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The Federal Power Act grants the Federal Energy Regulatory Commission exclusive jurisdiction over “the sale of electric energy at wholesale in interstate commerce.” 16 U.S.C. § 824(b)(1). FERC may regulate any “rule, regulation, practice, or contract affecting [a wholesale] rate.” *Id.* § 824e(a). But only states may regulate “any other sale of electric energy”—namely retail sales to consumers. *Id.* § 824(b)(1). Pursuant to the Federal Power Act, FERC adopted Order 745 addressing “demand response,” an innovation in energy markets that manages prices during periods of high demand by providing incentives to consumers to reduce consumption. Demand response is accomplished either by raising energy prices or compensating consumers for reduced energy consumption during peak periods. Recognizing that direct price regulation would exceed its authority, FERC addressed only consumer compensation. Order 745 provides that demand-response energy suppliers are to be compensated by wholesale-market operators using the same rate paid to traditional electricity generators and allocates the cost of this compensation among wholesale-market energy purchasers.

Today, the Supreme Court granted certiorari in *FERC v. Electric Power Supply*, No. 14-840, and *EnerNOC, Inc. v. Electric Power Supply Association*, No. 14-841, consolidating the cases to determine (1) whether FERC “reasonably concluded that it has authority under the Federal Power Act . . . to regulate the rules used by operators of wholesale electricity markets to pay for reductions in electricity consumption and to recoup those payments through adjustments to wholesale rates” and (2) whether Order 745 is arbitrary and capricious.

During the rulemaking process, the respondents, electricity generators and their trade associations, opposed the proposed Order 745 as beyond the authority of FERC and as substantively unsound. They argued that even though regulation of the rate paid to demand-response suppliers appears to apply to wholesale energy markets, its actual effect is to impermissibly regulate the price paid by consumers. In addition, even if FERC had the required authority, the respondents contended that paying demand-response suppliers the same as traditional energy suppliers overcompensated them. When Order 745 was promulgated over respondents’ objections and rehearing by FERC was denied, respondents appealed to the D.C. Circuit.

A divided panel of the D.C. Circuit determined that Order 745 was “an *ultra vires* agency action.” The majority refused to accept FERC’s position that regulating only “direct participants” was a viable “limiting principle” on its authority over matters “affecting” the wholesale energy rate. Instead, the court held that the limiting principle must be drawn from the express statutory bar on the regulation of retail sales. Moreover, even if FERC had the authority to promulgate Order 745, the rule is nonetheless invalid because it is arbitrary and capricious. The majority determined that FERC “failed to properly consider—and engage—Commissioner Moeller’s reasonable (and persuasive) arguments [in dissent] . . . that Order 745 will result in unjust and discriminatory rates,” as urged by respondents. Judge Edwards dissented because he concluded that limiting FERC’s regulatory authority to direct participants in wholesale energy markets was “straightforward and sensible.” In contrast to the majority, he did not believe it appropriate to treat the regulation of compensation for forgoing the consumption of electricity as falling within the bar on regulation of retail sales of energy. Judge Edwards also disagreed with the majority’s assessment of the adequacy of FERC’s response to Commissioner Moeller’s concerns.

The Supreme Court granted certiorari today to address the scope of FERC’s ability to regulate demand response measures indirectly through wholesale energy markets. The Court’s decision will be important not only to the traditional electricity generators and demand-response suppliers that participate directly in the wholesale market, but also to those that do business with them. Companies that seek credit for reduction in energy usage, among others, will be affected by whether Order 745 survives.

Absent extensions, which are likely, amicus briefs in support of the petitioner will be due on June 25, 2015, and amicus briefs in support of the respondent will be due on July 27, 2015. Any questions about the case should be directed to Joshua D. Yount (+1 312 701 8423) in our Chicago office.