ORAL ARGUMENT HAS NOT BEEN SCHEDULED

In the United States Court of Appeals for the District of Columbia Circuit

Nos. 14-1085 and 14-1136 (consolidated)

AMERICAN TRANSMISSION SYSTEMS, INC., *et al.*,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

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

BRIEF OF RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

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DECEMBER 4, 2015

CIRCUIT RULE 28(a)(1) CERTIFICATE

A. Parties and Amici

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

B. Rulings Under Review

1. *PJM Interconnection, L.L.C.*, 142 FERC ¶ 61,214 (2013) (Compliance Order), JA 57; and

2. *PJM Interconnection, L.L.C.*, 147 FERC ¶ 61,128 (2014) (Rehearing Order), JA 145.

C. Related Cases

By order of June 19, 2015, this Court ordered that oral argument in this matter be heard on the same day as argument in *Oklahoma Gas & Electric Co. v. FERC,* No. 14-1281. Each case presents similar issues concerning the *Mobile-Sierra* doctrine, which, when applicable, presumes that certain contract rates and practices are just and reasonable. Similar issues concerning *Mobile-Sierra* also are presented to this Court in *Emera Maine v. FERC*, No. 15-1139 (awaiting briefing), and to the Seventh Circuit in *MISO Transmission Owners v. FERC*, No. 14-2153 (briefing completed, awaiting scheduling of oral argument).

/s/ *Lona T. Perry*
Lona T. Perry
Deputy Solicitor

December 4, 2015

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GLOSSARY

Commission or FERC	The Federal Energy Regulatory Commission
Compliance Order	*PJM Interconnection, L.L.C.*, 142 FERC ¶ 61,214 (2013), JA 57
Order No. 1000	*Transm. & Cost Allocation by Transm. Owning & Operating Pub. Utils.*, Order No. 1000, 136 FERC ¶ 61,051 (2011), *order on reh'g and clarification*, 139 FERC ¶ 61,132, *order on reh'g and clarification*, 141 FERC ¶ 61,044 (2012), *aff'd sub nom. S.C. Pub. Serv. Auth. v. FERC*, 762 F.3d 41 (D.C. Cir. 2014).
PJM	PJM Interconnection, L.L.C., a Regional Transmission Organization operating in 13 eastern states and the District of Columbia
Rehearing Order	*PJM Interconnection, L.L.C.*, 147 FERC ¶ 61,128 (2014), JA 145
TO Br.	Brief of Petitioners and Intervenors Supporting Petitioners
TO Rehearing Request	The April 22, 2013 Request for Rehearing of The Indicated PJM Transmission Owners, R. 126, JA 89
Transmission Owners	Petitioners American Transmission Systems, Inc., Jersey Central Power & Light Co., Metropolitan Edison Co., Monongahela Power Co., Trans-Allegheny Interstate Line Co., and West Penn Power Co. (collectively FirstEnergy) and Public Service Electric and Gas Company, and supporting Intervenors PPL Electric Utilities Corp. and Exelon Corp.

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BRIEF OF RESPONDENT
FEDERAL ENERGY REGULATORY COMMISSION

STATEMENT OF THE ISSUES

This appeal involves a filing submitted by transmission-owning members of PJM Interconnection, L.L.C. (PJM), which operates the high-voltage transmission grid in multiple mid-Atlantic states, to comply with the Federal Energy Regulatory Commission's (FERC or Commission) Order No. 1000 rulemaking on transmission planning and regional cost allocation.[1] The PJM transmission owners

[1] *Transm. & Cost Allocation by Transm. Owning & Operating Pub. Utils.*, Order No. 1000, 136 FERC ¶ 61,051 (2011) (Order No. 1000), *order on reh'g and clarification*, 139 FERC ¶ 61,132 (Order No. 1000-A), *order on reh'g and*

assert that the Commission cannot remove or revise rights of first refusal to construct transmission facilities contained in their Transmission Owners Agreement without satisfying the *Mobile-Sierra* public interest standard.[2] The issues presented for review are:

1. Whether Transmission Owners[3] can demonstrate jurisdiction to review the challenged agency orders, where FERC did not require removal or revision of the cited provisions, and Transmission Owners failed to preserve for appeal their contention that the cited provisions constitute a right of first refusal?

2. Assuming jurisdiction, did the Commission reasonably determine that Transmission Owners' purported right of first refusal provision -- incorporated in a generally applicable agreement and agreed to among transmission owners commonly interested in precluding competition -- lacked characteristics necessary to justify application of a presumption that the provision is just and reasonable?

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clarification, 141 FERC ¶ 61,044 (2012) (Order No. 1000-B), *aff'd sub nom. S.C. Pub. Serv. Auth. v. FERC*, 762 F.3d 41 (D.C. Cir. 2014) (*South Carolina*).

[2] The doctrine is named for two Supreme Court cases: *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956); and *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956).

[3] "Transmission Owners" are Petitioners American Transmission Systems, Inc., Jersey Central Power & Light Co., Metropolitan Edison Co., Monongahela Power Co., Trans-Allegheny Interstate Line Co., and West Penn Power Co. (collectively FirstEnergy) and Public Service Electric and Gas Company, and supporting Intervenors PPL Electric Utilities Corp. and Exelon Corp.

COUNTERSTATEMENT OF JURISDICTION

Transmission Owners assert that they "are aggrieved because in the orders under review, FERC eliminated their contractual rights under the Owners Agreement, filed with and accepted by FERC, to construct and own certain transmission projects within their service territories." Brief of Petitioners and Intervenors Supporting Petitioners (TO Br.) at 24. Specifically, they rely upon sections 5.2 and 4.2.1 of the Transmission Owners Agreement as establishing rights of first refusal. *See id*. at 10-11.

As demonstrated more fully in Argument Section II *infra*, Transmission Owners have not demonstrated this Court's jurisdiction over these claims. The Commission did not order removal or revision of sections 5.2 and 4.2.1. Transmission Owners, moreover, have waived any claims that these provisions should be interpreted to constitute rights of first refusal. *See* Federal Power Act § 313(b), 16 U.S.C. § 825*l*(b) (mandatory rehearing requirement). Transmission Owners never relied upon (or cited) section 5.2 before the Commission on rehearing (or in their compliance filing) as constituting a right of first refusal. In the challenged orders, *PJM Interconnection, L.L.C.*, 142 FERC ¶ 61,214 (2013) (Compliance Order), *on reh'g*, 147 FERC ¶ 61,128 (2014) (Rehearing Order), the Commission found that section 4.2.1 did not create a right of first refusal, and granted PJM's request for clarification that it need not remove section 4.2.1 from

the Transmission Owners Agreement. Transmission Owners did not challenge this finding on rehearing to the Commission, nor have they challenged that finding in their brief on appeal.

STATUTES AND REGULATIONS

The relevant statutes and regulations are contained in the Addendum to this brief.

STATEMENT OF FACTS

I. STATUTORY AND REGULATORY BACKGROUND

A. Federal Power Act Ratesetting and the *Mobile-Sierra* Presumption of Reasonableness

Section 201 of the Federal Power Act, 16 U.S.C. § 824, gives the Commission jurisdiction over the rates, terms, and conditions of service for the transmission of electric energy in interstate commerce. Section 205 of the Federal Power Act, 16 U.S.C. § 824d, provides two mechanisms for ratesetting. First, regulated utilities may file "compilations of their rate schedules, or 'tariffs,' with the Commission," and provide service "on the terms and prices there set forth." *Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1*, 554 U.S. 527, 531 (2008) (citing Federal Power Act section 205(c), 16 U.S.C. § 824d(c)).

The Federal Power Act "also permits utilities to set rates with individual electricity purchasers through bilateral contracts." *Morgan Stanley*, 554 U.S. at 531 (citing Federal Power Act sections 205(c) and (d), 16 U.S.C. §§ 824d(c) and

(d)). *See also id.* (Federal Power Act "'departed from the scheme of purely tariff-based regulation and acknowledged that contracts between commercial buyers and sellers could be used in ratesetting.'") (quoting *Verizon Commc'ns Inc. v. FCC*, 535 U.S. 467, 479 (2002)); *New England Power Generators Ass'n, Inc. v. FERC*, 707 F.3d 364, 367 (D.C. Cir. 2013) ("Along with the unilateral filing of tariffs, the FPA also allows suppliers to set rates with individual purchasers via bilateral contract").

The *Mobile-Sierra* doctrine addresses "the authority of the Commission to modify rates set bilaterally by contract rather than unilaterally by tariff." *Morgan Stanley*, 554 U.S. at 532. *See, e.g., NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n*, 558 U.S. 165, 176 (2010) (remanding the question whether the rates set in a capacity auction qualified as a "contract rate" to which the *Mobile-Sierra* presumption of reasonableness applied).

Under the *Mobile-Sierra* doctrine, the Commission "must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just-and-reasonable' requirement imposed by law." *Morgan Stanley*, 554 U.S. at 530. This presumption is "grounded in the commonsense notion that '[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them.'" *Id*. at 545

(quoting *Verizon*, 535 U.S. at 479) (alteration by the Court). Thus, the *Mobile-Sierra* presumption rests on the premise that "the contract rates are the product of fair, arms-length negotiations." *Id.* at 554.

B. The Commission's Order No. 1000 Rulemaking

The Commission's efforts to foster wholesale electricity competition over broader geographic areas in recent decades have led to the creation of independent system operators and regional transmission organizations. *See Morgan Stanley*, 554 U.S. at 536-37. These independent regional entities operate the transmission grid on behalf of transmission-owning member utilities. *See NRG*, 558 U.S. at 169 & n.1 (explaining regional system operators' responsibilities). The Regional Transmission Organization involved here, PJM Interconnection LLC, takes its name from "Pennsylvania," "Jersey," and "Maryland," the home states of the first utilities to pool their excess power and capacity in 1927. *PPL Energyplus, LLC v. Solomon*, 766 F.3d 241, 247 (3d Cir. 2014). Today, the PJM region encompasses all or part of thirteen states and the District of Columbia. *Id.*

The Commission's Order No. 1000 rulemaking is the Commission's most recent reform of electric transmission planning and cost allocation. *See South Carolina*, 762 F.3d at 48. In that rulemaking, "the Commission required each transmission owning and operating public utility to participate in regional transmission planning that satisfies specific planning principles designed to prevent

undue discrimination and preference in transmission service, and that produces a regional transmission plan." *Id.* Among other things, to improve identification of more efficient or cost-effective transmission solutions, Order No. 1000 directed transmission providers "to remove provisions from Commission-jurisdictional tariffs and agreements that grant incumbent transmission providers a federal right of first refusal to construct transmission facilities selected in a regional transmission plan for purposes of cost allocation." Order No. 1000 P 253. *See also South Carolina*, 762 F.3d at 72 n.6 (an incumbent transmission provider is a utility that develops a transmission project within its own retail distribution territory, whereas a non-incumbent may be either a developer that does not have its own retail distribution territory or a provider proposing a project outside its own territory).

These rights of first refusal gave incumbents "the option to construct any new transmission facilities in their particular service areas, even if the proposal for new construction came from a third party," which discourages non-incumbent proposals. *South Carolina*, 762 F.3d at 72 (citing Order No. 1000 PP 256-57). The Commission was concerned that, "by deterring proposals from non-incumbents, rights of first refusal would impede the identification of some cost-efficient projects, resulting in the development of transmission facilities 'at a higher cost than necessary.'" *Id.* (citing Order No. 1000 PP 228-30). "Those

higher costs would be passed on to customers, yielding rates that were not 'just and reasonable.'" *Id*. The Commission thus "rested its right of first refusal ban on competition theory, determining that rights of first refusal posed a barrier to entry that made the transmission market inefficient, that transmission facilities would therefore be developed at higher-than-necessary cost, and that those amplified costs would be passed on to transmission customers." *Id*. at 77.

Some parties argued during the Order No. 1000 rulemaking proceeding that their right of first refusal provisions were protected by the *Mobile-Sierra* doctrine. The Commission determined that it would address assertions that individual jurisdictional tariffs and agreements contain a federal right of first refusal protected by *Mobile-Sierra* when it reviews the transmission providers' compliance filings, rather than in the generic rulemaking proceeding. Order No. 1000 P 292; Order No. 1000-A PP 388-89; Order No. 1000-B P 40.

On appeal, this Court fully affirmed the Order No. 1000 rulemaking, including its requirement that transmission providers remove rights of first refusal to construct transmission facilities selected in a regional transmission plan for purposes of cost allocation. *South Carolina*, 762 F.3d at 48-49, 72-81. The court found the *Mobile-Sierra* arguments premature, since the Commission deferred consideration of that issue to individual compliance proceedings. *Id.* at 81.

II. PJM's ORDER NO. 1000 COMPLIANCE PROCEEDING

A. PJM And The Transmission Owners Agreement

PJM was originally formed in 1927 as a power pool, which is a voluntary organization of utilities that operate generating and transmission facilities in a coordinated manner. *See Atl. City Elec. Co. v. FERC*, 295 F.3d 1, 5 (D.C. Cir. 2002). It became a "tight" power pool in 1956 by operating as a single control area with free-flowing transmission ties. *Id*. Under the 1956 operating agreement, the utility members of the PJM power pool agreed to place their generating facilities under the control of a central system dispatcher. *Id*. The PJM power pool utilities formed the PJM Interconnection Association in 1993, which served as the system dispatcher. *Id*.

In 1996, the utilities participating in the PJM power pool submitted a proposal to the Commission to transform the PJM Interconnection Association into the PJM Independent System Operator. *Id*. at 5-6. The PJM Independent System Operator would be a separate incorporated entity responsible for operating the transmission network, including dispatching generation to customers. *Id*. at 6.

PJM was approved as an Independent System Operator in 1997. *Id*. at 7. *See Pennsylvania -- New Jersey -- Maryland Interconnection*, 81 FERC ¶ 61,257 (1997), *on reh'g*, 92 FERC ¶ 61,282 (2000) (approving PJM as an Independent System Operator). Among the documents approved was a Transmission Owners

Agreement, entered into among eight transmission-owning utilities participating in the PJM power pool.[4] *See* 1997 Transmission Owners Agreement, attached to The Request for Rehearing of The Indicated PJM Transmission Owners (TO Rehearing Request), R. 126, JA 111-31. In that Agreement, each Transmission Owner agreed to transfer to the Independent System Operator the responsibility for administration of the PJM Transmission Tariff and regional transmission planning and operations. *See Pennsylvania -- New Jersey -- Maryland Interconnection*, 81 FERC ¶ 61,257 at 62,278.

In 2002, PJM was designated as the first Regional Transmission Organization. *FPL Energy Marcus Hook, L.P. v. FERC*, 430 F.3d 441, 442 (D.C. Cir. 2005).

On three occasions, PJM added new transmission-owning members in transactions that included separate Transmission Owners Agreements. *See PJM Interconnection, L.L.C. & Allegheny Power*, 96 FERC ¶ 61,060 (2001) (accepting PJM West Transmission Owners Agreement); *American Elec. Power Serv. Corp.*, 103 FERC ¶ 61,008 (2003) (accepting revised PJM West Transmission Owners Agreement), *on reh'g, New PJM Cos.*, 108 FERC ¶ 61,140 (2004); and *PJM*

[4] While ten transmission owners were designated on page 1 of the Agreement as "Parties," pursuant to section 6.5.1 on page 12 of the Agreement, three of those transmission owners are considered a single party for voting purposes.

Interconnection, L.L.C. & Va. Elec. & Power Co., 109 FERC ¶ 61,012 (2004) (accepting PJM South Transmission Owner Agreement), *on reh'g*, 110 FERC ¶ 61,234 (2005), *petition for review dismissed*, 468 F.3d 845 (D.C. Cir. 2006).

Concerned about the proliferation of Transmission Owner Agreements, both now and in the future, the Commission encouraged the Transmission Owners to consolidate the Transmission Owner Agreements into one document. *PJM Interconnection, L.L.C.*, 109 FERC ¶ 61,012 P 63. In response, PJM and the Transmission Owners entered into a single Consolidated Transmission Owners Agreement, dated December 15, 2005, which is attached to TO Br. as Appendix 1. Under that Agreement, all future Transmission Owners in PJM would be required to execute the Consolidated Agreement. *See* Consolidated Transmission Owners Agreement at sections 3.1 and 6.1, TO Br. Appendix 1 at 7, 16.

B. The PJM and Transmission Owners Order No. 1000 Compliance Filings

Order No. 1000 required that all public utility transmission providers submit filings with any revisions to tariffs and agreements necessary to comply with Order No. 1000, including the removal of federal rights of first refusal. *See* Order No. 1000-A P 389. Any provider that considered its contract to be protected by a *Mobile-Sierra* provision could present its arguments as part of its compliance filing. *Id*. The Commission stated that it would first decide, based on a more complete record, whether the agreement is protected by *Mobile-Sierra*, and if so,

whether the Commission has met the applicable standard of review to require modification. *Id*. If the Commission finds the agreement protected by *Mobile-Sierra*, and that the Commission cannot satisfy the public interest standard for modification, then the Commission would not consider the revisions proposed in the compliance filing. *Id*.

On October 25, 2012, PJM submitted its Order No. 1000 compliance filing, proposing conforming changes to its tariff and governing agreements. *See* Compliance Filing of PJM Interconnection, L.L.C., R. 19, JA 54. In that filing, PJM proposed no changes to eliminate federal rights of first refusal. *See id*. at 48-49, JA 55-56. PJM asserted that in *Primary Power, LLC*, 131 FERC ¶ 61,015 PP 62, 70 (2010), *on reh'g*, 140 FERC ¶ 61,052 PP 60-61 (2012), *petition for review dismissed*, *Pub. Serv. Elec. & Gas Co. v. FERC*, 783 F.3d 1270, 1274 (D.C. Cir. 2015), the Commission found that PJM's tariff and agreements contain no rights of first refusal. *See* PJM's 2012 Compliance Filing, R. 19 at 48-49, JA 55-56.

On the same day, the Transmission Owners made a separate compliance filing asserting that the 2005 Consolidated Transmission Owners Agreement and the PJM Operating Agreement contain provisions that provide Transmission Owners with a right of first refusal, and that "[n]either agreement includes any provision waiving *Mobile-Sierra* protections." *See* Compliance Filing by Indicated

PJM Transmission Owners Concerning *Mobile-Sierra* Protections For Right of First Refusal Provisions in PJM Agreements, R.18 at 2, JA 3.

In Transmission Owners' view, *Primary Power*, 140 FERC ¶ 61,052, found there is no right of first refusal in PJM's tariff applicable to "economic" projects (i.e. projects that are economically beneficial by reducing energy costs, as opposed to projects required for reliability or operational purposes). *See id*. at 4 n.12, 5 n.14, 16, JA 5, 6, 17. Under the 2005 Consolidated Transmission Owners Agreement, Transmission Owners argued that the section 4.2.1 obligation of Transmission Owners to build created a corresponding right of first refusal for reliability or operational projects. *Id*. at 5-6, JA 6-7. *See* Compliance Order P 156, JA 62-63. Transmission Owners also argued that various provisions of Schedule 6 of the PJM Operating Agreement supported the section 4.2.1 right of first refusal: sections 1.4(c) & (d), 1.5.6(f) & (g), 1.5.7(g), and 1.7. *See* Transmission Owners' 2012 Compliance Filing, R. 18 at 6-10, JA 7-11. *See also* Compliance Order PP 158-63, JA 63-64.

In response to the Transmission Owners' filing, protesters argued that *Mobile-Sierra* was inapplicable to the cited provisions because the provisions are more akin to "rules of general applicability" than "contractually negotiated rates," *see* Compliance Order P 168, JA 65, and because the provisions were not negotiated at arm's-length and were anticompetitive. *Id*. at PP 170-71, JA 65-66.

C. The Challenged Orders

The Commission found that Transmission Owners had not shown that the provisions they rely upon have the characteristics justifying the *Mobile-Sierra* presumption. Compliance Order P 182, JA 67. Specifically, the Commission found that the indicated provision of the Consolidated Transmission Owners Agreement was a prescription of general applicability that was not negotiated at arm's-length, and therefore application of the *Mobile-Sierra* presumption was not justified. *Id*. at PP 186-90, JA 68-69.

The Commission further found that PJM Interconnection was not in compliance with the Order No. 1000 directive to eliminate any federal rights of first refusal from Commission-jurisdictional tariffs and agreements. *Id*. at P 221, JA 74. Rather, the Commission found that certain provisions of the tariff and governing agreements were ambiguous, and directed PJM to remove or revise "any provision that could be read as supplying a federal right of first refusal for any type of transmission project that is selected in the regional plan for purposes of cost allocation." *Id*. P 222, JA 75.

The Commission, however, specifically rejected Transmission Owners' assertion that *Primary Power* upheld their interpretation of section 4.2.1 as a right of first refusal for non-economic (i.e. reliability or operational) projects. *Id*. P 223, JA 75. While *Primary Power* found the section 4.2.1 obligation to build

inapplicable to economic projects (i.e. projects that reduce energy costs), *id*. (citing *Primary Power*, 140 FERC ¶ 61,052 P 60), the Commission did not find it constituted a right of first refusal for non-economic projects. *Id*. Rather, the Commission pointed to its finding in Order No. 1000 that an obligation to build does not create a corresponding right of first refusal. *Id*. (citing Order No. 1000 P 261).

On rehearing, Transmission Owners did not reference the Commission's interpretation of section 4.2.1, but did challenge the Commission's determination that the purported right of first refusal provision in the Transmission Owners Agreement did not possess the characteristics warranting application of the *Mobile-Sierra* presumption. *See* TO Rehearing Request, R. 126 at 7-16, JA 95-104.[5]

In the Rehearing Order, the Commission reaffirmed its determination that Transmission Owners' cited provisions in the Transmission Owners Agreement and the PJM Operating Agreement are not properly read as federal rights of first refusal and are not entitled to *Mobile-Sierra* protection. Rehearing Order PP 96, 104-12, JA 150, 152-53.

[5] Transmission Owners also contended that a provision in a settlement agreement required application of *Mobile-Sierra*, *see id*. at 16-21, JA 104-09, a claim not raised on appeal.

The Commission also granted PJM's request for clarification that – in compliance with the Commission's directive to remove all provisions that could be read as providing a federal right of first refusal – PJM was *not* required to remove provisions, including section 4.2.1 of the Transmission Owners Agreement, that obligate Transmission Owners to build facilities selected in the Regional Expansion Plan. *See* Rehearing Order PP 122 & n.229, 129 & n.250, JA 156 & 168, 157-58 & 169. Having granted clarification, the Commission did not need to address PJM's alternative request for rehearing contending that those provisions do not establish a federal right of first refusal. *Id*. at P 129, JA 158.

SUMMARY OF ARGUMENT

On brief, Transmission Owners assert that sections 5.2 and 4.2.1 of the Transmission Owners Agreement provide them with a federal right of first refusal to construct transmission facilities that is subject to the *Mobile-Sierra* presumption of reasonableness. Transmission Owners assert that they "are aggrieved because in the orders under review, FERC eliminated their contractual rights under the Owners Agreement."

Transmission Owners have failed to demonstrate this Court's jurisdiction over these claims. The challenged orders did not require removal or revision of sections 5.2 or 4.2.1. Moreover, Transmission Owners' claims that these provisions constitute rights of first refusal are jurisdictionally barred.

Transmission Owners never relied upon (or cited) section 5.2 before the Commission on rehearing (or in their compliance filing) as constituting a right of first refusal. The challenged orders held that section 4.2.1 did not create a right of first refusal, and granted PJM clarification that it need not remove section 4.2.1 from the Transmission Owners Agreement because it did not constitute a right of first refusal. Transmission Owners did not challenge these findings regarding section 4.2.1 on rehearing, nor have they raised the issue in their brief on appeal.

Assuming jurisdiction, the Commission reasonably found, on two alternative bases, that the purported right of first refusal provision in the Transmission Owners Agreement lacked certain characteristics required for default application of a *Mobile-Sierra* presumption.

First, the Federal Power Act permits ratesetting through either generally-applicable "schedules" or individually-negotiated "contracts," but, under Supreme Court precedent, the *Mobile-Sierra* presumption of reasonableness applies only to the latter. Because those terms are undefined in the Federal Power Act, the Commission has discretion to interpret them. Here, the Commission determined that the Transmission Owners Agreement provision at issue has the characteristics of a rule of general applicability rather than an individually-negotiated contract. As the Commission explained, while the original PJM transmission owners had an

opportunity to negotiate the Transmission Owners Agreement, new owners must accept that Agreement as-is, with limited room for negotiation.

Transmission Owners acknowledge the distinction between generally-applicable tariffs and contracts, but contend that the *Mobile-Sierra* presumption of reasonableness necessarily applies to any "lawful contract." The Commission reasonably found this contention overbroad; while the type of freely-negotiated bilateral contract at issue in *Morgan Stanley* generally is subject to the presumption, other types of contracts are more properly viewed as tariffs, such as an agreement whose terms will be incorporated into the service agreements of all present and future customers. Tariffs themselves create contractual relationships, and generally-applicable tariff provisions may originate from private negotiations.

The record here supports the Commission's conclusion that the provisions at issue are more akin to generally-applicable tariffs than to individually-negotiated contracts. The Transmission Owners Agreement setting out the purported right of first refusal provisions was filed in 1997 by the eight original transmission owners. As Transmission Owners state, the purported right of first refusal provisions have never been renegotiated. New transmission owners seeking to join PJM are required to execute the Agreement. Any amendments to the Transmission Owners Agreement require a two-thirds majority of Transmission Owners.

Alternatively, the Commission reasonably found that the *Mobile-Sierra* presumption did not apply because the purported right of first refusal provisions were not the result of arm's-length bargaining. Transmission Owners have a common interest in protecting themselves from competition in transmission development.

Transmission Owners question the Commission's arm's-length inquiry, but *Morgan Stanley* establishes that the *Mobile-Sierra* presumption of reasonableness is premised upon the presence of fair, arm's-length negotiations, and the presumption should not apply where that premise is undermined. While Transmission Owners assert that PJM bargained against the Transmission Owners, PJM was not in fact a party to the 1997 Transmission Owners Agreement. Further -- while PJM was a signatory of (but not a "Party" to) the 2005 Consolidated Transmission Owners Agreement for limited purposes -- as the Commission found, PJM as the system operator is not a commercial entity with opposing economic self-interest. As a result, the purported right of first refusal provision lacks the assurance of reasonableness on which the *Mobile-Sierra* presumption is premised.

ARGUMENT

I. STANDARD OF REVIEW

The Court reviews FERC orders under the Administrative Procedure Act's arbitrary and capricious standard. *See, e.g.*, *Sithe/Independence Power Partners v. FERC*, 165 F.3d 944, 948 (D.C. Cir. 1999). The relevant inquiry is whether the agency has "examine[d] the relevant data and articulate[d] a rational connection between the facts found and the choice made." *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). The Commission's factual findings are conclusive if supported by substantial evidence. Federal Power Act § 313(b), 16 U.S.C. § 825*l*(b).

The Commission's determination regarding whether *Mobile-Sierra* properly applies to the Transmission Owners Agreement involves the interpretation of a FERC-jurisdictional statute. Section 205(c) of the Federal Power Act, 16 U.S.C. § 824d(c), allows utilities to set rates by filing "compilations of their rate schedules, or 'tariffs,' with the Commission," or they may set rates "with individual electricity purchasers through bilateral contracts." *Morgan Stanley*, 554 U.S. at 531 (citing Federal Power Act § 205(c) distinction between "schedules" and "contracts"). The *Mobile-Sierra* presumption of reasonableness applies only to "rates set bilaterally by contract." *Id*. at 532.

Accordingly, in determining whether *Mobile-Sierra* applies, the Commission must, in the first instance, differentiate between "rate schedules or 'tariffs'" and "contracts" under the Federal Power Act. *See id.* at 531. These terms are undefined in the statute and, therefore, the Commission has discretion to interpret them. *See, e.g., City of Arlington, Tex. v. FCC*, 133 S. Ct. 1863, 1870 (2013) (*Chevron* analysis applies to agency interpretation of a statutory provision); *ExxonMobil Gas Mktg. Co. v. FERC*, 297 F.3d 1071, 1084 (D.C. Cir. 2002) (affording deference to Commission jurisdictional "line-drawing"); *Pub. Utils. Comm'n v. FERC*, 143 F.3d 610, 615 (D.C. Cir. 1998) (affording deference to FERC's determination of the jurisdictional "line of demarcation" drawn by the statute). Accordingly, here, the Court should defer to the Commission's reasonable judgment regarding the line between a generally applicable "schedule," or tariff, and a negotiated "contract."

II. TRANSMISSION OWNERS HAVE FAILED TO ESTABLISH THIS COURT'S JURISDICTION OVER THEIR CLAIMS.

On brief, Transmission Owners assert that sections 5.2 and 4.2.1 of the 2005 Consolidated Transmission Owners Agreement constitute rights of first refusal. *See* Brief of Petitioners and Intervenors Supporting Petitioners (TO Br.) 10-11. Specifically, Transmission Owners argue that, in the Transmission Owners Agreement, they "agree to allow PJM to plan expansion of the PJM transmission system," *id*. at 10 (citing section 4.1.4, TO Br. Appendix 1 at 9), "but each PJM

Transmission Owner retains 'the right to build . . . all or any part of its assets, including transmission facilities.'" *Id*. (quoting section 5.2, TO Br. Appendix 1 at 15). "Each PJM Transmission Owner is also obligated to construct new transmission facilities specified in a PJM regional plan when PJM designates it to do so." *Id*. at 10-11 (citing section 4.2.1, TO Br. Appendix 1 at 9).

Transmission Owners assert that they "are aggrieved because in the orders under review, FERC eliminated their contractual rights under the [Transmission] Owners Agreement . . . to construct and own certain transmission projects within their service territories." *See* TO Br. 24. *See also id*. at 3 ("FERC's abrogation of the utilities' contractual rights [under the Consolidated Transmission Owners Agreement] aggrieves the utilities under the [Federal Power Act] and establishes constitutional standing.")

Transmission Owners have failed to establish the Court's jurisdiction over these claims. They are not aggrieved by any changes to sections 5.2 or 4.2.1 because the Commission did not require revision or removal of these sections in compliance with the directive to remove rights of first refusal. *See* Rehearing Order PP 139, 148, JA 160, 162 (accepting PJM's proposal to remove one sentence from the PJM Operating Agreement in compliance with the directive to remove rights of first refusal). Further, Transmission Owners failed to preserve on appeal any contention that these provisions in fact constitute rights of first refusal.

Section 5.2 was not raised to the Commission, and Transmission Owners failed to challenge on rehearing or before this Court the Commission's finding that section 4.2.1 does not constitute a right of first refusal.

A. Section 5.2 Was Not Raised To The Commission.

Transmission Owners have failed to preserve for appellate review any claim that section 5.2 constitutes a right of first refusal. *See* Federal Power Act section 313(b), 16 U.S.C. § 825*l*(b) ("No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do.").

Transmission Owners did not cite section 5.2 to the Commission in this proceeding on rehearing (or even in their compliance filing), let alone argue that section 5.2 constitutes a right of first refusal. *See* TO Rehearing Request, R. 126, at 13, JA 101 (arguing only that section 4.2.1 of the Transmission Owners Agreement constitutes a right of first refusal). *See also* Compliance Order PP 156-57, JA 62-63 (detailing Transmission Owners' arguments that section 4.2.1 of the Transmission Owners Agreement constitutes a right of first refusal); Compliance Filing by Indicated PJM Transmission Owners Concerning *Mobile-Sierra* Protections for Right of First Refusal Provisions in PJM Agreements, R. 18 at 5-6, JA 6-7 (arguing that section 4.2.1 constitutes a right of first refusal).

Having failed to rely upon – or even cite – section 5.2 before the Commission, Transmission Owners are jurisdictionally barred from asserting that section as a basis for a right of first refusal on appeal. *See, e.g., Constellation Energy Commodities Grp., Inc. v. FERC*, 457 F.3d 14, 21 (D.C. Cir. 2006) (no jurisdiction where petitioners "in fact never even cited the sections of the tariff upon which they now rely" before the agency); *Intermountain Mun. Gas Agency v. FERC*, 326 F.3d 1281, 1286 n.7 (D.C. Cir. 2003) (no jurisdiction where petitioner's "rehearing request did not even cite the statute or use the statutory phrase . . . on which it now relies").

That Transmission Owners raised section 5.2 in the earlier *Primary Power* proceeding – in which the Commission found section 5.2 does *not* constitute a right of first refusal[6] – does not change this analysis. *See, e.g., Ind. Util. Regulatory Comm'n v. FERC*, 668 F.3d 735, 739 (D.C. Cir. 2012) (arguments must

[6] *See Primary Power, LLC*, 140 FERC ¶ 61,052 P 61 (2012). "Article 5.2 states that transmission owners have reserved 'the right to build, finance, own, acquire, sell, dispose, retire, merge or otherwise transfer or convey all or any part of its assets, including any Transmission Facilities.'" *Id*. "This provision refers only to a transmission owner's right to construct and control its assets; the provision does not guarantee a transmission owner the right to construct all assets in a defined zone or geographic area." *Id*. This Court ultimately dismissed Transmission Owners' petition for review of *Primary Power* on the ground that, given intervening events, any decision in that case would constitute an impermissible advisory opinion. *Pub. Serv. Elec. & Gas Co. v. FERC*, 783 F.3d 1270, 1274 (D.C Cir. 2015).

be "set forth specifically" in request for rehearing; objections made in other filings are insufficient); *Allegheny Power v. FERC*, 437 F.3d 1215, 1220 (D.C. Cir. 2006) (objection cannot be preserved indirectly, but must be raised with specificity, and therefore arguments purportedly incorporated by reference in petition for rehearing did not preserve arguments).

B. Transmission Owners Failed to Challenge The Commission's Finding That Section 4.2.1 Does Not Constitute A Right Of First Refusal.

Transmission Owners assert that "[a]lthough the focus of this proceeding is on the provisions of the [Transmission] Owners Agreement, FERC did not construe the meaning of the Owners Agreement, but instead assumed that it contained the rights FERC sought to abrogate." TO Br. 25. To the contrary, in the challenged orders, the Commission did interpret the provisions that Transmission Owners contended constitute a right of first refusal. *See* Compliance Order P 178, JA 67 ("Specific arguments regarding whether [the provisions relied upon by Transmission Owners] are properly read as including a federal right of first refusal are addressed in the following section.")

Specifically, the Commission rejected Transmission Owners' claim that section 4.2.1 of the Transmission Owners Agreement creates a right of first refusal. Compliance Order P 223, JA 75. The Commission further granted PJM clarification that it did not need to remove or revise section 4.2.1 in compliance

with the directive to remove federal rights of first refusal. Rehearing Order P 129 & n.250, JA 157-58 & 169 (citing n.229, JA 168). Because Transmission Owners did not challenge these findings before the Commission or on appeal before this Court, Transmission Owners have waived any challenge to this determination.

1. Transmission Owners Failed to Seek Rehearing Of The Commission's Finding In The Compliance Order That Section 4.2.1 Does Not Constitute A Right Of First Refusal.

Order No. 1000 required that all public utility transmission providers submit compliance filings that include any necessary revisions to tariffs and agreements, including the removal of federal rights of first refusal. *See* Order No. 1000-A at P 389. Any provider that considered its contract to be protected by a *Mobile-Sierra* provision could present its arguments as part of its compliance filing. *Id.*

On October 25, 2012, PJM submitted its Order No. 1000 compliance filing, but proposed no changes to eliminate federal rights of first refusal. *See* Compliance Filing of PJM Interconnection, L.L.C., R. 19 at 48-49, JA 55-56.

On the same day, the Transmission Owners made a separate compliance filing asserting that the 2005 Consolidated Transmission Owners Agreement and the PJM Operating Agreement[7] contain provisions that provide Transmission

[7] Transmission Owners relied upon various provisions of Schedule 6 of the PJM Operating Agreement: sections 1.4(c) & (d), 1.5.6(f) & (g), 1.5.7(g), and 1.7. *See* Transmission Owners' 2012 Compliance Filing, R. 18 at 6-10, JA 7-11. *See also* Compliance Order PP 158-63, JA 63-64. The Compliance Order rejected the argument that the cited Operating Agreement provisions "are properly read as

Owners with a right of first refusal protected by *Mobile-Sierra*. *See* Compliance Filing by Indicated PJM Transmission Owners Concerning *Mobile-Sierra* Protections For Right of First Refusal Provisions in PJM Agreements, R.18 at 2, JA 3. As relevant here, Transmission Owners argued that section 4.2.1 of the 2005 Consolidated Transmission Owners Agreement created a right of first refusal. *Id*. at 5-6, JA 6-7. Section 4.2.1 provides that:

> Parties designated as the appropriate entities to construct and own or finance enhancements or expansions applicable to the PJM Region specified in the Regional Transmission Plan or required to modify Transmission Facilities pursuant to the PJM Tariff shall construct and own or finance such facilities or enter into appropriate contracts to fulfill such obligations.

See id. at 5 and Appendix A, section 4.2.1, JA 6, 24. Transmission Owners argued that, by this language, they "agreed to impose upon themselves the obligation to build whatever PJM deems necessary under its planning authority." *See id*. at 5, JA 6. In Transmission Owners' view, in *Primary Power*, the Commission tied the presence of a right of first refusal to the existence of an obligation to build. *Id*. at 16-17, JA 17-18. *See also id*. at 7, JA 8 (arguing that *Primary Power* held that "the obligation to build is a distinguishing characteristic in determining whether there is a [right of first refusal]") (citing *Primary Power*, 140 FERC ¶ 61,052 P 42).

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federal rights of first refusal and are entitled to *Mobile-Sierra* protection." Rehearing Order P 96, JA 150. *See also* Compliance Order P 182, JA 67. Transmission Owners do not raise any of these provisions and do not challenge the Commission's finding with regard to the Operating Agreement in their brief.

In the Compliance Order, the Commission found that PJM was not in compliance with the Order No. 1000 directive to eliminate any federal rights of first refusal from its tariffs and agreements. Compliance Order P 221, JA 74-75. Rather, the Commission found certain provisions ambiguous, and directed PJM to remove or revise "any provision that could be read as supplying a federal right of first refusal for any type of transmission project that is selected in the regional plan for purposes of cost allocation." *Id*. P 222, JA 75.

In the next paragraph, however, the Commission specifically rejected Transmission Owners' argument that their obligation to build in section 4.2.1 carried with it a corresponding right of first refusal. Compliance Order P 223, JA 75. While *Primary Power* found the section 4.2.1 obligation to build inapplicable to economic projects (i.e. projects built to decrease energy costs), that does not mean that section 4.2.1 creates a right of first refusal for non-economic projects (i.e. reliability or operational projects). *Id*. (citing *Primary Power*, 140 FERC ¶ 61,052 P 60). Rather, the Commission pointed to its finding in Order No. 1000 that an obligation to build does not create a corresponding right of first refusal. *Id*. (citing Order No. 1000 P 261).

On rehearing of the Compliance Order, Transmission Owners did not reference or challenge the finding in Compliance Order P 223, JA 75 regarding section 4.2.1. Rather, Transmission Owners asserted that the Commission had

"concluded in the [Compliance Order] that there is a [right of first refusal]. . . ." TO Rehearing Request, R. 126 at 6, JA 94. *See also id*. at 5, JA 93 ("[t]hat there is a PJM [right of first refusal] has already been established and is not at issue"). The Transmission Owners pointed to the Commission's finding that PJM had not complied with the directive to remove federal rights of first refusal because provisions of PJM's tariff and agreements were ambiguous. *Id*. at 5-6, JA 93-94 (citing Compliance Order P 221, JA 74-75). Therefore, Transmission Owners stated that "the issue on which the PJM Indicated Transmission Owners seek rehearing is whether or not *Mobile-Sierra* protections apply to the [right of first refusal]." *Id*. at 6, JA 94.

To preserve for appellate review its arguments that section 4.2.1 creates a right of first refusal, Transmission Owners were required to raise this issue on rehearing of the Compliance Order. Parties are obligated to seek rehearing where the Commission's order "provide[s] reasonable notice of its import." *E. Tex. Coop., Inc. v. FERC*, 218 F.3d 750, 754 (D.C. Cir. 2000). Here, the Compliance Order was sufficiently clear to put Transmission Owners on notice of the Commission's holding with regard to section 4.2.1. Certainly, "a reader schooled in [electric] regulation" would have "perceived a very substantial risk" that the Commission had rejected the claim that section 4.2.1 creates a right of first refusal. *ANR Pipeline Co. v. FERC*, 988 F.2d 1229, 1234 (D.C. Cir. 1993).

Even if the holding could be considered ambiguous, that does not excuse the obligation to seek clarification or rehearing. The remedy for ambiguity "is to petition the Commission for reconsideration within the [statutory time] period, enabling judicial review to be pursued (if Commission resolution of the ambiguity is adverse) after disposition of that petition." *ICC v. Brotherhood of Locomotive Engineers*, 482 U.S. 270, 286 (1987). *See also, e.g., ANR Pipeline*, 988 F.2d at 1234 (uncertainty as to potential interpretations, even if justifiable, does not excuse failing to ask for rehearing or clarification).

2. Transmission Owners Failed to Challenge The Commission's Clarification In The Rehearing Order That Section 4.2.1 Need Not Be Removed From The Transmission Owners Agreement Because It Does Not Constitute A Right Of First Refusal.

Unlike the Transmission Owners, PJM *did* request clarification, or in the alternative, rehearing, that it was *not* required to remove or revise section 4.2.1 of the Transmission Owners Agreement, in response to the Compliance Order directive to remove or revise provisions that *might* be read as a right of first refusal. *See* PJM Interconnection, L.L.C. Limited Request for Clarification or, in the Alternative, Rehearing, R. 129 at 5-7 & n.25, JA 137-39. PJM argued that "default reliability provisions" – including section 4.2.1 – that require transmission

owners to construct facilities if directed do not constitute a right of first refusal and need not be removed or revised pursuant to the Commission's directive. *See id.* [8]

The Commission granted PJM's request for clarification. *See* Rehearing Order P 129 & n.250, JA 157-58 & 169 (citing n.229, JA 168). The Commission found that "the directive in [the Compliance Order] to remove or revise any provision that could be read as granting a federal right of first refusal does not require PJM to remove or revise the reliability default provisions that obligate an incumbent transmission owner to build." *Id*. The Rehearing Order noted that PJM's request for clarification concerned section 4.2.1 of the Transmission Owners Agreement, as well as Schedule 6, section 1.7 of the PJM Operating Agreement. *Id*. at P 129 n.250, JA 157 & 169 (citing note 229, JA 168). The Commission further found that, "[h]aving granted PJM's request for clarification, we need not address PJM's alternative request for rehearing, in which PJM contends that certain provisions do not establish a federal right of first refusal." *Id*. at P 129, JA 158.

Accordingly, to preserve their arguments regarding section 4.2.1, Transmission Owners were obligated to seek rehearing of the Compliance Order

[8] In response to the Commission's directive to eliminate ambiguities regarding potential rights of first refusal, PJM proposed to eliminate one sentence in the PJM Operating Agreement, Schedule 6, section 1.5.6(k). *See* July 22, 2013 Compliance Filing, R. 143 at 21-22, JA 143-44. *See also* Rehearing Order P 139, JA 160 (setting out eliminated sentence); *id*. P 148, JA 162 (accepting change).

finding rejecting Transmission Owners' interpretation of section 4.2.1. *See Smith Lake Improvement & Stakeholders Ass'n v. FERC*, 768 F.3d 1, 2-3 (D.C. Cir. 2014) (court's jurisdiction is limited to cases in which petitioner seeks rehearing of and petitions for review of first aggrieving order). Even if the Compliance Order could be viewed as insufficiently clear to provide notice of the holding, thereby providing "reasonable grounds" for failure to seek rehearing, *see E. Tex.*, 218 F.3d at 754, the Commission's clarification on rehearing removed any doubt that the Commission did not regard section 4.2.1 as constituting a right of first refusal. As Transmission Owners did not seek rehearing of the Rehearing Order, their claims would in any event be barred. *Cf. E. Tex.*, 218 F.3d at 755 (jurisdiction preserved where petitioner filed for rehearing of the first order providing notice of holding).

Further, Transmission Owners' reliance on section 4.2.1 is "twice waived," as Transmission Owners failed to challenge the Commission's finding in their opening brief. *See, e.g., Consolidated Edison Co. of N.Y. v. FERC*, 347 F.3d 964, 970 (D.C. Cir. 2003) (finding an argument "twice waived" where it was not raised before the Commission or in petitioner's opening brief); *Xcel Energy Servs., Inc. v. FERC*, 510 F.3d 314, 318 (D.C. Cir. 2007) (same). Under these circumstances, Transmission Owners have demonstrated no right of first refusal in the Transmission Owners Agreement for the *Mobile-Sierra* doctrine to protect.

III. THE COMMISSION REASONABLY DETERMINED THAT THE *MOBILE-SIERRA* PRESUMPTION DOES NOT APPLY BECAUSE THE PURPORTED RIGHT OF FIRST REFUSAL PROVISION LACKS CHARACTERISTICS JUSTIFYING THE PRESUMPTION.

Assuming jurisdiction, the Commission reasonably determined that the purported right of first refusal provision in the Transmission Owners Agreement (section 4.2.1) lacks the requisite characteristics to warrant application of the *Mobile-Sierra* presumption of reasonableness.

In *Morgan Stanley*, the Supreme Court recognized that, under the Federal Power Act, utilities may set rates either by unilaterally filing compilations of their rate schedules or "tariffs" with the Commission, or they may "set rates with individual electricity purchasers through bilateral contracts." 554 U.S. at 531 (citing Federal Power Act section 205(c), 16 U.S.C. § 824d(c)). In the latter instance, "[u]nder the *Mobile-Sierra* doctrine," FERC "must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and can only modify the contract if it is required in the public interest. *Id*. at 530. The *Mobile-Sierra* presumption rests on the premise "that the contract rates are the product of fair, arms-length negotiations." *Id*. at 554.

Following *Morgan Stanley*, provisions in bilateral sales contracts freely negotiated at arm's-length would come within the presumption. Compliance Order P 184, JA 67-68. This case, however, poses the question of the applicability of

such a presumption to a multi-lateral Transmission Owners Agreement, the terms of which are applied to new transmission owners joining PJM on a "take-it-or-leave it" basis. *See id*. P 187, JA 68. This Court has in fact expressed doubt that *Mobile-Sierra* applies to a similar transmission owner's agreement in New England "particularly when that contract is a complex agreement establishing a new regional structure impacting all market participants." *Me. Pub. Utils. Comm'n v. FERC*, 454 F.3d 278, 284 (D.C. Cir. 2006) (finding that "[t]his hardly seems the situation *Mobile-Sierra* was designed to guard against").

Moreover, the particular type of provision at issue – a right of first refusal – has the effect of insulating the signatory incumbent transmission owners from competition from non-party, non-incumbent transmission developers, an interest that all the contracting transmission-owning parties share. Compliance Order P 189, JA 68; Rehearing Order P 110, JA 153. This Court has upheld the Commission's conclusion that such provisions are anticompetitive and unjust and unreasonable. *See South Carolina*, 762 F.3d at 77.

Under these circumstances, in the challenged orders, the Commission reasonably determined that the *Mobile-Sierra* presumption of reasonableness did not apply to the Transmission Owners' purported right of first refusal provision. Because of its "take-it-or-leave-it" nature, the Transmission Owners Agreement has the characteristics of a prescription of general applicability, or tariff, rather

than an individualized, negotiated contract, and, as a result, does not merit a *Mobile-Sierra* presumption of reasonableness. *See* Compliance Order PP 186-187, JA 68; Rehearing Order PP 104-05, 112, JA 152, 153.

Alternatively, the Commission also reasonably found that the *Mobile-Sierra* presumption does not apply to the Transmission Owners Agreement's purported right of first refusal provision because transmission owners have a common interest in protecting themselves from competition, which precludes arm's-length bargaining. Compliance Order PP 189-90, JA 68-69; Rehearing Order PP 107-10, JA 152-53.

Transmission Owners contend that the Commission had no basis in law or fact for making these alternative determinations. *See Pierce v. SEC*, 786 F.3d 1027, 1034 (D.C. Cir. 2015) ("A reviewing court will uphold agency action resting on several independent grounds if any of those grounds validly supports the result.") Transmission Owners' arguments lack merit.

A. The Commission Reasonably Determined That The *Mobile-Sierra* Presumption Does Not Apply Because The Transmission Owners Agreement Is More Akin To A Generally-Applicable Tariff.

The Commission reasonably determined that the provision of the Consolidated Transmission Owners Agreement that PJM Transmission Owners contended includes a federal right of first refusal is a prescription of general applicability rather than negotiated rate provision that is necessarily entitled to a

Mobile-Sierra presumption. Compliance Order P 186, JA 68. Any new PJM Transmission Owner is required to accept the provision as-is, with limited room for negotiation. *Id*. P 187, JA 68.

1. Supreme Court Precedent Distinguishes Between Generally-Applicable Tariffs And Individually-Negotiated Contracts For *Mobile-Sierra* Purposes.

As the Commission found, Supreme Court precedent on *Mobile-Sierra* requires that the Commission differentiate between "prescriptions of general applicability," like tariffs, and "contractually negotiated rates." Compliance Order P 186, JA 68 (quoting *NRG*, 558 U.S. at 176). Under section 205(c) of the Federal Power Act, 16 U.S.C. § 824d(c), utilities may set rates by filing "compilations of their rate schedules, or 'tariffs,' with the Commission," or they may set rates "with individual electricity purchasers through bilateral contracts." *Morgan Stanley*, 554 U.S. at 531 (citing Federal Power Act § 205(c)). *See also, e.g., NRG*, 558 U.S. at 171 (Federal Power Act "allows regulated utilities to set rates unilaterally by tariff; alternatively, sellers and buyers may agree on rates by contract"); *Mobile*, 350 U.S. at 339 (analogous provisions of the Natural Gas Act permit rates to be set either by uniform tariffs or by "individualized arrangements" between the utility and its customers). The *Mobile-Sierra* presumption of reasonableness applies only to "the authority of the Commission to modify rates set bilaterally by contract rather than unilaterally by tariff." *Morgan Stanley*, 554 U.S. at 532. *See also Verizon*, 535

U.S. at 478-79 (tariff schedules are reviewed under the ordinary just and reasonable standard, whereas negotiated contracts are subject to *Mobile-Sierra*).

Transmission Owners acknowledge the distinction between tariffs and contracts, *see* TO Br. 31-32, but argue that *Mobile-Sierra* applies to any instrument that is a "lawful contract." *Id*. at 30. The Commission reasonably found this view overly broad. Rehearing Order P 105, JA 152; Compliance Order P 182, JA 67. Under *Morgan Stanley*, the *Mobile-Sierra* presumption applies to "provisions in bilateral power sales contracts freely negotiated at arm's length between sophisticated parties." Compliance Order P 184, JA 67-68 (citing *Morgan Stanley*, 554 U.S. at 530, 534). The Commission recognized, however, that the terms of other contracts are more "properly classified as tariff rates," such as an agreement whose terms will be incorporated into the service agreements of all present and future customers. *Id*.; Rehearing Order P 105, JA 152. Even if a provision originates from individual negotiations, it is nevertheless a tariff rate when it is generally applied. *See, e.g*., *MCI Telecomm. Corp. v. FCC*, 917 F.2d 30, 38 (D.C. Cir. 1990) (recognizing that tariff rates may be "arrived at through negotiations between a carrier and an individual customer" and then made generally available to other customers); *Fla. E. Coast Ry. Co. v. CSX Transp., Inc*., 42 F.3d 1125, 1130 n.5 (7th Cir. 1994) (finding that, although "published tariffs may have been

determined initially by way of private negotiation," such rates are nonetheless tariff rates once they are published and generally applied).

The presence of a contractual relationship does not differentiate the categories of tariffs and contracts; both involve contractual relationships. As this Court has recognized, a tariff is "the contract which governs a pipeline's service to its customers." *ANR Pipeline Co. v. FERC*, 931 F.2d 88, 90 n.1 (D.C. Cir. 1991). *See also, e.g.*, *Metro E. Ctr. for Conditioning & Health v. Qwest Commc'n Int'l, Inc*., 294 F.3d 924, 926 (7th Cir. 2002) ("The tariff is an offer that the customer accepts by using the product.").

Tariffs differ from private contracts, therefore, not in the creation of a contractual relationship but, rather, because tariffs, unlike private contracts, "are not subject to alteration one customer (or one clause) at a time." *Metro East*, 294 F.3d at 926. A tariff is a "take-it-or-leave-it proposition" and thus not an "agreement" in the sense that it is reached by individual negotiation. *Id*. *See also Balt. & Ohio Chi. Terminal R.R. Co. v. Wis. Cent. Ltd*., 154 F.3d 404, 406 (7th Cir. 1998) (distinguishing "tariffs, which are publicly announced take-it-or-leave-it form contracts" from "individually negotiated agreements"). Transmission Owners themselves recognize that a buyer accepts a tariff "offer" by executing a service agreement incorporating the tariff provisions; "[t]he buyer does not, however, negotiate the provisions or affect them by its own bargaining conduct."

TO Br. 31-32. In *United Gas Pipeline Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103, 115 & n.8 (1958), the Supreme Court held that *Mobile-Sierra* did not apply to so-called "tariff and service" contracts that did not contain an individually-negotiated rate, but rather "refer[red] to rate schedules of general applicability on file with the Commission."

Thus, the Commission reasonably concluded, following the Supreme Court guidance in *NRG*, that an agreement may be more akin to a "prescription of general applicability" than a "contractually negotiated rate." Compliance Order P 186, JA 68 (quoting *NRG*, 558 U.S. at 176). Transmission Owners contend that *NRG* only addressed "certain parties' contention that *Mobile-Sierra* was inapplicable because the auction prices and transition rates in question were not contract rates," TO Br. at 35, and that "FERC agreed with contentions that the rates at issue were not themselves contract rates." *Id*. at 35, 36. As *NRG* stated, however, FERC did not agree that the rates at issue were not contract rates at all, but rather "FERC agree[d] that the rates covered by the settlement 'are not themselves contract rates to which the Commission was *required* to apply *Mobile Sierra*.'" *NRG*, 558 U.S. at 176 (quoting FERC's brief). *See, e.g.*, *Midwest Indep. Sys. Operator*, 147 FERC ¶ 61,127 P 117 (2014), *appeal pending, Midwest ISO Transmission Owners v. FERC,* No. 14-2153 (7th Cir.) ("We think it is clear from the context that when the Court [in *NRG*] referred to 'contract rates,' it was referring to rates to which the

Commission is required to apply a *Mobile-Sierra* presumption. Specifically, the Court acknowledged the Commission's use of the term 'contract rates' in this way.").

On remand, the Commission expressly recognized that the capacity auctions at issue in *NRG* possessed contractual characteristics: sellers bidding into the auction are committed to supply at the auction-clearing price, and buyers purchasing in the auction are obligated to pay.[9] *See Devon Power LLC*, 134 FERC ¶ 61,208 PP 22, 23, 25, *on reh'g*, 137 FERC ¶ 61,073 (2011). Nevertheless, the Commission found the auction results more akin to generally-applicable tariff rates than individually-negotiated contract rates because the result of the auctions – the clearing prices – "apply to all suppliers and purchasers of capacity within the ISO New England market," and the buyers and sellers do not contract individually with each other. *Devon Power*, 137 FERC ¶ 61,073 at PP 12-13. The Commission decided however, in an exercise of its discretion, to apply the *Mobile-Sierra* standard to future challenges to those rates. *See id.* at P 14. "[A]lthough these auctions will not result in contracts between buyers and sellers, we find that they nevertheless share with freely-negotiated contracts certain market-based features that tend to assure just and reasonable rates." *Id*. at P 19.

[9] As Transmission Owners note, the issue of transition payments was by this time moot. *See* TO Br. at 37 n.12.

On appeal of this determination, this Court acknowledged the issue presented in classifying the auction rates as either generally-applicable tariff rates or individually-negotiated contract rates. This Court noted that, while "[u]ntil recently, only two types of rates were involved: tariff rates and contract rates," the "debut of capacity auctions poses a new challenge." *See New England Power Generators*, 707 F.3d at 366. Ultimately, however, this Court did not reach this issue. "Assuming, without deciding, that the auction rates [were] not contract rates," this Court found it was within the Commission's "considerable discretion" under the just and reasonable standard to adopt the public interest standard for the capacity auction rates. 707 F.3d at 370-71.

Accordingly -- while not reaching the merits of the determination that auction rates were more akin to tariff rather than contract rates -- both *NRG* and *New England Power Generators* recognized that an issue existed as to whether or not the auction rates at issue were contract rates to which *Mobile-Sierra* necessarily applied. *See, e.g., Me. Pub. Utils. Comm'n v. FERC*, 625 F.3d 754, 759 (D.C. Cir. 2010) (remanding the *NRG* issues to the Commission, finding that "the Supreme Court's holding [in *NRG*] did not resolve this case, because as the parties' positions before it made clear, there was still an open question about whether the auction rates resulting from the settlement agreement were the type of rates to which *Mobile-Sierra* applied.").

2. The Commission Reasonably Determined That The Agreement Has The Characteristics Of A Generally-Applicable Tariff.

The Commission reasonably concluded that the *Mobile-Sierra* presumption does not apply to the Transmission Owners Agreement's purported right of first refusal provision because it is a prescription of general applicability rather than a negotiated rate provision, which new PJM Transmission Owners are required to accept as-is, with limited room for negotiation. Compliance Order PP 186-87, JA 68; Rehearing Order P 112, JA 153. "Amending the Transmission Owners Agreement requires action by a two-thirds majority of current PJM Transmission Owners (i.e., parties to the [Transmission Owners Agreement]), substantially inhibiting the ability of a new PJM Transmission Owner to negotiate a change to these provisions." Compliance Order P 187, JA 68 (citing Section 8.5.1 of the Consolidated Transmission Owners Agreement, attached to the TO Br. as Appendix 1, at 27). "As a result, new PJM Transmission Owners are placed in a position that differs fundamentally from that of parties who are able to negotiate freely like buyers and sellers entering into a typical power sales contract that would be entitled to a *Mobile-Sierra* presumption." *Id*.

Transmission Owners acknowledge that "as new parties sign on to the [Transmission Owners Agreement] they take on the terms of that contract." TO Rehearing Request, R.126 at 16, n.31, JA 104. In fact, the 2005 Consolidated

Transmission Owners Agreement, attached to the TO Br. as Appendix 1, provides that any transmission owner seeking to join PJM must become a Party to the Agreement. *See, e.g.*, 2005 Consolidated Transmission Owners Agreement section 3.1 (providing that any party transferring control of transmission facilities to PJM "shall become a Party to this Agreement") and section 6.1 ("PJM shall condition the transfer of functional control over an entity's Transmission Facilities to PJM on such entity becoming a Party to this Agreement."), TO Br. Appendix 1 at 7, 16.

These findings undermine Transmission Owners' claims that third parties joining the agreement are free to "try to bargain for different terms." TO Br. 41. Likewise, because the issue here is "the ability of a new PJM Transmission Owner to negotiate a change to these provisions," Compliance Order P 187, JA 68, *NRG*'s holding that *Mobile-Sierra* applies to non-party challenges to a *Mobile-Sierra* contract, *see* TO Br. at 42, is not relevant. Rehearing Order P 112, JA 153. There is no non-party challenge to the Transmission Owners Agreement at issue here. Rather, the issue is whether new parties to the Agreement are presented with an opportunity to negotiate or a take-it-or-leave-it proposition.

The negotiation among the original Transmission Owners, *see* TO Br. 42, does not undermine the Commission's conclusion. Although "published tariffs may have been determined initially by way of private negotiation," such rates are nonetheless tariff rates once they are published and generally applied. *Fla. E.*

Coast Ry. Co., 42 F.3d at 1130 n.5. *See also MCI Telecomm.*, 917 F.2d at 38 (recognizing that tariff rates may be "arrived at through negotiations between a carrier and an individual customer" and then made generally available to other customers).

Likewise, the fact that certain utilities executed separate owners' agreements (i.e., the PJM West and PJM South Transmission Owner Agreements, *see supra* p. 10-11), which are now consolidated into the Consolidated Transmission Owners Agreement, does not change the analysis. *See* TO Br. at 44. As Transmission Owners themselves state, while some provisions of the Transmission Owners Agreement were renegotiated for purposes of combining the three separate Transmission Owner Agreements into one Agreement, "the [right of first refusal] provisions have never been renegotiated." TO Rehearing Request, R. 126 at 16, n.31, JA 104. Further, the Consolidated Transmission Owners Agreement was executed in 2005, so, since that time, any transmission owner seeking to join PJM must join the Consolidated Agreement.

3. Transmission Owners' Purportedly Contrary Authority Does Not Support Applying *Mobile-Sierra* to Generally-Applicable Agreements.

On brief, Transmission Owners cite to decisions that they assert apply the *Mobile-Sierra* presumption of reasonableness to generally-applicable agreements. These arguments were not made to the Commission, and therefore the Commission

had no opportunity to respond to them. In any event, the cited authority does not support Transmission Owners' claims.

Transmission Owners assert that "[j]ust as FERC was bound by *Mobile-Sierra* to honor the filing provisions of the Owners Agreement at issue in *Atlantic City I*, it is bound to honor the transmission planning and construction provisions of the same agreement here." TO Br. 34 (citing *Atlantic City*, 295 F.3d at 10-11). Transmission Owners never argued to the Commission that *Atlantic City* held that *Mobile-Sierra* applied to the Transmission Owners Agreement; on rehearing they cited *Atlantic City* only for the proposition that "mere assertions that contract provisions are unreasonable and discriminatory are insufficient to justify involuntary contract modification." *See* TO Rehearing Request, R. 126 at 10, JA 98.

Atlantic City did not in any event find that *Mobile-Sierra* protected the filing provisions of the Transmission Owners Agreement. To the contrary, the Transmission Owners argued, and the Court agreed, that the Transmission Owners had *not* agreed by contract to cede their rights to make unilateral rate filings so *Mobile-Sierra* did not apply. *Atl. City*, 295 F.3d at 10-11. *See id*. at 10 ("As the Supreme Court stated in [*Memphis*, 358 U.S. at 113-14], the public utility, 'like the seller of an unregulated commodity, has the right . . . to change its rates . . . [at] will, unless it has undertaken by contract not to do so.'"). In contrast, *Atlantic City*

did find that *Mobile-Sierra* applied to a bilateral contract that was "negotiated at arms length." *Id*. at 14.

Indeed, this Court in *Me. Pub. Utils. Comm'n*, 454 F.3d at 284, rejected the argument that *Atlantic City* supported application of the *Mobile-Sierra* "public interest" standard to a transmission owners agreement in a regional transmission organization. This Court found that "the issue in *Atlantic City* was limited to the question of whether FERC had jurisdiction under either [Federal Power Act] Sections 203 or 205 to oblige public utilities to cede their rights to make future filings under Section 205." *Id*. "The [*Atlantic City*] court noted that the parties did not dispute FERC's authority to review their agreement at the outset, or to decide, based on evidence in the record, whether the entry and exit rights specified therein were just and reasonable within the meaning of Section 205." *Id*. at 284-85 (citing *Atl. City*, 295 F.3d at 12).

Transmission Owners also wrongly claim that the Commission's determination here is inconsistent with the Commission's treatment of bilateral rate agreements entered into under the umbrella Western Systems Power Pool Agreement, based on orders not cited to the Commission. *See* TO Br. 42-43 (citing *Puget Sound Energy, Inc. v. All Jurisdictional Sellers*, 137 FERC ¶ 61,001 (2011), *on reh'g*, 143 FERC ¶ 61,020 (2013), *appeal pending, People of the State of Cal. v. FERC*, No. 13-71276 (9th Cir.) (oral argument held June 16, 2015), and *Nev.*

Power Co. v. Enron Power Mktg., Inc., 103 FERC ¶ 61,353 (2003), *on reh'g*, 105 FERC ¶ 61,185 (2003), *rev'd on other grounds, Pub. Util. Dist. No. 1 of Snohomish Cnty. v. FERC*, 471 F.3d 1053 (9th Cir. 2006), *remanded on other grounds, Morgan Stanley*, 554 U.S. 527.

These decisions are entirely consistent with the Commission's decision here. Both *Puget Sound* and *Nevada Power* involved individual bilateral rate contracts entered into under the Western Systems Power Pool Agreement, which is an umbrella agreement establishing standardized terms for power transactions. *See Snohomish*, 471 F.3d at 1069; *Puget Sound*, 137 FERC ¶ 61,001 PP 18, 20. The terms of individual contracts entered into under that umbrella agreement are reflected in separate Confirmation Agreements establishing, *inter alia*, the price, volume, and duration of the contract -- contract terms that are particular to each contract, not standard terms under an umbrella agreement. *See Puget Sound Energy, Inc. v. All Jurisdictional Sellers*, 96 FERC ¶ 63,044 at 65,325 (2003). The Commission found *Mobile-Sierra* applicable to challenges to the rates established in those individualized, bilateral contracts. *See Nev. Power*, 105 FERC ¶ 61,185 P 28 (finding *Mobile-Sierra* applicable to individual Confirmation Agreements with a fixed price); *Puget Sound*, 137 FERC ¶ 61,001 P 18, *on reh'g*, 143 FERC ¶ 61,020 P 13 (finding *Mobile-Sierra* applicable to short-term bilateral rate contracts entered into under the Western Systems Power Pool Agreement).

In those cases, the Commission did *not* find *Mobile-Sierra* applicable to changes to the Western Systems Power Pool Agreement itself. To the contrary, *Puget Sound* expressly found that the Western Systems Power Pool Agreement itself is a generally applicable tariff, and changes to that Agreement properly are considered under the "ordinary" just and reasonable standard.[10] *See Puget Sound*, 143 FERC ¶ 61,020 P 15 & n.29 (distinguishing *W. Sys. Power Pool Inc.*, 129 FERC ¶ 61,055 (2009), applying the ordinary just and reasonable standard to its investigation of a rate cap in the Western Systems Power Pool Agreement because the rate cap was a generally-applicable tariff provision).

Likewise, Transmission Owners cited *Texaco Inc. v. FERC*, 148 F.3d 1091 (D.C. Cir. 1998), TO Br. 32-33, on rehearing only for the proposition that "absent language to the contrary, the *Mobile-Sierra* standard applies." TO Rehearing Request, R. 126 at 7 n.14, JA 95. Now on brief, Transmission Owners assert that *Texaco* applied the *Mobile-Sierra* presumption to "generally applicable" rates, i.e. "service agreements that incorporated rate schedules in a pipeline's tariff." *See* TO Br. 32-33 (citing *Texaco*, 148 F.3d at 1094; *Mojave Pipeline Co.*, 62 FERC ¶ 61,195 at 62,361 (1993)).

[10] *See Morgan Stanley*, 554 U.S. at 535 ("referring to the two differing applications of the just-and-reasonable standard as the 'ordinary' 'just and reasonable standard' and the 'public interest standard.'").

Texaco does not support any such proposition. Such a holding would run directly afoul of the Supreme Court's decision in *Memphis*, 358 U.S. at 115 & n.8, which held that *Mobile-Sierra* does not apply to "tariff and service" contracts that do not contain an individually-negotiated rate, but rather "refer to rate schedules of general applicability on file with the Commission."

Instead, the contracts at issue in *Texaco* and the Commission's *Mojave* order were individually-negotiated contracts between the Mojave pipeline and its initial shippers. The Mojave pipeline was certificated under the Commission's optional certificate procedures, which require a pipeline to assume the economic risks of the project, but permit the pipeline to share the risk with shippers through a negotiated reservation fee. *See Pac. Gas Transmission Co. v. FERC*, 998 F.2d 1303, 1306 n.1, 1307 (5th Cir. 1993) (describing optional certificate procedures applied to Mojave); *Mojave Pipeline*, 62 FERC ¶ 61,195 at 62,359 & n.2. Under its optional certificate, Mojave "individually negotiated rates with its firm shippers, subject to a Commission-mandated rate cap which is based on a Modified Fixed Variable rate design." *Mojave Pipeline*, 62 FERC ¶ 61,195 at 62,359. *See also, e.g., Pac. Gas*, 998 F.2d at 1307 (noting that Mojave negotiated reservation fees with its shippers within the parameters set out by the Commission); *Mojave Pipeline Co.*, 64 FERC ¶ 61,047 (1993) (Mojave's proposed reservation fee "was the result of arms-length negotiations between itself and its shippers"). It was the Commission's

modification of those "individually-negotiated rates" that was at issue in *Texaco*. *Mojave Pipeline*, 62 FERC ¶ 61,195 at 62,360. Specifically, the Commission "reassigned the risk of under use from Mojave to the shippers while leaving the contract otherwise intact." *Texaco*, 148 F.3d at 1095.

B. The Commission Reasonably Determined That The *Mobile-Sierra* Presumption Does Not Apply Because The Right of First Refusal Provision Did Not Result From Arm's-Length Bargaining.

Alternatively, the Commission also found that the *Mobile-Sierra* presumption does not apply to the Consolidated Transmission Owners Agreement provision that Transmission Owners contend includes a federal right of first refusal because that provision arose in circumstances that do not provide the assurance of reasonableness on which the *Mobile-Sierra* presumption rests. Compliance Order P 188, JA 68. Specifically, the Commission concluded that any purported right of first refusal provision would result from the Transmission Owners' common interest rather than from arm's-length bargaining. Compliance Order PP 189-90, JA 68-69; Rehearing Order PP 107-10, JA 152-53.

1. *Morgan Stanley* Requires That The *Mobile-Sierra* Presumption Apply to Contracts Negotiated At Arm's-Length.

While Transmission Owners claim that the arm's-length inquiry is a "newly minted exception to the *Mobile-Sierra* presumption," TO Br. 45, it is in fact required under *Morgan Stanley*. As *Morgan Stanley* held, the *Mobile-Sierra*

presumption rests on the premise "that contract rates are the product of fair, arms-length negotiations." *Morgan Stanley*, 554 U.S. at 554, cited Compliance Order P 188 n.340, JA 83. Since wholesale energy market buyers and sellers tend to be sophisticated businesses with equal bargaining power, the Supreme Court has explained, it can be expected that they will negotiate contracts containing just and reasonable rates, terms and conditions. *Id*. at 545 (citing *Verizon*, 535 U.S. at 479). *See also Me. Pub. Utils. Comm'n*, 625 F.3d at 759 ("A freely-negotiated contract rate, the Court held in *Morgan Stanley*, was presumptive evidence that the rate was just and reasonable because it reflected market forces."); *Atl. City*, 295 F.3d at 14 (finding *Mobile-Sierra* applied to a bilateral contract because it was "negotiated at arms length with Old Dominion and designed to provide both parties with long-term price certainty"); Compliance Order P 188 n.340, JA 83 ("Arm's-length bargaining serves an important role in confirming that the transaction price reflects fair market value.").

Transmission Owners claim that *Morgan Stanley* only recognizes an "exception" to *Mobile-Sierra* for contract formation defenses such as fraud and duress that "would render a contract invalid." TO Br. 46. *Morgan Stanley* certainly did not find that the *Mobile-Sierra* presumption applies to every contract unless it is found to be void *ab initio*; if a contract is *void ab initio* there is no contract and therefore no *Mobile-Sierra* issue to address. Rather, *Morgan Stanley*

addressed the circumstances under which "FERC should not apply the *Mobile-Sierra* presumption" in evaluating whether a contract rate is just and reasonable. *See* 554 U.S. at 547. *See also id.* at 554 (finding the *Mobile-Sierra* presumption "should not apply" where there is a causal connection between unlawful activity and the contract rate). The Court found that the Commission should not apply the *Mobile-Sierra* presumption where circumstances "'eliminate the premise on which the *Mobile-Sierra* presumption rests: that the contract rates are the product of fair, arms-length negotiations.'" Compliance Order P 188 & n.340, JA 68, 83 (quoting *Morgan Stanley*, 554 U.S. at 554). While certainly grounds for contract abrogation can undermine the assumption of fair, arm's-length negotiations, *see Morgan Stanley,* 554 U.S. at 547, so can other circumstances of contract formation, such as a contract provision agreed upon between parties with common interests to exclude competition.[11]

The contracts at issue in *Morgan Stanley* were of the same type at issue in *Mobile* and *Sierra* – bilateral power sales agreements between willing buyers and sellers who have obviously opposing "arm's-length" interests. *See* Compliance

[11] *Northeast Utils. Serv. Co. v. FERC*, 993 F.2d 937, 961-62 (1st Cir. 1993), TO Br. at 48 – which was not cited to the Commission – does not aid Transmission Owners. To the extent that decision can be read as rejecting consideration of arm's-length bargaining in the application of the *Mobile-Sierra* presumption, the decision of course pre-dated *Morgan Stanley*, which directed the Commission not to apply *Mobile-Sierra* where the premise for the presumption – fair, arm's-length bargaining – is absent. 554 U.S. at 554.

Order P 184, JA 67-68; *Morgan Stanley*, 554 U.S. at 532-33, 541. Likewise, the contracts at issue in the *Puget Sound* orders (which were not cited to the Commission), TO Br. 47-48, were also bilateral sales agreements between willing buyers and sellers. *See* pp. 46-48 *supra*. Under such circumstances, the Court required proof of seller behavior that "directly affects contract negotiations" to undermine the *Mobile-Sierra* premise of fair, arm's-length negotiations. 554 U.S. at 554. *See* TO Br. at 46-47.

Here, however, the Transmission Owners Agreement is far removed from the paradigmatic example of bilateral rate-setting contracts between willing buyers and sellers. The Agreement rather is "a complex agreement establishing a new regional structure impacting all market participants," as to which this Court has expressed doubt that *Mobile-Sierra* applies. *See Me. Pub. Utils. Comm'n*, 454 F.3d at 284. Presented with this issue of first impression, the Commission reasonably considered whether the type of contract provision at issue, a right of first refusal provision, fairly could be viewed as the product of arm's-length negotiation.

Likewise, while generally all provisions in bilateral sales contracts freely negotiated between willing buyers and sellers would come within the presumption. Compliance Order P 184, JA 67-68, "[g]iven the breadth and complexity of the [Consolidated Transmission Owners Agreement]," the Commission reasonably

concluded that "it is neither practical nor necessary to evaluate whether the preponderance of the [Consolidated Transmission Owners Agreement's] provisions include tariff rates or contract rates." *Id*. at P 185, JA 68. *See* TO Br. 53-56. Rather, the Commission found that "determining the standard of review that should apply to specific provisions of the [Consolidated Transmission Owners Agreement] is an appropriate way to recognize the distinctions among its provisions." *Id*.

This Court has recognized that the *Mobile-Sierra* presumption applies only when "there is no reason to question what occurred at the contract formation stage." *Town of Norwood v. FERC*, 587 F.2d 1306, 1312 (D.C. Cir. 1978). *See Me. Pub. Util. Comm'n*, 454 F.3d at 284; *Atl. City*, 295 F.3d at 14; *Potomac Elec. Power Co. v. FERC*, 210 F.3d 403, 409 (D.C. Cir. 2000) (all citing *Norwood* for this proposition). In *Norwood*, one transmission customer, the Town of Norwood, sought to obtain the benefit of a lower contractual rate provided to another customer, New England Power Company. The Commission determined that the New England Power Company contract was a *Mobile-Sierra* contract, and rejected Norwood's discrimination claim. *See id*. at 1311-12. The Court remanded the case to the Commission, based upon the Commission's failure to adequately consider "allegations which go to the fairness and good faith of the parties at the contract formation stage." *Id*. at 1313. "In particular, Norwood challenged the

very granting of the low rate to [New England Power Company] in the original contract. It asserts that the wheeling agreement was a 'sweetheart' deal negotiated at a time when the two companies were involved in merger discussions." *Id*. The Court found that where "there is some particular reason to depart from [the] preference [for protecting contracts that underlies *Mobile-Sierra*] -- as where there is evidence of some sort of collusive behavior among the contracting parties -- it may be more appropriate to conclude that the contractual customer has no entitlement to his fixed rate." *Id*. at 1314. *See also Cities of Bethany v. FERC*, 727 F.2d 1131, 1140 (D.C. Cir. 1984) (considering allegations that contract resulting in rate disparity was a "sweetheart" deal, implicating the fair conduct and good faith of the parties).

Here, the Commission found that Transmission Owners did not negotiate the Transmission Owners Agreement in bad faith. *See* TO Br. 57. That conclusion does not, however, answer the question of whether "in seeking to advance their interests, the parties are situated in relation to each other in a way that allows one to make a specific assumption about the results of their negotiations." Compliance Order P 189 n.341, JA 68, 83.

The Commission also reasonably concluded that arm's-length bargaining involves adversarial interests. Rehearing Order PP 107-08, JA 152-53 (citing cases); Compliance Order P 190 & nn.342-43, JA 68-69, 83-84 (citing

Commission precedent and regulation recognizing this point in market-based-rate/merger/affiliate contexts). The Commission concluded – based upon precedent – that arm's-length means "'adversarial negotiations between parties that are each pursuing independent interests.'" Rehearing Order P 107, JA 152 (quoting *Santomenno v. Transamerica Life Ins. Co.*, 2013 WL 603901 at *6 & n.3 (C.D. Cal. 2013)). Courts have characterized arm's-length transactions as transactions in which "'adversarial parties,'" i.e. '"business adversaries in the commercial sense,'" seek "'to further their own economic interests.'" *Id*. (quoting *A.T. Kearney, Inc. v. Int'l Business Machines Corp.*, 73 F.3d 238, 242 (9th Cir. 1995)). The "hallmark characteristics of arm's-length bargaining" are negotiations where parties "negotiated rigorously, selfishly and with adequate concern for price." *Id*. (quoting *Jeanes Hosp. v. Sec'y of Health and Human Servs.*, 448 Fed. Appx. 202, 206 (3d Cir. 2011)). In contrast, "[i]f the negotiating parties have a common economic interest in the outcome of the negotiations, they cannot bargain at arm's-length.'" *Id*. P 108, JA 152-53 (quoting *Nw. Central Pipeline Corp.*, 44 FERC ¶ 61,200 at 61,719 (1988)).

Thus, the Commission reasonably concluded that "arm's-length bargaining is a process in which each party pursues its individual interests, and a negotiation in which the parties pursue a single, common, and shared interest is thus inconsistent with such bargaining." *Id*. at P 109, JA 153. Transmission Owners

fault the authority relied upon by the Commission because it is not specific to the *Mobile-Sierra* context. *See* TO Br. 52. However, *Morgan Stanley* specifically identified the "arm's-length" nature of the negotiations as the premise for the *Mobile-Sierra* presumption of reasonableness. *See* 554 U.S. at 554. Nothing in *Morgan Stanley* suggests that it used the term "arm's-length" to mean anything exotic, specialized or contrary to its ordinary usage.

2. The Commission Reasonably Determined That The Purported Right Of First Refusal Provisions Did Not Result From Arm's-Length Negotiations.

The Commission reasonably concluded that the purported right of first refusal provision at issue here did not result from arm's-length negotiations. Compliance Order P 189, JA 68; Rehearing Order P 110, JA 153. "Unlike circumstances in which the Commission can presume that the resulting rate is the product of negotiations between parties with competing interests, the negotiation that led to the provisions at issue here were among parties with the same interest, namely, protecting themselves from competition in transmission development" by "delimit[ing], qualify[ing], or restrict[ing] the ability of any other potential competitor to engage in the subject activity." Compliance Order P 189, JA 68; Rehearing Order P 110, JA 153 (quoting Compliance Order P 186, JA 68). Thus, "[w]hile Indicated Transmission Owners may have engaged in extensive negotiations with respect to the Transmission Owners Agreement in general, their

common interest relating to the right of first refusal undermines any assurance of justness and reasonableness associated with arm's-length negotiations of the particular provisions at issue here." Rehearing Order P 110, JA 153. *See also* Compliance Order P 189, JA 68.

This distinguishes a right of first refusal provision from a requirements contract. TO Br. at 39-40. "There is a fundamental difference between an agreement where the parties agree to transact exclusively with each other and an agreement where the parties agree to prevent any other party from entering their line of business." Rehearing Order P 111, JA 153. Transmission Owners "fail to distinguish between contracts that are the product of competitive conditions, i.e. contracts that are freely negotiated at arm's-length, and contracts that by their terms seek to restrict competition by preventing entry into the market." *Id.*

While Transmission Owners assert that "PJM Transmission Owners are each independent entities with separate responsibilities to shareholders, customers and state regulators," TO Br. 56, they make no effort to demonstrate any divergence of interest with regard to preserving any rights of first refusal. *See*, *e.g.*, TO Br. 60 (arguing that a commonality of interest on rights of first refusal does not mean transmission owners are aligned on all issues). As the Commission observed, Transmission Owners themselves stated that, in the 1997 Agreement establishing PJM as an Independent System Operator, the Transmission Owners' "membership

within PJM was expressly made contingent upon the continuation of their pre-existing [rights of first refusal] being acknowledged and honored by PJM and all others." Rehearing Order P 102, JA 152 (citing TO Rehearing Request, R. 126 at 12, JA 100). *See also* TO Rehearing Request, R.126 at 11, JA 99 (noting that "Transmission Owners may have been united in invoking their [right of first refusal] rights").

Transmission Owners primarily argue that the purported right-of-first-refusal provisions were negotiated at arm's-length because PJM -- which was a signatory to the 2005 Consolidated Transmission Owners Agreement -- is independent from the Transmission Owners. TO Br. 49, 57-64. The Commission disagreed that, with respect to the right of first refusal provisions, PJM was seeking to "maximize its self-interest" so that its participation "constitute[d] the type of arm's-length bargaining that justifies a *Mobile-Sierra* presumption." Rehearing Order P 110 n.200, JA 153, 167. PJM is a nonprofit system operator, not a commercial entity with opposing economic self-interest. *See id*. *See also Morgan Stanley*, 554 U.S. at 536-37 (independent system operators are "not-for-profit entities that operate transmission facilities in a nondiscriminatory manner"); *NSTAR Elec. & Gas Corp. v. FERC*, 481 F.3d 794, 803 (D.C. Cir. 2007) (independent system operator has incentive to ensure grid stability and reliability). Indeed, PJM's participation in the 2005 Consolidated Transmission Owners Agreement is expressly limited to PJM's

own rights and commitments. *See* Consolidated Transmission Owners Agreement, attached to the TO Br. as Appendix 1, at 1 (providing that only the Transmission Owners are "Parties" to the Agreement and that the Agreement "is made by and between the Parties and PJM" "solely for the purpose of establishing the rights and commitments of PJM identified herein").

Further, the purported right of first refusal at issue pre-dated any participation by PJM in the Transmission Owners Agreement. *See* Compliance Order P 156, JA 62-63. As the Transmission Owners explain, the Transmission Owners' purported right of first refusal was carried forward from the 1997 Transmission Owners Agreement. *See* TO Rehearing Request, R. 126 at 12 & n.27, JA 100.[12] Subsequent to that 1997 Agreement, as Transmission Owners state, "the [right of first refusal] provisions have never been renegotiated." *Id*. at 16, n.31, JA 104.

Transmission Owners claim on brief that PJM was a party to the 1997 Transmission Owners Agreement. *See, e.g.*, TO Br. 6 (stating that the 1997 Transmission Owners Agreement was "among the PJM Transmission Owners and PJM"); *id*. at 23 (arguing that PJM had a role in the negotiations that led to the

[12] *See* 1997 Transmission Owners Agreement section 2.2.3 (predecessor to section 5.2 of the 2005 Consolidated Transmission Owners Agreement) and Article 7 (predecessor to section 4.2.1), R.126 (attachment to TO Rehearing Request) at 4, 12-13, JA 118, 126-27.

1997 Owners Agreement at issue in *Atlantic City*). This is not the case. As evidenced by the 1997 Agreement, PJM was not a party to the 1997 Transmission Owners Agreement. The Agreement was negotiated solely among the named transmission-owning "Parties." *See* the 1997 Transmission Owners Agreement, attached as an exhibit to the TO Rehearing Request, R. 126 (attachment) at 1, JA 115. Nor was PJM a party to the 1997 Transmission Owners Agreement when PJM was approved as a Regional Transmission Organization in 2002. *See* TO Br. 11. In fact, Transmission Owners and PJM's 2006 filing of the 2005 Consolidated Transmission Owners Agreement specifically stated that PJM was not a party to the 1997 Transmission Owners Agreement. *See* January 17, 2006 Filing of the 2005 Consolidated Transmission Owners Agreement at 2 n.1 ("PJM is not a party to the Transmission Owners Agreement [dated as of June 2, 1997], Rate Schedule FERC No. 29") (available in elibrary on ferc.gov at Accession No. 20060119-0193).

Moreover, the 1997 Agreement was before this Court in *Atlantic City*. *See* 295 F.3d at 6. Accordingly, this Court in that case did not "recognize[e] that the PJM Transmission Owners and PJM negotiated the Owners Agreement." TO Br. 57. Rather, the Court recognized that -- in attempting to revise the PJM tight power pool governance structure to qualify PJM as an Independent System Operator -- "[t]he PJM members had voluntarily proposed a sharing arrangement

on changes to rate design that attempted to balance the utility owners' rights and the ISO Board's independence." *Atl. City*, 295 F.3d at 6, 9. Thus, *Atlantic City* does not support the claim that the purported rights of first refusal in the Transmission Owners Agreement were the product of arm's-length bargaining between PJM and the Transmission Owners.

CONCLUSION

For the foregoing reasons, the Commission respectfully requests that the petitions for review be dismissed for lack of jurisdiction. If the Court proceeds to the merits, the orders on appeal should be upheld in all respects.

Respectfully submitted,

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December 4, 2015

American Transmission Systems, Inc. v. FERC,
Nos. 14-1085 and 14-1136 (consolidated)

CERTIFICATE OF COMPLIANCE WITH TYPE-VOLUME LIMITATION, TYPEFACE REQUIREMENTS, AND TYPE STYLE REQUIREMENTS

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this brief contains 13,923 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Word 2010 with 14-point, Times New Roman font.

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December 4, 2015

ADDENDUM

STATUTES

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Federal Power Act

for such purpose in such order, or otherwise in contravention of such order.

(d) Authorization of capitalization not to exceed amount paid

The Commission shall not authorize the capitalization of the right to be a corporation or of any franchise, permit, or contract for consolidation, merger, or lease in excess of the amount (exclusive of any tax or annual charge) actually paid as the consideration for such right, franchise, permit, or contract.

(e) Notes or drafts maturing less than one year after issuance

Subsection (a) of this section shall not apply to the issue or renewal of, or assumption of liability on, a note or draft maturing not more than one year after the date of such issue, renewal, or assumption of liability, and aggregating (together with all other then outstanding notes and drafts of a maturity of one year or less on which such public utility is primarily or secondarily liable) not more than 5 per centum of the par value of the other securities of the public utility then outstanding. In the case of securities having no par value, the par value for the purpose of this subsection shall be the fair market value as of the date of issue. Within ten days after any such issue, renewal, or assumption of liability, the public utility shall file with the Commission a certificate of notification, in such form as may be prescribed by the Commission, setting forth such matters as the Commission shall by regulation require.

(f) Public utility securities regulated by State not affected

The provisions of this section shall not extend to a public utility organized and operating in a State under the laws of which its security issues are regulated by a State commission.

(g) Guarantee or obligation on part of United States

Nothing in this section shall be construed to imply any guarantee or obligation on the part of the United States in respect of any securities to which the provisions of this section relate.

(h) Filing duplicate reports with the Securities and Exchange Commission

Any public utility whose security issues are approved by the Commission under this section may file with the Securities and Exchange Commission duplicate copies of reports filed with the Federal Power Commission in lieu of the reports, information, and documents required under sections 77g, 78*l*, and 78m of title 15.

(June 10, 1920, ch. 285, pt. II, § 204, as added Aug. 26, 1935, ch. 687, title II, § 213, 49 Stat. 850.)

TRANSFER OF FUNCTIONS

Executive and administrative functions of Securities and Exchange Commission, with certain exceptions, transferred to Chairman of such Commission, with authority vested in him to authorize their performance by any officer, employee, or administrative unit under his jurisdiction, by Reorg. Plan No. 10 of 1950, §§ 1, 2, eff. May 24, 1950, 15 F.R. 3175, 64 Stat. 1265, set out in the Appendix to Title 5, Government Organization and Employees.

§ 824d. Rates and charges; schedules; suspension of new rates; automatic adjustment clauses

(a) Just and reasonable rates

All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful

No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Schedules

Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Notice required for rate changes

Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Suspension of new rates; hearings; five-month period

Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and de-

Stat. 417 [31 U.S.C. 686, 686b])'' on authority of Pub. L. 97–258, §4(b), Sept. 13, 1982, 96 Stat. 1067, the first section of which enacted Title 31, Money and Finance.

§ 825*l*. Review of orders

(a) Application for rehearing; time periods; modification of order

Any person, electric utility, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this chapter to which such person, electric utility, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any entity unless such entity shall have made application to the Commission for a rehearing thereon. Until the record in a proceeding shall have been filed in a court of appeals, as provided in subsection (b) of this section, the Commission may at any time, upon reasonable notice and in such manner as it shall deem proper, modify or set aside, in whole or in part, any finding or order made or issued by it under the provisions of this chapter.

(b) Judicial review

Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the United States court of appeals for any circuit wherein the licensee or public utility to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of title 28.

(c) Stay of Commission's order

The filing of an application for rehearing under subsection (a) of this section shall not, unless specifically ordered by the Commission, operate as a stay of the Commission's order. The commencement of proceedings under subsection (b) of this section shall not, unless specifically ordered by the court, operate as a stay of the Commission's order.

(June 10, 1920, ch. 285, pt. III, §313, as added Aug. 26, 1935, ch. 687, title II, §213, 49 Stat. 860; amended June 25, 1948, ch. 646, §32(a), 62 Stat. 991; May 24, 1949, ch. 139, §127, 63 Stat. 107; Pub. L. 85–791, §16, Aug. 28, 1958, 72 Stat. 947; Pub. L. 109–58, title XII, §1284(c), Aug. 8, 2005, 119 Stat. 980.)

CODIFICATION

In subsec. (b), ''section 1254 of title 28'' substituted for ''sections 239 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 346 and 347)'' on authority of act June 25, 1948, ch. 646, 62 Stat. 869, the first section of which enacted Title 28, Judiciary and Judicial Procedure.

AMENDMENTS

2005—Subsec. (a). Pub. L. 109–58 inserted ''electric utility,'' after ''Any person,'' and ''to which such person,'' and substituted ''brought by any entity unless such entity'' for ''brought by any person unless such person''.

1958—Subsec. (a). Pub. L. 85–791, §16(a), inserted sentence to provide that Commission may modify or set aside findings or orders until record has been filed in court of appeals.

Subsec. (b). Pub. L. 85–791, §16(b), in second sentence, substituted ''transmitted by the clerk of the court to'' for ''served upon'', substituted ''file with the court'' for ''certify and file with the court a transcript of'', and inserted ''as provided in section 2112 of title 28'', and in third sentence, substituted ''jurisdiction, which upon the filing of the record with it shall be exclusive'' for ''exclusive jurisdiction''.

CHANGE OF NAME

Act June 25, 1948, eff. Sept. 1, 1948, as amended by act May 24, 1949, substituted ''court of appeals'' for ''circuit court of appeals''.

§ 825m. Enforcement provisions

(a) Enjoining and restraining violations

Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this

American Transmission Systems, et al. **Docket No. ER13-198, *et al.***
v. FERC
D.C. Cir. Nos. 14-1085 and 14-1136

CERTIFICATE OF SERVICE

In accordance with Fed. R. App. P. 25(d), and the Court's Administrative Order Regarding Electronic Case Filing, I hereby certify that I have, this 4th day of December 2015, served the foregoing upon the counsel listed in the Service Preference Report via email through the Court's CM/ECF system or via U.S. Mail, as indicated below:

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