

MITIGATING COSTS AND THE PREEMPTIVE EFFECT OF FEDERAL RATE ORDERS

*Frank P. Darr**

The role of federalism in the regulation of energy production is a long standing problem. In 1927, the Supreme Court created a regulatory void by concluding that the Commerce Clause precluded state regulation of interstate electric wholesale transactions.¹ The state commissions reacted by vocally opposing federal regulation that might affect their control of retail rates.² To alleviate some of those concerns, Congress set out in the Federal Power Act (FPA) clear recognition for the state role in setting local rates consistent with the states' existing constitutional authority.³ Utilities, however, have successfully asserted that federal orders restrict some local decision making.⁴ These successful efforts in turn have set off a new debate concerning the scope of federal authority to determine retail rates.⁵

The source of the debate is the application and extension of the filed rate doctrine. Under the filed rate doctrine, a federal order setting rates that is within the jurisdiction of the Federal Energy Regulatory Commission (FERC), the successor of the Federal Power Commission (FPC), preempts a conflicting order issued by a state commission.⁶ Although the doctrine had its origins in the preemption of state-ordered retail rates, the Supreme Court has extended the doctrine's application to preclude state review of the allocations

* B.A., 1979 The University of Akron; J.D., 1982 The Ohio State University College of Law; 1985-1987 Assistant Attorney General, Public Utilities Section, Office of the Ohio Attorney General; Assistant Professor, The Ohio State University College of Business.

1. *Public Util. Comm'n v. Attleboro Steam and Elec. Co.*, 273 U.S. 83 (1927).

2. CHARLES F. PHILLIPS, *THE REGULATION OF PUBLIC UTILITIES* 145-46 (2d ed. 1988). These concerns are also evident in the legislative history of Title 16. See *infra* notes 33-41 and accompanying text.

3. *Id.*

4. See *infra* notes 42-71 and accompanying text.

5. See, e.g., Andrea J. Ercolano & Peter C. Lesch, *Narragansett Update: From Washington Gas Light to Nantahala*, 7 *ENERGY L.J.* 333 (1986); Lorie J. Harris, *A Just Injustice: Mississippi Power & Light Co. v. Mississippi*, 25 *TULSA L.J.* 97 (1989); James E. Hickey, *Mississippi Power & Light Co.: A Departure Point for Extension of the "Bright Line" Between Federal and State Regulatory Jurisdiction over Public Utilities*, 10 *J. ENERGY L. & POL'Y* 57 (1989); Carl D. Hobelman, *The Narragansett Decision and Its Aftermath*, 6 *ENERGY L.J.* 33 (1985); Frank R. Lindh, *Federal Preemption of State Regulation in the Field of Electricity and Natural Gas: A Supreme Court Chronicle*, 10 *ENERGY L.J.* 277 (1989); Lehfeldt, *The Fading Bright Line: Federalism and Electric Regulation in the Reagan Years*, *ELECTRICITY J.* 16 (April 1989); Walter W. Nixon, III & Dr. Robert E. Johnston, *Nantahala Affirms Narragansett: Whither Pike County?* 8 *ENERGY L.J.* 1 (1987); Charles G. Stalon & Reinier H. J. H. Lock, *State-Federal Relations in the Economic Regulation of Energy*, 7 *YALE J. REG.* 427 (1990); Clinton A. Vince & John S. Moot, *Energy Federalism in the Wake of Mississippi Power & Light*, *ELECTRICITY J.* 24 (April 1989); Clinton A. Vince & John S. Moot, *Federal Preemption Versus State Utility Regulation in a Post-Mississippi Era*, 10 *ENERGY L.J.* 1 (1989); Elizabeth Newlin Taylor, *Pushing State Regulatory Commissions Behind the Bright Line: FERC Jurisdiction Prevails in Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 29 *NAT. RES. J.* 607 (1989); Sarah M. Foster, *Electric Energy Rate Regulation: Another Line Drawn in the Federal-State Jurisdictional Struggle*, 26 *WASHBURN L.J.* 632 (1987).

6. Vince & Moot, *Federal Preemption*, *supra* note 5, at 16.

of power and cost responsibilities among utilities or an individual utility's decision to incur the costs of joint nuclear construction.⁷ The effect of these decisions has been to rest increasing authority over retail rates with the FERC, a result all the more remarkable in that it came during the tenure of administrations which rhetorically discouraged the growth of federal intervention.⁸

Apart from the political posturing, however, the increasing role of federal regulators in retail rate making presents some difficult problems for retail rate regulation. As in the extensive litigation involving the construction of the Grand Gulf I nuclear plant, the FERC can order shifts of enormous amounts of new costs from one state to another by a preemptive federal order.⁹ Likewise, the FERC, under its authority to review and revise contracts between interstate pool members, can restructure the agreements that form the basis of many of the large power pools.¹⁰ Further, differences in FERC and state rate making methodologies, in combination with an expanded rule of preemption, may encourage forum shopping through corporate restructuring so as to achieve the right regulatory mix to recover costs and avoid review of those costs in some cases.¹¹ Taken together, these effects of the Court's extension of the filed rate doctrine challenge the ability of state regulators to hold local retail utilities accountable for their management decisions.

In response to these concerns, lower courts have attempted to limit the effect of the filed rate doctrine by excepting some transactions from its coverage. First, the courts have recognized that purchasing utilities must make a reasonable choice among alternative wholesale sources of power.¹² Second, they have recognized that state commissions may offset FERC-ordered costs by reductions in areas not subject to FERC jurisdiction.¹³ Thus, a FERC order causing an increase in one component of a retail utility's costs may not necessarily result in a dollar for dollar increase in the retail rate. In each case, the courts have found that there is no interference in the federal regulatory scheme caused by the state action and, as a result, an imprudent management decision may lead to a cost disallowance.

In a creative extension of that argument, the court in *New Orleans Public*

7. See *infra* notes 72-96 and accompanying text.

8. Leheldt, *supra* note 5, at 16-17, quoting Executive Order 12612 (Federalism).

9. Nixon & Johnston, *supra* note 5, at 13-15.

10. *Id.* at 15-16.

11. *Id.* at 30-31 & n.131. Vince and Moot note that variations of the filed rate doctrine and its preemptive effect arise in several other contexts including the federal requirements for setting small power producer and cogeneration rates, federal securities review, gasoline sales, and emergency planning. Vince & Moot, *Federal Preemption*, *supra* note 5, 45-62. In late 1991, the issue also emerged in the discussion of regional planning authorities to allow greater state involvement in the determination of resource mix and additions. Under the auspices of the Arkansas commission and the Entergy Corporation, a proposal emerged for the creation of regional planning boards to set policy for multistate holding companies. One of the stated reasons for the use of the multistate boards was to counteract the effects of the filed rate doctrine on state authority. *Arkansas, Entergy Air Regional Integrated Resource-Planning Scheme*, INSIDE FERC, Sept. 16, 1991, at 9.

12. See *infra* notes 54-63 and 125-131 and accompanying text.

13. See *infra* notes 64-71 and 117-124 and accompanying text.

Service, Inc. v. Council of New Orleans (NOPSI),¹⁴ found that a state imposed duty to mitigate the costs it incurred under a FERC-mandated allocation is not preempted by the filed rate doctrine. In theory, the utility may be required to attempt to sell its FERC allocation or absorb the costs.¹⁵ Although the court's theory does not fall within either of the two exceptions, the Supreme Court has recognized in prior dicta that it is consistent with the policy and statutory framework of the FPA and does not clearly interfere with federal regulation of wholesale electricity.

To explore this conclusion more fully, this article is divided into five parts. Following a summary of the *NOPSI* case in Part I, the article addresses the statutory and interpretive foundations of the filed rate doctrine in Part II. Part III discusses the Supreme Court's extension of the doctrine into greater federal management of retail rates and introduces the reaction of the lower courts to the Supreme Court's decisions. Part IV analyzes the *NOPSI* exception requiring a utility to mitigate the effects of a FERC order in light of the policy distinctions inherent in the filed rate doctrine and the recognized exceptions. Part V addresses a related policy issue of the appropriate venue for challenging state orders to deny costs arising from federal orders.¹⁶

I. THE NOPSI DECISION

Entergy Corporation's (formerly Middle South Utilities or MSU) construction of the Grand Gulf I plant has spawned three successful Supreme Court appeals.¹⁷ The disputes arose from the allocation of the completed and expensive Grand Gulf I nuclear power plant. While cost estimates in 1974 placed the cost for the construction of a two reactor facility at \$1.2 billion, the completed cost of a one reactor facility exceeded \$3 billion.¹⁸ To allocate the costs of the plant, the retail electric companies entered into agreements with Middle South Energy, the owner of the plant and a sister within the holding company structure, that were approved with major modifications by the FERC. *NOPSI*'s share of the plant costs based on the FERC-modified agreements amounted to 17% and was based on its share of nuclear generation costs within the holding company (as opposed to the 9% the Council argued for and the 29.8% urged in the original agreement).¹⁹ *NOPSI* then sought to recover the cost of its share by filing for a sixty percent increase in rates with

14. 911 F.2d 993 (5th Cir. 1990), *cert. granted*, 59 U.S.L.W. 3718, *appeal dismissed*, 60 U.S.L.W. 3376 (U.S. 1991) (*NOPSI*).

15. Vince & Moot, *Federal Preemption*, *supra* note 5, at 36.

16. This article does not attempt to critique either the FERC decisions or the Supreme Court's application and interpretation of the filed rate doctrine. Others have already addressed those issues and are likely to return to them. *See supra* note 5.

17. In addition to the current appeal, the Court considered matters related to preemption and abstention in *Mississippi Power & Light v. Mississippi ex rel. Moore*, 487 U.S. 354 (1988) and *New Orleans Pub. Serv. Inc. v. Council of New Orleans*, 109 S. Ct. 2506 (1989) (*NOPSI III*). In the most recent case, see *supra* note 14, the Court granted certiorari, but the parties voluntarily dismissed the case as part of a global settlement. Nagelhout, *Regional Planning and the Regulatory Gap*, *Pub. Util. Fortnightly* 62, 64-65 (Dec. 1, 1991).

18. *NOPSI*, 911 F.2d at 996.

19. *Id.* at 996 and n.3.

the Council of New Orleans.²⁰

The Council denied the rate request and began an investigation of the prudence of the utility's actions.²¹ After a substantial and generally unsuccessful attempt by NOPSI in the federal courts to prevent the Council's investigation, the Council issued a final order denying some of the requested increase. As a result of the order, NOPSI was allowed to charge retail customers for only fourteen percent of the Grand Gulf costs, rather than the seventeen percent allocated to it under the FERC-approved agreement.²² NOPSI then filed an action seeking federal court assistance to prevent the implementation of the Council's order and a parallel action in state court.²³ The district court abstained from deciding whether the filed rate doctrine prevented the Council's action, but the Supreme Court reversed that decision.²⁴ On remand, the district court held that the order was not facially preempted and stayed the remainder of the case in favor of state court resolution.²⁵ The Fifth Circuit affirmed.

The court of appeals began its analysis by detailing the expanded scope of the filed rate doctrine and its preemptive effect. The court reached its conclusion after a review of the Supreme Court's recent filed rate doctrine cases, summarizing their factual scope to prevent the Council from (1) relitigating the decision to participate in the project initially, (2) challenging the FERC allocation, or (3) penalizing NOPSI for buying too much Grand Gulf power.²⁶ If the effect of the order either directly or indirectly resulted in a redetermination of NOPSI's FERC-mandated share of Grand Gulf I, then the order was preempted.²⁷ Despite the apparent breadth of the filed rate doctrine when applied to a holding company, the court nonetheless concluded that the Council's order was outside the doctrine.

In reaching this conclusion, the court addressed the scope of the Council's review in the rate case. The court accepted the characterization that the Council was reviewing the decision of NOPSI to retain its full interest in the power from Grand Gulf after the risk of nuclear power became apparent.²⁸ The only remaining question was whether FERC jurisdiction extended to the retail seller's decision to diversify its power sources under the circumstances.

The court concluded that FERC jurisdiction did not extend to the decision to attempt diversification of power sources by the retail company. The court initially noted that the FERC did not assert jurisdiction to determine the "prudence [of NOPSI] in not acting to minimize losses" from the power shar-

20. *Id.* at 996-97.

21. *Id.* at 997.

22. *Id.*

23. *Id.*

24. *NOPSI III*, 109 S. Ct. 2506 (1989).

25. *NOPSI*, 911 F.2d at 998.

26. *Id.* at 999-1001.

27. *Id.* at 999.

28. *Id.* at 1001, citing *NOPSI III*, 109 S. Ct. at 2517. Without this characterization of the case, the Council's argument seems to degenerate into an attack on the FERC decision allocating the capacity. Under the court's description of the filed rate doctrine, that attack could not be sustained.

ing agreement.²⁹ Further, the court found that Congress had not committed the matter to the FERC's exclusive jurisdiction. There was no explicit evidence of congressional intent, and the extension of authority effectively would divest states of retail rate making authority over companies that participated in power sharing pools.³⁰ Finally, the court analogized to the exception to the filed rate doctrine recognized (but never applied) by the Supreme Court which allowed states to reduce rates if other costs of service decreased.³¹ The court concluded, "If states may deny pass through because costs have gone down in other areas, it seems logical that they should be able to deny them because costs would have gone down if the utility had not been imprudent."³²

The *NOPSI* decision thus presents a novel approach to avoiding the effects of the filed rate doctrine. The exception fundamentally rests on the notion that the purchasing utility is under an obligation to mitigate the effects of its prior decision even though it is bound by another agency to make that decision. In this sense, it presents an important new twist to the basic policy that the purchasing utility is responsible to its customers for the costs incurred in providing service.

II. THE ANALYTICAL PARADIGM FOR FILED RATE ISSUES

The starting point for an examination of the filed rate doctrine is the applicable statutory provisions. The statutory language and history provide ample evidence for strong local control. First, the statute provides a statement that local concerns remained local after the adoption of the FPA amendments in 1935. Second, a straightforward reading of the legislative history of the FPA suggests a strong element of local control.

A. *The Legislative Demarcation*

The FPA contains a seemingly redundant jurisdictional statement that indicates a strong congressional desire to leave retail regulation to the states. Section 201(a) of the act provides that "Federal regulation . . . extend[s] only to those matters which are not subject to regulation by the States."³³ Section 201(b)(1) then states much the same thing:

The provisions of this Part shall apply to the transmission of electric energy at wholesale in interstate commerce, but shall not apply to any other sale of electrical energy or deprive a state or state commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a state line.³⁴

Thus, the operative language of the statute separates state and federal jurisdiction, leaving to the states the obligation to set local or retail rates.

The legislative history of the FPA reinforces the congressional goal to

29. *Id.* at 1002.

30. *Id.*

31. *Id.* See *infra* text accompanying notes 54-63 and 125-131.

32. *Id.* at 1002.

33. Codified as 16 U.S.C. § 824(b)(1) (1988). Further references to the Federal Power Act are to Title 16, United States Code. Text references are to the section of the Federal Power Act.

34. *Id.* § 824(b)(2).

retain local control of local rates. The Senate report, for example, stated that the purpose of the Act was to regulate the increasingly large and important interstate market that the states could not regulate due to constitutional limitations on their powers.³⁵ The regulatory void was created by the Supreme Court's decision in *Public Utilities Commission v. Attleboro Steam & Electric Co.*,³⁶ which held that the states had no jurisdiction to regulate wholesale transactions in interstate commerce. To fill that void, Congress inserted federal regulation under the FPA but also decided not to interfere with existing state authority. Senate revisions of a House proposal aggressively followed that course.³⁷ The House later agreed and reinforced this message.³⁸ The section by section analysis of the House committee report stated, "As in the Senate bill no jurisdiction is given over local distribution of electric energy, and the authority of States to fix local rates is not disturbed even in those cases where the energy is brought in from another State."³⁹ Local regulation of retail rates thus appeared sacrosanct under the FPA.

Congress, however, did provide the Commission with a plenary powers to regulate interstate commerce in wholesale power. In section 202 of the FPA, the Commission is authorized to coordinate interstate sales and transmission.⁴⁰ In other sections, the Commission is directed to set rates and standards.⁴¹ While the potential then existed for conflict, the congressional solution seemingly left retail rate making to the states even when the electric power being purchased was in interstate commerce.

B. Creating a Jurisdictional "Bright Line"

The Supreme Court's initial decisions interpreting the jurisdiction of states and the federal commission over energy matters assumed a demarcation based on the physical nature of the activity. In a series of decisions, the Court

35. S. REP. NO. 621, 74th Cong., 1st Sess. 17 (1935).

36. 273 U.S. 83 (1927).

37. S. REP. NO. 621, *supra* note 35, at 18, states:

The revision has also removed every encroachment upon the authority of the States. The revised bill would impose Federal regulation only over those matters which cannot be effectively controlled by the States. The limitation on the Federal Power Commission's jurisdiction in this regard has been inserted in each section in an effort to prevent the expansion of Federal authority over State matters.

The sectional analysis of the report further states, "The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held [in *Attleboro*] to be beyond the reach of the States." *Id.* at 48.

38. H.R. REP. NO. 1318, 74th Cong., 1st Sess. 7-8 (1935) states:

[T]he Commission is given no jurisdiction over local rates even where the electric energy moves in interstate commerce. . . . The bill takes no authority from State commissions The new parts are so drawn as to be a complement to and in no sense a usurpation of State regulatory authority and contain throughout directions the Federal Power Commission to receive and consider the views of State commissions. Probably, no bill in recent years has so recognized the responsibilities of the State regulatory commission as does Title II of the bill.

39. *Id.* at 27. The Senate report similarly states, "This subsection leaves to the States the authority to fix local rates even in cases where the energy is brought in from another State." S. Rep. No. 621, *supra* note 35, at 48.

40. 16 U.S.C. § 824a (1988).

41. *Id.* § 824(d)-(e).

adopted a mechanistic “bright line” test based on a wholesale-retail division to separate state and federal authority.⁴²

Typical of the Court’s approach is the decision in *FPC v. Southern California Edison Co.*⁴³ In this case, the City of Colton purchased power from Southern California Edison for resale to Colton’s municipal residents. Thus, the purchases were wholesale. Moreover, some of the energy which the utility received was in interstate commerce since the utility connected to an interstate electrical grid. Rejecting the argument that the sale was essentially an intrastate one from a California utility to a California city, the Supreme Court found that the transaction was subject to the authority of the FERC. In an often cited portion of the decision, the Court stated:

[O]ur decisions have squarely rejected the view . . . that the scope of FPC jurisdiction over interstate sales of gas or electricity at wholesale is to be determined by a case-by-case analysis of the impact of state regulation upon the national interest. Rather, Congress meant to draw a bright line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis. This was done in the Power Act by making FPC jurisdiction plenary and extending it to all wholesale sales in interstate commerce except those which Congress has made explicitly subject to regulation by the States.⁴⁴

While one might complain about where the line was drawn, the test avoided the case by case balancing of much of the supremacy and commerce clause litigation of recent years.⁴⁵ The determination of jurisdiction turned on the nature of the transaction, not its effect (or lack of effect) on interstate commerce. Analysis did not look to trapping costs, choice, or the apparent fairness of state review. These “tests” would appear in the more recent vintage cases.

C. *The Parentage of the Filed Rate Doctrine*

The initial cases interpreting the jurisdictional provisions were just that—jurisdictional questions. The filed rate doctrine extension found its roots in another source as well. Rather than from the logical source of Supremacy Clause litigation,⁴⁶ certainly the source of the current doctrine, the doctrine arose in a decision dealing with primary jurisdiction. The case, *Montana-*

42. For a thorough discussion of the Supreme Court decisions, see Lindh, *supra* note 5.

43. 376 U.S. 205 (1964).

44. *Id.* at 215-16.

45. The courts address a less significant doctrinal task if Congress has provided a specific provision defining the relative spheres of authority. LAURENCE TRIBE, *AMERICAN CONSTITUTIONAL LAW* 479 (2d ed. 1988). As noted previously, the legislative history of the Federal Power Act attempted to fill the gap created by *Attleboro*, a decision that limited state power to regulate based on a mechanistic reading of the commerce clause. The legislation does not theoretically avoid issues involved with the commerce clause. At the margins, state regulation which is not preempted could violate the balancing test because the balance of state and federal interests do not favor state regulation. *Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm’n*, 461 U.S. 375, 389-95 (1983); LAURENCE TRIBE, *supra* at 408.

46. U.S. CONST. art VI, § 2, in part, provides, “This Constitution, and the Laws of the United States which shall be made in Pursuance thereof . . . shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.”

Dakota Utilities Co. v. Northwestern Public Utilities Service Co.,⁴⁷ involved a claim between two utilities for the sale of electricity from one to the other under a rate filing approved by the FPC. At the time of challenging the transactions, the two companies had interlocking directorates. After the utilities were separated, the plaintiff utility complained in a fraud action in federal court that it paid too much under the approved rate because the directors took advantage of the interlock to transfer costs.⁴⁸

The Supreme Court concluded that the district court had no basis for trying the case since the rates charged by the utilities for the power had been filed with the Commission. The Court reasoned that Congress had placed the decision concerning the appropriate rate in the hands of the Commission exclusively.⁴⁹ The basis for the claim rested on the statutory requirement that rates be reasonable. Statutory reasonableness, however, encompassed a range of values, and Congress assigned the function of determining the place within that range to the Commission.⁵⁰ From this assumption the Court concluded, "[Petitioner] can claim no rate as a legal right that is other than the filed rate, whether fixed or merely accepted by the Commission, and not even a court can authorize commerce in the commodity on other terms."⁵¹

The more interesting but seldom noticed portion of the decision is the Court's discussion of the preemption of a state-law based fraud claim. The petitioner argued that fraud caused by the interlocking directorate provided an avenue for relief from the filed rate doctrine. The Court, while recognizing the state fraud claim, nonetheless found that the Commission's approval of the prior interlocking directorate, as being in the private and public interest, precluded an assertion that the directorate's decisions were presumptively fraudulent.⁵² The effects of a federal decision on a state law thus began to emerge.

Despite this source of the filed rate doctrine as a source of preemption, the decision to deny recovery then did not involve a conflict between a state and federal jurisdiction. At issue was the right of a federal court to retroactively recalculate the reasonable rate. The Court concluded that the district courts were without authority to make that sort of decision. The obvious problem with the result, however, is that it left the petitioning utility without a remedy for the prior overcharges since the FPC lacked the authority to authorize repayment.⁵³ A similar problem would emerge in the modern filed rate cases when the FERC, without review, approved costs as prudent and that decision precluded the states from conducting their own investigations.

The extension of the doctrine as a matter of federal supremacy came from the application of the *Montana-Dakota* decision to a state rate making proceeding in several state court decisions culminating in *Narragansett Electric*

47. 341 U.S. 246 (1951).

48. *Id.* at 247-48.

49. *Id.* at 251.

50. *Id.*

51. *Id.*

52. *Id.* at 252-53.

53. *Id.* at 255-66 (Frankfurter, J., dissenting).

Co. v. Burke.⁵⁴ In this case, Narragansett purchased electric power from New England Power Company. Both were subsidiaries of New England Electric System.⁵⁵ Following a wholesale rate increase by New England Power approved by the FPC, Narragansett filed for an increase in its retail rates to reflect the increased cost of power with the Rhode Island commission. The Rhode Island commission asserted jurisdiction to investigate the reasonableness of the costs in the New England wholesale rate filing.⁵⁶ The state commission reviewed the cost of equity, capital structure, working capital requirements, and abandoned plant construction costs of New England Power. It also disallowed four million dollars of the Narragansett's requested nine million dollar annual increase based on the redetermination of the appropriate rate it deemed should be charged by New England Power.⁵⁷

The Rhode Island Supreme Court effectively merged the bright line jurisdictional test with the filed rate doctrine to reverse the commission's decision. The bright line between federal and state jurisdictions over energy matters provided state and federal authorities with exclusive authority within their own fields.⁵⁸ Although state authority extended to the determination of retail rates, the state nonetheless had to accept the determination of the wholesale rate as reasonable based on the Supreme Court's decision in *Montana-Dakota*.⁵⁹ As a result, the state commission erred when it investigated the New England wholesale rate structure because the reasonable rate was that which was filed or fixed by the FPC.⁶⁰

The Rhode Island Supreme Court left open one possibility for decreases associated with other costs incurred by the retail utility. Even though the wholesale cost of the electricity to Narragansett would increase due to the federal filing that the state must accept, the rates need not increase if other costs that the state investigated decreased.⁶¹ Thus, the state commission could "investigate the overall financial structure of Narragansett to determine whether the company [had] experienced savings in other areas which might offset the increased price for power."⁶² On that basis, the court remanded the case to the state commission "with the direction that . . . it must treat the FPC filed and bonded purchase price to [New England Power] as an actual operating expense."⁶³

Under *Narragansett*, the states could not attack the reasonableness of the

54. 381 A.2d 1358 (R.I. 1977), *cert. denied*, 435 U.S. 972 (1978). The Rhode Island Supreme Court was not the first court to address the issue. See *United Gas Corp. v. Mississippi Pub. Serv. Comm'n*, 240 Miss. 405, 127 So. 2d 404 (1961) and *Citizen Gas Users Ass'n v. Pub. Util. Comm'n of Ohio*, 165 Ohio St. 536, 138 N.E.2d 383 (1956). Nonetheless, its decision has come to be associated with the application of the filed rate doctrine to state utility proceedings.

55. *Narragansett*, 381 A.2d at 1359-60.

56. *Id.* at 1360-61.

57. *Id.* at 1361.

58. *Id.* at 1361.

59. *Id.* at 1362.

60. *Id.* at 1363.

61. *Id.* at 1363.

62. *Id.*

63. *Id.*

selling utility's rates, but the door remained open to attack the reasonableness of the purchasing utility's discretionary decision to buy at that price. In *Pike County Light & Power Co. v. Pennsylvania Public Utilities Commission*,⁶⁴ a state court concluded that a utility that had a choice for its purchases could be responsible when it made an unreasonable choice. Pike County, a subsidiary of Orange and Rockland Utilities, purchased power from its parent at a FERC-approved wholesale rate that was substantially above the cost of power offered to it by Pennsylvania Power.⁶⁵ When the state commission (PUC) disallowed over one half million dollars as imprudent costs incurred in the purchase, Pike County challenged the order on the basis that the state was preempted from challenging the reasonableness of the rate.⁶⁶ In the appeal, the court drew a distinction between the reasonableness of the selling price from the seller's and buyer's perspectives. As to the former, the court agreed that the FERC's decision preempted any state review.⁶⁷ As to the latter, however, the court found that there was no interference with federal authority. First, the review performed by the FERC did not concern Pike County.⁶⁸ Likewise, the FERC did not review the reasonableness of the purchase from the point of view of the purchaser.⁶⁹ In contrast, the state review was limited to the reasonableness of the purchasing transaction in light of its available alternatives.⁷⁰ Thus, the court concluded, "The regulatory functions of the FERC and the PUC . . . do not overlap, and there is nothing in the federal legislation which preempts the PUC's authority to determine the reasonableness of a utility company's claimed expenses."⁷¹

Importantly, state authority to review management choices did not disappear with the extension of the filed rate doctrine into a theory of preemption. Both in *Narragansett* and *Pike County*, the courts concluded that a local utility, as a purchaser, had to make reasonable choices. The limitation in *Pike County*, however, was the court's decision not to extend the preemptive effect of a FERC order to the purchaser's decision to buy at that rate. In effect, it could be unreasonable to purchase at a price that the seller could charge as a just and reasonable rate. But the scope of *Pike County* and the potential for other exceptions, such as that found in *NOPSI*, faced a sterner challenge in subsequent Supreme Court decisions.

III. EXPANDING THE PREEMPTIVE AUTHORITY OF FERC

In two decisions, the Supreme Court has extended the notion that federally filed rates preempt local rate making decisions that pushes federal jurisdiction much farther into the traditional realm of state rate making authority. On the theory that the failure to recognize federally ordered rates will result in

64. 465 A.2d 735 (Pa. 1983).

65. *Id.* at 736.

66. *Id.* at 737.

67. *Id.* at 737.

68. *Id.* at 738.

69. *Id.*

70. *Id.*

71. *Id.*

trapped costs, the Court has concluded that state regulatory commissions must honor FERC orders which largely determine local rates. Moreover, the scope of FERC authority extends not only to the actual rates on file but also to arrangements approved by the FERC which determine cost allocations such as the requirement to take a certain amount of power. While there may be an exception that allows for state regulation of those decisions that a retail utility makes if it has a choice of sources, rates and allocations within power pools otherwise set by the FERC are binding.

A. *Nantahala*

The first major decision by the Court applying the trapping theme to pre-empt state action was *Nantahala Power & Light Co. v. Thornburg*.⁷² In this case, two subsidiaries of Alcoa received low cost entitlement and high cost purchase power under an arrangement with the Tennessee Valley Authority. One of the subsidiaries, Tapaco, sold all of its allocations to Alcoa. The other, Nantahala, resold its power to retail customers and was regulated by the North Carolina commission. After the FERC set the allocation of low cost power at levels that the North Carolina commission opposed, the commission, in a subsequent rate case for Nantahala, determined that rates would be set at levels that reflected a greater allocation of low cost power. As a result of the reallocation, Nantahala would not recover in retail rates the costs it incurred for the additional high cost power it actually had to purchase under the FERC-ordered allocation.⁷³ The Supreme Court reversed.

The Court began its analysis with the necessary assumption that federal law controls conflicting state law.⁷⁴ The Court next asserted that the FERC had plenary authority over the provision of rates, again an unexceptional statement.⁷⁵ The Court then made a significant extension. The authority over rates extended to mandatory allocations of power since these determined the costs incurred by the utility.⁷⁶ Thus, the state's decision that Nantahala should have been allocated more of the low cost power ran directly counter to the FERC order.⁷⁷ As a result, Nantahala faced trapped costs under the state order. The commission's increase of the amount of low cost power available to Nantahala resulted in its failure to recover the full cost of the high power it was required to buy under the FERC allocation.⁷⁸ The state order thus could not stand as it operated in conflict with the federal order.

The Court nonetheless recognized that Nantahala's rates need not increase as a result of its decision. First, the Court noted that a reduction in costs not subject to FERC pricing might justify the state's failure to pass on

72. 476 U.S. 953 (1986).

73. *Id.* at 955-62.

74. *Id.* at 964.

75. *Id.* at 966.

76. The Court stated, "FERC's decision affects Nantahala's wholesale rates by determining the amount of low-cost power that it may obtain, and FERC required Nantahala's wholesale rate to be filed in accordance with that allocation." *Id.* at 967.

77. *Id.* at 968.

78. *Id.* at 970.

the increased FERC-ordered costs dollar for dollar in new rates (the *Narragansett* exception).⁷⁹ Second, the Court made a passing reference to the *Pike County* exception but concluded that it did not apply since no other power source appeared to be available to Nantahala.⁸⁰ The Court, however, described the potential exception in an unusual way. Instead of leaving open the issue that the purchase price for particular source might be too high, the Court stated:

Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore, reasonable, price."⁸¹

B. *Mississippi Power & Light*

In *Mississippi Power & Light Co. v. Mississippi ex. rel Moore*,⁸² the Court next determined that a state commission could not conduct a review of the reasonableness of costs incurred in the construction of a nuclear power plant whose costs were allocated under a federally approved power pooling agreement. Growing out of the Grand Gulf I nuclear power plant construction, the case stems from the same facts as the *NOPSI* litigation. As noted previously, the consortium constructing Grand Gulf I completed the construction at a cost six times the initial estimates.⁸³ MSU, the owner of the plant, filed a set of agreements with the FERC to allocate the costs of the plant by capacity purchases by the members of the Middle States pool.⁸⁴ The FERC revised the agreements and then approved an arrangement that required each of the members to incur some of the construction costs.⁸⁵ The FERC did not conduct a review of the reasonableness of the costs MSU incurred in the construction, although the Court concluded that the FERC implicitly accepted the companies' assertions that costs were prudent.⁸⁶ Following the approval of the new pool allocations, Mississippi Power and Light Co. filed for a substantial rate increase to which the Mississippi commission finally agreed in order to avoid forcing the company into insolvency.⁸⁷ On an appeal of the commission's decision, the state supreme court concluded that the increased costs could not be passed to consumers until the reasonableness of the costs was determined,

79. *Id.* at 967.

80. *Id.* at 973-74.

81. *Id.* at 972. Theoretically, the comparison is still over which is the less expensive alternative, but the phrasing is indeed odd since either price or quantity could be unreasonable in a particular transaction. For example, a company might contract for expensive backup power from gas turbines because it needs that power at a moment's notice. But, it probably would be unreasonable to supply base load power through purchases from those same turbines. In each case the quantity and price might be the same, but the justification for the purchase would differ dramatically.

82. 487 U.S. 354 (1988).

83. *Id.* at 359.

84. *Id.* at 360.

85. *Id.* at 361-62.

86. *Id.* at 363.

87. *Id.* at 365.

and it ordered the state commission to conduct a review.⁸⁸ Holding that the review was preempted, the Supreme Court once again reversed.

Because the case presented an apparently significant intrusion into state regulatory authority, the Court initially attempted to set out the parameters of federal authority. First, the FERC had exclusive authority to set wholesale rates.⁸⁹ Second, its authority extended to allocation decisions.⁹⁰ Third, states may not interfere with that authority by barring utilities from passing through to retail consumers the price effects of the assertion of FERC authority.⁹¹ The Court recognized once again that an exception may exist to allow state commissions to review the reasonableness of purchase decisions, the *Pike County* exception, but then closed the door to state review by concluding that exception did not apply when the FERC had prescribed the amount of power to be purchased by a particular utility within a power pool.⁹²

The conclusion that the state action was preempted easily followed. The state court erred when it found that FERC jurisdiction did not apply since the FERC had not conducted a review of the reasonableness of the costs.⁹³ According to the Court, FERC's decision could not be attacked by a state commission outside the FERC proceeding or an appeal from it if the decision was within FERC jurisdiction, whether or not the federal agency actually used its authority.⁹⁴ The Court then buttressed its position, stating that the reasonableness of costs could have been raised in the FERC proceeding and some of the issues pertinent to the state proceeding had already been addressed in the federal one.⁹⁵ Thus, the Court cut off an argument that the failure of the FERC to exercise its jurisdiction (a familiar complaint among those who fear that utilities will engage in forum shopping⁹⁶) did not preserve any state authority.

C. *The Lower Courts' Reaction*

The lower court's reaction to the expansion of the filed rate doctrine into a jurisdictional bulwark is mixed. Some courts have gone to some lengths to implement the Court's suggestion that decisions affecting federally approved

88. *Id.* at 366. See *Mississippi ex rel. Pittman v. Mississippi Pub. Serv. Comm'n*, 506 So. 2d 978 (Miss. 1987). The reasons for not holding a hearing at the FERC are somewhat obscure. The Supreme Court majority opinion first states that the FERC found that the decision to continue construction was prudent. *Mississippi Power*, 487 U.S. at 363. The Court then states that the issue could have been brought to the attention of the FERC and the administrative law judges, but that the states failed to do so. *Id.* at 375. The majority then reverses field again and concludes that some of the prudence issues were decided. *Id.* at 376. See also *id.* at 379 and n.* (Scalia, J., concurring). On the other hand, Justice Brennan's opinion casts some doubt about the scope of the review that one of the administrative law judge's concluded was available at the FERC in this proceeding. *Id.* at 388-89 and n.* (Brennan, J. dissenting).

89. *Id.* at 371.

90. *Id.*

91. *Id.* at 372.

92. *Id.* at 373-74.

93. *Id.* at 374.

94. *Id.* at 374-75.

95. *Id.* at 375-76.

96. See *infra* text accompanying notes 136-140.

rates are preempted, but others have suggested less aggressive use of the filed rate doctrine.

1. Paradigm Cases of Preemption

It is readily apparent that the state will not be successful in asserting jurisdiction over FERC ordered cost allocations. Cases concerning the allocation of transmission line construction costs and minimum billing are examples. In another case, one state supreme court treated a cost as requiring pass through even though the FERC did not claim jurisdiction to decide the matter. In each of the following cases, however, the FERC decision seems to preclude state involvement under the Court's version of the filed rate doctrine.

For example, the Fourth Circuit Court of Appeals in *Appalachian Power Co. v. Public Service Commission of West Virginia*⁹⁷ had little difficulty affirming an injunction against the West Virginia commission to prevent it from reviewing the costs of construction for an interstate high voltage transmission line. In this case, Appalachian Power Company filed for a retail rate increase to cover the costs associated with the FERC-assigned portion of the line constructed by a pool with which it was associated.⁹⁸ The state commission refused to allow the costs until it conducted a review of the contract under a statute that required commission review of deals made with affiliates.⁹⁹ Though the commission asserted that it was limiting its review to whether the utility had selected the most economic source for transmission, the court found that the investigation was preempted.¹⁰⁰ Initially, the court noted that the FERC had exclusive jurisdiction over interstate transmission of power.¹⁰¹ It then rejected the commission's argument that it would limit its review to the *Pike County*-type issues. The court found that the exception did not apply since there was no alternative available to the utility and the inquiry into reasonableness would overlap with the federal determination of the reasonableness of the contract allocation and result in the potential for a conflict between federal and state regulation of Appalachian.¹⁰² The court concluded its justification by noting that in this instance a broader perspective was appropriate since the transmission was multistate in nature and affected a multistate pool. Thus, the FERC was the proper venue for a decision since it could provide a comprehensive review and coordinated approach to the problems raised by the pooling arrangement.¹⁰³

Similarly, in *Kentucky West Virginia Gas Co. v. Pennsylvania Public Utilities Commission*,¹⁰⁴ the Third Circuit Court of Appeals concluded that a state commission must recognize minimum bill charges (charges for the cost of gas ordered but not delivered) authorized by the FERC. The state had anticipated

97. 812 F.2d 898 (4th Cir. 1987).

98. *Id.* at 900-01.

99. *Id.* at 901.

100. *Id.*

101. *Id.* at 902.

102. *Id.* at 903-04.

103. *Id.* at 904-05.

104. 862 F.2d 69 (3d Cir. 1988).

a reduction in the rates authorized and lowered the recovery at the retail level accordingly.¹⁰⁵ The court rejected the state's position and concluded that FERC-authorized rates were binding on the state commission until the FERC changed them.¹⁰⁶

The Illinois Supreme Court's decision to preempt state review in *General Motors Corp. v. Illinois Commerce Commission*¹⁰⁷ poses an even more interesting problem in that the FERC attempted to leave for the states the determination of the reasonableness of cost pass throughs by retail utilities. In Order No. 500,¹⁰⁸ the FERC directed pipelines to recover, in one of two methods, take or pay liability resulting from reduced purchases of natural gas by local distribution companies. The first allowed the companies to recover the full amount of the charges but subjected the companies to full rate review. The second allowed the companies to recover half the take or pay payments from customers if they agreed to absorb the other half. Pipelines serving Illinois took the second option, thus creating a potential fixed obligation for the recovery of costs from the local distribution companies to which they sold the gas.¹⁰⁹ Importantly, however, the FERC left open the question of whether utilities purchasing from the pipelines would have to absorb some of the costs for the take or pay liability.¹¹⁰

Despite the invitation by the FERC for the states to retain jurisdiction, the Illinois commission concluded that retail companies had to recover the full FERC-approved amount from retail customers under the filed rate doctrine,¹¹¹ and the state supreme court agreed. After the court concluded the filed rate doctrine applied to the costs of gas assigned to local utilities by the FERC order,¹¹² it then addressed the question of the FERC's attempt to refer the determination of whether the costs were reasonable to states. The court noted that the FERC could not authorize a result different than that provided by Congress in the Natural Gas Act.¹¹³ It then stated that the effect of the state order was to trap costs, an action not permitted under the statute according to Supreme Court interpretations.¹¹⁴ Nor did the *Pike County* exception apply since the FERC directed pipelines to charge the take or pay costs to retail utilities.¹¹⁵ Since the costs were mandatory, the local utilities had no choice but to incur the costs for the gas they had not purchased. Finally, the court offered its opinion that it could not see any basis for concluding that the costs the local companies were forced to incur could be imprudent since they could not have anticipated the changed economic and regulatory circum-

105. *Id.* at 72.

106. *Id.* at 74.

107. 574 N.E.2d 650 (Ill. 1991).

108. Order No. 500, *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, [1986-1990 Regs. Preambles] F.E.R.C. Stats. & Regs. ¶ 30, 761, 52 Fed. Reg. 30, 334 (1987).

109. 574 N.E.2d at 653-54.

110. *Id.* at 656, citing Order No. 500, 52 Fed. Reg. 30,334 (1987).

111. *Id.* at 654.

112. *Id.* at 655-56.

113. *Id.* at 657.

114. *Id.*

115. *Id.* at 658.

stances that led to the take or pay problems addressed in Order 500.¹¹⁶

These cases consistently follow the logic of the Supreme Court in the preemption cases. Costs mandated by the FERC cannot be tampered with even when the FERC does not claim that it has addressed the buyer's reasonableness in making the purchases.

2. Exceptions

The breadth of the Court's decisions, however, was tempered by the dicta in *Nantahala* concerning the purchaser's role. Though *Mississippi Power & Light* cast further doubt on the viability of the exceptions, lower courts nonetheless have found a place for it.

In the first *Kentucky West Virginia Gas Co.* case,¹¹⁷ for example, the Third Circuit found that the state's prudence review was not preempted when the utility could receive gas from multiple sources. Though the court anticipated its treatment of unavoidable costs, such as a minimum bill included in the purchase price,¹¹⁸ it nonetheless concluded, "FERC's interpretation of its statutory authority recognized that wholesale rate-making does not as a general matter determine whether a purchaser has prudently chosen from available supply alternatives."¹¹⁹ The court further noted that the reasonableness of the purchase was never before the FERC. As a result, there could not be any conflict with FERC jurisdiction over that matter.¹²⁰

Likewise, in *Pennsylvania Power Co. v. Pennsylvania Public Utilities Commission*,¹²¹ a state court concluded that an arrangement to buy back power at ten times the cost of other sources could be reviewed by the commission since there was an alternative source of power available to the purchaser. In this case, Penn Power attempted to pass through the very expensive power it purchased as part of a sale of an unneeded portion of a power plant it had agreed to construct.¹²² Though the contract for the buy back was filed and approved by the FERC as an interstate wholesale purchase, the court agreed that the unsupervised and essentially voluntary decision to purchase the power in trade for unloading part of its ownership in the plant was subject to state review.¹²³ The court distinguished the case from *Mississippi Power & Light* on the basis that the company, not the FERC, caused it to incur the very high price for the purchased power.¹²⁴

The state also retains the authority to review rates for other cost reductions, and this exception logically precludes immediate dollar for dollar pass through to rate payers once the FERC has acted. In *Arkansas Power & Light*

116. *Id.* at 659.

117. *Kentucky W. Va. Gas Co. v. Pennsylvania Pub. Util. Comm'n*, 837 F.2d 600 (3d Cir. 1988), *cert. denied*, 488 U.S. 941 (1988).

118. *Id.* at 610.

119. *Id.* at 609.

120. *Id.*

121. 561 A.2d 43 (Pa. Commw. Ct. 1989), *aff'd*, 587 A.2d 312 (Pa. 1991), *cert. denied*, 112 S. Ct. 80 (1991).

122. *Id.* at 45.

123. *Id.* at 49.

124. *Id.* at 51-52.

Co. v. Missouri Public Utilities Commission,¹²⁵ another of the Grand Gulf I cases, the FERC ordered the utility to begin payments of \$33 million for its share of Grand Gulf I, \$1 million of which was attributable to Missouri customers.¹²⁶ The utility filed a rate case with the Missouri commission to recover the increased FERC-imposed costs, but the state ordered a suspension of the proposed rates for the ten months allowed under state law.¹²⁷ The utility then filed suit to enjoin the suspension of rates.¹²⁸ The district court ordered immediate recovery and the commission appealed. While the appeal was pending, the utility collected rates at levels that the commission ultimately determined were too high.¹²⁹

Relying on the Supreme Court's dicta in *Nantahala* that the states are not precluded from reviewing costs that are not dictated by the FERC in determining the appropriate retail rate, the court of appeals concluded that the state could properly suspend rates to determine the validity of other cost claims, the allocation of the costs to jurisdictional and nonjurisdictional customers, and rate design.¹³⁰ Nonetheless the court stated that the suspension could not be used in bad faith or when it might force the company into insolvency.¹³¹ In this case, however, the court felt that the injunction was improper since the state was authorized to review the utility's costs and there was no showing of bad faith. As a result, the court of appeals reversed the district court's order enjoining the use of the suspension statute by the state commission.

D. Summary

As a result of the Court's decision in *Nantahala* and *Mississippi Power & Light*, there exists a significant potential for federalization of the rate making process. As the electrical system has become more interconnected, the possibility for pools to shift the decision making process from state commissions to a federal agency is readily apparent. In effect, the Court has provided that federal jurisdiction reaches far down into the cost structure and allocation process for setting local rates. Those may now be dictated by the FERC and cannot be rejected by state commissions in setting local rates even when the FERC has not exercised its authority to review the prudence of costs. The only exception recognized by the Court is for purchases by a utility outside pooling arrangements. Otherwise, the state must find savings in other areas of utility operations to offset proposed increased rates. As one might expect, this construction of the filed rate doctrine has not set well with the states.

125. 829 F.2d 1444 (8th Cir. 1987).

126. *Id.* at 1446-47.

127. *Id.* at 1447.

128. *Id.*

129. The Missouri commission determined that the rate increase should be reduced to \$6 million from the \$17 million that the company requested. *Id.* at 1448.

130. *Id.* at 1452.

131. *Id.*

IV. NOPSI, SUBSEQUENT DECISIONS, AND POLICY IMPLICATIONS

The appellate court's decision in *NOPSI* presents an alternative for denying costs premised on a duty to mitigate the costs of federally approved purchases. By definition, this "new" theory does not fall into any of the prior exceptions to the filed rate doctrine, but it draws from both of the *Narragansett* and *Pike County* cases. The effect of imposing a duty to mitigate the federally required purchases could have the same effect as denying the costs initially. (In fact, one of the arguments raised by the petition for certiorari was that the state was attempting to circumvent the logical implications of the FERC order. As proof, the petition noted the striking coincidence that the state-ordered disallowance resulted in the same rate levels as the position the state took in the FERC proceeding.)¹³² If the controlling interest the Supreme Court uses is the trapping of costs, then the argument does not appear supported by the current interpretation of the filed rate doctrine when applied to members of interstate power pools. On the other hand, the same kinds of arguments that support other exceptions seem to apply to the duty to mitigate.

A. *The Duty to Mitigate Costs*

Boiled to its essentials, the theory underlying the decision in *NOPSI* is that the utility had a continuing duty to mitigate the costs of its purchases of power. Having joined the pool, the utility was required by the FERC order to accept its allocation of wholesale power and pay for the allocation assigned to it. Following the purchase, however, the utility also was required to make some effort to mitigate the costs of the allocation by selling the power. Failure to do so resulted in a disallowance for what in effect was imprudently retained costs.¹³³

The current theory of preemption and the filed rate doctrine does not appear to permit the commission (or, in this case, the municipality) to make this sort of decision. The allocation to *NOPSI* was a FERC order that directed the pool member to incur certain costs. The order carries a stamp of reasonableness the state may not challenge. Furthermore, the effect of the order is to trap costs by not permitting the utility to recover the full amount of FERC ordered costs of Grand Gulf from the retail customer, as opposed to the equity holder.

Likewise, neither of the recognized exceptions to the filed rate doctrine apply. The *Pike County* exception is not applicable since the utility had no choice in making the purchase. (Moreover, this transaction and the inapplicability of *Pike County* were previously decided in *Mississippi Power & Light*).¹³⁴ Nor is the exception for other costs applicable. In this case, the disallowance is directly related to the FERC allocation for Grand Gulf. The New Orleans Council decided that the utility should sell a portion of its interest in the plant. Thus it is impossible to argue that other costs justified the disallowance

132. Petition for Writ of Certiorari at 7, *New Orleans Pub. Serv., Inc. v. Council of New Orleans*, Case No. 90-1156 (Jan. 1991).

133. See *supra* notes 17-32 and accompanying text.

134. See *supra* notes 82-96 and accompanying text.

directly by the Council. In short, neither argument offers a sanction for the challenged order.

B. Recognizing a Duty to Mitigate

None of the preceding discussion, however, should rule out the possibility of another exception to the Court's current theory of the filed rate doctrine. First, a duty to mitigate appears to be consistent with the policy concern implicit in the *Pike County* and *Narragansett* exceptions. Both of the exceptions are premised on the view that the purchaser retains some responsibility to retail consumers for the costs that it incurs. In the case of *Pike County*, the purchaser must choose among alternative wholesale sources and is responsible for its poor choices. In the case of *Narragansett*, the purchaser may not pass through the costs dollar for dollar (i.e. its other cost decisions remain subject to review). Thus both exceptions prefer holding the local utility responsible to local authorities for its ongoing retail operations when FERC authority is not affected.

In the same way, the duty to mitigate does not necessarily implicate FERC authority. Rather, the local authority is challenging the company to improve its profile of expenses. If the utility can show that it was prudent in retaining an interest in more expensive power or was unable through reasonable efforts to transfer its allocation, then the decision not to sell the power is justified. On the other hand, the cost is not justified if the utility could have mitigated the cost by disposing of the power and failed to do so or to attempt to do so. It remains the choice of the utility management whether to retain or attempt to sell the expensive power to another user. In either case, the decision does not infringe on the FERC decision making process or resolution.

Second, the recognition of a duty to mitigate is consistent with the plain language of the statute and its legislative history. Both houses of Congress reported that the function of local rate making was not affected by the adoption of the Act.¹³⁵ The decision to continue to incur an expense that it could choose to mitigate does not directly or indirectly fall into the responsibilities of the FERC. Its decision making authority ended with the decision to make the allocation. If better mixes can be obtained by the local utility without disturbing the payments among the wholesale pool members, the FERC allocation is not disrupted, and the retail function is left with the states as Congress anticipated.

Third, other federalism concerns do not present unique challenges to finding a duty to mitigate. One argument supporting the filed rate doctrine is the perceived predictability of its results.¹³⁶ The bright line that drove prior decisions, however, hardly remains a steady beacon. The FERC, for example, takes principled but inconsistent positions about its own authority with regard to gas and electric pricing.¹³⁷ (Moreover, its decisions concerning its own

135. See *supra* notes 35-42 and accompanying text.

136. Lindh, *supra* note 5.

137. This conclusion is evidenced by the different treatment offered to the states under electric pooling arrangements such as that associated with Grand Gulf I cost allocations and the provisions of Order No. 500 concerning take or pay liability.

authority to disclaim an area of review are not controlling.)¹³⁸ Second, the Commission has not been consistent within industries over time.¹³⁹ Third, one should not expect a system that is responsive to political breezes will remain closely alloyed to a particular approach. Thus the perceived light hand of the FERC today¹⁴⁰ could be tomorrow's club. Predictability (and the related concern about forum shopping) thus is not a telling argument.

The line drawing within the current framework likewise does not demonstrate an overriding claim that makes it a determinative value for deciding to adopt an additional exception. The current treatment of filed rates turns on whether one is a member of a pool or ordered to pay certain costs. The division between affiliated and unaffiliated or ordered and chosen costs is hardly a principled way to determine if the federally mandated costs present the most efficient mix for retail distribution. Indeed, the irony of the current division is that the more closely related the parties to a transaction are, the less likely the purchase can be challenged.¹⁴¹ Rather, there is an apparent need to review those costs from the purchaser's side of the transaction, without regard to the purchaser's ties to the wholesaler.

Finally, a duty to mitigate does not present any special challenges to interstate coordination. If the FERC mandates a pooling arrangement, that arrangement is intact even if a duty to mitigate applies. A secondary decision, however, remains as to who, consumer or stockholder, is responsible for those costs. Inherently that decision is a local one. If management acts imprudently, the accepted solution is to assign those costs to shareholders.¹⁴² Nothing in the federal scheme is injured if the purchasing management is responsible for a failure to manage the utility's costs to maintain the lowest reasonable costs.¹⁴³ Moreover, management might as well get used to these responsibilities. As the FERC places more emphasis on transmission access,¹⁴⁴ the utility will not be able to hide behind the veil of the filed rate doctrine.¹⁴⁵ Access implies choice, and with choice comes responsibility.

Trapping costs likewise does not provide a special barrier to finding a duty to mitigate. In dicta, the Supreme Court has recognized situations in which costs determined by the FERC to be reasonable are nonetheless trapped without legal infirmity. Every contract approved by the FERC is in a sense a FERC ordered decision that the seller's costs are just and reasonable; they must be under the statutory requirements of the Federal Power Act.¹⁴⁶ The

138. See *supra* notes 107-116, 138 and accompanying text.

139. Compare the discussion found in Hobelman, *supra* note 5, at 48-52, Nixon & Johnston, *supra* note 5, at 5-12, and Vince & Moot, *Federal Preemption*, *supra* note 5, at 28.

140. Nixon & Johnson, *supra* note 5, at 30-31 & n.131.

141. Nixon & Johnson, *supra* note 5, at 26.

142. Phillips, *supra* note 2, at 325-27.

143. Vince & Moot, *Federal Preemption*, *supra* note 5, at 72.

144. See, Thomas F. Berg, *FERC's Spotlight on Transmission Access*, Pub. Util. Fortnightly, Aug. 1, 1991, at 23.

145. Stalon & Lock, *supra* note 5, at 474; Richard J. Pierce, *The Future of the Nantahala Doctrine in the Gas Industry*, 4 NAT. RESOURCES & ENV'T. 21, at 22 (1989).

146. Pennsylvania Power & Light Co. v. Pennsylvania Pub. Util. Comm'n, 127 Pa. Commw. 109, 561 A.2d 43 (1987).

choice to enter that contract outside a pooling arrangement, however, does not arise unless the purchasing utility agrees to it. The selling price may be deemed reasonable but the choice to purchase at that price may not be. Under *Pike County*, the local regulator retains the authority to reject the purchaser's choice. In effect, then, the exception results in trapping costs the FERC determined were reasonable. Likewise, the utility may not have any choice in taking an allocation under a pooling agreement, but it may have a choice on whether it keeps it. That essentially local decision traps any FERC ordered costs in the same way and so would be treated the same way.¹⁴⁷

V. PREEMPTION AS A CHECK ON STATE ACTION

Apart from the traditional arguments concerning preemption, another concern about the potential disallowances may be driving the Court's decisions. Inherent in the Supreme Court's aggressive posture to the filed rate doctrine may be an agenda to limit state actions leading to significant disallowances. In rate making cases, the effects are often large, and that is especially true recently, given the spate of cost overruns associated with nuclear construction.¹⁴⁸ Likewise, state commission action has resulted in large write downs.¹⁴⁹ Given the more favorable environment afforded by the FERC rate making approach,¹⁵⁰ the Court may be playing an interesting end game to protect utilities from the perceived political unfairness (reflected in large disallowances) of state review.¹⁵¹

To the extent that the courts use the filed rate doctrine to counter the effects of a political imbalance, it is a clumsy tool. First, as noted above, the use of the filed rate doctrine simply moves the decision from one political actor to another. Today's choices may prove a disaster tomorrow. Second, the Court may have already signaled a more direct approach to balancing any political failure at the state level. Clearly, regulatory agencies are bound by constitutional limits on takings and due process, and the Supreme Court and lower courts appear to be returning to these root doctrines to establish param-

147. This argument suffers because it tends to prove too much. If trapping is a problem for the unaffiliated and the affiliated, then the logical result is to treat both the same way. The problem however, is less with that argument and more with the argument of trapping in the first instance. The Supreme Court has created a test and then drawn distinctions that do not logically follow from the text. The results of cases then seem to turn on the characterization of the action rather than whether costs are trapped or not. Thus, the Fifth Circuit can in *NOPSI* characterize the transaction as one involving mitigation and avoid the logical consequence of the FERC order allocating a portion of the capacity to New Orleans, a result otherwise precluded by *Nantahala*. The point here is not so much to criticize the test but to suggest that the duty to mitigate is consistent with the kinds of arguments that support the other exceptions to the filed rate doctrine.

148. As noted above, Grand Gulf I was completed at a cost of six times original cost estimates. Other examples of large overruns are common.

149. Richard J. Pierce, Jr., *Public Utility Regulatory Takings: Should the Judiciary Attempt to Police the Political Institutions?* 77 GEO. L.J. 2031, 2050-51 (1989); Michael A. Laros & Samuel A. Haubold, *The Shifting Standard of Prudence: Implications for Utilities*, Pub. Util. Fortnightly 21 (Oct. 29, 1987).

150. Nixon & Johnson, *supra* note 5, at 30-31 & n.131.

151. See generally, Pierce, *supra* note 149, for a discussion of the political failure within the current regulatory framework.

eters.¹⁵² While significant disagreements exist concerning the point at which state action is checked, there is no disagreement that a check exists.¹⁵³ To the extent that there is any unfairness in the current system of retail rate making, the solution is to use the appropriate constitutional tools, not to extend others to achieve a rough and ready compromise that may ultimately fail to realize the underlying goals.

VI. CONCLUSION

If there is a duty to mitigate, it follows that the complaints and concerns raised against power pools may be less significant than once thought. There would exist a tool by which local commissions could hold management responsible on a continuing basis for the decisions about power purchases that might otherwise escape continuing review. Since the major concerns associated with federalism and economic planning are not significantly impacted, the new exception offers a timely component to the regulatory mix. With the growing insistence for greater transmission access, it also is consistent with the likely trend in utility regulation toward greater local decision making. In this respect, at least, the goals of the Congress that passed the Federal Power Act in 1935 and current regulatory policy began to coincide in a useful way.

152. See, e.g., *Duquesne Light Co. v. Barasch*, 109 S. Ct. 609 (1989); *Jersey Central Power & Light Co. v. FERC*, 810 F.2d 1168 (D.C. Cir. 1987).

153. For a discussion of various positions on the nature of the constitutional takings standard in rate making cases, see Pierce, *supra* note 149; Richard McKenna & Ward W. Wueste, *An Answer to Professor Pierce: How Utility Regulation Can Be Reformed in Harmony with Constitutional Principles*, 27 CAL. W. L. REV. 81 (1990); John N. Drobak, *From Turnpike to Nuclear Power: Constitutional Limits on Utility Rate Regulation*, 65 B.U.L. REV. 65 (1985); Walter Pond, *The Law Governing the Fixing of Public Utility Rates: A Response to Recent Judicial and Academic Misconceptions*, 41 AD. L. REV. 1 (1989); Frank P. Darr, *The Constitutional Limits on Ratemaking: A Response to William [Walter] Pond*, 11 ENERGY L.J. 53 (1990); Walter Pond, *The Constitutional Limits on Ratemaking: A Reply to Frank Darr*, 12 ENERGY L.J. 111 (1991); Richard Goldsmith, *Utility Rates and "Takings"*, 10 ENERGY L.J. 241 (1989); A. Lawrence Kolbe & William B. Tye, *The Duquesne Opinion: How Much "Hope" is There for Investors in Regulated Firms?* 8 YALE J. ON REG. 113 (1991).