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NEW CHAPTERS IN THE *MOBILE-SIERRA* STORY: APPLICATION OF THE DOCTRINE AFTER *NRG POWER MARKETING, LLC V. MAINE PUBLIC UTILITIES COMMISSION*

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Synopsis: The *Mobile-Sierra* doctrine mandates respect for private contracts by shielding them from regulatory interference except when necessary in the public interest. Recent Supreme Court decisions have reaffirmed the continuing vitality of the doctrine, making it clear that any party — whether a seller, buyer, or third party (including the Federal Energy Regulatory Commission itself) — may not seek to modify a contract except in cases where a stringent "public interest standard" is satisfied. The Commission has now added a new twist to the *Mobile-Sierra* story by finding that it has the discretion to employ a similar, "more rigorous application of the just and reasonable standard" to protect non-contract rates, including those set forth in settlements regarding generally-applicable tariff provisions. This article traces the development, and addresses issues regarding the actual application, of the *Mobile-Sierra* doctrine and the new standard articulated by the Commission.

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I. INTRODUCTION

On February 27, 1956, the Supreme Court issued two decisions, *United Gas Pipe Line Co. v. Mobile Gas Service Co.* (*Mobile*)[1] and *FPC v. Sierra Pacific Power Co.* (*Sierra*),[2] which became "among the dozen best-known public utility decisions by the Supreme Court in [the 20th] century."[3] Together, these decisions resulted in the "*Mobile-Sierra* doctrine,"[4] which prohibits the Federal Energy Regulatory Commission (FERC or Commission)[5] from using its authority under the Federal Power Act (FPA) or the Natural Gas Act (NGA) to modify or abrogate existing contracts except in cases of "unequivocal public necessity"[6] or "extraordinary circumstances."[7]

While one court characterized *Mobile-Sierra* as "refreshingly simple,"[8] questions have repeatedly arisen regarding the scope of the doctrine and its impact on the FERC's obligations and authority under the FPA and the NGA.[9] The Supreme Court most recently addressed these issues in *NRG Power Marketing, LLC v. Maine Public Utilities Commission* (*NRG*),[10] where it confirmed that the *Mobile-Sierra* doctrine applies to "challenges to contract rates brought by noncontracting as well as contracting parties."[11] The lone dissenter, Justice Stevens, characterized this holding as "the third chapter in a story about how a reasonable principle, extended beyond its foundation, becomes bad law."[12] The authors do not share this view and submit that this third chapter, like the second chapter, followed naturally and logically from the Court's prior decisions. Nonetheless, there is little doubt that the *Mobile-Sierra* story has

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

2. FPC v. Sierra Pac. Power Co., 350 U.S. 348 (1956).

3. Boston Edison Co. v. FERC, 233 F.3d 60, 66 (1st Cir. 2000).

4. The Supreme Court also referred to the *Mobile-Sierra* doctrine as the "Mobile-Sierra presumption" in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*. 554 U.S. 527, 534 (2008).

5. The FERC and its predecessor, the Federal Power Commission, are also referred to herein, individually or together as applicable, as the "Commission."

6. *In re* Permian Basin Area Rate Cases, 390 U.S. 747, 822 (1968).

7. Arkansas La. Gas Co. v. Hall, 453 U.S. 571, 582 (1981). *Mobile* and *Sierra* were decided under "substantially identical" provisions of the NGA and the FPA, respectively. *Sierra,* 350 U.S. at 350. Decisions interpreting these provisions may be cited "interchangeably." *Arkansas La. Gas Co.*, 453 U.S. at 577 n.7.

8. Richmond Power & Light v. FPC, 481 F.2d 490, 493 (D.C. Cir. 1973).

9. As one commentator put it, *Richmond* and other cases demonstrate "that, on occasion, the interpretation and application of this 'refreshingly simple' rule has been frustratingly complex." Carmen L. Gentile, *The* Mobile-Sierra *Rule: Its Illustrious Past and Uncertain Future*, 21 ENERGY L.J. 353, 358 (2000).

10. NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693 (2010).

11. *Id.* at 697.

12. *Id.* at 701 (Stevens, J., dissenting).

developed beyond what some might have expected when *Mobile* and *Sierra* were decided in 1956. Indeed, the *Mobile-Sierra* story appears poised to continue into a fourth chapter, with *NRG* leaving the door open for the FERC to treat contract and non-contract rates "analogously,"[13] and *Devon Power LLC*,[14] the FERC's order on remand, holding that the Commission does, in fact, have the discretion to employ "a more rigorous application of the statutory 'just and reasonable' standard of review"[15] for certain non-contract rates.

II. THE EARLY CHAPTERS OF THE *MOBILE-SIERRA* STORY

The history and development of the *Mobile-Sierra* doctrine was discussed at length in the Supreme Court's 2008 decision in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County* (*Morgan Stanley*)[16] and has also been explored in a number of relatively recent law review articles.[17] Accordingly, rather than repeat the full history here, this section focuses narrowly on the aspects of that history that are relevant to the question of when, as a general matter, the doctrine applies and does not delve into exceptions that may apply in certain circumstances or, as a general matter, into the substantive effect of applying *Mobile-Sierra*.[18]

Irrespective of whether one shares Justice Stevens' assessment of the merits of the Supreme Court's *Mobile-Sierra* jurisprudence, his "chapters" provide a useful framework for looking at the story of the *Mobile-Sierra* doctrine. As Justice Stevens describes it, the story so far consists of:

- the "first chapter," in which the Court held that a regulated seller may "not unilaterally repudiate its contract obligations in response to changes in market conditions by simply filing a new rate schedule with the regulatory commission;"[19]
- the "second chapter," in which the Court held that "the same rule should apply to a buyer;"[20] and
- the "third chapter," in which the Court held that the *Mobile-Sierra* presumption, the presumption that rates fixed by contract are just

13. *Id.* at 701.

14. *Devon Power LLC*, 134 F.E.R.C. ¶ 61,208 (2011).

15. *Id.* at P 2.

16. Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527 (2008).

17. *See, e.g.*, John E. McCaffrey, Morgan Stanley Capital Group, Inc. v. Public Utility District No. 1 *Revisits the* Mobile-Sierra *Doctrine: Some Answers, More Questions*, 30 ENERGY L.J. 53 (2009); David G. Tewksbury & Stephanie S. Lim, *Applying the* Mobile-Sierra *Doctrine to Market-Based Rate Contracts*, 26 ENERGY L.J. 437 (2005); Carmen L. Gentile, *The* Mobile-Sierra *Rule: Its Illustrious Past and Uncertain Future*, 21 ENERGY L.J. 353 (2000).

18. This article only briefly addresses the substantive effect of applying *Mobile-Sierra*, a topic that would require a separate article to address in any depth. In particular, this article is not intended to focus on the differences between the public interest standard under *Mobile-Sierra*, the new more rigorous just and reasonable standard under *Devon Power*, and the traditional just and reasonable standard or the particular factors that the FERC may or should consider in determining whether a party seeking rate modification has met its burden under any of those standards.

19. NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693, 701 (2010) (Stevens, J., dissenting).

20. *Id.* at 702.

> and reasonable, applies to "rate challenges by noncontracting parties."[21]

A. The First Chapter: Mobile*,* Sierra*, and* Memphis

The "first chapter"[22] of the *Mobile-Sierra* story was written over a half a century ago in the Supreme Court's *Mobile* and *Sierra* opinions. In both of those cases, a utility made a filing with the Commission seeking to modify the rate set forth in a voluntarily-negotiated contract with a buyer. And, in each case, the Court found that the Commission had erred in accepting the revised rates, emphasizing that the FPA and the NGA "evince[] no purpose to abrogate private rate contracts" but instead "expressly recognize[] that rates to particular customers may be set by individual contracts."[23] Discussing ratemaking under the relevant provisions of the FPA (sections 205 and 206)[24] and the NGA (sections 4 and 5),[25] the Court explained:

> [E]xcept as specifically limited by the Act, the rate-making powers of natural gas companies were to be no different from those they would possess in the absence of the Act: to establish *ex parte*, and change at will, the rates offered to prospective customers; or to fix by contract, and change only by mutual agreement, the rate agreed upon with a particular customer.[26]

The Court described the conclusion that nothing in the FPA or the NGA "empower[s] [regulated] companies unilaterally to change their contracts" as being in accord with the statutes, because "[b]y preserving the integrity of contracts, it permits the stability of supply arrangements which all agree is essential to the health of the . . . industry."[27] At the same time, preventing utilities from unilaterally modifying "their contracts in no way impairs the regulatory powers of the Commission, for the contracts remain fully subject to the paramount power of the Commission to modify them when necessary in the public interest."[28]

Emphasizing that the purpose of the Commission's power to modify rates *sua sponte* or upon complaint "is the protection of the public interest, as distinguished from the private interests of the [regulated sellers]," the Court stated that while the Commission "may not normally impose upon a public utility a rate which would produce less than a fair return," a utility that had voluntarily "agree[d] by contract to a rate affording less than a fair return" should not necessarily be "entitled to be relieved of its improvident bargain."[29] In such cases, the Commission's "sole concern . . . would seem to be whether the rate is so low as to adversely affect the public interest — as where it might

21. *Id.* at 703.
22. *Id.* at 701.
23. United Gas Pipe Line Co. v. Mobile Gas Serv. Co., 350 U.S. 332, 338 (1956).
24. 16 U.S.C. §§ 824d, 824e (2006).
25. 15 U.S.C. §§ 717c, 717d (2006).
26. *Mobile*, 350 U.S. at 343.
27. *Id.* at 344.
28. *Id*.
29. FPC v. Sierra Pac. Power Co., 350 U.S. 348, 355 (1956) (citation omitted).

impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory."[30]

Two years later, the Court revisited the *Mobile-Sierra* doctrine in *United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division* (*Memphis*).[31] In that case, a court of appeals held that a seller that had contracted to provide service at the rate set forth in a specified rate schedule was precluded under *Mobile-Sierra* from unilaterally applying to the Commission to modify the rate.[32] The Supreme Court reversed, finding that the contract before it was "vitally different" from that in *Mobile*[33] and holding that *Mobile-Sierra* is inapplicable to rates set through a "tariff-and-service-agreement system."[34] In particular, the Court explained that the regulated seller in *Memphis* "bound itself to furnish [service] to these customers during the life of the agreements not at a single *fixed rate*, . . . but at what in effect amounted to its current *'going' rate*."[35] The reason that the seller in *Mobile* did not have the option of making unilateral application to the Commission to increase its rates "was because [it] had bargained away . . . the right to change its rates unilaterally."[36] Thus, the "important and indeed decisive difference" between *Memphis* and *Mobile* was that "in *Mobile* one party to a contract was asserting that the [statute] somehow gave it the right unilaterally to abrogate its contractual undertaking, whereas here [the seller] seeks simply to assert, in accordance with the procedures specified by the Act, rights expressly reserved to it by contract."[37] As such, the Court "perceive[d] no tenable basis of distinction" between the filing of a rate determined ex parte by the seller "in the absence of [a] contract and a similar filing under an agreement which expressly permits it."[38]

In a dissenting opinion, Justice Douglas, joined by two other justices who had also participated in the unanimous *Mobile* and *Sierra* decisions, objected to the majority's holding in *Memphis* as a "retreat" from *Mobile*, whose "essence," he argued, was that regulated sellers lack the statutory power "'unilaterally to change their contracts.'"[39] In so doing, Justice Douglas argued, the majority's decision in *Memphis* "makes a shambles of the Act so far as consumer interests are concerned; and they are the ones the Act was designed to protect."[40]

30. *Id*. In *Morgan Stanley*, the Court clarified that the three public interest factors set forth in *Sierra* were illustrative only and are "not the exclusive components of the public interest." Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 549 (2008).

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

32. *Id.* at 108.

33. *Id.* at 110.

34. *Id.* at 115 n.8.

35. *Id.* at 110 (emphasis added).

36. *Id.* at 111.

37. *Id.* at 112.

38. *Id.* at 112-13.

39. *Id.* at 116-17 (quoting *Mobile,* 350 U.S. at 344) (Douglas, J., dissenting).

40. *Id.* at 118-19.

B. The Second Chapter: Morgan Stanley

After *Memphis*, the Court did not again focus on when and how the *Mobile-Sierra* doctrine applies for another half century.[41] In *Morgan Stanley*, the Court addressed a series of complaints by two Nevada utilities (together, Nevada Power) and other buyers under long-term power sales contracts seeking to abrogate, or lower the rate set forth in, contracts that were allegedly overpriced as a result of market dysfunctions and manipulation during the California energy crisis of 2000-2001.[42] Echoing Justice Douglas's dissent in *Memphis*, the buyers and their supporters argued, and the Ninth Circuit agreed, that the FPA was intended to protect consumers and that the *Mobile-Sierra* doctrine should therefore be ignored or relaxed in favor of lowering consumers' rates.[43]

The Supreme Court disagreed, finding that "[t]he standard for a buyer's challenge must be the same, generally speaking, as the standard for a seller's challenge: The contract rate must seriously harm the public interest."[44] The Court further recognized that "contract stability ultimately benefits consumers, even if short-term rates for a subset of the public might be high by historical standards – which is why [the FPA] permits rates to be set by contract and not just by tariff."[45]

The Court also explained that the *Mobile-Sierra* doctrine "was grounded in 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.'"[46] As a result, the fact that the FERC had not substantively reviewed and determined the contracts to be just and reasonable at their inception did not exempt such contracts from the limitations of *Mobile-Sierra*. To the contrary, *Morgan Stanley* made clear that *the FERC* is bound by the *Mobile-Sierra* doctrine and "must presume that the rate set out in a freely negotiated . . . 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."[47]

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41. That is not to say that the Supreme Court was completely silent on the subject of the *Mobile-Sierra* doctrine during the intervening 50 years. *See, e.g.,* Verizon Commc'ns Inc. v. FCC, 535 U.S. 467, 479 (2002). Nonetheless, neither *Verizon* nor any of the Court's other decisions citing *Mobile* or *Sierra* during this period did much more than mention the doctrine in dicta.

42. Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 540-41 (2008).

43. Public Util. Dist. No. 1 of Snohomish Cnty. v. FERC, 471 F.3d 1053, 1089 (9th Cir. 2006).

44. *Morgan Stanley*, 554 U.S. at 548.

45. *Id.* at 551.

46. *Id.* at 545 (quoting *Verizon*, 535 U.S. at 479). The Supreme Court apparently did not find the fact that the electric industry was "historically characterized by natural monopoly and therefore subject to abuses of market power" to impede parties' ability to negotiate just and reasonable contracts. *Id.* at 531. The Court also made it clear that neither generalized assertions that spot market manipulation and dysfunction resulted in abnormally high contract rates nor dissatisfaction with the FERC's market-based rate regime were, by themselves, sufficient to justify stripping contracts of *Mobile-Sierra* protections. *Id.* at 547-48; *see also* Northeast Utils. Serv. Co. v. FERC, 993 F.2d 937, 961 (1st Cir. 1993) (rejecting argument that a seller's market power should automatically strip a contract of *Mobile-Sierra* protections because "some measure of market power could be present in a large number of contracts" and "it is not entirely clear . . . why the Commission should protect a buyer who voluntarily enters into an agreement with a dominant seller").

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

Focusing on *Morgan Stanley*'s finding that *Mobile-Sierra* is equally applicable to buyers and sellers, Justice Stevens characterized this "second chapter" of *Mobile-Sierra* as "unwisely and incorrectly [holding] that the [*Mobile-Sierra*] rule should apply to a buyer who had been forced by unprecedented market conditions to enter into a long-term contract to buy energy at abnormally high prices."[48] But while *Morgan Stanley* may have been the first time the Supreme Court spoke to this issue directly, the Court's decision hardly came out of the blue. Indeed, *Memphis* strongly implied that *Mobile-Sierra* should apply equally to seller-side and buyer-side complaints by making clear that the doctrine is about respecting contracts and is not, as Justice Douglas suggested in his *Memphis* dissent, exclusively about constraining regulated sellers for the benefit of consumers.[49] In addition, the notion that both buyer and seller are equally bound by their contractual obligations follows naturally from the Supreme Court's prior recognition in *Verizon* that *Mobile-Sierra* permits "sophisticated businesses . . . to negotiate a 'just and reasonable' rate as between the two of them."[50]

Courts of appeal (other than the Ninth Circuit) also applied *Mobile-Sierra* equally to buyers and sellers prior to *Morgan Stanley*. For example, the D.C. Circuit affirmed the FERC's decision to uphold transmission rates set by a pre-open access contract, despite the buyer's complaint that the contract rates were at least double those set forth in the transmission provider's open access transmission tariff.[51] Similarly, the First Circuit first overturned the FERC's attempt to reduce contract rates without considering the public interest standard under the *Mobile-Sierra* doctrine[52] and, then, affirmed the FERC's order on remand finding the same rate reductions to be necessitated by the public interest.[53] In another case involving an attempt to reduce a contract rate, the First Circuit warned the FERC to "stop trying to re-write deals that the parties have . . . made under the aegis of *Mobile-Sierra* — unless it properly invokes the public interest standard."[54] Elsewhere, the First Circuit observed that it is

48. NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693, 702 (2010) (Stevens, J., dissenting).

49. United Gas Pipe Line Co. v. Memphis Light, Gas and Water Div., 358 U.S. 103, 113 (1958) ("United, like the seller of an unregulated commodity, has the right in the first instance to change its rates as it will, unless it has undertaken by contract not to do so.").

50. Verizon Commc'ns Inc. v. FCC, 535 U.S. 467, 479 (2001).

51. Potomac Elec. Power Co. v. FERC, 210 F.3d 403, 409 (D.C. Cir. 2000).

52. Northeast Utils. Serv. Co. v. FERC, 993 F.2d 937, 960-62 (1st Cir. 1993).

53. Northeast Utils. Serv. Co. v. FERC, 55 F.3d 686, 692-93 (1st Cir. 1995) (finding that the "FERC ha[d] done more on remand than simply substitute the words 'public interest' for the forbidden phrase 'just and reasonable'"). At the same time, language in that decision suggested that the *Mobile-Sierra* public interest standard might be applied differently depending on whether a party was attempting to raise or lower the contract rate. *Id.* at 691 (although the public interest standard had been characterized as being "practically insurmountable" in a case where a buyer was attempting to raise the contract rate, "[w]e do not think that . . . the 'public interest' standard is practically insurmountable in all circumstances. It all depends on whose ox is gored and how the public interest is affected."). The Supreme Court, however, rejected that proposition. *Morgan Stanley*, 554 U.S. at 548 ("The standard for a buyer's challenge must be the same, generally speaking, as the standard for a seller's challenge."); *id.* at 551 n.6 ("[T]he circumstances identified in *Sierra* as implicating the public interest refer to something more than a small dent in the consumer's pocket, which is why our subsequent cases have described the standard as a high one.").

54. Boston Edison Co. v. FERC, 233 F.3d 60, 68 (1st Cir. 2000).

"logically inferable" that a buyer, as well as a seller, is not "'entitled to be relieved of its improvident bargain.'"[55]

III. THE THIRD CHAPTER: *NRG*

A. *The Court's Decision*

Less than two years after *Morgan Stanley*, another *Mobile-Sierra* dispute came before the Supreme Court.[56] In that case, a large number of participants in wholesale electricity markets administered by ISO New England Inc. (ISO-NE) had reached a settlement resolving disputes regarding ISO-NE's capacity market.[57] The settlement established a market in which capacity would be procured three years in advance of its use through annual auctions.[58] The settlement also specified that the *Mobile-Sierra* doctrine would apply to future challenges to the auction results, as well as to payments during a specified transition period.[59] The FERC ultimately approved the contested settlement, with 107 parties supporting the agreement and eight parties opposed.[60] On appeal, the D.C. Circuit found that applying *Mobile-Sierra* to challenges by non-settling parties that had "vociferously objected" to the settlement "unlawfully deprived [those] parties of their rights under the [FPA],"[61] and therefore concluded that "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply."[62]

Only one question was brought to the Supreme Court: Does "*Mobile-Sierra's* public-interest standard appl[y] when a contract rate is challenged by an entity that was not a party to the contract[?]"[63] Reversing the D.C. Circuit, the Court held that "the *Mobile-Sierra* presumption does not depend on the identity of the complainant who seeks FERC investigation. The presumption is not limited to challenges to contract rates brought by contracting parties. It applies, as well, to challenges initiated by third parties."[64] For its part, the majority viewed this holding as a natural extension of the second chapter of *Mobile-Sierra*, asking "if FERC itself must presume just and reasonable a contract rate resulting from fair, arms-length negotiations," as made clear in *Morgan Stanley*, "how can it be maintained that non-contracting parties nevertheless may escape the presumption."[65] The Court further explained that applying the doctrine to non-parties did not deprive them of any rights or protections as "the *Mobile-Sierra* doctrine does not overlook third-party interests; it is framed with a view to their protection. The doctrine directs the Commission to reject a contract rate

55. Boston Edison Co. v. FERC, 856 F.2d 361, 372 (1st Cir. 1988) (quoting *Northeast Utils*., 55 F.3d at 692).

56. NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693 (2010).

57. *Devon Power LLC*, 115 F.E.R.C. ¶ 61,340 at P 2 (2006).

58. *Id.* at P 16.

59. *Id.* at P 36.

60. *Id.* at P 15.

61. Maine Pub. Utils. Comm'n v. FERC, 520 F.3d 464, 467 (D.C. Cir. 2008).

62. *Id.* at 478.

63. NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693, 698 (2010).

64. *Id.* at 701.

65. *Id.* at 700.

that 'seriously harms the consuming public.'"[66] Justice Stevens, on the other hand, described the *NRG* decision as a "quantum leap" from *Mobile* and *Sierra* and characterized the majority's decision as "impos[ing] a special burden on third parties exercising their statutory right to object to unjust and unreasonable rates."[67]

Notwithstanding Justice Stevens's objections, it is fair to say that the third chapter was no more surprising than the second chapter. For example, in a 1993 decision, the First Circuit implicitly found the *Mobile-Sierra* doctrine to be applicable to third-party challenges when it rejected the FERC's attempt, in response to a protest by a non-party,[68] to modify a contract between a traditional utility and its prospective affiliate on the grounds that the FERC had "conflate[d] the 'just and reasonable' and 'public interest' standards, thereby circumventing the *Mobile-Sierra* doctrine."[69]

Moreover, the facts underlying *Morgan Stanley* belie the notion that there was any general perception that *Mobile-Sierra* was inapplicable, or even that it applied differently, to third-party challenges. As explained above, in that case, Nevada Power filed complaints seeking to reform contracts with various suppliers. Nevada Power's complaints were actively supported before the FERC and in the courts by the Office of the Nevada Attorney General, Bureau of Consumer Protection (Nevada BCP), as an intervenor. Had there been some general perception, or even a remote hope, that a third party challenge would be allowed to escape the restraints of *Mobile-Sierra*, one would have expected that the Nevada BCP would have been the party to file the complaints.[70]

Finally, as the Court itself recognized, the decision in *NRG* follows logically from *Morgan Stanley*. As indicated, *Morgan Stanley* characterized *Mobile-Sierra* not only as binding on the contracting parties but as tying the hands of the Commission, the quintessential third party arbiter. It would make

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66. *Id*.

67. *Id.* at 701 (Stevens, J., dissenting).

68. *Northeast Utils. Serv. Co. (Re Pub. Serv. Co. of N.H.)*, 50 F.E.R.C. ¶ 61,266, at pp. 61,831-32, 61,837-39 (1990) (describing protest by the Massachusetts Municipal Wholesale Electric Cooperative to proposed rate of return and setting issue for hearing), *reh'g denied*, 51 F.E.R.C. ¶ 61,177, *clarified*, 52 F.E.R.C. ¶ 61,046 (1990). The First Circuit's 1993 decision addressed petitions for review of the FERC's orders issued following a hearing required by the preceding orders. Northeast Utils. Serv. Co. v. FERC, 993 F.2d 937 (1st Cir. 1993).

69. *Northeast Utils.*, 993 F.2d at 961.

70. A few months after Nevada Power filed its complaints, similar complaints were filed by the California Public Utilities Commission (CPUC) and the California Electricity Oversight Board (CEOB) to challenge contracts under which the California Department of Water Resources (CDWR) agreed to purchase electricity from various suppliers. The CPUC and CEOB unsuccessfully argued that as non-contracting parties, they should not be bound by *Mobile-Sierra*. *Public Utils. Comm'n of the State of Cal. v. Sellers of Long Term Contracts to the Cal. Dept. of Water Res.*, 99 F.E.R.C. ¶ 61,087, at p. 61,383 (2002). Nonetheless, it appears that the fact that the complaints were brought by the CPUC and the CEOB, and not CDWR, may have had less to do with any expectation about being able to avoid the strictures of the *Mobile-Sierra* doctrine than with concerns over potential exposure if CDWR had challenged certain contracts itself. *See*, *e.g.,* CAL. STATE AUDITOR, CALIFORNIA ENERGY MARKETS: PRESSURES HAVE EASED, BUT COST RISKS REMAIN 162 (Dec. 2001) (describing contracts under which CDWR agreed not to petition the FERC to modify contract rates, including one contract under which the seller could "declare a default and demand the termination payment" if CDWR "engages in an action that results in a provision of the contract being declared unenforceable or that reduces the contract price or amounts payable under the contract"), *available at* http://www.bsa.ca.gov/pdfs/reports/2001-009.pdf.

no sense to require the FERC to presume that a contract is just and reasonable[71] if any interested (or even uninterested) non-contracting party could then negate that presumption simply by objecting. Indeed, such an approach would appear to "give short shrift to the important role of contracts in the FPA."[72] *Morgan Stanley* further emphasized that *Mobile-Sierra* does not tolerate unjust and unreasonable rates but, instead, "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context."[73] This characterization of the doctrine casts serious doubt on the D.C. Circuit's suggestion that third parties had to be exempted from the application of *Mobile-Sierra* in order to preserve their rights to just and reasonable rates.[74]

B. *Application of* Mobile-Sierra *After* NRG

NRG provides valuable certainty to parties negotiating contracts by resolving lingering questions about potential third party interference with contractual arrangements. As an initial matter, although *Morgan Stanley* made it clear that the Court looked unfavorably on any "disfigurement of the venerable *Mobile-Sierra* doctrine,"[75] the D.C. Circuit's *Maine Public Utilities Commission* decision illustrated that substantial questions remained regarding the impact of *Mobile-Sierra* on the FERC's obligations under the FPA to protect the well-being of consumers. Indeed, although, as explained above, *NRG* seemed a natural and predictable outgrowth of *Morgan Stanley*, various parties continued to urge the FERC not to apply *Mobile-Sierra* to third party complaints.[76] The Court's unequivocal holding that *Mobile-Sierra* "applies . . . to challenges initiated by third parties"[77] should eliminate such disputes in the future.

In addition, *NRG* provides at least some clarity on how the FERC is required to handle settlements. In particular, *NRG* would appear to preclude the return of a somewhat confusing policy adopted by the FERC, where it considered itself to have "the discretion to decline to be . . . bound" by *Mobile-Sierra* in "limited circumstances," such as when evaluating settlement agreements with "broad applicability."[78] In practice, however, *Mobile-Sierra*

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71. Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 530 (2008).

72. *Id.* at 551.

73. *Id.* at 546.

74. As described above, the Supreme Court also reiterated in *NRG* that the *Mobile-Sierra* standard is specifically "framed with a view to [third parties'] protection." NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693, 700 (2010).

75. *Morgan Stanley*, 554 U.S. at 548.

76. *See, e.g.*, Brief of the Public Utilities Commission of California as *Amicus Curiae* in Support of Respondent at 5, NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693 (2010) (No. 08-674) (arguing that, "[a]t the very least," *Mobile-Sierra* should not apply "when the rate is challenged by a state public utility commission"); Motion for Leave to Answer and Answer of the Public Utilities Commission of the State of California to Answer of Indicated Sellers and Answer of Sempra Generation at 8, FERC Docket Nos. EL02-60-003, EL02-62-003 (Feb. 9, 2009) ("*Morgan Stanley* sheds no light on the issue of whether challenges to a wholesale contract brought by a State commission that was not a party to the wholesale contract at issue can be subject to the *Mobile-Sierra* presumption that the contract is just and reasonable.").

77. *NRG*, 130 S. Ct. at 701.

78. *Los Esteros Critical Energy Facility, LLC*, 117 F.E.R.C. ¶ 61,350 at n.3 (2006); *see also Enron Power Mktg., Inc.*, 117 F.E.R.C. ¶ 61,109 at n.10 (2006); *Connecticut Mun. Elec. Energy Coop. v. Milford Power Co., LLC*, 122 F.E.R.C. ¶ 61,235 at P 26 (2008); *Midwest Indep. Transmission Sys. Operator, Inc.*, 119

protections were most frequently withheld from settlements resolving disputes over reliability must-run (RMR) agreements to which both the regulated seller and the customer had agreed,[79] even as such protections were approved with respect to settlements involving market rules and tariffs of general applicability.[80] The FERC explained its refusal to apply *Mobile-Sierra* protections to one RMR settlement as follows:

> RMR agreements suppress market-clearing prices and deter investment in new generation. Moreover, the market participants that pay for the agreements pay out-of-market prices for the service provided under the RMR agreements, which broadly hinders market development and performance. As a result of these factors, we have concluded that RMR agreements should be used as a last resort.[81]

This reasoning, which could apply equally to any number of other bilateral contracts, suggests that the FERC's decision was less about the breadth of the agreements' applicability than about other policy concerns about RMR contracts, leading to concerns that the applicability of *Mobile-Sierra* to settlements could turn on the FERC's policy goals at a specific time.

In light of *NRG*, however, it appears that such an approach would not withstand serious scrutiny, at least with respect to contract rates established by settlements. Specifically, the Supreme Court did not distinguish between fixed-rate contracts in, or arising out of, settlement agreements and other fixed-rate contracts and reiterated, "[i]n unmistakably plain language," that the FERC "must presume" that wholesale contracts are just and reasonable, unless the FERC "concludes that the contract seriously harms the public interest."[82] Thus, while leaving open the question of whether the FERC has the discretion to treat non-contract rates "analogously,"[83] the Court made it clear that, if rates agreed by settlement "qualify as 'contract rates,'"[84] the FERC is obligated to apply the

F.E.R.C. ¶ 61,129 at n.4 (2007); *Northwest Pipeline Corp.*, 118 F.E.R.C. ¶ 61,272 at n.3 (2007); *Bridgeport Energy, LLC*, 118 F.E.R.C. ¶ 61,243 at P 42 (2007); *Entergy Ark., Inc.*, 118 F.E.R.C. ¶ 61,217 at n.3 (2007); *National Fuel Gas Supply Corp.*, 118 F.E.R.C. ¶ 61,091 at n.2 (2007); *Pine Needle LNG Co.*, 118 F.E.R.C. ¶ 61,078 at n.3 (2007); *Williams Power Co.*, 117 F.E.R.C. ¶ 61,328 at n.9 (2006); *Dayton Power & Light Co.*, 117 F.E.R.C. ¶ 61,234 at n.1 (2006); *Transcontinental Gas Pipe Line Corp.*, 117 F.E.R.C. ¶ 61,232 at P 8 (2006); *Northern Border Pipeline Co.*, 117 F.E.R.C. ¶ 61,217 at P 8 (2006); *Southwest Power Pool, Inc.*, 117 F.E.R.C. ¶ 61,207 at P 29 (2006); *Westar Energy, Inc.*, 117 F.E.R.C. ¶ 61,172 at n.1 (2006); *Midwest Indep. Transmission Sys. Operator, Inc.*, 117 F.E.R.C. ¶ 61,156 at n.1 (2006); *Entergy Servs., Inc.*, 117 F.E.R.C. ¶ 61,155 at n.2 (2006); *Pacific Gas & Elec. Co.*, 117 F.E.R.C. ¶ 61,154 at n.2 (2006). This policy was based on a 2006 D.C. Circuit decision affirming orders in which the FERC declined to apply *Mobile-Sierra* to an agreement. Maine Pub. Utils. Comm'n v. FERC, 454 F.3d 278, 286-97 (D.C. Cir. 2006).

79. *Bridgeport Energy, LLC*, 118 F.E.R.C. ¶ 61,243 at P 42 (2007). *See, e.g., Los Esteros Critical Energy Facility, LLC*, 117 F.E.R.C. ¶ 61,350 at P 3 (2006); *Williams Power Co.*, 117 F.E.R.C. ¶ 61,328 at P 5 (2006).

80. *See, e.g., Northwest Pipeline Corp.*, 118 F.E.R.C. ¶ 61,272 at PP 2-3 & n.3 (2007) (finding that "the [*Mobile-Sierra*] public interest standard should apply" to a settlement involving a "general rate increase" that would, among other things, establish a "two-year moratorium . . . on [the pipeline] or any other party . . . proposing any [NGA] section 4 or section 5 to the levels of the [pipeline]'s general rates"); *Southwest Power Pool, Inc.*, 117 F.E.R.C. ¶ 61,207 at P 29 (2006) (allowing the parties to a settlement relating to the Southwest Power Pool, Inc.'s imbalance markets to bind the FERC to a *Mobile-Sierra* public interest standard, "because it provides the parties needed certainty").

81. 118 F.E.R.C. ¶ 61,243 at P 42 (internal citations omitted).

82. *NRG*, 130 S. Ct. at 700.

83. *Id.* at 701.

84. *Id.*

Mobile-Sierra presumption to any and all challenges to those rates[85] (unless, of course, the contracting parties have opted out of the *Mobile-Sierra* regime through a *Memphis* clause.)[86]

There are several possible scenarios in which a settlement could provide for rates that would qualify as contract rates subject to *Mobile-Sierra*. In the simplest case, the settlement agreement could itself fix a rate at which the public utility would provide a FERC-jurisdictional service to a particular customer (or customers), with the understanding that such rate will be subject to "change only by mutual agreement."[87] In that circumstance, the settlement agreement itself would be a fixed-rate contract, and the *Mobile-Sierra* presumption would apply to the FERC's initial review of the settlement agreement[88] and to subsequent challenges to the rates, terms, and conditions set forth therein.

Alternatively, a contract rate could result, directly or indirectly, from the provisions of the settlement. For instance, if a settlement package includes a fixed-rate contract or provides that the settling parties will execute a fixed-rate contract upon approval of the settlement, then the contract rate results directly from the provisions of the settlement. Similarly, if a settlement agreement establishes a process that results in the settling parties (or non-settling parties, for that matter) entering into fixed-rate contracts, a contract rate results indirectly from the provisions of the settlement. In either case, the fact that the rate-making process is the product of a settlement does not alter the nature of the resulting fixed-rate contracts, which should enjoy all of the protections of the *Mobile-Sierra* doctrine.[89]

85. Despite the apparently clear language in *NRG*, the D.C. Circuit on remand somewhat confusingly couched the application of *Mobile-Sierra* to contract rates established by settlement in permissive, rather than mandatory, terms, stating that the "FERC *can* approve a settlement agreement requiring adjudication of any rates resulting from that settlement agreement under *Mobile-Sierra* if the resultant rates are contract rates." Maine Pub. Utils. Comm'n v. FERC, 625 F.3d 754, 757 (D.C. Cir. 2010) (emphasis added); *see also id.* at 759 (*NRG* held that "*Mobile-Sierra could* apply to a rate challenge brought by a non-contracting party.") (emphasis added). This characterization cannot be squared with the Supreme Court's characterization of the doctrine. *See, e.g., NRG*, 130 S. Ct. at 696 (explaining that the "FERC *must* presume that a rate set by 'a freely negotiated wholesale-energy contract' meets the statutory 'just and reasonable' requirement") (emphasis added) (quoting *Morgan Stanley*, 554 U.S. at 530).

86. As the name suggests, a *Memphis* clause reflects the parties' agreement that the buyer will pay the going rate set forth in the service provider's tariff, rather than a fixed rate established in the contract, and is the means by which contracting parties may opt out of *Mobile-Sierra*.

87. United Gas Pipe Line Co. v. Mobile Gas Serv. Co., 350 U.S. 332, 343 (1956). That understanding could be reflected in express language in the settlement agreement or by the absence of a *Memphis* clause, because the general rule is that "absent contractual language 'susceptible to the construction that the rate may be altered while the contract[] subsist[s],' the *Mobile-Sierra* doctrine applies." Texaco Inc. v. FERC, 148 F.3d 1091, 1096 (D.C. Cir. 1998) (quoting Appalachian Power Co. v. FPC, 529 F.2d 342, 348 (D.C. Cir. 1976)).

88. Any interpretation of the FERC's procedural rules governing review of settlements as excusing the FERC from the obligation to apply *Mobile-Sierra* in its initial review of a settlement agreement that is a fixed-rate contract would improperly subordinate the substantive requirements of the organic statutes, in contravention of the principle that a regulation which "operates to create a rule out of harmony with the statute, is a mere nullity." Manhattan Gen. Equip. Co. v. Comm'r, 297 U.S. 129, 134 (1936). *See also* Dixon v. United States, 381 U.S. 68, 74 (1965).

89. Although these guiding principles may appear relatively straightforward at first blush, they may not always be easy to implement in practice. Under established contract law principles, the result of an auction should be considered to establish a contract, as an auction participant's bid is an "offer" that may be "accept[ed]" by the auctioneer "by the fall of the hammer or in other customary manner." U.C.C. § 2-328(2) (2010). *See also* RESTATEMENT (SECOND) OF CONTRACTS § 28(1)(a) (1981); 1 SAMUEL WILLISTON &

IV. THE "FOURTH CHAPTER": *DEVON POWER*

A. The FERC's Decision

Although, as discussed above, the Supreme Court in *NRG* confirmed that *Mobile-Sierra* applies when non-parties challenge contract rates, it remanded the case to the D.C. Circuit to consider "[w]hether the rates at issue qualify as 'contract rates,' and, *if not, whether FERC had discretion to treat them analogously*."[90] Because the FERC had not addressed these questions in its orders below, the D.C. Circuit, in turn, remanded back to the FERC.[91]

On remand, the FERC, in *Devon Power,* found that auction rates in that case "are not 'contract rates' that, under *Mobile-Sierra*, require a presumption that the rates are statutorily just and reasonable."[92] This determination was apparently based on the fact that the auctions conducted in accordance with the terms of the settlement would "apply to all suppliers and purchasers of capacity within the [ISO-NE] market, not just to the settling parties."[93] As a result, the FERC stated, "the rates set by the forward capacity auctions represent tariff, not contract, rates" because they are determined using a methodology that "applies even to parties who did not agree contractually to its adoption."[94] Proceeding to the Supreme Court's second question, the FERC held that it nonetheless has the "discretion to apply a more rigorous application of the 'just and reasonable' standard of review to future challenges to [such] rates and that it was appropriate to exercise that discretion here."[95] The FERC emphasized, however, that the application of the more rigorous just and reasonable standard to non-contract rates was a matter of discretion, that it would not always be amenable to applying such a standard in the settlement context, and that the application of

RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS § 4:12 (4th ed. 2007); 1 ARTHUR LINTON CORBIN & JOSEPH M. PERILLO, CORBIN ON CONTRACTS § 4.14 (rev. ed. 1993). *Cf.* Robertson v. United States, 343 U.S. 711, 713 (1952) ("The acceptance by the contestants of the offer tendered by the sponsor of the contest creates an enforceable contract."). Nonetheless, there was considerable disagreement about whether the forward capacity auctions at issue in *NRG* resulted in contract rates, and, in fact, the FERC on remand found that "these auctions will not result in contracts between buyers and sellers." *Devon Power LLC*, 134 F.E.R.C. ¶ 61,208 at P 19 (2011). The FERC determined that the auction rates "more closely resemble a tariff rate than a contract rate," because the "rate methodology applies even to parties who did not agree contractually to its adoption." *Id*. at P 13. On one hand, this reasoning is somewhat curious given *NRG*'s holding that non-settling parties can be bound by *Mobile-Sierra*. On the other hand, the FERC's reasoning at least hints at a potentially significant distinction between the forward capacity auctions and the more traditional auctions that inform the contract law principles described above. In the traditional auction, the seller has voluntarily elected to accept, *e.g.*, by the "fall of the hammer," U.C.C. § 2-328(2), a voluntary offer by the buyer. The same cannot necessarily be said of the participants on either side of ISO-NE's forward capacity auctions. As discussed below, even if the FERC is correct that these auctions do not result in contracts, the results may be sufficiently analogous as to warrant application of a more rigorous just and reasonable standard.

90. *NRG*, 130 S. Ct. at 701 (emphasis added).

91. Maine Pub. Utils. Comm'n v. FERC, 625 F.3d 754, 760 (D.C. Cir. 2010).

92. 134 F.E.R.C. ¶ 61,208 at P 9.

93. *Id.* at P 12 (also stating that "[a] non-settling party wishing to participate in the New England capacity market is as bound by the auction as a settling party, and, thus, a non-settling party's obligation to make a payment cannot be said to be based on a contract executed by that party").

94. *Id.* at P 13. As discussed above, the FERC's focus on the fact that there were parties that did not agree to the settlement is hard to reconcile with the Supreme Court holding in *NRG* that non-parties may be bound to a rate agreed to by others.

95. *Id.* at P 14.

such a standard did not preclude the FERC from reviewing the rate in the future.[96]

Dissenting in part, Commissioner Norris viewed the majority's position as being "inconsistent with the fundamental premise of the *Mobile-Sierra* public interest presumption, establish[ing] a policy that will be challenging for the Commission to administer and less protective of consumers, and potentially avoid[ing] our responsibility under the [FPA]."[97] In certain respects echoing Justice Douglas's dissent in *Memphis* and Justice Stevens's dissents in *Morgan Stanley* and *NRG*, Commissioner Norris stated that it "would be an abdication of [the FERC's] FPA responsibility to ensure that rates are just and reasonable, and poor public policy" for the FERC "to decide in advance of . . . future cases to bind a future Commission" to a heightened standard "without knowing the significant change in circumstances with which the Commission may be presented."[98] Commissioner LaFleur also concurred separately to emphasize "the narrow and fact-bound basis of today's decision."[99]

Since *Devon Power*, the Commission has addressed the application of the more rigorous just and reasonable standard in three cases.[100] The Commission found that the settlement agreement at issue in each case did not "warrant binding the Commission to the higher standard,"[101] because the settlements did not reflect "compelling circumstances" that "rise to the extraordinary level of those present in *Devon Power*."[102]

B. The FERC's Authority to Adopt a "More Rigorous" Just and Reasonable Standard

Since its inception, the *Mobile-Sierra* doctrine has been grounded in a recognition that the FPA and the NGA left intact parties' rights to enter into binding obligations by contract,[103] and that the Commission must therefore "respect certain private contract rights in the exercise of its regulatory powers."[104] Moreover, the doctrine is underpinned by "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

96. *Id.* at P 24.

97. *Id.* at p. 62,047 (Norris, Comm'r, dissenting).

98. *Id.* at p. 62,049 (Norris, Comm'r, dissenting).

99. *Id.* at p. 62,049 (LaFleur, Comm'r, concurring).

100. *High Island Offshore Sys., LLC*, 135 F.E.R.C. ¶ 61,105 (2011); *Petal Gas Storage, L.L.C.*, 135 F.E.R.C. ¶ 61,152 (2011); *Southern LNG Co.*, 135 F.E.R.C. ¶ 61,153 (2011).

101. 135 F.E.R.C. ¶ 61,105 at P 23; 135 F.E.R.C. ¶ 61,152 at P 16; 135 F.E.R.C. ¶ 61,153 at P 24.

102. 135 F.E.R.C. ¶ 61,105 at PP 24-25 (2011); 135 F.E.R.C. ¶ 61,152 at PP 17-18 (2011); 135 F.E.R.C. ¶ 61,153 at PP 24-25 (2011).

103. United Gas Pipe Line Co. v. Mobile Gas Serv. Co., 350 U.S. 332, 343 (1956) (The NGA did not change natural gas companies' rights "to establish *ex parte*, and change at will, the rates offered to prospective customers; or to fix by contract, and change only by mutual agreement, the rate agreed upon with a particular customer.").

104. Northeast Utils. Serv. Co. v. FERC, 993 F.2d 937, 960 (1st Cir. 1993). *See also* Atlantic City Elec. Co. v. FERC, 295 F.3d 1, 15 (D.C. Cir. 2002) ("[T]he purpose of the *Mobile-Sierra* doctrine is to preserve the benefits of the parties' bargain as reflected in the contract, assuming that there was no reason to question what transpired at the contract formation stage."); Texaco, Inc. v. FERC, 148 F.3d 1091, 1097 (D.C. Cir. 1998) ("[M]ore is required to justify regulatory intervention in a private contract than a simple reference to the policies served by a particular rule.").

power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them.'"[105] *Devon Power* now begins a new chapter of the *Mobile-Sierra* story by finding that similar protections may be available to non-contract rates, including those set forth in multi-party settlements involving tariffs of general applicability.[106] This new chapter thus extends *Mobile-Sierra*, a doctrine obligating the FERC to protect private contracts, "beyond its foundation."[107] Given the history of, and articulated rationales for, *Mobile-Sierra*, Commissioner Norris poses a fair question as to whether, in the absence of a fixed-rate contract, the FERC should be able to bind itself and future Commissions to a heightened standard of review.[108] But while *Devon Power*'s "more rigorous application of the just and reasonable standard"[109] is not a direct outgrowth of Congress's decision to "preserv[e] the integrity of contracts"[110] as such, there are other compelling factors that would appear to support the FERC's authority to apply such a standard.

As the FERC noted in *Devon Power*, it enjoys broad ratemaking discretion,[111] and it stands to reason that "[g]iven the flexibility inherent in the statutory 'just and reasonable' standard, the Commission may require varying types and degrees of justification for challenges to particular rates or practices, depending on the circumstances."[112] In particular, given the FERC's recognition

105. Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 545 (2008) (quoting *Verizon*, 535 U.S. at 479).

106. Prior to *Devon Power*, the FERC's traditional practice was to regard *Mobile-Sierra* as inapplicable when a customer takes service under a tariff of general applicability. Indeed, the FERC explained that, consistent with *Memphis*, it had adopted a "tariff-and-service agreement" regime for customers to obtain electric transmission service or natural gas transportation service under pro forma service agreements. Notice of Proposed Rulemaking, *Standard of Review for Modifications to Jurisdictional Agreements*, F.E.R.C. STATS & REGS. ¶ 32,596 at PP 5-6 (2005), 71 Fed. Reg. 303 (2006). In such circumstances, the FERC explained, "[t]he just and reasonable standard must apply, since it is provided for in the [service provider's tariff] and in the mandatory form of service agreement in the [service provider's] tariff." *Id.* at P 6. *See also* United Gas Pipe Line Co. v. Memphis Light, Gas and Water Div., 358 U.S. 103, 115 n.8 (1958) (Under the FERC's "tariff-and-service-agreement" regime, the customer is accepting an offer that "does not itself contain a price term, but [would] rather refer[] to rate schedules of general applicability on file with the Commission."); Order No. 890-B, *Preventing Undue Discrimination and Preference in Transmission* Service, 123 F.E.R.C. 61,299, at app. B, Pro Forma Open Access Transmission Tariff, at § 9 (2008) (*Memphis* clause stating that "[n]othing contained in the Tariff or any Service Agreement shall be construed as affecting in any way the right of the Transmission Provider to unilaterally make application to the Commission for a change in rates, terms and conditions, charges, classification of service, Service Agreement, rule or regulation under section 205 of the Federal Power Act and pursuant to the Commission's rules and regulations promulgated thereunder").

107. NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693, 701 (2010) (Stevens, J., dissenting).

108. *Devon Power LLC*, 134 F.E.R.C. ¶ 61,208, at p. 62,047 (2011) (Norris, Comm'r, dissenting).

109. *Id.* at P 1.

110. United Gas Pipe Line Co. v. Mobile Gas Serv. Co., 350 U.S. 332, 344 (1956).

111. 134 F.E.R.C. ¶ 61,208 at PP 15-16. *See also* Montana-Dakota Util. Co. v. Northwestern Pub. Serv. Co., 341 U.S. 246, 251 (1951) ("Statutory reasonableness is an abstract quality represented by an area rather than a pinpoint. It allows a substantial spread between what is unreasonable because too low and what is unreasonable because too high."); Alabama Elec. Coop., Inc. v. FERC, 684 F.2d 20, 27 (D.C. Cir. 1982) ("[G]reat deference is given to FERC's expertise and judgment on the reasonableness of a particular rate proposal-and courts will not be so presumptuous as to hold unlawful a rate approved by the Commission if, even if not in the court's judgment the 'ideal' design, it is nevertheless within a 'zone of reasonableness.'") (footnote and citations omitted).

112. 134 F.E.R.C. ¶ 61,208 at P 16.

that investment in electric and natural gas facilities depends on rate predictability and certainty,[113] the FERC could logically conclude that certain non-contract rates must be shielded from future challenge in order to promote investment or to protect parties that reasonably relied on those rates. For example, in circumstances where market rules were implemented to encourage new supply,[114] it could be reasonable for the FERC to afford those rules some heightened protection from future challenges to avoid disrupting the expectations of investors. Similarly, the application of the more rigorous just and reasonable standard could be justified in situations where parties have entered into settlement or other agreements after protracted bargaining and made future business decisions on the basis that, once approved by the FERC, the agreements will remain in place. In either case, the protection of legitimate expectations and reliance interests[115] would appear to comport with the Supreme Court's directive for the FERC to adopt ratemaking methodologies that reflect an appropriate "balancing of the investor and the consumer interests"[116] and to consider "the

113. *See, e.g., Midwest Indep. Transmission Sys. Operator*, 117 F.E.R.C. ¶ 61,128 at P 26 (2006) ("[A] degree of stability and predictability is crucial to the functioning of businesses and markets and to attracting investment in the utility business."); *Sound Energy Solutions*, 107 F.E.R.C. ¶ 61,263 at P 68 (2004) (finding that "predictability and uniformity in regulatory treatment" will encourage the "significant" and "for the most part, irretrievable" investments needed to develop new liquefied natural gas facilities); *New York Indep. Sys. Operator*, 103 F.E.R.C. ¶ 61,201 at P 31 (2003) (A "more stable and predictable" revenue stream will reduce "the risk to generation investors — and the cost of financing new investment."); *PJM Interconnection, L.L.C.*, 107 F.E.R.C. ¶ 61,112 at P 20 (2004) (explaining that "dependence on price volatility for investment is an inadequate foundation for cost-effective financing of new infrastructure" and that there was a "clear preference for long-term contracts and/or reliable revenue streams"); *PJM Interconnection, L.L.C.*, 115 F.E.R.C. ¶ 61,079 at P 6 (2006) (recognizing that "if the capacity market is to provide sufficient incentives for new entrants, the market must be confident that the capacity construct will continue long enough for entrants to recover their investment costs").

114. *See, e.g., PJM Interconnection, L.L.C.*, 117 F.E.R.C. ¶ 61,331 at P 1 (2006) (approving new "market rules that will enable PJM to obtain sufficient energy to reliably meet the needs of consumers within PJM"); *Devon Power LLC*, 115 F.E.R.C. ¶ 61,340 at P 122 (2006) (accepting locational feature of capacity market in order to "send correct price signals for investment"); *PJM Interconnection, L.L.C.*, 128 F.E.R.C. ¶ 61,157 at P 90 (2009) (approving market rule intended to prevent exercise of buyer-side market power because "[a] capacity market will not be able to produce the needed investment to serve load and reliability if a subset of suppliers is allowed to bid non-competitively"); *New York Indep. Sys. Operator, Inc.*, 122 F.E.R.C. ¶ 61,211 at P 105 (2008) (accepting market power mitigation measures because "properly constructed capacity markets can . . . encourage reliable and efficient levels of investment only if market participants can expect prices that provide a reasonable opportunity to recover the costs of needed investment").

115. Traditional reliance theories are used in the contract context to uphold a promisee's reasonable expectations resulting from the promises of its contracting counterparty. *See, e.g.,* Larry A. DiMatteo & Blake D. Morant, *Contract in Context and Contract as Context*, 45 WAKE FOREST L. REV. 549, 557 (2010); Curtis Bridgeman, *Contracts as Plans*, 2009 U. ILL. L. REV. 341, 351-53 (2009); Randy E. Barnett, *A Consent Theory of Contract*, 86 COLUM. L. REV. 269, 274-76 (1986). Similarly, the application of a heightened standard of review could be justified in the ratemaking context, as parties could be said to reasonably rely on promises made by the Commission to establish a particular set of market rules or provide for a specified level of rate recovery.

116. FPC v. Hope Natural Gas Co., 320 U.S. 591, 603 (1944). The Court further understood, at least in the *Mobile-Sierra* context, that the short-term interests of consumers in lower rates must be balanced against longer-term interests in the health of the industry. Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 551 (2008) ("The FPA recognizes that contract stability ultimately benefits consumers, even if short-term rates for a subset of the public might be high by historical standards — which is why it permits rates to be set by contract and not just by tariff.").

consequences of its orders for the character and future development of the industry."[117]

Heightened protection for certain non-contract rates could also be justified under something akin to the estoppel theories of *Mobile-Sierra* espoused by the Ninth Circuit and the D.C. Circuit. The Ninth Circuit conceived of *Mobile-Sierra* "'as the equivalent of an estoppel doctrine,' whereby an initial Commission opportunity for review prevents the Commission from modifying the rates absent serious future harm to the public interest,"[118] a notion that was squarely rejected by the Supreme Court in *Morgan Stanley*.[119] On remand from *NRG*, the D.C. Circuit also conceded that it had erroneously viewed *Mobile-Sierra* as "a form of estoppel, *i.e.*, a contracting party was not at liberty — short of extraordinary circumstances — to avoid its negotiated contract rate."[120] While the Supreme Court disagreed with the Ninth Circuit's and D.C. Circuit's estoppel theories with respect to *Mobile-Sierra* contract rates, nothing in *Morgan Stanley* or *NRG* precludes application of a more rigorous just and reasonable standard as a form of estoppel with respect to non-contract rates. Such a form of estoppel could operate against the FERC as a result of its substantive review and determination that a rate would "produce just and reasonable" results, which would protect that rate from subsequent attack by any party,[121] or against parties (*e.g.*, parties to a settlement agreement that does not result in contract rates) whose actions or inactions may be deemed to justify limitations on their future ability to challenge the covered rates.[122]

At the same time, it is likely that the courts of appeal will be asked, perhaps on review of *Devon Power*, to address concerns about whether the application of a more rigorous just and reasonable standard represents a dereliction of the FERC's responsibility under the FPA and the NGA to ensure that rates are, and remain, just and reasonable. In particular, *Mobile-Sierra*'s history has been speckled with allegations that the doctrine deprives the FERC of its ability to protect consumers, in violation of its responsibilities under the FPA and the NGA, and it is foreseeable that the same concerns will be raised with respect to the new standard described in *Devon Power*. For example, Commissioner Norris has already suggested that the application of such a standard could represent an "abdication" of the FERC's responsibilities and "poor public policy."[123] The

117. *In re* Permian Basin Area Rate Cases, 390 U.S. 747, 792 (1968) (The FERC should further consider whether a rate will "maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection to the relevant public interests, both existing and foreseeable.").

118. *Morgan Stanley*, 554 U.S. at 546 (citation omitted).

119. *Id*.

120. Maine Pub. Utils. Comm'n v. FERC, 625 F.3d 754, 759 (D.C. Cir. 2010).

121. *Devon Power LLC*, 134 F.E.R.C. ¶ 61,208 at P 19 (2011).

122. As a form of estoppel, heightened protection for non-contract rates would clearly stand apart from the traditional version of *Mobile-Sierra* applied to contract rates, and it will be important for the FERC and the courts to be clear as to the basis for the protection being invoked in a particular case. *See, e.g., Morgan Stanley*, 554 U.S. at 546 (disagreeing with the Ninth Circuit's reading of *Mobile-Sierra* as the equivalent of an estoppel doctrine).

123. 134 F.E.R.C. ¶ 61,208, at p. 62,049 (Norris, Comm'r, dissenting). Similar arguments have been made to oppose the application of *Mobile-Sierra*, including in Justice Stevens's *Morgan Stanley* dissent, which argued that the "FERC cannot abdicate its statutory responsibility to ensure just and reasonable rates through the expedient of a heavy-handed presumption." *Morgan Stanley*, 554 U.S. at 565 (Stevens, J., dissenting).

Supreme Court's determinations in the traditional *Mobile-Sierra* context suggest that these types of allegations may be unavailing. As discussed above, it is not the intent of this article to explore the burdens imposed by the different standards of review that may be applied by the FERC in assessing a rate or contract challenge. Nonetheless, even if the *Devon Power* standard were as stringent as the traditional *Mobile-Sierra* public interest standard, the Supreme Court has made it clear that application of such a standard would not deprive parties of their rights under the FPA, as the public interest standard simply represents a "differing *application* of th[e] just-and-reasonable standard,"[124] and does not prevent the FERC from acting to protect the public.[125] Moreover, while Commissioner Norris also questioned whether the FERC "can or should exercise discretion to . . . bind a future Commission to employing the more rigorous public interest application of the just and reasonable standard without knowing the significant change in circumstances with which the Commission may be presented,"[126] there is nothing unusual or untoward about the FERC taking actions today that limit its flexibility tomorrow. To the contrary, simply by accepting a rate under section 205 of the FPA, something that it does on a daily basis, the FERC constrains its flexibility to modify the rate in the future, because future modifications to that rate may only be ordered upon a finding that it is unjust and unreasonable pursuant to section 206.[127]

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124. *Morgan Stanley*, 554 U.S. at 553; *see also* 134 F.E.R.C. ¶ 61,208 at P 15 ("[T]he FPA requires only that rates be just and reasonable; it does not specify the manner in which that general formulation must be implemented in any particular context.").

125. NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693, 700 (2010) (explaining that the public interest standard "does not overlook third-party interests; it is framed with a view to their protection"); *see also* 134 F.E.R.C. ¶ 61,208 at P 25 (stating that "[t]he Commission's hands are not tied," despite application of the more rigorous just and reasonable standard and that the Commission can still "respond as necessary to the threat of serious harm to the public interest") (citation omitted).

126. 134 F.E.R.C. ¶ 61,208, at p. 62,049 (Norris, Comm'r, dissenting).

127. The courts have recognized that, as a practical matter, it may be more difficult to obtain relief as a complainant under section 206 than as protestor in a section 205 proceeding. *See, e.g.*, Cities of Carlisle & Neola, Iowa v. FERC, 704 F.2d 1259, 1262 (D.C. Cir. 1983) ("It is true that petitioners might suffer various procedural disadvantages in having to proceed via a section 206 rather than a section 205 proceeding. They, rather than the utilities, will bear the burden of proof; and even after successfully meeting this burden, they may be unable to obtain the refunds which would have been available under section 205.") (citations omitted); Municipal Elec. Util. Ass'n of Alabama v. FPC, 485 F.2d 967, 974 (D.C. Cir. 1973) ("[W]e approach the issue cognizant that, once a tariff has passed the Commission's scrutiny under § 205 of the Act and is made applicable to a particular customer, the likelihood of obtaining a rate reduction or alteration in terms or conditions of service by a proceeding under § 206(a) is indeed remote. Not only would the customer bear the heavy burden of showing the tariff had become unlawful in the period since its approval, but the cost and uncertainty of such proceedings make recourse to them problematical."); Alabama Power Co. v. FERC, 933 F.2d 1557, 1571 (D.C. Cir. 1993) (explaining that a party whose rate had been accepted pursuant to section 205 "would still be susceptible to a § 206 investigation, but in that eventuality would not bear the burden of proof and would risk only prospective rate changes") (footnote omitted); City of Winnfield v. FERC, 744 F.2d 871, 874-75 (D.C. Cir. 1984) ("§ 205, unlike § 206, allows the Commission to approve rate increases without a showing that current rates are unjust and unreasonable; it need only find the *proposed* rates to be just and reasonable.").

The Commission has also acknowledged the practical difference in the burden under sections 205 and 206. *Northern States Power Co.*, 53 F.E.R.C. ¶ 61,039, at p. 61,148 (1990) ("In seeking to have its filing reviewed under section 206 rather than section 205, Northern States seeks to shift to the Commission a burden which is properly borne by the proponent of the rate change. Instead of bearing the burden of establishing that the proposed changes in the rates are just and reasonable, as provided by section 205, Northern States would have the Commission bear the burden of instituting a section 206 proceeding to review the proposed changes in

Parties opposing the FERC's decision in *Devon Power* may also argue that, as a practical matter, there is no need for a special just and reasonable standard to promote predictability. Indeed, there have been numerous instances where the FERC has declined to take action that would disturb market expectations,[128] and as discussed below, the D.C. Circuit has also permitted the FERC to uphold settlements based on the application of a more stringent standard. But the fact that the FERC has been able to preserve the expectations of market participants without invoking *Mobile-Sierra* or some other more rigorous standard does not cast doubt on the FERC's *authority* to apply such a standard. At most, it may mean that the FERC would only need to exercise the newly-articulated authority sparingly.

C. Next Steps: Application of the Heightened Standard

As discussed above, it appears reasonable to conclude that the FERC has the authority to adopt a more rigorous just and reasonable standard on a discretionary basis, but certainly, there are outstanding issues the FERC will need to consider in the actual application of that heightened standard in the future.

As an initial matter, given the procedural history of *Devon Power*, there will be a natural inclination to rely on *Mobile-Sierra* precedent relating to fixed-rate contracts to inform any reading and application of *Devon Power*. This could result in a tendency to conflate *Devon Power*'s "more rigorous application of the statutory 'just and reasonable' standard of review"[129] with the *Mobile-Sierra* public interest standard. In *Devon Power*, the FERC was careful to recognize

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the rates, and bear the further burden in such a proceeding of establishing that the changed rates are unjust and unreasonable."); *Philadelphia Elec. Power Co.*, 25 F.E.R.C. ¶ 61,165, at p. 61,455 (1983) (stating that the Commission's prior order "did not indicate an intent to proceed under Section 206 and thereby shift the burden of proof to the staff").

128. *See, e.g., ISO New England, Inc.*, 135 F.E.R.C. ¶ 61,029 at PP 214, 218 (2011) (declining to apply buyer-side market power mitigation measures to new uneconomic entry because the "investment . . . has already occurred," even while acknowledging that the market rule intended to prevent such uneconomic entry "did not effectively address [such] entry"); *New York Indep. Sys. Operator, Inc.*, 133 F.E.R.C. ¶ 61,028 at P 23 (2010) (declining to "reopen finalized invoices" and order refunds because it "would be detrimental to NYISO's markets and its members who had no notice of the errors, but would be negatively impacted by the ordering of refunds for the affected 37 months"); *Texican N. La. Transport, LLC v. Southern Nat'l Gas Co.*, 132 F.E.R.C. ¶ 61,167 at P 51 (2010) (applying a prospective remedy only because "[o]verturning capacity awards is disruptive to the market and upsets expectations"); *Maryland Pub. Serv. Comm'n v. PJM Interconnection, L.L.C.*, 124 F.E.R.C. ¶ 61,276 at P 26 (2008) (finding that "[c]hanging a rate and quantity already determined in accordance with existing tariff provisions on which parties have relied would defeat the purpose of the forward binding commitment, and undo the incentives for new capacity resources"); *Maryland Pub. Serv. Comm'n v. PJM Interconnection, L.L.C.*, 123 F.E.R.C. ¶ 61,169 at P 49 & n.82 (2008) (stating that the Commission "generally exercise[s] [its] discretion over remedies and do[es] not order refunds that require re-running a market"); *Borough of Chambersburg, Pa. v. PJM Interconnection, L.L.C.*, 117 F.E.R.C. ¶ 61,219 at P 65 (2006) (declining to "upset[] customer expectations" where tariff methodology had been properly applied but had resulted in unintended consequences), *reh'g denied*, 119 F.E.R.C. ¶ 61,166 (2007); *Midwest Indep. Transmission Sys. Operator, Inc.*, 117 F.E.R.C. ¶ 61,113 at P 95 (2006) (declining to order refunds when it "'would create substantial uncertainty in the . . . markets and would undermine confidence in them,' and when 'customers cannot effectively revisit their economic decisions'") (internal citations omitted); *Bangor Hydro-Elec. Co. v. ISO New England, Inc.*, 97 F.E.R.C. ¶ 61,339 (2001) (finding that re-running markets even when an error was made "would do far more harm to wholesale electricity markets than is justifiable or appropriate" and be "fundamentally unfair to market participants").

129. 134 F.E.R.C. ¶ 61,208 at P 2.

the differences between these two standards, distinguishing circumstances where it is obligated to apply the *Mobile-Sierra* public interest standard from those in which it may voluntarily approve the application of a more stringent standard to non-contract rates.[130] The distinction between these two standards must be carefully maintained to ensure that *Devon Power* does not, over time, dilute the protections provided under the traditional *Mobile-Sierra* doctrine. In particular, in light of *Morgan Stanley*, it is now plain that the *Mobile-Sierra* public interest standard attaches automatically to contracts; by contrast, the *Devon Power* more rigorous just and reasonable standard only applies with the FERC's approval (*e.g.*, its approval of a settlement providing for a more rigorous just and reasonable standard). In addition, as discussed above, *Morgan Stanley* and *NRG* rejected the conceptions of the Ninth Circuit and the D.C. Circuit, respectively, of *Mobile-Sierra* as a form of estoppel.[131] If, by contrast, *Devon Power*'s heightened standard applied to non-contract rates is to be premised on estoppel theories, a clear delineation from *Mobile-Sierra* will need to be maintained so as to avoid conflict with the Supreme Court's determinations in *Morgan Stanley* and *NRG* that could erode *Mobile-Sierra* protections.

In addition, the FERC should be wary of applying the more rigorous just and reasonable standard based on, and as a means of advancing, its policy goals at any particular point in time. The Commission's past policy of withholding *Mobile-Sierra* protections from RMR agreements illustrates the danger in this regard. As indicated previously, this policy created undue confusion and uncertainty because, despite the Commission's stated concerns regarding the "broad applicability"[132] of such agreements, the disproportionate application of this policy to deny *Mobile-Sierra* protections to RMR agreements, even as they were granted to settlements involving market rules, suggested that the FERC was less focused on the breadth of an agreement's applicability than the nature of the agreement.[133] Moreover, the FERC may be tempted to bestow heightened

130. *Id.* at P 11 (recognizing that "the 'public interest' presumption does not apply, *of its own force*, when the parties have not agreed to set rates by contract") (emphasis added). The FERC was further careful not to state that it was applying the *Mobile-Sierra* standard or the public interest standard to the settlement rates at issue in *Devon Power*; instead, the FERC stated that it was applying a "more rigorous application of the just and reasonable standard." *Id.* at P 2. In its recent orders, the FERC has similarly drawn a distinction between *Mobile-Sierra* contracts and non-contract rates that could potentially be protected under *Devon Power*'s more rigorous just and reasonable standard. *High Island Offshore Sys., LLC*, 135 F.E.R.C. ¶ 61,105 at PP 17-21 (2011) (explaining that the *Mobile-Sierra* presumption did not apply to the non-contract rates at issue in an offer of settlement); *Petal Gas Storage, L.L.C.*, 135 F.E.R.C. ¶ 61,152 at PP 10-14 (2011) (same); *Southern LNG Co.*, 135 F.E.R.C. ¶ 61,153 at PP 17-21 (2011) (same).

131. Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 546 (2008); NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693, 700 & n.4 (2010). *See also* Maine Pub. Utils. Comm'n v. FERC, 625 F.3d 754, 759 (D.C. Cir. 2010) (acknowledging that its earlier decision, overturned in *NRG*, had erroneously viewed *Mobile-Sierra* as "a form of estoppel").

132. *See supra* note 78.

133. As the courts have observed, the FERC's adherence to *Mobile-Sierra* was spotty, at best, because of its continued ambivalence to the doctrine. *See, e.g.,* Boston Edison Co. v. FERC, 233 F.3d 60, 68 (1st Cir. 2000) (stating that the FERC is "becoming hostile to *Mobile-Sierra*"); Sam Rayburn Dam Elec. Coop. v. FPC, 515 F.2d 998, 1005 (D.C. Cir. 1975) (observing that the FERC's "distaste for the *Mobile-Sierra* doctrine is well known"); Borough of Lansdale, Pa. v. FPC, 494 F.2d 1104, 1110 (D.C. Cir. 1974) (stating that the FERC "very much dislikes the *Sierra Mobile* doctrine"). It may be unrealistic to expect the Commission to be any more consistent if it were given free rein to grant or deny the protections of the more rigorous just and reasonable standard on a discretionary basis.

protection as a means to limit review, either by the courts of appeal or future Commissions, of its decisions in heavily contested proceedings. While not necessarily impermissible under the FPA or the NGA, policy-based or strategic applications of the more rigorous just and reasonable standard could, in the long run, produce unpredictable results that could undermine the goals and rationales underlying the creation of that standard.

On a practical level, as Commission Norris pointed out, *Devon Power* potentially creates an "administrative quagmire" for the FERC and parties.[134] This may prove prophetic, as *Devon Power* does not provide guidance on the circumstances under which it may be appropriate for parties to request the more rigorous just and reasonable standard or what kind of demonstration they will need to make to justify such a standard.[135] The remainder of this section discusses circumstances under which the FERC might apply *Devon Power*'s more rigorous just and reasonable standard.

1. Application to Settlements

The application of *Devon Power*'s more rigorous just and reasonable standard to settlements would be consistent with well-established policies concerning settlements, even those that do not establish contract rates. As a general matter, the "policy of the law encourages compromise to avoid the uncertainties of the outcome of litigation as well as the avoidance of wasteful litigation and expense incident thereto."[136] Settlement agreements "should therefore be upheld whenever equitable and policy considerations so permit."[137] The Administrative Procedure Act expressly contemplates that agencies should

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134. 134 F.E.R.C. ¶ 61,208, at p. 62,048 (Norris, Comm'r, dissenting).

135. While not specifically addressed in *Devon Power*, the FERC could conceivably decide that it should undertake a detailed analysis of the impact of the rate on third parties in determining whether to apply the *Devon Power* heightened standard. Such an analysis is not required in the traditional *Mobile-Sierra* setting because, as the Supreme Court has explained, *Mobile-Sierra* contemplates two or more sophisticated parties agreeing by contract to allocate risks and benefits between or among themselves. In an *amicus curiae* brief filed in the *NRG* case, a number of respected economists further explained that there is a compelling economic logic for binding third parties in such a situation, because the efficiencies and incentives of the private contracting process are such that the contracting parties can "be expected to reach allocations of risk and reward that, over the long haul, are economically efficient as to third parties, and to do so without incurring the enormous transaction costs associated with a bargaining process that included all third parties that may ultimately be affected by a contract." Brief of Colin C. Blaydon et al. as *Amici Curiae* in Support of Petitioners at 14, NRG Power Marketing, LLC v. Maine Pub. Utils. Comm'n, 130 S. Ct. 693 (2010) (No. 08-674).

By contrast, outside the fixed-rate contract setting, there may be no similar presumption of free negotiation and arm's-length bargaining, and the FERC and the courts could have greater cause for concern about allowing parties to dictate rules that are not only binding on themselves but also on another party (who may not have agreed to such rules or even existed when such rules were implemented). *See, e.g.,* JOSEPH M. PERILLO, CALAMARI & PERILLO ON CONTRACTS 580 (6th ed. 2009) (noting the general presumption that "parties contract for their own benefit and not for the benefit of a third person") (citations omitted); Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 87-89 (1989) (noting the consensus among academics that "'immutable' rules," those "that parties cannot change by . . . agreement," are generally justifiable in order to protect parties internal or external to the contract); Ian Ayres, *Empire or Residue: Competing Visions of the Contractual Canon*, 26 FLA. ST. U. L. REV. 897, 901-902 (1999) (bargaining constraints may be justified to protect people not in contractual privity to the contract itself).

136. Pfizer Inc. v. Lord, 456 F.2d 532, 543 (8th Cir. 1972). *See also* Leppind v. Mukasey, 530 F.3d 862, 863 (9th Cir. 2008); Bass v. Phoenix Seadrill/78, Ltd., 749 F.2d 1154, 1164 (5th Cir. 1985).

137. Robinson v. Shelby Cnty. Bd. of Educ., 566 F.3d 642, 648 (6th Cir. 2009).

initiate settlement procedures to eliminate the need for "often costly and lengthy formal hearings in those cases where the parties are able to reach a result of their own which the appropriate agency finds compatible with the public interest," and is "of the 'greatest importance' to the functioning of the administrative process."[138] Consistent with these broad policies, the FERC has a longstanding and express policy to encourage settlements in order to "avoid the alternative of costly and often times lengthy litigation before the Commission."[139] Moreover, the FERC has found that settlements are essential "to the orderly and expeditious conduct" of its business as it "could not possibly cope with the flood of business engendered by its jurisdictional statutes if the outcome of a substantial proportion of that business were not the result of voluntary settlements."[140]

Given the recognized benefits of, and policies supporting, settlements, it seems reasonable for the FERC to conclude that procedures should be implemented to reassure settling parties that their settlements will not be casually disregarded in the future, for example, in response to concerns of a market participant that sat on the sidelines during the settlement process or a small subset of naysayers. In fact, beginning with *City of Bethany, Illinois v. FERC*,[141] a decision predating *NRG* by more than 25 years,[142] the D.C. Circuit has affirmed FERC orders affording heightened protection to settlements by analogizing settlements to contracts protected under *Mobile-Sierra*. In *Bethany*, the court recognized that settlements "may not be completely analogous to fixed rate contracts," but nonetheless concluded that the "policies articulated in *Mobile* and *Sierra* support treating a settlement agreement as a factual difference that may justify a rate disparity" without running afoul of the prohibition against undue discrimination in section 205(b) of the FPA.[143] The court further justified its holding by reasoning that, "[l]ike fixed rate contracts, settlements promote market stability and reduce litigation over rate filings" and "settlements would be severely discouraged, if not eliminated, if any resulting price disparities among customers were considered unlawfully discriminatory within the meaning of section 205(b)."[144] A later D.C. Circuit decision described *Bethany* as "extend[ing] the pro-contract policy of the *Mobile-Sierra* doctrine well beyond the circumstances of its origin" and "appl[ying] a weaker but broader variant to agreements falling short of setting a precise rate."[145] *Bethany* and its progeny thus would support the application of a heightened standard to preserve the benefits of settlements.

As a practical matter, the structure of settlements also makes them particularly well-suited to the application of the more rigorous just and reasonable standard. Not only are parties in settlement negotiations typically the same "sophisticated businesses" that the Supreme Court recognized as capable of

138. Pennsylvania Gas & Water Co. v. FPC, 463 F.2d 1242, 1247 (D.C. Cir. 1972).

139. Final Rulemaking, *Procedure for Submission of Settlement Agreements*, F.E.R.C. STATS. & REGS. ¶ 30,061, at 30,430, 44 Fed. Reg. 34,936 (1979) (codified at 18 C.F.R. pts. 1, 2).

140. *Id*.

141. City of Bethany v. FERC, 727 F.2d 1131, 1139 (D.C. Cir. 1984).

142. Interestingly, neither *NRG* nor *Devon Power* makes any mention of *Bethany* or its progeny.

143. *City of Bethany*, 727 F.2d at 1139.

144. *Id*.

145. Union Elec. Co. v. FERC, 890 F.2d 1193, 1194 (D.C. Cir. 1989).

"negotiat[ing] a 'just and reasonable' rate,"[146] but they also enjoy a few distinct advantages over parties negotiating a traditional *Mobile-Sierra* contract. At the very least, parties entering into settlement discussions will have considered their litigation positions and options. In addition, settling parties often will also benefit from the exchange of information (whether voluntary or through FERC-ordered discovery) and input from a FERC Administrative Law Judge and FERC trial staff. Moreover, the FERC and opposing parties have a full opportunity to comment on, and seek additional evidence regarding, the settlement terms,[147] and offers of settlement, even those that are uncontested, will only become effective after substantive review and approval by the FERC.[148] The settlement review process thus allows the FERC to determine if concerns raised by opposing parties are legitimate. For example, the FERC could determine that the settlement terms have been designed without consideration of, or at the expense of, a sector of the industry with less bargaining power, or that an opposing party is threatening the settlement process solely in an attempt to eke out greater concessions for itself. The FERC thus has a clear opportunity to gauge whether the circumstances surrounding the settlement, as well as the settlement terms, warrant the application of a more rigorous just and reasonable standard.

At the same time, the few orders that have been issued since *Devon Power* indicate that the Commission may be reluctant to apply the more rigorous just and reasonable standard to settlements involving "generally applicable" ratemaking issues.[149] Instead, the Commission suggested that the *Devon Power* standard may be applicable where (i) "the issue of price certainty [is] critical," as was the case with the FCM's goal of attracting and retaining investors; (ii) the settlement is "intended to correct serious deficiencies" in the market; or (iii) "demonstrable market forces" contribute to the derivation of the settlement rates.[150]

Of course, once the FERC makes a determination finding it appropriate to apply the more rigorous just and reasonable standard to a settlement agreement, that determination will be binding on future Commissions and third parties.[151] Accordingly, the FERC may be disinclined to grant settling parties heightened protections for extended periods.[152] Indeed, even in its review of settlements prior to *Devon Power*, the Commission declined to approve provisions in

146. Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 545 (2008) (quoting *Verizon*, 535 U.S. at 479).

147. 18 C.F.R. §§ 385.602(f) (permitting parties to submit comments on offers of settlement), 385.602(h) (2010) (the Commission may establish procedures to obtain additional evidence on contested matters).

148. 18 C.F.R. § 385.602(g)(3) (2010) ("An uncontested offer of settlement may be approved by the Commission upon a finding that the settlement appears to be fair and reasonable and in the public interest.").

149. *High Island Offshore Sys., LLC*, 135 F.E.R.C. ¶ 61,105 at P 24 (2011); *Petal Gas Storage, L.L.C.*, 135 F.E.R.C. ¶ 61,152 at P 17 (2011); *Southern LNG Co.*, 135 F.E.R.C. ¶ 61,153 at P 24 (2011).

150. 135 F.E.R.C. ¶ 61,105 at P 24; 135 F.E.R.C. ¶ 61,152 at P 17; 135 F.E.R.C. ¶ 61,153 at P 24.

151. *Devon Power LLC*, 134 F.E.R.C. ¶ 61,208 at PP 2, 14, 17, 25 (2011) (stating that the more rigorous just and reasonable standard would apply to all "future challenges"); *id.* at p. 62,048 (Norris, Comm'r, dissenting) (objecting to the decision to "[b]ind[] a future Commission to the more stringent application of the just and reasonable standard").

152. By contrast *Mobile-Sierra* by default applies throughout the term of the relevant contract, even where the results may be harsh, as in a case where *Mobile-Sierra* protection was afforded to a "perpetual contract[]" that had "already run for 72 years" and under which the seller had "suffered losses in 39 of the past 41 years." Metropolitan Edison Co. v. FERC, 595 F.2d 851, 859 (1979) (Wilkey, J., dissenting).

settlements "purporting to make the term of the agreement and the Commission's approval of its terms and conditions forever, regardless of possible changes in circumstance or policy,"[153] and it is likely that concerns regarding potential changed circumstances would be even more prevalent in the context of a request for application of *Devon Power*'s more rigorous just and reasonable standard. Accordingly, it would likely be beneficial for settling parties seeking application of the *Devon Power* standard to expressly specify how long they believe it is appropriate for the standard to apply, which will reassure the FERC that future rate challenges will only be restricted for a finite period.

2. Application to Non-Settlement Rates

Although *Devon Power* involved a settlement, the FERC did not expressly limit the application of the more rigorous just and reasonable standard to settlement scenarios, and it is foreseeable that parties will seek to push the envelope by seeking to have that heightened standard apply to their unilateral rate filings. In such a situation, the FERC's determination will likely involve a thorough examination of the rate at issue. For example, *Devon Power* suggests that it might be particularly appropriate to apply the more rigorous just and reasonable standard to protect the results of auctions that provide "a market-based mechanism to appropriately value capacity resources based on their location, satisfying cost-causation principles"[154] and ensure "market-disciplined results."[155]

In addition, *Devon Power* also suggests that it would be reasonable for parties to request, and for the FERC to apply, the more rigorous just and reasonable standard to preserve market expectations and promote stability,[156] consistent with the FERC's longstanding approach.[157] For example, it may be reasonable for a party poised to make a substantial investment in new transmission facilities to request that the Commission apply the heightened standard to any rate incentives authorized by the Commission under section 219 of the FPA. In this regard, it is noteworthy that *Devon Power* appears to contemplate the more rigorous just and reasonable standard would only apply on a prospective basis — that is, the FERC would determine at the time of a rate filing whether it is appropriate to apply a heightened standard to "future challenges" to such rate.[158] But given the FERC's recognition of the benefits of rate stability,[159] as well as its rejection of complaints that would disturb market expectations,[160] there remains an open question as to whether the FERC will be

153. *UGI Storage Co.*, 133 F.E.R.C. ¶ 61,073 at P 35 (2010) (noting that "the Commission would not have knowingly approved a provision purporting to make the term of the agreement and the Commission's approval of its terms and conditions forever, regardless of possible changes in circumstance or policy") (citations omitted).

154. 134 F.E.R.C. ¶ 61,208 at P 19.

155. *Id.* at P 20.

156. *Id*.

157. *See supra* note 128.

158. 134 F.E.R.C. ¶ 61,208 at P 2.

159. *See, e.g.*, *id*. at P 20; *see also supra* note 113.

160. *See supra* note 128.

willing to entertain requests to have the more rigorous just and reasonable standard apply to subsequent rate challenges, even where that standard was not expressly requested at the time the rate was filed.

It is also foreseeable that some parties will urge the application of the more rigorous just and reasonable standard to rates proposed by a regional transmission organization (RTO) or independent system operator (ISO), particularly where the proposed rates enjoy broad stakeholder support. In particular, parties may argue that RTOs and ISOs are independent entities charged with the reliable operation and planning of the transmission grid,[161] who can be relied on to craft just and reasonable market rules, and that proposals garnering broad, or unanimous, stakeholder support are akin to settlements. In the authors' view, it could be a mistake for the FERC to adopt such an approach for several reasons. As the FERC has recognized, when urged to defer to the product of RTO/ISO stakeholder processes, it cannot delegate its statutory duty to ensure that rates are just and reasonable to RTOs and ISOs or their stakeholders.[162] There are also differences between settlement negotiations and stakeholder processes that militate against equating the two. For example, it is well established that interested parties should be represented in settlement negotiations by persons authorized to make binding commitments on their behalf[163] and that parties fail to participate in settlement negotiations at their peril.[164] To the authors' knowledge, the FERC has never suggested that similar requirements apply to stakeholder processes. Indeed, if the degree of stakeholder support were to be a factor in determining the standard applied to RTO/ISO filings, stakeholders would necessarily need to commit additional resources to stakeholder processes in order to preserve their rights to challenge the product of those processes, even though, as the Commission has recognized, the costs of participating in RTO/ISO stakeholder processes already "present resource challenges for certain stakeholders, including many consumer

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161. 18 C.F.R. § 35.34 (2010).

162. Public Serv. Comm'n of Wis. v. FERC, 545 F.3d 1058, 1062-65 (D.C. Cir. 2008) (explaining that while the Commission may give weight to the negotiated stakeholder process, it must "make its own, independent assessment that the policy was 'just and reasonable'"); *ISO New England Inc.*, 132 F.E.R.C. ¶ 61,122 at P 22 (2010) (noting that the Commission has an "independent obligation under section 205 to examine each filing presented to it and determine whether the provisions of that filing are just and reasonable" and that "stakeholder support alone cannot ultimately prove that a rate design is just and reasonable") (internal citations and quotation omitted); *Midwest Indep. Transmission Sys. Operator, Inc.*, 122 F.E.R.C. ¶ 61,283 at PP 56-57 (2008) (finding that the Commission's independent obligation to review rates and practice under sections 201, 205, and 206 of the FPA applies to RTO/ISO markets); *American Elec. Power Serv. Corp. v. Midwest Indep. Transmission Sys. Operator, Inc.*, 122 F.E.R.C. ¶ 61,083 at P 172 (2008) (finding "regional or stakeholder consensus is an important factor to be considered" but "cannot ultimately prove that a rate design is just and reasonable").

163. 18 C.F.R. § 385.601(a)(2) (2010).

164. *See, e.g.,* 18 C.F.R. § 385.601(a)(3) (2010) ("If a party fails to attend the [settlement] conference such failure will constitute a waiver of all objections to any order or ruling arising out, or any agreement reached at, the conference."); *Calpine Corp. v. California Indep. Sys. Operator Corp.,* 133 F.E.R.C. ¶ 63,006 at P 42 (2010) (treating a settlement as uncontested despite comments requesting that approval of the settlement be conditioned on the grounds that, among other things, the "[commenter]'s failure to participate in most of the settlement discussions conducted at the Commission or by phone over the course of about one year cannot be ignored").

advocates, and may present barriers to the full, open participation of stakeholders in RTO/ISO governance matters."[165]

V. CONCLUSION

Although *Devon Power*'s more rigorous just and reasonable standard has the potential to promote the certainty and predictability needed for infrastructure investment and market participation, the usefulness of that standard is substantially undercut because of outstanding questions regarding, and possible inconsistencies in, its implementation. Indeed, Commissioner LaFleur's concurrence in *Devon Power* could even be read to suggest that the more rigorous just and reasonable standard was a "one-off" tailored specifically to justify upholding the settlement at issue in that case.[166] Nonetheless, some settling parties will inevitably want to invoke *Devon Power* to protect their proposed rates. Parties and their counsel will need to give careful consideration to the risks and benefits of the application of the more rigorous just and reasonable standard before making such a request, including the potentially restrictive effect of that heightened standard if market conditions change in the future. Parties and their counsel will also need to structure their requests carefully given the questions described above regarding the circumstances under which the FERC will find it appropriate to apply the new heightened standard and the scope of that standard. Accordingly, to the extent that the FERC and the courts are serious about making the more rigorous just and reasonable standard a viable option, they have some work ahead of them to provide additional guidance as to how the standard will, and will not, apply and the relationship between this new variant and the more traditional *Mobile-Sierra* doctrine.

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165. *ISO New England Inc.*, 133 F.E.R.C. ¶ 61,070 at P 67 (2010).

166. *Devon Power LLC*, 134 F.E.R.C. ¶ 61,208, at p. 62,049 (2011) (LaFleur, Comm'r, concurring) ("I write separately to emphasize what I see as the narrow and fact-bound basis of today's decision."). *See also High Island Offshore Sys., LLC*, 135 F.E.R.C. ¶ 61,105 at P 24 (2011) (emphasizing the "extraordinary" circumstances of *Devon Power*); *Petal Gas Storage, L.L.C.*, 135 F.E.R.C. ¶ 61,152 at P 17 (2011) (same); *Southern LNG Co.*, 135 F.E.R.C. ¶ 61,153 at P 24 (2011) (same).