ORAL ARGUMENT HAS NOT BEEN SCHEDULED

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

Nos. 07-1222, *et al.*

CITY OF ANAHEIM, CALIFORNIA, *ET AL*.,
PETITIONERS,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.

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

BRIEF FOR RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

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SEPTEMBER 12, 2008

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CIRCUIT RULE 28(a)(1) CERTIFICATE

A. Parties and Amici

All parties appearing before the Commission and this Court are listed in Petitioners' Rule 28(a)(1) certificate.

B. Rulings Under Review

The rulings under review appear in the following orders issued by the Federal Energy Regulatory Commission:

1. *Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 116 FERC ¶ 61,069 (2006) ("First Order"), JA 430;

2. *Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 116 FERC ¶ 61,297 (2006) ("Second Order"), JA 468;

3. *Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 118 FERC ¶ 61,096 (2007) ("Third Order"), JA 623;

4. *California Independent System Operator Corp.*, 118 FERC ¶ 61,097 (2007) ("Fourth Order"), JA 676;

5. *Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 119 FERC ¶ 61,266 (2007) ("Fifth Order"), JA 793;

6. *Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 121 FERC ¶ 61,276 (2007) ("Sixth Order"), JA 817.

C. Related Cases

This case has not previously been before this Court or any other court. Counsel is aware of the following case related to the instant one: *Sacramento Municipal Utility District, et al. v. FERC,* D.C. Cir. Nos. 07-1208, *et al.* (regarding California Independent System Operator long-term reliability measures).

Beth G. Pacella
Senior Attorney

September 12, 2008

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REGULATIONS

GLOSSARY

California ISO	California Independent System Operator Corporation
Cities	Petitioners, the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California
Commission	Federal Energy Regulatory Commission
FERC	Federal Energy Regulatory Commission
Fifth Order	*Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 119 FERC ¶ 61,266 (2007)
First Order	*Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 116 FERC ¶ 61,069 (2006)
Fourth Order	*California Independent System Operator Corp.*, 118 FERC ¶ 61,097 (2007)
Independent Energy Producers	Independent Energy Producers Association
NRG	NRG Power Marketing, Inc. and West Coast Power LLC
Second Order	*Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 116 FERC ¶ 61,297 (2006)
Sixth Order	*Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 121 FERC ¶ 61,276 (2007)
Third Order	*Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 118 FERC ¶ 61,096 (2007)

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BRIEF FOR RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

STATEMENT OF THE ISSUE

Following a lengthy and difficult agency rate proceeding, involving many issues and parties, the only remaining issue concerns the timing of a rate change:

Whether the Federal Energy Regulatory Commission ("FERC" or "Commission") reasonably determined that Settlement rates, which would allow generators required to offer generation to California markets to recover their fixed costs for doing so, would be effective prospectively, as requested in the Settlement, as of June 1, 2006, two months after the Settlement was filed.

STATUTORY AND REGULATORY PROVISIONS

The pertinent statutory and regulatory provisions are contained in the Appendix to this Brief.

INTRODUCTION

In the underlying proceeding, the Commission approved a Settlement resolving an August 26, 2005 complaint by the Independent Energy Producers Association ("Independent Energy Producers"), a group of wholesale electricity generators. The complaint explained that, under then-existing California Independent System Operator Corporation ("California ISO") must-offer obligation tariff provisions, generators were required to offer generation into the California ISO markets, but were not compensated sufficiently to cover their costs for doing so. R. 1 at 2, 11 and n.28, 19-21, JA 2, 11, 19-21. To resolve this until a long-term solution could be implemented, the complaint proposed that the California ISO tariff be amended to provide for compensatory Reliability Capacity Services Tariff rates. R. 1 at 1, 3, 5, JA 1, 3, 5.

On March 31, 2006, "parties with divergent interests on the issue of compensation to generators under the must-offer obligation," *Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 118 FERC ¶ 61,096 at P 48 (2007) ("Third Order"), JA 637 (*i.e.*, the Independent Energy Producers, the California ISO (operator of California's electric energy grid), the

California Public Utilities Commission (representing the interests of California retail customers), and California's three largest investor-owned utilities (Pacific Gas and Electric Company, San Diego Gas & Electric Company, and Southern California Edison)), filed an Offer of Settlement resolving the complaint. R. 43.

During the FERC proceedings, parties raised numerous substantive challenges to the Reliability Capacity Services Tariff rates first proposed in the complaint and then in the Settlement. None of those substantive challenges is raised on appeal. Instead, the sole claim on appeal is one of timing, *i.e.*, the effective date of the Reliability Capacity Services Tariff rates.

In the Petitioners' (the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (the "Cities")) view, the Reliability Capacity Services Tariff rates could not take effect until after the Commission accepted a compliance filing by the California ISO. The Commission found, however, that the Reliability Capacity Services Tariff rates properly could be made effective prospectively at an earlier date -- June 1, 2006, the date requested in the March 31, 2006 Settlement Offer. As the Commission explained, the complaint proceedings put all interested parties on adequate notice that the Settlement rates might be placed into effect on June 1, 2006. *Independent Energy Producers Ass'n v. California Independent System Operator Corp.*, 116 FERC ¶ 61,069 (2006) ("First

Order"), JA 430, *order on clarification*, 116 FERC ¶ 61,297 (2006) ("Second Order"), JA 468, *order on paper hearing*, 118 FERC ¶ 61,096 (2007) ("Third Order"), JA 623, *order on reh'g and compliance*, 119 FERC ¶ 61,266 (2007) ("Fifth Order"), JA 793, *order on reh'g and clarification*, 121 FERC ¶ 61,276 (2007) ("Sixth Order"), JA 817; *California Independent System Operator Corp.*, 118 FERC ¶ 61,097 (2007) ("Fourth Order"), JA 676.

STATEMENT OF FACTS

I. Events Leading To The Challenged Orders

A. The Must-Offer Obligation

On April 26, 2001, to help remedy the California energy crisis, the Commission, among other things, implemented a must-offer obligation requiring most generators serving California markets to offer for sale, in real time, all available capacity not already scheduled to run through bilateral agreements. First Order at P 2, JA 432 (citing *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Serv.*, 95 FERC ¶ 61,115 at 61,355-57, *order on reh'g*, 95 FERC ¶ 61,418, *order on reh'g*, 97 FERC ¶ 61,275 (2001), *order on reh'g*, 99 FERC ¶ 61,160 (2002), *pets. granted in part and denied in part, on other grounds sub nom. Pub. Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027 (9th Cir. 2006)). *See also Cal. Dep't of Water Res. v. FERC*, 341 F.3d 906, 909 (9th Cir. 2003) (discussing "must-offer" and related requirements).

B. The Complaint

On August 26, 2005, the Independent Energy Producers filed a complaint with FERC asserting that the must-offer obligation was no longer just and reasonable because it does not provide must-offer generators compensation for their fixed costs. R. 1 at 2, 11 and n.28, 19-21, JA 2, 11, 19-21. Independent Energy Producers noted that "existing units likely face early retirement due to insufficient net revenues received," threatening the continued existence of generation needed to ensure the California ISO grid's reliability. R. 1 at 19-20, JA 19-20. *See also* First Order at PP 6-12, JA 432-33.

Recognizing that efforts to formulate a long-term reliability solution to this problem were in the works, the Independent Energy Producers proposed that the California ISO tariff be amended "to implement an interim set of [Reliability Capacity Services Tariff] provisions" which would assure adequate compensation to must-offer obligation generators until a long-term solution could be implemented. R. 1 at 1, 3, 5, JA 1, 3, 5. Under Independent Energy Producers' proposal, "generating capacity that is not otherwise under a [reliability must run] contract, or under a long-term contract" would be required to provide capacity services that California ISO determines are needed for grid reliability, and those generators would be compensated "based on a regional benchmark of annualized

total fixed costs to add new peaking generation capacity . . . to the electricity system." R. 1 at 5-6, JA 5-6.

Numerous parties intervened and commented. On November 8-9, 2005, Commission Staff held a technical conference regarding the matters raised in the complaint. On November 14, 2005, Independent Energy Producers requested that the Commission defer action on the complaint pending settlement discussions. R. 38 at 1-2, JA 167-68.

C. The Settlement Offer

On March 31, 2006, parties with divergent interests filed an Offer of Settlement, with a proposed effective date of June 1, 2006. R. 43 at 2, JA 183; Third Order at P 48, JA 637. Like the complaint, the settlement proposed the institution of Reliability Capacity Services Tariff rates to "ensur[e] generators are compensated for the needed reliability and capacity that they provide" until long-term reliability measures are implemented. Settlement Offer, R. 43 at 4, JA 185; *see also* First Order at P 5, JA 432.

Under the Settlement, the California ISO would be able to procure capacity by designating Reliability Capacity Services Tariff units when resource adequacy requirements are not being met or when resources procured in meeting resource adequacy requirements are no longer sufficient to maintain reliability standards. Third Order at P 14, JA 627. Reliability Capacity Services Tariff units'

compensation would be based on the estimated cost of new entry, determined by a formula set out in the Settlement Offer. First Order at P 14, JA 434; Settlement Offer, R. 43 at 16-19, JA 224-27. The California ISO also would be able to procure capacity from must-offer generators, who would receive a compensatory capacity payment equal to $1/17^{th}$ of the monthly Reliability Capacity Services Tariff capacity charge for each day they are called on to provide service. R. 43 at 20, JA 228; First Order at P 15 and n.11, JA 434; Third Order at P 18, JA 628.

II. The Challenged Orders

After reviewing the complaint, the settlement offer, and the comments and responses regarding those filings, the Commission determined "that the compensation to generators under the must-offer obligation is no longer just and reasonable" because it "does not adequately compensate generators for the reliability services they provide." First Order at PP 1, 35, 38, JA 430, 439, 440. Specifically, the Commission found that, while "[t]he must-offer obligation requires generators to make their capacity available to the [California ISO]," it does not "provid[e] a mechanism to ensure sufficient fixed costs recovery to keep generation needed for reliability purposes available to the [California ISO]." First Order at P 36, JA 439; *see also id.* at P 37, JA 440 ("given the current compensation structure, we find that generators under the must-offer obligation

may not have sufficient opportunity to recover their fixed costs in the energy market.").

The Commission ordered further paper hearing proceedings to determine whether the proposed Reliability Capacity Services Tariff rates were just and reasonable. First Order at P 38, JA 440. Additionally, in accordance with FPA § 206(b), 16 U.S.C. § 824e(b), the Commission established a refund effective date of August 26, 2005, the date Independent Energy Producers filed the complaint initiating this proceeding. *Id.* at P 41, JA 440.

Moreover, the Commission determined that, "[u]pon approval of interim tariff sheets," it would "implement[] the Offer of Settlement rates on an interim basis, pursuant to Rule 602(h) of [its] regulation," 18 C.F.R. § 385.602(h). Second Order at PP 10, 14, JA 470, 472. In doing so, the Commission "emphasize[d] that the amounts collected by sellers [would be] subject to refund in accordance with [the Commission's] determinations after conclusion of [the] paper hearing procedures." Second Order at P 10, JA 470-71; *see also id.* at P 28, JA 475; First Order at P 40, JA 440.

The California ISO filed the interim tariff sheets on October 20, 2006, R. 141, but they were rejected as moot, Fifth Order at P 64 and Ordering P (B), JA 814, 816, because the Commission had since found, "as a result of the additional evidence provided in the paper hearing," that the Reliability Capacity Services

Tariff rates were just and reasonable. Third Order at P 2, JA 623-24; *see also* Third Order at PP 46, 48, 49, 76, 122, JA 636-37, 645, 656.

NRG Power Marketing, Inc. and West Coast Power LLC ("NRG") "assert[ed] that prospective implementation of the Offer of Settlement as of June 1, 2006 would constitute an insufficient remedy, because generators have been systematically denied just and reasonable compensation for the reliability services that they have provided in the past." Third Order at P 199 and n.21, JA 674, 632. They argued that, "because the Commission correctly found that compensation to generators under the must-offer obligation is not just and reasonable and established a refund effective date of August 26, 2005, the date [Independent Energy Producers] filed [their] original complaint," the Commission should make the settlement effective as of that date. *Id.* at P 199, JA 674. On the other hand, the Cities and Silicon Valley Power argued that the Commission could not make the Reliability Capacity Services Tariff rates effective until the Commission accepted a compliance filing containing those rates. *E.g.*, Fifth Order at PP 32, 34, JA 805.

The Commission rejected NRG's proposal to make the Reliability Capacity Services Tariff rates effective as of the refund effective date (August 26, 2005). Third Order at P 200, JA 674; *see* Cities' Br. at 12 (same). Instead, the Commission "exercise[d] [its] discretion to fashion an appropriate remedy in this

case," and "order[ed] prospective implementation of the Offer of Settlement, as of June 1, 2006, sixty days after the date the Offer of Settlement was filed." Third Order at P 200, JA 674. The Commission found "the Settling Parties' request to have the Offer of Settlement be made effective June 1, 2006 to be reasonable" because it would be too disruptive to the California ISO markets to apply the rate design and market rule changes involved all the way back to August 26, 2005. *Id.* (citing, *e.g.*, *Connecticut Valley Elec. Co. v. FERC*, 208 F.3d 1037, 1044 (D.C. Cir. 2000); *Niagara Mohawk Power Corp. v. FPC*, 379 F.2d 153, 159 (D.C. Cir. 1967)).

In addition, the Commission found no merit to the Cities' and Silicon Valley Power's claim that the Reliability Capacity Services Tariff rates could not be made effective until the Commission accepted a compliance filing containing those rates. As the Commission explained, interested parties had sufficient notice of the Reliability Capacity Services Tariff rates before they took effect on June 1, 2006 and, therefore, the filed rate doctrine and rule against retroactive ratemaking were satisfied. Fifth Order at P 36, JA 806-07; Sixth Order at P 13, JA 822.

SUMMARY OF ARGUMENT

The challenged orders resolved a number of issues regarding compensation for wholesale electricity generators serving California markets. The sole issue on appeal concerns the effective date of Reliability Capacity Services Tariff rates approved in those orders.

The March 31, 2006 Settlement proposed that Reliability Capacity Services Tariff rates, which provide compensation to must-offer obligation generators for the energy they provide, be made effective as of June 1, 2006. Under these circumstances, the Commission reasonably found that interested parties had sufficient notice of the Reliability Capacity Services Tariff rates before they took effect on June 1, 2006, and, therefore, that the filed rate doctrine and rule against retroactive ratemaking were satisfied.

The Cities principally argue that the Commission's notice rationale is irrelevant because, in their view, *Electrical District No. 1 v. FERC*, 774 F.2d 490 (D.C. Cir. 1985), establishes that the Reliability Capacity Services Tariff rates cannot take effect before the Commission accepts a California ISO compliance filing setting forth those rates. However, *Electrical District* was clarified and limited in *Transwestern Pipeline Co. v. FERC*, 897 F.2d 570, 578 (D.C. Cir. 1990). That and other cases make clear that notice is relevant, and the question of whether

the parties received adequate notice of a rate is to be decided on a case-by-case basis, as was done here.

ARGUMENT

I. STANDARD OF REVIEW

The Court reviews FERC orders under the Administrative Procedure Act's arbitrary and capricious standard. *E.g.*, *Sithe/Independence Power Partners v. FERC*, 165 F.3d 944, 948 (D.C. Cir. 1999). Under that standard, the Commission's decision must be reasoned and based upon substantial evidence in the record. For this purpose, the Commission's factual findings are conclusive if supported by substantial evidence. FPA § 313(b), 16 U.S.C. § 825*l*(b).

The Court is "particularly deferential to the Commission's expertise in ratemaking cases, which involve complex industry analyses and difficult policy choices." *North Baja Pipeline, LLC v. FERC*, 483 F.3d 819, 821 (D.C. Cir. 2007) (quoting *Exxon Mobil Corp. v. FERC*, 430 F.3d 1166, 1172 (D.C. Cir. 2005)). *See also Permian Basin Area Rate Cases*, 390 U.S. 747, 790 ("the breadth and complexity of the Commission's responsibilities demand that it be given every reasonable opportunity to formulate methods of regulation appropriate for the solution of its intensely practical difficulties."), quoted in *East Kentucky Power Cooperative, Inc. v. FERC*, 489 F.3d 1299, 1306 (D.C. Cir. 2007).

Furthermore, the Court "owe[s] FERC great deference in reviewing its selection of a remedy, for 'the breadth of agency discretion is, if anything, at its zenith when the action assailed relates primarily . . . to the fashioning of policies, remedies and sanctions." *Louisiana Public Serv. Comm'n v. FERC*, 522 F.3d 378, 393 (D.C. Cir. 2008) (quoting *Niagara Mohawk*, 379 F.2d at 159, and citing *Ariz. Corp. Comm'n v. FERC*, 397 F.3d 952, 956 (D.C. Cir. 2005) (noting that FERC wields maximum discretion when choosing a remedy)).

II. THE COMMISSION REASONABLY EXERCISED ITS BROAD REMEDIAL DISCRETION IN ALLOWING THE SETTLEMENT RATES TO BECOME EFFECTIVE PROSPECTIVELY 60 DAYS AFTER THE SETTLEMENT WAS FILED

The August 26, 2005 complaint initiating the underlying proceedings alleged that the California ISO's existing must-offer obligation tariff rates were no longer just and reasonable, and proposed that they be replaced with Reliability Capacity Services Tariff rates until long-term reliability solutions are implemented. R. 1 at 1-3, 5, 6, 11, 19-21, JA 1-3, 6, 11, 19-21. In accordance with FPA § 206(b), 16 U.S.C. § 824e(b), the Commission established August 26, 2005, the date the complaint was filed, as the refund effective date for this proceeding. First Order at PP 38, 41, JA 440.

The March 31, 2006 Settlement submitted to resolve the complaint proposed that the Reliability Capacity Services Tariff formula rates specified therein be

made effective two months later, on June 1, 2006. R. 43 at 2, 16-20, JA 210, 224-28. The Commission granted that proposal. Third Order at P 200, JA 674; *see also* Fifth Order at P 64 and Ordering P (B), JA 814-15, 816 (accepting the tariff sheets filed in compliance with the Third Order, which "reflect[ed] a June 1, 2006 effective date," Compliance Filing, R. 172 at Transmittal Letter p. 4, JA 728, "effective June 1, 2006"); Sixth Order at P 11, JA 821 (explaining that the Third Order "established prospective implementation of the Offer of Settlement, setting forth an effective date of June 1, 2006.").

The Cities claim that "FERC acted arbitrarily and capriciously and not in accordance with law when it approved collection of [Reliability Capacity Services Tariff] Rates by generators prior to acceptance of a [later] compliance filing setting forth the applicable rates." Br. at 22, *see also* Br. at 23-53. As explained below, the Commission reasonably found otherwise.

A. The Filed Rate Doctrine And The Rule Against Retroactive Ratemaking Were Satisfied As All Parties Were On Notice Of The Settlement Rates Before They Took Effect

"The filed rate doctrine prohibits the Commission from imposing a rate different from the one on file at the time [power] is sold or service made available." *Transwestern*, 897 F.2d at 577. The related rule against retroactive ratemaking prohibits the Commission from "imposing a rate increase for [power] already sold." *NSTAR Elec. & Gas Corp. v. FERC*, 481 F.3d 794, 800 (D.C. Cir.

2007) (quoting *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 578 (1981)). As these principles are intended to "enable purchasers to 'know in advance the consequences of the purchasing decisions they make,'" they are satisfied when "customers receive adequate notice of a rate in advance of the service to which it relates . . . ." *Western Resources, Inc. v. FERC*, 72 F.3d 147, 149-50 (D.C. Cir. 1995) (quoting *Transwestern*, 897 F.2d at 577; citing *Town of Concord v. FERC*, 955 F.2d 67, 75 (D.C. Cir. 1992), and *Columbia Gas Transmission Corp. v. FERC*, 831 F.2d 1135, 1140 (D.C. Cir. 1987)); *see also Pub. Utils. Comm'n of Cal. v. FERC*, 988 F.2d 154, 163-64 (D.C. Cir. 1993); Fifth Order at P 36, JA 806-07 ("The courts have found that as long as the affected parties have notice," the rule against retroactive ratemaking and filed rate doctrine are satisfied); Sixth Order at P 13, JA 822 (same).

"The filed rate doctrine simply does not extend to cases in which buyers are on adequate notice that resolution of some specific issue may cause a later adjustment to the rate being collected at the time of service." *Natural Gas Clearinghouse v. FERC*, 965 F.2d 1066, 1075 (D.C. Cir. 1992). "[I]t is not that notice relieves the Commission of the bar on retroactive ratemaking, but that it 'changes what would be purely retroactive ratemaking into a functionally prospective process by placing the relevant audience on notice at the outset . . . .'" *Id.* (quoting *Columbia Gas Transmission Corp. v. FERC*, 895 F.2d 791, 797 (D.C.

Cir. 1990), and citing *Columbia Gas*, 831 F.2d at 1140-41); *see also Louisiana Public Serv. Comm'n v. FERC*, 482 F.3d 510, 520 (D.C. Cir. 2007) (noting that, under Commission precedent, a refund ordered pursuant to FPA § 206 "would be 'prospective' from the refund date, rather than 'retroactive'") (citing *Blue Ridge Power Agency v. Appalachian Power Co.*, 57 FERC ¶ 61,100 at 61,374 (1991)).

The Commission reasonably found, under the facts here, that the "parties had sufficient notice of the [Reliability Capacity Services Tariff] rates" and, therefore, that the filed rate doctrine and rule against retroactive ratemaking were satisfied. Fifth Order at P 36, JA 806-07. The Settlement Offer, filed on March 31, 2006, proposed specific Reliability Capacity Services Tariff rates to be made effective two months later, on June 1, 2006. *See supra* pp. 6-7 (explaining calculation of Settlement rates based on cost of new generator entry, determined by a formula, and precise capacity payments). The Commission issued a notice of the Settlement Offer on April 14, 2006, R. 44, JA 348, which was published in the Federal Register on April 26, 2006, 71 Fed. Reg. 24,668.

Thus, the affected parties were on adequate notice well before June 1, 2006 that the Reliability Capacity Services Tariff rates specified in the Settlement might be made effective as of June 1, 2006. In fact, the parties were on notice as of the August 26, 2005 complaint proposing the implementation of Reliability Capacity Services Tariff rates that the Commission might make those rates (or some later

revision of those rates) effective as early as the date the complaint was filed. Under FPA § 206(b), 16 U.S.C. § 824e(b), the Commission may set the date a complaint was filed as the refund effective date. *See Port of Seattle v. FERC*, 499 F.3d 1016, 1031 (9th Cir. 2007) (complaint requesting specific refund effective date put parties on notice that that date might serve as the refund effective date).

While the Cities attempt to draw distinctions, for filed rate doctrine and rule against retroactive ratemaking purposes, between filings requesting rate increases and those requesting rate decreases, Br. at 27-28, as well as between rate filings made under FPA § 205 and those made under FPA § 206, Br. at 43-50, the Commission reasonably found no such distinctions. Fifth Order at P 36, JA 806-07. As the Commission explained, the "purpose of the rule against retroactivity, and the closely related filed rate doctrine, is to ensure predictability," and "as long as the affected parties have notice, these concerns are satisfied." *Id.*; Sixth Order at P 13, JA 822. *See also, e.g.*, *Canadian Ass'n of Petroleum Producers v. FERC*, 254 F.3d 289, 299 (D.C. Cir. 2001) ("So long as the parties had adequate notice that surcharges might be imposed in the future, imposition of surcharges does not violate the filed rate doctrine"), quoted in *Louisiana*, 482 F.3d at 520.

B. *Electrical District* Does Not Undercut The Commission's Analysis And Findings

The Cities contend that "[t]he Commission's 'notice' rationale is invalid," Br. at 41 (capitalization in heading altered). In their view, "*Electrical District* makes clear that the notice required is notice of the specific rates, terms, and conditions that will apply as set forth in tariff sheets accepted by the Commission," Br. at 43. In other words, the Cities assert that the Reliability Capacity Services Tariff rates cannot take effect "prior to acceptance of a compliance filing setting forth the applicable rates." Br. at 22. This contention ignores that, in *Transwestern*, 897 F.2d at 577-78, this Court clarified and limited *Electrical District*'s holding.

Electrical District held that the Commission's attempt to make a rate effective as of the date on which the Commission ordered the pipeline to make a compliance filing rather than the date on which the Commission accepted the compliance filing "violated the filed rate requirement because the purchasers did not know the 'numerical rate' they would be charged." *Transwestern*, 897 F.2d at 577 (citing *Electrical District*, 774 F.2d at 492). The Court found that "[p]roviding the necessary predictability is the whole purpose of the filed rate doctrine," but "[in direct frustration of this goal, FERC's new policy of making rates effective as of the date of an order setting forth no more than the basic principles pursuant to

which the new rates are to be calculated would make unforeseeable liabilities a regular consequence of rate adjustments under [FPA] § 206." *Electrical District*, 774 F.2d at 493. *Electrical District* "recognized that specificity of notice is often a matter of degree but rejected as too amorphous a standard that would turn on such degrees. Instead it adopted a bright-line insistence that a numerical rate be 'specified'" before a rate change can go into effect. *Transwestern*, 897 F.2d at 577 (citing *Electrical District*, 774 F.2d at 492-93).

Subsequently, in *Transwestern*, 897 F.2d at 577-78, having found that its "decisions on the necessary notice have not been altogether clear," the Court reconciled *Electrical District* with conflicting Court precedent by explaining that *Electrical District* simply stands for the proposition that the Commission may not "announce some formula and *later* reveal that the formula was to govern from the date of announcement (as it had done in *Electrical District*)." *Transwestern*, 897 F.2d at 578. The Court explicitly recognized that this limiting clarification "fail[ed] to implement [*Electrical District*'s] objective of eliminating the problems of drawing lines as to what notice is adequate . . . ." *Id.*; *see also id.* (FERC-approved rates need not be "specific, absolute numbers" but may follow rate formula or rule).

The Court's precedent since *Electrical District* confirms that the filed rate doctrine and the rule against retroactive ratemaking are satisfied by adequate notice

of a rate, which is to be determined on a case-by-case basis. *See, e.g.*, *Louisiana*, 482 F.3d at 520 (ordering refunds in a complaint proceeding does not violate filed rate doctrine as complaint puts all parties on notice that the Commission might find the challenged methodology unjust and unreasonable); *United Distribution Cos.*, 88 F.3d 1105, 1186 n.94 (D.C. Cir. 1996) (notice of proposed rulemaking put customers on notice that, if they continued to receive service after the date of that notice, they would be responsible for paying the new proposed charges for transactions after that date).

The Cities' contention also ignores that *Electrical District* was issued several years before "Congress added subsection (b) to § 206 of the [FPA], authorizing the Commission to order a refund when the Commission finds an approved rate has become unjust or unreasonable, in 1988." *Louisiana*, 482 F.3d at 519 (citing Regulatory Fairness Act, Pub. L. No. 100-473 § 2, 102 Stat. at 2299-300). The refund effective date set here was August 26, 2005; thus, all parties were on notice that the Reliability Capacity Services Tariff rates, as later approved (and perhaps modified by the Commission) might be made effective as early as that date. *See Transwestern*, 897 F.2d at 578 n.5 (noting that "[t]he rule of *Electrical District* also does not apply when the refund provisions of [the Natural Gas Act or analogous provisions of the FPA] are triggered").

In short, the Cities' reliance on *Electrical District* (and, likewise, on *Public Service Company of New Mexico v. FERC*, 832 F.2d 1201, 1225 (10th Cir. 1987), which followed *Electrical District*'s reasoning) as still standing for the proposition that, as a matter of law, the Reliability Capacity Services Tariff rates could not become effective before the Commission accepted a compliance filing regarding those rates, Br. at 28-35, 38-53, is erroneous.

C. The Commission Precedent Cited By The Cities Does Not Support Their Position

The Cities cite several Commission orders that, they assert, "have recognized the ruling in *Electrical District* and implemented the courts' holdings regarding § 206 rate increases." Br. at 32. None of the cited orders supports the Cities' contention that the Reliability Capacity Services Tariff rates could be made effective only after the Commission accepted a later compliance filing containing those rates.

The first cited case, *Kansas Gas & Electric Company*, 34 FERC ¶ 61,288 at 61,517 (1986), Br. at 32, does not help the Cities, as it was issued before this Court clarified *Electrical District* in *Transwestern*.

Houlton Water Company, 58 FERC ¶ 61,301 at 61,963-64 and n.31 (1992), Br. at 32, is also unhelpful. While that order cited *Electrical District* in stating that any rate increase would be implemented "on a prospective basis," as this Court has

noted, the Commission considers a rate change as of the refund effective date to be prospective. *Louisiana*, 482 F.3d at 520 (citing *Blue Ridge*, 57 FERC at 61,374).

The Cities' citation to *PacifiCorp Electric Operations*, 58 FERC ¶ 61,053 (1992), Br. at 33, also is inapposite. Unlike here, the proponent of the rate increase in *PacifiCorp* requested that the new rate not take effect until after final Commission action in that case. *PacifiCorp*, 58 FERC at 61,111.

Likewise, *Maryland Public Service Commission v. PJM Interconnection, L.L.C.*, 123 FERC ¶ 61,169 (2008), Br. at 33-34, is irrelevant to the circumstances here. In *Maryland*, the complainant requested that the Commission order refunds retroactive to a date more than one year before the complaint, which alleged a tariff violation, was filed. *Maryland*, 123 FERC at PP 5, 50-57. Here, by contrast, the Commission simply granted the Settling Parties' request that the rates proposed in the Settlement be made effective prospectively as of two months after the Settlement was filed – and nine months after the setting of the refund effective date.

D. The Cities Did Not Preserve The Right To Assert Certain Arguments Because They Did Not Raise Them On Rehearing

1. The Cities Did Not Raise On Rehearing The Argument That The Settlement Rates Could Not Be In Effect From The End Of The Fifteen Month Refund Effective Period Until "The Date The Commission Resolved This Case"

The Cities argue in passing that, "[e]ven if . . . the limited refund authority under § 206(b) were deemed to allow rate increases to be implemented as of the date of a complaint, that authority would have terminated on November 26, 2006, fifteen months after the August 26, 2005 refund effective date in this case." Br. at 28 n.19. "Upon the expiration of the limited refund authority," the Cities add, "the rate in effect prior to the complaint prevails until after the Commission resolves the case." Br. at 27.

The Cities failed to raise this argument on rehearing to the Commission, R. 113, JA 457; R. 143, JA 562; R. 169, JA 686; R. 170, JA 708, and, therefore, they are jurisdictionally barred from raising it on appeal. FPA § 313(b), 16 U.S.C. § 825*l*(b) ("No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure to do so.").

As this Court has explained, "[e]nforcement of this provision, which [the Court] ha[s] considered to pose a jurisdictional bar, enables the Commission to correct its own errors, which might obviate judicial review, or to explain why in its

expert judgment the party's objection is not well taken, which facilitates judicial review." *Save Our Sebasticook v. FERC*, 431 F.3d 379, 381 (D.C. Cir. 2005) (citations omitted); *see also California Dep't of Water Res. v. FERC*, 306 F.3d 1121, 1125 (D.C. Cir. 2002); *Town of Norwood v. FERC*, 906 F.2d 772, 774-75 (D.C. Cir. 1990).

Moreover, the "reasonable ground for failure" to raise an objection exception "is reserved for extraordinary situations," *Sebasticook*, 431 F.3d at 381-82 (citing *Wis. Power & Light Co. v. FERC*, 363 F.3d 453, 460 (D.C. Cir. 2004)), not present here. The Cities had ample opportunity to apprise the Commission of this contention in their several rehearing requests, but chose not to do so.

In any event, even if the Cities were correct on this issue, that simply would mean the Reliability Capacity Services Tariff rates could not be in effect from the end of the 15-month refund effective period (the end of November 2006) until either two-and-a-half months later (February 13, 2007) when the Commission issued the Third Order, which found the Reliability Capacity Services Tariff rates just and reasonable, or until six-and-a-half months later (June 11, 2007) when the Commission issued the Fifth Order, which accepted the Reliability Capacity Services Tariff compliance filing. If the Cities had raised this to the Commission, however, the Commission may well have rebalanced the equities and exercised its broad remedial discretion to place the Reliability Capacity Services Tariff rates

into effect earlier in the refund effective period. *See* Third Order at P 200, JA 674 (citing, *e.g.*, *Connecticut Valley*, 208 F.3d at 1044; *Niagara Mohawk*, 379 F.2d at 159). In fact, the Commission could have assured the just and reasonable Reliability Capacity Services Tariff rates were in effect for the same or even a longer period by placing those compensatory rates into effect, as NRG had requested, on August 26, 2005, nine months earlier than it did (June 1, 2006).

2. The Cities Did Not Raise On Rehearing The Claim That The Commission's Orders Are Contradictory As To The Rates' Effective Date

Also for the first time on appeal, the Cities assert that the challenged orders changed course, without explanation, as to the Reliability Capacity Services Tariff rates' effective date. Br. at 35-38. Specifically, the Cities complain that: (1) the First Order "determined that generators could collect increased charges for must-offer sales from the date of that Order (*i.e.*, July 20, 2006), provided that they agreed to refund any amounts collected in excess of the level later determined to be just and reasonable by the Commission," Br. at 35-36 (citing First Order at P 40, JA 440); (2) the Third Order "explicitly rejected a proposal by NRG to permit collection of the increased rates for must-offer service as of August 26, 2005," and "moved the effective date of the rate increase back to June 1, 2006," Br. at 36 (citing Third Order at P 200, JA 674); and (3) the Fifth Order at P 40, JA 808, "suggested the effective date of the must-offer increase would be August 26,

2005," but that was "contradicted . . . by the Commission's finding in the same Order at P 64[, JA 814,] that the Commission would accept the tariff sheets filed by the [California ISO] on March 15, 2007 'to be effective on June 1, 2006,'" Br. at 36-37. As the Cities failed to raise this inconsistency objection in any of their petitions for rehearing to the Commission, R. 113, JA 457; R. 143, JA 562; R. 169, JA 686; R. 170, JA 708, they are jurisdictionally barred from raising it on appeal. FPA §313(b), 16 U.S.C. § 825*l*(b).

This contention fails on its merits as well. First, the Commission explained that it initially intended to allow generators to collect the Reliability Capacity Services Tariff rates effective July 20, 2006, upon approval of interim tariff sheets, as an interim measure subject to refund once the Commission determined the just and reasonable must-offer obligation rates at the end of the paper hearing proceedings. First Order at PP 1, 35-38, 40, JA 430, 439-40; Second Order at PP 10, 14, JA 470-71, 472. The interim Reliability Capacity Services Tariff rates never took effect, however, because the Commission rejected the interim tariff sheets as moot after it found the Reliability Capacity Services Tariff rates just and reasonable. Third Order at PP 2, 200, JA 623-24, 674; Fifth Order P 64 and Ordering P (B), JA 814-15, 816.

The Commission also explained why it rejected NRG's proposal that the Reliability Capacity Services Tariff rates become effective as of the refund

effective date (August 26, 2005), and instead granted the Settling parties' proposal for implementation as of June 1, 2006, sixty days after the date the Settlement Offer was filed. Third Order at P 200, JA 674. The Commission determined, in exercising its broad remedial discretion to fashion remedies, that it would be too disruptive to the California ISO markets to apply the rate design and market rule changes involved here all the way back to August 26, 2005. *Id.* (citing, *e.g.*, *Connecticut Valley*, 208 F.3d at 1044; *Niagara Mohawk*, 379 F.2d at 159).

Finally, while the Cities now claim that the Fifth Order "appeared to adopt two different effective dates for the [Reliability Capacity Services Tariff] rates," both Paragraph 64 and Ordering Paragraph (B) of that order make clear that the Reliability Capacity Services Tariff rates became effective as of June 1, 2006. Fifth Order at P 64, JA 814 (accepting rates "to be effective on June 1, 2006"); *id.* at Ordering P (B), JA 816 (same); *see also* Compliance Filing, R. 172 at Transmittal Letter p. 4, JA 728 (noting that the attached tariff sheets "reflect a June 1, 2006 effective date"); Sixth Order at P 11, JA 821 (noting that the Third Order "established prospective implementation of the Offer of Settlement, setting forth an effective date of June 1, 2006."). The Cities apparently understood this when the Fifth Order issued, as they sought neither clarification nor rehearing regarding this matter.

CONCLUSION

For the foregoing reasons, the petitions for review should be denied.

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September 12, 2008

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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 6,141 words, not including the tables of contents and authorities, the certificates of counsel and the addendum.

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