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# Sherman Shorts Out: The Dimming of Antitrust Enforcement in the California Electricity Crisis

ROBERT B. MARTIN, III\*

*[M]en loved darkness rather than light, because their deeds  
were evil.*

—John 3:19

## INTRODUCTION

On an uncommon day in January 2001, the traffic lights went dark in San Francisco. Power was cut to police departments, fire stations, and state buildings. Students were trapped in elevators. Shopkeepers sold cigarettes by candlelight.<sup>1</sup>

From November 1999 through May 2001, California suffered an unprecedented electricity crisis, where state consumers experienced electrical blackouts and service interruptions on thirty-eight days.<sup>2</sup> Even when power was available, consumers faced a constant threat of further blackouts and interruptions.<sup>3</sup> The blackouts disrupted commerce, jeopardized public safety, and “directly affected approximately one-third of all Californians served by the three major investor-owned utilities [(IOUs)].”<sup>4</sup> William Massey, then Commissioner of the Federal Energy Regulatory

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\* J.D. Candidate, University of California, Hastings College of the Law, 2004; B.A. Claremont McKenna College, 1998. I would like to extend my greatest thanks to Dean Ashutosh Bhagwat, whose expertise and encouragement made this Note possible. Special thanks also to my family for their love and support, and to Brigid, of course, for bringing a little light to the law.

1. Maria L. La Ganga & John M. Glionna, *Life Goes On, Colder and Dimmer, As Lights Go Out*, L.A. TIMES, Jan. 18, 2001, at A1.

2. CAL. PUB. UTILITIES COMM’N, WHOLESALE GENERATOR INVESTIGATION REP. I (2002), available at <http://news.findlaw.com/hdocs/docs/energy/cpuc091702rpt.pdf> [hereinafter CPUC REPORT].

3. Jim Rossi, *The Electric Deregulation Fiasco: Looking to Regulatory Federalism to Promote a Balance Between Markets and the Provision of Public Goods*, 100 MICH. L. REV. 1768, 1768–69 (2002).

4. CPUC REPORT, *supra* note 2, at 9. During the crisis, the three major IOUs were Pacific Gas & Electric Company (PG&E), Southern California Edison Company (SCEC), and San Diego Gas & Electric Company (SDG&E), covering northern California, southern California, and San Diego, respectively. *Id.* at 8–9.

Commission (FERC), described the widespread chaos as an “apocalypse” in the power industry.<sup>5</sup>

The crisis brought massive increases in wholesale (and to some extent, retail) electricity prices. Before the crisis, wholesale electricity prices averaged between \$25 and \$30 per megawatt-hour.<sup>6</sup> During the height of the crisis from June 2000 to January 2001, average prices skyrocketed to between \$100 and \$294 per megawatt-hour.<sup>7</sup> Existing retail price caps forced the IOUs to absorb most of the cost increases, rather than passing them on to retail customers. This forced the IOUs “between a fiscal rock and a hard place,” rendering two of the IOUs insolvent and leading to the bankruptcy filing of PG&E.<sup>8</sup> Wholesale electricity generators (WEGs)<sup>9</sup> then began to refuse to sell electricity to the IOUs, resulting in a standoff which eventually required the California government to step in to ensure residents would still have electricity.<sup>10</sup>

Regarding the cause of the crisis, Dr. Paul L. Joskow, a professor at the Massachusetts Institute of Technology, wrote: “[t]here are five pri-

5. Nicholas W. Fels & Frank R. Lindh, *Lessons from the California “Apocalypse:” Jurisdiction over Electric Utilities*, 22 ENERGY L.J. 1, 1 (2001). FERC, a federal agency, regulates “the transmission of electric energy in interstate commerce and . . . the sale of electric energy at wholesale in interstate commerce.” 16 U.S.C. § 824(b)(1) (2000). In 1977, FERC succeeded the Federal Power Commission (FPC) which held equivalent authority over the transmission and sale of electricity in interstate commerce. See U.S. GEN. ACCOUNTING OFFICE, ENERGY MARKETS: CONCERTED ACTIONS NEEDED BY FERC TO CONFRONT CHALLENGES THAT IMPEDE EFFECTIVE OVERSIGHT 2 (2002), available at <http://www.gao.gov/new.items/do2656.pdf> [hereinafter GAO REPORT].

6. CPUC REPORT, *supra* note 2, at 12; John M. Broder, *California Power Failures Linked to Energy Companies*, N.Y. TIMES, Sept. 18, 2002, at A22. Generally, one megawatt-hour can power approximately 750 homes for one hour. Paul Joskow, *California’s Electricity Crisis*, 17 OXFORD REV. ECON. POL’Y 365, 375 (2001) [hereinafter Joskow I].

7. Fels, *supra* note 5, at 12.

8. Rossi, *supra* note 3, at 1778. As the energy markets in California were never fully deregulated, price caps remained on retail power sales, but did not exist on wholesale power sales. *Id.* During the price spikes, wholesale prices shot above the retail price cap, forcing the IOUs to pay far more for wholesale electricity than they were able to sell it for on the retail market. See *id.* The price variance led to both PG&E and SDG&E becoming insolvent. Joskow I, *supra* note 6, at 377. PG&E formerly declared bankruptcy on April 6, 2001. *Id.* at 365–66. For additional information on the IOUs’ travails, see generally *Pac. Gas & Elec. Co. v. Lynch*, 216 F. Supp. 2d 1016, 1042 (N.D. Cal. 2002).

9. The major WEGs in California during the crisis included: Duke Energy North America, LLC (Duke), Dynegy Power Marketing, Inc. (Dynegy), Mirant Americas Energy Marketing, LP (Mirant), Reliant Power Generation, Inc. (Reliant), and AES Corporation/Williams Energy Marketing and Trading Company (AES/Williams). See CPUC REPORT, *supra* note 2, at 8 n.1. Those five WEGs possessed a substantial market share within the California electricity generation market. See *id.* at 9 (stating the WEGs held a combined thirty-eight percent of the generation capacity of California market).

10. See Joskow I, *supra* note 6, at 366. From January to August 2001, California ultimately spent around \$10 billion in state funds to buy power from wholesale electricity generators. *Id.* It also entered into long-term wholesale electricity purchase contracts involving commitments exceeding \$60 billion. *Id.* Rejecting challenges by the California government, FERC recently upheld the validity of \$12 billion of those long-term contracts. Jonathan Peterson & Elizabeth Douglass, *Regulators Press Energy Firms but Uphold Disputed Contracts*, L.A. TIMES, June 26, 2003, at A1.

mary *interdependent* factors: (i) rising natural gas prices, (ii) a large increase in electricity demand in California, (iii) reduced imports from other states, (iv) rising prices for nitrogen oxide (NO<sub>x</sub>) emissions credits, and (v) market power problems."<sup>11</sup> This Note focuses upon that last factor: market power problems created by alleged market manipulations by the WEGs participating in the California electricity market.

Part I introduces the national move toward electricity deregulation and, in particular, California's implementation of its own deregulation scheme. It then summarizes publicly available indications of price manipulation and market power abuse by the WEGs.

Part II introduces the Sherman Antitrust Act and demonstrates why section 1 of the Sherman Act (hereinafter "section 1") is aptly suited to remedy past market power abuse within the California electricity market, and to deter future abuses. Part II also examines three antitrust "immunities" which limit the application of section 1 to the California crisis, including the filed rate doctrine which will likely bar private section 1 actions arising from the crisis.

Part II observes, however, the extremely poor fit of the filed rate doctrine to the facts of the crisis militates against its application to related section 1 actions. Due to that poor fit and the substantial criticism surrounding the doctrine, Part II suggests courts could construe the doctrine narrowly and avoid applying it to those actions.

Yet courts will likely adhere to the doctrine, and so Part III assesses the ability of FERC to remedy alleged market manipulations committed during the crisis and deter future abuses. As the Agency's powers appear largely inadequate to perform those functions, this Note calls upon Congress to overrule the filed rate doctrine, thus allowing application of section 1 with its concomitant remedies and deterrents, or alternatively to endow FERC with expanded authority to prevent similar market manipulations in the future.

## I. THE DEREGULATION OF THE ELECTRICITY INDUSTRY

Before the latter part of the twentieth century, federal and state governments largely regulated electricity markets as natural monopolies. Electricity markets are vital to the "public interest" due to the importance of electricity to the economy as a whole, and strict regulation was necessary to decrease the possibility of market power abuse arising from the natural monopolies.<sup>12</sup> By controlling electricity prices, profits, and en-

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11. Joskow I, *supra* note 6, at 377.

12. See Ray S. Bolze et al., *Antitrust Law Regulation: A New Focus for a Competitive Energy Industry*, 21 ENERGY L.J. 79, 79-80 (2000); Stuart M. Reynolds, Jr., *The Relationship of Antitrust Laws to*

try into the markets, the broad regulations sought to ensure “reasonable prices, non-discrimination and reliability” in the electricity markets.<sup>13</sup> Yet public support of the broad regulations began to erode because of an emerging view that competitive electricity markets could achieve greater benefits and efficiencies.<sup>14</sup> Beginning in the late 1970s, various legislative enactments began “deregulating” electricity markets to allow WEGs to compete for customers and for the market to establish prices.<sup>15</sup>

The basic theory behind deregulation was to move away from the use of regulated “cost-of-service” rates and replace them with competitively determined “market-based” rates. Cost-of-service rates established electrical retail prices by adding a utility’s cost with a reasonable rate of return.<sup>16</sup> Market-based rates established electrical retail prices through free-market competition.<sup>17</sup> This move to market-based rates placed a greater reliance on competition, “thus resulting in improved efficiencies, lower costs, and ultimately lower prices for consumers.”<sup>18</sup>

#### A. FERC PUSHES FOR DEREGULATION

Beginning in the late 1980s, FERC began encouraging deregulation in energy markets by granting WEGs “the authority to sell at ‘market-based rates’ if they could show that they lacked market power and that the prices at which they sold power would reflect the interplay of supply and demand in well-functioning markets.”<sup>19</sup> In 1996, through Orders 888 and 889, FERC adopted the “open access rule,” which required IOUs to open their respectively owned electricity transmission networks to their competitors.<sup>20</sup> This rule prevented IOUs from discriminating against their

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*Regulated Industries and Intellectual Property in the New Marketplace*, 4 TUL. J. TECH. & INTELL. PROP. 1, 12 (2002).

13. *Lynch*, 216 F. Supp. 2d at 1031; see Reynolds, *supra* note 12, at 12.

14. See *Lynch*, 216 F. Supp. 2d at 1031.

15. GAO REPORT, *supra* note 5, at 22; cf. Public Utility Regulatory Policies Act of 1978, 16 U.S.C. § 2601 (2000) (opening wholesale electric markets to non-utility electricity generators and allowing rates to be set not through cost-of-service regulation, but upon methods similar to competitive, market-based mechanisms).

16. *In re Cal. Wholesale Elec. Antitrust Litig.*, 244 F. Supp. 2d 1072, 1074 (S.D. Cal. 2003) (defining cost-of-service rates as “retail rates based upon cost and reasonable rate of return”); GAO REPORT, *supra* note 5, at 4 (basing cost-of-service rates upon a utility’s cost plus a fair return on investment).

17. See GAO REPORT, *supra* note 5, at 4.

18. *Id.* at 19; Reynolds, *supra* note 12, at 13.

19. Joskow I, *supra* note 6, at 367; see *Lynch*, 216 F. Supp. 2d at 1036 (noting FERC approval “of wholesale energy sales at market-based rates . . . in an effort to develop competitive bulk power markets”). FERC estimated deregulation of the wholesale electricity industry would result in annual savings from \$3.8 billion to \$5.4 billion. Jeffery D. Schwartz, Comment, *The Use of the Antitrust State Action Doctrine in the Deregulated Electric Utility Industry*, 48 AM. U. L. REV. 1449, 1451 (1999).

20. See GAO REPORT, *supra* note 5, at 23.

competitors by denying them equal access to the transmission networks used in the transmission and distribution of wholesale electricity.<sup>21</sup>

To further this policy, FERC encouraged IOUs to “functionally unbundle” their generation and transmission operations, where IOUs would separate their previously vertically integrated generation, transmission, and distribution networks.<sup>22</sup> The IOUs would retain ownership of their transmission and distribution networks, but the generation of electricity was left to independent, non-IOU WEGs.<sup>23</sup> FERC also encouraged establishment of Independent System Operators (ISOs).<sup>24</sup> IOUs would transfer operating control of their transmission facilities to an ISO, which would “control the power system . . . without special interest” as it would “own no generation, transmission or load.”<sup>25</sup>

FERC Order 888 involved a preemptive assertion of authority to require WEGs subject to its jurisdiction to adopt a standard tariff for transmission service to IOUs. FERC, however, limited its jurisdiction to WEGs only, leaving states to regulate IOUs and retail customers.<sup>26</sup>

## B. CALIFORNIA’S DEREGULATION OF ITS ELECTRICITY MARKET

Beginning with the California Public Utilities Commission’s (CPUC) 1995 decision to deregulate the state’s \$23 billion electricity industry, California became “the first state to deregulate retail power markets on a mass scale.”<sup>27</sup> In 1996, the California Legislature unanimously enacted the Public Utilities-Electrical Restructuring Assembly Bill 1890 (AB 1890), approving most of CPUC’s initiative and formally deregulating the electricity markets.<sup>28</sup> Through deregulation, the state legislature intended to benefit retail electricity customers by moving to “a framework under which competition would be allowed in the supply of electric power.”<sup>29</sup>

21. See *id.* Upon issuance of FERC Order 888, Elizabeth Anne Moler, the FERC Chairwoman at the time, stated “the future is here—and the future is competition.” Schwartz, *supra* note 19, at 1452.

22. See 18 C.F.R. pts. 35 & 385 (1996) [hereinafter FERC Order 888]; 18 C.F.R. pt. 37 (1996) [hereinafter FERC Order 889]; GAO REPORT, *supra* note 5, at 23.

23. *In re* Cal. Wholesale Elec. Antitrust Litig., 244 F. Supp. 2d 1072, 1074–75 (S.D. Cal. 2003).

24. See FERC Order 888, 18 C.F.R. pts. 35 & 385 (1996); GAO REPORT, *supra* note 5, at 23.

25. GAO REPORT, *supra* note 5, at 23.

26. The U.S. Supreme Court affirmed that FERC’s jurisdiction could extend to wholesale power generation even where the generating plant and retail consumer are within the same state. See *N.Y. v. Fed. Energy Regulatory Comm’n*, 535 U.S. 1, 20–21 (2002); Rossi, *supra* note 3, at 1783–84.

27. Rossi, *supra* note 3, at 1768.

28. See Public Utilities-Electrical Restructuring, A.B. No. 1890, 1995–1996 Reg. Sess. (Cal. 1995), 1996 Cal. Stat. 854 (1996) [hereinafter AB 1890]; Robert C. Fellmeth, *Plunging Into Darkness: Energy Deregulation Collides with Scarcity*, 33 *Loy. U. Chi. L.J.* 823, 832 (2002).

29. AB 1890, 1996 Cal. Stat. 854, § 10. The California Legislature’s intent to create a competitive energy market pervades AB 1890. See § 1(a) (AB 1890 will “ensure . . . [a] transition to a more competitive electricity market structure” and “create[] a new market structure that provides competitive, low cost and reliable electric service.”); § 10 (“Generation of electricity should be open to competition

Similar to FERC Order 888, AB 1890 required IOUs to separate their generation operations from their transmission and distribution operations.<sup>30</sup> To facilitate this unbundling, AB 1890 created two entities to operate the new competitive electricity market: the California Independent System Operator (CAISO) and the California Power Exchange (CAPX).<sup>31</sup>

CAISO<sup>32</sup> served as an independent operator of the electricity transmission network. IOUs transferred operating control (but not ownership) of their transmission facilities to CAISO,<sup>33</sup> which then controlled the statewide transmission grid and directed the necessary purchases of electricity to ensure the reliable operation of the electrical grid.<sup>34</sup>

CAPX<sup>35</sup> operated “an efficient, competitive auction to meet electricity loads of [CAPX] customers.”<sup>36</sup> Open on a nondiscriminatory basis to all WEGs, CAPX matched bids by the WEGs for the supply of wholesale electricity with demand bids by the IOUs.<sup>37</sup> Through the bid-matching, the CAPX auction determined short-term wholesale electricity prices

and utility generation should be transitioned from regulated status to unregulated status through means of commission-approved market valuation mechanisms.”).

30. AB 1890, 1996 Cal. Stat. 854, § 10.

31. AB 1890, 1996 Cal. Stat. 854, § 1(c); see § 10 (“competition will best be introduced by the creation of an Independent System Operator and an independent Power Exchange”). Pursuant to FERC Order 888 governing transmission operators, FERC held regulatory authority over both CAISO and CAPX. See *Pac. Gas & Elec. Co. v. Lynch*, 216 F. Supp. 2d 1016, 1020 (N.D. Cal. 2002); *In re Cal. Wholesale Elec. Antitrust Litig.*, 244 F. Supp. 2d 1072, 1074–75 (S.D. Cal. 2003); see generally FERC Order 888, 18 C.F.R. pts. 35 & 385 (1996); Joskow I, *supra* note 6, at 371. California retained regulatory jurisdiction over the delivery of retail electricity over the IOUs’ transmission and distribution systems. AB 1890, 1996 Cal. Stat. 854, § 10. Economists generally recognize the wholesale power generation market is better-suited to competition, while local transmission and distribution networks are more apt to exist as natural monopolies. See Rossi, *supra* note 3, at 1775 (citing RICHARD F. HIRSH, *POWER LOSS: THE ORIGINS OF DEREGULATION AND RESTRUCTURING IN THE AMERICAN ELECTRIC UTILITY SYSTEM* 101–17 (1999)).

32. Pursuant to AB 1890, CAISO is a non-profit, public benefit corporation. 1996 Cal. Stat. 854, § 1(c); Joskow I, *supra* note 6, at 369, 371.

33. AB 1890, 1996 Cal. Stat. 854, § 10.

34. AB 1890, 1996 Cal. Stat. 854, § 1(c); see *Cal. Wholesale Elec.*, 244 F. Supp. 2d at 1074–75; Joskow I, *supra* note 6, at 371–72; cf. GAO REPORT, *supra* note 5, at 23 n.11 (encouraging IOUs to commit operating control of transmission facilities to ISOs to protect against improper exercise of “special interest[s]”); Fels, *supra* note 5, at 8 (CAISO “responsible for assuring non-discriminatory access and system reliability”).

35. CAPX is also a non-profit corporation, AB 1890, 1996 Cal. Stat. 854, § 1(c), but operates independently of CAISO. See Fels, *supra* note 5, at 8. Due to the California crisis, CAPX stopped operating in January 2001 and subsequently declared bankruptcy on March 9, 2001. See Fels, *supra* note 5, at 12; Joskow I, *supra* note 6, at 383.

36. AB 1890, 1996 Cal. Stat. 854, § 1(c).

37. *Id.*

through a competitive, market-based rate structure.<sup>38</sup> AB 1890 required all IOUs to fill the vast majority of their day-ahead electricity demand through CAPX.<sup>39</sup>

By holding control of the transmission and distribution networks, CAISO and CAPX essentially operated as a clearinghouse for the sale and purchase of electricity. WEGs would sell electricity to the IOUs through CAPX, and CAISO would safeguard the balance of the electricity grid by procuring power to maintain the stability of the grid if CAPX did not meet customer demand.<sup>40</sup>

Pursuant to FERC regulatory authority,<sup>41</sup> CAISO and CAPX filed tariffs with FERC. The Agency reviewed and approved those tariffs in accordance with their responsibility to ensure “just and reasonable rates.”<sup>42</sup> The tariffs “comprised the rules for trading in the California wholesale electricity markets” and bound the WEGs in their participation within those markets.<sup>43</sup> The WEGs also filed tariffs with FERC, seeking authorization to sell electricity on CAPX and other wholesale markets at wholesale rates.<sup>44</sup>

In granting these [tariffs], FERC applied its standard analysis, looking at the share of generation capacity controlled by the [WEG applicant] and its affiliates in a geographic market usually comprised of northern California, southern California, or both. This form of analysis did not entail any inquiry into overall supply and demand projections, nor did it examine how the market as a whole would function under anticipated conditions.<sup>45</sup>

None of the tariffs approved by FERC were tested on judicial review.<sup>46</sup>

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38. *Cal. Wholesale Elec.*, 244 F. Supp. 2d at 1074–75; see Joskow I, *supra* note 6, at 369 (noting CAPX sold power on a day-ahead and hour-ahead basis).

39. Joskow I, *supra* note 6, at 369 (CAPX accounted for eighty percent of retail electricity sales in California); see also *Pac. Gas & Elec. Co. v. Lynch*, 216 F. Supp. 2d 1016, 1020 (N.D. Cal. 2002).

40. See *Cal. Wholesale Elec.*, 244 F. Supp. 2d at 1074–75; Paul Joskow & Edward Kahn, *A Quantitative Analysis of Pricing Behavior in California's Wholesale Electricity Market During Summer 2000*, ENERGY J., Oct. 1, 2002, at 1, 8 [hereinafter Joskow II].

41. See 16 U.S.C. § 824d(c) (2000) (all rates for transmission and sale of wholesale electricity must be filed with FERC).

42. *Cal. Wholesale Elec.*, 244 F. Supp. 2d at 1074–75; see also *Lynch*, 216 F. Supp. 2d at 1037 (noting FERC approved market-based wholesale electricity sales based upon a required retail rate freeze during the deregulation transition period and the mandatory sale of energy by WEGs through CAPX).

43. *Cal. Wholesale Elec.*, 244 F. Supp. 2d at 1074–75; Fels, *supra* note 5, at 9–10. A tariff is a legally binding document (upon approval) filed by a regulated firm with its regulatory agency, setting forth prices and policies the firm offers to its customers. See *Cost Mgmt. Servs. Inc. v. Wash. Natural Gas Co.*, 99 F.3d 937, 940 n.1 (9th Cir. 1996).

44. *Lynch*, 216 F. Supp. 2d at 1020.

45. Fels, *supra* note 5, at 10.

46. *Id.*



### C. INDICATIONS OF MARKET POWER ABUSE BY WHOLESALE ELECTRICITY GENERATORS IN CALIFORNIA'S DEREGULATED ELECTRICITY MARKET

Even before the crisis ended, commentators pointed to numerous causes to explain the significant increases in electricity prices.<sup>47</sup> This Note focuses on one of those factors: the allegation that WEGs with significant market power conspired to increase prices by limiting their electrical generation output. The potential for manipulation initially appears because electricity markets are particularly prone to market power abuse.<sup>48</sup> Electricity cannot be stored, substantial entry barriers exist in the market (which results in a fixed number of generating plants), and consumers are reluctant to cut their power usage in response to price increases.<sup>49</sup> Thus, "small supply decreases can cause very large price increases; so each entity with significant market share has an incentive to unilaterally raise market prices by restricting its own output."<sup>50</sup> When multiple firms collude to restrict output, prices increase even higher.<sup>51</sup>

Following an investigation into the crisis, FERC released a report stating "market manipulations contributed significantly" to price increases during the crisis.<sup>52</sup> The report included examples of two WEGs

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47. Other commentators have suggested California's deregulation process resulted in flawed market rules which then caused the crisis. One of the obvious flaws was the preservation of price caps upon retail sales and the removal of caps from wholesale sales. When wholesale prices exceeded the retail price caps, PG&E and SDG&E suffered millions of dollars in losses by selling electricity for less than it cost to purchase it. See Rossi, *supra* note 3, at 1778. FERC noted in a November 1, 2000 report California's new electricity market structure was "seriously flawed" and had "caused, and continue[s] to have the potential to cause, unjust and unreasonable rates for short-term energy . . . under certain conditions." Fels, *supra* note 5, at 13 (quoting San Diego Gas & Elec. Co., 93 F.E.R.C. ¶¶ 61,121, 61,349-50 (2000)). Several scholars have also explored the impact of the flawed market rules upon the crisis. See, e.g., Joskow I, *supra* note 6, at 369-70 (concluding California's deregulation resulted in "the most complicated set of wholesale electricity market institutions ever created on earth and with which there was no real-world experience"); Rossi, *supra* note 3, at 2 (noting "wrong-headed deregulation policies contributed to California's crisis"); Michael A. Yuffee, *California's Electricity Crisis: How Best to Respond to the "Perfect Storm"*, 22 ENERGY L.J. 65, 65 (2001) (noting FERC and CPUC have identified "significant flaws" in California's deregulation plan). Indeed, immediately after the crisis began, several sources attributed the cause of the crisis to the deregulation process itself (i.e., "flawed market rules"). See, e.g., CPUC REPORT, *supra* note 2, at 59; Rossi, *supra* note 3, at 1769. Blaming many of the crisis's symptoms upon the favoring of competitive markets over government regulation, some have called for a retreat from deregulation. See Rossi, *supra* note 3, at 1769.

48. See Joskow II, *supra* note 40, at 28-29. The California Legislature exhibited its prescience by recognizing during the deregulation process "[t]here is a need to ensure that no participant in these new market institutions has the ability to exercise significant market power so that operation of the new market institutions would be distorted." AB 1890, 1996 Cal. Stat. 854, § 10.

49. See CPUC REPORT, *supra* note 2, at 59.

50. *Id.* at 58.

51. *Id.*

52. FED. ENERGY REGULATORY COMM'N, FINAL REPORT ON PRICE MANIPULATION IN WESTERN MARKETS: FACT-FINDING INVESTIGATION OF POTENTIAL MANIPULATION OF ELECTRIC AND NATURAL GAS PRICES, DOC. NO. PA02-2-000, at I-1 (2003) (hereinafter "FERC FACT-FINDING REPORT").

“coordinating their efforts to manipulate western electricity prices.”<sup>53</sup> The report also stated that multiple WEGs participated in trading strategies designed to “game” the market and increase prices.<sup>54</sup> The trading strategies, described in detail in confidential memoranda released by Enron Corporation,<sup>55</sup> carried colorful names like “Ricochet,” “Fat Boy,” and “Death Star.”<sup>56</sup> “Load Shift,” a strategy which increased congestion in electricity transmission, was especially lucrative for Enron, earning the corporation around \$30 million in profits during fiscal year 2000.<sup>57</sup> FERC indicated Enron was not alone in using the strategies.<sup>58</sup>

[T]he evidence indicates that Enron, on its own, could not have implemented its trading strategies. It was only with the willing cooperation of others that these strategies could have been executed. Through Enron’s direction, other entities both inside and outside California made business decisions that capitalized on market conditions in an effort to maximize profits from their assets on a coordinated basis. The coordination activity of Enron and its partners clearly changed market outcomes in variety of ways. . . . Profits from this activity were typically shared.<sup>59</sup>

Political response to the report was swift. California Senator Dianne Feinstein called upon U.S. Attorney General John Ashcroft “to investigate fraud and antitrust allegations made by” California. Feinstein stated

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53. *Id.* at VI-55. FERC appears to have hedged its conclusions, however, by noting the report reflects the views of Staff only.

It has not been considered or adopted by the full Commission. In addition, whenever this Report concludes that prices were or appear to have been manipulated, it does so in the context of determining whether rates were unjust and unreasonable under the Federal Power Act . . . .

*Id.* at ES-4.

54. Jonathan Peterson & Nancy Rivera Brooks, *Calif. Report Widens Blame in Energy Plot*, L.A. TIMES, Mar. 3, 2003, at A1.

55. Memorandum from Christian Yoder & Stephen Hall, Stoel Rives LLP, to Richard Sanders, Assistant General Counsel, Enron Corp. 1 (Dec. 6, 2000), available at <http://news.findlaw.com/hdocs/docs/enron/stoelrives120600mem.pdf> [hereinafter Enron Memorandum].

56. “Ricochet” allowed WEGs to avoid “price caps by selling power out of state and then trading it back in again.” Peterson, *supra* note 54, at A1. “Fat Boy” entailed a WEG informing CAISO that it planned to use more power than it actually did, and in the process receiving extra payments. “Death Star” created false congestion on the electrical grid, allowing WEGs to receive a premium for easing the problem. *Id.*; Nancy Vogel, *E-mail Suggests DWP Role in Trading Scheme*, L.A. TIMES, June 23, 2002, at B1; Enron Memorandum, *supra* note 55, at 4-7.

57. Enron Memorandum, *supra* note 55, at 5.

58. FERC FACT-FINDING REPORT, *supra* note 52, at VI-35.

59. *Id.* at VI-43; see Peterson, *supra* note 54, at A1. Indeed, the confidential memoranda expressly noted “other market participants” were also using the strategies. Enron Memorandum, *supra* note 55, at 1.

the report “provide[s] significant evidence that there was a concerted effort to boost company profits at the expense of consumers.”<sup>60</sup>

FERC did not specifically consider whether WEGs physically withheld actual generation output, a tactic which would reduce the supply of available electricity and lead to higher prices.<sup>61</sup> California officials have been increasingly vocal, however, in their accusations of such physical withholding.<sup>62</sup> For example, a CPUC report suggested California’s five largest WEGs withheld capacity during the crisis by intentionally shutting down their generating plants.<sup>63</sup> The report hinted the unusual number of plant outages during the crisis, well above historical averages, showed anticompetitive motive.<sup>64</sup> The State later alleged Dynegy shut down one of their generators “for repairs but kept it shut down after repairs were completed ‘to force prices up.’”<sup>65</sup> California also cried conspiracy in allegations of collusion between Sempra Energy and Shell Oil affiliate Coral Energy.<sup>66</sup> Accusations of physical withholding echoed in other sources.<sup>67</sup>

60. Nancy Rivera Brooks, *FERC Releases Flood of Evidence in Its Case Against Power Suppliers*, L.A. TIMES, Mar. 27, 2003, at C1.

61. FERC FACT-FINDING REPORT, *supra* note 52, at ES-2. FERC noted it would address the issue of physical withholding separately, although it did describe one occurrence where Reliant appeared to have physically withheld generation over a two-day period. *Id.* at VI-54.

62. See David Barboza, *A Big Victory by California in Energy Case*, N.Y. TIMES, Nov. 12, 2002, at C1.

63. See CPUC REPORT, *supra* note 2, at 44. According to CPUC, on the days when blackouts or service interruptions occurred, thirty-seven percent to forty-six percent of the generators’ capacity was either out of service or not made available. *Id.* at 3. Service interruptions differ from blackouts in that certain large commercial and industrial customers agreed beforehand to limited service interruptions in exchange for lower rates. *Id.* at 1. In the event CAISO had to shut off power, those customers lost access to power for a set period of time and shut down operations for that period. *Id.*

64. *Id.* at 44. The report qualifies its conclusions by stating it “makes *no* finding that any of the blackouts or service interruptions was unavoidable.” *Id.* at 3, 20, 50 (noting the study “does not attempt to answer fully the question of why, at each plant and for each hour, the generators did not generate all available power during each service interruption hour” and more investigation is required to assess the WEG’s roles in contributing to the blackouts). The five named companies also responded to the report by stating “there were legitimate reasons for the service disruptions and that their plants were running as hard or harder during the crisis as before or since.” Broder, *supra* note 6, at A22.

65. Brooks, *supra* note 60, at C1.

66. *Id.*

67. See, e.g., Joskow I, *supra* note 6, at 381 (finding power plants had “unusually large amounts of generating capacity . . . out of service and [were] unavailable to supply electricity”); PAUL JOSKOW & EDWARD KAHN, IDENTIFYING THE EXERCISE OF MARKET POWER: REFINING THE ESTIMATES 3 (2001) [hereinafter JOSKOW III] (suggesting forced outages resulted from powerful “incentive to withhold” and that “observed behavior exceeds historic outage norms”). CPUC also cited “study after study” indicating generators used their market power to raise prices. CPUC REPORT, *supra* note 2, at 60 (citing three studies). Professors Joskow and Kahn also stated only two reasons could exist for the plant shutdowns: either “unusual operational problems” or a strategy to withhold power from the market “to increase prices.” Joskow II, *supra* note 40, at 3–4. Similarly, a report prepared by FERC suggested employees of AES/Williams improperly prolonged the shutdown of a generating plant to obtain premium pricing

Other indications of improper manipulation appeared in adjudicative settings. A FERC initial decision found that El Paso Corporation (El Paso) unlawfully used its market power to withhold natural gas from the California natural gas market.<sup>68</sup> El Paso subsequently reached a \$1.69 billion settlement with several western states, including California, over allegations of price manipulation.<sup>69</sup> AES/Williams paid over \$400 million to settle several civil claims of driving up prices and overcharging customers.<sup>70</sup> FERC ordered Williams Energy Marketing & Trading of Tulsa, a smaller energy producer, to pay CAISO \$8 million in refunds for improperly taking generating plants off-line and artificially limiting supply.<sup>71</sup> Dynegy paid \$5 million to the federal government to settle a price manipulation investigation.<sup>72</sup> Reliant paid \$13.8 million in a settlement with FERC regarding allegations of physical withholding over a two-day period.<sup>73</sup> And prosecutors accused two Enron traders, Timothy Belden and John M. Forney, of wire fraud and conspiracy charges for manipulating electricity prices during the crisis.<sup>74</sup>

Finally, Dr. Joskow and Edward Kahn prepared several reports analyzing wholesale electricity prices during the crisis. They discovered a significant gap between estimated competitive benchmark prices and the actual market prices charged over the summer of 2000.<sup>75</sup> The size of the gap was significant enough for Joskow and Kahn to suggest market manipulation influenced electricity price increases during the crisis.<sup>76</sup>

We find that [the WEGs] withheld capacity far in excess of what can be explained by historical outage rates or demand for ancillary services. High-cost and high-emissions units ran while more efficient units remained idle. The output gap was especially large on the highest-

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from CAISO. See FED. ENERGY REGULATORY COMM'N, NON-PUBLIC APPENDIX TO ORDER DIRECTING WILLIAMS ENERGY MARKETING & TRADING COMPANY AND AES SOUTHLAND, INC. TO SHOW CAUSE, DOC. NO. IN01-3-000, at 2, 9-10 (2002), available at <http://news.findlaw.com/hdocs/docs/ferc/williamsaes115020sc.pdf>; Toby Eckert, *Details of Shutdown Allegations Revealed*, SAN DIEGO UNION-TRIB., Nov. 16, 2002, at C1.

68. Pub. Util. Comm'n of State of Cal., 100 F.E.R.C. ¶¶ 63,041, 65,157 (2002). Generally, natural gas and electricity markets are separate markets, but the two markets are converging within the power industry. See GAO REPORT, *supra* note 5, at 26, 36, 41. El Paso subsequently shut down its natural-gas trading operation in November 2002, partly attributable to investigations into its trading practices. Alexei Barrionuevo, *El Paso Executive Quits Energy Firm*, WALL ST. J., Jan. 6, 2003, at A6.

69. See *El Paso Settles with California Over Gas Prices*, N.Y. TIMES, Mar. 22, 2003, at C3.

70. See Barboza, *supra* note 62, at C1.

71. See Fellmeth, *supra* note 28, at 841.

72. Christian Berthelsen, *Call for Oversight of Natural Gas*, S.F. CHRON., Jan. 30, 2003, at B1.

73. See FERC FACT-FINDING REPORT, *supra* note 52, at VI-54.

74. See Barboza, *supra* note 62, at C1 (noting Belden pleaded guilty to charges of conspiracy); Nancy Rivera Brooks, *FBI Arrests Former Enron Energy Trader*, L.A. TIMES, June 4, 2003, at C1 (noting charges against Forney).

75. Joskow II, *supra* note 40, at 14-15.

76. *Id.*

demand days. These results are consistent with the withholding behavior for strategic rather than engineering reasons that are expected given [the WEGs'] incentives.<sup>77</sup>

Joskow and Kahn wavered, however, on whether the WEGs conspired to restrict generating capacity. Circumstances suggested WEGs cooperated in restricting output in order to cause larger increases in prices.<sup>78</sup> Yet because of tight demand elasticity in electricity markets, especially when demand is high and supply is limited, an individual WEG can cause large price increases by restricting only a small amount of capacity.<sup>79</sup> Such unilateral behavior could lead to prices significantly above competitive levels during high demand periods.<sup>80</sup>

It is still unclear whether the WEGs engaged in collusive behavior to manipulate the electricity markets, and this Note draws no conclusion as to that fact. For purposes of discussion, however, this Note assumes such collusive behavior did exist and could be proved in a section 1 action arising from the crisis.

## II. THE SHERMAN ANTITRUST ACT

Free markets are no stranger to anticompetitive manipulation by those seeking higher profits. Long-standing policy, however, views such conduct as contrary to basic principles of free trade and fairness to other parties participating in the markets. Antitrust laws protect those basic principles and would likely benefit the operation of newly deregulated electricity markets.<sup>81</sup> Indeed, considering the developing antitrust issues in California's deregulated electricity market, it appears some market participants expect that protection.<sup>82</sup>

77. Joskow III, *supra* note 67, at 2, 18. Indeed, Joskow estimated that during summer 2000, "at least a third of the wholesale price can be attributed to market power . . . after accounting for changes in fundamental supply and demand conditions." Joskow I, *supra* note 6, at 381. Professor Fellmeth estimated the total overcharges from 2000 and 2001 at \$55 billion. See Fellmeth, *supra* note 28, at 860.

78. See Joskow II, *supra* note 40, at 19.

79. See Joskow I, *supra* note 6, at 374.

80. See *id.* at 374, 381 (noting a combination of inelastic demand and tight supplies permitted generators "to exercise market power *without* engaging in collusion"); Joskow III, *supra* note 67, at 3 n.5 ("We are not saying collusion did not occur . . . but only that collusion would not be necessary for market power to be exercised.").

81. See Bolze, *supra* note 12, at 80-81; Reynolds, *supra* note 12, at 13.

82. See Joskow II, *supra* note 40, at 28-29; Reynolds, *supra* note 12, at 11-12. On November 29, 2000, a San Diego superior court saw the first lawsuit filed under section 1 for alleged antitrust violations by the WEGs. See Fellmeth, *supra* note 28, at 837. California Attorney General Bill Lockyer also filed suit, alleging violations of state antitrust laws and unfair business practice statutes. See *Cal. ex rel. Lockyer v. Mirant Corp.*, No. C-02-1787-VRW, 2003 WL 21321243, at \*4-\*5 (N.D. Cal. Mar. 25, 2003); see also *In re Cal. Wholesale Elec. Antitrust Litig.*, 244 F. Supp. 2d 1072, 1074-75 (S.D. Cal. 2003) (considering antitrust claims arising from alleged wholesaler collusion in California electricity market).

## A. THE PRINCIPLES AND POLICIES BEHIND SECTION 1 OF THE SHERMAN ACT<sup>83</sup>

Couched in broad terms, section 1 declares in pertinent part: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is declared to be illegal."<sup>84</sup> Section 1 prohibits only *unreasonable* restraints of trade.<sup>85</sup> Specific types of unreasonable restraints are discussed below in Part II.B.

Congress considered numerous policies in enacting the Sherman Act. Paramount above them all is the protection of competition.<sup>86</sup> "Anti-trust laws in general, and the Sherman Act in particular, are the Magna Carta of free enterprise. They are as important to the preservation of economic freedom and our free-enterprise system as the Bill of Rights is to the protection of our fundamental personal freedoms."<sup>87</sup> The Act relies upon the premise that free competition yields the best prices, quality, allocation of economic resources, and the greatest progress, while preserving an "environment conducive to the preservation of democratic political and social institutions."<sup>88</sup>

In conjunction with the Clayton Act, both individuals and governmental entities can bring actions under the Sherman Act. The Depart-

83. See Sherman Act § 1, 15 U.S.C. § 1 (2003). Another oft-used provision within the Sherman Act is section 2, which proscribes the exercise of actual monopoly power or the attempted use of monopoly power. Sherman Act § 2, 15 U.S.C. § 2 (2003). A monopoly or attempted monopolization claim brought under section 2, however, requires the defendant to possess a significant market share, generally within the range of seventy percent to ninety percent. See *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 424 (2d Cir. 1945). The five major WEGs in California, however, held a *combined* market share of anywhere from thirty-eight percent to forty-four percent. See CPUC REPORT, *supra* note 2, at 8 n.1. That combined market share is insufficient to establish a monopoly or attempted monopolization claim under section 2, much less the lower individual market shares of each WEG. Thus, this Note focuses solely upon application of section 1.

84. 15 U.S.C. § 1 (2003). Congress purposefully used broad language to enable the courts to adapt section 1 to changed conditions and economic evolution. By conferring such a broad mandate, courts can draw upon lessons of accumulated experience and common-law tradition in interpreting section 1. See, e.g., *Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 688 (1978); *United States v. E.I. Du Pont de Nemours & Co.*, 351 U.S. 377, 386 (1956); *Apex Hosiery Co. v. Leader*, 310 U.S. 469, 489 (1940) ("[i]n consequence of the vagueness of its language, perhaps not uncalculated, the courts have been left to give content to the statute . . .") (footnote omitted).

85. *Standard Oil Co. v. United States*, 221 U.S. 1, 59-61 (1911).

86. See, e.g., *Gordon v. N.Y. Stock Exch., Inc.*, 422 U.S. 659, 689 (1975); *Standard Oil Co. v. Fed. Trade Comm'n*, 340 U.S. 231, 248-49 (1951).

87. *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 610 (1972).

88. *Northern Pacific Ry. Co. v. United States*, 356 U.S. 1, 4 (1958); Bolze, *supra* note 12, at 82 (antitrust policy assumes "free market forces and competition will maximize the wealth of the nation as a whole."); cf. *Nat'l Soc'y of Prof'l Eng'rs*, 435 U.S. at 692, 695 (subject to exceptions defined by statute, public interest always favors competition, and "the statutory policy precludes inquiry into the question whether competition is good or bad.").

ment of Justice (DOJ) generally enforces criminal violations of section 1, which are considered felonies and can include fines up to \$350,000 for individuals or \$10 million for corporations, and prison terms for individuals for up to three years.<sup>89</sup>

The primary deterrent force behind section 1 is the treble damages civil action brought by private individuals. Any person (including a corporation)<sup>90</sup> who has been injured in its "business or property" by reason of an antitrust violation can pursue a civil claim and recover treble damages, the costs of the lawsuit, and attorney's fees.<sup>91</sup> This provision is one of the chief tools in encouraging antitrust enforcement and serves as "a crucial deterrent to potential violators."<sup>92</sup> "The purposes of the antitrust laws are best served by insuring that the private [treble damages] action will be an ever-present threat to deter anyone contemplating business behavior in violation of the antitrust laws."<sup>93</sup>

## B. PRICE-FIXING AND "PER SE" ILLEGALITY

Section 1 proscribes certain types of restraints as presumptively unreasonable if the "practice facially appears to be one that would always or almost always tend to restrict competition and decrease output."<sup>94</sup> Such restraints, considered "per se" illegal, automatically violate section 1, assuming its jurisdictional boundaries are met.<sup>95</sup> The U.S. Supreme Court has long considered price-fixing agreements between competitors (i.e., horizontal price-fixing) to be per se illegal.<sup>96</sup> Even indirect horizon-

89. 15 U.S.C. §§ 1, 4 (2000). For example, two vitamin supplement manufacturers accused of criminal price fixing under section 1 settled with the DOJ and agreed to pay \$750 million in penalties. Additional civil claims against four other vitamin manufacturers pushed the total penalty award to \$1.1 billion. See *Bolze*, *supra* note 12, at 85 n.34 (citing *United States v. F. Hoffman-LaRoche, Ltd.*, No. 99-CR-184-R (N.D. Tex. May 20, 1999) (settling for \$500 million); *United States v. BASF AG*, No. 99-CR-200-R (N.D. Tex. May 20, 1999) (settling for \$250 million)).

90. A "person" can include corporations, individuals, partnerships, or states. See 15 U.S.C. § 12 (2000); 2 JULIAN O. VON KALINOWSKI, *ANTITRUST LAWS AND TRADE REGULATION* § 10.02[1] (2d ed. 2002).

91. 15 U.S.C. § 15 (2000).

92. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 635 (1985).

93. *Perma Life Mufflers, Inc. v. Int'l Parts Corp.*, 392 U.S. 134, 139 (1968), *overruled on other grounds* in *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 134 (1984); see *Ill. Brick Co. v. Ill.*, 431 U.S. 720, 746 (1977) (stating Congress had a legislative purpose of creating a group of "private attorneys general" in establishing the private treble damages action); *Am. Safety Equip. Corp. v. J.P. Maguire & Co.*, 391 F.2d 821, 826 (2d Cir. 1968).

94. *Broad. Music, Inc. v. CBS, Inc.*, 441 U.S. 1, 19-20 (1979).

95. See 2 VON KALINOWSKI, *supra* note 90, § 2.02[2][b]. Besides the per se rule, another evaluative method exists, termed the "rule of reason," in which courts will evaluate the specific circumstances of the dispute to determine whether the restraint promotes or suppresses competition. See *Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 691-92 (1978). Unlike the per se rule, analysis under the rule of reason does not automatically presume the restraint violates section 1. *Id.*

96. 2 VON KALINOWSKI, *supra* note 90, § 2.02[2][b][i].

tal price-fixing, such as an agreement between competitors to restrict output, falls within the per se proscription.<sup>97</sup>

A violation of section 1 requires three elements: (1) a contract, combination, or conspiracy (i.e., concerted activity between two or more actors); (2) which is an unreasonable restraint on trade; and (3) which affects interstate or foreign commerce.<sup>98</sup>

Unilateral conduct by one party cannot violate section 1. This results because unilateral conduct has a distinguishable economic effect from collusive anticompetitive conduct.<sup>99</sup> Collusive conduct between two or more actors generally poses a greater danger to competition than a single actor's unilateral anticompetitive conduct.<sup>100</sup> Thus, a party bringing a section 1 action against the WEGs who operated in California during the crisis would need to produce evidence that the WEGs colluded to manipulate electricity prices. While the publicly available indications of anticompetitive conduct may be a starting point, it is likely that more would be required.

The doctrine of conscious parallelism, used to show an agreement through evidence of a course of dealing or patterns of uniform business behavior by multiple parties, may arise in a section 1 action arising from the crisis.<sup>101</sup> Reports suggested several of the WEGs appeared to participate in similar courses of dealing by withholding output during the crisis.<sup>102</sup> Further, shared use of the gaming strategies also suggests uniform behavior.<sup>103</sup> And as the WEGs sold most of their wholesale electricity through CAPX, they could easily coordinate a reduced supply in order to increase and stabilize the price of electricity.<sup>104</sup> Conscious parallelism by

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97. *Id.* § 2.03[2][b][ii].

98. See 15 U.S.C. § 1 (2000); 2 VON KALINOWSKI, *supra* note 90, § 2.02. It is unlikely the third element would be disputed in a section 1 action related to the crisis. The WEGs largely involved in the crisis are "mostly Texas-based firms with interstate operations." Fellmeth, *supra* note 28, at 835. Further, the test to establish an effect on interstate commerce is extremely relaxed under section 1. See *Summit Health v. Pinhas*, 500 U.S. 322, 330–33 (1991) (finding effect on interstate commerce where the plaintiff, an ophthalmologist in Los Angeles, was injured by a group boycott of the defendant, a hospital in Los Angeles, because the result of the boycott, by removing ophthalmological services in Los Angeles, would also have an eventual resulting effect on interstate commerce). Thus, this Note will not discuss the interstate commerce element.

99. *Copperweld Corp. v. Independence Tube Corp.* 467 U.S. 752, 774–75 (1984); see 2 VON KALINOWSKI, *supra* note 90, § 2.02[1] (stating Congress required concerted activity to avoid dampening competition by individual enterprises).

100. *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761–62 (1984); see 2 VON KALINOWSKI, *supra* note 90, § 2.02[1][a][i].

101. See 2 VON KALINOWSKI, *supra* note 90, § 2.02[1][b][i].

102. See *supra* Part I.C.

103. See *id.*

104. See *Pac. Gas & Elec. Co. v. Lynch*, 216 F. Supp. 2d 1016, 1037 (N.D. Cal. 2002); CPUC REPORT, *supra* note 2, at 62; JOSKOW III, *supra* note 67, at 18.



itself, however, is insufficient to establish concerted action.<sup>105</sup> Courts generally require certain “plus” factors, such as a lack of valid business justification for a party’s behavior or evidence of meetings between the parties.<sup>106</sup>

As noted in Part I.C., it is unclear whether the WEGs conspired to manipulate the electricity markets. For purposes of further discussion, this Note will assume such a conspiracy did exist.

Turning to the unreasonable restraint element, the paradigm case involving section 1 and per se unreasonable price-fixing restraints is *United States v. Socony-Vacuum Oil Co.*<sup>107</sup> There, the respondents (twelve corporations and five individuals) were convicted for criminal section 1 violations for conspiring to raise and maintain gasoline prices by buying up “distress” gasoline<sup>108</sup> on the spot markets<sup>109</sup> and eliminating it as a market factor.<sup>110</sup> Assuming no change in demand, limiting the supply of distress gasoline on the spot market would result in an increase in the price of normal gasoline.<sup>111</sup>

Evidence of the conspiracy between the respondents consisted of testimony and numerous exhibits showing agreements between the parties to manipulate the market.<sup>112</sup> In response to several of the respondent’s arguments, the U.S. Supreme Court held: (1) the output restrictions were still illegal even if they were not the sole cause of the increase in prices;<sup>113</sup> (2) even though competition continued to exist within the affected market, the output restrictions still clearly curtailed its operation;<sup>114</sup> and (3) a price-fixing conspiracy was actionable under section 1 even if it did not result in a fixed and uniform price.<sup>115</sup>

This led to the Court’s seminal recitation of the rule against horizontal price-fixing agreements: “Under the Sherman Act a combination

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105. *Theatre Enters. v. Paramount Film Distrib. Corp.*, 346 U.S. 537, 541 (1954).

106. In the absence of direct guidance by the U.S. Supreme Court, lower courts developed a system of requiring the “plus” factors in addition to conscious parallelism to establish proof of concerted activity. See 2 VON KALINOWSKI, *supra* note 90, § 2.02[1][b][i]; see also Bolze, *supra* note 12, at 88 (listing certain factors).

107. 310 U.S. 150 (1940).

108. Different from normal gasoline, which was produced and sold by the respondents, “distress” gasoline could not be stored, had no regular sales outlet, and was sold at prices significantly below normal gasoline. *Id.* at 171.

109. A spot market is one in which shipment of purchased goods is made in the immediate future. *Id.* at 193.

110. *Id.* at 166–67.

111. *Id.* at 190–192, 216.

112. *Id.* at 177.

113. *Id.* at 219–220.

114. *Id.* at 220.

115. *Id.* at 222.

formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal *per se*.<sup>116</sup> Holding the respondents had formed such a conspiracy, the Court affirmed their convictions under section 1.<sup>117</sup>

Regarding the California crisis, assuming the WEGs agreed to physically withhold generation capacity from the wholesale electricity market, or engaged in gaming strategies which increased congestion within the transmission networks, the WEGs likely restricted the electricity supply available to the market.<sup>118</sup> Such a scenario harkens back to *Socony-Vacuum*. While other factors likely contributed to the price increases during the crisis, one source indicated at least one-third of the increase was attributable to alleged price manipulations by the WEGs.<sup>119</sup> Further, even a small decrease of supply in the heavy-demand electricity market would inexorably cause prices to increase.<sup>120</sup> Such an interruption of "the play of the forces of supply and demand,"<sup>121</sup> through the use of an intentional price-fixing scheme, would fall within section 1.<sup>122</sup>

A violation of section 1 would expose the offending WEGs to severe criminal and civil liability. Any criminal sanctions would pale in comparison with the potential civil liability the WEGs could face. One estimate placed total overcharges from the California crisis at \$55 billion dollars.<sup>123</sup> Assuming that figure as true and directly related to a price-fixing agreement, the treble damages provision alone would subject the WEGs to civil liability of \$165 billion dollars.<sup>124</sup>

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116. *Id.* at 223. The Court also noted that under traditional price-fixing arrangements, where the defendant sets a uniform price, a combination must have the power to fix prices by controlling a "substantial part of the commerce" in the commodity. *Id.* Yet when a combination uses a different mechanism, such as by limiting the supply of the commodity to the market, "such power [to fix prices] may be found to exist though the combination does not control a substantial part of the commodity." *Id.* at 223-24. Applying that rule to the California crisis, the five WEGs controlled approximately thirty-eight percent of the generating capacity in areas controlled by CAISO. See CPMC REPORT, *supra* note 2, at 9. Even though far below the eighty-two percent market control seen in *United States v. Trenton Potteries, Co.*, 273 U.S. 392, 394 (1927), the wholesale generator likely had power to fix prices through the use of output limitations, and as noted by Professor Joskow, appeared to affect a substantial part of the commerce in electricity through those output limitations. See Joskow II, *supra* note 40, at 16; Joskow III, *supra* note 67, at 18.

117. See *Socony-Vacuum*, 310 U.S. at 254.

118. See *supra* Part I.C.

119. See Joskow I, *supra* note 6, at 35.

120. See *id.* at 22-23, 35.

121. *Socony-Vacuum*, 310 U.S. at 220.

122. *Id.* at 222-23.

123. Fellmeth, *supra* note 28, at 860.

124. See 15 U.S.C. § 15 (2000). The \$165 billion does not account for costs or attorneys' fees, both of which would also be recoverable. While the size of the figure may raise some concerns as to the manageability of the actions or the possibility of recovery, one court recently affirmed class certification for an antitrust class action with possible damages exceeding \$100 billion dollars. *In re Visa*

### C. ANTITRUST IMMUNITIES

The U.S. Supreme Court has been historically reluctant to ascribe immunities to the Sherman Act, primarily because of its importance in protecting competitive markets. Even in regulated, non-competitive markets, the Court generally only allows an antitrust immunity where Congress is express in its intent to supersede the antitrust laws through regulation.<sup>125</sup>

The electricity industry generally enjoys no exception from that policy.<sup>126</sup> For example, in *Otter Tail Power Co. v. United States*, the petitioner, an electric utility company, appealed a finding it had violated section two of the Sherman Act for improperly using its market power by refusing to “wheel” power through its own transmission system to a municipal system.<sup>127</sup> The Court rejected the argument that the petitioner was immune from antitrust prosecution because of the Federal Power Commission’s (FPC) regulation of the electricity industry. It reasoned that FPC’s authority to compel power interconnections arose from standards only loosely related to antitrust considerations.<sup>128</sup> Finding no express congressional intent to immunize electric power companies, the Court instead observed the Federal Power Act indicates an overriding policy of maintaining competition to the maximum extent possible consistent with the public interest.<sup>129</sup>

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Check/MasterMoney Antitrust Litig., 280 F.3d 124, 147 (2d Cir. 2001), cert. denied, 536 U.S. 917 (2002).

125. See, e.g., *United States v. Phila. Nat’l Bank*, 374 U.S. 321, 350–51 (1963) (“Repeals of the antitrust laws by implication from a regulatory statute are strongly disfavored, and have only been found in cases of plain repugnancy between the antitrust and regulatory provisions.”) (citations omitted).

126. See *Otter Tail Power Co. v. United States*, 410 U.S. 366, 374–75 (1973).

It is clear, then, that Congress rejected a pervasive regulatory scheme for controlling the interstate distribution of power in favor of voluntary commercial relationships. When these relationships are governed in the first instance by business judgment and not regulatory coercion, courts must be hesitant to conclude that Congress intended to override the fundamental national policies embodied in the antitrust laws.

*Id.* at 374. The electric industry, regulated by FERC pursuant to the Federal Power Act, received no express antitrust immunity from Congress. See 16 U.S.C. § 824 (2000); 2 VON KALINOWSKI, *supra* note 90, § 7.07[1][b][ii], [2][a]. Indeed, the Federal Power Act contains a “savings clause,” stating: “[s]ections 824i, 824j, 824k, 824l, 824m of this title, and this section, shall not be construed to modify, impair, or supersede the antitrust laws.” 16 U.S.C. § 824k(e)(2). Yet sections 824d and 824e are the portions of the Act which grant FERC the ability to review and fix electricity rates according to their “just and reasonable” standard, and they were not included within that savings clause. See 16 U.S.C. §§ 824d, 824e, 824k(e)(2); *In re Cal. Wholesale Elec. Antitrust Litig.*, 244 F. Supp. 2d 1072, 1084 (S.D. Cal. 2003) (in antitrust case arising from the crisis, dismissing the plaintiff’s argument the savings clause also applied to §§ 824d–824e).

127. *Otter Tail*, 410 U.S. at 368.

128. *Id.* at 373.

129. *Id.* at 373–74.

Nevertheless, three immunities will likely appear in private section 1 actions arising from the crisis. The first, the indirect purchaser doctrine, may limit the particular parties able to bring a private civil section 1 action. The second, the state action doctrine, does not appear to apply due to the deregulated nature of the electricity markets. The third, the filed rate doctrine, presents formidable obstacles to civil enforcement and will likely bar all private party civil section 1 actions against the WEGs. Because of the minor nature of the first two immunities, this Note analyzes them briefly, but provides a more comprehensive discussion of the filed rate doctrine.

### 1. *The Indirect Purchaser Doctrine*

The indirect purchaser doctrine limits the particular parties who can bring a private civil section 1 action. The doctrine distinguishes between two types of parties: direct and indirect purchasers. The party purchasing the commodity directly from the alleged antitrust violator is the “direct” purchaser, while every other party further down the distribution chain, such as a consumer who repurchases the commodity, is an “indirect” purchaser.<sup>130</sup> Under the doctrine, an indirect purchaser lacks standing to bring a private civil section 1 action.<sup>131</sup>

The doctrine nullifies two types of arguments. Under an “offensive use” argument, an indirect purchaser plaintiff claims injury based upon overcharges “passed on” by the direct purchaser. While an overcharge resulting from an antitrust violation would naturally go first to the direct purchaser, the direct purchaser might then “pass on” all or part of the cost of the overcharge to its customers, the indirect purchasers.<sup>132</sup> On the other hand, “defensive use” of the doctrine “involves attempts by defendant antitrust violators to show that plaintiff direct purchasers were not injured because the direct purchasers had passed on the overcharge to their customers.”<sup>133</sup> The U.S. Supreme Court rejected both types of arguments, holding the direct purchaser suffers the full extent of the de-

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130. See 2 VON KALINOWSKI, *supra* note 90, § 10.02[2][c]. For example, take a price-fixing scenario with a three-link distribution chain, including a wholesaler (the price fixer), the retailer (the direct purchaser), and the consumer (the indirect purchaser). The wholesaler engages in price fixing, increasing the price of the commodity. The retailer pays the higher prices for the commodity, but will likely “pass on” some or all of those costs to the consumer when he resells the commodity. As can be seen, a single antitrust violation often has a “ripple” effect in those affected by an antitrust violation. See *id.*; Howard Benjamin Green, Note, *State Indirect Purchaser Statutes: The Preemptive Power of Illinois Brick*, 62 B.U. L. REV. 1241, 1245 (1982).

131. See *Ill. Brick Co. v. Ill.*, 431 U.S. 720, 735 (1977).

132. See Green, *supra* note 130, at 1241 n.8, 1242.

133. *Id.*

fendant's overcharge, regardless of any overcharges "passed on" to consumers or other parties.<sup>134</sup>

In *Illinois Brick Co. v. Illinois*, the U.S. Supreme Court explained the reasoning behind the doctrine. First, denying standing to indirect purchasers prevents the risk of exposing antitrust defendants to multiple liability and allowing duplicative recoveries.<sup>135</sup> For example, the direct purchaser could recover treble damages for the full overcharge suffered, and the indirect purchaser could also recover treble damages for any portion of the overcharge passed on to it.<sup>136</sup> Second, the Court noted the extreme difficulties inherent in calculating damages for indirect purchaser suits.<sup>137</sup> That burden could decrease the effectiveness of treble damages deterrence.<sup>138</sup> Third, as the Court barred defensive use of the doctrine ten years earlier in *Hanover Shoe Inc. v. United Shoe Machine Corp.*, it wanted to ensure the doctrine applied equally to both plaintiffs and defendants.<sup>139</sup> It could only do this by either extending the doctrine, or by overruling *Hanover Shoe*. Relying on *stare decisis*, it chose the former.<sup>140</sup>

In the California electricity markets, a three-link distribution chain existed. The WEGs generated the wholesale electricity, then sold it to the IOUs, who resold it to retail customers.<sup>141</sup> The IOUs purchasing the wholesale electricity were the direct purchasers, while retail customers were the indirect purchasers.

Pursuant to the doctrine, the IOUs, as direct purchasers, would be the only parties with standing to pursue a private section 1 action against the WEGs.<sup>142</sup> The doctrine would preclude indirect purchasers, such as retail consumers who paid higher retail electricity prices, from bringing such actions.<sup>143</sup>

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134. *Hanover Shoe, Inc. v. United Shoe Mach. Corp.*, 392 U.S. 481, 494 (1968); see Green, *supra* note 130, at 1247.

135. *Illinois Brick*, 431 U.S. at 730-31.

136. *Id.*

137. *Id.* at 731-32.

138. *Id.* at 741, 745.

139. *Id.* at 728.

140. *Id.* at 736 ("[W]e must bear in mind that considerations of *stare decisis* weigh heavily in the area of statutory construction, where Congress is free to change this Court's interpretation of its legislation.").

141. *Id.* at 726.

142. *Id.* at 735-36.

143. *Id.*

## 2. *The State Action Doctrine*

In *Parker v. Brown*,<sup>144</sup> the U.S. Supreme Court established that the Sherman Act only prohibits individual action, “not state action.”<sup>145</sup> There, the Court held section 1 did not apply to a state-controlled raisin marketing program because the State had adopted and enforced the program.<sup>146</sup> Although it based its decision on state sovereignty,<sup>147</sup> the Court warned a state cannot automatically “give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful . . . .”<sup>148</sup>

Building upon that warning language, the Court in *California Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc.*<sup>149</sup> set forth a two-element test to allow a private party immunity under the doctrine:

First, the challenged restraint must be ‘one clearly articulated and affirmatively expressed as state policy’; second, the policy must be ‘actively supervised’ by the State itself . . . . It is not enough that anticompetitive conduct is prompted by state action; rather, anticompetitive activities must be compelled by direction of the State acting as a sovereign.<sup>150</sup>

In *Midcal*, a California statute mandated resale price maintenance<sup>151</sup> within the wine production industry.<sup>152</sup> Although the statute required

144. 317 U.S. 341, 352 (1943).

145. *Id.* at 350–52.

146. *Id.* at 344–46, 352.

147. The Court reasoned that because the Sherman Act contained no language expressing a congressional purpose to override state sovereignty, it would not lightly attribute to Congress “an unexpressed purpose to nullify a state’s control over its officers and agents.” *Id.* at 351; see 2 VON KALINOWSKI, *supra* note 90, § 6.02[1] (observing state action doctrine “was limited by principles of federalism and state sovereignty stemming from the Supremacy Clause of the Constitution”) (footnote omitted); John Shepard Wiley, Jr., *A Capture Theory of Antitrust Federalism*, 99 HARV. L. REV. 713, 713–14 (1986) (noting when state or local regulatory policy conflicts with federal antitrust policy, the conflict poses an issue of federalism).

148. *Parker*, 317 U.S. at 351.

149. 445 U.S. 97, 104–05 (1980).

150. *Id.* (citation omitted). Generally, a state policy is “clearly articulated” if the State clearly intended to displace competition in a particular industry with a regulatory structure. See 2 VON KALINOWSKI, *supra* note 90, § 6.02[3]. Several courts of appeals use a “foreseeability standard” which determines that “conduct is immunized if it is the foreseeable result of state agency action and if circumstances justify an inference that the Agency intended to authorize the conduct.” See *id.* The “active supervision” prong ensures the State retains ultimate control over the conduct of private parties, including the authority to disapprove that conduct if it should offend the state policy. See Patrick v. Burget, 486 U.S. 94, 101 (1988). “Absent such a program of supervision, there is no realistic assurance that a private party’s anticompetitive conduct promotes state policy, rather than merely the party’s individual interests.” *Id.*

151. Resale price maintenance is a type of price fixing which is generally per se illegal under section 1 of the Sherman Act. See *Midcal*, 445 U.S. at 102; *Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 407 (1911).

152. *Midcal*, 445 U.S. at 102.

wine producers to sell only according to price schedules filed with the State,<sup>153</sup> the State maintained no direct control over the wine prices nor reviewed “the reasonableness of the prices set by [the] wine dealers.”<sup>154</sup> The Court determined the statute satisfied the first element of the test because the legislative history of the statute clearly stated “its purpose to permit resale price maintenance.”<sup>155</sup> The second element failed, however, because while the State authorized the price-setting and enforced the prices set by private parties, it did not establish the prices or review their reasonableness.<sup>156</sup> “The national policy in favor of competition cannot be thwarted by casting such a gauzy cloak of state involvement over what is essentially a private price-fixing arrangement.”<sup>157</sup>

It is highly unlikely that any WEG that engaged in anticompetitive conduct in California’s electricity markets could satisfy either element of the *Midcal* test.<sup>158</sup> While California clearly articulated its policy to transition its highly regulated electricity market into a deregulated, competitive market, it did not intend to “displace competition” in the electricity industry with a regulatory structure. To the contrary, it intended to displace a regulatory structure and replace it with competition.<sup>159</sup> Further, unlike the raisin program in *Parker*, where the State adopted and enforced the program in furtherance of a recognized governmental policy, California did not adopt or enforce any anticompetitive behavior by the WEGs.<sup>160</sup> Nor would such behavior comport with state policy, which clearly favored competition.<sup>161</sup>

Second, California could not have “actively supervised” any anticompetitive conduct by the WEGs.<sup>162</sup> Obviously, the State did not establish or review any prices resulting from such conduct.<sup>163</sup> Indeed, California now seeks \$8.9 billion from the WEGs for allegedly engaging

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153. *Id.* at 99.

154. *Id.* at 100.

155. *Id.* at 105.

156. *Id.* at 106.

157. *Id.*

158. See Rossi, *supra* note 3, at 1788 (encouraging courts to be cautious of applying state action doctrine to newly deregulated electric industries); Schwartz, *supra* note 19, at 1487 (noting that a legislative policy advocating deregulated, competitive markets removes the “clearly articulated . . . policy” of regulation historically common in electricity industry).

159. See *supra* note 29 and accompanying text.

160. See *Parker v. Brown*, 317 U.S. 341, 352 (1943).

161. Schwartz, *supra* note 19, at 1487.

162. See *supra* note 29 and accompanying text.

163. See *Midcal*, 445 U.S. at 105-06.

in such conduct.<sup>164</sup> Accordingly, the state action doctrine will not immunize the WEGs from private civil section 1 claims by the IOUs.<sup>165</sup>

### 3. *The Filed Rate Doctrine*

Unlike the relatively simple application of the two immunities previously discussed, the filed rate doctrine presents more nuanced considerations. The resolution of its application to the crisis is of vital concern, as the effect of the doctrine can bar all private civil section 1 actions against the WEGs.

In antitrust actions, the filed rate doctrine immunizes a defendant from private party section 1 actions when a plaintiff predicates the action upon a rate submitted to and approved by a regulatory agency.<sup>166</sup> Federal courts have applied the doctrine for rates approved by multiple federal agencies, including FERC.<sup>167</sup> And the doctrine still applies even if the filed rates resulted from a price-fixing conspiracy in violation of section 1.<sup>168</sup>

#### a. *Keogh v. Chicago & Northwestern Railway Co.*

The filed rate doctrine first appeared in an antitrust setting in *Keogh v. Chicago & Northwestern Railway Co.*<sup>169</sup> There, the petitioner, a manufacturer of excelsior and flax tow, alleged the respondents, a group of interstate freight carriers, formed a conspiracy to eliminate competition in interstate freight rates in violation of section 1. The petitioner, seeking treble damages, argued the conspiracy resulted in higher rates than those possible through free competition. The respondents, however, had filed the rates with the Interstate Commerce Commission (ICC), which approved the rates.<sup>170</sup>

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164. See *supra* note 10 and *infra* note 255 and accompanying text.

165. See *Cal. v. Mirant Corp.*, No. C-02-1787-VRW, 2003 WL 21321243, at \*7 (N.D. Cal. Mar. 25, 2003) (ruling the state action doctrine inapplicable in antitrust suit brought against WEGs for alleged anticompetitive conduct during the crisis).

166. See *Square D Co. v. Niagara Frontier Tariff Bureau, Inc.*, 476 U.S. 409, 422 (1986); *County of Stanislaus v. Pac. Gas & Elec. Co.*, 114 F.3d 858, 863 (9th Cir. 1997). Generally, once the federal regulatory agency approves the rates, the doctrine becomes active. See *Keogh v. Chi. & Northwestern Ry. Co.*, 260 U.S. 156, 160 (1922). The doctrine also applies when rates have been filed and lawfully take effect, even before approval. *Id.* However, if after the rates are filed, the Agency disapproves the rates, the doctrine does not bar a private antitrust suit. See generally 2 VON KALINOWSKI, *supra* note 90, § 7.02[3][a].

167. See, e.g., *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 573 (1981); 2 VON KALINOWSKI, *supra* note 90, § 7.0[3][a].

168. See, e.g., *Square D*, 476 U.S. at 422; *Keogh*, 260 U.S. at 162; *County of Stanislaus*, 114 F.3d at 863; see generally *Hall*, 453 U.S. at 580 (1981) (“[F]iled rate doctrine applies both to federal antitrust actions and to state law causes of action relating to rates established by federal agencies.”).

169. 260 U.S. 156 (1922).

170. *Id.* at 159–160.



The Court stated the sole question for decision was whether the petitioner could pursue a private civil section 1 action.<sup>171</sup> In determining that the fixed rates were “reasonable and non-discriminatory,” as settled and approved by the ICC proceedings, the Court answered its question in the negative.<sup>172</sup>

It initially reasoned that “[a] rate is not necessarily illegal because it is the result of a conspiracy . . . in violation of the Anti-Trust Act. What rates are legal is determined by the Act to Regulate Commerce [the statutory provision endowing ICC with regulatory authority].” In the event a conspiracy between the respondents resulted in unreasonably high or discriminatory rates contrary to ICC regulations, the petitioner had recourse to recover damages through ICC proceedings. Any additional remedy via treble damages, however, would be contrary to congressional intent.<sup>173</sup>

Second, noting the petitioner could only bring a private treble damages claim if he had been “injured in his business or property,”<sup>174</sup> the Court reasoned such an injury “implies violation of a legal right. The legal rights of shipper as against carrier in respect to a rate are measured by the published tariff. Unless and until suspended or set aside, this rate is made, for all purposes, the legal rate, as between carrier and shipper.”<sup>175</sup> Contract, tort, or antitrust law could not vary or enlarge those rights. “This stringent rule prevails, because otherwise the paramount purpose of Congress—prevention of unjust discrimination—might be defeated.”<sup>176</sup> If the petitioner could recover under antitrust, he would in effect receive a rebate which might give him “preference over his trade competitors.”<sup>177</sup> That preference would then negate the congressional goal of uniform treatment because no one could reasonably expect that “several juries and courts [would give] to each [competitor] the same measure of relief.”<sup>178</sup>

Third, for the petitioner to prevail, he would have to prove that the ICC would approve a “hypothetical lower rate” (i.e., a rate resulting from unfettered competition, rather than through conspiracy). As the Act to Regulate Commerce had conferred upon ICC the authority to ap-

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171. *Id.* at 161.

172. *Id.* at 161–62.

173. *Id.* at 162.

174. See 15 U.S.C. § 15(a) (2000).

175. *Keogh*, 260 U.S. at 163.

176. *Id.*

177. *Id.*

178. *Id.*

prove those rates, "it is [the ICC] which must determine whether a rate is discriminatory," not the courts.<sup>179</sup>

Finally, the Court reasoned that the petitioner's damages were "purely speculative" and impossible to prove. Since all the shippers, including the petitioner, had to pay the "legal rate," any advantages from a lower rate may have passed through to the customers or the ultimate consumer, in the form of lower prices, rather than to the petitioner or other shippers.<sup>180</sup> Accordingly, the Court used the doctrine to dismiss the petitioner's section 1 claim.<sup>181</sup>

*b. Square D Co. v. Niagra Frontier Tariff Bureau, Inc.*

From its beginning, *Keogh* has suffered from extensive criticism. Its immunizing effect from treble damages runs contrary to the "private attorney general" policy behind antitrust enforcement,<sup>182</sup> and its existence stands as a rare exception to the U.S. Supreme Court's hesitation to override jurisdiction of the Sherman Act.<sup>183</sup> Indeed, numerous sources have referred to the *Keogh* holding as "unwise" and poorly reasoned.<sup>184</sup>

In 1986, that criticism came to a head when the U.S. Supreme Court considered whether to overrule *Keogh*. In *Square D v. Niagara Frontier Tariff Bureau, Inc.*, the petitioners, a group of commercial shippers, alleged that the respondent motor carriers had illegally fixed freight transportation rates contrary to section 1.<sup>185</sup> Among other remedies, the petitioners sought treble damages.<sup>186</sup> The respondents argued that since they filed their rates with the ICC, the filed rate doctrine barred the petitioner's claim.<sup>187</sup> The Court agreed and ruled *Keogh* controlled the case before it.<sup>188</sup>

"The question, then, is whether we should continue to respect the rule of *Keogh*."<sup>189</sup> In responding to the petitioners' argument that the private treble damages action promotes competition and free markets, the

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179. *Id.* at 164.

180. *Id.* at 164-65.

181. *Id.* at 165.

182. See *supra* notes 90-93 and accompanying text.

183. See *Otter Tail Power Co. v. United States*, 410 U.S. 366, 374-75 (1973).

184. See, e.g., *Square D Co. v. Niagara Frontier Tariff Bureau Inc.*, 476 U.S. 409, 419-20 (1986) (stating *Keogh* "was unwise as a matter of policy"); HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE § 19.6, at 660 (1994) ("None of [*Keogh's*] arguments had much to be said for them at the time they were originally made, and they are even less sensible today.").

185. 476 U.S. at 410.

186. *Id.* at 413.

187. *Id.* at 414.

188. *Id.* at 417.

189. *Id.*

Court agreed, even indicating *Keogh* “was unwise as a matter of policy.” Nevertheless, the Court presumed Congress was “fully cognizant of this interpretation of the statutory scheme, which had been a significant part of our settled law for over half a century, and that Congress did not see fit to change it when Congress carefully reexamined this area of the law in 1980.”<sup>190</sup>

Responding to past criticism directed at *Keogh*, comprehensively discussed in the lower court of appeals,<sup>191</sup> the Court stated:

[I]t is also true that the *Keogh* rule has been an established guidepost at the intersection of the antitrust and interstate commerce statutory regimes for some 6½ decades. The emergence of subsequent procedural and judicial developments does not minimize *Keogh*'s role as an essential element of the settled legal context in which Congress has repeatedly acted in this area. . . .<sup>192</sup>

Thus, because of “careful, intense, and sustained congressional attention,” the Court concluded that “[i]f there is to be an overruling of the *Keogh* rule, it must come from Congress, rather than from this Court.”<sup>193</sup>

c. *FERC-Approved Rates and Market-Based Rates*

Courts have applied the filed rate doctrine to rates approved by FERC and also appear to have extended the doctrine to encompass market-based rates, rather than just fixed, cost-of-service rates. For example, in *County of Stanislaus v. Pacific Gas & Electric Co.*, the petitioners, seeking treble damages, alleged the respondents engaged in a price-fixing conspiracy in violation of section 1 by inflating the rates of natural gas above the prevailing market rate.<sup>194</sup> The rates at issue, however, had been filed and approved both by the Economic Regulatory Administration (ERA)<sup>195</sup> and FERC.<sup>196</sup> The “filed rate” reviewed by FERC was the prevailing market rate, apparently determined through two methods of price

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190. *Id.* at 419–20 (footnote omitted).

191. See *Square D Co. v. Niagara Frontier Tariff Bureau, Inc.*, 760 F.2d 1347, 1352–56 (2nd Cir. 1985), *aff'd*, 476 U.S. 409 (1986). In the court of appeals opinion for *Square D*, Judge Friendly comprehensively summarized the criticism directed at *Keogh*, and this section of the Note incorporates many of the opinion's arguments. Indeed, in the lone dissent in the U.S. Supreme Court opinion for *Square D*, Justice Marshall stated: “Judge Friendly cogently and comprehensively explained why the reasoning of [*Keogh*] has been rendered obsolete by subsequent developments in the law. . . . I am persuaded by his analysis. I therefore dissent.” *Square D*, 476 U.S. at 424–25 (Marshall, J., dissenting).

192. *Square D*, 476 U.S. at 423–424.

193. *Id.* at 424.

194. 114 F.3d 858, 860 (9th Cir. 1977).

195. *Id.* Like FERC, ERA is also a federal administrative agency.

196. *Id.* at 861. Similar to its authority over electricity rates, FERC has authority under the Natural Gas Act to ensure all gas rates are just and reasonable, 15 U.S.C. § 717(c)(a) (2000), and to fix a just and reasonable rate if it should find such rate to be unjust or unreasonable. 15 U.S.C. § 717d (2000).

calculation.<sup>197</sup> Yet the court noted ERA did not review and approve a fixed rate; instead, it reviewed and approved a volume quantity of natural gas imported by the respondents. The court determined the respondent's "import practices," reviewed and approved by ERA, were a "filed rate" for purposes of the filed rate doctrine.<sup>198</sup> Since the doctrine encompassed that "filed rate," the court applied the doctrine and dismissed the action.<sup>199</sup>

Similarly, in *Nantahala Power & Light Co. v. Thornburg*, a non-antitrust case, the U.S. Supreme Court recognized a FERC-ordered allocation of power as a legitimate "filed rate."<sup>200</sup> Stating that "the right to a reasonable rate is the right to the rate which [FERC] files or fixes,"<sup>201</sup> the Court held the lower court's ruling that the petitioner "had purchased an unreasonably large quantity of high-cost power . . . conflicts with FERC's orders in the same manner as would a refusal to recognize a FERC-approved price as a reasonable cost . . ." <sup>202</sup> Accordingly, the doctrine states that federal and state courts cannot determine that any other specific rate or approved ratemaking process, both considered "filed rates," is more reasonable than the rate approved by a federal agency.<sup>203</sup>

#### d. *The Filed Rate Doctrine and the California Crisis*

Assuming the WEGs participated in anticompetitive conduct in violation of section 1, it appears the U.S. Supreme Court's deference to the filed rate doctrine will lead to its application to related private section 1 actions, thus barring any treble damages claims brought by the IOUs.<sup>204</sup>

197. *County of Stanislaus*, 114 F.3d at 860 n.1.

198. *Id.* at 864.

199. *Id.* at 863, 867 (citing *Square D Co. v. Niagara Frontier Tariff Bureau, Inc.*, 476 U.S. 409, 422 (1986)).

200. 476 U.S. 953, 966 (1986).

201. *Id.* at 963 (quoting *Montana-Dakota Util. Co. v. Northwestern Pub. Serv. Co.*, 341 U.S. 246, 251-52 (1951)).

202. *Id.* at 973; see *Transwestern Pipeline Co. v. Fed. Energy Regulatory Comm'n*, 897 F.2d 570, 578 (D.C. Cir. 1990) (FERC "need not confine rates to specific, absolute numbers but may approve a tariff containing a rate 'formula' or a rate 'rule' . . .")

203. See *Nantahala Power & Light*, 476 U.S. at 963, 973; see also *In re Cal. Wholesale Elec. Antitrust Litig.*, 244 F. Supp. 2d 1072, 1077-78 (S.D. Cal. 2003) (finding the FERC-approved market structure operated by CAPX and CAISO fits within the filed rate doctrine); *Pac. Gas & Elec. Co. v. Lynch*, 216 F. Supp. 2d, 1016, 1041 (N.D. Cal. 2002) (holding broad interpretation of "filed rate" warranted applying doctrine to FERC-approved "rates" based on market-based rather than fixed, cost-of-service processes); *Duke Energy Trading & Mktg., L.L.C. v. Davis*, 267 F.3d 1042, 1056-57 (9th Cir. 2001) (noting that the "filed rate" definition includes block-forward contracts administered by CAPX and subject to CAPX tariffs).

204. As noted by the U.S. Supreme Court in *Square D*, the filed rate doctrine does not bar anti-trust scrutiny by the Government for possible criminal sanctions under section 1. *Square D Co. v. Niagara Frontier Tariff Bureau, Inc.*, 476 U.S. 409, 422 (1986). Yet this ignores the substantial deterrent effect of the private treble damages claim. See *supra* notes 91-93 and accompanying text.

Nevertheless, several convincing arguments exist which may militate against application of the doctrine to actions arising from the crisis. The doctrine has an extremely poor fit to the facts of the crisis, and as noted, suffers from extensive criticism. Even though *Square D* rejected that criticism, the Court did not face the doctrine's effect within a deregulated industry, nor foresee the mischief the doctrine could cause in a scenario similar to the California crisis. Indeed, application of the doctrine to the novel and unique nature of the deregulated California electricity markets appears to require a significant broadening of the doctrine, a measure which appears unwise considering the criticism surrounding the doctrine, its poor fit to the crisis, and the need for proper remedies for any anti-competitive conduct committed during the crisis.

In any private section 1 action arising from the crisis, the WEGs are likely to contend the rate tariffs they filed with FERC are "filed rates."<sup>205</sup> The rate tariffs, however, were not fixed, uniform rates, such as "cost-of-service" rates.<sup>206</sup> Instead, they were "market-based" tariffs, consisting of applications by the WEGs setting forth the process for them to sell electricity in California at wholesale rates.<sup>207</sup> These "market-based" tariffs were new to FERC and dramatically different from the fixed "cost-of-service" tariffs with which FERC had the most experience.<sup>208</sup> Indeed, FERC's cursory analysis of these new tariffs hints at the Agency's inexperience; it analyzed these applications solely by looking at the market share of each WEG, and being satisfied there was insufficient market share to manipulate the market, approved the applications.<sup>209</sup> Unlike "cost-of-service" rates, FERC never evaluated a fixed number under its "just and reasonable" standard, but instead approved a process by which the WEGs would sell wholesale electricity in California.<sup>210</sup>

Little practical reason exists for courts to pay deference to FERC oversight of the market-based tariffs. FERC generally looks to whether the tariffs are "just and reasonable," yet "market-based" tariffs have no fixed figure to evaluate under that standard; indeed, there was little for FERC to evaluate other than the market share of the WEG applicant. With little to approve or examine, FERC exercised minimal agency oversight over the tariffs filed by the WEGs. Further, the approved "market-based" tariffs set forth the process by which the WEGs were to sell

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205. See *supra* notes 44–46 and accompanying text.

206. See *supra* notes 16–18 and accompanying text.

207. See *Lynch*, 216 F. Supp. 2d at 1041.

208. See *supra* notes 45–46 and accompanying text.

209. See *id.*; Fels, *supra* note 5, at 10.

210. See *In re Cal. Wholesale Elec. Antitrust Litig.*, 244 F. Supp. 2d 1072, 1074–75 (S.D. Cal. 2003); see also *Lynch*, 216 F. Supp. 2d at 1020.

wholesale electricity. Assuming anticompetitive conduct by the WEGs, it cannot be said that FERC approved such conduct. Applying the doctrine to approval of those “market-based” tariffs would do little more than pay lip service to the policy of agency deference.

Justice Stewart recognized in *Otter Tail* a major difference between highly regulated markets and competitive markets. He stated the regulation of private utility rates is necessary because of heightened market power and monopolies present within the utility industry.<sup>211</sup> Because of that regulation, antitrust law is ill-suited to those highly regulated industries.<sup>212</sup> The converse could also be true, in that antitrust law is *well-suited* for deregulated electricity markets subject to competition, especially to deter anticompetitive manipulations by market participants.<sup>213</sup>

Moreover, in not allowing a private party to recover for antitrust violations, the doctrine ignores the difference between a “just and reasonable” rate and a rate obtained through free competition. That is, a rate may be reasonable to FERC, but may still result from a price-fixing conspiracy, thus being higher than a rate obtainable in a free market.<sup>214</sup> By denying antitrust recovery for a rate resulting from anticompetitive conduct, the IOUs lose the opportunity to receive the benefit of lower rates and are also subject to damages from incurring that higher rate.

These arguments, however, face an uphill battle. Past commentary suggests FERC’s oversight encompasses all “filed rates,” regardless of whether they are fixed rates or free-floating market-based rates.

There is no suggestion in any of the Supreme Court’s decisions that the *nature* of the particular federally-authorized rate (i.e., whether it be a fixed, cost-of-service-based rate, an indexed rate, or a free-floating market-based rate) should affect in any way the preemptive effect of the rate once the particular form of rate structure has been approved or accepted by the FERC. . . . [W]here the FERC continues to have statutory authority over wholesale power prices, the filed rate doctrine still applies, even though the FERC, in its exercise of that authority, chooses to allow wholesalers to charge market-based prices.<sup>215</sup>

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211. See *Otter Tail Power Co. v. United States*, 410 U.S. 366, 391 (1973) (Stewart, J., concurring in part, dissenting in part).

212. See *id.*

213. See GAO REPORT, *supra* note 5, at 7 (“[T]he potential for a company to engage in anticompetitive behavior and charge excessive prices for electricity is a significant concern when rates are determined by the marketplace instead of cost-of-service regulation . . . .”); *cf. Otter Tail*, 410 U.S. at 389 (Stewart, J., dissenting).

214. See *Square D Co. v. Niagara Frontier Tariff Bureau, Inc.*, 760 F.2d 1347, 1354 (2d Cir. 1985), *aff’d*, 476 U.S. 409 (1986) (noting a “zone of reasonableness” exists for rates within ICC’s reasonable and non-discriminatory rates determination).

215. Fels, *supra* note 5, at 16–17; see *Farmer’s Union Cent. Exch., Inc. v. Fed. Energy Regulatory Comm’n*, 734 F.2d 1486, 1501 (D.C. Cir. 1984) (FERC is not “required to adhere ‘rigidly to a cost-

The poor fit of the doctrine to the crisis provides additional reasons for courts to hesitate to apply the doctrine, especially as its application to the crisis does not further any of the policies enunciated in *Keogh*. There, the Court first reasoned that an injured plaintiff could already recover damages for an unreasonable rate through the authorized federal agency and expressed concerns that allowing antitrust remedies might result in various plaintiffs obtaining non-uniform relief from different juries.<sup>216</sup>

In the crisis, the potential for duplicative recoveries does arise. The IOUs have recourse to petition FERC to provide refunds for overcharges resulting from the WEGs' alleged anticompetitive conduct, and an additional antitrust action could duplicate those refunds.<sup>217</sup> Yet that concern ignores the power of a district court to modify a judgment to avoid such duplication.<sup>218</sup> And unlike FERC, an antitrust remedy could provide full compensation for any overcharges incurred. Because of its legislative authority, FERC appears limited in providing a full refund for overcharges incurred during the crisis.<sup>219</sup> FERC also lacks the authority to order monetary penalties against the WEGs for any anticompetitive conduct, and any FERC-ordered remedy would likely not carry any significant deterrent effect. Yet antitrust remedies can provide full compensation for past anticompetitive conduct and, through its treble damages provisions, deter any future misconduct. Due to the importance of that deterrent effect, Congress has recognized that the risk of double recovery should not preclude a treble damages action.<sup>220</sup>

*Keogh's* concern with non-uniform recoveries also does not arise here. For example, under *Keogh's* logic, should an IOU receive an antitrust remedy, it might serve as a rebate which may give the IOU an advantage over the other IOUs.<sup>221</sup> Further, different juries may grant varying awards to the different IOUs, thus implicating *Keogh's* concerns of price discrimination.

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based determination of rates.”) (citation omitted); *In re Cal. Wholesale Elec.*, 244 F. Supp. 2d at 1079 (“[T]he filed rate doctrine applies to bar claims challenging the rates set by FERC in a market-based rate system.”). The U.S. Supreme Court may have implicitly supported these conclusions by affirming FERC’s assertion of broadened authority through FERC Order 888, which established the basic rules for deregulation and implementation of “unbundled” wholesale generation and local transmission electricity distribution. See *N.Y. v. Fed. Energy Regulatory Comm’n*, 535 U.S. 1, 20 (2001).

216. *Keogh v. Chi. & Northwestern Ry. Co.*, 260 U.S. 156, 162 (1992).

217. See *infra* notes 252–53 and accompanying text.

218. See *Ill. Brick Co. v. Ill.*, 431 U.S. 720, 761–62 (1977) (Brennan, J., dissenting) (noting a district court’s ability to “fashion relief accordingly” to avoid duplicative recoveries).

219. See *infra* notes 252–54 and accompanying text.

220. See *Ill. Brick*, 431 U.S. at 762 (Brennan, J., dissenting) (stating that congressional intent shows that where double recovery is unavoidable, liability should still be imposed).

221. See *Keogh*, 260 U.S. at 163.

That argument also does not fit within the facts of the crisis. The IOUs participated within a deregulated, competitive electricity market, and thus paid different market rates due to the nature of the market. In the event of a price-fixing conspiracy by the WEGs, the market rates would be higher than those obtainable in an unfettered market, but the IOUs all had to pay those increased prices. Further, only three major IOUs exist within the California electricity market.<sup>222</sup> It would be a simple matter through joinder procedures for the IOUs to bring one antitrust action, resulting in one jury and avoiding the possibility of inconsistent awards.<sup>223</sup>

*Keogh's* second policy concern acknowledged the issue that in applying section 1, a court would have to decide upon a supposed "hypothetical lower rate" (i.e., a rate unaffected by an antitrust violation).<sup>224</sup> That determination supposedly risks court interference with the role previously reserved to the regulatory agency by Congress.<sup>225</sup>

Yet in section 1 actions arising from the crisis, a court need not determine whether the hypothetical rate would fit FERC's standards; instead, the court need only estimate what electricity prices would have been absent anticompetitive conduct.<sup>226</sup> A court would use that estimate for calculating damages, and nothing more. Such an estimate would inevitably be lower, thus running little risk it might be contrary to FERC's "just and reasonable" mandate. Even if a court had to decide whether a rate was "just and reasonable" according to FERC's standards, the court could still defer to congressional intent by referring such a question to the Agency. Indeed, the U.S. Supreme Court has engaged in similar referrals several times after *Keogh*.<sup>227</sup>

*Keogh's* third concern argued that damages claimed by a plaintiff would be "purely speculative" and impossible to prove.<sup>228</sup> The speculation would arise from a court's inability to determine whether a lower rate would benefit a plaintiff or whether the plaintiff would pass on the benefit of the lower rate to its customers.<sup>229</sup>

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222. See CPUC REPORT, *supra* note 2, at 8–9.

223. Cf. *Square D Co. v. Niagara Frontier Tariff Bureau, Inc.*, 760 F.2d 1347, 1352 (2d Cir. 1985), *aff'd*, 476 U.S. 409 (1986).

224. See *supra* note 179 and accompanying text.

225. See *Keogh*, 260 U.S. at 163–64.

226. See IA PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTI-TRUST LAW: AN ANALYSIS OF ANTI-TRUST PRINCIPLES AND THEIR APPLICATION 103–04 (2d ed. 2000).

227. See *Square D*, 760 F.2d at 1354 (citing three U.S. Supreme Court cases referring question of reasonableness of tariff to ICC).

228. See *Keogh*, 260 U.S. at 164–65.

229. *Id.*



Like the others, that argument also does not fit within the facts of the crisis. During the crisis, the IOUs could not pass on any overcharges to their retail customers because of the retail price caps imposed upon the electricity market by CPUC.<sup>230</sup> Indeed, PG&E became bankrupt because it could not pass on the higher prices.<sup>231</sup>

Further, in *Hanover Shoe*, the Court rejected a similar pass-on theory when raised in regard to the indirect purchaser doctrine.<sup>232</sup> There, the Court brushed aside *Keogh's* "speculative damages" argument, stating "we ascribe no general significance to the *Keogh* dictum for cases where the plaintiff is free to prove that he has been charged an illegally high price."<sup>233</sup> Instead, the court required the plaintiff to prove only that the defendant overcharged it and the amount of the overcharge.<sup>234</sup> Whether the plaintiff "passed on" some of the higher costs had no relevance to the action.<sup>235</sup>

Nevertheless, it is likely that courts will apply the filed rate doctrine to the California crisis,<sup>236</sup> especially considering the U.S. Supreme Court's broad deference to the doctrine in *Square D*. There, the Court emphasized the longevity of *Keogh* and its importance in a settled area of law.<sup>237</sup> "[I]t is more important that the applicable rule of law be settled than that it be settled right."<sup>238</sup>

230. See Rossi, *supra* note 3, at 1778.

231. See *id.* at 1769.

232. 392 U.S. 481, 494 (1968); see generally 2 VON KALINOWSKI, *supra* note 90, § 7.02[2].

233. See *Square D Co. v. Niagara Frontier Tariff Bureau, Inc.*, 760 F.2d 1347, 1353 (2d Cir. 1985), *aff'd*, 476 U.S. 409 (1986) (quoting *Hanover Shoe*, 392 U.S. at 491 n.8). The Court's reference to "cases where the plaintiff is free to prove that he has been charged an illegally high price" appears to refer back to *Keogh's* argument that a filed rate is the "legal rate," and an antitrust plaintiff can only challenge such a rate before the regulatory agency that reviewed it. See *supra* notes 174-76 and accompanying text.

234. See *Hanover Shoe*, 392 U.S. at 494.

235. *Id.*

236. In one of the first antitrust actions resulting from alleged manipulation of California's electricity market by the WEGs, a federal court held the filed rate doctrine precluded the plaintiff's claims under the Cartwright Act (California's state antitrust law). The district court found the filed rate doctrine preempted California state law in this instance. *In re Cal. Wholesale Elec. Antitrust Litig.*, 244 F. Supp. 2d 1072, 1078 (S.D. Cal. 2003). In a similar case, the California Attorney General challenged the application of the filed rate doctrine to antitrust claims arising from the crisis. The court rejected the challenge, stating "it is indisputable that the well settled doctrine flows from congressional intent . . . to which courts have given effect through strict application of the doctrine. Those substantive provisions have not been altered by Congress, and the court declines the AG's invitation to do so here." *Cal. v. Mirant Corp.*, No. C-02-1787-VRW, 2003 WL 21321243, at \*8 (N.D. Cal. Mar. 25, 2003). The Attorney General plans on appealing the ruling. Nancy Vogel, *State's Energy Firm Claims Denied*, L.A. TIMES, Mar. 26, 2003, at B6.

237. See *Square D*, 476 U.S. at 424 (footnote omitted).

238. *Id.*

Yet the facts of the crisis also defeat any reliance upon that broad deference. *Keogh* arose in an era of heavily regulated industries and “cost-of-service” rates. Over the past twenty years, those industries have undergone dramatic changes and have largely adopted “market-based” rates determined by competitive forces. While application of the doctrine to a highly regulated, “cost-of-service” industry is well-settled, its application to a deregulated, competitive market is a more modern invention. Due to the relative youth of deregulated industries, it does not appear as certain that the doctrine deserves the deference paid to it by the Court. Considering the Court’s own suggestion that *Keogh* “was unwise as a matter of policy,”<sup>239</sup> extending its application to those new industries only compounds the original error.<sup>240</sup>

Assuming, however, that courts do apply the doctrine to the California crisis, it would bar the IOUs from bringing private section 1 treble damages actions for any overcharges suffered from anticompetitive conduct by the WEGs. In discussing an antitrust immunity similar to the filed rate doctrine, Justice Blackmun’s comment echoes concerns about the dimming of antitrust enforcement in the California crisis:

But *Hanover Shoe* is on the books, and the Court feels that it must be ‘consistent’ in its application of pass-on. That, for me, is a wooden approach, and it is entirely inadequate when considered in the light of the objectives of the Sherman and Clayton Acts. . . . Nevertheless, we must now await still another statute which, as the Court acknowledges, the Congress may adopt. One regrets that it takes so long and so much repetitious effort to achieve, and have this Court recognize, the obvious congressional aim.<sup>241</sup>

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239. *See id.* at 420.

240. *See AREEDA, supra* note 226, at 108 (stating that since the filed rate doctrine is irrational, as conceded by the U.S. Supreme Court, “the best policy” is to construe it “narrowly”).

241. *Ill. Brick Co. v. Ill.*, 431 U.S. 720, 765–66 (1977) (Blackmun, J., dissenting); *see AREEDA, supra* note 226, at 110 (“stare decisis is no reason for expanding the domain of a poor decision”).

### III. INADEQUACY OF FERC AUTHORITY

As discussed, it appears that any private section 1 actions arising from the crisis will fail due to the filed rate doctrine.<sup>242</sup> Thus, FERC will possess exclusive jurisdiction over disputes of alleged anticompetitive conduct during the crisis, and will carry the burden of reviewing claims and awarding appropriate remedies for such conduct.<sup>243</sup>

Continued review of the electricity markets is a crucial matter. Even though the crisis abated, it became evident afterward that the electricity markets are still vulnerable to future anticompetitive manipulation.<sup>244</sup> For example, FERC recently acknowledged price manipulation continues in the natural gas markets, which indirectly affect electricity prices.<sup>245</sup> It is no surprise to hear FERC admitting the energy markets require “more-aggressive oversight.”<sup>246</sup>

Due to the unavailability of antitrust law, the electricity markets depend upon FERC to police and remedy any anticompetitive conduct within the markets.<sup>247</sup> In terms of providing any substantive or meaningful relief, however, FERC appears more fettered than formidable. While FERC instituted several “price mitigation” measures which partly alleviated the severe price fluctuations in the markets during the crisis,<sup>248</sup> the Agency largely played an inadequate role during the crisis.<sup>249</sup> This inadequacy flows from several holes in FERC’s agency hull: insufficient legislative authority; inexperience with deregulated, competitive electricity markets; and substantial human resources problems.

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242. See discussion *supra* Part II.C(3).

243. See 16 U.S.C. §§ 825e–825f (2000) (FERC may investigate and penalize unlawful conduct upon complaint or on its own motion); *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 966 (1986); *Fed. Power Comm’n v. S. Cal. Edison Co.*, 376 U.S. 205, 215–16 (1964); 2 VON KALINOWSKI, *supra* note 90, § 7.06[2] (FERC generally has exclusive jurisdiction over rates).

244. See *San Diego Gas & Elec. Co.*, 93 F.E.R.C. ¶¶ 61,121, 61,349–50 (2000).

245. FED. ENERGY REGULATORY COMM’N, 2003 NATURAL GAS MARKET ASSESSMENT 25 (2002–2003); see FERC FACT-FINDING REPORT, *supra* note 52, at III-55 (noting natural gas prices indirectly influence electricity prices).

246. See Berthelsen, *supra* note 72, at B1.

247. See 16 U.S.C. §§ 825e–825f (FERC may investigate unlawful conduct pursuant to complaint or upon its own motion); GAO REPORT, *supra* note 5, at 48 (FERC can set new rates and order refunds for the amount charged in excess of the just and reasonable rate); cf. Reynolds, *supra* note 12, at 11 (in the energy markets, FERC regulation largely took the place of competition in ensuring fairness to consumers).

248. See *San Diego Gas & Elec. Co.*, 95 F.E.R.C. ¶¶ 61,418, 62,548–49, 62,559 (2001); *San Diego Gas & Elec. Co.*, 93 F.E.R.C. ¶¶ 61,294, 61,982–83 (2000).

249. See Fellmeth, *supra* note 28, at 864.

FERC's congressionally mandated standard of review is whether a rate is "just and reasonable."<sup>250</sup> Should it determine a rate is "unjust, unreasonable, unduly discriminatory, or preferential," then FERC can determine a "just and reasonable rate" and fix it by order.<sup>251</sup> For existing rates found to be unjust or unreasonable, FERC can order a refund for the overcharge, that is, the difference between the FERC-set "just and reasonable" rate and the previous unjust or unreasonable rate. The power to order refunds, however, only arises sixty days after FERC receives a complaint or begins its own investigation into possible anticompetitive conduct.<sup>252</sup>

[R]efunds may only be ordered for the period following the refund 'effective date.' The earliest the refund effective date can be is sixty days after a complaint is filed with FERC or after a notice of Commission-initiated investigation is issued. As a result, this limitation provides no remedy for instances where market participants have charged unjust or unreasonable rates during the period before the refund effective date.<sup>253</sup>

This restriction initially resulted in FERC suggesting any refunds from the crisis will likely not exceed \$1 billion.<sup>254</sup> While later reports suggested FERC may increase the refund amount to \$3.3 billion, California officials still complain those amounts are far short of their initial claim of \$8.9 billion.<sup>255</sup> Taking Professor Fellmeth's estimated \$55 billion in overcharges as true,<sup>256</sup> a refund of \$3.3 billion amounts to only six percent of the total overcharges.

FERC also lacks the authority to order monetary penalties against WEGs who charge unjust or unreasonable rates for electricity.<sup>257</sup> "While this authority may not have been necessary for cost-of-service regulation, it is important if FERC is to pose a credible threat and deter anticompetitive behavior or violations of market rules by market participants."<sup>258</sup>

For example, in response to Enron's anticompetitive conduct during the crisis, FERC did not levy any monetary penalties. Instead, the

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250. 16 U.S.C. § 824d(a) (2000) ("All rates and charges . . . shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.").

251. 16 U.S.C. § 824e(a) (2000).

252. GAO REPORT, *supra* note 5, at 48.

253. *Id.*; see *Pac. Gas & Elec. Co. v. Lynch*, 216 F. Supp. 2d 1016, 1033 (N.D. Cal. 2002) (citing 96 F.E.R.C. ¶ 61,120, 61,505 (2001)) (noting FERC cannot order retroactive refunds).

254. See Fellmeth, *supra* note 28, at 849-50.

255. See Jonathan Peterson & Ricardo Alonso-Zaldivar, *Energy Markets Manipulated, Regulators Say*, L.A. TIMES, Mar. 27, 2003, at A1. Those reports suggested FERC may have found a loophole around this restriction. See FERC FACT-FINDING REPORT, *supra* note 52, at VI-10-11.

256. See Fellmeth, *supra*, note 28, at 860.

257. See GAO REPORT, *supra* note 5, at 49.

258. *Id.* at 5.

Agency stripped Enron “of their authority to sell electricity anywhere in the United States at market rates.”<sup>259</sup> That penalty, however, is merely symbolic; before FERC even contemplated the penalty, Enron “sold its energy trading business . . . and does not intend to reenter that business.”<sup>260</sup>

Considering the absence of legislative authority to provide meaningful remedies or penalties, it appears unlikely FERC will be able to adequately police electricity markets in the future. As noted by the U.S. General Accounting Office (GAO):

FERC lacks adequate enforcement ‘bite’ to deter anticompetitive behavior or other violations of market rules. Such deterrence is an important part of an effective oversight approach. . . .

. . . .

. . . As a result, it is difficult for FERC to curb and respond effectively and firmly to anticompetitive behavior, particularly for electricity markets.<sup>261</sup>

In addition, FERC lacks meaningful experience with deregulated, competitive electricity markets due to its concentration on the highly regulated markets of the past. FERC has yet to develop a detailed oversight approach to monitor deregulated electricity markets.<sup>262</sup> Its past efforts in adapting to these markets has been “incomplete or of limited effectiveness.”<sup>263</sup> FERC itself noted it misunderstood the level of oversight and investigation needed to prevent or mitigate the effects of the California crisis.<sup>264</sup> Instead, the Agency thought it could wait for the competitive electricity market structure to be fully in place before developing effective monitoring actions.<sup>265</sup> This unfortunately was not the case.

FERC’s inexperience resulted in a barrage of criticism following its response to the California crisis. CPUC claimed FERC’s “[c]ontinued enforcement inaction” raised questions as to FERC’s commitment to the

259. Jonathan Peterson & Elizabeth Douglass, *Regulators Press Energy Firms but Uphold Disputed Contracts*, L.A. TIMES, June 26, 2003, at A1.

260. *Id.*

261. GAO REPORT, *supra* note 5, at 7, 48; *cf. id.* at 78 (noting eighty-three percent of FERC employees believe FERC requires additional authority to levy penalties against market abusers).

262. *See id.* at 31, 51.

263. *Id.* at 31.

264. *See id.* at 34. FERC officials also stated the California crisis was a “wake up call” for FERC, and that it “ha[d] not done all that it could to oversee energy markets.” *Id.* at 6, 38. Indeed, over fifty percent of FERC employees believe FERC is not effective in “[d]etecting market power abuses in wholesale electricity markets” (compared with twenty-six percent who consider FERC effective). *Id.* at 75. Further, forty-four percent of FERC employees believe FERC is not effective in “[c]orrecting detected market power abuses in wholesale electricity markets (compared with thirty-five percent who believe FERC is effective). *Id.*

265. *See id.* at 51.

fairness and stability of California's electricity market.<sup>266</sup> Dr. Joskow indicated both FERC and CPUC "acted too slowly and ineffectively as the crisis deepened and spent most of their energies pointing fingers of blame at one another rather than working together cooperatively to find a solution."<sup>267</sup> Other commentators accused FERC of taking "an easygoing approach toward the corporations they regulate,"<sup>268</sup> and for not acting as the "antitrust cop . . . on the beat in the state" during the crisis.<sup>269</sup>

Finally, FERC's substantial human resource problems exacerbated its inability to effectively respond to the crisis. It has encountered difficulty recruiting staff "knowledgeable about competitive energy markets," largely due to competition with private sector salaries.<sup>270</sup> Indeed, FERC currently lacks sufficient staff with the required expertise to effectively oversee deregulated energy markets.<sup>271</sup> A large portion of its staff faces impending retirement, and it has replaced the head of its organization four times over the past five years.<sup>272</sup> "Such a high level of leadership turnover may have had a significant impact on the ability of the Agency to develop a new regulatory approach for emerging energy markets . . . ."<sup>273</sup>

Due to these issues, FERC appears overwhelmed by the complex pressures facing it. Those pressures likely contributed to the "lack of consistent management and direction for the Agency" as well as the "agency's lack of progress in developing and implementing a new regulatory approach for competitive energy markets" over the past five years.<sup>274</sup>

FERC continues operating under its antiquated legislative authority, designed primarily for highly regulated, cost-of-service systems, rather than for deregulated, market-based systems.<sup>275</sup> Further, its inexperience in deregulated markets, coupled with its human resources problems, suggests a continuing inability to effectively police California's electricity markets. Thus, it appears the conjunction of the filed rate doctrine and FERC's inadequacy at policing California's deregulated electricity markets resulted in a lawless frontier vulnerable to significant anticompetitive conduct. That vulnerability remains even now, albeit somewhat abated due to heightened public attention.

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266. See CPUC REPORT, *supra* note 2, at 67.

267. See Joskow I, *supra* note 6, at 53.

268. Peterson, *supra* note 255, at A1.

269. See Fellmeth, *supra* note 28, at 864.

270. GAO REPORT, *supra* note 5, at 5.

271. *Id.* at 8.

272. *Id.* at 5, 8.

273. *Id.* at 49.

274. *Id.* at 50.

275. See *id.* at 47, 50.

Considering the U.S. Supreme Court declined to overrule the filed rate doctrine in 1986,<sup>276</sup> Congress has the responsibility to provide the electricity markets with appropriate protection. As suggestions, two avenues may prove fruitful.

First, Congress could overrule *Keogh* by statute, thus allowing the courts to effectively oversee competitive electricity markets through anti-trust laws. This would comport with past congressional policy of protecting competition through antitrust laws.<sup>277</sup> Private treble damages actions would also provide sufficient deterrence to impede future anticompetitive behavior.<sup>278</sup>

Alternatively, Congress could provide FERC with expanded legislative authority to impose substantial and meaningful penalties on parties who commit anticompetitive conduct within deregulated electricity markets. This avenue is not as attractive as the first for several reasons. First, FERC itself has suggested it lacks the expertise necessary to effectively monitor deregulated electricity markets.<sup>279</sup> The GAO buttressed this suggestion in its analysis of FERC's performance during the crisis.<sup>280</sup> Congress would thus have to provide FERC with additional funding in order to hire the personnel needed for effective oversight. Finally, such an avenue would ignore the reliable policies of protecting competition through antitrust laws, as well as deterring anticompetitive conduct through private treble damages antitrust actions.<sup>281</sup>

### CONCLUSION

During the California electricity crisis, state residents and businesses suffered thirty-eight days of blackouts and service interruptions over a six-month period. The crisis caused significant price increases, resulted in the bankruptcy of one of California's largest IOUs, and cost the state billions of dollars to recover. Certainly, this is not what California legislators or FERC intended when they placed the California electricity markets on the road to deregulation.

While experts identified numerous causes of the crisis, including flawed market rules and high consumer demand, several sources suggested that the WEGs operating in California strategically manipulated the electricity markets through anticompetitive conduct. These sources also hinted the WEGs acted in concert in manipulating the markets.

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276. *Square D Co. v. Niagara Frontier Tariff Bureau Inc.*, 476 U.S. 409, 424 (1986).

277. *See supra* notes 86–88 and accompanying text.

278. *See supra* notes 91–93 and accompanying text.

279. *See supra* notes 264–65 and accompanying text.

280. *See GAO Report, supra* note 5, at 65–66.

281. *See supra* notes 86–93 and accompanying text.

At the turn of the 19th and 20th centuries, Congress recognized that collusive anticompetitive conduct endangered the free flow of supply and demand in competitive markets. Through section 1 of the Sherman Act, those conspiracies were “declared to be illegal.”<sup>282</sup> For over one hundred years, the courts have employed that simple but remarkably effective statute to protect our nation’s competitive markets.

Section 1 appears well-suited to provide appropriate remedies for any anticompetitive conduct suffered during the crisis. It also could serve as a powerful deterrent force to prevent future abuses, not just in California, but also nationwide. Despite that strong fit, it does not appear the nation’s electricity markets can depend upon the protections of section 1. The filed rate doctrine, developed by the U.S. Supreme Court during an era of highly regulated markets, has largely removed energy market participants from accountability under section 1. Yet the doctrine’s application to the California crisis invokes none of the policy concerns initially addressed in its development. Legal commentators, including the Court, have criticized it. And its poor fit to the crisis appears to militate against its application. Yet it remains. Courts have begun applying it to section 1 actions arising from the crisis, immunizing WEGs from accusations of anticompetitive conduct and market manipulation.

The immunizing effect of the doctrine results in inadequate remedies and the lack of any meaningful deterrent. FERC, which exclusively reviews accusations of anticompetitive conduct in the electricity markets, is ill-equipped to remedy abuses during the California crisis or deter future abuses. The Agency lacks the power to award sufficient remedies or penalties for anticompetitive conduct. Further, problems within the Agency predict its continued inability to adequately oversee energy markets in the future, at least without congressional intervention.

The Court indicated in 1986 that despite the origin of the filed rate doctrine, it is up to Congress to take the initiative to return the protections of antitrust law to affected industries. As the push for the deregulation of electricity markets continues, Congress should consider turning the power back on for the Sherman Act.

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282. 15 U.S.C. § 1 (2003).



APPENDIX A  
ACRONYM GLOSSARY

AB 1890	Public Utilities-Electrical Restructuring Assembly Bill 1890(California's deregulation statute)
CAISO	California Independent System Operator
CAPX	California Power Exchange
CPUC	California Public Utilities Commission
ERA	Economic Regulatory Administration
FERC	Federal Energy Regulatory Commission
FPC	Federal Power Commission (FERC's predecessor)
GAO	U.S. General Accounting Office
ICC	Interstate Commerce Commission
IOU	Investor-owned utility
ISO	Independent System Operator
PG&E	Pacific Gas & Electric Company (an IOU)
SCEC	Southern California Edison Company (an IOU)
SDG&E	San Diego Gas & Electric Company (an IOU)
WEG	Wholesale electricity generator