No. 06-1100

In The Supreme Court of the United States

STATE OF CALIFORNIA EX REL.
EDMUND G. BROWN JR., ATTORNEY GENERAL,

Cross-Petitioner,

v.

CORAL POWER, L.L.C., et al.,

Cross-Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

CROSS-PETITIONER'S REPLY BRIEF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page

CASES

TABLE OF AUTHORITIES – Continued

INTRODUCTION

The question presented by the cross-petition is whether Section 205 of the Federal Power Act ("FPA"), 16 U.S.C. § 824d (1994), permits utilities to charge unfiled rates subject only to *post hoc* challenges under FPA Section 206, 16 U.S.C. § 824e (1994). It does not.

In their oppositions, Coral Power L.L.C. et al. ("Sellers") and the Federal Energy Regulatory Commission ("FERC") try in various ways to skirt the issue, rather than address it directly. They insist that FERC has no obligation to "adhere rigidly to a cost-based determination of rates. . . ." Sellers Opposition ("Opp.") at 4 & n.3 (quoting *FERC v. Pennzoil Producing Co.*, 439 U.S. 508, 517 (1979)); FERC Opp. at 23. But that is a red herring. The issue is not whether the FPA requires cost-based rates, but whether rates are being *filed* as required by the statute. They argue that no "detariffing" has occurred because suppliers must file "market-based rate tariffs," Sellers Opp. at 11, despite the fact that "market-based rate tariffs" contain no rates whatsoever, just a statement that rates will be determined "by agreement." And they suggest that the Court should ignore the failure to file rates in tariffs on the grounds that FERC still "exercises substantial regulatory oversight." *Id*. But again, the issue is not whether FERC is doing an adequate job of market monitoring, but whether it is enforcing the FPA as written. Both FERC and the Sellers fail to come to grips with the text of the FPA or the numerous Supreme Court and circuit court decisions cited in the cross-petition which conflict squarely with the notion that a "market-based rate tariff" produces filed rates.

Although the California Attorney General continues to maintain that review should be denied in No. 06-888, if the Court decides otherwise, the cross-petition should also be granted because: 1) the question presented must be

resolved in order to properly consider the main petition; and 2) it independently warrants certiorari.[1]

A. The Question Presented By The Cross-Petition Must Be Resolved In Order To Properly Consider The Question Presented By The Main Petition.

The Sellers argue that the issue of whether market-based rate tariffs produce "filed rates" need not be resolved because the "central error of the Ninth Circuit was not its disregard of the filed rate doctrine," but that it granted FERC the power to award "reparations." Sellers Opp. at pp. 18-19. This is pure misdirection. The California Attorney General's complaint at FERC did not seek "reparations," and the Ninth Circuit did not grant FERC authority to award "reparations."

Rather, the complaint sought refunds as a remedy for widespread violations of the statutory rate filing requirement. *See* Complaint of State of California ex rel. Bill Lockyer, Attorney General, FERC Docket No. EL02-71, filed March 19, 2002, at 1-2 ("to the extent that any *non-filed* rates are found to exceed just and reasonable levels, the California Attorney General seeks refunds") (emphasis added). The Ninth Circuit – consistent with a long line of circuit court decisions – held that FERC has ample authority to award retroactive refunds in the face of such violations. *See* California Attorney General's Brief in Opposition, No. 06-888, filed Feb. 5, 2007, at 9-19.

In any event, the very authority on which the Sellers rely states that "Congress did not intend either court or Commission to have the power to award reparations on the ground that a *properly filed* rate or charge has in fact been unreasonably high or low." *Montana-Dakota Utils.*

[1] Contrary to the Sellers' claim, Sellers Opp. at 14 n.12, this case is an appropriate vehicle to decide the legality of FERC's use of "market-based rate tariffs." It involves a direct challenge to the legality of the scheme, FERC had an opportunity to rule on the merits and did so, and the Ninth Circuit addressed it on the merits, as well.

Co. v. Northwestern Pub. Serv. Co., 341 U.S. 246, 258 (1951) (Frankfurter, J., dissenting) (emphasis added). Thus, even if "reparations" were at issue in this case, the issue of whether the Sellers' "market-based rate tariffs" produced "properly filed" rates is inextricably bound up with the main petition.

B. The Cross-Petition Independently Warrants Review By The Court.

1. Taken together, *Electrical District No. 1 v. FERC*, 774 F.2d 490 (D.C. Cir. 1985) (Scalia, J.), *Regular Common Carrier Conference v. United States*, 793 F.2d 376 (D.C. Cir. 1986) (Scalia, J.), and *Southwestern Bell Corp. v. FCC,* 43 F.3d 1515 (D.C. Cir. 1995), hold that a filed tariff must specify the seller's "rate itself," *Electrical Dist. No. 1*, 774 F.2d at 492-93; *Southwestern Bell*, 43 F.3d at 1520-21 (same), or at the very least a rate "formula" that enables the public to determine how the rate will be determined. *Regular Common Carrier Conference* ("*RCC*"), 793 F.2d at 379-80. The Sellers' notion that a market-based rate tariff is a "filed rate" conflicts squarely with these and numerous other cases cited in the cross-petition.

The Sellers are incorrect that "*Electrical District* and its progeny" relate solely to what it means to "fix" a rate under FPA Section 206, and have no bearing on what it means to file a schedule "showing all rates" for "any" sale of wholesale power under FPA Section 205, 16 U.S.C. § 824d(c). Sellers Opp. at 13; *see also* FERC Opp. at 20. The holding in *Electrical District No. 1* – that FERC orders fixing rates must specify the rate itself – applies equally to FERC's acceptance of rates filed under Section 4 of the Natural Gas Act ("NGA"), 15 U.S.C. § 717c (2006), which is substantially identical to FPA Section 205. *See Columbia Gas Transmission Corp. v. FERC*, 831 F.2d 1135, 1141 (D.C. Cir. 1987); *see also Southwestern Bell*, 43 F.3d at 1521-22 (holding that Section 203(a) of the Communications Act of 1934 ("CA"), 47 U.S.C. § 203(a) (2002), the analog to FPA Section 205(c), contains a "clear congressional mandate"

that filed tariffs show the "actual rate proposed to be charged").[2]

The Sellers further suggest that if formula rates are acceptable, market-based rate tariffs must also pass muster. Sellers Opp. at 14-15 (citing *Transwestern Pipeline Co. v. FERC*, 897 F.2d 570, 578 (D.C. Cir. 1990)). That does not address the problem, however, because market-based rate tariffs are not formula rates. *See, e.g.,* Petitioners' Appendix ("Pet. App."), No. 06-888, at 40a. And market-based rate tariffs exhibit none of the characteristics which have made formula rates acceptable in some past cases. *E.g., Ocean State Power II*, 69 FERC ¶ 61,146, at p. 61,522 (1994) (a formula rate is premised on the rate design's "fixed, predictable nature").

The Sellers argue that market-based rate tariffs comply with FPA Section 205 because "competitors and customers alike know that prices will be set by the market," Sellers Opp. at 15, and that utilities with market-based rate authority can charge "only the rates set forth in their rate schedules." *Id*. at 10; *see also* FERC Opp. at 22 (arguing that market-based sales are made "in accordance with" a market-based rate umbrella tariff). This is just wordplay. There is nothing in "market-based rate tariffs" to "abide by." Sellers Opp. at 11. They contain no rates, and no standard at all that could be used to determine whether utilities are adhering to the rates supposedly pre-authorized (years in advance and sight unseen) by FERC.

In FERC's scheme, the supposed "filed rate" is *any* rate the market will bear, including a market rife with supplier market power and abuse, unless and until FERC revokes the seller's grant of market-based rate authority, if ever. *But see Arkansas Louisiana Gas Co. v. Hall* ("*Arkla*"), 453 U.S. 571, 577 (1981) (holding that "the Act bars a regulated seller of natural gas from collecting a rate other than the

[2] The Sellers do not attempt to distinguish *Southwestern Bell*, nor could they. CA Section 203(a), 47 U.S.C. § 203(a), requires "schedules showing all charges," which is virtually identical to FPA Section 205(c)'s mandate for "schedules showing all rates and charges." 16 U.S.C. § 824d(c).

one filed with the Commission"). Further, the public has no way of knowing what the "market" rate will be in any given circumstance, and hence no way to exercise its right of complaint about proposed rates under FPA Section 205(e), 16 U.S.C. § 824d(e). *See, e.g., RCC*, 793 F.2d at 379.[3]

2. In *MCI Telecommunications Corp. v. AT&T Co.*, 512 U.S. 218 (1994), the Federal Communications Commission ("FCC"), like FERC, allowed "non-dominant" long-distance carriers to dispense with rate filings only after it made a prediction, based on record evidence, that they were incapable of exercising market power. The FCC further argued, like FERC, that it would continue to monitor the market, field consumer complaints, initiate investigations on its own motion, and take other affirmative steps to ensure that rates *remained* just and reasonable. The Court, however, rejected the FCC's rationale and held the "permissive detariffing" rule invalid. In doing so, the Court rejected a regulatory model that is identical in all material respects to the one that FERC and the Sellers are trying to defend here.

Similarly, in *Maislin Industries, U.S., Inc. v. Primary Steel, Inc.,* 497 U.S. 116 (1990), the Interstate Commerce Commission ("ICC") allowed common carriers operating in competitive markets, i.e., common carriers that were presumptively incapable of exercising market power, to charge and collect privately negotiated, unfiled rates that were lower than rates already on file for the same service. This Court held the scheme invalid because, among other reasons, the ICC had no means of judging "in advance the reasonableness of *unfiled* rates," notwithstanding the "new

[3] The Sellers cite *Elizabethtown Gas Co. v. FERC*, 10 F.3d 866 (D.C. Cir. 1993), to support a claim that "*every court* to have opined" on the issue has upheld FERC's "market-based rate regime." *See* Sellers Opp. at 1 (emphasis in original). In fact, the D.C. Circuit refused to decide in that case whether a scheme similar to FERC's "market-based rate regime" for wholesale power complied with the NGA's rate filing requirements. *Elizabethtown,* 866 F.3d at 871.

competitive atmosphere" in the motor carrier industry. 497 U.S. at 121, 132.

The Sellers and FERC offer various distinctions in order to address the conflict with *Maislin* and *MCI*, but none withstands scrutiny. First, as discussed above, there is essentially no difference between filing a "market-based rate tariff" and filing no tariff at all. "Stripped of its semantic cover," *see Maislin*, 497 U.S. at 131, a "market-based rate tariff" functions as an *ultra vires exemption* from the rate filing requirement.

Second, the suggestion that *Maislin* and *MCI* are somehow inapplicable because the FPA permits customer-specific contracting – an argument that FERC explicitly rejected below[4] – is erroneous. *See* Sellers Opp. at 12; FERC Opp. at 21. The FPA permits utilities to set rates by contract or otherwise, but all contracts, and the rates charged in those contracts, must nonetheless be individually filed under FPA Section 205. *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp*. ("*Mobile*"), 350 U.S. 332, 339, 342 (1956); *see also Arkla*, 453 U.S. at 582 (the fact that utilities may set rates by contract does not in any way "affect the supremacy of the Act itself").[5] Further, *all* rates, whether set by contract or otherwise, must be just and reasonable. 16 U.S.C. § 824d(a).

The Sellers go so far as to suggest that rate filings – and, indeed, regulatory review of rate filings under FPA section 205 – are wholly unnecessary in the wholesale power industry because the contracting parties 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." Sellers Opp. at 12 (quoting *Verizon Communications Inc. v.*

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[4] *See* Pet. App. at 70a-71a.

[5] By comparison, Congress expressly permitted the ICC to completely exempt motor contract carriers from the ICA's rate filing requirement. *See Maislin*, 497 U.S. at 133 & n.13 (citations omitted). Congress has never authorized a similar exemption for FERC-jurisdictional public utilities.

FCC, 535 U.S. 467, 479 (2002)). But the argument has little or no bearing on this case, in which the Sellers claim that their "filed rate" is based *not* on customer-specific contracts, but a generally applicable, "umbrella tariff."

Further, the argument fundamentally misstates both the law and the legislative history of the FPA. The FPA departed from the common carrier model because the "vast number of retail transactions of railroads made policing them administratively impossible," whereas, at the time the FPA was enacted, there were "relatively few wholesale transactions," and "these typically require[d] substantial investment in capacity and facilities for the service of a particular [customer]." *See Mobile*, 350 U.S. at 338-39. Further, Congress presumed that public utilities possessed monopoly power, and that they would abuse that power absent effective public regulation. *E.g., Gulf States Utils. Co. v. FPC*, 411 U.S. 747, 758-59 (1973).

Finally, the fact that rates must be individually reported after-the-fact for market monitoring purposes, and to facilitate the filing of complaints *after* rates have already gone into operation, does not serve to distinguish *MCI*, *Maislin*, *Southwestern Bell*, *RCC*, or any of the other cases cited in the cross-petition. *See* FERC Opp. at 20-22, 24. In *MCI*, the court rejected the FCC's claim – identical to FERC's claim here – that *post hoc* monitoring and enforcement cures the failure to file all rates in advance. *Compare* 512 U.S. at 230-231 & n.4 *with* 512 U.S. at 243 & n.6 (Stevens, J., dissenting).

The FCC's failure to require the filing of *proposed* rates vitiated CA Section 204, 47 U.S.C. § 204 (2002), which is essentially identical to FPA Section 205(e). *MCI*, 512 U.S. at 230. Focusing solely on a utility's ability to exercise market power at the outset, instead of on the rates to be charged in individual transactions, may or may not be a better scheme for reviewing proposed rates, but it is "not the one that Congress established." *Id.* at 234.

FERC's response to this – that Sections 205(d) and (e) are "fully satisfied" by the filing of a "market-based rate tariff," FERC Opp. at 19 – simply ignores what the Ninth Circuit held about Section 205(e). *See* Pet. App. at 18a

(holding that the "§ 205(e) refund remedy is, practically speaking, eliminated under the scheme as FERC would have us interpret it.").[6] It also fails to come to grips with *MCI*, *Maislin* or any of the other cases cited in the cross-petition, or the text of the statute itself, which requires that each rate charged be individually filed. FERC cannot simply define all rate "changes" out of existence in this manner; such an approach would abrogate the statute's suspension and refund provisions under FPA Section 205(e). *Sun Oil Co. v. FPC*, 281 F.2d 275, 278 (5th Cir. 1960).[7]

Finally, *MCI*'s passing mention that the FCC could "modify" the rate filing requirement by, among other things, deferring the filing of rates in "limited circumstances" does not reconcile FERC's "market-based rate regime" with *MCI*, *Maislin*, and the FPA. *See* FERC Opp. at 23 (citing *MCI*, 512 U.S. at 234). Unlike the FCC, FERC has no parallel authority to "modify" the FPA's filing requirement. And, more to the point, rates are *never* filed under FPA Section 205, they are merely made public after-the-fact.

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[6] FERC and the Sellers purport to defend the Ninth Circuit's decision as an endorsement of the market-based rate regime, but the court only held the scheme does not violate the FPA "*per se*." Pet. App. at 18a. And it went on to hold that post-transaction reporting could not be used solely for "informational" purposes, but had to be treated as an "integral part" of the filed rate itself, with "enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds . . . ." *Id.* at 16a. Even after that, however, FERC and the Sellers maintain that quarterly reporting exists solely to facilitate the filing of complaints under FPA Section 206, a contention that the Ninth Circuit rejected on the grounds that such a scheme could not be justified under *Maislin* and *MCI*. *Id*. at 16a-18a.

[7] Contrary to FERC's recitation, the Sellers acknowledge that market-based rate tariffs are frequently (perhaps typically) filed under Section 205(c), and not Section 205(d). Sellers' Opp. at 5. In such cases there is no opportunity at *any* time for the public to exercise their right of complaint under FPA Section 205(e), because that section only applies to rate "changes" filed under Section 205(d), and not to rates filed under Section 205(c). *Middle South Energy, Inc. v. FERC*, 747 F.2d 763, 768-69 (D.C. Cir. 1984).

C. The Question Presented Is Not Whether Competition Is Desirable Or Achievable, But Whether The Use Of "Market-Based Rate Tariffs" Conflicts With *MCI*, *Maislin*, And The FPA.

The Sellers try to paint the cross-petition as a referendum on competitive markets, *see* Sellers Opp. at 20-22, but the question presented here has no bearing on whether competition is desirable or achievable, or whether FERC has discretion to rely on markets as a means of disciplining prices. The issue is whether FERC's use of umbrella, "market-based rate tariffs" conflicts with *MCI*, *Maislin*, and other decisions interpreting FPA Section 205 and other "well-established statutory filed rate requirements." *Maislin*, 497 U.S. at 135. It does.

Further, the Sellers' warning that competitive markets would be "impractical" without the unfettered pricing flexibility afforded by "market-based rate tariffs" is without foundation. Sellers Opp. at 20-22. The Sellers omit the fact that most of the power needed to serve customers is bought and sold under long-term arrangements, and there is no practical reason why long-term contracts that last months and years cannot be separately filed in advance of their taking effect under FPA Section 205.

With respect to short-term, "spot" markets with centralized clearing prices, the Sellers fail to make the case that such markets would be wholly unworkable without "market-based rate tariffs." FERC certainly never made such a determination. But even if they were right, the argument is at bottom a complaint about the FPA's prior notice and filing requirement, and not a reason to deny the cross-petition. "Market-based rate tariffs" may be the best way to sustain highly competitive and liquid spot markets, but only Congress can amend the FPA to permit such a regime, and it has not done so.[8]

[8] The Sellers argue vainly that the Energy Policy Act of 2005 somehow "ratified" FERC's reliance on "market-based rate tariffs." Sellers Opp. at 16-18. Contrary to their claim, new provisions prohibiting

(Continued on following page)

CONCLUSION

If the Court were to grant the petition in No. 06-888, it should also grant the California Attorney General's cross-petition.

Dated: May 29, 2007

Respectfully submitted,

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"market manipulation" and promoting price transparency in wholesale power "markets" do not necessarily "presume" the validity of "market-based rate tariffs." Indeed, there were wholesale power "markets" before the FPA was enacted. The salient fact is that Congress did not amend Section 205 to permit "market-based rate tariffs." In sharp contrast, Congress has acted on numerous other occasions to promote competition in regulated industries, or segments thereof, and it has done so specifically by eliminating or relaxing the rate filing requirement. *See, e.g., Worldcom, Inc. v. FCC*, 209 F.3d 760, 762-63 (D.C. Cir. 2000) (domestic long-distance carriers); *Cent. & S. Motor Freight Tariff Ass'n v. U.S.,* 757 F.2d 301 (D.C. Cir. 1985) (motor contract carriers).