

No. 08-674

In the
Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL.,
v.
MAINE PUBLIC UTILITIES COMMISSION, ET AL.,

**On Petition for a Writ of Certiorari to the
United States Court of Appeals
for the District of Columbia Circuit**

**BRIEF OF THE ELECTRIC POWER SUPPLY
ASSOCIATION, COLORADO INDEPENDENT ENERGY
ASSOCIATION, ELECTRIC POWER GENERATION
ASSOCIATION, INDEPENDENT ENERGY
PRODUCERS ASSOCIATION, INDEPENDENT
PETROLEUM ASSOCIATION OF AMERICA,
INDEPENDENT POWER PRODUCERS OF NEW YORK,
INTERSTATE NATURAL GAS ASSOCIATION OF
AMERICA, NATURAL GAS SUPPLY ASSOCIATION,
NEW ENGLAND POWER GENERATORS
ASSOCIATION, INC., NORTHEAST ENERGY AND
COMMERCE ASSOCIATION, NORTHWEST &
INTERMOUNTAIN POWER PRODUCERS COALITION,
PJM POWER PROVIDERS GROUP, AND WESTERN
POWER TRADING FORUM AS *AMICI CURIAE* IN
SUPPORT OF PETITIONERS**

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QUESTION PRESENTED

This Court’s recent decision in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), reaffirmed that, under the *Mobile-Sierra* doctrine, the Federal Energy Regulatory Commission “must presume that the rate set out in a freely negotiated wholesale-energy contract meets the ‘just and reasonable’ requirement imposed by law,” and that the “presumption may be overcome only if” the Commission “concludes that the contract seriously harms the public interest.” *Id.* at 2737. In conflict with *Morgan Stanley*, the D.C. Circuit below held that “when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply.” Pet. App. 22a.

The question presented is:

Whether the Commission’s authority to abrogate wholesale power contracts is constrained by the *Mobile-Sierra* doctrine when a contract rate is challenged by a non-contracting third party.

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INTEREST OF *AMICI CURIAE*¹

Amici and their members represent a diverse array of participants in the Nation's electric and natural gas industries that are directly affected by the issues raised in this case. *Amici's* members have made long-term financial commitments, involving hundreds of billions of dollars, in reliance on this Court's settled authorities protecting the integrity of privately negotiated wholesale power contracts. Because the D.C. Circuit's decision undoes much of this Court's work in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), and purports to grant the Federal Energy Regulatory Commission never-before-recognized authority to abrogate contracts challenged by non-contracting third parties, *amici* are concerned that, if left standing, the decision below will destabilize the Nation's power markets, discourage much-needed investment, and ultimately lead to higher costs for consumers.

The Electric Power Supply Association (“**EPSA**”). EPSA is a national trade association representing competitive electric power suppliers, including independent power producers, merchant generators, and power marketers. EPSA's mission

¹ The parties have consented to the filing of this brief in letters on file in the Clerk's office. Pursuant to S. Ct. R. 37.6, *amici* state that no counsel for any party authored this brief in whole or in part, and no person or entity, other than *amici* and its counsel, made a monetary contribution intended to fund the preparation or submission of this brief.

is to promote legislative and regulatory policies encouraging a competitive market for electricity.

Colorado Independent Energy Association (“CIEA”). CIEA is a trade association of competitive independent power producers operating in Colorado. Its 34 members and 12 associate members are an integral part of Colorado’s energy industry, producing electricity with clean, efficient natural gas-fired cogeneration and renewable technologies.

Electric Power Generation Association (“EPGA”). EPGA is a regional trade association of major electric generating companies that supply wholesale power in Pennsylvania and surrounding states. Its member companies collectively own and operate more than 141,000 megawatts of generating capacity.

Independent Energy Producers Association (“IEP”). IEP is a California non-profit mutual benefit corporation whose members collectively own and operate approximately one-third of California’s installed generating capacity.

Independent Petroleum Association of American (“IPAA”). IPAA is a national association representing thousands of independent oil and natural gas producers and service companies across the United States.

Independent Power Producers of New York (“IPPNY”). IPPNY is a not-for-profit trade association representing more than 100 independent power producers involved in the development of generation, and the marketing, and

sale of electric power and natural gas in the State of New York.

Interstate Natural Gas Association of America (“INGAA”). INGAA is a trade association that represents virtually all of the interstate natural gas transportation pipeline and interstate natural gas storage companies operating in the United States, as well as comparable companies in Canada and Mexico. Its members transport over 95 percent of the Nation’s natural gas through a network of 220,000 miles of pipelines.

Natural Gas Supply Association (“NGSA”). NGSA is a trade association that represents U.S.-based producers and marketers of natural gas on issues that broadly affect the natural gas industry. NGSA is the voice of suppliers who find, sell, transport, and deliver approximately 30 percent of the United States’ natural gas supply.

New England Power Generators Association, Inc. (“NEPGA”). NEPGA is a trade association representing electric generating companies in New England. Its member companies account for approximately 26,000 megawatts of generating capacity in the region.

Northeast Energy and Commerce Association (“NECA”). NECA is a trade association serving New England’s competitive electric power industry. Its 800 members include developers and owner/operators of competitive power projects, power marketers and traders, fuel and equipment suppliers, power consumers, and various service providers to the power industry.

Northwest & Intermountain Power Producers Coalition (“NIPPC”). NIPPC represents developers, owners, and operators of non-utility power plants in the Pacific Northwest and Intermountain region.

PJM Power Providers Group (“P3”). P3 is a nonprofit Delaware Corporation whose members serve nearly 12.2 million customers, employ more than 55,000 people, and own more than 75,000 megawatts of power and over 51,000 miles of transmission lines in the thirteen states and the District of Columbia that comprise the PJM Interconnection, LLC region.

Western Power Trading Forum (“WPTF”). WPTF is a California non-profit, mutual benefit corporation that supports the development of uniform operating rules and competitive electricity markets throughout Western electric markets.

INTRODUCTION AND SUMMARY OF ARGUMENT

This case arises out of a carefully negotiated settlement designed to remedy deficiencies in the New England wholesale energy market and to ensure that utilities operating in that market have sufficient electrical generating capacity to satisfy customer demand. The settlement establishes new market rules and an auction process through which rates will be fixed in binding commitments to buy and sell capacity. *See* Pet. Br. 8-12; U.S. Br. 9-12.

The settlement describes the legal standards that, once the settlement is approved by the Commission, will apply to any future complaints challenging (i) the new market rules, (ii) the agreed-on rates that apply during a transition period, or (iii) the contracts to purchase and sell capacity that ultimately result from the auction process. In particular, the settlement includes what is known as a *Memphis* clause, stating that the new market rules may be modified prospectively as long as any modifications are “just and reasonable” as required under the Federal Power Act. *See* 16 U.S.C. § 824d(a). In addition, the settlement includes a separate provision (section 4.C.) making clear that the *Memphis* clause does *not* apply either to the rates fixed by contract through the auction process, or to the agreed-upon transition payments. The settlement instead confirms that these contracted-for-rates cannot be modified unless changes are necessary in the public interest. The express purpose of section 4.C. is to “reduce regulatory uncertainty” by reassuring

market participants that the fixed-rate contracts contemplated under the settlement will be respected by the Commission. JA. 60-61.

The settlement's provisions are consistent with the Federal Power Act's requirements and this Court's precedents. As petitioners explain, this Court has long held that the statutory regime permits wholesale energy rates to be established by contract and protects the integrity of private contractual arrangements. *See* Pet. Br. 3–8. The *Mobile-Sierra* doctrine, named after this Court's landmark decisions, mandates that when wholesale energy rates are fixed by contract, the Commission has no authority to modify them except in “extraordinary circumstances” when unequivocally “necessary in the public interest.” *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956). This Court reaffirmed *Mobile-Sierra* just last year in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), emphasizing that Congress “intended to reserve the Commission's contract-abrogation power” only for “those extraordinary circumstances where the public will be severely harmed.” *Id.* at 2749.

In its orders below, the Commission approved the proposed settlement, concluding that it establishes an effective process for resolving “the deficiencies in New England's existing capacity market.” Pet. App. 135a. In addition, the Commission found that the settlement appropriately recognizes that rates fixed by contract through the capacity auction, as well as

the rates paid during the transition period, are subject to the *Mobile-Sierra* doctrine. Pet. Br. 12–14, U.S. Br. 10–11. The Commission thus confirmed that any parties choosing to participate in the capacity auction can rely on the outcome of that process, assured that contracted-for rates will not be changed unless unequivocally necessary in the public interest.

The court of appeals affirmed the Commission’s orders in every respect, except one—specifically, the D.C. Circuit held that the Commission could not “approve a settlement agreement that applies” *Mobile-Sierra*’s “highly-deferential ‘public interest’ standard to rate challenges brought by non-contracting third parties.” Pet. App. 21a. In reaching its decision, the lower court radically departed from this Court’s precedents, recasting *Mobile-Sierra* as a narrow exception to the Federal Power Act’s just-and-reasonable standard. *Id.* at 24a. The court of appeals held that “when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply” and “the proper standard of review remains the ‘just and reasonable’ standard.” *Id.* at 22a.

The decision below misunderstands the statutory requirements and is contrary to *Morgan Stanley*. By carving out a novel exception for rate challenges brought by non-contracting third parties, the D.C. Circuit has altered *Mobile-Sierra*’s balanced, even-handed public-interest standard on which thousands of wholesale power contracts are premised. If allowed to stand, the decision will subvert the long-settled expectations of market participants. It also will risk destabilizing the

Nation's energy markets, exposing consumers to the same types of high and volatile prices and supply shortages that prompted Congress to impose strict limits on the Commission's authority to undo private contractual arrangements.

This brief provides *amici's* perspectives on the important issues raised in this case. First, the brief explains why the D.C. Circuit's newly minted third-party exception to *Mobile-Sierra* is contrary to this Court's precedents and, if allowed to stand, will eviscerate the *Mobile-Sierra* doctrine, produce an improper asymmetrical standard that favors buyers over sellers, and destabilize the Nation's energy markets. Second, the brief addresses an issue that the Court need not reach, but on which respondents' briefing focused in the court below—namely, the extent to which settlement agreements are subject to *Mobile-Sierra*. Respondents contend that different rules apply when parties proceed by settlement. In fact, whether *Mobile-Sierra* applies turns not on the label of the parties' agreement, but instead on whether the parties have fixed a rate by contract, even if the resulting contract is the product of a settlement. Third, the brief addresses the Commission's contention that its orders approving the parties' settlement are entitled to *Chevron* deference. The contracts resulting from the auction process constitute binding commitments to buy and sell capacity at fixed rates and, therefore, are subject to *Mobile-Sierra* as a matter of law. Because the Commission must comply with the statutory requirements, the Court need not address the scope of the Commission's

discretion in circumstances where rates are not fixed by voluntary agreement.

ARGUMENT

I. The Decision Below Contravenes This Court’s Precedents And Misapplies The Statutory Requirements.

This Court has long held that when buyers and sellers establish rates by contract, the resulting rates are presumptively just and reasonable, and the Commission has no authority to modify them except in “extraordinary circumstances where the public will be severely harmed.” *Morgan Stanley*, 128 S. Ct. at 2749. The decision below carves out a large, novel, and destabilizing exception to this constraint on the Commission’s authority, concluding that rates are not presumptively just and reasonable when they are challenged by a non-contracting third party. The D.C. Circuit’s decision is contrary to the express teachings of *Morgan Stanley* and, if left uncorrected, will effectively nullify the freedom of contract promoted by “decisions of this Court and the Court of Appeals” for “the past 50 years.” *Id.* at 2739.

A. The D.C. Circuit’s Decision Conflicts With *Morgan Stanley*.

The Federal Power Act provides that wholesale rates may be “established initially by contract,” *Mobile*, 350 U.S. at 339, and the Court has clarified that, once rates are so established, the Commission has no authority to modify them, except in “extraordinary circumstances” when unequivocally “necessary in the public interest.” *Id.* at 344;

Sierra, 350 U.S. at 348. As petitioners explain, this constraint on the Commission’s authority, referred to as “the *Mobile-Sierra* doctrine,” has played a central role in the development of the Nation’s energy markets. *See* Pet. Br. 7–8; *see also* U.S. Br. 21–22.

Last Summer this Court affirmed *Mobile-Sierra*’s continuing vitality in *Morgan Stanley*. Reversing Ninth Circuit decisions that threatened “disfigurement of the venerable” doctrine, 128 S. Ct. at 2747, the Court reiterated that a “rate set out in a freely negotiated wholesale-energy contract” is presumed to satisfy “the ‘just and reasonable’ requirement imposed by law.” *Id.* at 2737. The Court emphasized that “uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller’s willingness to enter into long-term contracts,” which “in the long run” will “harm consumers.” *Id.* at 2749. Accordingly, because the “regulatory system created” by the Federal Power Act is “premised on contractual agreements voluntarily devised by the regulated companies[,] it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity.” *Id.* at 2739 (quoting *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968)).

Morgan Stanley should have prompted the D.C. Circuit to reconsider its decision below and to grant rehearing. *See* Pet. Br. 16–17; U.S. Br. 13. Instead, the D.C. Circuit left in place its initial decision (issued before *Morgan Stanley*), which characterized *Mobile-Sierra* as a narrow “exception” to the statutory requirement that rates

be “just and reasonable.” The D.C. Circuit held that *Mobile-Sierra* “does *not* apply” when a “rate challenge is brought by a non-contracting third party.” Pet. App. 22a (emphasis added). In the D.C. Circuit’s view, applying *Mobile-Sierra* to challenges brought by non-contracting third parties would deprive those parties of their “statutory right to have rate challenges adjudicated under the ‘just and reasonable’ standard.” *Id.* at 22a.

That reasoning is deeply flawed. See Pet. Br. 24–26; U.S. Br. 25–28. In *Morgan Stanley*, this Court went to great lengths to emphasize that it was not relying on the “obviously indefensible proposition that a standard different from the statutory just-and-reasonable standard applies to contract rates.” *Morgan Stanley*, 128 S. Ct. at 2740. Contrary to the conclusions reached by the court below, the *Mobile-Sierra* doctrine is not only about ensuring that parties to a contract are held to their “contractual obligations.” Pet. App. 24a. Instead, the doctrine recognizes the importance of contract integrity to the efficient working of the energy industry, and is premised on the notion that, because wholesale energy contracts are typically negotiated between sophisticated entities enjoying equal bargaining power, the contractually agreed-upon rate is expected to be, and by definition is, a “just and reasonable” rate. *Morgan Stanley*, 128 S. Ct. at 2746 (citing *Verizon Commc’ns, Inc. v. FCC*, 535 U.S. 467, 479 (2002)). The contracting process thus produces a rate that is “just and reasonable” both as between the contracting parties and as applied to everyone else. The *Mobile-Sierra* doctrine is not, as the D.C.

Circuit assumed, a narrow “exception” to the just-and-reasonable standard; instead, it is a “definition of what it means for a rate to satisfy” that standard when the rate is fixed by contract. *Id.*

Nor does applying the *Mobile-Sierra* doctrine deprive any party of its statutory rights. The Federal Power Act’s “just and reasonable” standard is properly viewed not as a right bestowed upon regulated parties, but as a constraint that frames the boundaries of Commission action. *See* Pet. Br. 27. The *Mobile-Sierra* doctrine protects the integrity of privately negotiated agreements by denying the Commission authority to look beyond the general public interest to individual interests and agendas. The statutory limits on the Commission’s authority do not change merely because a contract is challenged by a non-contracting third party.

B. The D.C. Circuit’s Decision Eviscerates *Mobile-Sierra*.

If allowed to stand, the D.C. Circuit’s newly minted third-party exception will eviscerate the *Mobile-Sierra* doctrine, and consign this Court’s *Morgan Stanley* decision to a mere footnote in the regulation of the energy industry. As a practical matter, a third-party exception to *Mobile-Sierra* ensures that virtually no wholesale energy contract is protected from abrogation.

In contrast to standing requirements that apply to disputes over ordinary commercial contracts, *cf. Miree v. DeKalb County, Ga.*, 433 U.S. 25 (1977) (state law applies to determine whether third party beneficiaries enjoy standing), the

Federal Power Act confers standing on extraordinarily permissive terms. The statute allows virtually anyone to file a complaint with the Commission challenging an energy contract as unjust, unreasonable, or unduly discriminatory. See 16 U.S.C. § 825e (2006) (“[a]ny person ... complaining of anything done ... by any ... public utility ... may apply to the Commission by petition”). As the Commission’s regulations state, “[a]ny person may file a complaint seeking Commission action against any other person alleged to be in contravention or violation of any statute, rule, order, or other law administered by the Commission, or for any other alleged wrong over which the Commission may have jurisdiction.” 18 C.F.R. § 385.206(a) (2009).

The upshot is that non-contracting third parties can, and routinely do, file complaints with the Commission seeking to re-write energy contracts on grounds that the rates are either too high or too low. For example, in 2007, the Illinois Attorney General filed a complaint seeking to abrogate freely negotiated contracts between Illinois utilities and 16 wholesale suppliers that she alleged would lead to excessive charges on Illinois consumers. See *Amended Complaint by the People of the State of Illinois, ex rel. Illinois Attorney General Lisa Madigan*, FERC Dkt. No. EL07-47-000 (Mar. 16, 2007). Similarly, a consumer group filed complaints challenging a series of freely negotiated contracts between utilities and energy suppliers in California. See *Section 206 Compl.*, FERC Dkt. No. EL07-50-000 (Mar. 26, 2007) (challenging contract between Southern California

Edison Co. and Blythe Energy, LLC); Section 206 Compl., FERC Dkt. No. EL07-40-000 (Mar. 2, 2007) (challenging contract between Pacific Gas & Electric Co. and Metcalf Energy Center, LLC and Los Medanos Energy Center, LLC); Section 206 Compl., FERC Dkt. No. EL07-37-000 (Feb. 22, 2007) (challenging contract between Southern California Edison Co. and Long Beach Generation, LLC).

Because long-term wholesale energy contracts are of concern not only to the parties who negotiate them but also to numerous third parties, there is no shortage of state regulators, consumer advocacy groups, retail consumers, industrial buyers, upstream suppliers, and other interested stakeholders willing to take advantage of the Federal Power Act's permissive standing requirements. In fact, as a practical matter, there will always be some non-contracting third party whose interests align with a buyer faced with contract rates that, in hindsight, appear too high. For this reason, allowing non-contracting parties to circumvent *Mobile-Sierra* would just as surely undermine "contract stability *as between the contracting parties*," Pet. App. 24a (emphasis in original), as would permitting a party to complain about contract rates to which it voluntarily agreed. When a contract rate becomes unfavorable due to unforeseen changes in market conditions or for any other reason, it is hard to fathom that any but the most noble or ignorant contracting parties would not seek to circumvent *Mobile-Sierra* by encouraging non-contracting parties to file

complaints challenging the contract as unjust and unreasonable.

This concern is highlighted in *Morgan Stanley's* companion cases, which were vacated and remanded to the Ninth Circuit for further consideration. See *Sempra Generation v. Public Utils. Comm'n of Cal.*, 128 S. Ct. 2993 (2008). Because those cases involve public entities that were not original contracting parties, an issue raised in the companion cases not addressed in *Morgan Stanley* is the validity of the Commission's determination that the complainants, the California Public Utilities Commission and the California Electricity Oversight Board, had "stepped into the shoes" of the buyer under the challenged contracts. See *Public Utils. Comm'n of Cal. v. FERC*, 474 F.3d 587, 592 n.4 (9th Cir. 2006) (acknowledging this open issue). The Ninth Circuit has now remanded that issue to the Commission, see *Public Utils. Comm'n of Cal. v. FERC*, 550 F.3d 767 (9th Cir. 2008), and interested parties have submitted extensive briefing addressing whether *Mobile-Sierra* should apply. See, e.g., Answer and Cross-Motion of Sempra Generation for Determination that the *Mobile-Sierra* Doctrine Applies to the California Public Utilities Commission, FERC Dkt. Nos. EL02-60-003, *et al.* (Dec. 19, 2008). Most relevant here, the complaining state agencies have argued that, in adjudicating their challenge to the contract rates, the Commission is not constrained by *Mobile-Sierra* because a different California agency signed the contracts and, therefore, the complainants qualify as "third parties" entitled to attack the contracts

under a *de novo* standard of review. See Answer of the Public Utilities Commission of the State of California to Cross Motion of Sempra Generation and Cross Motion for Summary Disposition, FERC Dkt. Nos. EL02-6-003, *et al.*, at 4–6 (Jan. 21, 2009) (citing the D.C. Circuit’s *Maine PUC* decision and arguing that *Mobile-Sierra* does not apply); see also Answer and Cross-Motion of the Public Utilities Commission of the State of California for an Order Governing Procedures on Remand, FERC Dkt. Nos. EL02-60-003, *et al.*, at 22-26 (Jan. 14, 2009).

Indeed, in *Morgan Stanley* itself, numerous third parties stood ready to challenge the parties’ contracts as imposing an “excessive burden” on third-party consumers. See, e.g., *Morgan Stanley v. Public Util. Dist. No. 1 of Snohomish County*, Nos. 06-1457 & 06-1462, Br. of AARP in Support of Respondents (Jan. 14, 2008); *id.*, Br. of Public Util. Law Project of New York, Inc. in Support of Affirmance (Jan. 16, 2008); *id.*, Br. of Colorado Office of Consumer Counsel, *et al.* in Support of Affirmance (Jan. 14, 2008). Recognizing the important role that contract sanctity has played in the development of the Nation’s energy markets, this Court rejected the view that *Mobile-Sierra* does not apply when contract rates arguably impose an “excessive burden” on consumers. *Morgan Stanley*, 128 S. Ct. at 2747-48. That ruling will be largely meaningless if the Commission is exempt from *Mobile-Sierra* and the respect for contracts the Federal Power Act demands merely because a complaint is filed by a non-contracting third party.

C. The D.C. Circuit's Decision Will Produce An Asymmetrical Standard.

Recognizing that the universe of third-party complainants is potentially boundless, the Commission has suggested that, if the D.C. Circuit's policy innovations are allowed to stand, the Commission will police rate challenges brought by third parties to prevent "inappropriate strategic behavior." U.S. Cert. Opp. 12. That is another reason to reverse the court of appeals. Any attempt to distinguish *bona fide* third parties from complainants acting as impermissible "proxies" for contracting parties, *id.*, will inevitably produce an asymmetrical standard that favors buyers over sellers.

In wholesale energy markets, load serving entities, such as utilities and power marketers that serve retail customers (*i.e.*, "load"), will typically be net buyers of power—that is, they purchase power to serve customers above and beyond the power generated by their own units. Accordingly, when a load serving entity enters into a contract with rates that, in hindsight, may appear to be "too high," there will be no shortage of non-contracting third parties (such as state regulators, consumer advocacy groups, and retail customers) clamoring for relief at the Commission. Because the challenged contracts undoubtedly will have some effect on the rates paid by the load serving entity's customers, the Commission will find it difficult to sort out which customers are "prox[ies]" engaged in "inappropriate strategic behavior." *Id.* Likewise, because the Federal Power Act has "special solicitude for states and state agencies," *Maryland*

People's Counsel v. FERC, 760 F.2d 318, 320 (D.C. Cir. 1985) (Scalia, J.), the Commission will be hard pressed to characterize a state agency complainant as a “proxy” for the load serving entity, except in the unusual case where the load serving entity is also a state agency in the same State. *Cf. Public Utils. Comm'n of Cal. v. Sellers of Long Term Contracts*, 105 FERC ¶ 61,182 at P 51 (2003).

In contrast, independent power producers, like many of *amici's* members, will almost always be net sellers of energy. If an independent power producer agrees to what, in hindsight, turns out to be an unfavorable deal, with rates that appear “too low,” the consequences will fall first upon the power producer and its shareholders and then, in the unusual case, upon its lenders. To the extent any non-contracting third party challenges the contract rates, that party will likely be a shareholder or lender. But a shareholder or lender is precisely the type of complainant that might easily be viewed as a “proxy for one of the contracting parties.” U.S. Cert. Opp. 12.

In other words, even if the Commission had discretion to mitigate the pernicious effects of the D.C. Circuit's new third-party exception, its attempts to do so will turn the even-handed *Mobile-Sierra* doctrine into a one-way ratchet that favors buyers over sellers. *See Morgan Stanley*, 128 S. Ct. at 2747 (recognizing that standard for buyer challenges “must be the same” as standard for seller challenges). Such a result is fundamentally at odds with *Mobile-Sierra's* reliance on arms-length contracting, which in no way depends on whether the contract rate turns out to be “too high”

or “too low” in light of subsequent market developments. Such a result also would upset the “balancing of [] investor and [] consumer interests” that informs the contract-focused ratemaking process under the Federal Power Act. *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944). When Congress enacted the Federal Power Act, it “was not only expressing its conviction that the public interest requires the protection of consumers from excessive prices,” but also “manifesting its concern for the legitimate interests of ... companies in whose financial stability the ... consuming public has a vital stake.” *United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103, 113 (1958).

D. The D.C. Circuit’s Decision Will Inject Uncertainty Into The Nation’s Energy Markets.

If allowed to stand, the D.C. Circuit’s third-party exception to *Mobile-Sierra* will upend the stability of long-term contracts on which the Nation’s energy markets depend. *See* Pet. Br. 40–41. In fact, because almost any contract could be challenged by a non-contracting third party, the D.C. Circuit’s decision threatens to expose consumers to the very types of high prices and frequent supply shortages the Federal Power Act was designed to prevent.

It is hard to overstate the importance of regulatory certainty and contractual integrity to the efficient working of the energy industry. As this Court has recognized, contract stability is crucial because investors are loath to invest in

highly volatile power markets unless they can rely on the sanctity of fixed-price contracts. See *Morgan Stanley*, 128 S. Ct. at 2749; CERA Advisory Services, *California Power Crisis Aftershock: The Potential Modification of Western Power Contracts*, at 4–7 (Apr. 2007) (“*Aftershock*”); The Electric Energy Market Competition Task Force, *Report to Congress on Competition in Wholesale and Retail Markets for Electric Energy*, at 4 (Apr. 2007). Energy suppliers, like other market participants, “require clear signals regarding national policies and confidence that those policies will be sustained over time in order to undertake the substantial investment needed to support expected increases in consumption.” Statement of Jim Wells, Director Natural Res. & Env’t, GAO, Meeting Energy Demand in the 21st Century, GAO-05-414T, at 8 (Mar. 16, 2005). These important supply signals will be scrambled if contract rates are subject to change at the request of non-contracting third parties.

From an investor’s perspective, it makes no difference whether a contract is subject to challenge by a disgruntled contracting party or by a “non-contracting third party.” In either instance, investors will discount the value of contracts if there is a material risk that the Commission may later abrogate them. Sophisticated investors “will not participate in a market in which” non-contracting parties are allowed to undo contracts, “at least not without charging a significant risk premium—a cost that will ultimately be borne by consumers.” *Standard of Review for Proposed Changes to Market-Based Rate Contracts for*

Wholesale Sales of Elec. Energy by Pub. Utils., Proposed Policy Statement, 100 FERC ¶ 61,145 at 61,545 (P 3) (2002) (Brownell and Breathitt, Comm'rs, concurring).

II. The Decision Below Rests On A Fundamental Misunderstanding Of The Statutory Requirements.

In carving out a novel third-party exception to *Mobile-Sierra*, the D.C. Circuit lapsed into error by accepting respondents' assertions that a settlement should not be permitted to "thrust" a "public interest" standard on non-contracting third parties. Pet. App. 22a. As petitioners emphasize, because the lower court's new third-party exception is improper and contrary to precedent, the Court should reverse without addressing the precise contours of when or to what extent a settlement may be protected under *Mobile-Sierra*. See Pet. Br. 20. If the Court does address the issue, however, it should recognize that whether *Mobile-Sierra* applies turns not on whether the parties are proceeding by settlement, but instead on whether the parties have fixed a rate by contract (even if the contract is the product of a settlement). It is the substance, not the label, of an agreement that determines whether it constitutes a fixed-rate contract protected from modification under the Federal Power Act.

A. *Mobile-Sierra* Applies To Rates Fixed By Contract.

The Federal Power Act contemplates two mechanisms for setting rates in the wholesale energy industry: either (i) by contract, or

(ii) unilaterally through *ex parte* filings. See *Mobile*, 350 U.S. at 343. Whether the *Mobile-Sierra* doctrine applies depends not on the identity of the party challenging the rate but on which mechanism is used to set the rate.

To ensure a stable and sufficient supply of affordable energy, Congress “rejected a pervasive regulatory scheme ... in favor of voluntary commercial agreements.” *Otter Tail Power Co. v. United States*, 410 U.S. 366, 374 (1973); see also *Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 154 (1960). When buyers and sellers fix rates by contract, the rates are presumed to satisfy “the ‘just and reasonable’ requirement imposed by law.” *Morgan Stanley*, 128 S. Ct. at 2737. In such circumstances, “the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power” who can be “expected to negotiate a ‘just and reasonable’ rate as between the two of them.” *Id.* at 2746 (citing *Verizon*, 535 U.S. at 479). Accordingly, the *Mobile-Sierra* doctrine applies and the parties’ contract may not be modified unless the Commission “concludes that the contract seriously harms the public interest.” *Id.* at 2737.

In contrast, the *Mobile-Sierra* doctrine does not apply when rates offered to prospective customers are established unilaterally through *ex parte* filings. See *id.* at 2746 n.3 (the “public interest” is “relevant” but not the “sole concern” when rates are set unilaterally) (citing *Sierra*, 350 U.S. at 355). The Federal Power Act provides that, in the “absence of any contractual relationship, rates determined *ex parte* by the seller may be filed”

with, and allowed to become effective by, the Commission. *Memphis*, 358 U.S. at 112 (unless “it has undertaken by contract not to do so,” a seller “has the right ... to change its rates ... [at] will”). Because a unilateral rate filing is not a contract, the rate schedule included in a generally applicable tariff on file with the Commission is merely an *offer* that a customer may accept either by taking service in accordance with the tariff’s terms or by executing a service agreement with the seller. See *Metro East Ctr. for Conditioning & Health v. Qwest Comms. Int’l, Inc.*, 294 F.3d 924, 926 (7th Cir. 2002) (a “tariff is an offer that the customer accepts by using the product”); see also 18 C.F.R. § 35.2(b) n.1 (2009) (defining “tariff”). Similarly, market rules contained in a generally applicable tariff establish the means by which offers may be made and accepted by the Commission. See Pet. Br. 47–52. In either scenario, the tariff provisions are established unilaterally and, therefore, the Commission’s authority to modify the tariff is not limited to instances of unequivocal public necessity.

In addition, because the Federal Power Act respects the integrity of privately negotiated agreements, the Court has held that parties may opt out of *Mobile-Sierra* by including in their contracts what is known as a *Memphis* clause. *Memphis*, 358 U.S. at 113. When parties include a *Memphis* clause in their agreement, they retain the right to make future unilateral filings with the Commission and the contract may be modified even if changes are not required in the public interest. See *id.* at 115 n.8. As this Court has recognized, parties retain “broad authority to specify whether”

the Commission may “review a contract rate solely for whether it violates the public interest or also for whether it results in an unfair rate of return.” *Morgan Stanley*, 128 S. Ct. at 2739.

Viewed against this backdrop, the fact that a contract rate is the product of a negotiated settlement does not (and should not) make any difference for purposes of applying the *Mobile-Sierra* doctrine. It is the substance, not the label, of the agreement that matters.

When a settlement involves, or results in, a fixed-rate contract, the contract is subject to *Mobile-Sierra* unless the parties specify a different level of Commission review. For example, to the extent a public utility and its customer resolve rate litigation through a settlement agreement that fixes a specific rate (or rate formula) for sales to that customer, the settlement agreement itself constitutes a fixed-rate contract subject to *Mobile-Sierra*, unless the parties have agreed otherwise. Similarly, merely because market rules are established through a Commission-approved settlement does not exempt contracts formed pursuant to those rules from the *Mobile-Sierra* doctrine. In short, the fact that a fixed-rate contract may flow from, or is embodied in, a settlement of a prior dispute does not change its essential character. *See* Pet. Br. 47.

In contrast, to the extent a settlement addresses only terms and conditions of service in a unilateral tariff of general applicability, the fact that a dispute is resolved by agreement does not transform the generally applicable tariff provisions

into a fixed-rate contract. In this context, when market rules are agreed upon by regulated parties and approved by the Commission, the rules can be prospectively changed and the Commission's authority is not constrained. In such circumstances, the settlement does not fix by contract the rate agreed upon with any particular customer; instead, it merely establishes (for example) either the terms of offers made through the tariff, or the process for the submission and acceptance of offers through organized markets.

This is not to say that the policies underlying *Mobile-Sierra* are irrelevant when a settlement involves only a unilateral tariff of general applicability. See U.S. Br. 36–37. Courts have recognized that, even in instances where the *Mobile-Sierra* doctrine does not apply directly, the “policies articulated in *Mobile* and *Sierra* support treating a settlement agreement as a factual difference that may justify a rate disparity” without running afoul of the Federal Power Act’s prohibition against undue discrimination. *Cities of Bethany v. FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984) (emphasis added); see also *Town of Norwood v. FERC*, 202 F.3d 392, 402 (1st Cir. 2000) (“public interest in promoting settlements” may justify disparate treatment); *Cities of Newark v. FERC*, 763 F.2d 533, 546 (3d Cir. 1985) (discussing “strong policy arguments favoring settlement agreements”). In other words, even if a settlement does not embody a fixed-rate contract, the policy considerations that inform *Mobile-Sierra* may still be relevant in assessing whether the terms of a settlement should or should not be modified.

None of this, however, changes the basic rule: When parties agree to a contract rate—regardless whether the contract is reflected in a written or oral contract, a settlement, or some other expression of agreement—the contract is subject to the *Mobile-Sierra* doctrine and the Commission may not modify the contract except as necessary in the public interest.

B. *Mobile-Sierra* Applies To The Contract Rates At Issue In This Case.

When one focuses on the difference between unilateral *ex parte* filings and fixed-rate contracts, it is clear that there is no basis for crafting a novel third-party exception to *Mobile-Sierra*. The Commission properly approved the parties' proposed settlement, including the provisions recognizing that *Mobile-Sierra* applies to rates fixed by contract.

To be sure, the settlement provisions establishing new market rules for New England are not themselves fixed-rate contracts. The settling parties acknowledged as much by including a *Memphis* clause in their agreement. But that does not mean that the contract rates embodied in, and contemplated under, the proposed settlement—specifically, (i) the transition payments, and (ii) the rates resulting from the auction process—are not subject to the *Mobile-Sierra* doctrine. Because in both instances the rates are established by contract, they cannot be modified by the Commission unless modifications are necessary in the public interest.

This point is especially clear with respect to the rates established through the capacity auction. *See* Pet. Br. 47–52. The settlement’s section 4.C. states that, although the rules for conducting the capacity auction are subject to modification by the Commission, once those rules are approved and in place, the rates fixed in contracts resulting from the capacity auction will be subject to *Mobile-Sierra*. *See* U.S. Br. 10. The D.C. Circuit accepted respondents’ assertions that this provision was somehow “thrusting” *Mobile-Sierra* on non-contracting third parties. In fact, the provision merely restates what the law already requires.

Section 4.C. was appropriately included in the settlement because it clarifies that the generally applicable tariff filed by ISO New England Inc. should not be construed to lift the ordinary *Mobile-Sierra* protections for rates fixed by contract. When a regional transmission organization (“RTO”) or independent transmission operator (“ISO”), files a unilateral tariff offering rates to prospective electric transmission customers, the tariff contains detailed rules for the organized markets administered by the RTO or ISO. Among other things, these rules set forth an offer-and-acceptance process through which parties may enter binding fixed-rate contracts without reducing their agreements to writing. Significantly, however, it is not unusual for these sorts of tariffs to include a *Memphis* clause. *See, e.g., Pro Forma Open Access Transmission Tariff*, § 9, Original Sheet No. 37; *see also* ISO New England Inc., FERC Electric Tariff No. 3, § I.8, First Revised Sheet No. 27. That unilaterally imposed provision preserves the RTO’s

or ISO's right to seek prospective changes to the tariff.

Although section 18 of the ISO New England tariff includes a provision that could be construed to be a *Memphis* clause, the settlement avoids confusion by making clear in section 4.C. that the provision does not apply to contracts resulting from the auction process. Section 4.C. thus serves to reassure market participants that the rates established through the capacity auction will be subject to the "default rule" of *Mobile-Sierra* and, therefore, treated the same as any other rates fixed by voluntary agreement. *Morgan Stanley*, 128 S. Ct. at 2739. Far from thrusting a unilateral standard on non-contracting parties, the settlement confirms that the Federal Power Act's ordinary requirements will apply.

More broadly, the D.C. Circuit's decision fundamentally misconstrues the *Mobile-Sierra* doctrine. Putting to one side the complexities of the settlement, the decision below appears premised on a notion that when parties agree to a contract rate, they are somehow disadvantaging non-contracting third parties by "thrusting" a more stringent standard of review on would-be challengers. But *Mobile-Sierra* recognizes that agreed-on rates that are the product of arms-length contracting are presumptively just and reasonable. The resulting standard of review flows ineluctably from that legal and regulatory framework and is not a disadvantage that is thrust upon non-contracting parties. Although such a presumptively reasonable rate may make it harder for third parties to challenge the rate, it no more

disadvantages third parties than reasonable government action disadvantages parties who could otherwise complain that the action is arbitrary and capricious.

III. This Court Should Reject The Commission's Attempt To Loosen The Statutory Constraints On Its Authority.

In opposing the petition for *certiorari*, the Commission soothingly suggested that it could “mitigate” the pernicious effects of the D.C. Circuit’s third-party exception by rejecting “rate challenges that amount to inappropriate strategic behavior, such as a third-party complaint challenging a contract filed by a ‘proxy’ for one of the contracting parties.” FERC Opp. 11-12. In its merits brief, the Commission tacks in a different direction, acknowledging that the D.C. Circuit’s third-party exception is improper, but arguing that the Commission is entitled to *Chevron* deference in determining when the *Mobile-Sierra* doctrine should apply. See U.S. Br. 24–25, 30-33 (citing *Chevron U.S.A., Inc. v. NRDC*, 467 U.S. 837 (1984)).

The Commission took a similar approach in *Morgan Stanley*, contending that its decision to apply *Mobile-Sierra* to the contracts in that case deserved *Chevron* deference. See *Morgan Stanley*, 128 S. Ct. at 2745. The Court rejected that contention. Because the contracts in *Morgan Stanley* were fixed-rate contracts, “the Commission was *required* ... to apply the *Mobile-Sierra* presumption in its evaluation of the contracts here.” *Id.* (emphasis in original). The Court did not, however, opine more broadly on whether there

may be other circumstances in which the Commission is entitled to *Chevron* deference. The Court should take a similar approach here.

In its brief on the merits, the Commission attempts to avoid the statutory constraints on its authority by arguing that the “results of the capacity auctions, although possessing certain characteristics of contracts, do not constitute contracts between buyers and sellers.” U.S. Br. 30. But the Commission cites *no precedent* supporting this startling proposition. It merely asserts that, although the capacity auction produces binding commitments to sell and purchase capacity, *see* Pet. Br. 10, the resulting agreements are not subject to *Mobile-Sierra* because they “are not recorded” in “separate” written documents and because the consequences of default are described in the tariff. U.S. Br. 30.

The notion that only separate, fully integrated written agreements are subject to *Mobile-Sierra* has long been rejected. Almost 35 years ago, the D.C. Circuit held that the *Mobile-Sierra* doctrine applies to unwritten contracts because the Commission has an obligation “to respect contractual obligations of whatever nature” when those contracts serve the purpose of fixing rates. *Sam Rayburn Dam Elec. Coop. v. FPC*, 515 F.2d 998, 1008-1009 (D.C. Cir. 1975). As petitioners correctly explain, the sales occurring through auction are contracts because they result from a voluntary contracting process that fixes the rate at which capacity is sold and purchased. *See* Pet. Br. 47-48 (citing precedent). Moreover, although contracts resulting from the capacity auction may

incorporate general terms and conditions from the tariff (just as private contracts may incorporate the Uniform Commercial Code or Commercial Arbitration Rules), the critical price and quantity terms are not incorporated from, or reflected in, the tariff. Instead, price and quantity are determined through the auction process itself and, under the settlement, are reflected in separate filings made with the Commission under section 205 of the Federal Power Act—the same statutory provision under which contracts, unilateral tariffs, and other rate schedules are traditionally filed. *See* ISO New England Inc., FERC Electric Tariff No. 3, § III.13.8.2, First Revised Sheet No. 7319L (requiring the ISO to file information, including the prices set through the auction process, a list of which resources received capacity supply obligations, and the amount of those obligations); *see also* J.A. 118 (same). Accordingly, precisely because the rates resulting from the capacity auction represent binding obligations fixed by voluntary agreement between buyer and seller, the contracts rates are protected under the Federal Power Act and the Commission has no authority to modify them.

As courts have recognized, the Commission has demonstrated a long-standing ambivalence to, and sometimes even hostility towards, the *Mobile-Sierra* doctrine. *See, e.g., Boston Edison Co. v. FERC*, 233 F.3d 60, 68 (1st Cir. 2000) (the Commission is “becoming hostile to *Mobile-Sierra*”); *Rayburn*, 515 F.2d at 1005 (the Commission’s “distaste for the *Mobile-Sierra* doctrine is well known”); *Borough of Lansdale v. FPC*, 494 F.2d

1104, 1110 (D.C. Cir. 1974) (same). This Court should therefore decline the Commission's invitation to loosen the statutory constraints on its authority. *Cf. Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374-75 (1986) (an "agency may not ... expand its power in the face of a congressional limitation on its jurisdiction"); David B. Spence & Frank Cross, *A Public Choice Case for the Administrative State*, 89 *Geo. L.J.* 97, 113 (2000) ("when an agency must make decisions about the reach of its own jurisdiction, self-interest propels the agency toward ever more expansive interpretations of the law"). Instead, to the extent it addresses the issue, the Court should reaffirm that, although the Commission is generally entitled to deference "in its rate decisions," *Morgan Stanley*, 128 S. Ct. at 2738, the Commission has no discretion to pick and choose which contracts are subject to the *Mobile-Sierra* doctrine.

This Court's decisions in *Mobile* and *Sierra*, as affirmed in *Morgan Stanley*, articulate a clear and binding interpretation of what the statutory language demands, recognizing that the statute imposes important constraints on agency decisionmaking by framing the boundaries of permissible Commission action. In particular, as described above, the Federal Power Act ensures that market participants can rely on the sanctity of long-term contracts by mandating that the Commission's interference with private contractual arrangements is limited. *See Public Serv. Comm'n of State of New York v. FERC*, 866 F.2d 487, 488-89 (D.C. Cir. 1989) (noting that courts have repeatedly "repelled" the Commission's "gambit" to

“compromise [the] limits ... on its power to revise rates”). Accordingly, because this Court has determined the Federal Power Act’s clear meaning, it need not “reach any issue of deference” to the Commission. *Lechmere, Inc. v. NLRB*, 502 U.S. 527, 536 (1992).

Having “bargain[ed] in the shadow” of *Mobile-Sierra* for more than five decades, *Boston Edison*, 233 F.3d at 66, energy market participants have ordered their affairs on the assumption that the Commission is permitted to modify contracts only in accordance with *Mobile-Sierra*’s well-defined understanding of “extraordinary circumstances” of “unequivocal public necessity.” *Permian*, 390 U.S. at 822. Upsetting those expectations not only engenders uncertainty, it invites an interlude of unpredictable agency reaction. The risk that market participants will be subject to uncertain Commission policies poses a further threat to the stability of our Nation’s energy markets. That threat can and should be defused by this Court’s reversal of the decision below.

CONCLUSION

For the foregoing reasons, the Court should reverse the judgment of the Court of Appeals.

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