas and the gas was (1) sold directly to industries, (2) sold to local distributors for resale, (3) distributed by the gas company itself acting as a public utility through a separate distribution department. The state commission ordered that schedules of rates and charges be submitted, and the case came up in the same manner as the principal case. It was held that the requiring of the reports would not "materially burden or unduly interfere with the free flow of commerce" but "in case the Department undertakes by some future action to impose what may be deemed unreasonable restraint or burden upon appellant's interstate business, through rate regulation or otherwise, that may be contested." Id. at 63. In that case however, it was not clear that the state commission had asserted regulatory jurisdiction over the industrial sales. Also through a separate department the company sold to houschold consumers by means of local distribution facilities. The latter factor would tend to make the information of greater import to the state commission. Cf. Southern Natural Gas Corp. v. Ala., 301 U.S. 148 (1937). Alabama imposed a franchise tax on the gas company, a Delaware corporation with its commercial domicile in Alabama. The Gas company sold natural gas to three distributing utilities and one industrial consumer, the Tennessee Coal, Iron & Railroad Company. Utilizing the "original package" doctrine the tax was sustained, the Court stating "from the agreed facts we are unable to conclude that the business thus conducted in Alabama was entirely an interstate business." See Stone, C.J., in Ill. Natural Gas Co. v. Public Service Co., 314 U.S. 498, 506 (1942): "In Southern Gas Corp. v. Alabama, 301 U.S. 148, 156-7, on which the Illinois Supreme Court relied, we held only that the sale of gas to a local industrial consumer by one who was piping the gas into the state was a local business sufficient to sustain a franchise tax on the privilege of doing business within the state, measured by all the taxpayer's property located there, including that used for wholesale distribution of gas to local public service companies."

transported in the state, balanced against the effect of such control on the commerce in its national aspect, is a more reliable touchstone for ascertaining state power than [are] . . . mechanical distinctions . . . "[32]

The essentiality of uniform regulation by a single authority is an important aspect of the elusive "undue burden" test.[33] In the principal case the Indiana Court found that uniformity of control of industrial sales was unnecessary and inferred that this was also the conception of Congress when it did not include such sales in its field of regulation. As a necessary consequence it was decided that the local interest is paramount. In the able opinion written by Judge Young, it was reasoned that the state controls all other consumer sales, and if it is not allowed to extend its regulatory powers to industrial sales the latter will be unregulated, at least for the moment. Such a result is "a weighty consideration in balancing national interest against local need."[34]

In *Missouri v. Kansas Gas Co.* it was held that as to sales to distributors "The paramount interest is not local but national—admitting of and requiring uniformity of regulation."[35] The basis on which that case could be distinguished from the principal one is that distributor sales are sales for resale while the direct sales to industrial consumers are sales for consumption.[36] That this differentiative treatment is valid is given support by the *Pennsylvania Gas Co.* case, *supra,* where it was held that direct sales to local consumers of a municipality were subject to state rate regulation although interstate commerce.[37] This case has surprisingly been a source of embarrassment to the Supreme Court.[38] Its import-

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32. Ill. Natural Gas Co. v. Public Service Co., 314 U.S. 498, 505-6 (1942).
33. See So. Pac. Co. v. Ariz., 325 U.S. 761, 768 (1945).
34. 71 N.E.2d 117, 125 (Ind. 1947).
35. 265 U.S. 298, 309 (1924).
36. The consumer sale aspect impressed Professor Powell. See Note, 58 Harv. L. Rev. 1072, 1082 (1945).
37. "The service is similar to that of a local plant furnishing gas to consumers in a city.
"This local Service is not of that character which requires general and uniform regulation of rates by congressional action, and which has always been held beyond the power of the States, although Congress has not legislated upon the subject." 252 U.S. 23, 31.
38. See n. 22 supra.

ance as precedent, if any, would seem to be that a pipeline company which acts in the capacity of a local distributing utility may be subject to rate regulation in the same manner as are local distributing companies.

The two lines of precedent then are the burner-tip sale to domestic consumers (states may regulate even where the sale is interstate commerce, as diversity of regulation is permissible) and the sale to the distributing company (states may not regulate, uniformity being essential). The direct industrial sale for consumption fits neither category with exactitude. With which is it more readily identifiable?

It is similar to the burner-tip sale in that it is a sale for consumption. The states have an interest in regulating that sale in order to preserve equality of economic opportunity among intrastate industrial concerns. And further, if the pipeline may undercut local distributing companies in sales to industry and take this business away from them, the rate burden on local householders will be increased and the state-wide system of regulation imperiled.[39] The states will be in position of impotence which, though not of equal degree, is comparable to their handcuffed status before the distributor sale was subjected to federal regulation.[40] These factors are the measure of the several states' interests in this regulation.

On the other hand, there are similarities between the industrial sale and the distributor sale. In one community a single industrial sale may even exceed in volume the dis-

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39. In Public Utilities Comm. v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927), the state commission argued that it could not effectively regulate sales to local consumers unless it was given power to regulate the distributor sale. Held: "Being the imposition of a direct burden upon interstate commerce from which the State is restrained by the force of the Commerce Clause, it must necessarily fall, regardless of its purpose . . . . [What Rhode Island could do for the benefit of its consumers Massachusetts could likewise do, ad infinitum] . . . . The rate is therefore not subject to regulation by either of the two states in the guise of protection to their respective local interests; but, if such regulation is required it can only be attained by the exercise of the power vested in Congress." 273 U.S. 83, 89-90. Cf. the recent case of Robertson v. California, 328 U.S. 440, 449 (1946): "And in view of the well-known conditions of competition in this field, such a result not only would free out-of-state insurance companies and their representatives of the regulation's effect, thus giving them advantage over local competitors, but by so doing would tend to break down the system of regulation in its purely local operation."

40. See n. 6 supra.

tributor sale which will serve the domestic consumers of the entire area.[41] The industrial sale is not an "on demand" sale to domestic consumers but the gas is transported extra-state and delivered pursuant to a private contract. Regulation of these sales reaches back of the state line through interim states to the gas field, just as regulation of sales for resale.[42] There is a question whether the state commissions have the machinery adequately to appraise the complex financial situation of large pipeline companies in order to determine industrial consumer price structure.[43] There is a further problem as to whether the facilities of the state public service commissions are adaptable to taking the natural second step by fixing quantities of gas to be delivered to state industrial consumers and concomitantly safeguarding local and industrial consumers' interests in sister states.

The above apply with equal force to distributor sales and indicate that as a factual matter it is with difficulty that the industrial sale is distinguished from them. As previously noted the states were held to be powerless to regulate distributor sales. Nevertheless, their interest in doing so here remains. Admitting that if the effect on commerce and the inconsistency with basic commerce clause purpose be considered, the principal case and the distributor sale cases cannot be realistically distinguished, does it follow that the state action must be struck down? The answer is a negative one. The

41. In the principal case the annual sale to the industrial consumer was regularly ten times larger in volume than the sale to the distributing company.

42. See Dowling, "Interstate Commerce and State Power," 27 Va. L. Rev. 1, 15 (1940), quoting Stone, J., in South Carolina Highway Dept. v. Barnwell Bros., 303 U.S. 177, 185 n. 2 (1938): ". . . when the regulation is of such a character that its burden falls principally upon those without the state, legislative action is not likely to be subjected to those political restraints which are normally exerted on legislation where it affects adversely some interests within the State."

43. The Federal Power Commission has found that as to the entire Panhandle Eastern system "these lines constitute the longest natural-gas pipe line in the world, serving more than 200 cities, towns, and communities with more than 700,000 retail customers in Texas, Kansas, Missouri, Illinois, Indiana, Michigan, and Ohio." Detroit v. Panhandle Eastern Pipe Line Co., 45 P.U.R. (N.S.) 203, 208 (1942), noted in Panhandle Eastern Pipeline Co. v. Federal Power Comm., 324 U.S. 635, 637 (1945). But see Natural Gas Act, 52 Stat. 821, § 17(c) (1938), 15 U.S.C. § 717p(c) (1939). "The Commission shall make available to the several State Commissions such information and reports as may be of assistance in State regulation of natural gas companies."

factors enumerated which presumably influenced the Court to declare in the distributor sale cases that there could be uniform regulation only by national authority are not of sufficient weight in the aggregate to lead to that conclusion when balanced against the interest of the states in regulating industrial sales, the problem which here struggles for attention and solution.

State efforts toward regulation of distributor sales have been pre-empted by the Natural Gas Act. This should make easier the acceptance of the suggestion here advanced that the Court, although the same result might be achieved by distinguishing them, should simply decline to follow those cases which held distributor sales to be beyond state power. The urgent local interest of the state indicates that there should be regulation. If this were equally true of the distributor sale cases, then let us frankly admit that they were ill-advised. Or more properly phrased, other approaches to reconciling state and federal power now press for recognition, and under present conceptions of sustaining both federal and state action where it is possible to do so a contrary result should be reached.[44] The door is ever left open for the supreme voice of Congress to speak. It should be unnecessary idly to abide that contingency. In the interim, industrial sales may be declared to admit of diversity of regulation and consequently to be within reach of the state. A complementary system of state and federal regulatory power should not fail in this "crucial situation."[45] If it is not to do so the state action must be upheld.

44. "But, just as in recent years the permissible scope for congressional commerce action has broadened, returning to Marshall's conception, the prohibitive effect of the clause has been progressively narrowed. The trend has been toward sustaining state regulation formerly regarded as inconsistent with Congress' unexercised power over commerce. To the extent this has occurred, the positive and negative pendulums have moved more and more in unison, not as mutually exclusive but as more mutually tolerant." Rutledge, "A Declaration of Legal Faith" 68 (1947).

45. See Final Report of the Federal Trade Commission to the Senate, Sen. Doc. 92, Pt. 84-A, 70th Cong., 1st Sess. 612 (1936): "Gas and pipe-line companies have asserted in some instances that they are solely within state jurisdiction and in other instances that they are so engaged in interstate commerce as to be entirely beyond state jurisdiction, whichever the exigencies of the particular case might seem to demand. There is a jurisdiction, either state or national which covers the entire country. Federal jurisdiction should be so utilized and coordinated as to produce effective reglation and the termination of existing abuses and leave no unregulated twilight zone. Otherwise our system fails in a very crucial situation."