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Take-or-Pay Provisions: Major Problems for the Natural Gas Industry Comment.

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COMMENTS

Take-or-Pay Provisions: Major Problems for the Natural Gas Industry

David L. Roland

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I. INTRODUCTION

Due to the increasingly turbulent and unpredictable natural gas market, most natural gas producers have included a clause in their gas purchase contracts referred to as a take-or-pay provision.[1] This take-or-pay provision

1. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 882 (10th Cir. 1985) (take-or-pay provisions reduce risk for producers), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986). Natural gas supplied energy to over 43.3 million residential establishments, 3.49 million commercial units, and 187.8 thousand industrial customers in 1980. *See* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 2(2)(b) (Supp. 1985); *see also* AMERICAN ENTERPRISE INSTITUTE, NATURAL GAS PROPOSALS 2

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requires the purchaser, usually a pipeline company, to "take" a certain amount of gas from the producer at a fixed price or pay for the quantity of gas, even if the purchaser does not use the quantity set forth in the contract.[2] The majority of take-or-pay contracts were executed during the 1970's, when a severe natural gas shortage was in existence.[3] Since most contracts in the gas industry are long-term, many take-or-pay contracts are still in effect.[4]

(1983) (natural gas accounts for 27% of energy used in United States; provides 40% of industry and agricultural needs; 55% of all commercial and residential customers use gas). Presently, Texas and Louisiana are the two leading producers of natural gas, combining for over 70% of total United States gas production. *See* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 4 (1982).

2. *See* WILLIAMS & MYERS, MANUAL OF OIL AND GAS TERMS 882 (6th ed. 1984). To better understand the operation and purpose of a take-or-pay provision, a brief overview of the organizational structure of the natural gas industry is helpful. *See generally* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 5-6 (1982) (explanation of industry structure). The producers explore, locate, and remove the gas from the ground. Producers sell the natural gas reserves to pipeline companies, whose main function is to transport the gas to local gas distributors or industrial consumers. *See id.* at 5. *But see* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83 n.1 (1983) (producers occasionally sell gas directly to local distributors). After the local distributor purchases the gas, the gas is resold to individual commercial, residential, and industrial consumers. *See* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 5 (1982); *see also* Pierce, *Reconsidering the Roles of Regulation and Competition in the Natural Gas Industry*, 97 HARV. L. REV. 345, 348 (1983) (title to gas passes with each transfer of possession). Take-or-pay provisions appear in contracts between producers and pipeline companies. *See* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83 (1983). The following is an example of a "typical" take-or-pay provision in a gas purchase contract:

> Commencing with the initial delivery of gas from each particular well hereunder and subject to the other provisions of this agreement, Seller agrees to sell and deliver to Buyer, and Buyer agrees to purchase and receive, or pay for if available and not taken, an average daily quantity of gas . . . from each of Seller's wells [equal to one hundred percent (100%) of the delivery capacity of Seller's wells] . . . [d]uring the period each year beginning November 1 through the following April 30. . . .

Paragon Resources, Inc. v. National Fuel Gas Distribution Corp., 723 F.2d 419, 420 (5th Cir. 1984).

3. *See* Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (gas shortage gave rise to gas contract litigation). Take-or-pay provisions aided producers during the gas shortage since the contracts guaranteed the pipeline companies would pay for a minimum quantity and promised a steady supply of cash flow, thereby rendering capital for producers to invest in further exploration. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 771-72 (1983) (reasons for long-term gas purchase contracts).

4. *See* Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (long-term contracts customary between pipelines and producers). All participants in the natural gas industry make significant investments in the exploration, production, transportation, or consumption stages of the industry; therefore, the continuity of gas supply to each participant is vital. *See* Pierce, *Reconsidering the Roles of Regulation and Competition in the Natural Gas Industry*, 97 HARV. L. REV. 345, 354 (1983); *see also* Apache Gas Prod. Corp. v. Oklahoma

The market, however, has changed and the shortage of the 1970's has been replaced by a natural gas surplus.[5] Consequently, the parties to these take-or-pay agreements have found themselves in totally unexpected positions dealing with uncontemplated and sometimes unfair results.[6] Pipeline companies are caught in the unenviable position of paying for gas that cannot be marketed because of insufficient demand.[7] Moreover, pipeline companies are not the only victim in this unfortunate scenario.[8] Since take-or-pay contracts have pipeline companies locked into purchasing gas at inflated prices, the high costs are eventually passed to the consumer in the form of high rates.[9] Due to the magnitude of the problem,[10] the take-or-pay issue is currently the subject of much litigation and debate in both the courts[11] and

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Tax Comm'n, 509 P.2d 109, 112-13 (Okla. 1973) (recognizing necessity for long-term contracts in gas industry). For a discussion of long-term agreements in the natural gas industry, see generally Pierce, *Natural Gas Regulation, Deregulation, and Contracts,* 68 VA. L. REV. 63, 77-82 (1982).

5. *See* Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (gas surplus currently exists). *See generally* McGrath, *Natural Gas, In Turmoil and Transition,* 5 J. OF ENERGY L. & POL'Y 197, 204 (1984) (gas deliverability surplus estimated at 3 trillion cubic feet).

6. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?,* 20 HOUS. L. REV. 771, 774-75 (1983) (parties are placed in vicarious positions under take-or-pay contracts). As an illustration of the take-or-pay problem, Panhandle Eastern Pipeline Company executed a take-or-pay contract with Algeria during the 1970's. *See id.* Once the market changed to oversupply, Panhandle was forced to purchase Algerian gas even though Algerian gas was much more expensive than the bountiful domestic gas. *See id.* at 775.

7. *See International Minerals & Chem. Corp. v. Llano, Inc.*, 770 F.2d 879, 885 (10th Cir. 1985) (if pipeline does not take delivery of gas, gas must still be paid for), *cert. denied,* — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986); Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (pipeline must pay for gas whether or not gas is taken).

8. *See* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1151 (D.C. Cir. 1985) (take-or-pay liabilities are fixed cost passed to consumer).

9. *See* Natural Gas Policy Act, 15 U.S.C. § 3431(c)(2)(B) (1982) (pipeline company given right to pass costs incurred through purchase from producer). The pipeline company may then effectively pass to the distributor any costs incurred from the purchase. *See* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1150-51 (D.C. Cir. 1985) (contract provisions permit pipelines to cover take-or-pay costs). The distributor covers his inflated costs through the use of higher rates to consumers. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?,* 20 HOUS. L. REV. 771, 775 (1983).

10. *See* Moody, *The Natural Gas Industry After Partial Deregulation,* 36 INST. ON OIL & GAS L. & TAX'N § 6.05 (1985) (expressing importance of take-or-pay issue). "If take-or-pay provisions are found to be either invalid or unenforceable, then the industry, and natural gas markets, will undergo a sea [of] change unlike any previously experienced. . . ." *Id.* § 6.05 at 6-15.

11. *See, e.g.,* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1149-51 (D.C. Cir. 1985) (determining enforceability of gas purchase contract); International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 881 (10th Cir. 1985) (challenging validity of take-or-pay provision),

legislature.[12]

This comment will fully explore the origin, operation, and significance of the take-or-pay contract, along with the conflicts surrounding the take-or-pay controversy. Furthermore, possible solutions will be presented from judicial, regulatory, and legislative perspectives, together with probable outcomes.

II. GENERAL BACKGROUND OF THE NATURAL GAS INDUSTRY

A. *History of Gas Regulation*

The roots of the natural gas industry can be traced back to the early Japanese cultures of the seventh century.[13] However, natural gas was not used extensively for commercial purposes until the early 1920's, due primarily to problems in transportation and competition from other resources, such as oil and electricity.[14] In fact, natural gas was generally recognized as a useless waste product of oil exploration and was normally burned at the drilling site.[15] The first interregional pipeline, which was completed in 1931, solved most of the transportation problems and gave the industry the boost needed to create a major national market.[16]

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cert. denied, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986); Maryland People's Counsel v. FERC, 761 F.2d 768, 770-72 (D.C. Cir. 1985) (conflict arising from take-or-pay problems). *See generally Annual Report on Natural Gas*, 1985 A.B.A. SEC. PUB. UTIL. L. REP. 208-09 (discussion of take-or-pay cases pending before courts).

12. *See, e.g.*, H.R. 511, 99th Cong., 1st Sess. (1985) (limiting amount of take-or-pay obligations); H.R. 294, 99th Cong., 1st Sess. (1985) (voiding all take-or-pay clauses); S. 689, 98th Cong., 1st Sess. (1983) (automatic reduction of all take-or-pay provisions).

13. *See* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 1.02 (1985). The Chinese were perhaps the first transporters of gas, utilizing bamboo as pipes during the tenth century. *See id.*; *see also* Commoner, *A Nearly Perfect Fuel*, THE NEW YORKER, May 2, 1983, at 66 (overview of natural gas history).

14. *See* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 1.03 (1985) (gas used primarily for lighting during nineteenth century). When the first incandescent electric lamp was patented in 1878, the demand for gas took a sharp decline. *See id.* § 1.06. Transportation of the gas was a major problem during the 1800's, as evidenced by the fact that in 1925 the longest pipeline extended only 300 miles. *See* Ringleb, *Natural Gas Producer Price Regulation Under the NGPA: Regulatory Failure, Alternatives, and Reform*, 20 HOUS. L. REV. 709, 713 n.12 (1983). After the discovery of electricity, the gas industry began to develop other products, such as gas stoves, furnaces, and water heaters. *See* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 1.06 (1985).

15. *See* Exxon Corp. v. Middleton, 571 S.W.2d 349, 352 (Tex. Civ. App.—Houston [14th Dist.] 1978) (recounting development of natural gas industry), *rev'd on other grounds*, 613 S.W.2d 240 (Tex. 1981).

16. *See* Commoner, *A Nearly Perfect Fuel*, THE NEW YORKER, May 2, 1983, at 66. By 1934, pipelines often extended 1,200 miles in length. *See* Ringleb, *Natural Gas Producer Price Regulation Under the NGPA: Regulatory Failure, Alternatives, and Reform*, 20 HOUS. L. REV. 709, 713 n.12 (1983). The rapid expansion was primarily a result of improved pipeline tech-

Once a considerable market developed, the Federal Trade Commission (FTC) recognized the need for regulation of the industry.[17] The lack of regulation resulted in excessive prices and corresponding unrestrained profits.[18] Thereafter, the FTC began an in-depth investigation,[19] which resulted in a report to the United States Senate in 1936 recommending regulation of interstate pipelines.[20] In 1938, Congress enacted the Natural Gas Act (NGA),[21] to protect consumers from the excessive prices charged by gas companies.[22] The NGA gave the Federal Power Commission (FPC)[23] the authority to regulate the transportation and price of natural gas sold in interstate com-

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nology. *See* Exxon Corp. v. Middleton, 571 S.W.2d 349, 352 (Tex. Civ. App.—Houston [14th Dist.] 1978) (World War II effort resulted in improvements in pipeline technology), *rev'd on other grounds*, 613 S.W.2d 240 (Tex. 1981); 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 3.04(3) (1985) (pipeline expansion possibly due to improvements in strength, size, and method of laying pipe).

17. *See* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 2.06 (1985) (industry free from federal regulation). In 1906, Congress amended the Interstate Commerce Act to exclude interstate natural gas pipelines from the jurisdiction of the Interstate Commerce Commission. *See* McGrath, *Natural Gas, In Turmoil and Transition*, 5 J. OF ENERGY L. & POL'Y 197, 198-99 (1984). Therefore, state public utility commissions became responsible for the regulation of the industry. *See id.* at 199. *But see, e.g.,* Public Util. Comm'n v. Attleboro Steam & Elec. Co., 273 U.S. 83, 91-93 (1927) (Brandeis, J., dissenting) (state commission in producing state cannot regulate price of gas sold outside producing state); Public Util. Comm'n v. Landon, 249 U.S. 236, 245-46 (1919) (state agency cannot dictate price between interstate pipeline and local distributor); West v. Kansas Natural Gas Co., 221 U.S. 229, 247-62 (1911) (state statute restricting pipeline from transporting local gas interstate held unconstitutional).

18. *See* FPC v. Louisiana Power & Light Co., 406 U.S. 621, 638 (1972) (concentration in gas industry cause of high prices); *see also* FED. TRADE COMM'N, REPORT OF THE FTC TO THE UNITED STATES SENATE, S. DOC. NO. 92, 70th Cong., 1st Sess. 28 (1935) (in 1935, four pipeline companies contolled 55% of gas pipelines). Due to the large market concentration, the pipeline companies were able to charge excessive prices while providing unsatisfactory service. *See* Pierce, *Reconsidering the Roles of Regulation and Competition in the Natural Gas Industry*, 97 HARV. L. REV. 345, 345 (1983).

19. *See* FED. TRADE COMM'N, REPORT OF THE FTC TO THE UNITED STATES SENATE, S. DOC. NO. 92, 70th Cong., 1st Sess. 588-91 (1935) (FTC investigation of gas industry).

20. *See id.* at 616-17 (recommendation that federal government regulate pipelines). The report further recommended that: (1) producing states enter into production quota agreements; (2) federal agencies should have the authority to force pipelines to serve nearby municipalities; (3) bank management of gas companies be forbidden; and (4) electric and gas utilities be separated. *See* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 2.07 (1985) (summary of FTC report).

21. *See* Natural Gas Act, 15 U.S.C. § 717-717w (1982).

22. *See* Atlantic Ref. Co. v. Public Serv. Comm'n, 360 U.S. 378, 389 (1959) (purpose behind NGA is consumer protection); FPC v. Hope Natural Gas Co., 320 U.S. 591, 610 (1944) (NGA intended to protect consumers from gas company exploitation). *See generally* Comment, *Natural Gas Regulation and Market Disorder*, 18 TULSA L.J. 619, 629-32 (1983) (discussion of regulation under the NGA).

23. *See* Department of Energy Org. Act of 1977, 42 U.S.C. § 7151a (1982) (FPC replaced

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merce.[24] The FPC's authority, however, did not include the regulation of gas producers.[25] The regulations were not extended to include sales between producers and pipeline companies until 1954, when the United States Supreme Court decided *Phillips Petroleum Co. v. Wisconsin*.[26]

After *Phillips*, the FPC had the authority to control the wellhead prices charged by producers of natural gas.[27] However, problems associated with the administration of setting price regulations quickly developed.[28] The

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by Federal Energy Regulatory Commission ("FERC")). For a discussion of the FPC, see generally Bagge, *The Federal Power Commission*, 11 B.C. INDUS. & COM. L. REV. 689 (1970).

24. *See* Natural Gas Act, 15 U.S.C. § 717 (1982) (FPC given power to set reasonable rates for interstate pipeline companies). Before selling or transporting natural gas, all companies were required to obtain a certificate of public convenience and necessity from the FPC. *See id.* § 717f(c); *see also* Kansas Pipeline & Gas Co. and North Dakota Consumers Gas Co., 2 F.P.C. 29, 34-35 (1939) (setting forth requirements for FPC granting application for certificate). *See generally* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 4.02(3) (1985) (overview of certificate of public convenience and necessity).

25. *See* Natural Gas Act, 15 U.S.C. § 717-717w (1982) (NGA not applied to production or gathering of gas); *see also* Colorado Interstate Gas Co. v. FPC, 324 U.S. 581, 597 (1945) (producers not within authority of Act); Panhandle E. Pipe Line Co. v. Public Serv. Comm'n, 332 U.S. 507, 516 (1947) (producer not within FPC's regulatory power). *See generally* Note, *Legislative History of the Natural Gas Act*, 44 GEO. L.J. 695 (1956) (general discussion of legislative history of NGA).

26. 347 U.S. 672 (1954). Phillips Petroleum was an independent natural gas producer that regularly sold gas to interstate pipelines. *See id.* at 674-75. Phillips decided to raise its wellhead price of gas sold to such pipelines, and the Wisconsin Public Service Commission consequently appealed to the FPC to regulate Phillips' sale of gas and keep Phillips from raising its prices. *See* Turner, *Natural Gas-Impact of Deregulation or Regulation on Sales Contracts*, 29 ROCKY MTN. MIN. L. INST. 501, 505 (1983). The FPC ruled that the Commission did not have jurisdiction over Phillips' rates. *See* Phillips Petroleum Co., 10 F.P.C. 246, 283 (1951). Wisconsin took the case to federal court, where it was determined that the FPC did have jurisdiction over the matter. *See* Wisconsin v. FPC, 205 F.2d 706, 712 (D.C. Cir. 1953), *aff'd*, 347 U.S. 672 (1954). The United States Supreme Court affirmed the court of appeals and held that the NGA required the FPC to regulate producers and wellhead prices. *See* Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672, 677 (1954). *See generally* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 20.02(3) (1985) (analysis of *Phillips* decision).

27. *See* Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672, 677 (1954) (interpreting NGA to include regulation of producers). The decision in *Phillips* left the natural gas market in a two-tiered state. *See* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 8-9 (1982) (discussing effects of *Phillips*). The FPC regulation was extended to include gas sold to pipelines for *interstate* transmission, but did not extend to gas sold by producers for use *intrastate*. Therefore, the market was sharply divided between gas used interstate and that used intrastate. *See id.* at 9.

28. *See* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 4.04(5) (1985) (immediate backlog of cases overloaded FPC). The FPC was designed to handle 700 pipeline rate cases per year. In the first year after the *Phillips* decision, the FPC received 709 pipeline cases *and* 10,978 filings from gas producers. *See id.* The resulting administrative disorder led one commentator to state, "The Federal Power Commission without question represents the outstanding example in the federal government of the breakdown of the admin-

FPC experimented with individual company determinations, which proved unworkable.[29] In 1960, the Commission decided to change from a company-by-company rate determination to an "area-rate" price for each producing region.[30] Under the "area-rate" method, rates were determined for each geographical area, rather than for each individual company.[31]

B. *Major Trends in the Gas Market*

In the early 1970's, a severe interstate gas shortage developed.[32] The shortage was mostly due to the area-rate determinations initiated a decade earlier.[33] The problem stemmed from the fact that the prices established through the area-rate method were based on out-dated cost estimates rather than estimates reflecting costs of recent production; therefore, the prices were irrationally low.[34]

By the mid-1970's, as a national energy crisis was brewing, it became evi-

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istrative process." *See* STAFF OF SENATE COMM. ON THE JUDICIARY, 86th Cong. 2d Sess., Report on Regulatory Agencies to the President-Elect 54 (Comm. Print 1960) (J. Landis), *quoted in* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 4.04(5) (1985).

29. *See* Southern La. Area Rate Cases v. FPC, 428 F.2d 407, 416 (5th Cir.) (company-by-company approach unsatisfactory), *cert. denied*, 400 U.S. 950 (1970). The goal behind the individual determinations was to set reasonable rates through the review of each company's total costs and leave a fair rate of return. *See* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 10 (1982). The inefficiency of the system became evident upon the initial rate-making proceeding, which coincidentally involved Phillips Petroleum Company. *See* AMERICAN PETROLEUM INSTITUTE, NATURAL GAS DECONTROL: THE TIME TO START IS NOW 58, 58-59 (Feb. 1982). The procedure took over four years, required 82 hearing days, over 10,000 pages of testimony, and 235 pages of exhibits. *See id.* at 58. The incompetence of the procedure was further expressed by Justice Jackson when he described the procedings as "little better than . . . [pulling] figures out of a hat." *See* Colorado Interstate Gas Co. v. FPC, 324 U.S. 581, 610 (1945) (Jackson, J., concurring).

30. *See* Southern La. Area Rate Cases v. FPC, 428 F.2d 407, 416-17 (5th Cir.) (switch from individual company approach to area approach), *cert. denied*, 400 U.S. 950 (1970).

31. *See* Breyer & MacAvoy, *The Natural Gas Shortage and the Regulation of Natural Gas Producers*, 86 HARV. L. REV. 941, 958-65 (1973). This procedure, however, also proved to be ineffective. *See* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 11 (1982) (first area rate determination lasted four and one-half years).

32. *See* FPC v. Louisiana Power & Light Co., 406 U.S. 621, 626 n.2 (1972) (severity of national gas shortage); MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 14 (1982) (gas shortage eventually caused eleven states to declare emergencies).

33. *See* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 11-12 (1982) (area price rates were major cause of shortage).

34. *See* Ringleb, *Natural Gas Producer Price Regulation Under the NGPA: Regulatory Failure, Alternatives, and Reform*, 20 HOUS. L. REV. 709, 715 n.26 (1983) (area-rate based on historical data); Pierce, *Natural Gas Regulation, Deregulation, and Contracts*, 68 VA. L. REV. 63, 67 (1982) (area-rate utilized unrealistic costs). The FPC subsequently adopted a new approach which set a fixed national rate. *See* Shell Oil Co. v. FPC, 520 F.2d 1061, 1066-69 (5th Cir. 1975) (national rate projected cost of finding and producing gas, with a 15% annual re-

dent that there was a dire need to end natural gas price controls.[35] As a result, Congress enacted the Natural Gas Policy Act of 1978 (NGPA),[36] which provided for gradual decontrol of most types of natural gas.[37]

The decontrol provisions contained in the NGPA were a major factor in the recent development of a surplus in the interstate gas market.[38] Under the NGPA deregulation program, prices eventually increased as planned; however, at the same time, demand for natural gas steadily declined.[39] The

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turn), *cert. denied*, 426 U.S. 941 (1976). For the first time, the FPC considered future costs estimates when determining price ceilings. *See id.* at 1066-69.

35. *See* FPC v. Louisiana Power & Light Co., 406 U.S. 621, 626 n.2 (1972) (quoting FPC STAFF REPORT NO. 2, NATIONAL GAS SUPPLY AND DEMAND 1971-1990, at xi (1972) for seriousness of gas shortage). Due to federal intervention, wellhead prices continued to decline during the 1960's. *See* McGrath, *Natural Gas, In Turmoil and Transition*, 5 J. OF ENERGY L. & POL'Y 197, 201 n.24 (1984) (prices declined 1.7% annually). Consequently, less exploration took place and less reserves were available. *See* AMERICAN GAS ASSOCIATION, GAS FACTS 1980 DATA 35, table 28 (1981) (number of completed wells dropped from 58,000 in 1956, to 27,000 in 1971). Additionally, the unequal treatment between interstate pipelines and intrastate pipelines under the NGA led to shortages in the interstate market because intrastate pipelines could pay higher prices for the available gas. *See* Mid-Louisiana Gas Co. v. FERC, 664 F.2d 530, 533 (5th Cir. 1981) (effects of dual market led to disadvantage for interstate pipelines), *vacated*, 463 U.S. 319 (1983). The situation became so intense that eleven states declared emergencies. *See* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 14 (1982). *See generally* Breyer & MacAvoy, *The Natural Gas Shortage and the Regulation of Natural Gas Producers*, 86 HARV. L. REV. 941, 965-67 (1973) (discussion of severity of gas shortage).

36. 15 U.S.C. §§ 3301-3432 (1982).

37. *See id.* §§ 3331-3333 (1982) (decontrol provisions); *see also* Dander Petroleum, Inc. v. Northern Natural Gas Co., 615 F. Supp. 1093, 1099-1100 (N.D. Tex. 1985) (explanation of NGPA pricing schemes); Abbott & Watson, *Pitfalls on the Road to Decontrol: Lessons from the Natural Gas Policy Act of 1978*, THE DEREGULATION OF NATURAL GAS 54 (1983) (illustration of NGPA pricing provisions). Under the NGPA, price controls will gradually be removed from most domestic gas supplies, leaving only 20% of total supplies still regulated in 1990. *See id.* For a thorough discussion of the development of the NGPA, see generally Note, *Legislative History of the Natural Gas Policy Act: Title I*, 59 TEX. L. REV. 101 (1980). The NGPA also extended price regulations to intrastate gas. *See* 15 U.S.C. § 3315 (1982); *see also* Tenneco, Inc. v. Sutton, 530 F. Supp. 411, 418-21 (M.D. La. 1981) (analysis of NGPA).

38. *See* Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (increased prices and impending decontrol under NGPA partial causes of gas surplus). *See generally* Turner, *Natural Gas-Impact of Deregulation or Regulation on Sales Contracts*, 29 ROCKY MTN. MIN. L. INST. 501, 510-11 (1983) (NGPA price increases factor in surplus).

39. *See* Wisconsin Gas. Co. v. FERC, 770 F.2d 1144, 1151 (D.C. Cir. 1985) (price of gas remained high during surplus); Turner, *Natural Gas-Impact of Deregulation or Regulation on Sales Contracts*, 29 ROCKY MTN. MIN. L. INST. 501, 511 (1983) (gas prices rose at annual rate of 40% between mid-1981 and December, 1981). Demand for natural gas, however, declined sharply as is evidenced by the fact that pipeline company sales were 12.3% lower in 1983 than in 1982. *See* DEPARTMENT OF ENERGY/ENERGY INFORMATION ADMINISTRATION, NATURAL GAS MONTHLY 29 (Mar. 1984).

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decline can be partly attributed to the energy crisis of a decade ago.[40] As a result of the crisis, consumers are conserving more energy and, therefore, using less natural gas.[41] In addition, alternative forms of fuel, most notably oil, are declining in cost and, consequently, natural gas users are rapidly converting.[42] When supply exceeds demand in a normal market situation, market forces usually work to gradually create a balance. However, a balance has not been the result in the natural gas industry, due mostly to the presence of take-or-pay provisions in gas purchase contracts.[43]

III. THE TAKE-OR-PAY PROVISION

A. *Evolution of the Take-or-Pay Concept*

1. Background

Take-or-pay provisions require the pipeline company to either take an amount of natural gas from the producer or, if the pipeline company does not want to take the gas, the company must pay for the specified amount.[44]

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40. *See* Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (energy conservation contributed to cause gas surplus).

41. *See id.*; *see also* DEPARTMENT OF ENERGY/ENERGY INFORMATION ADMINISTRATION, NATURAL GAS MONTHLY 29 (Mar. 1984) (demand for natural gas declined drastically in 1983).

42. *See, e.g.,* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1151 (D.C. Cir. 1985) (drop in oil prices reduced natural gas demand); Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (lower price of competing fuels caused surplus); Gulf Oil Corp. v. Tenneco, Inc., 608 F. Supp. 1493, 1495 (E.D. La. 1985) (oil prices factor in gas surplus); *see also* Greenwald, *Awash in an Ocean of Oil*, TIME, Feb. 3, 1986, at 52 (oil price on decline); Adair & Bloom, *Flexible Pricing and Other Partial Solutions to the Problems Faced by Gas Distributors*, 4 ENERGY L.J. 239, 239 n.1 (1983) (significant portion of industrial gas customers able to use other types of fuel). Additionally, the mild winter of 1982-83 adversely affected the natural gas market. *See* Gulf Oil Corp. v. Tenneco, Inc., 608 F. Supp. 1493, 1495 (E.D. La. 1985).

43. *See* Transcontinental Gas Pipe Line Corp. v. State Oil and Gas Bd., — U.S. —, —, 106 S. Ct. 709, 716, 88 L. Ed. 2d 732, 743 (1986) (recognition that supply and demand imbalance exists in natural gas market). In enacting the NGPA, Congress intended for the market to determine supply and demand of natural gas. *See id.* at —, 106 S. Ct. at 716-17, 88 L. Ed. 2d at 744.

44. *See* WILLIAMS & MYERS, MANUAL OF OIL AND GAS TERMS 882 (6th ed. 1984) (defining take-or-pay provision). Take-or-pay provisions are not limited strictly to natural gas contracts. *See, e.g.,* Allover Distrib., Inc. v. Kroger Co., 513 F.2d 1137, 1138-39 (7th Cir. 1975) (take-or-pay provision in contract for ice cream); Utah Int'l, Inc. v. Colorado-Utah Elec. Ass'n, Inc., 425 F. Supp. 1093, 1094-95 (D. Colo. 1976) (take-or-pay coal contract); Mobil Oil Corp. v. Tennessee Valley Auth., 387 F. Supp. 498, 501-02 (N.D. Ala. 1974) (take-or-pay electricity contract). Furthermore, a take-or-pay provision should be distinguished from a "take-and-pay" provision which requires the purchaser to take the quantity of gas and pay for the gas. *See* WILLIAMS & MYERS, MANUAL OF OIL AND GAS TERMS 881 (6th ed. 1984). The significant difference between the two provisions is that the purchaser is in default of the contract if he fails to "take" the gas under a take-and-pay clause, whereas under a take-or-pay clause, the purchaser does not breach the contract by not taking the gas. *See* Haughey v.

Take-or-pay provisions have not always been included in natural gas contracts.[45] Early agreements did not specify a minimum quantity of gas to be taken, and the amount that was actually taken was left to the purchaser's discretion.[46] When the buyers were not "taking" gas, producers simply shut down the wells and used them for storage reservoirs.[47]

Once interstate pipelines were constructed, however, minimum "take" clauses began to appear in gas sales contracts. The amounts of gas to be purchased under the clauses were calculated using various methods.[48] The most common method of calculation utilized was either taking a predetermined percentage of a producer's output,[49] or taking a fixed quantity from the producer.[50] The "take" provision was modified to "take-or-pay" to meet the producer's needs for current cash flow and insure performance by the pipeline companies.[51] The "take-or-pay" provision further allowed pipeline companies to choose when to take possession of the gas, thereby lessening

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Belmont Quadrangle Drilling Corp., 29 N.E.2d 649, 651 (N.Y. 1940) (example of take-and-pay provision in gas purchase contract).

45. *See* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 108-09 (1983) (early contracts did not contain take-or-pay provisions).

46. *See* Southwest Pipe Line Co. v. Empire Natural Gas Co., 33 F.2d 248, 250-51 (8th Cir. 1929) (example of early gas contract). *See generally* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 108-09 (1983) (discussion of early gas contracts).

47. *See* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 109 (1983) (practice of shutting down well when market for gas declined). Producers did not like to shut down their wells because such action is likely to result in water or sand encroachment. *See id.* at 110 n.84 (listing possible dangers involved in shutting in wells).

48. *See* Turner, *Natural Gas-Impact of Deregulation or Regulation on Sales Conracts*, 29 ROCK MTN. MIN. L. INST. 501, 522 (1983) (methods utilized were either fixed quantity of gas or fixed percentage of output).

49. *See* Turner, *Natural Gas-Impact of Deregulation or Regulation on Sales Contracts*, 29 ROCKY MTN. MIN. L. INST. 501, 522 (1983) (take-or-pay based on percentage of output). The percentages utilized in take-or-pay provisions fluctuate with the gas market. During the gas shortage, average take requirements were 90% of capacity. Currently, with the surplus, take requirements average 79%. *See id.*

50. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 881 (10th Cir. 1985) (fixed minimum amount of 4800 million BTU's per day), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986). *See generally* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 109 (1983) (during 1960's, one-thousand cubic feet ("MCF") per day for each 7300 MCF of reserves was common take requirement).

51. *See* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 110-11 (1983) (take-or-pay forces performance by pipeline). The provision enables a producer to receive a steady, assured income so the producer can pay operating expenses, taxes, etc. *See id.* at 111; *see also* Johnson, *Producer Viewpoint*, 1984 A.B.A. SEC. PUB. UTIL. L. REP.—PROCEEDINGS 90-91 (take-or-pay provides constant cash flow for producers); Watson, *Take or Pay Provisions in Producer Gas Sales Contracts*, in OIL & GAS AGREEMENTS 11-2 (1983) (provision guarantees cash flow).

the chance of over-filled storage facilities.[52]

2. Purposes

There are several purposes served by take-or-pay provisions, in favor of both producers and pipeline companies. First, the provision creates an atmosphere of stability in the producer-pipeline company relationship.[53] Prior to such provisions, pipeline companies took gas from producers only when the companies needed the gas, leaving the times and quantities of deliveries varied and unpredictable.[54] The resulting instability was unsatisfactory for the producer and inefficient as a whole, so the minimum "take" provision was utilized.[55]

Additionally, a take-or-pay provision minimizes the potentially harmful effect of a sudden change in market demand for gas.[56] But for the take-or-pay provision, a sudden decline in the market could leave producers with an unmarketable product.[57] Also, producers often use their take-or-pay contracts as collateral for securing loans for further exploration.[58]

Pipeline companies also derive a benefit from take-or-pay clauses.[59] Under a take-or-pay contract, the pipeline company can choose whether to pay for the gas or take the amount.[60] The quantity of gas specified in the take-or-pay provision may be considerably less than the quantity listed in the

52. *See* WILLIAMS & MYERS, MANUAL OF OIL AND GAS TERMS 882 (6th ed. 1984) (take-or-pay gives pipeline company choice of taking gas or paying for gas).

53. *See* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 108-09 (1983) (business between pipeline companies and producers erratic before utilization of take-or-pay).

54. *See id.* (prior to take-or-pay, producers forced to act at pipeline company's discretion); Johnson, *Producer Viewpoint*, 1984 A.B.A. SEC. PUB. UTIL. L. REP.—PROCEEDINGS 91 (take-or-pay protects producer from predatory acts of pipeline).

55. *See* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 108-09 (1983) (take-or-pay provision stablized pipeline company purchases).

56. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 882 (10th Cir. 1985) (take-or-pay eliminates market risks for producers), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986).

57. *See id.* (take-or-pay reduces the risk of fluctuations in cash flow, thereby encouraging investments in the natural gas industry; *see also* Transcontinental Gas Pipe Line Corp. v. State Oil & Gas Bd., — U.S. —, —, 106 S. Ct. 709, 712, 88 L. Ed. 2d 732, 738 (1986). The provision also compensates the producer for keeping his product ready for the pipeline company to purchase at any time. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 882 (10th Cir. 1985), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986).

58. *See* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 111 (1983) (guaranteed income from take-or-pay provisions act as collateral).

59. *See* WILLIAMS & MYERS, MANUAL OF OIL AND GAS TERMS 882 (6th ed. 1984) (take-or-pay allows flexibility in pipeline company's performance). *But see* Watson, *Take or Pay Provisions in Producer Gas Sales Contracts*, in OIL & GAS AGREEMENTS 11-2 (1983) (pipeline company has no self interest in take-or-pay provision).

60. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 885 (10th

contract itself, so the pipeline company can strategically choose which quantity to purchase.[61] Additionally, "makeup" clauses are often inserted alongside take-or-pay provisions.[62] A gas purchase contract with makeup rights allows the purchaser to pay for the gas and obtain delivery at a later time, often after a number of years.[63] Therefore, although the take-or-pay provision requires the pipeline company to pay for the gas, there is usually a certain amount of flexibility involved as to when the gas may be delivered.[64]

B. *Current Take-or-Pay Problems*

The effect of the take-or-pay provision has been blamed for the "chaos and turmoil" that currently exists in the natural gas industry.[65] Since the majority of gas purchase contracts are long term, the contracts currently in effect were entered into during the 1970's, when the industry was experiencing a severe gas shortage.[66] Today, pipeline companies are forced to purchase gas under terms that reflect a totally different market.[67] The end result is that the companies are still having to pay extremely high prices for a product that has declined sharply in demand.[68] Pipeline companies have entered

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Cir. 1985) (pipeline company performs by taking gas or paying bill), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986).

61. *See* WILLIAMS & MYERS, MANUAL OF OIL AND GAS TERMS 882 (6th ed. 1984) (take-or-pay gives pipeline company choice between alternatives). In a normal sales contract requiring the purchaser to take the product *and* pay for it, the buyer is in default if he chooses not to take delivery. *See id.* at 881 (example of normal contractual take-and-pay situation).

62. *See* Lone Star Gas Co. v. McCarthy, 605 S.W.2d 653, 654 (Tex. Civ. App.—Houston [1st Dist.] 1980, writ ref'd n.r.e.) (take-or-pay provision accompanied by makeup provision). The FERC now requires that all interstate gas contracts under its jurisdiction contain at least a five year makeup period. *See* 18 C.F.R. § 154.103 (1985) (requirement of five year makeup period in all gas contracts).

63. *See* Lone Star Gas Co. v. McCarthy, 605 S.W.2d 653, 656 (Tex. Civ. App.—Houston [1st Dist.] 1980, writ ref'd n.r.e.) (definition of makeup clause). For examples of makeup clauses, see Note, *Oil and Gas: "Take or Pay" Gas Contracts: Are They Subject to Royalty*?, 35 OKLA. L. REV. 150, 151-52 n.5 (1982).

64. *See* Lone Star Gas Co. v. McCarthy, 605 S.W.2d 653, 656 (Tex. Civ. App.—Houston [1st Dist.] 1980, writ ref'd n.r.e.) (makeup clause in gas purchase contract gives purchaser flexibility as to time of delivery).

65. *See* Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (quoting N. Clark & G. Clark, *Governments, Markets and Gas*, 1984 ENERGY, ECON. & ENVTL. INST. 16-17); *see also* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.05 (1985) (impact of take-or-pay issue on natural gas industry is substantial).

66. *See* Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (problem stems from market changing while long-term contracts still in effect).

67. *See id.* (prices in long term contracts based on erroneous 1978 expectations). The natural gas market changed from a market of shortages in 1978 to one of surplusage in 1982. *See* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1151 (D.C. Cir. 1985).

68. *See* DEPARTMENT OF ENERGY/ENERGY INFORMATION ADMINISTRATION, NATU-

into contracts with local distributors that effectively pass along the high prices[69] and eventually the consumer bears the inflated cost.[70] In addition, producers who could sell a less expensive product cannot disturb the already existing chain of long term contractual obligations and, therefore, cannot participate in the gas market.[71]

Furthermore, there is a certain amount of exigency involved in finding solutions for the problems plaguing the gas industry.[72] Demand for the product is continuing to decrease, and a significant number of present users are contemplating switching to an alternative, less troublesome fuel.[73] Consequently, the need to find an efficient answer to the take-or-pay problem is critical to the industry.[74]

RAL GAS MONTHLY 29 (Mar. 1984) (pipeline sales fell 12.3% between 1982 and 1983). Despite the drop in sales, gas prices rose at an annual rate of 40% during a six-month period in 1981. *See* Turner, *Natural Gas-Impact of Deregulation or Regulation on Sales Contracts*, 29 ROCKY MTN. MIN. L. INST. 501, 511 (1983); *see also* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1151 (D.C. Cir. 1985) (prices remained high during surplus).

69. *See* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1150 (D.C. Cir. 1985) ("minimum bill" contracts cover pipelines' take-or-pay obligations). Minimum bill provisions appear in contracts between pipelines and their customers (usually local distributors), and require the customer to pay for a quantity of gas regardless of whether the customer actually takes the gas. *See id.* at 1149. The minimum bill provision is similar to take-or-pay provisions, except involving different parties. *See id.* at 1150-51.

70. *See id.* at 1151 (take-or-pay costs passed to consumers through high rates). *See generally* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 774-75 (1983) (illustration of take-or-pay costs passing from producer to consumer).

71. *See* NEW YORK TIMES, Feb. 6, 1983, § 3, at 2, col. 1 (cheaper producers barred from gas market due to existence of long-term contracts in gas industry).

72. *See* 1558 FOSTER NAT. GAS REP. 1 (Mar. 6, 1986) (report of statements made by FERC Director). During a recent interview, Kenneth Williams, Director of the FERC Office of Pipeline and Producer Regulation, stated that the timely solution to the problems confronting the natural gas industry is "crucial" to the future of the industry. *See id.* at 1-3. As an illustration of the seriousness of the situation, take-or-pay prepayments for gas not taken by pipeline companies have risen from $51.6 million in 1977 to $1.148 billion in 1984. *See* 1559 FOSTER NAT. GAS. REP. 29 (Mar. 13, 1986) (discussion of American Gas Association study showing worsening of take-or-pay problems).

73. *See* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.02(1) (1985) (natural gas users switching to oil if no improvement in natural gas industry situation); *see also* Adair & Bloom, *Flexible Pricing and Other Partial Solutions to the Problems Faced by Gas Distributors*, 4 ENERGY L.J. 239, 239 n.1 (1983) (customers with dual fuel capacity [may use more than one type fuel] account for 52% of industrial market gas sales). Added to the alternative fuel availability threat is the availability of imported gas. *See* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.02(2) (1985) (imports of Canadian gas rose 20% between 1983 and 1984).

74. *See* 1567 FOSTER NAT. GAS REP. 17 (May 9, 1986) (discussion of severity of take-or-pay liabilities). As an example of the magnitude of the take-or-pay problem, Tennessee Gas Pipeline Co., a major pipeline company, predicts that by the end of 1986, it will be liable for

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IV. Previous Regulatory Treatment of Take-or-Pay Provisions

As take-or-pay provisions began to be utilized more often, the need to control the possibility of accompanying difficulties became evident. In the mid-1960's, the FPC required an annual report from each pipeline company, which included information on the company's take-or-pay obligations.[75] In 1967, the FPC issued a rule that required all subsequent take-or-pay contracts to contain a makeup clause which permitted the pipeline company at least five years to take the gas.[76] Furthermore, the FPC reviewed take-or-pay balances when deciding whether to issue the necessary certification for a producer to sell gas to a pipeline company.[77] In 1970, the FPC considered limiting the minimum take provision to a specific amount,[78] but decided not to enact the rule.[79] The FPC concluded that the limitations "might reduce the flexibility of negotiations between producers and pipelines and could, thereby, reduce gas supplies to the interstate market."[80]

The Federal Energy Regulatory Commission (FERC), which replaced the FPC in 1977,[81] issued a take-or-pay policy statement on December 23, 1982, indicating the Commission's growing concern toward problems associated

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$3.1 billion in take-or-pay contracts. *See id.* Between 1981 and December, 1984, seventeen pipeline companies had made take-or-pay prepayments (i.e., the pipelines made the payment without taking the gas) totalling $2.73 billion. *See id.* at 21.

75. *See* 18 C.F.R. § 260.7 (1985) (requires annual report of gas supply from pipeline companies); *see also* FPC v. Sunray DX Oil Co., 391 U.S. 9, 48 (1968) (FPC requires and publishes take-or-pay reports).

76. *See* 18 C.F.R. § 154.103 (1985) (requirement of five year makeup clause). The order applies to all natural gas contracts executed after February 1, 1967. *See id.*; *see also* FPC v. Sunray DX Oil Co., 391 U.S. 9, 50 (1968) (mandatory makeup provision intended to solve take-or-pay problems). *See generally* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 114-15 (1983) (discussion of legislative history of § 154.103 and effect of mandatory makeup order).

77. *See* FPC v. Sunray DX Oil Co., 391 U.S. 9, 47-52 (1968) (take-or-pay position factor in pipeline certification proceedings). Take-or-pay positions were considered evidence of whether the pipeline company actually "needed" the gas; if there was not a need, the pipeline company would not receive a certificate of public convenience and necessity, which is required before the company can do business. *See* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 115 (1983).

78. *See* Notice of Proposed Rulemaking, 35 FED. REG. 15,163 (1970); *see also* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 115 (1983) (FPC proposed limit on minimum take provision).

79. *See Limitation on Provisions in Natural Gas Rate Schedules Relating to Minimum Take Provisions, Docket No. R-400, Order Terminating Proposed Rulemaking*, 45 FPC 543, 544 (1971).

80. *Id.*; *see also* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 115-16 (1983) (discussion of denial of proposed rule).

81. *See* Department of Energy Org. Act of 1977, 42 U.S.C. § 7151a (1982) (FPC replaced by FERC).

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with the provision.[82] Among other things, the FERC recognized that high take-or-pay liabilities act to shield the price of deregulated gas from market forces.[83] In the statement, the FERC disclosed its intention to apply preferential treatment to future gas purchase contracts containing 75% annual take-or-pay liability or less.[84] The statement, however, does not affect existing contracts, and there has not been any indication that the FERC intends to reduce existing take-or-pay obligations.[85] Consequently, current take-or-pay provisions are given full force and effect.

V. SOLUTIONS

As the situation in the natural gas market deteriorated, pipeline companies were forced to disregard their take-or-pay obligations and purchase only the amount of gas they could market.[86] Not surprisingly, this action prompted a substantial amount of litigation.[87] Once the lawsuits were filed, however, a considerable amount of uncertainty existed as to whether the courts should resolve the issue or whether the FERC should become involved.[88] Presently, the proper forum for the take-or-pay issue has not been

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82. *See* 18 C.F.R. § 2.103 (1985). The FERC was concerned that under current conditions, pipeline companies may not have the flexibility to respond to a changing market. *See* Hollis, *Notable Recent Developments in Federal Natural Gas Regulation*, 34 INST. ON OIL & GAS L. & TAX'N 31, 38 (1983).

83. *See* 18 C.F.R. § 2.103(a) (1985) (statement of policy regarding take-or-pay provisions).

84. *See id.* § 2.103(b). The FERC stated that it would apply a rebuttable presumption to pipeline rate cases that future take-or-pay payments will not be given rate base treatment if: (1) the payments exceed 75% of annual deliverability, and (2) the contract is made or amended on or after December 23, 1982. *See id.*

85. *See* Hollis, *Notable Recent Developments in Federal Natural Gas Regulations*, 34 INST. ON OIL & GAS L. & TAX'N 31, 39 (1983) (policy statement does not apply to existing contracts). The FERC stated that it planned to continue its ongoing determination of whether to deal with take-or-pay provisions in pre-existing contracts. *See id.*

86. *See* 1567 FOSTER NAT. GAS REP. 24 (May 9, 1986) (example of pipeline company purchasing only the marketable quantity of gas). Southern Natural Gas Co., a major pipeline company, is currently disregarding their take-or-pay liabilities and making payments only on gas that can be marketed. *See id.* Natural Gas Pipeline Co. of America, another major pipeline, is currently practicing the same policy. *See id.* at 23.

87. *See, e.g.*, International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 884 (10th Cir. 1985) (buyer breached take-or-pay provision), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986); Danden Petroleum, Inc. v. Northern Natural Gas Co., 615 F. Supp. 1093, 1095 (N.D. Tex. 1985) (suit for breach of take-or-pay provision); Sid Richardson Carbon & Gasoline Co. v. Internorth, Inc., 595 F. Supp. 497, 498-99 (N.D. Tex. 1984) (pipeline company refused to make payment under take-or-pay provision).

88. *Compare* Danden Petroleum, Inc. v. Northern Natural Gas Co., 615 F. Supp. 1093, 1102-03 (N.D. Tex. 1985) (proper forum for take-or-pay issue is court rather than FERC) *and* Sid Richardson Carbon & Gasoline Co. v. Internorth, Inc., 595 F. Supp. 497, 499 (N.D. Tex. 1984) (court refused to refer case to FERC) *with* Gulf Oil Corp. v. Tenneco, Inc., 608 F. Supp.

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decided.[89] Therefore, the matter will be examined through both the judicial and regulatory perspectives, along with possible legislative resolutions.

A. *Judicial*

When the take-or-pay problem is before the court, the most promising defenses for the pipeline companies are basic contractual defenses, namely force majeure clauses, commercial impracticability, mutual mistake of fact, and frustration of purpose.[90] Of course, the probability of success of any contractual defense depends on the facts of each particular situation, such as the terms of the contract and the behavior of the parties.[91]

Most gas purchase contracts usually contain some form of force majeure clause.[92] A force majeure clause in a contract lists various events, the occurrence of any one of which excuses the parties from performance.[93] Under-

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1493, 1503-04 (E.D. La. 1985) (FERC should determine take-or-pay issue) *and* Post v. Perry Gas Transmission, Inc., 616 F. Supp. 1, 3 (N.D. Tex. 1983) (stay in proceedings to refer take-or-pay conflict to FERC).

89. *See* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.06(4) (1985) (indecision on proper jurisdiction for take-or-pay disputes). The central question involved in the jurisdiction issue is whether take-or-pay conflicts fall within the primary jurisdiction of the FERC. Traditionally, pipeline companies prefer to have their disputes settled with the FERC. *See id.* (FERC more favorable forum for pipelines). *See generally* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 66-81 (1984) (discussion of primary jurisdiction of FERC).

90. *See* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 81-85 (1984) (possible contractual defenses in take-or-pay dispute); MCCARTHY, *Interstate Pipeline Company Viewpoint*, 1984 A.B.A. SEC. PUB. UTIL. L. REP.—PROCEEDINGS 98-99 (force majeure and impracticability are take-or-pay defenses).

91. *See* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.07 (1985) (contractual defense dependent on specific contractual provisions). Additionally, the law on contractual defenses varies between jurisdictions. *See id.*

92. *See, e.g.*, International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 882 (10th Cir. 1985) (take-or-pay gas contract with force majeure clause), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986); Gulf Oil Corp. v. FERC, 706 F.2d 444, 447-48 (3d Cir. 1983) (force majeure contained in gas purchase contract), *cert. denied*, 464 U.S. 1038 (1984); Superior Oil Co. v. Transco Energy Co., 616 F. Supp. 98, 108 (W.D. La. 1985) (take-or-pay contract containing force majeure clause).

93. *See* WILLIAMS & MYERS, MANUAL OF OIL AND GAS TERMS 333-34 (6th ed. 1984). The following is an example of a force majeure clause found in a gas purchase contract containing a take-or-pay provision:

> Either party shall be excused for delay or failure to perform its agreements and undertakings, in whole or in part, when and to the extent that such failure or delay is occasioned by fire, flood, wind, lightning, or other acts of the elements, explosion, act of God, act of the public enemy, or interference of civil and/or military authorities, mobs, labor difficulties, vandalism, sabotage, malicious mischief, usurpation of power, depletion of wells, freezing or accidents to wells, pipelines, permanent closing of Buyers operations . . . or other casualty or cause beyond the reasonable control of the parties. . . .

International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 882 (10th Cir. 1985), *cert.*

standably, no general statements can be made regarding the effectiveness of the force majeure defense since its success depends on the specific events enumerated in the particular clause.[94] Very few force majeure clauses, however, contain provisions on market changes.[95] Therefore, given a strict reading of the clause, the pipeline company will not be relieved of take-or-pay obligations due to changes in the market.[96] If the force majeure clause contains general language providing for any event beyond the parties' control, an argument may be made that the declining gas market, economic recession, and unusually mild winters are factors fulfilling the provision's requirements for excuse.[97]

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denied, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986). *See generally* Kirkham, *Force Majeure—Does It Really Work?*, 30 ROCKY MTN. MIN. L. INST. §§ 6.01-6.06 (1984) (discussion of force majeure clause); Black, *Sales Contracts and Impracticability in a Changing World*, 13 ST. MARY'S L.J. 247, 251-54 (1981) (overview of force majeure clauses in sales contracts).

94. *See, e.g.*, Field Container Corp. v. ICC., 712 F.2d 250, 257 (7th Cir. 1983) (severe winter no excuse since not contained in force majeure clause), *cert. denied*, 464 U.S. 1039 (1984); Jon-T Chem., Inc. v. Freeport Chem. Co., 704 F.2d 1412, 1414-15 (5th Cir. 1983) (weather mentioned in force majeure clause excused nonperformance due to snowstorm); Gulf Oil Corp. v. FPC, 563 F.2d 588, 601-02 (3d Cir. 1977) (unavailability of natural gas no excuse since not listed in force majeure), *cert. denied*, 434 U.S. 1062 (1978). *See generally* Kirkham, *Force Majeure—Does It Really Work?*, 30 ROCKY MTN. MIN. L. INST. § 6.05(2)(b) (1984) (discussing drafting force majeure clause to include precise events).

95. *See* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 81 (1984) (typical force majeure does not refer to market).

96. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 882 (10th Cir. 1985) (force majeure clause in take-or-pay gas contract with no provision for market conditions did not excuse performance), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986); McCarthy, *Interstate Pipeline Company Viewpoint*, 1984 A.B.A. SEC. PUB. UTIL. L. REP.—PROCEEDINGS 98 (traditional gas contract force majeure clause makes no mention of gas market). However, there have been several recent instances of pipeline companies declaring force majeure on their take-or-pay obligations. *See* 1525 FOSTER NAT. GAS REP. 7-8 (July 11, 1985) (reporting pipeline companies invoking force majeure clauses). On June 27, 1985, ANR Pipeline Co. declared that they were involving force majeure under their take-or-pay contracts and would not honor their obligations under the contracts. *See id.* ANR listed mild temperatures, economic recession, low price of competing fuels, and increased consumer conservation as factors contributing to the decision. United Gas Pipe Line Company declared force majeure on their take-or-pay contracts on July 2, 1985. *See id.* at 7. On July 25, 1985, Transcontinental Gas Pipe Line Corp. invoked force majeure on its take-or-pay obligations, citing full storage capacity as the principle reason. *See* 1529 FOSTER NAT. GAS REP. 12 (Aug. 8, 1985).

97. *See* McCarthy, *Interstate Pipeline Company Viewpoint*, 1984 A.B.A. SEC. PUB. UTIL. L. REP.—PROCEEDINGS 98-99; *see also* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.07 (recognition that economy, weather, etc. are beyond pipeline company's control). Additionally, a pipeline company should argue that government intervention in the form of the pricing scheme set forth in the NGPA caused the pipeline company to be unable to take the gas and, therefore, was a primary cause of the nonperformance. *See* Kirkham, *Force Majeure—Does It Really Work?*, 30 ROCKY MTN. MIN. L. INST. § 6.03(4) (1984) (courts recognize government intervention as valid force majeure

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Another possible contractual defense for the pipeline company is commercial impracticability.[98] The defense of impracticability relieves a party of contractual obligations when performance has been made impracticable by an occurrence which significantly increases the cost, risk, or difficulty of the party's performance.[99] Under the impracticability theory, a pipeline company should be excused from taking the specific quantity of gas because economic factors, government intervention, and declining oil prices have combined to render performance unreasonable.[100] The major case in support of providing relief to pipeline companies is *Aluminum Company of America v. Essex Group, Inc.*[101] In *Aluminum Company of America* (ALCOA), the court excused ALCOA from performance when ALCOA's costs rose unexpectedly due to increased pollution control costs and OPEC price increases.[102] The case is an example of the court relieving a party of

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excusing performance); Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 81-82 (1984) (action by government legitimate force majeure defense in take-or-pay contract). *But see* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 885 (10th Cir. 1985) (force majeure will not excuse pipeline company in take-or-pay contract since pipeline can always perform by paying), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986). The doctrine of "ejusdem generis" may also prove to be an obstacle when a pipeline company's defense is based on a general cause beyond the control of the parties. *See* Carney, *The Nature and Extent of the Excuse Provided by a Force Majeure Event Under a Coal Supply Agreement*, 4 E. MIN. L. FOUND. § 11.02(1)(c) (1983). The rule states that a term such as "causes beyond the parties' control" will be interpreted to include only events similar to those events enumerated in the force majeure clause. *See id.* (rule strictly applied by courts).

98. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 886-87 (10th Cir. 1985) (buyer asserting impracticability as defense in take-or-pay contract), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986); Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 82 (1984) (commercial impracticability possible pipeline defense).

99. *See* U.C.C. § 2-615 (1984) (section dealing with commercial impracticability); *see also* Aluminum Co. of Am. v. Essex Group, Inc., 499 F. Supp. 53, 73 (W.D. Pa. 1980) (distinguishing impracticability from frustration of purpose). A preliminary search will reveal that gas purchase contracts are within the purview of the Uniform Commercial Code. *See* U.C.C. § 2-107(1) (section enumerating types of transactions included in the U.C.C.). Furthermore, section 2-615 is generally held to extend to buyers as well as sellers, although buyers are not specifically mentioned in the section. *See* Nora Springs Coop. Co. v. Brandau, 247 N.W.2d 744, 748 (Iowa 1976) (comment 9 of § 2-615 extends section to buyers). *See generally* Carney, *The Nature and Extent of the Excuse Provided by a Force Majeure Event Under a Coal Supply Agreement*, 4 E. MIN. L. FOUND. § 11.02(4) (1983) (discussing applicability of § 2-615 to buyers).

100. *See* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 82 (1984) (gas market changes rendered performance by pipeline companies impracticable). The pipeline company must also prove that the combined factors were not foreseeable at the time the parties made the agreement. *See id.*

101. 499 F. Supp. 53 (W.D. Pa. 1980).

102. *See id.* at 72-73. Aluminum Company of America (ALCOA) entered into a contract to smelt aluminum for Essex. *See id.* at 57. The contract's base price was to be derived using a

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contractual duties because of cost increases caused by unforeseeable changes in market conditions.[103] However, the vast majority of cases dealing with changes in the marketplace have denied relief for the burdened party.[104] The commercial impracticability defense, therefore, as currently interpreted, is not a promising means of excusing a pipeline company's performance under a take-or-pay provision.[105]

Frustration of purpose is another contractual defense that a pipeline com-

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price escalation formula which utilized the wholesale price index as a guide to account for increases in costs. *See id.* at 58. The index failed, however, to accurately reflect the rising cost of electricity; therefore, ALCOA was to suffer an estimated loss on the contract of $75 million. *See id.* at 58-59. ALCOA's electricity costs increased due to unexpected pollution control costs and rising oil prices. *See id.* at 58. The court reformed the contract to reduce ALCOA's future losses. *See id.* at 79-80. *But see In re* Westinghouse Elec. Corp. Uranium Contracts Litigation, 517 F. Supp. 440, 457-58 (E.D. Va. 1981) (criticizing ALCOA decision). *See generally* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 84-85 (1984) (analysis of pipeline recovery under ALCOA); Comment, *Equitable Reformation of Long-Term Contracts—The "New Spirit" of ALCOA*, 1982 UTAH L. REV. 985, 993-1007 (discussion of ALCOA decision).

103. *See* Aluminum Co. of Am. v. Essex Group, Inc., 499 F. Supp. 53, 72-73 (W.D. Pa. 1980) (impracticability valid defense when market change involved). Courts have also awarded relief when nonperformance is caused by governmental intervention. *See, e.g.*, The Kronprinzessin Cecilie, 244 U.S. 12, 20-24 (1917) (ship owner justified in not making voyage as per contract due to war); Eastern Air Lines, Inc. v. McDonnell Douglas Corp., 532 F.2d 957, 995-96 (5th Cir. 1976) (Vietnam War constituted governmental intervention excusing party from performance); The Claveresk, 264 F. 276, 281-82 (2d Cir. 1920) (government requisition of ship relieved party of performance). *See generally* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 81-82 (1984) (discussing effect of governmental intervention on take-or-pay defense).

104. *See, e.g.*, Iowa Elec. Light & Power Co. v. Atlas Corp., 467 F. Supp. 129, 134-35 (N.D. Iowa 1978) (seller not excused when market changed), *rev'd on other grounds*, 603 F.2d 1301 (8th Cir. 1979), *cert. denied*, 445 U.S. 911 (1980); Eastern Airlines, Inc. v. Gulf Oil Corp., 415 F. Supp. 429, 437-39 (S.D. Fla. 1975) (escalated costs due to oil embargo no excuse); Missouri Pub. Serv. Co. v. Peabody Coal Co., 583 S.W.2d 721, 727-28 (Mo. Ct. App. 1979) (market changes provide no relief under impracticability defense). *See generally* Black, *Sales Contracts and Impracticability in a Changing World*, 13 ST. MARY'S L.J. 247, 267-74 (1981) (discussion of commercial impracticability and market changes). Additionally, pipeline companies face an obstacle in asserting the impracticability defense since a pipeline can perform under a take-or-pay provision by either taking the gas or paying for it. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 885 (10th Cir. 1985), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986). Therefore, since the pipeline company can perform in two ways, the court is likely to hold that performance is not impracticable. *See id.* (impracticability of one alternative no excuse if other alternative is practicable).

105. *See* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 84 (1984) (commercial impracticability not promising defense for take-or-pay); Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 793-95 (1983) (probability exists that performance under take-or-pay contracts are not commercially impracticable).

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pany may assert.[106] The frustration of purpose defense is similar to that of commercial impracticability.[107] The only major difference between the two is that the performance of the parties is unhindered under frustration of purpose, while under impracticability performance has been impeded.[108] The frustration of purpose defense is more suited to the take-or-pay situation since performance by the pipeline company is still possible.[109] In the take-or-pay scenario, the pipeline company entered into the contract for the sole purpose of reselling the gas to local distributors.[110] Thus, when the gas market became virtually nonexistent, the pipeline company's purpose for entering the transaction was affected.[111] Although the frustration of purpose defense appears to be well-suited to the take-or-pay problem, American courts have traditionally not been receptive to the defense.[112] Consequently,

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106. *See, e.g.*, Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 81-85 (1984) (frustration possible contractual defense for pipeline); Pierce, *Natural Gas Regulaton, Deregulation, and Contracts*, 68 VA. L. REV. 63, 104-10 (1982) (frustration of purpose potential contract law remedy for pipelines); Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 779-83 (1983) (application of frustration defense to gas purchase contracts).

107. *See* RESTATEMENT (SECOND) OF CONTRACTS § 265, comment a (1981) (similarities between commercial impracticability and frustration of purpose).

108. *See id.*; *see also* Aluminum Co. of Am. v. Essex Group, Inc., 499 F. Supp. 53, 73 (W.D. Pa. 1980) (frustration of purpose applies when party's performance is rendered meaningless since principal purpose is frustrated). Although the frustration defense differs from commercial impracticability, the two defenses involve essentially the same considerations. *See* RESTATEMENT (SECOND) OF CONTRACTS § 265, comment a (1981). In order to obtain relief, the frustrated party must show: (1) that the contract's primary purpose is undermined; (2) that the frustration is substantial; and (3) that the non-occurrence of the event was a basic assumption underlying the making of the contract. *See id. See generally* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 781-82 (1983) (discussing frustration of purpose under RESTATEMENT (SECOND) OF CONTRACTS); Carney, *The Nature and Extent of the Excuse Provided by a Force Majeure Event Under a Coal Supply Agreement*, 4 E. MIN. L. FOUND. § 11.02(1)(a) (1983) (application of frustration of purpose defense to coal supply contracts).

109. *See* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 885 (10th Cir. 1985) (performance under take-or-pay accomplished by taking gas or paying for it), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986).

110. *See* MCDONALD, NATURAL GAS: THE NECESSITY OF DEREGULATION 5 (1982) (pipeline companies transport and sell gas to local distribution companies).

111. *See* RESTATEMENT (SECOND) OF CONTRACTS § 265 (1981) (party is excused from performance when purpose is frustrated). If the pipeline had known there was no market for the gas, it would not have entered into the contract to accept the gas. *See id.* § 265, comment a (requirement that principal purpose of contract be substantially frustrated); *see also* Carney, *The Nature and Extent of the Excuse Provided by a Force Majeure Event Under a Coal Supply Agreement*, 4 E. MIN. L. FOUND. § 11.02(1)(a) (1983) (under coal supply contract, buyers' purpose affected if buyer no longer needs coal).

112. *See, e.g., In re* Westinghouse Elec. Corp. Uranium Contracts Litigation, 517 F.

a court confronted with a take-or-pay conflict will likely reject the pipeline company's frustration of purpose argument and deny relief.[113]

A fourth possible contractual defense that could absolve the issue is the doctrine of mutual mistake.[114] The mutual mistake defense involves a basic assumption underlying the making of the contract which later proves to be erroneous.[115] The pipeline company could argue that there was a basic assumption, in the making of the take-or-pay contract, that the market for natural gas would remain constant.[116] Moreover, the fact that a gas shortage was in existence at the time the parties executed the contract is further support that the parties did not contemplate a complete reversal of market conditions.[117] The success of the mutual mistake defense in take-or-

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Supp. 440, 460 (E.D. Va. 1981) (party assuming risks associated with nuclear fuel contract precluded frustration of purpose defense); Haas v. Pittsburg Nat'l Bank, 495 F. Supp. 815, 819 (W.D. Pa. 1980) (frustration of purpose provides no relief where party has assumed risk of market changes); Ma v. Community Bank, 494 F. Supp. 252, 257 (E.D. Wis. 1980) (frustration of purpose not applicable since intervening events not substantial). *But see* West Los Angeles Inst. for Cancer Research v. Mayer, 366 F.2d 220, 223-26 (9th Cir. 1966) (seller of business relieved of performance under sales contract when IRS rule frustrated tax benefits), *cert. denied*, 385 U.S. 1010 (1967); Aluminum Co. of Am. v. Essex Group, Inc., 499 F. Supp. 53, 78 (W.D. Pa. 1980) (party entitled to relief under frustration of purpose defense). *See generally* Sirianni, *The Developing Law of Contractual Impracticability and Impossibility: Part I*, 14 U.C.C. L.J. 30, 37-40 (1981) (discussion of doctrine of frustration of purpose).

113. *See* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 81-85 (1984) (contractual defenses not likely to provide pipeline company relief in take-or-pay conflict); Smith, *Effect of the Uniform Commercial Code on the Operation and Litigation of Natural Gas Contracts*, 14 COLO. LAW. 1809, 1810-11 (1985) (relief for gas purchasers not likely under frustration of purpose).

114. *See* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 82 (1984) (mutual mistake possible defense for pipeline company).

115. *See* RESTATEMENT (SECOND) OF CONTRACTS § 152 (1981). In order to establish mutual mistake, the following requirements must be met: (1) the mistake was made at the time the contract was formulated; (2) the mistake concerns a basic assumption on which the contract was made; (3) the mistake has a material effect on performance under the contract; and (4) the party must not have assumed the risk. *See id.* The major difference between impracticability and mutual mistake is that the mistake must exist at the time the contract is made. *See* Murray, *Long-Term Supply Contracts: Foreseeing the Unforeseeable*, 2 E. MIN. L. FOUND. § 2.03(1) (1981) (comparison of mistake with impracticability).

116. *See* RESTATEMENT (SECOND) OF CONTRACTS § 152 (1981) (mutual mistake requires mistake as to basic assumption in existence at making of contract); *see also* Aluminum Co. of Am. v. Essex Group, Inc., 499 F. Supp. 53, 70 (W.D. Pa. 1980) (relief granted on grounds of mutual mistake dealing with changes in market). *But see* International Minerals & Chem. Corp. v. Llano, Inc., 770 F.2d 879, 882 (10th Cir. 1985) (producers purpose for take-or-pay is eliminating market risks), *cert. denied*, — U.S. —, 106 S. Ct. 1196, 89 L. Ed. 2d 310 (1986). Additionally, the mistake must be one of fact, and not a mere mistaken opinion or prediction concerning a future event. *See* KAUFMAN, CORBIN ON CONTRACTS § 579A (Supp. 1984).

117. *See* Maryland People's Counsel v. FERC, 761 F.2d 768, 771 (D.C. Cir. 1985) (current take-or-pay contracts executed during gas shortage). If, however, the pipeline companies

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pay contracts can only be estimated since the courts have yet to confront the issue.[118]

Finally, another potential pipeline company defense involves violations of public policy.[119] Courts generally refuse to enforce contracts that are deemed contrary to the public interest.[120] The take-or-pay provision needlessly inflates the cost of natural gas by forcing gas pipeline companies to pay prices that are well above current market prices.[121] The excess cost eventu-

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assumed the market would not take a drastic change, but the producers did foresee changes, the mistake may have been unilateral and, consequently, the pipeline companies would not obtain relief. *See* Leasco Corp. v. Taussig, 473 F.2d 777, 781 (2d Cir. 1972) (unilateral mistake does not make contract unenforceable); *In re* Westinghouse Elec. Corp. Uranium Contracts Litigation, 517 F. Supp. 440, 458 (E.D. Va. 1981) (one party's mistake cannot excuse its performance).

118. *See* Pierce, *Issues in Gas Contract Litigation*, 35 INST. ON OIL & GAS L. & TAX'N 61, 82 (1984) (mutual mistake possible defense for pipeline companies). Another contractual defense that deserves mention is the impossibility defense. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 778-79 (1983). In order for a party to successfully assert the impossibility defense, courts originally required performance to have been made impossible due to the destruction of the subject matter. *See* Taylor v. Caldwell, 122 Eng. Rep. 309, 314 (Q.B. 1863). Modern courts, however, have granted relief under the impossibility defense when economic hardship prevents performance; therefore, a pipeline company may possibly be successful in asserting the impossibility defense in take-or-pay situations. *See, e.g.*, Transatlantic Fin. Corp. v. United States, 363 F.2d 312, 315 (D.C. Cir. 1966) (impossibility defense excuses performance involving excessive cost); *In re* Westinghouse Elec. Corp. Uranium Contracts Litigation, 517 F. Supp. 440, 451 (E.D. Va. 1981) (impossibility equivalent to impracticability); Swift Textiles, Inc. v. Lawson, 219 S.E.2d 167, 170 (Ga. Ct. App. 1975) (proof of strict impossibility not required for relief under impossibility defense). *See generally* Comment, *The Energy Crisis and Economic Impossibility in Louisiana Fuel Requirements Contracts: A Gameplan for Reform*, 49 TUL. L. REV. 605, 607-23 (1975) (discussion of impossibility defense in economic hardship context).

119. *See* Sirianni, *The Developing Law of Contractual Impracticability and Impossibility: Part II*, 14 U.C.C. L.J. 146, 171-76 (1981) (contracts against public policy unenforceable).

120. *See, e.g.*, Northwest Airlines, Inc. v. Alaska Airlines, Inc., 351 F.2d 253, 256-58 (9th Cir. 1965) (contract unenforceable since opposed to public interest); Driessen v. Freborg, 431 F. Supp. 1191, 1196 (D.N.D. 1977) (labor contract requiring mandatory maternity leave unenforceable because contrary to public policy); Chicago & N.W. Ry. Co. v. Rissler, 184 F. Supp. 98, 101 (D. Wyo. 1960) (contract unenforceable if it contravenes public welfare). *See generally* Sirianni, *The Developing Law of Contractual Impracticability and Impossibility: Part II*, 14 U.C.C. L.J. 146, 173 (1981) (discussion of public policy defense); Sterk, *Enforceability of Agreements to Arbitrate: An Examination of the Public Policy Defense*, 2 CARDOZO L. REV. 481, 493-543 (1981) (discussion of public policy defense in arbitration context).

121. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 774-75 (1983) (take-or-pay causes pipeline companies to purchase high priced gas). Additionally, the long-term take-or-pay contracts bar producers with less-expensive gas from participating in the natural gas market. Consumers, therefore, are forced to pay high rates for high priced gas when lower priced gas is available. *See id.* at 775.

ally passes to the general public in the form of excessive rates.[122] Therefore, the general public is the ultimate victim of the effects of take-or-pay provisions.[123] The problem is so extensive[124] that all gas contracts containing take-or-pay provisions should be construed as being against public policy and should not be enforced.[125] Each of the contractual defenses previously discussed appears suited to provide an adequate solution to the take-or-pay problem. Consequently, the defenses should be seriously considered by any court confronted with the issue.

B. *Regulatory*

Assuming the proper forum for the take-or-pay issue is with the FERC, the Commission has several options for resolution of the problem. Initially, the FERC has the power to set aside or modify provisions in any existing contract.[126] The Natural Gas Policy Act's primary purpose is to protect consumers from exploitative pricing by gas companies.[127] The FERC

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122. *See* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1151 (D.C. Cir. 1985) (take-or-pay costs pass to consumer in form of high rates); *Natural Gas Regulation and Market Disorder*, 18 TULSA L.J. 619, 640 (1983) (consumer prices will continue to rise due to take-or-pay clauses); *see also* 15 U.S.C. § 717a (1982) (business of selling and transporting natural gas is affected with public interest).

123. *See* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1151 (D.C. Cir. 1985) (consumers charged high rates due to take-or-pay provision).

124. *See* 1 AMERICAN GAS ASSOCIATION, REGULATION OF THE GAS INDUSTRY § 2(2)(b) (Supp. 1985) (natural gas utilized in over 43 million residential dwellings).

125. *See* Sirianni, *The Developing Law of Contractual Impracticability and Impossibility: Part II*, 14 U.C.C. L.J. 146, 172 (1981) (harm must affect large group to entail violation of public interest). The public policy defense has yet to be construed in a take-or-pay context. *But see* Kerr-McGee Corp. v. Northern Util., Inc., 500 F. Supp. 624, 626-36 (D. Wyo. 1980) (gas contract provision resulting in exorbitant costs to consumers held unenforceable as violation of public policy), *rev'd*, 673 F.2d 323 (9th Cir. 1982). *See generally* Comment, *Contracts Affecting the Personal Rights of One Not a Party to the Contract—A Comment on Wynn v. Monterey Club*, 5 WHITTIER L. REV. 355, 372-81 (1983) (discussion of public policy defense).

126. *See* Permian Basin Area Rate Cases, 390 U.S. 747, 784 (1968) (Commission has authority to modify contractual provision violating public interest); Michigan Consol. Gas Co. v. Panhandle E. Pipe Line Co., 226 F.2d 60, 66 (6th Cir. 1955) (provisions in gas contract may be limited by Commission). The FERC is given the power to alter any contract it deems unjust, unduly discriminatory, preferential, or unreasonable. *See* United Gas Pipe Line Co. v. Mobil Gas Serv. Corp., 350 U.S. 332, 341 (1956).

127. *See, e.g.*, Atlantic Ref. Co. v. Public Serv. Comm'n, 360 U.S. 378, 389 (1959) (intent of Congress to protect consumer with regard to price); FPC v. Hope Natural Gas Co., 320 U.S. 591, 612 (1944) (provisions of NGA designed to protect consumer); West Virginia Pub. Serv. Comm'n v. United States Dep't of Energy, 681 F.2d 847, 854-55 (D.C. Cir. 1982) (NGPA protects consumer from exploitation by gas companies). The intent behind the pricing policy of the Act is that "gas should be sold at the lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest." *See* Cincinnati Gas & Elec. Co. v. FPC, 389 F.2d 272, 276 (6th Cir.), *cert. denied*, 393 U.S. 826 (1968); *see also* 15 U.S.C. §§ 3301-3432 (1982) (NGPA).

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should give effect to the underlying intent of the Act, even if pipeline companies and producers are adversely affected.[128] Since take-or-pay provisions effectively pass inflated gas prices to consumers,[129] the provisions are in direct conflict with the purposes of the Act.[130] The FERC, therefore, has the duty to either set aside or modify any take-or-pay provisions in existing gas purchase contracts.[131]

A second argument in favor of pipeline companies is that the payments made under take-or-pay provisions violate the maximum lawful ceiling prices set by the NGPA.[132] These violations should cause the contracts themselves to be deemed unenforceable.[133] The NGPA establishes a maximum lawful price that can be charged for natural gas.[134] Because pipeline companies under take-or-pay provisions are making payments for gas not actually received, the actual prices paid by the companies become slightly

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128. *See* Hall v. FERC, 691 F.2d 1184, 1198 (5th Cir. 1982) (intent behind Act is to protect public interest); California Gas Producers Ass'n v. FPC, 421 F.2d 422, 428-29 (9th Cir. 1970) (recognizing Commission's primary duty of consumer protection).

129. *See* Wisconsin Gas Co. v. FERC, 770 F.2d 1144, 1151 (D.C. Cir. 1985) (consumer eventually pays for high take-or-pay costs).

130. *See* Atlantic Ref. Co. v. Public Serv. Comm'n, 360 U.S. 378, 389 (1959) (NGA intended to protect consumer from excessive prices); California Gas Producers Ass'n v. FPC, 421 F. 2d 422, 428-29 (9th Cir. 1970) (consumer protection NGA's ultimate goal).

131. *See* 15 U.S.C. § 717d(a) (1982) (Commission should modify any contract deemed to be unreasonable); *see also* FPC v. Sierra Pac. Power Co., 350 U.S. 348, 355 (1956) (Commission has authority to alter contractual provisions when required by public interest). It has been held, however, that the FERC does not have the power to regulate contracts involving gas categories that are no longer subject to NGPA jurisdiction. *See* Pennzoil Co. v. FERC, 645 F.2d 360, 380-82 (5th Cir. 1981), *cert. denied*, 454 U.S. 1142 (1982); *see also* 15 U.S.C. § 3431(a)(1)(A) (1982) (categories of gas no longer under FERC jurisdiction).

132. *See* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.06(5) (1985) (NGPA price ceiling violation is possible pipeline company defense).

133. *See, e.g.*, Gulf Oil Corp. v. Tenneco, Inc., 608 F. Supp. 1493, 1495 (E.D. La. 1985) (pipeline asserted take-or-pay violated NGPA ceiling prices); Sid Richardson Carbon & Gasoline Co. v. Internorth, Inc., 595 F. Supp. 497, 500 (N.D. Tex. 1984) (pipeline claimed take-or-pay clauses were void due to violation of price ceilings); Post v. Perry Gas Transmission, Inc., 616 F. Supp. 1, 2 (N.D. Tex. 1983) (pipeline asserting maximum lawful price defense). *See generally* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.06(5) (1985) (discussion of violation of NGPA price ceilings by take-or-pay provisions).

134. *See* 15 U.S.C. § 3314 (1982) (provision for natural gas ceiling prices). The ceiling price limitation is applicable to any first sale of natural gas delivered during any one month. *See id.* § 3314(a); *see also* Mid-Louisiana Gas Co. v. FERC, 664 F.2d 530, 536 (5th Cir. 1981) (sale of gas by producer to pipeline company constitutes first sale under NGPA). *But see* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.06(5)(b) (1985) (producers argued transaction between producer and pipeline not sale under NGPA).

distorted.[135] To derive the actual price paid by a pipeline company, the total quantity of gas delivered to the pipeline in one month should be divided into the total amount of money paid to the producer.[136] It logically follows that if a pipeline company paid for gas not actually received, the total price for the gas actually delivered to the pipeline that month is increased and will most likely violate the NGPA price ceiling.[137]

Although the FERC has yet to totally resolve the take-or-pay issue, steps have been taken recently in an attempt to alleviate the problem.[138] In a recent order, the FERC amended various areas of regulation, including regulation concerning pipeline company/producer relationships.[139] The final version of the order, however, simply reaffirmed an earlier FERC policy statement on take-or-pay contracts that dealt with payments made by pipeline companies to producers, but did not directly confront any of the corresponding take-or-pay problems.[140] Consequently, the issue remains

135. *See* Sid Richardson Carbon & Gasoline Co. v. Internorth, Inc., 595 F. Supp. 497, 500 (N.D. Tex. 1984) (gas price actually received is elevated when gas paid for but not taken).

136. *See* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.06(5)(a) (1985).

137. *See* Sid Richardson Carbon & Gasoline Co. v. Internorth, Inc., 595 F. Supp. 497, 500 (N.D. Tex. 1984) (explanation of maximum ceiling defense). *See generally* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.06(5)(a) (1985) (illustrating pipeline company's argument for violation of NGPA maximum price ceiling). The maximum price ceiling issue has been argued before the FERC, but to date there is no controlling precedent. *See Annual Report on Natural Gas*, 1984 A.B.A. SEC. PUB. UTIL. L. REP. 191 (complaints pending before FERC on take-or-pay and maximum price issue). *But see Annual Report on Natural Gas*, 1985 A.B.A. SEC. PUB. UTIL. L. REP. 208-09 (citing *Koch Indus., Inc. v. Columbus Gas Transmission Corp.*, No. 83-990-A, slip op. at 10-11 (M.D. La. March 14, 1985) holding that take-or-pay payments do not violate NGPA maximum price ceilings).

138. *See* FERC Order No. 436, 50 Fed. Reg. 42,408 (1985) (rule concerning gas pipeline regulation).

139. *See id.* Order 436 approved a voluntary non-discriminatory gas transportation program for gas pipeline companies. *See id. See generally Natural Gas Deregulation: New Direction*, 7 CONG. RESEARCH SERV. REV. (Lib. of Cong.) No. 1, at 17 (Jan. 1986) (discussion of Order 436).

140. *See* FERC Order No. 436, 50 Fed. Reg. 42,408 (1985) (reaffirming FERC Statement of Policy, 50 Fed. Reg. 16,076 (1985)). The earlier statement of policy dealt with pipeline company payments made to producers in exchange for the producer revising the take-or-pay agreement. *See* FERC STATEMENT OF POLICY, 50 Fed. Reg. 16,076 (1985). Further research, however, indicates that the FERC intially intended to give any pipeline companies that participated in the transportation program preferential treatment as to their take-or-pay obligations. *See* FERC NOTICE OF PROPOSED RULEMAKING, 50 Fed. Reg. 24,130 (1985). *See generally* Williams, *The Proposed Sea-Change in Natural Gas Regulation*, 6 ENERGY L.J. 233, 242-62 (1985) (discussion of proposed version of FERC Order 436). The final version of Order 436 omitted the preferential treatment provisions. *See* FERC Order No. 436, 50 Fed. Reg. 42,408 (1985). In a motion filed on February 3, 1986, Tennessee Gas Pipeline Co. requested that the FERC review Order No. 436 and reconsider the Commission's decision not to directly

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unresolved with the probability of future Commission resolutions highly unlikely.[141]

C. *Legislative*

A third possible remedy for problems associated with take-or-pay provisions lies in the legislative process.[142] Although several commentators have expressed skepticism regarding the success of a legislative remedy,[143] the possibility nevertheless exists that a state[144] or federal law could resolve the take-or-pay issue.[145] Even though no action has yet been taken, several bills have already been introduced in Congress.[146] Most of the proposed legisla-

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confront the take-or-pay issue. *See* 1554 FOSTER NAT. GAS REP. 21-24 (Feb. 6, 1986). One other major pipeline company and two associations have since joined in the request for reconsideration of Order No. 436. *See* 1559 FOSTER NAT. GAS REP. 27-30 (Mar. 13, 1986) (report of requests made by Interstate Natural Gas Association of America, American Gas Association, and Transcontinental Gas Pipe Line Corp.).

141. *See* Moore, *Federal Agency Viewpoint*, 1984 A.B.A. SEC. PUB. UTIL. L. REP.—PROCEEDINGS 108 (prediction that FERC will not resolve take-or-pay problems); Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.06(6) (1985) (no indication FERC will take affirmative action on take-or-pay issue). The Acting Chairman of the FERC recently admitted that there is an "extreme reluctance to even breathe the word 'take-or-pay.'" *See* 1561 FOSTER NAT. GAS REP. 4 (March 27, 1986) (report of Acting Chairman Sousa's remarks at FERC meeting on March 26, 1986). The Commissioner of the FERC expressed further reluctance to deal with the take-or-pay issue, stating that the problems should be solved in the state and federal courts through use of contractual defenses. *See id.* (report of Commissioner Naeve's statements at FERC meeting).

142. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 798 (1983) (legislation may provide possible answer to take-or-pay issue).

143. *See, e.g.*, Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.09 (1985) (chances for gas legislation nonexistent); Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 798 (1983) (congressional legislation is compromising and politically delicate).

144. *See* Energy Reserves Group, Inc. v. Kansas Power & Light Co., 459 U.S. 400, 410-11 (1983) (state law affecting contractual obligations may be unconstitutional). The contract clause of the United States Constitution prohibits a state from passing a law that impairs "the obligation of contracts." *See* U.S. CONST. art. I, § 10. The Supreme Court, however, has interpreted the contract clause to allow such legislation when the public interest is involved. *See* Energy Reserves Group. Inc. v. Kansas Power & Light Co., 459 U.S. 400, 411-12 (1983) (law permitted when intended to cure general social or economic problem). Furthermore, state legislation which affects gas purchase contracts does not conflict with the contract clause. *See id.* at 418-19 (state law regulating price escalators in gas sales agreement held valid).

145. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 798 (1983) (legislation possible take-or-pay answer).

146. *See, e.g.*, H.R. 511, 99th Cong., 1st Sess. (1985) (all take-or-pay obligations limited to 60% of contract volume); H.R. 294, 99th Cong., 1st Sess. (1985) (all take-or-pay provisions deemed void); H.R. 1685, 98th Cong., 1st Sess. (1983) (existing take-or-pay provisions voida-

tion either suspends all take-or-pay provisions,[147] or limits the quantity of gas to be taken under the provision.[148] Other possible legislative requirements include shortening of contract terms or forcing distributors to contract with several pipeline companies at once.[149] The legislative approach, however, is extremely time-consuming and unpredictable, and does not appear to be the most promising means for achieving a solution to the take-or-pay problem.[150] Pipeline companies should, therefore, explore other proposals rather than expect a timely legislative resolution.[151]

VI. CONCLUSION

A prompt solution to the take-or-pay problem is vital to the survival of the natural gas industry. Although the critical nature of the situation is evident, the FERC appears hesitant to directly confront the issue. Natural gas legislation also does not promise a timely resolution. The courts have the power to provide a short term solution by applying contract law principles, but will likely not take action until they recognize the actual gravity and extent of the issue. Once the courts realize that the problem is threatening the very existence of the natural gas industry, as well as the continued operation of individual pipeline companies, it is likely that the aforementioned contract

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ble and future provisions prohibited). *See generally* Johnson, *Natural Gas Sales Contracts*, 34 INST. ON OIL & GAS L. & TAX'N 83, 117-21 (1983) (discussion of legislative proposals on take-or-pay issue).

147. *See* S. 291, 98th Cong., 1st Sess. (1983) (all existing take-or-pay provisions suspended); H.R. 1685, 98th Cong., 1st Sess. (1983) (take-or-pay provisions voidable).

148. *See* S. 1715, 98th Cong., 1st Sess. (1983) (providing for restriction of take-or-pay obligations to 50% in first year, 52.5% in second year, 55% in third year, 60% in fourth year).

149. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 798 (1983) (discussion of possible legislative actions).

150. *See* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.09 (1985) (prospects for natural gas legislation never more dismal). Congress has preferred to spend available time on tax and budget issues. *See id.* Furthermore, Congressional legislation is a slow process, and the natural gas industry needs a prompt solution. *See* Tannenbaum, *Commercial Impracticability Under the Uniform Commercial Code: Natural Gas Distributors' Vehicle for Excusing Long-Term Requirements Contracts?*, 20 HOUS. L. REV. 771, 798 (1983).

151. *See* Moody, *The Natural Gas Industry After Partial Deregulation*, 36 INST. ON OIL & GAS L. & TAX'N § 6.09 (1985) (industry must find answer in existing laws). The Chairman of the Senate Energy and Natural Resources Committee, Senator James McClure, stated on Jan. 28, 1986, that natural gas issues will take a low priority during the upcoming legislative session. *See* 1553 FOSTER NAT. GAS REP. 1-2 (Jan. 30, 1986) (report of statements made at natural gas conference). Instead, top priority will go to budget-related issues. *See id.* at 1; *see also* 1564 FOSTER NAT. GAS REP. 5 (April 17, 1986) (report of Senate Energy Subcommittee's remarks expressing doubt that natural gas legislation will pass).

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defenses will be utilized to relieve pipeline companies of take-or-pay obligations.

Eventually, the industry must find a long range solution that will permit flexible responses to future market alterations. The solution will more than likely be in the form of FERC regulation inasmuch as the FERC is the regulatory body most qualified to solve natural gas industry problems. Until an effective judicial or regulatory solution is reached, producers, pipeline companies, and local gas distributors must cooperate in an effort to alleviate the problems and minimize the damage take-or-pay provisions have already caused the industry.

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