NOS. 13-2419 (L); 13-2424 (CONS.)

IN THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

PPL ENERGYPLUS, LLC, ET AL.
Plaintiffs-Appellees,

v.

DOUGLAS NAZARIAN, ET AL.,
Defendants-Appellants.

On Appeal from the United States District Court
for the District of Maryland

BRIEF OF THE ELECTRIC POWER SUPPLY ASSOCIATION AND THE EDISON ELECTRIC INSTITUTE AS *AMICI CURIAE* IN SUPPORT OF APPELLEES

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UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT
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No. 13-2419 Caption: PPL EnergyPlus, LLC v. Nazarian

Pursuant to FRAP 26.1 and Local Rule 26.1,

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(name of party/amicus)

who is amicus curiae, makes the following disclosure:
(appellant/appellee/petitioner/respondent/amicus/intervenor)

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Amicus does not have a direct financial interest in the outcome of this litigation. We are aware of no entity, other than the parties to this appeal, that may have direct financial interests in the outcome of this litigation.

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6. Does this case arise out of a bankruptcy proceeding? ☐ YES ☑ NO
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Signature: /s/ Ashley C. Parrish Date: 3/17/14

Counsel for: Electric Power Supply Association

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I certify that on 3/17/14 the foregoing document was served on all parties or their counsel of record through the CM/ECF system if they are registered users or, if they are not, by serving a true and correct copy at the addresses listed below:

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STATEMENT OF INTEREST[1]

This appeal focuses on the Federal Power Act's bright line division of jurisdictional authority between state and federal regulators. The disposition of this appeal will have direct impacts on the wholesale markets regulated by the Federal Energy Regulatory Commission ("FERC"). It could also affect the delicate balance between competing policy objectives that FERC has achieved in approving the market rules for wholesale sales of energy and capacity within the multi-state region administered by PJM Interconnection, L.L.C. ("PJM").

Amici the Electric Power Supply Association ("EPSA") and the Edison Electric Institute ("EEI") are two of the power industry's leading trade associations, with members that operate across the country, including in the region administered by PJM. Through this brief, they seek to inform the Court of their perspectives on the important preemption issues raised in this appeal. They also seek to emphasize that the district court's judgment below can and should be affirmed without

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[1] All parties have consented to the filing of this brief. No counsel for any party authored this brief in whole or part; no party or counsel made a monetary contribution intended to fund the preparation or submission of this brief; and no person other than *amici curiae* made such a contribution.

impeding appropriate efforts by states to exercise their traditional powers to encourage generation development and promote reliability.

EPSA and EEI have a strong interest in this appeal because the Maryland Public Service Commission's order directly and adversely affects members of EPSA and EEI that participate in the organized wholesale energy and capacity markets. In particular, the Maryland Commission's order creates incentives for CPV to submit below-cost offers into capacity markets administered by PJM under rules on file with, and approved by, FERC. As a result, the order interferes with the markets' ability to produce just and reasonable rates, including by potentially changing the rates paid to EPSA and EEI members and others participating in those markets.

Equally important, because EPSA's and EEI's members are often subject to regulation at both the state and federal level, they have a significant interest in ensuring that the jurisdictional lines established under the Federal Power Act are respected, and that the markets regulated by FERC operate properly for the benefit of all market participants. The associations also have a strong interest in ensuring that states are not permitted to interfere with FERC's exclusive authority to regulate the organized wholesale markets in which their members participate.

INTRODUCTION AND SUMMARY OF ARGUMENT

The Federal Power Act grants FERC broad and exclusive jurisdiction over the transmission and sale of "electric energy at wholesale in interstate commerce." 16 U.S.C. §§ 824(b), 824d(a), 824e. That authority includes responsibility for ensuring that "rates and charges made, demanded, or received . . . for or in connection with the transmission or sale" of electricity at wholesale are "just and reasonable." *Id.* § 824d(a). It also obligates FERC to eliminate "unduly discriminatory or preferential" practices that might prevent market participants from competing on an even playing field. *Id.* § 824e(a).

Exercising this exclusive authority, FERC has approved competitive markets in the PJM region and market rules designed to ensure that wholesale rates are just and reasonable and not unduly discriminatory. The market rules allow suppliers within the multi-state region to compete for the opportunity to sell energy and capacity by participating in carefully structured market "clearing" processes. Among other things, suppliers submit offers of energy and capacity into the markets, and PJM accepts the offers from lowest to highest until it has secured a sufficient supply of energy or capacity. In each case, the highest offer accepted sets the "clearing price" paid to all suppliers offering at or below that price. FERC has determined that the rates set through these market processes are just and reasonable. When a supplier submits below-cost offers because it is recovering those costs through payments received outside the market, however, resources that are more economic will be displaced and the clearing price will be artificially suppressed, which will prevent the market from functioning as FERC intended.

Until the late 1990's, Maryland's utilities were vertically integrated, meaning that the same companies generated, delivered, and sold power to state retail consumers. In 1999, however, Maryland chose to end traditional retail regulation and to restructure its markets so that electricity sold to Maryland consumers is purchased from the organized PJM wholesale markets regulated by FERC. *See generally* Appellees' Br. 7–8. By making that decision, Maryland ensured that its consumers would share in the significant benefits provided by competitive markets, but it also agreed that it would comply with the market rules established by FERC for PJM's wholesale markets.

Against this backdrop, this case requires the Court to consider the legality of an order by the Maryland Commission that changes the rates paid to CPV for energy and capacity sold through the multi-state organized markets administered by PJM and distorts the clearing price in the capacity markets paid to all suppliers in that market. In the proceedings below, after a trial that spanned six days with extensive evidence and testimony from multiple witnesses, the district court made careful credibility determinations and issued a 149-page opinion finding that the Maryland Commission's order sets wholesale rates and is therefore preempted by federal law. *Amici* agree with appellees that the district court's findings of fact are entitled to deference, and that its judgment is correct and should be affirmed. *See* Appellees' Br. 22, 33, 55.

The purpose of this brief is to assist the Court by providing an industry-wide perspective on the negative implications of the Maryland Commission's order on the regulation and operation of organized wholesale markets such as those administered by PJM. The brief has three sections: Section I elaborates on arguments advanced in appellees' brief explaining why the Maryland Commission's order is preempted — both because it invades FERC's field of exclusive jurisdiction over wholesale sales of energy and capacity, and because it conflicts with federal law by interfering with the carefully structured PJM market rules approved by FERC. Section II responds to appellants' principal arguments against preemption and explains why they lack merit. Section III emphasizes that the Court can and should affirm the district court's judgment below without impairing a state's ability to take steps in appropriate circumstances to encourage generation development and promote reliability. This case does not require any curtailment of traditional state authority, but it does require confirming that, as the district court concluded, states have no authority to invade FERC's exclusive jurisdiction by changing the wholesale rates paid for energy and capacity cleared through the PJM markets.

ARGUMENT

I. The Maryland Commission's Attempt To Regulate Wholesale Rates Impermissibly Intrudes On FERC's Exclusive Jurisdiction.

The district court correctly determined that the Maryland Commission's order intrudes on FERC's exclusive jurisdiction because it attempts to change the rates paid for wholesale sales of energy and capacity. As appellees explain, the district court's findings of fact are entitled to deference and should be respected. *See* Appellees' Br. 22, 33, 55; *see also, e.g.*, *United States v. Grimmond*, 137 F.3d 823, 827–31 (4th Cir. 1998) (factual findings are entitled to deference unless clearly erroneous). Moreover, although the district court did not reach the issue of conflict preemption, Mem. 111–14 (Sept. 30. 2013) (JA310–13), the Maryland Commission's order is also preempted on that basis because it impermissibly interferes with, and seeks to impose the state's policy preferences on, the wholesale capacity market regulated by FERC. Under settled principles of preemption law, the Maryland Commission's order should not be allowed to stand.

A. The Federal Power Act Grants FERC Exclusive Jurisdiction Over Wholesale Sales Of Electricity.

Under the Supremacy Clause of the U.S. Constitution, state laws that contravene federal law are "void" and "without effect." *Maryland v. Louisiana*, 451 U.S. 725, 746–47 (1981). State laws are preempted "when the scope of a [federal] statute indicates that Congress intended federal law to occupy a field exclusively." *Freightliner Corp. v. Myrick*, 514 U.S. 280, 287 (1995); *see also Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 248 (1984). State laws are also preempted when they impermissibly conflict with federal law, either because they "stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," *Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293, 298 (1988), or because "compliance with both federal and state regulations is a physical impossibility." *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142–43 (1963).

In the case of the Federal Power Act, the statutory scheme renders unnecessary any "case-by-case analysis of the impact of state regulation upon the national interest." *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 966 (1986) (internal quotation marks and citation omitted). The Act grants FERC "*exclusive* authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce," *New England Power Co. v. New Hampshire*, 455 U.S. 331, 340 (1982) (emphasis added), as well as *exclusive* jurisdiction over any matters that "directly affect[] . . . wholesale rates." *Nantahala*, 476 U.S. at 966–67 (1986); *see also* 16 U.S.C. §§ 824(a), 824d(a), 824d(c), 824e(a). The Act thus draws a "bright line easily ascertained, between state and federal jurisdiction" and leaves "no power in the states to regulate . . . sales for resale in interstate commerce." *FPC v. S. Cal. Edison Co.*, 376 U.S. 205, 214–16 (1964).

Interpreting these provisions, the Supreme Court has long recognized that the Federal Power Act occupies the field with respect to the transmission and wholesale sale of electric energy in interstate commerce, and that any attempts by states to regulate within that field are preempted. *See, e.g.*, *Entergy La., Inc. v. Louisiana Pub. Serv. Comm'n*, 539 U.S. 39 (2003); *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354 (1988); *Nantahala*, 476 U.S. 953. Moreover, in recognition of FERC's exclusive jurisdiction over wholesale sales, the Supreme Court has held that "the right to a reasonable rate is the right to the rate" that FERC "files or fixes." *Montana-Dakota Utils. Co. v.*

Northwestern Pub. Serv. Co., 341 U.S. 246, 251 (1951). That principle, known as the "filed rate doctrine," is intended to "preserv[e] . . . the agency's primary jurisdiction over reasonableness of rates" by ensuring "that regulated companies charge only those rates of which the agency has been made cognizant," *Arkansas La. Gas Co v. Hall*, 453 U.S. 571, 577–78 (1981), and by prohibiting states from "usurp[ing] a function that Congress has assigned" to FERC. *Id.* at 582.

As the district court recognized, regulatory oversight of the electric industry is divided by a "bright line" drawn by Congress granting FERC exclusive jurisdiction over wholesale sales while reserving to the states jurisdiction over retail sales. *See* Mem. 77–78, 82 (JA276–77, 281) (discussing "dual federal/state regulatory regime"). Contrary to CPV's assertions, *see* CPV Br. 20–23, this "interlocking jurisdiction" over the industry does not allow for any "presumption against preemption" where wholesale sales subject to FERC's jurisdiction are involved. *See* Appellees' Br. 24–25. States have no authority to regulate interstate electric transactions, including transactions occurring in the multi-state region administered by PJM. *See Public Utils. Comm'n of R.I. v. Attleboro Steam & Elec. Co.*, 273 U.S. 83, 90 (1927).

Moreover, when Congress enacted the Federal Power Act, it "authorized federal regulation not only of wholesale sales that had been beyond the reach of state power, but also the regulation of wholesale sales" that had "previously [been] subject to state regulation" because they "did not directly burden interstate commerce." *New York v. FERC*, 535 U.S. 1, 21 (2002). Accordingly, as even the case on which CPV primarily relies makes clear, state regulations that "impinge[] on the comprehensive federal scheme regulating interstate" sales and rates cannot be permitted to stand. *Northwest Cent. Pipeline Corp. v. State Corp. Comm'n of Kan.*, 489 U.S. 493, 512 (1989). The presumption against preemption does not apply because the regulation of wholesale sales is an area "where there has been a history of significant federal presence." *United States v. Locke*, 529 U.S. 89, 108 (2000)*; see also Public Util. Dist. No. 1 of Grays Harbor v. IDACORP, Inc.*, 379 F.3d 641, 648 n.7 (9th Cir. 2004) (presumption against preemption "is almost certainly not applicable here because the federal government has long regulated wholesale electricity rates").

B. The Maryland Commission's Order Is Preempted Because It Changes And Directly Affects Rates For Wholesale Sales.

The Maryland Commission's order is preempted for two reinforcing reasons: *First*, by changing the compensation paid for sales of energy and capacity cleared in the PJM market, the order impermissibly invades a field that Congress exclusively reserved to FERC. *Second*, the Maryland Commission's order impermissibly conflicts with federal law by interfering with the FERC-approved market rules that govern PJM's energy and capacity markets.

1. The Maryland Commission's Order Impermissibly Changes The Rate Paid For Sales Through PJM's Energy And Capacity Markets.

The purpose and practical effect of the Maryland Commission's order is to change wholesale rates by compensating one generator, CPV, for the energy and capacity it sells in the organized multi-state markets administered by PJM at a price that differs from the market clearing price set through the processes approved by FERC. The Maryland Commission's order thus invades the field of FERC's exclusive jurisdiction over the rates "made, demanded, or received . . . for or in connection with" interstate wholesale sales. 16 U.S.C. § 824d(a). It is therefore preempted. *See generally* Appellees' Br. 22–42.

After a lengthy trial and considering extensive evidence, the district court found that the Maryland Commission's order changes the rates that CPV will be paid for wholesale energy and capacity sales in the PJM markets. *See, e.g.*, Mem. 86–87 (JA285–86). Appellants have made no showing that those findings are clearly erroneous. Instead, they urge the Court to make new factual findings and conclude that the Maryland Commission has merely encouraged CPV to construct a new power plant. *See* CPV Br. 16–20; MDPSC Br. 18–19. In their view, the Maryland Commission's order did not intrude on FERC's exclusive jurisdiction because the state-mandated payments are "not a 'price' for a FERC-jurisdictional 'wholesale sale,'" but instead merely serve as "a subsidy or rebate" in "consideration for CPV's agreement to build and operate a new power plant to meet Maryland's electricity needs." CPV Br. 30.

There is no basis for appellants' proposed alternative factual findings as to what the Maryland Commission's order requires. The contract payments are not just tied to the successful construction of new generating facilities; payment is "directly contingent upon CPV's clearing capacity" through the wholesale capacity auctions administered by PJM. Mem. 100 (JA299). As the district court found, "[e]ven if CPV constructs and operates" its new generating facility, it "will receive no payment under the compensation scheme if it does not clear capacity in" PJM's capacity auction. *Id.* at 100–101 (JA299–300). The district court also found that the CPV contracts require CPV to offer its energy into the PJM energy market, and that the payment to CPV is calculated "based on CPV's physical energy and capacity sales into the PJM Markets." *Id.*at 99 (JA298); *see also id.* at 102–05 (JA301–04) (noting former Maryland Commission Chairman Nazarian's acknowledgment that physical deliveries of energy and capacity by CPV into the PJM markets were a critical component of the Commission's order and the CPV contracts).

The Maryland Commission's order thus requires CPV to sell energy and capacity into the PJM wholesale markets and mandates that CPV be compensated for energy and capacity sold into the PJM market at prices different from the PJM market clearing prices. As the district court correctly determined, the Maryland Commission's order is therefore preempted. Because Congress granted FERC exclusive jurisdiction over wholesale rates, Maryland cannot lawfully alter those rates either directly by establishing "a 'price' of a FERC-jurisdictional 'wholesale sale,'" or less directly (but no less significantly) by making payments for energy and capacity sold through the PJM market as a subsidy or rebate. *See Silkwood*, 464 U.S. at 248 ("any state law falling within [an exclusively federal] field is preempted"); *cf. Altamont Gas Transmission Co. v. FERC*, 92 F.3d 1239, 1248 (D.C. Cir. 1996) (agency may not "do indirectly what it [may] not do directly").

There is likewise no merit to appellants' argument that, contrary to the district court's findings, the CPV contracts are "contracts for differences" that are structured as "hedges," or "financial" arrangements that fall beyond the scope of FERC's exclusive jurisdiction. *See, e.g.*, CPV Br. 32; MDPSC Br. 23. By paying CPV for energy and capacity cleared in PJM's markets, the state-mandated contracts set the terms and conditions of wholesale sales of energy and capacity and thus overstep the jurisdictional boundaries delineated by the Federal Power Act. *See* 16 U.S.C. § 824b.

CPV is also wrong in arguing that because "CPV sells neither energy nor capacity to the [electric distribution companies]," CPV Br. 2, and because "payments are furnished separately, outside of" PJM's capacity market, they should not be deemed to alter the wholesale price for capacity sold through the PJM capacity auctions. *Id.* at 31. The

Federal Power Act regulates the "rates and charges made, demanded, or received by any public utility for or in connection with . . . [the] sale of electric energy" subject to FERC's jurisdiction — *i.e.*, what public utilities are paid for electricity sold — not what purchasers pay for electricity purchased. 16 U.S.C. § 824d(a). It is irrelevant to the preemption analysis that the electric distribution companies "purchase no capacity or energy from CPV." CPV Br. 30. What is relevant — and fatal to appellants' case — is that the state-mandated payments are consideration for CPV's *sale* of energy and capacity to PJM. *See* Mem. 99 (JA298) (contract "mandates a financial settlement only if CPV clears the [capacity auction] in any given year" and settlement is "based on CPV's physical energy and capacity sales into the PJM Markets").

The Maryland Commission's observation that FERC does not "set rates in the first instance" and that rates are instead initially set by public utilities, MDPSC Br. 17, is also beside the point. The relevant rates in this case are the market rules governing PJM's organized markets, which were set "in the first instance" by PJM and accepted by FERC. The Maryland Commission's assertions that the CPV contracts are no different from any other bilateral contract (where buyers and sellers set the rate for wholesale sales as between themselves), *see* MDPSC Br. 17–18, ignores that PJM is the buyer in this instance. CPV Br. 8 (the contracts do not "require []or contemplate that the [electric distribution companies] will purchase capacity or energy from CPV"). PJM has not chosen the rate under the CPV contracts, but instead relies on rates "set" through the wholesale real-time and day-ahead energy and annual capacity auctions.

In short, through its order, the Maryland Commission has unlawfully and unilaterally attempted to change those rates by prescribing what CPV will be paid for sales of energy and capacity in PJM's organized markets. If the Maryland Commission had an objection to those rates, its recourse was to file a complaint under Section 206 of the Federal Power Act, not to engage in self-help. *See Massachusetts Dep't of Pub. Utils. v. United States*, 729 F.2d 886, 886 (1st Cir. 1984) (agreeing with FERC that if a state "objects to [a rate] rule . . . , it should file a complaint in accordance with . . . § 206 of the Federal Power Act"). The district court correctly determined that the Maryland Commission's order is preempted because it intrudes on a field of exclusive federal regulation.

2. The Maryland Commission's Order Impermissibly Conflicts With Federal Law.

The Maryland Commission's order is also preempted because it interferes with the carefully constructed federal regulatory regime governing PJM's markets. *Gibbons v. Ogden*, 22 U.S. (9 Wheat) 1, 211 (1824) (the Supremacy Clause invalidates state laws that "interfere with, or are contrary to," federal law). In setting wholesale rates, FERC is required to ensure that rates are just and reasonable, *see* 16 U.S.C. § 824d, and to balance "difficult (and often competing) objectives," *Buckman Co. v. Plaintiffs' Legal Comm.*, 531 U.S. 341, 349 (2000), for preserving the reliability and efficiency of the wholesale capacity markets. If it is not struck down, the Maryland Commission's order will upset the delicate balance of competing federal interests struck by FERC. Three points bear emphasis:

First, the Maryland Commission's order directly conflicts with the rules for the organized energy and capacity markets set forth in PJM's FERC-approved tariff. In approving PJM's energy and capacity market rules, FERC endorsed the principle that all suppliers with accepted offers would receive the same price for their energy capacity (and rejected arguments that payments should instead be based on each supplier's offer price). *See PJM Interconnection, L.L.C.*, 117 FERC ¶ 61,331, at P 141 (2006) ("*PJM I*"); *Pennsylvania-New Jersey-Maryland Interconnection*, 81 FERC ¶ 61,257, at 62,271 (1997). As FERC explained in approving the capacity market rules, "a competitive market with a single, market-clearing price creates incentives for sellers to minimize their costs." *PJM I*, 117 FERC ¶ 61,331, at P 141. Indeed, the single-clearing price is a core element of PJM's capacity market design. As FERC recognized, a single clearing price has "the benefit of encouraging all sellers to place bids that reflect their actual marginal opportunity costs," *id.* at P 141 n.101, resulting in "a competitive market in which the same price is paid to all suppliers based on the marginal cost of the least efficient supplier necessary to serve that market." *Maryland Pub. Serv. Comm'n v. PJM Interconnection, L.L.C.*, 127 FERC ¶ 61,274, at P 15 (2009).

The payment scheme established by the Maryland Commission directly interferes with the balance of regulatory objectives achieved by the FERC-approved market clearing process. CPV is selling capacity and energy into the PJM-administered markets but does *not* receive the "single[] market-clearing price" for that capacity and energy. *Id.* Instead, the price paid to CPV for wholesale energy and capacity cleared in the

PJM markets is based on the price in the contracts dictated by the Maryland Commission. Mem. 100–05 (JA299–304); *New Jersey Bd. of Pub. Utils. v. FERC*, No. 11-4245, 2014 WL 642943, at *8 (Feb. 20, 2014) ("*NJBPU*") ("the Maryland contracts require CPV to sell capacity in the PJM markets, and for the [electric distribution companies] to pay CPV any difference between the price received in the market and a predetermined contract price").

That is precisely the result FERC sought to avoid in requiring a single-clearing price. For example, in approving PJM's capacity market rules, FERC rejected a proposal calling for "side payments to individual new units," *PJM I*, 117 FERC ¶ 61,331, at P 77, and required that "all winning bidders would be paid a uniform price regardless of their actual cost of supplying electricity." *Id.* at P 141 n.101; *see also* Appellees Br. 11 (describing PJM's new entry price adjustment as a special exception to this general rule). The Maryland Commission's decision to provide "side payments" to CPV thus "undermine[s] the congressional scheme of uniform rate regulation" by allowing a state "to grant regulated sellers greater relief than they could obtain from [FERC] itself." *Arkansas La.*, 453 U.S. at 579. It also thwarts FERC's objective to "ensur[e] that generators always have an incentive to submit marginal cost bids." *PJM Interconnection, L.L.C.*, 119 FERC ¶ 61,318, at P 109 (2007); *see also PJM I*, 117 FERC ¶ 61,331, at P 141 n.101 (suppliers are expected to submit capacity offers that "cover[] [their] marginal cost"); *PJM Interconnection, L.L.C.*, 122 FERC ¶ 61,264, at P 56 (2008) (a "competitive seller of capacity is expected to bid its going-forward costs, *i.e.*, the fixed annual operating expenses that would not be incurred if a unit were not a capacity resource for a year").

Second, the Maryland contracts will suppress capacity prices and distort the wholesale market by introducing "thousands of megawatts of subsidized capacity into the PJM market." *NJBPU*, 2014 WL 642943, at *8. Rather than submitting offers that are based on its marginal costs, CPV has radically different incentives because of the payment scheme ordered by the Maryland Commission.

Because the Maryland contracts require CPV's capacity to clear in PJM's capacity auctions, CPV will be indifferent to the clearing price and will instead offer its capacity "into the PJM market at a price below its actual cost to ensure that [it] would clear." *Id.*; *see also id.* at *17–*18. That will both "crowd out other capacity that is priced at a higher, cost-based rate" and "result in a lower overall clearing price." *Id.* at *6. Indeed, it is "undisputed" that Maryland's "plans to introduce thousands of megawatts of new capacity" into PJM's auctions will effect "the prices of wholesale electric capacity in interstate commerce." *Id.* at *15; *see also id.* at *17 n.24 (Maryland does not dispute that its order "would affect clearing prices"); *ISO New England Inc.*, 135 FERC ¶ 61,029, at P 170 (2011) (below-cost offers from facilities receiving "out of market" subsidies have "the effect of suppressing capacity prices"); *California Indep. Sys. Operator Corp.*, 141 FERC ¶ 61,069, at P 44 (2012) (expressing concern with reliance on "out-of-market solutions, which tend to artificially depress market prices").

Third, market-wide price suppression appears to be precisely what the Maryland Commission had in mind when it designed the CPV contracts and their associated compensation scheme. As the Maryland Commission's order makes plain, the state is dissatisfied with PJM's capacity markets because PJM's capacity market construct "has brought no new generation to Maryland, in spite of the fact that clearing prices for capacity in [parts of Maryland] have averaged almost double those of" other regions. Generation Order 22–23 (Apr. 12, 2012) (JA1328–29). The

Maryland Commission further complained about "exorbitant capacity charges" that "have increased energy costs to Maryland ratepayers by hundreds of millions of dollars." *Id.*; *see also* Mem. 53 (JA252); (consumers in Maryland "pay much higher than average prices for wholesale (and thus retail) electricity") (quoting Maryland Commission). Although Maryland representatives raised similar complaints in proceedings before FERC, *see PJM I*, 117 FERC ¶ 61,331, at PP 74, 77, the Maryland Commission was evidently dissatisfied with FERC's response and elected to take matters into its own hands by overriding the "one year [price] signal, three years into the future" provided by PJM's capacity auctions. Generation Order 22 (JA1328).

II. Appellants' Attempts To Defend The Maryland Commission's Actions Are Unpersuasive.

With no good answers to basic principles of preemption law, appellants attempt to seek refuge in Maryland's undoubted authority to regulate generation. They also suggest that FERC's efforts to respond to the distorting effects of the CPV contracts somehow approves the state's interference with FERC's jurisdiction. Both arguments are unpersuasive and wrong.

A. Maryland's Authority To Regulate Generation Does Not Excuse The Maryland Commission's Intrusion On Matters Reserved To FERC's Exclusive Jurisdiction.

In attempting to defend the Maryland Commission's actions, appellants and their supporters repeatedly emphasize Maryland's authority to regulate the development of generating facilities. *See, e.g.*, CPV Br. 24; MDPSC Br. 19–21; CT PURA Br. 16–18. But the Federal Power Act's "savings clause" preserving state authority over generating facilities does not require jettisoning traditional preemption principles. *Cf. Geier v. American Honda Motor Co.*, 529 U.S. 861, 869 (2000) (a "saving clause . . . does not bar the ordinary working of conflict pre-emption principles"); *Northwest Cent. Pipeline*, 489 U.S. at 516 n.12 ("conflict-pre-emption analysis *is* to be applied, even though Congress assigned regulation of the production sphere to the States and Kansas has acted within its assigned sphere") (emphasis in original). Moreover, as noted above, the Maryland Commission went far beyond encouraging CPV to develop new facilities by impermissibly changing the wholesale rate paid for energy and capacity cleared in PJM's markets.

CPV asserts that the scheme of regulation under the Federal Power Act requires FERC to "accommodat[e]" state actions, CPV Br. 22, but that ignores that "[t]he congressionally designed interplay between state and federal regulation" denies Maryland authority to regulate wholesale rates "in the mere guise" of incentivizing generation. *Northwest Cent. Pipeline*, 489 U.S. at 518. If Maryland wanted to incentivize only the construction of new generating facilities, it could have accomplished that objective through regulatory approaches that did not reset prices in, or otherwise interfere with, the multi-state PJM markets. A state is "free to use" a generation facility even if such facility "fail[s] to clear the auction." *NJBPU*, 2014 WL 642943, at *16.

These alternatives would have permitted Maryland to pay for or encourage development of new generating facilities and allowed ratepayers to receive the benefits of such payments. But the Maryland Commission chose not to utilize those options. Instead, it implemented a compensation scheme that has the direct effect of changing the payments made for energy and capacity that clears through PJM's wholesale markets. *Cf. Northwest Cent. Pipeline*, 489 U.S. at 518 ("the means chosen must at least plausibly be related to matters of legitimate state concern"); Mem. 87 (JA286) (appellees sought only to challenge "the means by which the [Maryland Commission] sought to secure a new generation facility").

B. FERC's Efforts To Protect The Capacity Markets From State Interference Do Not Rescue The Maryland Commission's Order.

Appellants and their supporters argue that FERC's efforts to protect PJM's capacity market from the impacts of the Maryland Commission's order excuse the state's intrusion on FERC's jurisdiction and wash away any conflict with federal law. *See* MDPSC Br. 11; *see also* CPV Br. 26–27; MD People's Counsel Br. 16–18. The Maryland Commission goes so far as to suggest that FERC's approval is so comprehensive as to leave appellees with no justiciable injury, "because any claimed revenue loss results from the FERC-approved participation of CPV's resource[s] in PJM's capacity and energy markets." MDPSC Br. 8. These arguments fail for several reasons.

As appellees explain, FERC's efforts to protect PJM's organized markets and, in particular, its approval of a measure to protect the capacity market known as the "minimum price offer rule" are irrelevant to whether the Maryland Commission's efforts to control wholesale power rates are preempted by the Federal Power Act. *See* Appellees' Br. 40–41.

FERC has no authority to redraw the jurisdictional lines established by Congress. *See Kurns v. R.R. Friction Prods. Corp.*, 132 S. Ct. 1261, 1270 (2012) (holding that state requirements are field preempted notwithstanding federal government's contrary argument); *PLIVA, Inc. v. Mensing*, 131 S. Ct. 2567, 2575 (2011) (holding that state requirements conflict with federal law notwithstanding suggestion that state requirements were consistent). As the Supreme Court has recognized, when Congress "occupies an entire field . . . even complementary state regulation is impermissible," and all "state regulation in the area" is foreclosed, "even if it is parallel to federal standards." *Arizona v. United States*, 132 S. Ct. 2492, 2502 (2012).

FERC cannot abdicate or delegate its ratemaking responsibilities under the Federal Power Act. *See Alabama Elec. Coop., Inc. v. FERC*, 684 F.2d 20, 27 (D.C. Cir. 1982); *Entergy Servs., Inc.*, 120 FERC ¶ 61,020, at P 28 (2007) (FERC's "ratemaking obligations under the FPA cannot be delegated to a state"). Nor can FERC consent to state-mandated side payments for sales of capacity procured through the PJM auction process when those payments set wholesale rates that differ from the just and reasonable rates set through the auction process approved by and on file with FERC. *See, e.g.*, *Louisville & Nashville R.R. Co. v. Maxwell*, 237 U.S. 94, 97 (1915) (a deviation from the filed rate is "not permitted upon any pretext"); *see also Arkansas La. Gas*, 453 U.S. at 582. Indeed, by requiring FERC to exercise regulatory authority through the review and approval of generally applicable tariff provisions, and by prohibiting departures from the rates produced through that process, the Federal Power Act guards against "favoritism" and protects against other forms of undue discrimination. *New York, New Haven & Hartford R.R. Co. v. ICC*, 200 U.S. 361, 391 (1906).

In any event, even if FERC's efforts to protect the markets were relevant, appellants mischaracterize FERC's position. When it modified the minimum offer price rule, FERC made clear that its intent was "not to pass judgment on state and local policies," *PJM Interconnection, L.L.C. v. PJM Power Providers Grp.*, 137 FERC ¶ 61,145, at P 3 (2011) ("*PJM III*"), but to fulfill its statutory obligations to ensure just and reasonable rates. FERC recognized that "[a] capacity market will not be able to produce the needed investment to serve load and reliability if a subset of suppliers is allowed to bid non-competitively to suppress market clearing prices." *PJM Interconnection, L.L.C. v. PJM Power Providers Grp.*, 135 FERC

¶ 61,022, at P 16 (2011) ("*PJM II*") (citation omitted). The modifications made to the rule were thus designed to ameliorate impacts on the capacity auction of subsidized bids. But FERC's approval of the minimum offer price rule with modifications does not and cannot constitute approval for states to set wholesale power rates, which are exclusively FERC's responsibility.

Appellants suggest that FERC's approval of modifications to the minimum offer price rule means that it has approved the Maryland Commission's actions. CPV Br. 27, 36; MDPSC Br. 14; MD People's Counsel Br. 16–18. But FERC has done no such thing. To the contrary, FERC approved the minimum offer price rule in part because of the negative effects of the state law on the PJM capacity market. *Cf. NJBPU*, 2014 WL 642943 at *20 (FERC forced to act because "states were actually structuring contracts for the development of new resources in a way that would substantially suppress prices, threatening imminent economic harm"). FERC emphasized that, although "states are free to promote" policies seeking to encourage new generation, "there is no valid state interest in ensuring that uneconomic offers can submit below-cost offers into the . . . auction." *PJM II*, 135 FERC ¶ 61,022, at P 142. Given the multi-state nature of PJM's markets, FERC also "took into particular consideration the concern, as expressed by the Pennsylvania Public Utility Commission," that exempting state-sponsored uneconomic entry "could adversely affect other states that wished to rely on prices in the capacity market to incentivize new entry, as opposed to relying on state subsidies." *NJBPU*, 2014 WL 642943, at *19 (citing *PJM II*, 135 FERC ¶ 61,022, at P 142; *PJM III*, 137 FERC ¶ 61,145, at P 96).

That FERC has attempted to protect the PJM capacity market from the distorting effects of unlawful state initiatives does not mean that the Maryland Commission has not impermissibly interfered with the federal regulatory scheme. When the market is functioning properly, a new generator can be expected to offer its capacity into the capacity market at a level representing its long-run marginal cost. *See, e.g.*, *PJM I*, 117 FERC ¶ 61,331, at P 141 n.101. Where, as here, a generator is receiving subsidies outside the market, however, this market test fails and PJM must resort to an estimate of the generator's long-run marginal cost.

Estimating a new generator's long-run marginal cost is an inherently complex, imprecise, and controversial exercise, as illustrated by the disputes that have arisen over the appropriate level of CPV's bids.

CPV initially sought to submit an offer of $13.95 per megawatt-day. PJM's independent market monitor determined that CPV should be required to submit an offer of at least $136.87 per megawatt-day. PJM ultimately came down in the middle, finding that CPV should be required to submit an offer of at least $96.13 per megawatt-day. Mem. 68–71 (JA267–70). Similar disputes have led to extensive litigation regarding the application of a minimum offer price rule in a neighboring market. *See generally Hudson Transmission Partners, LLC v. New York Indep. Sys. Operator, Inc.*, 145 FERC ¶ 61,156 (2013); *Astoria Generating Co. L.P. v. New York Indep. Sys. Operator, Inc.*, 140 FERC ¶ 61,189 (2012); *Astoria Generating Co. L.P. v. New York Indep. Sys. Operator, Inc.*, 139 FERC ¶ 61,244 (2012).

Even minor miscalculations in the cost calculations underlying the minimum price offer rule can have drastic price suppressive effects on PJM's capacity auctions. *See* Mem. 71–73 (JA270–72) (decrease of 750 megawatts of capacity from bottom of supply stack would have increased clearing price from $167.46 per megawatt-day to $195 per megawatt-day). The upshot is that FERC's corrective measures cannot realistically be expected to be 100 percent effective. Markets and suppliers are still harmed by the State's unlawful actions notwithstanding those measures.

Finally, appellants contend that, unless FERC affirmatively acts to invalidate the state capacity payment scheme, there is no basis for finding the Maryland Commission's order to be preempted. But it is understandable that FERC has not on its own initiative rushed to address the legality of state-sponsored initiatives like the CPV contracts. *Cf.* Mem. 107 (JA306) (CPV filed contract with FERC but expressly stated it was "not requesting" that FERC "address or discuss its jurisdiction over the contract"); *Office of Consumers' Counsel, State of Ohio v. FERC*, 842 F.2d 1308, 1311 (D.C. Cir. 1988) (acknowledging that FERC might "wish to avoid deciding an important, unsettled jurisdictional issue in the difficult context of [a] highly complex case"); *ISO New England*, 135 FERC ¶ 61,029, at P 218 (declining to address allegations that Connecticut may have improperly sought to suppress capacity market prices where parties had not sought FERC "enforcement action"). FERC's willingness to tolerate, or even accommodate, a state's interference with its exclusive jurisdiction is irrelevant. *See Missouri Pac. R.R. Co. v. Stroud*, 267 U.S. 404, 408 (1925) (there "can be no divided authority over interstate commerce . . . the acts of Congress on that subject are supreme and exclusive"). Congress, not FERC, defines the scope of FERC's jurisdiction under the Federal Power Act.

III. Affirming The Judgment Below Should Not Impede Proper State Efforts To Encourage Generation Development And Reliability.

For all the reasons set forth above, the district court's judgment should be affirmed. It is important to recognize, however, that in striking down the Maryland Commission's order, this Court need not and should not limit a state's ability in other cases to take appropriate steps to encourage generation development and promote reliability. MDPSC Br. 20–21; CPV Br. 12. *Amici* EPSA and EEI agree with other *amici curiae* that the Court should be cautious not to affirm the lower court's decision on unnecessarily broad grounds.

As a general matter, EPSA and EEI agree that the Federal Power Act "does not displace the [s]tates' traditional authority to promote the development of new generation resources through procurements and long-term contracts between new generation resources and State public utilities." CT PURA Br. 31. The states also possess jurisdiction to examine the prudence of load-serving utilities' wholesale purchases in appropriate circumstances. *See, e.g.*, *Kentucky W. Va. Gas Co. v. Pa. Pub. Util. Comm'n*, 837 F.2d 600, 608–09 (3d Cir. 1988); *Pike Cnty. Light & Power Co.-Elec. Div. v. Pa. Pub. Util. Comm'n*, 465 A.2d 735, 738 (Pa. Commw. 1983). As the district court recognized, however, the problem with the Maryland Commission's order is not that the state has exercised its traditional powers with respect to generation facilities and load-serving utilities' wholesale procurement practices, but that the state has sought to change wholesale rates by mandating that CPV receive additional payments for energy and capacity sold in PJM's multi-state markets. *See* Mem. 102–05 (JA301–04).

Properly cabined, a decision affirming the district court's decision will not have "unintended consequences" for lawful state efforts to promote renewable generation resources or long term contracting that does not interfere with FERC's exclusive jurisdiction. AWEA Br. 5. In this regard, EPSA and EEI agree that "the wholesale electricity industry benefits when FERC respects the integrity of contracts." NRG Br. 31. But respect for the integrity of voluntary contracts, embodied in "the venerable *Mobile-Sierra* doctrine," *Morgan Stanley Cap. Grp. Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 548 (2008), does not mean that traditional bases for invalidating contracts should be cast aside where (as in this case) the contract interferes with FERC's exclusive ratemaking jurisdiction. *Cf.* Mem. 108–11 (JA307–10). Moreover, *Mobile-Sierra* deference does not extend to "involuntary" contracts like the state-mandated CPV contracts at issue here. A state simply cannot directly modify the rates received by suppliers for FERC-jurisdictional sales, or require specific behavior that directly affects clearing prices, in contravention of FERC's market design.

CONCLUSION

The Court should affirm the district court's judgment below.

Respectfully submitted,

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/s/ Ashley C. Parrish
Ashley C. Parrish

UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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