American Bar Association
www.supremecourtpreview.org

No. 08-674

IN THE
Supreme Court of the United States

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

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

BRIEF FOR PETITIONERS

MICHAEL R. BRAMNICK
General Counsel
CHRISTOPHER C. O'HARA
Assistant General Counsel
NRG ENERGY, INC.
211 Carnegie Center Drive
Princeton, NJ 08540
(609) 524-4601

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

JEFFREY A. LAMKEN
ROBERT K. KRY
BAKER BOTTS L.L.P.
1299 Pennsylvania Ave., N.W.
Washington, D.C. 20004
(202) 639-7700

Counsel for Petitioners

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

QUESTION PRESENTED

The Federal Power Act, 16 U.S.C. §§ 791a *et seq.*, requires that rates for the sale of electricity in interstate commerce be "just and reasonable." Under the *Mobile-Sierra* doctrine—named for this Court's decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956)—the Federal Energy Regulatory Commission ("FERC") must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737 (2008). In the decision below, the court of appeals held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply." Pet. App. 22a. The question presented is:

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

PARTIES TO THE PROCEEDINGS BELOW

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

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

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

Respondents Maine Public Utilities Commission, the Attorney General of Massachusetts, and the Attorney General of Connecticut were the petitioners in the court of appeals and parties before the Federal Energy Regulatory Commission.

Respondents Industrial Energy Consumer Group, NEPOOL Industrial Customer Coalition, and NSTAR Electric & Gas Corp. were intervenors in the court of appeals and parties before the Federal Energy Regulatory Commission.

CORPORATE DISCLOSURE STATEMENT

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

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

Page

CASES

TABLE OF AUTHORITIES—Continued

Page

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

Page

TABLE OF AUTHORITIES—Continued

IN THE
Supreme Court of the United States

NO. 08-674

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

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

BRIEF FOR PETITIONERS

DECISIONS BELOW

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

JURISDICTION

The court of appeals entered judgment on March 28, 2008. The court denied rehearing and rehearing *en banc* on October 6, 2008. Pet. App. 241a-248a. The petition for a writ of certiorari was filed November 21, 2008, and granted April 27, 2009. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Relevant provisions of the Federal Power Act, ch. 687, 49 Stat. 803 (1935) (codified as amended at 16 U.S.C. §§ 791a *et seq.*), are set forth at Pet. App. 251a-261a.

INTRODUCTION

The *Mobile-Sierra* doctrine requires the Federal Energy Regulatory Commission ("FERC") to "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737 (2008). That presumption can be overcome only in "extraordinary circumstances where the public will be severely harmed." *Id.* at 2749. Those longstanding restrictions on FERC's authority to set aside contract rates reflect the critical importance of contract stability in volatile energy markets, where suppliers must routinely commit hundreds of millions of dollars to build generating capacity—investments that can take decades to recover. "Competitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co.* v. *Duke Energy Trading & Mktg., L.L.C.*, 99 F.E.R.C. ¶ 61,047, at 61,190 (2002). "By preserving the integrity of contracts," *Mobile-Sierra* "permits the stability of supply arrangements which all agree is essential to the health of the * * * industry." *United Gas Pipe Line Co.* v. *Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956).

The court below held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-*

Sierra doctrine simply does not apply." Pet. App. 22a. Under that holding, *Mobile-Sierra* protects contracts from challenges by a contracting counterparty, but *any other entity* indirectly affected by a contract rate—any consumer, advocacy group, state utility commission, or elected official acting *parens patriae*—can challenge the rate without regard to *Mobile-Sierra*'s protections. Because that holding is inconsistent with this Court's precedents and threatens to reduce *Mobile-Sierra* to a historical footnote, the judgment below should be reversed.

STATEMENT

I. STATUTORY BACKGROUND

A. The Federal Power Act

The Federal Power Act ("FPA"), 16 U.S.C. §§ 791a *et seq.*, gives FERC exclusive authority to regulate the "sale of electric energy at wholesale in interstate commerce." 16 U.S.C. § 824(b)(1); see *New England Power Co.* v. *New Hampshire*, 455 U.S. 331, 340 (1982). The Act provides that "[a]ll rates and charges" subject to FERC's jurisdiction "shall be just and reasonable," and declares that any "rate or charge that is not just and reasonable is * * * unlawful." 16 U.S.C. § 824d(a). The Act also forbids any "undue preference or advantage" or any "unreasonable difference" in rates. *Id.* § 824d(b).

Traditionally, wholesale energy rates have been set in two ways. First, a supplier may set rates "unilaterally by tariff," offering to sell electricity to buyers on terms the supplier determines. See *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737-2738 (2008). Alternately, buyers and sellers can agree on rates by "contract." See *id.* at 2738.

Consistent with those two methods, Section 205 of the FPA requires suppliers to file with the Commission "schedules showing all rates and charges," together with "all contracts" related to the suppliers' rates. 16 U.S.C. §§ 824d(c), (d). FERC need not approve the filing for a rate to become effective. But FERC may conduct a hearing into the rate's lawfulness "either upon complaint or upon its own initiative without complaint," and can reject any rate it finds unlawful. See *id.* § 824d(e).

While Section 205 authorizes FERC to reject new rates, Section 206 empowers FERC to modify existing ones: "Whenever the Commission, after a hearing held upon its own motion or upon complaint, shall find that any rate * * * or contract affecting such rate * * * is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate * * * or contract * * * and shall fix the same by order." 16 U.S.C. § 824e(a). FERC can order refunds of certain amounts paid after such a proceeding begins. *Id.* § 824e(b).

B. The *Mobile-Sierra* Doctrine

The *Mobile-Sierra* doctrine originated in this Court's twin decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) ("*Mobile*"), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*"). Those cases interpreted the statutory phrase "just and reasonable" in the context of rates set by the parties through contract rather than by the seller through unilateral tariff.

1. In *Mobile*, a natural gas supplier (United) had contracted to provide gas to a distributor (Mobile) for ten years at a fixed rate. 350 U.S. at 335-336.[1] Several years

---

[1] Although *Mobile* arose under the Natural Gas Act rather than the FPA, see 350 U.S. at 333-337, the two statutes are "virtually identical" in relevant respects, *id.* at 346, and this Court's "established

into the contract, United filed schedules with the Federal Power Commission (FERC's predecessor) purporting to raise Mobile's rates. *Id.* at 336. This Court held the filing invalid. *Id.* at 347. The Act, the Court stated, "evinces no purpose to abrogate private rate contracts." *Id.* at 338. "To the contrary, by requiring contracts to be filed with the Commission, the Act expressly recognizes that rates to particular customers may be set by individual contracts." *Ibid.* The Act thus differed from statutes such as the Interstate Commerce Act, which required uniform tariffs. See *id.* at 338-339. "Absent the Act," the Court noted, "a unilateral announcement of a change to a contract would of course be a nullity." *Id.* at 339. The statutory filing requirement did not affect that result. "Th[at] section says only that a change *cannot* be made without the proper notice to the Commission; it does not say under what circumstances a change *can* be made." *Ibid.*

The Court explained that, although the Act authorizes the *Commission* to modify contract rates, the Commission can exercise that power only "when necessary in the public interest"—not for the "private interests" of the contracting parties. See 350 U.S. at 344. "By preserving the integrity of contracts," the Act "permits the stability of supply arrangements which all agree is essential to the health of the natural gas industry." *Ibid.* Contracting parties must often undertake "substantial investments which [they] would be unwilling to make without long-term commitments." *Ibid.* "[A]nd the distributor can hardly make such commitments if its supply contracts are subject to unilateral change by the natural gas com-

practice" is to "cit[e] interchangeably decisions interpreting the pertinent sections of the two statutes," *Ark. La. Gas Co.* v. *Hall*, 453 U.S. 571, 577 n.7 (1981).

pany whenever its interests so dictate." *Ibid.* United's filing was thus a "nullity," and "the contract rate remained the only lawful rate." *Id.* at 347.

2. Announced the same day as *Mobile*, *Sierra* involved an electricity supplier's similar attempt to raise rates several years into a contract. 350 U.S. at 351-352. The Commission had allowed the new rate to take effect, commenting that the contract rate was "'unreasonably low and therefore unlawful'" because it produced an inadequate return. *Id.* at 352, 354. Citing *Mobile*, the Court found the unilateral filing ineffective under Section 205. *Id.* at 353. Unlike in *Mobile*, however, the Commission had found the prior rate "unlawful," arguably exercising its Section 206 power to set aside unjust or unreasonable rates. See *ibid.*

This Court held that the Commission had erred by deeming the contract rate unreasonable "solely because it yield[ed] less than a fair return." 350 U.S. at 354-355. "[W]hile it may be that the Commission 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." *Id.* at 355. "[T]he sole concern of the Commission 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." *Ibid.* (emphasis added). The Court held that "the purpose of the power given the Commission by § 206(a) is the protection of the public interest, as distinguished from the private interests of the utilities." *Ibid.* Accordingly, "a contract may not be said to be either 'unjust' or 'unreasonable' simply because it is unprofitable to the public utility." *Ibid.*

3. That principle—that FERC cannot abrogate contract rates absent a sufficient showing of harm to the "public interest" (as opposed to the private interests of contracting parties)—has come to be known as the "*Mobile-Sierra*" doctrine. Just two Terms ago, in *Morgan Stanley Capital Group Inc.* v. *Public Utility District No. 1*, 128 S. Ct. 2733 (2008), this Court reiterated that *Mobile-Sierra* requires FERC to "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that this "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Id.* at 2737. The Court held that the demanding standard applicable to contract rates—known as the "public interest standard"—applies whether the complainant urges that the price is too high or too low. See *id.* at 2747-2749. And the Court rejected the Ninth Circuit's ruling that the more flexible standard applicable to a seller's unilateral tariff (best referred to as the "ordinary just-and-reasonable standard," see *id.* at 2740) applies to contract rates absent FERC's prior approval of the contract at issue. See *id.* at 2745-2747.

The *Mobile-Sierra* doctrine reflects "the commonsense notion that '[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.'" *Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon Commc'ns Inc.* v. *FCC*, 535 U.S. 467, 479 (2002)). It also reflects the "important role of contracts in the FPA" in providing a "key source of stability" that "ultimately benefits consumers." *Id.* at 2749. "'[U]ncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm customers in the long run.'" *Ibid.* (quoting *Market-Based Rates*, 72 Fed. Reg. 39,904, 39,906 (2007)).

Consistent with *Mobile-Sierra*'s emphasis on contracts, an agreement can *prescribe* a more lenient standard under which FERC (or the parties) can modify the agreed-upon rates. See *Morgan Stanley*, 128 S. Ct. at 2739. Such provisions are known as "*Memphis* clauses," after *United Gas Pipe Line Co.* v. *Memphis Light, Gas & Water Division*, 358 U.S. 103 (1958). Absent a *Memphis* clause, however, FERC's authority is limited: FERC can abrogate contract rates only in "extraordinary circumstances where the public will be severely harmed." *Morgan Stanley*, 128 S. Ct. at 2749.

II. THIS LITIGATION

A. The New England Capacity Market

This case arises out of efforts to ensure that New England has sufficient electrical generating capacity to meet demand. Roughly speaking, "capacity" is the *ability* to produce electricity as opposed to electricity itself. See *Conn. Dep't of Pub. Util. Control* v. *FERC*, Nos. 07-1375 *et al.*, 2009 WL 1754607, at *1 (D.C. Cir. June 23, 2009). Utilities purchase capacity from generators to ensure that the system has adequate electricity resources to meet demand at all times, averting blackouts or other reliability problems. See Pet. App. 2a. A utility purchasing capacity is essentially paying to ensure that electricity is available whether or not that electricity is ultimately used. See *ibid.*

New England's electric utilities have long integrated their transmission systems so that capacity in one area can be used to meet demand elsewhere. See, *e.g.*, *NEPOOL Power Pool Agreement*, 48 F.P.C. 538 (1972). In 1998, they created an independent entity—the New England Independent System Operator ("ISO-NE")—to manage those systems. See Pet. App. 3a & n.2; *New England Power Pool*, 83 F.E.R.C. ¶ 61,045 (1998).

New England's capacity market, however, was "rife with problems." Pet. App. 2a. The incentives to retain or attract generating capacity were insufficient. "'[E]xisting generators needed for reliability [we]re not earning sufficient revenues (and [we]re in fact losing money), and * * * additional infrastructure [wa]s needed soon to avoid violations of reliability criteria.'" *Ibid.* That deficiency had "persisted and gr[own]." *Id.* at 99a.

B. Proceedings Before FERC

ISO-NE struggled to resolve those problems. See Pet. App. 2a-5a. FERC largely rejected one approach, involving so-called "Reliability Must-Run" agreements, in 2003. See *id.* at 2a-3a. A FERC administrative law judge approved another proposal, which set prices using an "administratively-determined demand curve," in 2005. See *id.* at 4a-5a. But it too was "extremely controversial." *Id.* at 4a.

1. *The Settlement Agreement*

Finally, after four months of negotiations involving 115 parties, a settlement was reached. Pet. App. 110a. Of the 115 parties, eight opposed the settlement. *Ibid.* And only one of those eight—NSTAR Electric and Gas Corporation—is a utility that participates in the wholesale capacity market. See *id.* at 121a n.32. The other seven objectors—the Maine Public Utilities Commission and Public Advocate, the attorneys general of Connecticut and Massachusetts, two industrial consumer interest groups, and a consortium—are all at most indirectly affected by wholesale rates. See *id.* at 120a-121a & nn.31-32, 144a. A wide array of parties supported the settlement, including a host of power-purchasing utilities and power-supplying generators, ISO-NE, the Connecticut Department of Public Utility Control and Office of Consumer Counsel, and the public utility commissions of New Hampshire, Rhode Island, and Vermont. See *id.* at 220a-221a; J.A. 89-91.

To redress the market's prior failure to attract sufficient capacity, the agreement created a "Forward Capacity Market" in which annual auctions are used to meet demand. See Pet. App. 110a-116a; J.A. 97-160. Each auction takes place three years before the capacity will be needed. J.A. 98. Suppliers bid to provide capacity for a period of one year (or up to five years in the case of new entrants) after that three-year lead time. See *id.* at 98-99, 105. The three-year lead time exists so that bidders can build new generating facilities, thus allowing new entrants to compete with existing suppliers in the auction. See Pet. App. 110a; J.A. 68-69. At the end of the auction, the winning bidders are committed to supply capacity at the auction's "clearing price." See Pet. App. 110a; J.A. 66, 149. ISO-NE must file the auction results with FERC under Section 205, and interested parties have 45 days to challenge them. J.A. 118. Market participants are not required to buy or sell capacity at the auction price. Rather, utilities can contract for capacity in advance of and outside the auction (or commit to generate power themselves) and thereby "meet [their] capacity obligations without paying the auction clearing price." Pet. App. 112a; see p. 49, *infra*. Utilities that choose to acquire capacity through the auction, however, are responsible for paying for capacity at the auction price in proportion to their share of peak usage. See Pet. App. 112a; J.A. 70.[2]

The settlement also provides for "transition payments" to purchase necessary capacity until the capacity from the auctions becomes available. See Pet. App. 116a-118a; J.A. 163-169. Those fixed-rate payments, which run through May 31, 2010, see J.A. 164, were designed to "serve as a bridge" and to "help ensure that existing generators remain available until new resources can be built" based on the auction results. See Pet. App. 117a. ISO-NE's consumer-serving utilities (also known as "load-serving entities") are responsible for the transition payments in proportion to their share of peak usage. See *ibid.*; J.A. 163.

This case concerns the standard that will govern *future* challenges to the rates agreed upon as a result of the auction process and the transition payments set by the settlement agreement. The agreement includes a broad *Memphis* clause stating that, except as "expressly provided," the agreement "does *not* impose the *Mobile-Sierra* standard." J.A. 95 (emphasis added); see also *id.* at 58; Br. in Opp. 6. It provides two exceptions. First, the *Mobile-Sierra* public-interest standard applies to rates agreed upon through the capacity auctions (except during the 45-day review period following each auction, when the ordinary just-and-reasonable standard applies, see Pet. App. 78a, 120a, 202a). See J.A. 95. Second, the public-interest standard applies to the transition payments (and their implementing rules) following FERC's ap-

[2] In addition, buyers and sellers can exchange capacity obligations in periodic "reconfiguration" auctions. See J.A. 137-142.

proval of the settlement. See *ibid.*[3] That *Mobile-Sierra* standard, the agreement continues, applies "whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." *Ibid.* The settlement's explanatory statement notes that "one purpose for adopting the *Mobile-Sierra* standard for final auction prices is to reduce regulatory uncertainty and thus the risk premium that new entrants may require." *Id.* at 60-61.

2. *FERC's Decisions*

The parties filed the proposed settlement with the Commission. Pet. App. 103a. As the parties agreed, FERC reviewed the settlement under the ordinary just-and-reasonable standard, not *Mobile-Sierra*'s public-interest standard, see *id.* at 140a-144a, unanimously approving it as an effective way to "resolve the deficiencies in New England's existing capacity market," *id.* at 135a, 219a. "[A]s a package," FERC found, the agreement "achieves an overall just and reasonable result within a zone of reasonableness." *Id.* at 141a-142a.

FERC lauded the capacity auctions as a "market-based mechanism" that would "appropriately value capacity resources based on their location." Pet. App. 138a. The auctions would "provide appropriate signals to investors when new infrastructure resources are necessary with sufficient lead time to allow that infrastructure to be put into place before reliability is sacrificed." *Ibid.*

---

[3] The agreement thus states that "the 'public interest' standard of review set forth in [*Mobile*] and [*Sierra*]" governs "(i) challenges to the Capacity Clearing Prices derived through the [Forward Capacity Auctions] and prices resulting from reconfiguration auctions," and "(ii) proposed changes to * * * [the] Agreements Regarding Transition Period[ ] and the Market Rules implementing that part" following the agreement's "Effective Date." J.A. 95.

FERC also found the transition payments to be "within a range that * * * is just and reasonable." *Id.* at 143a.

Most important here, FERC held that the *Mobile-Sierra* public-interest standard could govern future challenges to auction rates and transition payments regardless of the challenger. FERC rejected the claim that applying *Mobile-Sierra* to challenges by non-contracting third parties would "'disenfranchise[ ]'" them from "'the protections against unjust and unreasonable rates provided in the FPA.'" Pet. App. 194a. FERC stressed the narrow scope of the provision, which addressed only two discrete sets of prices. See *id.* at 200a. And it noted that it had "routinely permitted the use of similar provisions in settlement agreements, including contested settlements." *Id.* at 200a & n.150 (collecting cases).

FERC explained that the stability provided by *Mobile-Sierra* was "particularly important in this case, which was initiated in part because of the unstable nature" of the existing market. Pet. App. 202a. "The Court's statement in *Mobile* that 'all agree . . . [that] the stability of supply arrangements . . . is essential to the health of the natural gas industry' is no less true with regard to the health of New England's electricity infrastructure." *Id.* at 203a (quoting 350 U.S. at 344). At the same time, the "limited *Mobile-Sierra* provision appropriately balances the need for rate stability and the interests of the diverse entities" affected. *Id.* at 202a. And FERC could still vindicate third parties' interests because "'[t]he *Mobile-Sierra* doctrine itself allows for intervention by FERC where it is shown that the interests of third parties are threatened.'" *Id.* at 201a (quoting *Ne. Utils. Serv. Co.* v. *FERC*, 993 F.2d 937, 961 (1st Cir. 1993)).

FERC later denied rehearing. Pet. App. 28a-101a. FERC rejected arguments that the matters covered by the *Mobile-Sierra* clause were not "contracts" to which *Mobile-Sierra* applied, *id.* at 70a-71a, 75a-76a, and that *Mobile-Sierra* could not apply to challenges by non-contracting parties, *id.* at 76a-79a.

C. The Court of Appeals' Decision

The D.C. Circuit upheld FERC's order in nearly all respects, but granted the petition for review with respect to applying the *Mobile-Sierra* standard to auction rates and transition payments. Pet. App. 1a-27a. Applying that standard to future challenges by non-contracting third parties, the court held, would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." *Id.* at 19a.

The court recognized that, "[u]nder the *Mobile-Sierra* doctrine, 'FERC may abrogate or modify freely negotiated private contracts * * * only if required by the public interest.'" Pet. App. 19a. FERC must apply "a strong presumption that the settled rate is just and reasonable" and "may only set aside the contract for the most compelling reasons." *Id.* at 20a. That public-interest standard, the court noted, is "'much more restrictive'" than the standard that governs unilateral tariffs. See *id.* at 19a. That different treatment of contract rates "recognizes the superior efficiency of private bargaining." *Ibid.*

The court of appeals held, however, that *Mobile-Sierra*'s public-interest standard could not be applied to "rate challenges brought by non-contracting third parties." Pet. App. 20a. The court observed that, "when a party files a complaint against a rate or charge, FERC must adjudicate the challenge under the 'just and reasonable' standard." *Ibid.* (quoting 16 U.S.C. § 824e(a)). The court asserted that *Mobile-Sierra* "carves out an exception to this rule based on the 'familiar dictates of contract law.'" *Ibid.* Relying on that understanding, the court held that the doctrine applies only where "'one party to a rate contract on file with FERC attempts to effect a unilateral rate change'"—not where a non-contracting party challenges a rate agreed to by contracting parties. See *id.* at 22a.

The court of appeals did not explain why *Mobile-Sierra*'s presumption of reasonableness (or the rationales underlying it) would cease to apply merely because a non-contracting party brought the challenge. Instead, quoting a case that addressed whether an arbitration agreement precludes non-signatories from seeking judicial relief, the court stated that "'a contract cannot bind a non-party.'" Pet. App. 22a (quoting *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279, 294 (2002)). The court asserted that the settlement, by requiring application of *Mobile-Sierra*, improperly "attempt[ed] to thrust the 'public interest' standard of review upon non-settling third parties." *Ibid.* "[W]hen a rate challenge is brought by a non-contracting third party," the court concluded, "the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in section 206 of the Federal Power Act." *Ibid.* Even though the *Mobile-Sierra* provision was of "'limited' applicability," the court continued, applying *Mobile-Sierra*'s public-interest standard to non-parties would still "deprive[ ] [them] of their statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." *Ibid.*

The court acknowledged that FERC had repeatedly approved similar provisions in the past, but it deemed those decisions irrelevant because they had not been judicially approved. Pet. App. 23a. In any event, the court asserted, those FERC decisions contravened the statutory text, which "quite clear[ly]" directs FERC to determine whether rates are "'unjust [or] unreasonable.'" *Id.* at 24a. The court stated that *Mobile-Sierra* is designed only "to ensure contract stability *as between the contracting parties—i.e.*, to make it more difficult for either party to shirk its contractual obligations." *Ibid.* Seeking to protect stability by applying the doctrine to third parties, the court claimed, "makes no sense." *Ibid.*

D. This Court's Intervening Decision in *Morgan Stanley* and the Denial of Rehearing

Shortly after the court of appeals' decision, this Court decided *Morgan Stanley*. In that case, the Court addressed (among other things) the relationship between *Mobile-Sierra*'s public-interest standard and the statutory requirement of "just and reasonable" rates. The Court acknowledged that lower federal courts and FERC had come to distinguish the *Mobile-Sierra* "public interest standard" applicable to contract rates from the "just and reasonable standard." 128 S. Ct. at 2740. But the Court declined to "take this nomenclature to stand for the obviously indefensible proposition that a standard different from the statutory just-and-reasonable standard applies to contract rates." *Ibid.* "Rather, the term 'public interest standard' refers to the differing *application* of that just-and-reasonable standard to contract rates." *Ibid.* *Mobile-Sierra*, the Court explained, simply "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Id.* at 2746.

FERC and other parties then sought rehearing of the decision below, urging that *Morgan Stanley* foreclosed the panel's holding that *Mobile-Sierra* was an "'exception'" to the statutory just-and-reasonable standard and that applying *Mobile-Sierra* would "'deprive[] non-settling parties of their statutory right to have rate challenges adjudicated under the "just and reasonable" standard.'" FERC Reh'g Pet. in Nos. 06-1403 *et al.*, at 5-6 (D.C. Cir. Aug. 8, 2008). *Mobile-Sierra*'s public-interest standard could not "deprive" anyone of their statutory right to "just and reasonable" review, FERC explained, because—as *Morgan Stanley* makes clear—the public-interest standard is merely an "'*application* of the just-and-reasonable standard to contract rates.'" *Ibid.* Stressing that this was the first time it had sought rehearing in almost five years, *id.* at 2 & n.2, FERC highlighted the serious consequences of the panel's error. The panel decision, FERC urged, "undermines the contract certainty needed for infrastructure investment emphasized in *Morgan Stanley*" and produces a "manifestly anomalous result." *Id.* at 11-12.[4]

The court of appeals denied rehearing. Pet. App. 241a-248a. On April 27, 2009, this Court granted the petition for a writ of certiorari. 129 S. Ct. 2050.

SUMMARY OF ARGUMENT

I. The *Mobile-Sierra* doctrine has protected the stability of contractual relations in the energy industry for

[4] Two Commissioners dissented from FERC's decision to seek rehearing. Pet. App. 224a-240a. Their dissent, however, did not defend the D.C. Circuit's holding that *Mobile-Sierra* is inapplicable to third-party challenges. Rather, it argued that *contested settlements* should not be reviewed under the *Mobile-Sierra* standard. See *ibid.* As explained in the petition (at 13 n.4) and below (p. 45, *infra*), this case does not concern the standard that governs FERC's review of a contested settlement. FERC reviewed the settlement here under the ordinary just-and-reasonable standard, not *Mobile-Sierra*. See p. 12, *supra*. This case concerns only the standard that governs *future* challenges to the contract rates produced by the capacity auctions and to the transition payments.

more than 50 years. Just two Terms ago, this Court reaffirmed that bedrock Federal Power Act doctrine, holding that FERC can abrogate contract rates only in "extraordinary circumstances where the public will be severely harmed." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2749 (2008). In the decision below, the court of appeals created an exception that all but swallows that rule, holding that "the *Mobile-Sierra* doctrine simply does not apply" whenever "a rate challenge is brought by a non-contracting third party." Pet. App. 22a. In the court of appeals' view, *any person* indirectly affected by a contract rate—any consumer, advocacy group, state utility commission, or elected official acting *parens patriae* (indeed, anyone but the contracting parties themselves)—can challenge the rate without regard to *Mobile-Sierra*'s protections.

If the court of appeals were correct, this Court's decision in *Morgan Stanley*—not to mention the half-century of *Mobile-Sierra* jurisprudence that preceded it—would have been an exercise in futility. The Court would have defended the FPA's principle of contract stability by rebuffing the ranks of immediate counterparties only to see the principle overwhelmed by hordes of motivated nonparties lying in wait not far behind. If *Mobile-Sierra*'s demanding public-interest standard protects contracts only from challenges by a select few—the contract counterparties—while exempting everyone else, it provides no stability at all.

But the court of appeals' view is not correct. To the contrary, it cannot be reconciled with this Court's precedents.

A. First, the court of appeals' rationale squarely conflicts with this Court's decision in *Morgan Stanley*. The court of appeals reasoned that applying the public-interest standard to non-parties would "deprive" them of their statutory right to review under the just-and-reasonable standard. But, as *Morgan Stanley* explains, *Mobile-Sierra*'s public-interest standard is merely one "*application* of that just-and-reasonable standard"—the one that governs "contract rates." 128 S. Ct. at 2740. *Mobile-Sierra* "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Id.* at 2746. The public-interest standard thus cannot "deprive" non-parties of their statutory right to just-and-reasonable review, because it *is* a form of just-and-reasonable review.

B. The public-interest standard, moreover, is a restriction on *FERC's authority* to abrogate contracts, not private parties' authority to challenge them, and it applies whether FERC's investigation is initiated in response to a contracting party's complaint, in response to a non-contracting party's complaint, or by FERC acting *sua sponte*. Indeed, the *public*-interest standard was developed for the precise purpose of protecting the interests of non-contracting members of the *public*. The standard by its terms applies to the public's challenges.

C. Nor can the court of appeals' holding be reconciled with the rationales underlying *Mobile-Sierra*.

1. This Court has premised the *Mobile-Sierra* doctrine on the sensible notion that rates negotiated by sophisticated buyers and sellers can be expected to be reasonable. That expectation of reasonableness cannot logically vary with the identity of the person who challenges the rate. And contract rates agreed to in a competitive wholesale market can be expected to benefit consumers and other non-contracting parties, not just the contracting parties themselves.

2. The court of appeals' decision likewise prevents *Mobile-Sierra* from providing any semblance of the contract stability the doctrine is supposed to provide—stability that is essential to critical infrastructure development. A presumption that protects contract rates from just a few persons (contracting counterparties) while allowing everyone else to challenge them free of *Mobile-Sierra*'s restrictions provides no stability at all.

D. Finally, the court of appeals' decision rests on a misunderstanding of contract principles. Applying *Mobile-Sierra* to a non-party's challenge does not "bind" the non-party to the contract. The existence of the contract is simply a *fact* that makes the rate more likely to be reasonable. And contract-law principles cannot justify making it easier for non-parties to challenge a contract rate, since contract-law principles normally would not allow non-parties to challenge the contract *at all*.

II. A. This Court need not address respondents' alternative argument that, even if *Mobile-Sierra* applies to non-contracting parties as a general matter, the particular rates at issue here are not "contract rates" for *Mobile-Sierra* purposes. This case does not present the question of what standard applies to FERC's review of a proposed *settlement*. FERC reviewed the settlement here under the ordinary just-and-reasonable standard, consistent with the agreement's *Memphis* clause. The agreement's *Mobile-Sierra* provision applies only to *future* challenges to two types of rates: auction rates and transition payments. The Court should leave the question of whether *those* rates are "contract rates" to be addressed, if at all, by the court of appeals in the first instance on remand.

B. In any event, the auction rates are precisely the sort of contract rates that *Mobile-Sierra* has long protected. Auctions create binding contracts. The auction rates are thus contract rates that would be entitled to *Mobile-Sierra* protection even if there had never been a settlement agreement. FERC could not have erred by approving a settlement provision that merely recites the standard for abrogation that would have applied of its own force even absent the settlement.

ARGUMENT

For more than 50 years, the *Mobile-Sierra* doctrine—named for this Court's twin decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) ("*Mobile*"), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*")—has "preserv[ed] the integrity of contracts" and thereby "permit[ted] the stability of supply arrangements which all agree is essential to the health of the * * * industry." *Mobile*, 350 U.S. at 344. Under that doctrine, FERC "must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737 (2008).

Mobile-Sierra represents an "application" of the Federal Power Act's general standard that "all wholesale-electricity rates [must] be 'just and reasonable.'" *Morgan Stanley*, 128 S. Ct. at 2737-2740 (quoting 16 U.S.C. § 824d(a)) (emphasis omitted). Where a supplier sets a rate unilaterally by tariff, FERC reviews the rate under what is called the "*ordinary* just-and-reasonable standard." See *ibid.* Under that standard, FERC has "discretion to take into account [all] the facts and circumstances" and can select any rate "'within a "zone of reasonableness."'" FERC Pet. Br. 10 (quoting *In re Per-*

mian Basin Area Rate Cases, 390 U.S. 747, 767 (1968)). By contrast, where a buyer and seller agree on a rate by contract, *Mobile-Sierra*'s public-interest standard provides the "definition of what it means for a rate to satisfy the just-and-reasonable standard." *Morgan Stanley*, 128 S. Ct. at 2746. Under the public-interest standard, FERC must "presume" that the contract rate is just and reasonable, and can modify it only in "extraordinary circumstances where the public will be severely harmed." *Id.* at 2737, 2749.

Time and again this Court has confirmed that FERC cannot overturn contract rates unless that public-interest standard is met. In *Mobile*, the Court noted that, "by requiring contracts to be filed with the Commission, the Act expressly recognizes that rates to particular customers may be set by individual contracts," and that the Act "evinces no purpose to abrogate [those] contracts." 350 U.S. at 338. The Commission, the Court concluded, could modify contract rates only "when necessary in the public interest." *Id.* at 344. In *Sierra*, the Court held that "a contract may not be said to be either 'unjust' or 'unreasonable' simply because it is unprofitable to the public utility," and that the "sole concern" of the Commission is whether the contract threatens the "public interest"—such as "where [the rate] might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." 350 U.S. at 355; see also pp. 4-7, *supra* (discussing *Mobile* and *Sierra*). "The regulatory system created by the Act is premised on contractual agreements voluntarily devised by the regulated companies; it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity." *Permian Basin*, 390 U.S. at 822. FERC thus "lacks affirmative authority, absent extraordinary circumstances, to 'abrogate existing contractual arrangements.'" *Ark. La. Gas Co.* v. *Hall*, 453 U.S. 571, 582 (1981). That "settled understanding of the FPA * * * has prevailed in this Court, lower courts, and the Commission for half a century." *Morgan Stanley*, 128 S. Ct. at 2749 n.6.

Mobile-Sierra reflects the "commonsense notion" that sophisticated businesses in wholesale energy markets can be "'expected to negotiate a "just and reasonable" rate as between the two of them.'" *Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon Commc'ns Inc.* v. *FCC*, 535 U.S. 467, 479 (2002)). (That is why it applies to rates "set bilaterally by contract" but not those set "unilaterally by tariff." See *id.* at 2738.) *Mobile-Sierra* also reflects the need for contractual certainty, a "key source of stability" in volatile energy markets where capital requirements are intensive and cost recovery can take decades. See *id.* at 2749; *Mobile*, 350 U.S. at 344; pp. 40-41, *infra*. As FERC has repeatedly stressed: "Competitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co.* v. *Duke Energy Trading & Mktg., L.L.C.*, 99 F.E.R.C. ¶61,047, at 61,190 (2002).[5] FERC must presume that

[5] See also *City of Burbank* v. *Calpine Energy Servs., L.P.*, 102 F.E.R.C. ¶61,268, at 61,832 (2003); *Pub. Util. Dist. No. 1* v. *Am. Elec. Power Serv. Corp.*, 100 F.E.R.C. ¶61,296, at 62,340 (2002); *PacifiCorp* v. *Reliant Energy Servs., Inc.*, 99 F.E.R.C. ¶61,381, at 62,614 (2002); *Pub. Utils. Comm'n of Cal.* v. *Sellers of Long Term Contracts*, 99 F.E.R.C. ¶61,087, at 61,383 (2002). The FERC proceedings in *Nevada Power* and *Public Utilities Commission of California* ultimately led to this Court's rulings in *Morgan Stanley* and related cases.

contract rates are reasonable because "[t]he FPA recognizes that contract stability ultimately benefits consumers." *Morgan Stanley*, 128 S. Ct. at 2749.

In this case, the D.C. Circuit held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply." Pet. App. 22a. In other words, although the doctrine protects contract rates from challenges by an immediate counterparty, *any other person* indirectly affected—any consumer, advocacy group, state utility commission, or elected official acting *parens patriae*—can challenge the rate, potentially years into a contract, without regard to *Mobile-Sierra*'s protections. That holding conflicts with this Court's decision in *Morgan Stanley*. It renders the public-interest standard inapplicable to challenges by the very members of the public the doctrine is designed to protect. It makes the presumption of reasonableness vary with the challenger, despite the fact that this Court's rationales for presuming reasonableness do not depend on the identity of the complainant who prompted FERC's investigation. It destroys the contract stability that *Mobile-Sierra* was designed to provide. And it rests on a fundamentally mistaken conception of contract law.

I. *MOBILE-SIERRA* REQUIRES FERC TO PRESUME THAT CONTRACT RATES ARE REASONABLE REGARDLESS OF THE CHALLENGER'S IDENTITY

A. *Morgan Stanley* Squarely Rejected the Court of Appeals' Rationale for Limiting *Mobile-Sierra* to Challenges by Contracting Parties

The court below held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in section 206 of the Federal Power Act." Pet. App. 22a.

That holding rested entirely on the premise that *Mobile-Sierra*'s public-interest test is inconsistent with the statutory "just and reasonable" standard. "[T]he relevant statutory language," the court noted, "is quite clear": FERC "must determine whether the challenged rate is 'unjust, unreasonable, unduly discriminatory or preferential.'" Pet. App. 23a-24a (quoting 16 U.S.C. § 824e(a)). The court acknowledged *Mobile-Sierra*'s public-interest standard, but characterized *Mobile-Sierra* as having "carve[d] out an exception" to the statutory just-and-reasonable requirement "based on the 'familiar dictates of contract law.'" *Id.* at 20a. Because "'a contract cannot bind a nonparty,'" the court reasoned, the public-interest standard cannot be "thrust" upon non-contracting third parties. *Id.* at 22a (quoting *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279, 294 (2002)). Doing so would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." *Id.* at 19a.

Over and over the court of appeals made that same point. The public-interest standard would "deprive[ ] non-settling parties of their statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." Pet. App. 22a. It would "derogat[e] [from] the[ir] statutory right to 'just and reasonable' review." *Id.* at 23a n.9. It "departs from the usual 'just and reasonable' standard and makes it harder for petitioners to successfully challenge rates in cases of changed circumstances." *Id.* at 23a. FERC cannot even apply *Mobile-Sierra* narrowly to discrete issues where stability is critical, the court declared, because doing so would be tantamount to "us[ing] an illegal standard sparingly." *Ibid.*

That reasoning cannot be reconciled with this Court's decision in *Morgan Stanley*. There, this Court flatly rejected the view that *Mobile-Sierra*'s public-interest standard departs from the statutory "just and reasonable" standard. The Court acknowledged that FERC and courts had begun to refer to the standard governing unilateral tariff rates as the "just and reasonable standard" and *Mobile-Sierra*'s standard for contract rates as the "public interest standard." 128 S. Ct. at 2740. But the Court rejected as "obviously indefensible" the claim that "a standard different from the statutory just-and-reasonable standard applies to contract rates." *Ibid.* "Rather, the term 'public interest standard' refers to the differing *application* of that just-and-reasonable standard to contract rates." *Ibid.* *Mobile-Sierra*'s public-interest standard simply "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Id.* at 2746.

The decision below thus adopted the very position this Court rejected in *Morgan Stanley*: that the public-interest standard "departs" from or is an "exception" to the Act's requirement that all rates be "just and reasonable." Applying *Mobile-Sierra* to non-party challenges cannot "deprive [non-parties] of their statutory right to challenge rates under the 'just and reasonable' standard," Pet. App. 19a, because *Mobile-Sierra*'s public-interest standard is simply an *application* of that statutory standard—the "definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Morgan Stanley*, 128 S. Ct. at 2746. Because the decision below rests on a premise this Court has squarely rejected, it should be reversed.

B. The Court of Appeals' Analysis Cannot Be Reconciled with the Requirement That FERC Apply the Public-Interest Standard to Address Third-Party Harm

The court of appeals' claim that *Mobile-Sierra* does not apply to challenges by non-contracting third parties also defies the settled framework under which FERC must address third-party harm. *Mobile-Sierra* limits *FERC's authority* to abrogate contract rates. And, under *Mobile-Sierra*'s public-interest standard, whether FERC can abrogate a contract rate depends on whether there is harm to the public interest, not on the identity of the party that filed the complaint. *Mobile-Sierra*'s "public interest" standard exists for the precise purpose of protecting the "public"—*i.e.*, non-contracting third parties. The court of appeals' holding stands *Mobile-Sierra* on its head, rendering the public-interest standard inapplicable to challenges by the very parties it was designed to protect.

1. *Mobile-Sierra*'s "public interest" standard exists to protect the interests of non-contracting third parties. Indeed, that is its *sole* purpose. In *Mobile*, the Court stated that its interpretation "preclud[ed] [suppliers] from unilaterally changing their contracts simply because it is in their *private* interests to do so." 350 U.S. at 344 (emphasis added). The *only* situation where suppliers would have an "avenue of relief," the Court explained, was where their "private interests" happened to "coincide with the public interest." *Ibid.* *Mobile* thus conditioned relief on harm to the *public*—*i.e.*, to non-contracting third parties—as opposed to the "private interests" of the contracting parties.

Sierra underscores that point. The "purpose of the power given the Commission by § 206(a)," the Court stated, "is the protection of the public interest, *as distinguished from the private interests of the utilities*." 350 U.S. at 355 (emphasis added). The "*sole concern* of the Commission" in contract cases is "whether the rate * * * adversely affect[s] the *public* interest." *Ibid.* (emphasis added). The Court then gave three examples of that "public" harm—"where [the rate] might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." *Ibid.* Each of those examples concerns harm to non-contracting third parties. The prospect that a utility might be unable to "continue its service" portends serious harm to the consuming public, which might find itself without electricity. Cf. *Blumenthal* v. *NRG Power Mktg., Inc.*, 104 F.E.R.C. ¶ 61,210, at 61,731 (2003) (refusing to abrogate a contract that would not "impair or interrupt the reliability of electric service to end users"). The prospect of casting an "excessive burden" on "*other* consumers" by its terms involves third-party harms. And "unduly discriminatory" rates concern third-party harms too, as that phrase refers only to rates that are "unduly discriminatory or preferential to the detriment of purchasers *who are not parties to the contract*." *Papago Tribal Util. Auth.* v. *FERC*, 723 F.2d 950, 953 n.4 (D.C. Cir. 1983) (Scalia, J.) (emphasis added); see also *Ne. Utils. Serv. Co.* v. *FERC*, 993 F.2d 937, 960-961 (1st Cir. 1993).

Later cases have elaborated on the *degree* of harm that *Mobile-Sierra* requires. See pp. 21-23, *supra*. But the relevant harm has always been harm *to the public*—*i.e.*, to third parties. See, *e.g.*, *Morgan Stanley*, 128 S. Ct. at 2747 (harm to "customers of the purchaser"); *Potomac Elec. Power Co.* v. *FERC*, 210 F.3d 403, 406-410 (D.C. Cir. 2000); *Pub. Serv. Comm'n* v. *FPC*, 543 F.2d 757, 796-

798 (D.C. Cir. 1974). "The focus of the *Mobile-Sierra* doctrine has always been on the impact * * * on third parties * * * ." *Blumenthal*, 104 F.E.R.C. ¶ 61,210, at 61,730.

2. This Court's cases, the statutory text, and decades of precedent make clear that the D.C. Circuit's approach—ignoring the "public interest" standard whenever the challenger is a member of the public—is wrong. *Mobile-Sierra*'s public-interest test defines *FERC's authority* to abrogate contract rates. And that authority depends on the extent of injury to the public—not on the identity of the complainant who prompted FERC's investigation.

This Court has consistently described *Mobile-Sierra*, not as a limit on *private parties'* ability to challenge contract rates, but as a restriction on *FERC's* authority to modify rates. Every reference in *Morgan Stanley* describes the doctrine in those terms: "Under the *Mobile-Sierra* doctrine, *the Federal Energy Regulatory Commission* * * * *must presume* that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." 128 S. Ct. at 2737 (emphasis added). *Mobile* and *Sierra* "addressed the *authority of the Commission* to modify rates set bilaterally by contract." *Id.* at 2738 (emphasis added). "[T]he FPA intended to reserve *the Commission's* contract-abrogation power for those extraordinary circumstances where the public will be severely harmed." *Id.* at 2749 (emphasis added). As the Court stated elsewhere: "[T]he *Commission itself* lacks affirmative authority, absent extraordinary circumstances, to 'abrogate existing contractual arrangements.'" *Ark. La.*, 453 U.S. at 582 (emphasis added). FERC likewise understands *Mobile-Sierra* as a restriction on *its own* authority—a doctrine that creates necessary certainty by prohibiting "*the Commission* [from] modify[ing] market-based contracts unless there are extraordinary circumstances." *Nev. Power*, 99 F.E.R.C. ¶ 61,047, at 61,190 (emphasis altered). Because *Mobile-Sierra* restricts FERC, not private parties, the complainant's identity is immaterial. Anyone aggrieved can file a complaint. *Mobile-Sierra* simply restricts FERC's authority to abrogate contracts in response.

The statutory text confirms that understanding. The statute charges *FERC* with determining whether rates are just and reasonable. 16 U.S.C. §§ 824d(e), 824e(a). "[T]he prescription of the statute is a standard for the Commission to apply and, independently of Commission action, creates no right which courts may enforce." *Montana-Dakota Utils. Co.* v. *Nw. Pub. Serv. Co.*, 341 U.S. 246, 251 (1951). FERC can initiate proceedings "upon its own motion or upon complaint," 16 U.S.C. § 824e(a), but nothing in the statute suggests that FERC's authority depends on how the investigation began. As FERC explained below, it would be "manifestly anomalous" to make "the Commission's ability to change an agreement * * * vary based on whether a third party filed a complaint, instead of the extent to which third parties are harmed by that agreement." FERC Reh'g Pet. in Nos. 06-1403 *et al.*, at 11 (D.C. Cir. Aug. 8, 2008). One of the sources on which the court below relied (Pet. App. 20a n.8) makes that very point: "While a substantive finding at the conclusion of a proceeding that third parties' interests are at stake and are damaged could be a legitimate factor * * * , the manner of initiating the investigation—*sua sponte* or at the request of a non-contracting party versus at the request of a contracting party—should have no bearing on the final Commission order." Gentile, *The*

Mobile-Sierra *Rule: Its Illustrious Past and Uncertain Future*, 21 Energy L.J. 353, 371 (2000). "Section 206 of the FPA * * * do[es] not vest the Commission with different authorities based on the manner in which an investigation is initiated." *Ibid.*

Lower courts have long applied *Mobile-Sierra* without regard to the challenger's identity. In *Northeast Utilities Service Co.* v. *FERC*, 993 F.2d 937 (1st Cir. 1993), for example, a non-party disputed the reasonableness of certain contract terms. See *Ne. Utils. Serv. Co.*, 50 F.E.R.C. ¶61,266, at 61,831-32, 61,837-39 (1990). FERC stated that, because "parties to a contract can[not] waive the section 206 rights of nonparties," "a nonparty challeng-[ing] a rate contract in a section 206 proceeding * * * need only show that the contract is unjust, unreasonable, unduly discriminatory or preferential." *Id.* at 61,838. The First Circuit reversed. It acknowledged FERC's concern that the contract "might unduly discriminate against entities not parties to the contract." 993 F.2d at 961. But that concern was "inadequate" to justify departure from *Mobile-Sierra* because "[t]he *Mobile-Sierra* doctrine itself allows for intervention by FERC where it is shown that the interests of third parties are threatened." *Ibid.* Harm to third parties, the court held, was not a "reason for departing from this public interest standard." *Ibid.* When FERC modified the contract again on remand, the First Circuit affirmed because FERC properly "applied the 'public interest' doctrine," "explaining how the disputed contractual terms may harm third parties." *Ne. Utils. Serv. Co.* v. *FERC*, 55 F.3d 686, 692-693 (1st Cir. 1995). Other cases are to the same effect.[6] And FERC itself has routinely applied *Mo-*

[6] In *Wisconsin Public Power, Inc.* v. *FERC*, 493 F.3d 239 (D.C. Cir. 2007), for example, the D.C. Circuit applied *Mobile-Sierra* despite

bile-Sierra to non-party challenges.[7]

non-parties' arguments that the contracts would "shift congestion costs to everyone else in the market." *Id.* at 273-275. And in *Town of Norwood* v. *FERC*, 587 F.2d 1306 (D.C. Cir. 1978), the court applied *Mobile-Sierra* to a *non-party's* complaint of undue discrimination, stating that FERC could modify a contract as a remedy only if the "heavy burdens" of *Mobile-Sierra* were met. *Id.* at 1312.

[7] See *Midwest Indep. Sys. Operator, Inc.*, 115 F.E.R.C. ¶ 61,174, at 61,615 (2006); *Vt. Elec. Coop., Inc.*, 114 F.E.R.C. ¶ 61,220, at 61,715 (2006); *Calpine Constr. Fin. Co.*, 114 F.E.R.C. ¶ 61,217, at 61,711 (2006); *Hermiston Power P'ship*, 114 F.E.R.C. ¶ 61,204, at 61,689 (2006); *San Diego Gas & Elec. Co.*, 114 F.E.R.C. ¶ 61,158, at 61,521 (2006); *Midwest Indep. Sys. Operator, Inc.*, 110 F.E.R.C. ¶ 61,380, at 62,469-70 (2005); *Midwest Indep. Sys. Operator, Inc.*, 110 F.E.R.C. ¶ 61,177, at 61,653-54 (2005); *Wis. Power & Light Co.*, 106 F.E.R.C. ¶ 61,112, at 61,410-11 (2004); *PJM Interconnection*, 105 F.E.R.C. ¶ 61,294, at 62,427, 62,430 (2003), *reh'g denied*, 108 F.E.R.C. ¶ 61,032, at 61,204 (2004); *Pub. Utils. Comm'n of Cal.* v. *Sellers of Long Term Contracts*, 105 F.E.R.C. ¶ 61,182, at 61,947 (2003); *Nev. Power Co.* v. *Enron Power Mktg., Inc.*, 103 F.E.R.C. ¶ 61,353, at 62,389 (2003), *reh'g denied*, 105 F.E.R.C. ¶ 61,185, at 61,985 (2003); cf. *Cent. Me. Power Co.*, 114 F.E.R.C. ¶ 61,184, at 61,621 (2006); *Pub. Utils. Comm'n of Cal.* v. *Sellers of Long Term Contracts*, 99 F.E.R.C. ¶ 61,087 at 61,382-83 (2002), *reh'g denied*, 100 F.E.R.C. ¶ 61,098, at 61,395-96 (2002).

Admittedly, FERC has sometimes declined to apply the public-interest standard to non-parties. See, *e.g.*, *Bridgeport Energy, LLC*, 118 F.E.R.C. ¶ 61,243, at 62,193-94 (2007); *PJM Interconnection, LLC*, 96 F.E.R.C. ¶ 61,206, at 61,878 & n.13 (2001); *Fla. Power & Light Co.*, 67 F.E.R.C. ¶ 61,141, at 61,394-99 (1994); *So. Co. Servs., Inc.*, 67 F.E.R.C. ¶ 61,080, at 61,226-29 (1994). But many of those decisions rest on special circumstances or the absence of FERC consent and thus do not support the categorical rule adopted below. In any event, FERC's sometimes overt hostility to *Mobile-Sierra*—a doctrine that constrains its discretion—is well documented. See, *e.g.*, *Boston Edison Co.* v. *FERC*, 233 F.3d 60, 67-68 (1st Cir. 2000) (FERC is "becoming hostile to *Mobile-Sierra*" and will "say anything it needs to achieve its ends"); *Richmond Power & Light* v. *FPC*, 481 F.2d 490, 497 (D.C. Cir. 1973) ("[T]he Commission simply does not understand, or more likely is not willing to abide by," *Mo-*

This Court's decision in *Mobile* compels that result. In that case, the relevant provision of the Natural Gas Act (unlike its FPA counterpart) did not give suppliers standing to file complaints. See 350 U.S. at 344-345; compare 15 U.S.C. § 717d(a) with 16 U.S.C. § 824e(a). The Court recognized that, as a result, a natural gas supplier's *only* "avenue of relief" was to "furnish[] to the Commission any relevant information and request[] *it* to initiate an investigation *on its own motion*" in the hope that the supplier's interests would "coincide with the public interest." 350 U.S. at 344-345 (emphasis added). *Mobile* thus demonstrates that the public-interest standard applies even when FERC initiates a proceeding itself. See also *Boston Edison Co.* v. *FERC*, 233 F.3d 60 (1st Cir. 2000).

The D.C. Circuit's holding that *Mobile-Sierra* applies *only* to challenges by *contracting* parties cannot be reconciled with *Mobile*'s conclusion that the doctrine applies to challenges FERC initiates itself. FERC, after all, is the quintessential non-contracting party. Nor does it make any sense that FERC, the federal regulator statutorily charged with protecting the public interest, would have to meet *Mobile-Sierra*'s demanding public-interest standard while state attorneys general, advocacy groups, and litigious third parties—which lack FERC's expertise and statutory authority—can challenge those same rates free of *Mobile-Sierra*'s restrictions. The simple fact is that *Mobile-Sierra*'s public-interest standard applies *whenever* FERC considers abrogating a contract—whether in response to a contracting party's complaint, in response to a non-contracting party's complaint, or on its own motion.

---

bile-Sierra); *Sam Rayburn Dam Elec. Coop.* v. *FPC*, 515 F.2d 998, 1005 & n.29 (D.C. Cir. 1975); *Borough of Lansdale* v. *FPC*, 494 F.2d 1104, 1110 (D.C. Cir. 1974).

C. The Court of Appeals' Decision Cannot Be Reconciled With *Mobile-Sierra*'s Underlying Rationales

The court of appeals' categorical exemption for non-party challenges also contravenes the rationales underlying *Mobile-Sierra*. Those rationales are implicated whenever FERC contemplates abrogating a contract, without regard to the complainant's identity.

1. *This Court's Conclusion That Contract Rates Can Be Expected To Be Reasonable Applies Regardless of Who Challenges the Rates*

This Court has repeatedly grounded *Mobile-Sierra* in the sensible notion that a rate agreed upon by a buyer and seller—as opposed to a tariff dictated unilaterally by the seller—can be expected to be reasonable. *Mobile-Sierra* reflects "the commonsense notion that '[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.'" *Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon*, 535 U.S. at 479). That is why FERC must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737.

That expectation—that a contract rate will generally be reasonable—logically cannot depend on the identity of the person who challenges it. Contract rates can affect a variety of persons, both contracting parties and non-parties. But the identities of the persons affected, and the magnitude of those effects, do not depend on how FERC's investigation begins. A reasonable effect on the public cannot be transformed into a serious harm to the public, or vice versa, based on who filed the complaint.

As a matter of logic, the presumption of reasonableness "would not necessarily cease to apply simply because the challenge to the rate came from a non-contracting party." FERC Pet. Br. 14.

Moreover, contract rates negotiated by sophisticated parties can be expected to be reasonable even insofar as they affect third parties. That basic economic principle underlies FERC's entire "market-based rate" regime. See *Morgan Stanley*, 128 S. Ct. at 2741 (describing regime). Courts have upheld that regime precisely because rates freely negotiated in a competitive market are likely to be "just and reasonable"—not in the narrow sense that the parties get what they bargained for, but in the broader sense of economic efficiency. "'In a competitive market, * * * it is rational to assume that the terms of [the parties'] voluntary exchange are reasonable, and specifically to infer that the price is close to marginal cost, such that the seller makes only a normal return on its investment.'" *Elizabethtown Gas Co.* v. *FERC*, 10 F.3d 866, 870-871 (D.C. Cir. 1993) (quoting *Tejas Power Corp.* v. *FERC*, 908 F.2d 998, 1004 (D.C. Cir. 1990)); *California ex rel. Lockyer* v. *FERC*, 383 F.3d 1006, 1012-1013 (9th Cir. 2004); see also *Market-Based Rates*, 72 Fed. Reg. 39,904, 40,015-20 (2007).[8] Whether a rate is "close to marginal cost" and yields "only a normal return" in the long run cannot depend on the identity of the person affected. The presumption that market-based rates are reasonable thus is entirely independent of the challenger's identity. The *Mobile-Sierra* presumption must be as well.

---

[8] Of course, the fact that market prices can be expected to approximate marginal costs *in the long run* does not mean that merely exceeding marginal cost in a particular case overcomes the presumption of reasonableness. See *Morgan Stanley*, 128 S. Ct. at 2748-2749 & n.5.

The D.C. Circuit made no effort to explain why the expectation that contract rates will be reasonable should depend on who challenges them. Although the court alluded to the "superior efficiency of private bargaining," Pet. App. 19a, it never explained why that "superior efficiency" disappears when the presumptively efficient results of that bargaining are challenged by a non-contracting party. Respondents invoke *Morgan Stanley*'s observation that sophisticated parties could be "'expected to negotiate a "just and reasonable" rate *as between the two of them*.'" Br. in Opp. 15 (quoting 128 S. Ct. at 2746 (emphasis added)). But respondents misinterpret the phrase "as between the two of them." The Court's point was simply that a rate that is "just and reasonable" for two parties engaged in one transaction would not necessarily be "just and reasonable" for a different transaction involving different parties. Nothing in that phrase implies that the presumption of reasonableness evaporates when a rate is challenged by a non-party.

There may be unusual situations where a contract, although satisfactory to the contracting parties, imposes excessive or discriminatory burdens on third parties. But that proves only that FERC must have authority to abrogate contracts that sufficiently *affect* third parties, not that FERC's authority should depend on the identity of the complainant who caused FERC to initiate its investigation. And the public-interest standard already provides the proper mechanism for FERC's exercise of that authority: It permits FERC to abrogate contracts that "seriously harm[ ]" the public interest. *Morgan Stanley*, 128 S. Ct. at 2737. No one claims the presumption of reasonableness should be irrebuttable. The question is only whether the basis for the presumption evaporates simply because a non-contracting party challenges the rate. Clearly it does not.

2. *Challenges to Contracts Threaten Stability Regardless of the Challenger's Identity*

This Court has also grounded *Mobile-Sierra* in the "important role" contracts play in the FPA by providing a "key source of stability" that "ultimately benefits consumers." *Morgan Stanley*, 128 S. Ct. at 2749. Contracting parties often must undertake "substantial investments which [they] would be unwilling to make without long-term commitments," and parties can "hardly make such commitments if [their] supply contracts are subject to unilateral change * * * whenever [the other party's] interests so dictate." *Mobile*, 350 U.S. at 344; see pp. 7-8, 23-24, *supra*. This Court could not have held that *Mobile-Sierra* promotes contract stability if the doctrine applied only to challenges by contracting parties. A presumption that protects contracts from only a few people—the counterparties—while allowing *everyone else* to challenge them without regard to *Mobile-Sierra*'s protections provides no stability at all.

Wholesale energy contracts indirectly affect a vast array of consumers and other entities. Under the broad principles of administrative-law standing, virtually any of those indirectly affected persons can file a complaint. The FPA authorizes "*[a]ny person*, electric utility, State, municipality, or State commission" to complain. 16 U.S.C. § 825e (emphasis added). FERC regulations similarly permit "*[a]ny person* [to] file a complaint seeking Commission action." 18 C.F.R. § 385.206(a) (emphasis added). And even an "'identifiable trifle'" may confer standing. *United States* v. *SCRAP*, 412 U.S. 669, 689 n.14 (1973). Thus, the field of potential complainants is vast. It includes not only the contracting parties, but thousands of retail electricity consumers or other downstream purchasers; any interest group with a perceived stake (whether it seeks lower prices to benefit consumers or higher ones to promote conservation); and any state utility commission, consumer advocate, or elected official acting *parens patriae*.

One need look no further than *Morgan Stanley* to see the impact of the court of appeals' holding. In that case, this Court overturned the Ninth Circuit's refusal to apply the public-interest standard. 128 S. Ct. at 2745-2747. But myriad non-contracting parties (including the Nevada Public Utilities Commission, various Snohomish County ratepayers, and a U.S. Senator) had challenged the contracts in the underlying FERC proceedings,[9] and one non-contracting party (the Office of Nevada Attorney General, Bureau of Consumer Protection) was a respondent in this Court, see Br. for Pub. Util. Dist. No. 1, Nevada BCP, *et al.*, in Nos. 06-1457 & 06-1462, at 20 (Jan. 7, 2008). On the D.C. Circuit's theory, *Morgan-Stanley* should have come out the other way.

In this case too, nearly all the objectors are at most indirectly affected. See Pet. App. 120a-121a & nn.31-32, 144a. They include a "non-profit trade association" representing "industrial users of electricity," Br. in Opp. ii; an "ad hoc association of large industrial and commercial end-users," *id.* at iii; a consortium with such members as Brandeis University and the Polaroid Corporation, see Pet. App. 121a n.32; the attorneys general of two States, *ibid.*; one public utilities commission, *id.* at 121a n.31; and one public advocate, *ibid.* The Connecticut Attorney General asserts that *Mobile-Sierra* should not apply to

[9] See *Nev. Power*, 103 F.E.R.C. ¶ 61,353, at 62,388-89; *Nev. Power*, 105 F.E.R.C. ¶ 61,185, at 61,985; see also *Pub. Utils. Comm'n of Cal.*, 99 F.E.R.C. ¶ 61,087, at 61,377, 61,382-83.

him even though that State's utility regulator (the Department of Public Utility Control) and utility ratepayer advocate (the Office of Consumer Counsel) both *supported* the settlement. See J.A. 89. Other examples of non-party challenges abound.[10]

It is thus no surprise that those who actually negotiate wholesale contracts see non-party challenges as a threat to contract stability. In the first 12 months following the decision below, FERC had to rewrite contracts applying the *Mobile-Sierra* standard to non-parties at least 41 times. See Pet. Reply App. 1a-10a. That so many thought it desirable to include such provisions confirms that non-party challenges are a real threat. Exempting *every* challenger from *Mobile-Sierra* except an isolated few—the contract counterparties themselves—would destroy the stability the doctrine was designed to promote.

The court of appeals asserted that "[i]t makes no sense to say that the values of 'stability' and 'certainty' are furthered by applying the deferential standard of review to * * * parties that refused to agree." Pet. App. 24a (emphasis omitted). Quite the opposite: It "makes no sense" to justify *Mobile-Sierra* on the need to ensure contract stability but then to exempt challenges by a vast field of potential complainants with powerful incentives to upset

---

[10] The Illinois Attorney General recently challenged contracts between 16 wholesale suppliers and utilities, and won a settlement. See *Illinois ex rel. Ill. Att'y Gen.* v. *Exelon Generation Co.*, 121 F.E.R.C. ¶ 61,015 (2007). And a California consumer interest group—CAlifornians for Renewable Energy, Inc., or "CARE"—challenged several contracts between suppliers and utilities. See *CAlifornians for Renewable Energy, Inc.* v. *Cal. Pub. Utils. Comm'n*, 119 F.E.R.C. ¶ 61,058 (2007) (dismissing complaints); *CAlifornians for Renewable Energy, Inc.* v. *Cal. Pub. Utils. Comm'n*, 120 F.E.R.C. ¶ 61,272 (2007) (same). Some of those challenges remain pending on appeal. See No. 08-70010 (9th Cir. filed Jan. 3, 2008).

the agreements. From the perspective of power suppliers, it makes no difference whether their contracts are abrogated—potentially years into a project—because their counterparties complained or because someone else did. Stability is destroyed either way. The D.C. Circuit's decision would thus reduce *Mobile-Sierra*'s role in ensuring contract stability to a historical footnote.

That result could not come at a worse time. Over the next two decades, demand for electricity is expected to grow substantially, requiring some $400 to $700 billion in additional infrastructure. See The Brattle Group, *Transforming America's Power Industry: The Investment Challenge 2010-2030*, at 13, 20-21 (2008), http://www.edisonfoundation.net. But building a power plant typically takes years, and recovering its costs takes many more. See Cambridge Energy Research Assocs., Inc., *California Power Crisis Aftershock: The Potential Modification of Western Power Contracts* 4-5 (2007), http://www2.cera.com/westernpowercontracts. Electricity prices, moreover, are notoriously volatile. See *id.* at 7-9. Without reliable long-term contracts to assure predictable revenue streams, infrastructure developers would face enormous risks, requiring them either to pay substantial risk premiums for financing (costs that are ultimately passed on to consumers) or to abandon development altogether. See *id.* at 4-26. As FERC has explained, "[c]ompetitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power*, 99 F.E.R.C. ¶61,047, at 61,190. Contract stability, moreover, is particularly important for renewable energy resources. See Cambridge Energy Research Assocs., *su-*

pra, at 19. The impending federal renewable-energy requirements thus make *Mobile-Sierra* even more crucial. See American Clean Energy and Security Act of 2009, H.R. 2454, 111th Cong., § 101.

The point is not that *Mobile-Sierra should* apply to third-party challenges because contract stability is good policy. The point is that *Mobile-Sierra must* apply to third-party challenges because the court of appeals' contrary rule makes nonsense of this Court's stated rationale for the doctrine. A presumption of reasonableness that governs challenges by a select few—counterparties—but exempts challenges by everyone else, including consumers, interest groups, elected officials, or any other member of the essentially boundless class of indirectly affected non-parties, simply cannot provide the "stability of supply arrangements which all agree is essential to the health of the * * * industry." *Mobile*, 350 U.S. at 344.

D. The Court of Appeals' Decision Rests on an Erroneous Understanding of Contract Law

The court of appeals' decision also rests on a mistaken understanding of contract law. The court exempted everyone but contract signatories from *Mobile-Sierra* on the theory that a contract "binds" contracting parties to the public-interest standard but cannot "bind" non-parties. "'[I]t goes without saying,'" the court reasoned, "'that a contract cannot bind a nonparty.'" Pet. App. 22a (quoting *Waffle House*, 534 U.S. at 294).

A contract, however, does not "bind" a non-party merely because its existence somehow *affects* that non-party. Every moviegoer, for example, is indirectly affected by dozens of contracts to which the theater owner is a party—the license agreement with the studio that provided the film, the employment contract with the projectionist, even the contract with the popcorn supplier.

But no one would say the moviegoer is "bound" by those contracts. This Court confirmed that common-sense principle in *Local No. 93, International Association of Firefighters* v. *City of Cleveland*, 478 U.S. 501 (1986), concluding that a union was not "b[ou]nd" by a settlement agreement to which it was not a party, even though the union claimed the agreement affected it by diminishing workforce competence. See *id.* at 507-512, 528-530. What mattered, the Court explained, was that the agreement "impose[d] no legal duties or obligations on the Union" and "d[id] not purport to resolve any claims the Union might have." *Id.* at 530.

Wholesale power contracts are no different. A utility's retail customers, for example, are not "bound" by the wholesale contracts between the utility and its power suppliers. Consumers have no rights or obligations under those contracts; they normally are not even third-party beneficiaries. Cf. 13 R. Lord, *Williston on Contracts* § 37:34, at 219 (4th ed. 2000). The wholesale contract rate may indirectly *affect* retail consumers by affecting the utility's costs and thus its retail rates. But that does not mean consumers are "bound" by the contract.

The same principle governs FERC's standard of review. Under *Mobile-Sierra*, the existence of a contract *affects* the standard that FERC must apply when it reviews a rate. It thus *affects* non-contracting parties' ability to obtain modification of the rate. But the contract does not *bind* either FERC or non-parties by its own legal force. The existence of the contract is simply a *fact* that makes the rate more likely to be just and reasonable. *Mobile-Sierra* requires FERC to presume that contract rates are just and reasonable because sophisticated wholesale market participants can be expected to negotiate reasonable rates and because the FPA recognizes that contract stability ultimately benefits consumers—not because FERC or non-parties are contractually "bound" to that standard. See pp. 34-41, *supra*.

For that reason, the court of appeals erred in relying on *Waffle House*'s observation that a contract cannot "bind" non-parties. Pet. App. 22a. The question in *Waffle House* was whether an employee's agreement to arbitrate barred the EEOC from seeking judicial relief for him. 534 U.S. at 282. The contract was potentially relevant only on the theory (rejected by the Court) that the agreement *bound* the EEOC *by its legal force* not to pursue judicial relief. See *id.* at 284, 294. *Mobile-Sierra*, by contrast, does not rest on the theory that a wholesale energy contract "binds" FERC or the public *by its own legal force*. The existence of the contract is simply a *fact* that makes the rate presumptively just and reasonable.

To the extent general contract-law principles are relevant, they cut *against* the court of appeals' decision. Contract law generally does not allow non-parties to challenge contracts between others. "Ordinarily, only a party * * * to a contract can challenge its validity," and "the fact that a third party would be better off if a contract were unenforceable does not give him standing to sue to void the contract." *In re Vic Supply Co.*, 227 F.3d 928, 930-931 (7th Cir. 2000) (Posner, J.); see also *Ope Shipping, Ltd.* v. *Allstate Ins. Co.*, 687 F.2d 639 (2d Cir. 1982) ("Where, as here, the parties to a [contract] are satisfied with their bargain, a third person * * * may not challenge the contract's validity * * * ."); cf. *Friend* v. *Lee*, 221 F.2d 96, 100 (D.C. Cir. 1955) (non-party "has no standing to sue to invalidate the contract"). Contract law, for example, gives shoppers no right to challenge the rate the local grocer agrees to pay a farmer for lettuce, even if that agreement affects the grocer's prices. Likewise, contract law would not itself allow consumers to challenge the rate a utility pays for capacity merely because that rate affects their electricity bills.

The FPA departs from contract-law principles by adopting the broad standing principles of administrative law and by authorizing FERC to abrogate contracts that seriously harm third parties' interests. See pp. 27-29, 37, *supra*. But contract law cannot justify a further expansion of FERC's authority based on the challenger's identity. One cannot invoke general contract-law principles to expand a non-party's ability to challenge a rate where those contract-law principles would not permit him to bring the challenge *at all*.

Ultimately, the court of appeals seems to have treated *Mobile-Sierra* as a contractual waiver or estoppel doctrine. The court seems to have reasoned that, when parties enter into a contract, they impliedly waive their own right to just-and-reasonable review—a waiver that cannot be thrust upon third parties without depriving them of their separate right to just-and-reasonable review. See Pet. App. 19a-24a. Even apart from that theory's patent conflict with *Morgan Stanley*, see pp. 24-26, *supra*, this Court has never justified *Mobile-Sierra* on waiver or estoppel grounds. The Court's actual rationales for presuming contract rates to be reasonable—that sophisticated parties can be expected to negotiate reasonable rates and that contract stability benefits consumers—do not depend on the challenger's identity. See pp. 34-41, *supra*.

In *Morgan Stanley*, this Court rejected a similar attempt to reconceptualize *Mobile-Sierra* and then narrow the doctrine's scope based on the reconceived rationale. There, the Ninth Circuit had treated *Mobile-Sierra* as an "estoppel" doctrine that applied only after FERC's initial opportunity for review. See 128 S. Ct. at 2745-2746. This Court rejected that estoppel theory, pointing out that its cases had "said nothing of the sort." *Id.* at 2746. The court of appeals' theory here is equally unsupported by precedent. And it is at least as destructive of the goals *Mobile-Sierra* is designed to serve.

II. THE COURT NEED NOT ADDRESS—AND IN ANY EVENT WOULD HAVE TO REJECT—RESPONDENTS' ALTERNATIVE GROUND FOR AFFIRMANCE

A. This Court Need Not Address Respondents' Alternative Argument

In their brief in opposition, respondents urged that *Mobile-Sierra* should not apply here because the agreements at issue are "fundamentally different from the privately negotiated bilateral energy contracts that were at issue in *Morgan Stanley*." Br. in Opp. 10-12. To the extent respondents contend that *Mobile-Sierra* cannot apply to FERC's review of a *settlement agreement* (*id.* at 10), this case does not present that issue. FERC reviewed the settlement under the ordinary just-and-reasonable standard, consistent with the agreement's *Memphis* clause. See pp. 11-12, *supra*. *Mobile-Sierra* governs only *future* challenges in two narrow contexts excepted from that *Memphis* clause—rates agreed upon through the auctions, and transition payments. See *ibid.* Nor does this case concern whether FERC could have required, as a condition to approving the settlement, an even broader *Memphis* clause that would have withheld *Mobile-Sierra* protection from those two categories of rates as well. FERC approved the settlement, including its *Mobile-Sierra* provision, after concluding that the agreement appropriately balances all competing interests. See Pet. App. 202a.

Respondents' argument thus reduces to the assertion that auction rates and transition payments are not "contract rates" entitled to *Mobile-Sierra* protection. This Court, however, need not and should not resolve that quite distinct issue (which was presented as a separate argument both before FERC, see p. 14, *supra*, and by intervenors in the court of appeals, see Joint Intervenors' Br. in Nos. 06-1403 *et al.*, at 16-28 (D.C. Cir. Sept. 5, 2007)). The court of appeals did not address that issue. Instead, the court based its decision on the identity of the complaining party: "[W]hen a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply * * * ." Pet. App. 22a. The correctness of that categorical holding is the only question presented by the petition. Pet. i. And that is the only question of broad and recurring importance that has divided the courts of appeals. See *id.* at 25-28.

This Court's normal practice is "not [to] decide in the first instance issues not decided below." *NCAA* v. *Smith*, 525 U.S. 459, 469-470 (1999); see also *Muehler* v. *Mena*, 544 U.S. 93, 102 (2005); *Roberts* v. *Galen of Va., Inc.*, 525 U.S. 249, 253-254 (1999). That practice is particularly appropriate here, where *no* court has previously addressed whether these particular types of rates are contract rates. This Court is "a court of review, not of first view." *Cutter* v. *Wilkinson*, 544 U.S. 709, 718 n.7 (2005). Accordingly, the Court should leave respondents' alternative argument to be addressed, if at all, by the court of appeals in the first instance on remand.

B. The Rates at Issue Are "Contract Rates" Entitled to *Mobile-Sierra* Protection

Respondents' alternative ground is, in any event, without merit. *Mobile-Sierra* distinguishes between "contract rates" agreed upon bilaterally (or multilaterally) by the parties and rates set "unilaterally by tariff." See *Morgan Stanley*, 128 S. Ct. at 2738-2740, 2746 n.3, 2749 n.6. Contract rates are entitled to *Mobile-Sierra* protection; unilateral tariff rates normally are not. See *ibid.*; pp. 21-22, *supra*.

The auction rates and transition payments are both contract rates. The results of the capacity auctions are clearly contracts—voluntary agreements for the sale of capacity between sellers and buyers who choose to participate in the auctions—wholly apart from the settlement. Those auction results would be contracts protected by *Mobile-Sierra* even absent a settlement agreement of any sort. FERC could not have exceeded its authority by approving a settlement provision that merely recited the standard that would apply in any event. The settling parties' transition-payment obligations are likewise contract rates, not unilateral tariff rates. Those fixed rates are expressly set forth in a contract—the settlement agreement—to which the settling parties agreed.

1. *The Auction Rates Are Contract Rates*

a. Respondents' contention that auction rates are not contract rates entitled to *Mobile-Sierra* protection ignores the black-letter rule that a sale by auction *is* a contract. The participant's bid constitutes the contractual "offer," and the auctioneer "accepts" the offer "by the fall of the hammer or in other customary manner." U.C.C. § 2-328(2); see *Restatement (Second) of Contracts* § 28(1)(a) (1981); 1 *Williston on Contracts* § 4:12, at 515-527; 1 J. Perillo, *Corbin on Contracts* § 4.14, at 637-645 (rev. ed. 1993).[11] Auctions thus result in the same binding

---

[11] By contrast, in an auction "without reserve"—where the auctioneer waives his right to withdraw the goods—the auctioneer's announcement constitutes the "offer" and the bid constitutes the "acceptance." See *Restatement (Second) of Contracts* § 28(1)(b). Capa-

obligations as any other sales contract: "The bidder in an auction * * * is obligated generally to fulfill his or her promise by paying the price bid. * * * [H]e or she is entitled to have the property delivered to him or her, and a refusal of delivery is a *breach of contract*." 7 Am. Jur. 2d *Auctions and Auctioneers* §§ 49, 52, at 398, 402 (1997) (emphasis added); see also 7A C.J.S. *Auctions and Auctioneers* § 53, at 642 (2004) (where winning bidder fails to pay, "the seller is justified in treating the contract as breached or rescinded"); cf. 1 *Corbin on Contracts* § 4.14, at 642 ("It is obvious that after a bid has been made, at a sale 'without reserve,' there is a contract * * * .").[12]

The capacity auctions are no exception. They produce voluntary contracts, not unilateral tariffs. In each auction, suppliers compete to provide capacity for a period of one year (or up to five years in the case of new entrants) starting three years after the auction. See Pet. App. 110a-111a; J.A. 98-99, 105. Before each auction, ISO-NE determines the amount of capacity it will purchase—the "installed capacity requirement"—according to processes it develops in consultation with utilities and other stakeholders. See Pet. App. 118a; J.A. 59-60, 70, 121-123; *ISO New England, Inc.*, 118 F.E.R.C. ¶ 61,157, at 61,758 (2007). The auction then follows a descending price format. See J.A. 131. The auctioneer announces a starting price, and suppliers decide how much capacity to offer at that price. J.A. 66. If the bidders offer more capacity at that price than is needed, the price drops, and each supplier again decides how much to offer. *Ibid.* That proc-

---

city auctions arguably fall into that category, but nothing turns on the distinction.

[12] The capacity auctions are "reverse auctions" in which sellers alter their offers in response to the auctioneer's prices, but the results are contracts regardless.

ess repeats itself until supply equals demand. *Ibid.* The resulting price is the "clearing price," and the remaining bidders are the winners. *Ibid.* They are committed to provide the capacity they offered for the prescribed period, and are entitled to receive the clearing price in return. See Pet. App. 110a-111a; J.A. 66, 149.

No utility is required to purchase capacity at the auction clearing price. Under the settlement agreement's "self-supply" provisions, utilities can "meet [their] capacity obligations without paying the auction clearing price" by contracting for capacity outside the auction or supplying it themselves. Pet. App. 112a; see J.A. 65, 84-85, 111-112, 142, 149.[13] Those that choose to acquire capacity through the auction, however, are responsible for paying for capacity at the auction price in proportion to their share of peak usage. See Pet. App. 112a; J.A. 70. Like any other contract rate, therefore, the auction rates reflect voluntary agreements between buyers and sellers.

By contrast, auction rates bear no resemblance to the unilateral tariffs subject to ordinary just-and-reasonable review. No single supplier dictates when the auction will end or what the clearing price will be. To the contrary, the outcome is determined by an iterative, multilateral

[13] Purchasers planning to self-supply must designate and qualify their generating resources in advance of the auction. See J.A. 111-112. Those resources are still "offered into" the auction in the sense that they offset a portion of the installed capacity requirement, see *id.* at 65, 112, but payments are set by the contract rather than the auction clearing price, see *id.* at 149; Pet. App. 112a. Market participants have in fact invoked the self-supply provision to acquire capacity by contract. See ISO New England Inc., *Internal Market Monitoring Unit Review of the Forward Capacity Market Auction Results and Design Elements* 32-33 (June 5, 2009), available at http://www.iso-ne.com/regulatory/ferc/filings/index.html (noting "994 MW of resources * * * under state contracts in Connecticut").

process in which many sellers and buyers participate. Auctions are a more sophisticated and competitive contracting process, but they still result in contracts by which buyers agree to purchase capacity from sellers at a specified rate. Cf. *Richmond Power & Light* v. *FPC*, 481 F.2d 490, 496-497 (D.C. Cir. 1973) (*Mobile-Sierra* "appl[ies] whether the parties agree to a specific rate or whether they agree to a rate changeable in a specific manner").

Respondents repeatedly urge that they should be allowed to challenge auction rates under the ordinary just-and-reasonable standard because they did not agree to the *settlement agreement*. See, *e.g.*, Br. in Opp. 15-17. But the fact that the settlement was contested does not alter the fact that auction results are voluntary contracts among willing auction participants. Where a utility has chosen to acquire capacity through the auction, rather than contracting for it elsewhere under the self-supply provisions, its commitment is a voluntary contract. The fact that a complainant objected to one contract (the settlement agreement) does not mean it is entitled to a different standard of review for another contract (the auction result). If the auctions were held in the absence of any settlement agreement, the resulting rates would unquestionably be contract rates entitled to *Mobile-Sierra* protection. FERC cannot have erred in approving a settlement provision that merely recited the standard that would apply to auction results even absent a settlement.

b. The rationales underlying *Mobile-Sierra* also apply with full—if not special—force here. First, just as "'sophisticated businesses enjoying presumptively equal bargaining power * * * could be expected to negotiate a "just and reasonable" rate,'" *Morgan Stanley*, 128 S. Ct. at 2746, sophisticated businesses participating in capacity auctions can be expected to arrive at a just-and-reasonable rate. As Judge Tatel observed when addressing these very auctions: "[T]he point of an auction mechanism like the Forward Market is to use a best approximation of demand and the power of competitive bidding to help locate [an efficient] price. * * * [T]he real world decision makers who use the Forward Market do so precisely for its ability to evaluate prices." *Conn. Dep't of Pub. Util. Control* v. *FERC*, Nos. 07-1375 *et al.*, 2009 WL 1754607, at *7 (D.C. Cir. June 23, 2009); see also J.A. 67-68; Pet. App. 138a. Economists likewise widely laud auctions—particularly single-clearing-price auctions—as a means "to reliably provide consumers electricity at minimum cost." Cramton & Stoft, *Why We Need to Stick with Uniform-Price Auctions in Electricity Markets*, Electricity J., Jan./Feb. 2007, at 26, 26-27.[14] These particular auctions, moreover, include various refinements to ensure that prices are set competitively. See Pet. App. 115a-116a. In addition, FERC approved the auction structure under the ordinary just-and-reasonable standard, *id.* at 135a-144a, and can review auction results under that standard for 45 days following each auction, see *id.* at 78a, 120a, 202a. Although not necessary for *Mobile-Sierra* to apply, see *Morgan Stanley*, 128 S. Ct. at 2745-2746, FERC's approval and ongoing oversight corroborate the expectation of reasonableness.

The need for contract stability is likewise compelling here. As FERC explained, "[s]tability is particularly im-

---

[14] See also Baldick, *Single Clearing Price in Electricity Markets* (2009), http://www.competecoalition.com/files/Baldick%20study.pdf; Kahn, *et al.*, *Uniform Pricing or Pay-as-Bid Pricing*, Electricity J., July 2001, at 70, 71-72. Professor Cramton also testified favorably regarding the proposed auction mechanism on behalf of ISO-NE below. See J.A. 41; C.A. App. 1790-1808.

portant in this case, which was initiated in part because of the unstable nature" of New England's capacity market and the resulting chronic shortage of generating capacity. See Pet. App. 202a; p. 9, *supra*. The auctions take place a full three years before capacity is needed so suppliers can plan and build new facilities. See Pet. App. 110a; J.A. 68-69. But auctions cannot create adequate incentives to build hundreds of millions of dollars' worth of infrastructure if the resulting prices are subject to revision years into the contract. See pp. 37-41, *supra*. As FERC observed, "[t]he Court's statement in *Mobile* that 'all agree . . . [that] the stability of supply arrangements . . . is essential to the health of the natural gas industry' is no less true with regard to the health of New England's electricity infrastructure." Pet. App. 203a (quoting 350 U.S. at 344). The need for stability is thus at least as pressing here as it was in *Mobile*, *Sierra*, or *Morgan Stanley*. And, because the auction rates are contract rates rather than unilateral tariffs, they are entitled to the stability that *Mobile-Sierra* provides.

2. *The Transition Payments Are Contract Rates*

Respondents' contention that the transition payments are not contract rates protected by *Mobile-Sierra* likewise fails. As an initial matter (and as explained at the petition stage, Pet. Reply 7 n.2), there is little and rapidly diminishing reason to address the issue. Unlike the annual auctions, the transition payments terminate at the end of May 2010. J.A. 163-164. Following extensive proceedings, FERC reviewed those rates under the ordinary just-and-reasonable standard and rejected respondents' challenges to them. See Pet. App. 140a-161a. Respondents have identified no changed circumstance that might justify a different result now—under *any* standard—and the likelihood of one emerging between now and May 2010 is remote. This issue should be addressed, if at all, by the court of appeals in the first instance on remand.

In any event, the transition-payment obligations *of the settling parties* are clearly "contract rates" entitled to *Mobile-Sierra* protection. The settlement agreement sets forth a fixed schedule of rates that settling buyers agree to pay sellers for capacity for specified periods—a classic *Mobile-Sierra* contract. See J.A. 163-164. That the terms are set forth in a settlement that resolves pending litigation does not make the agreement any less a "contract" (whatever else it might also be). See *Kokkonen* v. *Guardian Life Ins. Co. of Am.*, 511 U.S. 375, 381 (1994); *Firefighters*, 478 U.S. at 515-524; cf. *Cities of Bethany* v. *FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984). Like any other contract rate, those rates were negotiated by sophisticated market participants and thus can be expected to be reasonable. And FERC specifically noted the need to "increase the stability of the market during the transition period." Pet. App. 159a-160a. FERC thus did not err in concluding that the settling parties' transition-payment obligations could not be overturned—whether challenged by the settling parties themselves or by others indirectly affected by the settling parties' obligations—absent the showing that *Mobile-Sierra* requires.[15]

---

[15] Respondents argue that the transition payments more closely resemble a unilateral tariff to the extent any *non-settling* party (such as NSTAR) must itself make those payments. See Br. in Opp. 11; cf. *ITC Holdings Corp.*, 102 F.E.R.C. ¶ 61,182, at 61,491 (2003) (rationale for *Mobile-Sierra* "does not apply * * * [to] a contract that is essentially seeking to set not only the respective rights and obligations of the contractual parties, but also the rates that third parties will pay"). Whether transition-payment obligations imposed on non-signatories would be contract or unilateral tariff rates, and whether

CONCLUSION

For the foregoing reasons, the court of appeals' decision should be reversed.

FERC could impose *Mobile-Sierra* protection even in the latter event, are complex questions that this Court should not address in the first instance. See pp. 45-46, *supra*. The record makes clear, however, that NSTAR had a full and fair opportunity to challenge the level of transition payments under the ordinary just-and-reasonable standard, see Pet. App. 120a-121a & n.32, 144a-147a; that NSTAR lost on that issue before FERC, *id.* at 151a-161a; and that NSTAR lost on that issue again before the court of appeals, *id.* at 8a-15a. NSTAR cannot, consistent with ordinary *res judicata* principles, expect to resurrect its challenge absent a significant change of circumstances. In any event, the settlement does not in fact directly impose transition-payment obligations on non-parties. The transition payments are actually made by *ISO-NE*, which bills load-serving entities for their shares. See ISO New England, Inc., *Manual for Billing (M-29)* §§ 1.1.1(1)(i), 1.1.6 & revision 13 (16th rev. Sept. 5, 2008), available at http://www.iso-ne.com/rules_proceds/isone_mnls/index.html. Because ISO-NE signed the settlement agreement, see J.A. 90, the payment obligations are classic contract rates entitled to *Mobile-Sierra* protection; the fact that those obligations indirectly affect load-serving entities like NSTAR provides no basis for treating them differently from any other contract rate. Moreover, the widespread support for the transition payments provides a strong basis for expecting them to be reasonable. See *id.* at 89-91. If the agreement of *two* parties (a single buyer-seller pair) creates a presumption of reasonableness, the agreement of *dozens* of buyers and sellers creates a stronger presumption still. The need for contract stability, moreover, is still acute. See Pet. App. 158a-160a. Thus, even if *Mobile-Sierra* would not *compel* FERC to apply the public-interest standard in these circumstances, FERC's considered decision to apply that standard is entitled to respect.

Respectfully submitted.

MICHAEL R. BRAMNICK
General Counsel
CHRISTOPHER C. O'HARA
Assistant General Counsel
NRG ENERGY, INC.
211 Carnegie Center Drive
Princeton, NJ 08540
(609) 524-4601

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

JEFFREY A. LAMKEN
ROBERT K. KRY
BAKER BOTTS L.L.P.
1299 Pennsylvania Ave., N.W.
Washington, D.C. 20004
(202) 639-7700

Counsel for Petitioners

JULY 2009