UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA

LSP TRANSMISSION HOLDINGS, LLC,

Plaintiff,

v.

NANCY LANGE, Commissioner and Chair, Minnesota Public Utilities Commission; **DAN LIPSCHULTZ**, Commissioner, Minnesota Public Utilities Commission; **MATT SCHUERGER**, Commissioner, Minnesota Public Utilities Commission; **JOHN TUMA**, Commissioner, Minnesota Public Utilities Commission; **KATIE SIEBEN**, Commissioner, Minnesota Public Utilities Commission, and **MIKE ROTHMAN**, Commissioner, Minnesota Department of Commerce, each in his or her official capacity,

Defendants,

and

Northern States Power Company d/b/a Xcel Energy,

and

ITC Midwest, LLC,

Intervenor-Defendants.

Civil No. 0:17-cv-04490-DWF-HB

PLAINTIFF'S MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANTS' MOTIONS TO DISMISS

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I. INTRODUCTION

Plaintiff LSP Transmission challenges the constitutionality of Minnesota's right of first refusal statute, Minn. Stat. § 216B.246, which grants incumbent electric transmission owners, like Intervenor-Defendants Xcel and ITC Midwest and the Amici Utilities, the exclusive right to construct and own new regionally-approved electric transmission lines located in the state of Minnesota. Minnesota's law prohibits LSP Transmission and other out-of-state market participants from building new transmission lines in Minnesota that are approved through a federally mandated regional planning process. The law thus discriminates against interstate commerce in violation of the dormant Commerce Clause of the United States Constitution. LSP Transmission seeks a declaration that the Minnesota right of first refusal statute violates the dormant Commerce Clause and an order enjoining the State Defendants from enforcing the statute.

LSP Transmission submits this combined memorandum of law in opposition to the motions to dismiss filed by Defendants Commissioners of the Minnesota Public Utilities Commission and Commissioner of the Minnesota Department of Commerce (collectively, "State Defendants"), Intervenor Defendant Northern States Power Company d/b/a/ Xcel Energy ("Xcel"), Intervenor Defendant ITC Midwest, LLC ("ITC Midwest") (collectively, "Intervenor Defendants"), as well as the Amicus Brief filed by incumbent utilities, Great River Energy, Minnesota Power, Otter Tail Power Company, and the Southern Minnesota Municipal Power Agency (collectively, "Amici Utilities[1]"). The Intervenor Defendants

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[1] For clarity, LSP Transmission will use the term used by these entities in their brief.

and Amici Utilities are all protected from interstate competition by the Minnesota right of first refusal statute.

Neither the facts nor the law support Defendants' and Amici Utilities' arguments in support of their motions to dismiss for failure to state a claim upon which relief can be granted. The State Defendants argue that the Supreme Court's decision in *General Motors Corp. v. Tracy*, 519 U.S. 278 (1997) ("*Tracy*")—a decision addressing differential tax treatment of competitors in the natural gas industry—insulates Minnesota's law from the strictures of the dormant Commerce Clause. The State Defendants misconstrue and overextend the Supreme Court's narrow decision in *Tracy*. Here, unlike in *Tracy*, Intervenor Defendants, Amici Utilities, and LSP Transmission are all similarly situated, MISO qualified transmission developers competing in the same market, which means that Minnesota's exclusion of LSP Transmission from the Minnesota portion of that transmission market in order to favor Intervenor Defendants and Amici Utilities discriminates against interstate commerce.

Equally important, precedent does not support the arguments by Intervenor Defendants and Amici Utilities that the statute is not facially discriminatory because (1) not all of the incumbents are headquartered or incorporated in Minnesota, and (2) the law excludes other in-state incumbents from building any particular project that does not connect to their facilities. Prior court decisions have strongly rejected a formalistic definition of an "in-state" entity and have repeatedly held that laws protecting a subset of in-state entities can still be discriminatory and violate the dormant Commerce Clause.

Finally, all Defendants and Amici Utilities argue that LSP Transmission's claim fails under the *Pike v. Bruce Church* test because the right of first refusal statute does not place an undue burden on interstate commerce and benefits retail electric customers. This argument is premature because the *Pike* balancing test requires a factually intense inquiry that is inappropriate for the Court to undertake on a motion to dismiss. Moreover, Defendants' and Amici Utilities' arguments regarding the burdens and benefits associated with the right of first refusal statute are unsupported by fact, self-serving, and speculative. Indeed, Defendants' arguments ignore the substantial burden the Minnesota law places on both Minnesota ratepayers and those in the broader multi-state region who are denied the established benefits of competition. LSP Transmission therefore respectfully requests the Court deny the motions to dismiss.

II. BACKGROUND

Electricity is provided to consumers in a three-step process: (1) electricity is generated at various power plants; (2) electricity is transmitted on an integrated system of large power lines ("transmission lines") and (3) electricity is then distributed to consumers through a network of smaller power lines ("distribution lines"). Electricity placed on transmission lines becomes part of an integrated, interstate system. While states have retained control over the retail distribution of electricity, and, to the extent they exercise it, the siting of transmission, the federal government has exclusive jurisdiction over the rates for transmission of electricity in interstate commerce.

The interstate electric energy transmission market has undergone a fundamental transformation over the last century. In the early part of the twentieth century, electric utilities acted as separate, local monopolies that provided all three services to consumers (generation, transmission, and distribution). Referred to as "vertically integrated utilities," these retail-focused providers were subject primarily to state or local regulation. *New York v. FERC*, 535 U.S. 1, 5 (2002). Even then, however, states' broad authority to regulate public utilities was subject to the limits imposed by the dormant Commerce Clause. *Id.* at 5-6 (citing *Pub. Utils. Comm'n v. Attleboro Steam & Elec. Co.*, 273 U.S. 83, 89 (1927) (invalidating a state's regulation of interstate electricity sales)). These constitutional limits remained as the federal government increasingly sought to break up local monopolies and foster competition among electric transmission providers.

A. <u>FERC Acts to Increase Competition, Efficiency, and Transparency in the Transmission Market.</u>

In 1935, Congress enacted the Federal Power Act ("FPA"), which granted the Federal Power Commission, later renamed the Federal Energy Regulatory Commission ("FERC"), exclusive authority to regulate the transmission and sale of electricity at wholesale rates in interstate commerce. *New York*, 535 U.S. at 6. The FPA directed FERC to "divide the country into regional districts for the voluntary interconnection and coordination of facilities for the generation, transmission, and sale of electric energy," and assigned FERC the "duty" to "promote and encourage such interconnection and coordination." 16 U.S.C. § 824a(a); *see S.C. Pub. Serv. Auth. v. FERC*, 762 F.3d 41, 49 (D.C. Cir. 2014). As a result, interconnected-electric systems and long-distance transmission became increasingly prevalent and economical and smaller, lower cost power plants emerged as competitors to vertically integrated utilities. *See S.C. Pub. Serv. Auth.*, 762 F.3d at 50. Even as these reforms were occurring, traditional vertically integrated utilities attempted to retain their market share by refusing to deliver wholesale energy produced by competitors or by imposing higher rates and unfavorable terms on them. *New York*, 535 U.S. at 8-9. In order to combat the monopolistic, protectionist tendencies of these utilities, FERC enacted a series of reforms to promote the development of competitive markets.

In 1996, FERC promulgated Order No. 888, requiring each electric public transmission provider to unbundle its wholesale generation and transmission service, thus prohibiting utilities from favoring their own generation and opening up the electric grid to all sources of electric power. *See* Compl. ¶ 12. In 1999, FERC issued Order No. 2000, which encouraged the owners of electric transmission facilities operating in interstate commerce to cede operation of their transmission systems to independent system operators ("ISOs") or regional transmission organizations ("RTOs") to coordinate transmission planning, operation, and use on a regional and interregional basis. Compl. ¶ 13. ISOs are nongovernmental agencies that operate and plan the expansion of transmission grids within their regional footprints to ensure the reliability of the system and provide access to electricity at reasonable costs. Compl. ¶ 14-15. Although ISOs took over regional grid planning and FERC remained responsible for transmission rate decisions, Congress left the actual permitting, siting, and eminent domain authority for interstate transmission lines, as well as traditional control over the retail market, with the states.

In the Midwest, the Midcontinent Independent System Operator, Inc. ("MISO"), formerly the Midwest Independent System Operator, Inc., was created in 1998, and was approved by FERC as the first ISO in 2001. Compl. ¶ 16. MISO has approximately 50 transmission-owner members, which own over 49,000 miles of transmission line spanning 15 states, including Minnesota and parts of Canada. Compl. ¶ 16. Like any other ISO, MISO's authority comes from its Tariff, which is approved by FERC, and governs the relationship between an ISO and its members. Compl. ¶ 15. The Tariff lays out the terms on which members may participate in planning, building, expanding and/or operating the electric transmission grids within MISO's region. Compl. ¶ 16.

B. FERC Issues Order No. 1000 to Increase Competition for Transmission Projects Selected for Regional Cost Allocation.

In July 2011, as part of its continuous efforts to encourage competition, FERC issued Order No. 1000, which, among other key reforms, required the removal of rights of first refusal from FERC-approved tariffs and agreements for transmission projects selected for regional cost allocation. *See* Nauen Aff. at ¶ 2, Ex. 1 (hereinafter "Order No. 1000"). Prior to Order No. 1000, the MISO Tariff, like the tariffs of many other ISOs, included provisions—referred to as rights of first refusal—which gave incumbent transmission owners the exclusive right to construct new transmission facilities in their existing service areas. *See* Compl. ¶¶ 17, 21. These rights of first refusal discouraged non-incumbents from participating in the planning process for transmission lines and excluded non-incumbents from the opportunity to build new lines.

In Order No. 1000, FERC concluded that reforms were needed to ensure that transmission and related services provided by FERC continued to be offered at "rates, terms and conditions that are just and reasonable and not unduly discriminatory or preferential" as required by the Federal Power Act. Order No. 1000 at ¶ 13. FERC concluded that rights of first refusal discouraged non-incumbent transmission developers from investing in transmission and deprived customers of the benefits and savings associated with competition in transmission development, and therefore eliminated rights of first refusal in ISO tariffs for transmission projects selected for regional cost allocation.[2] Order No. 1000 at ¶¶ 257, 285.

Numerous incumbent transmission owners, including the Intervenor Defendants and Amici Utilities in this case, opposed Order No. 1000 and its efforts to benefit ratepayers through transmission planning reform and competition. *See* Compl. ¶ 28. Defendant Xcel, along with several other incumbent utilities, argued that FERC should not remove federal rights of first refusal because entities like LSP Transmission were not similarly situated to Xcel because they did not have an obligation to serve retail customers. *See* Order No. 1000 at ¶ 250, n. 225. FERC rejected these arguments and required removal of federal rights of first refusal for transmission projects selected for regional cost allocation. In the lawsuits that followed, the United States Court of Appeals for the District of Columbia Circuit on three separate occasions upheld FERC's decision to eliminate federal rights of first refusal in ISO tariffs. *See S.C. Pub. Serv. Auth.*, 762 F.3d at 75; *Okla. Gas & Elec. Co. v. FERC*, 827 F.3d 75, 80 (D.C. Cir. 2016); *Emera Maine v. FERC*, 854 F.3d 662, 671-72 (D.C. Cir. 2017). The United States Court of Appeals for the Seventh Circuit likewise upheld the

[2] Because these types of rights of first refusal arose under FERC-regulated tariffs, rather than under state law, they were, and still are, commonly referred to as "federal" rights of first refusal.

removal of the right of first refusal in the MISO Tariff, and the United States Supreme Court denied the incumbent transmission owners' petition for certiorari. *MISO Trans. Owners v. FERC*, 819 F.3d 329 (7th Cir. 2016), *cert. denied* 137 S. Ct. 1223 (2017).

C. LSP Transmission Successfully Pursued Competitive Opportunities after Order No. 1000.

To comply with Order No. 1000, MISO and the other ISOs removed rights of first refusal from their tariffs and created a competitive bidding process to select developers for regionally cost allocated projects. Compl. ¶ 40. MISO's competitive process currently applies to projects categorized as either Market Efficiency Projects or Multi Value Projects. Compl. ¶ 41. Both types of projects distribute all or a portion of costs system-wide to ratepayers in multiple states, regardless of whether the project itself crosses state lines or is located wholly within a single state. *See* Compl. ¶¶ 42-44.

Following regional implementation of Order No. 1000, LSP Transmission and its affiliates qualified as transmission developers in numerous RTOs and ISOs, including MISO. Compl. ¶ 35. Affiliates of LSP Transmission were selected as the more efficient or cost-effective transmission developer in three competitive solicitations held since FERC's issuance of Order No. 1000 for projects in the PJM Interconnection, LLC ("PJM"), the California Independent System Operator ("CAISO"), and MISO. Compl. ¶ 35. Each of LSP Transmission's successful proposals contained binding cost caps and multiple other cost reduction factors beneficial to ratepayers. Compl. ¶ 35. In the MISO region, LSP Transmission's subsidiary, Republic Transmission, was selected to develop the Duff-Coleman project, a transmission project with regional cost allocation, which will be located in Indiana and Kentucky. Compl. ¶ 37; *see* Nauen Aff. at ¶ 3, Ex. 2. MISO found Republic Transmission's proposal provided the greatest overall value to ratepayers out of eleven comprehensive proposals, including proposals from Defendants Xcel[3] and ITC Midwest. *See* Nauen Aff. at ¶ 3, Ex. 2, at 2-3.

D. Minnesota Passes the Right of First Refusal Law.

In the wake of Order No. 1000, at the behest of incumbent utilities, Minnesota enacted a statute creating a right of first refusal to protect those utilities from competition with qualified out-of-state developers. The Minnesota statute was introduced in early 2012 to "establish[] a right of first refusal for Minnesota utilities and electric transmission owners regarding the construction and ownership of electric transmission lines connecting to their own facilities." Nauen Aff. at ¶ 4, Ex. 3. Testifying in support of the bill, Xcel stated that it gave "Minnesota utilities . . . the first opportunity to invest in federal regionally planned transmission facilities," and that it was intended to "preserve the status quo." *See* State Br., Peick Aff., Ex. A at 4, 13. The enacted statute provides:

> An incumbent electric transmission owner has the right to construct, own, and maintain an electric transmission line that has been approved for construction in a *federally registered planning authority transmission plan* and connects to facilities owned by that incumbent transmission owner.

[3] Although entities like Xcel are active participants in the competitive processes created by Order No. 1000, Xcel sought to prevent competition in the areas in which it is an incumbent. Due in part to Xcel's influence, Minnesota, North Dakota, and South Dakota (all states in which Xcel is an incumbent) have enacted rights of first refusal laws. *See* Xcel Br., Zylstra Decl., Ex. A, at 7.

Minn. Stat. § 216B.246, Subd. 2 (emphasis added). If the line connects facilities owned by two different transmission owners, the right is shared between the incumbents. *Id.* After MISO approves a project, the incumbent need only give notice to the Minnesota Public Utilities Commission ("PUC") to exercise the right given by the law to construct, own, and maintain the electric transmission line. Minn. Stat. § 216B.246, Subd. 3(a).

E. MISO Acknowledges State Rights of First Refusal.

Although MISO complied with Order 1000 by removing the right of first refusal from its Tariff and creating a competitive bidding process, MISO simultaneously added language to its Tariff requiring it to recognize newly created state rights of first refusal, such as Minnesota's. *See* Compl. ¶ 45. FERC initially rejected MISO's inclusion of the new Tariff provision, however, on rehearing FERC concluded that the requirement that MISO recognize state law in deciding whether to apply its competitive process did not turn the Tariff provision into a "federal" right of first refusal, and therefore did not conflict with Order No. 1000. *See* Nauen Aff. at ¶ 5, Ex. 4. In addressing the competitive process in light of the new Tariff provision, then FERC Chairman Norman Bay, filed a concurring opinion questioning the constitutionality of state rights of first refusal, noting that such laws may "run afoul of the dormant commerce clause," but concluding that a determination of this question "lies with a different forum." *See id*. Contrary to Xcel's assertion, *see* Xcel Br. at 16, the constitutionality of Minnesota's right of first refusal law has never been addressed, either by FERC or a court. As Chairman Bay suggested, *this* Court is the appropriate forum for resolving the constitutionality of Minnesota's law.

F. Intervenor Defendants Exercise their Right of First Refusal.

The discriminatory effect of the Minnesota statute was demonstrated in December 2016, when MISO approved the Huntley-Wilmarth transmission line project. Compl. ¶ 69. Although designated by MISO as a Market Efficiency Project and, therefore, otherwise subject to competitive bidding, MISO automatically assigned the project to Xcel and ITC Midwest, because of the Minnesota statute. Compl. ¶ 71. Xcel Energy and ITC Midwest, timely submitted notice to the Minnesota PUC of their intent to construct, own, and maintain the Huntley-Wilmarth transmission line project. *See* Minn. Stat. § 216B.246, Subd. 3(a); Xcel Br., Zylstra Decl., Ex. C. In the absence of the right of first refusal statute, LSP Transmission would have competed for the project. Because of the statute, however, non-incumbent transmission companies were denied the opportunity to compete.

III. STANDARD OF REVIEW

Federal Rule of Civil Procedure 8 requires that a complaint present "a short and plain statement of the claim showing that the pleader is entitled to relief." To meet this standard, "a complaint must contain sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face." *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585, 594 (8th Cir. 2009). In deciding a motion to dismiss under Rule 12(b)(6), "a court assumes all facts in the complaint to be true and construes all reasonable inferences from those facts in the light most favorable to the complainant." *Sierra Club v. Clinton*, 689 F. Supp. 2d 1147, 1154 (D. Minn. 2010). "In sum, this standard calls for enough facts to raise a reasonable expectation that discovery will reveal evidence of the claim." *Id.* at 1154-55. Courts may also look beyond the complaint to "matters of public record, orders, materials embraced by the complaint, and exhibits attached to the complaint in deciding a motion to dismiss under Rule 12(b)(6)." *Guggenberger v. Minnesota*, 198 F. Supp. 3d 973, 990 (D. Minn. 2016) (citing *Porous Media Corp. v. Pall Corp.*, 186 F.3d 1077, 1079 (8th Cir. 1999)). In this case, the ample facts in the Complaint coupled with the publicly available documents cited in the Complaint make this case entirely inappropriate for dismissal under Rule 12(b)(6).

IV. ARGUMENT

The Supreme Court recognizes that "permitting the individual States to enact laws that favor local enterprises at the expense of out-of-state businesses 'would invite a multiplication of preferential trade areas destructive' of the free trade which the [Commerce] Clause protects." *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 329 (1977) (quoting *Dean Milk Co. v. Madison*, 340 U.S. 349, 356 (1951)). The Commerce Clause of the United States Constitution grants Congress the power to regulate Commerce among the several States. U.S. Const., art I, § 8, cl. 3. "The Supreme Court has long held that this grant of power to Congress contains negative implications that restrict the states' power to regulate interstate commerce." *Ben Oehrleins & Sons & Daughter, Inc. v. Henn. Cnty.*, 115 F.3d 1372, 1383 (8th Cir. 1997). The primary purpose of the dormant Commerce Clause is to prevent a state from providing a direct commercial advantage to local businesses to the disadvantage of out-of-state businesses. *Nw. States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 458 (1959).

The Supreme Court established a two-step approach to evaluating whether a law violates the dormant Commerce Clause. First, the court considers whether the challenged law discriminates against interstate commerce in favor of local business or investment. Discrimination for purposes of the dormant Commerce Clause simply means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter. *Or. Waste Sys., Inc. v. Dep't of Envtl. Quality of Ore.*, 511 U.S. 93, 99 (1994). A law may be discriminatory on its face, in its purpose, or in its effect. *S.D. Farm Bureau Inc. v. Hazeltine*, 340 F.3d 583, 593 (8th Cir. 2003).

Both discriminatory and non-discriminatory laws may be struck down under the dormant Commerce Clause. If a law is discriminatory, it is *per se* invalid. *Id.* This is because discriminatory laws are almost always reflective of a state's attempt to isolate itself from the national economy and to protect local actors. *Fort Gratiot Sanitary Landfill Inc. v. Mich. Dep't of Natural Resources*, 504 U.S. 353, 361 (1992). A court will only uphold a discriminatory law if a state demonstrates under rigorous scrutiny and through ***empirical evidence*** that it has no other means to advance a legitimate local interest. *See S.D. Farm Bureau Inc.*, 340 F.3d at 593; *Maine v. Taylor*, 477 U.S. 131, 144-45 (1986). If the law is not discriminatory, it will be struck down if the burden it imposes on interstate commerce is clearly excessive in relation to its putative local benefits. *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970). Both inquiries involve fact-intensive analyses that are generally not appropriate for resolution on a motion to dismiss. *See Maine*, 477 U.S. at 144-45 (state must present empirical evidence that it has no other means to advance a legitimate local interest); *Colon Health Ctrs. of Am. LLC v. Hazel*, 733 F.3d 535, 544-45 (4th Cir. 2013) (noting purpose and effect analysis is fact-intensive); *Cotto Waxo Co. v. Williams*, 46 F.3d

790, 795 (8th Cir. 1995) (reversing grant of summary judgment on *Pike* balancing inquiry due to factual disputes).

Defendants admit that the Minnesota right of first refusal statute, on its face, gives incumbent electric transmission owners the exclusive right to build and operate transmission lines that connect to their facilities in Minnesota. They argue, however, that such preferential treatment is allowed because (1) Minnesota's decision to favor incumbent transmission owners is not subject to the strictures of the dormant Commerce Clause pursuant to *General Motors Corp. v. Tracy*, 519 U.S. 278 (1997); (2) not all of the incumbents are headquartered or incorporated in Minnesota; and (3) other incumbents within Minnesota are excluded from building certain projects. They also argue that the law does not unduly burden interstate commerce. Each of these arguments is unsupported by the facts and legal precedent, is not appropriate for decision on a motion to dismiss, and should be rejected.

A. ***General Motors Corp. v. Tracy* is Inapposite.**

The State Defendants' primary argument is that LSP Transmission's claim is foreclosed by the Supreme Court's decision in *General Motors Corp. v. Tracy*, 519 U.S. 278 (1997), which involved differential tax treatment of natural gas providers. Defendants claim *Tracy* created a "public utilities exception" to the dormant Commerce Clause. They are wrong. Defendants misconstrue and overextend the Supreme Court's decision.

Tracy involved a challenge to an Ohio law that imposed a general sales and use tax on natural gas purchases from all sellers, except entities that met Ohio's statutory definition of a "natural gas company." *Id.* at 281-82. General Motors purchased natural gas from an entity that was subject to the tax and argued that the differential tax treatment violated the dormant Commerce Clause. *Id.* at 285-86. The Court disagreed, upholding the state's differential taxation and declining to delve into the state's decisions regarding captive retail markets. *Id.* at 297-99, 301-04, 310. *Tracy* is inapplicable here.

1. *Tracy* Does Not Create a Public Utilities Exemption.

State Defendants' Brief rests on the flawed assertion that *Tracy* creates a "public utilities" exception to the dormant Commerce Clause. This phrase is never used affirmatively by the Supreme Court. Rather, it is found only in a single dissent of Justice Scalia in another tax-related dormant Commerce Clause case. *See Camps Newfound/Owatonna, Inc. v. Town of Harrison, Me.*, 520 U.S. 564, 607 (1997) (Scalia, J., dissenting). And the other cases cited by the State Defendants are inapposite. *United Haulers Ass'n, Inc. v. Oneida-Herkimer Solid Waste Mgmt. Authority*, 550 U.S. 330 (2007) involved preferential treatment given to a *government-created* public benefit corporation, not a private corporation. *Levin v. Commerce Energy, Inc.*, 560 U.S. 413 (2010) involved a challenge to a state tax law that the Court dismissed based on comity principles. There is, quite simply, no broadly applicable "public utilities" exception to the dormant Commerce Clause.

2. Minnesota's Law Protects *All* In-State Transmission Owners from Competition by Out of State Transmission Providers, Not Just Retail Providers of Electricity.

Even if *Tracy* had created a broad "public utilities" exception to the dormant Commerce Clause in order to ensure that existing legal obligations to supply "utility" products to residential customers are not disrupted—which again, it did not—it is critical to recognize that, unlike the natural gas tax exemption in *Tracy*, the Minnesota right of first refusal statute does not single out for favored treatment retail providers of electricity to a captive residential market. Instead, it protects all transmission owning entities in Minnesota, regardless of whether they are retail providers of electricity or any other products. The statute defines "incumbent electric transmission owner" as:

> Any public utility that owns, operates, and maintains an electric transmission line in this state; any generation and transmission cooperative electric association; any municipal power agency; any power district; any municipal utility; *or any transmission company* as defined under section 216B.02, subdivision 10.

Minn. Stat. § 216B.246, Subd. 1(c) (emphasis added). Thus, unlike in *Tracy*, the statute does not just protect retail providers of electricity. This fact is illustrated by the nature of Intervenor Defendants and Amici Utilities themselves. Minnesota Power, Xcel Energy, and Otter Tail Power Company are vertically integrated public utilities that provide generation, transmission, and retail (distribution) services. Compl. ¶ 64(i), (l), (m). Great River Energy is a generation and transmission cooperative that sells electricity and transmission services at wholesale to distribution cooperatives, which in turn sell electricity to retail customers. Compl. ¶ 64(d). Southern Minnesota Municipal Power Agency is a municipal corporation that generates and transmits wholesale electricity to its member utilities. Compl. ¶ 64(o). And, most notably, ITC Midwest, which indicated its intent to exercise its right of first refusal to build the Huntley-Wilmarth transmission line, is an independent transmission company providing only transmission services and structured much like LSP Transmission's affiliates. Compl. ¶ 64(f).

The right of first refusal statute protects each of these incumbent transmission owners, not because they serve retail customers, *i.e.*, "the captive market," *Tracy*, 519 U.S. at 307, but simply because they own transmission facilities in the state of Minnesota. Thus, even if *Tracy* were as broad as Defendants would like it to be, it still would not foreclose Plaintiff's dormant Commerce Clause claim because, unlike the Ohio sales and use tax exemption that was the subject of *Tracy*, Minnesota's right of first refusal law does not single out retail electricity providers as the sole beneficiaries of the state's protection.

3. Unlike the Ohio Tax Law in *Tracy*, the Minnesota Right of First Refusal Statute Targets the Regional Market for Building Transmission Lines.

The Minnesota right of first refusal law also is distinguishable from the law at issue in *Tracy* because the Minnesota statute is specifically written to target the regional transmission market and to give Minnesota transmission owners a competitive edge in that market, to the exclusion of any other entity. *See* Minn. Stat. § 216B.246 ("An incumbent transmission owner has the right to construct, own, and maintain an electric transmission line that has been approved for construction in a *federally registered planning authority transmission plan* …") (emphasis added). To be clear, the projects that Minnesota has walled off from competition are not "distribution" projects that transmit electricity to retail customers; they are regional projects planned and developed by MISO, and are regionally cost-allocated, meaning that the costs are borne by transmission consumers, not just in Minnesota, but across the entire MISO multi-state/province region. *See* Compl. ¶¶ 41-44.[4]

[4] For example, although the Huntley-Wilmarth line is located entirely within Minnesota, it was planned and developed by MISO, and because it is categorized as a "Market Efficiency

This fact is crucial. The *Tracy* Court was concerned that repealing a generally applicable sales and use tax would hinder the ability of natural gas utilities to serve the captive retail market, a market within traditional state jurisdiction, by draining customers from that market. No such captive retail customers are at issue here. The statute applies exclusively to the market to build transmission projects approved in a "federally registered planning authority transmission plan," Minn. Stat. § 216B.246, Subd. 2, and has no application to the retail distribution market.

Xcel also argues that the Second Circuit's decision in *Allco Finance Limited v. Klee*, 861 F.3d 82 (2d Cir. 2017), reinforces the *Tracy* analysis. *Allco* is no more analogous to the Minnesota right of first refusal statute than *Tracy*. In *Allco*, a solar project developer claimed that Connecticut's Renewable Portfolio Standard ("RPS") violated the dormant Commerce Clause. *See id.* at 86-87. The RPS program required utilities to increase the percentage of their generation that came from renewable sources. *Id.* at 92. Utilities could accomplish this by generating renewable energy themselves or by purchasing renewable energy certificates ("REC") from other producers. *Id.* The only RECs that counted towards the RPS requirements, however, were those purchased from states in the Northeast Independent System Operator (ISO-NE) region and some adjacent states. *Id.* at 93. Allco argued it was discriminated against because utilities in Connecticut could not purchase RECs from Allco's solar power facility in Georgia to fulfil their RPS requirements. *Id.* at 93-94. The court held that Connecticut's program did not violate the dormant Commerce

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Project" by MISO, a portion of the costs will be allocated system-wide. *See* Compl. ¶¶ 43, 71.

Clause because Georgia's RECs did not meet the legal requirements of Connecticut's RPS program, and therefore, the RECs produced by generators in Georgia were different products than the RECs produced by generators in the ISO-NE. *Id.* at 105. The court concluded that these two offered "products" were not similarly situated. The court also emphasized that Connecticut's RPS program made geographic distinctions that followed the lines of the FERC-created ISO-NE, and that while Connecticut had *direct* access to electricity in the ISO-NE market, it only had *indirect* access to electricity outside that market (such as from Georgia). Thus, the court concluded that the two markets also were not similarly situated. *See id.* at 106-07.

This case is fundamentally different. It does not involve a product created by Minnesota, nor does Minnesota's law follow the jurisdictional lines of MISO. Rather, it involves Minnesota's attempt to restrict competition in the market for regionally planned and cost-allocated transmission projects by isolating Minnesota from the rest of MISO and insulating its in-state, incumbent transmission owners from competition for these projects. This is exactly the type of protectionist legislation that the dormant Commerce Clause is meant to prevent.

4. This Court is Not Required to Defer to the State's Policy Decision.

Defendants argue, based on *Tracy,* that this Court is unable to evaluate the potential benefits or consequences of eliminating the law and must simply defer to the state's policy choice in this matter and uphold the law. *See* Xcel Br. at 22. These arguments are misguided. The Court in *Tracy* expressed concern that it was ill-equipped to predict the effects of judicial interference with a state's regime of taxation in a captive retail utility market. *Tracy*, 519 U.S. at 304, 308-09. This case is different. As discussed, the law here does not touch on or have the potential to negatively impact the captive retail market, such that the concern expressed in *Tracy* is inapplicable as a threshold matter.

The effect of the two laws likewise is very different. The tax in *Tracy* may have hindered competitors in selling their product in the Ohio market, but did not *prohibit* competitors from doing so. The Minnesota statute, on the other hand, wholly excludes new entrants to the Minnesota portion of the regional market from opportunities to bid on, build, and own regionally planned transmission projects, simply handing those projects to Minnesota transmission owners.

In addition, the very fact that it was a *tax* at issue in *Tracy* was relevant to the Court's decision to abstain from evaluating the effect of eliminating it. 519 U.S. at 309 (stating it was "reticent . . . to consider subtle compensatory tax defenses."). In so finding, the Court was merely reiterating long-standing precedent that states are entitled to some deference in making taxation decisions. *See Nat'l Private Truck Council, Inc. v. Okla. Tax Comm'n*, 515 U.S. 582, 586 (1995) ("We have long recognized that principles of federalism and comity generally counsel that courts should adopt a hands-off approach with respect to state tax administration."); *U & I Sanitation v. City of Columbus*, 205 F.3d 1063, 1070 n.5 (8th Cir. 2000) ("The permissibility of state and local taxation measures, of course, is governed by a different framework.") (citing *Okla. Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 183 (1995)).

This case does not involve the subtle complexities of a tax. Rather, it involves blatant favoritism of in-state entities to the exclusion of all others. Thus, the factors that caused the Supreme Court's reluctance in *Tracy* to analyze the impacts of the state law do not exist here. Courts have long considered and evaluated the impact of protectionist state regulations on interstate commerce. *See, e.g.*, *S.D. Farm Bureau, Inc.*, 340 F.3d at 595-96 (evaluating evidence in the record showing that a state's Constitutional provision prohibiting corporations from acquiring farm land in South Dakota had a discriminatory purpose and noting the lack of evidence as to the law's effectiveness in preserving family farms); *U & I Sanitation*, 205 F.3d at 1069-72 (evaluating the benefits and burdens of waste hauling statute); *Cotto Waxo Co.*, 46 F.3d at 794-95 (evaluating and quantifying the economic burden of a state statute on interstate commerce). *Tracy* does not require this Court to defer to the state in this matter.

5. Eliminating the Right of First Refusal Would Not Adversely Impact Captive Retail Customers or the Electric Grid.

There is no evidence that eliminating the right of first refusal would negatively impact the captive retail market. In fact, unlike in *Tracy*, the evidence points to just the opposite result—eliminating rights of first refusal increases competition, drives down costs, and benefits consumers, just as Order No. 1000 predicted. That there may be a factual dispute on this issue between the parties merely highlights how inappropriate it would be to resolve this case on a motion to dismiss. The allegations in the Complaint and information available in the public record are more than sufficient for the Court to conclude, at this early stage in the litigation, that state rights of first refusal burden the interstate market, and that the elimination of such rights would have no adverse impact on the captive retail market, would bolster competition and benefit consumers.

Moreover, Xcel's argument disingenuously conflates the state's role in regulating "distribution" of electricity with its role in regulating "transmission." Distribution and transmission are distinct components of the three-step, generation-transmission-distribution electricity market notwithstanding the fact that some, but not all, entities provide all three components. The Minnesota right of first refusal statute has no application to the distribution of electricity. Thus, Xcel's lengthy recitation of its obligations as a *distributor* of electricity is irrelevant to the Court's analysis and serves no purpose other than to confuse the issues. *See* Xcel Br. 21-22. Because entities like Intervenor-Defendant ITC Midwest—a transmission owner that is not also a retail provider—are equally protected from competition by the right of first refusal, there can be no assertion that the law was intended to protect retail ratepayers. In addition, Xcel makes no concrete argument as to *how* eliminating the right of first refusal for transmission lines in a "federally registered planning authority transmission plan," Minn. Stat. § 216B.246, Subd. 2, will impact any of its rights and obligations as a retail distributor.

Even more important, removing the right of first refusal for projects approved through MISO will not, as Xcel suggests, eliminate or even affect Minnesota's ability to regulate the building of transmission lines in the state. *See* Xcel Br. 19-20. Any new entrant to the Minnesota transmission market selected through the MISO competitive process would have to apply for a certificate of need and route permit from the Minnesota Public Utilities Commission and follow all of the procedures laid out in statute and the Commission's rules to obtain the necessary approvals to build and operate the line. *See* Xcel Br. at 8-10. LSP Transmission, like ITC Midwest and every other transmission owner in Minnesota, also would be required to report every other year on present and foreseeable inadequacies in the transmission system, and about investments necessary to modernize the system. *See* Xcel Br. at 22. Contrary to Xcel's assertions, LSP Transmission *is not* advocating for an unregulated, *laissez-faire*, free-for-all in the market for developing transmission. *See* Xcel Br. at 32-33. There are numerous ways that Minnesota can and does regulate both new and existing transmission owners to ensure adequate and reliable service without violating the dormant Commerce Clause. What Minnesota may *not* do is construct a wall around the state in order to preserve the market for its incumbent transmission owners.

The allegations in the Complaint and the evidence in the record thus far point to the conclusion that rights of first refusal *harm* competition and transmission ratepayers. FERC has already determined that rights of first refusal have "the potential to undermine the identification and evaluation of more efficient or cost-effective alternatives to regional transmission needs, which in turn can result in rates from Commission-jurisdictional services[5] that are unjust and unreasonable, or otherwise result in undue discrimination by public utility transmission providers." Order No. 1000 at ¶ 226.

FERC's findings were tested and upheld in federal court. In *South Carolina Public Service Authority*, the D.C. Circuit affirmed FERC's authority to order the removal of federal rights of first refusal from tariff agreements. 762 F.3d at 75. The court found that FERC was free to rest its ban on rights of first refusal on competition theory, and to

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[5] Commission-jurisdictional services generally mean transmission and other services provided by FERC, via the rights granted to it by the Federal Power Act.

determine that "rights of first refusal posed a barrier to entry that made the transmission market inefficient, that transmission facilities would therefore be developed at higher-than-necessary cost, and that those amplified costs would be passed on to transmission customers." *Id.* at 77. Subsequent cases also affirmed FERC's decision to eliminate rights of first refusal, and FERC's economic reasons for doing so. *See* Compl. ¶ 33 (citing cases).

FERC's decision to increase competition in the market for building transmission lines has been put into practice via the elimination of rights of first refusal in ISO tariffs, and the subsequent enactment of competitive bidding processes for regionally planned and regionally cost-allocated transmission projects. LSP Transmission's successful proposals in PJM, CAISO, and MISO each contained binding cost caps and other cost-reduction factors beneficial to ratepayers. Compl. ¶ 35. In selecting LSP Transmission's subsidiary, Republic Transmission, to build the Duff-Coleman Transmission Project, MISO noted that its proposal provided the greatest overall value out of eleven comprehensive proposals, including proposals from Defendants ITC Midwest and Xcel Energy.[6] Nauen Aff. at ¶ 3, Ex. 2. The benefits that accompany these projects in the form of cost caps and other cost-reduction factors are flowing to regional ratepayers from states that, unlike Minnesota, have not placed unconstitutional burdens on interstate competition for regionally planned and cost-allocated transmission projects.

[6] It is notable that the same entities fighting to protect the right of first refusal and their market share in Minnesota are pursuing development and expansion opportunities in other states in an independent, non-incumbent capacity.

This Court is not writing on a blank slate. Unlike the Court in *Tracy*, which noted that the record before it "reveal[ed] virtually nothing about the details of that competitive market," 519 U.S. at 302, this Court has, in the public record, extensive evidence that the elimination of rights of first refusal increases competition, lowers costs, and benefits consumers, and does not adversely impact the ability of traditional utilities to serve the retail market. In any event, the allegations in Plaintiff's Complaint, which rely on the information available in public records, are more than sufficient to withstand a motion to dismiss, and it is inappropriate at this stage for the Court to undertake a searching analysis of the benefits and burdens of eliminating rights of first refusal.

B. The Statute Facially Discriminates Against Interstate Commerce.

Intervenor Defendants and Amici Utilities admit that on its face, the Minnesota right of first refusal statute gives in-state incumbents the exclusive right to build federally approved transmission line projects in Minnesota. *See* Amici Br. at 3; Xcel Br. at 22. However, they advance two arguments as to why the statute is not facially discriminatory. First, they argue that the right of first refusal does not discriminate against out-of-state interests in favor of in-state interests because some of the incumbents are not Minnesota corporations. This assertion denies the legislative history of the statute and Intervenor-Defendant Xcel's own statements. The "purpose" of the right of first refusal statute was to "establish[] a right of first refusal for *Minnesota utilities and electric transmission owners* regarding the construction and ownership of electric transmission lines connecting to their own facilities." Nauen Aff. at ¶ 4, Ex. 3. Testifying in support of the bill, Xcel stated that it gave "*Minnesota utilities* the first opportunity to invest in federal regionally planned transmission facilities," and that it was intended to "preserve the status quo" for those entities. *See* State Br., Peick Aff., Ex. A at 4, 13.

Intervenor Defendants and Amici Utilities also argue that the statute is not discriminatory because other in-state incumbents are excluded from building a transmission line that does not connect to one of their in-state facilities. Both arguments run counter to precedent, and should be rejected by this Court.

1. <u>Appellate Courts Reject Defendants' Formalistic Approach to Defining "In-State" Entities.</u>

Notwithstanding legislative history and their own prior statements, Intervenor Defendants and Amici Utilities argue that because a handful of the incumbent entities are not headquartered in Minnesota, they do not qualify as "in-state" entities for purpose of determining whether Minnesota's right of first refusal statute favors in-state interests. Xcel Br. at 7-8; Amici Br. at 4-6. Courts have rejected this formalistic approach to determining whether a state law discriminates against interstate commerce.

In *Florida Transportation Services, Inc. v. Miami-Dade County*, 703 F.3d 1230, 1234 (11th Cir. 2012), the Eleventh Circuit considered whether a local practice of automatically renewing permits for incumbent stevedores at the Port of Miami and denying permits to new applicants violated the dormant Commerce Clause. The County argued that there was no disparate impact on out-of-state interests because some of the incumbent permit holders that received automatic permit renewals were incorporated out-of-state or were owned by companies incorporated out-of-state.[7] *Id.* at 1259. The court, without deciding whether a disparate impact was required, rejected this argument, finding:

> [A] company's place of incorporation alone does not decide whether the . . . permitting practices . . . imposed a disparate impact on out-of-state or non-local companies for the benefit of local companies. If that were the case, then a state or municipality's dormant Commerce Clause liability would turn on the empty formality of where a company's articles of incorporation were filed, rather than where the company's business takes place or where its political influence lies.

Id. (citing *United Haulers Ass'n, Inc.*, 550 U.S. at 345). The court noted it was taking a "functional" approach to the question of whether the permitting practices favor local companies and burden "non-local" business interests, and found that "though some of the permit holders were incorporated out-of-state, *all* of the permit holders were operating locally at the Port or were otherwise entrenched at the Port as a cargo terminal operator or as a co-owner of an operating stevedore." *Id.*

The First Circuit likewise rejected a formalistic approach to distinguishing between in-state and out-of-state interests. In *Walgreen Co. v. Rullan*, 405 F.3d 50, 52 (1st Cir. 2005), the court considered the constitutionality of a Puerto Rico law that required all pharmacies seeking to open or relocate within the Commonwealth to obtain a certificate of necessity and convenience. Walgreen argued that the law discriminated against interstate commerce because the law gave existing pharmacies located within one mile of the proposed pharmacy the right to oppose the new pharmacy, and, in practice, every time a

[7]The court declined to decide whether the practice was *per se* invalid, finding that the district court did not err in determining that the practice failed the *Pike* test. *Fla. Transp. Servs., Inc*, 703 F.3d at 1257.

pharmacy expressed its opposition, the Secretary would send the case through a lengthy and expensive administrative hearing process. *Id.* at 53-54.

The Secretary defended the law in part on the grounds that there was no burden on interstate commerce because some of the existing pharmacies were owned by out-of-state interests.[8] The court rejected this, stating: "[h]olding otherwise would be tantamount to saying that a favored group must be *entirely* in state for a law to have a discriminatory effect on commerce." *Id.* at 58. The court noted that, "the Act favors the largely local group of established pharmacies over similarly-situated out-of-Commonwealth pharmacies seeking to open new stores. . . . the Act does not burden a particular firm, or subgroup of firms, but rather affects every pharmacy seeking to open in an area of Puerto Rico where an established pharmacy already operates." *Id.* at 59.

The same rationale applies in this case. Regardless of whether some of the incumbents are headquartered or incorporated out-of-state, each incumbent has an active business operation in Minnesota, has transmission facilities and employees here, and therefore has a firm base from which to wield political influence in Minnesota. On the other hand, LSP Transmission, as well as other interested out-of-state transmission developers, are excluded from the market for building new transmission lines in Minnesota that are approved through the regional planning process simply because they do not already own transmission facilities in Minnesota. Accordingly, like the permitting practices in Florida and Puerto Rico, the Minnesota right of first refusal statute operates to shield local

[8] *Walgreen Co.* was also decided under *Pike*, because the statute was neutral on its face.

and entrenched Minnesota entities from competition. Indeed, this case presents an even clearer case of discrimination because, unlike in the cases above where the law was neutral on its face but discriminatory in practice, the Minnesota right of first refusal statute on its face gives preferential treatment to incumbents by entirely excluding non-incumbents. In sum, the fact that some of the incumbents may be incorporated out-of-state is irrelevant to the Court's dormant Commerce Clause analysis.[9]

The incongruity of Intervenor Defendants' and Amici Utilities' position is underscored by considering the reverse implication, which the Eighth Circuit examined in *Ben Oehrleins and Sons and Daughter, Inc. v. Hennepin County*, 115 F.3d 1372 (8th Cir. 1997). The Eighth Circuit evaluated the constitutionality of a County ordinance that required that all designated waste be delivered only to a County-designated transfer station or processing facility. The court held that the ordinance was unconstitutional to the extent it prohibited waste from being transported out of state. *Id.* at 1384-85. However, with respect to waste transported *solely* intra-state, it upheld the ordinance. *Id.* at 1385-86. In doing so, it rejected the argument that the ordinance still discriminated against an out-of-state entity that might wish to build a new processing facility in Minnesota, but would not

[9] Xcel cites *Colon Health Centers of America v. Hazel*, 813 F.3d 145 (4th Cir. 2016), in support of its proposition that a court may rely on state-of-incorporation to determine whether a business is in-state or out-of-state for purposes of applying the dormant Commerce Clause. However, *Colon Health Centers of America* cites no supporting authority and is an outlier at odds with both the functional test adopted by the First and Eleventh Circuits and with the Eighth Circuit's reasoning in *Oehrleins*, discussed below. In addition, *Colon Health Centers of America* was not decided on a motion to dismiss, but rather on a motion for summary judgment, after extensive discovery regarding the in-state versus out-of-state issue.

be allowed to receive waste under the ordinance. *Id.* at 1386. The Court reasoned that this theory "assumes that an out-of-state concern that permanently locates an operation within the state is still an 'out-of-state' entity that can complain that a law that even-handedly restricts a local market is 'discriminatory.' . . . A Delaware corporation doing business in Minnesota could not argue that it is discriminated against by Minnesota laws that apply equally to all businesses operating in the state." *Id.* at 1386-87.

The Eighth Circuit's reasoning underscores that place of incorporation is not the deciding factor for purposes of determining whether a law benefits in-state entities and burdens out-of-state entities. *See also Tarek ibn Ziyad Academy v. Islamic Relief USA*, 794 F. Supp. 2d 1044, 1056 (D. Minn. 2011) (noting that the place where a business conducts its operations, rather than its place of incorporation, is relevant to the dormant Commerce Clause inquiry). Just as an out-of-state entity that permanently locates within a state cannot complain that purely local regulations discriminate against interstate commerce, a state cannot justify its discriminatory laws on the basis that some of the in-state entities it has chosen to protect happen to be headquartered or incorporated out of state. Each incumbent protected by the right of first refusal statute enjoys that protection for the sole reason that it owns facilities in the state of Minnesota.

Finally, Amici Utilities cite *Rocky Mountain Farmers Union v. Corey*, 730 F.3d 1070 (9th Cir. 2013), for the proposition that there is a reason, apart from the origin of the parties, to treat the incumbent utilities and LSP Transmission differently. In *Rocky Mountain*, Midwestern ethanol producers claimed California's Low Carbon Fuel Standard discriminated against them by using a complicated formula to quantify the carbon intensity of ethanol, which included as one factor the distance that the ethanol traveled to market. The Court found, however, that the origin was relevant only to the extent it affected the actual emissions associated with the fuel. *Id.* at 1089. Unlike the Low Carbon Fuel Standard in *Rocky Mountain*, the Minnesota right of first refusal law does not apply a neutral set of factors to determine which entity is eligible to build a transmission line. Instead, it gives that right exclusively to in-state electric transmission owners, and categorically denies out-of-state transmission developers from competing for those projects. Accordingly, the Court should reject Intervenor Defendants' and Amici Utilities' arguments that the Minnesota statute is not discriminatory on its face.

2. The State May Not Curtail Commerce and Divert Business to Its Favored Operators Simply Because It Also Discriminates Against Other In-State Operators.

It is axiomatic that a law that discriminates against interstate commerce is not saved by the fact that it also discriminates against other in-state interests. A state "may not avoid the Commerce Clause's strictures by curtailing movement of articles of commerce through subdivisions of the State, rather than through the State itself." *Fort Gratiot Sanitary Landfill, Inc.*, 504 U.S. at 353-54. The Supreme Court has acknowledged this proposition repeatedly. *See C & A Carbone, Inc. v. Town of Clarkstown, N.Y.*, 511 U.S. 383, 391 (1994) ("The ordinance is no less discriminatory because in-state or in-town processors are also covered by the prohibition."); *Dean Milk Co.*, 340 U.S. at 354 n.4 (finding it "immaterial that Wisconsin milk from outside the Madison area is subjected to the same proscription as that moving in interstate commerce"). And the proposition has applied regardless of whether a state favors one entity, *see C & A Carbone*, 511 U.S. at 392; or several, *see Dean Milk Co.*, 340 U.S. at 350. The intent of each of these statutes is to divert business to the "favored operator." *C & A Carbone*, 511 U.S. at 391.[10] The same is true of the Minnesota right of first refusal law. When a transmission line project that connects to an incumbent's existing Minnesota facility is approved, the incumbent has the exclusive right to capitalize on the opportunity and build the project. The fact that the right of first refusal statute excludes other in-state entities, as well as out-of-state entities, from the opportunity to build a particular project does not save the statute from the strictures of the dormant Commerce Clause.

C. The Right of First Refusal Statute Discriminates in Purpose and Effect.

Defendants do not make any new substantive arguments regarding the statute's discriminatory purpose or effect; rather, they repeat their earlier propositions that the statute does not distinguish between in-state and out-of-state interests; arguments refuted *supra* § IV.B.1. To the extent Amici Utilities address the issue, they assert "neither the purpose nor the effect of the challenged legislation is to foreclose out-of-state economic interests from competing to construct transmission service." Amici Br. at 7. This assertion denies reality. The statute forecloses any and all competition for building transmission lines approved through MISO, and retains for incumbents, all of whom by definition have facilities in Minnesota, the exclusive right to build those lines.

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[10] The court in *Oehrleins* held that a regulation that applied *purely* to intra-state transfers of waste did not violate the dormant Commerce Clause because the regulation allowed transfers of waste to out-of-state facilities. Here, the right of first refusal statute prohibits competition from both out-of-state entities as well as other in-state entities.

As discussed above, the discriminatory purpose of the law also is evident in its legislative history. *See supra* § IV.B; Compl. ¶ 51, 53; *S.D. Farm Bureau, Inc.*, 340 F.3d at 593 (finding the most obvious evidence of a discriminatory purpose is that the drafters intended to discriminate against out-of-state businesses). In addition, the hearing testimony, *see* State Br., Peick Aff., Ex. A, is replete with unsubstantiated concerns that state authority would be undermined by competition, demonstrating clearly that the statute was passed in an effort to undermine the effect of Order No. 1000 and protect incumbent transmission owners from the competition that Order No. 1000 envisioned to ensure just and reasonable regional rates. *See S.D. Farm Bureau, Inc.*, 340 F.3d at 594 (finding that the drafters of the law did not have any evidence that the law would protect the environment or preserve family farms). The discriminatory purpose and effect of the right of first refusal statute is plain on its face and in the circumstances surrounding its enactment. In any event, the question of whether a statute discriminates in purpose and effect is a fact-intensive inquiry that is inappropriate to resolve on a motion to dismiss. *See Colon Health Ctrs. of Am. LLC*, 733 F.3d at 544-45.

Southern Union Co. v. Missouri Public Service Commission, 289 F.3d 503 (8th Cir. 2002), upon which Defendants and Amici Utilities rely, is wholly inapposite. In that case, a natural gas utility attempted to obtain a five-year blanket approval to purchase stock from utilities that did not operate in Missouri. The Eighth Circuit found that the state's regulation of stock purchases was not discriminatory because it applied to all regulated utilities regardless of whether they were purchasing stock from an in-state utility or an out-of-state utility. *Id.* at 508. The facts of *Southern Union* simply have no parallel here. The law in *Southern Union* was a generally applicable regulation that merely required prior approval before a utility purchased stock from another utility. The right of first refusal, on the other hand, gives preferential treatment to a select group of entities, and wholly excludes any new entrants to the Minnesota transmission market. Accordingly, the Court should not dismiss the Complaint on the grounds that it fails to state a claim that the Minnesota right of first refusal statute discriminates in purpose and effect.

D. The Right of First Refusal Statute Fails the *Pike* Test.

Even if a statute does not "overtly discriminate against interstate commerce on its face, in its purpose, or through its effects," it "may still violate the dormant Commerce Clause if the local interests that it serves do not justify the burden that it imposes upon interstate commerce." *U & I Sanitation*, 205 F.3d at 1069. First, in assessing the burdens, the court must not only consider the burdens on the parties, but must adopt an "aggregate analysis" that considers "'what effect would arise if not one, but many or every, State adopted similar legislation.'" *Id.* (quoting *Healy v. Beer Inst.*, 491 U.S. 324, 336 (1989)). Second, if a burden is identified, the defendant cannot merely make a conclusory assertion regarding the purported benefits, but "must produce evidence that the law actually produces the benefits it purports to produce, that is, that the putative benefits to the state are not 'illusory.'" *Martin Marietta Materials, Inc. v. City of Greenwood, Mo.*, No. 06-697, 2008 WL 4832638, at *5 (W.D. Mo. Sept. 4, 2008) (citing *U & I Sanitation*, 205 F.3d at 1070-71)). Finally, even if a statute "serves some legitimate local purpose," the court must consider "the availability of a less burdensome alternative." *U & I Sanitation*, 205 F.3d at 1070; *see also R & M Oil & Supply, Inc. v. Saunders*, 307 F.3d 731, 736 (8th Cir. 2002)

("[W]e consider whether the local interest involved 'could be promoted as well with a lesser impact on interstate activities'") (quoting *Pike*, 397 U.S. at 142).

With the burdens and benefits properly assessed as described above, it becomes clear that the burden on interstate commerce caused by the right of first refusal statute vastly exceeds the illusory local benefits. And in any event, the *Pike* balancing test is a fact-intensive inquiry, and it is inappropriate for the Court to engage in this inquiry on a motion to dismiss. For these reasons, Defendants' motion should be denied.

1. <u>Given the Fact-Intensive Nature of the *Pike* Balancing Test, It Is Premature to Weigh the Benefits and Burdens of the Minnesota Statute at This Stage.</u>

The *Pike* balancing test is often fact-intensive, and Xcel's conclusory allegations of its benefits to "health, life, and safety" are insufficient to dismiss LSP Transmission's claims that the right of first refusal places an excessive burden on interstate commerce. In *Cotto Waxo Co.*, 46 F.3d at 795, the Eighth Circuit reversed a grant of ***summary judgment*** on the question of whether the burden on interstate commerce was excessive, even though the alleged burden was "slight," consisting primarily of a $38,000 loss of annual sales for the plaintiff. The court found that the law's constitutionality should be "tested at trial." *Id.*; *see also Blue Circle Cement v. Bd. Of Cnty. Comm'rs*, 27 F.3d 1499, 1510-12 (10th Cir. 1994) (finding the district court "failed to conduct the *Pike* analysis" where the district court had "summarily rejected" the allegation of an excessive burden on interstate commerce "by concluding that the Ordinance promotes the health, safety, and welfare of the . . . community" despite a lack of evidence of the supposed benefits[11]). Even the Fourth Circuit in *Colon Health Centers of America, LLC* , on which Xcel heavily relies, declined to dismiss the plaintiff's allegations before developing the record. 733 F.3d at 546 ("The fact-intensive character of this inquiry, however, counsels against a premature dismissal.").

In this case, hundreds of millions of dollars in regionally-cost allocated projects are at stake, there is *no evidence* (not even "miniscule" evidence, *see Cotto Waxo*, 46 F.3d at 795) of the right of first refusal's alleged benefits in the record, and the parties are still at the pleading stage. A dismissal at this stage would be even more inappropriate than the premature grant of summary judgment reversed by the Eighth Circuit in *Cotto Waxo*. Defendants' motion to dismiss therefore must be denied.

2. <u>The Right of First Refusal Statute Heavily Burdens Interstate Commerce, Both with Regard to LSP Transmission Individually and the Interstate Market in the Aggregate.</u>

If the Court chooses to engage in a preliminary analysis of the *Pike* balancing test, it will find that Defendants' arguments fall far short. First, even in the absence of a developed record, the Court can easily surmise that, if a right of first refusal statute was adopted by "every" state, *see U & I Sanitation*, 205 F.3d at 1069, the cumulative effect of such statutes would effectively nullify Order No. 1000's abolition of rights of first refusal in FERC-approved tariffs for regionally cost allocated transmission facilities and wholly eliminate competition for these projects, thereby undermining Order No. 1000's goals and

[11] On remand, the district court granted summary judgment in favor of the *plaintiff* pursuant to an analysis of the evidence under *Pike*, thus demonstrating the importance of considering the evidence. *See Blue Circle Cement v. Bd. Of Cnty. Comm'rs*, 917 F. Supp. 1514, 1523 (N.D. Okla. 1995).

"national uniformity in regulation." *See* State Br. at 13 (quoting *Tracy*). All incumbents across the country would retain rights of first refusal and there would be no competitive bidding, even for the largest regionally cost allocated projects. Thus, when the potential aggregate effects are considered, a state right of first refusal statute indisputably places a significant burden on interstate commerce. Indeed, as discussed *supra*, § IV.A.5, FERC has already weighed in on the benefits of eliminating rights of first refusal and on the negative effects that restricting competition has on innovation, efficiency, and costs to consumers.

Apart from the right of first refusal statute's burden on interstate commerce generally, it also burdens LSP Transmission individually by effectively barring it from competing via the FERC-approved process for regionally-planned projects approved for construction in Minnesota. The Eighth Circuit has held that a burden on even "a single firm's interstate activities can be excessive" in the *Pike* inquiry. *See Pioneer Military Lending, Inc. v. Manning*, 2 F.3d 280, 283 (8th Cir. 1993).[12] For example, if not for the right of first refusal statute, LSP Transmission would have been permitted to bid on the Huntley-Wilmarth project, just as it bid on (and won) the Duff-Coleman project. *See* Compl. ¶ 37. But, because of the Minnesota statute, the approximately $88 to $108-million Huntley-Wilmarth project was automatically assigned to the incumbents, Xcel and ITC

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[12] Amici Utilities' implication to the contrary is inaccurate. *See* Amici Br. at 9 (citation omitted). The language quoted by Amici did not "ma[ke] irrelevant the burden that a state regulation places on an individual business," but "merely emphasize[d] that the burden placed on any individual firm should be regarded in the context of the overall interstate market." *Pioneer Military Lending*, 2 F.3d at 283.

Midwest. *See* Xcel Br., Zylstra Decl., Ex. E, at 105. Even relatively small future projects subject to the right of first refusal statute may be worth tens of millions dollars. The inability to compete for such projects is a far heavier burden than the five- and six-figure costs imposed on the plaintiff in *Pioneer Military* that led the Eighth Circuit to invalidate the relevant statute under *Pike*.[13] 2 F.3d at 282; *see also Cotto Waxo*, 46 F.3d at 795 (finding a $38,000 burden on commerce should be tested at trial). Because the right of first refusal statute has an excessive burden on the market in the aggregate and on LSP Transmission individually, the Court should deny Defendants' motion.

3. The Right of First Refusal Statute's Purported Benefits are Entirely Speculative.

Where a law burdens interstate commerce, even slightly, it is not enough merely to assert local benefits in response. Rather, Defendants must "produce evidence" that the law "actually produces the benefits it purports to produce, that is, that the putative benefits to the state are not 'illusory.'" *Martin Marietta Materials, Inc.*, 2008 WL 4832638, at *5. For example, in *Pioneer Military Lending, Inc.*, the Eighth Circuit acknowledged the state's legitimate interest in "protecting its residents from usurious interests rates," but

[13] There is no basis for distinguishing, as Amici Utilities attempt to do, between "ongoing business," *see* Amici Br. at 9, and attempts to engage in new business. As Amici Utilities acknowledge, the "Commerce Clause . . . protects the interstate *market* . . . from prohibitive or burdensome regulations." *Id.* (emphasis in original). Here, the interstate "market" is for regionally-cost allocated transmission facilities approved by MISO. The Minnesota law places a "prohibitive or burdensome regulation" on that market to prevent out of state entities from competing for those projects to the extent that they are physically located in Minnesota. *See, e.g.*, *Dakota, Minn. & E. R.R. Corp. v. South Dakota*, 236 F. Supp. 2d 989, 1021 (D.S.D. 2002) (holding that "blocking a project" which had not yet been built imposed an excessive burden on interstate commerce under *Pike*), *affirmed in part and modified in part on other grounds*, 362 F.3d 512 (2004).

found that the interest does not apply where "[t]here was no evidence . . . that any . . . resident would be subject to higher interest rates as a result of [Plaintiff's] activities." 2 F.3d at 284. Accordingly, where "the 'ruinous' effects of competition are entirely speculative, their prevention cannot justify restricting market entry." *Medigen, Inc. v. Pub. Serv. Comm'n*, 985 F.2d 164, 167 (4th Cir. 1993). Additionally, the Court must consider the availability of less burdensome alternatives to secure the same benefits. Neither of these requirements has been met by Defendants or Amici Utilities in this case.

None of the Defendants provide any substantive, meaningful explanation—much less any supporting evidence—of how the right of first refusal statute improves the reliable delivery of electricity, improves the health, life, or safety of Minnesotans, avoids unnecessary duplication of facilities, or minimizes disputes between public utilities. *See* State Br. at 12; Xcel Br. at 30-31; Amici Br. at 9-12. The benefits of "regulation" listed by Xcel are quoted from the preamble of Chapter 216B (the chapter governing "Public Utilities" generally), which was last revised in 1989, long before Order No. 1000 was issued and the Minnesota right of first refusal statute was enacted. *See* Xcel Br. at 30-31 (quoting Minn. Stat. § 216B.01). In addition, many of these regulatory strictures do not apply to transmission owners protected by the right of first refusal law, such as ITC Midwest. There is no evidence that the right of first refusal statute confers any of these supposed benefits.

Amici Utilities claim that "if [incumbents] had no right of first refusal over the ownership, operation and maintenance of lines connecting to their systems, the loss of that control would compromise their ability to meet their service obligation," Amici Br. at 13 (citing only conclusory testimony on behalf of Xcel), but do not explain the causal chain, making their prediction of "'ruinous' effects . . . entirely speculative." *Medigen*, 985 F.2d at 167; *see also Cotto Waxo Co.*, 46 F.3d at 795 (finding that the Defendant "failed to submit any evidence" where the only evidence was the self-serving conclusory testimony of "a Minnesota manufacturer" with "no factual basis" for the figure he asserted). Both the qualification and developer selection processes in the MISO Tariff contain numerous stringent requirements to ensure, among other things, that only capable and reliable transmission developers will be able to secure a project through competition. *See* Nauen Aff. at ¶ 3, Ex. 2. On the other hand, the right of first refusal permits incumbents to secure projects without doing anything to "ensure the incumbent[s] . . . remained skilled, experienced, reliable, properly equipped, and safe." *See Fla. Transp. Servs., Inc.*, 703 F.3d at 1260-62 (finding "no local benefit" in "preserving" the local market "for a select few privileged" incumbents). Under such circumstances, any argument that a right of first refusal is necessary or even marginally helpful in securing reliable service requires credible supporting evidence, which is not and cannot be a part of the record at this stage.

Moreover, unlike the monopolies on gas distribution to local customers at issue in *Tracy*, the right of first refusal is not a widespread, established national phenomenon recognized in a multitude of court decision to be important for preserving reliable service for retail customers. Only a handful of states[14] have implemented rights of first refusal, while the remainder of the states have not interfered with the competitive bidding process

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[14] *See* N.D. Cent. Code § 49-03-02.2; S.D. Laws § 49-32-20; Neb. Rev. Stat. § 70-1014.2; N.C. Gen. Stat. § 62-100.

created after Order No. 1000. And, as discussed, projects have already been awarded through the competitive process, including the MISO-approved Duff-Coleman project awarded to LSP Transmission's affiliate. *See* Compl. ¶¶ 35-37. Defendants and Amici Utilities have not identified any negative impacts stemming from the award of these projects that would have been prevented by a right of first refusal statute.

Finally, even assuming the right of first refusal statute created local benefits such as reliable and adequate service, there are many, less discriminatory ways that states can ensure reliable transmission service that have not been developed in the record.

V. CONCLUSION

Defendants and Amici Utilities have failed to articulate a single supportable basis upon which the Court can dismiss LSP Transmission's Complaint. Plaintiff LSP Transmission therefore respectfully requests that the Court deny Defendants' motions to dismiss in their entireties.

Dated: January 9, 2018

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