



No. 14-614

In the
Supreme Court of the United States

DOUGLAS R.M. NAZARIAN, ET AL.,

Petitioners,

v.

PPL ENERGYPLUS, L.L.C., ET AL.,

Respondents.

**On Petition for a Writ of Certiorari to the
United States Court of Appeals for the
Fourth Circuit**

REPLY BRIEF FOR PETITIONERS

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Petitioners and Respondents agree that the Federal Power Act (FPA) prohibits states from setting rates for wholesale power sales. But the decision below—and Respondents’ defense of it—is based on two further, flawed premises: first, that a state engages in wholesale rate-setting when it compels retail utilities to contract with the winning bidder in a power-supply solicitation; and, second, that the rate established by the operator of a centralized wholesale power market is the only legal rate for sales in that market—precluding sellers from setting different rates or selling on other terms, subject to review by the Federal Energy Regulatory Commission (FERC). The first is essential to the decision’s field-preemption holding; the second to its conflict-preemption holding.

Both premises reflect fundamental misunderstandings of the FPA’s rate-setting machinery and this Court’s uniform precedent, under which utility sellers set initial FPA rates and can do so by contract, subject to FERC review. They also produce results at odds with decades of settled and critical industry practices. If the first premise were true, then states could not direct retail utilities to buy *any* FERC-jurisdictional product from a state-chosen seller. If the second were true, long-term contracts for power sales in central wholesale markets would be illegal, undermining key sources of market stability and essential support for investment.

Absent review, the decision’s field- and conflict-preemption holdings will enshrine an inaccurate, unworkable view of wholesale markets and rate-setting—one that gravely threatens the states’ police power to regulate electric power supplies by overseeing retail utilities’ contracts and rates. That is why eight states and the District of Columbia, five national associa-

tions—including all of the Nation’s state utility regulators and consumer advocates—and others have joined Maryland or New Jersey (in Nos. 14-634 and 14-694) in seeking review.

I. The decision below raises important, unsettled questions of law requiring immediate answers.

That the *contracts* here set rates—like all contracts do—does not mean that *Maryland* set rates by requiring the retail utilities to sign them. Respondents and the decision below conflate these inquiries. *See* Br.Opp’n 16. Respondents also wrongly paint as a factual dispute the question whether Maryland set rates. *Id.* 1, 15, 16.

The facts are undisputed: Maryland determined it needed new generation, and directed retail utilities to solicit offers from developers willing to build facilities and sell power on a long-term basis. Maryland selected the winner, CPV Maryland, LLC, and directed retail utilities to contract with it. CPV agreed to build facilities of a certain size and technology and to offer power into the regional wholesale market (and to comply with applicable federal rules) for twenty years. In exchange, CPV would receive fixed, contract rates. No one contests these facts. The constitutional dispute concerns their legal significance.

CPV proposed the rate and entered the contracts willingly. The retail utilities did not; Maryland directed them to do so.¹ Whether that means Maryland

¹ State law empowered Maryland to do so. *In re Calpine Corp.*, No. 24-C-12-002853, slip op. 16-17 (Balt. Cty. Cir. Ct. Oct. 4, 2013), available at <http://www.courts.state.md.us/business/tech/pdfs/mdbt2013-9.pdf>, appeal pending but stayed sub nom. *Md. Office of People’s Counsel v. Md. Pub. Serv. Comm’n*, No. 1738, Sept. Term 2013 (Md. Ct. Spec. App. docketed Nov. 6, 2013). Con-

“set” rates is a legal question—to which the FPA and this Court’s precedent provide the resounding answer. The FPA vests initial rate-setting authority—including the ability to set rates by contract—in wholesale sellers.² FERC has authority to review those rates. Maryland interfered with neither seller nor FERC. The state exercised no compulsion—or even leverage—over CPV. It directed retail utilities to accept CPV’s offer, producing a contract that FERC could have reviewed.

If Maryland could “set” a wholesale rate merely by directing the retail utilities to accept a seller’s offer, *see* Br.Opp’n 24, then *all* state directives to contract with a state-selected wholesale power supplier would be illegal. This cannot possibly be the law. Instead, the FPA preserves state authority over utility purchases.³ States supervise retail power procurements all the time, and our petition cited many examples of programs threatened by the decision below (including procurements already targeted by opponents wielding the decision). Md.Pet. 20-25.

Respondents argue that these examples involve ordinary power purchases, not contracts for differences (CFDs). Br.Opp’n 30. That contention is wrong.⁴ It also

trary to Respondents’ claims, Maryland’s decision to “do away with vertical integration” (Br.Opp’n 6-7) did not divest it of authority to direct retail utility contracting to support new generation. *In re Calpine*, slip op. 18, 20.

² *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 341 (1956) (*Mobile*); *Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1*, 554 U.S. 527, 531 (2008) (*Morgan Stanley*); *NRG Power Mktg., LLC v. Me. Pub. Utils. Comm’n*, 558 U.S. 165, 171 (2010) (*NRG*).

³ *New York v. FERC*, 535 U.S. 1, 24 (2002).

⁴ *See, e.g.*, Md.Pet. 23 & n.26 (discussing Connecticut procurement with CFDs). In other cases, programs either requested CFD pro-

highlights a difference without practical or statutory significance. We showed—and Respondents do not dispute—that CFDs accomplish in one step the same result as a bilateral power purchase followed by resale of the power into a wholesale market: the generator receives the contract price; the retail utility pays that price, and receives the market price.⁵

More important, the Respondents’ own field-preemption theory (adopted below) renders irrelevant any distinction between CFDs and bilateral sales. As Respondents explain, “*any* state law falling within [an exclusively federal] field is preempted.” Br.Opp’n 25 (quoting *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 248 (1984)). Preemption of state rate-setting extends to *all* FERC-jurisdictional wholesale sales—whether short- or long-term, to PJM Interconnection, L.L.C. (PJM) or another reseller. This unavoidably raises the stakes of the question presented—what *constitutes* preempted state rate-setting—and belies any labeling of the decision below as “narrow” (Br.Opp’n 1, 15).

Respondents downplay these concerns by observing that we identified no other program (besides New Jer-

posals or allowed bidders to offer either a CFD or a bilateral sale. E.g., *id.* 24 & n.32; Me. Pub. Utils. Comm’n, Supplemental Request for Proposals for Long-Term Contracts for Deep-Water Offshore Wind Energy Pilot Projects § 2.3 (2013), http://www.maine.gov/mpuc/electricity/rfps/standard_offer/deepwater2010/documents/SupplOffShoreRFP.pdf; *Re Generation Ret. Contingency Plans*, 304 P.U.R.4th 387, 396-397 (N.Y. Pub. Serv. Comm’n 2013).

⁵ Md.Pet. 7; *see also* Meg Gottstein & Lisa Schwartz, *The Role of Forward Capacity Markets in Increasing Demand-Side and Other Low-Carbon Resources: Experience and Prospects* 9-10 (Regulatory Assistance Project May 2010), [http://www.roadmap2050.eu/attachments/files/PolicyBriefMay2010RM2050\[4\].pdf](http://www.roadmap2050.eu/attachments/files/PolicyBriefMay2010RM2050[4].pdf) (describing CFDs and physical bilaterals as fungible alternatives).

sey's) yet invalidated on this theory. Br.Opp'n 30. But that is a heads-I-win, tails-you-lose argument. If other programs had been invalidated, Respondents would tout those decisions as demonstrating unanimity diminishing the need for review.

That gambit notwithstanding, the decision looms over the cited programs and jeopardizes the legal certainty necessary to finance them. It does not take much to scare off investors in billion-dollar capital projects, and ongoing litigation over the ability to recover costs from retail ratepayers is ample to the task. Even where states and project developers have fended off lower court challenges, opponents have appealed and projects have folded in the interim.⁶

The Nation cannot afford to await the kind of circuit split Respondents deem prerequisite to review (with different holdings on identical facts) or to see if some later state-supported project survives to bring the

⁶ Massachusetts prevailed in the district court preemption litigation brought by Cape Wind's opponents, *see Barnstable v. Berwick*, 17 F. Supp. 3d 113, 124 n.26 (D. Mass. 2014), *appeal pending*, No. 14-1597 (1st Cir. argued Jan. 5, 2015), but retail utilities terminated their contracts during the appeal, citing financing delays that Cape Wind traces to the litigation. *See* Letter from James G. Daly, Vice President, NSTAR Elec. Co., to Christopher Smith, Chief Financial Officer, Cape Wind Assocs. LLC (Jan. 6, 2015), *available at* <http://goo.gl/vyqmTc>; Letter from James S. Gordon, President, Cape Wind Assocs., to James Daly et al. (Dec. 31, 2014), *available at* <http://goo.gl/3kcD7Q>. A similar fate recently befell the FutureGen clean-coal plant after the Illinois Supreme Court agreed to hear state-law challenges to mandated retail-rate funding. Steve Daniels, *FutureGen 'Clean-Coal' Plant Is Dead*, CRAIN's Chi. Bus. (Feb. 3, 2015), *available at* <http://www.chicagobusiness.com/article/20150203/NEWS11/150209921/futuregen-clean-coal-plant-is-dead>; *Commonwealth Edison Co. v. Ill. Commerce Comm'n*, 21 N.E.3d 713 (Ill. 2014) (unpublished table decision) (allowing petition for leave to appeal).

issues back to this Court. The bigger and more important the project, the more prone it will be to death by uncertainty. The Court should resolve now the questions raised by the decisions below, eliminate conflicts with this Court's precedent (*supra* note 2), and remove the cloud threatening needed investments.

II. The decision below propagates dangerous confusion about the FPA and regional wholesale electricity markets.

Respondents' assertions of unanimity notwithstanding, neither the Maryland district court nor the Third Circuit reached their conflict-preemption claims. The core of the Fourth Circuit's conflict-preemption holding is an idea that runs throughout Respondents' brief: that states and sellers may not set by contract "different and more stable price[s] ... for sales *in [the PJM] market*" than that produced by PJM's auction. Br.Opp'n 28-29. Elevating PJM's auction above CPV's rate-setting and contracting authority, however, is a mistake that goes to the heart of the FPA and its application to regional wholesale markets.

1. Respondents and the decision below assume that only PJM can set rates for sales in the PJM market. But the FPA accords rate-setting power to wholesale *sellers* like CPV, not purchasers or brokers like PJM.⁷ While sellers may choose to accept PJM's price, they also may deem those rates inadequate and set their own rates instead (subject to FERC review). As the D.C. Circuit held, FERC's preference for regional organizations and markets does not entitle it to strip sellers of the statutory right to set their rates. *Atl. City Elec. Co. v. FERC*, 295 F.3d 1, 10 (D.C. Cir. 2002) (*At-*

⁷ See *supra* note 2.

lantic City), *mandate enforced*, 329 F.3d 856 (D.C. Cir. 2003).⁸

Respondents seem to concede (Br.Opp'n 26-27) that sellers like CPV may set rates and enter contracts for *bilateral* sales to utilities who serve retail load in PJM, which then re-sell the power in the auction as a means of fulfilling their load-serving obligations. Respondents say CFDs are different, but, as noted earlier, fail to show how the difference has any statutory significance.

The FPA empowers CPV to set initial rates and rate design (subject to FERC review), and does not require sellers to drop those rights at a regional market's borders. CPV's contract established a rate and rate design for building a power plant and offering power into the market on a long-term basis. The rate was the contract price. The rate design was that PJM pays the auction price by operation of its tariff, while the Maryland utilities pay or receive any difference between contract and market prices.

Respondents argue (Br.Opp'n 22) that CPV waived its right to set rates when it "opt[ed] into the PJM auction," but they identify neither any express waiver nor case law holding that a waiver is implied. To the contrary, *Atlantic City* holds that utilities selling FERC-jurisdictional services through regional organizations retain their rate-setting rights unless they expressly agree otherwise. Sellers in regional markets thus retain the right to set rates for wholesale sales, including

⁸ Respondents (Br.Opp'n 21) say we cited *Atlantic City* only once below, as if that number mattered. They apparently overlooked the four *Atlantic City* citations in our reply brief and rehearing petition. Respondents also imply that there can be no circuit split because Maryland and CPV emphasized different conflicts. That the decision below collides with precedent at multiple points is hardly a reason to deny the petition.

sales to or through entities like PJM, subject to FERC review. *Midcontinent Indep. Sys. Operator, Inc.*, 148 FERC ¶ 61,057, P 92 (2014) (*MISO*), *reh'g pending*.

Indeed, generators commonly make sales in PJM and other regional markets under contracts that function exactly like CFDs. These contracts, called “Reliability Must-Run” (RMR) agreements, secure continued operation of generation facilities that are needed for reliability but earn insufficient market revenues to continue operating. The contracts make up any difference between market prices and the seller’s cost of service. *See NRG*, 558 U.S. at 169; *Blumenthal v. FERC*, 552 F.3d 875, 879 (D.C. Cir. 2009).⁹ While FERC seeks market designs that minimize the need for RMR agreements, a number of PJM generators still operate under them,¹⁰ and their existence refutes any claim that PJM market sales can occur only at PJM-set rates. As FERC held in *MISO*, sellers, not market operators, set the rates in RMR agreements, subject to FERC review.

2. Respondents ignore crucial differences between the obligations under CPV’s contract and PJM’s tariff. The auction obligates and pays sellers on a year-by-year basis. Sellers choose annually whether to participate. The CFDs, in contrast, obligated CPV to offer power to PJM *for twenty years*. Respondents wrongly

⁹ *E.g.*, Reliability Support Services Agreement dated as of February 13, 2015, between R.E. Ginna Nuclear Power Plant, LLC and Rochester Gas and Electric Corporation § 3.1(b), Docket No. ER15-1047-000, Feb. 13, 2015, eLibrary No. 20150213-5233, <http://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=13773188>.

¹⁰ *See* PJM Interconnection, *Generation Deactivation Zonal Cost Allocation for Reliability Must Run Generating Units*, <http://www.pjm.com/planning/generation-deactivation/gen-deactivation-rmr.aspx> (last visited Feb. 20, 2015).

equate a twenty-year obligation with twenty single-year obligations, and assume that the compensation (determined *ex ante* in the first case and *ex post* in the second) must be the same. To the contrary, long-term obligations entail different risks than short-term ones, and merit different compensation.

This Court and FERC have so held. Long-term contracts play an “essential role ... fostering stability” in shorter-term markets, *NRG*, 558 U.S. at 174, and it would be a “perverse rule” that enforces such contracts only if they mirror volatile year-to-year arrangements. *Morgan Stanley*, 554 U.S. at 547. The decisions below vitiate this core precedent.

3. Respondents and the decision both treat FERC’s “New Entry Price Adjustment” (NEPA) orders as a federal policy against stabilizing new entrants’ rates for more than three years. But FERC merely declined to allow *all* new entrants to lock in their first-year auction price for many years, at PJM customers’ expense. FERC’s orders predated the CFDs, and did not address the bargain CPV struck here: a long-term revenue stream set by contract, in return for new generation with a long-term sales obligation, with any difference between contract and market prices to be paid (or received) by Maryland retail ratepayers.

III. FERC’s orders belie its Third Circuit *amicus* brief.

Respondents assert (Br.Opp’n 18) that the decision below “accords not only with settled preemption principles, but with FERC’s own view.” That is false. FERC is a five-person Commission that acts by majority vote reflected in published orders.¹¹ Respondents base their

¹¹ 42 U.S.C. § 7171(b)(1), (e); *Bangor Gas Co., LLC v. H.Q. Energy Servs.*, 695 F.3d 181, 190 (1st Cir. 2012).

characterization not on FERC's orders but on an *amicus* brief that contradicts them. The Third Circuit, which invited the brief, gave it no credence.¹² The government did not file the brief in the Fourth Circuit; Respondents did.

This Court explained in *Christopher v. SmithKline Beecham Corp.*¹³ that deferral to a government brief is unwarranted where its views are “plainly erroneous or inconsistent with the regulation” or “there is reason to suspect that [it] does not reflect the agency’s fair and considered judgment.” *Id.* 2166 (quotations omitted). That is so here. The *amicus* brief suggested New Jersey’s law was preempted because it suppressed PJM’s capacity auction prices. U.S.Br. 9. FERC’s orders ensured there could be no price suppression. FERC set rules by which state-contract-backed resources can participate in PJM’s auction without distorting prices, and CPV’s resource cleared under those rules. Pet.App. 125a-126a. FERC held that such resources are “economic,” “competitive,” and “[do] not artificially suppress market prices.” *PJM Interconnection, L.L.C.*, 135 FERC ¶ 61,022, PP 175, 177 (2011). FERC further held that the revised bidding rules “reconcile[d]” any “tension” between state generation-development programs and wholesale market needs. *PJM Interconnection, L.L.C.*, 137 FERC ¶ 61,145, P 4 (2011), *petition for review denied sub nom. N.J. Bd. of Pub. Utils. v. FERC*, 744 F.3d 74 (3d Cir. 2014).

The *amicus* brief further contended (U.S.Br. 13) that FERC’s need to “counter” the states’ laws was evi-

¹² *PPL EnergyPlus, LLC v. Solomon*, 766 F.3d 241, 255 (3d Cir. 2014) (mentioning the brief once, with a “*cf.*” signal, and declining to endorse the position).

¹³ 132 S. Ct. 2156 (2012).

dence that the states had transgressed. But FERC did not see it that way. It simply withdrew a previously-granted exemption that allowed certain state-supported resources to participate in PJM's auction without abiding by its offer rules. FERC's withdrawal of the exemption did not disapprove the states' actions; FERC merely regulated state-supported resources' participation in the auction. *PJM Interconnection L.L.C.*, 137 FERC ¶ 61,145, PP 3-4.

Where FERC has found that state programs encroach on its authority, FERC has not hesitated to say so.¹⁴ And FERC has express authority to seek injunctive relief when needed. 16 U.S.C. § 825m. FERC—the regulatory body, as opposed to its counsel—expressed no such views and sought no relief.

CONCLUSION

The Fourth Circuit wrongly voided an important state program to develop new generation facilities. It misapprehended how rates are set under the FPA and how the statute applies in regional wholesale markets. It adopted a field-preemption theory that outlaws state-directed power procurement and a conflict-preemption theory that precludes sales into regional

¹⁴ *E.g.*, *Cal. Pub. Utils. Comm'n*, 132 FERC ¶ 61,047, P 69, *on reh'g*, 133 FERC ¶ 61,059 (2010), *reh'g denied*, 134 FERC ¶ 61,044 (2011).

markets at cost-based rates or on a long-term basis. It did all this in conflict with decisions of this Court, sister Circuits, and FERC itself. The petition for a writ of *certiorari* should be granted.

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