Nos. 13-2419, 13-2424

In the United States Court of Appeals for the Fourth Circuit

PPL ENERGYPLUS, LLC, et al.,

Plaintiffs-Appellees,

v.

DOUGLAS R.M. NAZARIAN, et al.,

Defendants-Appellants,

and

CPV MARYLAND, LLC,

Intervenor-Appellant.

Appeal from Judgment of the United States District Court for the District of Maryland, No. 1:12-cv-01286-MJG, Hon. Marvin J. Garbis, U.S.D.J.

OPENING BRIEF FOR INTERVENOR-APPELLANT CPV MARYLAND, LLC

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CORPORATE DISCLOSURE STATEMENT

Pursuant to FRAP 26.1 and Local Rule 26.1, Intervenor-Appellant CPV Maryland, LLC states that:

It is not a publicly held entity;

It is 50% owned by wholly owned subsidiaries of Competitive Power Venture Holdings, LLC ("CPV Holdings"). The ownership structure, including affiliates, is as follows: CPV Maryland, LLC is 50% owned by CPV Maryland Holding Company, LLC. CPV Maryland Holding Company, LLC is 99% owned by CPV Power Development, Inc. and 1% owned by CPV Maryland Investment, LLC. CPV Maryland Investment, LLC is wholly owned by CPV Power Development, Inc. CPV Power Development, Inc. is wholly owned by CPV Holdings;

It is also 50% owned by Diamond St. Charles, LLC, an affiliate of Mitsubishi Corporation and Mitsubishi International Corporation;

No publicly held corporation or other publicly held entity owns 10% or more of the stock of CPV Maryland, LLC;

No publicly held corporation or other publicly held entity has a direct financial interest in the outcome of this litigation;

CPV Maryland, LLC is not a trade association; and

This case did not arise out of a bankruptcy proceeding.

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JURISDICTIONAL STATEMENT

The district court accepted jurisdiction under 28 U.S.C. § 1331 as a case arising under the Constitution. The court's judgment was filed on October 24, 2013. JA34. CPV Maryland, LLC's ("CPV") notice of appeal was filed on November 22, 2013. JA35. This Court has jurisdiction under 28 U.S.C. § 1291.

ISSUE PRESENTED

Faced with a looming shortage of electric capacity, the Maryland Public Service Commission ("MPSC") decided to procure the development of new, environmentally friendly power plants. To help cover the substantial costs of building a new plant, it offered the successful bidder, CPV, a stable revenue stream, directing three of the State's local electric distribution companies ("EDCs") to enter into a 20-year "contract for differences" ("CfD") with CPV, underwritten by the State's retail ratepayers. These CfDs require yearly payments, in the form of a subsidy or rebate, consisting of the difference between what CPV bid as its yearly revenue requirement necessary to construct and operate a plant and what it actually receives by selling capacity and energy in the federally supervised wholesale markets.

Notwithstanding that CPV sells neither energy nor capacity to the EDCs, the district court deemed the CfDs' supplemental payments to be an "ultimate price" for sales subject to the Federal Energy Regulatory Commission's jurisdiction and, on that basis, "field preempted." The following question is presented:

> Is Maryland's procurement of a new power plant through a contract that provides the developer with a yearly subsidy or rebate, beyond the revenue the developer earns selling in interstate wholesale markets, "field preempted"?

STATEMENT OF THE CASE

A. Brief Summary Of Proceedings

In December 2011, the MPSC solicited proposals for up to 1500 MW of new power plant capacity.[1] The solicitation required winning bidders to build plants within a specified region, and to use certain environmentally preferred technologies.

Because revenue uncertainty and price swings had discouraged new power plant construction, the MPSC offered successful bidders long-term, financially settled CfDs with the State's regulated EDCs. The CfDs would provide a stable revenue stream, at the winning bid price, sufficient to justify the enormous investment required for the new construction. JA261-62 (Dist. Ct. Mem. of

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[1] "Capacity" is a generation plant's size or capability of producing electricity. References to capacity sales mean that the generator agrees to use its plant to provide electricity as needed. JA227; *Conn. Dep't of Pub. Util. Control v. FERC*, 569 F.3d 477, 479 (D.C. Cir. 2009) *("CDPUC")*.

Decision ("Op.")). The MPSC's April 2012 Order No. 84815 (the "Generation Order") declared CPV's proposed 661 MW combined cycle natural gas plant, to be built in Charles County, Maryland, the sole successful bid, and directed the EDCs to enter into 20-year CfDs. JA265-66.

Two weeks later, Plaintiffs-Appellees – owners of existing plants that would compete with CPV's plant – filed this case claiming that the Generation Order violated the Supremacy Clause and the Commerce Clause. JA66-73 ¶¶ 79-103. The EDCs that are the parties to the CfDs did *not* join in the Complaint. The district court granted CPV's motion to intervene. JA77.

Following a March 2013 bench trial, Judge Garbis declared the Generation Order "field preempted," declined to reach Plaintiffs-Appellees' conflict preemption claim, and rejected their Commerce Clause claim. CPV and the MPSC separately appealed. JA351-53. On November 27, 2013, this Court consolidated the appeals as No. 13-2419 (L).[2] JA36.

B. Statement Of Facts

1. Historical Background

For more than a century, States have had the responsibility and authority to ensure the adequacy of electric generation resources to meet their citizens' needs,

[2] An appeal pending in the Third Circuit (Nos. 13-4330, 13-4394, 13-4501 (consolidated)), arising from New Jersey's use of CfDs to support new power plant development, raises similar issues. Opening briefs were filed on January 17, 2014.

and to set retail rates. JA207-08. Under the classic, early twentieth century industry paradigm, power plants were built and operated by vertically integrated utilities, which sold power to retail customers. JA208-11, 245-47. States ensured the adequacy of electric supply by guaranteeing recovery of prudent construction costs through ratepayer charges. The assurance of cost recovery allowed utilities to finance new construction while earning a reasonable return on invested capital.

Many States continue to have vertically integrated utilities, while others have partially "deregulated" them. Maryland's 1999 Electric Customer Choice and Competition Act ("1999 Act") required Maryland's utilities to divest their power plants to third parties or nonutility affiliates, JA201, 247, while permitting retail ratepayers to buy electricity from either their EDCs or third parties. These changes did not alter the MPSC's longstanding responsibility to ensure adequate electricity supply and to support needed power plant development.

By 2006, the General Assembly enacted "material amendments" to the 1999 Act.[3] In particular, it authorized the MPSC to support needed new construction by requiring state-regulated EDCs to enter into long-term power purchase agreements with developers. *See* Md. Code Ann., Pub. Util. Cos. § 7-510(c) (2013). Such

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[3] *In re Petition of Calpine Corp.*, No. 24-C-12-002853, slip op. at 8 (Md. Cir. Ct. Oct. 3, 2013).

agreements are often required to finance new construction, as they provide an assured long-term revenue stream, underwritten by ratepayers.

Similarly, the Generation Order provides for long-term ratepayer support of needed construction *via* the EDCs. It does so in a way that honors recent FERC initiatives providing for wholesale sales of capacity through a FERC-supervised regional auction. The Order leaves actual capacity and electric energy sales entirely to the FERC-supervised auctions, at FERC-approved rates. It then provides for supplemental payments, by or to the EDCs, measured against the revenue requirements underlying CPV's successful bid to construct and operate the plant.

2. The MPSC Conducted A Competitive Solicitation To Encourage Construction Of A New Power Plant

In 2007, echoing concerns voiced by various stakeholders, JA202, 251-53, the MPSC warned the General Assembly of a "looming capacity shortage," *id.*, and concluded that it could address this shortfall by requiring Maryland utilities to enter into long-term contracts that would support investment. The MPSC first used a CfD to address a capacity shortfall in a 2008 "Gap RFP" for "demand resources."[4] *See* JA253-54.

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[4] "Demand resources" are capacity resources that address shortfalls by reducing demand for, rather than increasing supply of, electricity. JA228-29.

In September 2009, the MPSC initiated a proceeding to determine whether there was a need for new power plants and, if so, how to meet it. *See* JA256. An MPSC-retained independent consultant recommended (1) issuance of an RFP soliciting environmentally friendly power plants, specifically "natural gas-fired combined-cycle generation"; and (2) that the plant be located in the SWMAAC zone – the area, which includes portions of Maryland and the entire District of Columbia, most at risk for reliability problems. JA260. The MPSC issued an RFP in December 2011, seeking up to 1500 MW of new natural gas plants, to be secured through MPSC-approved CfDs. JA260-65.

On April 12, 2012, the MPSC issued the Generation Order, finding that "the long-term demand for electricity in Maryland, and specifically in the SWMAAC zone, compels us to order new generation in the amount of 650 to 700 MWs in the SWMAAC zone in Maryland by 2015." JA1335. The Order reiterated the consultant's findings that Maryland should procure such generation

> because it is operationally flexible, clean relative to our current generation mix, and comparatively inexpensive to operate … [and that] the new generation should be limited to SWMAAC because that is the constrained zone that has seen the highest prices, the least generation development, and is at most risk for reliability problems.

JA1323-24. The MPSC explained that it was unable to rely solely on short-term market forces to spur needed construction because the market had not "provided sufficient certainty for prospective generation suppliers to secure financing in the current economic climate."[5] JA1328-29.

CPV's bid was selected as providing "the best price for [Maryland] [Standard Offer Service] ratepayers." JA266. The MPSC directed three EDCs to enter into 20-year CfDs with CPV. The CfDs require CPV to (1) build the new plant and to sell its output into federally supervised wholesale markets; and (2) undertake the project based on the yearly revenue requirements set forth in its successful bid, net of revenues received from wholesale market sales, with the difference paid by or to the EDCs.[6] If CPV's annual sales in FERC-regulated markets fall below the CfD revenue requirement, then the EDCs pay CPV the difference (and recoup that payment from ratepayers). JA328. If CPV's market earnings exceed the revenue requirement, then the EDCs are paid that difference, which is passed on to retail ratepayers. JA265. The result is a stable revenue stream, and a yearly subsidy or rebate, as the case may be. JA265, 290. The Generation Order thus meshes with FERC's market initiative by requiring CPV to sell its capacity and energy into FERC-supervised markets, at FERC-approved

[5] The district court confirmed significant fluctuations in yearly capacity prices. JA239.

[6] CPV's bid reflected its projected costs relating to construction, operation, finance and a reasonable rate of return. CPV modeled these projections "to determine the annual revenue requirements necessary to construct and operate its proposed generation resource." JA264-65.

rates, pursuant to FERC-approved requirements. The CfDs neither require nor contemplate that the EDCs will purchase capacity or energy from CPV.

3. FERC's Role

Under the Federal Power Act ("FPA"), 16 U.S.C. §§ 824 *et seq.* (2012), FERC regulates interstate wholesale energy markets, including ensuring "just and reasonable rates" in those markets. 16 U.S.C. § 824d(a). FERC has no authority to require construction of power plants. JA283-84. That crucial responsibility resides with the States. JA207-08.

To promote competition in wholesale markets, FERC has authorized formation of "regional transmission organizations," which bring together generators, transmission resources and wholesale purchasers, and operate certain energy and capacity markets. JA213-16. PJM Interconnection, LLC ("PJM"), spanning most of thirteen states, including most of Maryland, is the largest of these entities. Under FERC supervision, PJM manages the electric grid in its territory and administers wholesale energy and capacity markets. JA216-27. PJM has no authority to license or retire power plants, or to direct their construction.

PJM operates the Reliability Pricing Model ("RPM"), which includes a three-year forward capacity market, run as an auction. *See* JA226-27, 232-36. FERC regulates the auction, including tariff rules governing who may participate and how bids may be submitted, and FERC approves auction prices if they are "just and reasonable." JA232-36, 282 n.46.

In the annual auction, generators and other eligible resources bid to provide capacity for a single year – *i.e.*, the capability to provide a certain amount of electricity during that year – three years in the future. For example, the 2012 RPM auction set capacity prices for 2015. JA227. The auction clearing price is established at the highest bid that PJM must accept to acquire the total capacity needed to meet projected demand for that period. Resources that bid above that price are rejected. *See* JA234-39. Resources bidding at or below that price, including bids of zero that are allowed for incumbent generators, are paid the clearing price, no matter what they actually bid. Cleared capacity is sold at wholesale to PJM, the only buyer in this "market."[7] PJM then resells at wholesale to buyers that look to the RPM to meet some or all of their retail customers' needs. JA220-21, 226.

4. FERC And PJM Ensured That The Generation Order Would Not Interfere With PJM's Auctions

The RPM rules in effect since 2006 specify that new generators would have to bid at or above an administratively determined benchmark price, derived by

[7] Within the overall market, PJM accounts for locational constraints, resulting in separately modeled submarkets. JA240-43.

reference to a generic project's cost structure. The original rules exempted certain new state-supported projects from minimum bid requirements, allowing them to bid as "price takers." This meant that, like existing generators, these resources could bid zero, and be certain to clear the auction and receive the clearing price for their capacity. JA235.

Immediately after issuance of the Generation Order, various existing generators filed a complaint with FERC seeking to tighten conditions under which new state-supported plants, including CPV's Maryland resource and others planned for New Jersey, would be allowed to bid. PJM responded by proposing its own revisions to address state-sponsored projects. FERC subsequently approved those auction rule revisions effective for the May 2012 RPM auction.

Among other things, FERC eliminated the exemption from PJM's "minimum offer price" rules for state-sponsored projects like CPV's, requiring them to bid at set minimum prices unless the project sponsor could demonstrate costs below the applicable benchmark. Thus, instead of excluding CfD-supported resources from bidding into RPM, FERC set bid conditions for their participation, finding that a capacity resource that met FERC's conditions "is a competitive resource and should be permitted to participate in the auction regardless of whether it also receives a subsidy." *PJM Interconnection, LLC*, 135 FERC ¶ 61,022 (2011) at P 177. The resulting capacity clearing price was deemed just and reasonable.[8] CPV's project followed these new rules and bid into and cleared the 2012 RPM auction. JA268-70.

5. The District Court Decision

While recognizing Maryland's "legitimate interest and federally permissible role in securing an adequate supply of electric energy for Maryland residents in the present and in the future," JA284, the district court nevertheless found the Generation Order field preempted. It did so on the theory that the CfDs were not to be seen as providing for separate financial payments – subsidies or rebates – or offered to facilitate plant construction, but rather that they set the "ultimate[]" price for a sale subject to FERC jurisdiction. *See* JA292. The court declined to resolve Plaintiffs-Appellees' conflict preemption claim, JA311-12, and rejected their Commerce Clause challenge, finding no impermissible burden on interstate commerce, JA344.

STANDARD OF REVIEW

This case presents issues of constitutional law reviewed de novo by this Court. *See Anderson v. Sara Lee Corp.*, 508 F.3d 181, 191 (4th Cir. 2007); *Daly v. Hunt*, 93 F.3d 1212, 1216 (4th Cir. 1996).

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[8] *PJM Interconnection, LLC*, 143 FERC ¶ 61,090 (2013) at PP 120, 132, 143; *see also* JA270.

SUMMARY OF ARGUMENT

This appeal must be judged based on the strong presumption against preemption applicable to claims that federal law has displaced a State's exercise of its traditional powers. That presumption applies with special force under the FPA because the FPA preserved *the States'* authority over the matters at issue here: construction of new power plants to meet a State's electricity needs, and reliance upon a State's ratepayers to support that construction. The FPA granted *FERC* authority over the "sale of electric energy at wholesale," including whether prices for such sales are just and reasonable. The result is a framework that the Supreme Court has described as one of "interlocking regulation."

The legal consequence of this interlocking regulatory framework is that the circumstances under which preemption may be found are markedly limited. There is a continual, expected and permissible interaction between State and FERC authority. That a state program *affects* matters within FERC's control will not give rise to field preemption. Where States pursue permissible objectives, Congress anticipated federal "accommodation," not "preemption."

Indeed, it is especially important to avoid interpretations of federal law that would interfere with a State's performance of its responsibility to ensure adequate, reliable electric capacity. While promoting the construction of needed new power plants is a matter of national significance, Congress entrusted that responsibility to the States, not FERC.

There is no proper basis to find field preemption. Neither the Generation Order nor the CfDs govern capacity or energy sales agreements, or set rates for such purchases or sales. Accordingly, they do not intrude on FERC's authority to set rates for wholesale sales subject to its jurisdiction. EDCs do not buy capacity from CPV; PJM buys the capacity, but at rates determined by FERC to be just and reasonable. Payments made under the CfDs by the EDCs are made in consideration for CPV building and operating a new power plant to meet Maryland's electricity needs. They explicitly supplement – and do not supplant or displace – whatever market revenues CPV obtains by actually selling capacity or energy in the wholesale market under rules established, and rates determined, by FERC. The additional payments made under the CfDs, which support power plant construction, do not invade FERC rate-approval territory, but operate outside FERC's space entirely.

Equally important, even if the CfDs were subject to FERC jurisdiction, a state directive that its EDCs enter into contracts subject to FERC jurisdiction – which contracts FERC could approve or disapprove – does not lead to preemption. It simply reflects the ordinary operation of the FPA, under which FERC would have jurisdiction to judge the CfDs.

FERC has not even attempted to assert what would, at best, be doubtful jurisdiction over the CfDs. The district court's decision to take it upon itself to determine FERC's jurisdiction, and on that basis to preempt a traditional exercise of state authority, is precisely the kind of unwarranted expansion of federal authority, at the States' expense, that the case law cautions against.

FERC has accommodated its program of PJM-market supervision to state programs, such as those in Maryland and New Jersey, that support needed power plant construction. Maryland, in turn, has structured its program, and the CfDs, to respect and ensure CPV's participation in the FERC-supervised markets, and to respect FERC-approved rates. Such coordination between the States' programs and those of FERC, is not a sign of field preemption, but instead reflects how a "harmonious and comprehensive" framework of "interlocking" jurisdiction is supposed to work.

ARGUMENT

I. A STRONG PRESUMPTION AGAINST PREEMPTION APPLIES WHERE CONGRESS HAS EXPRESSLY PRESERVED STATE AUTHORITY

Federal law preempts state law when Congress says so expressly or where preemption is "implicitly contained in [a federal statute's] structure and purpose." *Gade v. Nat'l Solid Wastes Mgm't Ass'n*, 505 U.S. 88, 98 (1992) (internal quotation marks omitted). Courts recognize two forms of implied preemption.

Field preemption occurs "where the scheme of federal regulation is so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it"; and conflict preemption occurs "where compliance with both federal and state regulations is a physical impossibility, or where state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Id.* (internal quotation marks omitted).

Preemption analysis rests on two "cornerstones." *Wyeth v. Levine*, 555 U.S. 555, 565 (2009). The first is Congress's purpose, "the ultimate touchstone in every pre-emption case." *Id.* (internal quotation marks omitted). "[A] federal agency may pre-empt state law only when and if it is acting within the scope of its congressionally delegated authority." *New York v. FERC*, 535 U.S. 1, 18 (2002) (internal quotation marks omitted).

Second, "[i]n all pre-emption cases, and particularly in those in which Congress has legislated . . . in a field which the States have traditionally occupied . . . , we start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." *Medtronic, Inc. v. Lohr*, 518 U.S. 470, 485 (1996) (internal quotation marks omitted); *accord Altria Grp., Inc. v. Good*, 555 U.S. 70, 77 (2008); *see Anderson*, 508 F.3d at 192; *Pinney v. Nokia, Inc.*, 402 F.3d 430, 453 (4th Cir. 2005); *S. Blasting Servs., Inc. v. Wilkes Cnty.*, 288 F.3d 584, 589-90 (4th

Cir. 2002) ("Consideration under the Supremacy Clause starts with the basic assumption that Congress did not intend to displace state law.").

Congress cannot have expressed an intention to preempt state action where it has expressly preserved the States' authority to act. *See Nw. Cent. Pipeline Corp. v. State Corp. Comm'n*, 489 U.S. 493, 512-13 (1989). A statutory savings clause evinces the opposite intent. *See Chamber of Commerce of the U.S. v. Whiting*, 181 S. Ct. 1968, 1981 (2011) ("Given that Congress specifically preserved such authority for the States, it stands to reason that Congress did not intend to prevent the States from using appropriate tools to exercise that authority."); JA277. Thus, when faced with a statutory savings clause, the preemption inquiry focuses first on whether the State has acted within the scope of its preserved powers, and not on the effects of such within-scope action on the federal field. *See Nw. Cent. Pipeline*, 489 U.S. at 512-13.

II. THE FPA PRESERVES LONGSTANDING STATE AUTHORITY OVER GENERATING RESOURCES

The FPA's history speaks directly to the issue on appeal. Before the FPA, electricity regulation resided entirely with the States. *See New York*, 535 U.S. at 5. Local utilities built and operated power plants, and distributed electricity to their customers. JA209-10. State commissions set rates to allow utilities to recover prudently incurred costs and finance construction. JA210-11. Electric generation was deemed local in nature. *See Utah Power & Light Co. v. Pfost*, 286 U.S. 165, 181 (1932). *See generally* Everest Schmidt, *A Call for Federalism: The Role of State Government in Federally Controlled Energy Markets*, 65 Rutgers L. Rev. 573, 575-79 (2013).

Early in the twentieth century, utilities began to buy and sell electricity in interstate "wholesale" transactions, ensuring access to resources to meet peak demand. JA211. In 1927, the Supreme Court held that the Commerce Clause prohibited States from regulating interstate wholesale sales. *Pub. Util. Comm'n v. Attleboro Steam & Elec. Co.*, 273 U.S. 83, 89-90 (1927). That decision created a "regulatory gap," with no entity regulating these transactions. *New York*, 535 U.S. at 6; JA205-06. Congress filled this gap in 1935 with FPA Title II, Pub. L. 74-333, 49 Stat. 847 (codified as amended at 16 U.S.C. §§ 824-824h), vesting in what eventually became FERC authority over "transmission of electric energy in interstate commerce" and "sale of electric energy at wholesale in interstate commerce." 16 U.S.C. § 824(a), (b)(1).

The FPA expressly preserved the States' existing regulatory authority. Federal regulation extends "only to those matters which are not subject to regulation by the States." *Id.* § 824(a); *see also New York*, 535 U.S. at 6. FPA Section 201(b) provided that FERC "*shall not have jurisdiction*, except as specifically provided in this subchapter and subchapter III of this chapter, *over facilities used for the generation of electric energy*." 16 U.S.C. § 824(b)(1) (emphasis added). The FPA's history reveals a "constant purpose" to shield the States and "apportion federal and state jurisdiction over the industry." *Conn. Light & Power Co. v. FERC*, 324 U.S. 515, 525-531 (1945) *("CL&P")*.

Subsequent enactments have expanded FERC authority over interstate transmission and sales, but left unchanged the States' crucial responsibility – vital for States and for the Nation – to support new power plant construction. For example, while upholding FERC's authority to order utilities to provide access to unbundled transmission in interstate commerce, *New York*, 535 U.S. at 11, 23-24, the Supreme Court emphasized that "FERC has recognized that the States retain significant control over local matters," including "utility generation and resource portfolios." *Id.* at 24 (internal quotation marks omitted).

When the Energy Policy Act of 2005, Pub. L. No. 109-58, 119 Stat. 594, 16 U.S.C. §§ 824o-824w (2012), expanded FERC jurisdiction over transmission and reliability standards, Congress *declined* to allow FERC "to order the construction of additional generation or transmission capacity." 16 U.S.C. § 824o(i)(2). Instead, a savings clause preserved the States' authority over electric service reliability and adequacy:

> Nothing in this section shall be construed to preempt any authority of any State to take action to ensure the safety, adequacy, and reliability of electric service within that State, as long as such action is not inconsistent with any reliability standard . . . .

Id. § 824o(i)(3), *quoted in* JA208 n.11.

Indeed, FERC's own orders issued in connection with the issues in this case have expressly acknowledged the States' authority to ensure an adequate and reliable electricity supply. While FERC ensures that the RPM auctions produce just and reasonable rates, FERC's supervision of the auction was never intended to obstruct "state and local policies and objectives with regard to the development of new capacity resources, or unreasonably interfere with those objectives." *PJM Interconnection, LLC*, 137 FERC ¶ 61,145 (2011) at P 3. Rather, "[s]tate and municipal authorities retain the right to forbid new entrants from providing new capacity, to require retirement of existing generators, to limit new construction to more expensive, environmentally friendly units, or to take any other action in their role as regulators of generation facilities without direct interference from [FERC]." *Conn. Dep't of Pub. Util. Control v. FERC*, 569 F.3d 477, 481 (D.C. Cir. 2009) ("*CDPUC*").

In short, the "[n]eed for new power facilities, their economic feasibility, and rates and services, are areas that have been characteristically governed by the States." *Pac. Gas & Elec. Co. v. State Energy Res. Conservation & Dev. Comm'n*, 461 U.S. 190, 205 (1983) *("PG&E").*

III. THE BURDEN OF SHOWING FIELD PREEMPTION IS ESPECIALLY HIGH UNDER THE FPA WHEN THE STATE IS EXERCISING POWERS THAT CONGRESS ENTRUSTED TO IT

A. Federal Courts Should Resist Unwarranted Interpretations Of FERC Authority That Impair The States' Preserved Authority Under The FPA

Given the importance of the States' retained responsibilities within Congress' framework of divided responsibility, the presumption against preemption operates with particular force in energy matters. Courts must be careful not to extend federal authority in a way that intrudes on States' prerogatives and powers. *Nw. Cent. Pipeline*, 489 U.S. at 512 (cautioning against "an extravagant . . . mode of interpretation" extending FERC power into areas in which States have authority). With the FPA and subsequent statutes, Congress intended a "harmonious and comprehensive" division of "interlocking" jurisdiction between the States and FERC. *Id.* (internal quotation marks omitted); *Pub. Util. Comm'n of State of Cal. v. FERC*, 900 F.2d 269, 274-75 (D.C. Cir. 1990).[9] There is an inevitable interplay between wholesale rates supervised by FERC, which

[9] *Northwest Central Pipeline* construed federal-state jurisdiction under the Natural Gas Act. Because the relevant provisions of the FPA and the Natural Gas Act are "in all material respects substantially identical," there is an "established practice of citing interchangeably decisions interpreting the pertinent sections of the two statutes." *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981) (internal quotation marks omitted); *see Fed. Power Comm'n v. S. Cal. Edison Co.,* 376 U.S. 205, 211-12 (1964) ("[FPA § 201(b)] has its counterpart in § 1(b) of the Gas Act.").

necessarily impact decisions to build new power plants, and State decisions to support new plants, which impact wholesale rates. State programs will not be preempted merely because they impact wholesale rates within FERC's jurisdiction. *See Nw. Cent. Pipeline*, 489 U.S. at 512-13; *see also Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293, 308 (1988).

In *Northwest Central Pipeline*, the Court addressed whether a state regulation intended to encourage gas production, a state responsibility, 489 U.S. at 512-13, invaded federal territory because it impacted federally supervised rates. The Court rejected this notion, holding that where the industry "is subject to interlocking regulation by both federal and state authorities," *id.* at 506, the preempted field is necessarily narrowed, *see id.* at 510-11. To find preemption where state regulation simply impacts matters under FERC jurisdiction would erase the line drawn by Congress that guarantees the "States' retention of their traditional powers to regulate rates of production, conserve resources, and protect correlative rights." *Id.* at 514.

No penumbra of protection bars state actions that merely impact or border FERC-regulated matters. Indeed, courts have found the opposite. In *CDPUC*, the D.C. Circuit observed that a State's policy choices over generation capacity will "[o]f course . . . affect the pool of bidders in the [wholesale capacity] [m]arket, which in turn affects the market clearing price for capacity." 569 F.3d at 481.

"But this is all quite natural," and this interplay will not transform permissible state actions into preempted ones. *See id.*; *see also Nw. Cent. Pipeline*, 489 U.S. at 512-13.

Of course, where FERC has authority, such as over RPM administration, States structure their programs against the backdrop of FERC's initiatives. Maryland did that here by honoring the FERC-supervised PJM markets and insisting that its successful bidders participate in, and comply with, RPM requirements. On the other hand, because States are responsible for ensuring adequate and reliable electric service, FERC should accommodate state initiatives, as FERC did here. *Cf. Nw. Cent. Pipeline*, 489 U.S. at 517-18 (accommodation is inappropriate only where the state program's impact is "so extensive and disruptive" that "federal accommodation must give way to federal pre-emption.").

As to the courts, the Supreme Court's cases admonish lower courts to "take seriously the lines Congress drew in establishing a dual regulatory system," *id.* at 513, and to avoid interpreting federal authority so as to generate unwarranted interference with state initiatives. For example, as concerns nuclear power plant construction, the Court acknowledged the States' authority over the need "for new power facilities, their economic feasibility, and rates and services." *PG&E*, 461 U.S. at 205. At the margin, where a State's action could be characterized as preempted or not, the Court readily deferred to the State's asserted objectives, and found the State's actions to be outside the preempted sphere. *See id.* at 216.

Moreover, the Court has declined to resolve close jurisdictional issues abstractly, considering instead whether and how FERC or other agencies have actually asserted jurisdiction over the contested field. Thus, in *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, the Court found that state regulation of wholesale rates charged by rural electric cooperatives was not preempted under either the FPA or the Rural Electrification Act. 461 U.S. 375, 388-89 (1983). Even though the Rural Electrification Administration had "exclusive authority among federal agencies" over such cooperatives, its "refusal . . . to assert jurisdiction" over wholesale rates left the area open to state regulation. *Id.* at 384; *see also id.* at 388-89. Indeed, the Court has described the "bright line" between state and federal authority as turning not on the possibility of federal jurisdiction, but rather on whether FERC has, in fact, "properly exercised" its jurisdiction over a rate-related matter, thus precluding States from entering that field. *Miss. Power & Light Co. v. Miss. ex rel. Moore*, 487 U.S. 354, 374 (1988).

Within the framework of interlocking regulation, then, both FERC policy and federal preemption principles reflect the need to avoid unwarranted expansion of federal authority at the expense of the States' reserved powers.

B. Maryland's Actions Were Well Within Its Jurisdiction Over Generation Adequacy

The Generation Order's explicit purpose is to ensure an adequate electricity supply by supporting construction of a new, environmentally friendly power plant where needed. Maryland thus acted within the core of its historical mandate, in "a field that Congress expressly left to the States." *Nw. Cent. Pipeline*, 489 U.S. at 509. The means chosen are well-tailored to Maryland's goals, *see id.* at 513 n.10: The CfDs provide successful bidders a stable revenue stream through a financial support mechanism tied directly to traditional state jurisdiction over locally regulated EDCs and retail rates. Plaintiffs-Appellees concede that this encourages new construction. *See* JA42 ¶ 6 (CfDs "provide additional, state-directed incentives for investment."). Where a state regulation has a proper purpose, and its strategy is plausibly tethered to state authority, that is strong evidence that the regulation is permissible. *See Nw. Cent. Pipeline*, 489 U.S. at 513 n.10.

IV. THE GENERATION ORDER OPERATES OUTSIDE FERC'S JURISDICTION

The stakes here are very high. Ensuring that new power plants are built to meet the Nation's needs is a State, not a FERC, responsibility. The proposition that the States cannot support new construction using all of the traditional tools at their disposal, including ratepayer-supported subsidies, would circumscribe state power in ways that Congress could neither have anticipated nor desired given the importance of new energy generation to the Nation's welfare. Plaintiffs-Appellees have not met their burden of showing preemption.

A. Plaintiffs-Appellees' Theory That FERC Has Displaced State Efforts To Encourage New Power Plant Construction Is Unsupported

Much of Plaintiffs-Appellees' preemption argument was based on their assertion that FERC decided "that a market-based approach is the most efficient means of determining the wholesale price of energy and capacity, and signaling when and where new generation capacity is needed in PJM to meet reliability needs." JA44 ¶ 13. In arguing conflict preemption, Plaintiffs-Appellees claimed that the MPSC intruded into this free-market field by encouraging construction with a subsidy outside the market. JA64-65 ¶ 76.[10]

Yet Plaintiffs-Appellees' thesis that *only* "FERC's market-based policies" may determine whether new capacity should be constructed is unsupportable. *See* JA65 ¶ 76. FERC has never said that, nor has Congress authorized it. The claim contradicts the clear reservation to the States of their time-honored role in ensuring adequate and reliable electricity supplies, irrespective of whether the PJM markets or any other market forces alone satisfy those needs.

[10] FERC has no authority to order the construction of new generating plants, *see* 16 U.S.C. § 824(b); *see also CDPUC*, 569 F.3d at 481; JA283-84.

While FERC has noted that RPM auctions provide information about future capacity needs and could encourage new construction, that does not mean that one market *alone* – whether the "free market" writ large, the longstanding market for long-term bilateral energy or capacity sales contracts, or the RPM three-year forward capacity auction market – must be the exclusive source of power plant construction incentives.

To the contrary, public policy and planning play key roles in determining resource adequacy and new construction needs. As the Generation Order demonstrates, States may react to a looming crisis more quickly and effectively than the RPM market. States may look farther than three years into the future to assess long-term needs, and may consider environmental and other concerns that the RPM market does not, and was never intended to, address. Thus, the States' role is vital. But even if Congress or FERC could displace the States from their historical role, they have not done so, and certainly have not done so "clear[ly] and manifest[ly]." *See New York*, 535 U.S. at 18 (internal quotation marks omitted).

Indeed, FERC's response to the Generation Order (and similar state initiatives) belies the assertion that the RPM displaces the States. FERC has stated consistently that although resource adequacy is a "complex matter" at "the confluence of state-federal jurisdiction," FERC will "defer" to state and local entities' role in ensuring resource adequacy when possible, while also ensuring just and reasonable wholesale rates. *PJM Interconnection, LLC*, 119 FERC ¶ 61,318 (2007) at P 40 (internal quotation marks omitted).

Thus, responding to objections concerning State-sponsored CfD-supported generator participation in RPM, FERC modified the rules to allow those resources to participate competitively. Specifically, in 2011 FERC revised the minimum offer price rule to "reconcile the tension that has arisen between policies enacted by states and localities that seek to construct specific resources, and our statutory obligation to ensure the justness and reasonableness of the prices determined in the RPM." 137 FERC at P 4. FERC thus ensured that state-sponsored resources could participate in RPM, concluding that any such resource satisfying the modified rule is "a competitive resource and should be permitted to participate in the auction . . . *regardless of whether it also receives a subsidy*." *Id.* at P 133 (emphasis added). FERC explained that its new rule

> does not interfere with states or localities that, for policy reasons, seek to provide assistance for new capacity entry if they believe such expenditures are appropriate for their state. We only seek to ensure the reasonableness of the wholesale, inter-state prices determined in the markets PJM administers.

Id. at P 89. With these revisions, FERC confirmed that the PJM market would yield just and reasonable results, and that the 2012 auction *had* yielded just and reasonable results. 143 FERC at PP 132, 143.

B. FERC's Ratemaking Authority Does Not Preempt Maryland's Generation Order

The district court did not reach Plaintiffs-Appellees' conflict preemption theory that the Generation Order was preempted because it provided state-supported incentives for new plant construction. It held instead that the Generation Order was preempted because it "establishe[d] the price ultimately received by CPV for its actual physical energy and capacity sales to PJM in the PJM Markets." JA292. But the district court erred in finding that the CfDs set capacity or energy sale prices subject to FERC jurisdiction, and erred even more fundamentally in holding that its interpretation of FERC jurisdiction gave rise to *preemption* of Maryland's Generation Order.

1. At the outset, the district court disregarded the teachings of *Northwest Central Pipeline* and its progeny, which caution against conceiving needless jurisdictional conflicts between state and federal authority that would restrict the States' ability to fulfill their own responsibilities.

The court disputed that the Generation Order merited even the ordinary "strong presumption against preemption" applicable where States exercise traditional authority. JA309 n.60 (citing *United States v. Locke*, 529 U.S. 89, 108

(2000)).[11] The court's skepticism was unwarranted. As the district court acknowledged, the State's objective to encourage construction of power plants is a matter of traditional state responsibility. *See* JA283-84.

The court's stated concern was not with the State's objective, but with its method, which it saw as nontraditional. But that concern was equally misguided. Requiring local utilities to enter into long-term contracts to support new power plant construction, with ratepayers underwriting related costs, are time-honored tools. Payments by EDCs, passed through to ratepayers, have long been employed both to support new construction and to subsidize other initiatives such as renewable energy credits.[12] Indeed, the district court's own explanation why the presumption against preemption was inapplicable was circular, as it first assumed that the Generation Order intruded on FERC's ratemaking authority by setting wholesale capacity prices, and on that basis found the presumption inapt. *See*

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[11] *Locke* involved maritime commerce, a field in which the federal presence is longstanding and dominant. *See* 529 U.S. at 108. Here, by contrast, the States' role in energy matters long predated any federal involvement.

[12] *See, e.g.*, Steven Ferrey et al., *Fire And Ice: World Renewable Energy And Carbon Control Mechanisms Confront Constitutional Barriers*, 20 Duke Envtl. L. & Pol'y F. 125, 145 n.100 (2010); *see also Wheelabrator Lisbon, Inc. v. Conn. Dep't of Pub. Util. Control*, 531 F.3d 183, 189 n.10, 190 (2d Cir. 2008) ("[FERC has] explicitly acknowledge[d] that state law governs the conveyance of [renewable energy credits].").

JA310 n.60 ("Regulating in the field of wholesale price-setting is occupied by FERC, so therefore the strong presumption against preemption is not present.").

In light of the presumption against preemption, and the Supreme Court's admonition that courts should guard against extravagant expansions of federal authority at the expense of the States', *see Nw. Cent. Pipeline*, 489 U.S. at 512, the district court's conclusion that the Generation Order invades FERC's exclusive authority over wholesale ratemaking cannot be sustained.

2. The district court erred further in equating payments under the CfDs with an "ultimate price" for capacity or energy sales subject to FERC jurisdiction. The CfDs' subsidy/rebate arrangement is not a "price" for a FERC-jurisdictional "wholesale sale." The CfD is a contract that supports the power plant's construction by providing a subsidy or rebate, separate and apart from the wholesale price bid by CPV into the RPM, and from any revenues received by CPV from that market. And any payments to be made under the CfD are made by an EDC, which is not a party to any such purchase and sale transaction. In short, the actual capacity sale, in the RPM, will be to PJM at the RPM price, subject to FERC jurisdiction; the EDCs purchase no capacity or energy from CPV. Whether as a subsidy or rebate, CfD payments are consideration for CPV's agreement to build and operate a new power plant to meet Maryland's electricity needs.

The district court viewed the CfD requirement that CPV sell its capacity into the wholesale market as transforming the CfD itself into a FERC-jurisdictional capacity delivery contract. *See* JA301-03. But this view conflates two different transactions. *See* JA220, 222, 226, 233. The sale involving capacity "delivery" is CPV's sale to PJM, the buyer in the RPM auction, and is a wholesale sale subject to FERC jurisdiction. PJM is not a party to the CfD. When PJM buys capacity from CPV, PJM will pay CPV the FERC-approved price, just as is paid any other capacity resource that clears the auction.

CfD payments are furnished separately, outside of RPM, by different parties – the ratepayers, through the EDCs – in exchange for CPV's agreement to construct a plant. Plaintiffs-Appellees themselves explained that the Generation Order creates a price guarantee "outside of the auction," JA68 ¶ 83(b), and the district court accepted this characterization. JA292. But the CfDs' requirement that CPV sell its energy and capacity through the PJM auction mechanisms, and the use of the auction revenue as a baseline, or yardstick, for determining the yearly subsidy or rebate, does not make that yearly differential payment an energy or capacity sale subject to FERC jurisdiction. The differential payment reflects basic economics: It would make no sense for the State to support (or pay for) the construction of a plant whose output will not be sold, or whose sales' revenues do not offset the State's subsidy payment.

The district court emphasized that CPV's sales of energy and capacity into the wholesale market was a "central component" of the Generation Order. JA302. But that observation is beside the point. The State and its ratepayers certainly expect to benefit in important and permissible ways from CPV's power plant; these benefits will flow from the availability of this plant in the market. That would be true of any form of subsidy. That the State and its ratepayers will ultimately benefit from the sales of energy and capacity does not make them parties to any FERC-jurisdictional sale of energy or capacity.

Like any hedge, the CfD provides a stable yearly revenue, with Maryland ratepayers assuming the risk of yearly PJM-market short-term price volatility that otherwise would have been borne by the new generator. In return, the ratepayers obtain the construction of a new power plant. FERC has long recognized that it does not have jurisdiction over transactions that do not involve the actual physical purchase and sale of power or capacity, but instead are financial. *See Mkt.-Based Rates for Wholesale Sales of Elec. Energy, Capacity & Ancillary Servs. by Pub. Utils.*, 119 FERC ¶ 61,295 (2007) at P 1,062 n.1201 (disclaiming jurisdiction over contracts "designed to assist buyers and sellers of electricity in hedging against adverse price changes which are settled in cash and where parties do not take actual delivery of the electricity").[13]

The district court's further conclusion that a CfD "is not a *purely* financial contract," JA294 (emphasis added), is likewise beside the point. The proper question is whether the CfD usurps FERC jurisdiction. Various "performance" elements on which the court relied to find it not "purely" financial, such as the obligation to build a plant, JA298, are themselves not energy sales subject to FERC jurisdiction. Those that are – the capacity sales that CPV will make – remain fully subject to FERC's authority, and will be made at FERC-regulated prices.

The case law distinguishes between contracts that "directly govern[] the rate in a jurisdictional sale" (FERC jurisdictional), and those like the CfDs that indirectly affect rates (not FERC jurisdictional). *See, e.g.*, *Cal. Indep. Sys. Operator Corp. v. FERC*, 372 F.3d 395, 403 (D.C. Cir. 2004) (alteration in original) *("CAISO")*. In construing FERC's FPA ratemaking authority, *CAISO* drew upon analogous provisions of the NGA, and noted that "[c]ontracts that 'affect' a rate indirectly [] are beyond [NGA] § 5's reach" of setting just and

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[13] *See also Revised Pub. Util. Filing Requirements*, 97 FERC ¶ 61,317 (2001), at *4-5; *N.Y. Mercantile Exch.*, 74 FERC ¶ 61,311, (1996) at 61,986-87 (FERC has no jurisdiction over a futures contract that can be settled financially, unless the contract goes to delivery, involves energy in interstate commerce, and seller is a public utility.).

reasonable rates. *Id.* (internal quotation marks omitted; alterations added). FERC's jurisdiction is "limited to contracts [] which directly govern[] the rate in a jurisdictional sale – providing for the rate in whole or in part, or specifying or embodying it, or setting forth rules by which it is to be calculated." *Id.* (internal quotation marks omitted; first alteration added). The CfDs do not "directly govern" the rate in the RPM auction or any other jurisdictional sale.

Indeed, it is far-fetched to suggest that the FPA (or FERC) would preempt Maryland from using tax subsidies to facilitate the construction of an environmentally friendly plant, where its capacity would be sold into the wholesale market, and the extent of Maryland's subsidy would depend on the developer's actual annual market revenues. That the subsidy or rebate here is channeled through the EDCs to ratepayers – rather than being funded by taxpayers generally – does not bring it within FERC's exclusive ratemaking jurisdiction over the actual wholesale sale and delivery of capacity or energy.

In short, FERC does not have jurisdiction over the CfDs.

3. Even if FERC did have jurisdiction over the CfDs as embodying a jurisdictional sale, that would not give rise to preemption, but rather simply to a requirement that the CfDs be submitted for FERC approval. Thus, if the CfDs are, as Judge Garbis suggested, bilateral capacity sales agreements subject to FERC jurisdiction, then they are properly to be considered under, but not preempted by,

the FPA. *See NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n*, 558 U.S. 165, 171 (2010) ("The [FPA] allows . . . sellers and buyers [to] agree on rates by contract."). Under that scenario, the CfDs may be challenged, at which point FERC can decide its own jurisdiction and, if appropriate, determine whether the CfDs are just and reasonable. *See id.* (citing 16 U.S.C. § 824e(a)). That determination can be made only by FERC, not a federal court. *See Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 577 (1981). Agreements subject to FERC authority do not usurp FERC authority. Thus, even if the district court were correct that the CfDs are FERC-jurisdictional, they would not be preempted, but would simply fall within FERC's jurisdiction to judge.

4. The district court further overreached by analyzing difficult issues concerning FERC's jurisdiction without any showing that FERC has, in fact, "properly exercised its jurisdiction" over the CfDs. *Miss. Power & Light*, 487 U.S. at 374. Absent FERC action, such an abstract inquiry risks what the cases warn against: an hypothesized conflict of jurisdiction, based on an extravagant view of the federal role, at the expense of a responsibility entrusted to the States. *See Nw. Cent. Pipeline*, 489 U.S. at 512. Even if it plausibly could be argued that FERC could assert jurisdiction over the subsidy-rebate structure of the CfDs, FERC might decline to do so, precisely because the arrangement falls within traditional state authority. *See New York*, 535 U.S. at 22-24, 26-28 ("[FERC] had discretion to

decline to assert such jurisdiction . . . in part because of the complicated nature of the jurisdictional issues.”).

On the borderline between FERC and state authority, the Supreme Court has focused on whether FERC *has* asserted its authority, and whether that assertion of authority was proper. *Miss. Power & Light*, 487 U.S. at 380-82 (1988) (Scalia, J., concurring in the judgment). The “bright line” defining the respective areas of State and FERC authority turns on whether FERC actually and properly asserted jurisdiction, not whether it might debatably do so. *See id.* at 374.

“There may come a time when the [agency] changes its present policy,” *Ark. Elec. Coop.*, 461 U.S. at 388, and asserts jurisdiction over this type of subsidy arrangement. That would be the time to determine whether the assertion of jurisdiction is proper and whether the CfDs are just and reasonable. But absent an actual conflict between the Generation Order and “particular [FERC] regulations,” or obstruction of “important federal interests,” a court should refrain from “assum[ing] that such a hypothetical event is so likely to occur as to preclude” state action in the disputed field. *Id.* at 389. This is especially so here, where FERC has determined that so long as the CfD-supported generator complies with RPM auction rules it “is a competitive resource and should be permitted to participate in the auction regardless of whether it also receives a subsidy.” 135 FERC at P 177.

In passing, the district court cited *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 (1986), *Mississippi Power & Light*, 487 U.S. 354, and *Entergy Louisiana, Inc. v. Louisiana Public Service Commission*, 539 U.S. 39 (2003), as supporting exclusive FERC ratemaking authority, but without actually considering the filed rate doctrine on which those cases rest. *See* JA280-81. In fact, the filed rate cases highlight the district court's overreach in conceiving a jurisdictional conflict where none exists. The filed rate doctrine prohibits a State from denying effect to a FERC-approved rate. *See Nantahala*, 476 U.S. at 962. In each of the cited cases, FERC asserted jurisdiction and in each case, the State's failure to give effect to the FERC-authorized rate was manifest in the creation of a potential trapped cost that would effectively deny the benefit of the FERC-authorized rate to the purchasing party. *See, e.g.*, *Entergy*, 539 U.S. at 49 ("[The State's] order impermissibly 'traps' costs that have been allocated in a FERC tariff."). The Generation Order does no such thing. It does not undermine the FERC-approved rate or deny it effect. It *accepts* the FERC-approved RPM rate as a given, simply using it as the baseline for computing a separate, additional payment obligation under the CfD.

By providing for supplemental payments, beyond what the plant earns by selling in the wholesale market, the Generation Order supports construction of a needed power plant providing a source of clean energy. Given the structure of the

FPA, and the strong presumption against preemption, there is no basis here to conclude that Congress or FERC has expressed a "clear and manifest" intention to preempt the Generation Order.

CONCLUSION

The district court judgment should be reversed.

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Respectfully submitted,

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TYPE-VOLUME CERTIFICATION

This brief complies with the type-volume limitation in Fed. R. App. P. 32(a)(7)(B), because this brief contains 8,308 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). The "Word Count" function of Microsoft Word 2010 was used for this purpose.

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CERTIFICATE OF SERVICE

I hereby certify that I have on this 4th day of February, 2014, caused the foregoing brief to be served upon each party identified in the attached service list, via email through the Court's CM/ECF system or via U.S. Mail, first class, postage prepaid. I further certify that on this day eight hardcopies of this brief are being sent to the Clerk of Court via overnight delivery.

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