Mobile-Sierra Doctrine Will Severely Limit Third-Party Challenges to Wholesale Electricity Contracts

by Michael S. Hindus, Joseph H. Fagan and Deborah Carrillo

On January 13, 2010, in an 8-1 decision, the U.S. Supreme Court determined in NRG Power Marketing, LLC v. Maine Public Utilities Commission *(No. 08-674) that the* Mobile-Sierra *doctrine applies even when a wholesale electricity contract rate is challenged by an entity that was not a party to the contract. In so deciding, the Court reversed the DC Circuit's confinement of the doctrine to challenges brought by contracting parties. Thus, regardless of the identity of the challenger, when the parties have so agreed, the Federal Energy Regulatory Commission ("FERC") must presume that a electricity rate in a wholesale electricity contract is just and reasonable unless the FERC concludes that it seriously harms the public interest, a standard that is difficult to meet. Accordingly, the Court has continued to honor the intent of the parties to limit the scope of regulatory review of the deal.*

Under the *Mobile-Sierra* doctrine, the FERC must presume that "contract rates freely negotiated between sophisticated parties meet the just and reasonable standard." This presumption can be overcome only if the FERC determines that the contract seriously harms the public interest. Two years ago, the Court clarified the scope of the *Mobile-Sierra* doctrine by holding that the presumption applies not only to challenges brought by the regulated entities, the sellers, but also to challenges brought by purchasers of wholesale electricity.

The present case stems from the inclusion of a *Mobile-Sierra* provision in a settlement agreement ("Agreement") between New England generators, electricity providers, and power customers. The Agreement established rate-setting mechanisms for sales of capacity. Under the *Mobile-Sierra* provision included in the Agreement, all challenges to the rates set under the Agreement, including challenges by non-settling parties, had to meet the high bar of the public interest test. The FERC approved the Agreement and six

non-settling parties sought review of the FERC's decision in the DC Circuit. Although the DC Circuit upheld FERC's order approving the Agreement, the Court of Appeals agreed with objectors on the issue of the *Mobile-Sierra* provision, holding that the presumption applies only to parties to the contract.

The Decision

According to the Supreme Court, limiting *Mobile-Sierra* to contracting parties would "diminish[] the animating purpose of the doctrine: promotion of 'the stability of supply arrangements which all agree is essential to the health of the [energy] industry.'" Given that the Federal Power Act ("FPA") authorizes, "[a]ny person, electric utility, State, municipality, or State commission," to challenge a rate, in its opinion, the Court observed that if only applied to contracting parties, the *Mobile-Sierra* doctrine would have little stabilizing effect on the industry. However, in his dissent, Justice Stevens argued that while the Court's decision would aid in ensuring stability to the industry thereby promoting the animating purpose of the doctrine, the animating purpose of the FPA, "the protection of the public interest," would not be served. For its part, the majority noted that the public interest is safeguarded by the doctrine's requirement that the FERC reject contracts that seriously harm the public interest.

After reversing the DC Circuit's decision to the extent that it limited the *Mobile-Sierra* doctrine to challenges by contracting parties, the Court remanded two questions to the Court of Appeals. The first question is whether the rate setting methods in the Agreement yielded contract rates covered by the *Mobile-Sierra* doctrine. The Agreement relied on annual auctions to set capacity prices three years prior to actual utilization and transition period payments during the first three years of implementation of the Agreement. The parties challenging the Agreement claimed that the resulting rates were not contractually negotiated rates, thus the presumption does not apply. Second, if the methods did not yield "contract rates," the Court instructed the Court of Appeals to decide whether the FERC had discretion to treat them analogously.

The Significance

As a result of the Court's decision, any party seeking to challenge a rate set by a wholesale energy contract must demonstrate that the contract seriously harms the public interest: by all accounts, a difficult standard to meet. Given such a high bar, third parties will likely have limited success, if any, in contesting rates set by a wholesale energy contract. However, whether the *Mobile-Sierra* doctrine applies to the specific rates at issue in this case remains an open question to be considered by the DC Circuit.

If you have any questions about the content of this alert please contact the Pillsbury attorney with whom you regularly work, or the authors of this advisory:

Michael S. Hindus (bio)
San Francisco
+1.415.983.1851
michael.hindus@pillsburylaw.com

Joseph H. Fagan (bio)
Washington, DC
+1.202.663.9121
joseph.fagan@pillsburylaw.com