ORAL ARGUMENT HAS NOT YET BEEN SCHEDULED

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

No. 08-1201

TNA MERCHANT PROJECTS, INC. [formerly CHEHALIS POWER GENERATING, LLC], 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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FEBRUARY 6, 2009

FINAL BRIEF: MARCH 30, 2009

CIRCUIT RULE 28(a)(1) CERTIFICATE

I. Parties and Amici:

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

II. Rulings Under Review:

1. Chehalis Power Generating, L.P., 112 FERC \P 61,144 (2005),

JA 115; and

2. *Chehalis Power Generating, L.P.*, 113 FERC ¶ 61,259 (2005),

JA 133.

III. Related Cases:

Chehalis's previous appeal of the contested orders was dismissed by the

Court because proceedings before the Commission were not final. Chehalis Power

Generating, LLC v. FERC, D.C. Cir. No. 06-1055 (June 16, 2006). Counsel is not

aware of any other related cases pending before this or any other court.

Samuel Soopper Attorney

February 6, 2009

Final Brief: March 30, 2009

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GLOSSARY

Bonneville Bonneville Power Administration

Chehalis Power Generating, LLC, the name

of petitioner during the administrative

proceedings.

Florida Power & Light Co. v. FERC, 617

F.2d 809 (D.C. Cir. 1980)

FPA Federal Power Act

Middle South Energy, Inc. v. FERC, 747

F.2d 763 (D.C. Cir. 1984)

Rehearing Order Chehalis Power Generating, L.P., 113

FERC ¶ 61,259 (2005), JA 133

Southwestern Electric Power Co., 39 FERC

 \P 61,099 (1987).

Suspension Order Chehalis Power Generating, L.P., 112

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 \mathbf{v}_{\bullet}

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

BRIEF OF RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

STATEMENT OF THE ISSUE

Whether the Federal Energy Regulatory Commission (Commission or FERC) reasonably determined that a rate schedule filed by Chehalis Power Generating, LLC (Chehalis), governing its sale of reactive power to the Bonneville

¹ By an order issued January 14, 2009, the Court granted a motion to substitute TNA Merchant Projects, Inc. as petitioner in this appeal in place of Chehalis Power Generating, LLC. For the sake of consistency with the orders on appeal, as well as ease of comprehension, this brief will continue to refer to petitioner as Chehalis.

Power Administration (Bonneville), was for an existing service, and thus subject to the suspension and refund provisions of section 205(e) of the Federal Power Act (FPA), 16 U.S.C. § 824d(e).

STATUTORY AND REGULATORY PROVISIONS

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

STATEMENT OF THE FACTS

I. Statutory and Regulatory Background

A. Rate Filings Under FPA Section 205

Section 201(b) of the FPA, 16 U.S.C. § 824(b), gives the Commission exclusive jurisdiction to regulate the transmission and sale at wholesale of electric energy in interstate commerce. Sections 205(a) and (b) of the Act, 16 U.S.C. §§ 824d(a), (b), direct the Commission to assure that such jurisdictional services are just and reasonable and not unduly discriminatory.

Toward this end, section 205(c) of the Act, 16 U.S.C. § 824d(c), requires public utilities to file with FERC "schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission," as well as "classifications, practices, and regulations affecting such rates and charges," and "all contracts which in any manner affect or relate to such rates, charges, classifications, and services."

Under FPA section 205(d), 16 U.S.C. § 824d(d), "no change shall be made by any public utility in any such rate, charge, classification, or service" on file with the Commission unless the utility gives notice by filing a new schedule "stating plainly the change or changes to be made in the schedule or schedules then in force." *Id.* When a utility files such a "new schedule" under section 205(d), the Commission has authority under section 205(e), 16 U.S.C. § 824d(e), to conduct a hearing concerning the lawfulness of the new rate, to suspend the operation of the rate for up to five months, and to order refunds for the excess of any rate increase the agency subsequently finds to be unjust and unreasonable.

Thus, as this Court has explained:

[T]he Act empowers the Commission to scrutinize, and if necessary to change, any rate filed, whether it is a changed rate or the first rate a utility has ever filed. However, only if a filed rate is a changed rate may the Commission also suspend its operation or allow it into effect subject to refund.

Florida Power & Light Co. v. FERC, 617 F.2d 809, 812 (D.C. Cir. 1980) (footnote omitted); see also Middle South Energy, Inc. v. FERC, 747 F.2d 763 (D.C. Cir. 1984) (Commission has authority to suspend only changes in rates, not initial rate filings).

However, as the Court recognized in *Florida Power & Light*, "[t]he [FPA] does not define initial or changed rates, and it is therefore properly the Commission's task, using its technical expertise, to draw the line between them."

617 F.2d at 814. The Commission performed this task in *Southwestern Electric Power Co.*, 39 FERC ¶ 61,099 (1987), on remand from this Court's decision in *Southwestern Electric Power Co. v. FERC*, 810 F.2d 289 (D.C. Cir. 1987), prospectively establishing a policy that "an initial rate filing is one which provides for a new service to a new customer," *i.e.*, "both the service *and* the customer must be new." 39 FERC at 61,293 (emphasis in original). Therefore, the agency explained, "where the service is new, but the customer is not," or "[w]here a filing provides for the extension of an existing service to a new customer, the filing will be treated as a change in rate." *Id*.

In the Commission's view, this "broadened definition" of a rate change would provide greater refund protection to consumers, thus furthering the FPA's policy to defend "consumers from excessive rates and charges." *Id.* (citing *Towns of Alexandria v. FPC*, 555 F.2d 1020, 1028 (D.C. Cir. 1977) and other cases).

B. The Commission's Reactive Power Pricing Policy

Chehalis's filing before the Commission was a rate schedule "for the provision of Reactive Supply and Voltage Control from Generation Sources Service [*i.e.*, reactive power service] . . . from the Chehalis electric generating facility to the Bonneville Power Administration." R 1 at 1, JA 1. A brief explanation concerning reactive power is thus in order.

In its landmark Order No. 888, requiring non-discriminatory open access

transmission services by public utilities,² the Commission established six "ancillary services . . . necessary for the transmission provider to offer to transmission customers." Order No. 888 at 31,705. One of these services is "Reactive Supply and Voltage Control from Generation Sources," commonly known as reactive power, which helps maintain the proper transmission line voltage for a transaction between a generator and a transmission provider. *Id.* at 31,706. While a transmission system itself may supply reactive power, it is also possible "to use generating facilities to supply reactive power and voltage control." *Id.* It is this generator-supplied reactive power service which the Commission classified as an ancillary service, "which must be unbundled from basic transmission service." *Id.*

In American Electric Power Service Corp., 80 FERC ¶ 63,006 (1997), aff'd, 88 FERC ¶ 61,141 (1999), the Commission approved a specific method for a generator to recover the costs of reactive power supplied to a transmission provider, including an appropriate allocation factor to segregate the costs of

² Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, FERC Stats. & Regs. ¶ 31,036, 61 Fed. Reg. 21,540 (1996), clarified, 76 FERC ¶ 61,009 and 76 FERC ¶ 61,347 (1996), on reh'g, Order No. 888-A, FERC Stats. & Regs. ¶ 31,048, 62 Fed. Reg. 12,274, clarified, 79 FERC ¶ 61,182 (1997), on reh'g, Order No. 888-B, 81 FERC ¶ 61,248, 62 Fed. Reg. 64,688 (1997), on reh'g, Order No. 888-C, 82 FERC ¶ 61,046 (1998), aff'd sub nom. Transmission Access Policy Study Group v. FERC, 225 F.3d 667 (D.C. Cir. 2000), aff'd, New York v. FERC, 535 U.S. 1 (2002).

reactive power production from the production of other electric energy.

II. The Proceeding Before The Commission

Chehalis owns and operates an electric generating facility located in the State of Washington, within the transmission system of the Bonneville Power Administration. R 1 at 2, JA 2. On May 9, 2003, the Commission authorized Chehalis to sell power at market-based rates. *See Chehalis Power Generating, L.P.*, Docket No. ER03-717-000 (May 9, 2003) (unpublished letter order). The facility commenced commercial operation in October 2003. R 1 at 2, JA 2. Prior to that time, in 2001, Chehalis had entered into an interconnection agreement with Bonneville. (For the Court's convenience, a copy is provided in Addendum B to this brief).

On May 31, 2005, Chehalis filed a proposed rate schedule for the provision of reactive power to Bonneville. R 1, JA 1. The filing was predicated on a settlement by the parties that allowed Chehalis to "develop reactive power rates" based on the method previously established by the Commission in *American Electric Power Service Corp. Id.* at 3, JA 3. *See Transalta Centralia Generation, L.L.C.*, 111 FERC ¶ 61,087 (2005) (approving settlement).

On July 27, 2005, in the first order on review here, the Commission accepted the filing by Chehalis, "suspend[ed] it for a nominal period, to become effective

August 1, 2005, as requested, subject to refund," and established "hearing and settlement judge procedures." *Chehalis Power Generating, L.P.*, 112 FERC ¶ 61,144 at P 1 (2005), JA 115 (Suspension Order). The Commission rejected Chehalis's characterization of its tariff as an initial rate schedule, because it did not "involve a new customer and a new service." Suspension Order P 23, JA 120 (footnote and citations omitted).

Chehalis filed a timely request for rehearing before the Commission, asserting that the Commission erred by finding that the rate schedule "was a 'changed' rate that is subject to suspension and refund, rather than an 'initial' rate." R 11 at 1, JA 123.

In the second order on appeal, *Chehalis Power Generating, L.P.*, 113 FERC ¶ 61,259 (2005), JA 133 (Rehearing Order), the Commission denied Chehalis's request for rehearing. The agency held that, under its "well-settled precedent . . . that an initial rate is one that provides for a new service to a new customer," Chehalis's reactive power filing was for a changed rate. Rehearing Order P 10, JA 136 (footnote omitted). This was because, the Commission explained, Chehalis had already been "providing reactive power to [Bonneville]" pursuant to the parties' interconnection agreement. *Id.* P 12, JA 137.³

³ Chehalis's previous appeal of the contested orders was dismissed by the Court because proceedings before the Commission were not final. *See Chehalis Power Generating, LLC v. FERC*, D.C. Cir. No. 06-1055 (June 16, 2006).

Subsequently, a hearing was held before a Commission administrative law judge on whether Chehalis's proposed reactive power rate was just and reasonable. The judge issued an initial decision on January 16, 2006, determining the appropriate rate to be charged by Chehalis. *Chehalis Power Generating, L.P.*, 111 FERC ¶ 63,009 (2007). In an order issued on April 17, 2008, the Commission affirmed in part and reversed in part the initial decision. *Chehalis Power Generating, L.P.*, 123 FERC ¶ 61,038 (2008).

Neither Chehalis nor Bonneville sought further review of the Commission's April 17, 2008, rate order. Thus, the sole issue on appeal is whether the Commission properly determined in the contested orders that Chehalis's reactive power rate filing was subject to suspension and refund.

SUMMARY OF ARGUMENT

The Commission held that Chehalis's rate filing was not an initial rate, and thus was subject to suspension and refund under FPA section 205(e). The agency's decision is amply supported, both factually and legally.

- 1. The Commission determined that because Chehalis had previously been providing reactive power to Bonneville pursuant to the parties' interconnection agreement, its filing was not for an initial rate. Chehalis argues that its interconnection agreement with Bonneville is irrelevant here, and that the Commission's decision is lacking record support. Chehalis nonetheless concedes before this Court, as it did before the agency, that it had been providing reactive power to Bonneville pursuant to the specific terms of their interconnection agreement. In view of this admission by Chehalis, the Commission's conclusion is supported by substantial evidence.
- 2. The contested orders applied the longstanding FERC policy that an initial rate, not subject to suspension and refund, is defined solely as one providing a new service to a new customer. The Commission explained that by broadly defining a changed rate under FPA section 205(e), it was furthering the statutory goal of protecting consumers.

Chehalis argues that the Commission erroneously applied FPA section 205(e) to its filing because Chehalis had never before charged Bonneville a rate for

reactive power. However, the Commission reasonably exercised its broad discretion under the statute in determining that, because Chehalis had previously been providing a jurisdictional service to Bonneville, its filing was governed by FPA section 205(e).

Chehalis also argues that the Commission's decision is contrary to the terms of the FERC regulations governing initial rates. As the Commission explained, the regulations, which do not define initial or changed rates, were in effect when the agency established its initial rate definition, and should not be interpreted in a manner contrary to the FPA's purpose of protecting consumers. The Court should defer to the agency's reasonable reading of its own regulations.

Finally, Chehalis attacks the Commission's reliance on agency precedent.

However, Chehalis not only cites no precedent contrary to the agency decision here, but also concedes that the contested orders are fully consistent with at least one prior FERC decision.

ARGUMENT

I. STANDARD OF REVIEW

The Commission's orders are reviewed under the arbitrary and capricious standard, under which a "court must consider whether the decision was based on a consideration of the relevant factors and whether there has been a clear error of judgment. . . . The court is not empowered to substitute its judgment for that of the agency." *ExxonMobil Gas Marketing Co. v. FERC*, 297 F.3d 1071, 1083 (D.C. Cir. 2002) (citations and internal quotation marks omitted). *See also, e.g., Central Vermont Pub. Serv. Corp. v. FERC*, 214 F.3d 1366, 1369 (D.C. Cir. 2000).

Factual findings by the Commission are conclusive if supported by substantial evidence. FPA § 313(b), 16 U.S.C. § 825*l*(b). Substantial evidence "means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Richardson v. Perales*, 402 U.S. 389, 401 (1971) (quoting *Consolidated Edison Co. v. NLRB*, 305 U.S. 197, 229 (1938)) (internal quotation marks omitted).

- II. THE COMMISSION'S DECISION TO ACCEPT CHEHALIS'S RATE FILING SUBJECT TO REFUND WAS FULLY SUPPORTED, FACTUALLY AND LEGALLY.
 - A. The Commission Reasonably Concluded That Chehalis's Tariff Was For An Existing Service To An Existing Customer.

In applying its established policy limiting initial rates to those providing a new service to a new customer, the Commission understood Chehalis's filing to

present a straightforward factual situation:

Prior to its filing in this proceeding, Chehalis had been providing reactive power to [Bonneville] pursuant to its interconnection agreement with [Bonneville]. As a result, it is not now providing a new service nor is it now providing service to a new customer. Thus, Chehalis's filing is not an initial rate.

Rehearing Order P 12, JA 137. *See also* Suspension Order P 23, JA 120 ("Chehalis has been providing reactive power to [Bonneville] pursuant to an interconnection agreement, albeit without charge").

Chehalis challenges the Commission's factual premise, arguing that its proposed reactive power rate fits within the Commission's definition of an initial rate as "a new service to a new customer." Pet. Br. 17. To this end, Chehalis disputes the Commission's finding that it had been supplying reactive power to Bonneville, asserting that "[t]he existence of the interconnection agreement does not establish previous electric service by Chehalis." *Id.* 18.

However, Chehalis's position is simply not credible. In attempting to explain away the Bonneville interconnection agreement, Chehalis first claims that the Agreement was so immaterial that it "is not in the record of this case." Pet. Br. 18. However, this is not strictly true: while the interconnection agreement is not included in the record on appeal, Chehalis nonetheless itself introduced the agreement with Bonneville as Exhibit No. CPG-42 at the hearing before the FERC administrative law judge in its rate proceeding. The interconnection agreement is

thus part of the agency record upon which the Commission based its ultimate April 17, 2008, ratemaking order in this case (*see supra* p. 8), which Chehalis does not challenge here.

More importantly, as Chehalis's brief explicitly concedes, its own filing with the Commission acknowledged "that the interconnection agreement requires Chehalis to . . . provide reactive power support as a condition of the interconnection." Pet. Br. 19 & n.38 (citing R 1 at 2, JA 2). Indeed, Chehalis's proposed rate schedule itself states that Chehalis "provides . . . Reactive Power Service . . . from its generating facility" to Bonneville "in accordance with" the parties' "Interconnection Service Agreement." R 1, Attachment A at 1, JA 10.

In this circumstance, the Commission's taking official notice of the substance of the interconnection agreement between Chehalis and Bonneville was a routine exercise of its administrative authority. *See, e.g., Wisconsin Power & Light Co. v. FERC*, 363 F.3d 453, 463 (D.C. Cir. 2004) (agency can take notice of "matters known . . . through its cumulative experience and consequent expertise") (citation omitted).

Chehalis also complains that the Commission fails to "reference the specific provisions in the interconnection agreement that supposedly provide[] the foundation" for the Commission's finding that Chehalis has been supplying reactive power service to Bonneville. Pet. Br. 19. Once again, however, before

the agency Chehalis itself identified "Exhibit B of [its] generator interconnection agreement with [Bonneville]" as the provision which "requires Chehalis to . . . provide reactive power support." R 1 at 2, JA 2.

In light of these admissions, Chehalis's argument that "[t]here is simply no evidence in the record" (Pet. Br. 20) that it had been supplying reactive power service to Bonneville simply self-destructs. Thus, the factual basis of the Commission's determination, that Chehalis's reactive power tariff was not for a new service, is fully supported by the record.

B. The Commission's Decision That Chehalis's Filing Was For A Changed Rate Is Legally Sound.

In setting out the legal framework for its decision, the Commission naturally looked to this Court's decisions in *Florida Power* and *Middle South*, *see supra* p. 3, which held that the FPA did not permit the Commission to make initial rates subject to refund. However, as the Commission emphasized, in *Florida Power* the Court had "agreed to defer to the Commission's technical expertise to determine what rates are changed rates and what rates are initial rates, 'unless the Commission's judgment is unreasonable [and] cannot be rationally reconciled with the terms of the [FPA]." Rehearing Order P 10 & n.10, JA 135 (quoting *Florida Power*, 617 F.2d at 815). Similarly, the agency explained, *Middle South* did not attempt to define these terms, but "reaffirmed the latitude that the Commission has to interpret what constitutes a changed rate versus what constitutes an initial rate."

Id. P 10 & n.11, JA 135 (citing Middle South, 747 F.2d at 771 and Florida Power, 617 F.2d at 815).

The Commission went on to describe that, pursuant to the Court's deference on this issue, it had established "well-settled precedent . . . that an initial rate is one that provides for a new service to a new customer." Rehearing Order P 10 & nn. 12 & 13 JA 136 (citing, *e.g.*, *Calpine Oneta Power*, *L.P.*, 103 FERC ¶ 61,338 at P 11 (2003) (finding that Oneta's filing constituted a changed rate because Oneta was already providing reactive power to a transmission provider pursuant to the parties' interconnection agreement, albeit without charge)).

Finally, the Commission relied on *Southwestern Electric Power Co.*, *see supra* p. 4, where the agency had explained its rationale for broadly defining a rate subject to refund under the FPA, namely "to give customers refund protection and, therefore, [to] shield[] them from the ability of utilities to exploit any sort of regulatory lag by filing unjust and unreasonable rates." Rehearing Order P 11, JA 136-137 (footnote omitted).

Chehalis initially denies that it is disputing the Commission's legal standard. Pet. Br. 17 ("Petitioner is not in this case disputing that the FERC may narrowly define an initial rate as a new service to a new customer"). Chehalis nonetheless goes on to make a number of arguments attacking the legal basis of the contested orders.

First, Chehalis argues that the Commission's approach is contrary to the terms of FPA section 205: "When a rate filer has no previous rate filed, or required to be filed, under section 205(c) of the FPA, it is impossible for it to have a change in rate under sections 205(d) and (e)." Pet. Br. 21-22. Essentially, Chehalis appears to be arguing that the Commission was legally forbidden to consider Chehalis's prior service to Bonneville for purposes of determining whether the rate filing was for a rate change under section 205(e).

Chehalis's statutory argument should be rejected. This Court has long recognized that, because of the breadth of the Commission's section 205 authority, encompassing "an infinitude of practices affecting rates and service," it is "obviously left to the Commission, within broad bounds of discretion, to give concrete application to this amorphous directive." *City of Cleveland v. FERC*, 773 F.2d 1368, 1376 (D.C. Cir. 1985) (citation omitted). *See also, e.g., Richard Blumenthal v. FERC*, 552 F.3d 875, 881 (D.C. Cir. 2009) (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") (quoting *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 790 (1968)).

Here, the Commission concluded that, prior to its rate filing, Chehalis had been providing reactive power, a FERC-jurisdictional service, to Bonneville. The

Commission's consideration of that prior service in categorizing Chehalis's filing as one for a rate change easily falls within the agency's broad discretion under section 205.

Chehalis goes on to argue that the Commission's expansive interpretation of a changed rate under section 205 is outdated because Congress has amended FPA section 206, 16 U.S.C. § 824e, to enhance the agency's authority to award refunds. *See* Pet. Br. 25-28. However, as the Commission reasonably explained, the changes to section 206 do not in any way undermine the agency's interpretation here of section 205. Rehearing Order P 11 n.18, JA 137. The amendments to section 206 simply have no legal relevance in this case. As even Chehalis recognizes, distinctions remain between the two statutory sections, including the fact that FPA section 206 provides for only a limited fifteen-month refund period. Pet. Br. 27 n.52.

Chehalis also argues that the Commission's decision is contrary to its own regulations, which Chehalis reads as requiring a "sale" of electric energy with "payment or compensation." Pet. Br. 23 (quoting 18 C.F.R. § 35.2(a)) (internal quotation marks omitted). Therefore, Chehalis maintains, the regulations mandate that there is no "change' in rate schedule when a charge is first proposed." *Id*.

However, this regulatory language does not directly address the issue of whether a rate should be classified as initial or changed. And, as the Commission

explained, the same regulations were in effect when the agency established its policy defining an initial rate as a new service to a new customer. *See* Rehearing Order P 13, JA 137. Moreover, the Commission observed, the "regulations exist to complement rather than supplant the Commission's policy, under the FPA, of protecting customers from inequitable treatment by utilities." *Id.* The Court should defer to this reasonable interpretation by the agency of its regulations. *See, e.g., Western Massachusetts Electric Co. v. FERC*, 165 F.3d 922, 926 (D.C. Cir. 1999) (agency interpretation of its regulations receives "substantial deference" if logically consistent with regulatory language and "serves a permissible regulatory purpose") (quoting *Rollins Envtl. Servs. (NH), Inc. v. EPA*, 937 F.2d 649, 652 (D.C. Cir. 1991)).

Finally, Chehalis attacks the Commission's reliance on agency precedent in a section of its brief entitled "The Precedent Cited by the FERC in its Orders Below Does Not Support the FERC's Determination." Pet. Br. 23. However, unlike most petitioners raising this type of argument, Chehalis does not contend that the contested orders are inconsistent with the cited precedent. Indeed, Chehalis concedes that at least one prior case, *Calpine Oneta Power*, is exactly on point, holding "that a reactive [power] tariff is a change in rates where reactive power had been provided previously without charge." *Id.* 24 (submitting instead that the *Calpine Oneta Power* order "was wrongly decided;" other cited FERC

orders were either based on different facts or on "rule that an initial rate must

involve a new service and new customer, a concept that Petitioner does not

dispute"). Thus, this argument by Chehalis does nothing to further its position.

CONCLUSION

For the reasons stated, the Commission's orders should be affirmed in all

respects and the petition denied.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

In accordance with Fed. R. App. P. 32(a)(7)(C), I hereby certify that this brief contains 3,996 words, not including the tables of contents and authorities, the glossary, the certificate of counsel and this certificate.

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