16-2946, 16-2949

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

ALLCO FINANCE, LIMITED,
Plaintiff-Appellant

v.

ROBERT KLEE, in his Official Capacity as Commissioner of the Connecticut Department of Energy and Environmental Protection
Defendant-Appellee

and

KATHERINE S. DYKES, JOHN W. BETKOSKI, III and MICHAEL CARON, in their Official Capacities as Commissioners of the Connecticut Public Utilities Regulatory Authority
Defendants-Appellees

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

BRIEF OF MASSACHUSETTS, NEW YORK, OREGON, VERMONT, AND WASHINGTON AND THE CALIFORNIA AIR RESOURCES BOARD AS AMICI CURIAE IN SUPPORT OF DEFENDANTS-APPELLEES AND AFFIRMANCE

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IDENTITY AND INTERESTS OF AMICI

The undersigned States and state agency (collectively, State Amici) file this brief, pursuant to Federal Rule of Appellate Procedure 29(a), in support of the Connecticut Defendant-Appellees and, specifically, in support of the constitutionality of Connecticut's Renewable Portfolio Standard (RPS)—a program that requires electricity suppliers to provide Connecticut consumers with specified, and increasing, amounts of electricity from renewable sources.

Like many States with RPS programs, including State Amici, Connecticut has created and defined a tradable compliance instrument—a renewable energy certificate or REC—that its electricity suppliers may use to demonstrate they have met the RPS program's renewable energy requirements. Each Connecticut-certified REC represents the attributes of a megawatt-hour of electricity that satisfies Connecticut's RPS requirements—meaning, among other things, that the electricity was generated by a method that qualifies as renewable under Connecticut's program and that the electricity was capable of being delivered to Connecticut consumers. These requirements advance Connecticut's goals of increasing the amount of renewable generation, and displacing fossil-fuel-fired generation, in the electric grid that serves Connecticut's consumers.

Plaintiff Allco Finance (Allco) contends that Connecticut's definition of its RECs violates the dormant Commerce Clause because it excludes some out-of-state renewable generators. But Connecticut's RECs are compliance instruments created by state law for the purpose of advancing the State's particular policy objectives. States do not violate the Commerce Clause by issuing or accepting only those compliance instruments that advance the States' non-protectionist objectives, as Connecticut does here.

This appears to be the first case in which a Court of Appeals will consider the use of state-created, tradable compliance instruments, like RECs, under the dormant Commerce Clause. State Amici have a compelling interest in the proper application of this doctrine to state programs that utilize such instruments. Twenty-nine States currently have RPS programs. Many of those States, including State Amici here, allow the use of state-created RECs for compliance with at least part of their RPS programs' renewable energy requirements. And many other types of regulatory programs utilize tradable, state-created compliance instruments, as discussed in more detail below.

Tradable compliance instruments have proven to be effective and efficient in a number of contexts, and State Amici have substantial interests in ensuring that States continue to have the flexibility and discretion to create, define, and utilize these instruments to respond to the particular needs of the States and their citizens. Although each State's programs are different in important respects, Allco's dormant Commerce Clause argument could potentially, if accepted, curtail some of that flexibility and discretion and stymie the ability of States to carry out their responsibilities in an effective and efficient manner. Accordingly, State Amici respectfully offer this brief in aid of the Court's analysis of Connecticut's RPS program under the dormant Commerce Clause.[1]

SUMMARY OF ARGUMENT

Connecticut-certified RECs can only be issued to facilities capable of delivering power to the electric grid that serves Connecticut's consumers. That requirement reflects Connecticut's intention to increase the amount of renewable energy available to serve the State's consumers and to displace more-polluting, fossil-fuel-fired generation on the grid that serves those consumers. Allco objects to Connecticut's limitation on RECs, arguing, in essence, that, having chosen to create compliance instruments in the form of RECs, Connecticut is constitutionally obligated to accept RECs issued by

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[1] State Amici agree with Defendant-Appellees and with other amici that Connecticut's Request for Proposal process is not preempted by the Federal Power Act but do not address that issue in this brief.

any other State. Thus, according to Allco, Connecticut must accept RECs Allco claims to have from a facility in Georgia and RECs Allco claims it will generate from a facility in New York, even though neither facility qualifies for issuance of Connecticut-certified RECs because, as Allco itself alleges, neither delivers electricity to the grid that serves Connecticut consumers. *See* Complaint at ¶¶ 33, 34.[2] Allco's claim fails.

States issue tradable compliance instruments under a wide array of regulatory programs. Each of these state programs is unique because each was designed to advance the specific objectives, and respond to the particular challenges, of the regulating State. As the district court correctly recognized, the instruments issued under each of these diverse programs are also unique because those instruments embody the particular objectives and policy judgments of the issuing State. *See* A198. State-created compliance instruments are not, therefore, inherently fungible across state programs.

[2] At times, Allco appears to argue not that it *has* RECs from its New York and Georgia facilities but, rather, that Connecticut must *issue* RECs for those facilities. *See* A193 (noting that Allco seeks to alter Connecticut's statute so that the State would issue out-of-region RECs). But that argument is not meaningfully different because Connecticut is no more obligated to issue RECs that do not meet the State's requirements than it is obligated to accept such RECs for compliance.

The uniqueness of the instruments issued under each State's program defeats Allco's discrimination claim because "any notion of discrimination assumes a comparison of substantially similar entities." *See Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 298 (1997). A REC from Allco's Georgia facility is not substantially similar to a Connecticut-certified REC because the former does not advance Connecticut's interest in altering the energy resource mix available to Connecticut consumers. That interest is "well within the realm of what the States may reasonably promote and preserve," and Connecticut need not ignore the "values served by" its RPS program when it determines whether a REC qualifies under that program. *See id.* at 305, 307.

Further, state-created compliance instruments and their markets bear no resemblance to the kinds of products and markets with which the dormant Commerce Clause is ordinarily concerned. Indeed, as the district court correctly concluded, there is no naturally-functioning, national market for Connecticut-certified RECs. A197. This, too, undermines Allco's claim because "interfere[nce] with the natural functioning of the interstate market" is "[t]he common thread among those cases in which the Court has found a dormant Commerce Clause violation." *McBurney v. Young*, 133 S. Ct. 1709, 1720 (2013) (internal quotation omitted)

Finally, the constitutionality of Connecticut's decision to accept only Connecticut-certified RECs is confirmed by the constitutionality of Kentucky's decision to grant a tax exemption only to Kentucky-issued bonds. *See Kentucky v. Davis*, 553 U.S. 328 (2008). As the *Davis* decision demonstrates, States that decide to advance non-protectionist policy objectives through the use of state-created, tradable instruments, as Connecticut has done here, are not constitutionally obligated to treat other States' instruments the same way they treat their own.

Connecticut's qualifications for its state-created RECs are directly connected to important, non-protectionist objectives, and Connecticut did not violate the dormant Commerce Clause by adopting those qualifications.

ARGUMENT

I. STATE PROGRAMS UTILIZING TRADABLE COMPLIANCE INSTRUMENTS ARE WIDESPREAD, BUT EACH PROGRAM, AND EACH STATE-CREATED COMPLIANCE INSTRUMENT, REFLECTS THE PARTICULAR POLICY JUDGMENTS OF THE ISSUING STATE

A. Tradable Compliance Instruments Come in Many Forms and Play Important Roles in Advancing Environmental Objectives Effectively and Efficiently

The use of tradable compliance instruments is a well-established feature of environmental regulatory programs. The United States Environmental Protection Agency (EPA) first utilized tradable compliance instruments—in the form of marketable emissions "permits"—in the mid-1970s. U.S. EPA, *Tools of the Trade* (June 2003), at 2-11.[3] Under that program, regulated sources were required to "offset" any new or increased emissions by acquiring permits from other sources that had reduced their emissions. *Id*. Since then, regulatory programs utilizing tradable compliance instruments have been "increasingly considered and used worldwide for the cost-effective management of national, regional, and global environmental problems, including acid rain, ground-level ozone, and climate change." *Id.* at 1-1. Such programs have proven "to be highly effective from both an environmental and an economic standpoint." *See id*.

Renewable portfolio standards, like the Connecticut program at issue here, often utilize tradable compliance instruments as part of their program design. These programs typically mandate that utilities obtain a specified, and increasing, percentage of the power they are providing to the State's consumers from renewable sources. Barry G. Rabe, *Race to the Top*: *The Expanding Role of U.S. State Renewable Portfolio Standards* (June 2006), at

[3] Available at https://www.epa.gov/sites/production/files/2015-06/documents/tools.pdf, last visited Nov. 20, 2016.

5.[4] Iowa enacted the first RPS in 1983. *Id.* at 3. Several other States followed suit in the 1990s. *Id*. at 3. Adoption of RPS programs accelerated rapidly in the mid-2000s. *Id*. Currently, twenty-nine states and the District of Columbia have enforceable RPS programs or similar laws. U.S. Energy Information Admin., *Annual Energy Outlook* (2016) at LR-11.[5]

State RPS programs vary considerably, reflecting different States' policy determinations concerning issues such as how much electricity should come from renewables; how quickly, if at all, that amount should increase over time; what types of generation should qualify as renewable; and whether only new renewable generation should qualify. *See id*. The objectives of RPS programs also vary and can include developing a more reliable and diverse energy resource mix to serve the State's consumers, mitigating against price shocks from over-dependence on one type of fuel (e.g., coal, oil, or natural gas), reducing nuclear waste management needs, improving local air quality, and reducing climate-change-causing greenhouse gas emissions. *See Race to the Top* at 6-8.

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[4] Available at http://www.c2es.org/docUploads/RPSReportFinal.pdf, last visited Nov. 20, 2016.

[5] Available at http://www.eia.gov/forecasts/aeo/pdf/0383(2016).pdf, last visited Nov. 20, 2016.

Many States allow utilities to comply with their RPS programs by generating their own renewable energy, by purchasing renewable energy, or by purchasing RECs. *Annual Energy Outlook* at LR-12-15. As discussed above, RECs are tradable instruments, issued by the State or the State's agent, that represent the attributes of a megawatt-hour of electricity. The attributes represented in a REC typically include qualities "such as generator location, capacity, fuel-type and source, owner and the date when operations began." *See* Federal Energy Regulatory Commission, *Energy Primer* (November 2015) at 52.[6] Each State determines the attributes required for, and reflected in, its own RECs, based on the State's particular needs and policy objectives. *See Wheelabrator Lisbon, Inc. v. Connecticut Dept. of Public Utility Control*, 531 F.3d 183, 186 (2d Cir. 2008); *see also Annual Energy Outlook* at LR-12-15.

Cap-and-trade programs also involve the issuance of tradable instruments, which are typically called allowances. *Tools of the Trade* at 1-2. Each allowance represents authorization to emit a particular quantity of a pollutant, e.g., one ton of carbon dioxide. *Id*. Each regulated source must, at the end of each compliance period, surrender allowances equal to the

[6] Available at https://www.ferc.gov/market-oversight/guide/energy-primer.pdf, last visited Nov. 20, 2016.

quantity of the pollutant emitted. *Id.* This requirement ensures that the cap on emissions is not exceeded because the total number of allowances issued typically equals the level of the cap. *Id.*

Cap-and-trade programs designed to reduce greenhouse gas emissions include the Regional Greenhouse Gas Initiative in the northeastern United States (in which Connecticut and several State Amici participate), California's cap-and-trade program (which is linked to Quebec's program), and the European Union Emissions Trading System, which covers 31 countries. Cal. Public Utilities Comm'n, *Celebrating the Year of the Carbon* ("*Year of the Carbon*") (May 2016) at 4-22;[7] European Comm'n, *The EU Emissions Trading System* (September 2016) at 2.[8] Washington State also has a regulatory greenhouse gas reduction program that, although not a cap-and-trade program, allows regulated entities to acquire and sell "emission reduction units" that bear some similarity to allowances issued under cap-and-trade programs. Wash. Admin. Code § 173-442-100, *et seq.*

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[7] Available at http://www.cpuc.ca.gov/uploadedFiles/CPUC_Public_Website/Content/About_Us/Organization/Divisions/Policy_and_Planning/PPD_Work/PPD_Work_Products_(2014_forward)/PPD-COMarkets-5May2016.pdf, last visited Nov. 20, 2016.

[8] Available at https://ec.europa.eu/clima/publications/docs/factsheet_ets_en.pdf, last visited Nov. 20, 2016.

Yet another type of program that utilizes tradable compliance instruments is a low-carbon fuel standard. These programs typically require reductions, over time, in the carbon intensity of transportation fuels. These programs also typically issue tradable instruments—called credits—for the sale of lower-carbon fuels. *See* National Low Carbon Fuel Standard Project, *Policy Design Recommendations* (July 2012) at 6.[9] Those credits can offset a regulated party's sale of higher-carbon fuels or can be sold to other regulated parties. *See id.* at 12-13. The ability to trade credits gives a regulated party the flexibility "to invest directly in reducing GHG emissions," "to buy credits from other companies that can reduce emissions at less cost," or to do some of both. *Id.* at 12. California and Oregon have low carbon fuel standards. Cal. Code Regs. tit. 17, § 95480, *et seq*.; Or. Admin. R. 340-253-0000, *et seq*.

The federal government also employs tradable compliance instruments in its Renewable Fuels Standard program. See 42 U.S.C. § 7545(o). Under this program, refiners are required to sell specified amounts of renewable fuel each year. *See id.* The tradable compliance instruments created under this program—called renewable identification numbers—correspond to

[9] Available at http://nationallcfsproject.ucdavis.edu/files/pdf/2012-07-nlcfs-policy-design-recommendations.pdf, last visited Nov. 20, 2016.

volumes of qualifying renewable fuel.[10] Renewable identification numbers can be bought and sold until they are surrendered to EPA to demonstrate that the mandated volumes of renewable fuel have been produced and sold.[11]

Although the programs described above differ in their design and objectives, programs that utilize tradable instruments are generally designed to reduce compliance costs and provide flexibility for regulated parties, while ensuring that the program's goals are achieved. *See Tools of the Trade* at 1-2 to 1-4; *Policy Design Recommendations* at 12-13. For example, the ability to trade compliance instruments can, in essence, allow regulated parties with high compliance costs to pay those with lower compliance costs to achieve the program's goals. *See Tools of the Trade* at 1-3.

Many of these programs also provide financial incentives to develop and adopt new technologies. For example, revenue from the sales of instruments such as low-carbon-fuel-standard credits or RECs can incentivize or reward investments in lower-carbon fuels or renewable generation. *See Policy Design Recommendations* at 5, 12. According to the Federal Energy Regulatory Commission's Division of Energy Market

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[10] *See* https://www.epa.gov/renewable-fuel-standard-program/renewable-identification-numbers-rins-under-renewable-fuel-standard, last visited Nov. 20, 2016.

[11] *Id.*

Oversight, "[s]tate renewable portfolio standards … have been significant drivers in the growth of investment in renewable generation." *Energy Primer* at 51-52.

B. The Tradable Compliance Instruments Used in State Programs Are Created by State Law and Exist Only Because They Embody the State's Policy Objectives

As the discussion above demonstrates, tradable compliance instruments come in a wide variety of forms and are issued under numerous, diverse regulatory programs with an array of policy objectives. One thing they all have in common, however, is that each of these programs defines the qualifications for the instruments that may be used for compliance. *See, e.g.*, Conn. Gen. Stat. § 16-245a(b).

In fact, these compliance instruments are entirely creatures of the state (or federal) laws that create them. Both the Federal Energy Regulatory Commission (FERC) and this Court have recognized this core aspect of RECs. *Wheelabrator Lisbon, Inc.*, 531 F.3d at 190 (quoting FERC Order holding that "RECs are created by the States" and that "States … have the power to determine who owns the [RECs] in the initial instance and how they may be sold or traded"). Other tradable compliance instruments are similarly created and defined by state law. *See, e.g.*, Wash. Admin. Code

§ 173-442-020(1)(n) (defining "emission reduction unit"); Cal. Code Regs., tit. 17, § 95481(a)(24) (defining "credits").

Each State's definition of its instruments reflects that State's environmental and other policy objectives. For example, some States' RPS programs require some or all of the qualifying renewable generation to be "new" generation developed after a certain point in time. *See, e.g.*, Mass. Gen. Laws, ch. 25A, § 11F(c). Similarly, some States recognize landfill gas generation as renewable under their RPS programs, while other States do not. *See Annual Energy Outlook* at LR-12. Such decisions reflect policy judgments made by weighing complex sets of potential risks and benefits. *See* Natural Resources Defense Council, *Is Landfill Gas Green Energy?* (March 2003).[12] As these two examples illustrate, a REC issued under one State's RPS embodies different attributes—different policy judgments—from a REC issued under a different State's program.[13]

State-created instruments also embody other concerns and policy judgments. The aspect of Connecticut's RPS challenged here—the

[12] Available at https://www.nrdc.org/resources/landfill-gas-green-energy, last visited Nov. 26, 2016.

[13] Similarly, cap-and-trade allowances generally embody policy determinations such as at what level to set the cap, how quickly the cap should decline, which sources and industries should be covered, and whether to place constraints on allowance prices. *Year of the Carbon* at 5-23.

deliverability requirement for issuance of a REC—is one example. That requirement exists to advance the two primary and related objectives of Connecticut's RPS: 1) that, by 2020, 23 percent of the electricity serving the State's consumers should be renewable energy, as Connecticut defines that term; and 2) that the increase in renewable energy should displace more-polluting, fossil-fuel-fired generation on the electric grid that serves Connecticut. Conn. Gen. Stat § 16-245a(a)(15); Conn. Dept. of Public Utility Control, Decision in Docket No. 04-01-13 at 5 ("DPUC Decision").[14]

Connecticut's electricity needs are served by the New England Independent System Operator (ISO-NE) which operates the electric grid in New England. *Energy Primer* at 77. ISO-NE is connected to three other electric grids—New York's, Quebec's, and New Brunswick's—from which it can import power. *Id.* Connecticut's deliverability requirement authorizes REC issuance only to renewable generators directly connected to ISO-NE or capable of delivering into ISO-NE from one of the three connected grids. Conn. Gen. Stat. § 16-245a(b). This ensures that Connecticut-issued RECs "are only awarded for renewable energy that is consumed in the [ISO-NE] control area and displaces fossil fuel generation in New England." DPUC

[14] Available at http://www.ct.gov/pura/docketsearch.

Decision at 5. Put another way, Connecticut's regional REC requirement may appear, superficially, to be based on geography, but, in reality, it merely reflects the grid infrastructure and operations that determine the region from which energy is deliverable to ISO-NE. Thus, this requirement is necessary to advance the State's goals for the energy resource mix available on the electric grid that serves Connecticut consumers.

Compliance instruments can also embody additional policy concerns, such as how governments can verify the legitimacy of instruments, how they can enforce program requirements, and how they can guard against market manipulation and fraud. Experiences with early instrument-based programs demonstrated that these are potentially serious concerns.

For example, the European Union's cap-and-trade program initially employed separate allowance registries in each of its member States, opening the door to the exploitation of jurisdictional differences for the commission of tax fraud and allowance theft. Environmental Defense Fund, *The EU Emissions Trading System: Results and Lessons Learned* (2012), at 26-28.[15] EPA's Renewable Fuel Standard has also seen fraudulent activity

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[15] Available at https://www.edf.org/sites/default/files/EU_ETS_Lessons_Learned_Report_EDF.pdf, last visited November 20, 2016.

with respect to its compliance instruments, renewable identification numbers or RINs. In one case, a jury found that a biodiesel company's owner had implemented "a scheme in which he and his company generated and sold over 32 million RINs, but neither produced nor imported any renewable fuel." RFS Renewable Identification Number (RIN) Quality Assurance Program, 78 Fed. Reg. 12,158 12,163 (Feb. 21, 2013).

In choosing to utilize tradable compliance instruments, States must consider these potential risks, as well as geographical, jurisdictional, and other limits on their abilities to prevent or mitigate these risks. Accordingly, States may consider limiting the creation of tradable instruments to markets over which they may assert regulatory control or to regional, or other multi-jurisdictional, systems of which the State is a part. For example, Connecticut and the other States served by ISO-NE have agreed that a voluntary association—the New England Power Pool—will issue, track, and audit RECs for all of their RPS programs through the New England Power Pool Generation Information System.[16]

[16] *See* http://www.nepoolgis.com/about/, last visited Nov. 20, 2016; *see also* http://www.ct.gov/pura/cwp/view.asp?a=3354&q=415186 (describing Connecticut's verification requirements for RPS eligibility, which include on-site inspections).

In sum, the qualifications for a state-created compliance instrument issued under a particular state program—including geographical qualifications—reflect a set of complex judgments concerning that State's specific objectives. The resulting instrument embodies those judgments, meaning that one State's instrument is not the same as another's, even when the two instruments bear the same label.

II. A STATE MAY DECLINE TO ISSUE OR ACCEPT COMPLIANCE INSTRUMENTS THAT DO NOT MEET THE STATE'S REQUIREMENTS AND DOING SO DOES NOT VIOLATE THE DORMANT COMMERCE CLAUSE

A. Compliance Instruments from Different States Are Not All "Substantially Similar" to Each Other, and There Is No Discrimination in Recognizing These Differences

As the discussion above demonstrates, state-created compliance instruments embody the policy objectives and judgments of the issuing State and are not, therefore, fungible across state programs. This fact fatally undermines Allco's claim that Connecticut discriminates by declining to issue or accept RECs that do not meet the State's qualifications because "any notion of discrimination assumes a comparison of substantially similar entities." *See Tracy*, 519 U.S. 278, 298 (1997). Allco's RECs are not "substantially similar" to Connecticut-certified RECs. Therefore, differential treatment of these two types of RECs cannot constitute discrimination.

The United States Supreme Court has rejected discrimination claims when seemingly similar products were not similar enough such that differential treatment of them could constitute discrimination under the Clause.[17] In one of these cases, the Court concluded fresh-frozen salmon and frozen-to-be-canned salmon were not similarly situated products. *Alaska v. Arctic Maid*, 366 U.S. 199, 204 (1961). Accordingly, there was no discrimination in the differential treatment of two categories of ships—those catching salmon and freezing it for sale as fresh and those catching salmon and freezing it for later canning. *Id.* at 204-05.

In another case, the Court concluded that natural gas sold by utilities and "bundled with services and protections" that ensure reliability and availability at stable rates was a different product from unbundled natural gas sold by independent marketers. *Tracy*, 519 U.S. at 297. The Court went on to hold that the enterprises selling these different products "should not be

[17] The Court has also concluded that public entities are not "substantially similar" to private entities. *See United Haulers Ass'n, Inc. v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 342 (2007); *Davis*, 553 U.S. at 343.

considered 'similarly situated' for purposes of a claim of … discrimination under the Commerce Clause." *Id.* at 310.

In reaching this conclusion, the Court recognized that "the benefits of the bundled product for" residential and small business consumers were "well within the realm of what the States may reasonably promote and preserve," *id.* at 305, and stressed that application of the dormant Commerce Clause should seek "to accommodate state health and safety regulation," *id.* at 306. The Court expressly weighed "the values served by" state utility regulations "in the process of deciding the threshold question" of whether the products and the entities selling them were similarly situated. *Id.* at 307. The Court, accordingly, "conclude[d] that Ohio's regulatory response to the needs of the local natural gas market" resulted in a product—natural gas bundled with services—that was distinct enough from unbundled natural gas that differential treatment of the businesses selling these products could not be discrimination under the Commerce Clause. *Id.* at 310.

These cases confirm that RECs issued under different state programs are different "products" serving different functions, if indeed they are "products" at all (*see, infra*, Sec. I.B). The fact that all RECs share a common predicate—the generation of a megawatt-hour of electricity—does not make all RECs substantially similar "products." Fresh-frozen salmon and frozen-to-be-canned salmon also share a common predicate—catching and freezing the salmon. But that common predicate did not render either the ships engaged in those activities, or the resulting salmon products, substantially similar. *See Arctic Maid*, 366 U.S. at 204-05.

More significantly, state-created instruments, such as RECs, are creatures of state law. They exist only because they advance the policy objectives of the State that created them. *See Wheelabrator Lisbon, Inc.*, 531 F.3d at 186 ("RECs are inventions of state property law [representing] the renewable energy attributes … 'unbundled' from the energy itself.") By definition, a REC created under one State's program will embody different attributes from a REC created under a different State's program, and the two RECs are different "products." Some of those attributes reflect the State's policy decisions about the benefits of different forms of renewable generation. For example, electricity generated by burning landfill gas might generate a REC under Arizona law, assuming other relevant conditions were met, but would not generate a REC under Colorado law under any conditions. *See Annual Energy Outlook* at LR-12; *see also Energy & Env't Legal Inst. v. Epel*, 43 F. Supp. 3d 1171, 1180-81 (D. Co. 2014) (finding no violation of the dormant Commerce Clause in States recognizing different types of generation as renewable).

Other attributes embodied in RECs reflect different policy objectives. Relevant here, Connecticut intends to alter the energy resource mix available to serve its consumers by increasing the amount of available renewable energy and displacing fossil generation. Conn. Gen. Stat. § 16-245a(a)(15); DPUC Decision at 5. These objectives reflect Connecticut's interests in the resource portfolios that serve its consumers, in regional and local air quality, and in consumer protection from price volatility and shocks that can result from over-dependence on particular types of generation. *See* Conn. Dept. of Energy & Env. Protection, *2013 Comprehensive Energy Strategy for Connecticut* ("*Energy Strategy*") at 81-82.[18] Connecticut's regional limitation on RECs ensures that the financial incentives created by its RPS program, and provided via its RECs, go to generation facilities that further the State's policy objectives—facilities capable of effectuating Connecticut's goals regarding the energy resource mix available to serve the State's consumers. *See* A199 (recognizing "subsidy" in Connecticut's RPS). RECs that do not advance these objectives, such as those Allco claims to have, are not substantially similar to RECs that do.

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[18] Available at http://www.ct.gov/deep/lib/deep/energy/cep/2013_ces_final.pdf, last visited Nov. 21, 2016.

The distinction between RECs that advance Connecticut's objectives and RECs that do not is analogous to the distinction the Supreme Court drew in *Tracy* between bundled natural gas, with its reliability guarantees and rate stability, and unbundled natural gas, offered without such protections. Connecticut's objectives here—increasing the amount of renewable energy that serves its citizens and displacing more-polluting, fossil-fueled generation—are "well within the realm of what the States may reasonably promote and preserve." *See Tracy*, 519 U.S. at 305; *see also New York v. FERC*, 535 U.S. 1, 24 (2002) (discussing traditional state authority over "integrated resource planning," "utility buy-side … decisions," and "utility generation and resource portfolios"). "[S]tates have broad powers under state law to direct the planning and resource decisions of utilities under their jurisdiction[, including] order[ing] utilities to purchase renewable generation." *Entergy Nuclear Vermont Yankee*, *LLC v. Shumlin*, 733 F.3d 393, 417 (2d Cir. 2013) (internal quotation omitted).

Connecticut seeks to increase the amount of renewable energy in its energy mix for a variety of reasons related to the health and safety of its citizens—reasons from reducing air pollution to minimizing price shocks and volatility that can result from over-dependence on particular types of generation. *See Energy Strategy* at 81-82; *see also* Conn. Gen. Stat. § 16a-

35k. These "values served by" Connecticut's RPS program are embedded in its RECs and cannot be ignored "in the process of deciding the threshold question" here—namely whether a REC that advances Connecticut's legitimate policy objectives is "substantially similar" to one that does not. *See Tracy*, 519 U.S. at 306; *see also Nat'l Assn. of Optometrists & Opticians v. Brown*, 567 F.3d 521, 525-29 (9th Cir. 2009) (holding optometrists not "similarly situated" to opticians, despite some overlap in services offered, based in part on State's recognition of different risks from the two types of businesses).

It is not discriminatory for Connecticut to recognize differences in RECs (or in renewable generation facilities), even when doing so involves a regional limitation. Connecticut does not violate the dormant Commerce Clause by issuing and accepting only those RECs that further its legitimate, non-protectionist objectives, which are the very reasons the State created its RECs in the first place. Allco's Commerce Clause claim fails.

B. There Is No Natural, Interstate Market in State-Created Compliance Instruments, and, Therefore, Distinguishing Among These Instruments Does Not Violate the Dormant Commerce Clause

As discussed above, state-created compliance instruments, including RECs, are not inherently fungible across the different state programs that create them. For this reason, and because both these instruments and their corresponding markets result directly from state action, there is no naturally-functioning, national market at issue here, as the district court correctly concluded. A197 ("There is not an interstate market for RECs that comply with Connecticut requirements."). The lack of a natural interstate market presents an additional insurmountable obstacle for Allco's claim, as the district court recognized, because "[t]he 'common thread' among those cases in which the Court has found a dormant Commerce Clause violation is that 'the State interfered with the natural functioning of the interstate market either through prohibition or through burdensome regulation.'" *McBurney*, 133 S. Ct. at 1720 (quoting *Hughes v. Alexandria Scrap Corp.,* 426 U.S. 794, 806 (1976)); *see also* A197 (observing Connecticut is not "limiting access to commerce with a wide national distribution").

Significantly, a REC is not electricity. Rather, it is a state-created compliance instrument that exists only to encapsulate the attributes of a particular megawatt-hour of electricity, and, specifically, the particular attributes the State has determined will advance its policy objectives. Indeed, unlike traditional commodities such as milk, beer, or gasoline, neither the demand for these instruments, nor the instruments themselves, exists before the State creates the instruments and the regulatory program that requires them. *See* A197 ("Connecticut created the commerce in RECs.")

In addition to defining and issuing the instruments themselves, States also typically determine the level of either supply or demand in the markets for these instruments, further distinguishing them from naturally-occurring markets. For example, in its RPS program, Connecticut requires its electricity suppliers to obtain a specified, and increasing, amount of renewable energy each year, defined as a percentage of the total energy they provide to Connecticut consumers. Thus, Connecticut sets the level of demand for Connecticut-certified RECs, as Allco concedes. *See* AOB at 66 ("Connecticut is creating a demand in Connecticut-specific RECs that otherwise did not exist"). In other state-created-instrument programs, States may set the supply of the instruments, such as in many cap-and-trade programs where the State issues a certain number of allowances (equivalent to the total emissions level of the cap) each year. Whether the State sets the level of supply or the demand (or both), this feature of state-created compliance instrument markets underscores that these are not naturally-occurring, national markets of the kind the dormant Commerce Clause is intended to protect.

Allco's arguments based on hypothetical, "newly-defined product[s]" such as "electrical wire manufactured in the northeast" and "milk produced from cows located in the northeast" bear no resemblance to this case or to *Tracy*, *McBurney*, or any other applicable case. *See* AOB at 66-67. Unlike electrical wire or milk, RECs are entirely creations of state law. In addition, like the bundled gas in *Tracy* but unlike Allco's hypotheticals, the "products" here have significant intangible aspects, specifically the State's legitimate policy objectives—the health, safety, and environmental goals it has adopted on behalf of its citizens.[19] Indeed, unlike Allco's hypothetical "products," these instruments exist only to embody those objectives.

The "dormant Commerce Clause's fundamental objective" is to "preserv[e] … national market[s]." *Tracy*, 519 U.S. at 299.[20] That objective is not implicated, where, as here, there is no naturally functioning national

[19] This point also distinguishes Allco's other hypothetical—in which the State mandates the use of pollution-control equipment manufactured in the State. *See* AOB at 68-69. Pollution-control equipment is privately produced and tangible; it bears no resemblance to state-created compliance instruments that embody policy objectives through intangible attributes.

[20] This Court has also recognized that the Clause is implicated where state laws "alter[] the flow of the goods in question." *Brown & Williamson Tobacco Corp. v. Pataki*, 320 F.3d 200, 208 (2d Cir. 2003). Where, as here, there is no pre-existing flow (or even a pre-existing "good"), there is no Commerce Clause violation. (Connecticut's RPS also imposes costs on the State's utilities and other electricity suppliers, not on other States, and does not control any wholly out-of-state commerce. *See id.*)

market. *See McBurney*, 133 S. Ct. at 1720 (finding no Commerce Clause violation where the relevant market was "created … through a state program" and involved trade in "a product that the [State] created").

C. As *Kentucky v. Davis* Demonstrates, Connecticut's RPS Program Does Not Violate the Dormant Commerce Clause

The fatal flaws in Allco's claim are further confirmed by the Supreme Court's decision in *Davis*. Like this case, *Davis* involved both the State's issuance of financial instruments to further legitimate, non-protectionist policy objectives and the State's permissible distinctions among superficially similar instruments based on their origin.

In *Davis*, the United States Supreme Court addressed whether Kentucky could constitutionally grant a tax exemption to income earned on bonds issued by the State or its subdivisions, when no such exemption was available to income earned on any bonds issued by other States or by private entities. 553 U.S. at 332-33. There was no question that this tax exemption gave the State's offerings an advantage in the bond market, at least with respect to buyers who were subject to Kentucky income taxes. *Id.* at 333. Indeed, this was the "ostensible reason" for the exemption. *Id.* Nonetheless, the Court upheld this Kentucky-only, origin-specific tax exemption as non-discriminatory, concluding that the State's legitimate policy objectives were a far cry from the economic protectionism prohibited by the dormant Commerce Clause. *Id.* at 352-53. The Court's reasoning in *Davis* is applicable here and leads to the same result: Connecticut's regional limitation on RECs is non-discriminatory because it reflects Connecticut's non-protectionist policy objectives.

First, the Court held that Kentucky's state-specific tax exemption was "not susceptible to standard dormant Commerce Clause scrutiny owing to its likely motivation by legitimate objectives distinct from the simple economic protectionism the Clause abhors." *Id.* at 341. The Court explained that "the issuance of debt securities to pay for public projects is a quintessentially public function" with a "venerable history." *Id.* at 341-42. Likewise here, state-created compliance instruments are common and are increasingly being used by States to achieve similar "quintessentially public functions," including encouraging renewable energy development, diversifying energy resource mixes, protecting against price volatility, and reducing harmful pollution. *See, supra*, Sec. I.A. In addition, while the history of States issuing compliance instruments is not as lengthy as that of state-issued bonds, "apprehension" about judicial "interference" with these "traditional government function[s] is just as warranted here," given the widespread and important role these instruments play in traditional areas of state concern, including environmental quality, energy resource mixes, consumer protection, and public health., *See Davis*, 553 U.S. at 342 (internal quotation omitted).

Second, although the Court did not apply "standard dormant Commerce Clause scrutiny," the Court did satisfy itself that there was no "traditionally forbidden discrimination" in Kentucky's origin-specific tax exemption. *Id.* at 349. It did so by describing the "specific markets in which the exemption's effects are felt" and analyzing those effects. *Id.* at 349-51. While the Court described and analyzed three markets in *Davis*—the one involving "all fixed-income securities"; the "more specialized market" trading "solely in federally tax-exempt municipal bonds"; and an even narrower market involving only "bonds within the State of issue," *id.* at 349-50—here, there is only one market, the one for RECs certified by Connecticut as embodying and advancing Connecticut's policy objectives. There is no discrimination in this market because Connecticut does not distinguish among Connecticut-certified RECs. Further, Connecticut's RPS does not prevent any entity—whether in-state or out-of-state—from investing in renewable generation capable of serving Connecticut consumers and, thus, capable of generating Connecticut-certified RECs. Indeed, Allco itself claims to have invested in renewable energy generation in Connecticut.

See AOB at 21, 25, 32.[21] There is, thus, no discrimination in this ancillary investment market either.

Allco hypothesizes a non-existent, national REC market. *See* AOB at 67. The district court correctly concluded that no such market exists. A197. But even if that hypothetical market did exist, there would still be no discrimination. The only preference exercised by Connecticut is for RECs that—like the state-issued bonds in *Davis*—are issued by the State (through its agent) in furtherance of its legitimate public objectives. *See* 553 U.S. at 349. This preference on Connecticut's part certainly affects the REC purchasing decisions of firms supplying electricity to Connecticut. But that is not meaningfully different from the effect of Kentucky's tax exemption, which was designed to encourage Kentucky residents to purchase Kentucky-issued bonds. A State may grant itself—and the instruments it creates—a "preference … when it engages in activities serving public objectives." *Id.* In accepting only RECs that meet its objectives, that is all Connecticut has done here.[22]

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[21] This freedom for out-of-state investors renders this case entirely distinguishable from *Northeast Bancorp, Inc. v. Bd. of Governors of Fed. Reserve Sys.*, 472 U.S. 159, 174 (1985). *See* AOB at 62-63.

[22] Notably, as in *Davis*, Connecticut treats all private "substantially similar" actors the same. As discussed above in Section II.A, out-of-region

(continued…)

Third, States generally choose to employ tradable instruments to spread compliance costs in the most economically efficient manner, encourage projects in the public interest that would not otherwise occur (e.g., the development of renewable energy or low-carbon fuel), or both. *See, supra,* Sec. I.A. And these programs impose compliance obligations on in-state firms, meaning that the costs (if any) will typically be borne by the State's businesses and/or the State's consumers. In the case of electricity programs, including RPS programs, imposition of costs on the State's ratepayers is, in fact, often guaranteed by state law or through rate proceedings conducted by state commissions.[23] These are significantly parallel to the objectives and effects noted with approval by the *Davis* Court, including "sprea[ding] the costs of public projects over time," "plac[ing] the cost of a project on the citizens who benefit from it over the years," and "allow[ing] for public work beyond what current revenues could support." *See Davis*, 553 U.S. at 342

(…continued)
renewable energy generators are not "substantially similar" to in-region renewable generators, at least with respect to REC issuance, because the attributes of their energy do not advance the policy objectives that are the only reasons Connecticut issues RECs.

[23] *See, e.g.*, Mass. Dep't of Public Utilities Order in 13-146, 13-147, 13-148, 13-149, 2014 WL 806039, at *23 (Feb. 26, 2014) (reviewing proposal "to charge basic service customers for any RECs purchased under" power purchase agreements).

(internal quotation and citation omitted). These parallels in the State's objectives and the functions of the instruments underscore that, as in *Davis*, there is no discrimination here.

Finally, *Davis* is grounded in the "fundamental element of dormant Commerce Clause jurisprudence" discussed above—that "any notion of discrimination assumes a comparison of substantially similar entities." *Id.* at 342 (internal quotation omitted). The attributes of compliance instruments created under one State's laws are not the same as those of instruments created under a different State's laws. *See, supra,* Sec. I.B. Kentucky was not obligated to provide a level playing field for bonds issued by other States—bonds that would further the policy objectives of those other States. Likewise, Connecticut is not obligated to provide a level playing field for RECs issued by other States, even though those RECs would further the policy objectives of those other States. Like Kentucky, Connecticut has decided to advance legitimate policy objectives through the use of tradable financial instruments. And, like Kentucky, Connecticut may express its preference for its own non-protectionist policy objectives through a preference for the state-issued instruments that advance those objectives, even when that preference manifests itself as a state-specific distinction. Indeed, there is even more reason to apply the approach in *Davis* here because, unlike bond markets, state-created instrument markets are not "natural" manifestations of interstate commerce but instead are themselves instruments of state policy, as discussed above.

Just as the Court reasonably hesitated before invalidating a common and "century-old … practice" in *Davis*, courts should be as reluctant to curtail or hamstring the use of a policy tool that is proving to be more and more useful as States tackle complex environmental problems. To do so would fly in the face of long-recognized bedrocks of federalism, including the "degree of local autonomy" favored by the Framers and the ability of "courageous state[s]" to "try novel social and economic experiments." *See Davis*, 553 U.S. at 338; *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting). It would also be a strange use of a doctrine intended to "protect[] markets" to limit States' abilities to use markets to address complex problems. *See Tracy*, 519 U.S. at 299 (internal quotation omitted). Notably, Connecticut's RPS is intended to *expand* the renewable energy investment market and does not discriminate against interstate participation in that market, as evident by Allco's own ability to invest in Connecticut renewable energy projects. *See* AOB at 21, 25, 32. The core federalism concerns that animated the Court's decision to tread lightly in *Davis* are fully present here as well.[24]

It is non-discriminatory for Connecticut to issue and accept only those state-created instruments that further its legitimate and non-protectionist interest in the energy resource mix that serves Connecticut consumers. Allco cannot allege facts to support a claim to the contrary, and this claim was properly dismissed.

CONCLUSION

For the foregoing reasons, State Amici respectfully request that this Court affirm the district court's dismissal of Allco's dormant Commerce Clause claim.

[24] For similar reasons, any claim of undue burden would also fail here. *See Davis*, 553 U.S. at 354 (rejecting such a claim where balancing "would be a very subtle exercise" ill-suited to the judiciary).

Dated: November 29, 2016 Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

Pursuant to Federal Rule of Appellate Procedure 29(d) and 32(a)(7), this brief complies with the type-volume limitation because it contains 6,933 words, excluding the parts of the brief exempted by Federal Rule of Appellate Procedure 32(a)(7)(B)(iii).

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November 29, 2016	*/s/ M. Elaine Meckenstock*
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CERTIFICATE OF SERVICE

I hereby certify that on November 29, 2016, I caused to be served, using the Court's CM/ECF system, a copy of the foregoing Amici Curiae Brief to all counsel of record, consistent with Local Rule 25.1(h)(2).

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