Supreme Court, U.S.
FILED

No. 08-674 NOV 21 2008

OFFICE OF THE CLERK
William K. Suter, Clerk

IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

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

PETITION FOR A WRIT OF CERTIORARI

JEFFREY A. LAMKEN
MICHAEL G. PATTILLO, JR.
ADAM J. WHITE
BAKER BOTTS L.L.P.
1299 Pennsylvania Ave., NW
Washington, D.C. 20004-2400
(202) 639-7700

JOHN N. ESTES III
Counsel of Record
JOHN LEE SHEPHERD, JR.
SKADDEN, ARPS, SLATE MEAGHER & FLOM LLP
1440 New York Ave., NW
Washington, D.C. 20005
(202) 371-7338

Counsel for Petitioners

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D.C. 20002

QUESTION PRESENTED

Section 206 of the Federal Power Act (FPA), 16 U.S.C. § 824e(a), requires that rates for the transmission and sale of electricity in interstate commerce be "just and reasonable." Under the *Mobile-Sierra* doctrine—named for this Court's decisions in *United Gas Pipeline Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956)—the Federal Energy Regulatory Commission ("FERC") 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 "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737 (2008). In the decision below, 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." The question presented is:

Whether *Mobile-Sierra*'s public-interest standard applies when a contract rate is challenged by an entity that was not a party to the contract.

PARTIES TO THE PROCEEDINGS BELOW

Petitioners NRG Power Marketing, LLC (formerly NRG Power Marketing, Inc.), Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC intervened in the court of appeals and were parties in proceedings before the Federal Energy Regulatory Commission.

The following parties before the Federal Energy Regulatory Commission also intervened for the respondent in the court of appeals: Connecticut Department of Public Utility Control; TransCanada Power Marketing, Ltd.; International Power America, Inc.; Bridgeport Energy, LLC; Casco Bay Energy Co., LLC; NEPOOL Participants Committee; Milford Power Co., LLC; FPL Energy, LLC; Entergy Nuclear Generation Co., LLC; Entergy Nuclear Vermont Yankee, LLC; Mirant Energy Trading, LLC; Mirant Kendall, LLC; Mirant Canal, LLC; Boston Generation, LLC; Mystic I, LLC; Mystic Development, LLC; Fore River Development, LLC; Massachusetts Municipal Wholesale Electric Co.; Connecticut Municipal Electric Energy Cooperative; ISO New England, Inc.; Lake Road Generating Co.; Berkshire Power Co., LLC; MASSPOWER; Dominion Resources, Inc.; Dominion Energy Marketing, Inc.; Dominion Nuclear Connecticut, Inc.; Central Vermont Public Service Co.; PSEG Power, LLC; and PSEG Energy Resources & Trade LLC.

The Federal Energy Regulatory Commission was respondent in the court of appeals and is therefore a respondent here under this Court's Rule 12.6.

Respondents Maine Public Utilities Commission, the Attorney General of Massachusetts, and the Attorney General of Connecticut were the petitioners in the court

of appeals and parties before the Federal Energy Regulatory Commission.

The following parties before the Federal Energy Regulatory Commission intervened for the petitioners in the court of appeals: Industrial Energy Consumer Group; NEPOOL Industrial Customer Coalition; and NSTAR Electric & Gas Corp.

CORPORATE DISCLOSURE STATEMENT

Pursuant to this Court's Rule 29.6, petitioners NRG Power Marketing, LLC, Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC state that they are subsidiaries of NRG Energy, Inc. and that they have no outstanding shares of stock owned by the public. NRG Energy, Inc. is a Delaware corporation whose common stock is held by the public. NRG Energy, Inc. has no parent company and no publicly held company has a 10 percent or greater ownership in NRG Energy, Inc.

TABLE OF CONTENTS

	Page
Question Presented	i
Parties To The Proceedings Below	ii
Corporate Disclosure Statement	iii
Opinions Below	1
Jurisdiction	1
Statutory Provisions Involved	2
Statement Of The Case	2
I. Statutory Framework	2
A. The Federal Power Act	2
B. The *Mobile-Sierra* Doctrine	3
II. Proceedings Below	5
A. The New England Capacity Market	5
B. Proceedings Before FERC	6
1. The Proceedings And Settlement	6
2. FERC's Decision	8
C. Proceedings In The D.C. Circuit	10
1. The Panel Decision	10
2. This Court's Decision In *Morgan Stanley* And The Rehearing Petitions	12
Reasons For Granting The Petition	13
I. The Decision Below Raises An Issue Of Exceptional Importance And Upsets Decades Of Settled Understanding	16
A. *Mobile-Sierra* Has Been Critical To The Development Of Energy Infrastructure For Decades	16

TABLE OF CONTENTS—Continued

Page

B. The Court Of Appeals' Decision Upends *Mobile-Sierra* And Threatens Industry Stability 19

II. The Decision Below Squarely Contradicts This Court's Decision In *Morgan Stanley* And Decades Of Practice 23

A. This Court Rejected The Rationale Of The Decision Below In *Morgan Stanley* 23

B. The Decision Below Conflicts With Decades Of Settled Practice On An Important Issue 25

C. The Court Of Appeals' Decision Conflicts With Other Applicable Decisions And Principles 28

Conclusion 31

Appendix A – Court Of Appeals Opinion (March 28, 2008) 1a

Appendix B – FERC Order On Rehearing And Clarification (October 31, 2006) 28a

Appendix C – FERC Order (June 16, 2006) 102a

Appendix D – FERC Commissioners Kelly And Wellinghoff Dissenting Views (August 4, 2008) 224a

Appendix E – Court Of Appeals Order Denying Intervenors' Petition For Panel Rehearing (October 6, 2008) 241a

Appendix F – Court Of Appeals Order Denying Respondent's Petition For Panel Rehearing (October 6, 2008) 243a

TABLE OF CONTENTS—Continued

Page

Appendix G – Court Of Appeals Order Denying Intervenors' Petition For Rehearing En Banc (October 6, 2008) 245a

Appendix H – Court Of Appeals Order Denying Respondent's Petition For Rehearing En Banc (October 6, 2008) 247a

Appendix I – Court Of Appeals Briefing Order (August 22, 2008) 249a

Appendix J – Relevant Statutory Provisions........ 251a

TABLE OF AUTHORITIES

Page

CASES

Ark. La. Gas Co. v. *Hall*, 453 U.S. 571 (1981)........ 4, 14
Atl. City Elec. Co. v. *FERC*, 295 F.3d 1 (D.C. Cir. 2002)........ 10
Borough of Lansdale v. *FPC*, 494 F.2d 1104 (D.C. Cir. 1974)........ 11
Boroughs of Chambersburg v. *FERC*, 580 F.2d 573 (D.C. Cir. 1978)........ 26, 27
Boston Edison Co. v. *FERC*, 233 F.3d 60 (1st Cir. 2000)........ 26
Dynegy Power Mktg., Inc. v. *Pub. Utils. Comm'n of Cal.*, 128 S. Ct. 2993 (2008)........ 21
EEOC v. *Waffle House, Inc.*, 534 U.S. 279 (2002)........ 11, 30
FPC v. *Sierra Pac. Power Co.*, 350 U.S. 348 (1956)........ 3, 4, 11, 16, 17, 28
In re Vic Supply Co., Inc, 227 F.3d 928 (7th Cir. 2000)........ 31
Local No. 93, Int'l Ass'n of Firefighters v. *City of Cleveland*, 478 U.S. 501 (1986)........ 30, 31
Me. Pub. Utils. Comm'n v. *FERC*, 454 F.3d 278 (D.C. Cir. 2006)........ 11
Morgan Stanley Capital Group Inc. v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733 (2008)........ *passim*
Ne. Utils. Serv. Co. v. *FERC*, 993 F.2d 937 (1st Cir. 1993)........ 9, 26
N. Ind. Pub. Serv. Co. v. *Carbon County Coal Co.*, 799 F.2d 265 (7th Cir. 1986)........ 17

TABLE OF AUTHORITIES—Continued

Page

New England Power Co. v. *New Hampshire*, 455 U.S. 331 (1982) 2

Papago Tribal Util. Auth. v. *FERC*, 723 F.2d 950 (D.C. Cir. 1983) 9

Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 3, 4, 14, 17

Pub. Utils. Comm'n of Cal. v. *FERC*, No. 03-74207 (9th Cir. Oct. 20, 2008) 22

Pub. Utils. Comm'n of Cal. v. *FERC*, 474 F.3d 587 (9th Cir. 2006) 21

Pub. Serv. Co. of Indiana, Inc. v. *FERC*, 575 F.2d 1204 (7th Cir. 1978) 27

Sempra Generation v. *Pub. Utils. Comm'n of Cal.*, 128 S. Ct. 2993 (2008) 21

Town of Norwood v. *FERC*, 587 F.2d 1306 (D.C. Cir. 1978) 27

United Gas Pipe Line Co. v. *Memphis Light, Gas & Water Div.*, 358 U.S. 103 (1958) 5

United Gas Pipe Line Co. v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) .... *passim*

Verizon Commc'ns Inc. v. *FCC*, 535 U.S. 467 (2002) 3

Wis. Pub. Power, Inc. v. *FERC*, 493 F.3d 239 (D.C. Cir. 2007) 27

STATUTES

Federal Power Act, tit. II, ch. 687, 49 Stat. 803, codified as amended at 16 U.S.C. § 824 *et seq.* 2

16 U.S.C. § 824 2

TABLE OF AUTHORITIES—Continued

Page

16 U.S.C. § 824d(a) 2
16 U.S.C. § 824d(b) 2
16 U.S.C. § 824d(c) 2
16 U.S.C. § 824d(d) 2
16 U.S.C. § 824e(a) 2, 15
16 U.S.C. § 824e(b) 2
28 U.S.C. § 1254(1) 2

ADMINISTRATIVE MATERIALS

18 C.F.R. § 385.602(h) 8
72 Fed. Reg. 39,904 (2007) 5, 14, 18, 20
Californians for Renewable Energy, Inc. v. *Cal. Pub. Util. Comm'n*, 120 FERC ¶ 61,272 (2007) 18
Devon Power LLC, 107 FERC ¶ 61,240 (2004) 6
Devon Power LLC, 103 FERC ¶ 61,082 (2003) 6
Duke Energy Carolinas, LLC, 123 FERC ¶ 61,201 (2008) 22
NEPOOL Power Pool Agreement, 48 FPC 538 (1972) 6
Nev. Power Co. v. *Duke Energy Trading & Mktg., L.L.C.*, 99 FERC ¶ 61,047 (2002) 5, 14, 18
Nev. Power Co. v. *Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353 (2003) 18
Pac. Gas & Elec. Co., 7 FPC 832 (1948) 3

TABLE OF AUTHORITIES—Continued

Page

Pennsylvania-New Jersey-Maryland Interconnection, 108 FERC ¶ 61,032 (2004) 9

Pub. Utils. Comm'n of Cal., 105 FERC ¶ 61,182 (2003) 9

S. Cal. Edison Co., 125 FERC ¶ 61,096 (2008) 22

Trailblazer Pipeline Co., 87 FERC ¶ 61,110 (1999) 8

Trailblazer Pipeline Co., 85 FERC ¶ 61,345 (1998) 8

United Gas Pipe Line Co., 5 FPC 770 (1946) 3

MISCELLANEOUS

Lawrence J. Makovich, *California Power Crisis Aftershock: The Potential Modification of Western Power Contracts* (2007) 17, 22

IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

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

PETITION FOR A WRIT OF CERTIORARI

NRG Power Marketing, LLC, Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-27a) is reported at 520 F.3d 464. The order of the Federal Energy Regulatory Commission (Pet. App. 102a-223a) is reported at 115 FERC ¶61,340, and the order on rehearing (Pet. App. 28a-101a) is reported at 117 FERC ¶61,133.

JURISDICTION

The court of appeals entered its judgment on March 28, 2008. The court denied rehearing and rehearing en

banc on October 6, 2008. Pet. App. 241a-248a. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Relevant provisions of the Federal Power Act, tit. II, ch. 687, 49 Stat. 803, 838-63 (codified as amended at 16 U.S.C. §§ 824-824w), are set forth at Pet. App. 251a-261a.

STATEMENT OF THE CASE

I. STATUTORY FRAMEWORK

A. The Federal Power Act

The Federal Power Act ("FPA"), 16 U.S.C. § 824 *et seq.*, gives the Federal Energy Regulatory Commission ("FERC") "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce." *New England Power Co.* v. *New Hampshire*, 455 U.S. 331, 340 (1982); see 16 U.S.C. § 824. Section 205 of the Act requires that "[a]ll rates * * * made, demanded, or received" by wholesale sellers of electricity be "just and reasonable," 16 U.S.C. § 824d(a), and bars discriminatory pricing, *id.* § 824d(b). Under FPA § 205, sellers must file "schedules showing all rates and charges * * * together with all contracts" for the sale of wholesale electricity in interstate commerce. *Id.* § 824d(c). Sellers must also notify FERC of proposed rate changes. See *id.* § 824d(d).

Section 206 defines FERC's authority to change rates. Under that provision, FERC can investigate the lawfulness of any rate on its own motion or on complaint. 16 U.S.C. § 824e(a). If FERC finds a rate "unjust, unreasonable, unduly discriminatory or preferential," it must "determine the just and reasonable rate * * * to be thereafter observed and * * * shall fix the same by order." *Ibid.* FERC may order refunds of unjust or unreasonable charges made after the investigation or complaint is initiated. See *id.* § 824e(b).

The FPA "'departed from the [traditional] scheme of purely tariff-based regulation'" by allowing parties to

negotiate contract rates. *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2738, 2747 (2008) (quoting *Verizon Commc'ns Inc.* v. *FCC*, 535 U.S. 467, 479 (2002)). The FPA recognizes that parties to wholesale power contracts are generally "sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them." *Verizon*, 535 U.S. at 479. "The regulatory system created by the Act" thus "is premised" on preserving "contractual agreements voluntarily devised by the regulated companies." *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968).[1]

B. The *Mobile-Sierra* Doctrine

The *Mobile-Sierra* doctrine at issue here arises from this Court's twin decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) ("*Mobile*"), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*"). *Mobile-Sierra* limits FERC's authority under FPA § 206 to authorize or require changes in rates set by contract. See *Morgan Stanley*, 128 S. Ct. at 2738-40. In both *Mobile* and *Sierra*, sellers filed rate schedules and contracts with FERC's predecessor, the Federal Power Commission. *United Gas Pipe Line Co.*, 5 FPC 770 (1946); *Pac. Gas & Elec. Co.*, 7 FPC 832 (1948).

In *Mobile*, the seller unilaterally filed a new rate to replace an unfavorable contract rate. The Court declared that unilateral attempts to abrogate a previously-filed contract, by submitting a new rate for review, are a "nullity." 350 U.S. at 339. The Court held that, even if the new rate would be just and reasonable, an existing

---

[1] For many years, such contracts or rate formulas were filed with FERC, although FERC has since shifted to a market-based system that does not require each contract be filed before becoming effective. *Morgan Stanley*, 128 S. Ct. at 2740-42.

rate set by agreement between the parties may not be set aside unless it "conflict[s] with the public interest." *Id.* at 345.[2]

In *Sierra*, the Court held that the public-interest standard applies *even if* the Commission finds that the prior contract rate would be unjust and unreasonable absent an existing agreement. See 350 U.S. at 353-54. When a rate is established by contract, FERC's authority is limited: "[A] contract may not be said to be either 'unjust' or 'unreasonable' simply because it is unprofitable to the public utility." *Id.* at 355. Instead, a contract rate may be abrogated as contrary to the "public interest" only if it "might impair the financial ability of a public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." *Ibid.* Because "[t]he regulatory system created by the 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." *Permian Basin*, 390 U.S. at 822.

That protection for contractually negotiated rates, the Court explained, is critical not merely to the contracting parties but also to the welfare of the markets. Energy infrastructure projects, particularly power generation projects, are enormously capital intensive and may take years to complete; absent assurances that agreements to purchase electricity at a specific rate will be enforced, few could risk making those investments. "By preserving the integrity of contracts," the *Mobile-Sierra* doctrine "permits the stability of supply arrangements which

[2] While *Mobile* arose under the Natural Gas Act, key sections of that Act and the FPA are "substantially identical," 350 U.S. at 353, and the Court has "cite[d] interchangeably decisions interpreting the pertinent sections of the two statutes," *Ark. La. Gas Co.* v. *Hall*, 453 U.S. 571, 577 n.7 (1981).

all agree is essential to the health of the * * * industry." *Mobile*, 350 U.S. at 344. "[U]ncertainties regarding rate and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm consumers in the long run." *Morgan Stanley*, 128 S. Ct. at 2749 (quoting 72 Fed. Reg. 39,904, 39,906-907). Power markets "cannot attract the capital needed to build adequate generating infrastructure" unless everyone understands that FERC will uphold contract rates absent "*extraordinary* circumstances." *Nev. Power Co.* v. *Duke Energy Trading & Mktg., L.L.C.*, 99 FERC ¶61,047, 61,190 (2002).

This Court has also held that contracting parties can agree that a different standard—not the *Mobile-Sierra* public-interest standard—should govern future modifications. See *United Gas Pipe Line Co.* v. *Memphis Light, Gas & Water Div.*, 358 U.S. 103, 110-13 (1958) ("*Memphis*"). Such provisions are known as "*Memphis* clauses." But, absent such a clause, *Mobile-Sierra* requires FERC to "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Morgan Stanley*, 128 S. Ct. at 2737. That "presumption" applies once the contract is signed "regardless of when the contract is reviewed," and it "may be overcome only if FERC concludes that the contract seriously harms the public interest." *Id.* at 2737, 2745-46.

II. PROCEEDINGS BELOW

A. The New England Capacity Market

This case arises out of FERC's efforts to ensure the reliability of the electric power system in New England. To maintain reliability, regulators and utilities must ensure that the electric system has sufficient generation capacity to respond to peak demand. System operators measure the adequacy of generation by "installed capa-

city"—the volume of electricity each power plant can produce.

More than three decades ago, the electric system operators in New England "pooled" their systems to form the "New England Power Pool." See *NEPOOL Power Pool Agreement*, 48 FPC 538, 549 (1972). In the late 1990s, the New England electric markets again restructured, turning over operation of the transmission system to an "Independent System Operator[]," an entity charged with "operat[ing] transmission facilities in a nondiscriminatory manner." *Morgan Stanley*, 128 S. Ct. at 2741. Dubbed "ISO-NE," that new entity began administering auction-based markets for electricity. This case arises from further reforms to that market.

B. Proceedings Before FERC

1. The Proceedings And Settlement

The ISO-NE capacity market failed to function as anticipated. "For many years" it was "rife with problems." Pet. App. 2a. The market did not provide sufficient incentives to retain or attract generation capacity. "As the Commission explained in 2003, 'existing generators needed for reliability are not earning sufficient revenues (and are in fact losing money), and [] additional infrastructure is needed soon to avoid violations of reliability criteria.'" *Ibid.* (quoting Pet. App. 137a). "In other words, the supply of capacity was barely sufficient to meet the region's demand." *Ibid.*

To resolve those problems, FERC ordered ISO-NE to revise its capacity market to compensate existing generators and promote construction of new generation where needed to maintain grid reliability. *Devon Power LLC*, 103 FERC ¶61,082 at 61,271 (2003). ISO-NE complied by filing a new locational installed capacity market mechanism, which FERC then set for hearing under FPA §206. *Devon Power LLC*, 107 FERC ¶61,240 at 62,020 (2004). Years of litigation ensued. Eventually,

all but eight of the 115 participants reached a settlement. Pet. App. 5a. Among the opponents were the Maine Public Utilities Commission and the Attorneys General of Connecticut and Massachusetts. Only one wholesale customer in the market opposed the agreement.

The new agreement created a "forward" capacity market. Under that new approach, ISO-NE would run an annual auction, and the winning suppliers (those with the lowest prices) would be obligated to provide capacity for a one-to-five year period starting three years in the future. Pet. App. 110a-111a. That design would "allow potential new capacity to compete in the auctions" by letting new entrants bid based on their willingness to build additional generating plants. *Ibid.* If a new generator were chosen at auction, it would be obligated to construct its new plant within three years, and it would receive fixed payments for up to five years to support necessary capital investment and financing. *Id.* at 110a-111a, 113a. The new market structure did not, however, compensate existing suppliers of capacity until the end of the three-year lead-time period. To bridge that gap, the settlement also included transition payments to existing suppliers to compensate them for continuing to make their capacity available. *Id.* at 116a-118a.

2. This petition concerns disagreement over the standard that would govern *future* challenges to the amount of the transition payments or the rates agreed upon as a result of the auction process; it does not concern the standard FERC applied in this case when deciding whether to approve the settlement agreement itself. With respect to such potential future challenges, the agreement included a *Memphis* clause that generally exempted any such challenges from operation of the *Mobile-Sierra* presumption of reasonableness. Pet. App. 193a-194a (quoting agreement §4C). But the *Memphis* clause excepted two items: (1) the transition payments to

existing generators; and (2) the requirement that winning bidders in the capacity market be paid the amount set at auction. *Ibid.* The agreement specified that, with respect to those items, the *Mobile-Sierra* standard would apply to all future challenges, "whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." *Ibid.* The parties explained that, for transition capacity and future capacity markets, stability and certainty were absolutely critical, both to ensure that existing generators would continue to supply necessary capacity, and to provide the incentive for new entrants to invest the large sums necessary to build additional capacity. See *id.* at 196a-197a.

Consistent with FERC's regulations and precedent regarding contested settlements, the agreement provided that FERC would review the agreement itself (including the transition payments, auction, and review provisions) under the ordinary just-and-reasonable standard. 18 C.F.R. §385.602(h); *Trailblazer Pipeline Co.*, 85 FERC ¶61,345 at 62,339-45 (1998), order on reh'g, 87 FERC ¶61,110 at 61,438 (1999). But, once FERC found the agreement just and reasonable and any judicial review was complete, future challenges to auction prices or transition payments (whether based on changed circumstances or otherwise) would be governed by *Mobile-Sierra*. After each auction, ISO-NE would file the resulting auction price with FERC under FPA §205. Because the auction price reflected a voluntary agreement between a willing buyer and willing seller, anyone later challenging the auction price would have to overcome the *Mobile-Sierra* presumption. Likewise, once FERC accepted the transition payment schedule, any new challenge to those rates would be governed by *Mobile-Sierra* as well.

2. FERC's Decision

FERC approved the agreement as "a just and reasonable outcome for this proceeding consistent with the public interest." Pet. App. 103a. It specifically addressed section 4C's requirement that future challenges to transition payments (provided in the agreement) or to future auction prices (once mutually agreed-upon through the auction and filed with FERC) would be subject to *Mobile-Sierra* public-interest review. *Id.* at 200a-203a. FERC rejected the claim that *Mobile-Sierra* could not apply to future challenges brought by third parties. *Id.* at 194a, 196a. FERC explained that it had "routinely permitted the use of similar provisions in settlement agreements, including contested settlements." *Id.* at 200a & n.150 (listing cases). And FERC reaffirmed the validity of such provisions, declaring that there is "no Commission or court precedent that supports a finding that a non-signatory may unilaterally seek changes to a *Mobile-Sierra* 'public interest' contract under the 'just and reasonable' standard of review." *Id.* at 200a-201a (quoting *Pennsylvania-New Jersey-Maryland Interconnection*, 108 FERC ¶ 61,032 at 61,204 (2004) (citing *Pub. Utils. Comm'n of Cal.*, 105 FERC ¶ 61,182 at 61,947 (2003))).

FERC also found that applying *Mobile-Sierra* review to third-party rate challenges does not deny third parties any rights. "'[T]he *Mobile-Sierra* doctrine itself allows for intervention by FERC where it is shown that the interests of third parties are threatened,'" because the Supreme Court's *Mobile-Sierra* test specifically requires FERC to protect outside parties from "'undue discrimination' or imposition of an 'excessive burden.'" Pet. App. 201a & n.153 (quoting *Ne. Utils. Serv. Co.* v. *FERC*, 993 F.2d 937, 961 (1st Cir. 1993)) (citing *Papago Tribal Util. Auth.* v. *FERC*, 723 F.2d 950, 953 n.4 (D.C. Cir. 1983) (recognizing FERC's ability under *Mobile-Sierra* to re-

dress contract rates that are "unduly discriminatory or preferential to the detriment of purchasers who are not parties to the contract")). Commissioner Kelly concurred, emphasizing that the agreement used the "*Mobile-Sierra* public interest standard in a very constrained and time-limited manner," applying it "only to the stated transition period prices and the annual prices generated each year by the [capacity market] auctions." Pet. App. 223a. FERC later denied rehearing. Pet App. 75a-79a.

C. Proceedings In The D.C. Circuit

1. *The Panel Decision*

The D.C. Circuit granted the petition for review in relevant part but denied it in all other respects. Pet. App. 1a-27a.[3] Before the D.C. Circuit, some parties again urged that *Mobile-Sierra*'s presumption of reasonableness could not be applied to future challenges filed by those who were not parties to the agreement. Applying that presumption, they urged, would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." *Id.* at App. 19a. Unlike FERC, the court of appeals regarded the scope of *Mobile-Sierra*'s application to non-contracting objectors as a question of first impression.

The panel agreed that, under the *Mobile-Sierra* doctrine, "'FERC may abrogate or modify freely negotiated private contracts that set firm rates or establish a specific methodology for setting the rates for service . . . only if required by the public interest.'" Pet. App. 19a. (quoting *Atl. City Elec. Co.* v. *FERC*, 295 F.3d 1, 14 (D.C. Cir. 2002)). Under that standard, contract rates or methodologies cannot be altered except "for the most

[3] The portions of the D.C. Circuit's decision upholding FERC's decision, including FERC's ruling that the transition payments and the auction mechanism were just and reasonable, Pet. App. 8a-11a; see also *id.* at 11a-19a, 24a-26a (upholding other FERC determinations), are not challenged or at issue in this petition.

compelling reasons," such as where they would "'impair the financial ability of the public utility to continue its service, cast upon other customers an excessive burden, or be unduly discriminatory.'" *Id.* at 20a-21a (quoting *Sierra*, 350 U.S. at 355).

But the panel also observed that, under FPA § 206, "when a party files a complaint against a rate or charge, FERC must adjudicate the challenge under the 'just and reasonable' standard." Pet. App. 20a. The panel then characterized *Mobile-Sierra*'s public-interest test as having "carv[ed] out an exception to this rule based on the 'familiar dictates of contract law.'" *Ibid.* (quoting *Borough of Lansdale* v. *FPC*, 494 F.2d 1104, 1113 (D.C. Cir. 1974)). The exclusive purpose of *Mobile-Sierra*, in the panel's view, was "to ensure contract stability *as between the contracting parties*." Pet. App. 24a (quoting *Atl. City*, 295 F.3d at 14).

The panel therefore held that *Mobile-Sierra* applies only "when '*one party to a rate contract* on file with FERC attempts to effect a unilateral rate change,'" and is inapplicable when a *non-party* attempts to alter the rates. Pet. App. 22a (quoting *Me. Pub. Utils. Comm'n* v. *FERC*, 454 F.3d 278, 284 (D.C. Cir. 2006)) (emphasis added). A contract, the panel asserted, "cannot bind a nonparty." *Ibid.* (quoting *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279, 294 (2002)). "[W]hen a rate challenge is brought by a non-contracting third party," the panel summarized, "the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in section 206 of the Federal Power Act." *Ibid.* A contrary holding, the court stated, would "deprive[] non-settling parties of their statutory right" to have future "rate challenges adjudicated under the" statutory "'just and reasonable standard' * * * in cases of changed circumstances." *Id.* at 22a-23a.

The panel did not dispute that FERC had long applied *Mobile-Sierra* to third-party challenges. Pet. App. 23a. That longstanding position, the court stated, "does not necessarily support the policy's legality, since none of the cited orders have been subject to judicial review on the *Mobile-Sierra* issue." *Ibid.* And the court rejected FERC's contention that *Mobile-Sierra* was necessary "to promote price certainty and contract stability"—features that are indispensable to promoting investment in the large and long-term infrastructure projects required in the energy sector. *Id.* at 24a. Instead, the court reiterated its view that *Mobile-Sierra* provides contract stability only between the contracting parties, and does not apply to those who are not parties to the agreement. *Ibid.*

2. *This Court's Decision In* Morgan Stanley *And The Rehearing Petitions*

After the court of appeals issued its decision, this Court issued its decision in *Morgan Stanley*. In that case, this Court rejected the claim that the *Mobile-Sierra* public-interest standard is an atextual "exception" to the statutory "just and reasonable" standard. Reaffirming *Mobile-Sierra* and reversing a Ninth Circuit decision that declined to apply the doctrine in instances of alleged market failure, this Court rejected as "indefensible" the claim that *Mobile-Sierra* represents a departure from the statutory "just and reasonable" standard in FPA §206. 128 S. Ct. at 2740. The Court explained that, while "[t]here is only one statutory standard," *id.* at 2745, the *Mobile-Sierra* public-interest standard is a "differing *application* of that just-and-reasonable standard to contract rates." *Id.* at 2740. *Mobile-Sierra* requires FERC to "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737. And that mandatory "presumption may be overcome only

if FERC concludes that the contract seriously harms the public interest." *Ibid.*

Relying on *Morgan Stanley*, FERC and petitioners urged (among other things) that the panel had erred by characterizing *Mobile-Sierra* as an "exception" to the just-and-reasonable standard, Pet. App. 20a, and thus in "agree[ing]" that any application of that standard to challenges by non-parties would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard," *id.* at 19a. Under *Morgan Stanley*, they explained, the *Mobile-Sierra* public-interest standard is merely an "application" of the just-and-reasonable standard to contract rates. See FERC C.A. Reh'g Pet. 3-4, 6.[4]

On August 22, 2008, the court of appeals ordered a response to the rehearing requests. Pet. App. 249a-250a. On October 6, 2008, the court of appeals denied the petitions for rehearing and rehearing en banc. *Id.* at 241a-248a.

REASONS FOR GRANTING THE PETITION

For 50 years, the *Mobile-Sierra* presumption has encouraged investment in energy infrastructure by protecting contract rates. Under that doctrine, FERC must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct.

---

[4] Two FERC Commissioners dissented from the decision to seek rehearing. Pet. App. 224a. They indicated that a contested settlement itself should not be reviewed under the *Mobile-Sierra* standard, *id.* at 228a-229a (a position that was wholly consistent with the fact that FERC reviewed the settlement in this case under the ordinary just-and-reasonable standard, *id.* at 234a). This petition, however, concerns whether *Mobile-Sierra* can apply when non-parties bring *future* challenges to, for example, the rate set between a willing buyer and a willing seller in the forward capacity auctions—rates that generators must rely on to build new power plants over lengthy periods.

2733, 2737 (2008). That "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Ibid.* *Mobile-Sierra*'s public-interest standard precludes FERC from modifying or abrogating contract rates except in the most compelling cases. "[S]etting aside a contract rate requires a finding of 'unequivocal public necessity,' *Permian Basin [Area Rate Cases]*, 390 U.S. [47,] 822 [(1968)], or 'extraordinary circumstances,' *Arkansas Louisiana Gas Co.* v. *Hall*, 453 U.S. 571, 582 (1981)." *Morgan Stanley*, 128 S. Ct. at 2748.

Time and again this Court and FERC have recognized that *Mobile-Sierra* is critical to electricity and natural gas markets. "By preserving the integrity of contracts," *Mobile-Sierra* "permits the stability of supply arrangements which all agree is essential to the health of the * * * industry." *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332, 344 (1956). "[U]ncertainties regarding rate and contract sanctity can have a chilling effect on investments." *Morgan Stanley*, 128 S. Ct. at 2747 (quoting 72 Fed. Reg. 39,904, 39,906-907). "Competitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co.* v. *Duke Energy Trading & Mktg., L.L.C.*, 99 FERC ¶61,047, 61,190 (2002). Just last Term, this Court reaffirmed that the *Mobile-Sierra* doctrine is a "key source of stability" that reduces "volatility in[] the electricity markets" and thus "ultimately benefits consumers." 128 S. Ct. at 2749.

The decision below nonetheless holds that the *Mobile-Sierra* doctrine "simply does not apply" to the efforts of *non-parties* to challenge a contract rate. Pet. App. 22a. That unprecedented holding destroys the certainty and

stability that the electricity and natural gas markets require and that *Mobile-Sierra* attempts to provide. *Mobile-Sierra* cannot provide contractual certainty or stability if it applies *only* to challenges by contracting parties, but allows contract modification under a less rigorous standard in challenges brought by *anyone* else—whether it be one of millions of ratepayers, a state representative, a state attorney general (*parens patriae*), or FERC itself.

That destabilization will have a profound impact on the industry's ability to invest the enormous capital required to build additional power plants, transmission lines, and pipelines necessary to meet the demands of already energy-starved markets. This Court's decision in *Morgan Stanley* last Term rejected the Ninth Circuit's efforts to marginalize *Mobile-Sierra* as a species of "estoppel doctrine." 128 S. Ct. at 2746. This Court should likewise reject the current effort to marginalize *Mobile-Sierra* by making it applicable only when the challenge is brought by a contractual counterparty—but not when the challenge is brought by any one of the millions of other possible complainants.

The decision below, moreover, reaches that result by invoking a construction of the FPA indistinguishable from the one this Court rejected in *Morgan Stanley*. The D.C. Circuit ruled that the *Mobile-Sierra* "public-interest" test is "an exception" to the statutory just-and-reasonable standard in FPA § 206, 16 U.S.C. § 824e(a), and that applying it would deny third parties "their statutory right to challenge rates under the 'just and reasonable' standard." Pet. App. 19a, 20a; accord *id.* at 22a ("[W]hen a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in [FPA § 206]."). But this Court's decision in *Morgan Stanley* rejected, as

"obviously indefensible," the proposition that the *Mobile-Sierra* public-interest standard is "different from the statutory just-and-reasonable standard." 128 S. Ct. at 2740. Instead, the Court explained, the public-interest test represents a "differing *application* of that [statutory] just-and-reasonable standard to contract rates." *Ibid.* The decision below thus does not merely eviscerate a critical, 50-year-old protection against abrogation or modification of contract rates. It does so using a theory this Court just rejected last Term. Given the decision's dramatic consequences for electricity and gas markets, this Court's review is both warranted and necessary.

I. THE DECISION BELOW RAISES AN ISSUE OF EXCEPTIONAL IMPORTANCE AND UPSETS DECADES OF SETTLED UNDERSTANDING

The *Mobile-Sierra* doctrine has, for half a century, played a critical role in the development and preservation of our Nation's energy infrastructure. The decision below threatens to turn that doctrine into a legal relic that applies only when rate challenges are brought by the direct counterparties in a contract. That ruling overturns decades of settled understanding and eliminates the stability and certainty that are critical to the maintenance and development of energy infrastructure.

A. *Mobile-Sierra* Has Been Critical To The Development Of Energy Infrastructure For Decades

This Court's twin decisions in *Mobile*, *supra*, and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*"), establish what is now a bedrock principle of energy law: When two parties establish a wholesale rate by contract, FERC may not upset that rate unless it "conflict[s] with the public interest." *Mobile*, 350 U.S. at 345. That "public-interest" test is more demanding than the ordinary "just-and-reasonable" standard that FERC employs where the parties have not reached agreement. Absent a contract, FERC may reject a rate as "unjust"

or "unreasonable" if, for example, it would be unprofitable to one party. But once the parties agree to a rate by contract, that rate "may not be said to be either 'unjust' or 'unreasonable' simply because it is unprofitable to the public utility." *Sierra*, 350 U.S. at 355. Instead, a contract rate may be abrogated as contrary to the "public interest" only if it "might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." *Ibid.* Because "[t]he regulatory system created by the 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." *Permian Basin*, 390 U.S. at 822.

That doctrine is critical to energy providers and consumers alike. Building the infrastructure to generate and transmit electricity and natural gas requires enormous capital investments over lengthy periods. Absent certainty that promised rates will be paid, the incentive to build necessary infrastructure evaporates.[5] And because energy markets are exceedingly volatile, long-term fixed-price contracts are an essential hedge against volatility.[6] For those reasons, this Court's pathmarking

---

[5] See Lawrence J. Makovich, *California Power Crisis Aftershock: The Potential Modification of Western Power Contracts* 9 (2007), http://www2.cera.com/westernpowercontracts (emphasizing need for predictable enforcement given that "investment decisions must be made years in advance of operation, and these decisions must recognize that under the long operating lives of these assets, capital cost recovery must span numerous market cycles").

[6] As Judge Posner explained, "a fixed-price contract is an explicit assignment of the risk of market price increases to the seller and the risk of market price decreases to the buyer * * * . [If] the buyer forecasts the market incorrectly and therefore finds himself locked into a disadvantageous contract, he has only himself to blame and so cannot shift the risk back to the seller * * * ." *N. Ind. Pub. Serv. Co.* v. *Carbon County Coal Co.*, 799 F.2d 265, 278 (7th Cir. 1986).

Mobile decision recognized that preserving contract rates against after-the-fact challenge is critical to ensuring "the stability of supply arrangements which all agree is essential to the health of the * * * industry." 350 U.S. at 344. Just last Term, this Court rebuffed the Ninth Circuit's efforts to narrow the *Mobile-Sierra* doctrine, agreeing instead with FERC that "uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments." *Morgan Stanley*, 128 S. Ct. at 2747 (quoting 72 Fed. Reg. 33,906-907). The *Mobile-Sierra* doctrine, the Court continued, is a "key source of stability" that reduces "volatility in the electricity markets" and thus "ultimately benefits consumers." 128 S. Ct. at 2749.

FERC too has repeatedly underscored *Mobile-Sierra*'s critical role. "Competitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co.*, 99 FERC at 61,190. And *Mobile-Sierra* "has, if anything, become even more critical" in light of FERC's increasing reliance on markets and competition. *Ibid.* "The failure to protect parties' contractual expectations can harm customers by reducing the willingness of sellers and buyers to contract for rate certainty through fixed-rate contracts or by deterring sellers and buyers from making the investment needed to support the long-term contracts." *Californians for Renewable Energy, Inc.* v. *Cal. Pub. Utils. Comm'n*, 120 FERC ¶ 61,272 at 62,279 (2007).[7]

---

[7] See also *Nev. Power Co.* v. *Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353 at 62,393 (2003) (adopting ALJ's finding that "uncertainty [over] the enforceability of such contracts" would "erode investor confidence and willingness to invest in merchant energy projects, which, in turn, could have an adverse effect on infrastructure development").

B. The Court Of Appeals' Decision Upends *Mobile-Sierra* And Threatens Industry Stability

Notwithstanding the critical role that contract stability provides, the D.C. Circuit ruled that *Mobile-Sierra* provides protection only in a narrow category of cases—challenges brought by contractual counterparties—and provides no protection in challenges brought by non-parties. "[W]hen a rate challenge is brought by a non-contracting third party," that court held, "the *Mobile-Sierra* doctrine *simply does not apply*." Pet. App. 22a (emphasis added).

Left undisturbed, that "third-party exception" to *Mobile-Sierra*'s public-interest standard will engulf the rule and destroy the stability it is designed to provide. The decision would apply *Mobile-Sierra*'s presumption of reasonableness *only* to the two counterparties to the contract for the sale of power or natural gas. Literally *anyone else* that might be affected by a given contract would escape the presumption of reasonableness, including individual consumers, corporations, governmental entities, politicians, or state regulators. If any one of that boundless group of non-parties and potential surrogates asks FERC to abrogate a contract, they need not show, and FERC need not find, that the contract "seriously harm[s] the public interest." *Morgan Stanley*, 128 S. Ct. at 2743, 2746, 2748, 2750. It would be enough that the old rate looks "unjust" or "unreasonable" in light of new conditions—precisely the standard *Mobile-Sierra* and *Morgan Stanley* reject. Pet. App. 23a.

Subjecting fixed-price contracts to midstream abrogation if changing market conditions make one side of the contract (even temporarily) unattractive to any non-contracting entity destroys the purpose of those contracts. Such contracts could no longer serve as a "hedge" against spot-market volatility because, once that volatility arises, non-parties could challenge the contract rate as unreasonably low when compared to the then-

prevailing (much higher) market rates. Those expected to invest hundreds of millions of dollars developing new power plants will balk if the possibility of third-party challenges precludes them from relying on the promise to pay the contract price. Like the Ninth Circuit decision this Court reversed in *Morgan Stanley*, the decision below will "reduce the incentive" for both buyers and sellers to enter into long-term, fixed-price contracts. 128 S. Ct. at 2747. And as this Court observed in *Morgan Stanley*, consumers will suffer. "'[U]ncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm customers in the long run.'" *Id.* at 2749 (quoting 72 Fed. Reg. 39,906-907 (2007)).

This case illustrates precisely the dangers inherent in the court of appeals' new rule. FERC expressly approved the multiparty agreement here as just and reasonable, based on record evidence, after extensive litigation. Now, having litigated their objections to finality, non-parties will, if conditions change, get yet another chance to challenge the rates, exempt from the public-interest presumption. The resulting uncertainty is particularly problematic in connection with the auction pricing mechanism, which produces voluntary agreements to provide capacity three years in the future. See pp. 7-8, *supra*. That forward-capacity market is supposed to encourage new entrants to build additional generating capacity. To ensure that the promise to pay the amount set at auction provides an adequate incentive to invest the hundreds of millions necessary to build new capacity, the agreement provided *Mobile-Sierra* protection once the price is accepted by the buyer and seller through the auction process and is filed with FERC. But the promise to pay the auction amounts cannot provide the necessary incentive if the promise can be revisited continuously in light of changing circumstances. Only the

foolhardy (or those requiring enormous risk premiums) would invest millions to expand generation capacity with little certainty the contract price will be respected over the life of fixed-price agreement.

Nor will there be a shortage of non-contracting parties willing to challenge wholesale rate contracts. Because FERC regulates the middle of the distribution chain in both the electric and natural gas industries, there will always be interested non-parties as market conditions shift. If, in hindsight, the rate seems too high because the economy slips or demand declines, then retail customers, industrial buyers, state regulators and consumer advocates will step in to challenge the contract rate. If the rate seems too low because the economy heats up (or summer temperatures do), then an upstream supplier, lender, or any other entity interested in increasing contract prices—or avoiding what has become a money-losing contract—may likewise press for contract modification free from the dictates of the public interest presumption. The contract rate would be open to assault by interested parties on all sides.

One need look no further than the wake of this Court's decision in *Morgan Stanley* last Term to see the broad impact. One of the respondents in *Morgan Stanley* itself—the Office of the Nevada Attorney General, Bureau of Consumer Protection—was *not a party to the contract*. 128 S. Ct. at 2736. Following *Morgan Stanley*, moreover, this Court granted the petitions in companion cases, vacated the Ninth Circuit's judgment, and remanded for reconsideration in light of its decision. See 128 S. Ct. 2993 (mem.) (granting, vacating, and remanding *Pub. Utils. Comm'n of Cal.* v. *FERC*, 474 F.3d 587 (9th Cir. 2006), sub nom. *Sempra Generation* v. *Pub. Utils. Comm'n of Cal.* (No. 06-1454), and *Dynegy Power Mktg., Inc.* v. *Pub. Utils. Comm'n of Cal.* (No. 06-1468)). But the Ninth Circuit has now ordered briefing on

whether to apply the "third-party exception" to allow the complainants in those companion cases to avoid the public-interest presumption this Court articulated in *Morgan Stanley* instead of remanding the case to FERC. See *Pub. Utils. Comm'n of Cal.* v. *FERC*, No. 03-74207 (Oct. 20, 2008). It would be a rare case indeed where those seeking to evade *Mobile-Sierra* will be unable to find a non-party to join them in challenging the rates at issue.

The decision below has already created disarray in the industry and at FERC. Responding to that decision, FERC has adopted a new, nationwide policy that, if anyone files a contract that incorporates *Mobile-Sierra*'s public interest presumption, the contract must instead specify that it "imposes on non-contracting third parties the most stringent standard permissible under applicable law." *Duke Energy Carolinas, LLC*, 123 FERC ¶ 61,201 at 62,290 (2008).[8] No one knows exactly what that "most stringent standard" might be. But unless the decision below is reversed, it will *not* be the public-interest standard this Court reaffirmed in *Morgan Stanley*.[9]

The resulting "chilling effect on investments" could not come at a worse time. The electric and natural gas industries are highly capital intensive and fundamental to virtually all economic activity in this country. Over the next 15 years, the electric industry needs to invest an estimated $400 billion in new power plants and even more in additional infrastructure. See Makovich, *supra* note 5,

[8] FERC has applied the new policy announced in *Duke Carolinas* in 38 orders or letter orders, 36 of which post-date this Court's decision in *Morgan Stanley*. See, *e.g.*, *S. Cal. Edison Co.*, 125 FERC ¶ 61,096 at 61,517 & n.3 (Oct. 27, 2008).

[9] The court of appeals' decision invites forum shopping as parties who want to preserve their *Mobile-Sierra* rights flee the decision below by seeking judicial review in other circuits. Energy companies and energy markets will thus confront profound uncertainty until this question is settled by this Court.

at 13-15. Contract certainty will be essential to support that massive new investment. By eviscerating the *Mobile-Sierra* doctrine, the decision below threatens that new investment precisely when it is needed most.

II. THE DECISION BELOW SQUARELY CONTRADICTS THIS COURT'S DECISION IN *MORGAN STANLEY* AND DECADES OF PRACTICE

The decision below did not merely eviscerate the *Mobile-Sierra* doctrine. It did so by invoking a legal theory that this Court rejected just last Term. It rejects FERC's position that *Mobile-Sierra* properly applies to non-party challenges. Pet. App. 200a & n.150 (listing cases); *id.* at 22a-23a. And it adopts a position that conflicts with decades of settled practice.

A. This Court Rejected The Rationale Of The Decision Below In *Morgan Stanley*

The court of appeals' holding that *Mobile-Sierra* does not apply to challenges by non-parties rests on the premise that the *Mobile-Sierra* doctrine is inconsistent with the "just and reasonable" standard found in FPA §206. The court of appeals rejected application of *Mobile-Sierra* to non-party challenges because it would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." Pet. App. 19a. "[T]he relevant statutory language," the court held, "is quite clear" in that it requires "just and reasonable" review. *Id.* at 23a-24a. The court of appeals found that *Mobile-Sierra* "carve[d] out an exception" to the statutory "just and reasonable" standard based on contract principles. *Id.* at 20a. The court of appeals therefore ruled that *Mobile-Sierra*'s public-interest test is an "illegal standard" that "deprives non-settling parties of their statutory right" to have future "rate challenges adjudicated under the" statutory "'just and reasonable standard' * * * in cases of changed circumstances." *Id.* at 22a-23a.

That holding cannot be reconciled with this Court's subsequent decision in *Morgan Stanley*. That decision flatly rejected the view that *Mobile-Sierra* departs from the statutory "just and reasonable" standard. Rather, this Court held that there "is only one statutory standard for assessing wholesale electricity rates, whether set by contract or tariff—the just-and-reasonable standard." 128 S. Ct. at 2745. The *Mobile-Sierra* test, this Court held, merely represents the "mode of review" employed in the context of negotiated contract rates:

> Over the years, the Commission began to refer to the two modes of review—one with the *Mobile-Sierra* presumption and the other without—as the "public interest standard" and the "just and reasonable standard." Decisions from the Courts of Appeals did likewise. We do not take this nomenclature to stand for the obviously indefensible proposition that a standard different from the statutory just-and-reasonable standard applies to contract rates. Rather, the term "public interest standard" refers to the differing *application* of that just-and-reasonable standard to contract rates.

128 S. Ct. at 2740 (citations omitted). "*Sierra* thus provided a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context * * * ." *Id.* at 2746.

The decision below thus adopted the very position this Court rejected in *Morgan Stanley*. Indeed, it adopted the position of the *Morgan Stanley* dissent, which characterized *Mobile-Sierra*'s presumption of reasonableness as a judicial invention based on an "atextual reading of [FPA] §§ 205 and 206." 128 S. Ct. at 2754 (Stevens, J., dissenting). But the majority rejected that view, finding that "the dissent's interpretation, whatever plausibility it has as an original matter, cannot be squared with *Sierra*, which plainly distinguished between unilaterally and bi-

laterally set rates, and said that the only relevant consideration for the Commission in the latter case is whether the public interest is harmed." *Id.* at 2749 n.6.

The decision below also commits precisely the same error the Ninth Circuit committed in *Morgan Stanley*: treating *Mobile-Sierra* as "the equivalent of an estoppel doctrine" that applies to contract counterparties (who voluntarily assume an obligation) but to no one else. See *Morgan Stanley*, 128 S. Ct. at 2746. As *Morgan Stanley* makes clear, *Mobile-Sierra* is not an estoppel doctrine. Instead, it is a construction of the FPA that rests on two insights. First, "[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them." 128 S. Ct. at 2746 (quotation marks omitted). As a result, FERC must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737. There is no reason that presumption would disappear based on the identity of the challenging party. Second, contract stability and predictability are critical to the health of the market. *Id.* at 2749. There is no reason why instability caused by non-party challenges should be more acceptable than instability caused by party challenges. The square conflict between this case and *Morgan Stanley* is itself grounds for further review. At the very least, the Court should grant the petition, vacate the decision below, and remand the case to give the court of appeals an opportunity to reconsider the matter on a fresh slate in light of this Court's intervening decision in *Morgan Stanley*.

B. The Decision Below Conflicts With Decades Of Settled Practice On An Important Issue

For generations, interpretation of the *Mobile-Sierra* doctrine was "so uniform" and "settled" that this Court

had no reason to intervene until it became necessary to overturn the Ninth Circuit's "erroneous decision" in *Morgan Stanley* last Term. 128 S. Ct. at 2749 n.6. Over the past 8 years, FERC has relied on *Mobile-Sierra* more than 600 times; and the federal courts have invoked it in scores of decisions. *Morgan Stanley*, 128 S. Ct. at 2749 n.6. Yet we know of no court that has ever before held that the doctrine was inapplicable to third-party challenges. To the contrary, it has long been understood that *Mobile-Sierra* protects contract rates from all challenges—whether by parties or non-parties, including FERC acting *sua sponte*.

Thus, in *Northeastern Utilities Service Co.* v. *FERC*, 993 F.2d 937, 961-962 (1st Cir. 1993), and *Boston Edison Co.* v. *FERC*, 233 F.3d 60, 68 (1st Cir. 2000), the First Circuit held that when FERC—which is not a contracting party—seeks to challenge a contract rate as unjust or unreasonable, FERC too must overcome the *Mobile-Sierra* presumption. It is simply impossible to reconcile the requirement that FERC overcome the *Mobile-Sierra* presumption with the putative rule that *Mobile-Sierra* applies only to party challenges. Nor does it make any sense that FERC, the federal regulator charged with protecting the public interest in this area, would have to show serious harm to the public interest under *Mobile-Sierra* to overturn a contract rate, but a State Attorney General or a ratepayer, with no expertise or congressional mandate, would not. The fact is that the *Mobile-Sierra* standard has, until now, applied to all challenges to contract rates, regardless of who brings them.

Courts have routinely applied *Mobile-Sierra* to non-party challenges in the context of "undue discrimination" claims as well. For example, in *Boroughs of Chambersburg* v. *FERC*, 580 F.2d 573, 577-78 (D.C. Cir. 1978), a wholesale supplier filed rate increases that had different

impacts on customers depending on whether their contracts were subject to *Mobile-Sierra* protection. The disadvantaged customer (who lacked *Mobile-Sierra* protection) sought to invalidate the favored customer's contract, urging that the differential treatment was unduly discriminatory. The court of appeals rejected that claim, finding no undue discrimination because the utility was free to raise the non-settling parties' rates, but the settling parties' rate contracts were protected under *Mobile-Sierra. Chambersburg*, 580 F.2d at 577-78. In *Public Service Co. of Indiana, Inc.* v. *FERC*, 575 F.2d 1204, 1211-13 & n.12 (7th Cir. 1978), the Seventh Circuit similarly rejected a non-party's effort to challenge another customer's contract as discriminatory in light of *Mobile-Sierra*. Later that year, the D.C. Circuit in turn relied on *Chambersburg* and the Seventh Circuit's decision in *PSCI* to reach the same conclusion in *Town of Norwood* v. *FERC*, 587 F.2d 1306, 1310-14 (D.C. Cir. 1978). "[I]t is possible to have discrimination that violates §205(b)," the court ruled, "but does not dismantle the protection generally afforded to fixed-rate contracts under *Mobile-Sierra*" in challenges brought by third parties under FPA §206(a). 587 F.2d at 1314 n.21.

Just last year, the D.C. Circuit rejected an effort by non-contracting third parties to challenge FERC's more favorable treatment of certain grandfathered agreements under a new tariff regime, and rebuffed their claim that such agreements discriminated against them and shifted costs to non-contracting parties in violation of FPA §205. *Wis. Pub. Power Inc.* v. *FERC*, 493 F.3d 239, 270, 274 (D.C. Cir. 2007). The court held that the challengers had failed to show that modification of the grandfathered agreements was required by the "public interest" or that the alleged cost shifts imposed an "excessive burden" under the *Mobile-Sierra* doctrine. See *id.* at 273-75 (relying on *Norwood,* 587 F.2d at 1314 n.21). The federal courts thus have repeatedly invoked *Mobile-Sierra* to

reject the efforts of non-parties to invalidate (as discriminatory or unjust) the contracts of others. Those cases would make no sense if "the *Mobile-Sierra* doctrine simply does not apply" to challenges "brought by a non-contracting third party." Pet. App. 22a.

C. The Court Of Appeals' Decision Conflicts With Other Applicable Decisions And Principles

For the reasons given above, the court of appeals' reasoning cannot be reconciled with this Court's decision in *Morgan Stanley* or with *Mobile-Sierra*'s origins or purposes. See pp. 16-20, *supra*. Nowhere did the court of appeals explain why the presumption of reasonableness that arises from a negotiated contract, or the need for contract stability to encourage investment, would evaporate based on the identity of the challenging party. *Ibid.* But the court of appeals' decision is difficult to reconcile with this Court's precedents and general legal principles in other respects as well.

1. As an initial matter, the court of appeals' conclusion that *Mobile-Sierra* does not apply to non-contracting parties is difficult to reconcile with the test that *Mobile* and *Sierra* establish. The public-interest test under *Mobile-Sierra* is by its terms targeted to protecting non-contracting parties. *Sierra* listed three examples of where a contract might be contrary to the public interest: "where [the contract] might impair the financial ability of the public utility to continue its service, *cast upon other consumers an excessive burden, or be unduly discriminatory.*" 350 U.S. at 354-55 (emphasis added). The last two factors expressly consider the impact on non-contracting third parties. *Morgan Stanley* similarly focuses the public interest presumption on preventing "serious[] harm[]" to "the public," 128 S. Ct. at 2737—by definition an aggregate group of non-contracting third parties. It thus cannot be correct that "the *Mobile-Sierra* doctrine simply does not apply" to non-contracting third parties. Pet. App. 22a. It always has. Indeed, the

Mobile-Sierra standard is predicated on the protection of non-parties' interests.

2. Second, in *Morgan Stanley*, this Court made clear that *Mobile-Sierra*, far from being a limit on contracting parties' efforts to escape their obligations, is a limit on *FERC's authority* to abrogate or modify contract rates. Every mention of the *Mobile-Sierra* presumption in *Morgan Stanley* is formulated as a limit on *FERC's* authority. See, *e.g.*, 128 S. Ct. at 2737 ("Under the *Mobile-Sierra* doctrine, [FERC] must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law."); *id.* at 2745 ("[W]e conclude that the *Commission* was required, under our decision in *Sierra*, to apply the *Mobile-Sierra* presumption in its evaluation of the contracts here.").

Mobile-Sierra thus does nothing to prevent interested persons from filing a complaint at FERC contending that a rate is unjust and unreasonable. But where a rate is set by contract, FERC must presume the contract rate is reasonable, absent "extraordinary circumstances" or "unequivocal public necessity," because "the FPA intended to reserve the Commission's contract-abrogation power for those extraordinary circumstances where the public will be severely harmed." 128 S. Ct. at 2749. Likewise, the *Mobile-Sierra* clause in the agreement at issue here does not interfere with any statutory rights. No one is prevented from urging that a rate is unjust and unreasonable within the meaning of FPA § 206 if at some future date the transition rates or the auction results seem unreasonable. The agreement simply makes clear that, in deciding whether the rate is just and reasonable, FERC must apply the *Mobile-Sierra* presumption that the rate is reasonable unless that presumption is overcome by compelling proof of severe harm to the public

interest. FERC has approved contracts with such clauses for years.[10]

3. Without addressing any of the foregoing, the court of appeals held that "the *Mobile-Sierra* doctrine simply does not apply" to non-party challenges based on its assertion that "a contract cannot bind a nonparty." Pet. App. 22a (quoting *Waffle House,* 534 U.S. at 294). But the premise that *Mobile-Sierra* derives from, and is bounded in scope by, contract law is incorrect. *Mobile-Sierra* comes from the FPA, and its application to FERC-jurisdictional agreements must be determined by that statute. See pp. 23-26, *supra.* To the extent contract principles are relevant, however, they undercut the D.C. Circuit's view.

As an initial matter, *Waffle House* held that an arbitration agreement between an employer and an employee could not prevent the EEOC from *bringing a complaint* against the employer in its own name. 534 U.S. at 295-96 (finding the agreement did not effect "a waiver of a nonparty's statutory remedies"). But *Waffle House* left "open" whether "a settlement or arbitration judgment would affect the validity of the EEOC's claim or the character of relief the EEOC may seek." *Id.* at 297. That distinction is key. This Court has long held that an agreement will not be read to "bind" third parties merely because it will affect them negatively (even profoundly so). *See Local No. 93, Int'l Ass'n of Firefighters* v. *City of Cleveland,* 478 U.S. 501, 529-30 (1986). Thus, while the application of the public-interest presumption necessarily *affects* any attempt by a non-contracting third party to

---

[10] FERC and FPC cases reviewing *Mobile-Sierra* provisions in contracts and settlement agreements are too numerous to list. See, *e.g.*, Pet. App. 200a & n.150 (listing recent examples). This year alone, FERC has already issued more than 50 decisions accepting, rejecting, or modifying such provisions in contracts and settlement agreements. This process has, of course, become more difficult since the decision below issued. See note 8, *supra.*

modify or abrogate a contract, the contract itself does not bind them. Instead, under *Mobile-Sierra* and *Morgan Stanley*, the contract produces a presumption that binds *FERC* in its analysis of whether the rate is just and reasonable.

In any event, the court of appeals' analysis is upside-down even as a matter of contract law. While non-parties are not bound by a contract, they also ordinarily lack standing to challenge contract terms—even if those terms somehow affect them. *In re Vic Supply Co.*, 227 F.3d 928, 931 (7th Cir. 2000) ("Obviously the fact that a third party would be better off if a contract were unenforceable does not give him standing to sue to void the contract."). Here, the contract provision establishing the standard of review may *affect* later challenges by the non-settling parties, but it "does not bind [them] to do or not to do anything," "imposes no legal duties or obligations on [them] at all," and "does not purport to resolve any claims the[y] might have." *Firefighters*, 478 U.S. at 529-30. Yet the court of appeals afforded non-parties to the contract at issue a right to challenge contract terms in light of changed circumstances that is more expansive than the right enjoyed by the contracting parties themselves. That result is at odds with common law and common sense.

CONCLUSION

The petition for a writ of certiorari should be granted. At the very least, the Court should grant the petition, vacate the decision below in relevant part (Part IV), and remand for reconsideration in light of this Court's intervening decision in *Morgan Stanley*.

Respectfully submitted.

JOHN N. ESTES III
Counsel of Record
JOHN LEE SHEPHERD, JR.
SKADDEN, ARPS, SLATE
MEAGHER & FLOM LLP
1440 New York Ave., NW
Washington, D.C. 20005
202-371-7338

JEFFREY A. LAMKEN
MICHAEL G. PATTILLO, JR.
ADAM J. WHITE
BAKER BOTTS LLP
1299 Pennsylvania Ave., NW
Washington, D.C. 20004
202-639-7700

Counsel for Petitioners

November 21, 2008