

ORAL ARGUMENT HAS NOT YET BEEN SCHEDULED

**IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT**

No. 07-1175

**LOUISIANA PUBLIC SERVICE COMMISSION,
PETITIONER,**

v.

**FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.**

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

**BRIEF FOR RESPONDENT
FEDERAL ENERGY REGULATORY COMMISSION**

**CYNTHIA A. MARLETTE
GENERAL COUNSEL**

**ROBERT H. SOLOMON
SOLICITOR**

**CAROL J. BANTA
ATTORNEY**

**FOR RESPONDENT
FEDERAL ENERGY REGULATORY
COMMISSION
WASHINGTON, D.C. 20426**

JUNE 9, 2008

FINAL BRIEF: JULY 29, 2008

CIRCUIT RULE 28(A)(1) CERTIFICATE

A. Parties and Amici

To counsel's knowledge, the parties before this Court are as stated in Petitioner's Brief. In addition to those parties, the following were parties and intervenors before the Federal Energy Regulatory Commission in Docket Nos. ER03-583, ER03-681, ER03-682, and ER03-744:

FERC Trial Staff
EWO Marketing LP
Entergy Power, Inc.
Entergy Arkansas, Inc.
Entergy Gulf States, Inc.
Entergy Louisiana, Inc. and its successor, Entergy Louisiana, LLC
Entergy Mississippi, Inc.
Entergy New Orleans, Inc.
Calpine Corporation
Suez Energy Marketing NA (successor to Tractebel Energy Marketing, Inc.)

In addition to those listed above, the following were parties and intervenors in the underlying FERC proceedings before the Administrative Law Judge:

Arkansas Cities and Cooperative
Arkansas Electric Cooperative Corporation
Arkansas Electric Energy Consumers, Inc.
Conway Corporation
Dominion Resources Services, Inc.
Dominion Virginia Power
Dynergy Power Marketing
Electric Power Supply Association
InterGen Services
Louisiana Energy Users Group
NRG Companies
Occidental Chemical Corporation
Plum Point Energy Associates, LLC
Sempra Energy Resources
TECO Power Services Corporation
Williams Energy Marketing & Trading Company

B. Rulings Under Review

1. Opinion and Order Affirming In Part And Reversing In Part Initial Decision And Denying Rehearing, Opinion No. 485, *Entergy Services, Inc.*, 116 FERC ¶ 61,296 (2006), R. 528, JA 1; and
2. Opinion and Order on Rehearing and Clarification, Opinion No. 485-A, *Entergy Services, Inc.*, 119 FERC ¶ 61,019 (2007), R. 535, JA 56.

C. Related Cases

This case has not previously been before this Court or any other court. The FERC orders under review here relied in part on previous orders that were recently upheld in relevant part in *Louisiana Public Service Commission v. FERC*, 522 F.3d 378 (D.C. Cir. 2008). Like that case, the instant appeal concerns the allocation of production costs among the Entergy Operating Companies in different states.

Carol J. Banta
Attorney

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GLOSSARY

Affirming Order	Opinion and Order Affirming In Part And Reversing In Part Initial Decision And Denying Rehearing, Opinion No. 485, <i>Entergy Services, Inc.</i> , 116 FERC ¶ 61,296 (2006), R. 528, JA 1
ALJ	Administrative Law Judge
ALJ Decision	Initial Decision, <i>Entergy Services, Inc.</i> , 111 FERC ¶ 63,077 (2005), R. 506, JA 74
Bandwidth Proceeding	FERC proceeding that culminated in Opinion No. 480, establishing “bandwidth remedy” for roughly equalizing production costs in Entergy System
Br.	Petitioner’s brief
Commission or FERC	Federal Energy Regulatory Commission
Entergy	Entergy Corporation (corporate parent of the Operating Companies) or Entergy Services, Inc. (acting on behalf of Operating Companies)
Entergy Louisiana	Entergy Louisiana, LLC or its predecessor, Entergy Louisiana, Inc.
Entergy Operating Company or Companies	Individually or collectively, Entergy Arkansas, Entergy Gulf States, Entergy Louisiana, Entergy Mississippi, and Entergy New Orleans
Entergy System or System	Generation and transmission facilities owned and operated by Entergy Operating Companies in Arkansas, Louisiana, Mississippi, and Texas
FERC Orders	Collectively, the Affirming Order and Rehearing Order under review
FPA	Federal Power Act

GLOSSARY

Louisiana or Louisiana Commission	Petitioner Louisiana Public Service Commission
<i>Louisiana 1999</i>	<i>La. Pub. Serv. Comm'n v. FERC</i> , 174 F.3d 218 (D.C. Cir. 1999)
<i>Louisiana 2008</i>	<i>La. Pub. Serv. Comm'n v. FERC</i> , 522 F.3d 378 (D.C. Cir. 2008)
MW	Megawatt
New Orleans	Council for the City of New Orleans
Opinion No. 480	<i>La. Pub. Serv. Comm'n v. Entergy Corp.</i> , Opinion No. 480, 111 FERC ¶ 61,311, <i>on reh'g</i> , 113 FERC ¶ 61,282 (2005) (issued in Bandwidth Proceeding), <i>aff'd in part and rev'd in part</i> , <i>Louisiana 2008</i>
Rehearing Order	Opinion and Order on Rehearing and Clarification, Opinion No. 485-A, <i>Entergy Services, Inc.</i> , 119 FERC ¶ 61,019 (2007), R. 535, JA 56
River Bend 30	Refers to capacity from Entergy Gulf States's 30 percent interest in the River Bend Nuclear Station
State Regulators	Intervenors Arkansas Public Service Commission and Council for the City of New Orleans, and Mississippi Public Service Commission
System Agreement	Rate schedule that acts as an interconnection and pooling agreement for the Entergy System and provides for the joint planning, construction and operation of new generating capacity
Wholesale Base Load	Refers to Entergy Arkansas's excess base load capacity

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**BRIEF OF RESPONDENT
FEDERAL ENERGY REGULATORY COMMISSION**

STATEMENT OF THE ISSUE

Whether the Federal Energy Regulatory Commission (“Commission” or “FERC”), in affirming the findings of an administrative law judge after hearing, reasonably determined that the allocation of base load generating resources proposed by affiliated operating companies in the Entergy System was just and reasonable and not unduly discriminatory, and did not violate a right of first refusal provision in the Entergy System Agreement.

STATUTORY AND REGULATORY PROVISIONS

The pertinent statutes and regulations are contained in the Addendum to this brief.

INTRODUCTION

This appeal is the latest in a long line of cases concerning the unique arrangement in which five affiliated Entergy Operating Companies, which between them sell electricity in four states and are regulated by several state and local agencies, operate their transmission and generation facilities as a single, highly integrated electric system. Under this arrangement, the companies allocate the costs and benefits of generation resources among themselves, with the goal of roughly equalizing their production costs. This cross-jurisdictional operation and cost allocation affects numerous parties and interests, requiring the Commission to balance competing interests.

The present case arose from the Entergy Operating Companies' entry into several affiliate transactions. Following a five-month evidentiary hearing, the administrative law judge ("ALJ") largely approved those transactions. *See Entergy Services, Inc.*, 111 FERC ¶ 63,077 (2005) ("ALJ Decision"), R. 506, JA 74, *aff'd*,

116 FERC ¶ 61,296 (2006) (“Affirming Order”), R. 528, JA 1, *reh’g denied*, 119 FERC ¶ 61,019 (2007) (“Rehearing Order”), R. 535, JA 56.¹

This appeal concerns only two of the numerous rate issues that were litigated in the FERC proceeding. The ALJ, affirmed by the Commission, determined that the allocation of generation resources to two of the Entergy Operating Companies, intended to reduce their above-average production costs, was just and reasonable and not unduly discriminatory. In particular, the ALJ and the Commission found that the allocation was not unduly discriminatory against a third Operating Company, and did not violate a contractual provision giving Operating Companies a right of first refusal. ALJ Decision at PP 161-210, JA 130-47; Affirming Order at PP 123-34, JA 46-49. Of the numerous parties that participated in the FERC litigation, only the Louisiana Public Service Commission (“Louisiana” or “Louisiana Commission”) has sought judicial review; the other State Regulators² who were involved below support affirmance of the FERC Orders as to allocation.

¹ “R.” refers to a record item. “JA” refers to the Joint Appendix page number. “P” refers to the internal paragraph number within a FERC order.

² For purposes of this case, the Council of the City of New Orleans (“New Orleans”) is included as a “State Regulator” (together with the Arkansas Public Service Commission and the Mississippi Public Service Commission). In Louisiana, jurisdiction over retail electric service is divided between the Louisiana Commission and home-rule cities, such as New Orleans, that regulate utilities within their borders. *See generally New Orleans Pub. Serv., Inc. v. United Gas Pipe Line Co.*, 732 F.2d 452, 460 n.19 (5th Cir. 1984); *State ex rel. Guste v.* (continued...)

STATEMENT OF FACTS

I. Statutory And Regulatory Background

Section 201 of the Federal Power Act (“FPA”), 16 U.S.C. § 824, affords the Commission jurisdiction over the rates, terms, and conditions of service for the transmission and sale at wholesale of electric energy in interstate commerce. *See* 16 U.S.C. § 824(a)-(b). This grant of jurisdiction is comprehensive and exclusive. *See New York v. FERC*, 535 U.S. 1 (2002) (discussing statutory framework, and division between federal and state regulatory authority under the FPA). All rates for or in connection with jurisdictional sales and transmission services are subject to FERC review to assure that they are just and reasonable, and not unduly discriminatory or preferential. FPA § 205(a), (b), (e), 16 U.S.C. § 824d(a), (b), (e).

Council of City of New Orleans, 309 So. 2d 290, 292-93 (La. 1975); Motion for Leave to Intervene of the Council of the City of New Orleans, Case No. 07-1175 (D.C. Cir. filed June 29, 2007) (citing state and local authorities).

Entergy Louisiana is subject to regulation at the retail level by both the Louisiana Commission and New Orleans. Both Entergy Louisiana and Entergy Gulf States provide retail electric service to customers in Louisiana, subject to regulation by the Louisiana Commission, while both Entergy Louisiana and Entergy New Orleans provide such service to customers in portions of New Orleans, subject to regulation by New Orleans. *See State Regulators’ Joint Brief Opposing Exceptions* at 2-3 n.5, R. 524 (filed Nov. 10, 2005).

II. The Entergy System Agreement

A. Background

This case marks the latest episode in decades of litigation about the allocation and equalization of costs under the System Agreement. We begin with an overview of that unusual arrangement. (This Court provided a similar overview of Entergy’s system-planning approach in its recent opinion in *Louisiana Public Service Commission v. FERC*, 522 F.3d 378 (D.C. Cir. 2008) (“*Louisiana 2008*”).³)

The Entergy System comprises five operating companies selling electricity in Arkansas, Louisiana, Mississippi, and Texas: Entergy Arkansas, Inc.; Entergy Louisiana, Inc.⁴; Entergy Mississippi, Inc.; Entergy Gulf States, Inc.⁵; and Entergy New Orleans, Inc. (collectively, the “Operating Companies”). *Louisiana 2008*, 522 F.3d at 383. The Operating Companies are owned by a multistate holding

³ The Court issued its decision a few days after Louisiana filed its opening brief in this case. *See* Br. at 3 (noting pending decision in D.C. Cir. No. 05-1462).

⁴ During the course of the underlying FERC proceeding, Entergy Louisiana, LLC became the successor-in-interest to Entergy Louisiana, Inc. That change is not material to this case, so for convenience this Brief refers to both companies interchangeably as “Entergy Louisiana.”

⁵ Entergy Gulf States sold electricity in both Louisiana and Texas. In 2008, Entergy Gulf States separated into Texas and Louisiana companies. For purposes of this case, however, the FERC orders and this Brief refer to “Entergy Gulf States” as the single company that existed when the ALJ Decision and the FERC Orders were issued.

company, Entergy Corporation. *Id.* (What is now the Entergy System originated under Middle South Utilities, Inc., which owned the Operating Companies' predecessors.)

Entergy⁶ operates the Operating Companies' transmission and generation facilities as a single electric system (the "System"), dispatching generation on a least cost basis system-wide and without regard to ownership. *See La. Pub. Serv. Comm'n v. Entergy Servs., Inc.*, 113 FERC ¶ 61,282 at P 8 (2005), *aff'd in part, Louisiana 2008*. The Entergy System is highly integrated and generation facilities are planned, constructed, and operated for the benefit of the whole system. *See Entergy La., Inc. v. La. Pub. Serv. Comm'n*, 539 U.S. 39, 42 (2003). *See also Middle South Energy, Inc.*, 31 FERC ¶ 61,305, *reh'g denied*, 32 FERC ¶ 61,425 (1985), *aff'd, Miss. Indus. v. FERC*, 808 F.2d 1525 (D.C. Cir.), *vacated and remanded in part*, 822 F.2d 1103 (D.C. Cir. 1987). This pooling arrangement benefits the entire System by lowering energy and capacity costs to customers throughout the System and increasing reliability and efficiencies in operation. *See System Energy Res., Inc.*, 41 FERC ¶ 61,238 at pp.61,622-23 (1987), *on reh'g*, 42

⁶ For purposes of this Brief, "Entergy" refers either to Entergy Corporation, the corporate parent of the Entergy Operating Companies and their affiliates, or to Entergy Services, Inc., which is the Entergy Operating Companies' service affiliate and which acted on behalf of the Operating Companies in the underlying FERC proceeding.

FERC ¶ 61,091 (1988), *aff'd*, *City of New Orleans v. FERC*, 875 F.2d 903 (D.C. Cir. 1989); *see generally Entergy La.*, 539 U.S. at 42.

Transactions among the Entergy Operating Companies are governed by a System Agreement. *Miss. Indus.*, 808 F.2d at 1529. Over its history, Middle South Utilities (Entergy's predecessor) filed three successive System Agreements with the Commission, in 1951, 1973, and 1982. *Id.* The last of those Agreements, as since modified, now governs the Entergy System. *Louisiana 2008*, 522 F.3d at 383.

The Entergy System primarily allocates the costs and benefits of new generation resources through the assignment, by a systemwide operating committee, of new resources to individual Operating Companies, on a rotating basis. *Id.* Each Operating Company assumes the responsibility for financing and bearing the costs of its assigned new generation plant. *Id.* In return for bearing these costs and associated risks, the System Agreement allows an Operating Company and its customers to retain the benefits of the energy produced by units assigned to the Operating Company. *See Miss. Indus.*, 808 F.2d at 1530 & n.7.

The System Agreement allocates the costs of imbalances in the cost of facilities used for the mutual benefit of all the Entergy Operating Companies. *Entergy La.*, 539 U.S. at 42 (“[K]eeping excess capacity available for use by all is a benefit shared by the operating companies, and the costs associated with this

benefit must be allocated among them.”). The System Agreement requires that production costs be roughly equal among the Operating Companies. *Louisiana 2008*, 522 F.3d at 384; *see also Miss. Indus.*, 808 F.2d at 1530 (affirming FERC orders that allocated costs of nuclear generation investments to operating companies in proportion to demand for system energy). Thus, since the first System Agreement in 1951, the System has sought to iron out inequities through “equalization payments.” *Id.* The current System Agreement, filed in 1982, allocates production costs by requiring that “short” companies pay “long” companies.⁷ *See Entergy La.*, 539 U.S. at 42-43. This Court has recognized that “[t]his arrangement is mutually beneficial because companies that are long have a ready outlet for their surplus energy and are thereby compensated for carrying excess capacity, while companies that are short enjoy the benefit of a low cost and dependable way of meeting their energy requirements.” *La. Pub. Serv. Comm’n v. FERC*, 184 F.3d 892, 895 (D.C. Cir. 1999).

⁷ If an Operating Company’s share of the System’s generating capacity is greater than its share of the energy generated and distributed by the system as a whole, the Company is deemed to be “long.” *Miss. Indus.*, 808 F.2d at 1530. If the Operating Company’s share of the system’s generating capacity is less than its percentage of the system’s energy, it is deemed to be “short.” *Id.* The terms “long” and “short” do not refer to the Operating Company’s ability to provide enough energy to meet its customer’s requirements, but rather compare the share of system capacity that it contributes with the share of system energy that it uses. *Id.* n.8.

Because the Entergy System spans four states and involves numerous regulators and other interested parties — and, in particular, because the allocation of costs and resources among the Operating Companies affects retail rates in several jurisdictions — many disputes arising under the System Agreement have come before this Court over the years. *See Middle South Energy, Inc. v. FERC*, 747 F.2d 763 (D.C. Cir. 1984) (filing of 1982 System Agreement); *Miss. Indus.*, 808 F.2d 1525 (allocation of nuclear investment costs); *New Orleans*, 875 F.2d 903 (same, after remand); *City of New Orleans v. FERC*, 67 F.3d 947 (D.C. Cir. 1995) (costs of future replacement capacity after spin-off of generation plants); *La. Pub. Serv. Comm’n v. FERC*, 174 F.3d 218 (D.C. Cir. 1999) (“*Louisiana 1999*”) (determination of Operating Companies’ available capability for purposes of cost equalization); *La. Pub. Serv. Comm’n*, 184 F.3d 892 (allocation of capacity costs); *La. Pub. Serv. Comm’n v. FERC*, 482 F.3d 510 (D.C. Cir. 2007) (same, after remand); *Louisiana 2008* (bandwidth remedy — *see infra* pp. 10-11). The multi-state nature of the Entergy System also has brought cost allocation disputes to the U.S. Supreme Court. *See Entergy La.*, 539 U.S. 39 (preemption of state regulatory jurisdiction as to cost allocation); *Miss. Power & Light Co. v. Miss. ex rel. Moore*, 487 U.S. 354 (1988) (same). The instant appeal arises, yet again, from the Commission’s necessary balancing of the various parties and competing interests affected by the Entergy System.

B. Bandwidth Proceeding (Opinion No. 480 and *Louisiana 2008*)

This Court most recently considered allocation of costs under the Entergy System Agreement in *Louisiana 2008*. That case arose from a separate, earlier FERC proceeding that concerned equalization of production costs under the System Agreement (the “Bandwidth Proceeding”). The Bandwidth Proceeding began when the Louisiana Commission filed a complaint asserting that the cost allocations among the Entergy Operating Companies had become unjust, unreasonable, and unduly discriminatory, to the detriment of ratepayers under the jurisdiction of the Louisiana Commission and to the benefit of ratepayers in other Entergy jurisdictions.

Following an evidentiary hearing, Administrative Law Judge Lawrence Brenner found that the production costs of the Entergy Operating Companies were no longer in rough equalization, due to disparate fuel costs (in particular, the increased costs of natural gas-fired generation, on which Entergy Louisiana relies heavily, in contrast to Entergy Arkansas’s greater reliance on cheaper coal-fueled facilities). Initial Decision, *La. Pub. Serv. Comm’n v. Entergy Servs., Inc.*, 106 FERC ¶ 63,012 at P 25 (2004). Accordingly, the ALJ developed numerical percentage “bandwidths” to establish the outside bounds by which production costs would be permitted to deviate from the System average. *Id.* at PP 43, 50.

On exceptions, the Commission affirmed the ALJ's findings and his use of a bandwidth as a remedial device. Opinion Affirming In Part And Reversing In Part Initial Decision, *La. Pub. Serv. Comm'n v. Entergy Servs., Inc.*, Opinion No. 480, 111 FERC ¶ 61,311 ("Opinion No. 480"), *on reh'g*, 113 FERC ¶ 61,282 (2005). The Commission agreed that the allocation of production costs among the Entergy Operating Companies was no longer just and reasonable, because Entergy Louisiana was, and likely would continue to be well into the future, subject to much higher production costs than the other Operating Companies. Opinion No. 480 at PP 28-30. To remedy that situation, the Commission adopted the ALJ's bandwidth remedy but widened the acceptable range of cost disparities to +/- 11 percent from the System average. *Id.* at PP 136, 144.

On appeal (with Louisiana and some of the State Regulators, as here, taking opposing positions), this Court held that the Commission had jurisdiction to impose the bandwidth remedy and that the remedy was reasonable, supported by substantial evidence, and well within FERC's broad remedial discretion. *Louisiana 2008*, 522 F.3d at 383. (The Court remanded, for further proceedings, only the timing of the Commission's remedial decision. *Id.*)

III. The Commission Proceedings And Orders

A. ALJ Decision

The instant case began with Entergy's filing in early 2003, for Commission approval under FPA § 205, 16 U.S.C. §824d, of eight power purchase agreements for sales of electric power and associated capacity from certain Entergy subsidiaries (including Entergy Gulf States and Entergy Arkansas) to Entergy Louisiana and Entergy New Orleans. *See* Initial Decision, *Entergy Services, Inc.*, FERC Docket Nos. ER03-583, *et al.*, 111 FERC ¶ 63,077 at PP 1-3 (2005) ("ALJ Decision"), R. 506, JA 74, 75-76. More than 30 parties participated in the consolidated FERC proceedings concerning the eight power purchase agreements. *See* Record Index. Much of the ensuing FERC proceeding centered on the propriety of such affiliate transactions, and compliance with FERC's standards regarding affiliate abuse, which are not at issue in this appeal. *See, e.g.*, ALJ Decision at PP 7-160, JA 77-130.

Of relevance here, the Louisiana Commission protested the allocation of low-cost generation resources under four of the power purchase agreements to Entergy Louisiana and Entergy New Orleans, arguing that such allocation was unduly discriminatory against Entergy Gulf States, which should have been assigned some of the low-cost capacity. *See id.* at PP 165, 167, JA 131. Two of the agreements provided for Entergy Arkansas to sell wholesale base load capacity

(“Wholesale Base Load”), from relatively low-cost, solid fuel resources (coal and nuclear). *Id.* at P 161, JA 130. Starting in 2003, Entergy Arkansas had 220 MW of available low-cost Wholesale Base Load capacity, of which it would sell 110 MW each to Entergy New Orleans and Entergy Louisiana. *Id.* The other two agreements involved long-term, life-of-unit power transactions of capacity and associated energy from Entergy Gulf States’s 30 percent interest in the River Bend Nuclear Station (“River Bend 30”), totaling about 300 MW. *Id.* at P 163, JA 131. Entergy assigned 200 MW of that capacity to Entergy Louisiana and 100 MW to Entergy New Orleans. *Id.*

Accordingly, these four power purchase agreements, totaling 520 MW of capacity, were assigned as follows:

	Entergy Louisiana	Entergy New Orleans
Wholesale Base Load 220 MW total (sold by Entergy Arkansas)	110 MW	110 MW
River Bend 30 300 MW total (sold by Entergy Gulf States)	200 MW	100 MW
Total	310 MW	210 MW

See ALJ Decision at P 164, JA 131. The Louisiana Commission argued that some of this low-cost capacity should have been assigned to Entergy Gulf States. *See id.* at P 167, JA 131.

Judge Brenner, the same ALJ who had presided over the Bandwidth Proceeding, held a hearing (on all issues) in the consolidated proceedings that began on June 28, 2004 and ended on December 1, 2004, developing an evidentiary record that included nearly 13,000 pages of hearing transcripts and approximately 670 exhibits. *See id.* at P 5, JA 77. Following post-hearing briefing, Judge Brenner issued the 77-page ALJ Decision on June 30, 2005. That Decision addressed numerous issues, most prominently the affiliate transaction issues at the center of the case. *Id.* at PP 7-160, JA 77-130. Of relevant concern to the narrow issues now on appeal, the ALJ determined that Entergy's proposed allocation of base load resources was just and reasonable and not unduly discriminatory. *Id.* at PP 161-210, JA 130-47; *see also infra* Argument, Part II.A. The ALJ also found that Louisiana's proposed alternative allocation of resources was unjust and unreasonable. ALJ Decision at PP 167-85, JA 131-39; *see also infra* Argument, Part II.B. The ALJ also found that Entergy's allocation did not violate the right of first refusal provision in § 3.05 of the System Agreement. ALJ Decision at PP 174-82, JA 134-37; *see also infra* Argument, Part III.

In August and November 2005, Louisiana, the State Regulators, Entergy, FERC Staff, and other parties filed before the Commission briefs on and/or opposing exceptions to the ALJ Decision. *See* R. 510 to R. 514, R. 520 to R. 525.

B. Affirming Order

On September 27, 2006, the Commission issued its Opinion and Order Affirming In Part And Reversing In Part Initial Decision And Denying Rehearing, Opinion No. 485, *Entergy Services, Inc.*, 116 FERC ¶ 61,296 (2006) (“Affirming Order”), R. 528, JA 1. Much of the Affirming Order focused, as had the ALJ Decision, on the standards for affiliate transactions, including the Commission’s examination of the request for proposal process that resulted in four of the eight power purchase agreements. Specifically, the Commission affirmed the ALJ’s findings that the design and implementation of the process were adequate to ensure just and reasonable rates and did not constitute affiliate abuse, and the ALJ’s determination that six of the agreements were just and reasonable and not unduly discriminatory. Affirming Order at PP 2-4, 19-122, JA 5-6, 11-45.⁸ The Commission also affirmed the ALJ’s finding that two of the contracts were unjust,

⁸ The Commission reversed the ALJ Decision in part by limiting the term of two of the contracts, for reasons not relevant here. *See* Affirming Order at PP 67-74, JA 27-29. This Brief nevertheless refers to the opinion as the “Affirming Order” because, as to the only issues raised on appeal, the Commission affirmed the ALJ Decision.

unreasonable, and unduly discriminatory, and constituted affiliate abuse, because Entergy improperly used confidential bid information in pricing those agreements. *Id.* at PP 3, 75-82, JA 5, 29-32.

The Commission then turned to Louisiana's arguments about the allocation of the River Bend 30 and Wholesale Base Load agreements and the right of first refusal, which the Commission viewed (as had the ALJ) as two facets of the same allocation issue. *See id.* at P 18 (identifying allocation issue as one of five "miscellaneous issues" addressed on exceptions), JA 10. The Commission affirmed the ALJ's allocation findings in all respects. *See id.* at P 5 ("With respect to the remaining issues, we summarily affirm the presiding judge's findings in the [ALJ Decision] for the reasons set forth herein and deny the exceptions on those remaining issues."), JA 6; *id.* at P 18, JA 10.

First, the Commission affirmed the ALJ's approval of Entergy's allocation of capacity as reasonable. *Id.* at P 128, JA 47. Moreover, to the extent that those allocations might not achieve rough production cost equalization, the bandwidth remedy developed in Opinion No. 480 (later upheld by this Court) would ensure cost equalization. *Id.* The Commission also affirmed the ALJ's rejection of Louisiana's proposed alternative allocation, which both the ALJ and the Commission found would run counter to the goal of rough equalization. *Id.* (citing ALJ Decision at P 185, JA 137-39), JA 47-48.

Second, the Commission affirmed the ALJ's finding that the right of first refusal under § 3.05 of the System Agreement was not triggered by the one-month capacity sales. Affirming Order at P 134, JA 49. In any event, even assuming *arguendo* (as did the ALJ) that the right was triggered, § 3.05 "does not give any guidance on how an operating company's surplus capacity [should] be apportioned among the other operating companies." *Id.* But "the most important goal is to keep the operating companies within rough production cost equalization." *Id.*

Only Louisiana and Entergy requested rehearing. R. 530 (Louisiana), JA 304; R. 529 (Entergy) (seeking rehearing on issues not raised in this appeal).

C. Rehearing Order

On April 5, 2007, the Commission issued its Opinion and Order on Rehearing and Clarification, Opinion No. 485-A, *Entergy Services, Inc.*, 119 FERC ¶ 61,019 (2007) ("Rehearing Order," and together with the Affirming Order, the "FERC Orders"), R. 535, JA 56. In addition to addressing various arguments of Louisiana and Entergy that are not at issue in this appeal (*id.* at PP 12-34, 51-58, JA 60-66, 71-73), the Commission reaffirmed its analysis of the ALJ's findings regarding allocation.

The Commission again concluded that § 3.05 of the System Agreement was not triggered by the one-month capacity sales, based on both the language and purpose of § 3.05. Rehearing Order at PP 39-42, JA 67-68. Moreover, even

assuming that the short-term sales had given rise to a right of first refusal, nothing in § 3.05 indicated that Entergy Gulf States and Entergy Louisiana would be exclusively entitled to exercise that right. *Id.* at P 43, JA 68.

The Commission also found nothing new in Louisiana's arguments concerning the allocation of base load generating resources. The Commission thus reaffirmed its conclusion that the ALJ properly rejected Louisiana's alternative allocation proposal and that the bandwidth remedy established in Opinion No. 480 would ensure rough production cost equalization. *Id.* at P 49-50, JA 70-71.

This petition followed.

SUMMARY OF ARGUMENT

The Commission reasonably affirmed the administrative law judge's approval of the Entergy power purchase agreements, including the allocation of base load generation resources among Entergy companies operating in different jurisdictions. The Commission's cost allocation decision is based on substantial record evidence, reflects a reasonable reading of applicable tariff provisions, is responsive to the arguments of the parties, and is thus worthy of judicial respect under the applicable standard of review.

The Louisiana Commission protested Entergy's allocation of low-cost resources to Entergy Louisiana and Entergy New Orleans, to the perceived detriment of Entergy Gulf States. But the ALJ reasonably determined, and the Commission agreed, that the allocation was just and reasonable and not unduly discriminatory. The judge, having already overseen extensive litigation in the Bandwidth Proceeding concerning the rough equalization of production costs under the Entergy System Agreement, conducted another lengthy, multi-party hearing on transactions among Entergy affiliates. Based on that record, the ALJ determined that the allocation of low-cost generation resources to Entergy Louisiana and Entergy New Orleans was appropriate because those Operating Companies had the highest percentages of production costs relative to the System average, and the allocated capacity would reduce those costs. The ALJ concluded,

and the Commission agreed, that the allocation did not unduly discriminate against Entergy Gulf States because the benefit to Entergy New Orleans was proportionately greater than the disadvantage to Entergy Gulf States, whose relative production costs remained within the allowed +/- 11 percent bandwidth (recently upheld by this Court in *Louisiana 2008*) around the System average.

Moreover, the ALJ and the Commission reasonably concluded that the allocation of the power purchase agreements did not violate the System Agreement. The agreements, in which both the sellers and the buyers were Entergy Operating Companies, did not trigger the right of first refusal provided in § 3.05 of the System Agreement because they were not off-System transactions. And even if that provision were applicable, the ALJ and Commission reasonably found that § 3.05 does not dictate which Entergy Operating Companies must be afforded the right of first refusal, nor how capacity should be apportioned among them.

The ALJ and the Commission also properly concluded that the earlier short-term, off-System opportunity sales did not trigger a right of first refusal for the long-term, within-System power purchase agreements that were before the Commission in this case. Nevertheless, the ALJ and the Commission considered those earlier sales and reasonably determined that such short-term sales do not trigger the right of first refusal because they do not affect the long-term availability

of base load capacity that § 3.05 is designed to ensure for the Entergy Operating Companies.

ARGUMENT

I. STANDARD OF REVIEW

The Court reviews FERC orders under the Administrative Procedure Act's arbitrary and capricious standard. *See, e.g., Sithe/Independence Power Partners v. FERC*, 165 F.3d 944, 948 (D.C. Cir. 1999). A court must satisfy itself that the agency "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)).

The Commission's factual findings are conclusive if supported by substantial evidence. FPA § 313(b), 16 U.S.C. § 825l(b). The substantial evidence standard "requires more than a scintilla, but can be satisfied by something less than a preponderance of the evidence." *Louisiana 2008*, 522 F.3d at 395 (quoting *FPL Energy Me. Hydro LLC v. FERC*, 287 F.3d 1151, 1160 (D.C. Cir. 2002)). Substantial evidence means "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 477 (1951) (internal quotation marks and citation omitted); *accord*

Consol. Oil & Gas, Inc. v. FERC, 806 F.2d 275, 279 (D.C. Cir. 1986). If the evidence is susceptible of more than one rational interpretation, the Court must uphold the agency’s findings. See *Consolo v. Fed. Mar. Comm’n*, 383 U.S. 607, 620 (1966); accord, *Fla. Mun. Power Agency v. FERC*, 315 F.3d 362, 368 (D.C. Cir. 2003) (“The question we must answer . . . is not whether record evidence supports [petitioner]’s version of events, but whether it supports FERC’s.”). In a case that “calls upon FERC to make fact-intensive judgment calls on the basis of its superior technical expertise, [the Court] will only disturb FERC’s selection of one methodology over another if its choice is not the product of reasoned decisionmaking.” *Louisiana 2008*, 522 F.3d at 392.

The Commission’s decisions regarding rate issues are entitled to broad deference, because of “the breadth and complexity of the Commission’s responsibilities.” *Permian Basin Area Rate Cases*, 390 U.S. 747, 790 (1968); see also *Mo. Pub. Serv. Comm’n v. FERC*, 215 F.3d 1, 3 (D.C. Cir. 2000).

Additionally, under the *Chevron* standard, this Court gives substantial deference to the Commission’s interpretation of filed tariffs even where the issue simply involves the proper construction of language. See *Koch Gateway Pipeline Co. v. FERC*, 136 F.3d 810, 814 (D.C. Cir. 1998).

II. THE COMMISSION REASONABLY AFFIRMED THE ALJ'S APPROVAL OF ENTERGY'S CAPACITY ALLOCATION AS JUST AND REASONABLE

The Commission did not, as Louisiana contends (Br. 39-40), simply accept Entergy's allocation and rely on the bandwidth remedy to ensure rough equalization of costs. To the contrary, the ALJ, affirmed by the Commission, thoroughly considered Entergy's proposed allocation on its merits and found it to be just and reasonable and not unduly discriminatory, and sensible in the context of the System Agreement's goal of equalizing costs. The ALJ also carefully considered, and rejected, Louisiana's proposed alternative allocation, finding it unjust and unreasonable, and the Commission agreed. Only after completing that extensive analysis did the ALJ note, with the Commission's later approval, that the bandwidth remedy would also ensure that the Operating Companies' costs would remain roughly equal.

A. The Commission Properly Affirmed The ALJ's Determination That Entergy's Allocation Was Reasonable And Not Unduly Discriminatory

1. The ALJ And The Commission Reasonably Analyzed Entergy's Proposed Allocation

The key finding of the ALJ was that the allocation of the four power purchase agreements to Entergy Louisiana and Entergy New Orleans (one each for low-cost River Bend 30 capacity and one each for low-cost Wholesale Base Load capacity) was just and reasonable and not unduly discriminatory. The ALJ's

analysis, affirmed by the Commission, was thorough, well-reasoned, and supported by substantial evidence in the record.

The ALJ properly emphasized that, in allocating capacity among the Operating Companies, “the most important goal is to bring or keep the Operating Companies within rough production cost equalization.” ALJ Decision at P 186 (agreeing with testimony of FERC Staff witness), JA 139; *see also id.* at P 187 (citing support of allocation by State Regulators for same reason), JA 139. *Accord*, Affirming Order at P 128, JA 47-48.

Entergy New Orleans and Entergy Louisiana were the highest above the System average among the Operating Companies in 2001 and 2002. ALJ Decision at P 161, JA 130. Entergy New Orleans, with the highest relative production costs of any of the Operating Companies (*id.* at P 191, JA 140), was 26 percent above the System average for 2001 and 12 percent above for 2002; Entergy Louisiana was 10 and 11 percent above the System average for those same years. *Id.* at P 190 (citing data established in Bandwidth Proceeding), JA 140. (By contrast, Entergy Gulf States had costs that were exactly the System average for those years. *Id.*) For that reason, the State Regulators supported the allocation because they believed it would allow Entergy New Orleans and Entergy Louisiana to move closer to the System average. *Id.* at P 165, JA 131. (Indeed, both of those companies were projected to remain above the System average even with the

power purchase agreements. *Id.* at P 188, JA 139-40.) The ALJ agreed, concluding that, “[a]t the time decisions were made by Entergy on the allocation of the [power purchase agreements] at issue here, and even today, it made sense to try to drive down [Entergy New Orleans’s] and [Entergy Louisiana’s] high relative production costs as they were by far the highest cost companies.” *Id.* at P 205, JA 145.

The ALJ and the Commission recognized that allocation of resources in the Entergy System is, in a sense, a zero-sum situation: while operating all facilities as an integrated System benefits customers of all of the Operating Companies, assigning lower cost capacity to one Operating Company to reduce its relative production costs will necessarily affect the relative costs of Operating Companies that do not receive that capacity. *See* ALJ Decision at P 193, JA 141; Affirming Order at P 123 (“This [allocation] has the effect of somewhat increasing the total production costs of the operating companies now enjoying relatively lower total production costs.”), JA 46. A similar trade-off was at stake in *Louisiana 1999*, where Entergy’s decision to include certain reserve units in determining available capacity benefited Entergy Arkansas and Entergy New Orleans (which had relatively more such units and thus increased their available capacity) but disadvantaged Entergy Mississippi and Entergy Louisiana. 174 F.3d at 222, 224. This is “the nature of the System,” in which the Entergy Operating Companies are “collaborators . . . functioning for their mutual benefit,” but with consequences of

cost-shifting for retail ratepayers. *Louisiana 2008*, 522 F.3d at 394 (emphasis omitted).

In such cases, the Commission is uniquely qualified to balance the competing interests of parties such as the Louisiana Commission, which understandably focuses on the interests of Entergy Gulf States and Entergy Louisiana and the Louisiana ratepayers they serve, and the other State Regulators, each of whom is similarly concerned with one or two of the five Operating Companies. Indeed, this Court has recognized that, with regard to cost allocation among the Entergy Operating Companies, FERC “is perhaps in the best position to reach the most equitable result and to act in the public interest, rather than to be controlled by the necessarily parochial concerns of the States.” *Miss. Indus.*, 808 F.2d at 1549 (internal quotation marks and citation omitted).⁹ *See also Louisiana 1999*, 174 F.3d at 227 (deferring to FERC’s expertise in weighing System benefits and costs to ratepayers in various jurisdictions); *New Orleans*, 875 F.2d at 905-06 (deferring to FERC’s finding that allocation of nuclear investment costs to all Operating Companies was justified by indirect benefits to all).

⁹ *Cf. Miss. Power & Light*, 487 U.S. at 390 (Brennan, J., dissenting) (“[I]t makes a great deal of sense to read the [FPA] as allowing FERC to exercise jurisdiction over the allocation of costs among interstate pool members because otherwise every state commission would have a parochial incentive to claim that the costs must be imposed on the utilities located in other States. A neutral federal mediator is needed.”).

In any event, the impact on relative costs is not symmetrical in this case, as Louisiana implies (*see* Br. 40-41, 45). Because Entergy New Orleans (the smallest Operating Company) is substantially smaller than Entergy Gulf States (the largest), the effect of allocating capacity to one does not have a proportional impact on the other. In fact, the impact ratio is 6:1, “meaning that in moving resources around on the Entergy System, every one percent reduction in production costs for [Entergy Gulf States] results in a 6 percent increase in production costs for [Entergy New Orleans]” — and vice versa. ALJ Decision at PP 170, 193, 202 (citing testimony and data from Bandwidth Proceeding), JA 133, 141, 144.

For that reason, the ALJ specifically determined that the allocation did not unduly discriminate against Entergy Gulf States. He acknowledged that the allocation, in effect, transferred costs from Entergy New Orleans to Entergy Gulf States. *Id.* at P 193 (“This transfer of costs is apparently true.”), JA 141. Those Operating Companies did not, however, “switch[] positions.” Br. 45. Because of the 6:1 impact ratio, the ALJ agreed with the State Regulators that the direct correlation argued by Louisiana is “mathematically impossible.” ALJ Decision at P 201, JA 143. *See also id.* at P 202 (noting other factors, such as increases in fuel costs, that caused or contributed to the increase in Entergy Gulf States’s relative costs).

This Court has long understood that, under the Entergy System’s rough equalization standard, cost disparities will exist and will not necessarily constitute undue discrimination. *See Louisiana 2008*, 522 F.3d at 393 (“FERC could have done more to eliminate cost disparities within the System, but it need not have done more to eliminate *undue* disparities.”); *Miss. Indus.*, 808 F.2d at 1565 (holding it was enough that the Commission took action “sufficient to remedy the *undue* discrimination on the System; that is, the Commission could properly conclude that the remaining cost disparities do not constitute unlawful discrimination[.]”), *quoted in Louisiana 2008, supra*.

In Louisiana’s view, Entergy discriminates against Operating Companies with low production costs by “transferring” others’ higher costs, through preferential assignment of lower-cost resources. *See Br. 39, 46-47*. Here, Louisiana contends that the allocation of low-cost coal and nuclear capacity to Entergy New Orleans, as a means to reduce the latter’s high production costs (due to its reliance on gas), amounts to a discriminatory transfer of Entergy New Orleans’s high costs to other Operating Companies. *Br. 40-41*. But that is precisely how the System Agreement works — any allocation of costs might temporarily advantage one Entergy Operating Company in one state, to the relative disadvantage of another Operating Company in another state, but, within the range of “rough equalization,” not *unduly* so. To the extent that Louisiana contends that

Entergy's use of resource allocation to equalize costs is a "perverted" effect of the System Agreement (Br. 48), Louisiana's argument is yet another attack on the longstanding (and repeatedly upheld) equalization mechanism itself. *Cf. Louisiana 2008*, 522 F.3d at 393-94 (rejecting Louisiana's argument in favor of a narrower bandwidth); 10/13/04 Hrg. Tr. 9133:7-10 (testimony of FERC Staff witness John Sammon) (fact that resource allocation lowers one company's production costs by requiring other companies to pay for its higher-cost resources is "just the result of the philosophy of the System Agreement that says an Operating Company . . . has first call on the cheapest energy produced by the units it owns[]"), JA 144.

Furthermore, the assignment of 520 MW under the four power purchase agreements was not the only opportunity for resource allocation. Entergy identified additional tranches of low-cost Wholesale Base Load capacity that would be made available to other operating companies in subsequent years (200 MW in 2006 and 108 MW in 2009). ALJ Decision in PP 162, 205, JA 131, 145. Of that capacity, Entergy planned to assign 100 MW to Entergy Gulf States in 2006, and the entire 108 MW in 2009. *Id.* at P 205, JA 145. (Entergy planned to assign the other 100 MW available in 2006 to Entergy Mississippi. *Id.*) That capacity would likely reduce Entergy Gulf States's relative production costs in future years. *Id.*

Based on this analysis of the purpose of the System Agreement and the projected and actual impact on rough equalization of production costs across the Entergy System and, in particular, as between certain Operating Companies, the ALJ reasonably determined that Entergy's proposed allocation was just and reasonable and not unduly discriminatory against Entergy Gulf States. The Commission summarily affirmed the ALJ's determination as to allocation, and specifically adopted and endorsed his analysis as reasonable. Affirming Order at PP 5, 128, JA 6, 47; *see also id.* at PP 123-27, JA 46-47. *See generally Louisiana 2008*, 522 F.3d at 392 (Court defers to Commission's fact-intensive judgments if reasoned decisionmaking); *Sierra Pac. Power Co. v. FERC*, 793 F.2d 1086, 1088 (9th Cir. 1986) (FERC's conclusions on conflicting economic issues must be upheld so long as reasonable and based on evidence) (citing *City of Cleveland v. FPC*, 525 F.2d 845, 849 n.36 (D.C. Cir. 1976)). Louisiana argues that the Commission abdicated its duty by not conducting its own analysis. Br. 40. But in these circumstances, where the Commission set the matter for hearing, the ALJ conducted a thorough, fact-intensive inquiry, and the Commission found no fault with his reasoning, the Commission was not required to revisit the matter. *See, e.g., Pub. Serv. Comm'n of Ky. v. FERC*, 397 F.3d 1004, 1009 (D.C. Cir. 2005) (holding Commission adequately addressed issue where it reviewed and adopted ALJ's extensive analysis); *see also Louisiana 2008*, 522 F.3d at 392 (upholding

Commission’s determination that relied on ALJ Brenner’s analysis of competing methodologies).

2. The ALJ And The Commission Appropriately Considered The Production Cost Bandwidth

Louisiana also objects that the Commission referred to the bandwidth remedy adopted in Opinion No. 480 and upheld by this Court in *Louisiana 2008*; Louisiana argues that the Commission carelessly relied on that remedy to ensure rough equalization of costs, in lieu of reviewing Entergy’s initial allocation of resources. Br. 39-40. But the Commission cited the bandwidth remedy only as “an insurance policy” (Br. 39), consistent with the policy set forth in Opinion No. 480, 111 FERC ¶ 61,311 at P 44.

The ALJ discussed the bandwidth remedy — which the same ALJ had developed in the Bandwidth Proceeding — both as a reference point for analyzing the different allocations proposed by Entergy and Louisiana and as a backup mechanism to keep production cost disparities in check if the initial allocation failed to do so in the short term. In considering allocation, the ALJ suggested that the effects on relative production costs would not constitute discrimination so long as the Operating Companies remained within the +/-11 percent band: “Percentage cost disparities among the Operating Companies would be tolerable so long as the cost percentages were within the bandwidth. . . . Consequently, when the Operating Companies are within the numerical bandwidth and thus roughly

equalized, there is no undue discrimination among them.” ALJ Decision at P 192, JA 140; *see generally Miss. Indus.*, 808 F.2d at 1565; *supra* p. 28. Using that benchmark, the ALJ noted that the increase in Entergy Gulf States’s relative costs (even assuming the increase were attributable to the assignment of generation resources to Entergy New Orleans) to +7.80 percent over System average remained within the permissible bandwidth, and thus not unduly discriminatory. ALJ Decision at P 206, JA 145.

Additionally, the ALJ pointed to the bandwidth remedy, not as a substitute for the searching analysis of the initial allocation, but as a means to guard against short-term inequities that might occur in long-term allocations:

Direct assignment of power like this may be necessary to insure that all Operating Companies stay within rough equalization, but long-term allocations can have lumpy effects in the short-term on relative production costs. That is one reason why, *in addition to* [the] *best allocation attempts* [based on] *what is known at the time of decision*, a tariff bandwidth remedy like the one I ordered in the previous [Bandwidth P]roceeding is needed for finer tuning over shorter time periods and for insurance that there will be a reasonable brake on the potential divergence of relative production[] costs among the Operating Companies.

Id. at P 205 (emphasis added), JA 145.

The Commission likewise referenced the bandwidth remedy only as a backstop — the very purpose it was designed to serve. Having reviewed and affirmed the ALJ’s extensive analysis of Entergy’s allocation, the Commission added that, to the extent the allocations of the four power purchase agreements

presented in this case do not actually achieve rough production cost equalization among the Entergy Operating Companies as intended, then the remedy developed in the Bandwidth Proceeding (and upheld by this Court) would ensure such equalization. Affirming Order at P 128, JA 47; Rehearing Order at P 49, JA 70-71.

B. The Commission Reasonably Affirmed The ALJ's Rejection Of Louisiana's Alternative Allocation

Though the question in the underlying FERC proceeding was whether the power purchase agreements submitted by Entergy were just and reasonable and not unduly discriminatory, the ALJ and the Commission also fully considered Louisiana's alternative allocation proposal and explained why it would not be just and reasonable. Louisiana has not challenged the Commission's rejection of that alternative proposal on appeal; nevertheless, the ALJ's analysis of Louisiana's proposal was intertwined with his consideration of Entergy's allocation.

In the proceeding before the ALJ, Louisiana's witness, Stephen J. Baron, advocated assigning some of the excess low-cost capacity to Entergy Gulf States and allocating the capacity based on the relative load responsibility of each of the buyers. *See* ALJ Decision at PP 169-74, JA 132-34. As the ALJ explained, Louisiana's proposal "would drastically change" the assignment of capacity, by allocating both the Wholesale Base Load capacity and the River Bend 30 capacity among three of the Operating Companies — Entergy Gulf States as well as

Entergy Louisiana and Entergy New Orleans — based on relative load responsibility. *Id.* at P 169, JA 132-33. Under Louisiana’s methodology, nearly all of the available capacity would be allocated to Entergy Louisiana and Entergy Gulf States, leaving *only 14 MW* for Entergy New Orleans. *Id.*; *see also id.* at P 182 (noting that Louisiana “skew[ed] the allocations to its jurisdictional Operating Companies,” Entergy Louisiana and Entergy Gulf States, at the expense of an Operating Company it does not regulate — Entergy New Orleans), JA 136-37. *Cf. generally supra* p. 26 (citing this Court’s observation about “the necessarily parochial concerns of the States,” *Miss. Indus.*, 808 F.2d at 1549).

The ALJ was particularly disturbed by the potential impact on Entergy New Orleans. Due to the 6:1 impact ratio explained *supra* at p. 27, “shifting megawatts from [Entergy New Orleans]” — from 210 MW under Entergy’s proposal to a mere 14 MW under Louisiana’s — “has a large cost impact on New Orleans ratepayers.” ALJ Decision at P 170, JA 133. Indeed, Louisiana’s proposed allocation “would have a disproportionately negative impact on [Entergy New Orleans],” increasing the latter’s production costs by 5 to 6 percent for every 1 percent reduction to Entergy Gulf States’s costs. *Id.* at P 194, JA 141.

More important, the ALJ found, and the Commission agreed, that the allocation Louisiana proposed would actually thwart the System Agreement’s requirement of rough equalization: “To benefit [Entergy Gulf States] . . . [Entergy

New Orleans] would be placed much further from System average” *Id.*

Entergy Louisiana also would be disadvantaged, with some of its share of capacity reallocated to benefit Entergy Gulf States. *Id.* at P 195 (“[N]ot only is [Entergy Louisiana] far above System average, but [the Louisiana Commission’s] allocation would worsen [its] situation.”), JA 141. In fact, the ALJ concluded that, under the Louisiana Commission’s preferred allocation, Entergy Louisiana’s relative production costs might rise above +11 percent, outside the bandwidth set by the Commission, requiring other Operating Companies to give it equalization payments. *Id.*, JA 141-42; *see also id.* at P 190 (showing that even with Entergy’s allocation in place, Entergy Louisiana was projected to rise to +12 percent for 2003 and remain the highest in the System through 2005), JA 140; *id.* at P 198 (showing Entergy Louisiana rose to +17 to +19 percent through 2004), JA 143.

For those reasons, Louisiana’s proposal was not consistent with the System Agreement or the standards of FPA § 205:

The overarching important point on why [Louisiana’s] allocation proposal using load responsibility is unjust and unreasonable is that it runs counter to the goal of at least roughly equalizing the production costs of the Operating Companies to eliminate discrimination. . . . [Louisiana’s] recommendation does not bring the Operating Companies closer to System average production cost[.]

ALJ Decision at P 185 (quoting testimony of FERC Staff witness that Louisiana’s proposal would not bring Operating Companies closer to average System costs), JA 137-39; *accord*, Affirming Order at P 128 (“[W]e agree with the presiding

judge that the Louisiana Commission’s alternative allocation proposal ‘runs counter to the goal of at least roughly equalizing the production cost of the operating companies to eliminate discrimination.’”), JA 47-48; Rehearing Order at P 50, JA 71.

III. THE COMMISSION REASONABLY AFFIRMED THE ALJ’S DETERMINATION THAT THE ALLOCATION DID NOT VIOLATE THE SYSTEM AGREEMENT

Section 3.05 of the Entergy System Agreement provides as follows:

It is the long term goal of the Companies that each Company have its proportionate share of Base Generating Units available to serve its customers either by ownership or purchase. Any Company which has generating capacity above its requirements, which desires to sell all or any portion of such excess generating capacity and associated energy, shall offer the right of first refusal for this capacity and associated energy to the other Companies under Service Schedule MSS-4 Unit Power Purchase.

Ex. ETR-188 at 14, R. 738, JA 395. *See also* ALJ Decision at P 176 (“The purpose of Section 3.05 is to give the remaining Operating Companies the opportunity to purchase surplus capacity from another Operating Company at a cost-based rate prescribed in [the System Agreement].”), JA 135.

Louisiana first raised § 3.05 to support its alternative allocation proposal, arguing that the right of first refusal required excess capacity to be apportioned among Operating Companies based on relative load responsibility. *See* ALJ Decision at P 171, JA 133-34; *supra* p. 33. The ALJ and the Commission appropriately considered the issue primarily in that context. Louisiana, however,

also contended that certain earlier transactions, between Entergy Arkansas and various non-Entergy third parties, violated the System Agreement because Entergy Arkansas sold excess capacity on the wholesale market without first offering it to the other Entergy Operating Companies. ALJ Decision at P 177, JA 135. The ALJ and Commission properly found that those previous short-term sales had not triggered a right of first refusal as to the power purchase agreements between Entergy Operating Companies that were actually before the Commission, but nevertheless went on to address the applicability of § 3.05 to those prior non-affiliate sales.

On appeal, that peripheral issue has become the centerpiece of Louisiana's argument. As discussed below, Louisiana does not even address the key conclusion of the ALJ and the Commission: that the right of first refusal does not require Entergy to allocate the low-cost Wholesale Base Load and River Bend 30 capacity among all Operating Companies that are interested in buying such capacity, or to allocate that capacity according to relative load responsibility.

A. The Commission Reasonably Determined That The Affiliate Power Purchase Agreements Did Not Trigger The Right Of First Refusal Under § 3.05 Of The System Agreement

As discussed above, Louisiana argued in the FERC proceeding that Entergy should have allocated some of the low-cost capacity sold under the power purchase agreements to Entergy Gulf States. *See* ALJ Decision at P 171, JA 133-34.

Louisiana contended that the right of first refusal in § 3.05 of the System Agreement required Entergy Arkansas to offer the 220 MW of Wholesale Base Load capacity to all of the Entergy Operating Companies, not just to Entergy Louisiana and Entergy New Orleans. *See* Louisiana Rehearing Request at 13, JA 316; *see also* § 3.05 (Operating Company that desires to sell excess capacity “shall offer the right of first refusal . . . to the other Companies”).¹⁰

Before the ALJ, the relevance of § 3.05 stemmed from the proposal of Louisiana witness Baron to allocate the Entergy Arkansas Wholesale Base load capacity based on the relative load responsibility of each of the potential buyers. *See supra* Part II.B; ALJ Decision at P 171, JA 133-34. Mr. Baron conceded that § 3.05 does not address the allocation of excess capacity, but contended that the principles underlying the System Agreement suggested that relative load responsibility was an appropriate mechanism for allocation. *Id.*

But the ALJ, affirmed by the Commission, reasonably concluded that the inter-affiliate power purchase agreements did not trigger the right of first refusal because they did not involve sales outside the Entergy System: “Section 3.05 does not apply to a sale like the [Entergy Arkansas Wholesale Base Load power

¹⁰ Louisiana’s argument regarding § 3.05 applies only to the Entergy Arkansas agreements to sell Wholesale Base Load capacity, as Louisiana witness Baron acknowledged that the River Bend 30 capacity is unregulated and not subject to § 3.05. *See* ALJ Decision at P 174, JA 134.

purchase agreements], which are not off-system sales, but a sale from one Entergy Operating Company to two other Entergy Operating Companies.” ALJ Decision at P 176, JA 135; *id.* at P 180 (sales between Operating Companies “either bring into or keep capacity on the Entergy System, the complete opposite of the concern over off-system sales”), JA 136; *see also* Affirming Order at P 129 (explaining ALJ’s finding), JA 48. Section 3.05 requires a company that wishes to sell excess generating capacity to offer that capacity “to the other Companies” — exactly as the sellers did here.

Moreover, the Commission found that, even if the right of first refusal did apply to the inter-affiliate power purchase agreements, § 3.05 did not dictate *which* Operating Companies must be afforded that right: “[T]here is nothing in section 3.05 that supports Louisiana Commission’s position that this would entitle Entergy Gulf States and Entergy Louisiana to exclusively exercise these rights [of first refusal].” Rehearing Order at P 43, JA 68. Indeed, “the right of first refusal afforded each Entergy operating company under the System Agreement does not explicitly address the question of whether an operating company can offer its surplus capacity to any *particular* operating company, or if it must offer the capacity to *all* of the other operating companies.” *Id.* (emphases added) (noting testimony of FERC Staff witness). Therefore, the allocation of excess capacity to

two Operating Companies and not to the others (such as Entergy Gulf States) did not violate the System Agreement.

Finally, both the ALJ and the Commission concluded that, even assuming that the right of first refusal was triggered, “Section 3.05 does not give any guidance on how an operating company’s surplus capacity [should] be apportioned among the other operating companies.” Affirming Order at P 134, JA 49; ALJ Decision at P 182 (“Assuming *arguendo*, if not incredibly, that Section 3.05 applies to the [Wholesale Base Load power purchase agreements], no language in [that provision] requires the use of load responsibility ratios as abstractly argued by [Louisiana] . . .”), JA 136-37. In any event, the Commission noted, “the most important goal is to keep the operating companies within rough production cost equalization.” Affirming Order at P 134, JA 49.

Tellingly, on appeal Louisiana does not even address its § 3.05 challenge to the inter-affiliate power purchase agreements that were directly presented to the Commission. Instead, Louisiana focuses its entire argument about the right of first refusal on Entergy Arkansas’s short-term sales to third parties in 2002 — an issue that, as discussed in the next section, is irrelevant to the Commission’s analysis of the power purchase agreements at issue in this case.

B. The Commission Reasonably Determined That The Short-Term, Off-System Sales In 2002 Did Not Violate § 3.05

Rather than pursue its argument that the allocation of the Entergy Arkansas Wholesale Base Load capacity among Entergy affiliates contravened the right of first refusal under § 3.05 of the System Agreement, Louisiana devotes a substantial portion of its Brief to another matter: the propriety of an earlier, unrelated series of short-term non-affiliate sales. *See* Br. 28-39.

Louisiana's argument concerns a series of sales made by Entergy Arkansas in 2002 and 2003. Entergy Arkansas previously sold power to the City of North Little Rock as a wholesale requirements customer. When the City switched to another power supplier in mid-2002, Entergy Arkansas was left with 167 MW of excess capacity. *See* ALJ Decision at PP 147, 177, JA 126, 135. Starting in July 2002 and continuing through 2003, Entergy Arkansas made short-term opportunity sales from that excess capacity in the wholesale market. *Id.* at P 177, JA 135. Those sales were made to various non-affiliate customers for terms of about a month. *Id.* & n.26 (noting that the record showed sales to a number of different customers, rather than strings of sequential one-month transactions to the same customer(s)), JA 135.

In the course of the proceeding to consider the power purchase agreements between Entergy affiliates, including Entergy Arkansas's sales of 220 MW of Wholesale Base Load capacity to Entergy Louisiana and Entergy New Orleans, the

Louisiana Commission argued that Entergy Arkansas’s earlier sales in the wholesale market to non-affiliates had violated the right of first refusal. The ALJ determined that he “need not decide the abstract bounds of what would constitute an off-system wholesale sale that triggers Section 3.05.” ALJ Decision at P 180, JA 136. Rather, he found that the earlier short-term off-system sales did not bring the § 3.05 right of first refusal into his consideration of the affiliate power purchase agreements that were the subject of *this* proceeding:

On the material facts before me, I do find that the one-month opportunity type sales begun by [Entergy Arkansas] in 2002 after losing North Little Rock as a customer clearly do not trigger a right of first refusal for the life of unit [Entergy Arkansas Wholesale Base Load power purchase agreements]. *These* are the [agreements] before me for which the [Louisiana Commission] is trying to claim that its jurisdictional companies should have participated in a right of first refusal, *not* the short-term [Entergy Arkansas] sales.

Id. (emphases added). Accordingly, the lack of nexus between the (non-affiliate) short-term sales and (inter-affiliate) power purchase agreements “is dispositive of [Louisiana’s] § 3.05 issue” *Id.* at P 181, JA 136.

The Commission agreed: “Contrary to Louisiana Commission’s argument, the Commission did consider whether the one-month opportunity sales begun by Entergy Arkansas in 2002 . . . triggered a right of first refusal for the [life-of-unit] Entergy Arkansas Base Load [power purchase agreements]. . . . [W]e affirmed the presiding judge’s finding on this issue.” Rehearing Order at P 39, JA 67; *see also*

Affirming Order at PP 133, 134 (summarizing and agreeing with ALJ's finding), JA 49.

The ALJ and the Commission could well have stopped at that point. Indeed, both concluded that the question whether the other Entergy Operating Companies should have been entitled to buy the excess North Little Rock capacity on a short-term basis was a distinct matter that would have been appropriate for a separate complaint proceeding: "If [Louisiana] had wanted to complain that a right of first refusal for one-month sales should have been offered by [Entergy Arkansas] and accepted by other Operating Companies beginning in early 2002, it should have filed a complaint about that subject then." ALJ Decision at P 180, JA 136; *accord*, Affirming Order at P 134, JA 49.

Nevertheless, the ALJ went on to address the substance of Louisiana's argument that the short-term, off-system sales triggered the right of first refusal, concluding that, absent something "untoward," such as a series of short-term sales designed to avoid scheduling a long-term sale, as to which there was no allegation or evidence here, the right of first refusal should not apply to off-system sales of a month. ALJ Decision at P 181, JA 136. On exceptions, the Commission agreed. Affirming Order at P 134, JA 49.

On rehearing, the Commission further explained that, based on both the language and the purpose of § 3.05, it concluded the short-term non-affiliate sales

did not trigger the right of first refusal. The Commission looked first to the opening sentence of § 3.05, which emphasizes the “long-term goal” of the System Agreement for each Operating Company to have a proportionate share of base load generation available to serve its customers. Rehearing Order at PP 40-41, JA 67-68. By contrast, the Commission noted, that provision says nothing about ensuring that each Operating Company receives a proportionate share to meet short-term needs. *Id.* at P 41, JA 68.

Though Louisiana contends that the Commission “confuses” the goal of the System with the type of capacity sale, Br. 30, the Commission rejected that distinction: the Commission reasonably read the second, prescriptive sentence of § 3.05 as intended to effectuate the first, aspirational statement. That is, given the joint planning and cost allocation across the Entergy System, the long-term goal of allowing each Operating Company to have its proportionate share of base load generation is served by keeping such generation capacity within the System for the long term. But the Commission found that the one-month opportunity sales made to off-system buyers would not affect the long-term availability to each Operating Company of its proportionate share. Rehearing Order at P 42, JA 68. Nor would making such one-month (or shorter) opportunity sales available to other Operating Companies advance the System’s goal of providing each Company with a stable, certain generation supply to serve its base load demand. *See id.* (§ 3.05 “was

designed to ensure that the operating companies' long-term capacity needs were being met"). Thus, the Commission affirmed the ALJ's determination as "both a proper reading of [§ 3.05] and entirely reasonable." *Id.* at P 42, JA 68. Even if Louisiana disagrees, the Commission's interpretation is entitled to *Chevron*-type deference. *See Koch Gateway*, 136 F.3d at 814.

Furthermore, as discussed *supra* at p. 39, the Commission held that, even assuming that Entergy Arkansas's short-term sales had triggered a right of first refusal, Section 3.05 does not address whether an Operating Company can offer surplus capacity to a particular Operating Company, or must offer it to all of the other Operating Companies. Therefore, "there is nothing in [§] 3.05 that supports Louisiana Commission's position that [triggering that provision] would entitle Entergy Gulf States and Entergy Louisiana to exclusively exercise these rights." Rehearing Order at P 43, JA 68.

Though Louisiana now argues that its contract interpretation is supported by "key portions of the System Agreement" that the Commission did not address — specifically, §§ 3.01, 3.02, 3.07, 3.08, and 4.08 (Br. 31-32) — Louisiana failed to raise this argument before the Commission on rehearing. Accordingly, this argument is jurisdictionally barred. *See* FPA § 313(b), 16 U.S.C. § 8251(b); *see also Constellation Energy Commodities Group, Inc. v. FERC*, 457 F.3d 14, 21 (D.C. Cir. 2006) (barring argument about tariff interpretation that petitioners had

not raised before Commission: “The [petitioners] did not make this argument before the agency and in fact never even cited the sections of the tariff upon which they now rely for the interpretation of [the provision at issue].”); *W. Area Power Admin. v. FERC*, 525 F.3d 40, 57 (D.C. Cir. 2008) (“[P]etitioners have failed to show that they properly raised these precise contract claims with FERC so as to preserve them for judicial review.”).

Finally, in any event, if the Court were to disagree with the Commission’s interpretation of § 3.05 with regard to short-term sales, such a holding still would have no effect on the Commission’s approval of the power purchase agreements allocating long-term capacity to Entergy Louisiana and Entergy New Orleans.

CONCLUSION

For the reasons stated, the petition should be denied and the challenged FERC Orders should be affirmed in all respects.

Respectfully submitted,

Cynthia A. Marlette
General Counsel

Robert H. Solomon
Solicitor

Carol J. Banta
Attorney

Federal Energy Regulatory
Commission
Washington, DC 20426
TEL: (202) 502-6433
FAX: (202) 273-0901

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