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Federalism Obstacles to Advancing Renewable Energy

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Federalism Obstacles To Advancing Renewable Energy

By Michael B. Gerrard

Many states have been taking steps to increase the use of renewable energy sources such as wind and solar. However, because electricity is a commodity in interstate commerce and electrons once on the grid do not respect state borders, these state efforts have begun to collide with the dormant Commerce Clause (the principle that the Constitution's grant of authority to Congress to regulate commerce among the states also limits the ability of the states to discriminate against other states)[1] and related constitutional doctrines.

Increased renewable energy is (together with energy efficiency) the main way to reduce fossil fuel use, which in turn is the largest source of greenhouse gas emissions. Stark partisan divisions have paralyzed Congress from acting on climate change. Until this paralysis somehow ends, and either the federal government takes vigorous action on greenhouse gas emissions or the states are given a freer hand in doing so, the states will continue to be vulnerable to legal attacks over certain techniques to promote clean energy.

Fifty years ago the U.S. Supreme Court declared that Congress in enacting the Federal Power Act had drawn a "bright line" between federal and state jurisdiction over electricity.[2] Developments in technology and in environmental imperatives are blurring this line and leading to new conflicts that test the limits of state power over energy.

This article discusses several recent judicial decisions and pending cases that lie at the perilous intersection of renewable energy and the limitations on state power.

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Extraterritoriality

One significant decision, *State of North Dakota v. Heydinger*, was issued on April 18, 2014, by the U.S. District Court for Minnesota.[3] It involved a statute enacted in Minnesota in 2007 that in effect prevented large new coal-fired power plants located out of the state from selling their electricity into the state unless they undertook state-approved offset projects.

The court found that this broadly written law violates the doctrine against extraterritorial regulation because it applies to electric power and capacity transactions occurring wholly outside of Minnesota's borders. Transmission of electricity is much like transmission of information over the Internet—the product uncontrollably crosses state borders. Because of this extraterritorial effect, the Minnesota law was found to be per se invalid. The court declared:

> If any or every state were to adopt similar legislation (e.g., prohibiting the use of electricity generated by different fuels or requiring compliance with unique, statutorily-mandated exemption programs subject to state approval), the current marketplace for electricity would come to a grinding halt. In an interconnected system…entities involved at each step of the process—generation, transmission, and distribution of electricity—would potentially be subject to multiple state laws regardless of whether they were transacting commerce outside of their home state. Such a scenario is 'just the kind of competing and interlocking local economic regulation that the Commerce Clause was meant to preclude.'

Local Preferences

Another way that state renewable energy laws can stumble is if they give some sort of a preference to in-state companies. Last year the U.S. Court of Appeals for the Seventh Circuit found one such law to be unconstitutional, though ironically in a decision that otherwise favored renewable energy.

The case, *Illinois Commerce Commission v. Federal Energy Regulatory Commission*[4] (FERC), involved allocation of the costs of building a major electricity transmission project that would carry power from rural wind farms to the cities of the Midwest. Several states complained that under the FERC tariff, they would be paying more than their fair share of the costs. The court handed FERC a victory by upholding the tariff; though the matching of the costs and the benefits may be crude, "if crude is all that is possible, it will have to suffice," wrote Judge Richard Posner. This decision will aid FERC's efforts to pay for other transmission projects that will take renewable energy to market.

However, the State of Michigan raised a further objection. It has a renewable portfolio standard—a requirement that the electric suppliers that sell power within the state obtain a certain percentage of their power from renewable sources. Michigan's law allows utilities to get credit only for renewable energy generated within its borders. The court found that this provision "trips over an insurmountable constitutional objection. Michigan cannot, without violating the commerce clause of Article I of the Constitution, discriminate against out-of-state renewable energy." The decision did not itself invalidate the Michigan law, because the lawsuit did not directly involve that law; but it certainly cast a cloud over that law and others that favor in-state generators.

This is no small matter. A total of 29 states plus the District of Columbia have renewable portfolio standards.[5] As Professor Steven Ferrey has shown, most of these states favor in-state generators in one or more ways.[6] These states variously require that some or all of the renewable energy come from within the state or the region, or use a multiplier or other means to give greater credit for in-state resources.

Local preferences for renewable energy were also at issue in *Rocky Mountain Farmers Union v. Corey*,[7] in which the U.S. Court of Appeals for the Ninth Circuit in September 2013 reversed the portions of a 2011 district court decision that found California's low carbon fuel standard (LCFS) to be in violation of the dormant Commerce Clause. The LCFS requires a portion of the motor vehicle fuel used in California to consist of biofuels such as ethanol. It includes a formula that disadvantages ethanol that travelled a long distance to California.

The Ninth Circuit ruled that this consideration of the life cycle emissions of ethanol that travels long distances did not facially discriminate against out-of-state commerce, and that the LCFS did not violate the dormant Commerce Clause prohibition on extraterritorial regulation. The Ninth Circuit vacated the preliminary injunction imposed by the district court and remanded for consideration of whether the LCFS's ethanol provisions discriminate in purpose or practical effect, and for application of the *Pike v. Bruce Church*[8] balancing test to determine whether the LCFS's initial crude oil provisions impose a burden on interstate commerce that is "clearly excessive" in relation to their local benefits. The Ninth Circuit instructed that if the district court finds the ethanol provisions to be discriminatory in purpose or practical effect, it should apply strict scrutiny to those provisions, but that it must otherwise apply the Pike balancing test to the ethanol provisions.

> Because electricity is a commodity in interstate commerce, state efforts to increase the use of renewable energy sources have begun to collide with the dormant Commerce Clause.

In January 2014 the Ninth Circuit denied petitions for rehearing en banc of its September 2013 decision.[9] Seven of the court's active judges dissented. The dissent pointed to at least three ways in which in its view the court had erred. One, the majority had found "at least facially constitutional a protectionist regulatory scheme that threatens to Balkanize our national economy." Two, the majority "compound[ed] its error" by finding that the legitimate local concern of combating climate change justified the LCFS ethanol provisions when the state had admitted that they would have little to no effect on climate change. Three, the LCFS ethanol provisions impermissibly sought to control conduct in other states.

Although the court denied the petition for rehearing without an opinion, Judge Ronald M. Gould, who wrote the court's September 2013 majority opinion, wrote a concurrence supporting the September opinion and countering the "overstatements" of the dissent. Gould stated that "the tone and substance of the dissent is perhaps aimed at encouraging Supreme Court review." Unsurprisingly, a petition for certiorari was filed in March 2014.

Last week the U.S. District Court for the District of Massachusetts dismissed a case in which opponents of the controversial Cape Wind facility in Nantucket Sound alleged that the state's approval of a utility merger improperly favored this in-state wind energy project.[10] The court ruled that the action was barred by the Eleventh Amendment, but noted that "the result would be no different were the court to rule on the substance of the claims." The court said that plaintiffs had no standing to bring dormant Commerce Clause claims "as they do not compete in the power generation market" and because they could not claim standing to bring such claims as taxpayers or end-use consumers.

Pending Challenges

Several pending suits allege an impermissible preference for in-state companies in the promotion of renewable energy. In *Nichols v. Markell*, a fuel cell manufacturer based in Connecticut is challenging a Delaware statute that gives various preferences under the state's renewable portfolio standard to fuel cells built in the state and to power generated by these fuel cells. On April 17, 2014, the U.S. District Court for the District of Delaware dismissed an Equal Protection Clause challenge but allowed the manufacturer's Commerce Clause challenge to proceed.[11]

Energy and Environment Legal Institute v. Epel was brought in the U.S. District Court for Colorado by a non-profit group that changed its name from American Tradition Institute in 2013. This group has been heavily involved in efforts to attack the science underlying climate regulation, and it also promotes coal energy. The lawsuit challenges Colorado's renewable energy standard as a violation of the Commerce Clause because it limits sales by fossil fuel-fired power plants and reduces the interstate market for coal. On May 1, 2014, the court ruled that the group has standing to sue because one of its members, Alpha Natural Resources, Inc., operates coal mines whose sales would be hurt by the law.[12] A motion for summary judgment on the merits is pending.

Several suits that alleged interstate commerce violations were settled on terms favorable to plaintiffs, leading some to argue that the defendants knew they would likely lose. *Indeck Corinth, LP v. Paterson*[13] was a challenge to aspects of the Regional Greenhouse Gas Initiative (RGGI), a carbon dioxide emissions trading program that now involves nine northeastern states. The suit, in New York Supreme Court, Albany County, was brought by an independent power producer that was unable to pass the costs of buying emission allowances under the RGGI program along to its customers; the plaintiff received substantial relief from this burden under the settlement.

Another challenge to RGGI, *Thrun v. Cuomo*, was dismissed on statute of limitations grounds.[14] If RGGI moves more aggressively to assess fees on power plants whose electricity flows into the region from non-RGGI states, further Commerce Clause challenges can be anticipated.[15] California's cap-and-trade regime for greenhouse gases may also be subject to Commerce Clause challenges. For instance, it is widely believed that its "first deliverer" policy, which places the compliance obligation on whatever party first delivers electricity to the California grid,[16] will be challenged in court.

A settlement was also reached in a challenge to Massachusetts' Green Communities Act of 2008, which required electric distribution companies to contract with renewable energy generators located in the state. The plaintiff, TransCanada Power Marketing, owned a wind facility in Maine. TransCanada and the state settled, and in 2012 the Massachusetts legislature amended the act to remove the in-state requirement.[17]

The Missouri Public Service Commission adopted a rule giving a geographic preference to renewable energy credits that can be used by the state's electric service providers. A state trial court ruled this to be a violation of the Commerce Clause. The commission then withdrew that requirement, and the state appellate court declared the controversy to be moot.[18]

A decision from the U.S. Court of Appeals for the Fourth Circuit is now awaited in *PPL EnergyPlus v. Nazarian*, a challenge to the way that Maryland gives incentives to regulated electricity distribution companies to procure power from new capacity (i.e., new power plants and other ways to satisfy power demand). The U.S. District Court in Maryland found that the state incentive scheme was unconstitutional as a violation of the Supremacy Clause, because it effectively set rates for wholesale power transactions, a task that is exclusively within the jurisdiction of FERC. The decision found the program did not violate the Commerce Clause.[19]

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A similar decision was issued by the U.S. District Court in New Jersey in a challenge to New Jersey's comparable program.[20] The U.S. Court of Appeals for the Third Circuit heard oral argument on the New Jersey case on March 27, 2014; oral argument before the Fourth Circuit in the Maryland case has not yet been held. These decisions do not primarily concern renewable energy, but their outcomes could have bearing on renewable energy programs.

Both cases raise important issues under the Federal Power Act,which provides that wholesale rates for electricity sold in interstate commerce are set by FERC, while retail electricity rates are set by the states. In the Third Circuit case, FERC filed a brief arguing that the New Jersey program violated the Federal Power Act, 16 U.S.C. Secs. 824-824h, by impermissibly affecting wholesale electricity rates. If the Third or Fourth circuit adopts that view, and especially if they use broad language in doing so, lawsuits can easily be foreseen that would claim that certain state renewable programs also intrude into the exclusive federal power to set wholesale rates.

Conclusion

Most or all of the disputes described here could be resolved by congressional action clarifying the state and federal roles in promoting renewable energy, but no such action appears to be in the offing. More likely, a coming flashpoint on the respective federal and state authority over energy resources will be the Environmental Protection Agency's rules under Section 111(d) of the Clean Air Act, which will seek to regulate greenhouse gas emissions from existing fossil fuel-fired power plants; the draft regulations are expected in June.

1. See *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1 (1824).
2. 20. *Fed. Power Comm'n v. S. Cal. Edison Co.*, 376 U.S. 205, 215–16 (1964).
3. No. 11–cv–3232 (SRN/SER), 2014 WL 1612331 (D. Minn. April 18, 2014).
4. 721 F.3d 764 (7th Cir. 2013).
5. Renewable Portfolio Standard Policies, DATABASE OF STATE INCENTIVES FOR RENEWABLES & EFFICIENCY (DSIRE), (Mar. 2013), http://www.dsireusa.org/documents/summarymaps/RPS_map.pdf
6. See Steven Ferrey, "Threading the Constitutional Needle With Care: The Commerce Clause Threat to the New Infrastructure of Renewable Power," 7 TEX. J. OIL, GAS & ENERGY L. 59 app. A (2011-2012).
7. 730 F.3d 1070 (9th Cir. 2013).
8. 397 U.S. 137 (1970).
9. 740 F.3d 507 (9th Cir. 2014).
10. *Town of Barnstable, Massachusetts v. Berwick*, No. 14-CV-10148 (D. Mass. May 2, 2014).
11. *Nichols v. Markell*, No. 12-cv-777-CJB, 2014 WL 1509780 (D. Del. April 17, 2014). The court dismissed the dormant Commerce Clause claim of an individual energy consumer for lack of standing.
12. *Energy & Envtl. Legal Inst. v. Epel*, No. 11-cv-00859-WJM-BNB, 2014 U.S. Dist. LEXIS 60567 (D. Colo. May 1, 2014).
13. Index No. 5280/2009 (N.Y. Sup. Ct. Albany Co.).
14. *Thrun v. Cuomo*, 112 A.D.3d 1038, 976 N.Y.S.2d 320 (3d Dept. 2013), mot. for leave to appeal denied, 2014 WL 1316287 (NY. April 3, 2014).
15. See Shelley Welton, "State Dynamism, Federal Constraints: Possible Constitutional Hurdles to Cross-Border Cap-and-Trade," NAT. RESOURCES & ENV'T, Summer 2012, at 36.
16. See CAL. CODE REGS. TIT. 17, §95802(a)(102).
17. *TransCanada Power Marketing Ltd. v. Bowles*, No. 4:10-CV-40070 (D. Mass.); see Chapter 209 of the Acts of 2012, An Act Relative to Competitively Priced Electricity in the Commonwealth.
18. *State of Missouri ex rel. Mo. Energy Dev. Ass'n v. Pub. Serv. Comm'n of State of Mo.*, 386 S.W.3d 165 (Mo. Ct. App. 2012).
19. *PPL EnergyPlus, LLC. v. Nazarian*, No. MJG-12-1286, 2013 U.S. Dist. LEXIS 140210 (D. Md. Sept. 30, 2013).
20. *PPL EnergyPlus, LLC v. Hanna*, No. 11-745, 2013 U.S. Dist. LEXIS 147273 (D.N.J. Oct. 11, 2013).