ORAL ARGUMENT IS SCHEDULED FOR OCTOBER 7, 2008

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

No. 07-1343

ENTERGY SERVICES, INC.,
PETITIONER,
v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.

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

BRIEF OF RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

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JULY 29, 2008

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CIRCUIT RULE 28(a)(1) CERTIFICATE

A. Parties and Amici

The parties before this Court and before the agency are identified in the brief of petitioner.

B. Rulings Under Review

1. *Arkansas Electric Cooperative Corp. v. Entergy Arkansas, Inc.*, 117 FERC ¶ 61,099 (2006) (Opinion No. 488), JA 327; and

2. *Arkansas Electric Cooperative Corp. v. Entergy Arkansas, Inc*., 119 FERC ¶ 61,314 (2007) (Rehearing Order), JA 404.

C. Related Cases

This case has not previously been before this Court or any other court, and counsel is not aware of any other related cases pending before this or any other court.

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Samuel Soopper
Attorney

July 29, 2008

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GLOSSARY

Arkansas Electric	Arkansas Electric Cooperative Corporation
Entergy	Entergy Arkansas, Inc.
Initial Decision	*Arkansas Electric Cooperative Corp. v. Entergy Arkansas*, 114 FERC ¶ 63,015 (2006)
Opinion No. 488	*Arkansas Electric Cooperative Corp. v. Entergy Arkansas, Inc.*, 117 FERC ¶ 61,099 (2006)
Power Agreement	Power Coordination, Interchange and Transmission Service Agreement
Rehearing Order	*Arkansas Electric Cooperative Corp. v. Entergy Arkansas, Inc.*, 119 FERC ¶ 61,314 (2007)

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STATEMENT OF THE ISSUE

Whether the Federal Energy Regulatory Commission (Commission or FERC) reasonably interpreted the ambiguous terms of a FERC-jurisdictional contract between Entergy Arkansas, Inc. (Entergy) and Arkansas Electric Cooperative Corporation (Arkansas Electric) as preventing Entergy from billing Arkansas Electric for energy at a premium rate because of conditions on Entergy's transmission system, unrelated to Arkansas Electric's generating units.

STATUTORY AND REGULATORY PROVISIONS

The pertinent statutory and regulatory provisions are contained in Addendum A to this brief. Additionally, for the Court's convenience, Addendum B contains the pertinent provisions of the contract at issue.

STATEMENT OF THE CASE

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

This case arises from a complaint filed with the Commission by Arkansas Electric, contending that Entergy had violated the Power Coordination, Interchange and Transmission Service Agreement (Power Agreement) between the parties concerning electric generation facilities that they co-own, but are operated by Entergy. Specifically, Arkansas Electric asserted that in 2004, Entergy started billing it at a higher rate than authorized by the Power Agreement.

After a hearing, a FERC administrative law judge issued an Initial Decision holding that the plain terms of the Power Agreement and certain related contracts supported Entergy's new billing practice. *Arkansas Electric Cooperative Corp. v. Entergy Arkansas, Inc.*, 114 FERC ¶ 63,015 (2006), JA 311.

However, in the first order on review here, the Commission reversed the judge. Upon analysis, the Commission held that: (1) the billing provisions of the Power Agreement were ambiguous; and (2) those provisions, reasonably construed, required Entergy to charge Arkansas Electric the lower rate under the

circumstances, as had been Entergy's practice over the course of the contract. Order on Initial Decision, *Arkansas Electric Cooperative Corp. v. Entergy Arkansas, Inc.*, 117 FERC ¶ 61,099 (2006) (Opinion No. 488), JA 327. In the second order on review, the Commission denied Entergy's request for rehearing of its contract interpretation. *Arkansas Electric Cooperative Corp. v. Entergy Arkansas, Inc.*, 119 FERC ¶ 61,314 (2007) (Rehearing Order), JA 404.

II. STATEMENT OF FACTS

A. The Contract Between The Parties

Entergy is an investor-owned electric utility, engaged in the generation, transmission, distribution and sale of electric energy in Arkansas as part of the multi-state Entergy System. *See generally, e.g., Entergy Louisiana, Inc. v. Louisiana Public Service Comm'n*, 539 U.S. 39, 42-43 (2003) (describing multi-state operations and allocation of costs on the Entergy System).

This Court has had previous encounters with the Entergy System, most recently in *Louisiana Public Service Comm'n v. FERC*, 522 F.3d 378 (D.C. Cir. 2008). Entergy Arkansas is one of five operating companies of Entergy Corporation, a public utility holding company responsible for the sale and transmission of electric energy in Arkansas, Louisiana, Mississippi, and Texas. *Louisiana Public Service Comm'n*, 522 F.3d at 383. The five companies, including Entergy Arkansas, operate in a single integrated transmission system

(known as a control area), covering all of those states. *Id.*; *see also, e.g., Miss. Indus. v. FERC*, 808 F.2d 1525, 1529 (D.C. Cir. 1987).

Arkansas Electric is an electric generation and transmission cooperative providing wholesale electricity to its sixteen electric distribution cooperative members in the State of Arkansas. A portion of Arkansas Electric's load and resources are located in the Entergy System control area. For this load and these resources, Arkansas Electric relies on the Entergy transmission system to serve its members. *See* Arkansas Electric Complaint, R 16 at 5, JA 5. Among these resources are four coal-fired generation plants, in which Arkansas Electric shares an ownership interest with Entergy (Independence Steam Electric Station Unit Nos. 1 and 2, and White Bluff Steam Electric Station Unit Nos. 1 and 2). *Id.* at 7, JA 7.

Entergy and Arkansas Electric entered into the Power Agreement in June 1977, which "provides for the operation and scheduling of [Arkansas Electric]'s resources that are within the [Entergy] control area, including all of [Arkansas Electric]'s co-owned units." Answer of Entergy Arkansas to Complaint, R 23 at 7, JA 248. At the same time, the parties entered into several agreements concerning the construction, ownership and operation of their co-owned plants (collectively, the Co-Owner Agreements). *Id.* at 5-7, JA 246-248.

Under the terms of the Power Agreement, Entergy has full control over

dispatching and scheduling Arkansas Electric's share of energy from the co-owned units. Essentially, Entergy is given control over and use of Arkansas Electric's resources, while, in return, Entergy guarantees the delivery of energy to meet Arkansas Electric's loads on an hourly basis, whatever resources are employed. *See* Complaint at 8, JA 8; Entergy Answer at 7-8, JA 248-249.

The Power Agreement establishes a so-called "after-the-fact redispatch" billing method, *i.e.*, "theoretical redispatch," "to determine the amounts of energy from jointly-owned and other resources with which [Arkansas Electric] is to be credited." Entergy Answer at 7, JA 248.

The parties agree that for redispatch, *i.e.*, billing purposes, Entergy bills Arkansas Electric at different rates when it serves Arkansas Electric's load using different energy resources, depending upon whether energy was "available" from Arkansas Electric's energy resources, *i.e.*, the co-owned units. If such energy is available from Arkansas Electric's resources, the Power Agreement authorizes Entergy to bill Arkansas Electric at a relatively inexpensive rate, keyed to the incremental cost of fuel at Arkansas Electric's coal-based units, that Arkansas Electric otherwise would have incurred (the "Substitute Energy" rate). However, if Arkansas Electric's resources are not available for physical dispatch, the Power Agreement allows Entergy to charge Arkansas Electric the substantially more expensive "Replacement Energy" rate.

The parties' dispute centers on when Arkansas Energy's share of the co-owned units is to be considered "available" for theoretical after-the-fact redispatch, *i.e.*, billing purposes.

B. The Proceeding Before The Commission

Arkansas Electric filed its complaint with the Commission on October 25, 2004. Arkansas Electric Complaint, JA 1. Arkansas Electric contended that "after 24 years" of operation under the Power Agreement, Entergy had "unilaterally . . . changed the method of classifying and pricing" called for by the Agreement, resulting in "significant overcharges to [Arkansas Electric]." *Id.* at 2, JA 2.

Arkansas Electric asserted that, prior to 2004, Entergy correctly implemented the Power Agreement by considering Arkansas Electric's resources "available," and thus billing at the cheaper "Substitute Energy" rate, unless there was an actual operating constraint caused by an actual physical limitation of the co-owned units. However, Arkansas Electric alleged, as of June 23, 2004, Entergy changed its billing practice. Entergy now considered Arkansas Electric's co-owned units as "available" for billing purposes only when Entergy had actually dispatched energy from Arkansas Electric's resources. Thus, Entergy had begun billing Arkansas Electric at the higher rate even if Entergy's dispatch from alternate resources resulted from conditions unrelated to the units themselves, such

as operating constraints elsewhere on Entergy's transmission system. *See* Arkansas Electric Complaint 16, JA 16.

On November 17, 2004, Entergy filed its Answer to Arkansas Electric's complaint, disputing Arkansas Entergy's interpretation of the Power Agreement. Entergy Answer, JA 242. Entergy asserted that under the Power Agreement (as well as the Co-Owner Agreements), Arkansas Electric's resources had never been "available" for billing purposes if Entergy did not physically employ them for actual dispatch of energy. Thus, Entergy argued, to the extent that it does not actually use the output of the co-owned units due to any operational constraints on the Entergy System, the Power Agreement allows it to bill Arkansas Electric at the higher Replacement Energy rate. According to Entergy, such operational constraints include, *inter alia*, transmission constraints anywhere on the Entergy System, as well as the requirement that Entergy buy energy from cogeneration and small power production facilities pursuant to the Public Utility Regulatory Policies Act of 1978, 16 U.S.C. § 824a-3. *See* Entergy Answer at 10, JA 251.

In an order issued on December 22, 2004, the Commission set Arkansas Electric's complaint for a trial-type evidentiary hearing, to resolve the dispute over "what rate should be charged" under the Power Agreement "when Entergy[] reduces the output" of the generation units in question "due to alleged constraints on its operating system." *Arkansas Electric Cooperative Corp. v. Entergy*

Arkansas, Inc., 109 FERC ¶ 61,327 at Paragraph (P) 38 (2004). The hearing was held before a Commission administrative law judge in late August and early September 2005.

In the Initial Decision issued on January 26, 2006, the judge denied Arkansas Electric's complaint. In the judge's view, the dispute should be resolved with reference not only to the Power Agreement, but also the various Co-Owner Agreements. The judge concluded:

> When the terms of the contract are reviewed objectively . . . it is clear that the plain terms of the Co-Owner Agreements – all five agreements governing the relationship between [Entergy] and [Arkansas Electric] – call for [Entergy] to include system operating constraints in determining the hour-to-hour availability of the Co-Owned Units.

Initial Decision P 21, JA 314. Based on this finding, the judge agreed with Entergy that it could charge Arkansas Electric the higher Replacement Energy rate, even if Arkansas Electric's resources had been physically available for dispatch.

Arkansas Electric sought review by the Commission of the Initial Decision.

C. Opinion No. 488

In Opinion No. 488, the Commission reversed the Initial Decision, finding that the result "conforms neither to the specific billing provisions of the contract nor to the long-standing course of performance between the parties." Opinion No. 488 P 1, JA 327. Rather, the Commission concluded, a reasonable reading of the Power Agreement's billing provisions required Entergy to charge Arkansas

Electric only the lower Substitute Energy rate, unless Arkansas Electric's generation units were not physically available for dispatch. *Id.* PP 52-53, 56-57; JA 341-342, 344.

First, the Commission disagreed with the judge that the Power Agreement could be read according to its "plain language." Opinion No. 488 P 59, JA 345. In the Commission's view, the Co-Owner Agreements were irrelevant to this billing question. Instead, the Commission determined that the Power Agreement's billing provisions expressed the parties' intent on the issue. However, the Commission concluded, the relevant language of the Power Agreement was ambiguous with respect to the question of whether a generating unit was to be considered "available" for redispatch because of operating conditions elsewhere on the Entergy transmission system. *Id.*

Second, the Commission determined that the most reasonable reading of the relevant provisions of the Power Agreement supported Arkansas Electric's view, namely that the parties had intended "to render [Arkansas Electric] economically indifferent as to the actual amount of power that the Entergy dispatcher decides to dispatch from Arkansas Electric's units as long as the units are physically capable of generating the power needed to serve its own load." Opinion No. 488 P 68, JA 350.

In this regard, the Commission found that, pursuant to Article V, Section 5 and Redispatching Principle No. 6 of the Power Agreement, if the Arkansas Electric generation units were physically capable of producing the amount of power needed to serve its customers, but Entergy actually dispatched less than that amount from those units, Arkansas Electric would pay the lower Substitute Energy rate (*i.e.*, the inexpensive rate based on the incremental cost of fuel (coal) at its generating plants). Opinion No. 488 PP 53, 68, JA 341-342, 350. However, the Commission concluded, Entergy could only charge Arkansas Electric the more expensive Replacement Energy rate when Arkansas Electric's resources were not available, namely (1) if and to the extent that the power delivered to its customers exceeded the tested capacity of its units (Redispatching Principle No. 7); or (2) if the units were down for "Outages", *i.e.*, scheduled maintenance or emergencies (Power Agreement Article III, Section 5). Opinion No. 488 P 54, JA 342.

Finally, the Commission relied on evidence in the record concerning the parties' course of performance under the Power Agreement, which demonstrated that Entergy had long read the Agreement's billing provisions in the same manner as Arkansas Electric. Opinion No. 488 PP 69-71, JA 351-352.

D. The Rehearing Order

Entergy requested rehearing of Opinion No. 488 on a number of grounds (R 189, JA 357), all of which the Commission rejected in the June 25, 2007,

Rehearing Order. JA 404.

First, Entergy argued that the Commission's interpretation of after-the-fact redispatch in the Power Agreement conflicted with various provisions of the Co-Owner Agreements. However, the Commission held that the Co-Owner Agreements "has no bearing on the billing issue at hand, which is governed by the Power Agreement." *Id.* P 14, JA 412.

Entergy went on to fault Opinion No. 488 for allegedly misreading the Power Agreement itself. The Commission, however, affirmed that the terms of the contract, taken as whole, prevent Entergy from charging the higher "Replacement Energy" rate in the event that Entergy did not actually dispatch Arkansas Electric resources due to unrelated operating constraints. Rehearing Order PP 16-18, JA 412-414.

Finally, the Commission rejected Entergy's view that course of performance evidence was irrelevant because there had been no consistent billing practice under the Power Agreement. To the contrary, the Commission concluded, record evidence demonstrated that Entergy had not begun to "regularly bill" Arkansas Electric at the higher rate based on its new definition of availability, and had consistently charged Arkansas Electric the lower rate, "until July 1, 2004." Rehearing Order P 54, JA 428.

This appeal followed.

SUMMARY OF ARGUMENT

This case – Entergy's needlessly complex and jargon-filled arguments notwithstanding – is, at bottom, a garden-variety billing dispute. After more than 20 years of service, Entergy unilaterally raised its rates charged to Arkansas Electric. Entergy based that action on its belief that its Power Agreement with Arkansas Electric, and related Co-Owner Agreements, plainly allowed for higher rates.

After complaint and hearing, a FERC administrative law judge agreed with Entergy. However, the Commission on review disagreed, finding the relevant contract provisions ambiguous and susceptible to more than one reasonable interpretation, and that the most reasonable interpretation did not allow Entergy to raise Arkansas Electric's rates. Under the applicable standard governing judicial review of Commission contract interpretations, the Commission's reasonable interpretation of the ambiguous billing provision of the parties' Power Agreement is entitled to *Chevron*-type deference.

Specifically, the Commission read the relevant terms of the Power Agreement as requiring Entergy to charge Arkansas Electric the lower Substitute Energy rate, unless energy was not actually physically available for dispatch from Arkansas Electric's resources. In the latter situation only, the Commission determined, Entergy may charge Arkansas Electric the higher Replacement Energy

rate. The agency's interpretation reasonably construed the specific billing provisions and Redispatching Principles of the Power Agreement.

Entergy can demonstrate neither that its interpretation is required by the plain meaning of the Power Agreement, nor that the Commission's interpretation is otherwise unreasonable. As the Commission explained, its reading of the Power Agreement's billing provisions relied on the specific language therein, and took into account the different provisions of the Agreement as a whole. The Commission also properly rejected Entergy's contention that it had somehow interpreted the Agreement unfairly.

Finally, the Commission found that extrinsic evidence of the parties' course of performance under the Power Agreement supported its interpretation of the disputed billing provisions. This conclusion is fully supported by evidence in the record, and is thus worthy of judicial respect.

ARGUMENT

I. STANDARD OF REVIEW

This Court reviews Commission orders under the "arbitrary and capricious" standard set out in the Administrative Procedure Act at 5 U.S.C. § 706(2)(A). *Sithe/Independence Power Partners, L.P. v. FERC*, 165 F.3d 944, 948 (D.C. Cir. 1999). To satisfy this standard, the Commission must "demonstrate that it has made a reasonable decision based on substantial evidence in the record and the path of its reasoning must be clear." *Id.* (citations and internal quotations omitted).

The familiar two-step analysis established in *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), applies to an agency's interpretation of jurisdictional contracts. *Cajun Elec. Power Coop. v. FERC*, 924 F.2d 1132 (D.C. Cir. 1991). This is true even if the "issue simply involves the proper construction of language" and not a matter within the agency's special expertise. *National Fuel Gas Supply Corp. v. FERC*, 811 F.2d 1563, 1569-70 (D.C. Cir. 1987). *See also Koch Gateway Pipeline Co. v. FERC*, 136 F.3d 810, 814-15 (D.C. Cir. 1998) (applying *Chevron* analysis to Commission's interpretation of a FERC-jurisdictional tariff); *Cajun Elec. Power Coop.*, 924 F.2d at 1135 (noting that "[a]ny agreement that must be filed and approved by an agency loses its status as a strictly private contract and takes on a public interest gloss").

In applying *Chevron* principles to agreements subject to the Commission's jurisdiction, this Court first makes a *de novo* determination as to whether the relevant language unambiguously addresses the matter at issue. If the language is unambiguous, it controls. However, if the Court determines that the agreement is ambiguous as to the matter at issue, it will defer to any reasonable interpretation by the Commission. *See, e.g., Old Dominion Electric Coop. v. FERC*, 518 F.3d 43, 48-49 (D.C. Cir. 2008) (applying *Chevron* analysis to Commission's interpretation of a FERC-jurisdictional agreement); *Southwestern Electric Coop., Inc. v. FERC*, 347 F.3d 975, 979 (D.C. Cir. 2003) ("given [the] ambiguity" of a FERC-jurisdictional agreement "and the technical aspects of some of the determinations, the court's review is most deferential") (citing numerous cases).

II. THE COMMISSION'S REASONABLE INTERPRETATION OF THE POWER AGREEMENT BILLING PROVISIONS SHOULD BE AFFIRMED BY THE COURT.

A. The Commission Properly Held That The Power Agreement Was Ambiguous On The Issue Of The "Availability" Of Energy For Billing Purposes.

Entergy's most fundamental problem with the Commission's orders is their alleged failure to recognize that the "plain language" of the Power Agreement (as well as the Co-Owner Agreements) "allows for recognition of system operating constraints in the determination of the hour to hour capability of the Co-Owned Units available to [Arkansas Electric]." Pet. Br. 5. The Commission, however,

was unable to discern such a "plain" meaning, concluding that the Power Agreement was ambiguous on the precise issue presented.

This Court has long held that "[a] tariff or contract is ambiguous when it is 'reasonably susceptible of different constructions or interpretations.'" *Consolidated Gas Transmission Corp. v. FERC*, 771 F.2d 1536, 1544 (D.C. Cir. 1985) (quoting *Lee v. Flintkote Co.*, 593 F.2d 1275, 1282 (D.C. Cir. 1979)). As the Court has observed, such "[a]mbiguity easily arises when the contract is applied to its subject matter in changed circumstances," as petitioner claims in the case at bar. *Consolidated Gas Transmission Corp.*, 771 F.2d at 1545 (quoting *Pennzoil Co. v. FERC*, 645 F.2d 360, 388 (5th Cir. 1981). As we now demonstrate, the Commission correctly held that the Power Agreement fell into the category of ambiguous contracts. (While the administrative law judge held that the Power Agreement and Co-owner Agreements unambiguously supported Entergy's position, this Court has recently explained that an agency judge's findings "are not entitled to any special deference." *Louisiana Public Service Comm'n*, 522 F.3d at 395 (citing *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 853 (D.C. Cir. 1970)).

The key question in this case is what the parties intended by Article V, Section 5 of the Power Agreement, which provides that Arkansas Energy's

resources will be "used to theoretically redispatch" its load for billing purposes, considering their "availability on an hour-to-hour basis." Power Agreement, Article V, § 5, JA 111. The Commission concluded that "availability" of resources for the purpose of billing could mean two different things in the Power Agreement:

> (1) the capability of the unit to generate power irrespective of whether and in what amount power is actually dispatched, as Arkansas Electric interprets it, or (2) whether the power the unit is capable of generating is usable by the Entergy dispatcher based on operating conditions on the transmission system, as Entergy apparently interprets it.

Opinion No. 488 P 59, JA 345.

Entergy urges that the "plain meaning" of "availability" as used in the Power Agreement is to be found in the second definition. Pet. Br. 21. However, Entergy's attempt to explain this "plain meaning" is based on a long and convoluted argument that the Commission has not reasonably construed the contract terms, a different point from whether the contract language is ambiguous or not. *See id.* 22-24.

The fact is that the Power Agreement never specifically defines "availability" as it is to be applied in the context of billing. Rather, the Commission determined, what the Power Agreement means by "availability" of Arkansas Energy's resources for redispatch purposes can only be understood by construing the language of Article V, Section 5 in conjunction with the Redispatching Principles contained in the Agreement's Exhibit E, as well as the

"Outages" provision in Article III, Section 5. Opinion No. 488 PP 52-53, JA 341-342; Rehearing Order P 8, JA 408-409; *see also* Rehearing Order P 11, JA 410 (expressing the Commission's frustration that "the Power Agreement . . . scatters provisions explaining how billing is to occur in three separate parts" of the document).

It is fair to say, then, that as with the contracts at issue in *Southwestern Electric Coop.*, the Power Agreement required "[t]he Commission's efforts to interpret ambiguous language" in an "attempt to make sense out of the parties' intent." 347 F.3d at 979.

B. The Commission Reasonably Interpreted The Power Agreement's Billing Provisions As Deeming Arkansas Electric's Resources "Available" Irrespective Of Transmission System Constraints.

The Commission found that "the specific billing provisions and Redispatching Principles" of the Power Agreement are "most reasonably read" to permit Entergy to charge the more expensive Replacement Energy rate only if energy is actually unavailable from Arkansas Electric's generating units, not if Entergy is not using the units' energy because of other transmission system considerations. Rehearing Order P 19, JA 414; *see also* Opinion No. 488 PP 53-54, JA 341-343; Rehearing Order PP 8, 11, 19, JA 408-409, 410-411.

In this regard, the Commission relied on Article V, Section 5(a)(ii), the billing provision of the Power Agreement, together with Redispatching Principle

Nos. 6 and 7, and the "Outages" provision of Article III, Section 5. The Commission interpreted these provisions to mean that "billing for any deficiency between what Entergy chooses to dispatch from Arkansas Electric's generation resources and what Entergy actually supplies Arkansas Electric's customers is . . . to be at the inexpensive Arkansas Electric incremental fuel" cost, as long as the Arkansas Electric generating units are physically capable of producing the energy necessary to meet its customers' demand. Opinion No. 488 P 53, JA 341-342. *See also* Rehearing Order P 8, JA 408-409.

Accordingly, the Commission clarified that the "availability" of Arkansas Energy generation resources "can be defined as the tested capability of the Arkansas Electric generation resources in the absence of Outages of those generation resources." Rehearing Order P 11 (emphasis deleted), JA 411. Thus, if the full-rated capacity of the co-owned units was available for actual dispatch, "the fact that Entergy chooses to actually dispatch less" because of other considerations, such as operational constraints elsewhere on Entergy's transmission system, was not intended by the drafters of the Power Agreement to affect "theoretical redispatch," *i.e.*, the price Entergy uses for billing purposes. Opinion No. 488 P 58, JA 344; *see also* Rehearing Order P 8, JA 408-409.

A review of the contract language demonstrates that the Commission's interpretation of the parties' intent is reasonable. Article V, Section 5 of the Power

Agreement, entitled "Billing," establishes the concept of "theoretical redispatch," by means of which Arkansas Electric's resources will be used "considering their availability on an hour-to-basis." Power Agreement Article V § 5, JA 111. That provision goes on to set the appropriate rate to be paid both when Arkansas Electric's generation resources are available, and when they are not. Power Agreement Article V § 5(a) (ii), JA 112 (lower rate); Article V § 5(c), JA 113 (higher rate).[1]

However, to answer the question of what the parties intended by "resources . . . available," recourse is necessary to the Power Agreement's Redispatching Principles. The Commission found two of the Redispatching Principles (Nos. 6 and 7) particularly relevant to the issue. Redispatching Principle No. 6 states:

> If the capability of [Arkansas Electric] Resources is sufficient to supply [Arkansas Electric] requirements and if [Arkansas Electric] requirements are greater than the energy supplied from [Arkansas Electric] Resources in an hour, [Arkansas Electric] will pay to [Entergy] [Arkansas Electric's] incremental cost per [kilowatt hour] of the energy deficiency [*i.e.,* the lower rate].

Id. Exhibit E (6), JA 158. If, however, "the capability of [Arkansas Electric]

[1] Article III Section 5, the Outages provision of the Power Agreement, gives the only other circumstance permitting Entergy to charge Arkansas Electric the higher rate, *i.e.*, "when any [Arkansas Electric] Owned Resource is out of service because of emergency or planned maintenance." Power Agreement Article III § 5, JA 101.

Resources is not sufficient to supply [Arkansas] requirements in an hour," Redispatching Principle No. 7 permits Arkansas Electric to "purchase Replacement Energy" at the higher rate, in accordance with Article III, Section 5 of the Power Agreement (governing Outages) (*see* n.1, *supra*) and the other Redispatching Principles. *Id.* Exhibit E (7), JA 158.

As the Commission observed, Article II, Section 17 of the Power Agreement expressly defines "capability" to mean the "net generating capability based on tests." Power Agreement, Article II § 17, JA 98. Thus, the Commission determined that Principle No. 7 applies the higher Replacement Energy rate only to the amount of power Entergy actually delivers to Arkansas Electric's customers that exceeds the tested maximum capacity of the Arkansas Electric generating units. Opinion No. 488 PP 53-54, JA 341-342.

In the Commission's view, Redispatching Principle No. 7 "dovetails" with Redispatching Principle No. 6 by "apply[ing] the lower Arkansas Electric incremental fuel rate (substitute energy rate) to power Entergy supplies Arkansas Electric's customers that does not exceed the tested maximum capacity of Arkansas Electric's generating units." Rehearing Order P 8 (footnote omitted), JA 409. The Commission clarified that "availability" also includes whether the Arkansas Electric units are down for maintenance or emergencies, in which case the higher rate applies pursuant to the Outages provision (Article III, Section 5) of

the Power Agreement. *Id.* Thus, the Commission concluded, "Entergy transmission system operating constraints have no place in that construct." *Id.*, JA 409.

Finally, the Commission noted that its interpretation of the term "availability" in the Power Agreement was consistent with the "common industry definition" of the term. Opinion No. 488, P 59 & n.50, JA 345.

Because the Commission here reasonably interpreted the ambiguous terms of the Power Agreement, Entergy can only prevail before this Court by demonstrating that the agency's interpretation was unreasonable. *See, e.g., Koch Gateway Pipeline Co.*, 136 F.3d at 814-15. However, Entergy cannot meet this burden.

First, Entergy maintains that the Commission has incorrectly equated the term "availability" with "capability." Pet. Br. 12-13, 21-22. As Entergy describes it:

> The maximum dependable capability as determined by an annual test cannot change due to emergencies, outages, or system operating constraints. The hour-to-hour availability to the [Entergy] dispatcher, however, will be affected by each of these factors. It is the hour-to-hour availability that is the basis for determining the proper credit to give [Arkansas Electric] in after-the-fact redispatch and FERC fails to recognize this distinction.

Id. 22.

The Commission explained, however, that it did not confuse the two terms. Rather, it found that the meaning of "available" for billing purposes in Article V

Section 5 of the Power Agreement was informed by the language of Redispatching Principle No. 6, which requires Entergy to charge the lower rate "if the capability" of Arkansas Electric's resources "is sufficient to supply" its requirements (and there are no outages of the Arkansas Electric units), which would not include operating constraints elsewhere on the Entergy transmission system. *See* Rehearing Order P 29, JA 417-418.

Entergy also contends that the Commission's interpretation cannot be sustained because it effectively reads Redispatching Principle No. 3 out of the Agreement. Pet. Br. 12. In Entergy's view, Redispatching Principle No. 3 "expressly recognizes that system operating constraints should be considered" in determining energy availability for redispatch purposes. *Id.* 11.

But as the Commission sensibly observed, Redispatching Principle No. 3 must be "read in conjunction with Redispatching Principle Nos. 1 and 2, which establish the maximum and minimum operating levels for each unit, and, therefore, at each plant." Rehearing Order P 19, JA 414. It followed, the Commission explained, that "the term '*other* operating constraints' [in Redispatching Principle No. 3] is reasonably interpreted to refer to operating constraints at the plant that affect the ability of the generating units to produce power and does not necessarily include operating constraints on the Entergy transmission system." *Id.* (emphasis in original).

On a related point, Entergy argues that the Commission's interpretation cannot be squared with the definition of Replacement Energy (that is, the more expensive rate) in Article II, Section 18 of the Power Agreement. Entergy observes that this provision specifically contemplates that Arkansas Energy "may purchase Replacement Energy for multiple reasons, including 'transmission system operations,' rather than only when the rated capacity of [Arkansas Electric] resources is exceeded or when [Arkansas Electric] Resources experience an outage." Pet. Br. 16-17 (quoting Power Agreement Article II § 18, JA 98). Entergy maintains that FERC has improperly eliminated the reference to "transmission system operations" from this provision, by allowing Arkansas Electric to "only purchase Replacement Energy because of problems restricting [Arkansas Electric] Resources' output that originate at the plants." *Id.* 16.

However, the Commission explained that its interpretation does take into the account the reference in Article II, Section 18 of the Power Agreement to "transmission system operations":

> By its terms, the definition of Replacement Energy refers to "energy which one party desires to purchase from the other party" which could mean that either party, including Entergy, may wish to buy power from the other. Thus, Entergy may wish to buy power from Arkansas Electric as a consequence of Entergy transmission system operational constraints, which explains the inclusion of a reference to transmission system operations in the definition.

Rehearing Order P 24, JA 416.

Having failed to demonstrate that the Commission's interpretation of the Power Agreement is unreasonable, Entergy indulges in a lengthy argument that the Commission's interpretation of the Power Agreement is unfair, in that it fails to allocate Arkansas Electric responsibility for its contribution to operating constraints on Entergy's system. Pet. Br. 41-46.

The Commission properly rejected this argument, explaining that "[t]he issue turns on what the Power Agreement provides, not what Entergy believes it should provide in order to give Entergy a better deal." Rehearing Order P 50, JA 426. In any event, the Commission did not subscribe to the notion that its interpretation of the Power Agreement is unfair to Entergy, as Entergy had agreed to the relevant rates "[i]n return for obtaining over $600 million in capacity from Arkansas Electric." *Id.*

Finally, the agency indicated that if Entergy believed the Power Agreement had become unjust and unreasonable, its proper remedy would be to seek "a change in the Power Agreement, which is outside the scope of this proceeding." *Id.* In this regard, it bears mention that Entergy has preserved its right under the Power Agreement "to unilaterally seek amendments, changes and increases in the rates and charges set forth herein" before the Commission under section 205 of the Federal Power Act, 16 U.S.C. § 824d. Power Agreement, Article VIII § 1, JA 127.

C. Substantial Extrinsic Evidence Concerning The Parties' Intent Supports The Commission's Construction Of The Power Agreement.

The Commission determined that its interpretation of the Power Agreement was supported by extrinsic evidence of the parties' course of performance under the Agreement:

> The record is replete with evidence that for over twenty-three years *both* parties regarded Arkansas Electric as entitled to pay the lower incremental fuel (coal) cost of its units when the units were capable of meeting Arkansas Electric's load, regardless of whether and to what extent Entergy actually dispatched power from those units.

Opinion No. 488 P 70 (emphasis in original; footnote omitted), JA 351; *see also* Rehearing Order P 52, JA 427 ("The extrinsic evidence of Entergy's decades-long practice of charging the inexpensive substitute energy rate irrespective of transmission system conditions" sheds light on the meaning of the Power Agreement).

For example, the Commission relied on several instances in which the internal correspondence of Entergy's employees revealed that they understood Arkansas Electric's units to be "available" for redispatch billing purposes regardless of operational constraints elsewhere on Entergy's system. Opinion No. 488 PP 69-71 & nn. 61-62, 66-67, JA 351-352 (citing Exhibit AEC-44 at 1, JA 1166) (1996 e-mail of Entergy employee describing the "Substitute Energy process" as losing profit for Entergy because Arkansas Electric's unit is considered

"fully available" for billing purposes even if Entergy "is obligated to supply the energy from another source"); Exhibit AEC-53 at 21, JA 1187 (internal Entergy e-mail indicating that co-owners of generation units are "entitled to their share of the capacity of the unit at all times" absent a formal derating of the unit); Entergy Answer, Hurstell Affidavit P 44, JA 295; *id.* Castleberry Affidavit P 9, JA 305 (affidavits by Entergy witnesses acknowledging that prior to July 1, 2004, Entergy treated Arkansas Electric units as available for billing purposes regardless of what the units were actually capable of delivering in light of system operating constraints)).

The Commission's reliance on the parties' course of performance on this issue is fully consistent with this Court's longstanding precedent on contract interpretation. *See, e.g., South Dakota Public Utilities Comm'n v. FERC*, 934 F.2d 346, 351 (D.C. Cir. 1991) (course of performance of parties probative of their contractual intent; applying principle to situation where a party paid a particular contract price over a six year period); *Cities of Bethany v. FERC*, 727 F.2d 1131, 1144 (D.C. Cir. 1984) (evidence that parties agreed to a particular rate-fixing scheme under their contracts for prolonged period was "highly instructive as to the fair meaning" of the contracts).

Entergy disputes the Commission's reliance on the course of performance evidence here, asserting that even if the Power Agreement is ambiguous, certain

language of the Co-Owner Agreements governs. Pet Br. 35-56. Specifically, Entergy relies on language in one of those Agreements indicating that "in the event of any doubt whether the responsibility for a particular cost, obligation or liability is provided for in this agreement," the parties should proportionately share such costs. *Id.* (quoting Exhibit AEC-7 at 20-21, JA 986).

The Commission rejected this theory, on the ground that the provisions of the Co-Owner Agreements relied on by Entergy solely governed "[t]he allocation of costs of the Co-Owned generating units among the Co-Owners (such as fuel cost, operational expenses, maintenance costs, etc.)," and were thus "irrelevant to the issue of how Entergy is to bill Arkansas Electric for the power Entergy delivers to Arkansas Electric's customers." Rehearing Order P 52, JA 427.

The Commission's conclusion is reasonable. Not only does the cited language make no reference to billing under the Power Agreement, but also its general precatory language is by its terms limited to costs "provided for *in this agreement.*" Exhibit AEC-7 at 20 (emphasis added), JA 986.

Entergy further argues that the evidence cannot be found to demonstrate a course of performance on the ground that, as transmission constraints did not appear on Entergy's system until the 1990s, "no consistent practice for dealing with them developed." Pet. Br. 37. But as the Commission observed, the appearance of such constraints in the 1990s does not explain why "Entergy did not

regularly begin including transmission system constraints in its after-the-fact billing calculations until July 1, 2004." Opinion No. 488 P 71 (footnote omitted), JA 352; *see also* Rehearing Order PP 53-54, JA 427-428.

Entergy also argues that the extrinsic evidence can be read to show that "the implementation of certain provisions of the [Power Agreement] developed over time as constraints reached magnitudes sufficient to outweigh the practical difficulty in addressing them operationally and in redispatch billing." Pet Br. 38. However, as Entergy cannot demonstrate that the Commission's contrary view of the extrinsic evidence is unreasonable, the agency's conclusion must prevail. *See, e.g.*, *Louisiana Public Service Com'n*, 522 F.3d at 395 (quoting *Florida Mun. Power Agency v. FERC*, 315 F.3d 362, 368 (D.C. Cir. 2003) (Court's role is to determine "not whether record evidence supports [petitioner's] version of events, but whether it supports FERC's")).

CONCLUSION

For the reasons stated, the petition for review should be denied, and the Commission's orders affirmed in all respects.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

In accordance with Fed. R. App. P. 32(a)(7)(C)(i), I certify that the Brief of Respondent Federal Energy Regulatory Commission contains 6,135 words, not including the tables of contents and authorities, the certificates of counsel and the addendum.

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