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# Commerce Clause Issues Raised in State RPS

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# Background

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- Lawsuit filed by TransCanada Power Marketing in US District Court in Massachusetts alleged that a requirement for long-term contracting limited to in-state generators was in violation of the Commerce Clause of the US Constitution
  - ▶ A second violation was alleged based on the requirement that eligibility for the solar carve-out was limited to in-state generators
- Commerce Clause issues pertaining to RPS have also been raised recently in California and New Jersey

# Purpose

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- Examine existing state RPS laws and rules
- Explain and evaluate Commerce Clause challenges
- Offer guidance and options to states to avoid Commerce Clause restrictions

# What is the Commerce Clause?

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- Empowers Congress to “regulate commerce among the several states”
  - ▶ As interpreted by federal courts, states are also restricted from unjustifiably discriminating against or burdening the interstate flow of commerce (the dormant Commerce Clause)
- Prohibits economic protectionism
  - ▶ i.e., regulatory measures designed to benefit in-state economic interests by burdening out of state competitors

# RPS Policies Favoring In-State-1

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- Eligibility rules emphasize locally abundant resources
  - ▶ NC swine waste set-aside; MD Tier I poultry litter
- In-state multipliers
  - ▶ CO and MO offer 1.25x credit for in-state resources
- Priority for in-state resources
  - ▶ IL: in-state, then adjoining states, then other states if insufficient cost-effective resources
  - ▶ MD: owners of in-state solar systems must first offer solar RECs to in-state utilities
- Limits on out-of-state RECs
  - ▶ MI: eligible generators must be in-state or in the out-of-state service territory of a utility serving customers in Michigan
  - ▶ OH: min 50% of compliance must be in-state
  - ▶ NC and CA: min 25% must be from in-state resources

# RPS Policies Favoring In-State-2

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- Energy delivery requirements
  - ▶ MA, CT, RI, NH, ME: out-of-region generators must meet real-time energy delivery requirements into ISO-NE; must be in adjacent control area (except Maine)
  - ▶ PA: in-region requirement, where region is defined by PJM and MISO; MISO generator eligibility is limited to corner of PA
  - ▶ AZ: out-of-state generators must deliver energy to utilities
- Dedicated transmission requirements
  - ▶ TX: energy must be physically metered and verified in Texas; may not be commingled with non-renewable sources before being metered
  - ▶ NV: eligible facilities must be connected to a provider of electric service, and line may be shared with not more than one facility using nonrenewable energy

# RPS Policies Favoring In-State-3

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- Long-term contracting limited to in-state resources
  - ▶ MA and RI: requires long-term contracts with newly developed in-state projects
  - ▶ ME: requires long-term contracts with lowest price resources; in-state is included in priorities for consideration
- In-state DG or solar carve-outs
  - ▶ AZ: DG that is “located at a customer’s premises” and that displace conventional energy resources “that would otherwise be used to provide electricity to Arizona customers.”
  - ▶ MD: solar must be “connected with the electric distribution grid serving Maryland”
  - ▶ NJ: eligible SRECs must be “generated by a facility connected to the distribution system in this State.”

# Commerce Clause: Screening Test

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- Is the state law discriminatory on its face?
  - ▶ If YES, law is *per se* invalid unless there are no alternative means for the state to accomplish its goals. (“*per se*” test)
  - ▶ If NO, statute may still burden commerce. Courts apply “Pike balancing test” and weigh burdens to commerce against nature of state's interest

# Discriminatory or Neutral?

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- Example of “facially discriminatory” requirement:
  - ▶ Location-based RPS eligibility
- Example of facially neutral requirement:
  - ▶ Delivery-based RPS eligibility

# Motivation Matters

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- What are “permissible” state interests in Commerce Clause analysis?
  - ▶ Environmental health
  - ▶ Diversity of energy supply and conservation
  - ▶ Reliability and safety
- What are NOT permissible state interests?
  - ▶ Financing in-state projects
  - ▶ Economic development
  - ▶ Any other protectionist interests

# Commerce Clause Exception

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- Market Participant Rule
  - ▶ When a state participates in a market, it can favor its own facilities or resources
  - ▶ To be considered a market participant, state must own or directly fund the activity
- Do REC programs fit the market participant exception?
  - ▶ Probably not because they are regulatory in nature

# Surviving the Commerce Clause

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- What programs are likely to survive Commerce Clause scrutiny?
  - ▶ RPS eligibility based on delivery-requirements (facially neutral, necessary for states to capture environmental benefits of RPS)
  - ▶ Distributed generation carve-outs
    - Delivery or distribution interconnection requirements ensure states get DG and reliability benefits
    - Without RPS carve-out, utilities unlikely to include DG in portfolios - RPS may be only means to encourage DG

# General Guidance to States

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- Adopt facially neutral statutes (many discriminatory laws can be re-cast as neutral)
- Articulate legitimate state benefits in enabling language
- Consider programs that fall within exemptions
- Allow transitions for new RPS requirements to avoid undue burdens or ancillary issues that can trigger lawsuits (e.g., allow for grandfathering, apply requirements prospectively)
- Evaluate carefully market participant doctrine (more flexibility where states play active role in ownership of renewable plants or RECs)
- Take comfort that only one legal court challenge has been brought to date

# Massachusetts Case Study

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- 2008 Green Communities Act requires long-term contracts to “facilitate the financing of renewable energy generation within the jurisdictional boundaries of the [C]ommonwealth, including state waters, or in adjacent federal waters.”
  - ▶ Dec 2009: DPU adopted rules
  - ▶ Jan 2010: Utilities issued RFP
  - ▶ April: TransCanada filed complaint: limiting eligibility for long-term contracts to in-state projects is a violation of the Commerce Clause
  - ▶ June: TransCanada requested injunction to prevent signing or approving contracts
  - ▶ June: DPU suspended the requirement for in-state resources and issued emergency rules
  - ▶ July: DPU approved revised RFP
- In-state requirement was eliminated
  - ▶ September: Utilities issued revised RFP
  - ▶ Both parties requested stay until next May (stay granted Sep 30)

# Conclusions

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- Legal analysis suggests that some RPS statutes might be at risk, but at the same time, states have many options to avoid commerce clause challenges
- Legal challenges have been limited
  - ▶ Parties must have a lot of money at stake and be placed at a significant competitive disadvantage
  - ▶ Small projects are unlikely to support a legal challenge unless a developer can't otherwise participate in the state market

The Commerce Clause prevents states from creating protectionist barriers to interstate trade.... Discrimination under the Commerce Clause means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter, as opposed to state laws that regulate evenhandedly with only incidental effects on interstate commerce.... [A] discriminatory law is virtually per se invalid ... and will survive only if it advances a legitimate local purpose that cannot be adequately served by reasonable non-discriminatory alternatives.... The state bears the burden of showing legitimate local purposes and the lack of non-discriminatory alternatives, and discriminatory state laws rarely satisfy this exacting standard.

# Acknowledgments

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