

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

Nos. 07-73256 and 07-73547 (Consolidated)

**MONTANA CONSUMER COUNSEL, *ET AL.*,
PETITIONERS,**

v.

**FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.**

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

**SUPPLEMENTAL BRIEF FOR RESPONDENT
FEDERAL ENERGY REGULATORY COMMISSION**

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**SUPPLEMENTAL BRIEF OF RESPONDENT
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STATEMENT OF THE ISSUE

As directed by the Court's October 3, 2008 Amended Order, the issue for supplemental briefing is "the effect of the Supreme Court's decision in *Morgan Stanley Capital Group, Inc., v. Pub. Util. Dist. No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), on Petitioners' arguments relying on *Pub. Util. Dist. No. 1 of Snohomish County v. FERC*, 471 F.3d 1053, 1081 (9th Cir. 2006), and *Pub. Utils. Comm'n of Cal. v. FERC*, 474 F.3d 587 (9th Cir. 2006), and on the availability of the remedies sought."

ARGUMENT

The Supreme Court’s decision in *Morgan Stanley* has no effect on the instant case. Though several parties cited in their briefs the underlying decisions of this Court upon which the Supreme Court ruled in *Morgan Stanley*, the Supreme Court’s decision, affirming this Court’s judgment in *Snohomish* on alternative grounds while disagreeing with its analysis,¹ did not affect the issues before the Court in this appeal. The *Morgan Stanley* decision focused on the scope of the “*Mobile-Sierra*” doctrine, concerning modification of wholesale energy contracts, which has no bearing on this case; the Supreme Court expressly refrained from considering the legality of the market-based rate scheme developed by the Federal Energy Regulatory Commission (“Commission” or “FERC”), let alone any aspect of the market power analysis that the Commission uses in granting market-based rate authority.

A. Effect On Petitioners’ Arguments

This case concerns FERC’s decision to allow PPL to retain its authorization to charge market-based rates, over the objections of Petitioners Montana Consumer Counsel and Montana Public Service Commission (collectively “Montana”) to the

¹ See *Morgan Stanley*, 128 S. Ct. at 2749, 2751; see also *id.* at 2759 (Stevens, J., dissenting) (similarly disagreeing with lower court’s analysis). The Supreme Court vacated the judgment in the companion *PUC* case. *Sempra Generation v. Pub. Utils. Comm’n*, 128 S. Ct. 2993 (2008).

design and application of the market power study that FERC uses to grant such authority.

Montana’s Initial Brief cited *Snohomish* and *PUC* for the generic proposition that the Federal Power Act (“FPA”) requirement that wholesale electricity rates be “just and reasonable” applies to all FPA-jurisdictional sales. Montana Br. at 20 (citing, *inter alia*, *Snohomish* and *PUC*); *see also id.* at 25 (“This Court has emphatically held that this statutory command applies to *all* rates.”) (citing *Snohomish*)²; *accord*, Reply Brief of Petitioner-Intervenor REC Silicon Inc. at 6 (“FERC’s responsibility to ensure that rates are just and reasonable exists regardless of whether the Commission is reviewing rates derived using cost-based or market-based methodologies.”) (citing, *inter alia*, *Snohomish*).

² In its Initial Brief, Montana also went further, citing *Snohomish* and *PUC* for the proposition that *contract* rates must be determined to be just and reasonable (Montana Br. at 25) and that the Commission must analyze market power “at the time of the contracts’ formation” (*id.* at 26). As discussed *infra* at p. 7, however, this case arose from the Commission’s decision to renew PPL’s market-based rate authority, *not* from a challenge to the PPL-Northwestern contract itself.

In any event, Montana did not revisit that argument in its Reply Brief, and, except for a passing citation to its Initial Brief (*see* Montana Reply Br. at 2), did not even mention *Snohomish* or *PUC*. Nor had Montana raised that argument before the Commission. *See* FPA § 313(b) (issues not raised in rehearing request are jurisdictionally barred on appeal), 16 U.S.C. § 825l(b). Even if this issue were properly before this Court, the Supreme Court determined in *Morgan Stanley* that rates initially set by contract are presumed to be just and reasonable. *See* 128 S. Ct. at 2745-46.

That basic premise is not disputed. *Cf., e.g., Me. Pub. Utils. Comm'n v. FERC*, 520 F.3d 464, 471-72 (D.C. Cir. 2008) (reaffirming, in decision issued after briefing was completed in this case, that just and reasonable rate need not be tied to costs). But this Court, as well as the D.C. Circuit, has held that market-based rate authority satisfies the Commission's statutory duty under the FPA, if the Commission finds that the applicant lacks (or has effectively mitigated) market power and if there is meaningful subsequent oversight. *See California ex rel. Lockyer v. FERC*, 383 F.3d 1006, 1013 (9th Cir. 2004), *cert. denied sub nom. Coral Power, L.L.C., v. California ex rel. Brown*, 127 S. Ct. 2972 (2007); *Louisiana Energy & Power Auth. v. FERC*, 141 F.3d 364, 365 (D.C. Cir. 1998); FERC Br. at 4, 20-21. *Cf. Montana Br. 26* (contending that *Lockyer*, *Snohomish*, and *PUC* require FERC to find competitive market as prerequisite for granting market-based rate authority).

Morgan Stanley has no effect on that basic proposition, or on the continued precedential value of other cases that directly so held. In *Morgan Stanley*, the Supreme Court recognized that “[b]oth the Ninth Circuit and the D.C. Circuit have generally approved FERC’s scheme of market-based tariffs.” 128 S. Ct. at 2741 (citing *Lockyer* and *Louisiana*). *Cf. FERC Brief at 4, 20-21* (also citing *Lockyer* and *Louisiana*, as well as *Snohomish*, among other cases). Having provided an overview of the Commission’s development of market-based reforms, the Supreme

Court made clear that it would not address the legality of market-based rates in that case:

We have not hitherto approved, *and express no opinion today*, on the lawfulness of the market-based-tariff system, which is *not one of the issues before us*. It suffices for the present cases to recognize that when a seller files a market-based tariff, purchasers no longer have the option of buying electricity at a rate set by tariff and contracts no longer need to be filed with FERC (and subjected to its investigatory power) before going into effect.

128 S. Ct. 2741-42 (emphases added).³ The Court later emphasized that the issue was outside the scope of its decision: “We reiterate that we do not address the lawfulness of FERC’s market-based-rates scheme, which assuredly has its critics. But any needed revision in that scheme is properly addressed in a challenge to the scheme itself” *Id.* at 2747.

That challenge is not presented here. Though Montana hinted at a broader objection to the market-based tariff scheme in its Initial Brief (at 25-26) — but not in its Reply Brief or, more important (*see supra* note 2), in its request for rehearing before the Commission — its extensive arguments in both of its briefs focused on various aspects of the design of FERC’s generation market power standard and the results of its application to PPL.

³ The Court did reaffirm, however, that the Commission is entitled to “great deference” and “broad discretion” in exercising its statutory responsibility to balance investor and consumer interests in determining a “just and reasonable” rate. 128 S. Ct. at 2738; *see also* FERC Br. at 18 (standard of review).

Furthermore, even if Montana did wish to challenge the general lawfulness of market-based rates, the appropriate forum to do so would be FERC's Order No. 697 rulemaking,⁴ and appeal therefrom. *See* FERC Br. at 23. When principal briefing in this appeal was completed in March 2008, the Commission was still considering numerous requests for rehearing of its Order No. 697 rulemaking, including a request filed by Montana Consumer Counsel that raised many of the same issues raised in the instant case.⁵ On April 21, 2008, the Commission issued an Order on Rehearing and Clarification, *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697-A, FERC Stats. & Regs. ¶ 31,268, 123 FERC ¶ 61,055 (2008). A number of parties filed further requests for rehearing, which remain pending before the Commission.⁶

⁴ *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252, 119 FERC ¶ 61,295 (2007) (amending 18 C.F.R. pt. 35, subpt. H).

⁵ Once again, however, Montana Consumer Counsel chose *not* to challenge the legality of market-based rates in general, as several other parties did. *See* Order No. 697-A (defined *infra*) at PP 394-433 (responding to other parties' broad challenges).

⁶ *See* Order on Rehearing and Clarification, *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, 124 FERC ¶ 61,055 at P 4 (July 17, 2008) (addressing one discrete issue but stating that "[t]he remaining issues raised on rehearing of Order No. 697-A will be addressed in a subsequent order"); Order Requesting Supplemental Comments, (continued...)

On May 1, 2008, Petitioner Montana Consumer Counsel filed a petition for review of Order Nos. 697 and 697-A in this Court. *Montana Consumer Counsel v. FERC*, 9th Cir. No. 08-71827. Numerous other parties filed a total of six additional petitions for review in this Court and the D.C. Circuit. *See Revised Statement of Related Cases* (at the end of this Supplemental Brief).

B. Effect On Availability Of Remedies Sought

The Supreme Court’s decision in *Morgan Stanley* also has no effect on the remedies available in this case. Montana challenged FERC orders that found PPL had rebutted the presumption of market power and satisfied the Commission’s generation market power standard for the grant of market-based rate authority. *See PPL Montana, LLC*, 115 FERC ¶ 61,204 at PP 1, 30, 41 (2006), EOR 20, 25, 26, 31; *see also id.* at ordering para. (B) (accepting PPL’s market-based rate tariff), EOR 32. The available remedy, should the Court conclude (as it should not) that the Commission’s rationale cannot be sustained, is a remand to the agency to reconsider its analysis as to PPL’s authorization.

Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities, 124 FERC ¶ 61,213 at P 5 n.11 (Aug. 29, 2008) (noting, while requesting supplemental comments on another discrete issue, that “[o]ther issues have been raised on rehearing of Order No. 697-A and will be addressed in a subsequent order”).

By contrast, *Morgan Stanley* arose from requests to modify the terms of existing long-term contracts, and concerned the applicable standard of review for such modifications. Though Montana's opposition to FERC's grant of market-based rate authority to PPL may be motivated by Montana's dissatisfaction with a long-term contract between PPL and NorthWestern Corporation (which is not a party to this appeal), this case did not arise from a challenge to the terms of that contract, or a request to modify those terms. Indeed, the Commission noted in its Brief that the contract may properly be challenged in a separate proceeding: "PPL's rates, including those set forth in its 2007 contract with NorthWestern, remain subject to the enforcement and complaint procedures available pursuant to FPA § 206, 16 U.S.C. § 824e." FERC Br. at 24 (citing Order No. 697 at PP 333 n.324, 955, 967).

Accordingly, *Morgan Stanley* does not speak to the remedies available in this case.

CONCLUSION

For the reasons stated above and in FERC's Brief, the petitions should be denied, and the challenged FERC Orders should be affirmed in all respects.

Respectfully submitted,

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REVISED STATEMENT OF RELATED CASES

In May and June, 2008, after principal briefing was completed in this case, several related cases were filed in this Court and in the U.S. Court of Appeals for the District of Columbia Circuit. Petitioner Montana Consumer Counsel and other

parties have filed petitions for review of *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252, 119 FERC ¶ 61,295 (2007), which the Commission and other parties cited and discussed in their briefs, and *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697-A, FERC Stats. & Regs. ¶ 31,268, 123 FERC ¶ 61,055 (2008), which Petitioners and PPL addressed in letters submitted pursuant to Federal Rule of Appellate Procedure 28(j). Petitioner Montana Consumer Counsel filed *Montana Consumer Counsel v. FERC*, 9th Cir. No. 08-71827. Other petitions were filed in *Nat'l Rural Elec. Coop. Ass'n v. FERC*, 9th Cir. No. 08-72672; *Transmission Dependent Util. Sys. v. FERC*, 9th Cir. No. 08-72673; and *Am. Pub. Power Ass'n v. FERC*, 9th Cir. No. 08-72675. This Court is holding all four petitions in abeyance pending the outcome of ongoing agency proceedings. In addition, three petitions were filed in *Blumenthal, et al. v. FERC*, D.C. Cir. No. 08-1216; *El Paso E&P Co. v. FERC*, D.C. Cir. No. 08-1220; and *Pub. Citizen, Inc., et al. v. FERC*, D.C. Cir. No. 08-1223. The Commission has moved to transfer those D.C. Circuit petitions to this Court pursuant to 28 U.S.C. § 2112(a).