[Maine Law Review](https://digitalcommons.mainelaw.maine.edu/mlr)

Volume 65 | Number 1 Article 6

January 2012

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I. INTRODUCTION

Many industries are subject to regulation, whether by the federal government, the state, or both. Electric utility companies' retail rates are subject to regulation by the states, and their wholesale rates charged among enterprises involved in providing the electric power to retail sellers are regulated by the federal government.[1] Under the Federal Power Act of 1935 ("FPA"), the Federal Energy Regulatory Commission ("FERC") is responsible for ensuring that rates for wholesale electric power sales and electric transmission are "just and reasonable."[2]

The "classic scheme" of administrative rate setting called for rates to be established unilaterally by the regulated companies and set forth in rate schedules of general applicability (i.e., "tariffs"), subject to oversight by the relevant administrative agency.[3] However, the federal government has regulated rates for goods and services transferred *between businesses* differently from the way rates *between businesses and the public* are regulated.[4] The Supreme Court has noted that "[i]n wholesale markets, the party charging the rate and the party charged were 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."[5] With the FPA, Congress departed from a strict scheme of tariff-only rate regulation,[6] permitting wholesale arrangements between the parties to be established through individually-negotiated contracts, subject to FERC oversight.[7]

Over the years, the number of FERC-regulated transactions has grown, and FERC and electric utilities have developed new contractual vehicles under which to transact. Among other innovations, FERC has established organized markets, instituted a market-based rate program, and ordered electric industry restructuring (i.e., unbundling of power and transmission transactions). In addition, FERC has required electric utilities offering transmission service to do so pursuant to a standardized tariff of general applicability, with rates established under the "classic scheme" of administrative rate setting mentioned above.[8]

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* J.D., Cornell Law School. Thanks to all those who provided comments on the ideas expressed in this article, and to the Maine Law Review and its editors for their work in the production of this article. All remaining errors are my own.

1. See Verizon Commc'ns Inc. v. FCC, 535 U.S. 467, 478 (2002).
2. 16 U.S.C.A. §§ 824d(a), 824e(a) (2010 & Supp. 2012).
3. *See Verizon*, 535 U.S. at 478.
4. *See id.* at 479.
5. *Id.*
6. *See id.*
7. *See id.*; United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 338-39 (1956).
8. *See* New York v. Fed. Energy Regulatory Comm'n, 535 U.S. 1, 10 (2002) (noting that FERC had proposed and adopted the requirement "that public utilities owning and/or controlling facilities used

Another byproduct of the increase in FERC-regulated transactions is the greater reliance by FERC on the settlement process to resolve disputes involving jurisdictional rates. One observer has stated that, "[a]mong regulatory bodies, settlement is most pervasive at FERC," and "negotiated settlement has become the standard process for setting interstate gas and electricity rates."[9] In recent years, "approximately 80[%] of the contested proceedings set for hearing at [FERC] are settled"[10] and approximately 90 percent of FERC cases set for hearing achieved a partial or complete consensual agreement.[11]

Within this regulatory scheme, the Supreme Court in 1956 established the *Mobile-Sierra* doctrine,[12] which provides that when a challenge is brought to a rate that is set forth in a wholesale electric energy contract that is the result of negotiation and bargaining under FERC's jurisdiction, FERC must presume that the rate satisfies the FPA's requirement that all such rates must be "just and reasonable."[13] The presumption applies equally regardless of whether the challenge is brought by the buyer or the seller[14] or by a third-party,[15] and may be overcome only if FERC determines that the rate seriously harms the public interest.[16] Courts have observed that the public interest presumption is "practically insurmountable" and that attempts to change rates when the presumption applies hold only a "dim prospect, hardly worthy of recognition."[17] If the presumption does not apply, FERC would examine the challenged rate under cost-of-service or other rate principles to determine whether the rate is just and reasonable.

Decided in 2010, *NRG Power Marketing, LLC v. Maine Public Utilities Commission* ("*NRG*")[18] is the latest Supreme Court case to address the *Mobile-Sierra* doctrine. The case in *NRG* arose when utilities in New England proposed to FERC the establishment of a regional capacity market in an attempt to alleviate shortages in electric power supply in the region.[19] The FERC proceeding was the

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for the transmission of electric energy in interstate commerce have on file tariffs providing for nondiscriminatory open-access transmission services" (internal quotations omitted)).

9. Stephen Littlechild, *The Process of Negotiating Settlements at FERC*, U. CAMBRIDGE ELECTRICITY POL'Y RES. GROUP 2 (Jan. 2011, revised May 2011), http://www.econ.cam.ac.uk/dae/repec/cam/pdf/cwpe1116.pdf.

10. FEDERAL ENERGY REGULATORY COMMISSION, CONGRESSIONAL PERFORMANCE BUDGET REQUEST FISCAL YEAR 2011, at 18 (2010), *available at* http://www.ferc.gov/about/strat-docs/FY11-budg.pdf.

11. *Id.* at 88. The percentage of cases set for hearing that achieved a partial or complete consensual agreement were 91 percent for fiscal year 2008 and 90 percent for fiscal year 2009. *Id.* It was 88 percent for fiscal year 2007. *Id.*

12. *See Mobile*, 350 U.S. 332; Fed. Power Comm'n v. Sierra Pac. Power Co., 350 U.S. 348 (1956).

13. *See* 16 U.S.C.A. §§ 824d-824e (2010 & Supp. 2012).

14. *See* Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527 (2008).

15. NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, 130 S. Ct. 693 (2010).

16. *Mobile*, 350 U.S. 332; *Sierra*, 350 U.S. 348.

17. Papago Tribal Util. Auth. v. Fed. Energy Regulatory Comm'n, 723 F.2d 950, 954 (D.C. Cir. 1983).

18. 558 U.S. 165, 130 S. Ct. 693 (2010).

19. "Capacity" is different from actual electric power. For purposes here, the D.C. Circuit has explained that when a retail electric utility purchases capacity—as opposed to electric power—from an electric generator, the utility "compensates the generator for the *option* of buying a specific quantity of power irrespective of whether it ultimately buys the electricity." Me. Pub. Utils. Comm'n v. Fed.

subject of much debate; but, ultimately, a settlement was achieved among 107 of the 115 participants to the proceeding. The Settlement Agreement established a Forward Capacity Market ("FCM") under which there would be annual price-setting auctions for capacity. On certiorari, the Supreme Court found that FERC had failed to determine whether the rates produced by the FCM's auction mechanism were freely negotiated rates to which the *Mobile-Sierra* public interest presumption would apply in future challenges to those rates, or were unilaterally-established rates to which the public interest presumption would not apply. On remand, FERC determined that the FCM auction rates were not freely negotiated rates, but that it nonetheless possessed the discretion to determine in advance that it would presume the auction rates were just and reasonable in future rate challenges. A petition for review of FERC's orders on remand is pending at the D.C. Circuit.

This article argues that FERC's determination on remand was incorrect. FERC failed to recognize that settlements are the result of negotiation and bargaining. As such, rates established through a settlement agreement are imbued with the characteristics that the Supreme Court previously has determined trigger the application of the *Mobile-Sierra* public interest presumption. In this case, the Settlement Agreement does not contain a numerical rate for capacity prices, but it provides the mechanism through which the rate will be derived—the FCM auction. Because the 107 parties to the Settlement Agreement consented to the use of the FCM auction to produce the capacity prices, the rates paid by those parties should be presumed to be just and reasonable if challenged in the future. If the rates paid by any of the eight non-settling participants are challenged, the presumption would not apply. The effects of FERC's decision are potentially far-reaching because of the number of rate disputes that are resolved through settlement.

Part II of this article reviews the regulatory scheme under the FPA and the development of the *Mobile-Sierra* doctrine, up to the Supreme Court's 2008 case, *Morgan Stanley Capital Group, Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.* The Supreme Court's latest *Mobile-Sierra* doctrine case, *NRG*, is summarized in Part III, including the underlying proceedings at FERC in *Devon Power*, review by the D.C. Circuit and the Supreme Court, and FERC's orders on remand.

In Part IV, the article evaluates how FERC resolved the questions remanded by the Supreme Court and the D.C. Circuit. Part IV first summarizes the characteristics of rates to which the *Mobile-Sierra* public interest presumption must apply—namely, that the rates are the result of negotiations and bargaining among the parties to the agreement. This should include rates set forth in a tariff where the rates were established through a settlement, because settlements are the result of negotiations and bargaining as well. Part IV explains that because the FCM auction mechanism is the result of a settlement among most of the participants to the FERC proceeding in *Devon Power*, the *Mobile-Sierra* public interest presumption should automatically apply to challenges to the rates paid by the settling parties.

Finally, Part V describes the practical consequences that will arise from

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Energy Regulatory Comm'n, 520 F.3d 464, 467 (D.C. Cir. 2008) [hereinafter *Maine PUC I*] (quoting Keyspan-Ravenswood, LLC v. Fed. Energy Regulatory Comm'n, 474 F.3d 804, 806 (D.C. Cir. 2007)); *NRG*, 558 U.S. at ___,130 S. Ct. at 697.

FERC's determinations in *Devon Power*. Because FERC has failed to recognize that the *Mobile-Sierra* public interest presumption must apply to rates set forth in settlement agreements, those rates may be easily challenged. The effects may be far-reaching, particularly where such a large number of FERC rate proceedings are resolved through settlement.

II. RATE REGULATION UNDER THE FEDERAL POWER ACT AND THE *MOBILE-SIERRA* DOCTRINE

A. The Federal Power Act

Part II of the FPA[20] vests FERC[21] with jurisdiction over the electric utility industry, including over the transmission of electric energy in interstate commerce, the sale of electric energy at wholesale in interstate commerce, and facilities for such sales or transmission.[22] "[A]ny person who owns or operates facilities subject to the jurisdiction of [FERC] under [Part II of the FPA]" is a "public utility."[23]

Sections 205 and 206 of the FPA,[24] which provide for the regulation by FERC of rates for the sale and transmission of electric power, are the "bread and butter" of the FPA.[25] Sections 205 and 206 of the FPA are substantially identical to sections 4 and 5 of the Natural Gas Act ("NGA"),[26] and decisions construing the analogous provisions of the two statutes are interchangeable.[27] The fundamental command of these sections is that all rates charged must be "just and reasonable."[28] This standard is modeled on the Interstate Commerce Act ("ICA"),[29] which has required that charges for services rendered by common carriers be "just and

20. 16 U.S.C.A. §§ 824-824w (2010 & Supp. 2012). The Federal Power Act of 1935, Pub. L. No. 74-333, 49 Stat. 847, amended the Federal Water Power Act of 1920, Pub. L. No. 66-280, 41 Stat. 1063, by, among other things, adding Parts II and III. The amended statute was renamed the Federal Power Act.

21. Prior to October 1, 1977, jurisdiction under the FPA lay in the Federal Power Commission ("FPC"). However, on October 1, 1977, pursuant to the Department of Energy Organization Act, Pub. L. No. 95-91, 91 Stat. 565 (1977), and Executive Order No. 12009, 42 Fed. Reg. 46,267 (September 13, 1977), the FPC ceased to exist and its regulatory functions were transferred to FERC, an independent agency within the Department of Energy that was activated on October 1, 1977. In this article, "FERC" generally will be used to describe both agencies.

22. 16 U.S.C.A. § 824(b)(1) (2010). FERC's jurisdiction is limited, not general.

23. *Id.* § 824(e).

24. *Id.* §§ 824d-824e.

25. *See* JAMES H. MCGREW, FEDERAL ENERGY REGULATORY COMMISSION 21 (2d ed. 2009).

26. *See* 15 U.S.C. §§ 717c, 717d (2006); Fed. Power Comm'n v. Sierra Pac. Power Co., 350 U.S. 348, 350 (1956).

27. Ark.-La. Gas Co. v. Hall, 453 U.S. 571, 577 n.7 (1981) (citing *Sierra*, 350 U.S. at 350; Permian Basin Area Rate Cases, 390 U.S. 747, 820-21 (1968)). While *NRG*, *Devon Power*, and this article are primarily focused on the regulation of contracts for electric power and capacity under the FPA, cases interpreting the NGA are equally applicable to the arguments set forth herein. Likewise, the arguments set forth in this article are equally applicable to analogous contractual arrangements subject to regulation under the NGA.

28. 16 U.S.C.A. §§ 824d(a), 824e(a) (2010 & Supp. 2012); 15 U.S.C.A. §§ 717c(a), 717d(a) (2009 & Supp. 2012).

29. Ch. 104, 24 Stat. 379 (1887); *see* Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 531 (2008); Verizon Commc'ns Inc. v. FCC, 535 U.S. 467, 479 (2002); Mobil Oil Corp. v. Fed. Power Comm'n, 417 U.S. 283, 301 & n.22 (1974).

reasonable" and has prohibited "every unjust and unreasonable charge" for such services.[30]

Public utilities generally have been subject to rate regulation due to their position as natural monopolies.[31] The paradigm that developed included regulation over both retail rates charged directly to the public and wholesale rates charged among enterprises involved in providing the goods or services offered by the retail seller.[32] Retail rates were generally regulated by the states or municipal governments, and the regulation of wholesale rates was taken up by the federal government, since the transmission or transportation involved was generally deemed to be interstate in nature.[33]

The "classic scheme" of administrative rate setting called for rates to be set forth by the regulated utility company in rate schedules of general applicability (i.e., "tariffs"), based on the model applied to railroad carriers under the ICA.[34] This system was adopted by the federal government because the innumerable "retail transactions of railroads made the policing of individual transactions administratively impossible; effective regulation could be accomplished only by requiring compliance with a single schedule of rates applicable to all shippers."[35]

However, the federal government has regulated rates for goods and services transferred between businesses differently from the way states and municipalities have regulated rates between businesses and the public.[36] The Supreme Court has noted that "[i]n wholesale markets, the party charging the rate and the party charged were often sophisticated business enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them."[37] With the FPA and the NGA, Congress departed from a strict scheme of tariff-only rate regulation.[38] Under the FPA and NGA, Congress permitted wholesale arrangements between the parties to be established initially

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30. *See* 49 U.S.C. app. § 1(5)(a) (1988). Congress passed the Interstate Commerce Act ("ICA") in 1887 to regulate railroads. In 1906, the Hepburn Act applied the ICA to oil pipelines as well. Pub. L. No. 59-337, § 1, 34 Stat. 584, 584 (1906). Jurisdiction over oil pipelines was transferred from the Interstate Commerce Commission to FERC in 1977 by the Department of Energy Organization Act. Pub. L. No. 95-91, § 402(b), 91 Stat. 565, 584 (1977). The following year, Congress provided that oil pipelines were to be regulated under the version of the ICA that prevailed on October 1, 1977. Act of Oct. 17, 1978, Pub. L. 95-473, § 4(c), 92 Stat. 1337, 1470. The provision cited in this footnote refers to the 1977 version, which can be found in 49 U.S.C. § 1 *et seq.* (1976), and as an appendix to the 1988 edition of Title 49 of the United States Code, cited as 49 U.S.C. app. § 1 *et seq.* (1988). A brief background to the regulatory framework for oil pipelines is set forth, *inter alia*, in *Frontier Pipeline Co. and Express Pipeline LLC v. Fed. Energy Regulatory Comm'n*, 452 F.3d 774 (D.C. Cir. 2006).

31. *See* JAMES C. BONBRIGHT ET AL., PRINCIPLES OF PUBLIC UTILITY RATES 17-25 (1988).

32. *See Verizon*, 535 U.S. at 478.

33. *See id.* at 477 (citing CHARLES F. PHILLIPS, REGULATION OF PUBLIC UTILITIES 111-12 & n.5 (1984)).

34. *See id.* at 478.

35. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 338-39 (1956) (comparing regulation of industries under the ICA to regulation under the NGA).

36. *See Verizon*, 535 U.S. at 479.

37. *Id.*

38. *See id. But cf.* Mobil Oil Corp. v. Fed. Power Comm'n, 417 U.S. 283, 301 (1974) ("The [NGA] was patterned after earlier regulatory statutes that applied to traditional public utilities and transportation companies and that provided for setting rates equal to such companies' costs of service plus a reasonable rate of return.").

through individually-negotiated contracts.[39] Protection of the public interest would be achieved through supervision by FERC of the individual contracts.[40]

To that end, the FPA requires public utilities to file their individual contracts with FERC and grants to FERC the power to review rates subject to its jurisdiction that have been set initially by public utilities.[41] The relevant subsections here are FPA sections 205(c), 205(d), 205(e), and 206(a). Section 205(c) requires public utilities to file all rates and contracts with FERC.[42] Under section 205(d), changes in previously-filed rates or contracts generally must be filed with FERC at least sixty days before they go into effect.[43] However, FERC may under section 205(e) suspend the operation of a new rate for up to five months, pending a determination of the new rate's reasonableness.[44] If FERC has not reached a decision before the suspension period has expired, the filed rate shall go into effect, subject to a refund or adjustment to be made retroactive to that date.[45] Section 206(a) authorizes FERC to modify any rate or contract which it determines to be "unjust, unreasonable, unduly discriminatory or preferential."[46]

In 1956, in *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.* ("*Mobile*"), the Supreme Court explained that sections 205 and 206 are part of a "statutory scheme under which all rates are established initially by the [public utilities], by contract or otherwise, and all rates are subject to being modified by [FERC] upon a finding that they are unlawful."[47] However, FPA section 205 "purports neither to grant nor to define the initial rate-setting powers of [public utilities]."[48] Instead, the FPA (1) defines FERC's review powers, and (2) imposes duties on public utilities as are necessary for FERC to effectuate its powers.[49]

FERC's powers are defined by sections 205(e) and 206(a). Under section 206(a), FERC may set aside and modify any rate or contract which it determines to be "unjust, unreasonable, unduly discriminatory, or preferential."[50] The Court in *Mobile* stated that this was "neither a 'rate-making' nor a 'rate-changing' procedure. It is simply the power to review rates and contracts made in the first instance by [public utilities] and, if they are determined to be unlawful, to remedy them."[51] Section 205(e) only adds to this basic power the "further powers (1) to

39. *See Mobile*, 350 U.S. at 338-39; *Verizon*, 535 U.S. at 479. When compared to the ICA, relatively few wholesale transactions were regulated under the NGA, and they typically required substantial investments in capacity and facilities for the service of a particular gas distributor. *Mobile*, 350 U.S. at 339. Such circumstances demanded individual arrangements between jurisdictional natural gas companies and their customers, natural gas distributors. *Id.*

40. *Mobile*, 350 U.S. at 339.

41. *See id.* at 339, 343 (construing the analogous provisions of the NGA).

42. 16 U.S.C.A. § 824d(c) (2010 & Supp. 2012).

43. *Id.* at § 824d(d). FERC may, for good cause shown, allow changes to take effect without requiring the sixty days' notice. *Id.*

44. *Id.* at § 824d(e). FERC may convene a hearing concerning the reasonableness of a new rate upon complaint or on its own initiative. *Id.*

45. *Id.*

46. *Id.* at § 824e(a).

47. 350 U.S. 332, 341 (1956) (construing section 4(d) of the NGA).

48. *Id.*

49. *Id.* at 341-42.

50. *Id.* at 341.

51. *Id.*

preserve the status quo pending review of [a] new rate by suspending its operation for a limited period, and (2) thereafter to make its order retroactive, by means of the refund procedure, to the date the change became effective."[52]

The limitations on public utilities are set forth in section 205(c) and 205(d). Section 205(c) requires rate schedules and contracts in force to be filed with the Commission.[53] Section 205(d) requires all changes in such schedules and contracts to be filed with FERC at least sixty days before they go into effect.[54] The *Mobile* Court explained that section 205(d) was a prohibition, *not* a grant of power.[55] Otherwise valid changes to a contract *cannot* be put into effect without giving the required notice to FERC.[56] However, the FPA does not say under what circumstances a public utility can make such a change.[57]

In *Mobile*, the Court concluded that FPA sections 205 and 206 do not establish a rate-changing procedure or constitute a mechanism for initiating rate "proceedings."[58] Section 205 does not provide for the filing of rate "proposals"; it provides only for *notice* to FERC of the rates established by the public utility and for *review* by FERC of those rates.[59] If a public utility has the power to make a change to a rate schedule or contract, then the change is effectuated upon compliance with section 205(d)'s notice requirement.[60]

B. The Mobile-Sierra *Doctrine*

1. Mobile*,* Sierra*, and* Memphis

In twin cases decided on February 27, 1956, *Mobile*[61] (discussed above) and *Federal Power Commission v. Sierra Pacific Power Co.* ("*Sierra*"),[62] the Supreme Court addressed the authority of FERC to modify rates that had been negotiated bilaterally and set forth in contracts. In *Mobile*, the Court rejected a natural gas pipeline's argument that NGA section 4's requirement that all new rates must be filed with FERC authorized such pipelines to unilaterally change existing contracts.[63] As explained above, the NGA did not grant extra-contractual power to jurisdictional pipelines.[64] If a contract does not grant either party the unilateral right to make changes to the contract, no such right exists.[65]

52. *Id.*
53. 16 U.S.C.A. § 824d(c) (2010 & Supp. 2012).
54. *Id.* at § 824d(d).
55. *Mobile*, 350 U.S. at 339.
56. *Id.* at 339-40, 341-42.
57. *See id.*
58. *Id.* at 342.
59. *Id.* at 342-43.
60. *See id.* at 342.
61. *Id.* at 332.
62. 350 U.S. 348 (1956).
63. *Mobile*, 350 U.S. at 337-38.
64. *See id* at 339-40.
65. *See id.* at 339-42 (noting that under section 4 of the NGA, otherwise valid changes cannot be put into effect without giving the required notice to FERC). As the D.C. Circuit has explained, "[t]he contract between the parties governs the legality of the filing. Rate filings consistent with contractual

However, the Court in *Mobile* noted that NGA section 5 authorizes FERC to investigate rates "upon complaint," as well as on its own initiative.[66] The Court reasoned that although the jurisdictional natural gas pipelines were not enumerated among the list of entities that might file a complaint with FERC seeking the commencement of an investigation, "there is nothing to prevent them from furnishing to [FERC] any relevant information and requesting it to initiate an investigation on its own motions."[67] If FERC concludes after an investigation and hearing that the rate in a natural gas pipeline's contract is "so low as to conflict with the *public interest*, [FERC] may under [NGA] § 5(a) authorize the natural gas company to file a schedule increasing the rate."[68]

In *Sierra*, the Supreme Court applied the holding from *Mobile* to the analogous provision of the FPA—section 205.[69] The Court concluded that a public utility could not unilaterally file a new rate under FPA section 205(d) that was contrary to the terms of an effective contract.[70] However, *Sierra* involved an issue not present in *Mobile*—when FERC, under FPA section 206(a), was authorized to find that an existing contract rate was unlawful and to fix a new lawful rate.[71] The Court explained that FERC could not find that an existing contract rate was "unreasonable solely because it yields the public utility less than a fair return on net invested capital."[72] Faced with the question of how FERC must evaluate whether an existing contract rate is just and reasonable, the Court explained:

> [FERC's] conclusion appears on its face to be based on an erroneous standard . . . . [W]hile it may be that [FERC] may not normally *impose* upon a public utility a rate which would produce less than a fair return, it does not follow that the public utility may not itself agree by contract to a rate affording less than a fair return or that, if it does so, it is entitled to be relieved of its improvident bargain . . . . In such circumstances the sole concern of [FERC] would seem to be whether the rate is so low as to adversely affect the public interest—as where 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.[73]

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obligations are valid; rate filings inconsistent with contractual obligations are invalid." Richmond Power & Light Co. v. Fed. Power Comm'n, 481 F.2d 490, 493 (D.C. Cir. 1973).

66. *Mobile*, 350 U.S. at 344 (quoting 15 U.S.C. § 717d(a) (1938)). NGA section 5(a) states that a complaint may be brought by "any State, municipality, State commission, or gas distributing company." 15 U.S.C. § 717d(a) (1938). The Court described these entities as "those who represent the public interest" and "those who might be discriminated against." *Mobile*, 350 U.S. at 345. FPA section 206(a) does not enumerate or limit entities that may file a complaint. *See* 16 U.S.C. § 824e(a) (1938).

67. *Mobile*, 350 U.S. at 345.

68. *Id.* (emphasis added).

69. Fed. Power Comm'n v. Sierra Pac. Power Co., 350 U.S. 348, 352-53 (1956).

70. *Id.*

71. *Id.* at 353-55. FPA section 206(a) grants FERC the authority to prescribe a change in contract rates whenever it determines such rates to be unlawful, i.e., "unjust, unreasonable, unduly discriminatory or preferential." 16 U.S.C.A. § 824e(a) (2010 & Supp. 2012); *Sierra*, 350 U.S. at 353.

72. *Sierra*, 350 U.S. at 354-55.

73. *Id.* (emphasis added, citation omitted). The Court noted that the purpose of the power given to FERC by FPA section 206(a) is the protection of the public interest, as distinguished from the private interests of the utilities. *Id.* at 355 (citing 16 U.S.C.A. § 824e(a)). Therefore, a contract is not "unjust" or "unreasonable" simply because it is not profitable to the public utility. *Id.*

From these two cases, the eponymous "*Mobile-Sierra* doctrine" was born.[74] The doctrine acts as a presumption when such rates are investigated pursuant to FPA section 206(a).[75] As the Court has subsequently explained, 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 the FPA.[76] The presumption is only overcome if the contract seriously harms the public interest; that is, where the contract might (1) impair the financial ability of the public utility to continue its service, (2) cast upon other consumers an excessive burden, or (3) be unduly discriminatory.[77] Indeed, "[t]he regulatory system created by the [FPA] is premised on contractual agreements voluntarily devised by the regulated companies; it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity."[78] In neither case did the Court find that the public interest required the existing rates to be reformed.[79]

Both *Mobile* and *Sierra* involved attempts by sellers to change rates set forth in existing bilateral contracts negotiated by the parties, and where the contracts did not otherwise permit such changes.[80] In subsequent cases, the Supreme Court addressed whether the *Mobile-Sierra* presumption applies where rates are set forth in instruments other than individually-negotiated bilateral contracts, or contracts

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74. The Supreme Court did not use the term "*Mobile-Sierra* doctrine" until 2008. Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 551 n.6 (2008). Responding to Justice Stevens's dissent, *see id.* at 555 (Stevens, J., dissenting), the Court explained that it likely had never before used the phrase "*Mobile-Sierra* doctrine" because the understanding of the holdings in *Mobile* and *Sierra* was uniform and no circuit split arose concerning its meaning until the Ninth Circuit's erroneous decision in the cases on review, Pub. Util. Dist. No. 1 of Snohomish Cnty. v. Fed. Energy Regulatory Comm'n, 471 F.3d 1053 (9th Cir. 2006). *Id.* at 551 n.6.

75. 16 U.S.C.A. § 824e(a).

76. *Morgan Stanley*, 554 U.S. at 530.

77. *Sierra*, 350 U.S. at 355; *see Morgan Stanley*, 554 U.S. at 533.

78. *Morgan Stanley*, 554 U.S. at 534 (quoting *In re* Permian Basin Area Rate Cases, 390 U.S. 747, 822 (1968)). The *Mobile-Sierra* doctrine "recognizes the superior efficiency of private bargaining, and its purpose is 'to subordinate the statutory filing mechanism to the broad and familiar dictates of contract law.'" *Maine PUC I*, *supra* note 19, at 476 (D.C. Cir. 2008) (quoting Borough of Lansdale v. Fed. Power Comm'n, 494 F.2d 1104, 1113 (D.C. Cir. 1974)); *see also* Atlantic City Elec. Co. v. Fed. Energy Regulatory Comm'n, 295 F.3d 1, 14 (D.C. Cir. 2002) ("[T]he purpose of the *Mobile-Sierra* doctrine is to preserve the benefit of the parties' bargain as reflected in the contract, assuming that there was no reason to question what transpired at the contract formation stage.") (citation omitted). *Mobile* and *Sierra* "recognize that the FPA and the NGA provide that conventional regulation must give way to contracts that are the product of negotiation and market forces." Carmen L. Gentile, *The* Mobile-Sierra *Rule: Its Illustrious Past and Uncertain Future*, 21 ENERGY L. J. 353, 358 (2000).

79. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 347 (1956); *Sierra*, 350 U.S. at 353. Courts have observed that the public interest presumption is "practically insurmountable" and that attempts to change rates when the presumption applies hold only a "dim prospect, hardly worthy of recognition." Papago Tribal Util. Auth. v. Fed. Energy Regulatory Comm'n, 723 F.2d 950, 954 (D.C. Cir. 1983). One commenter has stated that "it could be said that it would be easier for a camel to pass through the eye of a needle than for a utility to increase a rate protected by the *Mobile-Sierra* rule." Gentile, *supra* note 78, at 356. It has been observed that it is more difficult to overcome the public interest presumption than to meet the business judgment standard used in bankruptcy cases. *See* Kendall Hollrah, Comment, *Learning to Live Together: Exploring Interactions Between Bankruptcy Law and Energy Law*, 42 HOUS. L. REV. 529 (2005).

80. *Mobile*, 350 U.S. at 336-37; *Sierra*, 350 U.S. at 351-52.

that specifically permit rate changes.

In *United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division* ("*Memphis*"), the Court held that parties could include in contracts the right to unilaterally change rates at will.[81] The Court distinguished the case from *Mobile*, noting that in *Mobile*, the natural gas pipeline had contractually bound itself to furnish gas throughout the contract term at a particular price and had "bargained away by contract the right to change its rates unilaterally."[82] However, the agreement at issue in *Memphis* did not state a single fixed rate, but included a rate provision that amounted to the pipeline's "'going' rate," reserving to the pipeline the power to make rate changes subject to the procedures and limitations of the NGA.[83] The Court found that the pipeline, when filing a new rate with FERC, simply sought to assert, in accordance with the notice procedures in the NGA, its rights expressly reserved to it by contract.[84] In a subsequent case, the Supreme Court referred to the rule from *Memphis* as permitting parties to "contract out of the *Mobile-Sierra* presumption" by including in their contracts a provision that would permit one or both parties to unilaterally establish a new rate that would supersede the existing contract rate.[85] The Supreme Court has stated that *Memphis* is consistent with the lead role of contracts in the FPA's regulatory scheme.[86] However, absent the presence of a "*Memphis* clause," the *Mobile-Sierra* presumption remains the default rule.[87]

Although the Court in *Memphis* did not, for purposes of its analysis, draw a distinction between rates set by bilateral contract and rates set forth in a tariff of general applicability, the arrangements at issue in *Memphis* involved such tariffs.[88] The Court noted that FERC had promulgated regulations requiring natural gas

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81. 358 U.S. 103, 113 (1958). *See* Jay A. Kyle, *The* Memphis *Case*, 8 AM. U. L. REV. 100 (1959), for a discussion of *Memphis*.

82. *Memphis*, 358 U.S. at 110-11 (quoted language at 111) (citing *Mobile*, 350 U.S. at 344-45).

83. *Id.* at 105, 110, 114 (quoted language at 105). The provision read:

> All gas delivered hereunder shall be paid for by Buyer under Seller's Rate Schedule (the appropriate rate schedule designation is inserted here), or any effective superseding rate schedules, on file with the Federal Power Commission. This agreement in all respects shall be subject to the applicable provisions of such rate schedules and to the General Terms and Conditions attached thereto and filed with the Federal Power Commission which are by reference made a part hereof.

Id. at 105.

84. *Id.* at 112.

85. Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 534 (2008). Such provisions have come to be known as "*Memphis* clauses." *See* MCGREW, *supra* note 25, at 201-02.

86. NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, ___, 130 S. Ct. 693, 699 n.3 (2010). *Memphis* clarified that contracts regulated under the NGA and FPA command the same respect as any other lawful contract and that the governing statutes do not contemplate the encroachment on the parties' contracts. Kyle, *supra* note 81, at 109 ("The integrity of the contract would be defeated if an outsider could place his interpretation on the pricing clause diametrically opposed to the intent and objectives of the parties to the contract.").

87. *Morgan Stanley*, 554 U.S. at 534; *see also* Texaco, Inc. v. Fed. Energy Regulatory Comm'n 148 F.3d 1091, 1096 (D.C. Cir. 1998) (citation omitted) (finding that no language is required to invoke the public interest presumption and that where there is no "contractual language 'susceptible to the construction that the rate may be altered,' . . . the *Mobile-Sierra* doctrine applies").

88. *Memphis*, 358 U.S. at 114-15.

pipeline companies to convert from using individual bilateral agreements to a "tariff-and-service-agreement" system.[89] Under the tariff-and-service-agreement system, natural gas pipelines must adopt system-wide "tariffs" that establish terms and conditions of service for their customers and rates for different classes of customers.[90] The tariff is not itself an agreement or contract between the pipeline and any customer. Customers must execute their own agreements with the pipeline. Instead of individually tailored contracts between pipelines and their customers, pipelines and customers execute "service agreements" containing references to rates set forth in the tariff's rate schedules of general applicability and incorporating the tariff's general terms and conditions.[91] In *Memphis*, the Court was satisfied that the parties to such arrangements could permissibly reserve for natural gas pipelines the right to change their rates.[92] The Court believed that it was not unlikely that customers would have agreed to be charged a "going rate" that could be changed consistent with the notice provisions under NGA section 4(d).[93]

The innovation of *Memphis* clauses and the introduction of the tariff-and-service agreement regime for natural gas pipelines resulted in fewer *Mobile-Sierra* doctrine issues for the natural gas industry.[94] However, the electric utility industry did not convert to a tariff-and-service agreement system for electric transmission service until FERC issued Order No. 888 in 1996.[95] Until then, electric utilities

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89. *Id.* at 115 n.8 (referring to FPC Order No. 144, 13 Fed. Reg. 6371 (Oct. 30, 1948), codified at 18 C.F.R. pt. 154 (1949)). 18 C.F.R. § 154.38(d)(3) (1949) reads in pertinent part:

> No Rule, regulation, exception or condition such as tax, commodity price index, wholesale price index, purchased gas cost adjustment clauses or other similar price adjustments or periodic changes shall be included in the rate schedule or any other part of the tariff which in any way purports to effect a modification or change of any rate or charge specified in the rate schedule, or the substitution therefor of any other rate or charge: *Provided, however*, a natural-gas company may state in the service agreement or in rate schedules filed pursuant to § 154.52 that it is or will be its privilege, under certain specified conditions, to propose to the Commission a modification, change or substitution of the then effective rate or charge: *Provided further*, That no such clause may effectuate a change in an effective rate or charge except in the manner provided in Section 4 of the Natural Gas Act, as amended, and the regulations in this part.

90. 18 C.F.R. § 154.38(d)(3); *see* MCGREW, *supra* note 25, at 201.

91. *Memphis*, 358 U.S. at 115 n.8; *see* MCGREW, *supra* note 25, at 201.

92. *Memphis*, 358 U.S. at 114-15. Order No. 144 states that natural gas companies' service agreements and rate schedules could include "adjustment" provisions, and that such adjustments must be accomplished by filing new rate schedules in accordance with the Part 154 regulations. Order No. 144, 13 Fed. Reg. at 6372. The Court noted that "tariff-and-service agreement" arrangements were adopted by Order No. 144, *see supra* note 89, promulgated in 1948, but that until the case giving rise to *Memphis*, no party connected to the natural gas industry seemed to have thought that natural gas pipelines were precluded from changing the rates set forth in their tariffs subject to NGA section 4(d) and 4(e) procedures. *Memphis*, 358 U.S. at 115. In *Memphis*, the controversy did not involve a conflict between the buyer and seller under the contract at issue; the buyer supported the position of the pipeline. The objection was made by an end-use customer of the buyer. *See* Kyle, *supra* note 81, at 102.

93. *Memphis*, 358 U.S. at 115 n.10.

94. *See* MCGREW, *supra* note 25, at 201. It would be unlikely for pipeline-sellers to conduct a large portion of their business under long-term contracts at fixed rates that could not be changed to reflect changing costs. *See* Kyle, *supra* note 81, at 108.

95. Promoting Wholesale Competition Through Open Access Nondiscriminatory Transmission Service by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities,

had entered into numerous bilateral and multiparty arrangements for the sale of bundled power—that is, power together with transmission.[96] Public utilities continue to enter into bilateral and multiparty arrangements for the sale of electric power and capacity. Thus, *Mobile-Sierra* issues continue to arise in the electric industry.[97]

2. Morgan Stanley

The next chapter in the story of the *Mobile-Sierra* doctrine came in the Supreme Court's 2008 case, *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County* ("*Morgan Stanley*").[98] The cases on review in *Morgan Stanley* presented the Court with two issues for review: (1) whether the *Mobile-Sierra* presumption applies only if FERC has had an initial opportunity to review a contract rate without the presumption; and (2) whether the *Mobile-Sierra* presumption imposes as high a bar to challenges by *purchasers* of wholesale electricity as it does to challenges by *sellers*.[99] The Court answered no to the first question and yes to the second.

Under FERC's market-based rate regime, a wholesale electricity seller that has demonstrated that it lacks (or has adequately mitigated) market power may enter into freely negotiated contracts with purchasers.[100] Those contracts are not filed

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Order No. 888, 61 Fed. Reg. 21,540 (May 10, 1996), *order on reh'g*, Order No. 888-A, 62 Fed. Reg. 64,688 (Mar. 14, 1997), *order on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part sub nom*. Transmission Access Policy Study Group v. Fed. Energy Regulatory Comm'n, 225 F.3d 667 (D.C. Cir. 2000), *aff'd sub nom*. New York v. Fed. Energy Regulatory Comm'n, 535 U.S. 1 (2002). *Memphis* clauses are found in electric industry contracts and tariffs as well.

96. *See* MCGREW, *supra* note 25, at 201-02.

97. For a discussion of the electric industry after restructuring, and the role of the *Mobile-Sierra* public interest presumption, see Stephen L. Teichler & Ilia Levitine, *Long-Term Power Purchase Agreements in a Restructured Electricity Industry*, 40 WAKE FOREST L. REV. 677 (2005).

98. 554 U.S. 527 (2008). As noted above, *supra* note 74, the Supreme Court did not use the term "*Mobile-Sierra* doctrine" until *Morgan Stanley*. For a discussion of *Morgan Stanley* and its effects, *see* Richard P. Bress, Michael J. Gergen & Stephanie S. Lim, *A Deal is Still a Deal:* Morgan Stanley Capital Group v. Public Utility District No. 1, 2007-2008 CATO SUP. CT. REV. 285; John E. McCaffrey, Morgan Stanley Capital Group, Inc. v. Public Utility District No. 1 *Revisits the* Mobile-Sierra *Doctrine: Some Answers, More Questions*, 30 ENERGY L. J. 53 (2009).

Dissenting in *NRG*, Justice Stevens referred to the story of the *Mobile-Sierra* doctrine as having three "chapters": *Mobile* and *Sierra* comprise the first chapter; *Morgan Stanley*, the second; and *NRG*, the third. NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, ___, 130 S. Ct. 693, 701-03 (2010) (Stevens, J., dissenting). One set of commenters has adopted Justice Stevens' characterization (though disagreeing with his evaluation of the second and third chapters), referring to FERC's order on remand in *Devon Power* as the fourth chapter. David G. Tewksbury, Stephanie S. Lim & Grace Su, *New Chapters in the* Mobile-Sierra *Story: Application of the Doctrine After* NRG Power Marketing, LLC v. Maine Public Utilities Commission, 32 ENERGY L. J. 433 (2011).

99. *Morgan Stanley*, 554 U.S. at 530-31.

100. *See id.* at 535-38. Prior to *Morgan Stanley*, there had been some discussion regarding whether the *Mobile-Sierra* public interest presumption should apply to electric power agreements entered into under FERC's market-based rate regime. *See* David G. Tewksbury & Stephanie S. Lim, *Applying the* Mobile-Sierra *Doctrine to Market-Based Rate Contracts*, 26 ENERGY L. J. 437 (2005). *Cf.* Gentile, *supra* note 78, at 387 (believing that the prospects for future litigation related to the *Mobile-Sierra* doctrine were diminished in part because electric power sales are frequently at market-based rates and under standardized short-term contracts).

with FERC before they go into effect; instead, market-based rate sellers must file quarterly reports summarizing each of the contracts into which they have entered.[101] In 2000 and 2001, prices for electricity in the western United States rose dramatically. As a result, retail utilities entered into long-term contracts with market-based rate sellers that locked in rates that were very high by historical standards.[102] After prices began to return to normal levels, many retail utility-purchasers asked FERC to modify the contracts, contending that the contracts should be reviewed without *Mobile-Sierra*'s public interest presumption that the rates are just and reasonable.[103] FERC disagreed, applied the public interest presumption to its review of the contracts, and determined that the purchasers could not overcome the presumption.[104] On appeal, the Ninth Circuit reversed, finding that because the market-based rate agreements had not been initially reviewed by FERC, the public interest presumption did not apply to the challenges.[105] In addition, the Ninth Circuit found that even if the presumption applied, the standard for overcoming the presumption is different when a purchaser challenges a high rate.[106] The Supreme Court granted certiorari.[107]

On its way to resolving the questions presented, the Court in *Morgan Stanley* reiterated and clarified several points about the *Mobile-Sierra* presumption that are relevant here. First, the Court noted, as it had in *Mobile* and *Memphis*,[108] that the FPA permits public utilities to set jurisdictional rates with electric power customers through individually-negotiated bilateral contracts as well as through tariffs of general applicability.[109] For tariffs, as opposed to individually-negotiated contracts, FERC traditionally reviewed rates under the "cost of service" method, ensuring that a public utility covers its costs plus a rate of return sufficient to attract investment.[110] Both individual contracts and tariffs of general applicability are subject to the FPA's notice and filing requirements.[111]

The Court next addressed how application of the *Mobile-Sierra* presumption fits within the FPA's requirement that jurisdictional rates be "just and reasonable." The Court noted that since 1956, FERC and the courts of appeals referred to two differing modes of review: one with the *Mobile-Sierra* presumption, i.e., the

101. *See Morgan Stanley*, 554 U.S. at 537. Sellers must also have on file with FERC a market-based rate "tariff." These tariffs do not set forth specific rate schedules, but simply state that the seller is permitted to enter into freely negotiated agreements at market-based rates. *See id.*

102. *See id.* at 538-40.

103. *See id.* at 540-42.

104. *See id.* at 542-43.

105. *See id.* at 543 (citing Pub. Util. Dist. No. 1 of Snohomish Cnty. v. Fed. Energy Regulatory Comm'n, 471 F.3d 1053, 1075-77, 1079-85 (9th Cir. 2006).

106. *See id.* at 544 (citing *Snohomish Cnty.*, 471 F.3d at 1088-90).

107. *See* Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 551 U.S. 1189 (2007).

108. *See* United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 338-39 (1956) (comparing regulation of industries under the ICA to regulation under the NGA); United Gas Pipe Line Co. v. Memphis Light Gas & Water Div., 358 U.S. 103, 109-10 (1958) (distinguishing arrangement at issue in *Memphis* from that in *Mobile*).

109. *Morgan Stanley*, 554 U.S. at 531 (comparing the FPA with the ICA, under which regulated carriers could charge rates only pursuant to filed tariffs).

110. *Id.* at 532 (citation omitted).

111. *Id.* at 531, 533 (citing 16 U.S.C. § 824d(c) (2006)).

"public interest standard"; and the other without, i.e., the "just and reasonable standard."[112] The Supreme Court explained that, notwithstanding this nomenclature, the "public interest standard" was *not* a different standard from the statutory "just and reasonable standard."[113] Instead, the Court concluded, the "public interest standard" refers to the differing *application* of the just-and-reasonable standard to freely negotiated rates.[114]

Thus, FERC's review of rates under the FPA's just and reasonable standard must begin with a threshold inquiry: whether the rate at issue is the result of bilateral (or multi-party) negotiations and bargaining. If so, FERC must apply the *Mobile-Sierra* presumption and can only make a finding that the existing rate is unjust or unreasonable—and, thereby, fix a new rate—where the existing rate seriously harms the public interest.[115] Application of the presumption is appropriate because, "[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."[116] The Court in *Morgan Stanley* explained that *Sierra* provided "a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context."[117] However, if the rate under review is *not* the result of bilateral (or multi-party) negotiations—or if the parties to the arrangement state that the *Mobile-Sierra* presumption does not apply—FERC would perform its review without applying the presumption and review the rate under cost of service (or other) principles.[118]

Establishing that the *Mobile-Sierra* presumption should be applied when rates are set through a negotiated agreement, the Court in *Morgan Stanley* answered the first question presented for review, holding that the FPA's just and reasonable standard is not applied differently depending on *when* a rate is challenged.[119] If a rate is one to which the *Mobile-Sierra* presumption should apply, the presumption applies *each* time the rate is reviewed by FERC. The FPA does not require FERC to review the rate under cost of service principles before the rate can be reviewed

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112. *Id.* at 535 (citations omitted).

113. *Id.* at 535, 545.

114. *Id.* at 535.

115. *Id.* at 545-46; Fed. Power Comm'n v. Sierra Pac. Power Co., 350 U.S. 348, 355 (1956). In *Sierra*, the Court outlined three instances where a rate might harm the public interest: (1) impair the financial ability of the public utility to continue its service, (2) cast upon other consumers an excessive burden, or (3) be unduly discriminatory. *Id.*

116. *Morgan Stanley*, 554 U.S. at 545 (quoting Verizon Commc'ns Inc. v. FCC, 535 U.S. 467, 479 (2002)).

117. *Id.* at 546.

118. *See id.* at 532. For a discussion of the cost-of-service standard of ratemaking as a basic standard of "reasonableness," *see, e.g.*, BONBRIGHT ET AL., *supra* note 31, at 108-23.

119. *Morgan Stanley*, 554 U.S. at 545; *see also* Tewksbury & Lim, *supra* note 100, at 461 (explaining that *Mobile* indicates that the statutory structure of the FPA and NGA does not support distinctions between newly proposed and already existing rates for purposes of determining whether the public interest presumption should apply); Bress, Gergen & Lim, *supra* note 98, at 301 ("In a regulatory scheme grounded on the ability of 'sophisticated businesses' to manage their own affairs and protect their own interests, there is no need for FERC to have an initial opportunity for plenary review before presuming that contract rates are just and reasonable.").

subject to the *Mobile-Sierra* presumption.[120] The Court stated that it was proper in a regulatory scheme to review rates set by negotiated contracts by evaluating whether the rates seriously harm the public interest, not whether the rates are unfair to one of the parties that voluntarily entered into the contract.[121] Thus, FERC may abrogate a valid contract only if that contract harms the public interest.[122]

Turning to the second question presented for review, FERC found that the *Mobile-Sierra* presumption applies equally regardless of whether the rate is challenged by *purchasers* of wholesale electricity rather than by *sellers* (as had been the case in *Mobile* and *Sierra*).[123] The Court noted that the three factors identified in *Sierra*—where a rate might (1) impair the financial ability of the public utility to continue its service, (2) cast upon other consumers an excessive burden, or (3) be unduly discriminatory—were not all directly applicable to a challenge brought by a purchaser,[124] and that the three factors from *Sierra* were not an exclusive list.[125] Where the challenge is brought by a purchaser, the primary concern is likely whether the rate imposes an excessive burden on *that* customer, not *other* customers (as in *Sierra*'s second prong).[126] However, the fact that the customer is the challenger does not transform the "excessive burden" prong into an inquiry as to whether the customer pays a cost above the public utility's marginal cost, in effect reverting to a form of cost-based analysis.[127] The Court concluded that the FPA intended to reserve FERC's power to abrogate negotiated contract rates only for those extraordinary circumstances where the public would be

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120. *Morgan Stanley*, 554 U.S. at 545-46.

121. *Id.* at 546-47 (citations omitted).

122. *Id.* at 548. The Court noted that FERC possesses the authority to set aside a contract if there is unfair dealing at the contract formation stage, e.g., fraud, duress, or market manipulation. *Id.* at 547, 552-55. However, the Court cautioned that that was no reason that FERC should be able to abrogate a contract on these grounds without a finding of a causal connection between the unlawful activity and the contract rate. *Id.* at 554-55. If a causal connection is established, then the *Mobile-Sierra* presumption should not apply. *Id.* at 555.

123. *Id.* at 548. The logic from *Mobile* establishes that the *Mobile-Sierra* rule is rate-neutral. *See* Gentile, *supra* note 78, at 363-65 (discussing earlier court of appeals cases that found that the *Mobile-Sierra* doctrine protects high rates as well as low rates). Moreover, FERC's market-based rate regime eliminates a policy rationale that may be used for differentiating between so-called "low-rate" and "high-rate" cases because neither the buyer nor the seller enjoys the protections of the regulatory compact. *See* Tewksbury & Lim, *supra* note 100, at 469-70. *But cf.* Northeast Utils. Serv. Co. v. Fed. Energy Regulatory Comm'n, 55 F.3d 686 (1st Cir. 1995) (suggesting that the application of the public interest presumption might be more relaxed in non-low-rate cases (such as *Mobile*) or in order to protect third parties); Northeast Utils. Serv. Co. v. Fed. Energy Regulatory Comm'n, 993 F.2d 937 (1st Cir. 1993). For a discussion of the *Northeast* cases, *see* Gentile, *supra* note 78, at 367-73 (noting, in an article published prior to *Morgan Stanley*, that the *Northeast* decisions might be the most significant *Mobile-Sierra* cases since 1956).

124. *Morgan Stanley*, 554 U.S. at 548 (citing Fed. Power Comm'n v. Sierra Pac. Power Co., 350 U.S. 348, 355 (1956)). In a market-based rate regime, under which the regulatory compact has been eliminated, the first prong from *Sierra*—i.e., impairing the financial ability of the public utility to continue its service—would not be applicable. *See* Tewksbury & Lim, *supra* note 100, at 470.

125. *Morgan Stanley*, 554 U.S. at 549.

126. *Id.* at 548-49 (citing record below).

127. *Id.* at 550-51.

severely harmed.[128]

III. *NRG POWER MARKETING, LLC V. MAINE PUBLIC UTILITIES COMMISSION*

Two terms after *Morgan Stanley*, the Supreme Court once again took up the *Mobile-Sierra* doctrine in *NRG*.[129] In *NRG*, the Supreme Court resolved that application of the *Mobile-Sierra* presumption does not depend upon the identity of the person challenging the rate at issue—i.e., whether the challenger is a party to the contested agreement, or a third-party.[130] The *NRG* case is discussed below, including the underlying FERC proceedings in *Devon Power*, review by the D.C. Circuit and Supreme Court, and FERC's orders on remand.

A. Proceedings at FERC: Devon Power LLC

The *NRG* case arose out of New England's difficulties in ensuring adequate electric power supplies and maintaining the reliability of the region's electric transmission grid.[131] For many years, the ISO-New England ("ISO-NE")[132] imposed on retail utilities an "installed capacity" ("ICAP") requirement,[133] requiring utilities to maintain specified amounts of ICAP based on their peak loads plus a reserve margin.[134] For years, New England's capacity market has been "rife with problems"[135] and "the supply of capacity was barely sufficient to meet the region's demand."[136] FERC, the ISO-NE, electric power generators, and retail

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128. *Id.* at 551. Although disagreeing with the Ninth Circuit's analysis of the two questions presented, the Supreme Court nonetheless affirmed the Ninth Circuit's reversal of FERC's decision because of defects in FERC's analysis. *Id.* at 552-55.

129. NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, 130 S. Ct. 693 (2010).

130. *Id.* at ___, 130 S. Ct. at 696-97, 701.

131. *See id.* at ___, 130 S. Ct. at 696.

132. "ISO" stands for "independent system operator." "An ISO is an independent company that has operational control, but not ownership," over the transmission facilities owned by its member utility companies. *See Maine PUC I*, *supra* note 19, at 468 n.2. An ISO "provide[s] open access to the regional transmission system to all electricity generators at rates established in a single, unbundled, grid-wide tariff . . . .'" *Id.* (quoting Midwest ISO Transmission Owners v. Fed. Energy Regulatory Comm'n, 373 F.3d 1361, 1364 (D.C. Cir. 2004)). In 2004, ISO-NE was organized as a "Regional Transmission Organization" or "RTO." *Id.* FERC grants greater regulatory flexibility to RTOs, provided that they, among other things, "are regional in scope, have exclusive operational control over all transmission facilities within their control, and have sole authority to approve or deny requests for transmission service" over facilities under their control. *Id*. (citing *Midwest ISO Transmission Owners*, 373 F.3d at 1365). RTOs and ISOs may also operate regional markets for electric power and capacity. *See* Wholesale Competition in Regions with Organized Electric Markets, Order No. 719, 73 Fed. Reg. 61,400 (Oct. 28, 2008), *order on reh'g,* Order No. 719-A, 74 Fed. Reg. 37,776 (July 29, 2009), *order on reh'g*, Order No. 719-B, 129 FERC ¶ 61,252 (2009).

133. In *Maine PUC I*, *supra* note 19, the D.C. Circuit noted that utilities generally purchase more capacity than is necessary to meet their customers' demand for electricity in order to ensure that the utilities are able to respond adequately to unexpected fluctuations in demand. *Id.* at 467; *NRG*, 558 U.S. at ___, 130 S. Ct. at 697.

134. *See* Devon Power LLC, 115 FERC ¶ 61,340, at 62,304 (2006).

135. *Maine PUC I*, 520 F.3d at 467. As FERC has subsequently explained, "existing generators needed for reliability [were] not earning sufficient revenues (and [were] in fact losing money), and . . . additional infrastructure [was] needed soon to avoid violations of reliability criteria." *Devon Power LLC*, 115 FERC ¶ 61,340 at 62,315.

136. *NRG*, 558 U.S. at ___, 130 S. Ct. at 697; *see also Maine PUC I*, 520 F.3d at 467.

utilities made several attempts to solve this problem.[137]

In 2003, FERC directed the ISO-NE to develop a new market mechanism that would separately set prices for capacity in different geographical sub-regions in order to encourage construction of new capacity in the sub-regions with greater capacity shortages.[138] In March 2004, the ISO-NE proposed a locational ICAP ("LICAP") mechanism that would set capacity prices for four separate sub-regions.[139] FERC established hearing procedures before an administrative law judge ("ALJ").[140] In June 2005, the ALJ issued an Initial Decision largely accepting the ISO-NE's proposal.[141] Several parties filed exceptions to the ALJ's Initial Decision; FERC subsequently heard arguments, and thereafter established settlement procedures to allow the parties to develop a revised market proposal.[142]

On March 6, 2006, a settlement was reached by 107 of the participants; however, eight participants opposed the settlement.[143] The Settlement Agreement established a "Forward Capacity Market" ("FCM") under which there would be annual price-setting auctions for capacity, held three years in advance of when the capacity would be needed.[144] Each retail utility would be required to acquire

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137. For example, FERC identified in the early 2000s several flaws in the ISO-NE's then-existing ICAP market. *See* ISO New England, Inc., 91 FERC ¶ 61,311, at 62,058 (2000); New England Power Pool & ISO New England, Inc., 100 FERC ¶ 61,287, at 62,259 (2002). Among other things, FERC noted that the then-existing ICAP market lacked a "locational requirement element" and "believe[d] that location is an important aspect of ensuring optimal investment in resources." *New England Power Pool & ISO New England, Inc.*, 100 FERC ¶ 61,287 at 62,278.

138. Devon Power LLC, 103 FERC ¶ 61,082, at 61,266 (2003); *see Maine PUC I*, 520 F.3d at 468; *NRG*, 558 U.S. at ___, 130 S. Ct. at 697.

139. *See* Devon Power LLC, 107 FERC ¶ 61,240, at 62,020 (2004); Maine PUC I, 520 F.3d at 468; *NRG*, 558 U.S. at ___, 130 S. Ct. at 697. Under the ISO-NE proposal, each of the four sub-regions would have a monthly auction for capacity. *Devon Power LLC*, 107 FERC ¶ 61,240, at 62,022. Among other aspects of the proposal, the ISO-NE would establish a demand curve that set the amount of ICAP that must be procured and the price for that capacity. *Id.* The D.C. Circuit noted that the term "demand curve" is misleading because, ordinarily, a demand curve is a model of the relationship between prices and consumer preferences in a free market. *Maine PUC I*, *supra* note 19, at 468 n.3. However, under the ISO-NE's proposal, the "demand curve" was an artificial construct that administratively determined the prices that must be paid for various quantities of capacity. *Id*. (citing *Devon Power LLC*, 107 FERC ¶ 61,240, at 62,022).

140. *Devon Power LLC*, 107 FERC ¶ 61,240, at 62,020; *see Maine PUC I*, 520 F.3d at 468-69*; see also NRG*, 558 U.S. at ___, 130 S. Ct. at 697.

141. Devon Power LLC, 111 FERC ¶ 63,063 (2005). The ALJ's Initial Decision largely adopted the "demand curve" proposed by ISO-NE. *Id.* at 65,211-63.

142. *See* Devon Power LLC, 113 FERC ¶ 61,075, at 61,271 (2005); *see also Maine PUC I*, 520 F.3d at 469; *NRG*, 558 U.S. at ___, 130 S. Ct. at 697. The parties requesting oral argument were mostly state entities and retail customers. *See* Devon Power LLC, 115 FERC ¶ 61,340, at 62,304, 62,306 (2006). Oral argument focused on whether the LICAP mechanism, or some other approach, would result in just and reasonable wholesale power prices in New England that would be adequate to encourage needed generation additions and whether LICAP or another approach would provide assurance that adequate electric generation capacity and reliability would be maintained. *See id.*

143. *See Devon Power LLC*, 115 FERC ¶ 61,340 at 62,306.

144. *See id.* at 62,304, 62,306-08; *see also Maine PUC I*, *supra* note 19, at 469; *NRG*, 558 U.S. at ___, 130 S. Ct. at 697. For the three-year gap between the first capacity auction and the time when the capacity procured in that auction would be provided, the Settlement Agreement provided for a series of fixed, transition-period payments to generators supplying capacity. *See Devon Power LLC*, 115 FERC ¶ 61,340, at 62,308-09; *Maine PUC I*, *supra* note 19, at 469; *NRG*, 558 U.S. at ___, 130 S. Ct. at 697. Although the transition payments were included among the issues presented to the D.C. Circuit and the

enough capacity to meet its share of the total installed capacity requirement—i.e., the minimum level of capacity needed to maintain the reliability of the grid, as determined by the ISO-NE.[145] The FCM proposal contained a locational component: before each auction, the ISO-NE would determine capacity zones by identifying transmission constraints.[146]

Of importance here, § 4.C of the Settlement Agreement provided that challenges to both transition-period payments and auction-clearing prices would be reviewed under "the 'public interest' standard of review set forth in *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956)[,] and [*FPC*] *v. Sierra Pacific Power Co.*, 350 U.S. 348, 76 S.Ct. 368, 100 L.Ed. 388 (1956) (the 'Mobile-Sierra' doctrine) . . . whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*.'"[147]

FERC approved the Settlement Agreement, finding that it was a "just and reasonable outcome" and "consistent with the public interest." [148] Among other things, FERC believed that the *Mobile-Sierra* provision "appropriately balances the need for rate stability and the interests of the diverse entities who will be subject to the [FCM's auction mechanism]."[149]

B. Judicial Review: Maine Public Utilities Commission v. FERC *and* NRG Power Marketing, LLC v. Maine Public Utilities Commission

Several of the parties who objected to the Settlement Agreement sought review in the D.C. Circuit.[150] Decided prior to the Supreme Court's decision in *Morgan Stanley*, the court largely affirmed FERC's decision.[151] However, the petitioners prevailed on the *Mobile-Sierra* issue: The D.C. Circuit held that the *Mobile-Sierra* doctrine could only apply to contracting parties; therefore, the parties to the Settlement Agreement could not "thrust the 'public interest' standard of review upon non-settling third parties who have vociferously objected to the terms of the [S]ettlement [A]greement."[152]

Supreme Court, this article focuses on the FCM auction mechanism because the transition payments lasted only for a limited time, with the final payment made in May 2010. *See* Devon Power LLC, 134 FERC ¶ 61,208, at P 22 (2011). As FERC explained in 2011, "the last transition payment was made over a year ago and, therefore, the controversy as to whether these payments represent contract or tariff rates is now moot." Devon Power LLC, 137 FERC ¶ 61,073, at P 28 (2011).

145. *See Devon Power LLC*, 115 FERC ¶ 61,340, at 62,307; *see Maine PUC I*, 520 F.3d at 469; *NRG*, 558 U.S. at ___, 130 S. Ct. at 697.

146. *See Devon Power LLC*, 115 FERC ¶ 61,340, at 62,307, 62,324-25.

147. *Devon Power LLC*, 115 FERC ¶ 61,340, at 62,309 & n.29; *see Maine PUC I*, *supra* note 19, at 469; *NRG*, 558 U.S. at ___, 130 S. Ct. at 697-98 (citations omitted).

148. *Devon Power LLC*, 115 FERC ¶ 61,340, at 62,304, *order on reh'g,* 117 FERC ¶ 61,133, at 61,712 (2006); *see Maine PUC I*, *supra* note 19, at 469; *NRG*, 558 U.S. at ___, 130 S. Ct. at 698.

149. *Devon Power LLC*, 115 FERC ¶ 61,340, at 62,335; *NRG*, 558 U.S. at ___, 130 S. Ct. at 698; *see also Maine PUC I*, *supra* note 19, at 470.

150. *Maine PUC I*, *supra* note 19, at 467, 470. The court of appeals identified the petitioners as the Maine Public Utilities Commission and the Attorneys General of Connecticut and Massachusetts. *Id*. However, the Supreme Court's opinion in *NRG* stated that *six* of the eight objecting parties petitioned for review. *NRG*, 558 U.S. at ___, 130 S. Ct. at 698.

151. *Maine PUC I*, *supra* note 19, at 467, 470.

152. *Id.* at 467, 470, 476-79 (quoted language at 478); *see also NRG*, 558 U.S. at ___, 130 S. Ct. at 698.

The Supreme Court granted certiorari in *NRG* to determine whether *Mobile-Sierra*'s public interest standard applies to a "contract rate" regardless of the identity of the party challenging the rate.[153] The Court reversed the D.C. Circuit's judgment insofar as it rejected application of the *Mobile-Sierra* public interest presumption to non-contracting parties.[154] The Court explained that if FERC itself must presume that a rate that results from fair, arms-length negotiations is just and reasonable, so too must non-contracting parties.[155] The *Mobile-Sierra* presumption applies "because well-informed wholesale-market participants of approximately equal bargaining power generally can be expected to negotiate just-and-reasonable rates."[156]

Although the Court determined that the *Mobile-Sierra* presumption applied to third-party challenges, it pointed out that the doctrine did not overlook third-party interests: rates may be rejected when they would seriously harm the consuming public.[157] Moreover, limiting the *Mobile-Sierra* doctrine to challenges by contracting parties would undermine the stability of contractual arrangements that the doctrine sought to ensure.[158]

However, the Supreme Court found that neither the D.C. Circuit nor FERC had previously determined whether the auction clearing prices qualified as "contract rates" to which the *Mobile-Sierra* doctrine must apply.[159] Accordingly, the Court remanded that issue to the D.C. Circuit; and, if the rates were not "contract rates," the D.C. Circuit was directed to resolve the additional issue of whether FERC possessed discretion to treat such rates analogously.[160]

On remand, the D.C. Circuit first recounted the proceedings up to that point, noting that the "case has characteristics of a chameleon; it has changed its colors—and its shape—at each stage of the proceedings."[161] Turning to the remanded issues, the D.C. Circuit noted FERC's argument that, even though the auction rates were not "contract rates," FERC nevertheless possesses discretion to approve § 4.C

153. *NRG*, 558 U.S. at ___, 130 S. Ct. at 698.

154. *Id.* at ___, 130 S. Ct. at 698, 701. Perhaps unsurprisingly, following *Morgan Stanley*, commenters opined that the portion of the D.C. Circuit's decision in *Maine PUC I* holding that FERC cannot approve an agreement that would require application of the *Mobile-Sierra* public interest presumption to rate challenges brought by third parties was wrongly decided. *See* Bress, Gergen & Lim, *supra* note 98, at 308-10; Catherine Ascani, Casenote, *Deal or No Deal: It's a Deal in* Morgan Stanley Capital Group, Inc. v. Public Utility District No. 1 of Snohomish County, Washington, 60 MERCER L. REV. 1025, 1041 (2009). *Cf.* McCaffrey, *supra* note 98, at 76-78 (stating that the applicability of the *Mobile-Sierra* public interest presumption to challenges to rates by third-parties "remains a developing issue").

155. *NRG*, 558 U.S. at ___, 130 S. Ct. at 700.

156. *Id.* at ___, 130 S. Ct. at 700 n.4. The Court also noted that "'contract stability ultimately benefits consumers.'" *Id.* (quoting Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 551 (2008)).

157. *Id.* at ___, 130 S. Ct. at 700 (citing *Morgan Stanley*, 554 U.S. at 530). Third parties could include end users, advocacy groups, state utility commissions, or elected officials. *Id.*

158. *Id.* at ___, 130 S. Ct. at 700-01 (citing United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 344 (1956)).

159. *Id.* at ___, 130 S. Ct. at 701. As noted above, *see supra* note 144, the rates at issue also included the transition payments.

160. *Id.*

161. Maine Pub. Utils. Comm'n v. Fed. Energy Regulatory Comm'n, 625 F.3d 754, 755 (D.C. Cir. 2010) [hereinafter *Maine PUC II*].

of the Settlement Agreement.[162] However, the D.C. Circuit found that it could not determine whether FERC's position was reasonable under the Administrative Procedure Act because "FERC never articulated *in its orders* a rationale for its discretion to approve a *Mobile-Sierra* clause outside of the contract context, or an explanation for exercising that discretion here."[163] The court of appeals explained that "FERC must explain why, if the auction rates are not contract rates, they are entitled to *Mobile-Sierra* treatment," suggesting that FERC should clarify how "the auction rates reflect market conditions similar to freely-negotiated contract rates" or on what other ground FERC bases its asserted discretion.[164] The D.C. Circuit remanded FERC's orders approving the Settlement Agreement for further proceedings.[165]

C. Remand to FERC

In response to the remand from the D.C. Circuit, FERC issued an order on March 17, 2011, to resolve

> whether the auction results [. . .] arising from a contested settlement approved by [FERC] earlier in this proceeding constitute "contract rates" where challenges can only be reviewed by [FERC] under a more rigorous application of the statutory "just and reasonable" standard of review; that more rigorous application is often characterized as the *Mobile-Sierra* "public interest" standard.[166]

FERC noted that "if the auction results [. . .] are not 'contract rates,'" there was the supplementary issue of "whether [FERC] may act within its discretion in nevertheless approving a settlement provision imposing the *Mobile-Sierra* 'public interest' standard on certain future challenges to the auction results and transition payments."[167]

As explained by FERC, the *Mobile-Sierra* presumption requires FERC to "presume that rates set by power sales contracts that are freely negotiated at arm's length between willing buyers and sellers meet the statutory 'just and reasonable' standard of review."[168] However, where the parties have not agreed to set rates by contract, *Mobile-Sierra*'s public interest presumption does not automatically apply.[169]

FERC found that the FCM auction rates were not "contract rates" that would

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162. *Id.* at 759.

163. *Id.* (citing Fed. Power Comm'n v. Texaco Inc., 417 U.S. 380, 397 (1974) ("[W]e cannot 'accept . . . counsel's *post hoc* rationalizations for agency action . . . ." (quoting Burlington Truck Lines, Inc. v. United States, 371 U.S. 156, 168-69 (1962)))).

164. *Maine PUC II*, *supra* note 161, at 759-60.

165. *Id.* at 760.

166. Devon Power LLC, 134 FERC ¶ 61,208, at P 1 (2011), *order on reh'g*, 137 FERC ¶ 61,073 (2011). Although not the focus of this article, the rates at issue also included the transition payments. *See supra* note 144.

167. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 1.

168. *Id.* at P 10 (citing Morgan Stanley Capital Grp, Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 530 (2008)); Devon Power LLC, 137 FERC ¶ 61,073, at P 29 (2011) (citing Morgan Stanley Capital Group, Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 530 (2008)).

169. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 11 (citing *Morgan Stanley*, 554 U.S. at 553).

necessarily be subject to the *Mobile-Sierra* public interest presumption when challenged.[170] In its order, FERC noted that the ICAP requirement is set by ISO-NE, not the purchasing entities.[171] FERC then described the FCM's auction mechanism and explained that once a price is determined—i.e., the "market clearing price"—the ISO-NE "assesses each utility a capacity charge equal to that utility's share of the installed capacity requirement multiplied by the market clearing price."[172] In a subsequent order responding to requests for rehearing, FERC stated that under this mechanism, the rates produced by the FCM auctions are "determined unilaterally by the ISO-NE tariff."[173] Further, because the auction applies to participants who did not agree to its adoption—that is, non-parties to the Settlement Agreement—FERC believed that the rates should not be considered "contract rates."[174]

Turning to the second question on remand, FERC began by noting that the FPA does not directly address how the "just and reasonable" standard should be applied or implemented in any particular context.[175] As such, FERC believed that it "has discretion to consider and decide whether future challenges to rates should be evaluated under a more rigorous application of the statutory 'just and reasonable' standard of review."[176] FERC noted that it is not "bound to any one ratemaking formula,"[177] and that nothing in the statute or case law precludes it from applying a standard like the "public interest" presumption when faced with challenges to rates other than contractually agreed-to rates, if relevant considerations make such application appropriate.[178]

In the circumstances of *Devon Power*, FERC believed that it was proper to exercise its discretion and determined that it would apply a more rigorous application of the "just and reasonable" standard if the FCM auction rates were

170. *Id.* at P 2, 9, 13-14, 19; *Devon Power LLC,* 137 FERC ¶ 61,073, at P 21-28.

171. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 13; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 22.

172. *Devon Power LLC,* 134 FERC ¶ 61,208, at P 13; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 22.

173. *Devon Power LLC*, 137 FERC ¶ 61,073, at P 21. "[T]he terms of purchase through the [FCM] auction are set unilaterally by tariff." *Id.* at P 27.

174. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 13; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 25. FERC also noted that because utilities buying capacity in the FCM do not actually participate in the auction that sets the market clearing price, the buyers cannot be considered to be contracting with the sellers of capacity. *Devon Power LLC,* 134 FERC ¶ 61,208, at P 13; 137 FERC ¶ 61,073, at P 23. Responding to requests for rehearing, FERC stated that nothing in the auction could "be reasonably viewed as voluntary agreements of any sort between the sellers of the capacity and the 'buyers' in the auction." *Devon Power LLC*, 137 FERC ¶ 61,073, at P 23.

175. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 15; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 30.

176. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 2, 9, 14-17 (quoted language at P 2).

177. *Id.* at P 15 (citing Morgan Stanley Capital Group, Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 532 (2008)); *Devon Power LLC*, 137 FERC ¶ 61,073, at P 30 (citing *Morgan Stanley*, 554 U.S. at 532). Because "the statutory requirement that rates be 'just and reasonable' is obviously incapable of precise judicial definition, courts have long afforded great deference to [FERC] in its rate decisions." *Devon Power LLC*, 137 FERC ¶ 61,073, at P 30 (citing *Morgan Stanley*, 554 U.S. at 532).

178. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 16; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 31.

challenged in the future.[179] FERC stated that the application of the "public interest" presumption would provide for rate stability while satisfying the "just and reasonable" standard.[180] Because the rates resulting from the FCM auctions would share certain market-based characteristics with freely-negotiated contracts, FERC could presume that such rates would be just and reasonable.[181] Furthermore, the Settlement Agreement might not have been reached without the inclusion of the "public interest" presumption in § 4.C.[182]

Finally, FERC stated that in other contexts it might be unjust and unreasonable to lock in a more stringent application of the "just and reasonable" standard, where there are not broader goals and purposes at issue (such as in *Devon Power*).[183] In each inquiry, FERC would focus on the particular facts presented.[184] In orders issued after the remand order in *Devon Power*, FERC has directed parties that have reached an uncontested settlement to modify their settlement agreements so as not to impose the "public interest" presumption on future challenges or changes proposed by FERC or non-settling parties.[185] In these cases, FERC found that the individual circumstances "did not rise to the compelling level of those present in *Devon Power* so as to warrant binding [FERC] and non-settling third parties to a more rigorous application of the statutory 'just and reasonable' standard of

179. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 2, 9, 17-20; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 32-36. FERC also determined that it would implement the "more rigorous" application of the "just and reasonable" standard to any future challenges to the transition payments. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 21. FERC noted that the D.C. Circuit had upheld the reasonableness of the transition payments, *id.* (citing *Maine PUC I, supra* note 19, at 470-75); that there was a heightened need for the payments because of the swift transition to the FCM auctions, *id.*; and that the transition payments lasted only for a limited time, with the final payment made in May 2010, making it unlikely that the transition payments would become unjust and unreasonable over time, *id.* at P 22.

180. *Id.* at P 17 (citing Devon Power LLC, 115 FERC ¶ 61,340, at 62,335 (2006) (noting that rate stability is particularly important because the case "was initiated in part because of the unstable nature of capacity revenues and the effect that instability has on generating units, particularly those critical to maintaining reliability"); *Devon Power LLC*, 137 FERC ¶ 61,073, at P 33.

181. *Id*. at P 19; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 32. FERC stated that the FCM auctions provide a market-based mechanism for valuing capacity and that the forward-looking nature of the FCM provides appropriate price signals to investors. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 19; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 32. In addition, the locational component of the FCM ensures that new infrastructure development is properly targeted. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 19; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 32-33.

182. *Devon Power LLC*, 137 FERC ¶ 61,073, at P 35. FERC noted that if the Settlement had not been reached, many of the deficiencies related to capacity shortages in New England might have persisted and litigation would have continued. *Id.*

183. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 24; *see Devon Power LLC*, 137 FERC ¶ 61,073, at P 36-37.

184. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 24; *see also Devon Power LLC*, 137 FERC ¶ 61,073, at P 37 (stating that "various proposed applications of the statutory 'just and reasonable' standard, including the *Mobile-Sierra* 'public interest' standard of review, [will be] on a case-by-case basis").

185. High Island Offshore Sys., LLC, 135 FERC ¶ 61,105 (2011) [hereinafter *HIOS*]; Petal Gas Storage, LLC, 135 FERC ¶ 61,152 (2011); S. LNG Co., 135 FERC ¶ 61,153 (2011); Carolina Gas Transmission Corp., 136 FERC ¶ 61,014 (2011) [hereinafter *Carolina Gas*]; S.C. Elec. & Gas Co., 137 FERC ¶ 61,081 (2011) [hereinafter *SCEG*]; Fla. Power & Light Co., 138 FERC ¶ 61,063 (2012) [hereinafter *FP&L*]; *see also Devon Power LLC,* 137 FERC ¶ 61,073, at P 36 (explaining cases).

review."[186]

FERC denied requests for rehearing of its *Devon Power* remand order on October 20, 2011.[187] A petition for review of FERC's orders was filed with the D.C. Circuit on October 31, 2011.[188]

IV. RESPONDING TO *NRG*'S REMANDED QUESTIONS

As explained above in Part III, the Supreme Court found that neither the D.C. Circuit nor FERC had previously determined whether the FCM auction market clearing prices qualified as "contract rates" to which the *Mobile-Sierra* doctrine must apply.[189] The Court remanded that issue to the D.C. Circuit.[190] If the rates were not "contract rates," the D.C. Circuit was directed to resolve the additional issue of whether FERC possessed the discretion to apply the *Mobile-Sierra* presumption to such rates.[191] The D.C. Circuit, in turn, remanded these questions to FERC.[192] FERC determined that the FCM auction rates were not "contract rates."[193] Nonetheless, FERC believed that it "has discretion to consider and decide whether future challenges to rates should be evaluated under a more rigorous application of the statutory 'just and reasonable' standard of review."[194]

FERC erred in its resolution of the first remanded question. FERC should have found that, for the 107 settling parties, the FCM auction rates are "contract rates" (in the Supreme Court's parlance) because, for those parties, the auction rates are the result of a negotiated settlement. Therefore, the *Mobile-Sierra* public interest presumption should apply automatically to challenges to the rates paid by any of the 107 settling parties. This article explores below the characteristics of so-called "contract rates," and suggests that it would be more accurate to describe a rate that is the result of successful negotiations and bargaining between the parties as a "bargained-for rate" ("BFR").[195] The term "contract rate," particularly when

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186. *HIOS*, *supra* note 185, at P 525; *Petal Gas*, 135 FERC ¶ 61,152 at P 17; So. LNG, 135 FERC ¶ 61,153 at P 24; *Carolina Gas*, *supra* note 185, at P 18; *SCEG*, *supra* note 185, at P 5; *FP&L*, *supra* note 185, at P 11; *see also Devon Power LLC*, 137 FERC ¶ 61,073, at P 36 (explaining cases).

187. *Devon Power LLC*, 137 FERC ¶ 61,073.

188. *See* New England Power Generators Ass'n Inc. v. Fed. Regulatory Comm'n, No. 11-1422 (D.C. Cir. Filed Oct. 31, 2011), http://www.ferc.gov/legal/court-cases/pend-case.asp#N.

189. NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, ___, 130 S. Ct. 693, 701 (2010). As noted above, *see supra* note 144, the rates at issue in *NRG* also included the transition payments.

190. *Id.*

191. *Id.*

192. *Maine PUC II*, *supra* note 161, at 759-60.

193. Devon Power LLC, 134 FERC ¶ 61,208, at P 2, 9, 13-14, 19 (2011); Devon Power LLC, 137 FERC ¶ 61,073, at P 21-28 (2011).

194. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 2, 9, 14-17 (quoted language at P 2).

195. The term "negotiated rate" may seem more suitable, but that term already has a particular understanding among FERC and NGA-jurisdictional natural gas pipelines. *See* Natural Gas Pipeline Negotiated Rates Policies and Practices, 104 FERC ¶ 61,134 (2003), *order on reh'g*, 114 FERC ¶ 61,042, *order denying reh'g*, 114 FERC ¶ 61,304 (2006) (modifying FERC's previous policy statement on negotiated rates); Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines, 74 FERC ¶ 61,076, *order on clarification*, 74 FERC ¶ 61,194, *order on reh'g*, 75 FERC ¶ 61,024 (1996).

distinguished from a "tariff rate,"[196] fails to recognize that parties often negotiate and bargain for rates that are ultimately set forth in tariffs. This article also provides examples of FERC-regulated agreements and explains whether such agreements are BFRs to which the public interest presumption should automatically apply. Finally, this article answers the question remanded by the Supreme Court in *NRG*, explaining that for the 107 settling parties, the FCM auction produces BFRs to which the *Mobile-Sierra* public interest presumption should automatically apply.

With respect to the second remanded question—whether FERC possesses discretion to apply a "more rigorous" application of the just and reasonable standard—this article suggests that FERC should not have determined in advance that it would apply a more rigorous application of the just and reasonable standard to future challenges of the auction rates paid by the eight non-settling participants.

A. Determining Whether the Mobile-Sierra *Public Interest Presumption Should Apply Automatically*

Public utilities under the FPA may either (1) "fix by contract, and change only by mutual agreement, the rate agreed upon with a particular customer";[197] or (2) unilaterally establish, and change at will, rates offered to prospective customers.[198] The *Mobile-Sierra* public interest presumption automatically applies to challenges to the first set of agreements—which the Supreme Court in recent cases has referred to as "contract rates." However, the public interest presumption does not (automatically) apply to the second set of agreements, which the Court has referred to as "tariff rates."[199]

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 the FPA.[200] The principal rationale for applying the presumption is that the parties who negotiated the rate 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."[201] The hallmark of these agreements—which this article shall refer to as "BFRs"—is that the agreement contains a rate which was the result of successful negotiation and bargaining between the parties. Thus, the *Mobile-Sierra* doctrine recognizes the importance of individual agreements containing BFRs and that the FPA's regulatory scheme "contemplates abrogation of these agreements only in circumstances of unequivocal public necessity."[202]

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196. In both *NRG* and *Morgan Stanley*, the Supreme Court drew distinctions between "contract rates"—to which the *Mobile-Sierra* public interest presumption automatically applies—and "tariff rates." *NRG*, 558 U.S. at ___, 130 S. Ct. at 698; Morgan Stanley Capital Group. Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 531-33 (2008).

197. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 343 (1956).

198. *Id.*

199. *See NRG*, 558 U.S. at ___, 130 S. Ct. at 698; *Morgan Stanley*, 554 U.S. at 531-33. Because the Court appears to have distinguished only between "contract rates" and "tariff rates," presumably all agreements to which the public interest presumption does not automatically apply are "tariff rates."

200. *Morgan Stanley*, 554 U.S. at 530.

201. *Id.* at 545 (quoting Verizon Commc'ns Inc. v. FCC, 535 U.S. 467, 479 (2002)).

202. *Id.* at 534 (citing *In re* Permian Basin Area Rate Cases, 390 U.S. 747, 822 (1968)).

However, the other category of rates under the FPA's regulatory scheme are subject to a public utility's right to unilaterally establish, and change at will, its rates offered to prospective customers;[203] in other words, unilateral rates. The *Mobile-Sierra* presumption does *not* (automatically) apply to such agreements. The Court described unilateral rate setting in a telecommunications case, *Verizon Communications, Inc. v. FCC*, stating that under "the classic scheme of administrative rate setting at the federal level," the "regulated utility companies [would set out their rates] in proposed tariff schedules," such as those employed under the ICA.[204] Interested parties would have an opportunity to comment, and the tariffs would be accepted by the regulatory agency so long as the rates contained therein were reasonable and not unduly discriminatory.[205] The Court recognized the use of such tariffs of general applicability for the natural gas industry in *Memphis*[206] and for the electric power industry (with respect to the *transmission* of electric power) in *New York v. FERC*.[207] Under the tariff-and-service agreement system, public utilities and natural gas pipelines adopt, subject to FERC approval, system-wide tariffs that establish the rates, terms, and conditions pursuant to which the utility company offers service to its customers, as those rates, terms, and conditions may be changed by the public utility or pipeline from time to time.[208] Customers execute "service agreements" with public utilities or natural gas pipelines containing (or incorporating by reference) standardized language for terms and conditions of service and references to FERC-approved rates set forth in the tariff's rate schedules of general applicability.[209] When such agreements are challenged at FERC, or when a party proposes to change a rate unilaterally, FERC must perform its review without applying the *Mobile-Sierra* public interest presumption.[210]

Thus, there are two types of regulated electric power agreements: (1) agreements that contain BFRs, established by mutual agreement of the parties, and therefore, to which the *Mobile-Sierra* public interest presumption automatically applies; and (2) agreements that contain rates established unilaterally by a public

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203. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 343 (1956).

204. *Verizon*, 535 U.S. at 478. In *Mobile*, the Court noted that the ICA required all rates to be the same for all shippers (customers) and that there was no provision under the ICA for the filing of individual contracts. *Mobile*, 350 U.S. at 345. However, the NGA and FPA recognize the need for private contracts that contain various rates, terms, and conditions, and provide for the filing of such contracts. *Id.*

205. *Verizon*, 535 U.S. at 478.

206. United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div., 358 U.S. 103, 114-15 (1958).

207. New York v. Fed. Energy Regulatory Comm'n, 535 U.S. 1, 10 (2002) (noting that FERC had proposed and adopted the requirement "that public utilities owning and/or controlling facilities used for the transmission of electric energy in interstate commerce have on file tariffs providing for nondiscriminatory open-access transmission services").

208. *Memphis*, 358 U.S. at 115 n.8 (referring to the FPC's Order No. 144, *see supra* note 89); MCGREW, *supra* note 25, at 201. *See supra* Part II.B.1 for a discussion of the tariff-and-service agreement system.

209. *Memphis*, 358 U.S. at 115 n.8. *See* 18 C.F.R. § 35.10a(a) (2012) (setting forth requirements for the inclusion of service agreements with public utility tariffs); MCGREW, *supra* note 25, at 201.

210. *See* Morgan Stanley Capital Group. Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 532, 534 (2008); *Memphis*, 358 U.S. at 114-15. FERC would review the rate under cost of service (or other) principles.

utility, often arising under the tariff-and-service-agreement method. The public interest presumption does not (automatically) apply to such agreements.

The Supreme Court has classified these two types of agreements as (1) "contract rates," and (2) "tariff rates."[211] At first blush, this appears to be convenient shorthand; however, the Court's terminology fails to recognize that the distinction between "contracts" and "tariffs" is not as clear as it once may have been.[212] The term "tariff rate"—as distinguished from a "contract rate"—implies that any agreement that results from the tariff-and-service-agreement system cannot be the result of negotiation and bargaining and, therefore, cannot be automatically subject to the *Mobile-Sierra* presumption. Similarly, the use of the term "contract rate" suggests that the public interest presumption cannot automatically apply to agreements other than traditional bilateral agreements.

This article explains below that the *Mobile-Sierra* public interest presumption should automatically apply to many agreements that include rates contained in tariffs. Rates set forth in tariffs may, in fact, be the result of bargaining and negotiation between a public utility and its customers, particularly in the case of settlement agreements. Therefore, the public interest presumption should apply when these rates are challenged. Instead of "contract rates" and "tariff rates," this article refers to BFRs and unilateral rates. These terms more accurately describe the characteristics of the rates, and recognize that the rates set forth in tariffs frequently are BFRs to which the public interest presumption should automatically apply.

B. BFRs vs. Unilateral Rates: Examples and Explanations

The *Mobile-Sierra* public interest presumption applies to FERC-jurisdictional agreements and rates that are the result of negotiation and bargaining between the parties, but the presumption does not apply to rates that are set unilaterally. This section provides examples that illustrate the difference between the two. The first examples discussed below are the most straight-forward: bilateral fixed-rate contracts and tariffs, classic examples of BFRs and unilateral rates, respectively. The next example is that of unilateral rates set forth in bilateral agreements. Finally, this section discusses unilateral rates that result in negotiated settlements.

1. Classic Bargained-For Rates (BFRs): Bilateral Fixed-Rate Contracts

The classic example of an agreement containing a BFR is a bilateral fixed-rate agreement between a utility company (seller) and its customer (buyer). Both *Mobile* and *Sierra* involved bilateral fixed-rate agreements containing BFRs.[213] In each case, the seller attempted to change the BFR set forth in its existing bilateral contract. In *Mobile*, United Gas Pipe Line Company ("United") entered into an

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211. NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, __, 130 S. Ct. 693, 698 (2010); *Morgan Stanley*, 554 U.S. at 531-33.

212. Another point of confusion that may arise from the use of the term "contract rate" is that it may suggest that other agreements are *not* contracts. However, as explained above, service agreements that incorporate rates, terms, and conditions contained in tariffs create binding obligations on the parties.

213. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 336-37 (1956); Fed. Power Comm'n v. Sierra Pac. Power Co., 350 U.S. 348, 351-52 (1956).

agreement to supply gas to Mobile Gas Service Corporation ("Mobile") for a duration of ten years at a rate that was the equivalent of 10.7 cents per MCF (thousand cubic feet).[214] However, prior to the expiration of that agreement, "United, without the consent of Mobile, filed new schedules with [FERC], which purported to increase the rate on gas to . . . 14.5 cents per MCF."[215] Similarly, in *Sierra*, Sierra Pacific Power Company ("Sierra") had entered into an agreement to purchase electric power from Pacific Gas and Electric Company ("PG&E") for a duration of fifteen years.[216] However, prior to the expiration of the agreement, "PG&E, without the consent of Sierra, filed with [FERC] . . . a schedule purporting to increase its rate to Sierra by approximately 28%."[217]

In both cases, the agreements at issue contained BFRs. United and Mobile, and PG&E and Sierra, respectively,[218] negotiated and entered into agreements where the rate was the result of arms-length bargaining. These agreements were traditional bilateral contracts and could not be changed without the consent of both parties.[219] Because the agreements contained BFRs, the public interest presumption applied, and neither United nor PG&E was permitted to unilaterally change the BFRs in the agreements.[220] In neither case did the Court find that the public interest required the rates to be reformed.[221]

2. Classic Unilateral Rates: Tariffs

Other agreements contain unilateral rates. As the Supreme Court's terminology suggests, the classic example of a unilateral rate is set forth in a tariff of general applicability. As discussed above, the use of tariffs for federally-regulated rates originated under the ICA.[222] In *Memphis*, the Supreme Court recognized that FERC had directed natural gas pipelines to adopt tariffs for natural gas transmission.[223] As part of the Order No. 888 series, initially issued in 1996, FERC required electric utilities to provide open access transmission service pursuant to a standardized, or "*pro forma*," tariff, which was set forth in Appendix

214. *Mobile*, 350 U.S. at 335-36.

215. *Id.* at 336.

216. *Sierra*, 350 U.S. at 352.

217. *Id.*

218. As the Supreme Court suggested in *Morgan Stanley* and *Verizon*, these four parties—United, Mobile, PG&E, and Sierra—were each "sophisticated businesses enjoying presumptively equal bargaining power," and therefore should "be expected to negotiate a just and reasonable rate as between . . . them." *Morgan Stanley*, 554 U.S. at 545 (citing Verizon Commc'ns, Inc. v. FCC, 535 U.S. 467, 479 (2002)).

219. *See Mobile*, 350 U.S. at 343 (stating that rates fixed by contract may only be changed by mutual agreement).

220. *Mobile*, 350 U.S. at 347 (finding that United's unilateral filing of a new rate "was a nullity insofar as it purported to change the rate set by its contract with Mobile and that the contract rate remained the only lawful rate"); *Sierra*, 350 U.S. at 353 (concluding that PG&E's unilateral filing of a new rate was not effective to change PG&E's agreement with Sierra).

221. *See Mobile*, 350 U.S. at 347; *Sierra*, 350 U.S. at 353.

222. Verizon Commc'ns, Inc. v. FCC, 535 U.S. 467, 478 (2002) (describing the use of tariffs as "the classic scheme of administrative rate setting at the federal level").

223. United Gas Pipe Line Co. v. Memphis Light, Gas and Water Div., 358 U.S. 103, 114-15 (1958).

D of Order No. 888.[224]

A tariff does not, on its own, constitute an agreement between the service provider and any customer. Customers must execute "service agreements" containing references to rates set forth in the tariff's rate schedules and incorporating the tariff's general terms and conditions.[225] Under a classic tariff scheme, customers do not negotiate with the utility the rates for service. Instead, the customer must accept the rates set forth in the tariff. The customer is protected because the regulatory agency, such as FERC, has found that the rates listed in the tariff are just and reasonable and not unduly discriminatory. Tariff rates generally constitute a utility's "going rates."[226] When the utility determines that the rates in the tariff no longer provide it with a sufficient return, the utility may unilaterally seek an increase by proposing a new rate to FERC.[227] The rate goes into effect automatically so long as FERC does not find that the rate is not just and reasonable.[228]

Because the tariffs apply to *all* of the utility's customers and tariffs are not limited to a specific duration, a utility must retain the right to change its rates when it requires a greater return. FERC has recognized as much. In Order No. 888, FERC's *pro forma* tariff for electric transmission service provides that the electric transmission provider retains the right to unilaterally propose rate changes and file those proposed rate changes with FERC pursuant to FPA section 205.[229]

3. Unilateral Rates in Bilateral Agreements

Tariffs are not the only contractual instruments through which a unilateral rate may be established. Changes to a bilateral agreement ordinarily must be agreed to by both parties;[230] but the FPA's regulatory scheme permits parties to include in

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224. Order No. 888, *supra* note 95, 61 Fed. Reg. at 21,706-24. As opposed to natural gas pipelines, which were permitted to propose their own individual tariffs, FERC-regulated public utilities providing transmission service were required to adopt the *pro forma* tariff. Utilities were permitted to propose deviations from the *pro forma* tariff if those individual changes could be shown to be consistent with, or superior to, the *pro forma* tariff. *Id.* at 21,619.

225. *Memphis*, 358 U.S. at 115 n.8; *see* McGrew, *supra* note 25, at 188-89, 201.

226. *See Memphis*, 358 U.S. at 105, 110, 114.

227. *Memphis*, 358 U.S. at 115 n.8 (noting that FERC expressly contemplated that a seller would reserve for itself the right to change rates under section 4 of the NGA).

228. *See* 16 U.S.C.A. §§ 824d(a), (d) (2010 & Supp. 2012).

229. Order No. 888, *supra* note 95, 61 Fed. Reg. at 21,710. The provision, section 9 of the *pro forma* tariff, provides, in relevant part:

> Nothing contained in the Tariff or any Service Agreement shall be construed as affecting in any way the right of the Transmission Provider to unilaterally make application to the Commission for a change in rates, terms and conditions, charges, classification of service, Service Agreement, rule or regulation under Section 205 of the Federal Power Act and pursuant to the Commission's rules and regulations promulgated thereunder.

The provision also provides that customers retain their rights to seek redress under FPA section 206:

> Nothing contained in the Tariff or any Service Agreement shall be construed as affecting in any way the ability of any Party receiving service under the Tariff to exercise its rights under the Federal Power Act and pursuant to the Commission's rules and regulations promulgated thereunder.

230. *See* United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 343 (1956) (stating that rates fixed by contract may only be changed by mutual agreement).

their bilateral agreements a provision that would permit one or both parties to unilaterally establish a new rate that would supersede the existing contract rate—i.e., a *Memphis* clause, in essence permitting the parties to "contract out of the *Mobile-Sierra* presumption."[231] The new rate would be subject to FPA section 205(d)'s requirement that it be filed with FERC but can take effect without FERC action.[232]

Two courts of appeals have identified another route by which two parties to a bilateral agreement can effectuate a rate change.[233] Parties may include in their contracts a provision that would permit FERC to act pursuant to FPA section 206(a) and set aside the existing rate if the rate is found not to be just and reasonable and replace it with a new rate.[234] Such a provision is different from a *Memphis* clause, which permits the seller to take unilateral action to increase rates, subject only to FPA section 205's filing requirements.[235] Such rate changes are effected solely by virtue of the utility's action and do not require a FERC order.[236]

Unlike a *Memphis* clause, a provision permitting rate changes pursuant to FPA section 206 requires FERC action to permit any proposed rate changes.[237] When the contract requires a FERC order, the parties "have bargained for and obtained a contractual authorization for a section 206(a) proceeding with its just and reasonable standard of proof."[238] The *Mobile-Sierra* public interest presumption would not apply in this context because the parties contemplated that they would be permitted to seek rate changes.[239] Because the rate change would be implemented

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231. Morgan Stanley Capital Group, Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 534 (2008); *Memphis*, 358 U.S. at 110, 114-15; *see also* Papago Tribal Util. Auth. v. Fed. Energy Regulatory Comm'n, 723 F.2d 950, 953 (D.C. Cir. 1983) (noting that one of the ways that rates may be revised under FPA sections 205 and 206 is for the parties to "agree that new rates can be unilaterally and immediately imposed by the utility, subject, under § 205, to [FERC] suspension for no longer than five months, and to ultimate [FERC] disallowance if they are not just and reasonable").

232. *See* 16 U.S.C.A. § 824d(d) (2010 & Supp. 2012).

233. *See Papago*, 723 F.2d at 953; Louisiana Power & Light Co. v. Fed. Energy Regulatory Comm'n, 587 F.2d 671, 675-76 (5th Cir. 1979). One commenter has referred to *Papago* as one of a series of cases that belong to the "Middle Age of the *Mobile-Sierra* Doctrine." Gentile, *supra* note 78, at 358-363.

234. *Papago*, 723 F.2d at 953; *see Louisiana Power*, 587 F.2d at 675-76. The Supreme Court in *Mobile* similarly observed that there was nothing in section 206 to prevent a utility "from furnishing to [FERC] any relevant information and requesting it to initiate an investigation on its own motion." United Gas Pipe Line Co. v. Mobile Gas Servs. Corp, 350 U.S., 332, at 344-45 (1956).

235. United Gas Pipe Line Co. v. Memphis Light, Gas and Water Div., 358 U.S. 103, 110, 114-15 (1958); *see Papago*, 723 F.2d at 953-55; *Louisiana Power*, 587 F.2d at 675.

236. *See Louisiana Power*, 587 F.2d at 676 (citing *Mobile*, 350 U.S. at 342).

237. *See Papago*, 723 F.2d at 955 (citing Papago Tribal Util. Auth. v. Fed. Energy Regulatory Comm'n, 610 F.2d 914, 928 (D.C. Cir. 1979)); *Louisiana Power*, 587 F.2d at 675. The contract provision at issue in the *Papago* cases stated that after a specified period of time, the rates would remain in effect "unless and until changed by [FERC], with either party hereto to be free unilaterally to take appropriate action before [FERC] in connection with changes which may be desired by such party." *Papago*, 723 F.2d at 953. In *Louisiana Power*, the provision stated that the agreements were "subject to amendment or alteration as a result of and in accordance with a valid applicable order of any governmental authority having jurisdiction hereof." *Louisiana Power*, 587 F.2d at 675.

238. *Louisiana Power*, 587 F.2d at 676.

239. *See Papago*, 723 F.2d at 954; Kansas Cities v. Fed. Energy Regulatory Comm'n, 723 F.2d 82, 87-89 (D.C. Cir. 1983) (Because the public interest presumption is "almost insurmountable," "to assume that a contractual provision pertaining to rate adjustments" would incorporate that presumption would

pursuant to FPA section 206(a), the rate would only apply prospectively from the date of the FERC order.[240]

Thus, the courts recognize that the entities regulated by FERC have established several options through which to contractually provide for changes to rates in existing bilateral agreements. "The rule of *Sierra*, *Mobile* and *Memphis* is refreshingly simple: The contract between the parties governs the legality of the filing. Rate filings consistent with contractual obligations are valid; rate filings inconsistent with contractual obligations are invalid."[241]

4. Unilateral Rate Setting that Results in a Settlement: A Mixed Case

Utilities' tariffs generally include *Memphis* clauses, permitting the utilities to unilaterally change rates set forth in the tariffs. Similarly, if a bilateral agreement contains a *Memphis* clause, the utility may make a unilateral change to a rate set forth in that contract. In both cases, the utility must comply with the notice provisions of FPA section 205(d).[242]

The prevalence of unilateral rate setting has caused FERC and utility practice with respect to FPA section 205 to evolve over time. The Supreme Court in *Mobile* characterized the FPA as *not* establishing a rate-changing procedure or a mechanism for initiating rate "proceedings."[243] FPA section 205 provides only for *notice* to FERC of the rates established by the public utility and for *review* by FERC of those rates.[244] Notwithstanding *Mobile*'s straightforward analysis of FPA section 205, that section's notice requirement and opportunity for review by FERC have become similar to the "traditional" unilateral rate-setting model,[245] where public utilities "seek approval" from FERC in order to implement a proposed rate.[246] FPA section 205 has been described as "the key pattern for much of

be "to assume that it was intended to be virtually inoperative; whereas to interpret it as referring" to the just and reasonable standard without the application of the presumption "is to give it a content that is both substantial and fair to both sides.").

240. *See* 16 U.S.C.A. § 824e(a) (2010 & Supp. 2012); *Louisiana Power*, 587 F.2d at 676.

241. Richmond Power & Light Co. v. Fed. Power Comm'n, 481 F.2d 490, 493 (D.C. Cir. 1973); *see also* Kyle, *supra* note 81, at 100 (stating that in *Memphis*, the Supreme Court held "that a contract between a seller and a buyer, and particularly a clear expression in a price provision therein, means exactly what it says").

242. *See* 16 U.S.C.A. § 824d(d) (2010 & Supp. 2012); United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 339-40, 341-42 (1956) (noting that FPA section 205(d) is not a grant of power to utilities, but merely indicates that otherwise valid changes to a contract cannot go into effect without providing the required notice to FERC).

243. *Mobile*, 350 U.S. at 342. *Cf.* Borough of Lansdale v. FPC, 494 F.2d 1104, 1113 (D.C. Cir. 1974) (stating that the purpose of the *Mobile-Sierra* doctrine is "to subordinate the statutory filing mechanism to the broad and familiar dictates of contract law").

244. *See Mobile*, 350 U.S. at 342-43.

245. As the Court explained in *Verizon*, under "the classic scheme of administrative rate setting at the federal level," the "regulated utility companies [would set out their rates] in proposed tariff schedules." 535 U.S. 467, 478 (2002). Interested parties would have an opportunity to comment, and the tariffs would be accepted by the regulatory agency so long as the rates contained therein were reasonable and not unduly discriminatory. *Id.*

246. Likely reflecting the change in practice resulting from the prevalence of unilateral rate setting, the D.C. Circuit has stated that "Section 205 of the [FPA] gives the utility the right to file rates and terms for services rendered with its assets." Atlantic City Elec. Co. v. Fed. Energy Regulatory Comm'n,

[FERC's] regulation: a public utility makes a proposed filing and [FERC] then acts to accept, reject, or modify the filing as necessary."[247]

When a utility's unilateral rate filing is contested by interested parties, FERC will frequently give the utility and the parties the opportunity to come to an agreement, or settlement, resolving differences in their positions. This article explains that when the utility and interested parties reach a settlement, through negotiation and bargaining, the rate they establish is a BFR. FERC's rate filing procedures and settlement practice are summarized below. This article argues that because settlements are the result of negotiation and bargaining, the public interest presumption should automatically apply when a settlement is challenged. An example of a unilateral rate filing resulting in a settlement is provided below, including an explanation of when and how the *Mobile-Sierra* public interest presumption would apply.

a. FERC's Rate Filing Procedures

FERC's regulations implementing FPA section 205(c)[248] and 205(d)[249] are set forth at 18 C.F.R. Part 35.[250] When a utility unilaterally submits a proposed rate increase to FERC, the utility initiates what is commonly referred to as a "rate case."[251] Consistent with FPA section 205(d), FERC's regulations require proposed changes to be submitted to FERC not less than sixty days or more than 120 days prior to the proposed effective date of the change.[252] FERC may waive the notice requirement if the proponent has shown good cause.[253] FERC's regulations require that the utility include the rationale and support for the increase, and to enable FERC and its staff to evaluate the merits of the "proposed" rate.[254] A utility may need to file up to thirty-eight different cost-of-service statements.[255]

After the utility makes its initial rate case filing, FERC will assign a new

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295 F.3d 1, 9 (D.C. Cir. 2002). In *Atlantic City Elec. Co.*, the court characterized FPA section 205's filing requirement as a statutory right to file changes to rates given to public utilities by Congress. *Id.* This characterization stands in stark contrast to *Mobile*'s pronouncement that section 205 bestowed no rights on utilities, but merely required utilities to provide notice of any rate change that they are permitted under their agreements to make. *See Mobile*, 350 U.S. at 339-40, 341-42.

247. MCGREW, *supra* note 25, at 21.

248. Section 205(c) requires effective rate schedules and contracts to be filed with FERC. 16 U.S.C.A. § 824d(c) (2010 & Supp. 2012).

249. Section 205(d) requires all changes in such schedules and contracts to be filed at least sixty days before the changes go into effect. 16 U.S.C.A. § 824d(d).

250. 18 C.F.R. § 35.1-35.47. These regulations apply both to proposed changes to rates on file at FERC as well as to proposed revisions to non-rate terms and conditions of contracts and tariff provisions.

251. Part 35's requirements also apply to the submission of BFRs to FERC pursuant to FPA section 205(d).

252. 18 C.F.R. § 35.3(a).

253. *Id.*

254. *See* 18 C.F.R. § 35.13.

255. *Id.* at § 35.13(h) (setting forth Statements AA through BM) (note that there is no Statement AZ). These Statements seek information relating to, among other things, earnings, labor, materials, operation and maintenance expenses, taxes, fuel, depreciation on plant, construction, interest costs for debt, and other costs. Not all thirty-eight Statements will be appropriate for each rate case.

docket number to that filing and issue a "notice of filing."[256] In the notice of filing, FERC will establish a deadline—usually twenty-one days after the date of filing—for interested parties to submit protests and motions to intervene in the docketed proceeding.[257] Through protests, interested parties, such as customers or state commissions, may set forth their objections to the rate change proposed by the utility. If no party protests a proposed rate change, FERC is more likely to permit the proposed change to become effective on the proposed effective date.[258] This practice is consistent with the traditional understanding of FPA section 205 expressed in *Mobile*, that section 205 is not a rate-change mechanism, but that otherwise valid rate changes can go into effect so long as the proponent provides the required notice to FERC and FERC has the opportunity to review the changed rate.[259]

Although FERC may reject a filing "which patently fails to substantially comply" with FERC's Part 35 requirements,[260] FERC generally will issue an order permitting the proposed rate to become effective on the date requested, or suspending the filing (for up to five months) and permitting it to become effective subject to refund.[261] The purpose of a suspension is to allow FERC to resolve issues of fact and to determine whether the proposed rate is just and reasonable, or what a just and reasonable rate would be.[262] If the proposed rate is suspended, it is generally set for hearing—a trial-type proceeding—before an ALJ.[263]

b. Settlement Practice at FERC

The settlement practice has been used by FERC to assist in managing its

256. *See* MCGREW, *supra* note 25, at 182.

257. *See* 18 C.F.R. § 35.8. The regulation establishes a period of twenty-one days as the default period during which an interested party may file a protest.

258. *See* MCGREW, *supra* note 25, at 182.

259. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 339-40, 41-42 (1956). FERC's regulations state that the fact that a rate goes into effect does not necessarily constitute "approval" by FERC of such rate. 18 C.F.R. § 35.4.

260. 18 C.F.R. § 35.5(a). A rate filing should only be rejected if it "patently is either deficient in form or a substantive nullity." Municipal Light Boards v. FPC, 450 F.2d 1341, 1345 (D.C. Cir. 1971). Rejection of a filing is appropriate "where the filing is so deficient on its face that the agency may properly return it to the filing party without even awaiting a responsive filing by any other party in interest." *Id.* at 1346.

261. *See* MCGREW, *supra* note 25, at 32. Where FERC's preliminary analysis indicates that the proposed rates may be unjust and unreasonable, and may be substantially excessive, FERC will generally impose a five-month suspension under FPA section 205. *See* W. Tex. Utils. Co., 18 FERC ¶ 61,189 (1982). If a rate is permitted to become effective "subject to refund," the utility is permitted to collect the proposed rate while the hearing takes place. *Id*. When the hearing is concluded, and FERC has determined a just and reasonable rate, the utility must refund the difference between the rate that was collected and the just and reasonable rate. *Id*.

262. *See* 16 U.S.C.A. § 824d(e) (2010 & Supp. 2012). In such situations, FERC typically will find that aspects of the proposed rate change cannot be resolved based on the record before it—i.e., the materials submitted by the proponent of the rate change and any protests thereto—and are more appropriately addressed in a hearing before an ALJ. *See, e.g.*, PacifiCorp, 137 FERC ¶ 61,247 at P 18 (Dec. 30, 2011).

263. *See* MCGREW, *supra* note 25, at 32, 183.

voluminous case load.[264] Because FERC hearings can be time consuming and expensive, parties often resolve the issues set for hearing by settlement.[265] FERC and the courts have determined that settlements are in the public interest because they provide for "voluntary, self-imposed resolutions" of issues that have been set for hearing.[266] In dockets where FERC has set issues for hearing, it is common practice for FERC to hold the hearing in abeyance and direct the parties to engage in settlement discussions aided by the appointment of a settlement judge.[267]

Parties may submit an offer of settlement at any time,[268] but settlements must be submitted to and approved by FERC in order to take effect. After an offer of settlement is submitted to FERC, all participants in the docketed proceeding have the opportunity to file comments and reply comments on the settlement offer.[269] Given the inherent nature of compromise involved in a settlement, a settlement offer may be considered a "black box" in which the settling parties agree to settle the case without specifying a rate of return.[270] If the offer of settlement is uncontested, FERC will approve the settlement if it is fair and reasonable and in the public interest.[271] Generally, if the settlement is uncontested, there are few procedural obstacles in the path to FERC approval.[272]

Settlements are reached through negotiation and bargaining, and the customers who join the settlement have agreed to the rate set forth in the settlement agreement.[273] As such, the *Mobile-Sierra* public interest presumption applies to

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264. *See* Tex. E. Transmission Corp. v. Fed. Power Comm'n, 306 F.2d 345, 347 (5th Cir. 1962). FERC relies on its informal settlement procedure to resolve most of its rate cases. *See, e.g.*, Littlechild, *supra* note 9, at 2, 32. Professor Littlechild provides a detailed account of how the settlement process at FERC operates in practice with respect to natural gas pipeline rate cases. Another article has used a theoretical model and empirical data from natural gas cases to examine three issues: (1) how the settlement process is different from the formal adjudicatory process; (2) how settlement outcomes are different from outcomes in litigation; and (3) why participants settle rate cases. Zhongmin Wang, *Settling Utility Rate Cases: An Alternative Ratemaking Procedure*, 26 J. OF REG. ECON. 141 (2004).

265. *See* Pa. Gas & Water Co. v. Fed. Power Comm'n, 463 F.2d 1242, 1247 (D.C. Cir. 1972) (noting that the purpose of the Administrative Procedure Act's informal settlement provision, 5 U.S.C. § 554(c), "is to eliminate the need for often costly and lengthy formal hearings in those cases where the parties are able to reach a result of their own which the appropriate agency finds compatible with the public interest"); MCGREW, *supra* note 25, at 35.

266. *See* MCGREW, *supra* note 25, at 36.

267. *See* 18 C.F.R. § 385.603 (2012).

268. *Id.* § 385.602.

269. *Id.* § 385.602(f).

270. *See* MCGREW, *supra* note 25, at 104; Littlechild, *supra* note 9, at 17; Wang, *supra* note 264, at 150.

271. 18 C.F.R. § 385.602(g).

272. *See* MCGREW, *supra* note 25, at 36.

273. *See* United Mun. Distribs. Grp. v. Fed. Energy Regulatory Comm'n, 732 F.2d 202, 205 (D.C. Cir. 1984) (characterizing approval of a settlement "allowing [the settling parties] to have the benefit of their bargain"); *see also* Littlechild, *supra* note 9, at 17-19 (describing the settlement procedure as a negotiation process), 32 (stating that FERC's "regulatory aim is to bring the parties into agreement, not to impose a preconceived settlement upon them" and "to facilitate the market process, not to replace it"); Wang, *supra* note 264, at 156, 161 (explaining that "[t]he settlement process is clearly a bargaining game" and that consenting parties to a settlement may "reap the benefits of their bargain"). *Cf.* McCaffrey, *supra* note 98, at 78-80 (noting that it can be argued that FERC should not "reject a settlement agreement negotiated by sophisticated parties to govern jurisdictional rates, terms and conditions").

issues that are resolved through settlement.[274] As discussed above in Part II, bargaining between parties is the hallmark of rates to which the public interest presumption must apply. Although proceedings to change rates may have commenced through a unilateral filing by a utility, the resolution through settlement transforms the unilateral rate "proposal" into a BFR.[275]

Settlements need not be unanimous and may be contested by participants of the proceeding.[276] If the offer of settlement is contested, FERC may decide the merits of the contested issues if it determines that the record is adequately developed to do so.[277] If the record is not adequate to make a determination on the

274. *See* Dominion Transmission, Inc. v. Fed. Energy Regulatory Comm'n, 533 F.3d 845, 853-56 (D.C. Cir. 2008) (finding that FERC was not permitted to modify the terms of a settlement agreement because the *Mobile-Sierra* public interest presumption was not overcome); *Maine PUC I*, *supra* note 19, at 476 (stating that "when the parties to a rate dispute reach a contractual settlement, FERC must enforce the terms of the bargain unless the public interest requires otherwise"); Union Elec. Co. v. Fed. Energy Regulatory Comm'n, 890 F.2d 1193, 1194-95 (D.C. Cir. 1989) (finding that the *Mobile-Sierra* doctrine's pro-contract policy "encompasses settlement agreements"); Cities of Newark v. Fed. Energy Regulatory Comm'n 763 F.2d 533, 546-47 (3d Cir. 1985) (noting that the "policies underlying the *Mobile-Sierra* doctrine apply with equal force to settlement agreements"); Cities of Bethany v. Fed. Energy Regulatory Comm'n, 727 F.2d 1131, 1139 (D.C. Cir. 1984) ("[T]he policies . . . in *Mobile* and *Sierra* support treating a settlement agreement" as permissible under FPA section 205(b)'s anti-discrimination requirement, even when other participants do not agree to the settlement and pay different rates). *Cf.* Tewksbury, Lim & Su, *supra* note 98, at 444 ("[I]f a settlement package includes a fixed-rate contract or provides that the settling parties will execute a fixed-rate contract upon approval of the settlement, then the contract rate results directly from the provisions of the settlement.").

275. It has been suggested that "negotiated settlements have generally led to better information flows and understanding in the industry, and to better relationships between the company and customers." Littlechild, *supra* note 9, at 24.

276. *See* 18 C.F.R. § 385.602(h). A key difference between settlements in administrative proceedings and those in civil litigation is that a settlement "do[es] not have to be consented to by all parties to the [administrative] proceeding, and if settlements are found to be 'equitable by the regulatory agency, then the terms of the settlement form the substance of an order binding on all parties, even though not all are in accord as to the result.'" Mary Ann Walker, *Settlement Practice at the FERC: Boom or Bane*, 7 ENERGY L. J. 343, 344 (1986) (quoting Pa. Gas & Water Co. v. Fed. Power Comm'n, 463 F.2d 1242, 1247 (D.C. Cir. 1972). Some commenters have argued that regulatory commissions should not accept contested or non-unanimous settlements. *See, e.g.*, Stefan H. Krieger, *Problems for Captive Ratepayers in Nonunanimous Settlements of Public Utility Rate Cases*, 12 YALE J. ON REG. 257 (1995). *But see* Alan P. Buchmann & Robert S. Tongren, *Nonunanimous Settlements of Public Utility Rate Cases: A Response*, 13 YALE J. ON REG. 337 (1996) (arguing that requiring unanimous settlements is neither necessary nor conducive to reasonable regulation). Other observers suggest that contested, or non-unanimous, settlements are abnormal, and that the uncertainty about the outcome and the cost and burden of carrying a case alone may make contested settlements unattractive to objecting parties. *See* Littlechild, *supra* note 9, at 19.

277. 18 C.F.R. § 385.602(h); *see Pa. Gas & Water Co.*, 463 F.2d at 1247-52 (finding that FERC may approve a non-unanimous rate settlement proposal and terminate proceedings over the objection of a participant in the proceeding). In *Trailblazer Pipeline Co.*, 85 FERC ¶ 61,345 (1998), *order on reh'g*, 87 FERC ¶ 61,110 (1999), FERC explained the standards it would use to rule on contested offers of settlement. If FERC concludes that a contested settlement provides an acceptable outcome for a case, it must next determine which of four approaches it will employ to address each of the contested issues on the merits: (1) FERC shall render a binding merits decision on each contested issue; (2) FERC shall approve the settlement based on a finding that the overall settlement as a package is just and reasonable; (3) FERC shall determine that the benefits of the settlement outweigh the nature of the objections, and the interests of the contesting party are too attenuated; or (4) FERC shall approve the settlement as

merits of a contested issue, FERC may provide for a limited hearing to supplement the record so that FERC may make such findings on the merits.[278] FERC may choose to sever contested issues or contesting parties, approving the uncontested portion of the settlement or approving the settlement as between consenting parties, if it finds it appropriate to do so.[279] However, most offers of settlement contain "non-severability" clauses, which require that the offer of settlement be approved as a package and that issues may not be severed.[280]

A settlement may be reached among all or some of the participants to the proceeding and may resolve all or some of the issues between the parties. FERC may impose aspects of a non-unanimous settlement on participants that contested the settlement.[281] The *Mobile-Sierra* public interest presumption should apply when an issue resolved by the settlement is challenged,[282] but not when an aspect of the settlement that was imposed on a contesting participant is challenged. This may be administratively inconvenient—where the public interest presumption would apply to a challenge to rates paid by settlement parties, but would not apply to a challenge to identical rates paid by a contesting participant. However, it recognizes that the parties to a settlement successfully negotiated and agreed to the rates and issues set forth in the settlement agreement, but that a participant contesting part (or all) of a settlement did not. It is also consistent with FERC's practice of severing contesting parties in order to effectuate a settlement among the consenting parties.[283] Courts of appeals have approved this practice, even though it results in participants to the same proceeding paying different rates.[284] Where a rate proceeding may result in participants paying different rates (because FERC may approve a settlement for parties consenting to the settlement agreement, but contesting participants would pay an administratively determined rate), it follows

uncontested for the consenting parties, and sever the contesting parties to allow them to litigate the issues raised. *Id.*

278. 18 C.F.R. § 385.602(h).

279. *Id.*; *see* United Mun. Distribs. Group. v. Fed. Energy Regulatory Comm'n , 732 F.2d 202, 204-05, 207-12 (D.C. Cir. 1984) (upholding FERC's decision, United Gas Pipe Line Co., 22 FERC ¶ 61,094, *order on reh'g*, 23 FERC ¶ 61,101 (1983), to approve a settlement as to all parties except the contesting party and to direct a full evidentiary hearing on the question of the contesting party's rates). *Cf.* Wang, *supra* note 264, at 161 (concluding that FERC's policy of approving a settlement as uncontested for consenting parties and severing contesting parties to litigate a rate case is more practical than adopting a unanimity requirement).

280. *See* Walker, *supra* note 276 at 353; Wang, *supra* note 264, at 150.

281. 18 C.F.R. § 385.602(h); *Pa. Gas & Water Co.*, 463 F.2d at 1247-52.

282. *See* Dominion Transmission, Inc. v. Fed. Energy Regulatory Comm'n, 533 F.3d 845, 853-56 (D.C. Cir. 2008); *Maine PUC I*, *supra* note 19, at 476; Union Elec. Co. v. Fed. Energy Regulatory Comm'n, 890 F.2d 1193, 1194-95 (D.C. Cir. 1989); Cities of Newark v. Fed. Energy Regulatory Comm'n 763 F.2d 533, 546-47 (3d Cir. 1985); Cities of Bethany v. Fed. Energy Regulatory Comm'n, 727 F.2d 1131, 1139 (D.C. Cir. 1984).

283. *See* 18 C.F.R. § 385.602(h).

284. *See United Mun. Distribs. Grp.*, 732 F.2d at 204-05, 207-12; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139. In *Cities of Newark* and *Cities of Bethany*, the Third Circuit and the D.C. Circuit, respectively, determined that rate disparities between customers as a result of a settlement with some customers are permissible and are not unlawfully discriminatory under FPA section 205(b), 16 U.S.C.A. § 824d(b) (2010 & Supp. 2012). The Third Circuit noted in *Cities of Newark* that there may be tension between FPA section 205(b)'s anti-discrimination mandate, and "the pro-settlement bias of the *Mobile-Sierra* doctrine." 763 F.2d at 546.

that there may be differing applications of the just and reasonable standard when rates established through a settlement are challenged. This is because the *Mobile-Sierra* public interest presumption would apply when rates paid by settling parties are challenged, but not when the rates paid by participants on whom the settlement rates were imposed by FERC are challenged.

c. Examples

Some examples may help to illustrate these principles. Suppose that Utility Co. has an electric tariff on file with FERC. The tariff contains three rate schedules for different electric services: Rates Schedules A, B, and C. Utility Co.'s tariff includes a *Memphis* clause, permitting Utility Co. to make unilateral rate changes to the rates set forth in Rate Schedules A, B, and C. Utility Co. does so, and submits the proposed rates to FERC on January 2, 2011, requesting an effective date of March 3, 2011—sixty days later. After FERC issues a notice of filing, wholesale customers of Utility Co.—W, X, and Y—file motions to intervene and protests to the proposed rate increases.[285] Z, a retail customer of W, also files a motion to intervene and protest. State Utility Commission intervenes and protests as well. FERC issues an order accepting the rates subject to refund, but suspending the effectiveness of the proposed rates for five months—until August 3, 2011—and instituting hearing procedures to investigate the justness and reasonableness of the proposed changes to the rates. However, FERC holds the hearing in abeyance and directs the parties to engage in settlement discussions.

After months of negotiations and bargaining, Utility Co. submits an offer of settlement to FERC with respect to Rate Schedules A and B. For Rate Schedule A, all parties—Utility Co., W, X, Y, Z, and State Utility Commission—have compromised and agreed to a smaller increase in the rate than proposed by Utility Co. For Rate Schedule B, Utility Co. has reached an agreement with W, X, and Z for a smaller rate increase than that originally proposed; however, Y and State Utility Commission object to the amount of the increase and do not join the settlement agreement with respect to Rate Schedule B. The settlement agreement stipulates that Utility Co. will not seek a rate increase with respect to Rate Schedules A and B for a period of five years after the effectiveness of the settlement rates[286]—that is, August 3, 2016. However, Utility Co. will be permitted to unilaterally seek a rate increase that may take effect no earlier than August 3, 2016. In addition, the settlement agreement states that the *Mobile-Sierra* presumption shall apply to any challenges to, or attempts to change, the rates for Rate Schedules A and B during the five year rate moratorium. Finally, no agreement is reached with respect to Rate Schedule C.

After the offer of settlement is presented to FERC,[287] FERC issues an order

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285. Each of W, X, and Y have executed individual service agreements under Utility Co.'s tariff.

286. One commenter has observed that "[i]t is remarkable that rate moratorium, a simple form of price cap regulation, arises endogenously from the settlement process of the traditional" rate cases. Wang, *supra* note 264, at 142. Although FERC is prohibited by the FPA and NGA from imposing a rate moratorium on the regulated utilities and pipelines, it "is free and willing to approve settlements with rate moratoria." *Id.*

287. When settlement discussions are before an ALJ, FERC's Rules of Practice and Procedure call for the ALJ to certify an offer of settlement to FERC. If, after comments are submitted on the offer of

finding that the rates for Rate Schedules A and B are fair and reasonable and in the public interest, notwithstanding the objections by Y and State Utility Commission with respect to Rate Schedule B.[288] Therefore, the rates set forth in the settlement agreement for Rate Schedules A and B take effect on the date contemplated by the five-month suspension—that is, August 3, 2011. FERC sets Rate Schedule C for hearing, and the parties proceed with trial-type hearing procedures before an ALJ to determine a just and reasonable rate. At the conclusion of the hearing, the ALJ determines that a rate increase is appropriate, but that the increase should be smaller than that proposed by Utility Co.[289] In a subsequent order, FERC approves of the ALJ's findings, and the new rate for Rate Schedule C goes into effect on August 3, 2011.

Suppose further that in July 2013, Utility Co. decides to seek a higher rate for services provided under Rate Schedule A and submits a proposed rate increase to FERC on July 15, 2013. FERC issues an order finding that Utility Co.'s rate filing is a legal nullity.[290] The rate for Rate Schedule A constitutes a BFR, agreed to in the settlement by Utility Co. and all interested parties.[291] Therefore, Utility Co. and the parties only possess the rights that are enumerated in the settlement agreement with respect to Rate Schedule A.[292] Utility Co.'s July 15 filing is similar to the proposed rate increase in *Mobile*, because Utility Co. does not have authority under the settlement agreement to unilaterally change the rate until August 3, 2016.[293] Because the *Mobile-Sierra* public interest presumption applies to Utility Co.'s proposed rate change, FERC may only permit the rate to be changed (prior to

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settlement, the ALJ determines that the settlement is uncontested, the ALJ shall certify to FERC that the offer of settlement is uncontested. *See* 18 C.F.R. § 385.602(g)(1). An uncontested offer of settlement may be approved by FERC upon a finding that the settlement appears to be fair and reasonable and in the public interest. *See id.* § 385.602(g)(3). If the ALJ determines that the offer of settlement is contested, either in whole or in part, the ALJ may certify all or part of the offer to FERC. *See id.* § 385.602(h)(2). If any part of the settlement is contested, it may be certified to FERC only if: (1) there are no genuine issues of material fact; or (2) the parties concur that the ALJ may omit preparation of an initial decision, and the record contains substantial evidence from which FERC may reach a reasoned decision on the merits of the contested issue. *See id.*

288. *See* Pennsylvania. Gas & Water Co. v. Fed. Power Comm'n, 463 F.2d 1242, 1247-52 (D.C. Cir. 1972) (finding that FERC may approve a rate settlement proposal and terminate proceedings over the objection of a participant in the proceeding, so long as there are no questions of material fact). In this situation, the ALJ could have certified as uncontested the offer of settlement as it relates to the rates in Rate Schedule A, severed from the contested offer of settlement with respect to Rate Schedule B. *See* 18 C.F.R. § 385.602(h)(2)(iv).

289. Subject to certain exceptions, at the conclusion of a hearing the ALJ who presides over the hearing shall prepare a written initial decision, which shall be certified to FERC with a copy of the record from the hearing. *Id.* at § 385.708.

290. *See* United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 347 (1956); Mun. Light Boards v. Fed. Power Comm'n 450 F.2d 1341, 1346 (D.C. Cir. 1971) (describing the Court in *Mobile* as rejecting United's rate filing as a nullity because United "had sought unilaterally to change a rate set by contract").

291. *See* Dominion Transmission, Inc. v. Fed. Energy Reg. Comm'n, 533 F.3d 845, 853-56 (D.C. Cir. 2008); *Maine PUC I*, *supra* note 19, at 476; Union Elec. Co. v. Fed. Energy Regulatory Comm'n, 890 F.2d 1193, 1194-95 (D.C. Cir. 1989); Cities of Newark v. Fed. Energy Regulatory Comm'n, 763 F.2d 533, 546-47 (3d Cir. 1985); Cities of Bethany v. Fed. Energy Regulatory Comm'n, 727 F.2d 1131, 1139 (D.C. Cir. 1984).

292. *See Mobile*, 350 U.S. at 343-44, 347.

293. *See id.* at 347.

August 3, 2016) if the change is required by the public interest.[294] FERC rejects the proposed change to the rate.[295]

Suppose that the following year, X and Y file complaints at FERC against Utility Co., alleging that the rates in Rate Schedule B are excessive. State Utility Commission believes that the rates paid by W under Rate Schedule B, some of which are passed on in retail rates to W's retail customer Z, are too high, resulting in excessive retail rates collected by W from Z. State Utility Commission also files a complaint with FERC against Utility Co., arguing that W is paying too much under Rate Schedule B. FERC consolidates all of these complaint proceedings because all complainants are challenging the rates in Rate Schedule B. In the consolidated proceedings, FERC must first determine whether the *Mobile-Sierra* public interest presumption automatically applies.

The public interest presumption must apply to the challenge made by X because X's rate is a BFR. The rate paid by X to Utility Co. is a BFR because Utility Co. and X agreed to that rate in the settlement agreement; therefore, FERC must apply the *Mobile-Sierra* public interest presumption to the challenge by X.[296]

Although the public interest presumption must apply to the challenge made by X, that is not the case with respect to the challenge made by Y. Y did not agree to the rate set forth in the settlement agreement for Rate Schedule B. Therefore, the rate paid by Y cannot be considered a BFR (even though it is the same rate paid by X). Because Y's rate is not a BFR, FERC would not automatically apply the public interest presumption to the challenge made by Y.

There may appear to be a conundrum: both X and Y pay the same rate under Rate Schedule B, yet X's rate is a BFR and Y's rate is not. However, this outcome is consistent with the principles underlying the *Mobile-Sierra* presumption—namely, that parties who have negotiated and agreed to a rate are bound to it. A BFR is established when both parties mutually agree to the rate, as when X and Utility Co. joined the settlement agreement,[297] and X bargained away the right to challenge its rate under Rate Schedule B prior to August 3, 2016. However, Y struck no such bargain and should not be bound by a contract term to which it did not agree. This may be administratively inconvenient for FERC, but it recognizes that each of a utility company's customers, including customers taking service pursuant to a tariff, have separate contractual agreements with the utility.[298]

In the case of the complaint filed by State Utility Commission, FERC must apply the *Mobile-Sierra* presumption to that challenge. Although State Utility

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294. *See id.* at 345; Fed. Power Comm'n v. Sierra Pac. Power Co., 350 U.S. 348, 355 (1956). *Sierra*'s three-pronged inquiry is set forth *supra*, at note 115.

295. The rate set forth in the settlement agreement remained the only lawful rate. *See Mobile*, 350 U.S. at 347.

296. *See Dominion Transmission*, 533 F.3d at 853-56; *Maine PUC I*, *supra* note 19, at 476; *Union Elec. Co.*, 890 F.2d at 1194-95; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139.

297. *See Dominion Transmission*, 533 F.3d at 853-56.

298. In a similar fashion, FERC has approved settlements among non-contesting parties while directing administrative hearings to determine the rate that would be paid by parties that did not join the settlement agreement. *See* United Gas Pipe Line Co., 22 FERC ¶ 61,094, *order on reh'g*, 23 FERC ¶ 61,101 (1983), *aff'd sub nom.* United Mun. Distribs. Group. v.Fed. Energy Regulatory Comm'n, 732 F.2d 202 (D.C. Cir. 1984); Potomac Edison Co., 17 FERC ¶ 61,167 (1981).

Commission did not join the settlement with respect to Rate Schedule B, State Utility Commission is not a customer of Utility Co. under Rate Schedule B. Therefore, State Utility Commission cannot argue that *it* is paying excessive rates under Rate Schedule B. Instead, State Utility Commission's complaint argues that the rates paid *by W* for service under Rate Schedule B are too high, in turn, resulting in excessive retail rates paid by Z to W. In *NRG*, the Supreme Court determined that the application of the public interest presumption does not depend on the identity of the challenger.[299] In this example, the *Mobile-Sierra* presumption would apply to State Utility Commission's challenge of W's rate because W was a party to the settlement agreement.[300] Therefore, under *NRG*, FERC and State Utility Commission must presume that W's rate is just and reasonable because W's rate is the result of negotiations that ended in settlement.[301]

C. Addressing NRG*'s Issues on Remand*

On remand, FERC was directed to determine whether the FCM auction market clearing prices should be considered "contract rates" (or BFRs) to which the *Mobile-Sierra* public interest presumption must apply.[302] And, if not, FERC was also directed to answer whether it possesses the discretion to apply the *Mobile-Sierra* presumption to such rates.[303] FERC determined that the rates were not BFRs.[304] Nonetheless, FERC believed that it "has discretion to consider and decide whether future challenges to rates should be evaluated under a more rigorous application of the statutory 'just and reasonable' standard of review."[305]

FERC's finding as to the first question was in error. The FCM auction produces BFRs. A BFR results from freely negotiated contracts,[306] including settlement agreements.[307] The ISO-NE's FCM is a unique creation that does not fit squarely within the traditional seller-purchaser contractual rubric. However, the

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299. *See* NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, ___, 130 S. Ct. 693, 696-97, 701 (2010).

300. *See Dominion Transmission*, 533 F.3d at 853-56; *Maine PUC I*, *supra* note 19, at 476; *Union Elec. Co.*, 890 F.2d at 1194-95; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139.

301. *See NRG*, 558 U.S. at ___, 130 S. Ct. at 700; *Dominion Transmission*, 533 F.3d at 853-56; *Maine PUC I*, *supra* note 19, at 476; *Union Elec. Co.*, 890 F.2d at 1194-95; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139.

302. *NRG*, 558 U.S. at ___, 130 S. Ct. 701; *Maine PUC II*, *supra* note 161, at 759-60. As noted above, *see supra* note 144, the rates at issue in *NRG* also included the transition payments.

303. *NRG*, 558 U.S. at ___, 130 S. Ct. at 701.

304. Devon Power LLC, 134 FERC ¶ 61,208, at P 2, 9, 13-14, 19 (2011); Devon Power LLC, 137 FERC ¶ 61,073, at P 21-28 (2011). *Cf.* Tewksbury, Lim & Su, *supra* note 98, at 445 n.89 (noting that there was "considerable disagreement about whether the [FCM] auctions at issue in *NRG* resulted in contract rates").

305. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 2, 9, 14-17 (quoted language at P 2).

306. Morgan Stanley Capital Group Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 530 (2008).

307. *See* Dominion Transmission, Inc. v. Fed. Energy Regulatory Comm'n, 533 F.3d 845, 853-56 (D.C. Cir. 2008); Maine Pub. Utils. Comm'n v. Fed. Energy Regulatory Comm'n, 520 F.3d 464, 476 (D.C. Cir. 2008); Union Elec. Co. v. Fed. Energy Regulatory Comm'n, 890 F.2d 1193, 1194-95 (D.C. Cir. 1989); Cities of Newark v. Fed. Energy Regulatory Comm'n, 763 F.2d 533, 546-47 (3d Cir. 1985); Cities of Bethany v. Fed. Energy Regulatory Comm'n, 727 F.2d 1131, 1139 (D.C. Cir. 1984).

principles outlined above can be used to determine the appropriate resolution to the Supreme Court's questions in *NRG*.

The FCM auction mechanism was set forth in the Settlement Agreement, which was agreed to by 107 of 115 participants in the *Devon Power* proceeding.[308] The Settlement Agreement was reached through painstaking negotiation and bargaining, and the settling parties agreed to the use of the auction mechanism to determine the price for capacity.[309] The results of the annual auctions are akin to the prices produced through the application of "formula rates." With a formula rate, "the formula itself is the rate."[310] As a utility's costs fluctuate over time, the costs can be plugged in to the formula to derive the resulting rate charged to customers. When FERC approves a formula rate, it is approving the formula, not the utility's inputs into the formula or the charges resulting from the application of the inputs into the formula.[311] One court of appeals has stated that a formula rate in a bilateral contract

> functions in many respects as a cost-of-service tariff. Rather than specifying a rate, it elucidates a formula for calculating a rate. The formula uses cost variables, or categories of costs, to measure most components . . . . As the utility's costs in each of these categories fluctuate, its charges vary proportionately, without the need for a rate change filing [pursuant to FPA section 205].[312]

As with a traditional formula rate, the Settlement Agreement in *Devon Power* and the ISO-NE tariff did not state what the auction clearing prices would be; rather, the Settlement Agreement established the FCM, under which the ISO-NE holds annual price-setting auctions for capacity.[313] The individual auction processes provide the inputs to the "formula" that result in the market clearing prices, i.e., the rates. Just as with formula rates, approval by FERC of the Settlement Agreement permitted the auction mechanism to go into effect.

The auction mechanism was established through a settlement that was reached by 107 parties in *Devon Power*.[314] As such, the FCM's auction process and the prices it produces constitute BFRs for those 107 parties.[315] The *Mobile-Sierra* public interest presumption should apply to challenges to capacity prices derived from FCM auctions paid by the 107 settling parties.[316]

With respect to the rates paid by the eight parties that did not join the settlement in *Devon Power* (if they are electric utilities that need to acquire

308. Devon Power LLC, 115 FERC ¶ 61,340, at 62,306 (2006).

309. *Id.*

310. *See* MCGREW, *supra* note 25, at 185.

311. *See id.* at 186.

312. Boston Edison Co. v. Fed. Energy Regulatory Comm'n, 856 F.2d 361, 366 (1st Cir. 1988) (citation to contract omitted).

313. *See Devon Power LLC*, 115 FERC ¶ 61,340, at 62,304, 62,306-08.

314. *Id.* at 62,306.

315. *See Dominion Transmission*, 533 F.3d at 853-56; *Maine PUC I*, *supra* note 19, at 476; *Union Elec. Co.*, 890 F.2d at 1194-95; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139. *But cf.* Tewksbury, Lim & Su, *supra* note 98, at 447 (suggesting that the FCM auction rates are not BFRs because they are not traditional fixed-rate contracts).

316. *See Dominion Transmission*, 533 F.3d at 853-56; *Maine PUC I*, *supra* note 19, at 476; *Union Elec. Co.*, 890 F.2d at 1194-95; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139.

capacity), the *Mobile-Sierra* public interest presumption would not (automatically) apply to challenges to their rates. Purchasers that did not join the Settlement Agreement must pay a price for capacity that was not the result of those purchasers' negotiations and assent. Therefore, the FCM auction mechanism and the resulting prices are not BFRs with respect to those purchasers.

It should be noted that if the challenger is not a capacity purchaser—for example, a state utility commission—the challenge is, inherently, to the price paid by some purchaser for capacity. As *NRG* made clear, application of the presumption does not depend on the identity of the *challenger*.[317] Rather, the inquiry turns on the nature of the agreement challenged. If a state utility commission challenges the price for capacity paid by a purchaser who was a party to the Settlement Agreement, then FERC should presume that the purchaser's rate was just and reasonable because the rate and the auction mechanism that led to the rate were the result of fair negotiations and voluntary agreement.[318] If the challenge is to a price paid by a purchaser that was *not* a party to the Settlement Agreement, the public interest presumption would not automatically apply.

FERC's orders on remand did not consider that the Settlement Agreement imbues the auction rates with the characteristics of BFRs. Instead, FERC focused on the FCM auction itself, finding that it produced rates that are "determined unilaterally by the ISO-NE tariff" because the ISO-NE assesses the purchasing utilities their respective capacity charges based on the FCM auction's market clearing prices.[319] FERC ignored the role of the settling parties in establishing the FCM. Although the ISO-NE's role in assessing capacity charges is set forth in the ISO-NE's tariff, it does not necessarily follow that the capacity charges constitute unilateral rates. When a utility offers services under a traditional tariff, the utility assesses charges to its customers. However, as explained above, not every rate set forth in a tariff is a unilateral rate. When a rate is the result of a successful settlement—that is, negotiation, bargaining, and mutual agreement—the rate is a BFR.[320] In *Devon Power*, 107 parties agreed to the FCM and its auction mechanism.[321] Therefore, the capacity charges that result from the FCM's auction paid by those 107 parties are BFRs.[322]

In the order addressing requests for rehearing, FERC noted that "ISO-NE's tariff does not create a contractual obligation by buyers to purchase capacity from

317. NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, ___ 130 S. Ct. 693, 696-97, 701 (2010).

318. *See Dominion Transmission*, 533 F.3d at 853-56; *Maine PUC I*, *supra* note 19, at 476; *Union Elec. Co.*, 890 F.2d at 1194-95; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139.

319. Devon Power LLC, 134 FERC ¶ 61,208, at P 13 (2011); Devon Power LLC, 137 FERC ¶ 61,073, at P 21-22 (2011).

320. *See Dominion Transmission*, 533 F.3d at 853-56; *Maine PUC I*, *supra* note 19, at 476; *Union Elec. Co.*, 890 F.2d at 1194-95; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139.

321. Devon Power LLC, 115 FERC ¶ 61,340, at 62,306 (2006).

322. For the participants that did not agree to the settlement, FERC is correct that the rates should not be considered BFRs. *See Devon Power LLC*, 134 FERC ¶ 61,208, at P 13; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 25.

sellers of that capacity."[323] This does not mean that the capacity charges are unilateral rates. With an ordinary tariff, the existence of the tariff does not obligate any entity to become a customer of the utility or to take particular services or purchase particular quantities. However, if a customer purchases a product or service offered through a tariff, the customer is obligated to pay the price set forth in the tariff. Here, utilities in New England must procure certain quantities of capacity.[324] If the utilities do not self-supply the capacity or procure it from another source, they must purchase capacity through the FCM.[325] Although the auctions do not create an obligation for the utilities to purchase, the auctions set the prices for utilities purchasing capacity through the FCM. If the utilities purchase capacity through the FCM, they are obligated to pay the price set through the auction process, just as a customer under a traditional tariff is obligated to pay the rate set forth in the tariff or the rate derived through a formula set forth in the tariff. Whether the rates are BFRs turns on whether the rate was the result of purely unilateral rate setting or through negotiations and bargaining.

Turning to the second question on remand, FERC was directed to answer, if the FCM auction rates were not BFRs, whether FERC "ha[s] discretion to treat them analogously" to BFRs.[326] FERC stated that it "has discretion to consider and decide whether future challenges to rates should be evaluated under a more rigorous application of the statutory 'just and reasonable' standard of review" and that future challenges to the FCM's auction prices would be subject to a "more rigorous application."[327] In reaching this decision, FERC relied on the fact that the rates resulting from the FCM auctions would have certain market-based characteristics, similar to freely-negotiated contracts to which the *Mobile-Sierra* public interest presumption must apply.[328] FERC also noted that a more rigorous application of the just and reasonable standard would promote rate stability, an important issue because of the variable nature of capacity revenues and the effect of that instability on generating units in New England.[329]

It should first be noted that, had FERC answered the first remanded question properly, it would not have needed to address the second remanded question with respect to the rates paid by the 107 parties to the Settlement Agreement because challenges to those rates should be automatically subject to the *Mobile-Sierra* public interest presumption. However, the question remains whether a more stringent application of the just and reasonable standard—such as the public interest presumption—can and should be applied to challenges to the rates paid by non-settling parties.

FERC's affirmative answer may be considered both incorrect and premature.

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323. *Devon Power LLC*, 137 FERC ¶ 61,073, at P 24.

324. *See Devon Power LLC*, 115 FERC ¶ 61,340, at 62,304.

325. *See id*. at 62,307; *see also Maine PUC I*, 520 F.3d at 469; NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, ___, 130 S. Ct. 693, 697 (2010).

326. *NRG*, 558 U.S. at ___, 130 S. Ct. at 701; *Maine PUC II*, *supra* note 161, at 759-60 (directing FERC to answer "why, if the auction rates are not [BFRs], they are entitled to *Mobile-Sierra* treatment").

327. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 2, 9, 14-17 (quoted language at P 2).

328. *Id.* at P 19; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 32.

329. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 20.

FERC was incorrect insofar as it purported to determine that a more rigorous application of the just and reasonable standard will *automatically* apply to future challenges to the rates paid by non-settling parties.[330] The automatic application of the *Mobile-Sierra* public interest standard to BFRs is appropriate because it respects the intent of the parties that negotiated the agreement.[331] However, where the challenged rate is not a BFR, as would be the case for rates paid by the non-settling parties in *Devon Power*, the rationale underlying the application of the *Mobile-Sierra* public interest presumption does not apply.[332] In *Devon Power*, the non-settling participants did *not* agree to the FCM auction, and did *not* agree to the application of the public interest presumption to challenges to their rates. In essence, FERC is attempting to bind the non-settling participants to the terms of the Settlement Agreement. In this way, FERC's response to the Supreme Court's second remand question may be considered to be incorrect.

FERC's response is also premature because FERC should determine whether a "more rigorous" application of the just and reasonable standard should apply to a challenge of an FCM auction rate paid by a non-settling participant at the time such a challenge is brought. Although FERC is correct that the FPA does not directly address how the "just and reasonable" standard should be applied or implemented in any particular context,[333] FERC can better determine at the time the challenge is made whether a more rigorous application of the just and reasonable standard is appropriate. In the orders on remand, FERC has offered reasons why it believes that challenges to the FCM auction results should be subject to application of the public interest presumption, including challenges to rates paid by non-settling parties.[334] There may be situations in which it is appropriate for FERC to apply a presumption to challenges of rates that are not BFRs; however, an examination of the possible application of the public interest presumption outside of the BFR context is beyond the scope of this article.[335] Because the auction rates paid by non-settling participants are not BFRs and application of a presumption would not

330. *See id.* at P 17-25. It is not clear whether FERC considers the more rigorous application of the just and reasonable standard that would be applied in FERC's discretion to be *Mobile-Sierra*'s "public interest" presumption, or a different (yet similar) application. One set of commenters believes that FERC has drawn distinctions between the public interest presumption and the new discretionary application. *Cf.* Tewksbury, Lim & Su, *supra* note 98, at 451-52.

331. FERC believed that the Settlement Agreement might not have been reached without the inclusion of the public interest presumption in section 4.C. *Devon Power LLC*, 137 FERC ¶ 61,073, at P 35. This purported rationale should be inapposite because the FCM auction produces BFRs for the parties to the Settlement Agreement; as such, the *Mobile-Sierra* public interest presumption would apply automatically to challenges, regardless of whether a *Mobile-Sierra* clause was included in the Settlement Agreement.

332. *See Devon Power LLC*, 134 FERC ¶ 61,208, at 62,048 (Norris, dissenting in part) ("[It is not] reasonable to . . . apply the more stringent public interest form of the just and reasonable standard dictated by the [public interest] presumption to situations where a contract [or BFR] is not present.").

333. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 15; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 30.

334. FERC stated that the FCM auction rates would be presumed to be just and reasonable because the rates would share certain market-based characteristics with freely-negotiated contracts. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 19; *Devon Power LLC*, 137 FERC ¶ 61,073, at P 32.

335. For a more expansive discussion of FERC's authority to apply a more rigorous application of the just and reasonable standard, *see* Tewksbury, Lim & Su, *supra* note 98, at 446-58.

be based on the negotiations and bargaining of the parties, FERC should not have determined in advance whether a presumption shall apply to future challenges of those rates. In this regard, FERC's answer to the second remanded question may be considered premature.

V. PRACTICAL CONSEQUENCES OF FERC'S ORDERS ON REMAND IN *DEVON POWER LLC*

It may at first appear that there is little practical difference between FERC's resolution of the issues remanded by the Supreme Court and the proposed resolution of those issues put forth by this article. In *Devon Power*, FERC found that even though the FCM auction rates were not BFRs (or "contract rates"), FERC could exercise its discretion to approve a settlement provision that would impose the *Mobile-Sierra* public interest presumption on future challenges to the auction results.[336] On the other hand, this article has explained that, for the parties to the Settlement Agreement, the auction results are BFRs and the *Mobile-Sierra* public interest presumption should apply to challenges to the rates paid by the 107 settling parties;[337] however, the public interest presumption would not automatically apply to challenges to the rates paid by the eight participants that objected to the Settlement Agreement. Thus, with respect to the participants in the *Devon Power* proceeding, FERC and this article agree that the *Mobile-Sierra* presumption should apply to future challenges to the rates paid by the 107 parties to the Settlement Agreement. FERC has also determined in advance that it will apply the public interest presumption to future challenges to auction prices paid by the eight non-settling parties, while this article suggests that any such determination should be made if and when such a challenge arises.

Notwithstanding the practical similarity between the outcome for the participants in *Devon Power* and the outcome that would arise following the analysis in this article, FERC's *Devon Power* precedent will have significant consequences on regulated utilities. The impact of FERC's determination will be felt most significantly in proceedings that are resolved through settlement. The Settlement Agreement in *Devon Power* resolved a unique situation. Routine changes to rates set forth in tariffs and bilateral agreements will arise more frequently than issues associated with the New England capacity market that was the subject of the controversy in *Devon Power*.

Since issuing its order on remand in *Devon Power*, FERC has addressed the inclusion of so-called "*Mobile-Sierra* clauses" in uncontested settlement agreements resolving proceedings to change rates set forth in tariffs several times.[338] In the post-*Devon Power* cases, FERC found that because the rates at

336. *Devon Power LLC*, 134 FERC ¶ 61,208, at P 2, 9, 14-17.

337. *See* Dominion Transmission, Inc. v. Fed. Energy Regulatory Comm'n, 533 F.3d 845, 853-56 (D.C. Cir. 2008); Maine Pub. Utils. Comm'n I, 520 F.3d 464, 476 (D.C. Cir. 2008); Union Elec. Co. v. Fed. Energy Regulatory Comm'n 890 F.2d 1193, 1194-95 (D.C. Cir. 1989); Cities of Newark v. Fed. Energy Regulatory Comm'n, 763 F.2d 533, 546-47 (3d Cir. 1985); Cities of Bethany v. Fed. Energy Regulatory Comm'n, 727 F.2d 1131, 1139 (D.C. Cir. 1984).

338. *See HIOS, supra* note 185; Petal Gas Storage, LLC, 135 FERC ¶ 61,152 (2011); Southern LNG Co., 135 FERC ¶ 61,153 (2011); *Carolina Gas, supra* note 185; *SCEG, supra* note 185; *FP&L, supra* note 185. A *Mobile-Sierra* clause states that future challenges to the terms of the agreement shall be

issue were set forth in tariffs, the rates were not BFRs, even though the proceedings were resolved through settlement. Although the settling parties could impose the *Mobile-Sierra* public interest presumption on future challenges to the rates paid by the settlement parties, FERC directed the settlement parties to modify their settlement agreements so as not to impose the "public interest" presumption on future challenges or changes proposed by FERC acting *sua sponte* or non-settling parties.[339] In these cases, FERC found that the individual circumstances in those cases "did not rise to the compelling level of those present in *Devon Power* so as to warrant binding [FERC] and non-settling third parties to a more rigorous application of the statutory 'just and reasonable' standard of review."[340]

Based on the analysis set forth above, FERC has erred in these cases by finding that the settlement agreements produced unilateral rates (or "tariff rates") rather than BFRs (or "contract rates").[341] A voluntary settlement among the participants of a FERC proceeding is the result of negotiations and bargaining,[342] even though those negotiations did not take place prior to the filing of the proposed rate change. Therefore, rates set forth in settlement agreements are BFRs for the customers that have joined the settlement agreement, and the *Mobile-Sierra* public interest presumption should apply to challenges to those BFRs.[343] However, the rates would not be BFRs for entities that were not parties to the settlement agreement.

For example, in *South Carolina Elec. & Gas Co.* ("*SCEG*"), SCEG submitted to FERC a settlement agreement that was the result of negotiations between SCEG and four customers.[344] As described above, FERC stated that the settlement agreement related to a tariff rate—not a BFR—and that FERC would use its discretion not to impose a more rigorous application of the just and reasonable

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subject to the *Mobile-Sierra* public interest presumption. As explained above, the inclusion of such clauses should be unnecessary because a settlement agreement produces a BFR and the public interest presumption automatically applies to a challenge to a BFR. However, the current practice is to include *Mobile-Sierra* clauses in settlement agreements, indicating the parties' wish for the public interest presumption to apply to future challenges to the settlement rates.

339. *HIOS, supra* note 185, at P 1; *Petal Gas*, 135 FERC ¶ 61,152 at P 1; *Southern LNG*, 135 FERC ¶ 61,153 at P 1; *Carolina Gas*, *supra* note 185, at P 1; *SCEG, supra* note 185, at P 5-6; *FPL, supra* note 185, at P 11-12.

340. Devon Power LLC, 137 FERC ¶ 61,073, at P 36 (2011). *See HIOS, supra* note 185, at P 5 24; *Petal Gas*, 135 FERC ¶ 61,152 at P 17; *S. LNG*, 135 FERC ¶ 61,153 at P 24; *Carolina Gas*, *supra* note 185, at P 17; *SCEG, supra* note 185, at P 5; *FP&L, supra* note 185, at P 11.

341. *See HIOS, supra* note 185, at P 19; *Petal Gas*, 135 FERC ¶ 61,152 at P 12; *Southern LNG*, 135 FERC ¶ 61,153 at P 19; *Carolina Gas*, *supra* note 185, at P 17; *SCEG*, *supra* note 185, at P 5; *FP&L, supra* note 185, at P 11.

342. *See, e.g.*, *SCEG*, *supra* note 185, at P 1 (stating that the settlement agreement was the result of negotiations between South Carolina Electric & Gas and its customers and resolved all the issues that were set for hearing).

343. *See* Dominion Transmission, Inc. v. Fed. Energy Regulatory Comm'n, 533 F.3d 845, 853-56 (D.C. Cir. 2008); *Maine PUC I*, *supra* note 19, at 476; Union Elec. Co. v. Fed. Energy Regulatory Comm'n, 890 F.2d 1193, 1194-95 (D.C. Cir. 1989); Cities of Newark v. Fed. Energy Regulatory Comm'n, 763 F.2d 533, 546-47 (3d Cir. 1985); Cities of Bethany v. Fed. Energy Regulatory Comm'n, 727 F.2d 1131, 1139 (D.C. Cir. 1984).

344. *SCEG*, *supra* note 185, at P 1. The four customers were Central Electric Power Cooperative, Inc., North Carolina Electric Membership Corporation, the City of Orangeburg, South Carolina, and the Town of Winnsboro, South Carolina. *Id.*

standard to future challenges to the settlement brought by FERC or non-settling third parties.[345] This determination was error. The rate set forth in the settlement agreement in *SCEG* constitutes a BFR between SCEG and the four customers that joined the settlement agreement. If any entity challenges the rate paid by one of those four customers pursuant to the settlement agreement, the *Mobile-Sierra* public interest presumption should apply to that challenge, whether the challenge is brought by one of the four customers, FERC, or a non-party to the settlement.[346] As the Supreme Court explained in *NRG*, application of the *Mobile-Sierra* presumption does not depend upon the identity of the person challenging the rate at issue—i.e., whether the challenger is a party to contested agreement, or a third-party.[347]

The situation created by FERC in *SCEG* and other proceedings is likely to be repeated in cases that are resolved through settlement agreements. The effects may be far-reaching because 80 to 90 percent of all rate proceedings set for hearing at FERC are resolved through settlement.[348] When FERC determines that a rate set forth in a settlement agreement is not a BFR to which the *Mobile-Sierra* public interest presumption automatically applies, FERC will likely further determine that it and non-parties to the settlement are free to challenge the rate paid by settlement parties without presuming that the rates are just and reasonable.[349] Just as in *SCEG*, these findings will be contrary to the principle that rates set forth in settlement agreements are BFRs and the holding from *NRG*—namely, that application of the *Mobile-Sierra* presumption does not depend upon the identity of the person challenging the rate.[350] In these cases, the bargain struck by the parties to the settlement agreement will be subject to being overturned by challenges brought by FERC or non-parties to the settlement agreement. Furthermore, FERC may be forced to re-visit issues that should have been finalized by settlement agreements. This compromises the stability that is purported to be undergirded by the FPA's agreement-based regulatory regime.

It should be noted that if there were another customer under the tariff at issue in *SCEG*—a customer that was not a party to the settlement agreement—that third-party customer could challenge the rate *it* pays under its own service agreement with SCEG without application of the public interest presumption to that challenge. This inconvenient situation may arise where a rate set forth in a tariff may be subject to differing applications of the just and reasonable standard depending on which *customer's rate* is being challenged: a settlement party's rate, or a third party's rate. Although this is not the most convenient way for FERC or utilities to

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345. *SCEG*, *supra* note 185, at P 5.

346. NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n, 558 U.S. 165, ___, 130 S.Ct 693, 696-97, 701 (2010); *see Dominion Transmission*, 533 F.3d at 853-56; *Maine PUC I*, *supra* note 19, at 476; *Union Elec. Co.*, 890 F.2d at 1194-95; *Cities of Newark*, 763 F.2d at 546-47; *Cities of Bethany*, 727 F.2d at 1139.

347. *NRG*, 558 U.S. at ___, 130 S. Ct. at 696-97.

348. FEDERAL ENERGY REGULATORY COMMISSION, FISCAL YEAR 2012 CONGRESSIONAL PERFORMANCE BUDGET REQUEST 75, 78 (2011), *available at* http://www.ferc.gov/about/strat-docs/FY12-budg.pdf.

349. *SCEG*, *supra* note 185, at P 5; *see also* Tewksbury, Lim & Su, *supra* note 98, at 455 ("FERC may be disinclined to grant settling parties heightened protections for extended periods.").

350. *NRG*, 558 U.S. at ___, 130 S. Ct. at 696-97, 701.

deal with challenges to rates, it respects the wishes of parties to settlement agreements, adheres to the principle of contract stability, and properly recognizes that settlement agreements should automatically be subject to the *Mobile-Sierra* presumption because they are the result of negotiation and bargaining.

VI. CONCLUSION

FERC's orders on remand in *Devon Power* and its subsequent orders addressing settlements have failed to recognize that settlement agreements are the result of negotiation and bargaining. FERC believed that it does not need to apply the *Mobile-Sierra* public interest presumption to future challenges to settlement rates. The effects of FERC's erroneous findings are potentially far-reaching because of the number of rate disputes that are resolved through settlement.

Parties to a settlement negotiate, often painstakingly, to reach a resolution that is agreeable to all parties. And, parties on both sides may "call that a bargain. The best [they] ever had."[351] The public interest presumption is intended to preserve for parties the benefits of their bargains and to provide much-needed stability to electric industry participants. FERC has undermined these goals. If *Devon Power* is not corrected by the courts, FERC and the electric industry will continuously confront the effects of this decision.

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351. THE WHO, *Bargain*, *on* WHO'S NEXT (Decca 1971).