Regulating Public Utility Performance:
The Law of Market Structure, Pricing and Jurisdiction

Chapter Eleven

Mobile-Sierra Doctrine: When Does Contract "Sanctity" Give Way to Government-Ordered Amendments?

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> *[T]here is nothing in the structure or purpose of the Act from which we can infer the right, not otherwise possessed and nowhere expressly given by the Act, of natural gas companies unilaterally to change their contracts.*[1]

In 1956, Dwight Eisenhower was reelected President, Don Larsen pitched baseball's only World Series perfect game,[2] and the U.S. Supreme Court established the *Mobile-Sierra* doctrine. The doctrine is "refreshingly simple: The contract between the parties governs the legality of the filing. Rate filings consistent with contractual obligations are valid; rate filings inconsistent with contractual obligations are invalid."[3] The question of how refreshing, and how simple, has occupied practitioners for more than 50 years.

11.A. Principle: The commission cannot let parties out of their contracts

1947: Pacific Gas & Electric had historically sold electricity to Sierra Pacific Power. Facing growing post-World War II demand growth, along with customer desires for lower rates, Sierra started negotiating with alternative suppliers. PG&E responded by offering Sierra Pacific a fifteen-year contract at a "special low rate." Sierra Pacific accepted. Five years into the contract, with Sierra's alternatives no longer available, PG&E filed at the Federal Power Commission (FPC) for a rate increase of 28 percent.

2000: California faced transmission and generation shortages, with power prices rising rapidly to unheard-of levels. Faced with a "dysfunctional market" and anxious about supply, Western retail utilities with an obligation to serve signed multi-year contracts to buy power at five times the historical prices. (The sellers had FERC-granted permission to charge these "market-based rates.") Several years later, the retail utilities filed complaints with FERC, asserting that the contract prices were not just and reasonable. They asked FERC to modify the contracts, prospectively and retroactively, to reduce the rates and order refunds.

In each of these situations, a contract signatory tried to escape the deal it signed. In the first example, the seller argued the price was unlawfully low; in the second example, the buyers argued the price was unlawfully high. How do regulators and courts respond? When can a regulator intervene in a private contract? That is the subject of the "venerable *Mobile-Sierra* doctrine," the Supreme Court's interpretation of the Natural Gas Act and the Federal Power Act. The doctrine was established for cost-based contracts in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.* and *Federal Power Commission v. Sierra*

1. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 343–44 (1956).
2. On October 8, 1956, the author's date of birth.
3. Richmond Power & Light v. FPC, 481 F.2d 490, 493 (D.C. Cir. 1973).

Pacific Power Co. and applied to modern, market-based transactions in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1.*[4]

The Mobile-Sierra doctrine distills to this principle: Under the Natural Gas Act (Mobile) and the Federal Power Act (Sierra), a party to a FERC-jurisdictional contract cannot unilaterally ask FERC to change the contract, unless the contract itself authorizes the change. "[T]here is nothing in the structure or purpose of the [Natural Gas] Act from which we can infer the right, not otherwise possessed and nowhere expressly given by the Act, of natural gas companies unilaterally to change their contracts." This restriction "fully promotes the purposes of the Act. By preserving the integrity of contracts, it permits the stability of supply arrangements which all agree is essential to the health of the natural gas industry."[5] Contract stability benefits consumers too: "[U]ncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm customers in the long run."[6]

To emphasize the statutory insistence on "contract sanctity," the Supreme Court has emphasized the "marked contrast" between the Natural Gas Act (which allows individual, bilateral contracts) and the Interstate Commerce Act (which precludes private contracts, allowing only uniform tariffs):

> The vast number of retail transactions of railroads made policing of individual transactions administratively impossible; effective regulation could be accomplished only by requiring compliance with a single schedule of rates applicable to all shippers. On the other hand, only a relatively few wholesale transactions are regulated by the Natural Gas Act and these typically require substantial investment in capacity and facilities for the service of a particular distributor. Recognizing the need these circumstances create for individualized arrangements between natural gas companies and distributors, the Natural Gas Act permits the relations between the parties to be established initially by contract, the protection of the public interest being afforded by supervision of the individual contracts, which to that end must be filed with the Commission and made public.[7]

4. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332 (1956); Federal Power Comm'n v. Sierra Pac. Power Co., 350 U.S. 348 (1956); Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1, 554 U.S. 527 (2008).
5. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. at 343–45.
6. Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1, 554 U.S. 527, 550–51 (2008) (quoting FERC's Order No. 697 on market-based rates, discussed in Chapter 7.C.1).
7. United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. at 338–39.