No. 14-634

IN THE

Supreme Court of the United States

CPV POWER DEVELOPMENT, INC.,

EIF NEWARK, LLC,

Petitioners,

v.

PPL ENERGYPLUS, LLC, *ET AL.*

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

REPLY IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

RICHARD M. ZUCKERMAN
DENTONS US LLP
1221 Avenue of the Americas
New York, NY 10020
(212) 398-5213

Counsel for EIF Newark, LLC

CLIFTON S. ELGARTEN
Counsel of Record
LARRY F. EISENSTAT
RICHARD LEHFELDT
JENNIFER N. WATERS
CROWELL & MORING LLP
1001 Pennsylvania Ave., N.W.
Washington, DC 20004
(202) 624-2500
celgarten@crowell.com

Counsel for CPV Power Development, Inc.

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PETITIONERS' REPLY

If allowed to stand, the Third Circuit's ruling would strip States of powers and responsibilities that Congress carefully reserved to them in the Federal Power Act ("FPA"). That ruling fundamentally misunderstands the FPA's allocation of authority, and the importance of the States' power to direct utilities to enter into long-term contracts to purchase power and support investment in new power plants.

On field preemption, the Third Circuit held that by requiring a utility to enter into a contract reflecting the price obtained through a competitive procurement, a State improperly "sets" or "guarantees" a rate. But States frequently direct procurements for local utilities, requiring them to enter into contracts at the price offered by the successful bidder. Until the Fourth Circuit's decision in the parallel case, and the decision below that followed it, the line between state and federal authority was brightly lit and well-described in FERC's own preemption cases. So long as the State did not dictate the price, allowing it to be set by bidders, there was no field preemption. That distinction is summarily swept away by the Third Circuit's ruling and in Respondents' Opposition.

Respondents' conflict preemption theories are equally indefensible. Respondents identify nothing in the FPA, from FERC or in this Court's cases, suggesting that prices, or rules, applicable to transactions in PJM's auction, are intended to limit *any* transactions outside the auction.

When coupled with the Fourth Circuit decision in the parallel Maryland case, the effect of these

decisions is to severely limit States' ability to support needed power plant construction. That limitation is flatly inconsistent with Congress' decision to leave responsibility for new electricity generation in the States' hands. And it dangerously creates a significant void in the ability to support new generation because FERC itself has no authority to direct new construction.

In their Opposition, Respondents do not dispute the frequency or importance of state-mandated procurements for long-term contracts supporting investment in electricity infrastructure, nor the effect of the decision below to severely restrict those procurements. Respondents are not concerned about the effect of these decisions on the States' ability to provide for new generation because they are, largely, owners of incumbent power plants, content to restrict new entry.

Instead, Respondents' principal argument against review rests on a repeated assertion that these rulings are mere "fact[] finding." Not so. The Third Circuit plainly stated legal conclusions. And those conclusions are inconsistent with settled principles, precedents, and long-standing practices used by States to support development of the Nation's electricity infrastructure.

The decision below is wrong, dramatic in its impact, and requires this Court's review.

I. Respondents' Opposition Reinforces the Circuit Court Errors

A. In State-Directed Competitive Procurements, States Do Not "Set" Rates

No one disputes that "States may *not* ... set the price ... at which electricity or capacity is sold at wholesale." Opp.-17 (emphasis in original). New Jersey did not do so here.

The prices in the SOCA contracts were not "set" by New Jersey. They were offered by CPV and EIF, bidders in an open competition. Pet.-4, 10. States have overseen procurements by regulated utilities for decades, with FERC's blessing and encouragement. And the distinction between States dictating a particular price, on the one hand, and supervising a procurement that produces a competitive price, on the other, is not new. The former is preempted; the latter is not.

State-supervised procurements that result in long-term contracts with a State's utilities are ubiquitous, and, until the decisions below, uncontroversial.[1] See Susan Tierney and Todd Schatzki, National Association of Regulatory Utility

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[1] Respondents propose to distinguish state-directed contracts from contracts "freely negotiated ... with purchasers." Opp.-22 (citing *Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1*, 554 U.S. 527, 531, 537 (2008)). But "freely negotiated" is not a preemption standard. It indicates that the contract should be granted a presumption of validity because it is disciplined by market forces. See *id.* Cases like *Allegheny, infra,* illustrate that competitive procurements equally supply market discipline.

Commissioners, *Competitive Procurement of Retail Electricity Supply* 1 (2008) (surveying the use of such competitive procurement processes). States have used such procurements for various purposes, including to ensure electricity supplies at a stable price over the long-term. *Id.* at 51 (identifying States that had recently ordered utilities to enter into long-term power purchasing contracts).

To support fuel-source diversity and innovation, 29 States direct utilities to procure a percentage of their power from renewable energy sources. Claire E. Kreycik, et al., *Procurement Options for New Renewable Electricity Supply* 1 (2011); see *CGE Fulton, L.L.C.*, 70 FERC ¶61,290, 62,080 (1995) ("states have broad powers under state law to direct the planning and resource decisions of utilities under their jurisdiction ... [and] may order utilities to purchase renewable generation"). States also direct their utilities to enter into contracts to ensure that failing natural gas or nuclear plants need not shut down. Pet-29. And many States direct utilities to competitively procure standard offer service.[2] Tierney, *supra*, at 1; see *Allegheny Energy Supply Company, LLC*, 115 FERC, ¶61,221, PP 5, 18, 19 (2006) (FERC approves standard offer service procured through a competitive process mandated and supervised by state regulator).

States have longstanding authority to "establish ... [c]ompetitive procedures for the acquisition of electric energy ... purchased at wholesale." 18

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[2] See *generally* American Public Power Association, *Power Supply Procurement in Retail Choice States* (2007).

C.F.R. §35.27. And FERC routinely approves contracts resulting from procurements to buy power over a fixed term. E.g., *Doswell Ltd. P'ship*, 50 FERC ¶61,251, 61,756-57 (1990) (approving contract with prices set by competition); *Allegheny*, *supra*, at PP 4-5 (state-supervised procurement where "winning bidders were selected solely on the basis of price").

As FERC has long held, such procurements are preempted only to the extent the State *dictates* the price, rather than allows it to be determined by competition. Pet.-9; *Midwest Power Sys., Inc.*, 78 FERC ¶61,067, 61,248 (1997) ("preempted to ... the extent [the State] set[s] rates for the wholesale sales of electric energy"); *Cal. Pub. Utils. Comm'n*, 132 FERC ¶61,047, P 69 (2010) ("preempted to the extent that the [State] is setting wholesale rates").

States have long conformed their exercise of authority over their utilities' purchasing decisions to the preemption principles described by FERC. Those principles are well-founded. State-directed purchasing decisions—reflecting judgments about quantities of capacity to be obtained, over what period, generated with what fuel—reflect core state prerogatives under the FPA. FERC's concern is with wholesale transactions and, most particularly, price. So long as the State doesn't itself calculate and impose the price it thinks proper—instead leaving that to market forces—it is not invading FERC territory.

Respondents literally ignore this longstanding principle, and suggest no way that it could survive the lower courts' rulings.

Instead, Respondents try to avoid review primarily by characterizing the lower courts' holdings as "fact[] finding," unworthy of this Court's attention. Opp.-1, 17, 24, 25, 30. But that characterization is transparently wrong. There are no facts in dispute with respect to field preemption (or, as shown below, conflict preemption). The question whether a price produced by a state-directed procurement is "set" by the State is a question of law, squarely presented on this record, by the Petition, and in the opinion below. And it is of unquestionable importance because it goes directly to whether States are allowed to fulfill their responsibility to ensure reliable electricity supplies by means of competitive procurements.[3]

B. The PJM Auction Does Not Set Prices Or Rules For Transactions Outside The Auction: There Is No Basis For Conflict Preemption

Implying that New Jersey defied FERC policy, Respondents argue that these contracts ensure that "'generators receive a different price for capacity they clear through PJM than what FERC intended.'" And "to make matters worse," this price extends for 15 years, though FERC rejected pleas to "expand NEPA's three-year fixed revenue guarantee." Opp.-

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[3] In passing, Respondents suggest that the State "set" the price because it retained authority to cancel the procurement. Opp.-26. But one can scarcely imagine *any* procurement being conducted without reserving the power to reject all bids and cancel the procurement. And the existence of such a residual power (not exercised here) would not, in any event, convert competition into impermissible rate-setting.

17-18. On this basis, Respondents suggest that conflict preemption can be found because New Jersey "set" rates different from auction rates and because New Jersey's outside-the-auction contracts are on different terms than transactions within the auction.

But there is no support for the premise of either theory. PJM auction rules, and auction prices, do not apply to transactions outside the auction. That transactions outside the auction take place on different terms than transactions in the auction is commonplace and creates no conflict with federal law.

To the contrary, as demonstrated in the Petition, see Pet.-14-15, the PJM auction was never intended to set the price of any transaction other than the transaction being solicited in the auction itself, an auction sale. Outside-the-auction transactions take place every day. The auction price represents a single-year sale of fungible capacity. Outside-the-auction contracts, including transactions involving capacity sold through the auction, are invariably at different prices, largely because, like the SOCAs here, they are for different products, such as long-term price commitments, or electricity produced by specified fuels or technologies. See *Morgan Stanley*, 554 U.S. at 547.

Nor does the "NEPA" rule or any other auction rule prescribe the terms of transactions taking place outside the auction. When States and developers asked FERC to extend the "NEPA" period in order to attain longer term rate stability *within the auction* itself, FERC declined. But FERC's refusal to change internal auction rules—which would impose costs on

purchasers in the auction—says nothing about whether a State can take actions *outside the auction*, under its own authority, such as requiring its utilities to procure capacity under long-term contracts. See Pet. No. 14-623-30.

Respondents observe that while the SOCA contracts are bilateral contracts, they are not contracts for an actual capacity purchase between a buyer and seller. Rather, they require the utilities to make supplemental payments, net of revenues earned by the generator selling its capacity into the PJM auction, and are measured against the yearly PJM capacity clearing price. Opp.-23.

Those supplemental payments, which operate as a hedge, are in consideration for several things important to the State, not merely a commitment to supply capacity to the market. They reflect a commitment to construct a new power plant of a designated capacity, at a designated locale, using a preferred technology, *and* (as required by FERC rules) to sell the capacity produced by the plant into the PJM auction over many years. Cf. Opp.-22-23. And because the contracts operate over the long term they afford generators, utilities and ratepayers long-term price stability that the auction does not.

In any event, Respondents do not explain why there should be a constitutional difference between a competitively-procured, long-term hedging-type contract, on the one hand, and a long-term competitively-produced power purchase agreement,

on the other.[4] Neither is field preempted because in neither format does the State "set" the price. As to conflict preemption, PJM's auction prices do not determine prices for any transactions taking place outside the auction. Moreover, whether the mechanism used is a hedge-style contract or a power purchase agreement, the economics of the transactions are identical. Pet.-31. In both instances, utilities, and ultimately ratepayers, pay the difference between the contract price and the auction clearing price, and PJM pays the generator only the clearing price. See Pet.-15-16.

The Third Circuit's logical leap—transforming auction rules and prices into edicts applicable outside the auction—opens the door to an array of challenges to state programs based on auction rules. That logical leap obviated the Third Circuit's need to identify any substantive conflict or frustration of federal law, and reflects the kind of "freewheeling judicial inquiry into whether a state statute is in tension with federal objectives" that is anathema to

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[4] Indeed, since the SOCAs are not contracts to purchase capacity (*i.e.*, the only product solicited in the auction), it is difficult to suggest that they contain rates for such purchases. And if they do not govern rates for a wholesale sale subject to FERC jurisdiction, that would be a second reason for rejecting Respondents' field preemption claim. Respondents argue that FERC can potentially "regulate" the SOCAs under FPA §205 because they contain a rate "'in connection with' [ ] wholesale transactions." Opp.-17. Perhaps. But proving that FERC might assert jurisdiction over the SOCAs does not mean preemption (unless, of course, the State "set" the rate). That a contract is subject to FERC jurisdiction means it is reviewable by FERC, not that it is preempted under the Supremacy Clause.

this Court's conflict preemption jurisprudence. *Gade v. Nat'l Solid Wastes Mgmt. Ass'n*, 505 U.S. 88, 111 (1992) (Kennedy, J., concurring in part and concurring in the judgment).

C. New Jersey Has Not Surrendered Its FPA Authority

Respondents argue that States that restructured their vertically-integrated utilities to foster wholesale or retail competition somehow "ceded" their authority to require purchases by their regulated utilities. Opp.-6.

New Jersey ceded no authority, and Respondents identify no law or mechanism to the contrary. By encouraging generators and utilities to participate in competitive markets, States necessarily agreed that they must abide by FERC-established rules for those markets. But compliance with market rules does not impose restrictions on state power *outside* those markets.

Nor did Congress or FERC contemplate any such relinquishment of power. To the contrary, Congress (and FERC) intended States to retain authority over utility buy-side decisions and power generation portfolios. See *New York v. FERC*, 535 U.S. 1, 24 (2002). And FERC itself rejected Respondents' relinquishment theory, assuring States (and the courts) that forward capacity auctions would not divest States of authority to support new generation, particularly through long-term contracts. See *Conn. Dep't of Pub. Util. Control v. FERC*, 569 F.3d 477, 480-81 (D.C. Cir. 2009); *PJM Interconnection, L.L.C.*, 107 FERC ¶61,112, P 20 (2004) (volatility of short-term auction markets offers "an inadequate foundation for cost-effective financing of new

infrastructure," better supported by long-term contracts).

Respondents argue that States could reclaim their historic authority by building their own power plants, or recreating the system of vertically-integrated utilities, leaving unstated how this could be accomplished. More importantly, Respondents leave unexplained why States cannot *both* encourage participation in competitive markets *and* support new construction when needed.

D. There Is No Trapped Cost Here

Respondents relegate *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354 (1988) to a footnote. For good reason. *Mississippi* involved a State's refusal to allow a utility to recover the cost of a power purchase that FERC had approved, thereby trapping that cost. But there is no trapped cost here; the State has guaranteed that the utilities will recover SOCA-related costs from their ratepayers. *Mississippi Power* therefore lends no support to Respondents' assertion that because a State may not bar utilities from recovering revenue needed to cover a FERC-approved rate, a State is likewise barred from authorizing payments beyond those costs in order to secure long-term pricing commitments from power generators. Cf. Opp.-22 n.4. Additional payments do not invalidate the auction rate.

E. FERC's Amicus Brief Deserves No Weight

Respondents tout FERC's Third Circuit *amicus* brief supporting preemption. But, as Respondents acknowledge, FERC did *not* embrace their theory that these contracts involve state rate-setting.

Instead, FERC took the inexplicable position that all state actions affecting auction rates are preempted. That theory was rejected by the Third Circuit as overbroad and inconsistent with this Court's precedents. Pet.-29a. And it was also inconsistent with FERC's specific ruling that state-sponsored generation, such as CPV and EIF's power plants, should be allowed to participate in the auction, notwithstanding any "subsidy." *N.J. Bd. of Pub. Utils. v. FERC*, 744 F.3d 74, 92 (3d Cir. 2014). Further, FERC disclaimed any intention to interfere with state authority to support new generation through these mechanisms. *PJM Interconnection, L.L.C.*, 135 FERC ¶61,022, P 142 (2011) ("[auction rules changes were not intended to] encroach on a state's ability to act within its borders to ensure resource adequacy or to favor particular types of new generation .... we reiterate that states are free to promote all of those policies"). It is *not* FERC's opportunistic *amicus* assertions, but rather FERC's regulatory rulings, that count.

II. The Questions Are Vitally Important

An unprecedented and dangerous shift in the allocation of state-federal authority to support power plant construction flows from the Third and Fourth Circuit decisions, which fundamentally misunderstand the underlying regulatory framework. But any such shift may only be announced by Congress, or by this Court, based upon its analysis of Congress' intentions, and of FERC's programs.

Amici highlight the importance of the questions presented. They include the National Association of Regulatory Utility Commissioners, representing all

state and territorial utility commissions; the National Association of State Utility Consumer Advocates, representing all retail ratepayers; the American Public Power Association and the National Rural Electric Cooperative Association, representing the Nation's publicly owned and member-owned electric utilities; and other States, public utility commissions, and similarly-interested governmental authorities.

As amici explain, the Third and Fourth Circuit decisions deprive States of basic tools required to ensure reliable and diverse electricity supplies. Those decisions require this Court's attention now. Planning for major energy infrastructure projects takes many years, and must be structured against a background of reliable legal principles. If the decisions below are allowed to stand, they will do more than severely limit States' options within the wide region covered by these two Circuits. They will also send the message more broadly that state support for energy development projects may end up illusory, vulnerable to preemption challenges by incumbent generators seeking to limit competition from more efficient generators and price decreases resulting from increases in overall electricity supply. And that, in turn, undermines the ability of investors to rely on state-promised ratepayer revenue commitments needed to support major energy infrastructure projects. This Court should grant certiorari and reverse.

CONCLUSION

The Petition should be granted.

Respectfully submitted.

RICHARD M. ZUCKERMAN
DENTONS US LLP
1221 Avenue of the Americas
New York, NY 10020
(212) 398-5213

Counsel for EIF Newark, LLC

CLIFTON S. ELGARTEN
Counsel of Record
LARRY F. EISENSTAT
RICHARD LEHFELDT
JENNIFER N. WATERS
CROWELL & MORING LLP
1001 Pennsylvania Ave., N.W.
Washington, DC 20004
(202) 624-2500
celgarten@crowell.com
Counsel for CPV Power Development, Inc.

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