

**IN THE UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT**

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**Nos. 03-72874, *et al.* (consolidated)**

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**PACIFIC GAS AND ELECTRIC COMPANY, *ET AL.*,  
Petitioners,**

**v.**

**FEDERAL ENERGY REGULATORY COMMISSION,  
Respondent.**

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**ON PETITIONS FOR REVIEW OF ORDERS OF THE  
FEDERAL ENERGY REGULATORY COMMISSION**

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**BRIEF FOR RESPONDENT  
FEDERAL ENERGY REGULATORY COMMISSION**

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**FOR RESPONDENT  
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**SEPTEMBER 2, 2004**

**CERTIFICATE OF COMPLIANCE WITH FED. R. APP. P.  
32(a)(7)(C) AND CIRCUIT RULE 32-1**

I hereby certify that, pursuant to Federal Rule of Appellate Procedure 32(a)(7)(C) and Ninth Circuit Rule 32-1, the attached answering brief is proportionately spaced, has a typeface of 14 points or more, and contains 7279 words.

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September 2, 2004

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**STATEMENT OF THE ISSUE**

Whether the Federal Energy Regulatory Commission (“Commission” or “FERC”) reasonably exercised its prosecutorial discretion to conduct investigations when it denied third-party requests for intervention in certain settled proceedings.

**COUNTERSTATEMENT OF JURISDICTION**

Petitioners incorrectly state (Pet. Br. 2, 38-42) that this Court has jurisdiction to consider their petitions for review. To the contrary, this Court lacks jurisdiction

to consider the challenged FERC orders. Those orders approved settlement agreements that resolved certain non-public investigations, and thus represent a non-reviewable exercise of the Commission's prosecutorial discretion. *See infra* pages 22-26. *See also, e.g., Heckler v. Chaney*, 470 U.S. 821, 831-33 (1985); *Friends of the Cowlitz v. FERC*, 253 F.3d 1161, 1170-72 (9<sup>th</sup> Cir. 2001); *Baltimore Gas & Electric Co. v. FERC*, 252 F.3d 456, 459-62 (D.C. Cir. 2001); 5 U.S.C. § 701(a)(2).

## **STATUTES AND REGULATIONS**

Pertinent statutes and regulations are set out in the Addendum to this brief.

## **STATEMENT OF THE CASE**

### **I. NATURE OF THE CASE, COURSE OF PROCEEDINGS, AND DISPOSITION BELOW**

With the second half of 2000 came an energy "crisis" that brought a sharp rise in wholesale electricity prices in California, frequent system emergencies and occasional blackouts, and financial distress to California utilities and market participants.<sup>1</sup> In response, the Commission initiated a series of adjudicatory and investigative proceedings, intended both to settle and reform markets going forward and to provide ratepayer relief going backward. *See, e.g., In re California Power Exchange Corp.*, 245 F.3d 1110, 1125 (9<sup>th</sup> Cir. 2001) (approving of the

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<sup>1</sup> The energy crisis actually affected a number of Western states, not just California, but the instant appeal is limited to California markets and prices. *See* Pet. Br. 4 n.5.

Commission's decision to focus first on prospective remedies and then turn to retroactive relief).

Within this context, the instant case involves **ten** consolidated petitions seeking judicial review of **seven** FERC orders approving the settlement of certain FERC-instituted investigative proceedings: *Fact-Finding Investigation Into Possible Manipulation of Electric and Natural Gas Prices*, 102 FERC ¶ 61,108 (2003), ER 1, *interventions denied*, 103 FERC ¶ 61,019 (2003), ER 61, *rehearings dismissed*, 104 FERC ¶ 61,146 (2003), ER 128; *Reliant Energy Services, Inc., et al.*, 105 FERC ¶ 61,008 (2003), ER 132, *rehearings dismissed*, 105 FERC ¶ 61,253 (2003), ER 224; and *Duke Energy North America, LLC, et al.*, 105 FERC ¶ 61,307 (2003), ER 226, *rehearings dismissed*, 106 FERC ¶ 61,177 (2004), ER 283.

**Four** Petitioners seek review of those orders: Pacific Gas and Electric Company; Public Utilities Commission of the State of California; People of the State of California *ex rel.* Bill Lockyer, Attorney General; and Southern California Edison Company (collectively, the "California Parties").<sup>2</sup> They seek review of the Commission's approval of **three** settlements resolving FERC-instituted investigations of **two** wholesale suppliers of energy in Western markets: Reliant Resources, Inc. and its affiliates (collectively, "Reliant"); and Duke Energy Corp.

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<sup>2</sup> A fifth member of the California Parties – the California Electricity Oversight Board – is participating in this consolidated appeal as an intervenor, rather than as a petitioner, and has filed a brief (along with intervenor Port of Seattle, Washington) in support of the California Parties' brief.

and its affiliates (collectively, “Duke”). Following a series of orders issued by this Court, the scope of judicial review is limited to only **one** issue: the reasonableness of the Commission’s denial of the California Parties’ attempts to intervene in the Reliant and Duke investigative proceedings as parties for the purpose of challenging the settlement of those proceedings.

## **II. STATEMENT OF FACTS**

### **A. The Commission’s Refund Proceeding**

A series of FERC orders dating back to 2000, issued in FERC Docket Nos. EL00-95, *et al.*, implemented a number of structural and pricing reforms intended to make California and Western electricity markets more stable and less susceptible to price spikes.<sup>3</sup> These orders are the subject of dozens of petitions for review, filed by dozens of petitioners, in *Public Utilities Commission of the State of California, et al. v. FERC*, 9<sup>th</sup> Cir. Nos. 01-71051, *et al.* See August 21, 2002 and July 27, 2004 Orders in Nos. 01-71051, *et al.* (holding appeals in abeyance).

In relevant respect, the Commission orders issued in FERC Docket Nos. EL00-95, *et al.* (collectively, the “Refund Proceeding”) established a methodology, ultimately effective June 21, 2001, for mitigating the price of electricity sold at

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<sup>3</sup> See *San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services, et al.*, 93 FERC ¶ 61,121 (Nov. 1, 2000); 93 FERC ¶ 61,294 (Dec. 15, 2000); 95 FERC ¶ 61,115 (Apr. 26, 2001); 95 FERC ¶ 61,418 (June 19, 2001); 96 FERC ¶ 61,120 (July 25, 2001); 97 FERC ¶ 61,275 (Dec. 19, 2001); 99 FERC ¶ 61,160 (May 15, 2002); 105 FERC ¶¶ 61,065 & 61,066 (Oct. 16, 2003); 107 FERC ¶¶ 61,165 & 61,166 (May 12, 2004); *rehearing pending*.

wholesale through centralized, single price auction spot markets operated by the California Independent System Operator (“ISO”) and, for a time, the California Power Exchange (“PX”). *See, e.g., California Power Exchange*, 245 F.3d at 1114-16 (explaining development and restructuring of California wholesale electricity markets and roles of the ISO and PX); *California v. Dynegy, Inc.*, 9<sup>th</sup> Cir. Nos. 02-16619, *et al.*, slip op. at 8835-38 (July 6, 2004) (same).

Looking backward, at the period from October 2, 2000 to June 20, 2001, the Commission established a process for re-calculating prices for rates that are adjudged to be unjust and unreasonable under section 206 of the Federal Power Act (“FPA”), 16 U.S.C. § 824e. Specifically, a Commission-established formula set the mitigated market clearing price during that period, and an evidentiary hearing was ordered to determine whether (and, if so, how much) refunds are owed by any sellers in the organized spot markets in California.<sup>4</sup>

The Commission limited the temporal scope of the Refund Proceeding to the window between October 2, 2000 and June 20, 2001 because FPA § 206(b), *see* 16 U.S.C. § 824e(b), limits refunds for unjust and unreasonable rates to a period commencing no earlier than 60 days after the filing of a complaint seeking refunds.

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<sup>4</sup> The Commission deemed a hearing necessary to develop a record from which to make findings of fact concerning: (1) the mitigated price in each hour of the refund period; (2) the amount of refunds owed by each supplier according to the FERC-prescribed methodology; and (3) the amount currently owed to each supplier by the ISO, utilities, and the State of California. *See* 96 FERC ¶ 61,120 at 61,520.

Because the Refund Proceeding commenced upon the August 2, 2000 filing of a complaint by San Diego Gas & Electric Company, October 2, 2000 was the earliest “refund effective date” allowed by the statute. *See, e.g.*, 96 FERC ¶ 61,120 at 61,504-11; 97 FERC ¶ 61,275 at 62,198-99.

The Commission clarified, however, that it has additional retroactive authority to direct additional remedies (including the disgorgement of profits) for rates charged **during any time period**, even prior to the date allowed by FPA § 206(b), in violation of Commission-filed tariffs. *See* 96 FERC ¶ 61,120 at 61,507-08 (noting that no violation of sellers’ market-based rate tariffs had yet been demonstrated).

### **B. The Commission’s Investigative Proceedings**

In early 2002, after the fall of Enron and in response to reports that it had abused its market-based pricing tariff authority, the Commission directed its enforcement staff to initiate a fact-finding investigation into whether any entity manipulated short-term prices in Western energy markets during the time period commencing January 1, 2000. *See Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Prices*, 98 FERC ¶ 61,165 (Feb. 13, 2002). The Commission afforded its staff broad authority to conduct its investigation: “In conducting this broad investigation, Commission staff may obtain information on any and all matters relevant to potential market manipulation



in the West. . . .” 98 FERC at 61,614. The Commission also afforded itself broad discretion how to use the information uncovered during the staff investigation: “Among other things the Commission may use the information developed by this fact-finding investigation to determine how to proceed on any existing or future FPA section 206 complaints . . . or any formal . . . proceedings initiated on our own motion.” *Id.*

In response, Commission staff engaged in extensive data gathering and analysis. Commission staff obtained over 2 terabytes of electronic data and hundreds of boxes of written materials. Staff shared information with the U.S. Department of Justice and other investigatory agencies, and sent data requests to hundreds of respondents representing all segments of the industry. In addition, Commission staff met with representatives of the California Parties and reviewed their submissions of ISO/PX bidding data and expert testimony and analyses. *See San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services*, 101 FERC ¶ 61,186 (2002), *order on reh’g*, 102 FERC ¶ 61,164 (2003) (allowing all parties to conduct discovery into market manipulation by various sellers after January 1, 2000 and specifying procedures for the submission of new evidence).<sup>5</sup>

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<sup>5</sup> The Commission permitted the California Parties (and other market participants) the opportunity to gather and introduce additional evidence of market manipulation after this Court, in an order issued August 21, 2002, granted their motion for leave to adduce additional evidence. As explained *infra* at page 22, however, the Court explicitly left to the Commission’s discretion how best to

Commission staff issued a Final Report on its investigation on March 26, 2003.<sup>6</sup> Staff concluded, among other things, that the tariffs of the California ISO and PX prohibit abuses of market power that impair the efficient operations of the ISO and PX markets. Staff identified various instances or allegations of possible market power abuses, violating tariff requirements, in the form of: (1) anomalous bidding behavior; and (2) physical withholding of generation resources from California markets.

In response to the Final Report, the Commission initiated a number of investigative proceedings, taking different forms, to examine instances of potential wrongdoing and to take remedial action as appropriate, regardless of when the wrongdoing occurred. Some proceedings took the form of public, on-the-record proceedings. For example, on June 25, 2003, the Commission directed dozens of entities – including both Reliant and Duke – to show cause, in evidentiary hearings, why their conduct after January 1, 2000 did not constitute gaming and/or anomalous market behavior in violation of applicable tariffs. The Commission directed the administrative law judges to hear evidence, render findings and conclusions quantifying the extent to which the identified entities may have been unjustly enriched as a result of their conduct, and recommend appropriate

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adduce and consider this information.

<sup>6</sup> A link to the lengthy Final Report on Price Manipulation in Western Markets, and a summary, can be found at <http://www.ferc.gov/industries/electric/indus-act/wem/pa02-2.asp>.

monetary and non-monetary remedies. *See American Electric Power Service Corp., et al.*, 103 FERC ¶ 61,345 (2003), *reh'g denied*, 106 FERC ¶ 61,020 (2004). *See also Reliant Energy Services, Inc.*, 102 FERC ¶ 61,315 (2003) (directing Reliant and BP Energy Company to show cause, in paper hearings, why their authority to sell power at market-based rates should not be revoked in light of apparent manipulation, identified in the Final Report, of energy prices at the Palo Verde trading hub).

Other proceedings took the form of non-public, off-the-record proceedings. *See* 18 C.F.R. Part 1b (rules relating to investigations). For example, on June 28, 2003, the Commission directed its staff to investigate all bids in the ISO and PX markets above \$250 per megawatt-hour, during the period May 1, 2000 to October 2, 2000, to determine whether any bids represented the type of anomalous bidding behavior identified in the Final Report as a tariff violation. *See Investigation of Anomalous Bidding Behavior and Practices in the Western Markets*, 103 FERC ¶ 61,347 (2003), ER 89.<sup>7</sup> Among other things, the Commission explained that it could remedy any tariff violation occurring after May 1, 2000 by ordering the disgorgement of any unjust profits in addition to refunds ordered in the Refund Proceedings. 103 FERC at 62,361, ER 91.

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<sup>7</sup> Commission staff previously was instructed to investigate allegations of physical withholding of generation resources from California markets during the period from May 1, 2000 to June 30, 2001.

In response to its directives, and in conducting its investigations, the Commission's staff compiled its own evidence, reviewed party-submitted evidence, and held meetings with the California Parties and other market participants.

### **C. The Reliant I Settlement Proceeding**

In the course of its fact-finding investigation, Commission learned that Reliant had withheld capacity offered into California power markets. Specifically, Reliant, responding to Commission requests for market data and transcripts of telephone conversations of Reliant traders, indicated that its traders reduced the amount of capacity bid into the California PX day-ahead market for delivery on June 21 and 22, 2000, for the purpose of increasing prices. Reliant elected to perform discretionary maintenance on generating units whose output otherwise would have been offered to California markets on those two days.

An order issued January 31, 2003 approved a settlement between Reliant and Commission investigative staff ("Reliant Settlement I"), resolving all issues concerning the June 21-22, 2000 withholding of capacity. *Fact-Finding Investigation Into Possible Manipulation of Electric and Natural Gas Prices*, "Order Approving Stipulation and Consent Agreement," 102 FERC ¶ 61,108 (2003), ER 1. Reliant agreed to pay approximately \$13.8 million to PX customers, which represented a worst case scenario of the effect of Reliant's withholding on

California markets. Reliant also agreed to various other undertakings (continued must-offer obligation, periodic outage audits) to prevent reoccurrence of similar trading misconduct.

In finding the settlement fair, reasonable, and in the public interest, *see* 18 C.F.R. § 385.602(g)(3) (standards for assessing uncontested settlement offer), the Commission stressed the narrow reach of the agreement. The settlement did not make any findings or limit any remedies as to Reliant's conduct on other days, did not resolve any other matters or issues that were the subject of other ongoing investigations of Reliant's conduct, and did not preclude any potential relief or remedy in any other proceeding – including the Refund Proceeding. 102 FERC at 61,286-87, ER 2-3; *see also* 102 FERC at 61,288-290, ER 4-6 (stipulated facts and settlement terms).

The California Parties and others subsequently moved to intervene in the Reliant I Settlement proceeding. The Commission, in an order issued on April 9, 2003, denied all motions for interventions. *Fact-Finding Investigation Into Possible Manipulation of Electric and Natural Gas Prices*, 103 FERC ¶ 61,019 (2003), ER 61. The Commission explained that, under its regulations, *see* 18 C.F.R. §§ 1b.11 and 385.101(b)(1), there is no right to intervene in non-public investigations. Nor was the Commission persuaded to permit intervention as a matter of discretion: “To allow third parties to participate in and second guess the

Commission's decisions in investigations could also cripple its ability to prosecute and settle such investigations, because the subjects of the investigations would be very reluctant to enter into settlements for fear that they could be reopened." 103 FERC at P15, ER 63; *see also id.* at P 17, ER 63 (intervention of third parties "would, in short, undermine the Commission's ability to investigate and, in particular, resolve matters within its jurisdiction").

A subsequent order, issued July 28, 2003, dismissed the California Parties' requests for rehearing of the order denying their intervention into the Reliant I Settlement proceeding. *Fact-Finding Investigation Into Possible Manipulation of Electric and Natural Gas Prices*, 104 FERC ¶ 61,146 (2003), ER 128. Under the explicit terms of the FPA, *see* 16 U.S.C. § 825l, only a "party" may seek agency rehearing (and, ultimately, judicial review). Under the Commission's implementing regulations, a "party" is defined, in relevant part, as a person whose intervention has been permitted. 18 C.F.R. § 385.102(c)(3). "[I]f their logic were accepted," the Commission explained in responding to the California Parties' request for intervention, "there would likely never be a case where the Commission could deny intervention." 104 FERC at P 15, ER 131. As a consequence, the Commission:

could never on its own settle any investigation; every investigation and every settlement would be subject to challenge and revision, and judicial review, at the behest of third parties. Such a reading is hardly consistent with the discretion that the statutes and the precedent grant

the Commission, and would undermine both the Commission's ability to settle investigations and its policies favoring settlement; thus it must fail.

104 FERC at P 15, ER 131 (internal citations omitted).

#### **D. The Reliant II Settlement Proceeding**

Reliant and Commission staff subsequently reached a broader settlement ("Reliant Settlement II"), resolving most issues arising from the Commission's investigation of Reliant's activities in Western energy markets in 2000 and 2001. Reliant agreed to pay \$25 million, plus up to \$25 million more from the proceeds from the auction of generating capacity in California, to Western electricity consumers. Reliant also agreed to enhanced reporting of trading data and trader communications.

An order issued October 2, 2003 approved the Reliant II Settlement. *Reliant Energy Services, Inc., et al.*, 105 FERC ¶ 61,008 (2003), ER 132. The Commission found that the settlement represented an "equitable resolution" of various matters, 105 FERC at P 26, ER 136, but did not resolve allegations of improper gaming practices by Reliant (which were the subject of a separate settlement agreement). The Reliant II Settlement also did not resolve or otherwise affect any obligations Reliant might have as a result of the Refund Proceeding. 105 FERC at PP 2, 8, 27, ER 133-34, 136. Citing to its earlier Reliant I Settlement orders, the Commission noted that it would not entertain requests for intervention

or requests for rehearing in the Reliant II Settlement proceeding. 105 FERC at P 26 n.6, ER 136.

Despite that admonition, the California Parties filed a request for rehearing, which was dismissed in an order issued November 26, 2003. *Reliant Energy Services, Inc., et al.*, 105 FERC ¶ 61,253 (2003), ER 224. Citing its earlier Reliant I orders, the Commission reiterated that there are no parties to its investigative proceedings, where the Commission has been delegated absolute discretion. 105 FERC at PP 3-4, ER 224-25. Because the California Parties lacked party status, they also lacked standing under the FPA to seek rehearing of the Commission's approval of a settlement terminating an investigative proceeding. 105 FERC at P 5, ER 225.

#### **E. The Duke Settlement Proceeding**

Like Reliant, Duke reached a broad settlement with Commission staff ("Duke Settlement"), resolving most issues arising from the investigation of Duke's activities in Western energy markets in 2000 and 2001. Reliant agreed to pay \$2.5 million to Western electricity consumers. Like the Reliant II Settlement, the Duke Settlement did not resolve allegations of improper gaming practices (which were the subject of a separate settlement agreement), nor did it affect any obligations Duke might have as a result of the Refund Proceeding.

An order issued December 19, 2003 approved the Duke Settlement. *Duke*



*Energy North America, LLC, et al.*, 105 FERC ¶ 61,307 (2003), ER 226. The Commission found that the settlement represented an “equitable resolution” of most matters, 105 FERC at P 17, ER 228, and, citing to earlier orders, again noted that it would not entertain requests for intervention or requests for rehearing. 105 FERC at P 17 n.4, ER 228.

The California Parties again disregarded this admonition and again filed a request for rehearing, which was dismissed in an order issued February 19, 2004. *Duke Energy North America, LLC, et al.*, 106 FERC ¶ 61,177 (2004), ER 283. Consistent with its approach in the Reliant I and II Settlement proceedings, and again citing its discretion in pursuing and terminating investigations, the Commission again denied the California Parties’ request to intervene as parties and dismissed their request for rehearing. 106 FERC at PP 3-5, ER 284.

#### **F. Limited Scope of Judicial Review**

In a series of procedural orders over the past year, the Court consolidated all petitions for review of the Reliant I, Reliant II, and Duke Settlement orders. The Court denied all requests by the California Parties to further consolidate review of the instant petitions with the petitions in Nos. 01-71051, *et al.* seeking review of the many Refund Proceeding orders. Similarly, the Court denied requests by the Commission to dismiss the instant petitions for lack of jurisdiction. The Court did, however, in orders issued November 3, 2003, December 16, 2003, and March 12,

2004, explicitly limit briefing in the instant appeals to the denial of requests for intervention, citing its opinion in *Covelo Indian Community v. FERC*, 895 F.2d 581, 585-86 (9<sup>th</sup> Cir. 1990) (holding that a party denied party status below is “not a party eligible to seek rehearing or judicial review of the merits of the [Commission’s] decision”).

### **SUMMARY OF ARGUMENT**

The Commission has broad, non-reviewable discretion to conduct and to settle its investigations of Reliant’s and Duke’s conduct in Western energy markets during 2000-2001. That discretion, which covers decisions whether to allow third-party intervention, follows from: (1) the governing statute (the Federal Power Act), which offers few guidelines or limitations on the Commission’s exercise of its investigative authority; and (2) Commission regulations that differentiate between investigative and adjudicatory proceedings. This Court, recognizing governing precedent that affords the Commission discretion in its conduct of investigations, explicitly left to the Commission’s discretion how best to consider evidence of market misconduct by Western energy suppliers.

The California Parties’ efforts to characterize the Reliant and Duke Settlement proceedings as adjudicatory proceedings fail. Contrary to their argument, there has been no transfer of issues from the adjudicatory Refund Proceeding to “splinter” settlement proceedings. Rather, the temporal and

substantive scope of the Refund Proceeding is entirely different than the scope of the Reliant and Duke proceedings. Indeed, the Commission initiated the Reliant and Duke proceedings (and other investigative proceedings) precisely to expand the scope of potential relief to California consumers and to allow them to pursue potential tariff violations by Western energy suppliers whenever they may have occurred.

The California Parties are similarly mistaken in arguing that the Commission, in denying their requests for intervention in the Reliant and Duke proceedings, denied them their due process rights. They were not denied the opportunity to participate in the proceedings. To the contrary, while they were unable to obtain the formal status of party-intervenors, they nevertheless were fully able to present evidence as to Reliant's and Duke's conduct and they were able to articulate their objections to the proposed settlements. In considering their evidence and comments, and ultimately approving the Reliant and Duke settlements without interventions, the Commission acted entirely in accord with its precedent.

## ARGUMENT

### I. STANDARD OF REVIEW

Judicial review of Commission orders is limited. *E.g., City of Centralia, Washington v. FERC*, 799 F.2d 475, 481 (9th Cir. 1986). A Commission ruling may be overturned only if it is arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law. 5 U.S.C. § 706(2)(A); *see, e.g., The Steamboaters v. FERC*, 759 F.2d 1382, 1388 (9th Cir. 1985). That narrow standard requires a court to satisfy itself that the agency "examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.'" *Motor Vehicle Mfrs. Ass'n of United States, Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (quoting *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168 (1962)). As long as the record shows that the agency's decision was "based on a consideration of relevant factors and there is no clear error of judgment," the decision was not arbitrary or capricious. *Arizona Cattle Growers' Ass'n v. U.S. Fish & Wildlife*, 273 F.3d 1229, 1236 (9<sup>th</sup> Cir. 2001).

Moreover, judicial review is particularly deferential when assessing the choice of procedures to govern the conduct of a particular proceeding, *e.g., Pacific Gas and Electric Co. v. FERC*, 746 F.2d 1383, 1386 (9<sup>th</sup> Cir. 1984), or, more

specifically, a decision whether to grant or deny intervention, *e.g.*, *Southern California Edison Co. v. Lynch*, 307 F.3d 794, 802-03 (9<sup>th</sup> Cir. 2002).

## **II. THE COMMISSION HAS BROAD DISCRETION TO DETERMINE HOW BEST TO CONDUCT AND RESOLVE AN INVESTIGATION**

The challenged orders correctly recognized that the Commission has broad prosecutorial discretion to determine how to conduct and conclude an investigation. *See* Reliant I Settlement, 103 FERC ¶ 61,019 at PP 14-15, ER 63, and 104 FERC ¶ 61,146 at PP 13-14, ER 130-31; Reliant II Settlement, 105 FERC ¶ 61,253 at PP 3-4, ER 224-25; Duke Settlement, 106 FERC ¶ 61,177 at PP 3-4, ER 284.

This discretion derives from a number of different sources. The Federal Power Act delegates to Commission broad authority to “investigate any facts, conditions, practices, or matters” to aid in the enforcement of the statute. FPA § 307(a), 16 U.S.C. § 825f(a); *see also, e.g.*, FPA § 309, 16 U.S.C. §825h (affording the Commission the authority to “perform any and all acts” necessary to enforce the statute). The Commission’s regulations follow the broad statutory delegation by distinguishing its investigative proceedings from other proceedings. For example, its Rules of Practice and Procedure, while generally applicable to public adjudications, do not apply to investigations. *See* 18 C.F.R. § 385.101(b)(1). Likewise, in relevant respect, the procedural rules generally applicable to the filing and consideration of motions for intervention, *see* 18 C.F.R. § 385.214, do not

apply to investigations: “There are no parties, as that term is used in adjudicative proceedings, in an investigation under this part and no person may intervene or participate as a matter of right in any investigation under this part.” 18 C.F.R. § 1b.11.

In denying the motions of the California Parties seeking formal participation as parties in the Reliant I, Reliant II and Duke settlement proceedings, the Commission explained that its procedural rules concerning investigations serve an important public interest – encouraging the timely and final settlement of disputes. Allowing third-party intervention would “undermine the Commission’s ability to investigate and, in particular, resolve matters within its jurisdiction.” Reliant I Settlement, 103 FERC ¶ 61,019 at P 17, ER 63. In particular, allowing third parties to intervene after a settlement is reached, so that they can challenge its terms, would be problematic because “the subjects of the investigations would be very reluctant to enter into settlements for fear that they could be reopened.” *Id.* at P 15, ER 63. In the instant cases, without the threat of continued third-party litigation and resulting uncertainty, the Commission was able to negotiate and approve settlements of investigations that served the public interest by accelerating both the return of money to California energy consumers and the public disclosure of market misconduct by energy suppliers. *See* Reliant I Settlement, 102 FERC ¶ 61,108 at 61,290, ER 6 (Massey, Comm’n’r, concurring).

The Commission's procedural rules and practices reflect the broad discretion that an agency enjoys to determine appropriate procedures and priorities to apply to its consideration of pending matters. *See Mobil Oil Exploration & Producing Southeast, Inc. v. United Distribution Cos.*, 498 U.S. 211, 230 (1991) (upholding the Commission's decision to address and resolve separate, but related, issues in separate proceedings). That discretion can be upset only in extraordinary circumstances:

Absent constitutional constraints or extremely compelling circumstances the administrative agencies should be free to fashion their own rules of procedure and to pursue methods of inquiry capable of permitting them to discharge their multitudinous duties. Indeed, our cases could hardly be more explicit in this regard.

*Vermont Yankee Nuclear Power Corp. v. NRDC*, 435 U.S. 519, 543-44 (1978) (citations and internal quotation marks omitted).<sup>8</sup> This case does not present such circumstances.

This Court has recognized the Commission's discretion to pursue issues arising from the California energy crisis, in a fashion the Commission deems best

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<sup>8</sup> *See also, e.g., Florida Municipal Power Agency v. FERC*, 315 F.3d 362, 366 (D.C. Cir. 2003) (upholding Commission's decision not to consolidate related proceedings, as "[a]dministrative agencies enjoy broad discretion to manage their own dockets"); *Swinomish Tribal Community v. FERC*, 627 F.2d 499, 510 (D.C. Cir. 1980) (holding that Commission was within its discretion in instituting a separate administrative proceeding to consider the impact of a hydroelectric project on downstream flow releases); *Natural Resources Defense Council, Inc. v. SEC*, 606 F.2d 1031, 1056 (D.C. Cir. 1979) ("[a]n agency is allowed to be master of its own house, lest effective agency decisionmaking not occur in any proceeding").

to fulfill its statutory duties. *See State of California v. FERC*, 329 F.3d 700, 715 (9<sup>th</sup> Cir. 2003) (explaining that “[b]alancing potentially conflicting factors relevant to the public’s energy needs is a task for the Commission’s discretion that we hesitate to second-guess”); *California Power Exchange*, 245 F.3d at 1125 (explaining that petitioners “do[] not appear to appreciate the flexibility FERC has under the FPA to address conditions leading to unjust and unreasonable rates in a market-based system by reforming market structures”). Indeed, the Court’s August 21, 2002 order, granting the California Parties’ motion for leave to adduce additional evidence of market manipulation by various sellers into California markets, explicitly “defer[ed] to the discretion of FERC to determine how this new evidence shall be adduced.” Order at 7-8. The Court thus recognized the broad sweep of discretion delegated to the Commission to investigate and consider facts, and thus correctly refrained from prescribing particular procedures for individual proceedings.<sup>9</sup>

### **III. THE COMMISSION’S EXERCISE OF ITS DISCRETION IN PURSUING INVESTIGATIONS IS NON-REVIEWABLE**

The challenged orders correctly recognized that the Commission’s prosecutorial discretion to conduct and to resolve an investigation is not only

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<sup>9</sup> On July 27, 2004, this Court denied motions of the California Parties (*see* Pet. Br. 12-13) which argued that the Commission failed to comply with the August 21, 2002 order by considering evidence of market misconduct (including evidence submitted by the California Parties) in separately-initiated investigative proceedings.



broad, but also non-reviewable. *See* Reliant I Settlement, 103 FERC ¶ 61,019 at P 15 & n.9, ER 63, and 104 FERC ¶ 61,146 at P 13 & n.14, ER 130; Reliant II Settlement, 105 FERC ¶ 61,008 at P 26 n.6, ER 136. *See also Fact-Finding Investigation of Potential Market Manipulation of Electric and Natural Gas Prices*, 105 FERC ¶ 61,063 at P 5, ER 153 (2003) (explaining that the Commission’s investigative and enforcement decisions are entrusted to its non-reviewable discretion).<sup>10</sup>

While there is a general presumption of reviewability under the Administrative Procedure Act, judicial review does not extend to cases where “agency action is committed to agency discretion by law.” 5 U.S.C. § 701(a)(2). As explained above, the FPA and the Commission’s implementing regulations, as well as recent orders and opinions of this Court, confer discretion on the Commission as to how to conduct its investigations and, more specifically, how to consider the evidence presented by the California Parties. Indeed, this Court held in *Friends of the Cowlitz v. FERC*, 253 F.3d 1161 (9<sup>th</sup> Cir. 2001), that the Commission “has virtually unreviewable discretion to enforce” under the plain language of the statute and regulations the Commission administers. *Id.* at 1162.

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<sup>10</sup> The Commission raised a similar jurisdictional argument in its motions to dismiss some of the consolidated appeals. The Court’s earlier denial of those motions does not foreclose later reconsideration of the argument in the parties’ briefs. *See National Industries, Inc. v. Republic National Life Insurance Co.*, 677 F.2d 1258, 1262 (9<sup>th</sup> Cir. 1982). Indeed, Petitioners have addressed this issue in their opening brief, Pet. Br. 38-42.

The Supreme Court explained in *Heckler v. Chaney*, 470 U.S. 821, 831 (1985), in construing the APA § 701(a)(2) exception to judicial review, that an agency's decision whether and how to investigate and enforce "often involves a complicated balancing of a number of factors which are peculiarly within its expertise," including the identification of agency priorities and the allocation of agency resources. Both *Heckler* and *Friends of the Cowlitz* specifically found an agency's decision not to undertake an enforcement action to be non-reviewable; however, their holding and reasoning extend more broadly to agency decisions about all types of investigative and enforcement actions.

For example, the court in *Baltimore Gas & Electric Co. v. FERC*, 252 F.3d 456 (D.C. Cir. 2001), found that the Commission's non-reviewable discretion extends not just to decisions to initiate an investigative or enforcement action, but also to decisions how to settle such actions. The court explained that *Heckler* "sets forth the general rule that an agency's decision not to exercise its enforcement authority, or to exercise it in a particular way, is committed to its absolute discretion." 252 F.3d at 459. This general rule is particularly suited to Commission enforcement and investigative proceedings, which are governed by statutes that "expressly confirm[] the breadth of the Commission's enforcement discretion." *Id.* at 461.<sup>11</sup> See also *Fort Sumter Tours, Inc. v. Babbitt*, 202 F.3d

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<sup>11</sup> In *Baltimore Gas & Electric*, the court confronted agency decisions under

349, 354 (D.C. Cir. 2000) (agency's decision to settle represents non-reviewable exercise of its prosecutorial discretion); *New York State Dep't of Law v. FCC*, 984 F.2d 1209, 1214 (D.C. Cir. 1993) (same).

The California Parties respond (Pet. Br. 39) that agency decisions are non-reviewable only when “there is no law to apply.” As this Court explained in *Friends of the Cowlitz*, however, the appropriate standard for reviewability is whether “Congress has provided clear legislative direction limiting an agency’s enforcement discretion.” 253 F.3d at 1167. <sup>12</sup> There, the Court reviewed provisions of the FPA and the Commission’s implementing regulations governing its investigative authority, *see supra* pages 19-20, and determined that there are no “meaningful guidelines” limiting the Commission’s discretion as to how to undertake or conclude an investigation: “FERC decisions to investigate (or not investigate),” because they are “clearly committed to the agency’s discretion,” are

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various provisions of the Natural Gas Act, whereas here the Commission’s decisions were exercised under analogous provisions of the Federal Power Act. The relevant provisions of the two statutes “are in all material respects substantially identical,” and precedents under either statute may be used interchangeably. *See, e.g., Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981); *Sierra Ass’n for Environment v. FERC*, 791 F.2d 1403, 1406 n.2 (9<sup>th</sup> Cir. 1986).

<sup>12</sup> The Court in *Heckler* questioned the applicability of the “no law to apply” standard, as the case that employed that standard, *Citizens to Preserve Overton Park v. Volpe*, 401 U.S. 402 (1971), cited here by Petitioners (at 39), involved much different circumstances: “an affirmative act of approval under a statute that set clear guidelines for determining when such approval should be given.” *Heckler*, 470 U.S. at 831. As explained above, here there are no such clear guidelines governing Commission action.

“therefore unreviewable by this court.” 253 F.3d at 1171-72; *see also Baltimore Gas & Electric Co.*, 252 F.3d at 461 (noting that the FPA, employing broad permissive language, offers no “discretion-restricting guideline” and indeed is “utterly silent on the manner in which the Commission is to proceed against a particular transgressor”).

Finding no statutory restrictions on the Commission’s discretion, the California Parties turn (Pet. Br. 11, 40-41) to this Court’s August 21, 2002 order granting their motion for leave to adduce additional evidence of market manipulation. They entirely overlook, however, the Court’s explicit grant of discretion to the Commission as to how best to adduce and consider new evidence. Order at 7-8. Moreover, they incorrectly claim that the Court directed the Commission to consider the California Parties’ evidence of market manipulation in the Refund Proceeding and thus restricted the Commission’s discretion to consider this evidence in its investigative proceedings. In fact, the August 21, 2002 order was not so prescriptive, as it only required the adducing of additional evidence “before FERC,” and not in any particular proceeding. Order at 7.

#### **IV. THE COMMISSION REASONABLY TREATED THE RELIANT AND DUKE PROCEEDINGS AS INVESTIGATIVE, NOT ADJUDICATORY, PROCEEDINGS**

Begrudgingly recognizing that the Commission “may have unreviewable discretion to initiate and settle some investigations,” Pet. Br. 22, the California

Parties argue that the Reliant and Duke proceedings are not investigative proceedings at all. Specifically, they argue that the Reliant and Duke proceedings should be treated as adjudicatory proceedings because they were “splintered” off from the adjudicatory Refund Proceeding (which they call the “Remedy Proceeding”). Pet. Br. 5, 13-14, 19-26, 39. The California Parties argue that the “transfer” of issues from the Refund Proceeding was undertaken solely to shield the Commission’s assessment of Reliant’s and Duke’s conduct from public and judicial scrutiny. Pet. Br. 2, 21-22.

The California Parties’ “transfer” theory is more fanciful than factual. Simply put, there has been no “transfer” of issues or evidence. The focus – both temporally and substantively -- of the Refund Proceeding differs entirely from the focus of the Duke and Reliant investigative proceedings. As explained *supra* at pages 4-6, the Refund Proceeding is a generic, industry-wide proceeding, addressing the extent to which rates charged after October 2, 2000 were unjust and unreasonable. The Duke and Reliant investigative proceedings are company-specific proceedings taking various public and non-public forms, and concern the extent to which Duke and Reliant may have violated applicable tariffs at any time, both before and after October 2, 2000.

Contrary to the California Parties’ contention (*e.g.*, Pet. Br. 5), the Duke and Reliant (as well as other company-specific) investigations were not “substitute

venues” for the Refund Proceeding. As explained earlier, *see supra* pages 5-6, the scope of the generally-applicable Refund Proceeding, which was instituted by a complaint filed under FPA § 206, 16 U.S.C. § 824e, was constrained by the statutory limits placed on the Commission’s authority to act on complaints. The company-specific investigations, on the other hand, were an outgrowth of the fact-finding investigation initiated in early 2002 and the staff report issued in early 2003, *see supra* pages 6-8, which revealed possible violations of FERC-approved market-based rate authority and FERC-approved tariffs. The Commission’s enforcement and remedial authority is much broader, both temporally and substantively, to rectify actions that violate tariff commitments and responsibilities.

<sup>13</sup> Possible remedies for tariff violations, occurring at any time, include the disgorgement of profits and the revocation of market-based rate authority – remedies not available in the Refund Proceeding.

As the company-specific investigations are not constrained, as is the Refund Proceeding, by the strictures of FPA § 206, those investigation address matters that are outside the purview of the Refund Proceeding. Thus, the investigations are not

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<sup>13</sup> As explained *supra* page 6, the Commission contemplated in the Refund Proceeding that additional relief extending prior to (as well as after) October 2000 might later become available if it later were to find that individual sellers acted in violation of California ISO and PX tariffs. The subsequent initiation of seller-specific investigations thus expanded, rather than truncated, the scope of relief available to the California Parties and other customers.

“substitutes” for the Refund Proceeding. Rather, they are wholly separate and apart from the Refund Proceeding as to the matters addressed.<sup>14</sup>

To the extent the Reliant and Duke proceedings are “splinters” of any proceedings, they break off from the Commission’s fact-finding investigation of potential tariff violations that commenced in early 2002, not from the Refund Proceeding. The separateness of proceedings is explicit in the Reliant I, Reliant II and Duke Settlements, and the Commission orders approving the settlements, all of which indicate that Commission approval of the settlements has no bearing on the California Parties’ right to relief in the Refund Proceeding. *See* Reliant I Settlement, 102 FERC ¶ 61,108 at PP 2, 10, ER 2-3, and 103 FERC ¶ 61,019 at P 20, ER 63-64; Reliant II Settlement, 105 FERC ¶ 61,008 at PP 2, 18, ER 133, 135, and 105 FERC ¶ 61,253 at P 2, ER 224; Duke Settlement, 105 FERC ¶ 61,307 at PP 2, 14, 19, ER 226, 228, and 106 FERC ¶ 61,177 at P 2, ER 284. In other words, the California Parties are mistaken in claiming (Pet. Br. 27-28) that the settlement of the Commission’s Reliant and Duke investigations, without their involvement as parties, resulted in the loss of legal rights being adjudicated in the Refund Proceeding.

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<sup>14</sup> For this reason, the Court, in a series of orders over the past year, properly rejected the repeated efforts of the California Parties to consolidate appeals of the Commission’s various investigative orders with appeals of its Refund Proceeding orders pending in Nos. 01-71051, *et al.*

**V. THE COMMISSION AFFORDED THE CALIFORNIA PARTIES DUE PROCESS IN CONSIDERING THEIR EVIDENCE AND OBJECTIONS**

Similarly, the California Parties are mistaken in claiming (Pet. Br. 5, 21-22, 29-34) that the Commission's settlement of the Reliant and Duke investigations, without first admitting them as parties, deprived them of the right to participate or otherwise stripped them of any opportunity to be heard. First, the Commission, in conducting its investigations and ultimately deciding to reach settlements with Reliant and Duke, did consider and analyze the evidence provided by the California Parties. *See* Reliant II Settlement, 105 FERC ¶ 61,008 at PP 10, 14, ER 134. Indeed, Commission staff met with the California Parties to discuss their data, expert testimony, and documentation. *See* Duke Settlement, 105 FERC ¶ 61,307 at P 12 & App. P 10, ER 227, 230. Second, the Commission, while it did not permit the California Parties to participate as formal parties with full rehearing and judicial review rights, did hear their objections to the proposed settlements. *See* Reliant I Settlement, 103 FERC ¶ 61,019 at PP 5-11, ER 62, and 104 FERC ¶ 61,146 at PP 8-12, ER 130; *see also* Reliant II Settlement, 105 FERC ¶ 61,253 at P 4, ER 225 (treating motions to intervene as motions to file comments); Duke Settlement, 106 FERC ¶ 61,177 at P 4, ER 284 (same).<sup>15</sup>

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<sup>15</sup> In addition, the Reliant II and Duke Settlements did not deprive the California Parties of the opportunity to participate fully, as party-intervenors, in other proceedings concerning allegations of improper gaming practices (which



In these circumstances, the Commission's actions represent a reasonable accommodation of competing interests. On the one hand, by denying third-party requests to intervene, the Commission acted to promote the expeditious and final resolution of disputes and a faster refund of substantial monies. On the other hand, the California Parties were able to present their evidence and to voice their comments, which the Commission was able to take into account in reviewing the settlements. *See Reliant I Settlement*, 102 FERC ¶ 61,108 at P 11, ER 3 (finding settlement, under the circumstances presented, to be "fair and reasonable and in the public interest"); *Reliant II Settlement*, 105 FERC ¶ 61,008 at P 26, ER 136 (finding settlement to be an "equitable resolution of this matter"); *Duke Settlement*, 105 FERC ¶ 61,307 at P 17, ER 228 (finding that settlement "provides an equitable resolution of this matter and is in the public interest"). All the California Parties were unable to obtain was the formal status of party-intervenors. *See In re California Power Exchange*, 245 F.3d at 1124 (Commission's choice of a "middle ground" is, "considering the competing interests involved, neither arbitrary nor discriminatory").

Due process requires no more. Two recent cases, both arising in this Court from California energy crisis facts, are particularly instructive. In *State of California v. FERC*, 329 F.3d 700 (9<sup>th</sup> Cir. 2003), the Court held, among other

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were the subject of separate settlement agreements). *See supra* pages 13-14.

things, that the Commission did not deny petitioners their due process rights when it approved expeditiously a corporate reorganization of certain Pacific Gas and Electric Co. affiliates **prior** to receiving motions for interventions (which the Commission initially denied). Observing that due process is assessed “case-by-case based on the total circumstances” presented, *id.* at 711, the Court found that the Commission fully considered petitioners’ evidence and arguments in their motions to intervene and petitions for rehearing – even though the Commission ultimately did not find that evidence and line of argument persuasive. *Id.* at 711-13. In the instant circumstances, the Commission similarly considered fully the evidence and comments of the California Parties and thus, while it did not find them persuasive to upset the proposed settlements or warrant intervention, fully satisfied their due process rights. *See* Reliant I Settlement, 103 FERC ¶ 61,146 at P 13 & n.15, ER 131 (citing *State of California* decision and recognizing case-by-case approach).

In *Southern California Edison Co. v. Lynch*, 307 F.3d 794 (9<sup>th</sup> Cir. 2002), the Court held, among other things, that a district court did not abuse its discretion in denying intervention to certain entities challenging the terms of a settlement. The Court found that the would-be intervenors did not demonstrate a “significant protectable interest” in the proceeding in which they wished to participate; moreover, their concerns were “sufficiently different from the issues in the

underlying action.” *Id.* at 802-03; *see also id.* at 807-08 (due process not denied when another party afforded only one day to comment on settlement). Similarly, here, in approving settlements and denying interventions, the Commission did not deny the California Parties’ the right to litigate any “protectable interest” in the Refund Proceeding, which, as explained above, involves different issues than those in the settled proceedings.

In other words, the Commission did not, as the California Parties claim (at 34), “eviscerate[e]” any party’s right to be heard. The Commission heard from the California Parties in presenting their evidence of market manipulation and objecting to the Reliant and Duke settlements, and it did not upset in any way their ability to continue to pursue claims for relief concerning Reliant’s and Duke actions during all time periods. Any doubt is dispelled by a settlement executed by the California Parties with Duke on July 12, 2004. As explained in the Intervenors’ Brief (at 2 n.4), that settlement resolves all pending issues as to Duke for all time periods, both prior to and after October, 2000.<sup>16</sup> The California Parties thus cannot plausibly argue (*see* Pet. Br. 31) that earlier settlements covered all of

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<sup>16</sup> As of the date of this Brief, the settlement between Duke and the California Parties had not yet been filed with the Commission. As reported, the settlement would return approximately \$172 million to California ratepayers. *See* July 13, 2004 Press Release of California Attorney General Bill Lockyer (also noting that, to that date, the California Parties have negotiated settlements resulting in \$2.1 billion in ratepayer benefits).

Duke's (and Reliant's) conduct prior to October, 2000 or otherwise stripped them of the ability to pursue their claims for relief.

## **VI. THE COMMISSION ACTED CONSISTENTLY WITH PRECEDENT IN DENYING INTERVENTION**

Finally, contrary to the California Parties' argument (Pet. Br. 35-38), the Commission did not depart from precedent in denying motions for intervention in the settled Reliant and Duke proceedings. The fact that the Commission allowed intervention in two other investigative proceedings cited by the California Parties (*Columbia*; *Williams*) does not necessarily mean that the Commission is compelled to allow intervention in all investigative proceedings. The Commission explained that its regulations do not permit intervention in investigative proceedings as a matter of right, but that intervention may be permitted as a matter of discretion. *See* Reliant I Settlement, 103 FERC ¶ 61,019 at PP 14-15, ER 63; *see also supra* pages 19-20 (citing regulations). The Commission distinguished the facts of the few cases in which it has exercised its discretion to permit the intervention of parties that were not targets of investigations, and noted that the exercise of its discretion is a case-by-case decision. *See* Reliant I Settlement, 104 FERC ¶ 61,146 at PP 13-14, ER 131.

Significantly, the California Parties totally disregard the leading precedent governing intervention in Commission investigations of possible tariff violations occurring during 2000-2001. In *Fact-Finding Investigation of Potential Market*

*Manipulation of Electric and Natural Gas Prices*, 105 FERC ¶ 61,063 at P 5 (2003), ER 153, the Commission, after reviewing legal authorities that confer prosecutorial discretion on its conduct of investigations, clarified that it would not admit third parties into its investigations as intervenors “in order to facilitate the timely resolution” of its proceedings. *Id.* at P 5, ER 153. The Commission also clarified that it would treat all motions to intervene as motions to file comments. *Id.* at P 7, ER 153.

In subsequent orders issued in the instant proceedings, the Commission cited that precedent (which the California Parties challenge in other appeals pending in 9<sup>th</sup> Cir. Nos. 03-73887, *et al.*) and followed it exactly. *See* Reliant II Settlement, 105 FERC ¶ 61,253 at P 4, ER 224-25 (noting that the reasoning of that precedent “still stands and is equally applicable here”); Duke Settlement, 106 FERC ¶ 61,177 at P 4, ER 284 (same). Thus, there is no inconsistency with, or departure from, precedent.

### **CONCLUSION**

For the reasons stated, the California Parties’ petitions should either be: (1) dismissed, as they seek review of the Commission’s non-reviewable exercise of discretion in conducting its investigations; or (2) denied, as they seek review of orders that reasonably denied their interventions in order to promote the timely and final settlement of its investigations.

**STATEMENT OF RELATED CASES**

As explained above, *see supra* page 4, appeals of FERC orders issued in the Refund Proceeding are pending in *Public Utilities Commission of the State of California, et al. v. FERC*, 9<sup>th</sup> Cir. Nos. 01-71051, *et al.*

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