

STATE OF NEW YORK
SUPREME COURT COUNTY OF MONROE

ROCHESTER GAS & ELECTRIC CORP.,

Plaintiff,

DECISION AND ORDER

v.

Ind # 2001/09621

NIAGARA MOHAWK POWER CORPORATION,
Defendant.

Defendant (NIMO) moves to dismiss the third, fourth and fifth causes of action of the amended complaint with prejudice based upon a lack of subject matter jurisdiction in light of the filed rate doctrine. Under the Federal Power Act (FPA) (FPA §§ 201, 205 and 206), the Federal Energy Regulatory Commission (FERC) has exclusive jurisdiction over all rates or charges related to the transmission and wholesale sale of electric energy in interstate commerce (see 16 U.S.C. §§ 824, 824d and 824e). Under the filed rate doctrine, "[t]he reasonableness of rates and agreements regulated by FERC may not be collaterally attacked in state or federal courts." Mississippi Power & Light Co. v. Mississippi ex rel. Moore, 487 U.S. 354, 375 (1988). The third, fourth and fifth causes of action of the amended complaint, as currently pled, are a collateral attack upon rates and an agreement regulated by FERC and thus NIMO's motion is granted. For the reasons stated in the conclusion, the order of dismissal is without prejudice.

FACTS

The parties are public utilities engaged in the transmission and wholesale sale of electricity in interstate commerce. As such, they are regulated by the FPA and subject to the jurisdiction of FERC. Before 1999, plaintiff (RG&E) purchased certain transmission services from NIMO at rates set forth in an agreement as amended from time to time, *i.e.*, Rate Schedule 176. Rate Schedule 176 was accepted for filing by FERC in August 1991.

In 1997, the parties reached an agreement settling a dispute over Rate Schedule 176, and in September 1997 that agreement was approved by FERC. The agreement settling that dispute anticipated the replacement of Rate Schedule 176 by an Exit Agreement. In June 1998, the parties executed the Exit Agreement subject to FERC's approval.

The Exit Agreement established certain annual payments to be made by RG&E to NIMO and obligated NIMO to provide certain Transmission Congestion Contracts (TCCs) to RG&E. In addition, the Exit Agreement provided for RG&E's leasing of certain transmission facilities from NIMO for rent included as part of the annual payments already described. Schedule 1 of the agreement listed the annual payments to be made to NIMO. It also showed the portions of the annual payments attributable to the transmission of electricity from RG&E's share of facilities known

as "Oswego 6" and "Nine Mile Point 2" (NMP-2). Schedule 2 of the agreement listed the six facilities to be leased by RG&E, the percentage of those facilities to be leased, and the lease term.

In July 1999, the parties tendered the Exit Agreement to FERC for filing pursuant to sections 205 and 296 of the FPA (16 U.S.C. §§ 824d and 824e). By letter dated August 12, 1999, FERC notified the parties that their submission was deficient in several respects, including the failure of the parties to "[p]rovide cost support for the annual payments" set forth in schedule 1 of the Exit Agreement. In September 1999, the parties addressed those deficiencies in a supplemental submission to FERC in which they explained the cost support as follows:

The schedule of payments in Schedule 1 to the Exit Agreement was arrived at by setting the payments in Year 1 equal to RG&E's current annual payments under Rate Schedule 176. The annual payments in Years 9 through June 2035 are equal to Niagara Mohawk's annual carrying costs associated with transmission facilities constructed by Niagara Mohawk to accommodate service currently provided to RG&E under Rate Schedule 176. The annual payments during the period June 2035 through June 2043 are also equal to such annual carrying costs, with the assumption that the Oswego 6 generating unit will be retired after June 2035, obviating the need for the transmission facilities associated with RG&E's share of Oswego 6's output. The annual payments during the period from Year 2 to Year 9 represent a straight-line transition from current annual payments to the payments representing annual carrying costs, in order to prevent an abrupt change in Niagara Mohawk's revenues.

In November 1999, FERC notified the parties that the Exit Agreement was accepted for filing.

Thereafter, a dispute arose between the parties regarding the continued obligation of RG&E to make payments under the Exit Agreement after the sale of its interests in Oswego 6 in October 1999, and NMP-2 in December 2000. In August 2001, RG&E commenced the within action against NIMO seeking judgment declaring that it was no longer obligated under the Exit Agreement to make those payments. In December 2001, NIMO filed a complaint with FERC alleging that RG&E had breached the Exit Agreement by refusing to make any more payments.¹

RG&E then moved in this Court for summary judgment. NIMO opposed the motion and cross-moved for an order dismissing the complaint or staying the action pursuant to the doctrine of primary jurisdiction. "The doctrine of 'primary jurisdiction' recognizes that an administrative agency, such as FERC, should be able to participate in decisions affecting a regulated industry,

¹ At issue in the dispute, which has yet to be finally resolved, is the following provisions of the Exit Agreement: (1) that part of section 2.3 that provides: "If ownership of ... [NMP-2] is transferred from RG&E, RG&E reserves the right to transfer the corresponding facility obligations including related facilities costs prescribed under Schedules 1 and 2 of this Agreement to the new owner(s)."; (2) that part of section 2.4 that provides: "If ... [NMP-2] is retired from service, RG&E shall have the right to terminate the associated facility obligations as described under footnotes 3 and 4 of Schedule 1. This termination provision shall not apply to any unit that is placed in cold standby or long term cold standby pursuant to NYPP procedure MP-2 or comparable ISO requirement."; and (3) a footnote to schedule 1 that provides: "If [NMP-2] is transferred or retired prior to 06/43, RG&E's payment to [NIMO] and RG&E's TCCs shall be reduced by the amounts shown on page 3 of this Schedule1."

even when the agency does not have exclusive jurisdiction." Gulf States Util. Co. v. Alabama Power Co., 824 F.2d 1465, 1472 (5th Cir. 1987), amended, 831 F.2d 557 (5th Cir. 1987). This Court (Stander, J.) agreed with NIMO's contention that FERC should first be given an opportunity to review the matter and, in February 2002, stayed the action for a period of 180 days. During that period, FERC fully reviewed the matter and declined to exercise jurisdiction. In dismissing the complaint before it, FERC indicated that "[c]onstruing the Exit Agreement's provisions concerning the reduction or termination of transmission facility payments is a straightforward matter of contract interpretation that is better left to New York courts." Niagara Mohawk Power Corp. v. Rochester Gas and Electric Corp., 98 FERC ¶61,307, at 7.

The Court, thereafter, denied RG&E's renewed motion for summary judgment and granted NIMO's cross motion to compel responses to outstanding discovery demands. The order denying summary judgment was affirmed by the Appellate Division (309 A.D.2d 1198 [4th Dept. 2003]) and substantial discovery followed. It was not until July 2004 that RG&E served an amended complaint with leave of the court, asserting additional causes of action, arising in part out of the disclosure during discovery that NIMO's transmission facility costs were grossly inflated, a characterization that the court now must accept as true for purposes of this motion. The three additional causes of action

at issue here are premised upon the allegation that, in negotiating the Exit Agreement, NIMO overstated its costs with respect to each of the six facilities listed in Schedule 2 that were to be leased by RG&E. RG&E alleges that, whereas NIMO represented that the "original book costs" of these six facilities was \$171 million, it was in fact \$37.4 million. The third cause of action is for fraud; the fourth cause of action is for negligent misrepresentation; and the fifth cause of action is for mutual mistake. Because the payment schedule set forth in the Exit Agreement is derived in part from NIMO's stated costs, RG&E seeks relief in the form of damages and reformation of the payment schedule and, in the alternative, rescission of the Exit Agreement and restitution.

In seeking dismissal of the third, fourth and fifth causes of action for lack of subject matter jurisdiction, NIMO contends that these causes of action do not involve an issue of contract interpretation subject to the doctrine of primary jurisdiction, but constitute a collateral attack on the rates embodied in the payment schedule, which, under the filed rate doctrine, may only be brought before FERC. RG&E contends that application of the filed rate doctrine to its claims is unwarranted and that the Court has jurisdiction over contract claims and contract formation issues. RG&E additionally contends that, if any part of the amended complaint is subject to dismissal under the filed

rate doctrine, it should be granted leave to replead to cure any the defect.

THE FILED RATE DOCTRINE

The filed rate doctrine bars not only regulated entities from charging rates for their services other than the rates properly filed with the appropriate regulatory authority, Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571, 577 (1981), but also the courts from becoming involved in the rate-making process. Wegoland LTD. v. NYNEX Corp., 27 F.3d 17, 19 (2d Cir. 1994). Its purpose is not only to prevent price discrimination (the so-called non-discrimination strand) but also to preserve the exclusive role of the regulatory authorities in approving rates as reasonable, a function that they alone are deemed competent to perform (the so-called nonjusticiability strand). Marcus v. AT&T Corp., 138 F.3d 46, 58 (2d Cir 1998).

Application of the filed rate doctrine in any particular case is not determined by the culpability of the defendant's conduct or the possibility of inequitable results. Nor does the doctrine's application depend on the nature of the cause of action the plaintiff seeks to bring. Rather, the doctrine is applied strictly to prevent a plaintiff from bringing a cause of action even in the face of apparent inequities whenever either the nondiscrimination strand or the nonjusticiability strand underlying the doctrine is implicated by the cause of action the plaintiff seeks to pursue.

Id. 138 F.3d at 58-59.

FERC "regulates the sale of electricity at wholesale in

interstate commerce," Eneergy Louisiana Inc. v. Louisiana Pub. Serv. Commn., 539 U.S. 39, 42 (2003) and has the "exclusive authority to determine the reasonableness of wholesale [electricity] prices." Mississippi Power & Light Co., 487 U.S. at 371. See Nanthala Power & Light Co. v. Thornburgh, 476 U.S. 953, 961 (1986). Thus, the filed rate doctrine applies to an exercise of authority by FERC. "[I]nterstate power rates filed with FERC or fixed by FERC must be given binding effect," Nanthala Power & Light Co., 476 U.S. at 962 and "[t]he reasonableness of rates and agreements regulated by FERC may not be collaterally attacked in state or federal courts." Mississippi Power & Light Co., 487 U.S. at 375.

FRAUD EXCEPTION TO THE FILED RATE DOCTRINE

RG&E contends that the filed rate doctrine is not applicable to claims, as here, that the jurisdictional rate was inflated by reason of fraud. RG&E relies on a footnote in a 1981 decision by the Supreme Court indicating that the Court reserved "for another day the question whether the filed rate doctrine applies in the face of fraudulent conduct." Arkansas Louisiana Gas Co., 453 U.S. at 583 n.13. RG&E principally cites in support of its opposition to NIMO's motion the Fifth Circuit decisions in Gulf States, 824 F.2d 1465, supra and Matter of Mirant Corp. v. Potomac Elect. Power Co., 378 F.3d 511 (2004).

Notwithstanding the footnote in Arkansas Louisiana Gas Co.,

the Supreme Court previously applied the filed rate doctrine in Montana-Dakota Util. Co. v. Northwestern Pub. Serv. Co., 341 U.S. 246, 251-252 (1951) even when one party allegedly defrauded the other in reaching an agreement as to the rates each would charge. After Arkansas Louisiana Gas Co., the Supreme Court discussed the decision in Montana-Dakota, clearly indicating that the allegations of fraud in that case had been irrelevant. Nanthala Power & Light Co., 476 U.S. at 962-963. The Court wrote:

In Montana-Dakota, two power companies with interlocking directorates and joint corporate officers each received some of the other's power, at rates that the FPC [Federal Power Commission, predecessor of FERC] had determined were reasonable. After separation, of the two companies' management, one of the companies alleged that it had paid unreasonably high rates for the electricity that it had received unreasonably low rates for the electricity that it had provided. The complaining company laid the blame for these allegedly fraudulent and unlawful rates at the door of the previously interlocking management, and brought suit in federal court.

This Court dismissed the claim. Emphasizing that Congress had given the FPC the right to determine the reasonableness of the rates, the Court stated:

[The complaining company] cannot separate what Congress has joined together. It cannot litigate in a judicial forum its general right to a reasonable rate, ignoring the qualification that it shall be made specific only by exercise of the Commission's judgment, in which there is some considerable element of discretion. It can claim no rate as a legal rate that is other than the file rate, whether fixed or merely accepted by the Commission, and not even a court can authorize commerce on other terms. ...' [341 U.S. at 251-252].

The existence of the interlocking management of the two utilities, and the resulting allegations of fraud were irrelevant.

Id., 476 U.S. at 963.

In another post Arkansas-Louisiana Gas Co. case decided the same term as Nanthala Power & Light Co., the Supreme Court gave no intimation that there is an exception for fraud. Square D Co. v. Niagara Frontier Tariff Bureau, 476 U.S. 409 (1986). In that case, the Supreme Court considered an alleged conspiracy to submit fraudulently inflated rates to a regulating agency. The Court held that an antitrust action could not be based on allegations that rates filed with that agency were fixed pursuant to an agreement prohibited by the Sherman Act.

These decisions, and others like them, have caused the Second Circuit to conclude that there is no fraud exception to the filed rate doctrine, whether that fraud is perpetrated upon the regulating agency, see Sun City Taxpayers' Assoc. v. Citizens Utilities Co., 45 F.3d 58, 61-62 (2d Cir. 1995), cert. denied, 514 U.S. 1064; Wegoland, 27 F.3d at 20-22, or another party. Marcus, 138 F.3d at 59-60.² As the Second Circuit explained in Wegoland:

² Other circuits have reached the same conclusion. 8th Circuit: H.J., Inc. v Northwestern Bell Tel. Co., 954 F.2d 485, 489 (1992), cert. denied, 504 U.S. 957. 9th Circuit: Transmission Agency of N. Cal. v. Sierra Pac. Power Co., 295 F.3d 918, 930 (2002), cert. denied, 539 U.S. 914. 11th Circuit: Taffet v Southern Co., 967 F.2d 1483, 1494-1495 (1992) (criminal fraud under Rico), cert. denied, 506 U.S. 1021.

If courts were licensed to enter this process under the guise of ferreting out fraud in the rate-making process, they would unduly subvert the regulatory agencies' authority and thereby undermine the stability of the system. For only by determining what would be a reasonable rate absent the fraud could a court determine the extent of the damages. And it is this judicial determination of a reasonable rate that the filed rate doctrine forbids.

Id. 27 F.3d at 21.

In New York, the Second Department has made a similar determination: "There is no 'fraud' exception to the filed rate doctrine, whether the alleged fraud be perpetrated on the regulatory agency or directly on consumers," Porr v. NYNEX Corp., 230 A.D.2d 564, 576 (2d Dept. 1997), lv. denied, 91 N.Y.2d 807. The Second Department cited with approval the district court's determination in Marcus, 938 F.Supp. 1158, 1170 that: "'As long as the carrier has charged and the plaintiff has paid the filed rate, what bars a claim is not the harm alleged, but the impact of the remedy sought. Any remedy that requires a refund of a portion of the filed rate - whether an award of damages for fraud on an agency or an award of damages for fraud on consumers - is barred.'" Porr, 230 A.D.2d at 573-574.

The Ninth Circuit recently addressed the applicability of the filed rate doctrine to an action seeking restitution and, alternatively, rescission or reformation on the grounds of mutual mistake, unilateral mistake, duress and unconscionability. Pub. Util. Dist. No. 1 of Gray's Harbor County Washington v. Idacorp,

Inc., 379 F.3d 641 (9th Cir. 2004). In that case, a retail provider sought to void its contract with a wholesale provider to purchase electrical power at "market rate," alleging that the market rate was agreed to only because the retail provider believed that the rate was based on a properly functioning market, when in fact the price resulted from a dysfunctional, manipulated market. The court determined that there was no jurisdiction to decide the issues raised as the relief sought would have required the district court to determine a fair price and FERC has preempted that field.

In the cases cited by RG&E, the Fifth Circuit has indicated that a court may set aside an energy contract obtained by fraud without running afoul of the filed rate doctrine if the order is based on a reason entirely separate and distinct from the filed rates. In Gulf States, 824 F.2d 1465, supra, in particular, one utility company contracted to buy electricity from another for a 10-year period under agreements filed with FERC. As a result of certain unforeseen market conditions and adverse regulatory action, the purchasing-utility sought to invoke a contractual provision permitting renegotiation of the agreements. After the selling-utility refused to renegotiate, the purchasing-utility brought suit to void its contractual obligations and for money damages. The Fifth Circuit determined that claims seeking to set aside the contracts on the ground that the selling-utility

committed fraud and deceptive trade practices by falsely promising to negotiate in good faith did "not interfere with the FERC's rate-making powers," provided that the district court did not set aside the contracts on the theory that the rates filed with FERC were too high. Id. at 824 F.2d 1472.

This determination is consistent with the Fourth Department's determination in Delaware County Electric Cooperative v Power Authority of State of New York, 96 A.D.2d 154 4th Dept. 1983), aff'd, 62 N.Y.2d 877 (1984). In that case, the plaintiff sought to void an energy agreement, which had been filed with FERC, on the ground that the parties to that agreement had failed to comply with certain hearing requirements under state law. The court held that there was no violation of the filed rate doctrine because resolution of the action would "not contravene congressional intent by altering the effective price schedule without necessary federal approval." Id. 96 A.D.2d at 160. There does not appear to have been any relief sought other than that the parties comply with the hearing requirements.

CONCLUSION

The overwhelming weight of authority supports dismissal of the third, fourth and fifth causes of action as currently pled pursuant to the filed rate doctrine. The filed rate doctrine is strictly applied when either of the two strands underlying the doctrine is implicated by the cause of action a plaintiff seeks

to pursue. Marcus, 138 F.3d at 58-59. It is of no moment that the nondiscriminatory strand of the filed rate doctrine may not be implicated here. Contrary to RG&E's contention, the doctrine is strictly applied whenever either strand underlying the doctrine is implicated. Marcus, 138 F.3d at 58-59. There is no support in the Supreme Court's decisions for plaintiff's view that the nonjusticiability strand is only a prophylactic measure designed to serve the interests of the nondiscrimination strand.

Here, the relief sought by plaintiff is damages and reformation and, alternatively, rescission and restitution. To determine the amount of damages or restitution, and certainly to reform the schedule of payments as RG&E has requested, the court would have to determine fair value, thereby infringing upon the exclusive authority of FERC to determine the reasonableness of rates and agreements subject to its regulation. See Mississippi Power & Light Co., 487 U.S. at 375. Even a claim for rescission ultimately would be met by a counterclaim for quantum meruit, again drawing the court into a determination of fair value. Because the nonjusticiability strand underlying the doctrine is implicated, these causes of action as pled must be dismissed.

Unlike the alleged fraud in Gulf States, which involved a failure to renegotiate a contract in good faith, the allegations underlying the three causes of action here directly implicate the rate-making function of FERC. Indeed, FERC rejected the initial

filing of the Exit Agreement, in part, because the parties failed to provide cost support for the annual payments set forth in Schedule 1 to the agreement. It was only after the parties indicated that the payments were based on NIMO's "annual carrying costs" for the facilities in question that FERC accepted the Exit Agreement for filing. Delaware County is distinguishable on this basis also. This also is why the issues underlying these three causes of action are different from the issues of contract interpretation previously referred to FERC.

It does not matter that the filed rate doctrine results in a windfall for NIMO, as RG&E contends. As the Second Circuit stated in Marcus, 138 F.3d at 58, "the doctrine is applied strictly ... even in the face of apparent inequities." See also, Maislin Indus., U.S., Inc. v. Primary Steel, 497 U.S. 116, 129 (1990) ("we have never accepted the argument that such 'equities' are relevant to the application of [the filed rate doctrine]").

Finally, RG&E contends in its memorandum of law that, if any part of the amended complaint is dismissed under the filed rate doctrine, it should be granted leave to replead to cure the defect. In particular, RG&E requests leave to replead a cause of action for declaratory relief with reference to the allegations underlying the three causes of action at issue here.

There is precedent supporting this contention. In Pub. Util. Dist. No. 1, 379 F.3d at 652-653, the Ninth Circuit granted

plaintiff leave to replead a cause of action for declaratory relief with reference to the contract formation issues in that case, reasoning that such a cause of action could be resolved without a "fair rate" determination by the court in violation of the filed rate doctrine. The court indicated that "[s]hould [the plaintiff] ... prevail and receive a determination that no valid contract exists, ... [plaintiff's] ... avenue of relief at that point, if any exists, would be with FERC." Id. 379 F.3d at 653. This is consistent with what the Supreme Court did in Arkansas Louisiana Gas Co. Although the damages and other relief ordered were set aside, id. 453 U.S. at 584 ("filed rate doctrine prohibits the award of damages"), the court left intact the liability judgments entered in state court. Id. 453 U.S. at 579 n.9, 584-85 ("[i]n all other respects, other than those relating to damages, the judgment . . . is affirmed"). In Wegoland, the court did not reach this issue, but its discussion focused on the damages remedy as the element of the fraud cause of action that offended the filed rate doctrine. Id. 27 F.3d at 21 ("extent of damages"). The same was true in Marcus, where the court affirmed dismissal of the "fraud claims to the extent that they seek compensatory damages and other pecuniary relief," dismissed "all of the remaining state law claims for damages," Marcus, 138 F.3d at 62 (emphasis supplied), and would have left intact the request for an injunction if fraud had otherwise been established

because the prayer for injunctive relief did not violate the filed rate doctrine. Marcus, 138 F.3d at 62-63.

Unfortunately, however, RG&E has not cross-moved to replead, but has only requested that relief in its memorandum. Indeed, at oral argument, RG&E speculated that there may be other forms of relief, besides declaratory and injunctive, that might be available and would not violate the filed rate doctrine. Under these circumstances the court's order granting NIMO's motion to dismiss is without prejudice.

SO ORDERED.

KENNETH R. FISHER
JUSTICE SUPREME COURT

DATED: January 21, 2005
Rochester, New York