103 FERC ¶ 61,355
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, and Nora Mead Brownell.

PacifiCorp	Docket Nos. EL02-80-001
	EL02-80-002
v.	EL02-81-001
	EL02-81-002
Reliant Energy Services, Inc.,	EL02-82-001
Morgan Stanley Capital Group Inc.,	EL02-82-002
Williams Energy Marketing & Trading	EL02-83-001
Company, and	EL02-83-002
El Paso Merchant Energy, L.P.	
	(Consolidated)

ORDER ON INITIAL DECISION, REQUESTS FOR
REHEARING, AND MOTION TO REOPEN RECORD

(Issued June 26, 2003)

1. This case is before the Commission on exceptions to an Initial Decision[1] issued in this proceeding. This proceeding addresses complaints filed by PacifiCorp seeking to modify twelve forward bilateral contracts for delivery of energy entered into during the Western energy crisis of 2000-2001. The complaints allege that dysfunctions in the California electricity spot markets caused these contracts to be unjust and unreasonable, justifying contract modification.

2. In the order issued on June 28, 2002,[2] the Commission set the instant complaints for hearing. After an evidentiary hearing, the Administrative Law Judge (ALJ) concluded that the applicable standard of review intended by the parties for the contracts

---

[1] PacifiCorp v. Reliant Energy Services, Inc., et al., 102 FERC ¶ 63,030 (2003). (Initial Decision).

[2] PacifiCorp v. Reliant Energy Services, Inc., et al., 99 FERC ¶ 61,381 (2003). reh'g pending. (June 28 Order).

at issue here is the "public interest" standard[3] and that the Complainant has failed to meet their burden under this standard of review.

3. In this order, we affirm the ALJ's decision denying the complaints for the reasons stated below. In denying the instant complaints, we have considered the evidentiary record developed in this proceeding, findings of the Commission Staff's Final Report on Price Manipulation in Western Markets in Docket No. PA02-2-000 (Staff Report), and evidence submitted in the 100-Day Discovery Proceeding in Docket No. EL00-95, et al.[4]

4. Specifically, we affirm the ALJ's findings that the applicable standard of review for the contracts at issue here is the "public interest" standard and that, on this record, the Complainant has failed to meet its burden under this standard of review.

5. Before discussing the specific facts of the case before us, it is important to understand the historical context in which the "public interest" standard has been applied by the courts, and the legal parameters within which the Commission must address requests for contract reformation. The "public interest" standard of review was first introduced by the U.S. Supreme Court in the 1956 Mobile case and the concurrently decided Sierra case. The U.S. Supreme Court held that, in order to justify modification of its contract, the seller in that case had to show that the contract rate was so low that it was contrary to the public interest. In the Mobile and Sierra decisions, the Court sought to mesh the respect for the sanctity of contracts under the Federal Power Act (FPA)[5] and Natural Gas Act[6] with the traditional scheme of regulation under these statutes. The Court held that, where the utility and its customer contracted for a particular rate and did not reserve for the seller the right to unilaterally propose a rate change, the utility cannot unilaterally (i.e., without the customer's consent) file a new rate under Section 205 of the

---

[3] See United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332 (1956) (Mobile); FPC v. Sierra Pacific Power, 350 U.S. 348 (1956) (Sierra); and United Gas Pipe Line Co. v. Memphis Light, Gas and Water Div., 358 U.S. 103 (1958).

[4] San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Serv., 101 FERC ¶ 61,186 (2002), order on clarification and reh'g, 102 FERC ¶ 61,164 (2003).

[5] 16 U.S.C. §§ 796 et seq. (2000).

[6] 15 U.S.C. §§ 717 et seq. (2000).

FPA[7] to supersede the agreed-upon rate. The Court also ruled that the Commission's power under Section 206 of the FPA[8] to alter the existing contract rate, after its acceptance by the Commission, is limited.[9]

6. In the Sierra decision, the Court gave examples of factors that would meet the "public interest" standard and allow the selling utility to modify its contract. The selling utility was required to demonstrate that "the rate is so low as to adversely affect the public interest -- as where it might impair the financial ability of a public utility to continue service, cast upon other consumers an excessive burden, or be unduly discriminatory."[10]

7. Both Mobile and Sierra addressed seller challenges to contract rates alleged to be too low. In later cases, the Mobile-Sierra doctrine was applied to contracts containing rates that allegedly were too high.[11] The Mobile and Sierra cases were decided in a cost-based rate regime and consequently dealt with changes proposed to contracts that were already on file with the Commission. The application of the Mobile-Sierra doctrine was later extended to contracts that were not on file with the Commission.[12]

8. In a more recent case involving a long-term, fixed-rate contract, the court held that a showing of "a mere rate disparity or a benefit to the purchasing utility or its customers for a rate modification does not suffice, without more, to satisfy [the 'public interest']

---

[7] 16 U.S.C. § 824d (2000).

[8] 16 U.S.C. § 824e (2000).

[9] Boston Edison Co. v. FERC, 233 F.3d 60, 64-65 (2000) (citing Sierra, 350 U.S. at 352-55; accord Mobile, 350 U.S. at 347).

[10] See Sierra at 355.

[11] See, e.g., Public Service Commission of the State of New York v. FPC, 543 F.2d 757, 798 (D.C. Cir. 1974).

[12] See, e.g., Richmond Power & Light v. FPC, 481 F.2d 490, 493 (D.C. Cir. 1973) (holding that "the contract between the parties governs the legality of the filing. Rate filings consistent with contractual obligations are valid; rate filings inconsistent with contractual obligations are invalid."). Borough of Lansdale, Pennsylvania v. FPC, 494 F.2d 1104, 1112 (D.C. Cir. 1974).

standard."[13] In PEPCO, the court also noted that the purchaser seeking a lower rate failed to "offer any evidence (beyond speculation) that the only potential non-parties here, its ratepayers, were adversely affected by the existing rates; it did not, for example, even attempt to show how much if any of the rate disparity was passed on to PEPCO ratepayers rather than borne by the utility itself."[14] While PEPCO claimed an excessive burden on its customers and discriminatory impact from the disparity between the contract rates and the OATT rate charged by the same transmission provider, the court said that "other than pointing out that the contract rate is twice [Allegheny's] OATT rate, [PEPCO] has presented no evidence regarding how the contract rates are unduly discriminatory or excessively burdensome on PEPCO ratepayers."[15] The court noted the Commission's precedent which holds that "the fact that a contract has become uneconomic to one of the parties does not necessarily render the contract contrary to the public interest."[16]

9. Based on our review of the evidence and the totality of circumstances, we conclude that the Complainant has failed to meet its burden of proof under the "public interest" standard, as defined in past cases. We find that the challenged contracts are not contrary to the public interest because the Complainant has failed to demonstrate that the contracts in question caused financial distress for the Complainant so as to threaten its ability to continue service, that the contracts cast an excessive burden on other customers, that the contracts were unduly discriminatory to the detriment of other customers that are not parties to this proceeding, or that any other factors on this record demonstrate that the

---

[13] See Potomac Electric Power Company v. FERC, 210 F.3d 403, 404 (D.C. Cir. 2000).

[14] Id. at 408.

[15] Id. at 409.

[16] See, e.g., Gulf States Utilities Company v. Southern Company Services, Inc., et al., Opinion No. 300, 43 FERC ¶ 61,003, at 61,016, reh'g denied, Opinion No. 300-A, 43 FERC ¶ 61,394 (1988), aff'd sub nom. Gulf States Utilities Company v. FERC, 886 F.2d 442 (1989); accord Soyland Power Cooperative, Inc. v. Central Illinois Public Service Company, 51 FERC ¶ 61,004, at 61,014-15, reh'g dismissed as moot, 52 FERC ¶ 61,149 (1990); Public Service Company of New Mexico, 43 FERC ¶ 61,469, at 62,152, reh'g denied, 45 FERC ¶ 61,034 (1988), aff'd sub nom. San Diego Gas & Electric Company v. FERC, 904 F.2d 727 (D.C. Cir. 1990).

contracts are contrary to the public interest. At the time of contract execution, other alternatives were available to the Complainant; however, it chose to enter into the contracts in question, accepting market risks. The Complainant benefitted from resales of the energy purchased under these contracts during the relevant period; however, after the drop in prices in mid-2001, the Complainant became dissatisfied with their bargains and sought contract modification. The law is quite clear on that point. The fact that a contract becomes uneconomic over time does not render it contrary to the public interest. We therefore deny the instant complaints.

10. We deny requests for rehearing, as discussed below. We will also address PacifiCorp's motion to reopen the record.

11. This order is in the public interest because it balances effective rate regulation with respect for the sanctity of contracts, as dictated by the U.S. Supreme Court under the Mobile-Sierra doctrine.

I. Background

12. On July 26, 2000, the Commission issued an order initiating an investigation of the conditions of bulk power markets in various regions of the country.[17] On August 2, 2000, San Diego Gas & Electric Company filed a complaint, requesting that the Commission impose a $250 price cap for sales into the California Independent System Operator (ISO) and Power Exchange (PX) spot markets. The Commission denied the request in an order issued on August 23, 2000.[18] In that order, the Commission instituted hearing procedures to investigate the justness and reasonableness of the rates of public utility sellers into the California ISO and PX markets. The hearing was held in abeyance pending completion of the Commission Staff fact-finding investigation of the conditions of bulk power markets, which was completed in October 2000.

13. On November 1, 2000, the Commission issued an order proposing measures to address the dysfunctions in the California market and remedy the problems identified by the Staff investigation.[19] The Commission specifically identified the following rules and regulatory policies as flawed: the California Public Utilities Commission's (CPUC) requirement that the three California Investor-Owned Utilities (IOUs) buy and sell all

---

[17] Order Directing Staff Investigation, 92 FERC ¶ 61,160 (2000).

[18] San Diego Gas & Electric Co., 92 FERC ¶ 61,172 (2000).

[19] San Diego Gas & Electric Co., 93 FERC ¶ 61,121 (2000).

their energy needs through the PX; the CPUC restrictions on the IOUs' ability to contract forward; the lack of retail demand responsiveness; and underscheduling due to the ISO's replacement reserves policies.[20] To correct the above identified market design problems, the Commission proposed, among other things, elimination of the requirement that the California IOUs sell all their generation into and buy all their requirements from the PX.

14. On December 15, 2000, the Commission issued an order [21] adopting, among other things, a benchmark price to provide guidance for assessing the prices of long-term electric supply contracts;[22] and market monitoring and price mitigation for the ISO and PX spot markets, including a $150 per MW price breakpoint.

15. Subsequent orders issued on April 26, 2001[23] and June 19, 2001[24] adopted further market monitoring and mitigation measures for the California markets, and extended those measures to all Western markets.

16. To put the contracts at issue in this case in context, PacifiCorp's contracts were executed during April, May and June 2001. On May 2, 2002, PacifiCorp filed separate complaints against the following four entities: Reliant Energy Services, Inc. (Reliant), Morgan Stanley Capital Group Inc. (Morgan Stanley), Williams Energy Marketing & Trading Company (Williams), and El Paso Merchant Energy, L.P. (El Paso).[25] These complaints seek to modify short-term, 90-day, contracts for delivery of power from July 1, 2002 to September 30, 2002 at prices ranging from $126 to $226 per MWh. Half of these transactions were entered into pursuant to the agreement based on the Edison Electric Institute Master Agreement (EEI Master Agreement), and other contracts were executed pursuant to the Western Systems Power Pool (WSPP) Agreement. During the

---

[20] Id. at 61,354-5.

[21] San Diego Gas and Electric v. Sellers of Energy, 93 FERC ¶ 61,294 (2000).

[22] The benchmark for five year contracts for supply around–the-clock was set at $74/MWh. Id. at 61,994.

[23] San Diego Gas & Electric Co., 95 FERC ¶ 61,115 (2001) (April 26 Order).

[24] San Diego Gas & Electric Co., 95 FERC ¶ 61,418 (2001) (June 19 Order) .

[25] Initially, along with these four complaints, PacifiCorp also filed a complaint against Enron Power Marketing, Inc. (Enron) in Docket No. EL02-84-000. However, on June 21, 2002, PacifiCorp filed a Notice of Withdrawal of Complaint against Enron, stating that the contracts between PacifiCorp and Enron had been terminated.

relevant period the Complainant entered into a large number of contracts for purchase as well as for sale of energy; however, out of all these contracts the Complainant seeks to modify only a relatively small number of contracts included in the instant complaints.

17. On June 28, 2002, the Commission issued an order setting the instant complaints for a trial-type evidentiary hearing. In the June 28 Order, the Commission instructed the ALJ to examine the following issues: (1) whether the challenged contracts should be reviewed under the "just and reasonable" standard or the more stringent "public interest" standard of review; and (2) whether the dysfunctional California ISO and PX spot markets adversely affected Western long-term bilateral markets, and if so, whether contract modification is warranted.

18. The hearing on these issues was held from December 13, 2002 to January 3, 2003. The Initial Decision was issued on February 26, 2002. In the Initial Decision, the ALJ found that the Mobile-Sierra "public interest" standard of review applies to the contracts at issue and that the Complainant failed to satisfy its burden of proof under the "public interest" standard, to justify contract modification. Accordingly, the ALJ dismissed PacifiCorp's complaints with prejudice. Briefs on and opposing exceptions were filed by PacifiCorp., Respondents jointly, the Commission Trial Staff (Staff) and an intervenor, Public Utility District No. 1 Snohomish County, Washington (Snohomish).

19. On November 20, 2002, the Commission issued an order allowing parties in the Docket No. EL00-95, et al. proceeding to adduce evidence that was either indicative or counter-indicative of market manipulation that may have occurred during the California energy crisis of 2000-2001 (100-Day Discovery Proceeding).[26] The submission of evidence in the 100-Day Discovery Proceeding was completed on March 20, 2003.

20. On March 26, 2003, the Commission released the Staff Report. The Staff Report, among other things, found that many spot market trading strategies undertaken by certain sellers were in violation of anti-gaming provisions of the Commission-approved tariffs for the California ISO and PX. Upon Staff's recommendation, the Commission issued certain "show cause" orders requiring the named market participants to respond to market manipulation allegations of the Staff Report. Additionally, the Staff Report addressed the issue of whether the dysfunctional spot market had an impact on the forward prices reflected in long-term power supply contracts. The Staff Report analysis found that spot prices influenced forward prices negotiated during the January 1, 2000 through June 21, 2001 crisis period and that the influence was the greatest for contracts with one to two

[26] See supra n.4.

years terms.
21. Subsequent to release of the Staff Report, PacifiCorp requested an opportunity to have oral argument before the full Commission. On May 1, 2003, the Commission granted this request. The oral argument took place on May 15, 2003.

II. Issues for Discussion

A. Applicable Standard of Review

22. In the June 28 Order, the Commission set for hearing the issue of whether the applicable standard of review for the Complainant to prevail is that a challenged contract was contrary to the public interest, or that the contract was not just and reasonable. The Commission determined that certain contracts identified by PacifiCorp were made subject to the WSPP Agreement appearing to have a contractual provision which may affect parties' rights to make changes to contracts entered into under the WSPP Agreement. The Commission noted that this provision addressed sellers' rights under Section 205 of the Federal Power Act (FPA),[27] not buyers' FPA Section 206[28] rights, to modify rates affecting WSPP transactions. The Commission also found that other contracts were based on the EEI Master Agreement which does not contain a specific provision addressing the parties' rights under the FPA.

1. Initial Decision

23. The ALJ ruled that the applicable standard of review for the instant complaints is the "public interest" standard.[29] In particular, the ALJ found that there is no language in any of the challenged contracts susceptible of the construction that the rates set forth therein may be altered in any manner except by mutual consent of the parties. The ALJ's conclusion was based on the fact that the EEI Master contract and the Confirmations entered thereunder are silent on the subject. The ALJ found that Section 6.1 of the WSPP Agreement[30] is also silent on the ability of a party to apply unilaterally to the

---

[27] 16 U.S.C. § 824d (2000).

[28] 16 U.S.C. § 824e (2000).

[29] See Initial Decision, slip opin., at 10.

[30] Section 6.1 of the WSPP Agreement states in part as follows: "Nothing contained herein shall be construed as affecting in any way the rights of the Parties to
(continued...)

Commission for a change in rates, terms, or conditions agreed upon by the parties. According to the ALJ, Section 6.1 seems to say only that the parties to the contract may jointly apply to the Commission for such a change.[31]

24. The ALJ identified two reasons explaining why neither the text of the contracts nor the circumstances surrounding their creation address the criteria for changing the rates agreed to by the parties. First, according to the ALJ’s finding, the parties did not expect the rates to change; in a competitive marketplace, the obligations of the parties to commodity futures contracts are "firm," at least in the absence of some catastrophic occurrence in the nature of a world war. Second, the ALJ found that the contracts are short-term arrangements calling for deliveries of electricity and payment of the prices during a period of only 90 days. In the ALJ's opinion, in that context, it could hardly have occurred to either PacifiCorp or any of the Respondents that PacifiCorp, or its counterparty, might apply to the Commission for a change in the contract prices.[32] The ALJ thus concluded that the parties' silence on the subject of the methodology for changing the rates, terms and conditions of their bargains means that the Mobile-Sierra doctrine applies to the 12 contracts at issue in this proceeding and prohibits the Commission from changing the contract rates in the absence of a finding that the "public interest" standard has been satisfied.[33]

25. In addition, the ALJ dismissed PacifiCorp's argument that the Mobile-Sierra doctrine does not apply to contracts made under market-based rate authority. The ALJ stated that if PacifiCorp's argument were correct, no contract made under market-based authority would be valid.[34] The ALJ also disagreed with PacifiCorp's contention that the “public interest” standard does not apply to the contracts at issue because, although both the EEI Master Agreement and the WSPP Agreement may have

---

[30](...continued)
jointly make application to FERC for a change in the rates and charges, classification, service, terms, or conditions affecting WSPP transactions under Section 205 of the Federal Power Act and pursuant to FERC rules and regulations promulgated thereunder..."

[31] See Initial Decision, slip opin., at 9.

[32] Id. at 8.

[33] Id. at 10.

[34] Id. at 10 and 11 .

been filed with the Commission in other proceedings, the specific 12 Confirmation Agreements at issue here "have never been filed, reviewed, or accepted by the Commission."[35] The ALJ noted that the Commission expressly and definitively rejected that proposition.[36] The ALJ stated that the rules for sellers in Respondents' category holding market-based rate authority do not require them to file contracts for Commission review before the contracts may be placed into effect, and all that is required is periodic transaction reports.[37] The ALJ reasoned that if neither party to a market-based rate transaction could be assured that the transaction could be legally enforced without first securing Commission approval of their agreement, no one except a vertically-integrated electric utility with the legal right and ability to pass through its costs to ratepayers would bother to participate in the marketplace or would risk the capital to do so.[38]

2. Exceptions

26. On exceptions to the Initial Decision, PacifiCorp argues that in the market-based rate context, the contracts that are silent regarding the applicable standard of review must be evaluated using the "just and reasonable" standard. PacifiCorp explains that because in a market-based rate contract, specific rates are only reviewed by the Commission after implementation, the imposition of the "public interest" standard of review, in essence, circumvents the protections afforded to market participants by the FPA. PacifiCorp adds that they did not intend to waive their right to have the challenged contracts to be reviewed under the "just and reasonable" standard. Further, it states that the ALJ's ruling is inconsistent with the Proposed Policy Statement.[39] PacifiCorp also argues that the ALJ erred in failing to apply a flexible "public interest" standard to the contracts in question. Snohomish supports PacifiCorp's position.

---

[35] Id. at 10-12.

[36] The ALJ cited to State of California ex rel. Lockyer v. British Columbia Power Exchange Corp., 99 FERC P61, 247, reh'g denied, 100 FERC P61,295 (2002), appeal filed sub nom. State of California v. FERC, No. 02-73093, 9th Cir. See Id. at 11-12.

[37] The ALJ cited to Order No. 2001 Revised Public Utility Filing Requirements, FERC Stats. & Regs. ¶ 31,127 (2002) and PacifiCorp Power Marketing, Inc., 74 FERC ¶ 61,139 (1996). See Id. at 12.

[38] Id. at 11.

[39] Standard of Review for Proposed Changes of Market-Based Rate Contracts for Wholesale Sales of Electric Energy by Public Utilities, 100 FERC ¶ 61,145 (2002).

27. Respondents and Staff argue that the ALJ properly applied the "public interest" standard of review to the contracts at issue. They disagree with PacifiCorp's and Snohomish's assertion that the "public interest" standard of review does not apply to the challenged contracts because they have not been previously filed with the Commission. In Respondents' opinion, the application of the Mobile-Sierra doctrine cannot depend on the filing and approval of a contract where no such approval process is available. Staff believes that PacifiCorp's position is a collateral attack on the Commission's market-based rate policy. Furthermore, Respondents and Staff argue that the ALJ's conclusion that contractual silence implicates the "public interest" standard is consistent with past precedent and does not contradict the Proposed Policy Statement, which, if adopted, will not apply retroactively. In addition, Respondents argue that application of a flexible "public interest" standard is not warranted in this case, as the Mobile-Sierra doctrine does not distinguish between a seller's and buyer's challenges to a contract.

3. Commission Determination

28. The issue of the applicable standard of review was set for hearing because we did not believe that we had a sufficient record to definitively address the Mobile-Sierra issue. We now have the benefit of a complete evidentiary record on the issue of the applicable standard of review. The record shows that the challenged contracts were entered into under two standardized agreements, EEI Master Agreement and WSPP Agreement[40] and, consequently, incorporate theirs terms and conditions.

29. The WSPP Agreement contains a provision, Section 6.1, which allows parties to jointly seek modification of the rates, terms and conditions of a contract under FPA Section 205, but does not address customer rights to file a complaint pursuant to FPA Section 206. On first glance, Section 6.1 is confusing since Section 205 is the statutory provision by which a seller makes a rate change filing[41] and Section 206 is the provision by which a non-seller (purchaser or other affected person) may seek a rate change. However, we conclude that the reference to a "joint" Section 205 filing evidences an intent that neither seller nor buyer be able to seek changes under Section 205 or 206 of the FPA other than under the "public interest" standard of review. Although the parties

---

[40] PacifiCorp's Complaints at 2 and 7; Ex. RES-1 at 5.

[41] Section 205 applies only to rate changes by public utility sellers. Thus, a buyer under a contract does not file either individually or jointly for a rate change under Section 205. It may intervene in support of a public utility's Section 205 rate filing but does not institute rate change filings under that Section.

could have used specific language disallowing a unilateral filing by the seller under Section 205, or the filing of a complaint by the buyer under Section 206 of the FPA, the most reasonable reading of Section 6.1 is that they intended to exclude any unilateral filings at the Commission. As explained in the Initial Decision on very similar complaints in the Nevada Power proceeding, "under the maxim 'expressio unius est exclusio alterius,' (the expression of one thing is the exclusion of the other), the only interpretation of Section 6.1 of the [WSPP Agreement] is that the parties thought about, contemplated, and provided for applications to FERC, excluding all applications not specifically provided for in the contracts."[42] Therefore, the parties to the challenged contracts did not intend to retain for the Complainant the right to unilaterally seek changes to its contracts. Thus, we conclude that the Complainant must demonstrate that the contracts entered under the WSPP Agreement are contrary to the public interest in order to support modification of the contracts.

30. The other group of contracts being challenged by PacifiCorp was executed pursuant to the EEI Master Agreement. Unlike the WSPP Agreement, the EEI Master Agreement is completely silent on the subject of the applicable standard of review. The burden was on the Complainant to present evidence on the parties' intent as to the

[42]Nevada Power Co. and Sierra Pacific Power Co. v. Enron Power Marketing, Inc., et al., 101 FERC ¶ 63,031, at 65,276 (2002) . An opposite interpretation would fly in the face of the D.C. Circuit Court decision in Texaco Inc. v. FERC, 148 F.3d 1091 (D.C. Cir. 1998). Mojave, a natural gas pipeline company, and Texaco, a shipper, entered into service agreements that established a formula rate for transportation services and in which Mojave agreed that it "shall not exercise [its] rights under Section 4 of the [NGA] to change the rates to be paid by the Shipper." Id. at 1095. In subsequent proceedings to reform the contracts, the Commission found that the contracts were not subject to the Mobile-Sierra doctrine because "by expressly prohibiting only unilateral rate changes proposed under NGA Section 4, the contracts . . . implicitly recognize the Commission's ability to take the instant Section 5 action." Id., quoting Mojave Pipeline Co., 62 FERC ¶ 61,195 at 62,365 (1993). The Court rejected the Commission's approach and explained that "the law is quite clear: absent contractual language 'susceptible to the construction that the rate may be altered while the contract[] subsists,' the Mobile-Sierra doctrine applies." Id., 158 F.3d at 1096, quoting Appalachian Power Co. v. FPC, 529 F.2d 342, 348 (D.C. Cir. 1976). Sections 4 and 5 of the NGA are similar to Sections 205 and 206 of the FPA and should be interpreted consistently. Transmission Access Policy Study Group v. FERC, 225 F.3d 667, 686 (D.C. Cir. 2000). Our conclusion that contracts entered into pursuant to the terms and conditions set forth in the WSPP Agreement are subject to the Mobile-Sierra doctrine is consistent with Texaco.

applicable standard of review. The Complainant, however, failed to offer extrinsic evidence on this point.[43] We thus have to rely on other evidence in the record and the ALJ's analysis of that evidence to make a determination on this issue. The record demonstrates that the contracts at issue were brokered transactions, i.e., a broker matched bids and offers between parties who did not negotiate with each other on a face-to-face basis.[44] These contracts are short-term arrangements calling for deliveries of electricity and payment of the prices during a period of only 90 days. The ALJ also found that the parties did not expect the rates to change[45] and that "in a competitive marketplace, the obligations of the parties to commodity futures contracts are 'firm,' at least in the absence of some catastrophic occurrence in the nature of a world war."[46] The ALJ thus concluded that "in that context, it could hardly have occurred to either PacifiCorp or any of the Respondents that it, or its counterparty, might apply to the Commission for a change in the contract prices."[47] We agree with the ALJ that in the circumstances presented in this record, the parties could not have contemplated that their contracts would be modified in the absence of some unforeseen extraordinary circumstances. We thus find that the challenged contracts entered into pursuant to the EEI Master Agreement must also be reviewed under the "public interest" standard.

31. PacifiCorp also asserted that applying the "public interest" standard in the instant case would be inconsistent with the Proposed Policy Statement. Under the Proposed Policy Statement, unless a contract contains the proposed language, the "just and reasonable" standard of review would apply to the contract.[48] If adopted, the Policy

---

[43] See Initial Decision, slip opin., at 8. We also note that PacifiCorp provided only conclusory allegations on the issue of the applicable standard of review. That is, no PacifiCorp witness testified that the parties communicated to each other an intent to adopt either of the standards of review, or that PacifiCorp unilaterally expressed its intent to its broker or counterparty.

[44] Id. at 2.

[45] Id. at 35.

[46] Id. at 8-9.

[47] Id. at 9.

[48] Two Commissioners issued a joint concurrent statement to the Proposed Policy Statement stating that the "public interest" standard of review should apply in the absence

(continued...)

Statement will apply on the prospective basis only, specifically to contracts entered into 30-day after the date of issuance of the Final Policy Statement. Numerous parties filed comments to the Proposed Policy Statement raising various issues. The Commission will issue a Final Policy Statement after careful consideration of the comments.

32. The Complainant also argues that the "public interest" standard does not apply to the market-based rate contracts at issue here because these contracts have not been previously reviewed and accepted for filing by the Commission. The need for prior Commission review in these circumstances was met when, after determining that the Respondents lacked market power or had taken steps to mitigate it, the Commission authorized all of the Respondents in this proceeding to make sales of power at market-based rates.[49] A seller that has been granted market-based rate authority may enter into power sales contracts without first seeking Commission authorization of the provisions of an individual contract (except for certain affiliate contracts). The Commission is not required specifically to review each agreement since the Commission, when it grants umbrella market-based rate authorization, pre-determines that rates under future contracts entered into pursuant to the market-based rate authorization will be just and reasonable. The "just and reasonable" standard of Section 205(e) of the FPA[50] is satisfied by the Commission's determination that the utility (and its affiliates) lacks market power or has taken sufficient steps to mitigate market power.[51] As noted in GWF Energy, LLC,[52] if we were required to examine every long-term service agreement as if the seller was seeking new market-based rate authority, it would make the original grant of market-based rate authority (i.e., the original acceptance of the market-based rate tariff) a pointless exercise of no value to anyone. For these reasons, the Commission has

[48](...continued)
of contractual language to the contrary.

[49] See Morgan Stanley Capital Group, Inc., 69 FERC ¶ 61,175 (1994); Noram Energy Services Inc., Director Letter Order, Docket No. ER94-1247-000 (July 25, 1994); Tenneco Energy Marketing Company, Director Letter Order, Docket No. ER95-428-000 (March 30 ,1995); Transco Power Trading Company, Director Letter Order, Docket No. ER95-305-000 (May 10, 1995).

[50] 16 U.S.C. § 824d(e) (2000).

[51] See, e.g., State of California ex rel. Bill Lockyer v. British Columbia Power Exchange Corp., et al., 99 FERC ¶ 61,247, at 62,063 (2002).

[52] See GWF Energy, LLC, et al., 98 FERC ¶ 61,330, at 62,390 (2002).

expressly excluded from the subjects set for hearing issues concerning the Commission's policies on granting market-based rate authority or on regulation of sellers with such authority.[53]

B. Whether Contract Modification is Warranted under the "Public Interest" Standard of Review

33. In its complaint, PacifiCorp alleged that the prices in its forward bilateral contracts were the product of the California ISO and PX spot market dysfunctions. In the June 28 Order, we concluded that in the evidence presented thus far, the Complainant failed to show that the dysfunctional California ISO and PX spot markets had an adverse effect on the long-term bilateral markets in the West. We further stated that to meet its burden of proof to reform these market-based contracts, the Complainant would need to demonstrate that there was such an adverse effect and, if so, whether modification of any individual contract at issue is warranted.[54]

34. To this end, the Commission instructed the ALJ to consider and the parties to submit evidence on the totality of purchases and sales and the conditions present at the time the contracts were entered into. In particular, the Commission proposed the following list of evidentiary factors: (1) Complainant's overall portfolio as well as their own sales (e.g., pattern, duration, price); (2) whether Complainant's transactions were physical or financial in nature and designed to serve Complainant's load; (3) the terms, conditions and rate over the entire duration of each contract (e.g., whether the contract is front-end loaded); (4) what other alternatives were available to the buyer and sellers; (5) whether at the time it was a reasonable decision to enter into these contracts (e.g., duration, scope and time period, and the participants' expectations as to the duration of dysfunctions in the California ISO and PX markets); (6) the terms and conditions of any request for proposals, and the process and procedures the complainants used to evaluate the contracts, including any changes in offered rates, terms, and conditions mandated or negotiated by the Complainant; and (7) the relation of the contract rates to the Commission's previously identified benchmark for long-term contracts. The parties were also encouraged to present evidence on: (1) the effect of the contracts on the financial health of Complainants; (2) the effect of the contracts on wholesale and retail customers; (3) the impacts contract modification may have on the nation's energy markets, including, but not limited to, impacts on investment in new generation and transmission infrastructure, and effect on confidence in competitive markets; (4) the willingness of

---

[53] See June 28 Order at 62,615.

[54] Id.

market participants to enter into long-term contracts in the future and the prices and terms and conditions of such contracts; and (5) the potential modification of other existing energy contracts.

1. Initial Decision

35. As an initial matter, the ALJ made certain findings of fact in regard to the circumstances surrounding execution of the contract. In particular, it was found that all challenged contracts are standard products arranged by independent third party brokers.[55] The brokers located for PacifiCorp several counterparties who quoted prices that PacifiCorp found acceptable and were willing to do business with the utility under either the WSPP Agreement or EEI Master Agreement.[56] With one possible exception, PacifiCorp had no idea of who its counterparties were until the confirmations arrived in its mailbox.[57] The ALJ also found that using brokers' services to find acceptable counterparties had been PacifiCorp's purchasing strategy for quite a while. According to the ALJ's finding, PacifiCorp had followed a practice of purchasing six-by-sixteen packages for delivery during the summer months for some time, varying the number of packages to reflect the prices being offered in the futures marketplace. When the six-by-sixteen contracts provided more energy than it actually needed to serve its loads, PacifiCorp typically sold the shoulder-hour surplus on the futures market in an effort to recoup some of its expenditures.[58]

36. The ALJ further found that none of the challenged contracts went to physical delivery. During Summer 2002 PacifiCorp "booked out" these contracts, either by the payment of money or by the delivery of energy at Palo Verde to some other party who had participated in the forward market.[59] By doing so, PacifiCorp and its counterparties were spared the expense of transmitting the contracted-for energy from Palo Verde to a delivery point on the PacifiCorp system.

37. The ALJ also determined that PacifiCorp's transactions with Williams were

---

[55] Initial Decision, slip opin., at 2.

[56] Id. at 4.

[57] Id.

[58] Id. at 3.

[59] Id. at 4.

"sleeve" transactions. According to the ALJ's finding, the counterparty that the broker located was not on PacifiCorp's list of creditworthy counterparties with which it would do business in the futures market, and in that case, Williams (which was on PacifiCorp's approved list) agreed to step into the transaction as a "sleeve," acting as the nominal counterparty so that the deal could be consummated. The ALJ concluded that Williams was not the real party in interest in these transactions and performed its "sleeve" function largely as an accommodation. It received no compensation for being the sleeve on two of the contracts and earned only 50 cents per MWh on the third (the May 7, 2001 contract).[60]

38. The ALJ concluded that PacifiCorp failed to establish on the record that it should be granted relief under the "public interest" standard of review.[61] The ALJ employed the three-prong "public interest" test[62] to determine whether PacifiCorp met its burden of proof.[63] The ALJ found that the challenged contracts were not the cause of PacifiCorp's financial distress. PacifiCorp reported having financial difficulties nine months prior to entering the contracts in question.[64] The ALJ further determined that the company's reports to its ultimate stockholders filed after PacifiCorp "booked out" the contracts in question were upbeat.[65]

39. As for the current financial situation of PacifiCorp, the ALJ concluded that PacifiCorp should have no more difficulty raising new capital than other utilities in the same sector of the country.[66] According to the ALJ's finding, PacifiCorp is on track to double its operating profit to £1 billion or more over the next three years.[67] PacifiCorp

---

[60] Id. at 4.

[61] Id. at 12.

[62] See FPC v. Sierra Pacific Power, 350 U.S. 348, 355 (1956).

[63] Initial Decision, slip opin., at 12-13.

[64] Id. at 13.

[65] Id. at 13-14.

[66] Id. at 14.

[67] Id.

has received authorization from its ultimate shareholder to issue new common stock.[68] PacifiCorp's current debt ratings, both for long-term and short-term debt, are average-to-above-average.[69]

40. Additionally, the ALJ found that PacifiCorp may be able to pass through a significant share of the cost of the contracts to its retail ratepayers.[70] The ALJ determined that PacifiCorp has already received regulatory authorization to do so in Oregon and has applied for pass-through authority in California and Wyoming.[71] According to the ALJ's findings, in Washington, PacifiCorp is subject to a five-year plan adopted in August 2000, which prevents PacifiCorp from filing for a rate increase until 2005, with the increase to be effective in 2006 at the earliest. PacifiCorp has, however, asked the Washington Commission for authority to "defer" its excess purchased power costs, i.e., to capitalize the costs as a regulatory asset and amortize them over a period of time.[72] It was also found that PacifiCorp had not even asked for authority to pass through the additional expenses to its Idaho ratepayers; however, PacifiCorp retains that option in the future. The ALJ found that the only jurisdiction in which PacifiCorp is prevented from recovering the costs from its ratepayers is Utah, where PacifiCorp agreed to a rate-case settlement that precludes it from filing for a rate increase until May 2003, with the increase becoming effective not earlier than January 2004.[73]

41. In addition, the ALJ did not find credible PacifiCorp's estimates of "out-of-market" costs attributable to the contracts. According to the ALJ's finding, PacifiCorp's estimates are based on the assumption that, if markets had been "normal," PacifiCorp would have been able to fulfill its need for Summer 2002 forward contracts at the prices predicted by its February 2002 price curve, that is, $37.48/MWh for July 2002, $42.68/MWh for August 2002 and $32.67/MWh for September 2002.[74] The ALJ found no explanation for using those predicted prices as the starting point for calculating the

---

[68] Id.

[69] Id.

[70] Id.

[71] Id.

[72] Id.

[73] Id. at 15.

[74] Id

downside risk that PacifiCorp assumed and also noted that it was PacifiCorp, not anyone else, who chose to use the February 2002 data.[75]

42. Further, the ALJ assumed that these power-purchase costs PacifiCorp estimated to have incurred under the contracts at issue are an accurate representation of PacifiCorp's loss and that these costs will not be recovered from retail ratepayers. Notwithstanding these assumptions, the ALJ concluded that the estimated $53 million loss is not sufficient to warrant regulatory intervention under the "public interest" standard.[76] The ALJ found that $53 million spread over PacifiCorp's 2001 net system load would result in a rate increase of less than one dollar per MWh. According to the ALJ's finding, this would translate into an increase of residential, commercial and industrial rates during the year by only 1.5 percent, 1.8 percent and 2.7 percent, respectively.[77] The ALJ also found that the total amount of power involved in the 12 contracts represents only about one-half of one percent of PacifiCorp's portfolio.[78] The ALJ thus concluded that these figures are too close to the de minimis level to satisfy the Sierra "public interest" test.

43. Moreover, the ALJ determined that PacifiCorp failed to meet its burden of proof even under the "just and reasonable" standard of review.[79] In particular, it was found that Respondents were price-takers rather than primary producers in a position to withhold production from the market place.[80] The ALJ also found that although PacifiCorp had only 13 suppliers that it deemed creditworthy,[81] during the May 2000-June 2001 it purchased power from 80 different sellers and sold power to 98 different buyers.[82] From these numbers, the ALJ inferred that neither of the Respondents could have dominated the market, as there were plenty of competitors ready, willing and able to do business with PacifiCorp. The ALJ also observed that it is understandable that none

---

[75] Id.

[76] Id.

[77] Id.

[78] Id

[79] Id. at 15-16.

[80] Id. at 16.

[81] Id. at 17.

[82] Id.

of the parties offering electric energy for delivery during the three summer months of 2002 was willing to sell to PacifiCorp for less than it cost to buy the energy.[83]

44. Furthermore, the ALJ afforded no weight to PacifiCorp's witness testimony purporting to establish that the Respondents exercised market power. According to the ALJ's findings, PacifiCorp took the position that "market power" consisted of nothing more than the ability to sell electricity at a price above PacifiCorp's idea of the cost of production plus a reasonable return. PacifiCorp's witness estimated that price to be $100 per MWh; however, no basis was provided for this figure.[84]

45. Further, the ALJ examined the question of whether the California ISO and PX spot market dysfunctions adversely affected prices in forward markets. The ALJ found that the PacifiCorp witness testimony on this issue only established correlation between price trends in the spot market and price trends in the forward market.[85] The ALJ concluded that while correlation has some probative weight, it does not amount to causation.[86] The ALJ also observed that current spot market conditions have an effect upon current prices in forward markets simply because they expand the range of possibilities that participants are prone to consider when they negotiate contracts for future payment upon future delivery of the relevant commodity. The ALJ thus determined that the forward market for electricity was not "dysfunctional" in the West during the late Spring of 2001 because many of the institutional factors that created dysfunction in the spot markets were absent.[87] Another explanation for this finding offered by the ALJ was that when spot market prices become irrationally high, forward market prices are supposed to escalate significantly, in order to draw price-reducing resources into the marketplace and cause buyers to reduce their demand.[88]

46. In addition, the ALJ found that none of the usual common law grounds for reforming a contract was present, since there was no fraud or mutual mistake of fact or

---

[83] Id.

[84] Id. at 27.

[85] Id. at 19.

[86] Id. at 25.

[87] Id. at 26.

[88] Id. at 27.

law, nor did the Commission's June 19, 2001 order amount to commercial frustration of all or any of the contracts.[89]

47. The ALJ further examined evidentiary factors suggested for consideration in the June 28 Order. In particular, the ALJ found that there is no explanation for PacifiCorp's entering into the challenged contracts so far in advance, especially considering the fact that none of the contracts went to physical delivery.[90] The ALJ also determined that PacifiCorp regularly sold into both the spot and forward markets.[91] The ALJ further found that during the period from December 2001 through April 2002, PacifiCorp sold a total of 475 MWh, which is one-and-one-half times the total amount it purchased under the contracts at issue here, for delivery at Palo Verde during the third quarter of 2002.[92] The ALJ also determined that PacifiCorp's resources, including its own generation and its purchases, were substantially in excess of what it needed to serve load.[93] The ALJ thus concluded that PacifiCorp's vigorous participation in the marketplace suggests that PacifiCorp engaged in speculative trading.[94]

48. The ALJ also identified the forward sales PacifiCorp made to Williams during the time when it was making forward purchases from the Respondents. The prices in those transactions range from $150 to $330 per MWh.[95]

49. The ALJ also found that even assuming that PacifiCorp was not just speculating but fulfilling the perceived need to secure sufficient supply for the next summer, it undertook a rigid and inflexible strategy to attain that objective. PacifiCorp relied for the most part on weekly forward fixed-price six-by-sixteen purchases of 20 to 50 MW

---

[89] Id. In drawing this conclusion, the ALJ relied on McCulloch v. Liquori, 88 Cal. App. 2d 366, 199 P.2d 25 (1948); Lloyd v. Murphy, 25 Cal. 2d 48, 153 P.2d 47 (1944); Wood v. Bartolino, 48 N.M. 175, 146 P.2d 883 (1944); and Robitzek Investing Co. v. Colonial Beacon Oil Co., 265 A.D. 749, 40 N.Y.S.2d 819 (1943).

[90] Id. at 28.

[91] Id.

[92] Id.

[93] Id. at 29.

[94] Id. at 30.

[95] Id. at 29.

packages purchased through brokers. The ALJ determined that PacifiCorp could have hedged its risk by purchasing option contracts instead of the must-take products it bought.[96] According to the ALJ's finding, PacifiCorp could have purchased energy under monthly contracts or it could have purchased index contracts or longer-term contracts.[97] The ALJ further found that PacifiCorp also limited its alternatives by specifying that it would do business only with a relatively small number of counterparties who satisfied its self-imposed creditworthiness standards.[98]

50. The ALJ also noted the statements on the subject of the forward bilateral contracts that PacifiCorp made in pleadings in other proceedings before the Commission.[99] The ALJ observed that these statements contradict PacifiCorp's position in the instant case.[100]

51. On the issue of whether or not PacifiCorp could have foreseen the Commission imposition of the mitigation measures following its April 26 Order, the ALJ concluded that it depends largely upon which side of the price-cap debate PacifiCorp thought would prevail. According to the ALJ, reasonable utility executives, surveying the legal-politico-economic landscape in April, May and the early part of June 2001 could have thought that the Commission would adhere to its oft-stated preference for allowing the market place to set limits on electricity prices. However, the ALJ also noted that it could not be concluded that PacifiCorp's executive were totally shocked to find the Commission issuing a "hard" price cap in the middle of June 2001.[101]

52. Further, the ALJ examined possible impacts of contract modification on energy markets in general. The ALJ concluded that a successful after-the-fact attack on the validity of a power sale agreement negotiated between knowledgeable and sophisticated parties on the open market will have a deleterious effect on the flow of investment capital into independent generation enterprises. The ALJ determined that while the California

[96] Id. at 30.

[97] Id.

[98] Id.

[99] Id. at 31-32.

[100] Id. at 32.

[101] Id. at 34.

energy crisis was an unusual, and perhaps unique, phenomenon, that would not change the investment community's apprehension that such a phenomenon, having once occurred, may occur again. The ALJ thus concluded that if the Commission uses the California energy crisis as the occasion for setting aside or modifying the obligation of a power sales agreement, it can anticipate that it will craft a precedent others will attempt to use under other circumstances.[102]

53. Based on the above findings, the ALJ dismissed PacifiCorp’s complaints with prejudice.

2. Exceptions

54. PacifiCorp argues that even if the "public interest" were to apply to the contracts at issue, contract modification is warranted. In PacifiCorp's opinion, the Initial Decision impermissibly focuses only on one of the aspects of the "public interest" test, that is, financial health of the Complainant. PacifiCorp also believes that the ALJ incorrectly assessed harms to Complainant and its customers resulting from the challenged contracts. In addition, PacifiCorp contends that the Staff Report's finding of evidence of market manipulation and the disproportionately large effect of the spot market dysfunctions on prices in short-term forward contracts constitute extraordinary circumstances warranting contract modification in this case.

55. PacifiCorp further states that granting refunds in this proceeding will increase general confidence in the market, as it will indicate to market participants that the Commission is monitoring the markets for bad behavior. PacifiCorp takes issue with the ALJ's findings on the circumstances surrounding execution of the challenged contracts. Finally, PacifiCorp states that the record demonstrates that the contract prices at issue are unjust and unreasonable and that allowing them to stand would be contrary to the public interest.

56. Snohomish supports PacifiCorp's position. Snohomish argues that contract reformation in this case can be justified by the fact that there was a market failure in the industry. Snohomish also disagrees with the ALJ's finding that the rate increase resulting from the challenged contracts is de minimis.

57. Respondents and Staff agree with the ALJ's ruling that modification of PacifiCorp's contracts cannot be justified under the "public interest" standard.

[102] Id. at 37.

Respondents also believe that even considering the Staff Report findings, contract reformation is not warranted. Respondents argue that PacifiCorp failed to present any evidence showing that Respondents' specific acts affected the challenged contracts. Furthermore, they state that the Staff Report findings would be relevant only under the "just and reasonable" standard of review. Staff, however, believes that the Commission should not consider the Staff Report because the record of the instant proceeding contains sufficient evidence for the Commission to make a final determination.

58. In addition, Staff states that the ALJ correctly found that the negative impact on PacifiCorp and its ratepayers is minimal. Respondents also agree with the ALJ's conclusions that when executing the contracts in question PacifiCorp pursued a strategy designed to maximize profits. In their opinion, PacifiCorp filed these complaints because it incurred losses resulting from that risky purchasing strategy.

3. Oral Argument

59. At the May 15 oral argument, PacifiCorp argued that the California-Western energy crisis amounts to extraordinary circumstances warranting contract modification in this case and that the Commission can grant relief on the basis of the excessive level of the prices prevalent in the forward market during the relevant period. PacifiCorp also suggested that if the Commission finds market manipulation relevant to this case, the record should be reopened to allow the Complainant to introduce evidence on market manipulation. PacifiCorp also stated that the Staff Report confirms the evidence already in the record demonstrating the causal link between the spot market dysfunctions and high forward prices.

60. Respondents argued that the record does not contain evidence establishing the adverse impact of the spot market dysfunctions on forward prices. In their opinion, the Staff Report conclusions represent a correlation analysis and do not establish that spot market dysfunctions caused price spikes in the forward market. Respondents also stated that the Staff Report findings could be relevant only in cases where the applicable standard of review is the "just and reasonable" standard.

4. Commission Determination

61. In deciding whether the Complainant has met its burden of proof under the "public interest" standard of review to justify contract modification in this case, we rely on the evidentiary record developed in this proceeding and also take into consideration the findings of the Staff Report and evidence submitted in the 100-Day Discovery Proceeding. The Staff Report found that spot market distortions flowed through to

forward power prices, particularly those for contracts of a short-term nature, i.e., one to two years time to delivery. In addition, the Staff Report and the 100-Day Discovery Proceeding suggest that the California ISO and PX markets were subjected to market manipulation and gaming. The Staff Report conclusions and the 100-Day Discovery Proceeding documents are being contested in "show cause" proceedings involving allegations and/or findings of manipulation in the spot markets. However, even if we were to assume that these allegations and/or findings were true, they would not be determinative of the issues in the instant proceeding. The Commission has already concluded that the California ISO and PX spot markets were dysfunctional during the relevant period and that rates in those markets were unjust and unreasonable.[103] Evidence of market manipulation merely suggests yet another cause of the spot market dysfunctions and the unjust and unreasonable rates in the spot markets. However, a finding that the unjust and unreasonable spot market prices caused forward bilateral prices to be unjust and unreasonable would be relevant to contract modification only where there is a "just and reasonable" standard of review.[104] As we have previously concluded, the contracts at issue in this proceeding do not provide for such a standard but rather evidence an intent that the contracts may be changed only pursuant to the "public interest" standard of review. Under the "public interest" standard, to justify contract modification it is not enough to show that forward prices became unjust and unreasonable due to the impact of spot market dysfunctions; it must be shown that the rates, terms, and conditions are contrary to the public interest.[105] As fully discussed below, we conclude that the Complainant failed to make such a showing.

62. As determined by the ALJ and affirmed in this order, the Complainant in this proceeding must meet the "public interest" standard in order to justify the requested contract modification. Based on the record, we conclude that the Complainant has failed to demonstrate that any of the three prongs announced in the Sierra case has been met or that any other factor introduced into evidence warrants a finding that any of the contracts is contrary to the public interest and should be modified.

---

[103] See, e.g., San Diego Gas & Electric Co. v. Sellers and Ancillary Serv., 93 FERC ¶ 61,121, at 61,359-60 and 61,372 (2000); order on reh'g and clarification, 97 FERC ¶ 61,275, at 62,225 (2001).

[104] This conclusion is consistent with the Staff Report recommendation that, only for contracts subject to the "just and reasonable" standard of review, the Commission should send the Staff Report findings on the influence of spot prices on forward prices to the ALJs to use as they see fit to resolve complaints. See Staff Report at V-19.

[105] See, e.g., FPC v. Sierra Pacific Power Co., 350 U.S. 348, 354-5 (1956).

63. There is no credible record evidence that the contracts at issue are placing the Complainant in financial distress so as to threaten its ability to continue service or that other customers will bear an excessive burden as a result of upholding the challenged contracts. In addition, there is no evidence that the contracts terms are unduly discriminatory.

64. We agree with the ALJ that PacifiCorp's estimates of its "out of market" costs associated with the challenged contracts are not credible, since they are based on arbitrary assumptions.[106] However, even assuming that these estimates are accurate, their negative effect on PacifiCorp and its ratepayers is not sufficient to abrogate the contracts. If PacifiCorp will be able to recover all of these costs by passing them through to its ratepayers,[107] the rate increase would amount to 1.5 percent, 1.8 percent and 2.7 percent for PacifiCorp's residential, commercial and industrial customers respectively.[108] The total amount of power involved in the 12 contracts represents only about one-half of one percent of PacifiCorp's portfolio.[109]

65. Also, it would be difficult to describe PacifiCorp's current situation as financial distress. PacifiCorp is expected to double its operating profit to £1 billion or more over the next three years.[110] According to the report of PacifiCorp's ultimate shareholder, Scottish Power, PacifiCorp's operating profit for the quarter ending September 30, 2002 amounted to £ 141 million.[111] PacifiCorp's access to capital is also not impeded as a

---

[106] Initial Decision at 14-15; Tr. 344:18-345:1; Ex. PAC-41, at 3 n.1; and Ex. S-6 at 20.

[107] Ex. PAC-41 at 6 and 7. The rate recovery allowed in the State of Oregon accounts for $17.7 million, or thirty-three percent of the contracts' $53 million "out-of-market"costs. Id. See also Tr. 581:4-582:9; Ex. MSC-47; Ex. PAC-41 at 7:18-20. Tr. 312:11-15 and 334:19-335:14.

[108] Ex. S-6 at 22.

[109] Ex. EPME-24 at 12.

[110] Ex. MSC-43 at 1; Ex. EPME-37 at 4.

[111] Ex. S-6 at 23:5-9.

result of the challenged contracts; its current debt ratings, both for long-term and short-term debt, are average to above-average.[112]

66. PacifiCorp also failed to present evidence showing that the challenged contracts are unduly discriminatory. The type of discrimination that can be considered in this context is whether contract rates, terms, and conditions are discriminatory or preferential to the detriment of other purchasers who are not parties to the contract.[113] No such showing has been made by PacifiCorp.

67. In addition to the evidence on the effects of the challenged contracts on the parties and Complainant's customers, the ALJ has developed an extensive evidentiary record on the totality of circumstances preceding and following the execution of the contracts at issue. Specifically, the record shows that PacifiCorp's contracts were standard products arranged through independent third-party brokers and, consequently, the Respondents were price takers.[114] PacifiCorp did not issue a Request for Proposals (RFP). It also appears from the record that PacifiCorp was engaged in a policy of "dollar averaging."[115] The challenged contracts provided more energy than PacifiCorp actually needed to serve its loads; the electricity supplied during the so-called "shoulder hours" was surplus. PacifiCorp typically sold the shoulder-hour surplus on the forward market in an effort to recoup some of its expenditures. PacifiCorp sold power at wholesale to 98 different buyers during the relevant period.[116] During the period from December 2001 through April 2002, PacifiCorp sold one-and-one-half times the total amount it purchased under the contracts at issue.[117]

---

[112] Tr. 587-88.

[113] See Papago Tribal Authority v. FERC, 723 F.2d 950, 953 n. 4 (D.C. Cir. 1983).

[114] Ex. RES-1 at 5-6.

[115] Ex. RES-33. PacifiCorp's Internal Report, "Risk Forum," dated of June 6, 2001.

[116] Ex. EPME-44 at response (a) to Data Request EPME-PAC-8.

[117] Ex. RES-9 at 4.

68. It is also worth noting that PacifiCorp sold power to Respondent Williams at prices ranging from $150 to $330 per MWh,[118] whereas the prices in the challenged contracts range from $126 per MWh to $262 per MWh, with a weighted average price of $181.00 per MWh.

69. Additionally, PacifiCorp failed to hedge for the possible risk that spot market prices might fall, and it did not pursue a mix of products to reduce risks associated with market volatility through portfolio diversification. For example, PacifiCorp could have hedged its risk by purchasing option contracts instead of the must-take products it bought.[119] Furthermore, PacifiCorp could have purchased energy under monthly contracts.[120] It could also have purchased index contracts or longer-term contracts. However, PacifiCorp did not pursue all these options.

70. Furthermore, the record demonstrates that from May 2000 until June 19, 2001, PacifiCorp purchased power from 80 different sellers[121] In addition, during the relevant period PacifiCorp made more than 250 forward contracts for delivery more than a month in advance at prices that ranged from $100 to $570 per MWh.[122] Thus, considering the number of sellers available and of purchases actually made, it can be reasonably concluded that PacifiCorp had choices, i.e., it was free to reject offers and turn to other suppliers.

71. Based on the above, we conclude that the contracts at issue were the result of choices voluntarily made by the Complainant. The record also establishes that the Complainant had better alternatives and was not compelled to enter into the contracts at issue here. PacifiCorp could have pursued a more balanced purchasing strategy, that is, instead of buying standard products with three months to delivery, PacifiCorp could have pursued a diversified portfolio of contracts of different lengths arranged through the RFP process, as well as independent brokers.

---

[118] Ex. WIL-1 at 15.

[119] Ex. RES-9 at 5-6.

[120] Ex. EPME-28 at 46.

[121] Ex. EPME-44 at response (k) to Data Request EPME-PAC-6.

[122] Initial Decision, slip opin., at 6 n.6.

72. Finally, there is nothing in the record before the ALJ, in the Staff Final Report, or in the 100-Day Discovery Proceeding evidence to support a finding that there was market manipulation specific to the long-term contract negotiations resulting in prices and terms being challenged here.

73. Therefore, based on the record, it appears that the Complainant's only basis for contract modification is its dissatisfaction with the bargain. Commission and court precedent clearly establish that allegations that contracts have become uneconomic by the passage of time do not render them contrary to the public interest under the FPA.[123] The record clearly indicates that the challenged transactions were the result of the Complainant's voluntary choices. Therefore, because there is no evidence of unfairness, bad faith, or duress in the original negotiations, the Complainant is not entitled to change its bargain.[124]

74. For these reasons, we affirm the ALJ's ruling and find that the Complainant has failed to meet its burden of proof under the "public interest" standard and contract modification in this case is thus not warranted. Accordingly, we deny the exceptions.

III. Miscellaneous Issues

A. Motion to Reopen the Record

75. PacifiCorp filed a motion requesting that the Commission reopen the record to admit, or in the alternative, take official notice of the Stipulated Facts and Transcripts associated with the Commission's January 31, 2003 Settlement with Reliant.[125] PacifiCorp explains that this evidence is relevant to the instant proceeding because it suggests that Reliant manipulated the PX spot market with the purpose of affecting the prices in forward markets. PacifiCorp argues that this evidence goes to the heart of this case and demonstrates that the spot market dysfunctions affected forward prices.

---

[123] See Potomac Elec. Power Co. v. FERC, 210 F.3d 403, 409 (D.C. Cir. 2000) (citing Soyland Power Coop. Inc. v. Central Illinois Pub. Serv. Co., 51 FERC ¶ 61,004, at 61,013 (1990). See also Papago, 723 F.2d at 953. Sierra, 350 U.S. at 354-355.

[124] See Potomac Electric Power Company v. FERC, 210 F.3d 403, 410 (D.C. Cir. 2000).

[125] Order Approving Stipulation and Consent Agreement, 102 FERC ¶ 61,108 (2003).

PacifiCorp also states that Reliant failed to provide these materials before the evidentiary record was closed. In connection with this, PacifiCorp requests that the Commission impose sanctions on Reliant in accordance with Rule 411 of the Commission's Rules of Practice and Procedure.[126]

76. In its answer to PacifiCorp's motion, Reliant provides an explanation for its failure to provide the materials in question. According to Reliant, after PacifiCorp received Reliant's objections to certain PacifiCorp data requests, PacifiCorp's counsel discussed the objections with Reliant; however, the objections to production of the materials at issue here were never addressed. Reliant further states that the evidence PacifiCorp seeks to introduce is not relevant to the issues in this proceeding.

77. On May 7, 2003, PacifiCorp filed a supplement to its motion to reopen, requesting that the Commission adduce in the record, or in the alternative, take official notice of the Staff Report on price manipulation in the Western markets; evidence submitted in the 100-Day Discovery Proceeding, the Puget Sound proceeding in Docket No. EL01-10, et al.,[127] and the Enron investigation proceedings in Docket Nos. EL02-113, EL02-114 and EL02-115; and all public documents relating to the settlement in Docket No. IN01-3[128] and the public records from other pending Western forward contract proceedings.[129]

78. Respondents filed a joint answer to PacifiCorp's supplemental motion to reopen. They argue that there is no procedural basis for reopening the record because PacifiCorp has failed to show that an extraordinary change in core circumstances has occurred since the record was closed. Similarly, Respondents object to PacifiCorp's alternative request to take official notice of evidence from other proceedings. Respondents argue that the Commission should not consider either reopening the record or taking official notice of

---

[126] 18 C.F.R. § 381.411 (2003).

[127] Puget Sound Energy, Inc. v. Jurisdictional Sellers of Energy, 101 FERC ¶ 61,304 (2002), order on clarification, 102 FERC ¶ 61,163 (2003).

[128] AES Southland, Inc. & Williams Energy Marketing & Trading Co., 95 FERC ¶ 61,167 (2001).

[129] Nevada Power Co. and Sierra Pacific Power Co. v. Enron Power Marketing, Inc., et al., 99 FERC ¶ 61,047, order on reh'g, 100 FERC ¶ 61,273 (2002), reh'g pending and Public Utilities Com'n of the State of California v. Sellers of Long-Term Contracts to the California Dep't of Water Resources, et al., 99 FERC ¶ 61,087 (2002), order on reh'g, 100 FERC ¶ 61,098 (2002).

evidence from other proceedings because addition of new material to the record in this proceeding will not change the outcome of this proceeding.

79. PacifiCorp filed an answer to Reliant's answer to PacifiCorp's motion. Reliant filed an answer to PacifiCorp's answer to its answer. Answers to answers are generally not permitted pursuant to Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2), unless otherwise permitted by the decisional authority. We are not persuaded to allow these answers to answers.

80. The Commission may reopen the record in its discretion where there is good cause.[130] The Commission views good cause as consisting of extraordinary circumstances, that is, a change in circumstances that is more than just material, but goes to the very heart of the case.[131] In deciding whether to exercise its discretion, "the Commission looks to whether or not the movant has demonstrated the existence of extraordinary circumstances that outweigh the need for finality in the administrative process."[132] As the Commission explained in Opinion No. 238, "we recognize of course that changes have occurred since the close of the record. But such changes always occur. Yet litigation must come to an end at some point. Hence the general rule is that the record once closed will not be reopened."[133]

81. The information now in the record provides a sufficient basis for our conclusions here. The evidence that the Complainant seeks to introduce into the record will not change the outcome of this proceeding, as more fully discussed above.

82. Now we turn to PacifiCorp's alternative request to take official notice of the Staff Report and evidence submitted in the proceedings specified by Snohomish. We find that PacifiCorp's request inasmuch it pertains to the Staff Report and 100-Day Discovery

---

[130] 18 C.F.R. § 385.716 (2003).

[131] CMS Midland, Inc., 56 FERC ¶ 61,177 at 61,624, reh'g denied, 56 FERC ¶ 61,361 (1991).

[132] East Texas Electric Coop., Inc. v. Central and South West Serv., Inc., 94 FERC ¶ 61,218 at 61,801 (2001) (denying reopening of record where movant sought to use actual data which became available after the close of the record in place of hypothetical data used at hearing).

[133] Transwestern Pipeline Co., Opinion No. 238, 32 FERC ¶ 61,009 (1985), reh'g denied, Opinion No. 238-A, 36 FERC ¶ 61,175 at 61,453 (1986).

evidence to be moot because we have considered these findings and evidence as part of the record of this proceeding. As previously discussed, we conclude that, even if we assume that the allegations and findings contained in the Staff Report and the 100-Day Discovery Proceeding were true, they would not be determinative of the issues in this proceeding. However, we deny PacifiCorp's request to take official notice of evidence submitted in other proceedings. The records of those proceedings contain thousands of submittals, most of which are case-specific and not relevant to the issues in the instant proceeding; the documents that could be relevant have been submitted in the 100-Day Discovery Proceeding.

83. We also deny PacifiCorp's motion requesting imposition of sanctions on Reliant. We do not find sanctions warranted in these circumstances.

B. Requests for Rehearing

84. The requests for rehearing and clarification of the June 28 Order were filed by Respondents jointly with intervenors, Mirant Americas Energy Marketing, LP and Sempra Energy Resources (collectively, Respondents), as well as by PacifiCorp and Snohomish.

85. On rehearing, Respondents argue that the Commission erred in not dismissing the complaints on the ground that the Complainant failed to establish a prima facie case. We disagree with these assertions. The June 28 Order found that the Complainant established a prima facie case. We believe that the Complainant's allegations were extensive and were adequate to support the Commission's initiation of a proceeding under Section 206 of the FPA to determine whether these allegations are valid.[134] Therefore, we established an evidentiary hearing[135] to address the question of whether the dysfunctional California ISO and PX spot markets adversely affected Western long-term bilateral markets; and, if so, whether contract modification is warranted.

86. Respondents further contend that the Commission erred in setting the issue of the

[134] See, generally, Panhandle Eastern Pipe Line Company, 37 FERC ¶ 61,199, at 61,479 (1986).

[135] We note that the decision as to whether to conduct an evidentiary hearing is in the Commission's discretion. See, e.g., Woolen Mill Associates v. FERC, 917 F.2d 589, 592 (D.C. Cir. 1990) (citing Cerro Wire & Cable Co. v. FERC, 677 F.2d 124, 128 (D.C. Cir. 1982).

applicable standard of review for hearing instead of applying the "public interest" standard as a matter of law. PacifiCorp and Snohomish, however, argue that the Commission should have applied the "just and reasonable" standard of review as a matter of law. We find that the contentions on both sides are without merit. The Commission needed additional information in order to determine the applicable standard of review for the contracts in question because they did not contain explicit Mobile-Sierra language. The evidentiary hearing was established to, among other things, interpret the terms of such contracts and to ascertain the intent of the parties at the time these contracts were signed. As we have previously observed, contract interpretation is often a complex process, involving the scrutiny of the contract itself, related documents, and at times parol or extrinsic evidence. We have explained that, where the contract at issue contains ambiguous language, it is appropriate for us to consider extrinsic evidence.[136]

87. PacifiCorp and Snohomish argue that the Commission introduced a new, heightened, standard of review when it characterized the burden of proof under the "just and reasonable" standard as a heavy one. Contrary to these assertions, in the June 28 Order we did not introduce a new standard of review. Section 206 complaints can be reviewed only under either the "just and reasonable" standard or the "public interest" standard. By emphasizing that a complainant bears a heavy burden of proof, we stated the obvious that the sanctity of contracts is presumed and that the Commission will not lightly undo the terms of existing contracts regardless of the applicable standard of review.

88. Furthermore, PacifiCorp argues that the Commission failed to recognize that PacifiCorp established that the spot market dysfunctions influenced forward prices. We disagree. We carefully reviewed PacifiCorp's complaints and the supporting materials; however, we found that "[i]n the evidence presented thus far, the Complainant ... failed to show that the dysfunctional ISO and PX spot markets had an adverse effect on the forward bilateral markets in California."[137] We, therefore, set this issue for hearing. At the conclusion of the hearing, the ALJ determined that PacifiCorp failed to establish the linkage between the spot market dysfunctions and forward prices.

89. PacifiCorp and Snohomish argue that the evidentiary factors listed in the June 28 Order unjustifiably focus on the buyers' actions rather than the sellers' actions. They

[136] See Oglethorpe Power Corporation v. Georgia Power Company, 69 FERC ¶ 61,208, at 61,825 (1994), order on reh'g, 72 FERC ¶61,065 (1995); Delmarva Power & Light Company, 69 FERC ¶ 61,144, at 61,525-26 (1994).

[137] See June 28 Order at 62,614-15.

request the Commission to clarify that this evidentiary list is not exclusive and that the Complainant is allowed to present evidence on seller's actions. PacifiCorp also contends that the evidentiary list contains items that are not relevant to the issues in this proceeding.

90. Contrary to these assertions, the list of evidentiary requirements is not exclusive. The parties were free to offer other evidence deemed by the ALJ to be relevant to the Commission-prescribed scope of the hearing. We also believe that the June 28 Order's evidentiary requirements are applicable to both the sellers and the buyers and are not biased toward the Complainant. However, we note that the burden to justify contract modification rests on the Complainant. In addition, we deny Snohomish's and PacifiCorp's requests for clarification as moot.

The Commission orders:

(A) The Initial Decision is affirmed, as discussed in the body of this order.

(B) The complaints are hereby denied.

(C) PacifiCorp's motion to reopen the record is hereby denied, as discussed in the body of this order.

(D) PacifiCorp's motion to take official notice is hereby denied in part and granted in part, as discussed in the body of this order.

(E) Requests for rehearing are hereby denied, as discussed in the body of this order.

(F) Requests for clarification are hereby denied as moot.

By the Commission. Chairman Wood concurring in part with a separate statement attached.

(S E A L) Commissioner Massey dissenting with a separate statement attached.

Commissioner Brownell concurring with a separate statement attached.

Linda Mitry,

Acting Secretary.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

PacifiCorp	Docket Nos.	EL02-80-001
		EL02-80-002
v.		EL02-81-001
		EL02-81-002
Reliant Energy Services, Inc.		EL02-82–001
Morgan Stanley Capital Group Inc.		EL02-82-002
Williams Energy Marketing & Trading		EL02-83-001
Company, and		EL02-83-002
El Paso Merchant Energy, L.P.		

(Issued June 26, 2003)

Wood, Chairman, concurring in part:

In voting on this order, I do not agree with the ALJ's interpretation that, in the absence of an express contractual manifestation of the parties' intentions with respect to the method of changing their agreement, the rate provided in the contract may not be altered unless the Commission determines that the public interest standard has been satisfied. See Initial Decision at P 18. I concur in the conclusion that the public interest standard of review applies to the contracts at issue in this case based solely on the specific circumstances surrounding execution of those contracts and the parties' intent.

Pat Wood, III
Chairman

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

PacificCorp	Docket Nos. EL02-80-001
	EL02-80-002
	EL02-81-001
v.	EL02-81-002
Reliant Energy Services, Inc.,	EL02-82-001
Morgan Stanley Capital Group, Inc.	EL02-82-002
Williams Energy Marketing & Trading	EL02-83-001
Company, and	EL02-83-002
El Paso Merchant Energy, L.P.	
	(Consolidated)

(Issued June 26, 2003)

MASSEY, Commissioner, dissenting:

I am dissenting from this order, not because I relish abrogating contracts because I do not, but because I believe this Commission has a higher calling than simply the sanctification of long term contracts with prices reaching as high as $290 per MWh, contract prices that were multiples of traditional prices, shockingly high prices, completely unprecedented by historic standards. Our primary calling under the Federal Power Act is to ensure that prices are just and reasonable 24 hours a day, seven days a week. When prices soar to unprecedented levels, when prices exceed a just and reasonable level by multiples, we have the obligation to make it right. That is the way I read the law.

Many of the contracts challenged here provide for prices that are unlawful by any reasonable measure, and there is no persuasive public interest rationale for sanctifying contracts negotiated during the height of the Western electricity crisis, where the skyrocketing prices in an out of control spot market in California strongly influenced long term contract prices, wildly dysfunctional market conditions clearly allowed for the exercise of market power, and there was "epidemic" manipulation of the market according to our staff's Western Markets Report.

Protecting contracts entered into in this horribly tainted environment violates the Federal Power Act's forceful declaration that contracts are absolutely unlawful and must be reformed if not just and reasonable. Turning Commission policy on its head, today's order will encourage wholesale electricity purchasers to "ride the spot market" because the Commission has shown a willingness to mitigate, and provide refund protection from, unjust and unreasonable spot market prices, at least in the California spot markets.[1] By the same token, buyers will be discouraged from forward contracting because they will not enjoy protection from unlawful contract prices. Power buyers, consumers and retail policymakers will lose faith in the concept of wholesale electricity markets if they cannot trust the Commission to protect them from unjust and unreasonable contract terms resulting from a wildly dysfunctional market, market power and epidemic market manipulation.

The J&R standard is the appropriate standard of review in this instance

One of the fundamental questions that must be addressed in evaluating whether a contract must be reformed is the standard of review. Where there is clear language in the contract indicating that the parties intended that the "public interest" standard must be met before terms may be modified, then that is the appropriate standard. Where the contract lacks a clear statement of intent, the correct standard to apply is not that clear. Today's order finds that the more stringent public interest standard must be satisfied even for contracts with no clear statement of intent. I do not agree.

It is my view that except where the contract has a Mobile-Sierra clause restricting the right of the buyer to file a Section 206 complaint, the just and reasonable standard applies. I concede that the law in this area is not the model of clarity, and the argument that the public interest standard controls is not without merit. Nevertheless, I believe a customer's waiver of Section 206 just and reasonable rights must be explicit. As the Commission observed in Order 888-A:

> We note that the fact that a contract may bind a utility to a Mobile-Sierra public interest standard does not necessarily mean that the customer is also bound to that standard. Unless a customer specifically waives its Section 206 just and reasonable rights, the Commission construes the issue in favor of the customer.[2]

---

[1]In an case decided today, the Commission denies refund protection to spot market buyers in the Pacific Northwest during the crisis period. Puget Sound Energy, Inc, 103 FERC ¶ 61,348 (2003).

[2]Order No. 888-A, FERC Stats. & Regs. ¶ 31,048 (1997) at 30, 191, footnote 31.

The Commission's proposed policy statement on standard of review is consistent with that position. The Commission would apply the just and reasonable standard of review unless specific language to the contrary is concluded in the contract.[3]

Perhaps more important, the just and reasonable standard should control the review of contracts negotiated *in the circumstances of this case* where the sellers were acting under a market-based pricing authorization granted by the Commission. The Mobile-Sierra doctrine arose in a cost-of-service regime. Once approved by the Commission as just and reasonable, a contract, rate or classification should not be modified unless a higher standard justifies the modification. This makes sense. Most cases arose in the context of a seller making a filing to justify a higher rate. In such a case, the doctrine appeared to have a customer protection rationale.

Today's order states that in a market based regime, the Commission's authorization for a public utility to sell at prices set by the discipline of the market, based upon a finding that the seller cannot exercise or has mitigated market power, amounts to a "predetermination" that any contract negotiated by such seller is just and reasonable. Hence, according to the majority, the just and reasonable standard of Section 205 is satisfied, and a later contract modification would have to be justified by the higher public interest standard.

There are three flaws in this logic as applied here. First, virtually all of the Commission's orders granting market based pricing authority to the public utility sellers in the West explicitly declared that the Commission's action could not be construed as approving any contract negotiated pursuant thereto. These orders say:

> (t)his action does not constitute approval of any service, rate, charge, classification...or any...contract...affecting such rate or service..., nor shall such action be deemed as recognition of any claimed contractual right or obligation affecting or relating to such service or rate; and such action is without prejudice to any findings or orders which have been or may hereafter be made by the Commission in any proceeding...

Based upon this language, it seems clear that these contracts have never been approved as just and reasonable under section 205.

---

[3]Standard of Review for Proposed Changes to Market-Based Rate Contracts for Wholesale Sales of Electric Energy by Public Utilities, 100 FERC ¶61,145 (2002) at paragraph 7.

Second, even ignoring the rather plain language of the above-quoted paragraph, any possible presumption of the justness and reasonableness of contracts negotiated pursuant to the blanket authorization was flatly contradicted by the conclusions reached in the Commission's November 1, 2000 and December 15, 2000 orders, and in the July 2001 order requiring refunds. The November order found the market in California to be seriously flawed, and market conditions "have caused and continue to have the potential to cause, unjust and unreasonable rates for short term energy." Further: "There is clear evidence that the California market structure and rules provide the opportunity to exercise market power when supply is tight and can result in unjust and unreasonable rates."[4] In the December 15 order the Commission said that "we reaffirm our findings that unjust and unreasonable rates were charged and could continue to be charged, unless remedies are implemented."[5] It should be clear from both the breathtaking rise in prices after the December order and the June 2001 intervention by the Commission that the remedies in the December order did not work. Effective remedies were not put in place until June 2001 when the Commission imposed full time price controls. I would also note that the Commission's grant of market based pricing authority "depends on a functioning competitive market... unimpaired by market manipulation." Implicit in the grant of such authority is "a presumption that a company's behavior will not involve fraud or deception."[6] Circumstances indicate that this condition and presumption were not fulfilled. The Commission has found evidence of market manipulation in the California markets and is also investigating whether sellers withheld power from the market or engaged in excessive bidding.

In light of all of these circumstances, the predetermination rationale is without merit. The Commission's July 2001 order granting refunds for a nine month period beginning October 2, 2000 and ending June 19, 2001 was based upon a finding that during such period spot prices were not just and reasonable. It defies logic to rely upon a "predetermination" of justness and reasonableness contradicted by later Commission orders that reviewed real market conditions, found the opportunity to exercise market power, and required several billions of dollars in refunds based upon the explicit conclusion that actual prices charged in fact were not just and reasonable.

---

[4]San Diego Gas & Electric Company, 93 FERC ¶ 61,121 (2000) at 61,349.

[5]San Diego Gas & Electric Company, 93 FERC ¶ 61,294 (2000) at 61,999.

[6]Reliant Energy Services, et al, 102 FERC 61,315 (2003) at paragraph 12; and Enron Power Marketing Inc., et al, 102 FERC¶ 61,316 (2003).

Third, the rates charged by sellers in the California spot markets were under the same regulatory scheme that produced the forward contracts at issue here, i.e., a preliminary finding at the certificate stage that a seller lacked or had mitigated market power and, hence, rates sought to be charged by such seller would by definition be just and reasonable. This "predetermination" applied equally to spot prices and to long term contract prices. Yet, in July 2001 the Commission wisely and correctly decided to apply the just and reasonable standard to justify modifying the California spot prices and ordering refunds. Satisfying the public interest standard was not required. The Commission did not protect unjust and unreasonable spot prices (which were derived under tariff conditions and are akin to hourly contracts), yet decides today to protect unjust and unreasonable longer term transactions negotiated under the same regulatory framework. This distinction in the standard of review, based solely upon the length of the transaction, does not comply with sections 205 and 206 of the Act, and in my view is not reasoned decision making.

There is an additional reason that the just and reasonable standard should govern in this case. It is obvious that the buyers detrimentally relied upon the Commission's admonition in the December 2000 order that market participants enter into long term contracts.[7] In that same order, the Commission assured buyers that they would be protected from the exercise of market power. The Commission set a $74 MWh benchmark to use "in assessing any complaints regarding the justness and reasonableness of pricing of such long-term contracts negotiated under current market conditions."[8] The Commission promised to monitor prices "to address concerns about potentially unjust and unreasonable rates" in the long term markets.[9]

The buyers reasonably relied upon the Commission's declaration that complaints about long term contracts would be judged according to just and reasonable standards and they would be protected. Given that reliance, it is simply unfair to adopt a standard of review today that gives these buyers substantially less protection. In addition, after the Commission declared in December 2000 that $74 MWh was a just and reasonable benchmark for long term contracts negotiated thereafter, it seems unconscionable now to validate contracts that allowed sellers to fetch upwards of $250 MWh, $260 MWh, and

[7]"...those who remain in the spot market for buying their residual load or selling their residual supply should be there in full recognition of the effects on price of last minute sales and purchases." 93 FERC at 61,996.

[8]93 FERC at 61,982.

[9]93 FERC at 61,994.

$290 MWh - - multiples of the benchmark. The Commission effectively said to buyers "get into long term contracts, $74 is a reasonable benchmark price and, hey, don't worry, we'll protect you from unjust and unreasonable contract prices." Today's order utterly fails to keep that commitment.

The nexus between the California spot market and the forward contract market

A second fundamental issue in this case is whether the dysfunctional California spot markets adversely affected the long-term bilateral markets. I frankly do not understand why the hearing order in this case treated this as an open issue, and I said so at the time. The relationship between the spot market prices and long term contract prices seems rather obvious, and the Commission has explicitly recognized that "maintaining an accurately priced spot market is the single most important element for disciplining longer term transactions."[10] In our Standard Market Design proposal, the Commission found that:

> Bilateral contracts generally reflect buyer and seller expectations of prices in spot markets. Therefore, market power mitigation in the organized spot market will effectively discipline market power in the bilateral markets as well [footnote omitted].[11]

More to the point, the Commission has specifically recognized the relationship between the California spot markets and bilateral markets in the West. Our November 1, 2000 order stated:

> Therefore, the operation of the California electricity market can affect prices throughout the entire Western Interconnection. The Staff Report demonstrates that during the summer of 2000 correlations between PX prices and Western bilateral prices were quite strong.[12]

And our June 19, 2001 mitigation order recognizes that "(t)here is a critical interdependence among the prices in the ISO's organized spot markets, the prices in the

---

[10]AEP Power Marketing, 97 FERC ¶ 61,219 (2001) at 61,972.

[11]Standard Market Design NOPR, 100 FERC ¶ 61,138 (2002) at paragraph 405.

[12]93 FERC at 61,357 to 358.

bilateral spot markets in California and the rest of the West, and the prices in forward markets."[13] Thus, it is beyond comprehension why there is any doubt on this issue.

But if there was any doubt whatsoever regarding whether there was a nexus between the spot and forward markets, the staff's Western Markets Report should dispel it. Staff's analysis found that there was a statistically significant relationship between spot and forward power prices during the period January 1, 2000 through June 30, 2001.[14] The contracts at issue here were negotiated during this time period. The Commission should respect staff's analysis. It was performed by a nationally recognized econometrician with a specialty in energy futures markets and with access to the most comprehensive database of forward power contracts for the period and locations in question. Thus, based on logic, the Commission's prior statements, and the conclusions of our staff's strong analysis, it is beyond dispute that the prices and other terms of the forward contracts at issue here were influenced by the California spot markets.

The just and reasonable standard is met

The prices and other terms of the forward contracts at issue here are unjust and unreasonable and should be reformed. I base this conclusion on three factors. First, the Commission has found that the California spot markets resulted in unjust and unreasonable rates for the refund period (October 2, 2000 to June 19, 2001). This is the period during which the contracts at issue here were negotiated. Second, the California markets were subjected to various forms of manipulation, which may have included withholding.[15] Third, there was a clear nexus between the California spot market and the forward contract markets. The unlawful California spot prices strongly influenced forward contract prices. And fourth, the prices in many of these contracts are multiples of

[13]San Diego Gas & Electric Company, 95 FERC ¶ 61,418 (2001) at 62,547.

[14]Western Markets Report at VI-18.

[15]See Enron Power Marketing, Inc., et al, 103 FERC ¶ 61,343 (2003) where the Commission revokes the market-based authorities and terminates the blanket marketing certificates of various Enron affiliates. See also American Electric Power Service Companies, et al, 103 FERC ¶ 61,345 (2003), Enron Power Marketing, Inc. et al (2003) and Investigation of Anomalous Bidding Behavior and Practices in the Western Markets, 103 FERC ¶ 61,347 (2003) where the Commission establishes proceedings to investigate manipulative and questionable bidding behavior.

the $74 MWh price the Commission had declared would be used as a rough just and reasonable benchmark.

The public interest standard is met

Even if the majority is correct and the appropriate standard of review is the public interest standard, these agreements still do not withstand scrutiny and must be reformed. The tone of today's order is that the Mobile-Sierra line of cases places a thumb heavily on the scale in favor of sanctity of contracts, and thus sets an exceptionally high threshold in meeting the public interest standard. While the threshold may be high, it is not as high as today's order would place it for the particular contracts at issue.

The Mobile-Sierra case law involves contracts negotiated under a cost of service regime, and thus we do not know how the courts would instruct the Commission to address contracts negotiated in a market-based regime, especially under market conditions characterized by dysfunctional market rules, widespread manipulative conduct, and a lack of effective regulatory oversight. We are on new ground here, and the Commission is free to decide what circumstances give rise to the public interest.[16] We are clearly not limited to the traditional three-prong test that gets so much attention. Today's order as well as court precedent point out that those three factors are only examples of what to consider in determining the public interest.[17] Indeed, the Commission has great discretion in carrying out its statutory responsibilities, even where the public interest standard controls:

> ... even if contracts fall within the scope of the Mobile-Sierra decisions, the Supreme Court has emphasized that the relevant agency, here FERC, may always reform a contract found to be 'unlawful" or 'contrary to the public

---

[16]"...nowhere in the Supreme Court opinion is the term 'public interest' defined. Indeed, the Court seems to assume that the Commission decides what circumstances give rise to the public interest." Northeast Utilities Service Company v. FERC, 55 F.3d 686, 690 (1st Circuit 1995).

[17]"This definition of what is necessary in the public interest was formulated in the context of a low-rate case. It was not and could not be an across-the-board definition of what constitutes the public interest in other types of cases." Northeast Utilities, 55 F.3d at 690. Also see today's order at paragraph 6.

> interest,' i.e., that "contracts remain fully subject to the paramount power of the Commission to modify them when necessary in the public interest."[18]

The Commission's order setting this case for hearing implicitly recognized our discretion in evaluating these contracts under the public interest standard when it held that "the Commission will not modify market based contracts unless there are extraordinary circumstances."[19] We are instructed by the courts that "(w)hen there is no reason to question what occurred at the contract formation stage, the parties may be required to live with their bargains."[20] What's at issue then is rendering judgement regarding whether there were extraordinary circumstances at play during the contract formation stage that warrant contract reformation.

In evaluating whether to reform contracts involving a seller with market-based authority, we must be guided by the market circumstances that affected the negotiations and contract terms. It has already been established that the conditions in the California markets infected markets across the West, including the forward contracts, such as those at issue in this case. What were the circumstances under which buyers negotiated these contracts?

- The structure and rules of California markets were flawed, market power could be exercised in them, unjust and unreasonable rates had been charged and the potential existed that unlawful rates could be charged in the future. This is what the Commission found in November and December of 2000.

- Due to a combination of factors, there was a shortage of electricity that resulted in unprecedented, high, volatile, and unjust and unreasonable prices in the spot markets. As a result, the Commission admonished buyers to move load into forward contracts or suffer the consequences.

- The electricity market during this same time frame was manipulated through a number of strategies by sellers. These are documented in the Western Markets Report and in orders decided today where the Commission requires more than

---

[18]Northeast Utilities, 55 F.3d at 693.

[19]PacifiCorp v. Reliant Energy Services, Inc., et al, 99 FERC ¶ 61,381 (2002) at paragraph 25.

[20]Town of Norwood v. FERC, 587 F.2d 1306, 1312 (D.C. Cir. 1978).

fifty power sellers to defend against charges that they engaged in one or more manipulative strategies to pump up electricity prices.[21] The Commission is still investigating whether generation was strategically withheld from the market.

- During this same time frame, the price of natural gas, the fuel input for the marginal generation resources in the West, was manipulated by epidemic false reporting. This is documented in the Western Markets Report.

- As prices soared out of control, buyers had no basis to expect that this Commission would act forcefully to control them. The measures imposed in the December 2000 order were clearly ineffective and prices continued to rise. The Commission approved as just and reasonable spot prices of $273 MWh, $430 MWh and $300 MWh for the first three months of 2001, respectively,[22] and the Commission's then chairman reportedly advised Californians at the time that the only way out of the crisis was to "start putting shovels in the ground."[23]

This is the unprecedented environment in which these contracts were negotiated. The economic signals that formed the basis of the negotiations, and consequently the contract terms, were severely tainted. Buyers had their backs to the wall under these circumstances and essentially negotiated out of fears of yet higher prices or blackouts for their customers. Such conditions, spread over an area as large as the western United States, are truly extraordinary. And those conditions had extraordinary effects. For example:

---

[21]See American Electric Power Service Companies, et al, 103 FERC ¶ 61,345 (2003), Enron Power Marketing, Inc. et al (2003) and Investigation of Anomalous Bidding Behavior and Practices in the Western Markets, 103 FERC ¶ 61,347 (2003) where the Commission establishes proceedings to investigate manipulative and questionable bidding behavior.

[22]See, respectively, 94 FERC ¶ 61,245 (2001), 94 FERC ¶ 62,245 (2001), and an unpublished Notice of Proxy Price for April Wholesale Transactions in the California Wholesale Electric Market issue by the Director, Office of Markets, Tariffs and Rates, April 16, 2001.

[23]Statement attributed to Chairman Hebert, San Francisco Chronicle, April 12, 2001 (as reported on the San Francisco Chronicle's web site - - www.sfgate.com.)

- This Commission found it necessary in June 2001 to cap prices across this entire thirteen state region, 24 hours a day, seven days a week.[24] Such broad market intervention by this agency was unprecedented.

- A major California utility, Pacific Gas and Electric, declared bankruptcy as a direct result of the crisis and a second utility, Southern California Edison, teetered on the edge of bankruptcy.

- Local economies suffered devastating effects as a result of these market conditions. In the Pacific Northwest, factories closed and jobs were lost. The aluminum industry has exited the region for all intents and purposes.

- The movement toward competitive electricity markets at the national and state levels was almost brought to a halt. Consumers and policymakers were shocked and outraged that an out of control electricity market could wreak such havoc.

The tainted atmosphere in which these contracts were negotiated was unprecedented and extraordinary. The most influential benchmark used in negotiating forward contracts - - the spot market and expectations of future spot prices - - was wildly dysfunctional. When these contracts were negotiated, the Commission had already declared that conditions in the California markets allowed the exercise of market power and rates were unjust and unreasonable. And we now know that there was unprecedented manipulation of both the natural gas and electricity markets and epidemic false reporting of natural gas trading data.

There is simply no persuasive public interest rationale for protecting and sanctifying contracts negotiated in this unprecedented and extraordinary environment. Those market conditions certainly tainted any contracts negotiated during this time frame. It would simply defy logic to conclude that the high prices in these contracts were not adversely influenced by market conditions that included the exercise of market power and widespread market manipulation. Upholding such contracts violates the public interest. These contracts must be reformed.

Remedy

[24] San Diego Gas & Electric Company, 95 FERC ¶ 61,418 (2001).

I would remand this case to an Administrative Law Judge to determine specifically how each contract should be reformed. I would also recommend that the judge use the method set out in staff's Western Markets Report for determining the mitigated price in each contract. I suggest this method because staff's analysis has great credibility - - it had access to the most comprehensive data base of forward price contracts for the period and locations in question.

Staff's econometric analysis estimates the statistical relationship between spot power prices and forward contract prices (the "spot power elasticity"). This relationship shows how much forward prices rise for each percentage increase in spot prices. Staff also developed a formula representing the relationship between the degree to which spot power prices were excessive and the appropriate level for mitigated forward prices. This formula can be used to set mitigated forward contract prices. The excessiveness of spot prices (or the "spot power distortion" in staff's formulation) can be estimated by using the mitigated market clearing prices (MMCPs) being developed in the California refund proceeding. The MMCPs will represent the just and reasonable prices in the California spot markets. The spot power distortion can then be plugged into staff's formula to develop the mitigated forward prices.[25]

For these reasons, I dissent from today's order.

William L. Massey
Commissioner

[25]See pages V-16 to V-18 of the Western Markets Report.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

PacifiCorp	Docket Nos.	EL02-80-001
		EL02-80-002
		EL02-81-001
v.		EL02-81-002
		EL02-82-001
Reliant Energy Services, Inc.		EL02-82-002
Morgan Stanley Capital Group, Inc.		EL02-83-001
Williams Energy Marketing & Trading Company		EL02-83-002
El Paso Merchant Energy, L.P.		

(Consolidated)

(Issued June 26, 2003)

BROWNELL, Commissioner, concurring

1. I have been very clear in my prior statements about my belief in the sanctity of contracts. However, the issue of how to weigh contract sanctity in the context of the Western power crisis is, to say the least, a very difficult one, and I have struggled with it. The parties in this case were afforded the opportunity of a trial-type hearing and I have reviewed the evidence developed during that hearing. I have read the ALJ's Initial Decision and considered the parties' briefs on that Decision. I have also reviewed Staff's Final Report on Price Manipulation in Western Markets and the evidence submitted in the 100-Day Discovery Proceeding in the context of this case. Finally, the Commission took the unusual step of providing the parties an additional opportunity to address the issues in an oral argument before the Commission itself, and I have carefully considered all points raised during that oral argument. After reviewing all of this information, I agree with the order's conclusion that these were contracts voluntarily entered into and the Complainants have not met their burden of proving that the contracts are contrary to the public interest.

2. I am writing separately to express my concern about one aspect of the order: the rationale for concluding that modification of the contracts is subject to the public interest standard of review. When these cases were set for hearing, I noted that existing judicial case law seemed to indicate that the public interest standard applied to all of these contracts based solely on the contracts' silence as to the buyer's right to seek unilateral

changes under section 206.[1] Nevertheless, I was willing to set the issue for hearing so that the parties and the ALJ could have an opportunity to further explore whether my understanding of the case law was accurate. Three ALJs have now independently come to the same conclusion: judicial case law establishes that in the absence of clear contractual language allowing unilateral contract modification, the party seeking the change must meet the public interest standard.[2]

3. This order could have simply affirmed the ALJ's conclusion on this point and ended there the analysis of which standard to apply. That is what I am voting to do. Unfortunately, today's order fails to do so and instead bases the finding of the applicable standard on an analysis of the extrinsic evidence that parties did or did not present at hearing. By doing so, the order ignores the law. The Mobile-Sierra doctrine is not an invention of the FERC that we are free to mold as we wish; it is a directive from the Supreme Court. Moreover, the order misses an opportunity to provide clarity and certainty to all market participants and leaves open the possibility that the Commission may order unnecessary fact-finding on the parties' intent in future contract abrogation cases.

Nora Mead Brownell

[1] PacifiCorp v. Reliant Energy Services, Inc., et al., 99 FERC ¶ 61,381 (2002) (citing Texaco Inc. v. FERC, 148 F.3d 1091, 1096 (D.C. Cir. 1998) and Boston Edison Co. v. FERC, 233 F.3d 60, 67 (1st Cir. 2000)).

[2] Public Utilities Commission of the State of California v. Sellers of Long-Term Contracts to the California Department of Water Resources, et al., 102 FERC ¶ 63,013 at P 28 (2003); Nevada Power Company and Sierra Pacific Power Company v. Duke Energy Trading and Marketing, L.L.C., et al., 101 FERC ¶ 63,031 at P 27 (2002); and PacifiCorp v. Reliant Energy Services, Inc., et al., 102 FERC ¶ 63,030 at P 18 (2003).