NOS. 14-614 and 14-623

In the
Supreme Court of the United States

W. KEVIN HUGHES, ET AL., *Petitioners*,
v.
TALEN ENERGY MARKETING, LLC, ET AL.,
Respondents.

CPV MARYLAND, LLC, *Petitioner*,
v.
TALEN ENERGY MARKETING, LLC, ET AL.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

REPLY BRIEF FOR NO. 14-614 PETITIONERS

JAMES A. FELDMAN
5335 Wisconsin Ave., NW
Washington, DC 20015
(202) 730-1267
wexfeld@gmail.com

SCOTT H. STRAUSS*
Counsel of Record
PETER J. HOPKINS
JEFFREY A. SCHWARZ
Spiegel & McDiarmid LLP
1875 Eye Street, NW, Suite 700
Washington, DC 20006
(202) 879-4000
scott.strauss@spiegelmcd.com
Counsel for Petitioners

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INTRODUCTION

Respondents paint Maryland as a rogue state "schem[ing]" to overturn the Federal Power Act (FPA) and Federal Energy Regulatory Commission (FERC) decisions. The truth is exactly opposite.

Maryland ran a competitive procurement, picked a winner, and directed distribution utilities to enter contracts that FERC could have regulated, for a new generator whose auction bids FERC *did* regulate. Maryland worked within the FPA and FERC rules to achieve a shared federal–state objective: inducing a multi-hundred-million-dollar investment[1] in a generation facility that FERC found "competitive," "economic," and "needed by the market," whose presence "does not artificially suppress market prices."[2]

The lower court held that Maryland's procurement "set" CPV's rate. Pet. App. 19a, 23a.[3] That ruling, which focuses on the distribution utilities' volition and not CPV's, upends the FPA. *See* Md. Br. at 26-33. By invalidating Maryland's procurement, the courts frustrated Maryland's resource decisions, CPV's choice to enter the contracts, and FERC's ability to review them. Respondents acknowledge that, but for the decisions below, the "contracts [would be] subject to FERC review." Resp. Supp. Br. at 2.[4] They leave unexplained

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1 CPV Br. at 21; JA 761-62; *see also* NRG Br. at 10.

2 *PJM Interconnection, L.L.C.,* 135 FERC ¶ 61,022, PP 175, 177, *on reh'g*, 137 FERC ¶ 61,145 (2011), *reh'g denied*, 138 FERC ¶ 61,160, *reh'g denied*, 138 FERC ¶ 61,194 (2012), *review denied sub nom. N.J. Bd. of Pub. Utils. v. FERC*, 744 F.3d 74 (3d Cir. 2014) (*N.J.*).

3 Pet. App. references are to the No. 14-614 petition appendix.

4 Respondents claim petitioners "belated[ly]" (*id.*) acknowledged that the contracts were subject to FERC review, but CPV and

how retail regulation that produces contracts *subject to* FERC's authority can be *preempted by* that authority.

Respondents miscast PJM's market design, complaining that the contracts give CPV a different, longer-term price than is available in the auction. But the FERC-approved design incorporates both a short-term auction and long-term contracts. FERC "understands that … guaranteeing new generators a fixed return on their sales to PJM … could incentivize more new generation." Resp. Br. at 36. The auction produces short-term price signals, which inform parties' decisions about "how much capacity to build or procure in long-term contracts … and how much to obtain through PJM's auction." *PJM Interconnection*, *L.L.C.*, 115 FERC ¶ 61,079, P 169 (2006). In adopting this design, neither PJM nor FERC purported to deprive CPV of its FPA right to set contract rates for its long-term sales; nor could they have done so consistent with the statute.

Respondents argue that the CPV-distribution utility contracts are unlawful because CPV is selling to PJM. Resp. Br. at 51. Yet Respondents concede that Maryland could have accomplished the same result by requiring the distribution utilities to *buy* CPV's capacity. Resp. Br. at 50-51. Had Maryland done so, CPV would have received the same contract price, and the purchasers unquestionably would have offered the capacity into PJM's auction to offset charges imposed on them. *See* Md. Br. at 15. No offset occurs unless bilat-

Maryland argued to the district and circuit courts that the contracts were *either* non-jurisdictional financing arrangements *or* jurisdictional market-based-rate agreements—and in neither case preempted. *See* JA 11, item 103 (CPV motion to dismiss preemption claim); Pet. App. 156a-157a, 159a; Md. C.A. Br. at 16; Md. C.A. Reply Br. at 11.

erally purchased capacity is "bid into and 'clear[s]' the capacity auction." U.S. Br. at 8. The challenged contracts were the functional equivalent of two concededly legal transactions rolled into one.

Respondents complain that CPV would receive no contract payment unless its resource cleared. But the same thing would happen without a contract; CPV would be paid only if its resource cleared PJM's auction. This approach protected Maryland ratepayers from having to pay both CPV *and* PJM, with no offsetting revenue, if the resource failed to clear. Far from precluding this arrangement, the FPA accords parties the freedom of contract needed to tailor agreements to their needs.

Contrary to Respondents' accusations, Maryland did not encourage below-cost bids to "displace more efficient … resources" (Resp. Br. at 57) and "depress the PJM rate" (*id*. at 58). The contracts required compliance with PJM auction rules. JA 390; Pet. App. 33a. And Maryland knew that CPV's resource would be subject to the minimum-bid rule precluding below-cost bids. *PJM* set CPV's bid, based on cost estimates that excluded contract revenues, and the resource cleared.

Clearing meant CPV was "competitive," "economic," and "needed by the market," "regardless of whether it also receives a subsidy." 135 FERC ¶ 61,022, PP 175, 177. CPV's cost-based offer placed it among the "least-cost, competitively-priced combination of resources necessary to meet the region's reliability objectives," 137 FERC ¶ 61,145, P 90, whose "presence in the market … does not artificially suppress market prices." 135 FERC ¶ 61,022, P 175. FERC's findings dispose of all artificial-price-suppression claims.

Respondents next argue that FERC's minimum-bid orders are themselves signs of preempted intrusion.

But the need to regulate and adjust the minimum-bid rule was inherent in the auction's design. The auction invites bids by all entities with existing or planned resources, including some with incentives to bid below cost, and FERC adopted the rule at the outset to counteract those incentives. That FERC modifies the rule when needed to ensure just and reasonable rates (here, by *withdrawing* a previous exemption) is "powerful evidence" (Resp. Br. at 43) of FERC doing its job, not Maryland overreaching. Instead, in revising the rule, FERC "acknowledge[d]" states' rights to "pursue legitimate policy interests," but ensured that their actions would not distort the auction. 135 FERC ¶ 61,022, P 143. CPV complied, and cleared.

Showing their cards, Respondents imply that CPV should not "sell into PJM" at all (Resp. Br. at 52), because CPV would not exist "but for the long-term pricing guarantee" (*id.* at 44). But Maryland's procurement was lawful, and CPV's resource cleared only because it was "competitive" and "needed" regardless of the contracts. Combining Maryland's procurement with the PJM auction rules furthered the FPA's core purpose: development of plentiful and economic supplies.

Respondents—incumbents who benefit from blocking competitive entry—were unhappy that FERC's orders did not exclude CPV, so they undertook this preemption litigation. In doing so, they subverted not only Maryland but, also, the federal statute and the federal agency they purportedly defend.

The judgment should be reversed.[5]

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[5] Respondents contend that "if this Court were to find the order not preempted, it would need to remand to allow the Fourth Circuit to consider the Commerce Clause objection." Resp. Br. at 21 n.2. But Respondents failed to preserve that objection. The district court's judgment (C.A. JA 349-50) dismissed their Commerce

ARGUMENT

I. There is no single rate for sales to PJM.

Respondents claim that the auction clearing price is the "only … legal rate for capacity sales to PJM" (Resp. Br. at 50), leaving Maryland's procurement preempted because the contracts gave CPV "something different from that FERC-approved rate for [the] very same wholesale sales" (*id*. at 1).

That argument misunderstands the legal and regulatory framework. Filed rates for short-term sales do not foreclose different rates for longer ones. PJM's tariff and FERC's orders contemplated the coexistence of short- and long-term sales. FERC provided for capacity under long-term contracts to be offered in PJM's auction, and did not specify the form of those contracts. By entering these contracts, CPV exercised its FPA-protected right to set rates of its choosing for its long-term sales.

A. The one-rate argument misunderstands PJM's tariff and FERC's orders.

Filed rates for short-term sales do not bar different rates for longer ones. *See Fla. Mun. Power Agency v. Fla. Power & Light Co.*, 64 F.3d 614, 616 (11th Cir. 1995). Short- and long-term prices need not be—and almost never are—the same. "[O]ne of the reasons that parties enter into wholesale-power contracts is precise-

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Clause claims with prejudice, while granting a declaration under 28 U.S.C. § 2201 that the Generation Order "violat[ed] the Supremacy Clause" and was FPA preempted. Commerce Clause relief would alter the judgment. Respondents failed to cross-appeal, and can no longer raise such arguments. *El Paso Nat. Gas Co. v. Neztsosie*, 526 U.S. 473, 480 (1999) ("[I]n more than two centuries of repeatedly endorsing the cross-appeal requirement, not a single one of our holdings has ever recognized an exception.").

ly to hedge against the volatility" of short-term markets. *Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cty.*, 554 U.S. 527, 547 (2008) (*Morgan Stanley*).

Far from being the "same … sales," CPV's contracts bound it to obligations very different from those assumed by resources participating in PJM's auction without long-term agreements. CPV committed to continue selling for twenty years, despite regulatory, technological, fuel-supply, and other risks. Resources without contracts—including Respondents' decades-old, coal-fired plants[6]—have no comparable long-term obligations. Reliability risks from potential retirement of these "high risk" coal plants were among the concerns prompting Maryland's procurement. Pet. App. 50a-51a ("PJM … acknowledged that retirement of [the Crane or Wagner plants] … would likely result in potential reliability violations" and "exacerbate" transmission constraints.).

FERC's PJM-market orders expressly contemplated short-term auction prices *and* long-term contract rates. The auction produces price signals for single-year commitments, which inform parties' decisions whether to contract for longer periods and at what price. 115 FERC ¶ 61,079, PP 57, 70 (auction "create[s] an incentive for longer-term bilateral contracts" and enables participants to "manage their risk more effectively … through bilateral contracting or otherwise"); *PJM Interconnection, L.L.C.*, 119 FERC ¶ 61,318, P 91 (auction produces "stable forward price signal that encourages long-term forward contracting, which …

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[6] S*ee* Talen Energy, C.P. Crane Power Plant, http://perma.cc/V5MS-4UXM and Talen Energy, H.A. Wagner Power Plant, http://perma.cc/PG37-Z6FS.

provides greater forward certainty for both capacity price and capacity adequacy"), *reh'g denied*, 121 FERC ¶ 61,173 (2007), *review denied sub nom. Pub. Serv. Elec. & Gas Co. v. FERC*, 324 F. App'x 1 (D.C. Cir. 2009) (unpublished).

Capacity under contract can be offered in the auction and offset auction payment obligations if the resource clears. U.S. Br. at 7-8; *see also* 115 FERC ¶ 61,079, P 91 ("[A]uction revenues received by the [load-serving entity] for its capacity would … offset [its auction] purchase payments."). This includes capacity purchased under long-term contracts. *Id.* P 172.

1. **Contract-form objections have no basis in the FPA or PJM's tariff.**

Respondents concede that PJM's market design allows bilateral contracts even if they are long-term (Resp. Br. at 49) and state-mandated (*id.* at 55). But they claim that the contracts here "are not *really* bilateral contracts for the sale of energy or capacity from CPV to the [distribution utilities]" (*id.* at 51) but, rather, contracts between the distribution utilities and CPV for CPV's sale to PJM. *See also id.* at 47-48; U.S. Br. at 30. That objection is meritless.

The FPA is "premised on contractual agreements voluntarily devised by the regulated companies," *In Re Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968), and leaves sellers with the same freedom of contract as purveyors "of an unregulated commodity," *United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103, 113 (1958) (*Memphis*). Neither the FPA nor FERC specifies any structure for wholesale-power contracts. The FPA empowers FERC to modify contracts it finds unjust, unreasonable, or unduly discriminatory—a power it retained here until the lower courts voided the contracts.

FERC champions expanding, not limiting, contracting parties' options. In Order No. 719,[7] FERC expressed concern that "market participants … may not be aware of the full range of contract options available to them, including the full range of potential contract counterparties" (*id.* P 282), so it required market operators to "post offers to buy or sell under long-term agreements" on their websites (*id.* P 304), and rejected "any action … to standardize long-term contracts" (*id.* P 306). And contracts like those challenged here are common in the industry. *See* NRG Br. at 2, 11, 16, 17; Md. Br. at 40-41.[8]

Respondents' objection that Maryland "forced" the distribution utilities into the contracts (*e.g.*, Resp. Br. at 16) does not affect the contracts' validity. It bears at most on whether FERC must presume the contracts reasonable. *Morgan Stanley*, 554 U.S. at 530.

2. The contract-form objections lack substance and logic.

Respondents acknowledge that "capacity purchased through a bilateral contract may be resold to PJM at the PJM rate." Resp. Br. at 51. When that happens, the seller "receives the bilateral contract rate," and "the buyer reselling to PJM receives the PJM rate for that

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[7] Wholesale Competition in Regions with Organized Electric Markets, Order No. 719, 73 Fed. Reg. 64,100 (Oct. 28, 2008), FERC Stats. & Regs. ¶ 31,281 (2008), *corrected*, 126 FERC ¶ 61,261 (2010), *on reh'g*, Order No. 719-A, 74 Fed. Reg. 37,776 (July 29, 2009), FERC Stats. & Regs. ¶ 31,292 (2009), *on reh'g*, Order No. 719-B, 129 FERC ¶ 61,252 (2009).

[8] Contracts of this basic type—in which A (Maryland ratepayers) contracts for B (CPV) to provide a service to C (PJM) that benefits A—have been recognized for hundreds of years. *See* 9 John E. Murry, Jr., *Corbin on Contracts* § 42.1, at 11 n.7 (rev. ed. 2007) (citing *Taylor v. Foster* (1600), 78 Eng. Rep. 1034, Cro. Eliz. 807).

resale." *Id.* The contracts here accomplished the same result: CPV received the contract rate, and the distribution utilities received the PJM rate (offsetting the auction price they pay to PJM). *See* Md. Br. at 41-43; JA 388.

Both approaches transfer the risk of market-revenue fluctuations from the generator to the distribution utility. This is a win-win because the generator gets stable revenues to help with financing, and the distribution utilities get variable revenues that offset the fluctuating costs they pay PJM. Both approaches hedge market risk, promote price stability, and support investment in new facilities. But this works only if the resource clears.

The contract structure chosen here enabled the parties to protect Maryland ratepayers against the risk the resource would not clear. When a distribution utility buys capacity, it pays the generator up front and takes the risk that the capacity will fail to clear, producing no revenue. Here, CPV agreed to bear that risk—just as it would absent a contract. Respondents identify no reason to allow mandated long-term purchases followed by resales to PJM but forbid contracts that achieve the same result in a more ratepayer-protective fashion.

The United States contends there is some difference between (a) allowing a distribution utility to bid purchased capacity into the PJM auction (as it inevitably would, *see* U.S. Br. at 8) and (b) "requir[ing]" CPV to bid, as it asserts Maryland did. *Id.* at 31. But Maryland could not require CPV to bid. CPV *agreed* to bid when it entered the contracts. And the two cases are identical in incentive and outcome: in each case, the offeror would be incentivized to bid low, but FERC would control its offers and require cost-based bids.

3. **FERC's 2009 NEPA orders did not prohibit contracts like those here.**

Respondents (like the Fourth Circuit but unlike the United States) claim a conflict between Maryland's order and FERC orders addressing proposed changes to the auction's New Entry Price Adjustment (NEPA). But NEPA governs the auction, not long-term contracts.

FERC adopted NEPA to overcome a design limitation that otherwise might prevent the auction from inducing new entry in small (constrained) delivery areas. In such areas, entry of larger resources could create a glut, reducing prices for years to come. *PJM Interconnection, L.L.C.*, 128 FERC ¶ 61,157, P 101 (2009). Knowing this, a new entrant might not enter with only a one-year payment guarantee. *Id.* NEPA lets such resources lock in auction prices for up to three years while demand grows and the glut shrinks. *Id.*

In 2009, PJM, its market monitor, several states (including Maryland), and others asked FERC to expand NEPA eligibility to a broader set of entrants and extend its duration.[9] FERC declined, finding no need to expand NEPA beyond its original purpose (128 FERC ¶ 61,157, PP 101-102), and left the market design unchanged. As FERC explained, the auction provides "forward price signals and not necessarily long-term

[9] Describing the request as "Maryland's proposal" (Resp. Br. at 14) is misleading, and the implication that Maryland sought judicial review on this issue (*id.* at 15) is false. Maryland sought review on other issues. *Md. Pub. Serv. Comm'n v. FERC*, 632 F.3d 1283, 1284 (D.C. Cir. 2011).

revenue assurance."[10] The revenue assurance comes from auction-prompted contracts, not the auction itself.

FERC's minimum-bid orders, issued two years *after* the NEPA rulings, confirmed that NEPA did not foreclose long-term contracts with resources bidding in the auction. Responding to the exact state programs the courts later found preempted,[11] FERC reiterated that "[l]oad serving entities are free to contract with any generator they choose," while the minimum-bid rule "affects only the price that *such a generator* will be permitted to bid into the capacity market." 137 FERC ¶ 61,145, P 206 (emphasis added). Such contracts would be pointless if their terms and prices had to match auction clearing prices. Even more: the language quoted above presupposes the legality of the contracts here, under which CPV would receive a long-term contract price while bidding capacity in compliance with auction rules.

B. The one-rate argument ignores CPV's rate-setting rights.

Even if PJM's market design had not expressly contemplated long-term capacity contracts, CPV has an independent statutory right to set rates for its long-term sales to PJM by entering into contracts. Respondents claim (Resp. Br. at 50, without citation) that the only way an auction participant can avoid the "terms that PJM imposes" is to sell to someone else. But that is not the law.

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10 *PJM Interconnection, L.L.C.*, 126 FERC ¶ 61,275, P 150, *corrected*, 127 FERC ¶ 61,036, *clarified*, 127 FERC ¶ 61,104, *on reh'g*, 128 FERC ¶ 61,157 (2009).

11 U.S. Br. at 12-13 (explaining that Maryland and New Jersey programs "precipitated a change in PJM's minimum-offer-price rule").

"PJM is the buyer" in its auction, and CPV is the seller. Pet. App. 92a. Even when a seller has its own rate on file with FERC, it remains free to change that rate under FPA section 205. CPV, like an unregulated commodity seller, has the right to file and "change its rates as it will, unless it has undertaken by contract not to do so." *Memphis*, 358 U.S. at 113. *See also United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 343 (1956); *Morgan Stanley*, 554 U.S. at 551; *NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n*, 558 U.S. 165, 174 (2010).

In its brief opposing certiorari (at 23-24), the United States argued that PJM auction sellers waived the right to seek prices different than the auction price for their PJM sales, but it no longer advances that argument. As we showed (Md. Br. at 34), PJM's tariff expressly preserves parties' rights under the FPA as they would exist absent the tariff,[12] and neither PJM nor FERC could require CPV to cede its FPA rights in any event. Sellers do not relinquish their FPA-protected rights by participating in or selling to a regional wholesale market. *Atl. City Elec. Co. v. FERC*, 295 F.3d 1, 10 (D.C. Cir. 2002), *mandate enforced*, 329 F.3d 856 (D.C. Cir. 2003); *Bonneville Power Admin. v. FERC*, 422 F.3d 908, 922-23 (9th Cir. 2005); *Midcontinent Indep. Sys. Operator, Inc.*, 148 FERC ¶ 61,057, P 92 (2014), *reh'g denied in relevant part*, 153 FERC ¶ 61,062, PP 67-68 (2015).

Under the FPA, CPV could sell power to PJM, credit revenues to Maryland ratepayers, and receive from them a long-term contract rate of its choosing—especially given the extra-auction obligations it in-

[12] PJM Interconnection, L.L.C., PJM Open Access Transmission Tariff § 9 (effective Dec. 20, 2010), http://perma.cc/8P8M-5W7H.

curred in committing to build a plant and sell power into the auction for twenty years.[13] The lower courts' rulings wrongly defeated CPV's rate-setting right and FERC's ability to review CPV's contracts.

II. As FERC found, Maryland did not distort PJM's auction.

Respondents, the United States, and PJM's "market monitor" argue that Maryland distorted PJM's auction, but their arguments impermissibly attack controlling, judicially affirmed FERC decisions.[14]

Addressing Maryland's procurement (and New Jersey's) and knowing of the contemplated contracts, FERC held that resources like CPV's, which clear an auction with a rule-compliant, cost-based bid, are "competitive," "economic," and "needed by the market" even if they also receive external subsidies.[15] FERC made plain that such resources "[do] *not* artificially suppress market prices." 135 FERC ¶ 61,022, P 175 (emphasis added). No one—including the United States—may now argue otherwise.[16]

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[13] Far from "procur[ing] nothing in exchange for their [contractual] payments" (Resp. Br. at 26), the distribution utilities and their ratepayers enjoy the reliability, environmental, and economic benefits of 660 megawatts of new generation "to meet Maryland's anticipated long-term electricity demands." Pet. App. 54a.

[14] *City of Tacoma v. Taxpayers of Tacoma*, 357 U.S. 320, 336-37 (1958); *B&B Hardware, Inc. v. Hargis Indus., Inc.*, 135 S. Ct. 1293, 1304-05 (2015).

[15] 135 FERC ¶ 61,022, PP 175, 177; *see also* 137 FERC ¶ 61,145, P 133.

[16] Amicus Monitoring Analytics, LLC, advises on PJM market issues, *see* Monitoring Analytics Br. at 1-2, but forgets how FERC responded to the advice it gave on these issues. Monitoring Analytics advised Maryland that "offers from Generation Order selected resources would suppress capacity market prices below

The United States chides that entities participating in FERC-regulated markets "must … do so under FERC's rules." U.S. Br. at 29. *But that is what Maryland and CPV did*. And they were powerless to do otherwise. "[E]very aspect" of the PJM capacity auction "is approved by FERC" (Resp. Br. at 11), administered by PJM (U.S. Br. at 8), and "actively regulate[d]" by FERC, which "deems the prevailing [auction] prices … to be 'just and reasonable'" (Resp. Supp. Br. at 5).[17]

Maryland knew when it issued the Generation Order that any resource it selected would be subject to the minimum-bid rule.[18] The rule requires bids at or above a default level, unless an offeror justifies a lower bid based on its costs. CPV invoked the generator-specific method. PJM then estimated CPV's costs, excluding contract revenues, and set the minimum bid for CPV's resource—which proved to be far below the auction's eventual clearing price. Pet. App. 125a-126a. This meant CPV's resource was less costly than all of

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competitive levels." *Id.* at 10. But that was almost three months *before* FERC ensured such resources would be subject to the minimum-bid rule and *fifteen* months before Maryland acted. Monitoring Analytics does not mention FERC's 2011 minimum-bid orders, which were applied to CPV. While PJM and Monitoring Analytics calculated CPV's costs differently (PJM's determination controlled), CPV would have cleared under either estimate (Pet. App. 125a-126a). Monitoring Analytics cannot pretend these events never happened.

[17] JA 661 ("FERC decides what the rules are. And our [Generation Order] followed those rules, as it had to.").

[18] This alone refutes Respondents' oft-repeated, consistently incorrect assertion that Maryland issued the Generation Order "to lower the market-clearing price below what FERC considers just and reasonable." Resp. Br. at 52. The district court conducted a six-day trial and did not question Maryland's reliability-related reasons for its actions. Pet. App. 138a; C.A. JA 350.

the resources that failed to clear (and some of the other resources that cleared) the auction. CPV did not distort the auction or displace any lower-cost resource as Respondents and the United States claim (Resp. Br. at 44; U.S. Br. at 17, 24, 26).

Respondents and the United States suggest that if Maryland's goal was to bolster reliability by obtaining extra capacity, it should have kept the CPV resource out of the auction. Resp. Br. at 57; U.S. Br. at 31. But their understanding of Maryland's reliability need is inaccurate,[19] and their argument is perverse. FERC *wants* capacity bid into its auction, at cost, so that the auction can find the "least-cost, competitively-priced combination of resources necessary to meet the region's reliability objectives." 137 FERC ¶ 61,145, P 90. That included CPV's resource. Absent CPV's participation, the auction would have procured and charged customers for another, more expensive resource.

Keeping competitive supply out of the auction is contrary to FERC policy and the FPA. "[T]he principal purpose of [the FPA is] to encourage the orderly development of plentiful supplies of electricity … at reasonable prices." *NAACP v. FPC*, 425 U.S. 662, 669-70 (1976). And whoever owns the capacity (whether CPV or the distribution companies) has an incentive to monetize it by bidding it into the auction, as the rules permit. To do what Respondents and the United States suggest, Maryland would have had to seek to prohibit a market participant from doing that which FERC encourages.

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[19] Maryland faced potential retirements and transmission-project cancellations. It did not need *more* capacity immediately; it needed newer, more dependable capacity, with certain characteristics, to guard against these risks and to "meet … anticipated long-term electricity demands." Pet. App. 49a-54a.

The United States adverts (U.S. Br. at 17-18) to possible price suppression from what it regards as a loophole in the minimum-bid rule: that a resource with costs *higher* than the default could nonetheless bid at the default level and displace resources whose costs exceed the default by a smaller margin. But that did not happen here. CPV's costs (as determined by PJM) were below the default. Pet. App. 125a-126a.

FERC also rejected calls to set the default bid higher to address the situation the United States posits. *N.J.*, 744 F.3d at 109. As the Third Circuit explained, affirming: "FERC is permitted to weigh the danger of price suppression against the counter-danger of over-mitigation, and determine where it wishes to strike the balance." *Id.* Arguments on brief that contradict FERC's orders are of no moment. *Christopher v. SmithKline Beecham Corp.,* 132 S. Ct. 2156, 2166 (2012). Just as the Court does not uphold FERC on the basis of arguments the Commission itself did not make, *Morgan Stanley*, 554 U.S. at 544, it should not strike down Maryland's actions based on positions contrary to FERC's orders.

III. FERC's minimum-bid orders are not evidence of preempted intrusion.

The United States contends that even if FERC "actually prevent[ed] the distortive effect," Maryland's order "would still be preempted" because FERC "was compelled to take steps to address" the state's program. U.S. Br. at 26-27. Respondents label FERC's April 2011 order a "countermeasure[]" (Resp. Br. at 36) providing "evidence of a preemption problem" (*id.* at 25).

These arguments have no force here. As designed, the PJM auction invites bids from any existing or planned resource, regardless of ownership, including some with incentives to bid below cost.[20] FERC blocked these incentives from the outset with the minimum-bid rule, but initially exempted some resources to help states meet their reliability responsibilities. *Id.* PP 34, 103-104. FERC later withdrew the exemption out of concern for its auction effects, but stressed that states could still "provide assistance for new generation entry" so long as the resources bid into the auction at cost, excluding the assistance. 135 FERC ¶ 61,022, PP 122, 141.

To assert that FERC's action signaled a preempted intrusion is contrary to FERC's orders and its representations to the Third Circuit on review. The argument upends FERC's desire to help states by *granting* the exemption in the first place and its later assurance that *withdrawing* the exemption would not interfere with state programs, but would only require resources to bid at cost. *See* Final Br. for Resp. FERC at 45, No. 11-4245 (3d Cir. Apr. 2, 2013) (FERC's 2011 minimum-bid order "does not interfere with states or localities that for policy reasons seek to provide assistance for new generation entry" but "does prevent subsidized resources from artificially depressing Auction prices." (internal quotation marks omitted)); *N.J.*, 744 F.3d at 97, 98.

The argument also undercuts claims about the purported narrowness of the lower court decisions. *See* Resp. Br. at 1; U.S. Br. at 15. Respondents and the United States claim states still have an "array of tools" (Resp. Br. at 26) to support new generation, including "direct subsidies" (*id.* at 3), "tax incentives" (*id.* at 40),

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[20] *PJM Interconnection, L.L.C.*, 117 FERC ¶ 61,331, P 34 (2006), *reh'g granted in part*, 119 FERC ¶ 61,318, *reh'g denied*, 121 FERC ¶ 61,173 (2007), *review denied sub nom. Pub. Serv. Elec. & Gas Co. v. FERC*, 324 F. App'x 1 (D.C. Cir. 2009) (unpublished).

or similar "financial support untethered to a generator's wholesale market participation" (*id.*).[21] *See also* U.S. Br. at 32-33.[22]

Like Maryland's initiative, the point and effect of each such program would be to alter a generator's costs and revenues to make construction more attractive, which necessarily would affect its auction bidding incentives. If Maryland had simply given CPV $50 million cash (to pick a random amount) or provided a tax incentive with the same value, that would have reduced by $50 million the amount that CPV needed to earn in the PJM auction, enabling it to submit a lower auction bid if the rules permit.

A state has many ways to give money or its equivalent, and PJM and FERC, as gatekeepers for PJM's auction, will determine whether to revise auction rules to address the effects of different programs. To treat

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[21] Respondents (but not the United States) also suggest that Maryland "could have pursued FERC's fixed resource requirement option" (*id.* at 40), under which large vertically integrated utilities can opt out of the PJM auction, *N.J.*, 744 F.3d at 84. But the Third Circuit found "convincing evidence" that this was "not a viable alternative" for restructured states like Maryland. *Id.* at 102.

[22] The United States' claim that states have un-preempted alternatives is cold comfort. Consider the past. FERC first said that states could support with long-term contracts new resources that were needed for reliability, which could bid into the auction without restriction. When Maryland (and New Jersey) began to procure needed resources, FERC revoked the exemption and required the resources to bid at cost. A year later, Maryland implemented a program that comported with FERC's rules and selected a resource that FERC found "needed" and "competitive." Yet the United States argues here that Maryland's action was unconstitutional because it somehow disrupted the market. In these circumstances, Maryland should be forgiven for doubting that the United States' assurances are "somehow real," *N.J.*, 744 F.3d at 102.

those decisions as preemption-triggering events strips FERC of the ability to control the consequences of its regulatory decisions, and improperly allows litigants and courts to seize federal energy policy.

IV. Maryland did not regulate or target any wholesale matter.

Respondents claim this Court's *EPSA* decision "bolsters" their preemption argument. Resp. Supp. Br. at 1. But *EPSA*'s underscoring of the breadth of FERC's authority argues *against* preemption here, not for it.

Respondents' argument turns on their endlessly repeated and baseless premise that Maryland "[did] precisely what *EPSA* reiterates that FERC alone [may] do—namely, regulate 'transactions occurring on the wholesale market.'" *Id.* (quoting *FERC v. Elec. Power Supply Ass'n*, 84 U.S.L.W. 4084, 4090 (U.S. Jan. 25, 2016) (*EPSA*)). Maryland did not "regulate," "dictate," "guarantee," or "mandate" any wholesale sale, either directly or indirectly. It told state utilities to enter into contracts (with a willing seller) that FERC could regulate, for a new power plant whose auction offers FERC *did* regulate. Maryland did not challenge FERC's authority; it submitted to it.[23]

States may not "oversee" auction offers. *EPSA*, 84 U.S.L.W. at 4092. Maryland did not do so. It neither compelled CPV to enter the contracts nor ordered it to bid. CPV agreed to bid in accordance with FERC regulations. JA 391; Pet. App. 33a. Maryland has no power over PJM's auction, and could not control whether PJM would adjust CPV's bid, whether it would clear, or how (if at all) its participation would affect auction prices.

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[23] Recall that Maryland was among the states that *supported* FERC's jurisdiction in *EPSA*.

PJM administers these things, and FERC regulates them comprehensively.

The United States makes the same mistake in turning to the Court's *Oneok* decision (which found no preemption). *Oneok, Inc. v. Learjet, Inc.,* 135 S. Ct. 1591 (2015). The United States says the contracts' so-called bid-and-clear payment condition "directly target[ed] the PJM market mechanism for determining wholesale capacity rates." U.S. Br. at 21. But, again: Maryland did not require CPV to bid; CPV *agreed* to bid, and PJM and FERC controlled how PJM would treat the bid and whether it cleared.[24]

Maryland did not "target" or "aim" at wholesale matters as this Court has used those terms. In two cases the United States cites, the state regulated a FERC-jurisdictional interstate pipeline. *Compare Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293, 306-08 (1988), and *N. Natural Gas Co. v. State Corp. Comm'n*, 372 U.S. 84, 94 (1963), *with Nw. Cent. Pipeline Corp. v. State Corp. Comm'n*, 489 U.S. 493, 514 (1989) (state regulation of gas producers is not preempted, even though the regulation affected interstate pipelines). A comparable preempted action here would have been to attempt to regulate CPV or PJM—perhaps by ordering PJM to buy from CPV even if its

[24] The United States also errs in calling the contract payments a subsidy; the contracts establish a long-term rate for CPV's agreement to sell power to PJM for twenty years. Over the contracts' life, Maryland expected its ratepayers to receive market revenues under the contracts exceeding the fixed prices they would pay CPV. Pet. App. 57a; JA 620 (explaining that "consultants evaluate[d] the competitive bids to determine whether it was a positive economic proposition for the ratepayers over the life of the contract. If it had not been, if it had been a bad deal, we were not obliged to accept any of them.").

offer had not cleared. Maryland's order instead lawfully regulated state-jurisdictional distribution utilities, directing them to contract with a willing wholesale seller, subject to FERC review, for the purpose of supporting new generation that Maryland needed for local reliability. *See* Md. Br. at 28-31.

Likewise, in *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354 (1988), the state second-guessed FERC-mandated power allocations. But Maryland did no such thing. FERC here has allowed parties to bid contracted resources into the auction, without making any *ex ante* determination about contract prices or terms. CPV agreed to the contracts here (as the FPA authorized it to do), and, but for the decisions below, FERC could have reviewed them. Maryland overrode nothing.

Consistent with state authority, the FPA, and FERC's orders,[25] Maryland ordered its distribution utilities to support new generation needed to resolve a reliability problem—precisely what FERC said states could do when it accepted the PJM auction. 115 FERC ¶ 61,079, P 172. The contracts reflected a FERC-jurisdictional seller's voluntarily offered price, subject to FERC review. The generator's auction participation was subject to FERC's plenary control, and FERC found the generator competitive and needed. Respondents and their amici, like the court of appeals, would subvert not only Maryland, but also the very statute and agency they purport to defend.

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[25] *See* Md. Br. at 6-12, 28-31.

CONCLUSION

The court of appeals' judgment should be reversed.

Respectfully submitted,

Scott H. Strauss*
Peter J. Hopkins
Jeffrey A. Schwarz
**Counsel of Record*
Spiegel & McDiarmid LLP
1875 Eye Street, NW, Suite 700
Washington, DC 20006
(202) 879-4000
scott.strauss@spiegelmcd.com

James A. Feldman
5335 Wisconsin Ave., NW
Washington, DC 20015
(202) 730-1267
wexfeld@gmail.com

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