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 OF MORGAN STANLEY CAPITAL GROUP INC., THE INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC., AND THE FINANCIAL INSTITUTIONS ENERGY GROUP AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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BRIEF OF MORGAN STANLEY CAPITAL GROUP INC., THE INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC., AND THE FINANCIAL INSTITUTIONS ENERGY GROUP AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

Morgan Stanley Capital Group Inc., the International Swaps and Derivatives Association, Inc., and the Financial Institutions Energy Group respectfully submit this brief as *amici curiae* in support of the petitioners.[1]

INTEREST OF *AMICI CURIAE*

Morgan Stanley Capital Group Inc. (Morgan Stanley), the commodities division of Morgan Stanley, is a "power marketer": an entity with regulatory approval from the Federal Energy Regulatory Commission (FERC or the Commission) to buy and sell, at market-based rates, wholesale electricity that it does not produce. Morgan Stanley was one of the first entities approved to sell power in this manner, having initially received its market-based authority in 1994 and then having repeatedly received authorization thereafter. *See Morgan Stanley Capital Group, Inc.*, 69 F.E.R.C. ¶ 61,175 (Nov. 8, 1994), *see also*, *e.g.*, *Morgan Stanley Capital Group, Inc.*, No.

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[1] Pursuant to Rule 37.6, counsel for *amici curiae* state that no counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person or entity other than *amici curiae*, their members, or their counsel has made a monetary contribution to the preparation or submission of this brief. The parties have filed letters of consent to the filing of this brief. Letters reflecting such consent have been filed with the Clerk.

ER94-1384-029 (June 26, 2001) (application filed November 8, 2000).

The International Swaps and Derivatives Association, Inc. (ISDA), which represents participants in the privately negotiated derivatives industry, is the largest global financial trade association by number of member firms. ISDA was chartered in 1985 and today has over 825 member institutions from 57 countries on six continents. These members include most of the world's major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end users that rely on over-the-counter derivatives to manage efficiently the risks inherent in their core economic activities. Since its inception, ISDA has pioneered efforts to identify and reduce the sources of risk in the derivatives and risk management business.

The Financial Institutions Energy Group (FIEG) is a group of banks and other financial institutions, all of which play a vital role in the electric utility industry. The businesses of FIEG members (and their affiliates) as they relate to the energy sector are very diverse. They are directly involved in the purchase and sale of electric energy, capacity, and ancillary services, and many, like Morgan Stanley, are power marketers with market-based rate authority. They are also involved in a wide array of other businesses that are only incidentally related to the electric industry. For example, FIEG members may act as market-making dealers, participants in physically and financially settled derivative transactions designed to hedge certain counterparty risk or to establish a proprietary position in the market, arrangers of loan facilities, and underwriters of debt and equity securities.

Members of ISDA and FIEG are substantial participants in the market for wholesale electric power. Some members own interests in companies that produce electric power and sell it in the wholesale market. Some members own interests in retail distribution companies that purchase power in the wholesale market and distribute it to end users. Predominantly, however, members of these *amici*, like Morgan Stanley, operate as power marketers in the wholesale market; they contract with power producers, distribution companies, and other power marketers to buy or sell wholesale power that will ultimately be produced, resold, or distributed by others.

Power marketers like Morgan Stanley and the members of ISDA and FIEG play an extremely important role in wholesale power markets. Their expertise and extensive trading operations allow them to mitigate the financial risks that power manufacturers or distributors would otherwise have to incur in producing or distributing power. By assembling a diverse portfolio of contractual obligations to buy and sell power at different times and different prices, power marketers can insulate themselves from many of the risks of temporary price volatility, which are inherent in the energy market, as well as longer term unfavorable price trends. By contracting with producers and distributors of power, these marketers also allow producers and distributors to avoid those risks.

Unlike power producers, which generally participate in the energy market as sellers, and distribution companies, which participate as buyers, power marketers tend over the long term to be neither net sellers nor net purchasers of power. Consequently, they have no vested interest in rules that systematically favor either sellers or buyers. Their interest, instead, is in rules that ensure that the *market* operates effectively. They therefore are especially well suited to address the implications of the court of appeals' decision below for the effective functioning of the market for wholesale energy sales and purchases.

Both ISDA and FIEG accordingly participated as *amici curiae* in support of petitioners in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008). Morgan Stanley of course was a petitioner in that case. Morgan Stanley, ISDA, and FIEG now participate as *amici curiae* in this case principally to explain that, whereas the Court's recent decision two Terms ago in *Morgan Stanley* strongly reaffirmed the central role of contractual stability in securing the effective functioning of the market for wholesale power, an affirmance of the court of appeals in this case would essentially negate the decision in *Morgan Stanley* and the vital protection of contractual stability on which the decision is grounded.

INTRODUCTION AND SUMMARY OF ARGUMENT

Under the Federal Power Act (FPA), 16 U.S.C. §§ 791a *et seq.*, FERC possesses authority to regulate the transmission and sale of wholesale electricity. The FPA prescribes that all wholesale energy rates must be "just and reasonable," and any rate failing to qualify as "just and reasonable" is "declared to be unlawful." 16 U.S.C. § 824d(a). The FPA grants FERC authority to review, on its own initiative or in response to a complaint, whether existing rates comply with the "just and reasonable" standard, and to determine and fix by order a "just and reasonable rate" upon concluding that an existing rate is "unjust, unreasonable, unduly discriminatory or preferential." 16 U.S.C. § 824e(a).

The degree of latitude possessed by FERC to modify an existing rate on the ground that it fails to qualify as "just and reasonable" varies depending on whether the rate was established unilaterally by tariff or instead by a negotiated contract. The *Mobile-Sierra* doctrine, *see United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956), establishes a presumption that wholesale energy contracts negotiated by sophisticated parties produce just and reasonable rates. Contract rates, that is, presumptively *are* "just and reasonable," and may be set aside by FERC only in narrow situations in which their continued enforcement would "violate[] the public interest." *Morgan Stanley*, 128 S. Ct. at 2739. In the case of a rate established unilaterally by tariff, FERC retains greater latitude to set aside the rate as unjust and unreasonable "if it results in an unfair rate of return, not just if it violates the public interest." *Id.*

Those two forms of review—the more stringent public interest standard for contract rates and the "ordinary" just-and-reasonable standard for non-contract rates—each constitute applications to their distinct contexts of the FPA's overarching "just and reasonable" standard. *Id.* at 2740. The *Mobile-Sierra* public-interest standard therefore "refers to the differing application of th[e] just-and-reasonable standard to contract rates." *Id.*

This Court strongly reaffirmed the vitality of the *Mobile-Sierra* presumption for contract rates in its decision two Terms ago in *Morgan Stanley*. In doing so, the Court emphasized "the important role of contracts in the FPA" and the FPA's "recogni[tion] that contract stability ultimately benefits consumers." *Id.* at 2749. Conversely, the Court explained, "uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm customers in the long run." *Id.* (quoting Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities, 72 Fed. Reg. 39,904, 39,906–07 (July 20, 2007)).

The court of appeals below confined the *Mobile-Sierra* presumption to rate challenges brought by a contracting party, holding the "*Mobile-Sierra* doctrine simply does not apply" when "a rate challenge is brought by a non-contracting third party." Pet. App. 22a. That approach, if affirmed, would substantially undermine, if not completely destroy, the vital protection of contract stability secured by the recent reaffirmation of *Mobile-Sierra* in *Morgan Stanley*. The court of appeals' decision enables any affected third party to challenge and potentially invalidate any wholesale energy contract as "unjust and unreasonable" without regard to the "public interest" standard, thus allowing any third party to seek to set aside a contract rate free from the presumption of validity demanded by *Mobile-Sierra*.

Indeed, the court of appeals' decision below affects the sanctity of the very contracts at issue in *Morgan Stanley* itself. One of the respondents in the *Morgan Stanley* case, the Nevada Bureau of Consumer Protection, has argued before FERC on remand from this Court's decision that, under the D.C. Circuit's decision below, it can freely challenge the rates in the *Morgan Stanley* contracts unencumbered by the *Mobile-Sierra* presumption. The Court's opinion in *Morgan Stanley*, however, nowhere suggests that the public interest standard it ordered the Commission to apply was applicable only to the contracting respondents. On the contrary, the Court emphasized that "[t]here is only one statutory standard for assessing wholesale electricity rates"—the just-and-reasonable standard—and when that standard is applied to contracted-for rates, it permits the Commission to overturn only rates that would "seriously harm the public interest." *Morgan Stanley*, 128 S. Ct. at 2745, 2747. The D.C. Circuit's decision varies the application of the statutory standard, to the very same rate, based on who asks FERC to apply it. There is no justification for applying a varied interpretation to the fixed terms of the statute in that manner.

Such an approach is particularly problematic in the context of the FPA. Contracts play an integral role in that statutory scheme, and contract stability is essential to the wholesale energy markets to which the statute applies. The uncertainty created by the court of appeals' approach would thoroughly undermine contractual integrity, with substantial adverse implications for the effective functioning of those markets. In particular, the court of appeals' approach would (i) make it very difficult to attract sufficient capital to build and maintain the expansive (and expensive) infrastructure necessary to produce, transport, and deliver energy; (ii) encourage power marketers, who depend on the enforceability of their contracts to make a profit, to shift their capital to other markets with lesser levels of costs and risks; and (iii) discourage power sellers from entering into long-term agreements precisely when their capacity and price certainty are most needed by buyers. The result ultimately would be to harm the consumers that rely on the wholesale energy market for the power they use every day.

ARGUMENT

I. THE COURT OF APPEALS' NON-PARTY EXCEPTION TO *MOBILE-SIERRA* WOULD ESSENTIALLY NULLIFY THIS COURT'S DECISION MERELY TWO TERMS AGO IN *MORGAN STANLEY*

Two Terms ago, this Court in *Morgan Stanley* strongly reaffirmed its landmark 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), and the centrality of contractual integrity to the operation of the FPA. But that recent victory—for the petitioners in that case, for the effective functioning of wholesale energy markets, and ultimately for the consumers who rely on them—has been put substantially at risk by the court of appeals' decision below. The D.C. Circuit's decision cannot be reconciled with this Court's precedent or with the terms of the FPA, which establish one—and only one—standard governing the review of rates established by contract, regardless of the identity of the party bringing a challenge.

A. *Morgan Stanley* Preserved and Reaffirmed the Centrality of Contract Stability under the Federal Power Act

Morgan Stanley arose out of a dispute involving, *inter alia*, a long-term wholesale power contract between Morgan Stanley and respondent Public Utility District No. 1 of Snohomish County Washington (Snohomish), during the 2000-2001 crisis in the energy markets in the Western States. Eventually, the prevailing market rates for short-term power fell below the rate established in Snohomish's contract with Morgan Stanley. Snohomish then filed a complaint with FERC, seeking to set aside the terms of its contract with Morgan Stanley. Other companies likewise challenged contracts they made during the crisis to purchase power. Certain non-contracting entities and individuals, including the Nevada Attorney General, Bureau of Consumer Protection (BCP), and a Senator from the State of Washington, sought to intervene before the Commission on the challengers' behalf. FERC rejected those challenges, emphasizing the importance of contract stability under the FPA. The Ninth Circuit reversed, holding that the *Mobile-Sierra* presumption was inapplicable in those circumstances for a number of reasons. *See Morgan Stanley*, 128 S. Ct. at 2743-45.

This Court largely reversed the decision of the Ninth Circuit. The Court began by reiterating that, "[u]nder the *Mobile-Sierra* doctrine, [FERC] must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and it may revise those rates only if they place "an excessive burden on consumers or otherwise seriously harm the public interest." *Id.* at 2737, 2750. The Court concluded that the Ninth Circuit had failed to abide by the *Mobile-Sierra* rule, and had given "short shrift to the important role of contracts in the FPA" in several respects. *Id.* at 2749.

First, by limiting application of *Mobile-Sierra* to instances in which FERC had pre-approved the market-based contract rates, the Ninth Circuit had erroneously "read *Sierra* as the equivalent of an estoppel doctrine" rather than "a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Id.* at 2746 (internal quotation marks omitted). Second, by limiting the application of *Mobile-Sierra* where there was a possibility of market dysfunction, the Ninth Circuit had "enabl[ed] sophisticated parties who weathered market turmoil by entering long-term contracts to renounce those contracts once the storm ha[d] passed," thus "reduc[ing] the incentive to conclude such contracts in the future" and "undermin[ing] the role of contracts in the FPA's statutory scheme." *Id.* at 2747. Third, by adopting a "zone of reasonableness" test to evaluate a buyer's challenge that rates are too high, the Ninth Circuit had failed "to accord an adequate level of protection to contracts." *Id.* at 2747, 2749. As this Court explained, "[a] presumption of validity that disappears when the rate is above marginal cost is no presumption of validity at all." *Id.* at 2748.

Finally, the Court turned to two issues on which it concluded remand to the Commission was required: (i) whether the challenged agreements imposed an excessive burden on customers "down the line," and (ii) whether any party had engaged "in such extensive unlawful market manipulation" as to affect negotiation of the contract rates. 128 S. Ct. at 2747, 2749-51. The Court remanded the case for the Commission to "amplify or clarify" its findings on those two issues. *Id.*

B. The Decision Below Is Irreconcilable with *Morgan Stanley*

The Court's decision in *Morgan Stanley* reaffirms a long line of precedent in which this Court has recognized that Congress "built the regulatory system" of the National Gas Act and FPA "on a foundation of private contracts." *Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 154 (1960). The decision of the D.C. Circuit in this case puts that foundation, including the outcome in *Morgan Stanley* itself, at risk.

The court of appeals' "third-party exception" to the presumption of reasonableness would effectively swallow the *Mobile-Sierra* rule. By misreading *Mobile-Sierra* as "depart[ing] from the usual 'just and reasonable' standard," the court of appeals misunderstood the FPA to permit virtually anyone but a contracting party—including individual end consumers, corporations, governmental entities, and state regulators—to attack contractually negotiated rates as unjust and unreasonable without any presumption of validity. *See* Pet. App. 22a (explaining that "[i]t goes without saying that a contract cannot bind a nonparty") (internal quotation marks omitted). The decision thus eliminates any semblance of the contractual integrity that this Court has long recognized to be integral under the FPA. A contracting party desiring to set aside a negotiated rate without having to overcome the *Mobile-Sierra* presumption need only find some non-contracting party willing to take up the challenge.

Indeed, one of the respondents in the *Morgan Stanley* case itself has argued that the case should have been decided differently under the rule established by the court of appeals in this case. Several of the parties that opposed the contracts at issue in *Morgan Stanley* were non-parties to the agreements. *See*, *e.g.*, *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 F.E.R.C. ¶ 61,353, at 62,388-89 (2003) (discussing Senator's request for rehearing); *Pub. Utils. Comm'n of Cal. v. Sellers of Long Term Contracts*, 99 F.E.R.C. ¶ 61,087, at 61,377, 61,382-83 (2002) (discussing complaints filed by the Public Utilities Commission of the State of California and the California Electricity Oversight Board), *reh'g denied*, 100 F.E.R.C. ¶ 61,098 (2002). One of those non-parties, the Office of the Nevada Attorney General, Bureau of Consumer Protection (Nevada BCP), was a respondent before this Court. *See Morgan Stanley*, 127 S. Ct. at 2736.

This Court's mandate in *Morgan Stanley* made plain that the Commission on remand was to apply the *Mobile-Sierra* public-interest standard to the contracts at issue in the case.[2] The Nevada BCP nonetheless has argued on remand that the D.C. Circuit's opinion below "precludes application of the *Mobile-Sierra* presumption of justness and reasonableness in evaluating the Nevada BCP's challenge" to the very same contracts. Nevada Attorney General, Bureau of Consumer Protection Answer to Snohomish's Cross-Motion for Procedures on Remand of *Morgan Stanley* at 3-4 (Dec. 9, 2008) (Nevada BCP Answer). The BCP accordingly asserted that the Commission could, "based on its findings to date, conclude that the rates included in the . . . Nevada contracts [before the Commission] are unjust and unreasonable" and "order refunds" based on "the difference between the contract rates and just and reasonable rates." *Id.* at 4.

The Commission rejected Nevada's argument as "premature," and "strongly encourage[d] all parties in th[e] matter to settle their disputes." FERC Order on Remand at 15 n.63 & 18, No. EL02-28-006, *et al.* (Dec. 18, 2008). The BCP, however, filed a petition for rehearing, arguing that the paper hearing ordered by FERC "was unnecessary and inappropriate" in that the "Commission erred in failing to specify that, pursuant to *Maine PUC*, the *Mobile-Sierra* presumption of justness and reasonableness does not apply to the Nevada BCP's challenge to the NV Energy contracts at issue in [*Morgan Stanley*]." Re-

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[2] *See*, *e.g.*, *Morgan Stanley*, 128 S. Ct. at 2750 (Commission on remand to consider whether increase in rates during the crisis was "so great that, even taking into account the desirability of fostering market-stabilizing long-term contracts, the rates impose an excessive burden on consumers or otherwise seriously harm the public interest").

quest for Rehearing of the Office of the Nevada Attorney General, Bureau of Consumer Protection at 2, 7 (Jan. 20, 2009). FERC has yet to rule on the petition for rehearing.

The Nevada BCP's position in *Morgan Stanley* vividly illustrates the mischief that the decision below would enable. Contrary to the argument of the BCP and the decision of the court of appeals below, there is no basis for concluding that the justness and reasonableness of a contract rate could depend upon who is challenging it. As this Court emphasized in *Morgan Stanley*, "[t]here is only one statutory standard for assessing wholesale electricity rates," *i.e.*, "the just-and-reasonable standard." 128 S. Ct. at 2745. And there is only one "definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context": the public interest requirement of *Mobile-Sierra*. *Id.* That standard applies uniformly when assessing the validity of a contracted-for rate, "regardless of when the contract is reviewed," *id.*, and regardless of the identity of the party bringing a challenge.

II. THE COURT OF APPEALS' DECISION WILL HARM CONSUMERS BY IMPEDING THE EFFICIENT OPERATION OF THE WHOLESALE POWER MARKET

The *Mobile-Sierra* presumption rests on the intuition that markets generally cannot operate efficiently unless contracting parties have confidence that contractual commitments will be enforced. The need for contract stability is especially critical in the market for wholesale power, which requires clear, stable, and enforceable contract rights for its very existence. Without that guarantee, the market (i) will not be able to attract sufficient capital to build and maintain the extensive and expensive infrastructure required for the production, transportation, and delivery of energy; (ii) will not be able to secure the participation of power marketers, who make the market more competitive; and (iii) will not be able to ensure that energy is provided to the public when the need for such power is at its greatest. A market operating under these constraints will fail to provide the service required by consumers who rely on it for their daily energy needs.

1. The contractual stability secured by *Mobile-Sierra* is critical to the wholesale power market, first and foremost, because the massive investments needed to build and maintain the infrastructure for the production, transportation, and delivery of power require that market participants have confidence that their agreements will remain binding in the future, even if one of the parties comes to conclude in hindsight that the original deal was improvident. As this Court recognized in *United Gas Pipe Line Co. v. Memphis Light, Gas & Water Division*, 358 U.S. 103 (1958), without reliable legal protection of energy producers' contract rights, "the maintenance and expansion of their systems through equity and debt financing would become most difficult, if not impossible." *Id.* at 113. Since the enactment of the FPA, "[e]conomies of scale have justified the construction of large . . . generation facilities" that produce power more efficiently and cheaply than ever before—but that also require ever-more significant amounts of capital to create. *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 681 (D.C. Cir. 2000).

Contract stability is so important in the context of the energy markets that, in certain instances, FERC has "encourage[d] investment in new generation capacity by ensuring increased stability in . . . revenues, not [by adopting] higher rates across the board." *Elec. Consumers Res. Council v. FERC*, 407 F.3d 1232, 1237 (D.C. Cir. 2005). As FERC recognized when it ordered enforcement of the contracts in *Morgan Stanley*, "[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 Co. v. Duke Energy Trading & Mktg. L.L.C.*, 99 F.E.R.C. ¶ 61,047, at 61,190 (2002).

Application of the *Mobile-Sierra* presumption affords that certainty. When the public interest standard is properly applied, litigation over long-term supply contracts is rare. *See Cities of Bethany v. FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984) ("[F]ixed rate contracts . . . promote market stability and reduce litigation over rate filings."). Until the Ninth Circuit's opinion in *Morgan Stanley* (which, of course, this Court largely reversed) and the D.C. Circuit's opinion in this case, the breadth and continued vitality of this Court's landmark decisions in *Mobile* and *Sierra* had never been seriously threatened. *See Boston Edison Co. v. FERC*, 233 F.3d 60, 66 (1st Cir. 2000) (Boudin, J.) (noting that "the two cases are probably among the dozen best-known public utility decisions by the Supreme Court in this century"). Relying on this consistent precedent, contracting parties have understood that, as a matter of practical reality, "[t]he obstacle that the public-interest standard presents to a rate change is almost insurmountable." *Kan. Cities v. FERC*, 723 F.2d 82, 87-88 (D.C. Cir. 1983) (Scalia, J.).

In contrast to the "refreshingly simple" *Mobile-Sierra* standard, *ASARCO, Inc. v. FERC*, 777 F.2d 764, 769 n.3 (D.C. Cir. 1985) (internal quotation marks omitted), the ordinary just-and-reasonable standard applicable to non-contract rates permits FERC to modify rates whenever they deviate from an ill-defined "zone of reasonableness." *See Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968). And, if affirmed, the court of appeals' approach would cause even more uncertainty—not only because it would freely permit avoidance of the *Mobile-Sierra* presumption when a non-party asserts a challenge, but also because it will require litigation over questions such as whether a non-party is really a "proxy for one of the contracting parties" such that *Mobile-Sierra* would nonetheless apply. *See* Br. for the FERC, *NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n* No. 08-674 (cert. stage) at 11-12 (Mar. 18, 2009).

Furthermore, under the application of the court of appeals' decision envisioned by the Nevada BCP in *Morgan-Stanley*, a non-contracting party may wait until a contracting party has filed a complaint—indeed, may wait until after a court of appeals has remanded a Commission decision on a contracting party's complaint—and only then step in to request FERC to invalidate a contract under the ordinary just-and-reasonable analysis. *See* Nevada BCP Answer at 11 (arguing that Commission could apply ordinary just-and-reasonable standard, even though "the third-party issue was not addressed on appeal," because "[o]nce the Commission reacquires jurisdiction of a remanded decision, it has the discretion to reconsider the whole of its original decision"). But regardless whether a non-party is permitted to piggyback off an existing complaint in that manner, under the decision below, extended litigation and high litigation costs would be the norm—and freely entered contractual relations could not be counted upon to justify capital investments or other resource commitments necessary to produce power in needed amounts.

2. The turmoil occasioned by the decision below would be especially burdensome for power marketers. In that intensely competitive business, profit margins are modest and will be substantially eroded if the contracts that are most favorable to a seller can be enforced, if at all, only by spending large sums on litigation. As FERC has recognized, when power marketers undertake their operations—even in a system in which contracts are regularly enforced—they "assume significant risk." *Citizens Power & Light Corp.*, 48 F.E.R.C. ¶ 61,210, at 61,776 (Aug. 8, 1989). They may "purchase products for which [they have] no immediate buyer, or . . . commit to sell products before [they have] a guaranteed purchase." *Id.* And because they own no transmission or generation facilities, power marketers have "no rate base on which to earn a traditional rate of return" and subsidize any losses they incur in trading. *Id.* For power marketers in particular, therefore, success in the energy market depends entirely on their ability to capitalize on the contracts they make to buy and sell at certain rates. A regulatory

environment that creates uncertainty about contract enforcement, and thus impedes the ability to manage risk, will tend to raise the costs, reduce the financial rewards, and increase the risks of companies that trade in wholesale power markets.

The decision below severely impedes contracting parties' ability to manage the risk posed by the ordinary just-and-reasonable standard. As this Court's precedent makes clear, contracting parties have always been free to contract around the *Mobile-Sierra* "public interest" standard by negotiating for the inclusion of so-called "*Memphis* clauses" that permit a party to petition FERC at any time to adjust agreed-upon rates under the ordinary just-and-reasonable standard. *See Memphis Light, Gas & Water Div.*, 358 U.S. at 112; *see also Williston Basin Interstate Pipeline Co. v. FERC*, 519 F.3d 497, 499 (D.C. Cir. 2008) (discussing origin of *Memphis* clauses). Before the D.C. Circuit's opinion in this case, power marketers (like any market participant) could induce other contracting parties to forgo the protection of a *Memphis* clause and lock in agreed-upon rates by offering more attractive contract terms than they might otherwise make available under the ordinary just-and-reasonable standard. In other words, the parties to each and every contract could decide for themselves whether they wished to be bound—or not to be bound—by *Mobile-Sierra*.

Under the decision below, in contrast, every contract effectively has a built-in *Memphis* clause for non-parties, denying both sellers and buyers the ability to negotiate for the certainty *Mobile-Sierra* affords. And FERC has, "in light of the *Maine PUC* decision," required replacement of "provisions that seek to impose a 'public interest' standard of review on non-contracting third parties," with "a substitute provision that imposes on non-contracting third parties 'the most stringent standard permissible under applicable law,'" *Duke Energy Carolinas, LLC*, 123 F.E.R.C. ¶ 61,201 at P 10 & n.10 (2008). *See* Pet'r Reply Br. (cert. stage) at 5 (citing examples in Reply App. 1a-10a).

Rather than increasing risk premiums to reflect the uncertainty caused by voidable contracts, moreover, power marketers may simply refrain from offering forward supply contracts and commit their capital to other markets that entail less risk. Like power producers or distribution companies, which will likely refuse to invest the significant amounts of capital required to create or replace capacity in an uncertain market, firms that function principally as power marketers have broad flexibility on the extent to which they will continue to engage in that business, because they buy and sell wholesale power that will ultimately be produced or distributed by others.

If that were allowed to happen, the cost to the electric power industry, and to the public, which depends on that industry daily, will be very large. As "deal-maker[s] and risk-taker[s]," power marketers must "focus on efficiency enhancing trades because [they] cannot survive unless [they] do." *Citizens*, 48 F.E.R.C. at 61,777. As such, power marketers "can increase efficiency in power supply markets and in turn ultimately lower the cost of electricity." *Id.*

3. What is more, the uncertainty engendered by the court of appeals' approach would make power marketers and other sellers least likely to enter into

long-term energy contracts precisely when the need for such contracts (and energy generally) is at its greatest. During times of high energy price volatility, like the Western energy crisis that spurred the litigation in *Morgan Stanley*, sensible regulatory policies encourage long-term contracts, which allow "buyers and sellers [to] lock in prices over an extended period," and thus "hedg[e] and allocat[e] risk to specialists willing and able to take on that risk." *Nev. Power Co. & Sierra Pac. Power Co. v. Enron Power Mktg., Inc.*, 101 F.E.R.C. ¶ 63,031, at 65,287 (Dec. 19, 2002); *see Morgan Stanley*, 128 S. Ct. at 2743 (noting that part of FERC's "emergency effort" to combat the crisis in the West was "to shift . . . purchases to the forward market" and to encourage investor-owned utilities "to enter into long-term contracts").

In a system where every contract is subject to a post-hoc challenge for "reasonableness" by a non-party, however, buyers will be hard-pressed to find any seller willing to take such a risk. That is because, when market prices are notably high, the likelihood that prices will decline in the future is correspondingly great, and the risk of suit from customers who become unhappy with their utilities' long-term deals would impose costs too high to make such sales worthwhile. The decision below, therefore, will discourage deals at the time when the public is most in need of a stable supply of energy. Combined with the decreased participation of power marketers generally, and the inability to attract capital for development moving forward, the consequences of the turmoil induced by the court of appeals' bifurcated approach to contractual reasonableness will severely undermine the efficacy of the power markets and harm the consumers that must rely on them.

4. Because the court of appeals misinterpreted the *Mobile-Sierra* standard to apply only to rate challenges brought by contracting parties, it had no occasion to address respondents' alternative argument that the rates agreed to in the forward capacity market auctions and the transition payments in the settlement agreement fail to constitute contract rates entitled to *Mobile-Sierra* protection. *See* Opp. at 10-12. This Court need not and should not reach that question. *See F. Hoffmann-La Roche Ltd. v. Empagran S.A.*, 542 U.S. 155, 175 (2004) ("The Court of Appeals . . . did not address this argument, . . . and, for that reason, neither shall we.") (internal citation omitted). As petitioners have explained, *no* court has addressed whether these types of auctions and payments constitute contracts to which *Mobile-Sierra* attaches. Pet'r Br. 46. It would thus be especially prudent in this case to allow the court of appeals to address that issue (if at all) in the first instance. *See Cutter v. Wilkinson*, 544 U.S. 709, 718 n.7 (2005).

In any event, the arguments advanced by the government in this Court provide no reason to question the applicability of *Mobile-Sierra* to the forward capacity auction results provided for in the parties' settlement. While acknowledging that the capacity auction results "possess[] certain characteristics of contracts," the government nonetheless contends that they "do not constitute contracts" because they "are not recorded in separate agreements between a particular generator and a particular purchasing entity" and "do not specify the consequences of default."

Gov't Br. 30. But this Court has never suggested that application of *Mobile-Sierra* could turn on the way in which multiple parties choose to record their agreed-upon rates or how parties specifically plan for any breach of their agreements. Nor is there any principle in contract law that makes those considerations salient. *See* Joseph M. Perrillo, *Corbin on Contracts*, § 52.1, at 278 (2005) ("Two or more may contract with one, together making a promise to her . . . . [they] may as a group all promise that a single performance shall be rendered, or they may each promise a separate performance."); *id.* § 58.1, at 397 (explaining that only "under certain conditions" can parties "determine in advance what damages will be assessed in the event of a breach").

The *Mobile-Sierra* standard, as the government recognizes, rests upon the "presumption that rates set out in a freely-negotiated whole-sale energy contract are just and reasonable." Gov't Br. 14. In a related case, the court of appeals has suggested that the auctions at issue in this case will result in just and reasonable rates, just as would other contractual negotiations. *See Conn. Dep't of Pub. Util. Control v. FERC*, Nos. 07-1375, 07-1460, 08-1175, 2009 WL 1754607, at *4 (D.C. Cir. June 23, 2009) ("[T]he purpose of the Forward Market is only to locate the price at which market incentives will be sufficient to meet th[e] expected demand [for capacity]."). If the Court elects to reach this question of first impression, therefore, the formalities emphasized by the government afford no basis for denying the market the stability *Mobile-Sierra* demands for a fairly negotiated rate. Rates agreed upon by "'sophisticated businesses enjoying presumptively equal bargaining power,'" *Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon Commc'ns Inc. v. FCC*, 535 U.S. 467, 479 (2002)), are presumptively just and reasonable and reviewed under the public interest standard, regardless of the particular form in which they may be memorialized.

CONCLUSION

For the foregoing reasons, as well as those stated by petitioners, the Court should reverse the decision of the court of appeals.

Respectfully submitted,

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