

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

Not For Publication

In re:

ENRON CORP., *et al.*,

Reorganized Debtors.

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Chapter 11

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Case No. 01 B 16034 (AJG)

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:
(Confirmed)

OPINION SUSTAINING DEBTORS' OBJECTION TO PROOF OF CLAIM NO. 12231
FILED BY VALLEY CENTER MUNICIPAL WATER DISTRICT; TO PROOF OF CLAIM
NO. 12238 FILED BY SWEETWATER AUTHORITY; AND TO PROOF OF AMENDED
CLAIM NO. 23154 FILED BY PADRE DAM MUNICIPAL WATER DISTRICT
REGARDING STATE LAW CLAIMS IN ELECTRICITY MARKET

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ARTHUR J. GONZALEZ
United States Bankruptcy Judge

On October 11, 2002, plaintiff's counsel filed separate proofs of claims ((Claim Nos. 12231, 12238, and 23154 (amending and superseding Claim No. 12232), collectively the "Claims")) in unliquidated amounts on behalf of Valley Center Municipal Water District, Sweetwater Authority, and Padre Dam Municipal Water District (collectively, the "Claimants") against Enron Corporation ("Enron") and certain of its affiliated entities (collectively, the "Debtors"). The Claims are based on actions filed by the Claimants and other plaintiffs against Enron Energy Services, Inc. ("EESI"), Enron Power Marketing, Inc. ("EPMI") and other defendants in the Superior Court of the State of California for San Diego County.

The Claimants allege that the Debtors manipulated energy markets in California and overcharged for energy through unlawful and anti-competitive acts during the western power crisis of 2000 and 2001. They maintain the alleged manipulation in the electricity market constitutes a violation of state antitrust law and unfair competition law, and seek disgorgement, restitution, actual and treble damages together with interest and injunctive relief.¹ On February 18, 2005, the Debtors filed objections to the Claimants' state law claims and argued that the Federal Power Act (the "FPA") preempts the state laws and the filed rate doctrine precludes consideration of these claims.

The issues before the Court are whether the Claims are preempted by the Federal Power Act (the "FPA") and precluded by the filed rate doctrine. The Court finds that because the

¹ California Antitrust Law, Business & Professional Code § 16720 *et. seq.* (The Cartwright Act) and California Unfair Competition Law, Business & Professional Code § 17200. Claimants allege that the Debtors' violation of the Cartwright Act, by engaging in acts and practices which constitute anti-competitive practices, violates Business & Professional Code § 17200's proscription against engaging in unlawful business acts and practices.

Federal Energy Regulatory Commission (“FERC”) has exclusive jurisdiction over interstate sales of wholesale electricity, the state law claims sought to be enforced by Claimants in the prosecution of the Claims are preempted by the FPA. Further, the filed rate doctrine precludes consideration of such Claims.

I. BACKGROUND

Commencing on December 2, 2001, and from time to time continuing thereafter, the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the “Bankruptcy Code”). On July 15, 2004, the Court entered an Order confirming the Debtors’ Supplemental Modified Fifth Amended Joint Plan of Affiliated Debtors (the “Plan”) in these cases. The Plan became effective on November 17, 2004.

This litigation arises out of the California energy crisis of 2000-01. Prior to the energy crisis, the California legislature had passed Assembly Bill 1890² (the “Bill”) to create two non-governmental entities, the California Power Exchange (the “PX”) and the California Independent System Operator (the “ISO”), to operate markets and manage the sale of electricity. The PX and the ISO were organized under California law, but regulated by FERC. *California v. Dynege, Inc.*, 375 F.3d 831, 850 (9th Cir. 2004). The central transactions, wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC “jurisdictional” ISO and PX. Further, the centralized wholesale spot electricity markets operated by the ISO and the PX were established subject to FERC review and approval. The ISO and the PX served as clearinghouses. Since August 2, 2000, FERC has commenced refund proceeding, and partnership and gaming proceeding to investigate certain of the Debtors. FERC found that the

² 1996 Cal. Stat. 854

Debtors engaged in gaming³ in the form of inappropriate trading strategies and further engaged in the deliberate submission of false information or the deliberate omission of material information. *Enron Power Mktg., Inc., et al.*, 106 FERC ¶ 61,024 (2004). Both proceedings are ongoing, including the determination of remedies by FERC.

II. DISCUSSION

A. Legal Standard of Preemption

“Federal preemption of state law is rooted in the Supremacy Clause, Article VI, clause 2, of the United States Constitution.” *Transmission Agency of Cal. v. Sierra Pacific Power Co.*, 295 F.3d 918, 928 (9th Cir. 2002). Where Congress manifests intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted. *Metro. Life Ins. Co. v. Taylor*, 481 U.S. 63-64 (1987). Federal courts have rarely identified legislation that has been found to completely preempt state jurisdiction. *Caterpillar, Inc. v. Williams*, 482 U.S. 393 (1987).

Here, neither party raises the argument that complete preemption is applicable, nor is there any evidence in the record that would support the conclusion that Congress intended for complete preemption to apply in this case. In the absence of an express preemption by Congress, state law is preempted (1) “when Congress intends that federal law occupy a given field.” *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 248 (1984) (“Field Preemption”), and (2) “to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress.” *Id.* (“Conflict Preemption”).

³The ISO tariff, through the ISO’s Market Monitoring and Information Protocol defines gaming, in part, as “taking unfair advantage of the rules and procedures set forth in the PX or the ISO tariffs, Protocols or Activity Rule ... to the detriment of the efficiency of, and of consumers in, the ISO markets.” *Am. Electric Power Service Corp., et al.*, 103 FERC ¶ 61,346 (2003).

B. Preemption

1) Field Preemption

The Debtors, in support of their position that the state law claims should be barred by FERC's exclusive jurisdiction, cite to *Grays Harbor v. Idacorp Inc.*, 379 F.3d 641 (9th Cir. 2004), *Dynergy*, and *Snohomish County v. Dynergy Power Marketing Inc.*, 384 F.3d 756 (9th Cir. 2004). These cases addressed FERC's exclusive jurisdiction and its remedial power concerning the wholesale electricity market. The Debtors argue that state law claims in the instant case, alleging violations of state antitrust and unfair competition law, are nearly identical to those involved in the cited cases, and for the reasons set forth in those cases, field preemption is applicable here.

The *Dynergy* court ruled that "state actions against wholesale electricity suppliers alleging violations of California's unfair business practices law are preempted by FPA because the conduct the state sought to condemn was expressly governed by the ISO tariffs and they encroach upon the substantive provisions of the tariff, an area reserved exclusively to FERC, both to enforce and to seek remedy." 375 F.3d at 852.

The Court finds that the statute's framework under the FPA supports the conclusion in *Dynergy* that FERC has been granted broad authority by Congress, in addition to the authority to determine the "just and reasonable rates" for wholesale power. The statute delegates to the Federal Energy Commission "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states." Federal Power Act, 16 U.S.C. § 824-824m.

Claimants do not dispute that the transactions at issue involved wholesale interstate sales. Further, there has been no evidence presented or any representation by either party that the sales that gave rise to this dispute should be characterized as either retail sales of electricity or wholesale intrastate sales. The statute provides that upon a determination by FERC that "any rate charge, or classification, demanded, observed, charged, or collected by any public utility for any *transmission or sale* subject to the jurisdiction of the Commission, or that any rule, regulation, *practice, or contract affecting such rate, charge, or classification* is unjust, unreasonable, unduly discriminatory or preferential, *the Commission shall determine* the just and reasonable rate, charge, classification, rule, regulation, *practice, or contract* to be thereafter observed and in force, and shall fix the same by order." Federal Power Act, 16 U.S.C. § 824e (emphasis added).

Moreover, pursuant to the statute, FERC possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rulemaking rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. Federal Power Act, §§ 205, 206(a), as amended, 16 U.S.C.A. §§ 824d, 824e; Department of Energy Organization Act, § 403(c), 42 U.S.C.A. § 7173(c).

In addition, after the deregulation of California energy markets, the central transactions and the wholesale sales of energy in interstate commerce were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Having examined FERC's regulatory authority over the deregulated electricity market in California, the *Snohomish* court concluded, "FERC is

doing enough regulation to justify federal preemption of state laws under the market-based system of setting wholesale electricity rates.” *Snohomish*, 384 F.3d at 760-61. For instance,

(1) FERC continued to oversee wholesale electricity rates by reviewing and approving a variety of documents filed by the PX and the ISO. FERC approved the market-based tariffs only upon a showing that the seller lacked or had mitigated its market power. (2) FERC required each seller to file quarterly reports under FPA §205(c) 16 U.S.C. §824d(c). (3) FERC reviewed and approved detailed tariffs filed by the PX and the ISO, which described in detail how the markets operated by each entity would function. *Id.*

In addition, “[e]ach participant in the PX and the ISO markets was required to sign an agreement acknowledging that the tariff filed by either the PX or the ISO would govern all transactions in that market.” *Id.*

The Court also recognizes that “entities that transact through the ISO or [the] PX and engage in improper practices⁴ are in violation of filed tariffs FERC and the Market Surveillance Unit are directed by the ISO’s Market Monitoring and Information Protocol to refer matters to the FERC for enforcement.” 103 FERC ¶ 61,346. Here, Claimants do not dispute the fact that it procured electricity through the market administered by the ISO.

Moreover, the Court finds that *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973), and *California v. Federal Power Commission*, 369 U.S. 482 (1962) are not controlling in the instant case. In both cases, the Supreme Court found that Congress does not intend to bar governments from bringing actions in violation of antitrust laws related to filed tariffs before

⁴ Since 1998, the ISO and the PX tariffs have contained provisions that identify and prohibit “gaming” and “anomalous market behavior” in the sale of electric power. “Anomalous market behavior” is (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; b) unexplained or unusual redeclarations of availability; c) unusual trades or transactions; d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges.” *Am. Elec. Power Serv. Corp. et al.*, 103 FERC ¶ 61,346(2003).

regulatory commissions. However, two important differences exist. First, both cases discussed issues of the interaction between federal administrative law and federal antitrust law; thereby no state law preemption issue was presented in these cases. In *California v. Federal Power Commission*, a gas company filed a motion to dismiss the antitrust suit pursuant to the Clayton Act, § 7 as amended 15 U.S.C.A. §18, or in the alternative, to stay it, pending completion of the proceedings for its authority to acquire another company's assets pursuant to the Natural Gas Act (the "NGA"), § 7(c) as amended 15 U.S.C.A. §717f(c), before the Power Energy Commission. 369 U.S. at 483. In *Otter Tail Power*, the government brought an action against an electric power company to enjoin violations of the Sherman Act, 15 U.S.C.A. §2. 410 U.S. at 368. In order to protect market competition in certain cases, Congress did not expressly displace federal antitrust laws. The Court will not address whether, as a result, Congress has left room for enforcement of state antitrust laws.

Second, and more importantly, a critical distinction between the instant matter and the two cited cases is that there is a regulatory scheme against anti-competitive behavior that has been entrusted to FERC. As the Court discussed above, the statute under 16 U.S.C.A. §§ 824d, 824e(a) provides FERC with broad remedial authority to address anti-competitive behavior. In fact, FERC has exercised this power to act in the proceedings instituted against the Debtors concerning alleged market manipulation during the energy crisis. FERC has asserted that it "can order disgorgement of monies above the post-October 2, 2000 refunds ordered in the California Refund Proceeding, if it finds violations of the ISO and the PX tariffs and finds that a monetary remedy is appropriate for such violations. It can additionally order additional disgorgement of unjust profits for tariff violations that occurred after October 2, 2000." 103 FERC ¶ 61,346. Further, "implicit in Commission orders granting market-based rates to the marketers is a

presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority.” 106 FERC ¶ 61,024.

In contrast, the court in *California v. Federal Power Commission* concluded that the NGA did not contain a provision to immunize the carriers involved in the mergers from the Clayton Act. 369 U.S. at 485. “The Commission’s standard, set forth in § 7 of the NGA, will serve ‘the public convenience and necessity.’ If existing natural gas companies violate the antitrust laws, the Commission is directed by § 20(a) to ‘transmit such evidence’ to the Attorney General.” *Id.* at 486. Similarly, the Court in *Otter Tail Power* found that the limited authority of the Federal Power Commission to order interconnections was not intended to be a substitute for the Sherman Act. 410 U.S. at 375. Moreover, the Supreme Court in *Carnation Co. v. Pacific Westbound Conference*, 383 U.S. 213 (1966) declined to grant antitrust immunity to a shipping company because “the provisions of the Shipping Act, 46 U.S.C.A. §801, can not reasonably be construed as an implied repeal of antitrust regulation of the shipping industry’s rate-making activities.” *Id.* at 217. The Shipping Act does not give the Federal Maritime Commission (the “FMC”) any mandate to regulate rate competition and the statutory scheme was designed to minimize the role of the FMC. *Square D Co. v. Niagara Frontier Tariff Bureau*, 476 U.S. 409, 422 (1986).

The Court further finds that *Grays Harbor* and *Gulf States Util. Co. v. Alabama Power Co.*, 824 F.2d 1465 (5th Cir. 1987) are not applicable in the instant case. The courts in both cases concluded that the state law claims concerning contractual disputes were not within the scope of FERC’s jurisdiction. The facts here are distinguishable. First, the state law claims in the cited cases were related to contractual issues, which exclusively fall within a state’s

jurisdiction. The court in *Grays Harbor* granted the utility leave to amend its complaint to seek declaratory relief only as to issues of contract formation. 379 F.3d. at 652-53. Similarly, the court in *Gulf States* held that executed contract performance, such as the failure to negotiate in good faith and fraud, were not preempted by the FPA. 824 F.2d at 1474. Here, no evidence or argument presented before the Court demonstrates that there is an issue involving contractual disputes. Second, contract formation issues would not necessarily intrude upon the rate-setting jurisdiction of FERC. *Grays Harbor*, 379 F.3d. at 653. Therefore, field preemption bars the Claimants from pursuing its state law claims before the Court.

C. Conflict Preemption

As to conflict preemption, for the foregoing reasons, the Court concludes that FERC has broad authority concerning anti-competitive activities related to the filed rate, apart from that FERC has authority to determine the “just and reasonable” rates for wholesale power. A conflict between the FPA in which grants FERC jurisdiction over the anti-competitive acts and state antitrust claims exists. Accordingly, conflict preemption also bars the Claimants from pursuing state law claims before the Court.

D. Filed Rate Doctrine

Another threshold question before the Court is whether the Court would have to determine a tariff. The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. *E. & J. Gallo Winery v. Encana Energy Servs., Inc.*, Case No. CV F 03-5412 AWILJO. at 15. The Court recognizes that the filed

rate doctrine “forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority.” *Ark. L.A. Gas Co. v. Frank Hall*, 453 U.S. 571, 577-78 (1981). The Court also acknowledges that the purpose of the doctrine is “preservation of the agency’s primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant.” *City of Cleveland v. FPC*, 525 F.2d 845, 854 (D.C. Cir. 1976).

In addition, FERC required each seller to file quarterly reports pursuant to FPA §205(c) 16 U.S.C. §824d(c) on transaction-specific information about its sales and purchases at market-based rates. The court in *Grays Harbor* concluded “while market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine.” 379 F.3d at 651.

Further, the Court agrees with the opinion of the *California v. FERC* court which concluded that “the reporting requirements are an integral part of a tariff, with FERC’s implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates.” 383 F.3d at 1016. On August 13, 2002, FERC’s Initial Report in Docket No. PA02-2-000 concluded that the Debtors engaged in the deliberate submission of false information or the deliberate omission of material information.⁵ Then, FERC concluded that such behavior constituted market manipulation and resulted in unjust and unreasonable rates and violated the express requirements in the orders allowing the Debtors to make sales at market-based rates. 106 FERC ¶ 61,024. As noted by FERC,

⁵ FERC found that the Debtors failed to inform FERC in a timely manner of changes in their market shares that resulted from their gaining influence/control over others’ facilities, as required under their market-based rate authorization. 106 FERC ¶ 61,024.

implicit in Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority. The Debtors were expressly directed, when they were granted market-based rate authority, to inform the FERC promptly of changes in status (which would include changes in their generation market shares) that reflect a departure from the characteristics that the FERC relied upon in granting market-based rate authority. *Id.*

Moreover, the Court in *California v. FERC*, indirectly recognized the application of the filed rate doctrine when marketers had not properly reported to FERC where such improper reporting affected the reasonableness of the tariff approved by FERC. 383 F.3d at 1016.

Without the availability of retroactive refunds, “[p]arties aggrieved by the illegal rate would have no FERC remedy, and the filed rate doctrine would preclude a direct action against the offending seller. That result does not comport with the underlying theory or the regulatory structure established by the FPA.” *Id.*

The Court finds that determining the liability or the legal right of Claimants against the Debtors for violation of the antitrust laws would have to be measured by the tariff. Therefore, the filed rate doctrine would be applicable.

In addressing the right of action that a violation of the antitrust laws give to one who has been injured in its business or property, the Supreme Court in *Keogh v. Chicago & N.W.R.Y. Co.*, 260 U.S. 156 (1922), stated that “[i]njury implies violation of a legal right.” *Id.* at 163. The Supreme Court concluded that “the legal rights of [a] shipper as against [a] carrier in respect to a rate are measured by the published tariff.” *Id.* at 163. Justice Brandeis explained “[a] rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the Anti-Trust Act. What rates are legal is determined by the Act to Regulate Commerce. Under Section 8 of the latter act . . . the exaction of any illegal rate makes the carrier liable to the ‘person injured thereby for the full amount of damages sustained in consequence of any such

violation.” *Id.* at 162. Thus, the finding of liability in antitrust laws would be integral to the Court’s determination of whether the Debtors are liable due to their violations of state antitrust law and unfair competition law. For instance, the Court could not determine the overcharge claim owed by the Debtors for any electricity market manipulation without first deciding the reasonableness of the filed tariff.

The Supreme Court case, *Arkansas Louisiana*, further supports the Court’s position that the filed rate doctrine should apply here. “In asserting that the filed rate doctrine had no application, respondents in *Arkansas Louisiana* contended that the state court has done no more than determine the damages they have suffered as a result of the breach of a contract by a gas company.” 453 U.S. at 579. The Supreme Court rejected this argument by reasoning that “the mere fact that respondents brought this suit under state law would not rescue it, for when Congress has established an exclusive form of regulation . . . there can be no divided authority over interstate commerce Under the filed rate doctrine, FERC alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged.” *Id.* at 580-84.

Moreover, to award monetary relief, the Court would have to determine a “fair price.” Thus, the filed rate doctrine bars the Court from awarding monetary damages sought by Claimants. Nonetheless, the Court finds that injunctive relief would also be unavailable to Claimants. The Court agrees with the Ninth Circuit’s decision in *Snohomish*, which declined to grant injunctive relief because such relief is barred by the filed rate doctrine and preemption principle. 384 F.3d at 762. “Remedies for breach and non-performance of FERC-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC.” *Dynegy*, 375 F.3d at 836.

The decisions from the Second Circuit in *Sun City Taxpayers' Association v. Citizens Utilities Co.*, 45 F.3d 58 (2d Cir. 1995) and *Wegoland Ltd. v. NYNEX Corp.*, 27 F.3d 17 (2d Cir. 1994), provide an additional basis for dismissal of the Claims sought by Claimants. The Second Circuit in *Sun City Taxpayers' Association* affirmed the decision from the district court, which had declined the plaintiff's invitation to find a fraud exception to the filed rate doctrine. In determining whether the filed rate doctrine applied, the court focused on the impact the court's decision would have on agency procedures and rate determination. *Sun City Taxpayers' Ass'n v. Citizens Utils. Co.*, 847 F.Supp. 281, 291 (D. Conn. 1994). The Second Circuit in *Wegoland* recognized that the filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate-making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime. 27 F.3d at 21.

Therefore, having considered the policy objectives, the Court finds it is inappropriate to frustrate FERC's jurisdiction afforded by Congress. The Court lacks authority to impose a different rate than the one approved by a federal agent. Any other conclusion departing from this principle would undermine the filed rate doctrine. The Court, therefore, rejects Claimants' challenge to the application of the filed rate doctrine. Accordingly, the filed rate doctrine bars the relief sought by Claimants.

III. Conclusion

For the foregoing reasons, the Court concludes that the state law claims sought by Claimants concerning electricity market manipulation are preempted by the FPA and precluded by the filed rate doctrine. Therefore, the Court sustains the Debtors' objection to the Claims.

Counsel for the Debtors is directed to settle an order consistent with this opinion.

Dated: New York, New York
July 22, 2005

s/Arthur J. Gonzalez
UNITED STATES BANKRUPTCY JUDGE