

HAS THE “COMPLETE AND PERMANENT BOND OF PROTECTION” PROVIDED BY FERC REFUNDS ERODED IN THE TRANSITION TO MARKET-BASED RATES?

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Synopsis: The Federal Energy Regulatory Commission (FERC or Commission), and its predecessor, the Federal Power Commission, have a long history of providing refunds to consumers for rates collected by natural gas companies or public utilities that are determined to be unjust and unreasonable or not in conformance with the lawful filed rate. Over the past two decades, the Commission has undertaken natural gas and electric industry restructurings that have encouraged the development of markets where natural gas or electricity can be bought or sold. Unlike traditional cost-based rates, however, the market-rate payable to all sellers into a market can be affected by the actions of a single market participant. This article first reviews the Commission’s historical refund authority and the basics of refund calculations under cost-based, formula-based, and market-based regulation. It then takes a more in-depth look at refunds under market-based rates. It concludes that under market-based rates, consumers are less likely to be made whole when rates are found to be unjust and unreasonable, or unlawful, than under traditional cost-based regulation.

I.	Introduction	42
II.	The FERC’s Discretion at Its “Zenith:” Law, Equity, and Refunds	45
	A. NGA Section 4 and Section 205 – Rate Filings	45
	B. NGA Section 5 and FPA Section 206 – Complaints	46
	C. NGA Section 16 and FPA Section 309 – “all necessary or appropriate actions”	46
	D. The Distinction Between Ratemaking Refunds and Enforcement Remedies	47
	E. The Filed Rate Doctrine, the Rule Against Retroactive Ratemaking, and Their Impact on Refunds	48
	F. Statutes of Limitations	49
	G. The FERC’s Authority Preempts State Action	50
	H. The Risk of Undercollections	51
	I. Limits on Undercollections – The Coastal Rule	52
	J. Limits on the Commission’s “Discretion”	53
III.	The Basics of Refund Calculations	53
	A. The Principal Component of a Refund	53
	B. The Interest Component of a Refund	54
	C. Recordkeeping Requirements and Refund Reports	55
	D. Adjustments to Traditional Refund Calculations	56
	1. Interest Adjustments	56
	a. Granting Interest Waivers	56

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	b. Rejecting Interest Waivers	56
	c. Escrow Accounts	57
	d. Sharing the Interest “Shortfall”	57
	2. Offsets of Refunds and Revenues	58
IV.	Refund Calculations Under Cost-Based, Formula-Based, and Market-Based Regulatory Regimes	58
	A. Cost-Based Rate Refunds	59
	B. Formula Rate Refunds	59
	C. Market-Based Rate Refunds	60
	1. Refunds Calculations for Market-Based Bilateral Contracts	61
	2. Refunds Calculations in Single-Price Clearing Markets	61
V.	The FERC’s Legal Authority to Provide Refunds Under Its Market-Based Rate Regime	63
	A. Reprising the Commission’s Discretion	63
	B. Market-Based Contracts	64
	C. Single-Price Clearing Markets	65
	1. The Potential Impact of a Single Seller on the Market	65
	2. New Entrants in Manipulated Markets	67
	3. The Filed Rate in a Single-Price Clearing Market	67
	4. The Just and Reasonable Standard in a Single-Price Clearing Market	69
	D. Illustrative Cases	69
	1. TEP I: Real Time Energy Price Corrections	70
	2. TEP II: The Operating Reserves Markets	70
	3. TEP III: The Energy Market Price Spikes	71
	4. The Bangor Hydro-Electric Complaint	72
VI.	Conclusion	73

I. INTRODUCTION

Over the past two decades, the FERC has encouraged and approved the development of “competitive” markets as a means of providing consumers with efficiently priced energy and energy transportation under the Natural Gas Act (NGA)¹ and the Federal Power Act (FPA).² As described in a recent symposium on the changing landscape of energy law:

Part II of the Federal Power Act and the Natural Gas Act have changed from a regulatory scheme that controlled market power exercise by utilities, pipelines, and producers through classic rate regulation to a regulatory regime that controls the exercise of market power through reliance on a mixture of competition and regulation. This change was accomplished by congressional amendments to Part II of the Federal Power Act and the National Gas Act and through reinterpretation of the laws by FERC and the courts. It could be argued that more dramatic change was accomplished through reinterpretation than through enactment of legislative amendments.³

Although there have been numerous challenges to the Commission’s “reinterpretation” of its organic statutes and efforts to encourage competition in markets it regulates, including critical commentary on the legal basis for and

1. Natural Gas Act (NGA), 15 U.S.C. §§ 717-717z (2006).

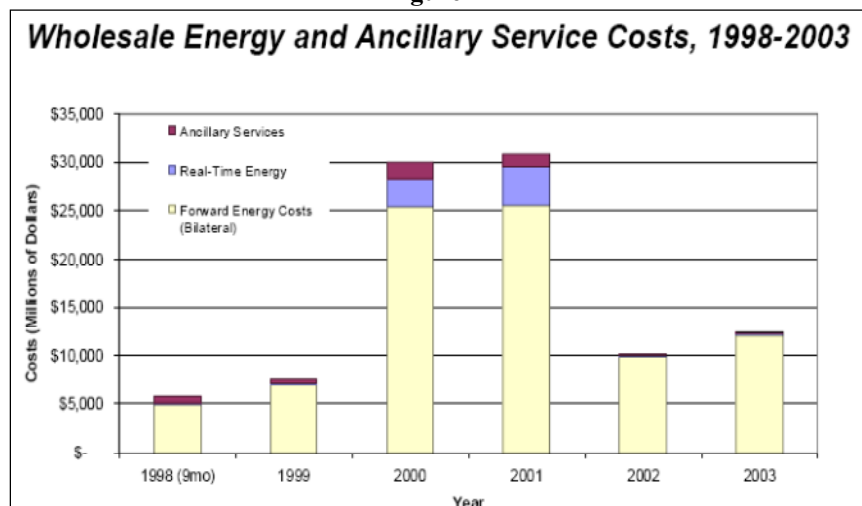
2. Federal Power Act (FPA), 16 U.S.C. §§ 791a-828c (2006).

3. Joseph T. Kelliher & Marie Farinella, *The Changing Landscape of Federal Energy Law*, 61 ADMIN. L. REV. 611, 613 (2009).

practical consequences of such rates,⁴ the courts that have addressed the issue have uniformly upheld the FERC's market-based initiatives.⁵

Even under market-based rate regimes, however, the FERC retains jurisdiction and the concomitant responsibility to ensure that rates in these markets remain just and reasonable, and, unless there are countervailing equitable reasons, to provide refunds to make consumers whole when rates depart from the just and reasonable.⁶ Even under a market-based regulatory regime, "[t]he FPA cannot be construed to immunize those who overcharge and manipulate markets in violation of the FPA."⁷ Figure 1, which shows total electricity costs in California for 1999-2003, dramatically illustrates the impact that market (or regulatory) dysfunction can have on consumers.⁸

Figure 1⁹



Indeed, this figure understates the total cost to consumers during the

4. See, e.g., Gerald Norlander, *May the FERC Rely on Markets to Set Electric Rates?*, 24 ENERGY L.J. 65, 69 (2003) (arguing that the FERC lacks statutory authority to set market-based rates under the FPA); Jacqueline Lang Weaver, *Can Energy Markets Be Trusted? The Effect of the Rise and Fall of Enron on Energy Markets*, 4 HOUS. BUS. & TAX L.J. 1 (2004); Jeffrey McIntyre Gray, *Reconciling Market-Based Rates with the Just and Reasonable Standard*, 26 ENERGY L.J. 423, 423 (2005).

5. *Montana Consumer Council v. FERC*, 659 F.3d 910, 922-923 (9th Cir. 2011) (upholding market-based regulatory policy established in FERC Order against facial challenge); *Elizabethtown Gas Co. v. FERC*, 10 F.3d 866, 870 (D.C. Cir. 1993) (upholding market-based rates for pipeline's merchant sales of natural gas where Commission had found market to be "sufficiently competitive"); *Louisiana Energy & Power Auth. v. FERC*, 141 F.3d 364, 371 (D.C. Cir. 1998) (upholding market-based rates for wholesale sales of electricity).

6. *Pennsylvania Power Co. v. FPC*, 343 U.S. 414, 418 (1952) ("A major purpose of the whole [FPA] is to protect power consumers against excessive prices.").

7. *Lockyer v. FERC*, 383 F.3d 1006, 1017 (9th Cir. 2004), *cert. denied*, 551 U.S. 1140 (2007).

8. For purposes of this article, "California Energy Crisis" refers generally to the natural gas and electricity market dysfunction in California and the Western United States during 2000 and 2001. "California Refund Proceedings" refers to the complex of cases at the FERC seeking refunds for overcharges and alleged overcharges during this period. These proceedings are described in detail in the Commission's December 27, 2005, report to Congress. FERC, *THE COMMISSION'S RESPONSE TO THE CALIFORNIA ELECTRICITY CRISIS AND TIMELINE FOR DISTRIBUTION OF REFUNDS* (2005) [hereinafter FERC 12/27/05 REPORT TO CONGRESS].

9. ANJALI SHEFFRIN, CAL. INDEP. SYS. OPERATOR, 2003 STATE OF THE CALIFORNIA ISO MARKETS REPORT 5 (2004), available at <http://www.slideserve.com/victoria/2003-state-of-the-california-iso-markets-report>.

California Energy Crisis since it does not include the costs associated with multiple rolling blackouts or the opportunity costs of the funds that were used for energy purchases and thus could not be used for other investment, consumption, or services. It is unlikely that a market will fail again in the spectacular manner and for the extended period that occurred in California in 2000 and 2001. However, it is still quite probable that there will be future market deviations from just and reasonable rates that, like passing hurricanes, tornados, or earthquakes, will occur episodically with damages that cannot be evaluated until after the event. Understanding the FERC's refund authority when this occurs is important both for consumers who should receive the protection from excessive prices but also for those sellers who may be required to make such refunds.

The question of the FERC's authority to provide refunds in the market-based context is also highly relevant because, by occupying the field, the FERC is now the *only* venue where consumers can obtain redress from unjust and unreasonable electric or natural gas market-based rates or rates that do not conform to market rules subject to the FERC's FPA or NGA jurisdiction.¹⁰

This article begins with an overview of the law and policy of refunds at the FERC under the NGA and the FPA.¹¹ It then undertakes a review of refund computations rules and policies, including interest calculations and departures from traditional calculations, with illustrative examples of refund computations for cost-based and market-based rates. The article next examines in more detail the provision of refunds in market-based rate regimes. Because much of this law has developed in the context of markets for electricity and ancillary services, this article likewise focuses on these markets.¹² The article concludes that full refunds may not be provided under the FERC's market-based rate regulation and that it is consumers who will now shoulder the burden of lost refunds. An important caveat to keep in mind, however, is that this article does not address the possible benefits of competition which may, or may not, outweigh this consumer loss and, thus, takes no position on the ultimate policy wisdom of the "mixture of competition and regulation" now used to determine whether and how to administer refunds in market-based rate regimes.¹³ It also does not address issues relating to the administration and design of these markets.¹⁴

10. See, e.g., *California v. Dynegy, Inc.*, 375 F.3d 831, 843 (9th Cir. 2004) (finding plaintiff can not circumvent FERC jurisdiction when issues involved claims under the FPA); *Public Util. Dist. No. 1 of Snohomish County v. Dynegy Power Mktg., Inc.*, 384 F.3d 756, 762 (9th Cir. 2004) (district court can not preempt FERC jurisdiction over matters involving rates subject to FERC jurisdiction).

11. Because of substantive differences in the "reparations" available under the Interstate Commerce Act (ICA), 49 U.S.C. app. §§ 1-80 (1988), amended by, Pub. L. No. 102-486 § 1801(a), 106 Stat. 3010 (Oct. 24, 1992), as compared to "refunds" available under the NGA and FPA, this article does not address refund issues under the ICA, although the Commission's market-based rate efforts have extended to oil pipelines regulated under the ICA as well. 18 C.F.R. § 342.4(b) (2011). See also, *Colonial Pipeline Co.*, 95 F.E.R.C. ¶ 61,377 (2001) (permitting oil pipeline to charge market-based rates where there was apparent lack of market power).

12. This article uses the term "single-price clearing market" to refer to a market where the highest accepted bid price for energy or ancillary services or capacity sets the market clearing price for all successful bidders into that market. For additional description of these markets, see, e.g., Susan Kelly & Elise Caplan, *Time for a Day 1.5 Market: A Proposal to Reform RTO-Run Centralized Wholesale Electricity Markets*, 29 ENERGY L.J. 491, 495 (2008) (explaining types and extent of RTO markets).

13. Kelliher & Farinella, *supra* note 3, at 613.

14. For more information on this topic, see, e.g., Kelly & Caplan, *supra* note 12, at 511-14 (describing studies assessing costs and benefits of restructured electric markets).

II. THE FERC'S DISCRETION AT ITS "ZENITH:" LAW, EQUITY, AND REFUNDS

It is a maxim of FERC regulatory law that the FERC's authority is at its "zenith" when crafting remedies.¹⁵ However, where does that authority come from in the first instance? What are its bounds? And how much flexibility does the FERC actually have to craft equitable remedies or to limit refunds? This section identifies those sources and explains how their interaction gives the FERC broad authority on the one hand, but authority that is constrained by statute, and on occasion by equity, on the other.

The FERC's authority to provide refunds or remedies for rates that the FERC finds to be unjust or unreasonable or not in accord with the filed rate is contained in sections 4, 5, and 16 of the NGA and the analogous sections 205, 206, and 309 of the FPA.¹⁶ Although there are differences between the NGA and the FPA, mostly relating to timing issues, courts have interpreted their analogous substantive provisions *in pari materia*.¹⁷ Thus, the discussion relating to the substantive provisions of one act generally will be applicable to the other.

In addition to reviewing the statutory sources for the FERC's refund and remedial authority, this section further: highlights the distinction that has been drawn between rate refunds and enforcement remedies; introduces the "filed rate" and "retroactive ratemaking" concepts; addresses FERC jurisdiction and preemption; covers the traditional allocation of over- and under-recovery risk; and concludes with a section on the limits of the FERC's remedial discretion.

A. NGA Section 4 and Section 205 – Rate Filings

Section 4 of the NGA and section 205 of the FPA each provide for refunds where a natural gas company or public utilities files at the FERC for a rate or rate increase.¹⁸ Each section, *inter alia*, provides that the FERC "may" order refunds, with interest, of that "portion of such increased rates or charges as by its decision shall be found not justified."¹⁹ Refunds are from the date that the higher proposed rate is charged until the effective date established by the FERC for a lower rate.²⁰ If the approved rate is the same as the proposed rate, that is, if the proposed rate is determined to be just and reasonable, then no refunds would be due.

Refunds are limited on the downside by the floor established by the prior effective and lawful rate, except to the extent that a NGA section 4 or a FPA

15. *Niagara Mohawk Power Corp. v. FPC*, 379 F.2d 153, 159 (D.C. Cir. 1967); *Laclede Gas Co. v. FERC*, 997 F.2d 936 (D.C. Cir. 1993); *California Pub. Util. Comm'n v. FERC*, 462 F.3d 1027, 1053 (9th Cir. 2006).

16. NGA, 15 U.S.C. §§ 717c, 717d, 717o (2006); FPA, 16 U.S.C. §§ 824d, 824e, 825h (2006).

17. *Kentucky Utils. Co. v. FERC*, 760 F.2d 1321, 1325 n.6 (D.C. Cir. 1985) ("It is, of course, well settled that the comparable provisions of the Natural Gas Act and the Federal Power Act are to be construed *in pari materia*."); *accord Florida Power & Light Co. v. FERC*, 660 F.2d 668, 677 n. 23 (5th Cir. 1981) (citing *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956)).

18. 15 U.S.C. § 717c; 16 U.S.C. § 824d.

19. 16 U.S.C. § 824d(e) (with minor, non-substantive modifications, this same language is contained in 15 U.S.C. § 717c(e)).

20. 15 U.S.C. § 717c(d); 16 U.S.C. § 824d(d). There is a notice period of thirty (NGA) or sixty (FPA) days, as well as an optional suspension period that may be imposed by the Commission of up to five months, before the proposed rate become effective. 15 U.S.C. § 717c(d), (e); 16 U.S.C. § 824d(d), (e). The Commission may waive the notice period for good cause, thus permitting the earlier collection of filed-for costs. 15 U.S.C. § 717c(d); 16 U.S.C. § 824d(d).

section 205 rate proceeding is coupled with a NGA section 5 or a FPA section 206 complaint action. Where this occurs, additional refunds or a prospectively lower rate may be available, consistent with the requirements and limitations of NGA section 5 or FPA section 206.²¹

B. NGA Section 5 and FPA Section 206 – Complaints

Section 5 of the NGA and section 206 of the FPA address circumstances where either a complaint has been filed or the FERC on its own motion initiates a proceeding to investigate whether a natural gas company's or public utility's rates have become unjust and unreasonable.²² There is a two part showing required under these sections: first, the Commission must find that the existing rate is unjust or unreasonable; second, it must then establish a new rate that is just and reasonable.²³ Section 206 of the FPA provides for the establishment of a refund effective date as early as the initiation of a customer complaint regarding, or notice of the investigation by the Commission into, wholesale rates, charges, terms, and conditions.²⁴ In contrast, under section 5 of the NGA, just and reasonable rates established as a result of a complaint or a Commission initiated investigation are effective prospectively only from the date of the Commission's order establishing new rates, and thus, refunds are not available before the effective date of the Commission ruling.²⁵

C. NGA Section 16 and FPA Section 309 – “all necessary or appropriate actions”

Section 16 of the NGA and section 309 of the FPA contain identical language that provides the general administrative powers of the Commission to “perform any and all acts . . . as it may find necessary or appropriate to carry out the provisions of [the NGA or the FPA].”²⁶ Over the years since enactment of the NGA and FPA, the Commission or courts have cited these sections repeatedly and interchangeably as the legal authority for a variety of remedial actions by the FPC,²⁷ the FERC, or the courts.²⁸ It is to these sections too that

21. The lack of retroactive refunds for complaints under the NGA and FPA contrasts with “reparations” available under the ICA. Reparations may be obtained under the ICA for up to two years prior to the date of a complaint if the Commission finds the rate to be unjust and unreasonable, subject to limitations based on the type of rate established under the ICA. 49 U.S.C. app. § 13(1) (1988). See also, *SFPP, L.P.*, 121 F.E.R.C. ¶ 61,240 at PP 62-63 (2007) (explaining basis for and limitations on reparations); *Arizona Grocery Co. v. Atchison, Topeka & Santa Fe Ry.*, 284 U.S. 370 (1932) (upholding legality of reparations).

22. 15 U.S.C. § 717d; 16 U.S.C. § 824e.

23. See *Robin Pipeline Co. v. FERC*, 795 F.2d 182, 184 (D.C. Cir. 1986) (the FERC may order rate change under NGA section 5 “if FERC finds that the existing rate is unjust or unreasonable and the proposed new rate is both just and reasonable”).

24. 16 U.S.C. § 824e(b). Refunds under this provision are limited, however, to a period of fifteen months; if a final ruling has not occurred by that time, there is a gap in the refund obligation until a final Commission ruling, unless the Commission finds the delay was due to dilatory behavior by the public utility. *Id.*

25. 15 U.S.C. § 717d(a).

26. 15 U.S.C. § 717o; 16 U.S.C. § 825(h).

27. The FPC was the predecessor agency to the FERC. The FERC was established by the Department of Energy Organization Act, Pub. L. No. 95-91, 91 Stat. §§ 401-407 (1977). In addition to the responsibilities of the former FPC, the FERC also was assigned regulatory authority for transportation by oil pipelines regulated under the ICA. 49 U.S.C. app. § 40(b).

courts look when evaluating the equitable or “practical” breadth of Commission action. For example, in upholding refunds ordered by the FPC, the Supreme Court observed that it was the duty of the Commission to look at “the backdrop of the practical consequences . . . and the purposes of the Act,” in exercising its discretion under § 16.²⁹

The D.C. Circuit similarly highlighted the FERC’s authority to evaluate appropriate remedies, including the possibility of ordering no refund at all:

With reference to refunds, FERC’s authority to order them is derived from section 16 of the NGA This provision in no way qualifies as a statutory command that refunds be ordered whenever overcharges have been identified, and FERC may in some situations decline to order any refund at all. . . . In determining whether to require a refund, and by implication in setting the amount, FERC need only establish that its decision constitutes a “reasonable accommodation” of the “relevant factors,”³⁰ . . . and that the remedy provided is “equitable in the circumstances,”³⁰

While NGA section 16 provides the FERC with considerable discretion, that discretion is not unbounded. The next several sections explore the contours of its refund and remedial authority. One key issue, and one that is often muddled in discussions relating to the FERC’s refund authority, is the distinction between rate-related refunds and enforcement-style remedies (which may also take the form of refunds).

D. The Distinction Between Ratemaking Refunds and Enforcement Remedies

Courts have recognized a distinction between refunds arising from a ratemaking context, that is under NGA sections 4 and 5 and FPA sections 205 and 206, and remedies (which may also include refunds) relating to violations of the act or enforcement proceedings:

It is well established that there is a fundamental difference between FERC’s role in ratemaking proceedings and its role in assigning remedies to redress violations of the NGA. *In the ratemaking context, FERC must ensure that “[a]ll rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas . . . shall be just and reasonable.” 15 U.S.C. § 717c(a).* By contrast, *FERC enjoys a great deal of flexibility in the remedy phase of an enforcement proceeding.* Indeed, as we have often noted, FERC’s discretion is “at [its] zenith when the action assailed relates primarily . . . to the fashioning of . . . remedies and sanctions.”³¹

In other words, where a rate increase is proposed by a natural gas company or public utility, there is an expectation that full refunds of the difference between the claimed or challenged rate and the rate determined to be just and reasonable will be ordered. In these cases, determinations of negligence or fault

28. See, e.g., Robert D. Horvath, Jr., *The Federal Energy Regulatory Commission’s Authority to Order in Kind Refunds of Natural Gas*, 33 CASE W. RES. L. REV. 458, 458 (1982-83) (providing a detailed analysis of the applicability of section 16 in ordering “in kind” refunds from natural gas producers in the context of the abandonment or curtailment of gas production).

29. *Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 147 (1960).

30. *Laclede Gas Co. v. FERC*, 997 F.2d 936, 944 (D.C. Cir. 1993) (internal citations omitted); *accord Concord v. FERC*, 955 F.2d 67, 72 (1992) (upholding Commission decision to not order refunds under the FPA where utility’s minor error did not warrant refund).

31. *Laclede Gas*, 997 F.2d at 944 (emphasis added) (quoting *Niagara Mohawk Power Corp. v. FPC*, 379 F.2d 153, 159 (D.C. Cir. 1967); further citing *Consolidated Gas Transmission Corp. v. FERC*, 771 F.2d 1536, 1549 (D.C. Cir. 1985), *Columbia Gas Transmission Corp. v. FERC*, 750 F.2d 105, 109 (D.C. Cir. 1984)).

are generally not an issue; the just and reasonable rate approved or established by the FERC determines the refund that will be owed or due.

Where, however, the issue involves enforcement actions related to violations of the statute or of the filed rate, the negligent or intentional actions of a defendant to such an action will often be a central issue.³² In these cases, the Commission has significant discretion, or “flexibility,” to craft a remedy,³³ which may include a distribution to harmed parties of any funds that are required to be disgorged.³⁴ As the Commission has observed, “[w]hile civil penalties serve a deterrent function, disgorgement monies are an important tool to ensure that persons harmed by the alleged misconduct are made whole to the extent possible and that the public interest is served.”³⁵

The distinction between ratemaking and enforcement-type proceedings – and between no-fault and fault-based refunds or remedies – is not just of academic interest. It is precisely this line that becomes blurred in a market-based regime where the “filed rate” is defined by a market-based tariff that does not include any kind of numerical rate but, instead, comprises a set of market and behavioral rules under which an authorized seller is permitted to participate in a given market or under which a market is authorized to operate.³⁶ Rules violations typically fall under the enforcement rubric; however, in a single-price clearing market those rules and any violations of them can also have a very real impact on the *prices* received by all sellers and paid by all consumers.

E. The Filed Rate Doctrine, the Rule Against Retroactive Ratemaking, and Their Impact on Refunds

Retroactive refunds (or surcharges) are limited by the filed rate doctrine and its corollary, the rule against retroactive ratemaking. The filed rate doctrine “bars a regulated seller . . . from collecting a rate other than the one filed with the Commission and prevents the Commission itself from imposing a rate increase for gas [or electricity] already sold.”³⁷ The rule against retroactive ratemaking provides that “costs . . . incurred in order to provide current or future service

32. See, e.g., *Brian Hunter*, 135 F.E.R.C. ¶ 61,054 at P 32 (2011) (affirming Administrative Law Judge decision finding Mr. Hunter had manipulated natural gas markets), *reh'g denied*, 137 F.E.R.C. ¶ 61,146 (2011).

33. Order No. 673, *Amendments to Codes of Conduct for Unbundled Sales Service and for Persons Holding Blanket Marketing Certificates*, F.E.R.C. STATS. & REGS. ¶ 31,207 at P 38, 71 Fed. Reg. 9,709 (2006) (to be codified at 18 C.F.R. pt. 284) (explaining that while section 5 refunds are not retroactively available under the NGA, “the Commission clearly has authority to order disgorgement of profits associated with an illegally charged rate, *i.e.*, a rate other than the rate on file or in violation of a Commission rule, order, regulation, or tariff on file”).

34. See, e.g., *Energy Transfer Partners L.P.*, 128 F.E.R.C. ¶ 61,269 at PP 11-12 (2009) (establishing \$25 million disgorgement fund to which eligible parties could apply for reimbursement). The settlement also included a \$5 million penalty that was paid to the U.S. Treasury. *Id. Accord, Sempra Energy Trading LLC*, 125 F.E.R.C. ¶ 61,360 at P 1, 11 (2008) (approving enforcement settlement and providing for disgorged amounts to be distributed to energy assistance programs and penalty to be paid to U.S. Treasury).

35. 128 F.E.R.C. ¶ 61,269 at P 15.

36. See, e.g., Gray, *supra* note 4, at 433 (explaining difference between disgorgement remedy for violation of Market Behavior Rules and refund mechanism under FPA section 206).

37. *Arkansas La. Gas Co. v. Hall*, 453 U.S. 571, 578 (1981); *accord Pacific Gas & Elec. Co. v. FERC*, 373 F.3d 1315, 1320 (D.C. Cir. 2004) (applying rule against retroactive ratemaking in context of the FPA).

cannot be retroactively billed to customers based upon their past purchasing decisions.”³⁸

Retroactive refunds may, however, be available where either the applicable tariff or filed rate was incorrectly applied³⁹ or where such adjustments are necessary to cure legal error.⁴⁰ These are not really exceptions from the filed rate doctrine but implement it by ensuring that the legal rate on file is the rate charged at any given point in time, even if it requires retroactive refunds or surcharges to make it so.⁴¹

F. Statutes of Limitations

There is no statute of limitations for rate refunds under the NGA or FPA.⁴² In contrast, for actions relating to civil penalties imposed under the NGA or FPA, the Commission has held that the general federal five-year statute of limitations for civil penalty actions, 28 U.S.C. § 2462,⁴³ should apply.⁴⁴ The Commission has also held, however, that it would “exercise prosecutorial discretion in determining whether to pursue an alleged violation based on all the

38. *Panhandle E. Pipe Line Co. v. FERC*, 95 F.3d 62, 68 (D.C. Cir. 1996); *accord* *Public Serv. Co. of N.H. v. FERC*, 600 F.2d 944, 950 (D.C. Cir. 1979) (denying retroactive adjustments under the FPA), *cert. denied*, 444 U.S. 990 (1979).

39. *City of Holland, Mich. v. Midwest Indep. Transmission Sys. Operator, Inc.*, 111 F.E.R.C. ¶ 61,076 at P 24 (2005) (“The Commission may order refunds for past periods where a public utility has either misapplied a formula rate or otherwise charged rates contrary to the filed rate.”); *Maislin Indus., U.S. v. Primary Steel, Inc.*, 497 U.S. 116, 130-31 (1990) (requiring retroactive surcharges to be paid by shippers to carriers for amounts charged *below* the rate on file, even where the companies at issue had negotiated to pay a rate lower than the tariff rate).

40. *United Gas Improvement Co. v. Callery Props.*, 382 U.S. 223, 229 (1965) (“An agency, like a court, can undo what is wrongfully done by virtue of its order.”); *accord* *Natural Gas Clearinghouse v. FERC*, 965 F.2d 1066, 1074 (D.C. Cir. 1992) (permitting retroactive rate adjustment to correct legal error).

41. When rates are made effective subject to refund, it is possible that changes in policy made during the rate suspension could affect the rate that is ultimately approved and, thus, refunds. Whether such policy changes can be given retroactive effect largely depends on whether the policy change represents a change in existing policy or a new policy. *Wisvest-Connecticut, LLC v. ISO New England, Inc.*, 104 F.E.R.C. ¶ 61,262 at P 9 (2003) (holding that “retroactivity is not authorized when a new rule is substituted for an old rule that was reasonably clear so that the settled expectations of those who had relied on the old rule are protected,” even where the old rule may have resulted in excessive charges); *but see* *Williams Natural Gas Co. v. FERC*, 3 F.3d 1544, 1553-55 (D.C. Cir. 1993) (permitting retroactive effect for disallowance of costs where case fell “squarely within [the court’s] precedents authorizing retroactivity for agency rules that do not represent a shift from ‘a clear prior policy.’”).

42. Order No. 670, *Prohibition of Energy Market Manipulation*, F.E.R.C. STATS. & REGS. ¶ 31,202 at P 62, 71 Fed. Reg. 4,244 (2006) (codified at 18 C.F.R. pt. 1c) [hereinafter Order No. 670] (“no statute of limitations of general applicability appears in the NGA or FPA”); *Gulf Oil Corp. & Texas E. Transmission Corp.*, 56 F.P.C. ¶ 3,492, at p. 3,503, 1976 WL 15180 (F.P.C.) (1976) (explaining that refunds under the NGA that were designed to leave “consumers in approximately the same [situation] they would have been in if they [had] received the gas” was not a penalty and thus the general federal statute of limitations of five years did not apply); *J.R. Cone*, 33 F.E.R.C. ¶ 61,125, at p. 61,276 (1985) (government generally exempt from “the various statutes of limitations or laches unless the sovereign deigns to impose a limitation on itself.”) (citing *United States v. Weintraub*, 613 F.2d 612, 619 (6th Cir. 1979)).

43. 28 U.S.C. § 2462 (2006) (imposing a five-year limitations period running “from the date when the claim first accrued” on any “action, suit, or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise.”).

44. Order No. 670, *supra* note 42, at P 62.

facts presented, including the time elapsed since the violation is alleged to have occurred.”⁴⁵

For a short period, the Commission mandated that complaints alleging a violation of the market behavior rules must be filed within ninety days from either the end of the calendar quarter in which a transaction occurred or from the date when a complaining party should have known of the violation.⁴⁶ The Commission subsequently rescinded this rule, noting that the general five-year federal statutory limitation would apply instead.⁴⁷ The order implementing this short-lived limitation was appealed in a case that was later withdrawn;⁴⁸ its legality, thus, remains untested.

G. *The FERC’s Authority Preempts State Action*

It is settled law that the FERC’s authority to set interstate wholesale rates preempts state authority over those rates.⁴⁹ “Moreover, the filed rate doctrine is not limited to ‘rates’ *per se*,”⁵⁰ but may also extend to issues affecting rates, such as the allocation of low-cost power.⁵¹ *Nantahala* explains that this preemption authority derives from the filed rate doctrine as enforced by the Supremacy Clause of the U.S. Constitution.⁵²

The FERC’s jurisdiction over wholesale market-based rates and contracts likewise has been held to preempt state jurisdiction.⁵³ As explained by a U.S. District Court where plaintiffs had sought rate relief from market-based rates charged in California markets during 2000 and 2001:

the key feature of California’s recently deregulated wholesale energy markets is the markets’ reliance on “market-based rates.” These rates are still subject to FERC oversight, but to a much lesser extent than traditional “cost-based rates.” Thus, the determinant question in this case in regard to the application of the filed rate doctrine is whether the doctrine applies to the relatively new innovation of “market based rates” governing wholesale energy trading.⁵⁴

Finding that the filed rate doctrine did apply, the court concluded:

The Court agrees with Defendants – the filed rate doctrine indeed bars Plaintiff’s claims. As the Ninth Circuit stated in *County of Stanislaus v. Pacific Gas & Elec. Co.*, 114 F.3d 858, 863 (9th Cir. 1997), “the filed rate doctrine bars all claims – state and federal – that attempt to challenge a rate that a federal agency has reviewed and filed.” Moreover, the Ninth Circuit has made clear that “the filed rate

45. *Id.* at P 63.

46. *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 105 F.E.R.C. ¶ 61,218 at app. B (2003), *reh’g denied*, 107 F.E.R.C. ¶ 61,175 at PP 146-53 (2004).

47. Order Revising Market-Based Rate Tariffs and Authorizations, *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 114 F.E.R.C. ¶ 61,165 at P 52 (2006).

48. Clerk’s Order Granting Motion to Dismiss, *Cinergy Mktg. & Trading, L.P. v. FERC*, Nos. 04-1168 et al., 2006 U.S. App. LEXIS 14193 (D.C. Cir. June 7, 2006).

49. *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 965 (1986).

50. *Id.* at 966.

51. *Id.* at 967.

52. *Id.* at 963; *see also* U.S. CONST. art. VI, cl. 2.

53. *Duke Energy Trading & Mktg., LLC v. Davis*, 267 F.3d 1042, 1057 (9th Cir. 2001) (explaining that state action commandeering contracts for purchase of electricity subject to FERC jurisdiction was “an impermissible intrusion into FERC’s territory”).

54. *Public Util. Dist. No. 1 of Snohomish Cnty. v. Dynegy Power Mktg., Inc.* (*In re Cal. Wholesale Elec. Antitrust Litig.*), 244 F. Supp. 2d 1072, 1076 (S.D. Cal. 2003), *aff’d*, 384 F.3d 756 (9th Cir. 2004), *cert. denied*, 545 U.S. 1141 (2005).

doctrine [prohibits] not just a state court (or a federal court applying state law) from setting a rate different from that chosen by FERC, but also from assuming a hypothetical rate different from that actually set by FERC.”⁵⁵

The limited exception to the FERC’s preemptive refund authority relates to sales by certain governmental entities and non-public utilities defined in section 201(f) of the FPA.⁵⁶ Before 2005, these entities were fully exempt from the FERC’s refund authority.⁵⁷ In the Energy Policy Act of 2005 (EPA 05), Congress partially closed this jurisdictional gap by making voluntary short-term sales by such entities into FERC-jurisdictionally organized markets subject to the FERC’s refund authority, subject to: (a) an exclusion for any such entity that sells less than 8,000,000 MWh per year; (b) an exclusion for all electric cooperatives; and (c) limitations on its applicability to the Bonneville Power Administration, the Tennessee Valley Authority, or Federal power marketing agencies.⁵⁸ In those circumstances where the FERC still does not have refund authority over such entities, refunds may be available but would require claims to be made under alternative causes of action, such as in contract, in venues other than the FERC.⁵⁹

H. *The Risk of Undercollections*

The general rule has long been that it is the regulated company, *not the consumer*, that shoulders the risk of undercollections if its filed rate is insufficient to recover its costs:

The company having initially filed the rates and either collected an illegal return or failed to collect a sufficient one must, under the theory of the Act, shoulder the hazards incident to its action including not only the refund of any illegal gain but also its losses where its filed rate is found to be inadequate.⁶⁰

Similarly, where a regulated entity enters into a contract that in retrospect may be improvident, it is likewise bound by that agreement as long as the *public interest* is not otherwise adversely affected:

But, while it may be that the Commission may not normally impose upon a public utility a rate which would produce less than a fair return, it does not follow that the public utility may not itself agree by contract to a rate affording less than a fair return or that, if it does so, it is entitled to be relieved of its improvident bargain. In such circumstances the sole concern of the Commission would seem to be whether the rate is so low as to adversely affect the public interest – as where it might impair

55. *Id.* at 1077 (quoting in part *Transmission Agency of N. Cal. v. Sierra Pac. Power Co.*, 295 F.3d 918, 929-30 (9th Cir. 2002)).

56. 16 U.S.C. § 824(f). *Bonneville Power Admin. v. FERC* suggested that “the remedy, if any, may rest in a contract claim.” 422 F.3d 908, 925 (9th Cir. 2005) (citing *Alliant Energy, Inc. v. Nebraska Pub. Power Dist.*, Civ. No. 00-2139, 2001 WL 1640132 (D. Minn. Oct. 18, 2001), *aff’d*, 347 F.3d 1046 (8th Cir. 2003) (finding non-jurisdictional entity to be contractually liable to pay refunds)).

57. *Bonneville*, 422 F.3d at 911 (holding that the “FERC does not have refund authority over wholesale electric energy sales” made in FERC-jurisdictional markets “by governmental entities and non-public utilities”).

58. Energy Policy Act of 2005, Pub. L. No. 109-58, 119 Stat. 594, § 1286 (adding new section 206(e) to the FPA).

59. *Bonneville*, 422 F.3d at 925-26 (suggesting that “the remedy, if any, may rest in a contract claim” (citing *Alliant Energy, Inc. v. Neb. Pub. Power Dist.*, Civ. No. 00-2139, 2001 WL 1640132 (D. Minn. Oct. 18, 2001), *aff’d*, 347 F.3d 1046 (8th Cir. 2003) (finding non-jurisdictional entity to be contractually liable to pay refunds)).

60. *FPC v. Tennessee Gas Transmission Co.*, 371 U.S. 145, 153 (1962).

the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory.⁶¹

This presumption is commonly referred to as the “*Mobile-Sierra* doctrine,” and has been the source of considerable litigation and legal commentary, particularly since the advent of natural gas and electric deregulation and the rise of market-based rates.⁶² Notably, the *Mobile-Sierra* presumption is not a departure from the just and reasonable standard, but instead, it requires a more rigorous showing that the existing rates are not “just and reasonable.”⁶³ That is, as expressed recently by the Supreme Court, only if the existing rates “seriously harm the consuming public may the Commission declare [them] not to be just and reasonable.”⁶⁴

Although the *Mobile-Sierra* doctrine applies to contracts, in one recent case the Commission, invoking its discretion to determine just and reasonable rates, held that it would permit the same presumption to apply to tariff rates established in the context of a settlement of a market-based auction for electric generation capacity.⁶⁵ Whether this case is *sui generis* or will be the founding precedent for future discretionary applications of *Mobile-Sierra* to tariff rates is, at this time, unknown.⁶⁶

I. Limits on Undercollections – The Coastal Rule

The losses that a regulated company can be made to shoulder is limited in cases where disgorgement is ordered that could result in a company not recovering its costs. In *Coastal Oil & Gas Corp. v. FERC*, the U.S. Court of Appeals for the Fifth Circuit reversed a Commission disgorgement order to the extent it would have resulted in Coastal not recouping its costs, finding that such a remedy exceeded both the injury caused by Coastal and its unjust enrichment and, thus, constituted a penalty that the FERC was not authorized to assess under the NGA.⁶⁷ Similarly, the Commission required Carolina Power & Light Company to make refunds where it had failed to file rates as required by the FPA but determined that it would not require Carolina to refund any amounts below

61. *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 355 (1956) (internal citation omitted); *accord* *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344-345 (1956).

62. See generally Carmen L. Gentile, *The Mobile-Sierra Rule: Its Illustrious Past and Uncertain Future*, 21 *ENERGY L.J.* 353 (2000); David G. Tewksbury & Stephanie S. Lim, *Applying the Mobile-Sierra Doctrine to Market-Based Rate Contracts*, 26 *ENERGY L.J.* 437 (2005); 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 & Grace Su, *New Chapters in the Mobile-Sierra Story: Application of the Doctrine After NRG Power Market, LLC v. Maine Public Utilities Commission*, 32 *ENERGY L.J.* 433 (2011).

63. *Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 545-46 (2008).

64. *Id.*

65. *Devon Power LLC*, 134 F.E.R.C. ¶ 61,208 at P 2 (2011), *reh'g denied*, 137 F.E.R.C. ¶ 61,073 (2011), *pet. for rev. pending*, *New England Power Generators Ass'n. v. FERC*, Case No. 11-1422 (D.C. Cir. filed Oct. 31, 2011).

66. Even in *Devon Power*, the Commissioners themselves had different views of this potential. Commissioner Norris dissented in part due to the possibility that “it may prove difficult to limit the exercise of discretion the majority uses today to only a few exceptional cases,” while Commissioner LaFleur concurred to emphasize the “narrow and fact-bound basis” for the decision. 134 F.E.R.C. ¶ 61,208, at p. 62,048-49 (Norris, Comm’r, dissenting in part), and at p. 62,049 (LaFleur, Comm’r, concurring).

67. *Coastal Oil & Gas Corp. v. FERC*, 782 F.2d 1249, 1253 (5th Cir. 1986).

the variable costs (such as fuel and variable operations and maintenance expenses) incurred by Carolina for providing the service at issue.⁶⁸

J. Limits on the Commission's "Discretion"

The Commission's discretion to not provide, or at least consider, a remedy under NGA section 16 or FPA section 309 is not unbounded. As the U.S. Court of Appeals for the Ninth Circuit explained in remanding the Commission's decision barring a remedy for pre-complaint violations during the California Energy Crisis:

[T]he California Parties seek a market-wide refund remedy for *tariff* violations pursuant to § 309 through its adjudicative filing. The fact that FERC may be seeking similar remedies against specific companies in its § 1b investigations does not justify its denial of the California Parties' request for § 309 relief. When parties seek adjudicative relief from an agency, they are entitled to a reasoned response from the agency. Here, the California Parties filed a cognizable request for relief and tendered credible evidence in support of their request. *A party's valid request for relief cannot be denied purely on the basis that the agency is considering its own enforcement action that may impart a portion of the relief sought.* If an aggrieved party tenders sufficient evidence that tariffs have been violated, then it is entitled to have FERC adjudicate whether the tariff has been violated and what relief is appropriate.⁶⁹

Before turning to the topic of refunds in market-based contexts, the next section reviews the mechanics of refund calculations, including equitable adjustments to those calculations that the Commission may make when circumstances warrant.

III. THE BASICS OF REFUND CALCULATIONS

This section first reviews the two key components of any refund: the principal and the interest associated with the refund. It briefly describes the record keeping requirements associated with rate refunds and the refund reports that are commonly required after refunds are made. It then looks at waivers or exceptions where the Commission has permitted departures from its usual refund requirements.

A. The Principal Component of a Refund

Section 35.19a of the Commission's regulations details the refund requirements for FPA section 205 cases where a proposed rate increase has been accepted, suspended, and made subject to refund.⁷⁰ As provided in that section, a utility "shall refund at such time in such amounts and in such manner as required by final order of the Commission *the portion of any increased rates or charges found by the Commission . . . not to be justified*, together with interest."⁷¹ Section 154.501 of the Commission's regulations provides a similar refund requirement for rates accepted and suspended, subject to refund, under NGA section 4, with an identical interest rate calculation.⁷²

68. *Carolina Power & Light Co.*, 87 F.E.R.C. ¶ 61,083 (1999).

69. *Public Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1051 (9th Cir. 2006) (emphasis added).

70. 18 C.F.R. § 35.19a (2011).

71. *Id.* § 35.19a(a)(1) (emphasis added).

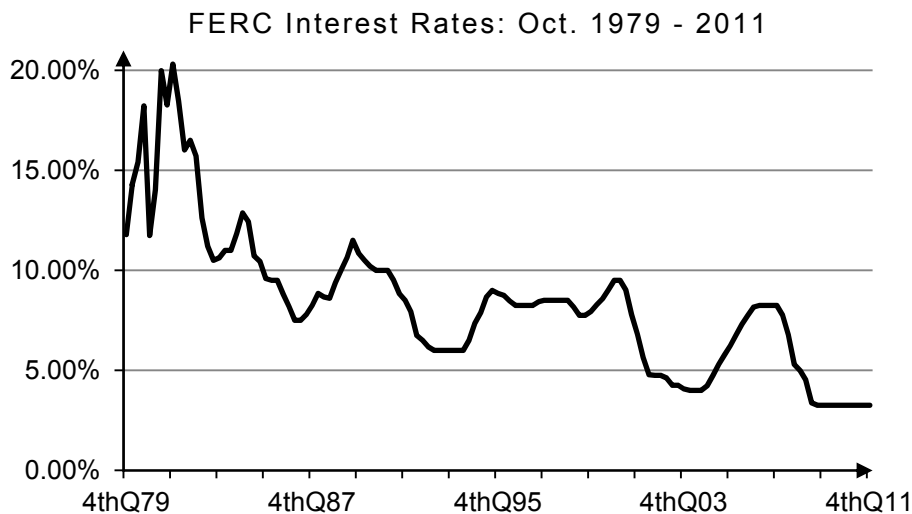
72. *Id.* § 154.501. Because the electric and gas refund requirements are essentially identical, the references below are limited to the electric section; however, they are equally applicable to gas rate refunds.

While calculating the principal of a refund may at first blush appear straight forward, it, in fact, can involve multiple calculations depending on the number of transactions and varying volumes over a period of time. Moreover, because of the quarterly compounding of interest applicable to most refunds since October 1, 1979, the principal amount must be adjusted each quarter to reflect the interest accrued during the quarter on which new interest is then applied.⁷³

B. *The Interest Component of a Refund*

Since October 1, 1979, the Commission has required that the interest rate for refunds be computed based on an average prime rate for each calendar quarter, with quarterly compounding.⁷⁴ Between October 10, 1974 and September 30, 1979, the FERC used a simple interest rate of 9% per annum; before October 10, 1974, the applicable rate was 7%.⁷⁵ As shown in Figure 2, interest rates since 1979 have varied considerably, from a high of 20.31% in the fourth quarter of 1981, to a low of 3.25% for multiple quarters beginning in the third quarter of 2009.

Figure 2⁷⁶



The purpose of interest is straightforward: to ensure that the refunds those consumers (or other entities) that overpaid receive include the time value for the funds that they in essence loaned to the regulated company. That is, when a regulated company obtains funds that it did not have the right to and has the use

73. *Id.* § 35.19a(a)(2)(iii)(B).

74. Section 35.19a(a)(2)(iii)(A) details this calculation and the sources for the prime rate figures; section 35.19a(a)(2)(iii)(B) details the compounding methodology. *Id.* § 35.19a(a)(2)(iii)(A), (B).

75. *Id.* § 35.19a(a)(2)(i), (ii). The Commission's switch from simple interest to a prime rate with compounding methodology was upheld in *United Gas Pipe Line Co. v. FERC*, 657 F.2d 790 (5th Cir. 1981).

76. Compiled from data available on the FERC web site: *Interest Rates*, FERC (Dec. 7, 2011), <http://www.ferc.gov/legal/acct-matts/interest-rates.asp#skipnav>.

of those funds at the same time consumers do not have the use of the funds, refunds should include interest.⁷⁷

Interest on the full difference between the collected rate and the rate ultimately determined to be just and reasonable must be refunded, regardless of the tax consequences that may occur when over-recovery takes place in one tax period and the refund is made in a later period.⁷⁸ As the Commission explained, “Customers are required to pay the full amount of the overcharge, and their costs are in no way diminished by the effect of income taxes on the sellers. To require interest on only a portion of their overpayments would not be fair.”⁷⁹

The Commission has regularly used the interest rate calculated under these sections for refunds in a variety of contexts beyond just NGA and FPA rate suspensions, including, *inter alia*, for oil pipelines subject to FERC regulation under the ICA,⁸⁰ gas producers subject to FERC regulation under the Natural Gas Policy Act of 1978 (NGPA),⁸¹ and for disgorgement of profits due as the result of a FERC enforcement action.⁸² In other words, entities that are required by the FERC to make refunds can generally expect that they will be required to do so with interest computed in accordance with sections 35.19a or 154.501 of the Commission’s regulations.⁸³

C. Recordkeeping Requirements and Refund Reports

To ensure that refunds can be readily made to parties to whom they may be owed, the Commission requires utilities to keep records of payments made while rates are under suspension “for each billing period, specifying by whom and in whose behalf such amounts are paid.”⁸⁴ Public utilities and gas pipelines required to make refunds under either section 35.19a or section 154.501 are also required to bear the costs of such refunding.⁸⁵

Entities required to make refunds can also expect that a compliance report detailing the refunds made will be required by the Commission. Section 154.501(e) explicitly requires such a report to be filed within thirty days of a rate refund by natural gas pipelines,⁸⁶ although there is not a parallel requirement for

77. *Louisiana Land & Exploration Co. v. FERC*, 788 F.2d 1132, 1138 (5th Cir. 1986) (where a company “had the use of consumer money to which it was not entitled during the time period involved, it was only fair that the refund be repaid with interest.”).

78. *See, e.g., Sea Robin Pipeline Co.*, 19 F.E.R.C. ¶ 61,340, *order denying reh’g*, 21 F.E.R.C. ¶ 61,155 (1982) (denying request to apply interperiod tax allocation on refunds and transportation revenue credited to Account No. 191).

79. Order No. 47, *Natural Gas Policy and Procedures*, F.E.R.C. STATS. & REGS. ¶ 30,083, at p. 30,548, 44 Fed. Reg. 53,493, *order on reh’g*, Order No. 47-A, *Rate of Interest on Amounts Held Subject to Refund*, F.E.R.C. STATS. & REGS. ¶ 30,099, 44 Fed. Reg. 65,740 (1979) (codified at 19 C.F.R. pts. 270, 273, 284), *order clarifying*, Order No. 47-B, F.E.R.C. STATS. & REGS. ¶ 30,121, 45 Fed. Reg. 3,888 (1980), *aff’d*, *United Gas Pipeline Co. v. FERC*, 657 F.2d 790 (5th Cir. 1981).

80. 18 C.F.R. § 340.1(c) (2011).

81. 15 U.S.C. §§ 3301-3402 (2006).

82. *Revised Policy Statement on Penalty Guidelines*, 132 F.E.R.C. ¶ 61,216, app. FERC Penalty Guidelines § 1B1.1, at p. 62,152-53 (2010).

83. 18 C.F.R. §§ 35.19a, 154.501 (2011).

84. *Id.* § 35.19a(b); *accord id.* § 154.501(e) (describing materials that must be included in natural gas company refund report).

85. *Id.* §§ 35.19a(a)(3), 154.501(b).

86. *Id.* § 154.501(e).

public utilities, such reports are usually mandated as part of FERC orders requiring refunds.⁸⁷

D. Adjustments to Traditional Refund Calculations

The Commission has on occasion departed from a strict application of its rate refund calculation requirements in circumstances where the traditional calculations were unworkable or where there were overriding equitable considerations. Most frequently, these adjustments have been applied to the interest component of the refund. Where challenged, they have generally, though not uniformly, been upheld by courts of appeals.

1. Interest Adjustments

a. Granting Interest Waivers

In a case involving two gas pipeline companies, the Commission declined to order interest where it was curing its own legal error and seeking to put the parties into the position they would have occupied but for that error.⁸⁸ Finding that “the allowance of interest on refunds is a matter of equity,” the Commission held that but for the Commission’s error the subject pipelines could have earlier recovered the costs and, therefore, that only the principal amount should be refunded.⁸⁹

Panhandle Eastern relied in part on *Estate of French*, a case where the court found that because the Commission had unreasonably delayed a decision, it should not, on equitable grounds, have assessed interest on the refund resulting from that decision.⁹⁰

The Commission similarly granted equitable waiver of both principal and interest based on review of the financial situation of a gas royalty interest owner who owed refunds to a producer.⁹¹ Finding that the financial condition of the upstream royalty interest owner made it unlikely the producer could recover the refunds owed, the Commission waived the payments of refunds associated with those funds that it could not collect from the royalty interest owner.⁹²

b. Rejecting Interest Waivers

The results in *Panhandle Eastern*, *Estate of French*, and *Robert F. White* contrast with other cases where the FERC or the courts have found that a waiver was not justified based on the equities of a particular situation. Thus, for example, the Commission generally denied waivers of interest on refunds owed by gas producers who had over-collected the statutory NGPA price finding that

87. See, e.g., *Southern Cal. Edison Co.*, 137 F.E.R.C. ¶ 61,016 at P 42 (2011) (requiring refund report within fifteen days after refunds are made); *Pacific Gas & Elec. Co.*, 136 F.E.R.C. ¶ 61,095 at P 4 (2011) (requiring refund report within thirty days of refunds made pursuant to settlement).

88. *Panhandle E. Pipeline Co.*, 69 F.E.R.C. ¶ 61,048, at pp. 61,189-90 (1994), *orders denying reh'g*, 70 F.E.R.C. ¶ 61,167, 71 F.E.R.C. ¶ 61,039 (1995), *aff'd in relevant part*, *Panhandle E. Pipeline Co. v. FERC*, 95 F.3d 62 (D.C. Cir. 1996).

89. 69 F.E.R.C. ¶ 61,048, at p. 61,189.

90. *Estate of French v. FERC*, 603 F.2d 1158, 1167-8 (5th Cir. 1979) (requiring suspension of interest, based on equitable considerations, where the Commission unreasonably delayed its decision).

91. *Robert F. White*, 71 F.E.R.C. ¶ 61,185 (1995).

92. *Id.* at pp. 61,662-63 (finding waiver to be equitable where royalty interest owner was elderly, disabled, and facing bankruptcy, and had assigned her interest to her caregiver son).

“[i]nterest, which merely represents use of the money, is ordinarily part of the refund of any overcharge, absent compelling reasons for not requiring its payment to the injured party.”⁹³

The Commission similarly observed in a case involving refunds under the NGPA that while “waivers may be appropriate in specific cases, . . . interest charges reflect a reimbursement to the rightful owners of the value of the use of funds” and that “[f]airness to consumers dictates that . . . sellers pay interest on the . . . refund amounts owed.”⁹⁴

In *Shell Oil Co.*, the Commission had permitted the refunding company to continue to use a 7% interest rate, even though the FERC’s rules had raised that rate to 9%, and later to the prime rate, with compounding.⁹⁵ The court found that the FERC failed to adequately articulate an appropriate reason for departing from its general rules regarding the calculation of interest:

FERC may exercise its equitable discretion and stray from the use of its general regulations. In order to do so, however, FERC must articulate valid reasons for the departure. The exercise of such discretion without expressing such valid reasons may be considered arbitrary and capricious. FERC’s exercising its equitable discretion for the sake of exercise or simply because it possesses equitable discretion is an insufficient justification for departing from the application of its general regulations.⁹⁶

c. Escrow Accounts

In a few instances, the Commission has permitted companies that had placed funds that were due to be refunded into an escrow account to use the interest rate paid on that account.⁹⁷ This approach may be allowed, at the Commission’s discretion, where the funds are actually being held in escrow and, thus, are not available to the company.⁹⁸

d. Sharing the Interest “Shortfall”

In the California Refund Proceeding, the Commission took yet another approach to modifying its interest requirements where the use of an escrow account by an intermediary that itself did not owe refunds resulted in an interest shortfall. Although it had initially required full interest to be paid, on rehearing it permitted the use of escrow account interest where disputed amounts were being held.⁹⁹ However, in subsequent rehearing orders, it changed course and

93. *Public Serv. Co. of Colo.*, 80 F.E.R.C. ¶ 61,264, at p. 61,951 (1997).

94. *Id.* (quoting Order No. 399-A, *Refunds Resulting from Btu Measurement Adjustment*, [Regs. Preambles 1982-1985] F.E.R.C. STATS. & REGS. ¶ 30,612, at p. 31,207, 49 Fed. Reg. 46,353, 49 Fed. Reg. 49,284 (1985) [hereinafter Order No. 399-A]).

95. *Shell Oil Co. v. FERC*, 664 F.2d 79, 83 (5th Cir. 1981).

96. *Id.*

97. *Alabama-Tennessee Natural Gas Co.*, 32 F.E.R.C. ¶ 61,085, at p. 61,210 (1985) (noting that a party’s interest obligation would be at the Commission’s interest rate, except for refunds placed in escrow, “where the interest obligation [would be] the accrued interest in the escrow account”); *Champlin Petroleum Co.*, 35 F.E.R.C. ¶ 61,336, at p. 61,764 (1986) (finding request to use an escrow account to hold refunds reasonable, “with . . . interest accruing on such account [i]njuring to the benefit of” refund recipients); and Order No. 399-A, *supra* note 94, at p. 31,218.

98. 32 F.E.R.C. ¶ 61,085, at p. 61,210.

99. *San Diego Gas & Elec. Co.*, 105 F.E.R.C. ¶ 61,066 (2003), *order on reh’g*, 107 F.E.R.C. ¶ 61,165 (2004).

instead required that any shortfall in interest between the escrow rate and the FERC interest rate should be shared equally by the payors and the recipients of refunds.¹⁰⁰

This unique split-the-difference, or share-the-pain, approach was predicated on the Commission's conclusion that "both buyers and sellers alike should share the burden of the shortfall equally . . . because the shortfall is attributable to [a third party's] actions, and therefore, it would be inappropriate to require either the buyers or the sellers to shoulder the entire burden."¹⁰¹ Upon being presented with multiple options for implementing this share-the-pain approach and finding that there was "no perfectly equal allocation," the Commission pragmatically selected an option it viewed as "transparent, simple to apply, and . . . [that] should reduce further litigation."¹⁰²

2. Offsets of Refunds and Revenues

The Commission generally does not permit refunds to be offset with revenues.¹⁰³ When the Commission did permit such an offset in circumstances where it had first rejected an offset and then on rehearing permitted the offset, the offset was rejected by the U.S. Court of Appeals for the D.C. Circuit which observed that:

permitting producers to offset their refund obligations would bring delay and confusion into an already complex area. Moreover, the principles of law and the customers involved in the refund arrangement are far from identical to those implicated in the [other] proceedings. By prohibiting offsets, FERC designed the system most likely to assure that customers will receive refunds due them. Involving disparate issues in a matter on appeal to another court can only complicate, delay, and obfuscate the refunds at issue here.¹⁰⁴

In sum, while the Commission has occasionally departed from the traditional principal plus interest formulation of a refund calculation otherwise required under its regulations or orders, such adjustments have historically been rare and have come in unique circumstances where the equities of a situation justified the departure.

IV. REFUND CALCULATIONS UNDER COST-BASED, FORMULA-BASED, AND MARKET-BASED REGULATORY REGIMES

This section provides short narratives describing the refund calculations that must be undertaken under the different regulatory regimes. As shown below, the computational complexity increases from cost-based to formula-based to market-based refunds, with the potentially most complex being after-the-fact, market-wide refunds in single-price clearing markets.

100. *San Diego Gas & Elec. Co.*, 109 F.E.R.C. ¶ 61,218 (2004), *order on reh'g*, 110 F.E.R.C. ¶ 61,336 (2005), *pet. for rev. pending sub nom.*, *Pacific Gas & Elec. Co. v. FERC*, Case No. 05-71831 (9th Cir. filed Apr. 1, 2005).

101. 109 F.E.R.C. ¶ 61,218 at P 32.

102. 110 F.E.R.C. ¶ 61,336 at PP 55-56.

103. *Southern Cal. Edison Co.*, 137 F.E.R.C. ¶ 61,016 at PP 41, 61 (2011) (explaining that the "Commission generally prefers not to consolidate the revenue adjustments related to separate proceedings in the absence of compelling circumstances.") (citing *San Diego Gas & Elec. Co.*, 93 F.E.R.C. ¶ 61,333, at pp. 62,133-34 (2000) (rejecting crediting proposal and requiring customer refunds) and *Otter Tail Power Co.*, 17 F.E.R.C. ¶ 61,151 (1981) (denying motion for offset)).

104. *Interstate Natural Gas Ass'n v. FERC*, 756 F.2d 166, 171 (D.C. Cir. 1985).

A. Cost-Based Rate Refunds

Over the years since passage of the NGA and the FPA, the FPC and the FERC have in innumerable natural gas and electric rate proceedings ordered refunds of rates found to be unjust and unreasonable following a cost-based review, thus, providing consumers with the “protection from excessive rates and charges” due under the NGA and the FPA.¹⁰⁵

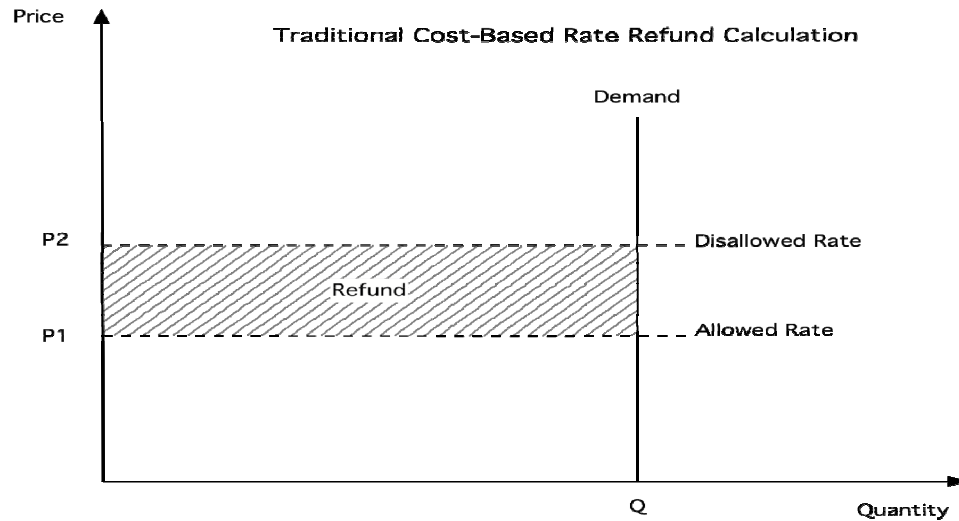
Prices in a cost-based regime are typically stated on a price per unit basis. Refunds would be calculated consistently with Figure 3,¹⁰⁶ thus providing consumers with the refunds shown by the cross-hatched area, plus interest, of any excessive charges from (a) the date a rate filing is made effective, subject to refund, (b) the date of a complaint under the FPA, or (c) prospectively from the date of a FERC order on a complaint in the case of the NGA.¹⁰⁷

The calculation for a cost-based refund can be stated algebraically as:

$$\text{Refund} = ((P2-P1) \times Q) + I,$$

where P1, P2, and Q are shown on Figure 3 and I equals the total interest or time value on the refund amount. Because this refund is calculated and paid by a single seller, with time value, consumers would be made whole.

Figure 3



B. Formula Rate Refunds

As noted by the U.S. Court of Appeals for the D.C. Circuit, the Commission has been using formula rates in place of stated price per unit rates since the early 1970s:

105. *Atlantic Ref. Co. v. Public Serv. Comm'n of New York*, 360 U.S. 378, 388 (1959).

106. The graphics and refund analysis used in this section of the article follows that presented in Peter Fox-Penner et al., *Competition in Wholesale Electric Power Markets*, 23 ENERGY L.J. 281, 292-99 (2002). This article highlights key economic and policy issues faced by regulators in the enforcement of market-based rates in wholesale markets. Notably, however, the article *assumed* that the FERC need not determine who is at fault in order to insist on just and reasonable prices. *Id.* at 297.

107. *See supra* Sections II.A and II.B.

The Commission has been accepting formula rates since the early 1970s. As defined by the Commission, a formula rate specifies the cost components that form the basis of the rates a utility charges its customers. The Commission's acceptance of formula rates is premised on the rate design's "fixed, predictable nature," which both allows a utility to recover costs that may fluctuate over time and prevents a utility from utilizing excessive discretion in determining the ultimate amounts charged to customers. . . .¹⁰⁸

The court went on to observe that "in any event, the court has rejected the notion that charges assessed pursuant to a formula rate violate the filed rate doctrine; rather, the formula itself is the filed rate that provides sufficient notice to ratepayers for purposes of the doctrine."¹⁰⁹

Like the cost-based refund, the formula is capable of calculation by a seller that yields a specific price for a given point in time. Thus, the refund calculation is much like that for a cost-based regime, though the price itself may vary over the course of a refund period. In this instance, a refund calculation could be algebraically viewed as:

$$\text{Refund} = ((F2-F1) \times Q) + I,$$

where F2 is the proposed or challenged formula, F1 is the formula rate found to be just and reasonable, Q is the quantity taken for each rate period yielded by the formula, and I equals the total interest or time value on the refund amount.

Because the results of the formula can change at specified intervals (*e.g.*, monthly, annually, or some other specified period), it requires the summation of the various prices as they change over those intervals times the quantity sold in each interval. While calculating the results of a formula adds complexity to tracking the actual prices (and thus the calculation of refunds if they are found to be due), the basic refund calculation is the same as for the cost-based refund. Once again, because there is only one seller, consumers are made whole when that seller makes full refunds with interest.

C. Market-Based Rate Refunds

There are two distinct types of market-based rates under the Commission's market-based jurisprudence: (i) contract-based markets and (ii) single-price clearing or auction markets.¹¹⁰ The first type of market-based rate involves sellers found to lack market power that then negotiate rates bilaterally. These bilateral deals can be long or short-term, may be made pursuant to individually negotiated agreements or under the terms of standardized or "master" contracts,¹¹¹ and are generally accorded a presumption that the negotiated price is just and reasonable.¹¹²

108. *Public Utils. Comm'n of Cal. v. FERC*, 254 F.3d 250, 254 (D.C. Cir. 2001) (internal citations omitted); *accord Transwestern Pipeline Co. v. FERC*, 897 F.2d 570, 578 (D.C. Cir. 1990) ("where the Commission explicitly adopts a formula and indicates when it will take effect, courts may not (without invading the Commission's province) say that such a formula may never qualify as a 'rate'").

109. *Public Utils. Comm'n of Cal.*, 254 F.3d at 254 n.3 (emphasis added) (citation omitted).

110. These markets can be used for a variety of products, including day-ahead and real-time energy, congestion, capacity, and ancillary services.

111. See, *e.g.*, Andrew Katz, *Using the EEI-NEM Master Contract to Manage Power Marketing Risks*, 21 ENERGY L.J. 269 (2000) (explaining why standardized power contracts are important in electric markets and describing the Edison Electric Institute/National Energy Marketers Association Master Agreement); *California*

The second type of market-based rate involves energy sales into organized auction markets, usually where there is a single price that clears the market for each interval that the market is run. These single-price clearing markets are generally found within the confines of a regional transmission organization (RTO) or independent system operator (ISO) and are subject to market rules provided in the RTO or ISO tariffs that are filed with the FERC, as well as related operating or business manuals or procedures.¹¹³

The distinction between these two basic types of markets was recently articulated by the Commission:

In [a single-price clearing] market, all sellers are paid the price bid by the marginal seller. In contrast, in a market that operates solely through bilaterally negotiated contracts, each seller receives only what a specific buyer agrees to pay for a given transaction and each buyer has the opportunity to attempt to negotiate a lower price.¹¹⁴

The next two sections will discuss refunds under these two quite different types of market-base regulatory regimes.

1. Refunds Calculations for Market-Based Bilateral Contracts

Market-based bilateral contracts themselves fall into two general types: long term and short term. Because these agreements generally have only two parties – a buyer (often a utility) and a seller (often an electric generator or marketer) – if refunds are found to be due, the refund calculation can be straightforward and similar to the calculation for a cost-based or formula-based rate refund. This is particularly the case for long-term contracts where the contract price will typically either take the form of a fixed or formula rate. Pricing provisions in these agreements also may use a market reference price or index for determining the rate to be charged under the contract. Where refunds are required, the refund calculation would follow the calculation for a cost-based or formula rate shown in Figure 3.

2. Refunds Calculations in Single-Price Clearing Markets

Refunds in a single-price clearing market can be significantly more complicated than refunds under cost-based rates, formula rates, or market-based contracts. This is because *any* market participant, or combination of participants,

ex rel. Brown v. Powerex Corp., 135 F.E.R.C. ¶ 61,178 (2011) (addressing bilateral power purchases made under the framework of the Western Systems Power Pool Agreement); Karen Goepfert, *For the Long Haul: The Suitability of the Base Contract for the Sale and Purchase of Natural Gas for Long-Term Transactions*, 27 ENERGY L.J. 583 (2006) (describing applicability of the North American Energy Standards Board “base contract” widely used for short-term natural gas markets to long-term transactions).

112. *Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527 (2008) (affirming that the *Mobile-Sierra* doctrine applies in context of market-based contracts).

113. The Commission’s general policy is that only the RTO or ISO tariff must be filed for approval at the FERC; business manuals or similar guidance documents by an RTO or ISO are not required to be filed. *See, e.g., California Indep. Sys. Operator Corp.*, 119 F.E.R.C. ¶ 61,076 at P 656 (2007) (explaining the Commission has “consistently rejected arguments that every manual or operating procedure should be on file with the Commission”).

114. *Puget Sound Energy, Inc. v. All Jurisdictional Sellers of Energy*, 137 F.E.R.C. ¶ 61,001 at P 24 (2011); *see also* *Port of Seattle v. FERC*, 499 F.3d 1016, 1026 (9th Cir. 2007) (summarizing *Puget Sound Energy, Inc. v. All Jurisdictional Sellers of Energy*, 106 F.E.R.C. ¶ 61,109 (2004)).

may be able to affect the market-clearing price that then is paid to all participants in that market. This possibility is graphically illustrated in Figure 4.

Figure 4

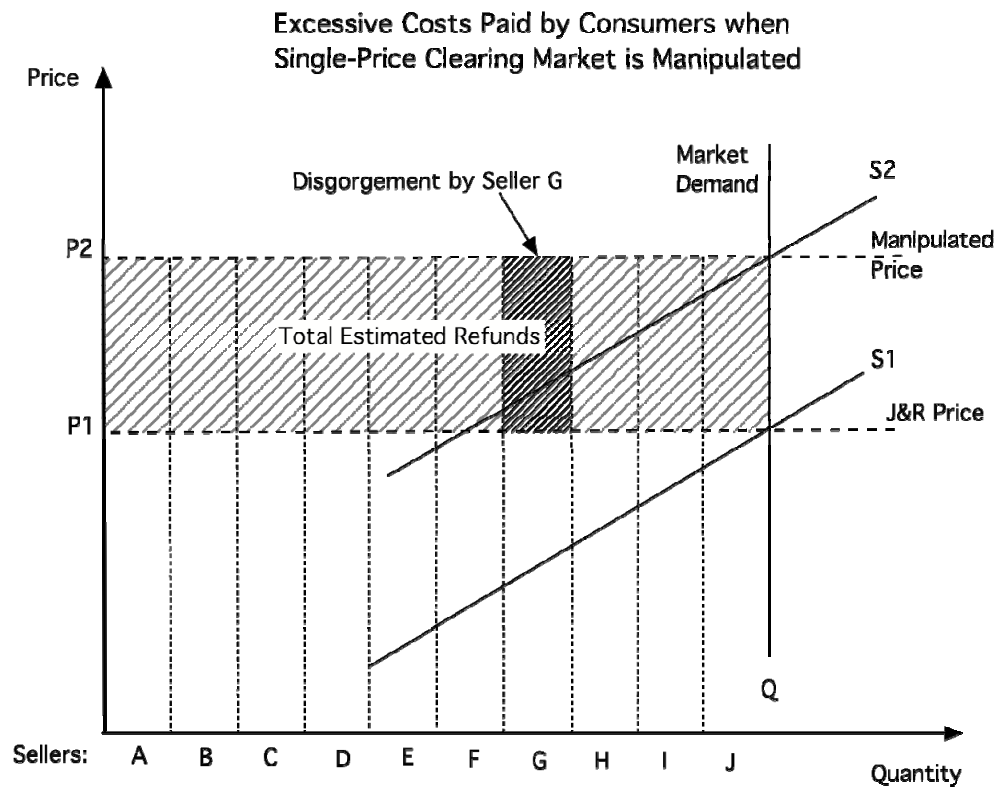


Figure 4 assumes there are ten sellers in the market: Seller A through Seller J. If Seller G withholds supply or takes some other manipulative action that results in a shift of the supply curve from the competitive curve, S1, to a manipulated curve, S2, all the sellers will receive an increased price.¹¹⁵ Where the short-term demand curve approaches vertical, indicating demand inelasticity, consumers will pay an amount in excess of the just and reasonable supply curve equal to the full shaded area on the graph.¹¹⁶

While it may appear that it should be a simple matter to provide refunds for this market manipulation, in fact, it is extraordinarily complicated. First, it may not be evident, *post*-manipulation, what the competitive supply curve would have looked like if there had not been manipulation. While it may be possible to “rerun” or “model” the market by making assumptions about what the market would have looked like before it was manipulated, such calculations may require facts, such as the marginal or variable costs of all the supply sources that make

115. The shape of the actual supply curves would not be the straight lines shown here but, more likely, step functions representing the marginal quantity and cost of each succeeding unit of generation (or demand response program) as it comes on line to meet (or reduce) current demand.

116. For a cogent explanation of the reason for and implications of the inelasticity of short-term demand for electricity, see Fox-Penner et al., *supra* note 106, at 299-305.

up the curve, which may not be readily available to the market or the regulator.¹¹⁷ The complexity becomes even greater if strategic seller and buyer responses are considered or if there are related markets.¹¹⁸

The practical difficulty of rerunning a market is amply illustrated by the process that has been underway for over a decade to rerun the market and provide refunds to consumers in response to the California Energy Crisis. As described by the FERC in 2005, this process involved four stages:

1. [S]ettling past accounts to have an accurate baseline from which to calculate refunds . . . ;
2. establishing just and reasonable market clearing prices through use of a formula . . . ;
3. adjusting the refund obligation to account for emissions, fuel and general cost recovery offsets; and
4. final accounting and payment.¹¹⁹

During these proceedings, each element of this calculation has been vigorously contested before the FERC and in the courts (where significant aspects of the refund process and calculations remain pending). As the FERC noted in 2005, the evidentiary hearing to establish the just and reasonable market clearing prices alone took eighteen months with a hearing record of over 5,000 pages and twenty shelf feet of exhibits.¹²⁰ To date, there have been over 1,400 issuances by administrative law judges or the Commission in over 250 sub-dockets in the main EL00-95 refund proceeding docket,¹²¹ with petitions for review filed in response to virtually every appealable order.¹²²

In sum, the calculation of refunds for market-based rates first depends on whether the sales occur pursuant to a contract or in an organized single-price clearing market. If the former, the refund or disgorgement computation should be relatively straight forward, but the contract itself must be accorded a just and reasonable presumption under the *Mobile-Sierra* doctrine, unless the contract itself is illegal or the parties to the contract have agreed otherwise. If the latter, the refund computation becomes significantly more complicated as do the underlying legal and equitable issues. These issues will be further developed in the next section.

V. THE FERC'S LEGAL AUTHORITY TO PROVIDE REFUNDS UNDER ITS MARKET-BASED RATE REGIME

A. Reprising the Commission's Discretion

As is now abundantly clear, the Commission enjoys considerable discretion in fashioning remedies, particularly when they involve rules, as opposed to rates, as long as it adequately explains the basis for its actions:

117. *Id.* at 292-296.

118. *Id.* at 295 (noting "possibility of a variety of strategic competitor and buyer responses"), 335-36 (explaining relationship between spot and forward markets).

119. FERC 12/27/05 REPORT TO CONGRESS, *supra* note 8, at 20.

120. *Id.* at 4-5.

121. These statistics are based on a search for all FERC issuances in Docket No. EL00-95 in the FERC eLibrary system available at www.ferc.gov (last visited on Nov. 25, 2011).

122. FERC 12/27/05 REPORT TO CONGRESS, *supra* note 8, at 25-26 (describing appeals as of 2005; since then, numerous additional appeals have been filed in response to subsequent Commission orders).

The difficult problem of balancing competing equities and interests has been given by Congress to the Commission with full knowledge that this judgment requires a great deal of discretion. Accordingly, it is not the role of the courts to second guess the Commission's judgment because we think we could devise a better solution than that which the agency has adopted so long as the agency's determination has a rational basis.¹²³

Similarly, in addressing the legality under the FPA of the FERC's implementation of market-based rates in Order No. 697, the U.S. Court of Appeals for the Ninth Circuit, applying the familiar *Chevron* analysis, concluded that:

The question before us here is not whether we think market-based rates are a good idea; instead, it is whether the market-based rate policy embodied in Order 697 exceeds FERC's authority as conferred by the FPA. Taking into account *Chevron* deference, the law of our circuit, other relevant precedent, and the direction of the Supreme Court as to how we should approach such administrative law issues concerning federal agencies, we conclude that Order 697, as presented to us in this petition, does not per se violate the FPA.¹²⁴

The Commission should likewise enjoy considerable discretion in fashioning remedies when markets do not work as expected. However, this discretion has limits. The remainder of this section explores the Commission's refund authority in the context of market-based contracts and single-price clearing markets.

B. Market-Based Contracts

Contracts under the NGA and the FPA, including market-based contracts, are *presumed* to be just and reasonable under the "*Mobile-Sierra*" doctrine, a doctrine whose continuing vitality has been reinforced in two recent Supreme Court decisions,¹²⁵ unless the parties to the contract agree otherwise,¹²⁶ the FERC determines that the contract "seriously harms the public interest,"¹²⁷ or where there is a "causal connection between unlawful activity and the contract rate."¹²⁸ Thus, market-based contracts enjoy a just and reasonable presumption that may make challenges to such contracts, particularly on a market-wide basis, difficult to sustain.¹²⁹ As the Supreme Court observed in *Morgan Stanley*, "the mere fact

123. *Arizona Elec. Power Coop. v. FERC*, 631 F.2d 802, 809 (D.C. Cir. 1980) (citing *Gulf Oil Corp. v. FPC*, 563 F.2d 588, 608 (3d Cir. 1977)).

124. *Montana Consumer Counsel v. FERC*, 659 F.3d 910, 922-23 (9th Cir. 2011) (referencing *Chevron, U.S.A., Inc. v. Natural Res. Def. Council*, 467 U.S. 837, 842 (1984)).

125. *NRG Power Mktg., LLC v. Maine Pub. Utils. Comm'n*, 130 S. Ct. 693, 696 (2010); *Morgan Stanley Capital Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527 (2008); *see also, PacifiCorp v. Reliant Energy Servs., Inc.*, 105 F.E.R.C. ¶ 61,184 (2003) (affirming that the *Mobile-Sierra* doctrine applies to market-based rate contracts, even if not specifically reviewed by the Commission).

126. *Morgan Stanley*, 554 U.S. at 534 (citing *United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103, 110-113 (1958)) (providing that parties can use a "Memphis" clause to contract out of the *Mobile-Sierra* presumption).

127. *NRG*, 130 S.Ct. at 696; *Morgan Stanley*, 554 U.S. at 530.

128. *Morgan Stanley*, 554 U.S. at 554-555.

129. *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983) (finding the public interest standard to be "practically insurmountable"); Tewksbury et al., *New Chapters*, *supra* note 62, at 443-444 (explaining that the Supreme Court has made clear that where rates qualify as contract rates, "the FERC is obligated to apply *Mobile-Sierra* presumption to . . . those rates" (in absence of *Memphis* clause) unless "the contract seriously harms the public interest") (quoting *NRG*, 130 S.Ct. at 700).

that the market is imperfect, or even chaotic, is no reason to undermine the stabilizing force of contracts that the FPA embraced as an alternative to ‘purely tariff-based regulation.’¹³⁰

One recent effort to obtain refunds in the context of market-based contracts for energy purchased during the California Energy Crisis was summarily rejected by the Commission in an order that highlighted the elevated showing that would be required on a contract-by-contract basis, finding “the California AG must first prove that individual sellers violated the FPA or their filed tariffs and that such violation resulted in an unjust and unreasonable contract.”¹³¹ The Commission went on to explain that “[s]econd, to the extent the California AG is claiming that the short-term bilateral sales contracts were unjust and unreasonable, he has not adequately pleaded or otherwise advanced evidence sufficient to address the *Mobile-Sierra* presumption regarding contract modification.”¹³²

The Commission also denied market-wide relief finding that,

in the context of short-term bilateral contracts, a market-wide refund remedy for tariff violations would be appropriate only if a complainant clearly demonstrated that all sellers had engaged in tariff violations. Otherwise, sellers following the law would be penalized because of someone else’s bad conduct, an unfair and unreasonable result.¹³³

This case was followed by *Puget Sound Energy, Inc. v. All Jurisdictional Sellers of Energy and/or Capacity at Wholesale into Electric Energy and/or Capacity Markets in the Pacific Northwest, Including Parties to the Western Systems Power Pool Agreement*, which established a hearing to take new evidence but cautioned that “parties seeking refunds must submit evidence not only on whether unlawful market activity occurred, but must also demonstrate a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract”¹³⁴ and that there must be “evidence that demonstrates that the seller’s behavior ‘directly affect[ed]’ contract negotiations.”¹³⁵

C. Single-Price Clearing Markets

1. The Potential Impact of a Single Seller on the Market

While the jurisprudence of refunds for market-based contracts appears to have clarified over the past several years, the same cannot yet be said for refunds in single-price clearing markets. The basic difficulty is illustrated in Figure 4, where only Seller G manipulated the market, but every other seller (and there may be hundreds of sellers in some markets) benefited from the higher price obtained through this manipulation.

130. *Morgan Stanley*, 554 U.S. at 547-548 (quoting *Verizon Communs., Inc. v. FCC*, 535 U.S. 467, 479 (2002)).

131. *California ex rel. Brown v. Powerex Corp.*, 135 F.E.R.C. ¶ 61,178 at P 2 (2011), *request for reh’g pending*.

132. *Id.* at P 5.

133. *Id.* at P 77 (footnote omitted).

134. *Puget Sound Energy, Inc. v. All Jurisdictional Sellers of Energy*, 137 F.E.R.C. ¶ 61,001 at P 21 (2011).

135. *Id.*

FERC Commissioner Massey highlighted this same issue in 2003 when he concurred on a prescriptive set of market behavior rules:

Market manipulation can raise the market prices paid by all market participants and collected by all sellers. *In such a case, the appropriate remedy may be that the manipulating seller makes the market whole.* I would prefer to not take this or any monetary remedy off of the table, but instead to allow the Commission the flexibility to tailor the remedy to the circumstances of each case.¹³⁶

The real world impact that a single seller can have was dramatically illustrated on May 25, 1999, when an Enron trader submitted a schedule to the California Independent System Operator Corporation (CAISO) to move power across an electric line near Silver Peak, California.¹³⁷ The proposed schedule was far more than the line could accommodate, causing congestion and a significant price rise in the California electric market.¹³⁸ Overall, this single action resulted in California consumers being overcharged by an estimated \$4.6 to \$7 million.¹³⁹ Consumers never received a refund; Enron was fined \$25,000 by the CAISO and “promised” not to repeat its experiment.¹⁴⁰

Commissioner Massey’s suggestion that the wrongdoer should make the market whole may initially appear to be a fair and focused remedy, particularly where there is an intent to distort an entire market. Practically, however, it may not be possible for the wrongdoer to make the market whole simply because the cost of doing so would be in excess of the net value of the wrongdoer. That is, if Seller G in the example in Figure 4 is required to make the market whole, its refund obligation would be ten times the amount it actually collected in excess of the just and reasonable rate; if there were 100 equally-sized participants, it would be 100 times greater.

Moreover, this remedy may be suspect under a *Coastal* analysis since Seller G would be required to forego far more than its costs.¹⁴¹ And, if Seller G does

136. *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 105 F.E.R.C. ¶ 61,218, at p. 62,172 (2003) (Massey, Comm’r, concurring) (emphasis added); *see also* Fox-Penner et al., *supra* note 106, at 294 (explaining that action by one seller can raise market price for all buyers).

137. John R. Wilke & Robert Gavin, *Brazen Trade Marks New Path of Enron Probe*, WALL ST. J., Oct. 21, 2002, at C1; Kurt Eichenwald, *A Powerful Flawed Witness Against Enron*, N.Y. TIMES, Oct. 21, 2002, <http://www.nytimes.com/2002/10/21/business/a-powerful-flawed-witness-against-enron.html?pagewanted=all&src=pm>.

138. Eichenwald, *supra* note 137.

139. Wilke & Gavin, *supra* note 137.

140. *Id.*; Eichenwald, *supra* note 137.

141. This analysis presumes that the additional recovery is not a penalty. Pursuant to FPA sections 316 and 316A penalties of up to \$1 million per day per violation may be assessed for specified violations of the FPA or Part II of the FPA. 16 U.S.C. §§ 825o to 825o-1 (2006). However, unlike funds obtained through disgorgement, which may be distributed to the harmed party or parties, civil penalties required by the FERC are usually paid directly to the U.S. Treasury. *Revised Policy Statement on Penalty Guidelines*, 132 F.E.R.C. ¶ 61,216 at P 216 (2010) (explaining different purposes and dispositions of disgorged funds and penalties). The FERC has held that penalties that are assessed under FPA section 215 and 16 U.S.C. § 824o, relating to reliability violations, may be paid either to the U.S. Treasury, to the North American Electric Reliability Corporation (NERC), or to a designated regional reliability organization, depending on who initiated or investigated the violation. 18 C.F.R. pt. 39 (2011); *Rules Concerning Certification of the Electric Reliability Organization*, 114 F.E.R.C. ¶ 61,104 at PP 626-29 (2006); *see also PacifiCorp*, 137 F.E.R.C. ¶ 61,176 at P 23 (2011) (order on settlement providing that one-half of a penalty be paid to the U.S. Treasury and the other half to NERC, reflecting “the dual nature” of the subject investigation).

not make the market whole, consumers are positively harmed by the shortfall, while entities that received the unjustly high market price enjoy a windfall.

2. New Entrants in Manipulated Markets

If the market manipulation is not quickly corrected, the higher prices may also attract other market participants whose costs are above the theoretical competitive price curve but lower than the manipulated price. These participants would profit under the manipulated price curve but, if required to make refunds, could argue that any refunds above their costs was unlawful.¹⁴² On the other hand, to the extent that revenues resulting from above-competitive market prices could be viewed as an “unjust enrichment, which the Commission is empowered to prevent,”¹⁴³ they too could be subject to refund or disgorgement.

3. The Filed Rate in a Single-Price Clearing Market

If Seller G alone cannot make refunds sufficient to make consumers whole, can other market participants who received the benefit of Seller G’s wrongdoing be made to shoulder the burden of refunds caused by Seller G’s wrongdoing? In at least two cases, the Commission has answered that question as yes: that the filed rate within a market is the entire set of rules of that market, and, therefore, refund liability could be imposed on all sellers in a market:

- We remind the parties that, consistent with the filed rate doctrine, the ISO already has the authority, and is required, to correct all prices that do not reflect operation of the [ISO’s] market rules (which are the filed rate).¹⁴⁴
- [A]ll sellers of energy in the California ISO and PX spot markets should be subject to refund liability . . . based on our review of the controlling law, the involvement of . . . sellers in the California centralized ISO and PX spot markets, and the equities of the situation.¹⁴⁵

More recently, however, the Commission appears to be taking a more restrictive view of the filed rate, holding that it is a particular seller’s “market-based rate tariff, with its appurtenant conditions and requirement for filing transaction-specific data in EQRs [(electronic quarterly reports)], [that] is the filed rate.”¹⁴⁶ In this formulation, an individual seller’s market-based rate can not be stated on a dollars per unit basis but, instead, is a *set of rules and ex post filing requirements* that presumably, taken across all sellers and in conjunction with market rules established by the relevant market (*e.g.*, an ISO or RTO), will

142. Indeed, it was this concern that led the Commission in the California Refund Proceedings to permit refunds to be reduced by sellers who could show the refund methodology resulted in an “overall revenue shortfall” in the relevant markets. FERC 12/27/05 REPORT TO CONGRESS, *supra* note 8, at 23-24.

143. *Texas Gas Exploration Corp.*, 24 F.E.R.C. ¶ 61,098, at p. 61,262, *order on reh’g*, 24 F.E.R.C. ¶ 61,405 (1983), *aff’d*, *Columbia Gas Transmission Corp. v. FERC*, 750 F.2d 105 (D.C. Cir. 1984) (requiring refunds to reflect outcome of a dispute that had been a condition of the gas sales).

144. *ISO New England, Inc.*, 90 F.E.R.C. ¶ 61,141, at p. 61,425 (2000) (emphasis added).

145. *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Service*, 96 F.E.R.C. ¶ 61,120, at p. 61,511 (2001) (emphasis added); *see also supra* text accompanying note 56 (subset of these sellers was later determined not to be subject to FERC refund jurisdiction at the time this order was issued).

146. Order No. 697, *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, F.E.R.C. STATS. & REGS. ¶ 31,252 at P 961, 72 Fed. Reg. 39,904 (2007) (to be codified at 18 C.F.R. pt. 35) [hereinafter Order No. 697].

yield a competitive rate for the entire market and thus for each seller in that market.

This view of the filed rate was upheld in *Montana Consumer Counsel* with the court observing that “the ‘rate’ filed by authorized power wholesalers is the ‘market rate,’ and that rate does not ‘change’ even though the prices charged by the wholesalers may rise and fall with the market.”¹⁴⁷ The court then went on to hold that the “FERC’s assertion that a rate ‘change’ occurs only once, when an authorized seller files a market-based rate, is a reasonable interpretation.”¹⁴⁸ In other words, the court delinked the seller’s filed rate from the overall market price.

The delinking of a seller’s “filed rate” from the “market price” then leads to a critical question for refunds in a market-based regime: if a seller has followed the rules that comprise its filed rate, can the seller be held liable and made to pay refunds if *another* seller (Seller G in Figure 4) causes an unjust price increase? That is, if a seller is not at fault, has followed its tariff rules, and has not acted in a manner inconsistent with the market-wide tariff rules, should it nonetheless be required to make refunds if the market-wide price is found to be unjust and unreasonable?¹⁴⁹

Order No. 697 itself did not directly answer this question, instead focusing just on the *seller* receiving market-based rate authorization and the remedies that could be assessed against that seller:

The Commission may also, based on its review of EQR filings or daily market price information, investigate a specific utility or anomalous market circumstances to determine whether there has been any conduct in violation of RTO/ISO market rules or Commission orders or tariffs, or any prohibited market manipulation, and take steps to remedy any violations. These steps could include, among other things, disgorgement of profits and refunds to customers if a seller is found to have violated Commission orders, tariffs or rules, or a civil penalty paid to the United States Treasury if a seller is found to have engaged in prohibited market manipulation or to have violated Commission orders, tariffs or rules.¹⁵⁰

Once again, it appears that the focus is on the ability to correct the behavior of individual actors within the market but not on a remedy that would, when manipulative behavior results in market-wide price distortions, return the entire market to what should have been charged, that is, to the *status quo ante*. Returning to the example in Figure 4, if the entire market is not rerun, the difference between the amount that may be obtained from disgorgement from Seller G and the impact that Seller G had on the full market, an amount equal to 90 percent of the total overcharge, is allocated to consumers.

When examined using traditional regulatory precedent, it appears that requiring *full* refunds from *all* sellers is in fact the logical answer that continues to “afford consumers a complete, permanent and effective bond of protection

147. *Montana Consumer Council v. FERC*, 659 F.3d 910, 921 (9th Cir. 2011).

148. *Id.* at 921-22.

149. This same issue was identified by Fox-Penner et al. who noted that “[o]ne of the most important questions is whether the FPA mandates [the restoration of just and reasonable prices when competition fails] as a strict or fault-based liability standard.” Fox-Penner et al., *supra* note 106, at 297. Finding the issue to be one of legal interpretation, Fox-Penner et al. did not attempt to answer the question, instead assuming for purposes of its economic analysis that the standard was strict liability. *Id.*

150. Order No. 697, *supra* note 146, at P 964.

from excessive rates and charges.”¹⁵¹ Whether it will also be the legal answer has yet to be conclusively determined. And if it is the legal answer, whether it will then be followed by the FERC or in most cases set aside on “discretionary” or “equitable” grounds remains an open question.

4. The Just and Reasonable Standard in a Single-Price Clearing Market

Tariff rates, which include rates set in single-price clearing markets pursuant to the tariffs of marketers and system operators, are generally subject to the traditional just and reasonable standard of review. However, in a recent order on remand of *Maine Public Service*, the Commission held that where the parties to a settlement had invoked the *Mobile-Sierra* presumption, the Commission would permit that presumption to apply to tariff rates for electric capacity that were set in a market auction process.¹⁵² In dissent, Commissioner Norris expressed the concern that:

the approach adopted in this order is inconsistent with the Commission’s obligations under the FPA, in non-contract rate situations, to ensure that rates, terms and conditions of service are just and reasonable and not unduly discriminatory. I also believe today’s order establishes a policy that will be difficult to administer in practice and could hurt the Commission’s ability to adequately protect consumers over the long-term.¹⁵³

Commissioner Norris was further concerned that this precedent would lead to additional proposals to apply the *Mobile-Sierra* presumption in cases involving market-based rates, proposals that would potentially bind future Commissions.¹⁵⁴

D. Illustrative Cases

Three cases relating to markets operated by the New York Independent System Operator, Inc. (NYISO), together with a case from the New England ISO Inc. (NE-ISO), illustrate the range of Commission responses to requests for market-wide relief. The first three cases relate to NYISO’s Temporary Extraordinary Procedures (TEP) which were “designed to address unanticipated market design flaws and transitional abnormalities . . . in the first ninety days of [NYISO] operations and . . . in emergencies impose, extraordinary corrective measures.”¹⁵⁵ A similar provision remains in the NYISO tariff today which provides that “[the NYISO] shall review market clearing prices calculated for Energy and Ancillary Services and shall correct any price it determines not to have been calculated in accordance with the [NYISO] tariffs.”¹⁵⁶ In the first case, the Commission denied relief to a seller that claimed the adjustments were

151. *Atlantic Ref. Co. v. Public Serv. Comm’n of N.Y.*, 360 U.S. 378, 388 (1959); *accord*, *NAACP v. FPC*, 520 F.2d 432, 438 (D.C. Cir. 1975) (“Commission’s primary task . . . is to guard the consumer from exploitation . . .”).

152. *Devon Power LLC*, 134 F.E.R.C. ¶ 61,208 at P 2 (2011).

153. *Id.* at p. 62,047 (Norris, Comm’r, dissenting in part).

154. *Id.*

155. *New York Indep. Sys. Operator, Inc.*, 88 F.E.R.C. ¶ 61,228, at p. 61,752 (1999).

156. NYISO, MST ATTACHMENT E: PROCEDURES FOR RESERVING AND CORRECTING ERRONEOUS ENERGY AND ANCILLARY SERVICES PRICES at § 20 (2011), available at http://www.nyiso.com/public/webdocs/documents/tariffs/market_services/ms_attachments/att_e.pdf (Attachment E of NYISO’s Market Administration and Control Area Services Tariff is part of the NYISO tariff filed in FERC Docket No. ER10-1657-000 on June 30, 2010; the full tariff is available on FERC’s eLibrary system).

not justified and were made without timely notice,¹⁵⁷ in the second case, the Commission invoked its discretion and denied refunds to buyers;¹⁵⁸ in the third case, the Commission granted relief to sellers and required prices to be adjusted upward where the NYISO had used its TEP authority to reduce prices.¹⁵⁹

In the NE-ISO case the Commission denied refunds, finding that even where there may have been overcharges, refunds were not justified on, *inter alia*, equitable grounds where notice of a possible adjustment had not been provided and there was no evidence of actual market manipulation.¹⁶⁰

1. TEP I: Real Time Energy Price Corrections

On December 11 to 12, 1999, the NYISO miscalculated real-time energy prices due to a software error, an error that it quickly recognized and corrected.¹⁶¹ NRG Power Marketing, Inc. complained that the adjustments to correct this error were unjustified and that the notice of the adjustment, which resulted in a significant downward price revision for the affected hours, had not been provided in accordance with the FERC orders approving the TEP.¹⁶²

The Commission rejected the complaint finding that the NYISO did not need to rely on TEP authority to correct incorrect energy clearing prices. It explained that “the ISO has the authority, and is required, to correct all prices that do not reflect operation of the ISO market rules (which are the filed rate).”¹⁶³ Refunds in this case were not required because the corrected prices – prices that reflected the filed rate – were reposted shortly after the corrections, thus permitting consumers to obtain the benefit of the lower prices immediately.¹⁶⁴

2. TEP II: The Operating Reserves Markets

During a period from January 29 through March 27, 2000, the NYISO excluded a pumped-storage unit and western suppliers from its operating reserves market.¹⁶⁵ As a result, prices for non-spinning reserves were higher than what they otherwise would have been.¹⁶⁶ Following a series of orders involving potential reruns of the NYISO operated reserve markets, and two trips to the D.C. Circuit Court of Appeals, the FERC ultimately ruled that the NYISO did not abuse its discretion when it refrained from using its TEP authority to

157. *NRG Power Mktg., Inc. v. New York Indep. Sys. Operator, Inc.*, 91 F.E.R.C. ¶ 61,346 (2000).

158. *New York Indep. Sys. Operator, Inc.*, 91 F.E.R.C. ¶ 61,218 (2000), *order on reh'g*, 97 F.E.R.C. ¶ 61,155 (2001), *order on reh'g*, 99 F.E.R.C. ¶ 61,125 (2002), *pet. for rev. granted in part*, Consolidated Edison Co. of N.Y. v. FERC (*ConEd I*), 347 F.3d 964 (D.C. Cir. 2003), *order on remand*, 110 F.E.R.C. ¶ 61,243, *order on reh'g*, 113 F.E.R.C. ¶ 61,155 (2005), *aff'd*, Consolidated Edison Co. of N.Y. v. FERC (*ConEd II*), 510 F.3d 333 (D.C. Cir. 2007).

159. *H.Q. Energy Services, Inc.*, 97 F.E.R.C. ¶ 61,218 (2001), *reh'g denied*, 100 F.E.R.C. ¶ 61,028 (2002), *pet. for rev. granted sub nom.*, PSEG Energy Res. & Trade LLC v. FERC, 360 F.3d 200 (D.C. Cir. 2004), *order on remand*, 110 F.E.R.C. ¶ 61,243, *order on reh'g and clarification*, 113 F.E.R.C. ¶ 61,184 (2005), 114 F.E.R.C. ¶ 61,059, *order approving uncontested settlement*, 116 F.E.R.C. ¶ 61,031 (2006).

160. *Bangor Hydro-Electric Co. v. ISO New England, Inc.*, 97 F.E.R.C. ¶ 61,339 (2001).

161. 91 F.E.R.C. ¶ 61,436, at p. 62,163.

162. *Id.*

163. *Id.* at p. 62,166.

164. *Id.*

165. *New York Indep. Sys. Operator*, 110 F.E.R.C. ¶ 61,244 at P 10 (2005).

166. *New York Indep. Sys. Operator, Inc.*, 91 F.E.R.C. ¶ 61,218, at p. 61,794 (2000).

rerun markets and recalculate prices in the subject markets, even where there may have been technical tariff violations.¹⁶⁷ The FERC also declined to provide retroactive relief, finding it would violate the filed rate doctrine and rule against retroactive ratemaking.¹⁶⁸

ConEd I upheld the FERC's action with regard to the filed rate and retroactive ratemaking arguments but remanded the case to the FERC for inadequately explaining why it did not require refunds for the tariff violation, noting that the Commission "has an obligation to explain why it is departing from its 'general policy of granting full refunds.'"¹⁶⁹ On remand, the Commission again declined to order a rerun of the market or refunds.¹⁷⁰ It explained that the pricing method helped protect reliability and that refunds in these circumstances would penalize generators who received no windfall from the tariff violation.¹⁷¹ *ConEd II*, using a deferential standard of review, upheld the FERC's decision on remand of *ConEd I* to again not require refunds, noting that "[o]n remand, FERC [has] considered the relevant factors, balancing the several interests at stake, including the tariff violation, market context, high . . . prices paid, expectations of affected entities, various tariff provisions, and the need to balance fair prices and system reliability."¹⁷² The court went further, however, observing that the "decision not to order refunds for the NYISO's tariff violation was not inconsistent with the FPA's 'core purpose'" and that "the FPA has multiple purposes in addition to preventing 'excessive rates,' including protecting against 'inadequate service,'" and "promoting the 'orderly development of plentiful supplies of electricity.'"¹⁷³

3. TEP III: The Energy Market Price Spikes

The NYISO invoked its TEP authority to reset prices for two days, May 8 and 9, 2000, when energy prices unexpectedly spiked to over \$3,000 per MWh.¹⁷⁴ The NYISO reduced the prices to a range of \$331 through \$350 per MWh.¹⁷⁵ The Commission initially found that NYISO had acted within its authority and denied complaints that the NYISO should not have reset prices.¹⁷⁶ On review, however, the court found that the FERC had not adequately responded to the argument that there was no actual market flaw where a seller

167. *New York Indep. Sys. Operator, Inc.*, 91 F.E.R.C. ¶ 61,218 (2000), *order on reh'g*, 97 F.E.R.C. ¶ 61,155 (2001), *order on reh'g*, 99 F.E.R.C. ¶ 61,125 (2002), *pet. for rev. granted in part*, Consolidated Edison Co. of N.Y. v. FERC (*ConEd I*), 347 F.3d 964 (D.C. Cir. 2003), *order on remand*, 110 F.E.R.C. ¶ 61,244, *order on reh'g*, 113 F.E.R.C. ¶ 61,155 (2005), *aff'd*, Consolidated Edison Co. of N.Y. v. FERC (*ConEd II*), 510 F.3d 333 (D.C. Cir. 2007).

168. 113 F.E.R.C. ¶ 61,155 at P 48.

169. *ConEd I*, 347 F.3d at 974 (citing *Towns of Concord, Norwood, & Wellesley, Mass. v. FERC*, 955 F.2d 67, 76 (D.C. Cir. 1991)).

170. 110 F.E.R.C. ¶ 61,244, *order on reh'g*, 113 F.E.R.C. ¶ 61,155.

171. 113 F.E.R.C. ¶ 61,155 at PP 51-52.

172. *ConEd II*, 510 F.3d at 341.

173. *Id.* at 342 (internal citations omitted).

174. *H.Q. Energy Services, Inc.*, 97 F.E.R.C. ¶ 61,218, at p. 61,961 (2001), *reh'g denied*, 100 F.E.R.C. ¶ 61,028 (2002), *pet. for rev. granted sub nom.*, PSEG Energy Res. & Trade LLC v. FERC, 360 F.3d 200 (D.C. Cir. 2004), *order on remand*, 110 F.E.R.C. ¶ 61,243, *order on reh'g and clarification*, 113 F.E.R.C. ¶ 61,184 (2005), 114 F.E.R.C. ¶ 61,059, *order approving uncontested settlement*, 116 F.E.R.C. ¶ 61,031 (2006).

175. 97 F.E.R.C. ¶ 61,218, at p. 61,961.

176. *Id.* at p. 61,966, *reh'g denied*, 100 F.E.R.C. ¶ 61,028 (2002).

had bid its opportunity costs.¹⁷⁷ In remanding to the Commission, the court expressed skepticism that the FERC could reach the same result on remand without directly addressing that argument.¹⁷⁸

On remand, the Commission found that the price spike was not a market design flaw and, therefore, ordered the NYISO to make adjustments to sellers' payments based on what they would have received had the NYISO not reset prices.¹⁷⁹ As the Commission explained,

a market design flaw is defined as a situation in which the application of the ISO Procedures would result in inefficient markets or prices that would not be produced in a workably competitive market. Here, the NYISO market design permitted the NYPA to bid its true opportunity costs. Moreover, the acceptance of NYPA's bid cannot be found to be a market design flaw, because, at the time, the NYISO's system was experiencing a severe shortage of power.¹⁸⁰

Notwithstanding the complicated nature of the refunds, including issues relating to the flow through of refunds or surcharges from one market participant to another, the Commission affirmed its decision to require refunds to sellers, with interest, and established a hearing and settlement judge procedures to resolve the computational issues.¹⁸¹ The case eventually settled.¹⁸²

4. The Bangor Hydro-Electric Complaint

Bangor Hydro-Electric Co. filed a complaint with the Commission alleging that implementation errors in the ISO New England Inc. electricity market caused it to incur over \$1 million in excessive costs.¹⁸³ As described by the Commission:

On June 15, 2001, Bangor Hydro-Electric Company (Bangor Hydro) filed a complaint against ISO New England Inc. (ISO-NE), claiming that ISO-NE violated Market Rule 15 by failing to notice and correct "erroneous" energy clearing prices (clearing prices) so that they reflect the actual market prices. Bangor Hydro contends that these clearing prices resulted from a design flaw, within the meaning of Market Rule 15, in the electric dispatch system software (dispatch software) implemented by ISO-NE that produced unnecessary spikes (both downward and upward) in the real time marginal price of electricity. Bangor Hydro requests that the Commission issue an order directing ISO-NE to retroactively correct the erroneous clearing prices that occurred.¹⁸⁴

The ISO-NE conceded that there was a market implementation error that caused "very expensive" units to be dispatched to meet forecast demand, "producing high levels of price volatility."¹⁸⁵ The Commission, however, denied the complaint, noting that while there were implementation errors that resulted in higher prices, "the [market] clearing prices were established in accordance with

177. *PSEG Energy Res.*, 360 F.3d at 205.

178. *Id.* at 205-06.

179. 110 F.E.R.C. ¶ 61,243, at p. 61,997, *order on reh'g and clarification*, 113 F.E.R.C. ¶ 61,184.

180. 113 F.E.R.C. ¶ 61,184 at P 33 (internal quotation marks omitted).

181. *Id.* at PP 59-62.

182. 116 F.E.R.C. ¶ 61,031.

183. *Bangor Hydro-Electric Co. v. ISO New England, Inc.*, 97 F.E.R.C. ¶ 61,339, at p. 62,587 (2001), *reh'g denied*, 98 F.E.R.C. ¶ 61,298 (2002).

184. 97 F.E.R.C. ¶ 61,339, at p. 62,586.

185. *Id.* at p. 62,588.

ISO-NE's market rules and therefore did not violate the filed rate doctrine."¹⁸⁶ The Commission found, *inter alia*, that because notice was not given of a possible market rate change within seventy-five minutes as required by the tariff for implementation errors, requiring refunds would "go against" the design of the market rules.¹⁸⁷ The Commission further relied on equitable concerns raised by market participants:

to go back at this point and change those prices, when no notice was given by ISO-NE that such a disruption might occur, would do far more harm to wholesale electricity markets than is justifiable or appropriate in light of the circumstances . . . and would be fundamentally unfair to market participants. For instance, there is no dispute that the clearing prices at issue reflected the bids of units that were actually dispatched by ISO-NE, and there is no evidence that their bids were unjustified or resulted from the exercise of market power or market manipulation. Therefore, the generators responded in good faith to ISO-NE's dispatch instructions,¹⁸⁸ running their units with the expectation that they would be paid their bid price.

Thus, even after recognizing that there were excessively high payments, the Commission found that, beyond the filed rate limitations, equitable concerns relating to notice and reliance further foreclosed refunds, particularly where there was no evidence of market manipulation.

VI. CONCLUSION

In *Atlantic Refining*, the Supreme Court stated that the "[NGA] was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rate and charges."¹⁸⁹ This "bond of protection from excessive rates and charges," which is equally applicable to the FPA, has long ensured that consumers received full refunds, with interest, under cost-based rate regimes.¹⁹⁰

It now appears, however, that consumers are much less likely to receive refunds where excessive charges result from market dysfunctions or distortions. In the case of bilateral market-based contracts, such refunds would be available only in those rare cases where direct causality between unlawful activity and the contract rate can be proved or the "public interest" standard under the *Mobile-Sierra* doctrine can be overcome.

In the case of single-price clearing markets, there appears to be a trend to deny market-wide refunds on "equitable" grounds; however, there are not yet enough cases to evaluate whether in fact the FERC will rerun markets when circumstances warrant. Moreover, it does not yet appear there is a definitive legal answer to the question of whether the filed rate in a single-price clearing market is a seller-specific rate or whether refunds will be required for excessive market charges resulting from actions by another seller. While the overarching purpose of the NGA and FPA suggest that it should be sellers and not consumers that bear these costs, the goal of market finality and complications of rerunning markets after the fact may tilt the Commission to not require refunds on "equitable" grounds, as in the *TEP II* and *Bangor Electric* cases. Finally, the

186. *Id.* at p. 62,589.

187. *Id.* at p. 62,590.

188. *Id.*

189. *Atlantic Ref. Co. v. Public Serv. Comm'n of N.Y.*, 360 U.S. 378, 388 (1959).

190. *Id.*

Commission's action in *Devon* raises questions about the just and reasonable standard that may be applied in future market-based tariff cases.

That does not mean, however, that, the California Energy Crisis aside, overall consumers are not better off under competition than they would have been under traditional regulation. RTOs and ISOs do bring at least some consumer benefits but may also bring additional costs against which the benefits must be weighed.¹⁹¹ This calculus though is beyond the scope of this article. On one hand, the complexity of the markets and the even greater complexity of undoing unjustly high market rates – with the attendant disputes when refunds are attempted – make clear it is unlikely, even where a market rate is found to be unjust or not in conformance with the filed rate, that consumers will receive timely refunds for amounts paid in excess of the rate later determined to be just and reasonable. In addition, the Commission's focus on prevention of exercises of market power, using *ex ante* behavioral rules, coupled with *ex post* reporting requirements and aggressive oversight and enforcement at both the market and regulatory levels, may significantly limit future market dysfunctions. Thus, it is at least arguable that in cases where the manipulation is quickly identified and stopped, competitive markets will provide sufficient overall benefits such that consumers will still be better off than they would have been under traditional regulation.

What is clear, however, is that every time a market is manipulated resulting in higher than just and reasonable “competitive prices,” unless the market is fully rerun, consumers will no longer be made whole. Rather, it will now be consumers that “shoulder” the refund shortfalls when remedies are limited to disgorgement from individual sellers as opposed to market-wide refunds.

191. See, e.g., Kelly & Caplan, *supra* note 12, at 511-14.