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

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No. 91-1370

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INDIANA AND MICHIGAN MUNICIPAL
DISTRIBUTORS ASSOCIATION AND THE
CITY OF AUBURN, INDIANA,
PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT

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

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# BRIEF FOR RESPONDENT
# FEDERAL ENERGY REGULATORY COMMISSION

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## STATEMENT OF THE ISSUE

Whether the Commission reasonably concluded that a most favored nations clause in petitioners' service contract did not entitle petitioners to a rate moratorium.

## STATUTES AND REGULATIONS

All applicable statutes and regulations are attached to this brief in the Statutory Appendix.

**STATEMENT OF THE CASE**

Indiana Michigan Power Company (I&M) is engaged in the generation, transmission, distribution and sale of electric energy at retail, and at wholesale to rural electric cooperatives, municipalities, and other public utilities in Indiana and Michigan. Indiana Michigan Municipal Distributors Association (IMMDA) and the City of Auburn, Indiana (Auburn) (collectively, "Cities") are a group of municipal wholesale customers of I&M who receive full requirements service under I&M's FERC Tariff MRS, and are seeking a moratorium against a rate increase filed by I&M in March 1990. Wabash Valley Power Association, Inc. (WVPA) is a rural electric cooperative, which initially received full requirements service under I&M's FERC Tariff REC-1, but later restructured its service to become a partial requirements customer.

Cities' claim here is that the restructuring of WVPA's service triggered a "most favored nations" clause in a 1988 Cities/I&M settlement agreement which, they allege, requires I&M to grant Cities a rate moratorium until August 1992. For that reason, Cities in this case are challenging two Commission orders which have declined to impose any such rate moratorium requirement on I&M. These orders are: 1) Indiana Michigan Power Company, "Order Accepting and Suspending Proposed Rates, Noting and Granting Interventions, Denying Motions to Reject, Dismissing Requests to Institute Complaint Proceedings Under Section 206 of the Federal Power Act, Denying Motions For Summary Disposition,

Consolidating Dockets, and Establishing Hearing Procedures," 51 FERC ¶ 61,191 (May 18, 1990); and 2) Indiana Michigan Power Company and Indiana and Michigan Municipal Distributors Association, et al. v. Indiana Michigan Power Company, "Order Denying Rehearing," 56 FERC ¶ 61,019 (1991).

## STATEMENT OF THE FACTS

### A. Background: The 1987 I&M Rate Proceedings

The most favored nations clause at issue in this proceeding had its genesis in Commission rate proceedings that were commenced in October 1987. On October 15, 1987, I&M filed with the Commission separate rate increases for each of its five affected customer classes. 1/ Various I&M wholesale customers, including Cities and WVPA, intervened and filed protests against these proposed increases. On December 15, 1987, the Commission issued an order in which it accepted I&M's proposed rates for filing, set them for a hearing to determine whether they were excessive, and suspended them, allowing them to become effective December 22, 1987, subject to refund. See IMMDA and City of

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1/ Docket No. ER88-30-000 affected Michigan Power Company (MPCO). Docket No. ER88-31-000 affected Richmond Power and Light Company. Docket No. ER88-32-000 affected the Cities of Anderson and Frankton, Indiana, members of the Indiana Municipal Power Agency. The rate increase proceeding affecting Cities was assigned Docket No. ER88-33-000. Another proceeding, docketed as ER88-34-000, affected WVPA and one other rural electric cooperative customer, Wayne County (REMC).

Auburn v. Indiana Michigan Power Company, 41 FERC ¶ 61,310 (1987). 2/

**1. I&M's Settlement With WVPA In Docket No. ER88-34-000**

Even before I&M had filed for these rate increases (as early as July 2, 1987), WVPA notified I&M that it intended to cease purchasing power from I&M, effective August 1, 1988. (R. 1950, J.A. 69.) On August 31, 1988, I&M and WVPA reached a proposed settlement resolving all issues raised by WVPA's protest in Docket No. ER88-34-000.

Under the proposed settlement, WVPA would continue, until July 31, 1989, to receive full requirements service from I&M under the latter's increased rate levels that became effective December 22, 1987, in Docket No. ER88-34-000. (R. 1952; J.A. 71.) This settlement also provided that for the period August 1, 1989 through December 31, 1997, the service between I&M and WVPA would be completely restructured so that WVPA, instead of remaining a full requirements customer of I&M, would receive a defined block of power and associated energy (50 megawatts (MW)) at a rate that was virtually fixed for the remaining 8.4 year duration of the

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2/ Some months earlier, on October 2, 1987, Cities had filed a complaint with the Commission (docketed as No. EL88-1-000) alleging that I&M had unlawfully overcharged its wholesale ratepayers for coal (and related transportation costs) used as fuel for the generation of electric power. The December 15 order also consolidated this complaint proceeding, Docket No. EL88-1-000, with all of the October 15 rate cases. See note 1, supra.

new contract. (R. 1953; J.A. 72.) 3/ Although fixed, the rate for demand charges was subject to adjustment "every three years beginning August 1, 1992 based on 33% of the average annual percentage change" in the Producer Price Index (PPI) for the prior three years. Id. 4/

As part of the restructured service, I&M and WVPA also agreed that, for the same 8.4 year period, I&M would provide WVPA firm transmission service ("wheeling") enabling WVPA to import power generated by non-I&M facilities and to have that power redelivered to designated WVPA delivery points. (R. 1955-57;

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3/ The I&M/WVPA settlement agreement stated:

> Except for the rates for Firm power service and transmission service . . . , nothing contained herein shall be construed as affecting in any way the right of the party furnishing service under this rate schedule to unilaterally make application to the FERC for a change in rates or conditions for service under section 205 of the Federal Power Act and pursuant to the Commission's rules and regulations promulgated thereunder.

(R. 1971; J.A. 90.)(Emphasis added.)

4/ The level of variable (energy and customer) charges for WVPA's restructured service was also substantially controlled by the settlement. WVPA agreed to pay only those "energy and customer charges contained in Tariff REC-1 in effect at the time that the service commences . . . subject to fuel adjustment." (R. 1952; J.A. 71.) The settlement agreement further provided that "[i]f REC-1 is superseded by a new tariff which replaces REC-1, I&M can make adjustments to energy charges to reflect only changes to the fuel base and line losses." Id.

J.A. 74-76.) The parties agreed that WVPA would pay a fixed rate per/kw for this wheeling service. (R. 1958, J.A. 77.) 5/

**2. I&M's Settlement With Cities In Docket No. ER88-33-000**

On September 8, 1988, I&M also reached a proposed settlement with Cities (Docket No. ER88-33-000; R. 1833, J.A. 10) Unlike WVPA, Cities remained full requirements customers of I&M. The settlement package provided for a two-phased rate decrease for Cities. The first decrease was effective during the period from December 22, 1987 through December 31, 1988, 6/ and reduced I&M's revenues by approximately $1.7 million. I&M's rates to Cities were again reduced on January 1, 1989, effectively decreasing I&M's revenues by another $1 million.

This proposed settlement also included a rate moratorium for up to fifteen months: the reduced rates would remain in effect

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5/ The 1988 I&M/WVPA settlement agreement expressly provided that when the new, firm, defined-block power service and the firm transmission service became effective:

> I&M will terminate full requirements service to WVPA under I&M Tariff REC-1 and I&M will no longer be obligated to supply WVPA's members full power and energy requirements. Should WVPA desire full requirements service in the future, WVPA must provide I&M with five years' written notice.

If such notice was given, the agreement specified that the parties would then enter into negotiations to determine whether I&M will provide such new full requirements service. (R. 1967; J.A. 86.)

6/ Cities received a special lump sum refund for the period between December 22, 1987 through September 8, 1988, for the amounts already paid I&M in excess of the new settlement rate. (R. 1846, J.A. 23.)

until January 1, 1990, or until the in-service date of the Rockport Unit No. 2 generating plant, 7/ whichever first occurred. (R. 1835, J.A. 12.) The settlement agreement also included a most favored nations clause, which provided, as relevant here:

> if I&M negotiates a settlement in any of its remaining consolidated rate dockets on terms that are more favorable to the customers affected by those dockets than the terms of this agreement, I&M will amend this Agreement to provide to Cities the effect of the more favorable terms.

(R. 1841, J.A. 18.) 8/

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7/ Rockport No. 2 is a new coal-fired 1300 MW generating unit, that was then half-owned by I&M, and was then scheduled to commence operations in the last quarter of 1989. See American Electric Power Service Corp., 49 FERC ¶ 61,377 at p. 62,376 n.1 (1989).

8/ The most favored nations clause went on to state:

> For purposes of this paragraph, Cities have reviewed the Settlement Agreement filed in Docket No. ER88-30-000 between I&M and Michigan Power Company (MPCO) and agree that the settlement does not contain any terms more favorable to MPCO than the terms of this settlement are to Cities. Any settlement Agreement in Docket Nos. ER88-31-000, ER88-32-000 or ER88-34-000 which is consistent with this settlement and the settlement in Docket No. ER 88-30-000 also will be deemed to not contain terms more favorable than the terms of this settlement.

(R. 1841, J.A. 18.)

The Commission accepted I&M's proposed settlements with WVPA and Cities by Letter Order issued December 1, 1988. See American Electric Power Service Corp., 45 FERC ¶ 61,501 (1988). 9/

**B. The Proceedings Before The Commission**

On March 21, 1990, I&M commenced the proceedings in this case by filing proposed rate increases for Cities and its other wholesale customer classes. 10/ On April 11, 1990, Cities intervened and filed a protest and a motion to reject I&M's new rate filing. In these pleadings, Cities characterized the I&M's 1988 settlement with WVPA as providing for a rate moratorium until August 1992. Cities argued that the most favored nations clause in its 1988 settlement entitled it to the same "rate moratorium" extended to WVPA.

**1. The Commission's May 18, 1990 Order Denying Cities' Rate Moratorium Claim**

On May 18, 1990, the Commission issued an order in which it set I&M's newly proposed rates for hearing, and suspended them

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9/ The I&M/Cities' settlement also disposed of Cities' complaint filed against I&M in Docket No. EL88-1-000. See note 2, supra.

10/ These proposed rate increases applied to the same five customer classes affected by I&M's October 1987 rate filing, and, at least initially, became the subject of five separate rate cases: Docket No. ER90-269-000 (Michigan Power Company; Docket No. ER90-270-000 (Richmond Power and Light Company); Docket No. ER90-271-000 (Indiana Michigan Power Agency); Docket No. ER90-272-000 (Cities); and ER90-273-000 (Wayne County). These cases were consolidated in the Commission's May 18, 1990 order (discussed infra).

These proposed rate increases did not, however, apply to WVPA, which, as explained above, was subject to a long-term fixed rate contract with I&M.

for five months; this allowed the rates to become effective on October 21, 1990, subject to refund. At the same time, the May 18 order summarily denied Cities' request that they be granted a rate moratorium until August 1992.

The Commission found that although Cities and WVPA had once been similarly situated full requirements customers, WVPA's 1988 arrangement with I&M completely restructured WVPA's service. 51 FERC at p. 61,523 and n.11; R. 1649, J.A. 2 and n.11. Under the restructured service, the Commission found, WVPA would be receiving a limited amount of power, with fixed demand charges that were subject only to triennial adjustments. Id. Rejecting Cities' characterization of this triennial adjustment mechanism as a "rate moratorium," the Commission stated:

> The most favored nations clause in Cities' settlement with Indiana Michigan, however, does not permit them to equate a formulary adjustment (pegged to an external index) to a rate for a totally different service with a rate moratorium on their full requirements rate.

51 FERC at p. 61,523 (R. 1649-50, J.A. 2)(footnotes omitted).

The Commission also found that the most favored nations clause was not operable here because Cities showed no interest in receiving a restructured form of service similar to WVPA's:

> Cities' [most favored nations clause] argument would be relevant if they were seeking a similar major change in their service package with Indiana Michigan along with similar terms relating to the scheduling of rate modifications. Instead, Cities focus on but one aspect of the Indiana Michigan-Wabash Valley settlement agreement -- that the first formulary adjustment to the demand charge for a block of firm power occurs on

> August 1,1992 -- and argue that it constitutes a more favorable term to which Cities are entitled in the form of a moratorium for their full requirements rate.

51 FERC at p. 61,523 n.13 (R. 1650, J.A. 2 n.13.)

**2. Cities' Request For Rehearing**

On June 15, 1990, Cities filed a request for rehearing of the Commission's May 18 order. 11/ Specifically, Cities argued that, as a general rule, settlement agreements are enforceable under the Sierra-Mobile doctrine, 12/ and thus the most favored nations clause was part of an enforceable agreement. Cities maintained that the Commission erred in refusing to enforce WVPA's "rate moratorium," which, they claimed, was made applicable to Cities by virtue of the most favored nations clause in their 1988 settlement with I&M.

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11/ Shortly after filing their rehearing request, Cities filed a complaint against I&M, docketed EL90-37-000, in which they raised most of the same issues that were raised in their protest. This filing was in apparent response to a separate ruling in the Commission's May 18, 1990 order that the relief Cities were seeking in their protest must be made the subject of a separate complaint. This complaint was later settled and is not germane to this appeal.

12/ FPC v. Sierra Pacific Power Co., 350 U.S. 348 (1956); United Gas Pipe Line Co. v. Mobile Gas Service Corp., 350 U.S. 332 (1956). Collectively, Sierra and Mobile stand for the proposition that, where electric utilities have contractually committed themselves to a fixed rate (and thus have surrendered the right to file rate changes to reflect changing costs), unilateral rate filings purporting to change the rates are a nullity unless an increase in the rate is required in order to serve the public interest.

Cities further argued that their 1988 settlement with I&M specifically contemplated that its terms would be compared with any other settlement reached in the other consolidated rate cases (see note 1, supra), including the I&M/WVPA settlement. (R. 1677, J.A. 134.) But, other than attempting to equate the triennial adjustment mechanism in WVPA's rate to a rate moratorium, Cities did not attempt to make any direct comparison between their settlement and WVPA's 1988 settlement. Rather, they undertook a comparison of rate levels and demand charges between WVPA's settlement and a third settlement involving Wayne County, a company in the same customer class (Docket No. ER88-34-000) in which WVPA had previously been situated. 13/

While their rehearing request was pending, all parties to I&M's 1990 rate proceedings, including Cities, reached a settlement which resolved virtually all issues. 14/ The only issue reserved by the 1990 settlement was Cities' claim that they

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13/ In comparing the WVPA and Wayne County settlements, Cities maintained that as a result of a reduction in firm power sold to WVPA due to its restructured service, WVPA's rates would contribute less to I&M's recovery of certain deferred costs associated with the Rockport No. 2 plant than Wayne County's rates. (R. 1683-85; J.A. 140-142.) Furthermore, Cities asserted that their comparison of WVPA's rate levels with Wayne County's rate levels over a period of time suggested an overall lower rate for WVPA. (R. 1683; J.A. 140.). This allegedly translated into a higher rate for Cities, given Cities' assertion that it was "undisputed" that there was "parity" between its settlement and Wayne County's settlement. (R. 1682, J.A. 139.)

14/ The Commission approved this settlement by letter order issued June 18, 1991. American Electric Power Service Corp., 55 FERC ¶ 61,502 (1991).

were entitled to a rate moratorium lasting until August 1992. 15/

### 3. The Commission's July 2, 1991 Order On Rehearing

On July 2, 1991, the Commission issued an order denying Cities' rehearing request. Initially, the Commission recognized that Cities' 1988 settlement containing the most favored nations clause is a legally enforceable agreement. The Commission again concluded, however, that the triennial adjustment mechanism in WVPA's demand charge "was not the equivalent of a rate moratorium for the service that I&M provides Cities." 56 FERC at p. 61,082.

In addition, the Commission reached the same conclusion on rehearing that the most favored nations clause did not authorize Cities to isolate and demand only favorable provisions from completely restructured settlements, without also taking less desirable provisions:

> Cities' attempt to enforce the most favored nations clause in this case results in an attempt to pick and choose among component parts of the I&M/Wabash settlement agreement, and, in fact, to pick and choose just a single element of the rate agreed to in the I&M/Wabash settlement. If Cities want the

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15/ As relevant here, Paragraph 1 of this settlement agreement provided:

> No issues are reserved for decision, with the exception of the ultimate resolution, by Commission order or by appeal from such order, of the issue of whether the "Most Favored Nations" clause in the settlement of Docket Nos. ER88-33-000 and EL-88-1-000 [the complaint docket] is applicable to [the instant proceeding] . . . .

(R. 2093, J.A. 148.)

> benefit of one element of the rate in the Wabash settlement agreement, they must be ready to accept the entire rate, and that they are apparently unwilling to do.

56 FERC at p. 61,083. (R. 1818, J.A. 9.)(Footnote omitted.)

Moreover, the Commission reiterated its view that in order to avail themselves here of the most favored nations clause in their 1988 settlement agreement Cities must, at a minimum, be willing to accept a similarly restructured settlement package:

> As we stated in our original order, if Cities were arguing that they desired similar service and similar rates, with a rate that includes a demand charge with an every three-years formulary adjustment, Cities' argument would have been more compelling. However, the services provided and the rate charged are dissimilar, i.e., Wabash takes a defined block of power and associated energy at a rate with a fixed demand charge with an every-three years formulary adjustment, while Cities take requirements service at a traditional stated rate subject to I&M filing for an increase to reflect changing costs.

Id. (Footnotes omitted.)

The Commission also questioned the relevance of Cities' claims that the rates charged WVPA may be less than their own rates, and may produce a smaller recovery of certain deferred costs associated with the Rockport plant than other customers' rates. 56 FERC at p. 61,083. (R. 1819-20; J.A. 9.) Initially, the Commission noted that the claims as to the relative rate levels did not contradict the Commission's findings that WVPA's underlying service was very different from the underlying service that Cities received, and did not respond to the question of

whether I&M/WVPA settlement contained a rate moratorium. Id. (R. 1820, J.A. 9.)

Second, the Commission pointed out that Cities cannot now be heard to complain about its rate level or about deferred cost recovery issues since Cities had settled all issues as to rates, other than the issue whether I&M and WVPA agreed to a rate moratorium. Id. Finally, the Commission concluded that Cities cannot be heard to complain that its rates may now be higher than WVPA's rates because:

> Cities are not asking for the same service Wabash receives or to be charged the same rates that Wabash is being charged, but rather Cities are only asking that they be granted a rate moratorium until August 1992.

Id.

This appeal followed.

## SUMMARY OF ARGUMENT

The Commission's interpretations of the I&M/WVPA settlement and of the most favored nations clause in the I&M/Cities settlement agreement are entitled to substantial deference, if found to be reasonable. The Commission reasonably concluded that Cities were not entitled to an August 1992 rate moratorium (on the basis of their most favored nations clause) because there was no August 1992 rate moratorium contained in the I&M/WVPA settlement. The triennial formulary rate adjustment clause in the I&M/WVPA settlement was not a rate moratorium; it was part of a fixed rate agreement (that lasts until December 1997) that only authorized periodic adjustments in the rate.

The Commission also reasonably concluded that Cities' most favored nations clause did not authorize them to pick and choose among components parts of a rate for a completely restructured service. The record establishes that WVPA was no longer receiving comparable service from I&M, and Cities were not interested in receiving a restructured form of service similar to WVPA's.

The Commission also properly declined to undertake a comparison of the overall rate levels in the I&M/WVPA and I&M/Cities settlements. It is self-evident from Cities' lack of interest in WVPA's service as a whole that WVPA's overall rate level, coupled the other terms and conditions of WVPA's new service, are not "more favorable terms" within the meaning of Cities' most favored nations clause.

Contrary to Cities' assertions, the Commission did not determine that the Sierra-Mobile doctrine was inapplicable here. It did not rule out the possibility of enforcing the most favored nations clause if Cities had been interested in a restructured form of service similar to WVPA's. The Commission's conclusion that Cities were not authorized to take only the favorable terms of WVPA's rates, without accepting the less favorable terms of WVPA's new service, was supported by the wording of Cities' most favored nations clause. Finally, the Commission's orders will encourage settlements by promoting precision in drafting settlement agreements, and by preserving stability and innovation in the settlement process.

## ARGUMENT

### I. THE COMMISSION REASONABLY CONCLUDED THAT I&M'S RESTRUCTURED SERVICE WITH WVPA DID NOT TRIGGER CITIES' MOST FAVORED NATIONS CLAUSE IN A MANNER THAT ENTITLED CITIES TO A RATE MORATORIUM

#### A. A Reasonable Commission Interpretation Of The I&M/WVPA Settlement And The Most Favored Nations Clause In The I&M/CITIES Settlement Is Entitled To Deference

The rulings below involve Commission interpretations of the I&M/WVPA settlement agreement and of the most favored nations clause in the I&M/Cities settlement, and, if reasonable, those interpretations are entitled to substantial deference from this Court. Although, in the past, interpretations of most favored nations clauses by the Federal Power Commission (the Commission's predecessor) were subject to de novo review by the courts, see e.g., Texas Gas Transmission Corp. v. Shell Oil Co., 363 U.S. 263, 268-70 (1960) (Texas Gas); Warren Petroleum Corp. v. FPC, 282 F.2d 312, 315 (10th Cir. 1960), this is no longer the case. In National Fuel Gas Supply v. FERC, 811 F.2d 1563 (D.C. Cir. 1987)(National Fuel), this Court interpreted the U.S. Supreme Court's opinion in Chevron 16/ as modifying "earlier cases that adhered to the traditional rule of withholding deference on

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16/ Chevron U.S.A., Inc. v. Natural Resources Defense Council, 467 U.S. 837 (1984).

questions of contract interpretation," and specifically discussed Texas Gas as one of the cases modified by Chevron. Id. at 1570.

In National Fuel, this Court went on to state:

> We think that the better view, particularly in light of Chevron, is that deference [to an agency's interpretation of a settlement] should be given because the congressional grant of authority to the agency indicates that the agency's interpretation typically will be enhanced by technical knowledge. Construction of a settlement will be influenced by the agency's expertise in the technical language of that field and by its greater knowledge of industry conditions and practices, including its more comprehensive experience with the kinds of disputes and negotiations that generally produce such an agreement.

Id. Accord, Transcontinental Gas Pipe Line Corp. v. FERC, 922 F.2d 865, 869 (D.C. Cir. 1991); Duke Power Company v. FERC, 864 F.2d 823, 826-27 (D.C. Cir. 1989); Vermont Dept. of Public Service v. FERC, 817 F.2d 127, 135 (D.C. Cir. 1987).

As this Court further recognized, "particularly with regard to issues of contractual interpretation pertaining to the application of the Sierra[-Mobile] doctrine," it is proper to defer to the Commission's expertise if its decision is supported both factually and legally." Kansas Cities v. FERC, 723 F.2d 82, 87 (D.C. Cir. 1983) (citations omitted). Finally, this Court has also observed that courts owe deference to the Commission's reasonable interpretations of ambiguous language in agreements filed with the Commission. See Cajun Electric Power Cooperative, Inc. v. FERC, 924 F.2d 1132, 1135 (D.C. Cir. 1991).

## B. The Commission Reasonably Concluded That I&M's Agreement With WVPA Did Not Contain A Rate Moratorium Which Was Available To Cities Under The Most Favored Nations Clause Of Their Agreement With I&M

### 1. The terms of the restructured agreement between WVPA and I&M did not amount to a rate moratorium

In light of the principles outlined above, this Court should find that the Commission reasonably concluded on the basis of the record before it that Cities are not entitled to a rate moratorium lasting until August 1992. Thus, in the orders below, the Commission correctly concluded that the triennial formulary rate adjustment mechanism in WVPA's settlement agreement was not the equivalent of a rate moratorium. A rate moratorium is typically characterized by an express promise by a power supplier made in the course of a settlement that, for a limited period of time, it will temporarily forego its right to make unilateral rate filings under section 205 of the Federal Power Act. See e.g., Carolina Power & Light Company, Opinion No. 717, 52 F.P.C. 1841 (1974). Once the rate moratorium period ends (and absent any other contractual restriction), the power supplier is free to file for rate increases with the Commission to reflect changing costs, without its customers' consent.

The triennial adjustment feature in WVPA's service agreement can in no sense be characterized as a rate moratorium. Rather, it is quite clearly a periodic adjustment mechanism, analogous to a periodic fuel adjustment clause, that is an inseparable component of WVPA's long-term, fixed-rate contract. Cf. Elec. and Water Plant Board, Frankfort, Ky., et al. v.

Kentucky Utilities Company, 55 FPC 2035, 2046-47 (1976), aff'd, 569 F.2d 159 (D.C. Cir. 1977) (formulary fuel adjustment clause considered an inseparable, integral part of fixed rate contract which cannot be modified unless the total rate is excessive).

Moreover, the triennial formulary rate adjustment feature of WVPA's rate cannot be considered a true rate moratorium because it does not "expire" in August 1992. At that time, I&M will not be free to unilaterally increase WVPA's rates subject to Commission review under the "just and reasonable" standard of Section 205(d) of the FPA. Rather, WVPA's demand charge remains fixed until expiration of the long-term contract, or until December 31, 1997, subject only to adjustment of the demand charge every three years to track a percentage change in the PPI. Accordingly, even if Cities were authorized to pick and choose among "favorable terms" in the I&M/WVPA settlement, there is no "rate moratorium" in that settlement available to Cities.

### 2. Petitioners were in any event not entitled to a rate moratorium because the Commission reasonably concluded that their most favored nations clause did not authorize Cities to "pick and choose" among provisions of the I&M/WVPA agreement

As noted, the Commission concluded that Cities' most favored nations clause did not authorize Cities to "pick and choose among component parts of the I&M/Wabash settlement agreement" or "to pick and choose just a single element of the rate" agreed to in that settlement. (R. 1818; J.A. 9.) This was a reasonable interpretation of the most favored nation clause given that it is beyond dispute that Cities and WVPA were no longer receiving

comparable service from I&M, and Cities were not interested in receiving a restructured form of service similar to WVPA's.

Before I&M and WVPA reached a settlement in August 1988, WVPA and Cities were similarly situated wholesale customers insofar as both were full requirements customers whose rates were not fixed, but were subject to modification under section 205 of the FPA to reflect I&M's changing costs. Upon WVPA's restructuring, however, Cities and WVPA were no longer similarly situated. Rather, unlike Cities, WVPA became a partial requirements customer, entitled only to a limited quantity of power (50MW), as well as expanded firm transmission service, from I&M for the remaining 8.4 years at a fixed rate, 17/ while Cities remained a full requirements customer with no limits on their period of service and with rates subject to modification.

As the Commission has recognized in other cases, full and partial requirements customers are not similarly situated. See Central Power and Light Company, Opinion No. 326, 47 FERC ¶ 61,339 (1989)(CP&L); Boston Edison Company, Opinion No. 809-A, 1 FERC ¶ 61,229 (1977). In CP&L, the Commission found (based on expert testimony) that full requirements customers are not subject to any contract demand limitations--they receive all their energy needs from the same supplier. Their loads are reasonably predictable. And the supplier is responsible for predicting load growth of full requirements customers, as well as

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17/ At the end of this period, WVPA does not automatically revert to full requirements customer status. See note 5, supra.

for planning the acquisition of new generating capacity to meet that growth. Id. at 62,166.

On the other hand, partial requirements customers exercise "autonomy in power supply planning and operations because they can currently supply some or all of their own energy needs" through alternative sources. Id. In addition, partial requirements customers have less predictable load patterns that justify different cost allocation methods for full and partial requirements customers. Id. 18/

Had Cities and WVPA remained in a comparable position with respect to service, a side-by-side comparative approach of individual terms (e.g., the "term" approach advocated by Cities in their brief (Pet. Br. 20)) might have been possible. As the Commission's orders effectively recognize, however, the "term" approach became impossible once WVPA completely restructured its service. As the Commission correctly determined, if Cities wished to exercise its most favored nations clause to obtain any specific benefit extended to WVPA, it was incumbent upon Cities to seek a restructured form of service similar to WVPA's new service. Because Cities has shown no interest in the WVPA settlement package as a whole, the Commission acted well within its discretion in declining to apply Cities' most favored nations clause to grant Cities a rate moratorium to coincide with WVPA's

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18/ See also Boston Edison Company, Opinion No. 809-A, 1 FERC ¶ 61,229 (1977), at p. 61,592 ("[L]oad characteristics of a partial requirements service may be quite different from the characteristics of full requirements service . . . .").

first triennial rate adjustment. In short, the Commission had no obligation to treat "apples" as "oranges."

The Commission also properly declined to undertake a comparison of the overall rate levels in the I&M/WVPA and the I&M/Cities settlements. It was unnecessary for the Commission to engage in any overall rate level comparison between Cities and WVPA: Cities' lack of interest in WVPA's new service as a whole was itself an admission that WVPA's overall rate level, coupled with other terms and conditions of WVPA's restructured service, were not "more favorable terms" for the purpose of Cities' most favored nations clause.

Furthermore, Cities are not raising any claims that their current rate levels are excessive, or that I&M's rates are unduly discriminatory. In their request for Commission rehearing (filed before Cities settled all issues as to rates), Cities conceded that

> [i]f the IMMDA/Auburn Settlement was not in existence and this proceeding arose under a discrimination claim by IMMDA and Auburn under Section 205(b) of the FPA, a Commission decision could be defended which held that a comparison of the rates, terms, and conditions of the service of IMMDA/Auburn and WVPA was not appropriate due to the "restructuring" of the WVPA service. This is not, however, a Section 205(b) discrimination case . . . . (R. 1679 n.9; J.A. 136 n.9.) (Emphasis added.) 19/

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19/ In any event, as noted (see note 13, supra), Cities have attempted only a vague and indirect comparison of their rate level with WVPA's rates by comparing the demand charges of WVPA and Wayne County, and by asserting that Cities' rates were in "parity" with Wayne County's rates. (R. 1682, (continued...)

As the Commission correctly observed (56 FERC at p. 61,083), Cities ultimately settled all issues in this case relating to rate levels, and a comparison of rate levels has little to do with whether WVPA has been granted a rate moratorium lasting until August 1992.

## II. PETITIONERS' CLAIMS TO THE CONTRARY LACK MERIT

A. In their brief, Cities make a number of assertions, all of which are insubstantial. Initially, they argue (Pet. Br. 14-15) that the Commission failed to apply the Sierra-Mobile doctrine requiring enforcement of Cities' most favored nations clause. But the Commission did not quarrel with the notion that Sierra-Mobile would require enforcement of Cities' most favored nations clause under appropriate circumstances. 20/ Instead, the Commission's refusal to grant Cities a rate moratorium was based on its interpretation of the I&M/WVPA settlement, and the absence of any rate moratorium in that settlement. See 56 FERC at p. 61,082 ("every-three-years formulary adjustment to the

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19/(...continued)
J.A. 139.) Because of Cities' concession that this is not a discrimination case, the relevance of these comparisons is unclear. In any event, Cities has failed to explain how even a disparity in rate levels would translate into a rate moratorium until August 1992. The Commission properly concluded that if Cities desire WVPA's rate level, they must seek a similarly restructured service package.

20/ As Cities acknowledge (Pet. Br. 14), the Commission specifically found that the I&M/Cities settlement agreement contained a most favored nations clause, and was a legally enforceable agreement. 56 FERC at p. 61,082.

demand charge for the service I&M provides Wabash was not the equivalent of a rate moratorium . . . .").

B. Second, Cities make much of the fact that the I&M/WVPA settlement was executed eight days before the I&M/Cities settlement was executed, and therefore, they argue (Pet. Br. 17) that the Commission erred in concluding that WVPA's restructuring rendered their most favored nations clause inapplicable to the WVPA settlement. However, the sequence in which the two settlements were reached is entirely irrelevant to this case because the Commission's orders do not hold that Cities' most favored nations clause is inapplicable to WVPA's settlement as a whole. That is, the Commission's orders specifically left open the possibility of its enforcement if Cities had sought a restructured form of service similar to WVPA's.

C. Next, Cities argue that the Commission erred in interpreting their most favored nations clause as requiring Cities to take WVPA's entire settlement package, instead of permitting Cities to isolate and select only those terms that it considers more favorable than terms in the I&M/Cities settlement. Cities maintain that the language of their most favored nations clause reflects that the parties adopted a "term" approach, and not a "package" approach. This claim, too, is erroneous.

The Commission's orders do not eschew a "term" approach in favor of a "package" approach, or vice versa. That is, the Commission's orders do not rule out a comparison of isolated terms when two settlements govern similarly situated

customers. 21/ Rather, the orders below simply recognize that when one customer's service has been restructured so significantly that the new terms and conditions no longer permit any meaningful side-by-side comparison with the unrestructured service, a most favored nations clause, to be applicable, should not focus on individual terms, but on the new service as a whole.

D. Cities are also wrong in suggesting (Pet. Br.20) that the wording of their most favored nations clause requires Cities to have the benefit of individual terms from other settlements under all circumstances. As relevant here, the most favored nations clause states

> if I&M negotiates a settlement in any of its remaining consolidated rate dockets on terms that are more favorable to the customers affected by those dockets than the terms of this agreement, I&M will amend this Agreement to provide to Cities the effect of the more favorable terms.

(R. 1841, J.A. 18.)(Emphasis added.)

If Cities had wished to reserve the right to pick and choose among separate components or parts of the rate agreed to

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21/ Thus, the fact that Cities' most favored nations clause (see note 8, supra) acknowledges that I&M's settlement with Michigan Power Company (Docket No. ER88-30-000) "does not contain any terms more favorable to MPCO than the terms of this settlement are to Cities" (R. 1841, J.A. 18; emphasis added) does not compel a different result. There is no evidence in the record, and indeed, Cities have never claimed, that the I&M/MPCO service was completely restructured in a manner similar to WVPA's underlying service.

other settlements under all circumstances, it could readily have provided for this eventuality by insisting that the most favored nations clause expressly state so. Instead, that clause uses only the word, "terms," to describe the basis for comparison. 22/ The word "terms" authorizes the collective approach deemed appropriate in this case where the Commission was reviewing dissimilar services and rate structures.

E. Finally, Cities argue (Pet. Br. 21-22) that, if left standing, the Commission's orders will have a "chilling effect" on settlements, would permit suppliers like I&M to walk away from their obligations under favored nations clauses, and would violate the Commission's policy favoring settlements. None of these contentions withstand analysis. 23/

A settlement is typically a carefully negotiated accord reflecting a nice balance of competing economic interests between power suppliers and wholesale customers. The Commission's orders below that a wholesale customer may not invoke a most favored

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22/ Cities concede (Pet. Br. 20) that "[i]f the [Cities] Settlement reflected a 'package' approach, Paragraph 17 would have required that [Cities] elect, under the Most Favored Nations Clause, to take the entire package."

23/ Cities also argue (Pet. Br.20-21) that favored nations clauses would be rendered meaningless if they are applied only to settlements that have no significantly different features. The short answer to this is that favored nations clauses will still apply to restructured service arrangements. Nothing in the Commission's orders suggests that these clauses are inoperative when a disgruntled customer seeks to obtain the same or similar service as the customer who has restructured.

nations clause only to "skim the cream" from a differently structured settlement will, in the long run, encourage settlements. 24/ A contrary ruling would wreak havoc with the settlement process, as it would invite customers with most favored nations clauses, though complete strangers to a restructured settlement process, to go seeking benefits in such settlements, secure in the knowledge that they will not have to bear any of the burdens of other unfavorable terms in those settlements.

Such a result, moreover, would frustrate the main purpose of settlements--the avoidance of time-consuming and costly litigation over rate issues. It would simply substitute for the case that has been settled another kind of complex rate case, i.e., one devoted to a comparison of totally different contracts, services, and rates, as well as subjective judgments about whether or not entirely different features constitute "more favorable terms." Equally significant, such a result would destroy innovation in the settlement process, as suppliers would be exposed to significant risks unless all settlement packages were basically uniform. In sum, rather than acting to chill settlements, the Commission's orders encourage precise drafting,

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24/ The Commission's rulings will also ensure that parties to a settlement are precise in spelling out their agreement. See NFGS, 811 F.2d at 1572 n.5; Texas Eastern Transmission Corp. v. FPC, 306 F.2d 345, 347-48 (5th Cir. 1962), cert. denied, 375 U.S. 941 (1963); accord, Mitchell Energy Corp. v. FPC, 519 F.2d 36, 40-41 (5th Cir. 1975); City of Chicago v. FPC, 385 F.2d 629, 640 (D.C. Cir. 1967), cert. denied, 390 U.S. 945 (1968).

and preserve both stability and innovation in the settlement process.

## CONCLUSION

For the foregoing reasons, the orders of the Commission should be affirmed.

Respectfully submitted.

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