Eminent Domain in the Public Utility Space: General Concepts

Scott Hempling, Attorney at Law LLC
shempling@scotthemplinglaw.com
www.scotthemplinglaw.com[1]

I. General principles

A. Eminent domain power is the governmental power to take private property for a public use, subject to paying the owner just compensation. State statutes typically grant this power to public utilities, who can exercise it directly, or after obtaining commission permission to do so.

B. An example is Rhode Island's provision, Section 39-1-31:

> "Before exercising any power of condemnation a company shall present a petition to the commission describing the land, right of way, easement or other interest in property it proposes to acquire and setting forth why it is necessary to acquire it by eminent domain . . . If the commission shall determine that the proposed taking is for the benefit of the people of the state, and that it is necessary in order that the petitioner may render adequate service to the public, and that the use to which the property taken will be put, will not unduly interfere with the orderly development of the region and scenic development, it shall issue a certificate authorizing the company to proceed with condemnation."

C. The case of *Narragansett Electric Company*, 65 PUR4th 198 (1985), *cert. denied*, 544 A.2d 121 (1988), illustrates the eminent domain principles typically used in the public utility context. Narragansett, a Rhode Island utility, sought to construct a 345 kV transmission line. Applying its statute, the Rhode Island Public Utilities Commission declared that the utility has the burden of proof to satisfy three criteria:

1. *Benefit to the public:* The utility must use the eminent domain power to provide necessary services to its utility customers, not to advance its private business interests. "[P]romotion of the production, supply and reliability of electric power," the Commission found, is an appropriate

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public purpose; and the transmission line was "the most viable means of meeting the company's future growth needs."

2. *Necessary for adequate service:* There must be a "clear necessity" for the specific property to provide adequate service to the public. The need must "materialize in the reasonably foreseeable future." Immediate need was not necessary, if the need was "reasonably foreseeable" or "fairly anticipated." The issue is not timing, but relative certainty. The Commission found that as consumer demand was reaching utility system's physical limits, there was a risk to reliability. The need was not speculative, even though the utility had twice revised the projected need date. That the line would function as a backup rather than as a primary supply line did not weaken the argument for "necessity." What mattered was that the line "will contribute" to reliability in Rhode Island.

3. *No undue interference:* The use cannot not unduly interfere with the "orderly development and the scenic development" of the region. The Commission interpreted this criterion as requiring the utility to select "a route designed to best develop the natural area intruded upon and to minimize the harm which might come to the scenic beauty of such area."

D. If the utility meets these three criteria, the Rhode Island Commission will defer to its routing decision, unless the decision is arbitrary, capricious, an abuse of discretion or in bad faith.

II. Mixed use: Can a utility use eminent domain powers for non-utility purposes?

An awkwardness arises when a utility using eminent domain powers is engaged in both public service and private merchant activities. This was the problem in *Consumers Power Co.*, 140 PUR4th 332 (1993).

A. Consumers Power, a franchised utility serving in Michigan, sought to condemn property for a long distance, high voltage transmission line. The line would interconnect Consumers Power's Michigan transmission system with that of an Indiana utility (then called Public Service of Indiana), at the Michigan-Indiana border. The new line, in conjunction with one to be built by PSI in Indiana, would, according to the Commission, "form a 116-mile pathway over which Consumers and PSI could exchange up to 500 megawatts (Mw) of electricity."

B. Consumers Power was a subsidiary of a holding company called CMS Energy. CMS Energy, in turn, owned a wholesale generation affiliate; that is, a company that had no retail franchise obligation to serve but had unused generation capacity

in a large power plant, "MCV." This MCV affiliate was seeking to sell its surplus output as a merchant in wholesale competitive markets.

C. To prevail in its Circuit Court condemnation action, Consumers had to prove that its proposed line was (a) for a public purpose and (b) necessary. The court referred the case, by agreement, to the state utility commission for fact-finding."

D. The evidence before the Commission indicated that line would have two effects. It would (1) help Consumers' parent, CMS, acquire or "pool with" Indiana utility;[2] and (2) allow the MCV affiliate to transmit power to the Indiana utility.

E. Concerned about possible dual purpose of the line, the Michigan Commission applied a 'heightened scrutiny test'" (although it stated the test was not legally required). That is, because the line could serve both a public use (carrying out Consumers' franchise obligation to serve its retail load efficiently) and a private use (advancing CMS Energy's merchant strategy of serving wholesale markets in Indiana), special attention was necessary so that the public eminent power was not used for a private purpose. Opponents presented internal company documents tending to show that the line's origins lay in CMS-PSI communications about MCV delivering power to PSI.

F. In overlapping opinions, two of the three commission members held that the line was *useful* for a public purpose. These benefits included additional capacity, ability to sell excess power to new markets, and enhanced competition. Two found, however, that it was not *necessary* to that purpose. One commissioner found that it was neither useful nor necessary. The effect of the decision was to allow the line costs to be recovered in retail rates (because the line was useful), but to advise the Circuit Court that the condemnation standard was unmet because the line was not "necessary."

G. The Commission also warned (noting that "Consumers has, on occasion, misinformed the Commission and attempted to circumvent its orders") that "if the assertions in the record regarding the intended use of the line or the magnitude of its expected public benefits later prove to be untrue, the Commission will take appropriate action. This includes, but is not limited to, denying recovery of the ...

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[2] Pooling is category of power sales transactions, in which two or more utilities exchange power to suit their individual needs. Exchanges of capacity between a winter peaking utility and a summer peaking utility, for example, allow each utility to avoid owning extra capacity to serve its peak. Other forms include "economy exchanges" (sometimes called "split-savings exchanges" where, for a specific hour, the utility with lower operating costs sells its power to a utility with higher operating costs, with the two utilities splitting the savings), and maintenance exchanges, where the two utilities stagger their maintenance outages so that each can rely on the other's surplus.

line's costs in future rate cases and compensating rate-payers through the power supply cost recovery process for any failure to use the line in a manner that produces the lowest possible costs for Consumers' customers."

H. Three weeks after receiving the Commission's views, the state court ruled against Consumers (not on the grounds of public vs. private use but on the grounds that the line was not necessary). Condemnation was not unavailable, and the line was never built.

III. Effective competition: What if eminent domain statutes distinguish among types of sellers or types of technologies?

The problem of public vs. private use arises under traditional utility statutes enacted long before the possibility of generation competition entered the electric industry. With generation competition, two related problem have emerged. First, what if a traditional utility and a non-utility both seek to build generation, in competition to serve retail or wholesale customers, but the statutes grant eminent domain power only to the utility? Second, what if the eminent domain power is available only for some technologies but not others? Do these differential treatments distort competition, harming consumers by impeding entry by new sellers who might bring lower-cost service?

A. Types of technologies

1. Since 1917, Section 27-7 of the Oklahoma statutes had this language:

> "Except as otherwise provided in this section, any person, firm or corporation organized under the laws of this state, or authorized to do business in this state, to furnish light, heat or power by electricity or gas, or any other person, association or firm engaged in furnishing lights, heat or power by electricity or gas shall have and exercise the right of eminent domain in the same manner and by like proceedings as provided for railroad corporations by laws of this state."

2. The 2011 General Assembly added this sentence:

> "The power of eminent domain shall not be used for the siting or building of wind turbines on private property."

3. Supporters justified the new sentence as protection for landowners from land rushes and bad faith dealing. One cannot escape the fact, however,

that the statute unbalances the competition between wind and other energy sources.

4. Similar examples have arisen in Wyoming, Utah and other states.

B. Types of sellers

1. The connection between eminent domain and evenhanded competition among different sellers is well-illustrated by FERC's orders on transmission "interconnection." In 1996, FERC issued its landmark *Order No. 888* on nondiscriminatory transmission access. The Order requires each investor-owned, transmission-owning utility to make its transmission facilities available to others, including its competitors, on terms comparable to how the utility uses the facilities for its own customers. In a sequel to *Order No. 888*, FERC issued *Order No. 2003*, identifying "interconnection" as a distinct service requiring the same nondiscriminatory treatment.

2. Interconnection service involves designing, constructing and connecting the line that connects a generator to the main transmission system, sometimes over large distances. Access to private land may be necessary. Recognizing that some states make eminent domain power available only to traditional utilities (and not to the new, non-utility "merchant" generators whose market entry FERC sought to assist), FERC's interconnection rule included a provision described by the Court of Appeals as "forbidding [transmission owners] from discriminating in the exercise of eminent domain powers to the detriment of independent generators and to the advantage of affiliates."[3]

3. The utilities attacked FERC's requirement as "commandeering states' eminent domain authority." The Court of Appeals disagreed:

> "We recognize that a state's authority to exercise the eminent domain power, and to license public utilities to do so, is an important state power. But FERC has done nothing more than impose a non-discrimination provision on public utilities. The orders explicitly leave state law untouched, specifying that any exercise of eminent domain by a public utility pursuant to the orders' non-discrimination mandate be "consistent with state law." [citations to FERC's orders omitted] Thus the states remain

[3] *National Association of Regulatory Utility Commissioners, et al. v. Federal Energy Regulatory Commission,* 475 F.3d 1277 (D.C. Cir. 2007).

> completely free to continue licensing public utilities to exercise eminent domain, or to discontinue that practice. To be sure, if hitherto a utility would not have exercised eminent domain to enable interconnection with an independent generator, the orders, conditionally, compel the utility either to broaden its use of the state-provided authority for the benefit of independents, or to drop the use for its own and its affiliates' power. But the modifier conditionally is critical. Nothing in the federal rule compels either continued state retention of the license, or public utilities' continued employment of eminent domain. ... [T]he orders here leave state law completely undisturbed and bind only utilities-not state officials."

4. Given that state law eminent domain power is often not available to non-utilities, FERC told the utilities that if they were using for their own or affiliates' generation, they had to use it for their competitors too.

5. Another approach is to expand the class of entities authorized to use the power. This Massachusetts statute makes eminent domain powers available to both utilities and non-utilities:

> "Any electric or gas company, generation company, or wholesale generation company may petition the department for the right to exercise the power of eminent domain with respect to the facility or facilities specified and contained in a petition submitted in accordance with section 69J or a bulk power supply substation if such electric or gas company is unable to reach agreement with the owners of land for the acquisition of any necessary estate or interest in land. The applicant shall forward, at the time of filing such petition, a copy thereof to each city, town, and property owner affected...."

Mass. Gen Laws ch. 164 sec. 69R.

6. Yet another approach, where the statute grants the eminent domain power only to public utilities, is to interpret the "public utility" term to include entities other than traditional utilities. In Pennsylvania, discoveries of shale gas in the Marcellus region has attracted businesses seeking to build pipelines to move the gas to markets. Some of these businesses have sought public utility status, so as to gain the eminent domain power available only to public utilities. In granting one such request, the

Pennsylvania Public Utilities Commission applied a four-part test, finding that the applicant, as summarized by one commentator:

a. "will be transporting or conveying natural or artificial gas by pipeline or conduit for compensation;

b. will serve any and all potential customers needing to move gas through the pipeline system;

c. intends to utilize negotiated contracts to secure customers; contracts are not meant to be exclusionary, but rather to establish technical requirements, delivery points, and other terms and conditions of service; [and]

d. has made a commitment to expand its capacity, as needed, to meet increased customer demand."

D.A. Tice, "Eminent Domain for Pennsylvania Pipelines?" http://www.marcellusshalelawmonitor.com/marcellus-development/eminent-domain-for-pennsylvania-pipelines (last checked Jan. 9, 2012).

IV. Federal roles

This discussion has focused on the traditional public utility whose obligation to serve, and eminent domain powers, arise from state law. There are also federal statutes that have granted eminent domain powers to entities that might not otherwise have them under state law.

A. Section 7(h) of the Natural Gas Act, 15 U.S.C. sec. 717F(h), grants the right of eminent domain to an entity that has received from FERC a certificate of public convenience and necessity under Section 7(c). The eminent domain power is available when the certificate holder "cannot acquire by contract, or is unable to agree with the owner of property to the compensation to be paid for, the necessary right-of-way ... and the necessary land or other property...."

B. Section 216 of the Federal Power Act, 16 U.S.C. sec. 824P, authorizes FERC to grant a "construction permit" to an applicant for the "construction or modification of electric transmission facilities in a national interest electric transmission corridor." The applicant must work through a multi-steps process.

C. First, the U.S. Department of Energy must have designated the area crossed by the transmission facilities to be a "national interest electric transmission corridor." To designate a corridor, DOE must find that the area is "experiencing electric energy

transmission capacity constraints or congestion that adversely affects consumers," based on a consideration of five factors.[4]

D. Second, assuming the facility is located within a DOE-designated corridor, FERC can grant the permit if it makes all of five findings set forth in Section 216(b). The first finding has stirred controversy. FERC must find the State in which the facility will be built has not approved, or cannot approve the siting of the facility, because, to paraphrase: it lacks authority to approve or to consider interstate benefits; or does not recognize the applicant as the type of entity eligible to site a project because it does not serve end-use customers; or, the state has "withheld approval for more than a year" or conditioned its approval "in such a manner that the proposed construction or modification will not significantly reduce transmission congestion in interstate commerce or is not economically feasible." In other words, FERC's jurisdiction to issue a permit is triggered only if the state cannot act or does not act.[5]

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[4] The five factors that the DOE "may consider" are set forth in Section 216(a)(4):

> "(A)the economic vitality and development of the corridor, or the end markets served by the corridor, may be constrained by lack of adequate or reasonably priced electricity;
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> (B) (i) economic growth in the corridor, or the end markets served by the corridor, may be jeopardized by reliance on limited sources of energy; and (ii) a diversification of supply is warranted;
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> (C) the energy independence of the United States would be served by the designation;
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> (D) the designation would be in the interest of national energy policy; and
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> (E) the designation would enhance national defense and homeland security."

In *California Wilderness Coalition v. U.S. Department of Energy* (9th Cir. 2011) the U.S. Court of Appeals vacated the Congestion Study required of DOE by Section 216(a)(1), for failure to consult with states sufficiently, and also vacated DOE's designation of particular corridors because it did not consider properly the environmental consequences under the National Environmental Protection Act ("NEPA").

[5] The meaning of the phrase "withheld approval" was addressed by the Court of Appeals in *Piedmont Environmental Council v. FERC*, (4th Cir. 2009). FERC had interpreted the phrase to include a state saying "no," i.e., rejecting an application. The Court disagreed: "Withheld" means only not acting; it does not mean acting negatively. A state's rejection thus ousts FERC's jurisdiction to issue a construction permit.

E. If FERC's jurisdiction is triggered for one of the reasons listed in Section 216(b)(1), the FERC can grant the permit, if it first makes all of five other findings that relate to the public interest.[6]

F. The permit holder's rights are similar to those stated in the Natural Gas Act. Section 216(e) of the Federal Power Act grants a permit holder the right of eminent domain if the permit holder "cannot acquire by contract, or is unable to agree with the owner of the property to the compensation to be paid for, the necessary right-of-way to construct or modify the transmission facilities...."

[6] Those five findings, stated in Section 216(b)(2)-(6), are:

"(2) the facilities to be authorized by the permit will be used for the transmission of electric energy in interstate commerce;

(3) the proposed construction or modification is consistent with the public interest;

(4) the proposed construction or modification will significantly reduce transmission congestion in interstate commerce and protects or benefits consumers;

(5) the proposed construction or modification is consistent with sound national energy policy and will enhance energy independence; and

(6) the proposed modification will maximize, to the extent reasonable and economical, the transmission capabilities of existing towers or structures."