Commerce Clause Issues Raised in State RPS

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Background

- 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

- 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?

- 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

- 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

- **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

- 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.”
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?

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

- Example of facially neutral requirement:
  - Delivery-based RPS eligibility
Motivation Matters

- 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

- **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

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
  o Delivery or distribution interconnection requirements ensure states get DG and reliability benefits
  o Without RPS carve-out, utilities unlikely to include DG in portfolios - RPS may be only means to encourage DG
General Guidance to States

- 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

- 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

- 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.
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