

D.C. Circuit Reopens Controversy Concerning Regulated Master Limited Partnership Taxation

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On Friday, July 1, 2016, a panel of the United States Court of Appeals for the District of Columbia Circuit reopened the issue of whether pipelines organized as partnerships can claim a tax allowance for ratemaking purposes in *United Airlines Inc., et al. v. FERC, et al.*, No. 11-1479. This decision is the third chapter in litigation arising out of challenges to the rates of SFPP, L.P., a common carrier pipeline regulated by FERC under the Interstate Commerce Act; however, the decision has potentially broader applicability to any FERC regulated utility partnership operating under cost-based rates.

In 2004, a panel of the D.C. Circuit held that FERC had failed adequately to explain its rationale for permitting pipeline partnerships to recover an income tax allowance and remanded the issue to FERC for further review. *BP West Coast Products, LLC v. FERC*, 374 F.3d 1263 (D.C. Cir). Following proceedings on remand, FERC permitted pipeline partnerships to recover a tax allowance based on taxes paid by partner-investors that were attributable to partnership earnings. The D.C. Circuit subsequently affirmed FERC's decision. *ExxonMobil Corp. v. FERC*, 487 F.3d 945 (D.C. Cir. 2007).

In *United Airlines*, the panel held that, in its *ExxonMobil* decision, it had implicitly reserved the question of whether the interaction of FERC's use of (1) a discounted cash flow methodology that ensured pipelines an adequate after-tax return to attract investment, and (2) an income tax allowance, resulted in a "double-recovery" of income taxes. The panel found that FERC had not adequately justified its policy and remanded for further procedures in order for FERC to demonstrate no such double recovery .

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